IN THE HIGH COURT OF JUDICATURE, ANDHRA PRADESH
AT HYDERABAD
(Special Original Jurisdiction)

FRIDAY, THE FIFTEENTH DAY OF FEBRUARY,
TWO THOUSAND AND THIRTEEN

PRESENT

THE HON'BLE SRI JUSTICE GODA RAGHURAM
AND
THE HON'BLE SRI JUSTICE M.S. RAMACHANDRA RAO

W.P.Nos. 14212 of 2010, 3339 and 3358 of 2012

W.P.No.14212 of 2010

M/s.Sanofi Pasteur Holding SA,
represented by its Chairman, President
and Chief Executive Officer.

... PETITIONER

VERSUS

The Department of Revenue
Ministry of Finance,
Government of India,
New Delhi and others

... RESPONDENTS

Counsel for petitioners : Sri Aravind Datar, Senior Counsel
Sri Poras Kaka, Senior Counsel
Sri Ravi S, Senior Counsel
Sri Ch. Pushyam Kiran
Sri Thoom Srinivas
Ms. Divya Datla

Counsel for respondents : Sri Ponnam Ashok Goud
(Asst. Solicitor General),
Sri Mohan Parasaran, Additional
Solicitor General for India,
Sri S. Sasidhar Reddy (SC for Income Tax)

The Court made the following :

THE HONOURABLE SRI JUSTICE GODA RAGHURAM
AND
THE HONOURABLE SRI JUSTICE M.S. RAMACHANDRA RAO

W.P.Nos.14212 of 2010, 3339 and 3358 of 2012

COMMON ORDER : (*per* JUSTICE GODA RAGHURAM)

Competing narratives presented for consideration in these cases arise essentially out of the perception of Indian tax authorities - executors of the Indian – Income Tax Act, 1961 (the Act) that petitioners' claim for immunity (to tax under provisions of the Act; on a transaction involving sale of shares of a company registered and resident in France to another and similarly circumstanced corporate entity), is an Indian tax avoidance stratagem. Petitioners contend to the contrary.

An agreement between India and France *inter alia* for avoidance of double taxation, duly notified for effectuation in India (hereinafter more fully described and referred to as the Double Taxation Avoidance Agreement – the DTAA), also enters into the equation. Synergies between DTAA provisions and those of the Act; and how these inform the core issue - as to the liability to tax; and direct the allocation of the tax chargeable on the transaction in issue, to one or the other contracting State (India or France), is the quintessential problematic that falls for our consideration. In the context, we are of the considered view that a prefatory overview, of the origins and evolution of tax treaties and how these conflate, co-operate with domestic tax legislation and converge to signal a unified raft of applicable norms, is appropriate.

Tax treaties and domestic tax legislation : norms of co-existence :

International juridical double-taxation could generically be defined as imposition of comparable taxes in two or more States on the same tax-bearer in respect of the same subject matter and for identical periods. In recognition of the pejorative effect on exchange of goods and services and movement of capital, technology and persons, agreements/treaties/conventions/ protocols evolved for removing obstacles that double-taxation presents to development of economic relations between nations. Current international law permits taxation of foreign economic transactions when a sufficient nexus exists between the tax-payer and the taxing State, such as through residence, citizenship, habitual abode, *situs* of capital and the like. Normatively, customary international law does not forbid double-taxation, resulting from the interaction of the domestic laws of two or more States, as long as legislation of each of the concerned States is consistent with international law.

International law has yet to develop an adequate raft of norms to regulate the incidence of double-taxation by introduction of rules establishing which of the two or more States having a nexus with the transaction in question is entitled to the levy of tax, to what extent and other allied norms. A major component of this irritant phenomenon is therefore regulated by bilateral (or multi-lateral) double-taxation treaties. The concept of bilateralagreements between individual States for avoidance of double-taxation emerged towards the end of the 19th century. Only federally related or closely allied States were involved in the initial phase, of State-centric taxation regimes evolving organically to adapt to the accelerating pace of the globalizing and coalescing economic order.

The process gathered momentum after the 1st World War in Central Europe and spread to other areas in the western hemisphere. Efforts of the League of Nations also contributed substantially to assimilation of existing bilateral treaties and to the development of uniform model treaties. Efforts of the Organization for European Economic Co-operation (OEEC) and of its successor, the Organization for Economic Co-operation and Development (OECD) to develop a system for the avoidance of double-taxation picked up from where the efforts of the League ofNations tapered-off. Between 1956 and 1961, the OECD's Committee on fiscal affairs submitted a series of model treaty articles in four interim reports followed by a summary report in 1963. The OECD Council *inter alia* recommended that member States should continue efforts to enter bilateral double-tax agreements while adopting as a basis for their negotiations the model submitted by the fiscal committee and as interpreted by the commentaries in the report, while making allowances for the limitations and reservations in the commentary. The OECD complete model treaty and the commentaries thereon were revised from time to time. This process continues.

Double tax treaties are international agreements, their creation and consequences determined according to the rules contained in the Vienna Convention on the Law of Treaties, 1969 (VCLT). The conclusion of a treaty/convention is preceded by negotiations. States intending to conclude a treaty are represented by the appropriate level of executive, political or diplomatic expertise according to individual practices and judgment of the participant States. There are several steps in the negotiations phase eventually leading to conclusion of the treaty.

Treaties or conventions are thus instruments signaling sovereign political choices negotiated between States. The efficacy of a treaty over domestic law turns upon either State - specific conventions operating to govern the sovereign practices, or where there is a written Constitution provisions of that Charter. See Introduction[1]

Double-taxation treaty rules do not "authorize" or "allocate" jurisdiction to tax to the contracting State nor attribute the "right to tax". As is recognized by public international law and constitutional law, States have the original jurisdiction to tax, as an attribute of sovereignty. What double taxation treaties do is to establish an independent mechanism to avoid double taxation through restriction of tax claims in areas where overlapping taxclaims are expected, or at least theoretically possible. Essentially therefore, through the mechanism of a treaty, thecontracting States mutually bind themselves not to levy taxes, or to tax only to a limited extent, in cases where the treaty reserves taxation for the other contracting States, either wholly or in part. Contracting States thus and *qua*treaty provisions, waive tax claims or divide tax sources and/or the taxable object.

Unlike rules of private international law tax treaty norms assume that both contracting States tax according to their own law. Treaty rules do not lead to the application of foreign law. What treaty rules do is, to limit the content of the tax law of both the contracting States to avoid double-taxation. In effect, double taxation avoidance treaty rules merely alter the legal consequences derived from the tax laws of the contracting States, either by excluding application of provisions of the domestic tax law where these apply or by obliging one or both of the concerned States to allow a credit against their domestic tax for taxes paid in the other State. *Klaus Vogel* (supra) explains that rules of double taxation are thus not conflict rules, similar to that in private international law but are rules of limitation of law, comparable to those of international administrative law.

In India, Article 253 of the Constitution (fortified by a *non-obstante* clause *qua* the normal distribution of legislative powers in the Indian federal context set out in Part XI) authorizes Parliament power to make any law for the whole or any part or territory of India for implementing any treaty, agreement or convention with any other country or countries or any decision at any international conference, association or other body.

Article 253 read with Entries 13 and 14 of the Seventh Schedule would imply that in implementing a treaty, or a convention with another country or countries, or any decision made in an international conference, association or other body, the limitations imposed by Articles 245 and 246(3) are eclipsed and the total field of legislation is open to the Parliament, enabling Parliament to invade fields of legislation enumerated in List II as well, insofar as may be necessary for the purpose of implementing the treaty, etc., obligations of India - *Maganbhai Ishwarbhai Patel v. Union of India*[2]; *HM Seervai*[3] .

Our Courts have held that regard must be had to international conventions and norms while interpreting domestic law provisions, when there is no inconsistency between them and there is a void in the domestic law; that Courts are under an obligation, within legitimate limits to so interpret municipal law as to avoid confrontation with the comity of Nations or well-established principles of international law and where municipal law is not in variance with the international treaty - *Visakha v. State of Rajasthan*[4]; *Gramophone India Co. v. Birendra Bahadur Panday*[5]; and*RD Upadhyay v. State of Andhra Pradesh*[6].

However, this is not to say that a treaty must be given effect to without a law or in the absence of municipal law. Thus a treaty entered, to which India is a signatory cannot become a law of the land or be implemented unless Parliament passes a law referable to Article 253. Obligations arising under international agreements or treaties are not automatically binding. Thus, the trajectory of a municipal law would not be impeded or deflected, though at variance with provisions of a treaty unless Parliament enacts a law to provide dominant efficacy to treaty provisions.

Section 90 of the Act, in particular sub-section 2 thereof is a law made by Parliament referable to Article 253 read with Entries 13, 14 and 82 of List 1 of the Seventh Schedule. The provision (sub-section 2) enacts that where the Central Government has entered into an agreement with the Government of any other country under Sub-section (1) for grant of relief of tax or avoidance of double-taxation, then, in relation to the assessee to whom such grant applies, the provisions of the Act shall apply to the extent they are more beneficial to that assessee.

From the above very brief and broad-strokes analyses of the origins, evolution and trajectory of tax treaties and the *modus vivendi* of treaty provisions and domestic laws, we infer that the DTAA and the applicable domestic law - the Act are overlapping and competing magisteria. This would imply that full faith and credit (Article 261) and fidelity/respect [Article 51(c)] must be accorded to provisions of the DTAA, in as full a measure as to provisions of the Act. How that critical and delicate balance is achieved in the facts of the case before us, is the generic and substrating issue that is presented for consideration in these Writ Petitions.

1. The three writ petitions pertain to a tax dispute between the petitioners and the Indian Tax authorities (for short, 'the Revenue') in relation to the acquisition in August, 2009 by M/s.Sanofi Pasteur Holding SA, France (for short, 'Sanofi') of the entire share capital of M/s. ShanH SAS, France (for short, 'ShanH'), a Joint venture company, from its constituents M/s.Merieux Alliance, France (for short, 'MA') and M/s. Groupe Industriel Marcel Dassault (for short, 'GIMD'). As on the date of acquisition by Sanofi (of the entire share capital of ShanH), ShanH held about 80% of the shares in Shanta Biotechnics Ltd, Hyderabad (for short, 'SBL').

<u>The challenge in the writ petitions</u> :

2. <u>W.P.No.14212 of 2010</u> :

Sanofi assails the order dated 25-05-2010 of the 3rd respondent. The 3rd respondent (comprehended within the generic expression "the Revenue") determined the petitioner to be an "assessee in default" in respect of payments made by it to MA and GIMD for acquisition of the majority control/stake in SBL through transfer of ShanH shares, under Section 201(1) of the Act; determined the long-term capital gain at Rs.2625,73,98,171/-; and the consequent tax liability at Rs.594,99,26,425/-. The order also determined liability to interest, on the default of tax deduction at source at Rs.53,54,93,378/-, under Section 201(1A). A consequent notice of demand (also dated 25-05-2010), under Section 156 was served on the petitioner.

After issuing notice to the petitioner and receipt of its responses, a rectification order under Section 154 of the Act was passed on 15-11-2011 re-computing the long-term capital gain, tax thereon and the consequent interest. The total demand is now asserted at Rs.1058,06,83,952/-.

The substantive order dated 25-05-2010; the notice of demand of even date and the rectification order dated 15-11-2011, are challenged herein.

3. <u>W.P.Nos.3339 and 3358 of 2012</u> :

GIMD and MA are the respective petitioners. Pursuant to applications by the petitioners under Section 245Q-1 of the Act, the Authority for Advance Ruling (for short, "AAR" passed an order dated 28-11-2011. The AAR ruled (on a question presented by both petitioners) that the capital gain arising from the sale of ShanH shares (a French incorporated entity) by the petitioners (also French incorporated entities), to Sanofi (a French incorporated entity as well) is taxable in India in terms of Article 14(5) of the DTAA; that in view of this ruling, question No.2 (presented by MA) does not arise. Question No.2 presented by MA (without prejudice to Question No.1), was: *whether the controlling interest (assuming while denying that it is a separate asset) is liable to be taxed in France under Article 14-6 of the DTAA.*

The ruling dated 28-11-2011 by the AAR is challenged in these writ petitions.

Maintainability and scope of adjudication :

Counsel for the petitioners contended and the learned Additional Solicitor General for India (ASG) agreed that on principle and binding authority (vide *Columbia Sportswear Company v. DIT, Bangalore*[7]), the challenge to the order dated 28-11-2007 of the AAR could be presented before this Court u/A. 226 of the Constitution. In *Columbia Sportswear*, the Court ruled that the AAR being an authority and a body exercising judicial power conferred on it vide the provisions in Chapter XIX - B of the Act, is an authority (and a Tribunal) whose decision could be challenged under Articles 226 and/or 227 of the Constitution; and that such challenge should be heard directly by a Division Bench of the High Court.

Maintainability of these Writ Petitions, challenging the ruling dated 28-11-2011 of the AAR, is therefore neither contested nor is contestable.

Counsel for the respective parties specifically urged that in the facts and circumstances of the case and the legislative objective and purposes substrating the provision for an advance ruling mechanism (i.e., expeditious determination), this Court should also adjudicate and record findings on the merits of the questions presented by the petitioners and on which the impugned ruling is issued; and not merely set aside the AAR ruling (if found erroneous and unsustainable) and order a remit for *de novo* consideration by the AAR.

In the light of the authority of *Columbia Sportswear* (holding that the decision of AAR could be challenged under Articles 226 and/or 227), observations in the Constitution Bench decision in *H.V. Kamath v. Ahmad Ishaque and others*[8](to the effect that while in *certiorari* the High Court could only annul the erroneous decision of an inferior Tribunal, it could while exercising (supervisory) jurisdiction under Article 227 also issue further directions in the matter; and in the light of the conjoint plea by the respective parties (adverted to supra), in the event we hold that the impugned ruling of the AAR is erroneous to a degree susceptible to judicial and/or supervisory review under Articles 226/227 and is on such review unsustainable, we would quash the impugned ruling exercising *certiorari* and, if need be, issue appropriate declarations/directions, particularly since expeditious disposition is the uncontested legislative purpose underlying the provision of an Advance Ruling Authority, in Chapter XIX – B of the Act.

4. A brief account of SBL, MA, GIMD and Sanofi :

SBL : a company incorporated under the Companies Act, 1956 on 10-03-1993, having its registered office at Hyderabad,India. SBL is *inter alia* engaged in the business of research and development of technologies for pharmaceutical products, including bio-pharmaceuticals, life-saving drugs, employing genetic engineering and polymer-chain reaction technology; and carrying on the activity of research and development of laboratories and designing DNA probes; and commercialization of products developed with in-house research or otherwise.

SBL was initially set up by, Mr. K.I. Varaprasada Reddy (VR). United Overseas Investment Limited (UOIL) became a shareholder of SBL pursuant to a financial collaboration agreement dated 17-02-1994 executed between VR, SBL and

UOIL. H.E. Yousuf Alawi Abdullah along with his associates (hereinafter, 'H.E.') held approximately 92% and Mr. Khalil Ahmed approximately 8% of the issued and paid up share capital of UOIL. UOIL was set up in Mauritius as a special purpose investment vehicle and held a major shareholding in the issued and paid up share capital of SBL (see the shareholders' agreement dated 07-11-2006 between MA, SBL, Mr. K.Ahmed and UOIL.

On 06-11-2006 a share purchase agreement (SPA) was entered into for purchase of 89,96,750 SBL shares - (analyses of this SPA will be considered hereinafter). As on the date of the SPA the shareholding pattern in SBL was :

1. UOIL - 46.05%
2. H.E. Shaikh Ghassan I. Shaker - 0.46%
3. V R and Family - 17.94%
4. Mr. Khalil Ahmed - 1.36%
5. Others - 34.19%

On completion of this SPA (entered into between MA, SBL, HE and 1 to 4 above), the shareholding of SBL stood altered as:

1. United Overseas Investment Limited (UOIL) - 4.09%
2. ShanH - 61.38% (a company registered and resident in France and at this stage a wholly owned subsidiary of MA)
3. V.R. and Family - 17.94%
4. Mr. Khalil Ahmed - 1.36%
5. Others - 15.21%

(vide Schedule I Part B of the SPA dt.06-11-2006)

MA : the holding company of Alain Merieux family is active and engaged in four core areas - (a) In-vitro diagnostics (through a subsidiary bioMerieux, France) wherein MA holds 58.9% shares; (b) food and quality nutrition (through a subsidiary, SGH France) which in turn holds 87.3% shareholding in Sillikar Group USA; (c) immunology and therapeutic vaccines, operating in developed countries, (through a subsidiary, TSGH France) wherein MA has 94.9% shareholding. TSGH France operates through ABL, USA and Transgene, France, wherein TSGH France has 56.68% shareholding; and (d) Prophylactic vaccines in emerging countries operated through ShanH (a French resident entity), now a joint venture wherein MA has 80% shareholding.

GIMD:a separate business conglomerate registered in France engaged in various businesses such as Defense Systems,Avionics and the like. Even earlier to association with MA in ShanH, GIMD was an investor along with MA in ABL,USA and Transgene, France. GIMD invested in 20% shareholding of ShanH while MA held the other 80%.

5. Preview of evolution of ShanH : :

- During August/September, 2006, MA was negotiating with GIMD, inviting the latter for a strategic association for investment in SBL through a holding structure (emails dated 10-08-2006, 18-08-2006, 08-09-2006 and 23-11-2006 - between MA and GIMD representatives and law advisor of GIMD).
- Pursuant to the 26-10-2006 meeting of the MA Board, resolving to allow ShanH (a contemplated MA subsidiary) to acquire 54% share of SBL, ShanH was incorporated on 31-10-2006 and registered in the home jurisdiction (theFrench Republic), with MA as the sole and unique shareholder holding a nominal share capital of 370 shares, of a value of €37,000/-.
- 31.10.2006 - meeting of ShanH shareholders (with MA as the "unique shareholder"), presided over by Mr.Michel Dubois CEO, decided :
  - (i) to appoint Mr.Philippe Sans (who previously served as the President and CEO of Bio Merieux NorthAmerica) as the Chairman of the Board of ShanH;
  - (ii) to acquire the shares of SBL;
  - (iii) to confer on him powers to represent ShanH, either individually or along with Mr.Michel Dubois or Ms. Dominique Takizawa for negotiations, conclusion and drawing up of necessary agreements for theacquisition; and
  - (iv) to sign a housing agreement in Lyon with MA.
- On 02-11-2006 and 03-11-2006, Escrow agreements were entered into with Calyon Bank, Lyon and with Blom Bank, Geneva, by ShanH and UOIL to facilitate sale of UOIL shares to ShanH. The agreements reveal that consideration for purchase of the UOIL shares flowed from ShanH.
- 06.11.2006 - UOIL, MA, SBL, H.E. VR and family, Mr.Khalil Ahmed and H.E. Shaik Ghassan I Shaker, entered into a Share Purchase Agreement (SPA) envisaging sale by UOIL to MA of 89,96,750 SBL equity shares held by UOIL so that MA may cause ShanH or any other wholly owned subsidiary to purchase the said shares.
- 07.11.2006 - shareholders agreement (SHA) entered into between MA, SBL, VR and family members.
- 07.11.2006 - another SHA between MA, SBL, Mr. Khalil Ahmed and UOIL.
- The two SHA's enumerate the *inter se* rights of parties thereto, relating to transfer of shares, right of first refusal, tag-along rights, put option, etc., on acquisition by MA of UOIL's SBL shares.
- ShanH acquired SBL shares representing 61.4% of the registered capital and voting rights of SBL, on 07-11-2006.
- After ShanH incorporation on 31-07-2006 and its acquisition of SBL shares, GIMD decided to subscribe to a minority interest in ShanH, on the basis of information transmitted by MA.
- 08.03.2007 - The ShanH partnership agreement between MA and GIMD, in the presence of ShanH.
- To ensure liquidity of its investments, GIMD as a strategic investor suggested introduction of ShanH on a stock exchange for transfer of its shares or for the takeover/merger by a listed company within four to six years from the date on which the partnership agreement was entered into between MA and GIMD (i.e., 08-03-2007).

- ShanH share capital was increased to 5,99,630 shares of which MA subscribed to 4,79,630 shares and GIMD to 1,20,000 shares as on 12-03-2007.
- On 25-03-2009 ShanH capital was increased by 1,00,000 shares (to 7,00,000) contributed by MA and GIMD in the 80:20 ratio.
- ShanH (now a joint-venture (JV) of MA and GIMD) acquired 20,000 shares of UOIL; 17,500 shares from Indian resident shareholders and 4,23,600 shares from non-resident shareholders of SBL in 2007; and a further 1,90,640 shares from UOIL, 10,78,920 shares from Indian resident shareholders and 14,57,150 shares from non-resident shareholders of SBL, in 2008.
- During March, 2008, a capital increase in SBL by 4,49,830 shares were subscribed directly by ShanH, which remitted US $5,000,000 to SBL towards advance and share application money (vide certificate of foreign inward remittance, dated 08-03-2008 issued by IOB, Chennai).
- 05.05.2009 - shareholders agreement executed pursuant to which Mr. Georges Hibon purchased 10,400 shares from MA and 2,600 shares from GIMD. After this transaction, of the 700,000 shares of ShanH, 78.5% held by MA; 19.6% by GIMD and 1.9% by Mr. Georges Hibon.
- July and August, 2009 - ShanH purchased a further 5,57,500 shares from UOIL and 2,00,000 shares from Indian Resident shareholders of SBL.
- For 2006-07, 2007-08 and 2008-09, SBL remitted dividends to ShanH account in Calyon Bank, Lyon, (vide copies of statements issued by IOB, Hyderabad Branch, dated 11-10-2007, 25-11-2008 and 21-07-2009).
- By July, 2009, ShanH held about 78.75% of the SBL share capital and voting rights. MA, GIMD and Mr. Georges Hibon owned the 7,00,000 shares of ShanH representing 100% of the authorized and issued share capital of ShanH.

FIPB approved ShanH purchase of SBL shares :

- Vide SBL application to FIPB dated 22-09-2006; FIPB proceedings dated 13-06-2007; ShanH application to FIPB dated 12-04-2007; SBL application to FIPB dated 18-04-2007; and FIPB letter to SBL dated 13-06-2007.
- 08-07-2009 - SBL intimates FIPB that ShanH holds 78.75% of its shares.

Custody agreement with HSBC Ltd. :

- 16-04-2008 - Custody agreement between ShanH and HSBC Ltd. for designating HSBC as agent of ShanH for holding and dealing with seller's documents in Escrow, in relation to ShanH intending to purchase approximately 15% of SBL shares from SBL shareholders.

SPA - between GIMD, MA and Sanofi :

10-07-2009 - SPA entered into between MA/GIMD as the sellers and Sanofi as the buyer, in respect of ShanH shares. The covenants, warranties and terms of this agreement (relevant and material for the purposes of this *lis*) are:

(i) ShanH is a company registered and resident in France with a share capital of €70,000,000.00; SBL is an Indian resident and registered company with a share capital of Rs.160,439,100/- and a subsidiary of ShanH which owns 12,634,210 shares representing about 78% of the share capital and voting rights of SBL. As on the date of the SPA (10-07-2009), the sellers (MA and GIMD) along with Mr.Georges Hibon own 700,000 shares of ShanH, representing 100% of the issued and outstanding share capital of ShanH, holding 78.51% (MA); 19.63% (GIMD) and 1.86% (Mr.Georges Hibon).

(ii) MA and GIMD shall acquire the shareholding of Mr.Georges Hibon in ShanH so that eventually MA would own 80.37% and GIMD 19.63% of the issued and outstanding SBL share capital;

(iii) MA and GIMD shall sell, convey, assign, transfer and deliver to Sanofi, 100% of the issued and outstanding share capital of ShanH for a consideration of €550,000,000.00.

(iv) On closure of the transactions contemplated by the SPA, the sellers (MA and GIMD) shall deliver or cause to be delivered to Sanofi :

(a) the original and duly completed (by MA and GIMD), executed and dated share transfer forms pertaining to the transfer of the MA and GIMD shares to Sanofi;

(b) originals of the share transfer register and shareholder accounts of ShanH and the SBL share certificates held by ShanH, at the closing date; and

(c) other specified documents in original or certified copies to effectuate transfer of the entire ShanH shareholding to Sanofi *qua* existing entitlements, rights or interests of MA, GIMD or Mr.Georges Hibon under the Articles of Association of ShanH or the SHA's, dated 08-03-2007 (between MA and GIMD) and dated 05-05-2009 between GIMD and Mr.Georges Hibon.

- Article II of the SPA sets out joint warranties by MA/GIMD to Sanofi - that MA, GIMD and ShanH are corporations duly organized and validly existing under the laws of France and inhere the requisite corporate power and authority to own respectively the shares of ShanH; and that ShanH is duly qualified to conduct business under laws of the jurisdiction of incorporation (France).
- Article VIII (S.8.1) incorporates the assurance that the sellers and the buyer shall use their best efforts towards completion of sale of Shantha West (an SBL subsidiary).
- It is however represented (at the hearing before this Court) that the sale of Shantha West has not occurred.
- Article IX sets out a confidentiality agreement whereunder Sanofi acknowledges that the confidential proprietary information or documents provided to it or any of its affiliates pursuant to this SPA shall be "Confidential Information" subject to the confidentiality agreement dated 12-02-2009 (entered into between Sanofi and MA); and that the SPA and the confidentiality agreement shall constitute the entire agreement between Sanofi and its affiliates on the one hand; and MA, GIMD and when relevant their affiliates on the other, with respect to the subject matter of the SPA.
- The SPA was signed by representatives of MA, GIMD and Sanofi.

6. <u>Revenue assessed ShanH u/S.201(1) of the Act</u> :

- 04.08.2009 : Survey u/S.133A of the Act in SBL office premises (on Revenue's assumptions based on newspaper reports that Sanofi is to acquire more than 80% stake in SBL from ShanH, referred to as a subsidiary of MA); that the acquisition attracts provisions of TDS u/S.195 of the Act; and that ShanH had originally acquired stake in SBL in November, 2006, by acquiring shares from different non-residents, payments relating to which also attract the provisions of Section 195. The survey revealed (on verification of the Memorandum of Share Transfer register of SBL) that ShanH made payments totaling Rs.359.87 crores, Rs.20.6 crores and Rs.82.12 crores during FY 2006-07, 2007-08 and 2008-09 respectively, to various NRI's for purchase of SBL shares.
- 14.12.2009 : The Revenue [Dy. Director of IT (INTL TAXN)-II Hyderabad], passed two orders for FY 2007-08 and 2008-09, both bearing reference Nos.DDIT(IT)-II/Order 201/2009-10, u/S.201(1) of the Act, against ShanH. The orders determined the tax and interest liability, as specified therein. Revenue accepted ShanH to be the purchaser of SBL shares (after survey and verification of relevant documents).

- Significantly Revenue accepted the claim that sale of SBL shares held by UOIL (to ShanH) is not liable to tax in India, as the withholding tax provision (Section 195) is inapplicable in view of the Indo-Mauritius Tax Treaty.
- Consequent notices of demand of even date were issued to ShanH. ShanH asserts to have paid the tax and claims that there is no tax due against ShanH on this account. There are however appeals, stated to be pending, before the ITAT.

7. MA and GIMD seek Advance ruling :

- 20.11.2009 : MA and GIMD filed separate applications before the Authority for Advance Rulings (AAR), u/S.245Q(1) of the Act for an advance ruling on two questions, viz.:-

  Question (1):

  In terms of the provisions of the double taxation avoidance treaty dated 6th September, 1994, as amended from time to time, entered between the Republic of India with the Government of French Republic ("Indo-French Tax Treaty") read with Section 9o of the income Tax Act, 1961, whether the Capital gains arising from the sale of shares of ShanH (French Incorporated Entity) by the Applicant (French incorporated Entity) to Sanofi (French incorporated Entity) is liable to tax in France or in India.

  Question (2):

  Without prejudice to above, whether controlling interest (assuming while denying that it is a separate asset) is liable to be taxed in France under Article 14 (6) of the Indo — French Tax Treaty?

  GIMD raised only the first question and sought a ruling thereon.

- 17.12.2009 : AAR admitted applications by MA and GIMD seeking advance ruling , ruling that the applications are not hit by proviso to Section 245(R)(2) of the Act; and directed issue of notice to the parties, for hearing.

Revenue's challenge to the order dated 17-12-2009 of AAR :

- Assailing the order of the AAR dated 17-12-2009 (admitting the applications of MA and GIMD, for a ruling on merits), Revenue filed W.P.Nos.18132 and 18133 of 2010. By the Order dated 25-03-2011 two learned Judges of this Court (comprising the Division Bench) differed on whether the issue of admissibility must be determined as a preliminary issue [i.e., with regard to the threshold bar under the 1st proviso to Section 245R(2)], by recording reasons in writing; and whether Revenue is entitled to a hearing before an application seeking advance ruling is admitted. One learned Judge concluded that the AAR was not required to decide as a preliminary issue the threshold bar nor is required to record reasons while admitting an application for a further examination leading to an advance ruling or for refusing to do so on the ground of the bar. The other learned Judge concluded to the contrary and on the further ground that as Revenue was not intimated by the AAR as required u/5.245R(1) and the order admitting the applications was bereft of reasons, the same should be quashed. The matter was referred to a third learned Judge, for resolving the conflict of opinion.
- The reference was answered by the final order dated 15.07.2011. This Court ruled that if the AAR admits anapplication for pronouncing an advance ruling, recording of reasons at that stage is not required nor is hearing of the Revenue contemplated. Only on admission of an application and before pronouncing the advance ruling, is hearing of the Revenue provided, if the AAR considers it so necessary but not at the

threshold stage, of admitting the application. The writ petitions by Revenue were dismissed.

