

Uasc/Csl Ltd. Vs. Dy. Cit

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Court : Income Tax Appellate Tribunal ITAT Mumbai

Decided On : Aug-25-2006

Judge : K Thangal, Vice-, K Boliya

Appellant : Uasc/Csl Ltd.

Respondent : Dy. Cit

Judgement :

2. Though the assessee has urged as many as four grounds, in effect it is directed against the order of the Commissioner (Appeals), holding that article 8 of the Agreement for Avoidance of Double Taxation between India and Mauritius did not apply in the instant case of the assessee. It is the case of the assessee that the Commissioner (Appeals) went wrong in holding that the place of effective management is not Mauritius. Further, according to the assessee, the Commissioner (Appeals) should have held that no part of assessee's profit from the operation of ships was taxable in India in view of article 8(1) of the Double Taxation Avoidance Agreement.

3. Without prejudice to the above, it is the case of the assessee that the assessee had no permanent establishment in India, as such no part of assessee's income was taxable in India, in view of the provisions of article 7(1) of the Double Taxation Avoidance Agreement.

Assessee-company filed the return on 7-8-1998 declaring income at Rs. 1,25,57,700. Assessee had gross receipts under freight to the extent of Rs.

16,74,36,024 and applying the provisions of Section 44B, the income has been adopted @ 7.5% of the receipts. The tax on the same was worked out @ 48% at Rs. 60,27,696.

Assessee, a shipping company incorporated in Mauritius, claimed 100% DIT relief as per Indo Mauritius Double Taxation Avoidance Agreement (DTAA for short). Tax Residency Certificate issued by the tax authorities of Mauritius was filed in support of the claim, according to which the assessee is a resident of Mauritius for tax purpose.

5. Assessing officer formed the opinion that the claim of the benefit of article 8 of DTAA entered into between India and Mauritius cannot be extended in the case of the assessee. According to the assessing officer, as per article 8 of the DTAA, profits from the operation of ships in international traffic is taxable only in the Contracting State in which the place of effective management of the enterprise is situated. In the instant case of the assessee, assessing officer formed the opinion that Mauritius is not effective place of management. Hence, he issued a notice calling for objections from the assessee. Assessee asked for time and was not co-operative. Assessing officer held that since the assessee has not substantiate that its place of effective management is Mauritius, benefit of article 8 of the DTAA entered into between India and Mauritius cannot be extended to the assessee. He held that the effective management of the enterprise of the assessee is not in one of the Contracting States (i.e. India/ Mauritius) but it is situated in a third State. Hence, the assessee cannot claim the benefit extended under article 8 of the DTAA. He held, in view of the above, income of the assessee is to be computed as per article 7 and not under article 8 of the DTAA. He further held that since the assessee has a Permanent Establishment (PE hereinafter referred to as) in the form of an exclusive agent, M/s Consolidated Cargo Services, Bangalore (CCS hereinafter referred to as), article 7 of the DTAA is clearly applicable and the assessee is liable to be taxed in India. He held, CCS is doing the agency work in all the ports in India in terms of the agency appointment letter dated 4-9-1997 from the assessee to CCS. CCS is the dependent agent, who is habitually concluding contracts on behalf of the assessee in the form of clearances from Government departments like Customs, revenue, Reserve bank of India, Mumbai Port Trust,

etc. CCS was doing all the functions by deciding the brokers, contracting with parties, loading of cargo, dealing with labourers for loading and unloading, collecting freight on behalf of the assessee, maintaining and operating bank account on behalf of the assessee, etc.

6. Assessing officer held, as per the definition of "Permanent Establishment" under article 5.1, it is clear that Permanent Establishment means a fixed place of business through which the business of the enterprise is wholly/partly carried on. He held the Honble Andhra Pradesh High Court in the case of CIT v. Visakhapatnam Port Trust had the occasion to consider the meaning of Permanent Establishment. The Honble High Court held that Permanent Establishment connotes a projection of the foreign enterprise itself into the territory of taxing State in a substantial and enduring form.