- 08.07.2010: AAR considered the representation of the CIT and objections of the Department as to admissibility of the applications by MA and GIMD (for advance ruling), found no compelling reason to revoke the earlier order of admission (dated 17.12.2009) and posted the applications for hearing on merits u/S.245(R)(4).
- 03.08.2010: AAR recorded its anguish that there is an apparent attempt on the part of the CIT to defeat or delay the remedy invoked (for advance ruling); and observed that such strategies would have a pejorative impact on the image of tax administration in the country.

8. Sanofi is assessed to tax on purchase of ShanH shareholding :

- 07-08-2009: letter to MA addressed by the Deputy Director of Income Tax (International Taxation)-I, Hyderabadin respect of proposed sale of its shares to Sanofi, details sought.
- 26-8-2009: MA responded stating that : (a) the proposed transaction - the transfer of shares to Sanofi would not involve any transfer of shares of SBL, which will remain under the control of its current majority share holder i.e., ShanH; (b) the deal with Sanofi is not concluded and is under discussion; (c) details of acquisition of SBL shares by ShanH are not relevant; (d) provisions of the Act are inapplicable; (e) MA holds no shares in SBL nor had received any dividends from SBL; and (f) MA is not directly involved in the control and management of SBL.
- 17-09-2009: the Deputy Director of Income Tax (International Taxation) - II, Hyderabad issued notice to Sanofi contending that: (a) Sanofi had paid consideration to MA for purchase of shares in Shan H, which owned a majority stake in SBL; (b) MA made a substantial gain on disposal of their investment and controlling rights in SBL, an Indian Company; (c) such gain is a direct result of realization of "investment" of MA in India by its sale to Sanofi; (d) the same is chargeable to tax in India as under Section 9 (1) (i) of the Act, income accruing indirectly through or from any business connection in India is deemed to accrue or arise in India; (e) under Section 195 of the Act, Sanofi should have deducted tax at source on the payment made to MA; (f) Sanofi should show cause under Section 201 (1) of the Act, why it be not treated as an assessee in default, of the tax liability of MA in India in respect of the gains made by MA from disposal of its investment in India; and (g) Sanofi should submit various agreements and details of the transactions with MA.

- 20-10-2009: Sanofi responded, contending that :(i) provisions of the Act do not apply to the transaction ofpurchase of shares of ShanH, a French Company in France by Sanofi, another French Company from MA and GIMD, both French companies; (ii) provisions of the Act have no extra territorial operation; (iii) Indian tax authorities have no jurisdiction to require it, a non-resident, to deduct tax in respect of payments made outside India; (d) Sanofi cannot be treated as an assessee in default; and (e) under the DTAA, the transaction would be subject to tax in France and not in India. Sanofi furnished other details sought by Revenue.
- 09-11-2009, 10-11-2009 and 11-11-2009: Revenue recorded sworn statements of Sri N.Rajasekhar, CFO of SBL, Sri K.I. Vara Prasada Reddy, M.D of SBL and Mr.Khalil Ahmed, Executive Director of SBL, respectively.
- 17.11.2009: The Directorate General of Public Finance, France, on MA's request issued a letter stating that MA, having sold its share holding in the capital of ShanH (a French company) amounting to 80.37%, the resulting profit would be subject to corporation tax in France vide Article 209-I of the General Fiscal Code of France and as per Article 14.5 of the DTAA.

- 19.02.2010: Revenue issued a further and elaborate show-cause notice refuting the stand of the Sanofi and sought explanation why Sanofi be not deemed an assessee in default u/S.201(1) for failure to comply with the statutory liability of TDS u/S.195(1).
- 11.03.2010: Sanofi sought further time till 31.03.2010.
- 26.03.2000: Sanofi submitted a detailed reply to the show-cause notice dated 19.02.2010 and sought opportunity to cross-examine Mr.Khalil Ahmed.
- 31.03.2010: Revenue responded stating that opportunities to cross-examine Mr. Khalil Ahmed were not earlier availed; and granted time to Sanofi to secure other statements recorded u/S.131. By letter dated 08.04.2010 Sanofi (after collecting statements of other persons recorded u/S.131, i.e., N. Rajasekhar and VR), sought time to make submissions and to furnish written submission by 15.04.2010 and for a personal hearing from the Revenue.
- 05.05.2010: Revenue intimated Sanofi of scheduling the hearing to 10.05.2010. On 10.05.2010 Sanofi sought time and requested re-scheduling the hearing to 21.05.2010 or later.
- 21.05.2010: Hearing of Sanofi's liability to tax.

- There is a dispute between Sanofi and Revenue with regard to whether adequate and reasonable opportunity was provided to Sanofi. During hearing of Sanofi's writ petition (W.P.No.14212 of 2010) counsel referred to averments in the writ petition to assert that on 21.05.2010 Sanofi's counsel sought leave to make further submissions on 22.05.2010 and 23.05.2010 (Saturday and Sunday); that this request was not considered by the Revenue; that Sanofi's counsel was directed to conclude arguments within an hour on 21.05.2010; and having no alternative Sanofi filed a letter dated 25.05.2010 in the Office of the Presiding Officer on26.05.2010 setting out circumstances in which Sanofi was disabled from concluding its arguments in respect of legal submissions and seeking further opportunity.

- 25.05.2010: Assistant Director of Income-Tax (Intl.Txn.) - II, Hyderabad, passed an order u/S.201(1)/(1)A of the Act. Sanofi was held liable to tax and interest on long-term capital gain at Rs.5,94,99,26,425/- and interest (from 01.09.2009 to 25.05.2010 at Rs.53,54,83,378/- in all Rs.6,48,54,09,803/-). A notice of demand u/S.156 of the Act of even date was also issued.

- 15.11.2011: After a due process, a rectification order was issued re-determining the long-term capital gains tax at Rs.8,33,12,47,206/- and interest for twenty-seven months (September, 2009 to November, 2011) at Rs.2,24,94,36,746/- The total amount set out being Rs.10,58,06,83,952/-.

- W.P.No.14212 of 2010 by Sanofi challenges the order of assessment dated 25.05.2010, the consequent demand notice of even date and the rectification order dated 15.11.2011 (vide amended relief as per order dated 28.08.2012 in W.P.M.P.No.39713 of 2011).

9. <u>Conclusions of the impugned AAR ruling</u> :
:

(a) The transaction of sale of shares by GIMD/ MA in Shan H to Sanofi is commercially real. A permissible commercial scheme was adopted to acquire the shares, the underlying assets and control of the Indian Company (SBL). It is not necessary to ignore the existence of Shan H to come to a conclusion that ShanH was a facade in the context of tax law and would amount to a scheme for avoidance of tax;

(b) Though facially the transaction is taxable in France and as earlier concluded commercially real and taken step by step valid, the scheme or the scope of the transaction could nevertheless be considered as a whole on the point of view of taxation. So viewed, it is a scheme for avoidance of tax in India. In substance what is dealt with are the underlying assets and the controlling interest in SBL. The transfer of ShanH shares may have commercial and business efficacy or validity. That however, does not prevent the authority from looking at the transaction in the context of the Act/DTAA and assessing its efficacy from the point of view of taxation;

(c) The legal validity of a transaction or the adoption of a series of transactions commonly used like creating a fully owned subsidiary for making such investments in another country, cannot stand in the way of the question being asked whether it is acceptable in the context of the taxing statute;

(d) The transaction of transfer of shares of Shan H would amount to transfer of assets of SBL, an Indian Company, if not of its shares formally; and this is a scheme for avoidance of tax in India;

(e) While the decision in *Azadi Bachao Andalan* is binding on this authority it may not be the final word when the authority is approached for an advance ruling. *Azadi Bachao Andalan* incorrectly proceeds on the basis that the views expressed by Chinappa Reddy, J (in *McDowell and Co. Ltd*.) are his own and do not represent the view of the Court as a whole. The view that has emerged in England is that notwithstanding the legal validity of a transaction or a set of transactions, if the purpose was to create a legal smoke-screen to avoid the payment of tax that would legitimately be due as having arisen on the basis of a transaction or an event, the legal efficacy of the transaction in the context of the taxing statute, has to be considered, notwithstanding its reality or validity. (emphasis is added)

(f) After observing that *Azadi Bachao Andolan* incorrectly appreciated the *ratio* of *McDowell*, AAR concluded that there was a reversal of curial opinion in England; and referring to *IRC v. Burmah Oil Company Ltd*[9] and *HMRC v. Tower MCashBack LLC*[10] concluded that notwithstanding the legal validity of a transaction or set of transactions, if the purpose was to create a legal smokescreen to avoid payment of tax that would legitimately be due and having arisen on the basis of a transaction or an event, the legal effect of the transaction in the context of the taxing statute, has to be considered,notwithstanding its reality or validity.

(g) The AAR concluded that the relevant sequence of events (MA investing in acquisition of SBL shares through a subsidiary ShanH; eventually acquiring a controlling interest, the shares having been acquired in the name of ShanH; subsequently GIMD coming on to acquire a 20% equity in ShanH; shares in SBL being the only asset of ShanH with no other business; and eventually MA and GIMD offloading shares in ShanH to Sanofi) is a process whereby what really passed is the underlying assets and control of SBL an Indian company; a gain is generated by this transaction; and by repeating the process the control over the Indian assets and business can pass from hand to hand without any liability to tax incurred under the Act, if the transaction were accepted at face value. Further held that it is not necessary to ignore the existence of ShanH to come to the conclusion that the series of transactions is a façade in the context of the tax law and would amount to a scheme for avoidance of tax and in that view, the fact that GIMD and Mr.Georges Hibon held shares in ShanH would not make a difference.

(h) On question No.1 mentioned above, held that the transaction of sale of shares by GIMD/MA in Shan H to Sanofi is taxable in India in terms of Article 14(5) of the DTAA; and

(i) The second question posed by MA in its application No.847 of 2009, did not arise in view of the ruling on question No.1.

(j) AAR also held that clause (iii) of Section 245 R (2) of the Act would apply and that it accordingly declines to rule on the questions raised.

10. Heard Sri S.Ravi, learned Senior Counsel for the petitioner (Sanofi) in W.P.No.14212 of 2010, Sri Arvind Datar, learned Senior Counsel for the petitioner (GIMD) in W.P.No.3339 of 2012, Sri Porus Kaka, learned Senior Counsel for the petitioner (ShanH) in W.P.No.3358 of 2012 and Sri Mohan Parasaran, the learned Additional Solicitor General for India (ASG) for the Revenue /respondents. We have considered the legal and factual submissions presented and the pleadings and documents filed in the respective writ petitions.

11. Learned counsel for the respective parties advanced extensive arguments; referred to several instruments andprecedents to support the respective contentions. We will deal with the several propositions, contentions and citations during our analyses to follow.

12. Sri Porus Kaka summarized the legal submissions on behalf of MA (W.P.No.3358 of 2012) into the following propositions (summary of oral argument and written submissions) :

<u>Propositions on behalf of MA</u> :

(i) *Qua* Section 90 of the Act read with relevant provisions of the DTAA, the capital gains in the transaction in question is taxable only in France;

(ii) Only Article 14(4) of the DTAA accommodates/permits a limited "see through", not Article 14(5);

(iii) Neither in law nor *qua* Article 14 of the DTAA could an asset held by a company be treated as an asset held by a shareholder;

(iv) Controlling interest is not a separate asset, independent of the shares;

(v) Assuming while denying that the controlling interest over SBL by ShanH could be viewed as a separate right or asset, [independent of the shares not falling under Article 14(5)], even so the *situs* of the controlling interest is also located and taxable only in France under Article 14(6) of the DTAA;

(vi) AAR ruling is flawed on account of incorrect reference to the (foreign) decision – *Tower MCashBack*;

(vii) The AAR ruling is contrary to settled legal principles and erroneous;

(viii) There being no cost of acquisition determinable for controlling rights and underlying assets, no date of acquisition nor there being any part of the consideration apportionable to these rights, the computation provision of capital gains would fail and taxing the transaction on the underlying assets theory would be inoperative;

(ix) The principles propounded/affirmed in *Vodafone International Holdings BV vs. Union of India*[11] and in *Union of India v. Azadi Bachao Andolan*[12] continue to hold the field and capital gains arising from the transaction would be liable to tax only in France under the DTAA and provisions of the Act; and immune to levy of tax under the Act;

(x) By its ruling dated 28-11-2011 (impugned in W.P.Nos.3339 and 3358 of 2012), AAR reviewed its earlier order dated 17-12-2009 admitting the applications of MA and GIMD seeking advance ruling. The admission order was reiterated by the subsequent order dated 03-08-2010 as well. Revenue challenged the order dated 17-12-2009 unsuccessfully and the High Court by its final order dated 15-07-2011 dismissed the challenge to the AAR admission order, dated17-12-2009 (in W.P.Nos.18132 and 18133 of 2010, preferred by the Revenue). The AAR has neither the power to review its order of admission (of the applications) nor is authorized to do so in view of the decision of this Court, dated 05-07-2011.

13. ASG summarized the legal submissions on behalf of Revenue into "core issues" and "questions" arising therefrom, by written submissions supplementing oral argument.

Issues and questions arising therefrom formulated by Revenue :

The generic contentions :

(a) On analyses and a holistic consideration of the several transactional documents, surrounding circumstances,conduct and intent of the parties, in substance, the transaction (involved in the SPA dated 10-07-2009 betweenMA/GIMD and Sanofi) was exclusively for acquisition of the control, management and business interests in SBL, the Indian company. The transaction was not merely a divestment of ShanH shares (a French company) butresulted in transfer of capital assets in India wherefor capital gains had arisen to MA/GIMD in India.

(b) In the facts and circumstances of the transaction, provisions of the Act apply to the transaction in terms of DTAA provisions and the right to tax the transaction stands allocated to India, under Article 14(5) thereof. On this view of the matter there is no conflict between provisions of the Act [pursuant to the retrospective amendments vide the Finance Act, 2012 (Act No.23 of 2012)] and provisions of the DTAA.

Determinations necessitated in the light of the above contentions by Revenue :

1. Who is the real owner of SBL shares?

(a) Had ShanH a distinct corporate status, so as to be the legal/beneficial owner of SBL shares?

(b) What was the extent and degree of control of MA/GIMD over ShanH, in the context of the SPA, SHA's and other transactional documents?

(c) Did SBL shares vest with ShanH as the legal owner thereof from the inception of the transfer of shares (in2006); and was there ever an assignment by MA/GIMD (of SBL shares) in the light of the transactionaldocuments?

2. Is the corporate status of ShanH immune to enquiry as to its commercial substance merely on account of ShanH being a joint venture?

3. What is the subject matter of the transaction involved in the SPA dated 10-07-2009 between MA/GIMD and Sanofi? and

4. Who transferred the right, title and interest in SBL shares and realized the capital gains on the transfer of the SBL shares?

14. According to Revenue :

The case of Revenue as predicated on its interpretation of the transactional documents, leading to and including the SPA dated 10-07-2009 (between MA/GIMD and Sanofi), may be noticed :

- In substance the transaction involved in the SPA dated 10-07-2009 was only for acquisition of the control, management and business interests in SBL, the Indian company and was not a mere divestment of ShanH shares, a French company. As a result, capital assets in India were transferred and capital gains had accrued to MA/GIMD, in India.

- The transaction is taxable in India since that right is allocated to India, under Article 14(5) of the DTAA.
- There is no conflict between provisions of the Act pursuant to the retrospective amendments carried out by the Finance Act, 2012 and the DTAA.
- Provisions of the Act, on the facts of the case are squarely applicable to the transaction in terms of the provisions of DTAA itself, as the right to tax the transaction is allocated to India in terms of Article 14(5).

Inferences from SPA, SHA's and SBL's amended AOA :

(i) ShanH is a company of no substance;

(ii) is neither the legal nor beneficial owner of SBL shares;

(iii) is not an assignee of MA in respect of SBL shares;

(iv) ShanH made no payments for acquisition of SBL shares; subsequent accounting of the purchase consideration as a loan from MA, at a later date is of no consequence;

(v) ShanH had no control over SBL management nor enjoyed any rights and privileges in SBL as a shareholder;

(vi) ShanH is at best a nominee of MA in relation to SBL shares.

Re chargeability under Article 14(5) of the DTAA :

- Since ShanH is not a company with an independent status and is only an *alter ego* of MA/GIMD, the latter is the legal and beneficial owner of SBL shares. The transaction involved in the SPA dated 10-07-2009 (between MA/GIMD and Sanofi) is acquisition of SBL shares.
- Only MA /GIMD participated directly in SBL, in its capital, control and management and such participation was more than 10%.
- On conclusion of the transaction contemplated by the 10-07-2009 SPA, MA/GIMD realized the gain on alienation of shares representing participation of more than 10% in the capital, control and management of SBL (an Indian company). The gains are thus chargeable to tax in India, in terms of Article 14(5) of DTAA.
- Double Taxation Avoidance Agreements allocate taxing rights to the country of residence or of source; or to both. Once the source country gets the right of taxation, domestic law provisions operate to bring to tax, reference income in the source country.
- Since the source country derives the right to tax the gains arising from alienation of shares of a company located within its territory, it is immaterial whether such gains are

realized by "disposal of asset" or "deemed disposal of asset". DTAA provisions would apply in both cases and the source country inheres the right to tax such gains.

- For a proper and purposeful construction of DTAA provisions, the expression "alienation of shares" in Article 14(5) must be understood as direct as well as indirect alienation.
- The expression "alienation" is not defined in the DTAA. Therefore in terms of Article 3(2), the expression would derive its meaning from domestic law. Domestic law comprehends disposal of capital assets within the meaning of the word "transfer" [u/S.2(47) of the Act]. Since transfer is widely defined in Section 2(47) of the Act to cover direct as well as indirect transfers, the transaction covered by the 10-07-2009 SPA, which constitutes indirect transfer of SBL shares under the guise of transfer of ShanH shares is chargeable to tax in India.

- The retrospective amendment to Section 2(47) of the Act (by the Finance Act, 2012) clarifies that "transfer" would mean and would deem to have always meant, the disposal of an asset whether directly or indirectly or voluntarily or involuntarily.
- Since, MA/GIMD are owners of SBL shares (both legal and beneficial), it is MA/GIMD which have the participating interest in SBL. The disposal of such participating interest, whether directly or through a nominee entity like ShanH, would not take the gains out of the ambit of Article 14(5) of the DTAA. If the right to tax vests in India, the mode of disposal is immaterial, whether direct, indirect or deemed disposal.
- "Alienation" does not mean mere disposition of assets (as contended by the petitioners). It includes transfer of assets as well.
- The residuary provision (Article 14(6) of the DTAA) is inapplicable to the facts. This provision applies if capital gains do not come within the ambit of Article 14(1), (2), (4) and (5).
- The retrospective clarificatory amendments (vide the Finance Act, 2012) do not seek to override the DTAA. In case of a conflict between the domestic law and the DTAA, DTAA will prevail, in terms of Section 90 of the Act. There is however no conflict between DTAA and provisions of the Act, in the present case. Once the right to tax the gains stands allocated to the source country (under the DTAA), domestic law provisions of the source country will have to be read into the DTAA in terms of Article 3(2), where any expression has not been defined in the DTAA. Since "alienation" is not defined in the DTAA, its meaning has to be imported from the domestic law. This exercise does not amount to overriding the treaty and in fact amounts to giving effect to Article 3(2) of the DTAA.

15. Issues for determination :

In view of the competing contentions/submissions and orders (the ruling of the AAR and orders of the Revenue) challenged in the writ petitions, the following issues arise for consideration:

ISSUES :

(1) Is ShanH not an entity with commercial substance; is a sham or illusory contrivance, a mere nominee of MA and/or MA/GIMD being the real, legal and beneficial owner(s) of SBL shares; and a device incorporated and pursued only for the purpose of avoiding capital gains liability under the Act ?

(2) Was the investment, initially by MA and thereafter by MA and GIMD through ShanH in SBL, a colourable device designed for tax avoidance? If so, whether the corporate veil of ShanH must be lifted and the transaction (of the sale of the entirety of ShanH shares by MA/GIMD to Sanofi) treated as a sale of SBL shares?

(3) Is the transaction (on a holistic and proper interpretation of relevant provisions of the Act and the DTAA), liable to tax in India?

(4) Whether retrospective amendments to provisions of the Act (by the Finance Act, 2012) alter the trajectory or impact provisions of the DTAA and/or otherwise render the transaction liable to tax under the provisions of the Act?

(5) Whether the AAR ruling dated 28-11-2011 is sustainable? If not, what is the appropriate relief that could be granted to the petitioners (in W.P.Nos.3339 and 3358 of 2012); and whether the orders by the Revenue dated 25-05-2010 and 15-11-2011 are valid and sustainable? and

(6) Whether the order dated 25-05-2010 (challenged in W.P.No.14212 of 2010) determining the petitioner-Sanofi to be an "assessee in default" in respect of payments made by it to MA and GIMD for acquisition of ShanH shares, u/S.201(1) of the Act; the consequent notice of demand dated 25-05-2010; and a rectification order dated 15-11-2011 (u/S.154 of the Act) re-computing the long-term capital gain, the tax thereon and the consequent interest, are valid ?

ANALYSIS :

16. Issues 1 and 2 :

Issues 1 and 2 require integrated analyses of the material on record, applicable precedents, authorities and competing contentions with regard to liability of the transaction consequent on the 10-07-2009 SPA (alienation of ShanH shares to Sanofi by MA/GIMD), to tax under provisions of the Act. Hence these issues are considered together.

We prefer to begin with a generic analysis of the precedents cited at the Bar, insofar as relevant to issues 1 and 2.

17. What curial guidance points to ?

Circumstances justifying lifting of the corporate veil; identifying the real and substantial nature of the transaction; whether corporate shareholding is tantamount to *pro tanto* ownership of corporate property and assets; relevant principles regarding construction of the transactional documents; and appropriate scrutiny standards in the context of an operating tax treaty - analysis of precedents.

The Revenue angle :

In support of the contention (that analysis of the relevant transactional documents, chronology of events and the surrounding circumstances, warrant lifting of the corporate veil of ShanH and on such intrusive scrutiny, the transaction in issue is one of transfer of shares and of the control, management, business interests and the value of the underlying assets of SBL by MA/GIMD [MA being the true, legal and beneficial owner of SBL shares] in favour of Sanofi), Revenue has cited the following precedents :

National Cement Mines Industries, Ltd vs Commissioner of Income Tax, West Bengal, Calcutta[13]*; Juggilal Kamlapat vs Commissioner of Income Tax, U.P.*[14]*; Commissioner of Income Tax, Madras vs Sri Meenakshi Mills Ltd*[15]*; M/s McDowell and Company Limited vs Commercial Tax Officer*[16]*; Workmen Employed in Associated Rubber Industry Ltd, Bhavnagar vs Associated Rubber Industry Ltd., Bhavnagar and Another*[17]*; State of U.P. and Others vs Renusagar Power Co. and Others*[18]*; New Horizons Limited and Another vs Union of India and Others*[19]*; Ebrahimi vs Westbourne Galleries Ltd and Others*[20]*; DHN Food Distributors Ltd and Others vs London Borough of Tower Hamlets*[21]*; Radha Sundar Dutta vs Mohd. Jahadur Rahim*[22]*; Puzhakkal Kuttappu vs C. Bhargavi and Others*[23]*; Ford against Beech*[24]*; Inntrepreneur Pub Co Ltd vs East Crown Ltd*[25]*; Investors Compensation Scheme Ltd vs West Bromwich Building Society*[26]*; Hideo Yoshimoto v Canterbury Golf International Limited*[27]*; Aditya Birla Nuvo Limited [Formerly known as Indian Rayon & Industries Limited] vs The Deputy Director of Income Tax, [International Taxation], Mumbai and Ors.*[28] and *Provident Investment Co. Ltd. v. CIT, Bombay City*[29]

When is it legitimate to lift the veil? What precedents instruct ?

Revenue relied on *National Cement Mines Industries Ltd.*; *Juggilal Kamlapat*; *Sri Meenakshi Mills Ltd.*; *McDowell; Associated Rubber Industry Ltd; Renusagar Power Co.*; *New Horizons Ltd.*; *Ebrahimi*; and *DHN Food Distributors Ltd.*, in support of its claim for lifting the corporate veil of ShanH and thereafter proceed to treat the transaction as one for transfer of the management, control and underlying assets of SBL to Sanofi, thus liable to capital gains tax under the Act.

National Cement Mines Industries Ltd. interpreted a deed dated 07-05-1935 to confirm the view taken all through, that the transaction in question was substantially a commercial transaction for sharing profits of the commercial activities of Associated Cement Limited and that the recitals under Clause (1) of the deed also fortify the conclusion that the receipts were in the nature of income and not capital.

Juggilal Kamalapat justified lifting of the veil while confirming the finding (by Income Tax authorities) that the corporate entity was contrived solely for the purpose of tax evasion, to circumvent tax obligations and to perpetrate a fraud on the Revenue.

Similarly, in *Sri Meenakshi Mills Ltd.*, the transaction in question was determined to constitute a basic arrangement or scheme between the assessee-companies and the Bank (Madurai Bank Ltd. at Pudukottai), to evade income tax. For this reason, the Supreme Court while reiterating the generic and established principle (that a company is a legal personality, distinct from its members and capable of distinctly enjoying rights and being subject to duties apart from its members) ruled that in exceptional circumstances the Court would lift the corporate veil and identify the economic realities beyond the legal façade, such as when the corporate entity is a device used for tax evasion or to circumvent tax obligations.

<u>The McDowell plurality</u> :

In *McDowell* there were concurring opinions; Ranganath Misra, J. (for himself and on behalf of Chandrachud, C.J., Desai and Venkataramiah, JJ) and a concurring opinion by Chinnappa Reddy, J. A brief reference to the relevant facts of the case is in order. The question was whether the component of excise duty paid directly to excise authorities of the State by wholesale buyers of liquor (from the manufacturer-McDowell) should be included in McDowell's turnover for the purpose of assessment under the State Sales Tax Act. Notwithstanding the definition of "excise duty" in the State Excise Act, a practice was contrived whereby wholesale buyers used to remit the excise duty (payable by the manufacturer-McDowell) at the time of lifting of stocks of liquor from the manufacturer. This component was not reflected in McDowell's books of account. Rejecting McDowell's appeal and upholding the determination by Sales Tax Authorities that the excise duty component should be included in the appellant's turnover, Misra, J observed :

> *45. Tax planning may be legitimate provided it is within the framework of law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges.*

and at para – 46 stated :

> *46. On this aspect one of us, Chinnappa Reddy, J., has proposed a separate and detailed opinion with which we agree.*

Chinnappa Reddy, J., in the concurring opinion traced the history and evolution of the judicially crafted distinction between "tax avoidance" and "tax evasion", commencing from the observations of Lord Sumner in *IRC v. Fisher's Executors*[30] and reiterated by Lord Tomlin in *IRC v. Duke of Westminster*[31]; referred to developments and shift in judicial attitudes since World War-2; the observations of Lord Wilberforce in *W.T. Ramsay v. IRC*[32]; explanation of the paradigm shift in judicial opinion offered by Lord Diplock and Lord Scarman in *Burmah Oil Company Ltd.,* and by Lord Brightman, Lord Fraser and Lord Roskill in *Furniss (Inspector of Taxes) v. Dawson*[33] and concluded :

17. We think that time has come for us to depart from the Westminster *principle as emphatically as the British Courts have done and to dissociate ourselves from the observations of Shah, J. and similar observations made elsewhere. The evil consequences of tax avoidance are manifold. First there is substantial loss of much needed public revenue, particularly in a Welfare State like ours. Next there is the serious disturbance caused to the economy of the country by the piling up of mountains of black-money, directly causing inflation. Then there is "the large hidden loss" to the community (as pointed out by Master Wheatcroft) by some of the best brains in the country being involved in the perpetual war waged between the tax-avoider and his expert team of advisers, lawyers, and accountants on one side and the tax-gatherer and his perhaps not so skilful, advisers on the other side. Then again there is the "sense of injustice and inequality which tax avoidance arouses in the breasts of those who are unwilling or unable to profit by it". Last but not the least is the ethics (to be precise, the lack of it) of transferring the burden of tax liability to the shoulders of the guileless, good citizens from those of the 'artful dodgers'. It may, indeed, be difficult for lesser mortals to attain the state of mind of Mr. Justice Holmes, who said: "Taxes are what we pay for civilized society. I like to pay taxes. With them I buy civilization". But, surely, it is high time for the judiciary in India too to part its ways from the principle of*Westminster *and the alluring logic of tax avoidance. We now live in a Welfare State whose financial needs, if backed by the law, have to be respected and met. We must recognize that there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is a pretence to say that avoidance of taxation is not unethical and that it stands on no less moral plane than honest payment of taxation. In our view, the proper way to construe a taxing statute, while considering a device to avoid tax, is not to ask whether the provisions should be construed literally or liberally, nor whether the transaction is not unreal and not prohibited by the statute, but whether the transaction is a device to avoid tax, and whether the transaction is such that the judicial process may accord its approval to it. A hint of this approach is to be found in the judgment of Desai, J. in* Wood Polymer Ltd. and Bengal Hotels Limited, In re *where the learned Judge refused to accord sanction to the amalgamation of companies as it would lead to avoidance of tax.* (emphasis added)

Whether the opinion of Chinnappa Reddy constituted the operative principle by the Constitution Bench was considered in later decisions, analyzed *infra*.

In *Associated Rubber Industry Ltd.,* the Court lifted the corporate veil of the respondent-Company. In the context of its observations and conclusions, that the obvious purpose of creating a subsidiary company (by the respondent-Company) was to reduce its income so as to avoid or reduce the bonus payable to its workmen (the appellants), the Supreme Court observed that wherever ingenuity is expended to avoid taxing or welfare legislations, it is the duty of the Court to go beyond the smokescreen and discover the true state of affairs.

The corporate veil was again lifted in *Renusagar Power Co. and others*. The Court treated power generation by Renusagar as power generated by Hindalco, to determine the appropriate rates of duty under provisions of the UP Electricity (Duty) Act, 1952. The Court spelt out several factors to justify the assumption that both the entities (the subsidiary-Renusagar and the holding company-Hindalco) were one concern viz., the profits of Renusagar were treated as profits of Hindalco; Renusagar had no separate existence apart from and independent of Hindalco; persons generating and consuming energy were the same; and earlier the State and its instrumentalities had also treated the two corporate entities as indivisible.

In *New Horizons Ltd,* the appellant-NHL's tender was rejected and the offer of the 4^{th} respondent accepted by the Department of Telecommunications, on the ground that the appellant (a joint venture) did not satisfy the "past experience" criterion. The Supreme Court reversed the decision of the High Court (rejecting the challenge to rejection of its tender, by NHL) and ruled that credentials of an entity must be examined from a commercial point of view. The Supreme Court found NHL to be an association of Companies jointly undertaking a commercial enterprise wherein all the constituents would contribute assets, will share risk and have a community of interest. The Court found that the appellant would have access to expertise of its parent group companies in the several relevant areas. Consequently the Court "looked through" the NHL corporate veil to conclude that since the appellant is a joint venture, expertise of its various constituents must be considered by the Tender Evaluation Committee (TEC), as a prudent business consideration. Rejection of the appellant's tender (which offered nearly five time the amount offered by the successful tenderer – the 4th respondent), by the TEC was held to be arbitrary and irrational.

In *Ebrahimi*, the issue was whether the respondent - company - Westbourne Galleries Ltd. ought to be wound-up under Section 222 (f) of the (U.K.) Companies Act, 1948, on just and equitable grounds. On analyses of the relevant facts, House of Lords found that removal of the appellant as a Director of the respondent-company, on the strength of an ordinary resolution passed by the other two shareholders who held a majority of the stock, constituted inequitable conduct on the part of these shareholders (father and son), employing their legal rights to the prejudice of the appellant.

In *DHN Food Distributors Ltd.* the Court (of Appeal) allowed the appeal and held that the appellant was entitled to compensation for disturbance under Section 5 of the (UK) Land Compensation Act, 1961. Under the Act, compensation is to be made for the value of the land and for disturbance of the business as well. Factually however, the firm (DHN) and its property were not under single ownership. It was owned by three companies. The business was owned by the appellant and parent company – DHN; the land at the time of acquisition was owned by a subsidiary – Bronze Investors Ltd.,(Bronze) and the vehicles by another subsidiary – DHN Food Transport Ltd., (Transport). DHN held all the shares, in both subsidiary companies – "Bronze" and "Transport". Compensation for disturbance under the 1961 Act to the appellant – "DHN" and "Transport" was denied, though the Local Authority admitted that "DHN" and "Transport" had suffered substantial business dislocation. In these circumstances and in the context of considering whether the appellant – DHN was entitled to compensation for disturbance of its business, the Court of Appeal lifted the corporate veil of 'Bronze' and 'Transport' and ruled that the three companies (DHN, Bronze and Transport) should not be treated separately so as to be defeated on a technical point and should not be denied compensation which should justly be paid for disturbance. The Court held that the three companies should, for the present purposes, be treated as one, and the parent company-DHN, treated as that one and be entitled to claim compensation without the necessity for them to go through a conveyancing device, to obtain compensation.

<u>Aditya Birla Nuvo Ltd.</u> :

The judgment of the Bombay High Court records *prima facie* observations based on a matrix of facts distinct from those in the *lis* before us. In *Aditya Birla* there were two different transactions at distinct levels :

(a) Sale of shares of an Indian joint venture company by a Mauritius company to an Indian company; and

(b) Sale of shares of the Mauritius company to another Indian company.

The distinguishing features (from the facts before us) are :

(i) The Mauritius company was not a joint venture, unlike ShanH. It was a 100% subsidiary interposed above the joint venture company;

(ii) Indian Rayon had acquired the shares of the Indian company and there was no implication requiring interpretation of a capital gain Article similar to Article 14 of the DTAA;

(iii) The Bombay High Court followed its own judgment in Vodafone which was subsequently over-ruled in *Vodafone*;

(iv) The High Court held that *Azadi Bachao Andolan* is not applicable to the facts of the case (just as the Hon'ble AAR had discarded, not distinguished, *Azadi Bachao Andolan*);

(v) During the hearing of *Vodafone* the Supreme Court permitted Aditya Birla to intervene and its counsel made several submissions on legal principles regarding treaty interpretation, and separate existence of parent and subsidiary companies;

(vi) The Bombay High Court in clear terms recorded that the opinion expressed by it is *prima facie* and all contentions of both parties are kept open, to be determined in the assessment proceedings; and

(vii) The *prima facie* observations (in *Aditya Birla*) were made in the context of a writ in the nature of prohibition presented to challenge initiation of proceedings u/S.148 of the Act.

It also requires to be noticed that several contentions urged on behalf of *Aditya Birla* (though not on the specific facts that were before the Bombay High Court) were noticed and observations made thereon, in *Vodafone*. The following observations in *Vodafone* are significant:

> *Mr. Aspi Chinoy, learned senior counsel contended that in the absence of LOB clause in the India Mauritius Treaty, the scope of the treaty would be positive from Mauritius special purpose vehicles (SPVs) created specifically to route investments into India, meets with our approval. We acknowledge that on a subsequent sale/transfer/disinvestment of shares by the Mauritian company, after a reasonable time, the sale proceeds would be received by the Mauritius company as the registered holder/owner of such shares, such benefits could be sent back to the foreign principal/100 per cent shareholder of Mauritius company either by way of a declaration of special dividend by Mauritius company and/or by way of repayment of loans received by the Mauritius company from the foreign principal/shareholder for the purpose of making the investment. Mr. Chinoy is right in his contention that apart from the DTAA, which provides for tax exemption in the case of capital gains received by a Mauritius company/shareholder at the time of disinvestment/exit and the fact that Mauritius does not levy tax on dividends declared and paid by a Mauritius company/subsidiary to its foreign shareholders/principal, there is no other reason for this quantum of funds to be invested from/through Mauritius.*
>
> *We are, therefore, of the view that in the absence of LOB clause and the presence of Circular No.789 of 2000 and TRC, on the residence and beneficial interest/ownership, Tax Department cannot at the time of sale/disinvestment/exit from such FDI, deny benefits to such Mauritius companies of the Treaty by stating that FDI was only routed through a Mauritius company, by a company/principal resident in a third country; or the Mauritius company had received all its funds from a foreign principal/company; or the Mauritius subsidiary is controlled/managed by the foreign principal; or the Mauritius company had no assets or business other than holding the investment/shares in the Indian company; or the foreign principal/100 per cent shareholder of Mauritius company had played a dominant role in deciding the time and price of the disinvestment/sale/transfer; or the sale proceeds received by the Mauritius company had ultimately been paid over by it to the foreign principal/its 100 per cent shareholder either by way of special dividend or by way of repayment of loans received; or the real owner/beneficial owner of the shares was the foreign principal company. Setting up of a WOS Mauritius subsidiary/SPV by principals/genuine substantial long-term FDI in India from/through Mauritius, pursuant to the DTAA and Circular No.789 can never be considered to be set up for tax evasion.* (Pages - 101, 102 of ITR)

In any event, the *prima facie* analyses by the Bombay High Court in *Aditya Birla* must yield to the binding precedents *inter alia, Azadi Bachao Andolan* and *Vodafone*.

In a 1953 decision in *Provident Investment Co. Ltd.*, Chagla, CJ, relied on *Bank of Chettinad v. CIT, Madras*[34] where the Privy Council considered it necessary to reiterate its protest against the suggestion that in revenue cases the substance of the matter may be regarded as distinguished from the strict legal position. Privy Council ruled that if the strict legal position were clear, the Court is not permitted to look at the substance of the matter and ignore the true legal position. For this principle, reliance was placed by the Privy Council on *Duke of Westminster*. Bombay High Court answered the reference in favour of the assessee and ruled that the transaction in question was not liable to the charge on capital gains u/S.12(B) of the Indian Income Tax Act, 1922.

Petitioners' version :

Petitioners contended that precedents cited by the Revenue are inapplicable and inappropriate to the facts and circumstances of the case. ShanH is a Joint Venture (JV) and genuineness of JV's has never been disputed in any jurisdiction, either in India or France. No jurisdiction ignores joint ventures because of the ultimate control exercised by the parent(s). None of the decisions cited by the Revenue deal with transactions involving implication of a tax treaty. Lifting the corporate veil is impermissible under Article 14(5) of the DTAA as it does not accommodate a "see through". Only Article 14(4) accommodates a limited "see through". Petitioners alternatively contend that even on lifting the corporate veil of ShanH, the legal and beneficial owner of SBL shares is ShanH and ShanH alone; the transaction falls within the provisions of the DTAA; is chargeable to capital gains tax in France; and even if Revenue's far-fetched and creative "underlying assets" theory is considered, the chargeability to tax is allocated to France under Article 14(6) of the DTAA. Petitioners rely on the following in support of their several contentions :

> *Charanjit Lal Chowdhury v. UOI*[35]; *Bacha F Guzdar v. CIT*[36]; *Smt. Maharani Ushadevi v. CIT*[37]; *Western Coalfields Ltd. v. Bharat Aluminium Company Ltd.*[38]; *LIC of India v. Escorts*[39]; *Venkatesh (Minor) v. CIT*[40]; *UOI and another vs Azadi Bachao Andolan*[41]; *CIT v. Walfort Share & Stock Brokers P. Ltd.*[42]; *Vodafone International Holdings BV v. UOI*[43]; *Federal Commissioner of Taxation v. Lamesa Holdings BV*[44]; *Prevost Car Inc. v. R*[45] and *Her Majesty The Queen v. Prevost Car Inc.*[46].

The generic principles flowing from the decisions in *Charanjit Lal Chowdhury; Bacha F Guzdar; Maharani Ushadevi; Western Coalfields Ltd* and *LIC of India* could be summarized as under:-

i) A shareholder's interest in a company is represented by his shareholding, which is immovable property with all the attributes thereof.

ii) A company as a juristic *persona* is distinct from its shareholders. It is the company which owns the property, not the shareholder(s).

iii) The rights of shareholders are such as are delineated in provisions of the Companies Act. A shareholder while having no rights of ownership in the assets of the company has a voice in administering the affairs of the company and would be entitled, as provided by the Articles of Association to a declaration of dividends, distributed out of profits of the company to the shareholders.

The above principles find resonance in several other decisions including *RC Cooper v. Union of India*[47] (the Bank nationalization case) where the Court reiterated the principle that a company registered under the Companies Act is a legal person, separate and distinct from its individual members; its property is not the property of the shareholders who have merely an interest in the company arising under the Articles of Association, measured by a sum of money for the purpose of liability and by sharing the profit; and that where companies are incorporated for a lawful purpose their properties are owned by them and there is no reason for even taxation purposes that their property should be treated as belonging to the shareholders.

The Madras High Court built on these underlying principles in *Venkatesh (Minor)* for rejecting the assessees' creative contention that a part of the value received on sale of shares, constituting a controlling interest in a company was for transfer of the controlling interest, and that component of the value received did not amount to a capital gain. The Court held that on a sale of shares the fact that the vendor has a controlling interest and is in a position to place the vendee in control of the company (by transfer of his shares or such part as would enable the vendee to exercise control over the company with the aid of transferred shares) would only enhance the value of the shares transferred. The price paid by the vendee for acquisition of such shares remains the price of those shares though the price paid be higher than the market price. Controlling interest is only an incidence of shareholding and has no independent existence, held the Court and went on to add that controlling interest can not be transferred without transferring the shares.

Revenue has referred to *Clariant International Ltd. and another v. Securities and Exchange Board of India*[48] to buttress its contention that MA (and not ShanH) is the legal and beneficent owner of SBL shares. According to Revenue (noticed earlier) since the amended SBL AOA (as amended on 14-02-2007, after the 06-11-2006 SPA and the two SHA's dated 07-11-2006) defines 'MA' to mean 'Merieux Alliance' and there is no mention of or reference to ShanH either in Articles 45(A), 102(A), 132 or 136(A) (these Articles also refer to MA and not ShanH), MA is the holder of the SBL shares, not ShanH. Petitioners' contentions in response have already been adverted to, viz., that the amended Article 45(A) acknowledges/incorporates provisions of the 06-11-2006 SPA and the 07-11-2006 SHA's by stating that : *The transfer of shares held by MA or VR (including its family members) or KA shall be subject to the restrictions/terms of any agreement entered into between MA, VR and/or KA dated on or prior to the completion date*. Therefore ShanH is comprehended wherever MA is referred to; ShanH is explicitly specified to be the investment vehicle of MA, through which the SBL shares were purchased; and that as on the date of this amended SPA (14-02-2007), MA was the sole and unique shareholder of ShanH (GIMD having joined ShanH as a strategic investment partner later, on 08-03-2007). Petitioners also rely on the (same) *Clariant* decision to contend that it is ShanH and not MA which is the legal and beneficial owner of SBL shares.

The *Clariant* Court (paragraphs 50 - 52) pointed out that members holding equity share capital of a company and whose names are entered as beneficial owner in the records of the depository shall be members of the company concerned; that in *Howrah Trading Co. Ltd. v. CIT*[49], the Court had pointed out that the expression "shareholder" used in Section 18(5) of the Companies Act, 1956 means a person denoted by the same expression in the Indian Companies Act 1913; and that the Court in *Howrah* had quoted with approval the following observations of Chitty, J in *Wala Wynaad Indian Gold Mining Co., In re*[50] :

> '*I use now myself the term which is common in the courts, "a shareholder", that means the holder of the shares. It is the common term used, and only means the person who holds the shares by having his name on the register.'*

Clariant also referred to the decision in *Balkrishan Gupta vs. Swadeshi Polytex Ltd.*[51]. In *Balkrishan Gupta*, the Court on analyses of relevant provisions of the Companies Act, 1956 ruled that subscribers of the Memorandum of Association of a company shall be deemed to have agreed to become members of the company and on its registration shall be entered as members in its register of members; a subscriber of the memorandum is liable as the holder of the shares which he has undertaken to subscribe for; any other person who agrees to become a member of a company and whose name is entered in its register of members shall be a member of the company; that in his case the two conditions, viz., (that there is an agreement to become a member and that his name is entered in the register of members of a company) are cumulative; and both conditions must be satisfied to enable him to exercise rights of a member. The Court also quoted with approval the statement in *Buckley*[52] which states that as between the shareholder and the company, the person entitled to exercise the right of voting is a person legally entitled to the shares, the member whose name is on the register; and the company cannot enquire into beneficial ownership.

Para – 53 of *Clariant* (on which Revenue placed reliance) observes that rights of a shareholder are purely contractual and would be such as are granted to him by the company's Memorandum of Articles of Association together with the statutory rights conferred on him by the Companies Act.

On a true and fair reading of *Clariant* and a holistic, non-manipulative synthesis of its *ratio*, we are of the considered view that the observations (at para – 53) must not be considered in isolation or out of context. We understand *Clariant* to mean that a person whose name is entered in the register of members of the company must be regarded as a shareholder of the company and would be entitled to all the rights and benefits as such, and to the extent of the shareholding, *qua* provisions of the Companies Act, 1956 and of the Memorandum and Articles of Association of the company.

Azadi Bachao Andolan :-

Azadi Bachao Andolan is a critical precedent. The judgment invited a conflating interpretation and synthesis of provisions of a tax treaty and of the domestic tax legislation – the Act. To recollect, the AAR in its ruling dated 25.5.2010 (impugned in W.P.No. 14212/10) specifically observed (Para 18 of the order) that *Azadi Bachao Andolan* incorrectly appreciated the governing *ratio* in *McDowell,* in stating that the views expressed by Chinnappa Reddy,J (in the concurring opinion in *McDowell*) are his own and do not represent the view of the Court. The *McDowell* facts did not require consideration of implications of an operative tax treaty, while considering several issues such as when the corporate veil could be lifted; how a step or series of steps leading to a transaction should be interpreted; and how provisions of the Act should be construed and the like. *Azadi Bachao Andolan* is a clear and explicit tax treaty case and was required to identify the normative synergies between treaty and domestic law provisions.

A brief account of the facts and circumstances leading to the decision *Azadi Bachao Andolan* require to be noticed.

- Governments of India and of Mauritius entered into an agreement on 01.04.1983 for avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income and capital gains and for encouragement of mutual trade and investment (the Indo-Mauritius agreement – IMA). IMA was brought into force by a notification dated 06/12/1983 issued under Sec. 90 of the Act.
- CBDT by a circular dated 30/03/1994 (exercising powers u/Sec. 90 of the Act) clarified that capital gains of any resident of Mauritius by alienation of shares of Indian companies shall be taxable only in Mauritius according to Mauritius Taxation laws and will not be liable to tax in India. On the basis of this clarification a large number of Foreign Institutional Investors (FIIs) invested large amounts of capital in the shares of Indian companies, expecting immunity to capital gains tax under the Act on the profits made in the sale of shares of Indian companies.
- Around the year 2000 Income Tax Authorities issued notices to some FIIs proposing imposition of tax on profits and on dividends accrued to them in India. The basis for the show cause notices was that the recipients were mostly "shell companies" incorporated in Mauritius operating through Mauritius with the main purpose of investment of funds in India but allegedly controlled and managed from countries other than India or Mauritius. On this assumption and alleging that they were not 'residents of Mauritius' so as to derive benefits from the tax treaty, they were put on notice for levy of tax under the Act.
- The show cause notices apparently created a panic in the FIIs resulting in hasty withdrawal of funds. Thereafter to clarify the situation, CBDT issued a circular dated 13.04.2000. This circular *inter alia* clarified that wherever a certificate of residence is issued by Mauritian authorities, such certificate would constitute sufficient evidence, to accept the status of residents as well beneficial ownership for applying the provisions of

the IMA. The circular further clarified that the test of residence mentioned above would also apply in respect of income from capital gains on sale of shares; and that FIIs etc, which are residents in Mauritius would not be taxable in India, on income from capital gains arising in India on sale of shares as per Article-13(4) of the IMA.

- Challenging the CBDT circular dated 13.04.2000, writ petitions by way of PIL were filed. The Delhi High Court allowed the writ petitions and quashed the circular of the CBDT *inter alia* relying on the decision in *McDowell* andholding that it is open to the Income Tax Officer in a given case to lift the corporate veil, to ascertain whether the purpose of the corporate entity is avoidance of tax; and such function (of assessment) being *quasi Judicial*,could not be interfered with, prohibited or chilled by a CBDT circular. The circular was held *ultra vires* on the ground that it interfered with the *quasi judicial* functions of the Assessing Officer.
- Aggrieved, Union of India appealed to the Supreme Court. Supreme Court allowed the appeal.
- *McDowell* analyzed the salient features of the IMA. Suffice to note and for the purposes of this case, that provisions of IMA and of DTAA are substantially similar. Art.3(2) of both agreements provides, that in the application of provisions of the agreement by a contracting State, any term not defined therein, shall, unless the context otherwise require, have the meaning which it has under the law of that contracting State concerning the taxes to which the convention applies. Art.14 of the DTAA broadly corresponds to Art.13 of the IMA. Paras 1 and 2 of Art.14 of DTAA correspond to Paras 1 and 2 of Art.13 of the IMA; Para 3 of Arts.14 and of 13 (of DTAA and IMA, respectively) are substantially similar; and Art.14(6) of DTAA corresponds to Art.13(4) of the IMA.

<u>*Rationes* and conclusions in *Azadi Bachao Andolan*</u> :

- *When a double-taxation avoidance treaty, convention or agreement (for short, "Treaty") becomes operational and is notified by the Central Government for implementation of its terms u/S.90 of the Act, provisions of the Treaty, with respect to cases to which they would apply, would operate even if inconsistent with provisions of the Act. As a consequence, if a tax liability is imposed by the Act, the Treaty may be referred to for negativing or reducing it. In case of conflict between provisions of the Act and of the Treaty, provisions of the Treaty would prevail and are liable to be enforced – CIT v. Visakhapatnam Port Trust[53]; CIT v. Davy Ashmore India Ltd.[54]; CIT v. R.M. Muthaiah[55]; andArabian Express Lanes Ltd. of UK v. Union of India[56], approved.*
- *Since the general principle of chargeability of tax u/S.4 and the general principle of ascertainment of total income u/S.5 of the Act are subject to the provisions of the Act, provisions of the Treaty would automatically over-ride provisions of the Act in the matter of ascertainment of chargeability to income tax and ascertainment of the total income, to the extent of inconsistency with Treaty terms.*
- *Liability to taxation is a legal situation while payment of tax is a fiscal fact. For application of Article 4 of the IMA, what is relevant is the legal situation, i.e., liability to taxation and not the fiscal fact of actual payment of tax.*
- *In the light of the terms of the IMA the contention that off-shore companies incorporated and registered under theMauritius Off-shore Business Activities Act, 1992 (MOBA) are not liable to taxation under Mauritius tax laws, is unacceptable. Such companies must be considered "resident" in Mauritius within the meaning of Articles 3 and 4 of the IMA.*
- *Unlike an ordinary taxing statute a tax Treaty must be given a liberal interpretation with a view to implementing the true intention of the parties. A literal or legalistic interpretation must be avoided when the basic object of the Treaty might be defeated or frustrated insofar as the particular item under consideration is concerned –*

observations of the Federal Court inJohn N. Gladden v. Her Majesty The Queen[57]*, quoted with approval.*

- *As a general principle authorities and courts are empowered to lift the veil of incorporation where necessary or appropriate while applying the domestic law. Where the terms of Treaty apply, even if these derogate the provisions of the Act, the principle of lifting the veil of incorporation cannot be applied. The whole purpose of a Treaty is to ensure that benefits thereunder are available even if they are inconsistent with the provisions of the Act.*
- *Treaties (including for double-taxation relief) are negotiated and entered into at a political level and have several considerations as their bases. Treaty provisions must be seen in the context of aiding commercial relations between treaty partners and as being essentially the bargain between two treaty countries as to the division of tax revenues between them in respect of income falling to be taxed in both jurisdictions. Since Treaty negotiations are largely a bargaining process, with each side seeking concessions from the other, the final agreement will often represent a number of compromises, and it may be uncertain as to whether a full and sufficient quid pro quo is obtained by both sides – observations in Francis Bennion : Statutory Interpretation and David R. Davis : Principles of International Double Taxation Relief, referred to.*
- *There are many principles in fiscal economy, including Treaty shopping, which at first blush might appear to be evil, or tolerated in developing economies in the interest of long-term development. Terms of a Treaty are essentially policy trade-offs negotiated at the diplomatic level between sovereign Nations. When the Treaty becomes operative however, it is not the function or domain of tax administrators or courts to consider the fairness or equity of the policy; and the terms of a Treaty must be given full faith and credit.*
- *The majority judgment in McDowell has not endorsed the concurring view of Chinnappa Reddy, J. The "extreme view" of Chinnappa Reddy, J militates against the observations in the majority represented by the leading judgment of Ranganath Misra, J. Chinnappa Reddy, J's observation in McDowell that the principle in Duke of Westminster has been departed from subsequently by the House of Lords, is fallacious. Decisions of the House of Lords in Craven v. White*[58] *and MacNiven (H.M. Inspector of Taxes) v. Westmoreland Investments Ltd.*[59] *considered. M.V. Valliappan v. ITO*[60]*; Banyan and Berry v. CIT*[61]*; CWT v. Arvind Narottam*[62] *and Mathuram Agrawal v. State of Madhya Pradesh*[63]*, distinguishing the observations of Chinnappa Reddy in McDowell, quoted with approval.*
- *The principle in IRC v. Duke of Westminster is still "alive and kicking in England" and has also acquired judicial benediction of the Constitution Bench in India, notwithstanding the temporary turbulence created in the wake of McDowell. Further observed that the situation in United States and other jurisdictions is similar.*
- *An Act which is otherwise valid in law cannot be treated as non-est merely on the basis of some underlying motive supposedly resulting in some economic detriment or prejudice to the national interests. There has been no drastic change in the fiscal jurisprudence in India as would warrant a departure from the Westminster principle.*

A review application by the writ petitioners was dismissed on 29-01-2004 and a curative petition thereafter was also dismissed, in *limine* on 08-12-2004.

Walfort Share and Stock Brokers P. Ltd. :

The core issue involved in this decision was succinctly stated by the Court :

The main issue involved in this batch of cases is – whether in a dividend stripping transaction (alleged to be colourable device by the Department), the loss on *sale of units could be considered as expenditure in relation to earning of dividend income exempt under section 10(33), disallowable under section 14A of the Act?*

In a clear dividend stripping transaction, the assessee claimed the dividend received as exempt u/S.10(33) and claimed set-off for the loss occasioned on the sale of the shares against its taxable income, thereby seeking to reduce its tax liability and gain tax advantage. Revenue relied on *McDowell* to contend that the assessee had designedlyentered into a pre-meditated transaction, of buying and selling units yielding exempted dividends with full knowledge of the fall in NAV after the record date and the payment of tax-free dividend; and therefore the loss on sale was not genuine.

Supreme Court rejected Revenue's contention observing that the assessee had made use of the provisions of the Act and such use cannot be termed "abuse of law". Even assuming that the transaction was pre-planned there was nothing to impeach the genuineness of the transaction. Responding to Revenue's reliance on the *McDowell* ruling, the Court observed :

> *... It may be stated that in the later decision of this court in Union of India v. Azadi Bachao Andolan it has been held that a citizen isfree to carry on its business within the four corners of the law. That, mere tax planning, without any motive to evade taxes throughcolourable devices is not frowned upon even by the judgment of this court in McDowell and Co. Ltd.'s case (supra).*

Vodafone :

- Vodafone International Holdings BV (Vodafone), a company resident for tax purposes in Netherlands acquired the entire share capital of CGP Investments (Holdings) Ltd. (CGP), a company resident for tax purposes in Cayman Islands *qua* a transaction dated 11-02-2007. On 31-05-2010 Revenue passed an order u/S.201(1) and 201(1A) of the Act declaring the transaction to be taxable under the Act. Revenue raised a demand for tax on capital gains arising out the sale of CGP share capital contending that CGP, while not a tax resident in India, held the underlying Indian assets [of (Hutchisson Essar Ltd.)HEL] and the aim of the transaction was acquisition of a 67% controlling interest in HEL, an Indian company. On a writ petition by Vodafone, the Bombay High Court ordered a remit on the question whether Indian Tax Authorities hadjurisdiction to tax the transaction. Vodafone challenged this decision unsuccessfully. Against the dismissal of the writ petition by the Bombay High Court, Vodafone appealed to the Supreme Court.
- Hutch group (Hong Kong) through participation in a joint venture vehicle invested in telecommunications business in India in 1992. The JV later came to be known as Hutchison Essar Ltd. (HEL). In 1998 CGP was incorporated in Cayman Islands, with limited liability and as an "exempted company". CGP later became a wholly owned subsidiary of a company which in turn became a wholly owned subsidiary of a Hong Kong company - HTL which was later listed on the Hong Kong and New York Stock Exchanges in September, 2004.
- *Vodafone*, though not directly a case involving Tax-Treaty implications on domestic tax laws (there being no tax Treaty between India and Cayman Islands), nevertheless considered the application and interpretation of Indian Tax Legislation (the 'Act') in the context of an applicable and operative tax treaty, since the correctness of *Azadi Bachao Andolan* was raised by Revenue. Revenue contended that *Azadi Bachao* requires to be over-ruled to the extent it departs from *McDowell* and on the ground that *Azadi* mis-construed the essential *ratio* of *McDowell*and had erroneously concluded that Chinnappa Reddy, J's observations were not wholly approved by the *McDowell*majority *qua* the leading opinion of Ranganath Misra, J.