PE postulates the existence of a substantial element of an enduring or permanent nature of a foreign enterprise in another country, which can be attributed to a fixed place of business in that country. Assessing officer held, in the instant case of the assessee, the assessee established to have carried part of its business through a fixed place of business, i.e., through CCS. The assessee falls within the definition of Permanent Establishment under article 5.1. This is particularly so, he held, because Clause 7 of the agreement states that the agent shall provide suitable office space for one principals representative free of charge to the principal. He further noted that as per Clause 6 of the agreement, CCS must not accept the agency of other lines trading in the sphere of principals services without the consent of the principal. Further, CCS was not to engage in any canvassing activity for any shipping line, which compete with the principals liner services. Assessing Officer adopted the impugned amount as income of the assessee at page 5 of his order, observing as under: It may also be pertinent to mention that paragraph 2 of article 5 provide certain places to include in the definition of permanent establishment. As per paragraph 2(h), premises used as a sales outlet is also included in the definition of permanent establishment. It may also be pertinent to mention that paragraph 4 of article 5 gives certain exclusions from the definition of permanent establishment. The assessee does not fall within the category of excluded persons/places referred to in paragraph 4 of article 5.

Paragraph 5 of article 5 provides that where a person - other than an agent of an independent status to whom paragraph 6 applies is acting in one of the States on behalf of an enterprise of the other State, that enterprise shall be deemed to have a permanent establishment in the other State. Paragraph 6 excludes such agents from the operation of paragraph 5 who are of an independent status acting in ordinary course of their business. However, paragraph 6 is not applicable in such cases where the activities of the agent of an independent status are devoted wholly or almost wholly on behalf of the foreign enterprise.

From the above, it is clear that the assessee has a PE in India within the meaning of article 5 of the DTAA and hence, the assessee's income is taxable under article 7 of the Indo-Mauritius DTAA. The assessee has declared total receipt from shipping activities amounting to Rs. 16,74,36,204 on which income @ 7.5% applying the provisions of Section 44B/ 172 works out to Rs. 1,25,57,702. This would be adopted as income of the assessee.

Aggrieved by the above order, assessee approached the first appellate authority.

7. It was contended before the Commissioner (Appeals) that the assessee is a Non-Resident Shipping Company registered in Mauritius, carrying on the business of shipping line. Assessee appointed CCS as their agent in India vide agreement dated 4th September, 1997. M/s United Arab Shipping Co. (SAG), Kuwait and M/s Clipper Shipping Lines Ltd., America; are two shareholders of the assessee-company in Mauritius holding 50% shares. It was further submitted that out of the 4 Directors, 2 Directors are resident of Mauritius, whose names are - Mr.

Ashraf Ramtoola and Miss Yamnick Roussety. The assessee obtained Tax Residency Certificate in Mauritius, after compliance of the necessary conditions, i.e. to say- It was the case of the assessee that the assessing officer rejected assessee's claim for the benefit of article 8 of Indo-Mauritius Treaty and applied article 7, treating CCS as PE, not considering the entire facts. It was submitted that the assessing officer has not taken into consideration that the assessee is registered in Mauritius and has Registration Number issued by the Registrar of Companies. Assessee was considered to have carried the business through its agent, CCS. It was further submitted that the assessing officer has not considered

article 5.5 of DTAA, which provides that an enterprise shall not be deemed to have a PE in other Contracting State merely because it carries on the business in other State through a broker, general commission agent or through some other agents of independent status, where such agents are acting in the ordinary course of business. In the case of the assessee, CCS was carrying on the business of acting as agent of the assessee.

But CCS is an independent entity and it has independent status for the following reasons: (i) CCS is a registered partnership firm in India and the partners are Indian nationals; and (ii) Directors /Shareholders of the Non-Resident Shipping Company are not related to the partners of the firm.

It was further submitted that the Indian agent is independent. They are free to take their own decisions and carry on their own business and not dependent on the assessee. CCS cannot be considered as an exclusive dependent agent; as such provisions of article 7 cannot be applied.

8. The issue was decided against the assessee by the learned Commissioner (Appeals) by his well reasoned order, which reads as under: 2.3 I have considered the submission of the appellants counsel and the order of the assessing officer carefully. As stated in the earlier paragraph, the AR himself had admitted that the appellant has been granted Tax Residency Certificate of Mauritius after satisfying certain conditions as mentioned in para 2.2. It is also an admitted fact that the shareholders are United Arab Shipping Co., Kuwait and Clipper Shipping Lines Ltd., America, with 50% shares held by each of them i.e. none of the shareholders are resident of Mauritius. Apart from the two directors Mr. Abdoulla Al Shamsi of UAE and Mr. Handrik Lund Dal of Switzerland, the other two directors are on the companys board only to satisfy the conditions of the Mauritius Government. In the board minutes which have been produced, it is found that all the decisions are routine in nature. Merely by getting the company registered in Mauritius and obtaining the Registration Number cannot prove that the place of effective management is also situated in Mauritius. In fact there is a separate article in convention which indicates that there can be effective management in other than two Contracting States. Article 8(I) and 8(2) reads as under: (1) Profits from the

operation of ships or aircraft in international traffic shall be taxable only in Contracting State in which the place of effective management of the enterprise is situated.