Relevant observations/conclusions in *Vodafone* :

- Tracing the history and evolution of relevant principles by the English Courts commencing with *Duke of Westminster* through *W. T. Ramsay Ltd.; Furniss (Inspector of Taxes)* and *Craven*, *Vodafone* explained that the *Westminster* principle was neither dead nor abandoned; *Westminster* did not compel the court to look at a document or transaction isolated from the context to which it properly belonged and it is the task of the court to ascertain the legal nature of the transaction and while so doing to look at the entire transaction as a whole and not adopt a dissecting approach;
- *Westminster*, read in the proper context permitted a "device" which was colourable in nature to be ignored as a fiscal nullity; *Ramsay* enunciated the principle of statutory interpretation rather than an over-arching anti-avoidance doctrine imposed upon tax laws; *Furniss* re-structured the relevant transaction, not on any fancied principle that anything done to defer the tax must be ignored but on the premise that the inserted transaction did not constitute "disposal" under the relevant Finance Act; from *Craven* the principle is clear that Revenue cannot start with the question as to whether the transaction was a tax deferment/saving device but must apply the "*look at*" test to ascertain its true legal nature; and that strategic tax planning has not been abandoned.
- *McDowell* majority held that tax planning may be legitimate provided it is within the framework of law; colourable devices cannot be a part of tax planning and it would be wrong to encourage the belief that it is honourable to avoid payment of tax by resorting to dubious methods; and agreed with Chinnappa Reddy,J's observations only in relation to piercing the (corporate) veil in circumstances where tax evasion is resorted to through use of colourable devices, dubious methods and subterfuges.
- *McDowell* does not hold that all tax planning is illegal/illegitimate/impermissible. While artificial schemes and colourable devices which constitute dubious methods and subterfuges for tax avoidance are impermissible, they must be distinguished from legitimate avoidance of tax measures.
- Reading *McDowell* properly and as above, in cases of treaty shopping and/or tax avoidance, there is no conflict between *McDowell* and *Azadi Bachao* or between *McDowell* and *Mathuram.*

Vodafone on International Tax aspects of holding structures :

- In matters of corporate taxation, provisions of the Act delineate the principle of independence of companies andother entities subject to income tax. Companies and other entities are viewed as economic entities with legal independence vis-à-vis their shareholders/participants. A subsidiary and its parent are distinct taxpayers. Consequently, entities subject to income tax are taxed on profits derived by them on stand-alone basis, irrespective of their actual degree of economic independence and regardless of whether profits are reserved or distributed to shareholders/participants.
- It is fairly well-settled that for tax treaty purposes a subsidiary and its parent are totally separate and distinct taxpayers.
- The fact that a group parent company gives principle guidance to group companies by providing generic policy guidelines to group subsidiaries and the parent company exercises shareholder's influence on its subsidiaries, does not legitimize the assumption that subsidiaries are to be deemed residents of the State in which the parent company resides. Mere shareholder's influence (which is the inevitable consequence of any group structure) and absent a wholesale subordination of the subsidiaries' decision-making to the parent company, would not *per se* legitimize ignoring the separate corporate existence of the subsidiary.

- Whether a transaction is used principally as a colourable device for the division of earnings, profits and gains must be determined by a review of all the facts and circumstances surrounding the transaction. It is in the aforementioned circumstances that the principle of lifting the corporate veil or the doctrine of substance over form or the concept of beneficial ownership or of the concept of *alter ego* arises.
- It is a common practice in international law and is the basis of international taxation, for foreign investors to invest in Indian companies through an interposed foreign holding company or operating company (such as Cayman Islands or Mauritius based) for both tax and business purposes. In doing so, foreign investors are able to avoid the lengthy approval and registration processes required for a direct transfer, (i.e., without a foreign holding or operating company) of an equity interest in a foreign invested Indian company.
- Holding structures are recognized in corporate as well as tax law. Special purpose vehicles (SPV) and holding companies are legitimate structures in India, be it in Company law or takeover code under the SEBI and provisions of the Act.
- When it comes to taxation of a holding structure, at the threshold the burden is on Revenue to allege and establish abuse in the sense of tax avoidance in the creation and/or use of such structure(s). To invite application of the judicial anti-avoidance rule, Revenue may invoke the "substance over form" principle or "piercing the corporate veil" test only after Revenue establishes, on the basis of the facts and circumstances surrounding the transaction, that the impugned transaction is a sham or tax-avoidant. If a structure is used for circular trading or round tripping or to pay bribes (for instance), then such transactions, though having a legal form, could be discarded by applying the test of fiscal nullity. Again, where Revenue finds that in a holding structure an entity with no commercial/business substance was interposed only to avoid tax, the test of fiscalnullity could be applied and Revenue may discard such inter-positioning. This has however to be done at the threshold. In any event, Revenue/Courts must ascertain the legal nature of the transaction and while doing so, look at the entire transaction holistically and not adopt a dissecting approach.
- Every strategic FDI coming to India as an investment destination should be seen in a holistic manner; and in doing so, must keep in mind several factors: the concept of participation in investment; the duration of time during which the holding structure exists; the period of business operations in India; generation of taxable Revenues in India; the timing of the exit; and the continuity of business on such exit. The onus is on the Revenue to identify the scheme and its dominant purpose.
- There is a conceptual difference between a *pre-ordained transaction* which is created for tax avoidance purposes, on the one hand, and a transaction which evidences *investment to participate* in India. In order to find out whether a given transaction evidences a preordained transaction in the sense indicated above or constitutes *investment to participate,* one has to take into account the factors enumerated hereinabove, namely, duration of the time during which the holding structure existed, the period of business operations in India, generation of taxable revenue in India during the period of business operations in India, the timing of the exit, the continuity of business on such exit, etc. Where the court is satisfied that the transaction satisfies all the parameters of "participation in investment" then in such a case, the court need not go into the questions such as *de-facto* control vs. legal control, legal rights vs. practical rights, etc.
- A company is a separate legal *persona* and the fact that all its shares are owned by one person or by its parent company has nothing to do with its separate legal existence. If the owned company is wound up, the liquidator, and not the parent company, would get hold of the assets of the subsidiary and the assets of the subsidiary would in no circumstance

be held to be those of the parent, unless the subsidiary is acting as an agent. Even though a subsidiary may normally comply with the request of the parent company, it is not a mere puppet of the parent. The distinction is between having power and having a persuasive position.

- Unlike in the case of a one man company (where one individual has a 99% shareholdings and his control over thecompany may be so complete as to be his *alter ego),* in the case of a multi-national entity its subsidiaries have a great measure of autonomy in the country concerned, except where subsidiaries are created or used as sham. The fact that the parent company exercises shareholders' influence on its subsidiary cannot obliterate the decision making power or authority of its (subsidiary's) Directors. The decisive criterion is whether the parent company's management has such steering interference with the subsidiary's core activities that the subsidiary could no longer be regarded to perform those activities on the authority of its own managerial discretion.
- Exit is an important right of an investor in every strategic investment and exit coupled with continuity of business is an important telltale circumstance, which indicates the commercial/business substance of the transaction.

Analyses of the transaction and *persona* of CGP :

- Two options were available for Vodafone acquiring a controlling participation in HTIL, the CGP route and the Mauritius route. The parties could have opted for anyone of the options and opted for the CGP route for a smooth transition of business on divestment by HTIL. From the surrounding circumstances and economicconsequences of the transaction, the sole purpose of CGP was not merely to hold shares in subsidiary companies but also to enable a smooth transition of business, which is the basis of the SPA. Therefore, it cannot be said that the intervened entity (CGP) had no business or commercial purpose.
- Above conclusions, of the business and commercial purpose of CGP were arrived at despite noticing that under the Company laws of Cayman Islands an exempted company was not entitled to conduct business in the Cayman Islands; that CGP was an exempted company; and its sole purpose is to hold shares in a subsidiary company situate outside Cayman Islands.
- Revenue's contention that the *situs* of CGP shares exist where the underlying assets are situated (i.e., in India),rejected on the ground that under the Companies Act, 1956 the *situs* of the shares would be where the company is incorporated and where its shares can be transferred. On the material on record and the pleadings, held that the *situs* of the CGP shares was situate not in India where the underlying assets (of HEL) are situate but in Cayman Islands where CGP is incorporated, transfer of its shares was recorded and the register of CGP shareholders maintained.
- *Vodafone* concluded that the High Court erred in assuming that Vodafone acquired 67% of the equity capital of HEL. The transaction is one of sale of CGP shares and not sale of CGP or HEL assets. The transaction does not involve sale of assets on itemized basis. As a general rule, where a transaction involves transfer of the entire shareholding, it cannot be broken up into separate individual component assets or rights such as right to vote, right to participate in company meetings, management right, controlling right, controlled premium, brand licenses and so on, since shares constitute a bundle of rights - *Charanjit Lal Chowdhury; Venkatesh (Minor)* and*Smt. Maharani Ushadevi* referred to with approval and followed.
- Merely since at the time of exit capital gains tax does not become payable or the transaction is not assessable to tax, would not make the entire sale of shares a sham or tax avoidant.
- Parties to the transaction have not agreed upon a separate price for the CGP share and a separate price for what is called "other rights and entitlements" [including options, right to

non-compete, control premium, customer base, etc]. It is therefore impermissible for Revenue to split the payment and consider a part of such payment for each of the above items. The essential character of the transaction as an alienation is not altered by the form of consideration, the payment of the consideration in installments or on the basis that the payment is related to a contingency ("options", in this case), particularly when the transaction does not contemplate such a split up.

Lamesa Holdings B.V. :

The judgment of the Federal Court of Australia in *Lamesa* was referred to and quoted with approval both in *Azadi Bachao Andolan* and in *Vodafone*.

Factual matrix of the Lamesa *lis* :

- The issue was whether Lamesa is liable to pay income tax in Australia in respect of profits made by it from the sale of shares in an Australian public listed company - ARL. In 1992 US business became interested in acquiring Australian listed mining companies. For that purpose US investment vehicle was established, which acquired an Australian subsidiary (ARL) through an interposed Netherlands registered company - *Lamesa*. ARL owned 100% of an Australian Mining Company - ARM, which acquired a 100% interest in *Arimco*, a listed mining company incorporated in Queensland. *Arimco* owned (100%) of *Arimco* Mining, a subsidiary which held a number of mineral exploration rights. During 1994 - 1996 Lamesa sold its shares in ARL, first by way of float and the balance by way of private sale. Lamesa was assessed to capital gains on the resultant profits. Objections to these assessments were allowed but further assessments issued on the basis that profits of about $220 Million were the ordinary income of Lamesa. Lamesa's objections were disallowed. The admitted factual position was that Lamesa had no permanent establishment in Australia through which it carries on business. Further, unlike other and recent treaties, the Agreement is concerned only with tax on income and has no direct concern with capital gains.
- Lamesa successfully persuaded a learned single Judge of the Federal Court [Einfeld,J] that Article 13 of the Netherlands-Australia Double Tax Agreement ('the Agreement') did not apply to allow Australia to tax profits made by Lamesa on the sale of shares in its Australian subsidiary (ARL) since Lamesa did not acquire direct interest in land or in exploration rights in *Arimco* or *Arimco Mining*.
- Relevant provisions of the Agreement : Commencing with Art.6, the Agreement allocates the jurisdiction to tax in respect of income. Art.6 deals with income from real property and the power to tax income from real property is allocated to the State in which the real property (including mines, quarries, or natural resources) is situate. *Qua* Art.6(2), income from a lease of land and income from any other direct interest in or over land is to be regarded as income from real property. Art. 7 deals with business profits and Art.7(1) provides that the profits to an enterprise in one of the States shall be taxable only in that State unless the enterprise carries on business in the other State through a permanent establishment situated therein. Clause (5) of Art.7 statesthat for the purpose of this Article, except as provided in the Articles referred to in this Paragraph, the profits of an enterprise do not include items of income dealt in Articles 6, 8, 10 to 14, 16 and 17. While Art.13 provides that income from the alienation of real property may be taxed in the State in which that property is situated; Art. 13(2)(b)(iii) provides that real property would include, where it consists of shares or a comparable interest in a company, the assets of which consist whole or principally of direct interest in or over land in one of the States, or all rights to exploit, or to explore for, natural resources in one of the States - in the State in which the assets or the principal assets of the company are situated.
- In appeal Australian Revenue put forth four principal contentions to support the impugned assessment. The first two contentions proceed on the basis that

since Lamesa had a control over the subsidiaries *(ARL - ARM -Arimco - Arimco Mining),* in a lineal sense ARL had a direct interest in the assets of the subsidiary which was in the nature of a link in a practical and commercial sense. The transaction is thus liable to be taxed in Australiau/Art.13(2)(a). The third contention based on Art.13(2)(b)(iii) requires to treat as there having been a sale of a "comparable interest", contending that the assets of the subsidiary are a comparable interest to the case as what is exploited is the shares in a company, the assets of which consists wholly or principally of directinterests. Revenue's fourth contention invited adoption of an "in substance approach" i.e., piercing the corporate veil to treat assets of the subsidiary companies *(Arimco Mining)* as assets of the parent *(ARL* and *Lamesa).*

- The first three contentions were rejected (affirming the view of the learned single Judge). The court held that under the Agreement (Art.13), in allocating taxing power over profits arising from alienation of real property, the negotiating parties chose the place of *situs* as that having the greatest connection with the profits; under Art.13(2)(a)(iii) shares in a company are personality and since the place of incorporation of a company or the register upon which shares were registered would not form a particularly close nexus with shares to ground the jurisdiction to share profits; double tax treaties leave profits from the alienation of shares to be dealt in accordance with Art.7 in the context of an enterprise; the Agreement as a policy chose to assimilate shares or comparable interests of the kind described in Art.13(2)(iii) to real property, in limited circumstances; the assimilation would only arise by the specific provisions of the Agreement and its specific provisions set the extent to which the assimilation of shares to reality may operate. When the Agreement uses the word "comparable interest in a company" in Art.13(2), it speaks to avoid technicality inherent in the word "shares"; the Article will operate whether the property alienated was stock or warrant, provided that it is possible to say of the interest alienated that it is comparable to a share. In any event it is not possible to contend that rights to underlying assets of a subsidiary are interest in the nature of shares. That is not what the words "comparable interest in a company" are concerned with.
- The fourth contention of the Revenue (inviting lifting of the corporate veil) was also rejected observing that the agreement was intended to assimilate as reality only one tier of the company rather than numerous tiers. Separate legal personality is a doctrine running not only through common law but the civil law as well and that is consistent with the plain and quite unambiguous language which the Agreement has employed. When the Legislation speaks of the assets of one company it invariably does not intend to include within the meaning of that expression assets belonging to another company, whether or not held in the same ownership group.

- Revenue's appeal was dismissed.

Prevost Car Inc. :

- Revenue's appeal against the judgment of the Tax Court of Canada, Ottawa was rejected by the Federal Court of Appeal.

- A Canadian resident corporation - *Prevost Car Inc, (Prevost Car)* paid dividends to its shareholders - *Prevost Holding B. V. (Prevost Holding),* a corporation resident in Netherlands. *Prevost Holding* in turn paid dividends in substantially the same amount to its corporate shareholders - *Volvo* (a Swedish resident company) and to *Henlys*(a U.K. resident company), in terms of a shareholders' agreement between *Volvo* and *Henlys* dated 03-05-1995. If*Prevost Holding* were found to be the beneficial owner, the rate of withholding tax under the Canadian Income Tax Act r/w Art.10 of the Tax Treaty would be 5%; if *Volvo* and *Henlys* were to be found the beneficial owners of the dividend, under provisions of the Canadian domestic Tax law r/w relevant provisions of the Canadian-Swedish Tax Treaty and the Canadian - UK Tax Treaty, the withholding tax would be 15% and 10%, in respect of*Volvo* and *Henlys,* respectively.

- The Tax Court of Canada found the beneficial owner to be *Prevost Holding BV* and not *Volvo* or *Henlys* as claimed by the Revenue.
- Canadian Revenue proceeded against *Prevost Car* on the basis that the beneficial owner of the dividends were the corporate shareholders of *Prevost Holding, i.e., Volvo* and *Henlys.*
- The Canada - Netherlands 1986 Tax Treaty (1986 Tax Treaty) was based on the OECD model Tax Convention on Income and on Capital, 1977 (Model Convention). Art.10(1) of the 1986 Tax Treaty provided that dividends *paid by a company which is a resident of Contracting State to a resident of the other Contracting State may be taxed in that other State.* Article 10(2) provided *however, such dividends may also be taxed in the State of which a company paying the dividends is a resident, and according to the laws of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed : (a) 5% of the gross amount of the dividends if the beneficial owner is a company (other than a partnership), that holds directly or indirectly at least 25% of the capital or at least 10% of the voting power of the company paying the dividends... ...*
- The expression "beneficial owner" or the equivalent expressions in the French or the Dutch versions of the Treaty are not defined either in the 1986 Treaty or the Model Convention. The relevant commentary of Art.10 of the Model Convention stated that the limitation of tax in the State of source [under para - 10(2)] is not available when an intermediary, such as an agent or nominee is interposed between the beneficiary and the payer, unless the beneficial owner is a resident of the other Contracting State; States which wish to make this more explicit are free to do so during bilateral negotiations. The Tax Court noticed that there were no negotiations betweenCanada - Netherlands which explicated the expressions in Art.10(2).
- The revised 2003 OECD commentaries on Art.10 explained that the term "beneficial owner" in Art.10(2) of the Model Convention is not used in a narrow technical sense but should be understood in its context and in the light and the object of the purposes of the Convention, including avoiding double-taxation and the prevention of fiscal evasion and avoidance. Art.3(2) of the 1986 Treaty (similar to Art.3(2) of the DTAA) provided that in the application of the convention by a State any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which the Convention applies.
- The Tax Court after due consideration including of expert opinion, dictionary meanings of the expressions "beneficial" and "owner" and the meaning given to the expression "beneficial owner" in decisions of the Canadian Supreme Court, concluded that the beneficial owner of dividends is a person who receives the dividends for his/her own use and enjoyment and assumes the risk and control of the dividend received; is the person who enjoys and assumes all the attributes of ownership; the dividend is for the owner(s) own benefit and this person is not accountable to anyone for how he deals with the dividend income.

- RIP ACJ (for the Tax Court of Canada) observed that when corporate entities are concerned, one does not pierce the corporate veil unless the corporation is a conduit for another person and has absolutely no discretion as to the use or application of funds put through it as a conduit, or has agreed to act on someone else's behalf pursuant to that person's instructions without any right to do other than what that person instructs it, such as a stockbroker who is a registered owner of the shares it holds for clients. This is not the relationship between PHBV and its shareholders – *Volvo* and *Henlys*. The Court found no evidence that *Prevost* Holding was a conduit for*Volvo* and *Henlys* despite it having no physical office or employees in the Netherlands or elsewhere; nor was there evidence that dividends from *Prevost Car* were *ab initio* destined for *Volvo* and *Henlys* with *Prevost Holding*as a mere funnel for flowing of dividends. The Court observed that *Prevost Holding* was a statutory entity carrying on business operations and corporate activity in accordance with the Dutch law and under which it wasconstituted; it was not a party to the shareholders' agreement (dated 03-05-1995 between *Volvo* and*Henlys);* and neither *Volvo* nor *Henlys* could take action against *Prevost Holding* for failure to follow the dividend policy described in the shareholders' agreement. The appeal of *Prevost* was allowed.

Rejecting Revenue's appeal, the Federal Court of Appeal ruled that Crown's interpretation (that the expression "beneficial owner" must mean that person who can, in fact, ultimately benefit from the dividend) appears nowhere in the OECD documents and such interpretation would jeopardize the relative degree of certainty and stability that the Tax Treaty seeks to achieve. The Appellate Court added that the Crown was inviting the Court to adopt a pejorative view of holding companies which neither the Canadian domestic taw, the international community nor the Canadian Government through the process of objection, have adopted.

It is significant to note that in *Prevost Car Inc.* there was a tax treaty shopping. Mr. Backstrom of *Volvo* had stated that tax implication was a consideration, though not an over-riding consideration; and that a Dutch holding company - *(Prevost Holding B.V.)* was chosen on professional recommendation *inter alia* to avoid tax schemes from UK or Sweden and other international tax issues, for effective management and control of the holding company. Further, minutes of the appellant, of *Prevost Car Inc.* shareholders' meeting dated 23-03-1996 had recorded that the meeting was attended by proxies for the parent companies *(Volvo* and *Henlys)* of thesubsidiary, at a time when the appellant had only one shareholder - *Prevost Holding B. V.*

<u>Precedents on the interpretation/construction of documents</u> :

The decisions of the Supreme Court in *Radha Sunder Dutta* and *Puzakklal Kuttapu;* in *Ford v. Beech; Inntrepreneur;West Bromwich Building Society;* and in *Hideo Yoshimoto,* all spell out principles pertaining to construction of documents.

Lord Hoffmann in the leading opinion of the House of Lords (with which the other learned law Lords concurred) in *West Bromwich Building Society,* while observing that almost all the old intellectual baggage of "legal" interpretation was discarded, summarized the principles by which contractual documents are presently considered, as under :

(1) *Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.*

(2) *The background was famously referred to by Lord Wilberforce as the 'matrix of fact', but this phrase is, if anything,* an*understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the documents would have been understood by a reasonable man.*

(3) *The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective* intent. *They are admissible only in* an *action for rectification. The law makes this distinction for reasons of practical policy and,* in *this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear. But this is* not *the occasion on which to explore them.*

(4) *The meaning which a document (or* any *other utterance) would convey to a reasonable man is* not *the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may* not *merely enable the reasonable* man *to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax (Mannai Investment Co Ltd v. Eagle Star Life Assurance Co Ltd (1997) All ER 352, (1997) 2 WLR 945.*

(5) *The 'rule' that words should be given their 'natural and ordinary meaning' reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents.* On *the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had. Lord Diplock made this point more vigorously when he said in Antaios Cia Naviera SA v. Salen Rederierna AB, The Antaios (1984) 3 All ER 229 at 233, (1985) AC 191 at 201.*

'... if detailed semantic and syntactical analyses of words in a commercial contract is going to lead to a conclusion that flouts business common sense, it must be made to yield to business common sense.'

In *Hideo Yoshimoto,* Thomas, J for the New Zealand Court of Appeal after quoting with approval the restatement of law by Lord Hoffmann in *West Bromwich Building Society* and noting that the five principles Lord Hoffmann articulated were reiterated and applied by the New Zealand Court of Appeal in *Boat Park Ltd. v. Hutchison*[64], referred to a paradigm shift in the interpretative principles noticed by W*igmore*[65] and agreed with the observation : *The history of the law of interpretation is the history of a progress from a stiff and superstitious formalism to a flexible rationalism;* and proceeded to state : *The cardinal rule of contractual interpretation must be to ascertain the intention of the parties. To the extent this rule is not implemented, the courts must incur the criticism of failing to give effect to the reasonable expectations of the parties. Surely the parties are reasonably entitled to expect that the courts will strive to ascertain their true intention or, certainly, not to arrive at a meaning of their contract which is at variance with their actual intention. They cannot expect that the judicial exercise of construing their contract will be buried under a stockpile of excessive formalism.*

Lewison[66] refers to a lucid summary of the relevant principles set out in the judgment of Saville, J in *Vitol B.V. v. Compagnie Europeene des Petroles*[67] : *The approach of the English law to questions of the true construction of contracts of this kind is to seek objectively to ascertain the intentions of the parties from the words which they have chosen to use. If those words are clear and admit of only one sensible meaning, then that is the meaning to be ascribed to them - and thatmeaning is taken to represent what the parties intended. If the words are not so clear and admit of more than one sensible meaning, then the ambiguity may be resolved by looking at the aim and genesis of the agreement, choosing the meaning which* *seems to make the most sense in the context of the contract and its surrounding circumstances as a whole. In some cases, of course, having attempted this exercise, it may simply remain impossible to give the words any sensible meaning at all in which case they (or some of them) are either ignored, that is to say, treated as not forming part of the contract at all, or (if of apparent central importance) treated as demonstrating that the parties never made an agreement at all, that is to say, had never truly agreed upon the vital terms of their bargain.*

It is thus reasonable to infer, on the guidance received from the matrix of precedents and authority referred to, that curial role in the construction of documents/instruments is to identify the intention of the parties. The role is in a sense facilitative, i.e., to ascertain what the mutual intentions of the parties were as to the legal obligations each assumed by the words in which they sought to express them, to iron out the creases where there is a contextual,grammatical or syntactical deficit; but not normally to manipulate the construction, with a purported intent of achieving an elusive *fair outcome* in the case before it.

18. <u>Analyses of the relevant matrix of facts, transactional documents and surrounding circumstances :</u>

Revenue points out (in its written submissions) that ascertainment of the real *persona* of ShanH and the chargeability of the transaction in issue, to tax in India is dependent on determination of the following core criteria :

(i) Whether ShanH had a distinct corporate status so as to be the legal/ beneficial owner of SBL shares?

(ii) What was the extent and degree of control of MA/GIMD over ShanH in the light of the SPA's, SHA's and other transactional documents?

(iii) Was there an assignment by MA/GIMD in favour of ShanH; or in the light of the transactional documents, whether it could be legitimately inferred that from inception, SBL shares vested in ShanH as a legal owner?

(iv) Merely since a joint venture (ShanH) was holding SBL shares, whether the corporate status of ShanH is immune to enquiry as to its commercial substance?

(v) What is the subject matter of the transaction involved in the SPA dated 10-07-2009 between MA/GIMD and Sanofi? and

(vi) Who is the transferor of the right, title and interest in SBL shares; and who realized the capital gains on the transfer of SBL shares?

<u>Revenue interpretation of the ShanH persona</u> :

The case of the Revenue is premised around the following inferences from the transactional documents :

- SBL was a vibrant and sound commercial and economic proposition having developed and commercializedIndia's first R-DNA Hepatitis B vaccine which was pre-qualified by WHO and was since supplied to UN Agencies as well. The business of SBL thus generated and developed a huge market potential. This occasioned Sanofi approaching MA (a majority stakeholder in SBL) for acquisition of the business and economic interests in SBL.
- Since the purchasers needed to carry out due diligence of SBL for which access to SBL records was necessary, a confidentiality and non-disclosure agreement dated 12-02-2009 was entered into between MA and Sanofi. The parties to this agreement were MA, SBL and Sanofi. ShanH was not a party to this agreement. If the

intention was sale of ShanH shares only, there appears no justification for involving SBL along with MA in the 12-02-2009 agreement.

- The basis of Sanofi's offer dated 22-06-2009 is the assumption that SBL would be awarded a minimum annual allocation of thirty-five million doses of the vaccine developed by SBL. The payment and quantum of thepurchase price (for acquisition by Sanofi of ShanH shares) is conditioned upon certain contingencies relating to the business prospects of SBL and not ShanH.

- SPA dated 10-07-2009 (between MA/GIMD and Sanofi, for acquisition of ShanH shares) contains elaborate references to SBL, revealing that the control, management of commercial enterprise and of the assets of SBL was the basis for the transaction, viz.,
  (i) the definition clause in the SPA mentions SBL; "Applicable law" in relation to SBL is defined to mean Indian Law; "Fully diluted basis", "Key employees", "Lien", "Material Adverse Effect", are all expressions defined with reference to SBL;
  (ii) Section 1.3(b)(v) of the SPA stipulates that the sellers (MA/GIMD) should *inter alia* deliver to the buyer (Sanofi) the share certificates of SBL held by ShanH. This leads to the inference that ShanH was a mere nominee of MA/GIMD and mere transfer of ShanH shares would not have consummated the real transaction which was the transfer of SBL to Sanofi, as the underlying transaction;
  (iii) Other provisions of the SPA such as requirement of resignation of SBL Directors; Meeting of SBL Board for ensuring resignation of existing Directors and appointment of new Directors; requirement of the sellers delivering a copy of the long-term supply agreement between SBL and UNICEF relating to supply of vaccines to Sanofi; provisions relating to adjustment of the closing price with reference to SBL's past accounting practice; payment of the price complement in Section 1.5(b) being dependent on phases of clinical study of vaccines developed by SBL, submission of product to WHO, progress in relation to new drugs, etc., reveal that the underlying transaction was the commercial substance of SBL. The above and other provisions of the SPA disclose that the real intent of the parties to the transaction is acquisition of SBL (the Indian company) and its business, driven primarily by the development of vaccines by SBL and the market potential consequently generated. This is so since ShanH is an entity with no commercial substance and the SPA could not have intended acquisition of shares of a "non-descript" company (ShanH).

<u>SPA dated 06.11.2006</u> :

- Terms of the SPA dated 06-11-2006 indicate MA's intent to participate in SBL by obtaining ownership/control over 60% of the paid-up capital and issued equity share capital of SBL; and stipulate that purchase of SBL shares by MA or any other subsidiary wholly owned by it shall be deemed purchase by MA.
- MA paid US $200,000 to SBL for purchase of stamp duty and Clause 4(7) of the SPA obligates SBL to handover duly stamped share transfer forms to MA (not to ShanH or any other subsidiary).

- Clause 4(8) of the SPA requires MA and UOIL to enter into 10% and 90% Escrow agreements; Schedule 2 to this SPA defines 10% and 90% Escrow agreements as those executed between the respective banks (acting as Escrow agents); and MA and UOIL. ShanH is not contemplated to be a party to the Escrow agreements.
- There is no material to indicate that payments into the Escrow accounts were made by ShanH; the SPA requires MA to make such payments. Later if ShanH records payments made into Escrow accounts as loan from MA, that would not alter the factual position that payments at the relevant time were made by MA directly into Escrow accounts.
- Other clauses of the SPA [4.9(b), 4,9(c), 4.11, 5.2(b), 5.6, 7.2 and 12] clearly indicate ShanH to be a mere nominee of MA. Thus, even if SBL shares are transferred in the name of ShanH it is only as a nominee of MA.

- Though before the AAR and this Court it was initially the stand of the petitioners that ShanH is the assignee of MA (in the preamble to the SPA, MA is defined to include its successors and permitted assignees), petitioners in their rejoinder have taken the categorical stand that there was no need for an assignment since the ownership of SBL shares vested in ShanH since inception and without any assignment from MA.
- Though Schedule 1, Part B of the SPA enumerates ShanH to be the holder of SBL shares, in the totality of the circumstances ShanH must be considered a nominee of MA and the ownership of the SBL shares continues with MA.

<u>Shareholder's agreements (SHA's) dated 07-11-2006</u> :

- There were two SHA's (substantially similar), both dated 07-11-2006 :
  (a) between MA, SBL and Varaprasad Reddy; and
  (b) between MA, SBL, Khalil Ahmed and UOIL.
- ShanH is not a party to the SHA's despite the claim that it is a registered shareholder of SBL shares.
- In the SHA's though MA is again defined to include its successors and permitted assignees, there being noassignment by MA in favour of ShanH, MA must be inferred to be itself and not its successor or permitted assignee.
- Various clauses of the SHA's [2, 2.2, 3, 4.2, 4.6, 4.7, 5.1, 7.1 and 8.3] indicate (in the absence of any assignment of SBL shares by MA in favour of ShanH) that it is MA which owned the SBL shares; ShanH being a mere nominee or *alter ego* of MA.