(2) If the place of effective management of a shipping enterprise is aboard a ship, then it shall be deemed to be situated in the Contracting State in which the home harbour of the ship is situated or, if there is no such home harbour, in the Contracting State of which the operator of the ship is a resident.

Thus, it is clear that there is also a possibility of effective management being in a third State other than the two Contracting States. The assessing officer has specifically written in his assessment order that when the assessee was asked to substantiate that its place of effective management is in Mauritius, no further details were filed by the assessee to substantiate the same. In my opinion, the place of effective management is the place where the key and commercial decisions that are necessary for the business are taken. In substance the place of effective management will originally be a place where the most senior person or a group of persons sit and make its decisions, the place where the action to be taken for the entity as a whole is determined. In view of the above facts, I too, feel that the effective management of the appellant is neither in Mauritius nor in India.

2.4 Mr. Klaus Vogel in his book of International Taxation, who is an eminent authority of International Taxation, has stated that if the effective management of an enterprise is not in one of the Contracting States but is situated in the third State, the benefit of the article 8 cannot be extended. The same is reproduced as below: Article 8 furthermore applies only when the enterprises place of effective management is situated in a Contracting State. Whenever it is situated in a third State, the relationship between the two Contracting States is Government by the permanent establishment principle laid down in article 7. In a case in which the DTC article corresponding to article 8 MC established that an exemption of income was dependent on the aeroplane being registered in the other Contracting State, but where it was registered in the USA, the IRS likewise applied the treaty provision corresponding to article 7 instead (LTR 9513008 : DTC USA/Ireland).

Therefore, in view of the above, once it is held that the effective management of the appellant was neither in India nor in Mauritius, the benefit of article 8 of the Treaty will not be available and the income will have to be assessed in accordance with article 7 of the DTAA. The next question therefore comes whether in the circumstances of the case there exists a PE of the appellant. The assessing officer has observed that the appellant has PE in the form of its exclusive agent M /s Consolidated Cargo Services. In fact the following observations of the assessing officer are worth quoting: The assessee has an exclusive agent in the form of M/s Consolidated Cargo Services, Bangalore (CRS) who is doing the agency work in all the Indian ports in terms of the agency appointment letter dated 4-9-1997 from the assessee to CRS. CRS is the dependent agent which is habitually concluding contracts on behalf of the assessee in the form of all the clearances from the Government departments like Customs department, Income-tax department, Reserve bank of India, Mumbai Port Trust, etc. They are doing all the functions from deciding the brokers, contracting with the parties, for loading of cargo, dealing with labourers for loading and unloading, collecting the freight on behalf of the assessee, maintaining and operating a bank account on behalf of the assessee, etc.

Further, the assessing officer has pointed out that Clause 7 of the Agreement between the appellant and the agent clearly states that the agent shall provide suitable office place for one representative of the principal, free of charge. Also, as per Clause 6 of the Agreement, it is clearly provided that the agent must not accept the agency of other Lines trading in the sphere of the principals services without the consult of the principal. The agent also undertakes not to engage in any canvassing activity in favour of any Line which might compete with the principals liner services.

2.5 In the course of appellate proceedings, the AR has tried to rebut the assessing officers contention by saying that the restriction in Clause 6 of the Agreement does not mean that the Indian agent cannot carry on any business. The Indian agent is not supposed to carry on business of acting as agent of any other non-resident shipping company which is carrying on similar business in the same sector. However, if the Indian agent carries on business of canvassing cargo to a sector

which does not compete with the service of the principals liner service such agent cannot be treated as exclusive agent and provisions of article 5.4 does not apply and the provisions of article 5.5 apply.

2.6 I have considered the aforesaid contention of the AR as well as the assessment order. The moot point for consideration is whether in view of the factual position in this case can it be said that there exist a PE of the appellant company in India. The term PE has been defined in article 5.1 of the Indo-Mauritius DTAA as under: "For the purposes of this convention, the term permanent establishment means a fixed place of business through which the business of the enterprise is wholly or partly carried on." 2.7 The Honble Andhra Pradesh High Court had an occasion to consider the meaning of the term Permanent Establishment (PE) in the case of Visakhapatnam Port Trust (144 ITR 146). Their Lordships held that "Permanent Establishment" connotes a projection of the foreign enterprise itself into the territory of the taxing State in a substantial and enduring form. The word "Permanent Establishment" postulates the existence of substantial element of an enduring or permanent nature of a foreign enterprise in another country which can be attributed to a fixed place of business in that country. It was further held that when there is virtual projection of the foreign enterprise of one country into the soil of another country, the foreign enterprise would be considered to have a permanent establishment in the other country.