<u>Amended AOA of SBL</u> :

- SBL Articles of Association were amended to give effect to the SPA dated 06-11-2006 and SHA's dated 07-11-2006. In the amended AOA, MA is defined to mean itself; not including its successor or assignee. There is no mention of ShanH; and MA is depicted as the legal and beneficial owner of the SBL shares.

- Clause 45A of the amended AOA stipulates :

> *45A. The Transfer of shares held by MA or VR (including his family members) or KA shall be subject to the restrictions/terms of anyagreement entered into between the MA, VR and/or KA dated on or prior to the Completion Date, which restrictions shall also be setout by way of restrictive legend on the share certificate so held or, in the case of dematerialized shares, shall also be communicated in writing to the concerned depository of the Company and the concerned depository participant(s).*

- Provisions of the amended AOA belie the petitioners' claims that ShanH was the shareholder of SBL in its independent, corporate status or as the assignee of MA.

Distillate of conclusions by Revenue on the transactional documents :

(a) ShanH is a company of no commercial substance :

- ShanH is a holding company which has never operated, owned nor currently operates or owns any business or any material or fixed assets other than SBL shares; and neither had nor has employees on its rolls.
- Even prior to ShanH incorporation (on 31-10-2006), due diligence with respect to SBL was carried out on themandate of MA (legal, financial, tax and environmental due diligence) to assist MA in the evaluation of SBL. GIMD was not associated at this stage and became a JV partner in ShanH later, vide the SPA dated 08-03-2007.
- MA Board meeting dated 26-10-2006 (prior to ShanH incorporation on 31-10-2006) resolved to allow itssubsidiary company ShanH to acquire participation of approximately 54% of SBL shares; and authorized theChairman and General Director of MA (to be free to act separately or delegate their powers to any thirdperson), to take any decision in ShanH in order to facilitate ShanH acquire a majority shareholding of SBL; to sign shareholder's agreement, the contract of deposit of money and generally any legal documentnecessary to achieve the projected acquisition.

(b) ShanH is neither the legal nor the beneficial owner of SBL shares.

(c) ShanH was not an assignee of MA in respect of SBL shares.

(d) ShanH did not make payments for acquisition of SBL shares. Subsequent accounting of the purchase consideration (by MA) as a loan from MA in its accounts prepared later, would not alter the reality.

(e) The expression "MA" does not include ShanH in the SPA or SHA's, as no assignment was made by MA in favour of ShanH.

(f) ShanH had no control over the management of SBL nor enjoyed any rights or privileges of a shareholder of SBL.

(g) ShanH was thus a mere nominee of MA in relation to SBL shares.

Our analyses of the ShanH persona *qua* the transactional documents and surrounding circumstances :

It is pleaded and contended by MA (and not contradicted by Revenue) that :

(i) It is and has been the inveterate policy and practice of the MA group that all investments out of France are routed through a subsidiary incorporated in MA's natural home jurisdiction (France). This business policy and practice is adopted as an organizational norm since it facilitates MA to maintain distinct lines of business such as in-vitro vaccines; food quality and nutrition; prophylactic vaccines, immuno therapy in developed countries; and immuno therapy in developing countries, etc. Further, such organizational structure enables MA to identify and group various activities by business units and to possibly have other investors/partners (shareholders) in each business unit; besides ensuring risk containment.

(ii) MA group also explores external investors into specific entities engaged in specific businesses. Until 2007, GIMDwas an investor in TSGH, a special purpose vehicle (SPV) set up in France, which in turn held shares in ABL (USA) and Transgene (France). Setting up of SPVs in the home jurisdiction (France) is considered necessary to ensureinterests of the investors (who/which though not sectoral experts are looking to maximize their return on investments) by granting investors, participative and protective rights (preemptive rights, liquidity undertaking, joint transfer applications, joint assignment rights, etc.) through the SPV route.

(iii) Consistent with the aforesaid policy and practice and in conformity with the investment pattern adopted in previous transactions, ShanH was incorporated. Without ShanH incorporation as a distinct investment entity, it would not have been possible to interest GIMD (with no expertise in the field of vaccines) to come on board ShanH, as an investor partner. Familiarity with the home jurisdiction catalyzed incorporation of ShanH as a JV inFrance; and without a French JV company, the Foreign Direct Investment in India (in SBL) would not have occurred.

Genesis and Registration of ShanH :

- Negotiations for the proposed investments in SBL began in August, 2006. In the normal course as an investor, due diligence on SBL was carried out at the instance of MA. Subsequent to due diligence processes and negotiations and consistent with the business policy and practices (of the MA group), MA incorporated ShanH, initially as its wholly owned subsidiary, on 31-10-2006, with a nominal share capital of 370 shares, as an entity registered and resident in France.

Escrow agreements :

- On 02-11-2006 an Escrow agreement was entered into between ShanH (the purchaser); UOIL (the seller); andCalyon (a French Banking Institution, the Escrow Agent).

- MA is not a party to this agreement. The agreement reveals ShanH to be the intended purchaser of SBL shares held by UOIL under an SPA to be executed between the seller, the purchaser and other parties. Clause-4 of the agreement requires ShanH (the purchaser) to credit the specified amount in "Euros" to the Escrow account. Other clauses of the agreement establish ShanH to be the prospective purchaser of SBL shares from UOIL (the seller) and others.
- Initially (during oral argument) it was pointed out by Revenue that Mrs.Dominique Takizawa (a representative ofMA) was the signatory to the Escrow agreement on behalf of ShanH (and not a ShanH official), thereby suggesting that the entire transaction of purchase of the SBL shares was for the legal and beneficial ownership by MA, with ShanH being a mere "smoke-screen" or a nominee of MA. On behalf of the petitioner (MA) it was explained that on account of certain travel glitches, a ShanH representative could not be present to sign the Escrow agreement and in the circumstances a representative of MA (the unique and singular shareholder ofShanH, as on that date) signed the agreement on behalf of ShanH. In its written submissions however, Revenue did not pursue this line of interpretation.
- Though the authorized signatory to the Escrow Agreement (and in fact almost all agreements) on behalf of UOIL was Mr. Khalil Ahmed, Revenue was not heard to contend that UOIL is the *alter ego* of Mr. Khalil Ahmad.
- On 06-11-2006 "joint instructions" from authorized representatives of the purchaser and seller were addressedto the Calyon Bank (the Escrow Agent) intimating that the transaction contemplated under the share purchaseagreement (dated 06-11-2006) executed amongst the parties has been completed and Calyon is authorized to operate the Escrow account in terms of the said agreement. The "joint instructions" was signed by Mr. Philippe Sans (President, ShanH) apart from Mrs.Dominique Takizawa; the seller being represented by its signatory, again Mr. Khalil Ahmed.

- Another Escrow agreement was entered into on 03-11-2006 between ShanH (the purchaser); UOIL (the seller); and Blom Bank, Switzerland (the Escrow Agent). Schedule II to this agreement specified the authorized representative of the purchaser to be Mrs.Dominique Takizawa and Mr. Michel Dubois, the Secretary General and Director General, respectively of MA and Mr. Philippe Sans, President of ShanH.

- Copy of the general ledger of ShanH reveals that remittances into the Escrow accounts, in Calyon Bank and Blom Bank (the Escrow agents) were by ShanH. Payments to SBL on account of the direct subscription of its shares were also by ShanH.

<u>Acquisition of SBL shares by ShanH</u> :

- On 26-10-2006 (earlier to ShanH incorporation and registration as a French resident company on 31-10-2006) MA's Board authorized its proposed subsidiary ShanH to acquire a participation representing around 54% (shares) in SBL.

- It is contended on behalf of the petitioners and this Court believes this to be the case, that though ShanH was not yet incorporated by 26-10-2006, ShanH as a corporate entity (with MA as the unique shareholder, being the owner of 370 shares representing the capital stock of ShanH) was authorized to acquire a majority stake in SBL, since the necessary documents in relation to the incorporation of ShanH (including the MOA, AOA and the By-laws, etc.) were finalized and being processed for filing with the Registrar of Companies in France.

- The 06-11-2006 SPA, the two SHA's dated 07-11-2006; and the several applications for and consequent Government approvals granted, recognized that the purchase of SBL shares since inception was only by ShanH.

<u>The SPA dated 06-11-2006</u> :

- The 2006 transaction involved purchase of SBL shares by ShanH, from foreign nationals (the Omanis) and other nonresident Indians. The 06-11-2006 SPA *qua* which the transaction came about specifically designated ShanH as the purchaser of the shares and the permitted assign of MA. MA is defined in the SPA to include its successors and permitted assignees.

- Clause 2.1 of the 06-11-2006 SPA specifically states that MA *may cause ShanH or any other wholly owned subsidiary to purchase the Sale Shares and for the purposes of this Agreement such purchase shall be deemed as a purchase made by MA and any such purchaser will be entitled to all the benefits accruing to MA including the representations, warranties and indemnities contained herein.*

- Schedule I - Parts B and C clearly establish that the SBL shareholding is by ShanH.

- In view of the MA Board's decision dated 26-10-2006; MA being defined in the 06-11-2006 SPA (subject to a contrary context) to mean and include its successors and permitted assignees; provisions of Clause 2.1 of this SPA clearly facilitating MA to cause ShanH (by now a French registered and resident company) to purchase SBL shares, clearly stipulating that such purchase shall be deemed a purchase by MA and any such purchaser would be entitled to all the benefits accruing to MA including the representations, warranties and indemnities contained in the SPA, it is clear and the inference is compelling that participation in SBL (by acquisition of shares) is by ShanH and no assignment by

MA to ShanH of the SBL shares was necessary to constitute ShanH the legal and beneficial owner of SBL shares.

- Post the negotiations and due diligence of SBL by MA in August/September, 2006, events appeared to have gathered a momentum culminating in MA's Board decision dated 26-10-2006. By this date the preparatory work for incorporation of ShanH was in full steam and ShanH was therefore determined to be the entity which would acquire a majority stake in SBL. Within five days thereafter ShanH was incorporated and registered as a French resident company. The SPA dated 06-11-2006 followed, clearly indicating (Clause 2.1) the unqualified liberty of MA to cause ShanH to purchase SBL shares.

<u>Response to Revenue interpretation of amended SBL AOA</u> :

Petitioner's assert that Revenue interpretation and inferences premised on the amended SBL-AOA provisions areerroneous and proceed on a misconception and a strained construction of the relevant documents and surrounding circumstances. Petitioners state that the amended memorandum and AOA form part of the SHA's dated 07-11-2006 and are referred to in the definition of "amended charter documents" and in Clause 1.2(f) to the Memorandum and Articles of Association of SBL. It is further contended that *qua* Clause 45(A) of the amended AOA, the Articles are subject to terms of any agreement. This means the 06-11-2006 SPA and this SPA sets out all the rights of MA including the right to assign or cause ShanH to purchase SBL shares. Article 45-A of the amended AOA also refers to "completion date" which is defined in the 06-11-2006 SPA (entered into between MA, SBL and the sellers). Since the amended SBL memorandum and AOA must be read in consonance with the governing and contemporaneous documents, viz., the SHA's dated 07-11-2006 and the 06-11-2006 SPA, holistically considered, it is ShanH and not MA which holds and is the beneficial owner of SBL shares. Petitioners further refer to the explanatory statement *(pursuant* to Section 173(2) of the Companies Act, 1956) appended to the EGM notice of SBL, scheduled to be held (and held) on 14-02-2007. Item.1 of the explanatory statement pertains to "Alteration of Articles of Association" and reads :

> *Merieux Alliance (MA), a French Company, has purchased major shareholding from the existing shareholders and currently holds 60% equity of the Company <u>through its investment company, ShanH.</u> As per the agreement entered with the majority shareholders, the Company has to insert new articles and delete some existing articles and also substitute some new terminology by replacing some of the existing articles.* (emphasis added)

Petitioners, assert that reference to only MA in the amended AOA of SBL does not therefore legitimize the Revenue inference that ShanH is not the holder and beneficial owner of SBL shares.

<u>Did MA assign SBL shares to ShanH</u> ?

- As earlier adverted to in brief, one of Revenue's key contentions is that though the 06-11-2006 SPA defines MA to mean and include its successors and permitted assignees, there was no deed of assignment by MA in favour of ShanH (assigning SBL shares) brought on record. Revenue suggests that it is therefore legitimate to infer that since inception it is MA and not ShanH which is the legal and beneficial owner of SBL shares.
- The above contention does not commend acceptance. As earlier noticed Clause 2.1 of the 06-11-2006 SPAspecifically stipulates that MA may cause *inter alia* ShanH to purchase SBL shares; for the purpose of the SPA such purchase shall be deemed to be purchase by MA; and such purchaser entitled to all the benefits accruing to

MA including the representations, warranties and indemnities, contained therein. On behalf of MA it is specifically contended that there is no deed of assignment nor is one necessitated, since ShanH had purchased and owns SBLshares since inception.

- Our analysis shows that ShanH (and not MA) acquired SBL shares. In view of this circumstance and other reasons to be recorded by us *infra*, on analyses of the relevant transactional documents and the surrounding circumstances, we hold that absence of a deed of assignment (of SBL shares by MA in favour of ShanH) does not establish that MA and not ShanH is the legal and beneficial owner of the SBL shares.
- Since as on this date MA was the unique shareholder of ShanH, we do not consider it incongruent that the 06-11-2006 SPA should record MA to be a party to the SPA while clearly stipulating that ShanH would be authorized by MA to purchase SBL shares. The evolution of ShanH as a distinct entity (though a wholly owned subsidiary of MA at this stage) was an organic and nascent process culminating eventually into a JV. More of this later.

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Two SHA's dated 07-11-2006 :

- Revenue contends that ShanH is not a party to the SHA's despite the claim of being the registered holder of SBLshares. Petitioners however contend that the SHA's ought to be read in consonance with the 06-11-2006 SPA which clearly evidences that ShanH (with MA as the unique and sole shareholder as on 07-11-2006) and notMA is the owner of SBL shares.
- Though ShanH is not a party to the SHA's and only MA is a party, the recitals of SHA's clearly indicate that MA had decided to invest in the company by acquiring SBL shares from UOIL under the SPA. The 06-11-2006 SPA is clearly indicated by definition : *the share purchase agreement dated November 06, 2006 amongst MA, UOIL, VR, KA, HE and GS.*

The ShanH partnership agreement dated 08-03-2007 between MA and GIMD :

- This partnership agreement was entered into in the presence of ShanH (described for short, as the "Company") represented by its president Mr. Philippe Sans. Recitals of this agreement clearly indicate that on 07-11-2006 ShanH (not MA) acquired 8.9 million shares of SBL representing (as on the date of their acquisition) 61.4% of the registered capital and voting rights of SBL. GIMD agreed to subscribe for a minority interest in the registered capital of ShanH purely as a strategic investor. This is clear from the recitals in Clause - C of the agreement, which stipulates that GIMD agreed (to the proposals by MA) to subscribe for the registered capital of ShanH in recognition of the prospect of ensuring liquidity of its investment *by, in particular, the introduction of the company* (ShanH) *on a stock exchange, the transfer of shares or the takeover - merger by a listed company, within four to six years as from the date of the agreement,* which MA agreed to.
- Consequent on the agreement, the capital of ShanH stood increased from 370 shares to 6,00,000 shares with MA and GIMD holding 80% and 20% of the ShanH shareholding, respectively.
- Clause 3.1 of the agreement (setting out representations and warranties of MA) stipulates that :
  (i) ShanH has been duly incorporated and validly listed with the Lyon Commercial and Companies Registry(France);

  (ii) As on date MA holds all of the registered capital of ShanH;

  (iii) On 07-11-2006 ShanH (not MA) acquired and to date holds 8.9 million shares representing (as on the date of acquisition), 61.4% of SBL registered capital and voting rights; according to the terms of the acquisition, ShanH has the control of SBL and its subsidiary Shantha West Inc, as defined in the relevant Article of the(French) Commercial Code; and copies of the SPA and SHA's (dated 06-11-2006 and 07-11-2006) areappended to the agreement.

- Other clauses of the agreement (clauses 4 to 6 and 10, in particular) clearly indicate GIMD's entitlement (in proportion to its investment) to participation and decision-making in the management, affairs and control of ShanH.

- The terms of this agreement legitimize and compel the inference that ShanH is (post the agreement) a JV entity of MA and GIMD.

- GIMD made a cash contribution of €12 million to pick up the 20% share in ShanH (Article 2 of the agreement). It is inconceivable that a major business conglomerate with vast international experience and business savvy in defence systems, avionics and the like would have committed such huge investment to pickup a 20% stake in ShanH, if MA and not ShanH were the legal and beneficial owner of SBL shares. The only commercial substance of ShanH (a company registered and resident in France) was as an investment vehicle with participation as a majority shareholder holding 61.4% of SBL shareholding (as on the date of this agreement).
- Pursuant to the ShanH partnership agreement dated 08-03-2007 and GIMD consequently acquiring 20%participation in ShanH (shares), it is clear ShanH evolved into a JV company.
- On 25-03-2009 ShanH capital was increased by 1,00,000 shares. The entire shareholding of ShanH was subscribed proportionately (80:20 percent), by MA and GIMD.

<u>Entry of Mr.Georges Hibon into ShanH</u> :

- In May, 2009 Mr.Georges Hibon (associated with Connaught Vaccines and Merck; neither an employee nor director in MA) purchased 10,400 shares from MA and 2,600 shares from GIMD in ShanH.

- At this stage, the capital of 7,00,000 shares in ShanH was held : 78.5% by MA; 19.6% by GIMD and 1.9% by Mr. Georges Hibon.
- Acquisitions by ShanH of SBL shares (subsequent to its evolving from being a wholly owned subsidiary of MA to a JV; initially of MA and GIMD and thereafter of MA, GIMD and Mr. Georges Hibon, i.e., post the 08-03-2007 SPA) require to be reiterated :

  (i) ShanH acquired in 2007 a further 20,000 shares from UOIL; 17,500 shares from Indian resident shareholders; and 4,23,600 shares from non-resident shareholders of SBL.

  (ii) In 2008 acquired a further 1,90,460 shares from UOIL; 10,78,920 shares from Indian resident shareholders; and 14,57,150 shares from non-resident shareholders of SBL.

  (iii) In March, 1998, there was a capital increase of SBL, viz., 4,49,830 shares, subscribed directly by ShanH.

  (iv) In July/August, 2009 ShanH purchased a further 5,57,500 shares from UOIL and 2,00,000 shares fromIndian resident shareholders of SBL.

(v) The SBL Board meeting dated 19-03-2008 (copy of the minutes on record and not contested) took note of the minutes of the share transfer committee meeting held on conclusion of the previous board meeting held on 18-12-2007 along with the statement of share transfers disclosing transfer of SBL shares held by VR, members of his family and UOIL, in favour of ShanH. The statement appended to Item.8 (of the minutes of this meeting) sets out the number of shares transferred, particulars of the transferor, distinctive numbers of the certified share certificates and the consideration for which the shares were transferred, including the stamp duty thereon. ShanH is recorded as the transferee. This meeting also recorded approval of the SBL board for allotment of 4,49,830 SBL shares in favour of ShanH, on preferentialallotment basis for a total consideration of Rs.20,24,23,500/-.

(vi) As on 31-03-2007 (post GIMD acquisition of 20% stake in ShanH, vide the partnership agreement dated 08-03-2007) ShanH holding in SBL was around 61.4%. MA, the 80% shareholder in ShanH by itself had thus no controlling interest. Only ShanH, the JV of MA/GIMD had the controlling interest, i.e., 61.4%, in SBL.

Correspondence with Indian authorities :

- 18-04-2007: SBL addressed FIPB intimating that UOIL had sold 89,96,750 shares to ShanH and that ShanH holds a majority of shares in SBL, i.e., 61.40% of the SBL equity; that approval is sought for allotment of 15,00,000 new equity shares by way of fresh issue of capital from SBL to ShanH; and for transfer of 17,00,000 shares from existing NRI's, OCB's and Indian shareholders to ShanH; i.e., about 12.60% of the current equity capital of SBL, in addition to ShanH's current holding of about 61.40% of SBL shares.
- 13-06-2007 : FIPB (in response to SBL's letters dated 18-04-2007, 30-05-2007 and 08-06-2007) conveyed approval of the Indian Government to allotment of 15,00,000 new equity shares by way of a fresh issue of capital from SBL to ShanH, (described as a French company); and for transfer of 17,00,000 shares from existing NRI's, OCB's and Indian shareholders to ShanH, in addition to its existing shareholding of ShanH of about 61.40% of SBL shares. These proceedings of FIPB record that on completion of the earlier approved transaction and the current proposed transaction, the shareholding of SBL would *inter alia* reflect ShanH holding70.70% of SBL shares, i.e., 1,21,69,750 shares.

- 12-04-2007 : ShanH addressed FIPB intimating its current holding of 61.4% of SBL shares and seeking permission to buy 70,00,000 equity shares from existing NRI's, OCB's and Indian resident shareholders and to subscribe to 15,00,000/- new shares, in SBL and grant of sanction to SBL to enable ShanH to purchase equity shares and subscribe to new shares, as indicated in its letter.

- 29-04-2008: FIPB informed SBL (in response to SBL's letters dated 15-02-2008, 21-03-2008 and 22-04-2008), that transfer of shares from NRI's and Indian resident shareholders of the SBL to ShanH is permissible under the automatic route; and that SBL's request for transfer of its 2,00,000 shares from OCB to ShanH, if included in the permission conveyed by the FIPB approval dated 13-06-2007 (supra), no further approval is required.

- 08-07-2009 : SBL intimated FIPB that it has equity participation by NRI's, foreign institutional investors and foreign investors, for which it obtained approvals from the Secretariat for Industrial Approval (SIA), FIPB and RBI; that the current shareholding pattern of SBL includes 78.75% shareholding by ShanH; and that MA intends to purchase through its existing subsidiary ShanH or through any other of its subsidiaries the balance 21.25% of SBL shareholding from existing shareholders, NRI's, Indian residents and OCB's and approval for the same is sought.

- 13-07-2009 : FIPB addressed SBL (in response to SBL's letter dated 08-07-2009) intimating that transfer of shares is permissible under the automatic route and SBL should approach RBI and avail the general permission route.

- 21-07-2009: ShanH addressed FIPB seeking permission to buy about 34,00,000 shares of SBL from existing NRI's, OCB's and Indian resident shareholders and sought necessary sanction to SBL to enable the acquisition by ShanH.

- 05-08-2009 : FIPB intimated SBL that transfer of SBL shares from resident, NRI and erstwhile OCB to ShanH is permissible under the automatic route subject to compliance with provisions of Press Note No.1 of 2005 read with Press Note No.3 of 2005, issued by the Department of Industrial Policy and Promotion.
- The above noted and other correspondence between SBL and ShanH on the one hand and the Government of India /FIPB on the other clearly establish that SBL, ShanH and the Government of India were clearly on the same page, viz., that the existing holder and intending purchaser of further SBL shares (either as fresh issue of capital, purchases from Indian residents, NRI's, OCB's) is ShanH. Though in some of the correspondence SBL or FIPB had described ShanH as a subsidiary of MA (even after 08-03-2007 when ShanH became a JV of MA/GIMD) such description would not alter the fact that the legal and beneficial holder of SBL shares was ShanH. The ascription in the correspondence, of ShanH being a subsidiary of MA would not alter the non-derogable fact that post 08-03-2007 (the partnership agreement between MA and GIMD in the presence of ShanH), ShanH became a JV company (with MA and GIMD being joint partners in the venture, proportionate to their holding in ShanH), as an operational reality.

<u>Did ShanH contribute for acquisition of SBL shares</u> ?

- According to Revenue, since Clause 4.7 of the 06-11-2006 SPA recites that MA remitted to SBL an amount equal to US $200,000/- for purchase of stamp duty payable on the share transfer forms, it is a clear indication that MA is the legal and beneficial owner of SBL shares. It is however asserted on behalf of MA and the assertion is borne out by the copy of the general ledger of ShanH (on record) that ShanH remitted to MA, the amount advanced by MA towards stamp duty in respect of the share transfer forms pertaining to SBL shares acquired by ShanH consequent on the 06-11-2006 SPA.
- There are other entries in the ShanH general ledger extract which evidence remittances from ShanH to SBL towards acquisition of SBL shares. Other entries in the general ledger set out remittances to Blom Bank and Calyon (the Escrow Agents) as well.
- Copy of a certificate dated 08-03-2008 regarding foreign inward remittances, issued by the Indian Overseas Bank, Chennai Branch attest to receipt of US $5,000,000 from ShanH to the credit of SBL towards application money for acquisition of SBL shares.

<u>Who received SBL Dividends - ShanH or MA</u> ?

Bank statements of SBL disclose remittances of dividends for FYs 2006-07, 2007-08 and 2008-09, to the credit of ShanH, vide statement of Indian Overseas Bank, Chennai branch, (copy on record not contested or disputed). US $ 68.705,32; 75.729,53; and 2.614.154,76, were remitted to the credit of ShanH account in Calyon Bank, Lyon, for the respective years.

Revenue neither contests this assertion, disputes the material furnished by MA in support thereof, nor explains the effect of SBL dividend payments to ShanH on its contention that the legal and beneficial owner of SBL shares is MA and not ShanH.

How did Revenue treat ShanH in relation to SBL shares ?

- In August, 2009 Revenue conducted a survey under Section 133A of the Act in the office premises of SBL (on anassumption based on news reports that Sanofi is going to acquire more than 80% stake in SBL from ShanH) and this acquisition would attract provisions of TDS under the Act; that ShanH had initially acquired a stake in SBL in November, 2006 by purchase of shares from different non-residents, the payments relating to which also attract provisions of Section 195 of the Act.
- Eventually, on 14-12-2009 Revenue passed two orders u/S.201(1) of the Act, in respect of FY 2007-08 and FY 2008-09. Para 1.1 of the order notes that during survey operation it was revealed that Sanofi entered into an agreement with MA on 26-07-2009 for acquisition of majority stake in SBL from ShanH by acquiring the shares of ShanH, approximately 80% of SBL shares. Para 1.2 of the order notes that on a verification of the "memorandum of share transfer" obtained from SBL during the survey, it is revealed that ShanH made (specified) payments during the FYs 2006-07, 2007-08 and 2008-09 to various NRI's for purchase of SBL shares; and ShanH received dividends from SBL in respect of its SBL shareholding.
- By the orders dated 14-12-2009 (pertaining to the FYs 2007-08 and 2008-09), Revenue, having initiatedproceedings u/S.201(1) and 201(1)(A) read with Section 195 of the Act, determined ShanH to be an "assessee in default" for failure to withhold taxes while making payments to sellers.
- The orders passed by the Revenue establish that the conclusion [that ShanH (not MA) acquired SBL shares] wasarrived on consideration and analyses of the shareholders register of SBL and other documents collected during the survey, including the SPA dated 06-11-2006.
- It is the contention of MA (not disputed by Revenue) that pursuant to the 14-12-2009 orders and consequent taxrecovery notices issued, ShanH had remitted the balance tax liability, to the tune of approximately Rs.1.33 crores; appeals thereagainst were preferred which were however rejected by the CIT(A); and further appeals are pending before the ITAT.
- During oral argument and in the written submissions it is contended on behalf of Revenue that the 14-12-2009 orders passed u/S.201 of the Act (treating ShanH as an assessee in default) could be treated as orders of protective assessment. This is a contention that is stated to be rejected as extravagant.
- Protective, precautionary or alternate assessment is one made *ex abundanti cautela* by an assessing authority when Revenue has any doubt as to the person who is or will be deemed to be in receipt of taxable income. While protective assessment is permitted, protective recovery is not – *Jagannath Hanumanbux v. ITO*[68]; *CIT v. Cochin Co. (P) Ltd.*[69]; and *Cotton Agents Ltd. v. CIT*[70]. Clearly while protective assessment is permissible (though not textually provided in the Act but evolved as a departmental practice that has gained judicial recognition), recovery of tax even if styled as protective recovery is not– *Jagannath Bawri v. CIT*[71]; and *CWT v. Begum Brigees Zahoor Quasim*[72]. This Court in *CIT v. Khalid Mehdi*[73] observed that where an assessment is intended to be protective it should be so expressed.
- The orders dated 14-12-2009 passed u/S.201(1) and 201(1)(A) are not and cannot be construed as orders of protectiveassessment and do not assert to be so either. Further, the undisputed fact that recovery notices were issued and the balance tax liability pursuant to these orders has also been collected from ShanH, puts paid to such contention by Revenue.
- The 14-12-2009 orders constitute determination by Revenue that ShanH (not MA) is the legal and beneficial owner of SBL shares. Such determination is a conscious, reasoned determination on analyses of the material gathered during survey operations including the memorandum of share transfer of SBL and the SPA dated 06-11-2006.

Is ShanH an entity having commercial substance ?

- Consistent with the organizational structure of the MA group, ShanH was incorporated (on 31-10-2006) as a French company with MA as the unique shareholder. Since 08-03-2007, ShanH evolved into a JV with MA and GIMD having 80:20 participation, GIMD joining as a strategicinvestor. In May, 2009 Mr. Georges Hibon acquired 1.9% participation in ShanH having purchased 13,000 shares from MA and GIMD (10,400 shares and 2,600 shares, respectively).
- The learned ASG (responding to a specific query from the Court, on 30-08-2012) fairly conceded that it is not the case of Revenue that in 2006 itself ShanH was conceived as a preordained scheme to avoid tax in India. Revenue asserts that since MA and GIMD claim that the capital gains liability arises only in France, it must be inferred that "it" is a pre-ordained scheme to avoid Indian tax liability.
- This argument on behalf of the Revenue does not commend acceptance by this Court. If ShanH, was not a pre-ordained scheme or arrangement conceived to avoid Indian tax liability at its inception in 2006 (as conceded by Revenue), the point in time when the *bona fide* corporate genesis of ShanH as a French resident tax paying entity stood transmuted into a pre-ordained Indian tax avoidance arrangement must be clearly asserted and established.
- Revenue's case on this aspect is ambivalent and incoherent. Revenue appears to suggest that the petitioners' claim (based on DTAA provisions), of immunity from capital gains liability under the Act (for theTransaction in issue) transforms the entirety of the antecedent exertions by ShanH (of purchase of SBL shares from time to time), its genesis as a registered resident tax paying entity in France, its origin as a wholly owned subsidiary of MA and evolution thereafter into a JV comprising MA and GIMD in March, 2007 and thereafter as JVcomprising MA, GIMD and Georges Hibon in 2009, a scheme or an arrangement for avoidance of capital gains liability under the Act. We are not persuaded to accept this incoherent syllogism. We accordingly reject the same.

  This Court is of the considered view that ShanH as a French resident corporate entity (initially a subsidiary of MA, thereafter a JV of MA/GIMD and eventually a JV comprising MA/GIMD/Georges Hibon) is a distinct entity of commercial substance, distinct from MA and/or GIMD and/or Georges Hibon, incorporated to serve as an investment vehicle, this being the commercial substance and business purpose, i.e., of foreign direct investment in India, by way of participation in SBL.

Extent of MA control over SBL :

- After purchase of SBL shares by ShanH (both consequent on the 06-11-2006 SPA and later *de hors* this SPA as well) SBL at all points in time was controlled and managed by its qualified board of directors comprising Mr. Georges Hibon as the Chairman, Mr. Johannes Burlin, Dr. K.I. Varaprasad Reddy, Mr. Philippe Sans, Mr. Abhey Yograj, Mr. Alain Merieux and Ms. Takizawa, serving as directors, at different points in time. Mr. Georges Hibon, who had twenty years of experience with Merck and had worked with Connaught Vaccines was appointed as the Chairman of the SBL Board. Mr. Philippe Sans and Ms. Takizawa, who were earlier associated with bioMerieux, were directors of ShanH. These persons actively participated and contributed to the business development of SBL.
- The SBL Board meeting (held at Paris) 07-11-2006 records : that Mr. Georges Hibon was associated with Merck and Connaught Vaccines; that Mr. Philippe Sans had been with the MA group for over twenty years and had served as the President and CEO of bioMerieux North America, for five years; that Mr. Johannes Burlin had earlier been with the

MA group and is currently working as president and CEO of Advanced Bio Science Laboratories, Inc., USA; and that Mr. Georges Hibon (a person totally unconnected with MA) is elected to serve as Chairman of the SBL Board. Minutes of this meeting also record the re-constitution of various committees of SBL directors such as the audit committee, the remuneration committee and the share transfer committee involving participation of Mr. Philippe Sans, Mr. Burlin and others.

- Minutes of the SBL Board meeting dated 29-11-2006 and 04-06-2009 (at Hyderabad and Chicagorespectively) evidence active participation of Mr. Philippe Sans. No choking, chilling or extra-ordinary control, invasion or interference by MA or MA/GIMD in SBL affairs is apparent.
- *Vodafone* pointed out that a group parent company giving principle guidance to group companies by providing generic policy guidelines to group subsidiaries; parent company exercising shareholder's influence on its subsidiaries and absent evidence of wholesale subordination of the subsidiaries' decision-making to the parent company, is not a circumstance that would not legitimize an inference, of the subsidiary being the *alter ego* or a puppet of the holding company nor would permit ignoring the separate corporate existence and identity of the subsidiary.
- On analyses of the relevant material on record we find no documentary or other bases to legitimize an inference that either MA or MA/GIMD exercised any extra-ordinary or chilling control over the affairs of SBL except *qua*their participative rights as JV partners in ShanH and through ShanH.
- From the uncontested pleadings; analyses of competing interpretations of the organizational structure of the MAgroup; the transactional documents (the 06-11-2006 SPA, the 07-11-2006 SHA's and the 08-03-2007 ShanH partnership agreement between MA and GIMD), it is clear that the MA group, (an established player in in-vitro diagnostics, food quality and nutrition, prophylactic vaccines, immuno-therapy in developed and developing countries) as part of its forays into the preventive vaccine business in developing countries, incorporated ShanH on 31-10-2006 as a French resident company with itself as the sole and unique shareholder.
- Even prior to ShanH incorporation, MA was negotiating with GIMD to come on board an investment vehicle, *inter alia* as a strategic investor to constitute a JV. The intention was clearly that ShanH (an investment vehicle operating as a JV) would acquire a controlling stake in SBL.
- In reality, since the very inception ShanH had acquired SBL shares, both *qua* the 06-11-2006 SPA and even thereafter and independent of this SPA. Having a footprint in India in the prophylactic vaccine business through controlling participation (shareholding) in SBL is the clear commercial substance and business purpose of ShanH.
- No curial or academic authority is placed before us to hazard a conclusion that a corporate entity must necessarily involve itself either in manufacture or marketing/trading in/of goods or services to qualify for the ascription of being in business or commerce. Creation of wholly owned subsidiaries or joint ventures either for domestic or overseas investment is a well established business/commercial organizational protocol; and investment is of itself a legitimate, established and globally well recognized business/commercial avocation.
- ShanH is a special purpose joint venture investment vehicle, established initially by MA and co-adopted in due course by GIMD and eventually by Mr.Georges Hibon, to facilitate investment by way of participation in the shareholding of SBL. That is the ShanH business and its commercial purpose.

<u>Was there a transfer of SBL shares to Sanofi under the 10-07-2009 SPA</u> ?

- Revenue in its written submissions while asserting that certain enumerated questions have to be decided by thisCourt [for deciding the core issue : *whether the substance of the transaction involved in the SPA dated 10-07-2009between MA/GIMD and Sanofi was for acquisition of control, management and business interests in SBL and liable tocapital gains liability under the Act?],* framed one of the integral questions requiring to be decided as :

  *(d) Who is the transferor of the right, title and interest in the shares of Shantha (*SBL*) and who realized the capitalgains on the transfer of the shares of Shantha?* (written submissions by ASG - para 2(d), pg.4)

- This Revenue assumption (that the transaction involved a transfer of the SBL shares to Sanofi) is fundamentally misconceived. There was no transfer of the right, title and interest in or transfer of SBL shares. The transaction covered by the SPA dated 10-07-2009 between MA/GIMD and Sanofi is clearly and only for transfer of ShanH shares (a French registered resident and JV) in favour of Sanofi. Indisputably, ShanH which acquired over 80% shareholding of SBL exists as a corporate entity and continues to hold the SBL shares, even after the 10-07-2009 transaction. Accordingly, this assertion by the Revenue commends rejection.

<u>What is the significance of the confidentiality and non-disclosure agreement dated 12-02-2009</u> ?

- <u>According to Revenue</u> : the 12-02-2009 confidentiality agreement was entered between MA and Sanofi, to which MA, SBL and Sanofi were parties and ShanH not. On this basis, Revenue contended that if the intention of the eventual transaction with Sanofi was only sale of ShanH shares, there is no justification for involving SBL and not ShanH along with MA, in the agreement.
- <u>The response</u> : MA submitted that the agreement was entered prior to effectuation of the transaction in issue (dated 10-07-2009), with a view to maintaining confidentiality in relation to the potential transaction. This agreement has no relevance to determination of the tax liability of the transaction *qua* the DTAA; since SBL was an indirect subsidiary of MA (through ShanH), MA signing the confidentiality agreement in relation to SBL is not an unnatural event, and has no legal significance on the status of ShanH (either in respect of its status as separate and legal entity or in respect of its being the holder and beneficial owner of SBL shares). Further, the confidentiality agreement is to ensure an obligation of non-disclosure in relation to the assets of SBL and is not concerned with the shares of SBL. Alternatively, in the event it is to be construed (though impermissible) that the 12-02-2009 confidentiality agreement must lead to the inference that SBL assets were sold (to Sanofi) *qua*the transaction in issue, then u/A.14(4) and/or u/A.14(6) of the DTAA the transaction would be taxable only in France; and in no event would the tax be allocable to India, under the treaty provisions.
- The agreement obligates Sanofi – the recipient of the "confidential information" (defined to include data, reports, interpretations, forecasts, transactions of the respective businesses of the parties, their employees, officers, directors, customers, and/or ventures, or concerning the existence, status, contemplation, structure, concepts and details of the transaction as well as financial information, customer lists and other customer information, pricing information, know-how, designs, technical specifications, manufacturing processes or improvements, market definitions and information, inventions and ideas), to keep the confidential information and the fact that the recipient has received the confidential information, confidential; and not to disclose, use or exploit any of the confidential information in any manner whatsoever. The information in respect of which confidentiality is agreed to be maintained pertains to SBL.

- Since the transaction in issue relates to sale of ShanH shares by MA/GIMD to Sanofi and not SBL shares; *qua* the transaction Sanofi would acquire control of ShanH, which in turn has a majority shareholding in SBL (this being the essential business purpose and commercial substance of ShanH as a SPV), it is natural that Sanofi desires to learn of the vitality of SBL. The agreement is to ensure that the critical information regarding SBL operations gained by Sanofi during the process is not misused so as to eventually have a pejorative effect on SBL which would eventually adversely impact ShanH as the majority stakeholder of SBL as well. As on 12-02-2009 MA/GIMD and Sanofi were still negotiating towards the transaction in issue. Safeguard by way of such a confidentiality agreement is, in our view, a natural precaution in the circumstances. This instrument, in any event, has no relevance to identifying the substance and character of ShanH or the true nature of the transaction in issue.

Effect of Sanofi's offer letter dated 22-06-2009 :

- Contention by Revenue : the basis of Sanofi's offer (for acquisition of 100% share capital of ShanH) is *inter alia*that SBL would be awarded a minimum annual allocation of thirty-five million doses of vaccines developed by SBL and other contingencies relating to the business prospects of SBL; and not ShanH.
- The non-binding offer by Sanofi's letter dated 22-06-2009 however discloses that Sanofi offered €550 million towards purchase price for 100% of ShanH share capital, based on an enterprise value of SBL and another €50 million (only) towards the incremental enterprise value of SBL but conditioned upon certain contingencies defined in Schedule – "A" of the offer letter. Schedule – "A" lists ongoing vaccine development processes by SBL which comprise Rota Virus in the South, Cholera for the South, Cholera for the U.S. market and typhoid conjugate.
- There is no dispute about the fact that the value of ShanH shareholding substantially comprises its majority participation (shareholding) in SBL. After all, ShanH (as already analyzed supra) is a special purpose foreign direct investment vehicle, that being its commercial substance and business purpose. In the circumstances, mention in Sanofi's offer letter that the price offered for acquisition of 100% ShanH shareholding is predicated upon the enterprise value of ShanH, both current and prospective, does not by itself tantamount to the subsequent transaction in issue, constituting sale of SBL shares (and not shares of ShanH), to Sanofi.

In view of the principles gleaned from *Venkatesh (Minor)*; *Walfort Share and Stockbrokers Pvt. Ltd.*; *Azadi Bachao Andolan*; *Vodafone*; *Lamesa*; *and Prevost Car Inc.*, the transaction in issue, considered in the light of the DTAA provisions (a detailed analysis on this to follow), cannot be considered as a transfer of either SBL shares of its underlying assets.

Relevance of statements recorded u/Sec.131 of the Act :

Revenue referred to statements by Mr. Khalil Ahmad (former executive Director of SBL), recorded on 11-11-2009 to support its contention, that SBL shares were acquired by MA; that ShanH is a mere *alter ego* of MA and had no independent role over affairs of SBL; and MA had a deep and pervasive control over SBL affairs.

It requires to be noticed that apart from the statement of Mr. Khalil Ahmad, statements of Mr. N. Rajasekhar (CFO of SBL) and of Mr. K.I. Varaprasada Reddy (MD of SBL) were also recorded, earlier on 09.11.2009 and 10.11.2009, respectively.

Statements by the CFO and MD of SBL regarding the role of ShanH in the active management/control of SBL; ShanH having acquired the SBL shares, as a subsidiary of MA; ShanH participating in SBL management through its nominee Directors; and SBL dealing only with ShanH on business decisions at the Board level, contradict Mr. Khalil Ahmad's statement.

The contradictory assumptions, in the statement of Mr. Khalil Ahmad on the one hand and of the CFO and MD of SBL on the other, as to the purpose of the 06.11.2006 SPA and of the status of ShanH and its role in the management of SBL, do not provide any coherent account of the true nature of the several transactions; the personality of ShanH or even whether ShanH or MA had active participation and involvement in SBL business affairs and management.

As pointed out in *Radha Sundar Dutta,* the true nature of a document/contract/agreement is a matter to be decided on a construction of the term of the written instrument; no evidence is admissible on a question of construction of a contract; and construction of the terms of a document, is a question of law. In our considered view, a statement of Mr. Khalil Ahmad, made under Sec. 131 of the Act, is therefore of no vital significance and has no critical relevance to ascertainment, of the true nature of the transactional documents, the legal and beneficial owner of SBL shares, the independent existence and the commercial and business reality of ShanH and whether MA exercised invasive influence in SBL management and affairs.

19. <u>Conclusions on issues 1 and 2</u> : <u>Facts and precedents analyses</u> :

We have already adverted to, categorized and analyzed precedents and other textual authority, relevant to issues 1 and 2, cited at the Bar by the parties herein. Analyses of the transactional documents and surrounding circumstances synthesized with guidance derived from precedents and other authority referred to, leads us to the conclusion that :

(i) Under the 06-11-2006 SPA; thereafter and independent of this SPA as well, ShanH (not MA or MA/GIMD) had purchased SBL shares and remitted the value therefor. The shares were registered in the name of ShanH, which is the recorded shareholder in the SBL shareholders' register. In view of the rulings and *rationes* in *Charanjit Lal Chowdhury*;*Bacha F Guzdar*; *Maharani Ushadevi*, *RC Cooper*; *Western Coal Fields Ltd.*, *Balkrishnan Gupta*; *LIC of India* and *Clariant*, ShanH is the legal and beneficial owner of SBL shares, being the registered shareholder, having been recorded as such in the shareholders register of SBL;.

(ii) On a true and fair construction and a holistic analyses of the uncontested facts, the relevant transactional documents, surrounding circumstances and orders and correspondence by Indian authorities and Revenue, enumerated hereunder :

(a) E-mails evidencing negotiations between MA and GIMD during August/September, 2006;
(b) minutes of the meeting of the MA Board dated 26-10-2006;
(c) incorporation and registration of ShanH on 31-10-2006 as a French corporate entity;
(d) resolutions of the ShanH shareholders meeting dated 31-10-2006;
(e) Escrow agreements dated 02-11-2006 and 03-11-2006 between ShanH, and Calyon Bank, Lyon and Blom Bank, Geneva, respectively and UOIL;
(f) The SPA dated 06-11-2006;
(g) The two SHA's dated 07-11-2006;
(h) The ShanH partnership agreement dated 08-03-2007 between MA and GIMD, in the presence of ShanH;
(i) The acquisition/subscription by ShanH in March, 2008 of SBL shares and remittances by ShanH to SBL, (evidenced by the certificate of foreign inward remittance dated 08-03-2008, issued by IOB, Chennai);
(j) The shareholders' agreement dated 05-05-2009 *qua* which Mr. Georges Hibon acquired a minority participation (13,000 shares) in ShanH from MA and GIMD;
(k) Further purchases by ShanH of SBL shares from UOIL and others during July and August, 2009;
(l) SBL dividend remittances to ShanH account for 2006-07, 2007-08 and 2008-09 evidenced by IOB bank statements of SBL;
(m) Amended (on 14-02-2007) Articles of Association of SBL read with the 06-11-2006 SPA and the two 07-11-2006 SHA's;

(n) Correspondence *inter alia* by FIPB recognising and adverting to ShanH being the holder of SBL shares;
(o) The 16-04-2008 custody agreement between ShanH and HSBC;
(p) SPA dated 10-07-2009 between MA/GIMD and Sanofi;
(q) Notice dated 04-08-2009 issued by Revenue u/S. 133A of the Act; and
(r) Orders of assessment dated 14-12-2009,

- assessed and analyzed in the light of principles delineated in the Supreme Court decisions in *Radha Sundar Dutta* and *Puzhakkal Kuttappu*; and in *Ford v. Beech*; *Intreprenneur*; *West Bromwich Building Society*; *Hideo Yoshimoto* and the textual authority of *Lewison*, (pertaining to construction of documents/contracts), compel the conclusion that :

(i) ShanH is a company registered and resident in France;
(ii) though a wholly owned subsidiary of MA at its incorporation on 31-10-2006, evolved thereafter into a JV corporate entity (of MA/GIMD) and thence of MA/GIMD and Mr. Georges Hibon;
(iii) is not a sham, illegal or illusory contrivance, a mere nominee or an *alter ego* of either MA and/or MA/GIMD;
(iv) in the light of the discussion, analyses and *rationes* in *Azadi Bachao Andolan* and *Vodafone*, ShanH is not a corporate entity brought into existence and pursued only or substantially for avoiding capital gains liability under provisions of the Act;
(v) ShanH is an investment vehicle; foreign direct investment in SBL being its commercial purpose and substance;
(vi) observations of Chinnappa Reddy, J (in his concurring opinion) do not constitute the operative *McDowellratio*, as discernible from the analyses in *M.V. Valliappan*; *Banyan and Berry*; *Arvind Narottam*; *Mathuram Agrawal*; *Azadi Bachao Andolan*; *Walfort Share and Stockbrokers Pvt. Ltd.*; and *Vodafone*;
(vii) *apropos* the concession by Revenue and even otherwise, on an independent and holistic analyses of the transactional documents and surrounding circumstances, ShanH was not conceived for avoiding capital gains liability under the provisions of the Act. As observed in the *Vodafone* factual context (equally applicable herein), ShanH was conceived and incorporated in consonance with MA's established business practices and organizational structure, as a wholly owned subsidiary to serve as an investment vehicle. ShanH thereafter transformed as a JV comprising MA/GIMD and eventually evolved as a JV comprising MA/GIMD/Mr.Georges Hibon. ShanH was established and functioned as a special purpose investment vehicle, to facilitate foreign direct investment and to cushion potential investment risks of MA/GIMD, on direct investment in SBL;
(viii) the uncontested assertion by petitioners, that a higher rate of capital gains tax is payable and has been remitted to Revenue in France (than would have been the case, if liable under provisions of the Act), lends further support to the inference that ShanH was not conceived, pursued and persisted with to serve as an Indian tax-avoidant device;
(ix) ShanH since its inception was the legal and beneficial owner of SBL shares and this constitutes its participation in SBL investment. ShanH since its incorporation (on 31-10-2006) has been in existence till the transaction in issue (*qua* the SPA dated 10-07-2009); and what is significant and uncontested, continues to exist even thereafter and currently. The commercial and business purpose of ShanH as a special purpose investment vehicle (for investment in SBL) constitutes its business operations in India; ShanH hitherto received and continues to receive dividends on its SBL shareholding which have been and are assessable to tax under provisions of the Act; and even post the transaction in

issue, the commercial and business purpose of ShanH as an investment vehicle is intact. These indicators/factors are, in the light of *Vodafone*, adequate bases to legitimize the conclusion that ShanH is not a gossamer, sham or conceived-only –for-Indian tax-avoidance structure. Consequently, as observed in *Vodafone* a further enquiry as to *de facto* control versus legal control and legal right versus practical rights by ShanH over SBL is unwarranted.

(x) since Revenue failed to establish, (on the basis of the facts and circumstances leading to the transaction in issue) that the genesis or continuance of ShanH establishes it to be an entity of no commercial substance or business purpose and/or that ShanH was interposed only as a tax-avoidant device, no case is made out for piercing or lifting the corporate veil of ShanH - vide *Bank of Chettinad*; *Provident Investment Co. Ltd.*; *Lamesa*; *Venkatesh (Minor)*; *Azadi Bachao Andolan*; *Prevost Car Inc.*; *Walfort Share and Stock Brokers P. Ltd.*; and *Vodafone*;

(xi) *De hors* conclusion (x) *supra*, even on piercing the corporate veil of ShanH, the transaction in issue is clearly one of the transfer by MA/GIMD of their ShanH shareholding (and of the marginal shareholding of Mr. Georges Hibon in ShanH as well) to Sanofi; and is not expressly or by any legitimate inference of the transactional documents and surrounding circumstances, a transfer of SBL shareholding, which continues with ShanH;

(xii) subsequent to the transaction in issue and currently as well, ShanH continues in existence as a registered French resident corporate entity and as the legal and beneficial owner of SBL shares; and

(xiii) the transaction in issue clearly and exclusively is one of transfer of the entire shareholding in ShanH, by MA/GIMD in favour of Sanofi. Transfer of SBL shares in favour of Sanofi is neither the intent nor the effect of the transaction.

(xiv) Revenue's perception of the ShanH *persona* and interpretation of the transactional documents (including the amended SBL AOA) and surrounding circumstances is fundamentally misconceived for another reason. If MA is considered as only MA *qua* the amended SBL AOA; that the 06-11-2006 SPA and the 07-11-2006 SHAs were instruments under which MA (not ShanH) acquired the SBL shares and that consequently the legal and beneficial owner of SBL shares is MA and not ShanH; then and on this interpretation/construction, the following transactional documents would irretrievably fail : the 07-11-2006 SHA's; the Escrow agreements dated 02-11-2006 and 03-11-2006; the ShanH partnership agreement dated 08-03-2007 between MA and GIMD; the May, 2007 purchase of ShanH shares by Mr. Georges Hibon from MA/GIMD; and even the 10-07-2009 SPA between MA/GIMD and Sanofi. As a consequence of Revenue's interpretation *qua* the 08-03-2007 SPA, GIMD would have acquired a 20% shareholding of ShanH which had neither a commercial substance, a business purpose or any value whatsoever; the Escrow agreements dated 02-11-2006 and 03-11-2006 with the French and Swiss Banks would be of no consequence; and under the 10-07-2009 SPA, Sanofi would have acquired 100% shareholding of ShanH, a wholly vacuous corporate entity, since this SPA was not for acquisition of MA/GIMD shareholding of SBL but for the ShanH shareholding of these JV partners. Further, the findings and conclusions of Revenue in the 14-12-2009 assessment of ShanH, for AY 2008-09 and 2009-10 u/S.201(1) of the Act, would become illegal and the tax of Rs.1.33 crores remitted by ShanH to Indian Revenue tantamount to unlawful collection of tax on a non-existent transaction involving no capital gain. Such fundamentally extravagant consequences must, in our considered view, be avoided, particularly by conjectural assumptions based on artificial interpretations pursuing a dissected approach instead of a holistic analysis of the transactional documents and the surrounding circumstances.

20. Whether this transaction constitutes transfer of the control, management, business and shareholding interests in and the underlying assets of SBL to Sanofi (from MA/GIMD), and if so with what legal consequences, will be considered separately *infra*.

21. How AAR discards Azadi :

 We have already noticed that *Azadi Bachao Andolan* clearly ruled that Chinnappa Reddy, J's formulation in McDowell did not constitute the majority view; that a transaction otherwise valid in law cannot be treated as *non-est* merely on the basis of some underlying motive supposedly resulting in some economic detriment or prejudice to national interests; that the "extreme view" of Chinnappa Reddy, J militates against observations in the majority judgment; and Reddy J's observations have also been distinguished in *M.V. Valliappan*; *Banyan and Berry*; *Arvind Narottam*; and *Mathuram Agrawal*. *Azadi* interpretation of *McDowell* was reiterated and followed in *Walfort* and in *Vodafone*, as well.

 Though *Vodafone* is subsequent to the AAR ruling and *Walfort* does not appear to have been brought to the notice of the AAR, the manner in which *Azadi* was discarded (not distinguished) is interesting, given the non-derogable obligation of an Indian Tribunal/Court (the AAR), of fidelity to the binding ruling/*ratio* of the jurisdictional superior judicial authority. In para – 16 (of the order) the Authority observes that while *Azadi* is binding on it, it may not be the final word in a given circumstance; that it finds "some difficulty" in accepting arguments based on *Azadi*; that *Azadi* "incorrectly" proceeded to assume that the views expressed by Chinnappa Reddy, J do not represent the *McDowell* majority; and developments in English decisions reveal that the *Ramsay* principle was pursued in *Ensign Tankers (Leasing) Ltd. v. Stokes*[74] and though the *Ramsay* principle was attempted to be restricted in *Craven, Ramsay* was resurrected and applied in *Commissioners for Her Majesty's Revenue and Customs v. Tower MCashback LLP 1 and another*[75].

Apart from the axiomatic and non-derogable principle that the learned AAR as a *quasi-judicial* Tribunal was bound by the law declared in *Azadi*; and it would be inconsistent with hierarchical discipline to question the correctness of the *Azadi* conclusion [that Chinnappa Reddy, J's views do not constitute the operative *McDowell ratio* and *McDowell* did not outlaw legitimate tax planning by a transaction or a step or steps in a transaction which are not devious, circuitous or vacuous (having no business or commercial purpose)], since the AAR referred to the 2011 decision of the UK Supreme Court in *Tower MCashback* to fortify its conclusion, we will briefly advert to the factual context of and the principles delineated in this decision.

Tower MCashback :

 The appeal before the UK Supreme Court concerned claims by the respondents - Tower MCashback LLP's (1 and 2) for first year allowances (FYA's under the Capital Allowances Act, 2001). Revenue disallowed the whole of LLP 1's claim on the ground that it had not been trading during the 2003-04 tax year and 75% of LLP 2's claim on analyses of the expenditure issue. Respondents' appeals were allowed on the procedural issue and though the expenditure issue was rendered academic in the context, that issue was also considered and concluded in favour of the respondents though the appeal of LLP 1 was rejected on the trading issue. In further appeals by the respondents, the Court of Appeals reversed the First Appellate Court's view on the procedural issue but agreed with it on the expenditure issue. As a result, Revenue preferred an appeal to the Supreme Court on the expenditure issue while the respondents preferred cross-appeals on the procedural issue (which went against them in the Court of Appeal).

- The (UK) Supreme Court noted that investor members of the LLP's were individuals with large incomes who themselves put up only 25% of the consideration said to have been paid for acquiring rights in software and the remaining 75% was provided by interest-free loans on non-recourse terms, made to the investor members by Special Purpose Vehicles set up for the purpose; that Revenue strongly asserted the circularity of the transactions, which realistically assessed, disclosed that much less than the full claimed expenditure was incurred on acquisition of software rights. Lord Walker (the leading opinion with concurrences by Lord Hope, Lord Rodger, Lord Collins, Lord Kerr, Lord Clarke and Lord Dyson) analysed the wider transaction as indisputably showing that the sequence of events amounted to a pre-arranged composite transaction of the type to which Lord Wilberforce referred to in *Ramsay*.

- Tracing the historical context of the *Ensign* decision and developments since *Ramsay* following through the opinion of Lord Diplock in *Burmah Oil Co. Ltd.;* Lord Brightman's opinion in *Furniss* and that of Lord Hoffman in *MacNiven v. Westmoreland Investments Ltd.*[76], the Supreme Court observed that the need to recognize *Ramsay* as a principle of statutory construction, the application of which must always depend on the text of the taxing statue in question was clearly recognized in *Craven.* The Court also referred to the judgments in the Court of Final Appeal of Hong Kong in *Collector of Stamp Revenue v. Arrow Town Assets*[77]. Having considered the House of Lords decision in *Ensign Tankers* (1992) and the later decision in *Barclays Mercantile Business Finance Ltd. v. Mawson*[78], Supreme Court observed that one of the lessons of the *Barclays* decision is that it is not enough for Revenue, in attacking a scheme of this sort (the case on hand) to point to the money going round in a circle; and a closer analyses is required. The Court observed: … "*in the present case, by contrast, the borrowed money did not go to MCashback, even temporarily; it passed, in accordance with a solicitor's undertaking, straight to R&D where itproduced no economic activity (except a minimal spread for the two Guernsey banks) until clearing fees began to flow from MCashback to the LLPs (in an arrangement comparable, though not closely similar, to the arrangements between LPI and VP in Ensign).*"
- The Court concluded that *there was a loan but there was not in any meaningful sense, an incurring of expenditure of the borrowed money in the acquisition of software rights. It went into a loop in order to enable the LLP's to indulge in a tax avoidance scheme.*
- Revenue's appeal was allowed.
- *Tower MCashback* is not a tax treaty case. The claim for FYA's under the (U-K) Capital Allowances Act, 2001 was disallowed on the basis of detailed analyses in the primary order, of the Special Commissioner (Revenue). This was approved by the Supreme Court. Revenue found that there was no incurring of expenditure of the borrowed money and the borrowed money was by a circuitous route put into a loop in order to enable the respondents to indulge in a tax avoidance scheme.
- It is significant to note that after elaborate analyses of several precedents *Tower MCashback* clarified that *Ramsay* must be recognized as a principle of statutory construction, the application of which must always depend on the text of the statute in question; and this was recognized in *Craven*. The statues in question (to be considered in the present case) are the DTAA and the Act.
- Neither on the matrix of the facts on the basis of which the decision is grounded nor on principle is it legitimate to assume or proceed on the basis that the *Ramsay* principle was resurrected (in *Tower MCashback*), in the manner assumed by Chinnappa Reddy, J

in *McDowell* or that the *ratio* of *McDowell*, as ascertained and clarified in *Azadi* has become inoperative or its binding efficacy eclipsed on account of the decision in *Tower MCashback.*

22. Issues 3 and 4 :

Revenue : The transaction (vide the 10-07-2009 SPA) is chargeable to capital gains tax under the provisions of the Act as amended by the Finance Act 2012 :

The learned ASG advanced a contention (on 30-08-2012), that since neither of the expressions "alienation" or "participation" in Article 14(5) is defined; in view of Article 3(2) of the DTAA, these terms would bear the meaning ascribed to them under provisions of the Act [as the law of (India) one of the Contracting States], as regards application of the DTAA. Learned senior counsel for the Petitioner-MA (Mr. Porus Kaka, on 31-08-2012) raised seriousobjection to this contention (orally urged on behalf of Revenue) and asserted that since it is an issue pertaining to fundamental policy i.e., as regards applicability of the retrospective amendments to provisions of the Act (by the Finance Act, 2012), to interpretation of provisions of the DTAA, this contention must be pleaded in an affidavit, to place on record this specific stand by the Union of India. Sri S.R. Ashok, learned senior learned counsel for the Income Tax department deputing on behalf of the learned ASG however responded (on 31-08-2012) that no affidavit need befiled as the contention is one of law, requiring an interpretative process.