2.8 Now keeping the above in view-point, one has to look into the factual aspects of the case, particularly the following: The appellant has an agent who is doing the agency work in all of the Indian ports. The agent is responsible for concluding contracts on behalf of the appellant in the form of all the clearances from the Government departments like Customs department, Income-tax department, Reserve bank of India, Mumbai Port Trust, etc. It is doing all the functions such as deciding brokers, contracting with parties, for loading of cargo, dealing with labours for loading unloading, collecting the freight on behalf of the appellant, maintaining and operating bank account on behalf of the appellant; As per Clause 6 of the agency agreement entered into between the appellant and M/s Consolidated Cargo Services on 4-9-1997, unless mutually agreed, the agent shall not undertake directly or indirectly any business which may cause conflict with the

principals business interest, nor shall be the agent represent without prior approval of the principal any other common carrier feeder vessels or commercial company with whom the interest of the principal may come into conflict; The agent is required to provide suitable office space for one representative of the principal free of charge to the principal.

2.9 The above stated factual position brings out that the appellants case falls under article 5(l) of the DTAA when the business of the appellant is carried out through a fixed place through the agents in India wherein the agent was to maintain the office for the principals representative. Further, I also do not agree with the contention of the AR on not constituting a PE in this case through agent. It is an admitted position in this case that all the work of the appellant in India is carried out by its agents namely M/ s Consolidated Cargo Services. The Honble Mumbai D Bench of ITAT had an occasion to deal with a similar situation in the case of ACIT v. DHL Operations B.V. Netherlands (ITA Nos. 7987 and 7988/Bom./92) where the Honble ITAT has discussed the concept of Agency PE threadbare. The relevant portion of the said order is quoted hereunder: It is well-settled principle of law that the words in a statute or document take its colour from the context. When we keep in mind that the enquiry to be made is relating to the activities of the non-resident vis-a-vis the activities of the agent of independent status, it is not difficult to appreciate that the enquiry to be made as per paragraph 6 is not as to whether the agent is carrying on various activities other than the activity of being an agent of the non-resident but as to whether the entire activities relating to the non-resident are carried on wholly or almost wholly by the agent on behalf of the non-resident enterprise. In this case Airfreight Ltd. is an agent of independent status but it has carried on the activities of the respondent wholly in India. Therefore, paragraph 6 of article 5 is not applicable in this case. Therefore, the contention advanced on behalf of the respondent that paragraph 6 of article 5 applied to the case of Airfreight Ltd. and therefore paragraph 5 cannot be invoked to hold that the respondent has carried on its business activities through a permanent establishment in India is hereby rejected. In the final analysis, it is held that the respondent has carried on part of its business activities in India through its permanent establishment, namely Airfreight Ltd. within the meaning of article 5 paragraph 1 of DTAA as also article 5 paragraph 5.

2.10 Thus applying the above decision of the Honble ITAT also I hold that there exists a PE of the appellant in India. Accordingly I uphold the assessing officers action of denying the benefit of article 8 of the IndoMauritius DTAA and taxing the income under Section 44B of the Income Tax Act. This ground of appeal is decided against the appellant." Aggrieved by the above order, assessee is in appeal before the Tribunal.

9. Learned Counsel for the assessee submitted that the issue now stands squarely covered by the decision of the Honble Supreme Court in the case of Union of India v. Azadi Bachao Andolan (2003) 263 ITR 706.

Learned Counsel submitted, in this case the Honble Supreme Court held that Certificate of Residence issued by Mauritius authorities would constitute sufficient evidence and valid and within the powers of Central Board of Direct Taxes. Learned Counsel submitted exactly identical issues were before the Honble Supreme Court and decided in assessee's favour. This was a case arising out of the judgment of the Honble Delhi High Court. The Honble High Court quashed and set aside Circular No. 789, dated 13-4-2000 issued by the CBDT, by which certain instructions were given to the Chief Commissioners/ Directors General of Income-tax, with regard to the assessment of cases in which the Indo Mauritius Double Tax Avoidance Convention of 1983 applied. In this case the Honble High Court accepted the contention that the Circular is ultra vires the provisions of Sections 90 and 119 of the Income Tax Act, 1961 also otherwise bad and illegal. The order of the Honble High Court was set aside by the Honble Supreme Court and held that the Circular is valid learned Counsel further submitted that the Circular referred to above clarified certain points regarding taxation of income from dividends, etc.

10. In the Circular mentioned above it is clarified that wherever Certificate of Residence is issued by Mauritius authorities, such Certificate will constitute sufficient evidence for accepting the status of residence as well as beneficial ownership of the shares. This was challenged. Learned Counsel submitted, coming to the instant case of the assessee, the assessee had produced Tax Residency Certificate after compliance of the conditions, which have been

mentioned vide para 7 hereinabove. Hence, learned Counsel submitted that the issue is to be decided in assessee's favour.

11. On the other hand, the learned departmental Representative supported the orders of the revenue authorities and submitted that merely getting the company registered in Mauritius and obtaining Registration Number is not evidence to show that place of effective management is also situated in Mauritius. He particularly brought our attention to article 8(2), which states that "if the place of effective management of a shipping enterprise is aboard a ship, then it shall be deemed to be situated in the Contracting State in which the home harbour of the ship is situated or, if there is no such home harbour, in the Contracting State of which the operator of the ship is a resident." Hence, the learned DR submitted that it is also possible that effective management could be controlled from a third State other than the Contracting States; exactly as is in the instant case of the assessee. Learned DR also submitted that the assessee is having an exclusive agent and work through the agent, which amounts to PE. Assessee is thus having a fixed place of business, through which the business of the enterprise is wholly/partly carried on through CCS. CCS is prevented from having any similar agreement with competitors of the assessee and also CCS is to provide free of expenditure an office to a nominee/person of the foreign party.

12. Hearing the rival submissions, we are of the view that the issue has to go in assessee's favour, particularly in view of the decision of the Honble Supreme Court in the case of *Azadi Bachao Andolan* (supra).

Among other, one of the contentions taken before the Honble High Court (Delhi) was that the conclusiveness of a certificate of residence issued by the Mauritius tax authorities is neither contemplated under DTAC, nor under the Income Tax Act; whether a statement is conclusive or not, must be provided under a legislative enactment such as the Indian Evidence Act and cannot be determined by a mere circular issued by the CBDT. Another important contention taken was that "Treaty shopping" by which the resident of a third country takes advantage of the provisions of the agreement, is illegal and thus necessarily forbidden. These are the main two contentions and the reasons adopted by the Commissioner

(Appeals) in fact to reject assessee's contention.

Reading of the order of the assessing officer, it is clear that Tax Residency Certificate issued by the tax authorities of Mauritius in support of assessee's claim of resident status was rejected by the assessing officer and confirmed by the Commissioner (Appeals) mainly relying upon article 8(1) of DTAA between the Contracting States (India and Mauritius), wherein it speaks of the place of effective management assessing officer held and Commissioner (Appeals) confirmed that since only two Directors are of Mauritius and all other management are for name sake, in reality the benefit goes to a third country, which is not acceptable in view of article 8(1) of DTAA. Taking the benefit by a third country has been discussed by the Honble Supreme Court in the case of *Azadi Bachao Andolan* (supra) at pages 746 and 747, briefly, as under: Treaty shopping" is a graphic expression used to describe the act of a resident of a third country taking advantage of a fiscal treaty between two Contracting States. According to Lord McNair, "provided that any necessary implementation by municipal law has been carried out, there is nothing to prevent the nationals of third States, in the absence of any expressed or implied provision to the contrary, from claiming the right or becoming subject to the obligation created by a treaty" (Lord McNair, *The Law of Treaties*, page 336 (Oxford, at the Clarendon Press, 1961)).

Reliance is also placed on the following observations of Lord McNair: Lord McNair, *The Law of Treaties*, page 336 (Oxford, at the Clarendon Press, 1961): that any necessary implementation by municipal law has been carried out, there is nothing to prevent the nationals of third States, in the absence of any express or implied provision to the contrary, from claiming the rights, or becoming subject to the obligations, created by a treaty; for instance, if an Anglo-American Convention provided that professors on the staff of the universities of each country were exempt from taxation in respect of fees earned for lecturing in the other country, and any necessary changes in the tax laws were made, that privilege could be claimed by, or on behalf of, professors of those universities who were the nationals of third States." 13. In this case the Honble Supreme Court held that in the absence of specific exclusion of a third country taking the benefit by enactment of the Act, the revenue cannot do the same, which exactly the revenue authorities is

proposing to do in the instant case of the assessee. In view of the above, respectfully following the decision of the Honble Supreme Court in the case of Azadi Bachao Andolan (supra), we allow the claim of the assessee.

14. Since we allowed the appeal of the assessee on the first ground itself, it is not necessary for us to decide other alternative grounds.

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