The above contention by Revenue was neither asserted before the AAR, in earlier proceedings nor in the counters filed to the present writ petitions. The contention was advanced only *qua* oral argument in these proceedings and reiterated in written submissions by the ASG. Contours of the contention may be noticed :

(i) In the facts and circumstances, ShanH is not a company with an independent and distinct status; is a mere *alter ego* of MA/GIMD, who are the legal and beneficial owners of SBL shares;

(ii) Consequently, the transaction in issue is for acquisition of SBL shares. MA/GIMD participated directly in the capital, control and management of SBL; and such participation was more than 10% of SBL;

(iii) On conclusion of the transaction in issue, MA/GIMD realized the gain on alienation of shares, representing participation of more than 10% in the capital, control and management of SBL. Therefore, the gain is chargeable to tax in India in terms of Article 14(5) of the DTAA;

(iv) Tax treaties *inter alia* allocate taxing rights to the country of residence or of source or to both. Since the source country (India) gets the rights of taxation [*qua* contentions (i) to (iii) *supra]*, provisions of the Act operate to bring to tax the income (capital gain) in India;

(v) Petitioners erroneously contend that tax rights over capital gain, except in paragraphs (1), (2) and (4) of Article 14 are allocated to the resident State (of which the alienator is a resident). The right to tax over the gains comprehended in Article 14(5) being gain from alienation of shares other than those mentioned in Article 14(4) [representing a participation of at least 10% in a company which is a resident of a Contracting State], the same is also allocated to the source State. The State of residence is allocated taxation rights over capital gains only in paragraphs (3) and (6) of Article 14 and a limited right to the State of residence where the gains do not arise from alienation of a participation of less than 10% in a company which is a resident of the source State;

(vi) Since the transaction in issue does not relate to real estate companies (where the value of the share could be derived from immovable property), the relevant provision to determine taxation rights over capital gains is Article 14(5). This provision authorizes the source State to tax a gain on the alienation of shares of a company resident of that State whether the alienation occurs within or outside the State, where the alienation represents a participation of at least 10% of the company resident in that State. Once the source country inheres a right to tax gains arising from alienation of shares of a company located in the source country, it is immaterial whether such gains are realized by "disposal" or "deemed disposal" of assets. Treaty provisions apply in either case and the source country would have the right to tax such gains;

(vii) The expression *alienation of shares* in Article 14(5) must be read and understood, as direct as well as indirect alienation, for a proper and purposeful construction of DTAA provisions. The expression *alienation of property* is used to cover particular gains resulting from the sale or exchange of property and also from partial alienation, expropriation, transfer to a company in exchange for stock, the sale of a right, gift and even the passing of property on death; and is therefore intended to have a wider scope than the expression - *sale or exchange;*

(viii) The transaction in issue clearly involves deemed disposal of SBL shares if not actual disposal; and since the transaction involves deemed disposal of SBL shares and the expression *alienation* is not defined in DTAA, this expression would derive its meaning from provisions of the Act [in terms of Article 3(2)]. Since the Act comprehends disposal of capital assets within the meaning of the word *transfer* in Section 2(47) [in terms of Article 3(2) and read with Section 2(47) of the Act], the undefined expression *alienation* in Article 14(5) would cover direct as well as indirect transfers;

(ix) Black's law dictionary defines *transfer* to embrace every method - direct or indirect, absolute or conditional, voluntary or involuntary - of disposing of or parting with property or with an interest in property. The retrospective clarificatory amendment to Section 2(47) of the Act (vide the Finance Act, 2012) defines *transfer* to mean and to always have meant the disposal of an asset whether directly or indirectly voluntarily or involuntarily;

(x) Contrary to petitioners contention, *see through* is permitted not only in Article 14(4) but in Article 14(5) as well. Since Article 14(4) seeks to tax the underlying assets of the company in the source State in the form of immovable property, the expression *directly or indirectly* is employed therein. Since the basis of allocation of rights to the source country in Article 14(5) is however participation in excess of 10% in the company, the words *directly* or *indirectly,* being unnecessary has not been eschewed;

(xi) Revenue is not seeking to tax the underlying assets. The case of the Revenue is that MA/GIMD being owners of SBL shares both legal and beneficial, they have the participating interest in SBL. Disposal of such participating interest (in SBL) whether achieved directly or through a nominee entity like ShanH would not take the gains derived therefrom, out of the ambit of Article 14(5). Since the right to tax vests in India, the mode of disposal whether direct, indirect or deemed is immaterial; and

(xii) The residuary provisions in Article 14(6) are inapplicable to the facts. These provisions operate if capital gains do not come within the ambit of Article 14(1), (2), (4) and (5).

Each of the contentions and bases of each of the steps leading to the generic contention (of Revenue) on this aspect have been contested by the petitioners. On analyses, we are in general agreement with Petitioners' submissions and consider Revenue's contention as premised on a fundamentally erroneous factual substratum, fallacious and misconceived. We therefore consider it appropriate and to facilitate brevity, incorporate the relevant arguments and submissions of Petitioners as part of our analyses on this aspect. We set out provisions of the Act and of the DTAA, insofar as relevant and material for analyses, hereinafter.

<u>Relevant provisions of the Act and the DTAA</u> :

- Certain provisions of the Act were amended by the Finance Act, 2012, to operate with retrospective effect from 01-04-1962. Provisions of the Act relevant to adjudication of this *lis,* (pre and post the Finance Act, 2012) are set out in a tabular form in the Annexure to this judgment (for convenience and to avoid visual clutter). Relevant provisions of the DTAA are reproduced *infra.*

DTAA :

Governments of India and of the French Republic concluded a Convention (DTAA) for avoidance of double-taxation and prevention of fiscal evasion with respect to taxes on income and capital. The Convention has come into force on 01-08-1994, (on a notification by both the contracting States to each other on the completion of the procedures under their respective laws for bringing into force the Convention), in accordance with paragraph 1 of Article 30 of the DTAA.

The Government of India in exercise of powers conferred *inter alia* by Section 90 of the Act issued Notification No.9602 [F.No.501/16/80 - FTD], dated 06-09-1994, as amended by Notification No.SO. 650(E), dated 10-07-2000. Provisions of the DIM relevant for the purposes of this *lis* are:

Relevant DTAA provisions :

> ARTICLE 1 — Personal scope — This Convention shall apply to persons who are residents of one or both of the Contracting States.
>
> ARTICLE 2 - Taxes covered —
>
> 1. The taxes to which this Convention shall apply are :
>
> (a) in India :
>
> (i) the income-tax including any surcharge thereon;
>
> … … …
>
> ARTiCLE 3 — General definitions —
>
> 1. In this Convention, unless the context otherwise requires :
>
> … … …
> … … …
>
> (c) the terms "a Contracting State" and "the other Contracting State" mean India or France as the context requires;
>
> (d) the term "person" includes an individual, a company and any other entity which is treated as a taxable unit under the taxation laws in force in the respective Contracting States;
>
> (e) the term "company" means any body corporate or any entity which is treated as a company or body corporate under the taxation laws in force in the respective Contracting States;
>
> 2. As regards the application of the Convention by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of

thatContracting State concerning the taxes to which the Convention applies.

ARTICLE 4 — Resident —

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that Contracting State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature.

ARTICLE 5 — Permanent establishment —

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which thebusiness of an enterprise is wholly or partly carried on.
2. The fact that a company which is a resident of one of the Contracting States controls or is controlled by a company, which is a resident of the other Contracting State, or which carries on business in that other Contracting State (whether through a permanent establishment orotherwise), shall not of itself constitute either company a permanent establishment of the other.

ARTICLE 14 — Capital gains -

1. Gains derived by a resident of a Contracting State from the alienation of immovable property, referred to in article 6, and situated in the other ContractingState may be taxed in that other Contracting State.
2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State or of movable property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or together with the whole enterprise) or of such fixed base, may be taxed in that other Contracting State.
3. Gains from the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State of which the alienator is a resident.
4. Gains from the alienation of shares of the capital stock of a company the property of which consists directly or indirectly principally of immovable property situated in a Contracting State may be taxed *in* that Contracting State. For the purposes of this provision, immovable property pertaining to the industrial or commercial operation of such company shall not be taken into account.
5. Gains from the alienation of shares other than those mentioned in paragraph 4 representing a participation of at least 10 per cent in a company which is a resident of a Contracting State may be taxed in that Contracting State.

6. Gains from the alienation of any property other than that mentioned in paragraphs 1, 2, 4 and 5 shall be taxable only in the Contracting State of which the alienator is a resident.

ARTICLE 25 - Elimination of double taxation –

1. Double taxation shall be avoided in the following manner : … … …

2. In the case of France :

(a) Profits and other positive income arising in India and which are taxable in that Contracting State in accordance with the provisions of this Convention, are taken into account for thecomputation of the French tax where such income is received by a resident of France. The Indian tax shall not be deductible from such income. The beneficiary shall be entitled to a tax credit against French tax attributable to such income. Such tax credit shall be equal:

(i) in the case of income referred to in paragraph 2 of article 9, articles 11, 12, 13, paragraph 5 of article 14, paragraph 3 of article 16, article 17, paragraphs 1 and 2 of article 18 and paragraph 3 ofarticle 23, to the amount of tax paid in India in accordance with the provisions of those articles. However, it shall not exceed the amount of French tax attributable to such income;

•• ••• •• ••

<u>Issue 3 and 4 analyses</u> :

Responding to the contention on behalf of Revenue (regarding applicability of retrospective amendments to provisions of the Act by the Finance Act, 2012), petitioners contended that in view of the legislative intent underlying the amendatory exercise and on a proper interpretation as well, retrospective amendments are inapplicable where tax treaties operate alongside domestic tax legislation. Support for this contention is placed on the speech dated 07-05-2012 of the Hon'ble Finance Minister, while introducing the Finance Bill, 2012. The relevant portion reads :

> *7. Hon'ble Members are aware that a provision in the Finance Bill which seeks to retrospectively clarify the provisions of the Income Tax Act relating to capital gains on sale of assets located in India through indirect transfers abroad, has been intensely debated in the country and outside. I would like to confirm that clarificatory amendments do not override the provisions of Double Taxation Avoidance Agreement (DTAA) which India has with 82 countries. It would impact those cases where the transaction has been routed through low tax or no tax countries with whom India does not have a DTAA.* (emphasis added)

Revenue contended that provisions of the Act including the retrospective amendments thereto must be construed on the basis of the legislative text and permissible context and resort to the speech of the Finance Minister while introducing the Finance Bill (leading to the retrospective amendments) is impermissible. The learned ASG referred to the following passage from the

Constitution Bench judgment in *Sanjeev Coke Manufacturing Company v. Bharat Coking Coal Limited and Anr.*[79] :

> *26. Shri Ashok Sen drew pointed attention to the earlier affidavit filed on behalf of Bharat Coking Coal Company and commented severally on the alleged contradictory reasons given therein for the exclusion of certain coke oven plants from the Coking Coal Mines (Nationalisation) Act. But, in the ultimate analysis, we are not really to concern ourselves with the hollowness or the self-condemnatory nature of the statements made in the affidavits filed by the respondents to justify and sustain the legislation. The deponents of the affidavits filed into Court may speak for the parties on whose behalf they swear to the statement. They do not speak for the Parliament. No one may speak for the Parliament and Parliament is never before the Court. After Parliament has said what it intends to say, only the Court may say what the Parliament meant to say. None else. Once a statute leaves Parliament House, the Court's is the only authentic voice which may echo (interpret) the Parliament. This the court will do with reference to the language of the statute and other permissible aids. The executive Government may place before the court their understanding of what Parliament has said or intended to say or what they think was Parliament's object and all the facts and circumstances which in their view led to the legislation. When they do so, they do not speak for Parliament. No Act of Parliament may be struck down because of the understanding or misunderstanding of Parliamentary intention by the executive government or because their (the Government's), spokesmen do not bring out relevant circumstances but indulge in empty and self-defeating affidavits. They do not and they cannot bind Parliament. Validity of legislation is not to be judged merely by affidavits filed on behalf of the State, but by all the relevant circumstances which the court may ultimately find and more especially by what may be gathered from what the legislature has itself said. We have mentioned the facts as found by us and we do not think that there has been any infringement of the right guaranteed by Article 14.*

It however requires to be noticed that the passage in *Sanjeev Coke*, while reiterating the established position (that no one may speak for the legislature and legislation must be interpreted on its textual basis; and reference to other permissible aids to construction is legitimate only where the legislative text inheres an ambiguity and thus invites external aids to the appropriate construction of its text), ruled that statements made in affidavits filed by parties to a *lis* (respondents, in the case) do not constitute legitimate aids to interpretation/construction of legislation.

Whether the speech by the Finance Minister while introducing a Bill for enactment of fiscal legislation, is a legitimate aid to construction of a fiscal statute (and if there be an ambiguity) is an altogether different issue.

In *Sole Trustee, Lok Shikshana Trust v. The Commissioner of Income Tax, Mysore*[80], the issue whether resort can be had to external aids for resolving textual ambiguity in legislation, and in particular, whether reliance on the speech of the Finance Minister in the Parliament (explaining introduction of Section 2(15) in the Act), is permissible was considered. The following passages in *Lok Shikshana Trust* are relevant:

> *32. It is true that it is dangerous and may be misleading to gather the meaning of the words used in an enactment merely from what was said by any speaker in the course of a debate in Parliament on the subject. Such a speech cannot be used to defeat or detract from a meaning which clearly emerges from a consideration of the enacting words actually used. But, in the case before us, the real meaning and purpose of the words used cannot be understood at all satisfactorily without referring to the past history of legislation on the subject and the speech of the mover of the amendment who was, undoubtedly, in the best position to explain what defect in the law the amendment*

had sought to remove. It was not just the speech of any member in Parliament. It was the considered statement of the Finance Minister who was proposing the amendment for a particular reason which he clearly indicated. If the reason given by him only elucidates what is also deducible from the words used in the amended provision, we do not see why we should refuse to take it into consideration as an aid to a correct interpretation. It harmonises with and clarifies the real intent of the words used. Must we, in such circumstances, ignore it ?

33. ……………………

34. In the case before us, a reference was made merely to the fact that a certain reason was given by the Finance Minister, who proposed an amendment, for making the amendment. What we can take judicial notice of is the fact that such a statement of the reason was given in the course of such a speech. The question whether the object stated was properly expressed by the language of Section 2(15) of the Act is a matter which we have to decide for ourselves as a question of law. Interpretation of a statutory provision is always a question of law on which the reasons stated by the mover of the amendment can only be used as an aid in interpretation if we think, as I do in the instant case, that it helps us considerably in understanding the meaning of the amended law. We find no bar against such a use of the speech."

Proper interpretation of the provisions of Section 52(2) of the Act fell for consideration in *K.P. Varghese v. ITO, Ernakulam and another*[81]. The primary objection against a literal construction of Section 52(2) (urged on behalf of the appellant – assessee) was that it leads to manifestly unreasonable and absurd consequences. The Court proceeded to construe the provision not on a strictly literal interpretation of the text but in due regard to the object and purpose which the legislature had in view in enacting the provision and in the context and the collocation of other relevant provisions in which the particular provision occurs. The Finance Minister's speech while moving the amendment introducing sub-Section (2) was considered relevant for ascertaining the legislative object and purpose of the provision. What is relevant for the present *lis* is the following passage:

Now it is true that the speeches made by the Members of the Legislature on the floor of the House when a Bill for enacting a statutory provision is being debated are inadmissible for the purpose of interpreting the statutory provision but the speech made by the Mover of the Bill explaining the reason for the introduction of the Bill can certainly be referred to for the purpose of ascertaining the mischief sought to be remedied by the legislation and the object and purpose for which the legislation is enacted. This is in accord with the recent trend in juristic thought not only in western countries but also in India that interpretation of a statute being an exercise in the ascertainment of meaning, everything which is logically relevant should be admissible. In fact there are at least three decisions of this Court, one in Lok Shikshana Trust v.CIT, the other in Indian Chamber of Commerce v. Commissioner of Income Tax[82] *and the third in Additional Commissioner of Income Taxv. Surat Art Silk Cloth Manufacturers' Association*[83] *where the speech made by the Finance Minister while introducing the exclusionary clause in Section 2, clause (15) of the Act was relied upon by the Court for the purpose of ascertaining what was the reason for introducing that clause. The speech made by the Finance Minister while moving the amendment introducing sub-section (2) clearly states what were the circumstances in which sub-section (2) came to be passed, what was the mischief for which Section 52 as it then stood did not provide and which was sought to be remedied by the enactment of sub-section (2) and why the enactment of sub-section (2) was found necessary.*

Lok Sikshana Trust and *K.P. Varghese* authorize reference to a speech by the mover of a Bill, particularly of the Finance Minister regarding a fiscal legislation, to ascertain the object and purpose of the legislative measure and to get a fix on the context; and where there is a serious question as to whether the literal meaning of a provision corresponds to its legal meaning. As to "literal meaning", "legal meaning" and categories of "ambiguity", we analyze these concepts *infra*.

<u>Retrospective amendments to domestic tax legislation and tax treaty provisions : The Canadian context</u> :

In *R. v. Melford Development Inc.,*[84] the Canadian Supreme Court spelt out principles applicable to interpretation of domestic tax law and international tax conventions, where their provisions are said to compete.

<u>The Factual context</u> :

- There was in force and operation, relevant to the transactions in question, the Canada-Germany Tax convention (the Convention) brought into effect in Canada by the Canada-Germany Income Tax Agreement Act, 1956 (for short 'the 1956 Act'); a distinct legislation, by the Canadian Parliament.
- The respondent-Melford Developments Inc., made payments to a German Bank, which admittedly had no permanent establishment in Canada; the payment being towards fee payable to the German Bank for guaranteeing the Melford loan advanced by a Canadian Bank (the Bank of Nova Scotia). Canadian Revenue sought to recover withholding tax on payments by *Melford*.
- Revenue contended that the payment by Melford is subject to withholding tax under Section 212(1)(b) and 214(15)(a) in Part XIII of the (Canadian) Income Tax Act where a provision is made for the taxation of non-residents. Revenue contended that the payment in question is, for the purpose of (the Canadian) Income Tax Act "interest".
- In defense, Melford asserted that whatever provisions of the Income Tax Act may provide, these cannot override provisions of the Convention and in particular provisions of the 1956 Act introducing the Convention to the domestic law of Canada.

  Section 3 of the 1956 Act provided : *In the event of any inconsistency between the provisions of this Act, or the Agreement (*Convention*), and the operation of any other law, the provisions of this Act and the Agreement prevail to the extent of the inconsistency*. (broadly corresponding to Section 90(2) of the Act)
- Article III of the Convention provided that the contracting states have agreed that industrial or commercial profits of an enterprise in Germany would not be subject to tax in Canada unless it carried on business in Canada through a permanent establishment here.
- Article II (2) of the Convention provided that undefined terms in the Convention shall take the meaning which they take in the laws in force in the contracting countries. (corresponding to Article 3(2) of DTAA)
- In 1974, Parliament introduced Section 214(15) to the Income Tax Act with a view to extend withholding tax to interest, to payments by way of guaranty fees or standby charges.

<u>The issue in *Melford*</u> :

- Whether the 1974 amendment to the Income Tax Act amends the Convention so as to expose Melford to the burden of withholding tax at the prescribed rate when making payment of the guaranty fees to the non-resident guarantor-the German Bank was the core issue involved.

- The Supreme Court of Canada concurred with the Federal Court of Appeal to rule that payment by the respondent to the German Bank constituted industrial or commercial profits of the German enterprise which did not carry on a trade or business in Canada or have permanent establishment and was therefore exempt from subjection to tax in Canada.

How is dominance of Convention provisions eclipsed :

- The next question that arose was whether with reference to Article II (2) of the Convention *laws in force in Canada relating to the taxes which are the subject of this Convention* mean laws as they existed in 1956 (when the Convention became operative in Canada *qua* the 1956 Act) or the laws of Canada from time to time in force, in particular whether the expression *laws in force* in Article II (2) of the Convention includes the 1974 amendments to the Income Tax Act.
- Supreme Court ruled:

(i) the Convention does not authorize taxation of industrial and commercial profits of a non-resident where those profits were not earned through a permanent establishment in Canada; that the guarantee fee paid by Melford to the German bank falls into this category; and the revenue received by the German bank by reason of its guarantee of a Canadian lender (the Bank of Nova Scotia) represents industrial and commercial profits received from within Canada but not earned in an enterprise carried on through a Canadian permanent establishment;

(ii) laws enacted by Canada to re-define taxation procedures and mechanisms with a reference to income not subjected to taxation by the Convention are not incorporated in the expression laws in force in Canada, as employed by the Convention; a contrary assumption would mean that Article – II(2) of the Convention authorizes Canada or Germany to unilaterally amend Convention provisions from time to time as their respective domestic needs dictate;

(iii) As Parliament is supreme within its constitutionally assigned jurisdiction it follows that Section 3 or any other part of the 1956 Act could be repealed or amended. However, collateral legislative action in connection with the Income Tax Act (and not the 1956 Act) would not amend the 1956 Act, ruled the Supreme Court, observing :

... ... There are 26 concluded and 10 proposed tax conventions, treaties or agreements between Canada and other nations of the world. If the submission of the appellant is correct, these agreements are all put in peril by any legislative action taken by Parliament with reference to the revision of the Income Tax Act. For this practical reason one finds it difficult to conclude that Parliament has left its own handiwork of 1956 in such inadvertent jeopardy. That is not to say that before the 1956 Act can be amended in substance it must be done by Parliament in an Act entitled "An act to Amend the Act of 1956". But neither is the converse true, that is that every tax enactment adopted for whatever purpose, might have the effect of amending one or more bilateral or multilateral tax conventions without any avowed purpose or intention so to do.

There is no doubt, in my view, that the effect of s. 3 is to make the operation of any other law of Parliament, including the Income Tax Act, subject to the terms of the 1956 Act and the incorporated Agreement. The only exception to this result would be where Parliament has expressly set out to amend the 1956 statue. Then, of course, there is no conflict between the 1956 Act and "any other law". This interpretation has the necessary result of embodying in the Agreement, by reason of Article II(2), as definitions of the words not therein defined, the meaning of those words at the time the Agreement was adopted. Thus any legislative action taken for whatever reason which results in a change or expansion of a definition of a term such as "interest" does not prevail over the terms of the 1956 statute because of the necessary meaning of s.3 thereof; and concluded

(iv) *In the final analyses the appellant must fail because the 1956 statute, being the legislative adoption of the international tax Agreement, has not been amended by the income tax amendments of 1974 and accordingly Article III(1) of the Agreement prevents the application of the Income Tax Act to the guaranty fees paid by the respondent to the non-respondent bank. ...*

From the Canadian decision *Melford Development Inc.*, it is apparent that tax treaty provisions are operationalised within that jurisdiction by enactment of a distinct legislation by the Parliament of Canada. In India the same effect is achieved by a notification issued under Section 90(2) of the Act, to effectuate a treaty entered into between India and another or other Contracting State(s). The principle of non-derogability of treaty provisions so effectuated (whether *qua* a separate legislation in Canada or operationalised by a notification under provisions of the Act in India), has resonances *in pari materia* in both jurisdictions – India and Canada, though by distinct processes.

Other clear indicators (apart from the speech of the Finance Minister, adverted to *supra*) to negate Revenue's contention that retrospective amendments to the Act would over-ride provisions of the DTAA (or other tax treaties) may be noticed :

- The Finance Act, 2012, apart from introducing several retrospective amendments to tax indirect transfers, has also introduced provisions (Sections 95 to 102) in relation to GAAR, vide Chapter X – A of the Act. The purpose of these provisions is to invoke provisions of the Act in instances of abuse of treaty provisions. GAAR provisions specifically seek to over-ride tax treaties (proposed to be operationalised w.e.f. 01-04-2014).
- Section 90 of the Act has been amended, inserting sub-Section 2(A) (w.e.f. 01-04-2013), to enable application of Chapter X–A even if the same be not beneficial to the assessee [enacting an override effect over provisions of Section 90(2)]. Section 98 in Chapter X-A is inserted with the specific intention to over-ride tax treaties, where an arrangement is declared to be an impermissible avoidance agreement, as defined in Section 96;
- In contra-distinction, the retrospective amendments, sought to be relied upon by Revenue in the present case [Explanation 2 to Section 2(47)]; and Explanations 4 and 5 to Section 9) are not fortified by a *non-obstante* clause expressed to over-ride tax treaties.
- There is a presumption against a repeal by implication and the reason underlying this principle is premised on the theory that Legislature while enacting a law has a complete knowledge of the existing laws on the same subject matter, and therefore, when it does not provide a repealing provision it signals an intention not to repeal existing legislation - *Municipal Council, Palai v. T.J. Joseph*[85]; *Tansukhrai v. Nilratan Prasad*[86]; *Northern India Caterers (P) Ltd. v. State of Punjab*[87]; *Delhi Municipality v. Shivshanker*[88]; *Ratanlal Adukia v. Union of India*[89]; *R.S. Raghunath v. State of Karnataka*[90]; *Union of India v. Venkatesan*[91]; *State of M.P. v. Kedia Leather and Liquor Ltd.,*[92] ;

Also, continuance including efficacy of existing legislation, in the absence of an express provision of a repeal, being presumed, the burden to show that there has been a repeal by implication (including override of a tax treaty), lies on the party (Revenue, in this case) asserting the same.

The U.S. Supreme Court in *United States v. United Continental Tuna*[93] expounded a similar principle, disfavoring repeal by implication, by observing: *It is, of course, a cardinal principle of statutory construction that repeals by implication are not favoured.*

Relevant principles of statutory interpretation :

We notice and have endeavored to conform to principles of statutory construction, relevant to the *lis* before us. We are conscious that the democratic integrity of law, depends entirely upon the degree to which its processes are legitimate and as Judge Robert H. Bork[94] cautioned, a judge who announces a decision must be able to demonstrate that he began from recognized legal principles and reasoned in an intellectually coherent and politically neutral way to his result; and that the desire to do justice, whose nature seems to him obvious, is compelling while the concept of the legal process is abstract, the signals occasionally ambivalent and the abstinence it counsels (from encroaching into the realm of other organs of Government) unsatisfying. We are also conscious of Cardozo's[95] stately admonition, more appropriate to pursuing the interpretive role in adjudication; and that choice of appropriate interpretive principles is a hermeneutic choice not a political or a policy choice. The relevant principles:

(i) *The task of interpretation is to arrive at the legal meaning of an enactment. This is not necessarily the same as its grammatical meaning. Salmond[96] observed: the object of interpreting a statute is to ascertain the intention of the legislature enacting it;*

(ii) *The grammatical meaning of an enactment is its linguistic meaning taken in isolation from legal considerations, i.e., the meaning it bears when, as a piece of English prose, it is construed according to the rules and usages of grammar, syntax and punctuation (the verbal formulae) and the accepted linguistic canons of construction. An enactment is grammatically ambiguous where grammatically capable of more than one meaning. A modern statement of the nuanced principle on this aspect is clear from the following passage in the speech of Lord Simon of Glaisdale:Suthendran v. Immigration Appeal Tribunal[97] :*

Parliament is prima facie *to be credited with meaning what is said in an Act of Parliament. The drafting of statues, so important to a people who hope to live under the rule of law, will never be satisfactory unless courts seek whenever possible to apply 'the golden rule' of construction, that is to read the statutory language, grammatically and terminologically, in the ordinary and primary sense which it bears in its context, without omission or addition. Of course, Parliament is to be credited with good sense; so that when such an approach produces injustice, absurdity, contradiction or stultification of statutory objective the language may be modified sufficiently to avoid such disadvantage, though no further,* a passage quoted with approval in *Harbhajan Singh v. Press Council of India*[98];

(iii) *Identifying the legal meaning of an enactment from its grammatical meaning requires an informed interpretation, which according to the rule propounded by Oliver, LJ, in relation to taxing statutes in – Wicks v. Firth (Inspector of Taxes)[99], is however of general application. The formulation reads: accepting once more that the subject is not to be taxed except by clear words, the words must, nevertheless, be construed in the context of the provisions in which they appear and of the intention patently discernible on the face of those provisions from the words used;*

(iv) *Where, in relation to the facts of a given case, the enactment is grammatically ambiguous, the legal meaning is the one to which on balance of factors arising from the relevant interpretative criteria accord the greater weight;*

(v) *Ambiguity could be semantic, syntactical or contextual. The latter is where there is a conflict between the enactment and its internal or external context. Thus, where there are two possible grammatical meanings of the enactment in relation to its internal or external context, it is ambiguous;*

(vi) *Grammatical ambiguity in the above sense could be general or relative, the latter when it is ambiguous only in relation to certain facts;*

(vii) *In a case of relative ambiguity the facts must be brought into the equation;*

(viii) The unit of interpretation is not merely the subset of the relevant provision falling to be construed, the provision itself or the generic enactment in which it occurs but the whole universe of applicable and relevant legal rules of which the enactment is a part;

In the case on hand therefore, the meaning and the trajectory of the retrospective amendments to the Act (by the Finance Act, 2012), must be identified by ascertaining the legal meaning of the amendments, considered in the light of provisions of the Act; the mischief, the amendments are intended to address; and other applicable legal norms; which in the context include provisions of the DTAA, an instrument effectuated under constitutional text and authority and duly notified under provisions of the Act; and the amendment ought be confined to its legitimate locus and orbit.

As earlier observed, provisions of the Act and of the DTAA are overlapping and competing legal magisteria and the proper interpretive role requires, on a harmonious construction and in accordance with the relative weight and priority, giving effect to both competing provisions, as per the *inter se* weightage mandated by the overarching legal norms, set out in Section 90(2) of the Act.

<u>Revenue interpretation of DTAA, to justify application of provisions of the Act : Analysis</u> :

Petitioners and Revenue are agreed that provisions of paragraphs (1) to (4) of Article 14 of the DTAA have no bearing or application to chargeability to tax or the Contracting State to which tax on the capital gain involved, is allocated, in respect of the transaction in issue. Though Article 14(4) is not relevant and admittedly so, reference to this provision would assist elucidation of the true meaning, purpose and trajectory of the provisions of Article 14(5). Petitioners and Revenue agree that Article 14(5) is the relevant and applicable provision; though while petitionerscontend that the tax on the capital gain is allocated to France, Revenue claims that it stands allocated to India. Petitioners additionally contend that if Revenue's "underlying assets" theory is pursued to its logical conclusion, the tax on the capital gain is allocated to France, under Article 14(6).

Article 14(4), [as admitted by Revenue - vide written submissions - paragraph 6 (sub-paras 6 and 16)], has no application as this provision pertains to gains from alienation of shares of the capital stock of a company, the property of which consists directly or indirectly principally of immovable property situated in a Contracting State. Clearly, the explicit intent and reach of this provision is to tax capital gain derived from alienation of shares of real estate companies, whose assets are comprised principally of immovable property, subject however to exclusion of immovable property pertaining to the industrial or commercial operations of such company from computation of the taxablecapital gain.

Provisions of Article 14(4) have been set out. On a true, fair and grammatical construction of the provision, it is clear that the expression "directly or indirectly" is incorporated, to accommodate a "see through". Thus, while considering whether the gain from alienation of shares of the capital stock of a company is chargeable to tax, assessment of the transaction must necessarily involve the enquiry whether the property of the company principally (whether directly or indirectly), consists of immovable property. The expression "directly or indirectly" is intended to clarify the treaty intent that gain from alienation of shares of a company, whose property consists principally of immovable property, *whether directly or indirectly,* is chargeable to tax and the right to tax is allocated to the Contracting State whereat the immovable property of the company so liable, is situate.

The requisites for application of Article 14(4) are, in our considered view, the following :

(i) The transaction must involve alienation of shares of the capital stock of a company [as defined in Article 3(1)(e)]; and

(ii) The property of such company must principally comprise (directly or indirectly), immovable property;

On fulfillment of the two criteria above, the contracting State allocated the right to tax such gain is the one where immovable property of such company, is situate.

Article 14(5) deals with alienation of shares (excluding those comprehended within paragraph 4) representing a participation of at least 10% in a company which is a resident of a Contracting State and the right to tax is allocated to that contracting State in which the company is a resident.

On an interactive analyses of paragraphs (4) and (5), in our considered view, the scope and reach of Article 14(5) is :

(a) the transaction must involve gains from alienation of shares [not being shares of the capital stock of a company, the property of which principally comprises, directly or indirectly of immovable property - Art.14(4)], representing participation of at least 10% in the company; and

(b) on indicators in *(a)* being satisfied, the gains derived from alienation of shares of such company may be taxed in the contracting State whereat the company is resident.

On no rational interpretive principle is it legitimate to consider provisions of Article 14(5) as permitting a "see through". The provision, on a true, fair and non-manipulative interpretation, does not accommodate reckoning of the inherence of control by an intermediary/interpositioned joint venture company (ShanH), of the affairs, management and assets of its subsidiary (SBL), as alienation of shares by or of the control over the affairs, management and assets of the subsidiary (SBL), by one or all of the distinct participants of the interpositioned JV i.e., by MA/GIMD, who are distinct and French resident corporate entities themselves.

The DTAA is a treaty. As noticed in our prefatory observations, treaty provisions are expressions of sovereign policy, of more than one sovereign State, negotiated and entered into at a political/diplomatic level and have several explicit and/or subliminal and unarticulated considerations as their bases. A tax treaty must be seen in the context of aiding commercial relations between treaty partners and as being essentially a bargain between contracting States as to the division of tax revenues between them in respect of income falling to be taxed in bothjurisdictions. As *Azadi Bachao Andolan* has noticed, treaty negotiations are essentially a bargaining process, with each side seeking concessions from the other. The final agreement would often represent several compromises and it may be uncertain as to whether a full and sufficient *quid pro quo* is obtained by both sides. Many developed countries tolerate or encourage even treaty shopping, even if it were unintended, improper or unjustified, for other and non-tax reasons, unless it leads to significant loss of tax revenue; and allow the use of treaty network to attract foreignenterprises and off-shore activities. Some States favour treaty shopping for outbound investment to reduce foreign taxes of their tax residents but dislike their own loss of tax revenue on inbound investment or trade of non-residents. All these are sovereign policy choices.

Developing countries need foreign investments and treaty shopping opportunities could be an additional factor to attract them. There are many principles in a fiscal economy which, though may facially appear inequitable, are tolerated in a developing economy in the interest of long-term development.

Principles relevant to treaty interpretation are not the same as those pertaining to interpretation of municipal legislation. *Francis Bennion*[100] observes (quoted with approval in *Azadi Bachao Andolan): the drafting of treaties is notoriously sloppy usually for very good reason. To get agreement, politic uncertainty is called for.*

Revenue's strained construction of the provisions of Article 14(5) is wholly premised upon its seminal contention and contrived substrate, that MA/GIMD are the owners of SBL shares (legal and beneficial) and have the participating interest in SBL; that ShanH is a sham and nominal entity with no business or commercial purpose and is a device contrived to avoid liability to Indian tax.

As already noticed, Revenue while conceding that ShanH was not at inception (in October, 2006) a tax avoidant device, failed to explain when ShanH, conceived and born as a legitimate corporate entity transmuted into a tax avoidant device. Be that as it may.

The substrate of Revenue's case on this aspect is also that the transaction in issue involves a disposal (or deemed disposal) of the participating interest of MA/GIMD in SBL through the *alter ego* ShanH.

<u>The *ratio* in *Tradehold Ltd*</u> :

Revenue placed reliance on the dictum of the South African Supreme Court of Appeal in *Commissioner for theSouth African Revenue Services v. Tradehold Ltd.*[101] to contend that since the transaction in issue involved *deemed disposal* of SBL shares, the resultant tax stands allocated to India under Article 14(5) itself. To support this contention reliance is placed on the observations set out in Paragraphs 19 to 26 of *Tradehold Ltd*.

The relevant facts may be noticed. On 02-07-2002 Tradehold Ltd., resolved that all further Board meetings be held in Luxembourg. As a consequence, the company (incorporated and resident in South Africa - SA) became effectively managed in Luxembourg. It however continued to be a *resident* in SA notwithstanding the re-location in view of the definition of the term *resident* in the South African Income Tax Act 1962 (the 1962 Act). On amendment of the definition of the term *resident* in the said Act w.e.f. 26-02-2003, Tradehold Ltd ceased to be a resident of SA. SA Revenue relying on provisions of the 1962 Act asserted that the company is deemed to have disposed of its only relevant assets i.e., 100% shareholding in another company (Tradegrow Ltd) resulting in capital gain being realized; and levied tax accordingly.

The assessee, in the appeal before the Tax Court contended that if there was a deemed disposal of investments during the relevant year, the resultant capital gain was taxable in Luxembourg, not in SA. This contention was predicated on the basis that at the relevant time Tradehold Ltd, was deemed to be a resident of Luxembourg in terms of Art. 4(3) of the Double Tax Agreement between South Africa and Luxembourg, the terms of which applied to the transaction. Under Article 4(3), the deemed place of residence of a company is where its effective management is situated. Art. 13(4) of the treaty provides that: *Gains from the alienation of any property referred to in Paras 1, 2 and 3, shall be taxable only in the Contracting State of which the alienator is a resident* (a provision corresponding to Art.14(6) of the DTAA). The Tax Court rejected the contention (by SA Revenue) that the expression *alienation* does not include deemed disposal of the property, as deemed disposal of assets falls within Para 12 of the Eighth Schedule of the 1962 Act.

The appeal by the Revenue was rejected by the Supreme Court of Appeal. The Supreme Court referred to Sec.108(2) of the 1962 Act which provides that a tax agreement (treaty) on approval by the Parliament and its notification would be effective as if enacted in the 1962 Act. The Court noticed that the expression *alienation* is not defined in the treaty. Therefore, Art.3(2) [corresponding to Art.3(2) of the DTAA] applies and the undefined expression must bear a meaning ascribed to it under the 1962 Act. The Court observed that an international treaty must be interpreted so as to give effect to its provisions; that the first step is to determine into which Article of the treaty the particular tax falls; that Art. 13 includes within its ambit capital gains derived from the alienation of all properties; it must be assumed that the parties to the treaty were aware of provisions of the 1962 Act and have intended Art. 13 to apply to capital gains of the kind provided therein (the 1962 Act). The Court reasoned that Art. 13(4) incorporates no distinction between capital gains that arise from actual or deemed alienation of property; and there is no reason in principle why the parties to the treaty would have intended that Art.13 should apply only to taxes of actual capital gains resulting from actual alienation of property.

The Court concluded that *alienation* being a neutral term having a broader meaning as well (comprehending both actual and deemed disposal of assets), Art.13(4) would apply to the transaction in question; the tax is allocated to Luxembourg and is consequently immune to levy and collection in SA, under provisions of the 1962 Act.

In our considered view, *Tradehold Ltd.* affords no assistance to this aspect of Revenue's contention. Art. 3(2) of DTAA permits adoption of the meaning ascribed to an undefined term, which it has under the law of a ContractingState, *unless the context otherwise requires* (emphasis). The context of Art.14(5) provisions vis-à-vis other provisions of the DTAA, in particular Paragraphs (4) and (6) of Art.13 must also be considered. On a true, fair and good faith interpretation, no provision of Art.14 of DTAA accommodates dual taxation i.e., by both the Contracting States. The allocations are clearly to one Contracting State or the other.

It therefore cannot be, that the transaction in issue is permitted (under the DTAA regime) to be taxed in Indiaon the basis that there is a *deemed alienation* of SBL shares; and in France on the basis that there *actual alienation*,of ShanH shares. Neither the text nor the context of Art.14(5) legitimize such interpretation. Strained construction which subverts the policy underlying India entering into a double taxation avoidance treaty with another State, by enabling dual taxation through artificial interpretation of treaty provisions, is in our view, an impermissible exercise of judicial discretion (of choosing among alternative interpretations).

There is a further problematic in accepting this contention. If there be a deemed alienation of SBL shares to Sanofi chargeable to capital gains under the Act, henceforth Sanofi would be the legal and beneficial owner of SBL shares (*qua* provisions of the Act), entitled to its dividends and liable to tax accordingly. ShanH would (also and independent of Sanofi) continue as the registered shareholder of SBL shares, under provisions of the Indian Companies Act and consistent with the rulings in *Charanjit Lal Chowdhury; Bacha F Guzdar; Maharani Ushadevi; Western Coal Fields Ltd; LIC of India; RC Cooper; Clariant International Ltd; Howrah Trading Co Ltd; Balakrishan Gupta* and several other decisions apart from unvarying textual authority, entitled to SBL dividends. ShanH and Sanofi would not be joint owners of SBL shares but would own the same SBL shares independent of each other. ShanH would also be denuded of the entirety of its commercial substance and business purpose. It is axiomatic that *purposive construction* ought not to result in extravagant and absurd consequences, in particular when the interpretation subverts the essential purposes for which the DTAA was entered into i.e., for avoidance of double taxation.

It requires to be noticed in passing and while on analysis of *Tradehold Ltd.* that Art. 13(4) of the South Africa –Luxembourg treaty substantially corresponds to Art. 14(6) of the DTAA. On the basis of the *Tradehold* dictum, if the transaction in issue involves a deemed alienation (meaning *transfer* as defined u/Sec.2(47) of the Act), of the control and underlying assets of SBL (as integral to alienation of ShanH shares to Sanofi), the resultant tax is allocated toFrance under Art. 14(6) of the DTAA, since MA/GIMD - the alienators, are resident in France.

We have earlier adverted to the fact that Revenue has itself (vide orders dated 14-12-2009), assessed ShanH on the foundational premise that it was the purchaser of SBL shares. In paragraphs 1.2 of the assessment order Revenue concluded :

> *On verification of the 'Memorandum of Share Transfer' obtained from SBL during the course of survey, it was found that* SHS (ShanH) *had made payments totalling to Rs.359.87 crores, Rs.20.6 crores and Rs.82.12 crores respectively during FY 2006-07, 2007-08 and 2008-09 to various NRIs for purchase of shares of the Indian company SBL.* (emphasis added)

We have already recorded *qua* our conclusions on issues 1 and 2 (on analyses of the transactional documents and surrounding circumstances considered in the light of the several precedents) that it is ShanH and not MA/GIMD, who hold and beneficially own the SBL shares; that ShanH is a company registered and certified to be resident of France; is a corporate *persona* with a distinct legal status and a clear, commercial and business substance as well, viz., as a special purpose joint investment vehicle (initially a wholly owned subsidiary of MA, transformed thereafter into a

JVcomprising MA and GIMD and thereafter of MA, GIMD and Mr. Georges Hibon); that the chronology of events leading to the incorporation of ShanH as a subsidiary of MA and its subsequent transformation into a JV does not legitimize the inference that ShanH is a device, subterfuge or a gossamer entity, contrived for avoidance of tax liability in India.

We also advert to in passing that it is the specific plea and contention of the petitioners that capital gains at a higher rate (than in India, if liable) is chargeable and has been paid in France, on the transaction. This assertion has not been contested by Revenue and we presume that this contention has lead to Revenue's strategic concession that ShanH was not an Indian tax avoidant device at its inception.

The uniform precedential authority (adverted to in our analyses on issues 1 and 2) is also to the effect thatcorporate shareholding does not amount to ownership of the corporate assets; that a company is a juristic *persona*distinct from its shareholders; and while controlling interest would be an incidence of shareholding, it has no independent existence. Even ShanH is not therefore the owner (or a majority owner) of the underlying assets of SBL.

The transaction in issue is of alienation of ShanH shares by MA/GIMD and Mr. Georges Hibon (who together hold 100% of the stock of ShanH) to Sanofi. ShanH owns about 80% of SBL stock. Though, as an incident of the transaction in issue, Sanofi acquires a steering influence over the management and assets of SBL, such influence is the consequence of the shareholding in ShanH, an entity which has a majority participation in SBL. There is neither an actual nor a deemed transfer of the underlying assets of SBL in favour of Sanofi *qua* the transaction in issue; and ShanH continues to exist with its participatory controlling interest in SBL operative and extant; participation understood as shareholding, as considered in *Vodafone*.

Clearly, the transaction in issue involves a gain from alienation of ShanH shares (not SBL shares) by MA/GIMD and Mr. Georges Hibon to Sanofi, representing a participation of more than 10% (in fact 100%) in ShanH (not SBL), a company registered and resident in France. The alienation is admittedly outside the scope of Article 14(4) and falls to be considered under Article 14(5). The later provision in clear, unambiguous and explicit terms allocates the resultant capital gains tax to France (the contracting State, whereat ShanH is indisputably a resident).

Qua Art.14(5), where shares of a company which is a resident of France are transferred, representing a participation (shareholding – see *Vodafone*) of more than 10% in such entity, the resultant capital gain is taxable only inFrance. Even where the underlying value of such shares is located in the jurisdiction of the other contracting State(India), this fact is irrelevant under DTAA provisions; except where the alienation is of shares of a company the property of which consists principally (whether directly or indirectly) of immovable property and in the later circumstance the entitlement to tax stands allocated u/Art. 14(4) to the contracting State within whose jurisdiction such property is situate. To reiterate, the fact that the value of the shares alienated comprise underlying assets located in the other contracting State is irrelevant in the context of Art.14(5).

The creative interpretation by Revenue of provisions of Art. 14(5) on the substrate of its "underlying assets" theory (premised on its "MA/GIMD are the legal and beneficial owners of SBL shares" assumption); and in the context of SBL assets comprising immovable property pertaining to its industrial and commercial operations as well; would render provisions of Art.14(4) otiose.

In *CIT v. P.V.A.L.Kulandagan Chettiar*[102] the respondent assessee carried on the business of rubber plantation in Malaysia and had no permanent establishment in India. Whether the business income of the assessee from the rubber plantation could be taxed in India and in the context of a tax treaty between India and Malaysia though the property was located in Malaysia where the assessee had set up a permanent establishment, was in issue. Except the primary assessing authority, the CIT (Appeals), the Tribunal and the High Court held in favour of the assessee.Dismissing the appeal by Revenue, the Supreme Court observed that taxation policy is within the power of the Government and Sec. 90 of the Act enables the Government to formulate its policies through treaties entered into by it and such treaties determine the fiscal domicile in one State or the other and this determination in the treaty prevails over other provisions of the Act.

On the above analyses, considering the interplay between Article 14(4) and (5), gain from alienation of ShanH shares (by MA/GIMD) to Sanofi, if construed as falling beyond the contours of paragraphs (4) and (5) (paragraphs 1, 2 and 3 being admittedly and clearly inapplicable) would fall within provisions of the residuary Article 14(6) and be clearly taxable only in France, whereat MA/GIMD is (are) resident.

Petitioners have contended (a contention that commends our acceptance) that the UN Model Convention provides that countries negotiating a treaty have an option in Article 14(5) to permit the clause to operate only in instances where a substantial portion of the company's assets are situate in that contracting State, mere residence of a company would not suffice and its underlying assets should also be situate in that State. The relevant commentary on the UN Model Convention, at paragraph-11, mentions that such a clause must be incorporated as part of a treaty. The relevant part of the commentary reads :

> *Some countries might consider that the Contracting State in which a company is resident should be allowed to tax the alienation of its shares, only if a substantial portion of the company's assets are situated in that State, and in bilateral negotiations might urge such a limitation. Other countries might prefer that paragraph to be omitted completely.*

The DTAA does not incorporate such a clause and accommodating a "see through" in Article 14(5) would transgress the negotiated terms of the DTAA since the capital gains tax arising from the transaction, which standsallocated to France in terms of the DTAA would be susceptible to double-taxation, both in India and France, by an artificial and strained construction of the provisions of Article 14(5).

Ram Jethmalani and others v. UOI and others[103] approvingly referred to the *General Rule on Interpretation* of (VCLT), which provides that a treaty *shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose*, while proceeding to observe that though India is not a party to VCLT, the Convention contains many principles of customary international law and the principle of interpretation in Article 31 provides a broad guideline as to what should be an appropriate manner of interpreting a treaty in the Indian context as well.

We have earlier adverted to Revenue's contention, that Article 14(5) be *purposively construed* and interpreted as incorporating a "see through", though absent a textual basis. In our considered view, Article 14(5) does not admit of a grammatical, syntactical or contextual ambiguity legitimizing a strained construction. The grammatical and literal meaning of the provision wholly corresponds to its legal meaning and therefore authorizes no strained construction. There is yet another problematic in accepting Revenue's invitation to *purposive construction*.

Whose purpose is the question? It is axiomatic that while tax legislation may principally be for revenue augmentation that need not, in all circumstances, be the singular legislative purpose. Sovereign power to tax may be and often is (in contemporaneous governmental objectives, across nations) pursued for effectuating a cornucopia of State objectives; including nurture of societal equilibrium, minimizing economic or other disparities and health or ecological concerns (to mention a few). Normatively, promotion of international trade and commerce, in goods and services is thus a legitimate governmental purpose that may be pursued through tax legislation.

The Act (Section 90) authorizes, effectuation of a tax treaty (to which India is a signatory) and for the prevalence of the duly notified treaty provisions over provisions of the Act, as well.

Strained construction of treaty provisions, where not authorized by settled principles of statutory construction, either by the tax administrator or by the judicial branch at the invitation of Revenue of one of the contracting States to a treaty would also transgress the inherent and vital constitutional scheme, of separation of powers. Treaty-making power is integral to the exercise of sovereign legislative or executive will according to the relevant constitutional scheme, in all jurisdictions. Once the power is exercised by the authorized agency (the legislature or the executive, as the case may be) and a treaty entered into, provisions of such treaty must receive a good faith interpretation by every authorized interpreter, whether an executive agency, a *quasi-judicial* authority or the judicial branch. The supremacy of tax treaty provisions duly operationalised within a contracting State [which may (theoretically) be disempowered only by explicit and appropriately authorized legislative exertions], cannot be eclipsed by employment of an interpretive stratagem, on misconceived and ambiguous assumption of revenue interests of one of the contracting States. Where the operative treaty's provisions are unambiguous and their legal meaning clearly discernible and lend to an uncontestable comprehension on good faith interpretation, no further interpretive exertion is authorized; for that would tantamount to usurpation (by an unauthorized body - the interpreting Agency/Tribunal), intrusion and unlawful encroachment into the domain of treaty-making under Article 253 (in the Indian context), an arena off-limits to the judicial branch; and when the organic Charter accommodates no participatory role, for either the judicial branch or the executors of the Act.

For the above reasons as well, we decline Revenue's invitation to *purposively construe* provisions of Article 14(5).

<u>Revenue : "Alienation" and "Participation" in Article 14(5) of DTAA not being defined, meaning of these terms must be derived from provisions of the Act</u> :

Revenue places reliance on Article 3(2) to contend that since the terms *alienation* and *participation,* in Article 14(5) are not defined in the DTAA, these expressions require to be understood by reference to the meaning of the term*transfer*, as defined in the retrospectively amended section 2(47) of the Act, and consequently the transaction is liable to tax in India and in terms of Article 14(5) itself.

Vogel (cited supra) notes that the earlier literature on international law records active disputes on whether statutory text or statutory purpose should control the interpretation of an international agreement and that there was also a difference of opinion regarding the meaning of protocols of negotiations and other material, with the widely held view being that Treaty provisions are to be interpreted restrictively, since parties to a treaty in doubtful cases should only be presumed to have waived their sovereignty to the extent unequivocally apparent from the text of the treaty. According to *Vogel* VCLT rendered many of the earlier conflicts of opinion with regard to treaty interpretation obsolete and while VCLT contains only relatively general rules and cannot therefore make allowances for the peculiarities of tax treaties, has nevertheless resolved some of the uncertainties in prior international practice. Therefore, rules of the Vienna Convention are used in case law on the interpretation of double-taxation treaties today as a basis even with regard to States which have not yet ratified the Convention. Article 31 of the VCLT sets out thegeneral rules of interpretation of a treaty and Clause (1) thereof states that *a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its objects andpurpose. Ram Jethmalani* (as already noticed) recognizes the applicability of the above VCLT principle of treaty interpretation in the Indian context as well. *Ram Jethmalani* also refers with approval observations in *Azadi BachaoAndolan* and the dictum of Lord Widgery, CJ (quoted in *Azadi) that the words of a treaty are to be given their general meaning, general to lawyer and laymen and alike ... the meaning of the diplomat rather than the lawyer. Ram Jethmalani* further observes that according to this principle of interpretation, with respect to treaties and theprovisions therein, the ordinary meanings of words be given effect to, unless the context requires otherwise; and thefact that such treaties are drafted by diplomats, and not lawyers, leading to sloppiness in drafting also implies that care has been taken to not render any word, phrase, or sentence redundant, especially where rendering of such word, phrase or sentence redundant would lead to a manifestly absurd situation, particularly from a constitutional perspective.

Article 3(2) of the DTAA (extracted supra) provides that any term not defined therein shall, unless the context otherwise require, have the meaning which it has under the law of that contracting State concerning the taxes to which the Convention applies. From the unambiguous provision [Article 3(2)], a definition from the domestic law may be adopted, only if not defined in the treaty and the context otherwise requires.

We are in agreement with the petitioners and in the light of our preceding analyses, discern no textual,grammatical or syntactic ambiguity in Article 14(5), warranting an interpretive recourse. In the circumstances, invoking provisions of Article 3(2) by an artificial insemination of ambiguity (to accommodate an expanded meaning to the DTAA provision), would be contrary to good faith interpretation. A further problematic of contriving an ambiguity to unwarrantedly invite application of domestic law of a contracting State would be that while India would interpret an undefined DTAA provision according to the provisions of the Act, France could do so by reference to its tax code. As a consequence, the purpose of entering into a treaty with a view to avoiding double-taxation of cross-border transactions would be frustrated.

Revenue contends (already noted) that since *alienation* is not defined in the DTAA, *qua* Article 3(2) provisions of the Act should legitimately be referred to for its definition. The Act does not define *alienation* and Article 3(2) permits, in the circumstance adoption of the meaning of a term defined in the domestic law, only when the term employed in the domestic law is identical (not synonymous) to the undefined term in the DTAA.

Petitioners contend and we agree, that when India and France negotiated the terms of DTAA, the definition of the term *transfer* [as defined in Section 2(47) of the Act] was known, as was the international meaning of the term *alienation*. Representatives of India and France have however, chosen not to define either the term *transfer* or *alienation* in the treaty.

In the India-Canada tax Treaty, the right to tax such transactions was allocated to both countries. In the treaty *alienation* is specifically defined to include the meaning of the term *transfer* as defined in Section 2(47) of the Act. Article 13(2) of the India-Canada treaty provides: *gains from the alienation of any property, other than those referred to in paragraph 1 may be taxed in both Contracting States.* Amendments to provisions of the main treaty were agreed by way of a protocol, at the signing of a treaty. Clause (4) of this protocol (agreed to be an integral part of the treaty)provides: *that the term "alienation" includes a "transfer" within the meaning of the Indian taxation laws.*

In the Indo-Mauritius agreement (a tax treaty) (earlier adverted to in another context), Article 13(5) defines the term "alienation" for the purposes of the said Article, to mean *the sale, exchange, transfer or relinquishment of the property or the extinguishment of any rights therein or the compulsory acquisition thereof under any law in force in the respective Contracting States.* No similar explication of the term *alienation*, to include *extinguishment of any rights to the property or relinquishment thereof* is present in DTAA provisions. This circumstance signifies a conscious choice by the contracting States, while negotiating the DTAA and entering into it. Good faith interpretation does not permit incorporation of a *see through* or *look through* provision in Article 14(5) by the interpretive route or ascription of an intent (in the DTAA), to cover indirect or incidental transfer of rights in or control over assets of SBL, when the transaction in issue is one of alienation of ShanH shares. As pointed out in *Vodafone:*

Para 91. ... ... Certainty is integral to rule of law. Certainty and stability form the basic foundation of any fiscal system. Tax policy certainty is crucial for taxpayers (including foreign investors) to make rational economic choices in the most efficient manner. Legal doctrines like "Limitation of Benefits" and "look through" are matters of policy. It is for the Government of the day to have them incorporated in the Treaties and in the laws so as to avoid conflicting views. Investors should know where they stand. It also helps the tax administration in enforcing the provisions of the taxing laws. ... ... (emphasis added)

We are of the considered view, that absent such a provision in the DTAA, it would be impermissible to construe the expression *alienation*, though undefined in the DTAA by ascribing to it the meaning drawn from the definition of adifferent term *transfer*, defined in Section 2(47) of the Act. This invitation by Revenue, in our considered view, transcends the interpretive role and intrudes into the proper domain of the federal Executive/legislative power, viz., treaty making. We politely, but firmly, decline this invitation by the Revenue, to jurisdictional aggression/overreach.

In *MIL (Investments) SA v. Canada*[104] the core issue considered by the Tax Court Canada was whether selection of a low tax jurisdiction was abusive; and whether double taxation agreement must be interpreted as inherently containing the anti-avoidance rule.

- There was an operative convention between Canada and The Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital (the Convention).
- The Taxpayer held shares in a Canadian company through a company incorporated in Cayman Islands. The value of the shares rose rapidly due to a mineral find. The Taxpayer shifted the Cayman Islands company toLuxembourg. Soon thereafter, in view of certain events, such as the unexpected death of a business partner, he sold all his shares to another company which had made a takeover offer. Under the Convention, the sale was taxable in Luxembourg. For the purposes of the Luxembourg tax law however, the shares were valued at the date on which the company had become a Luxembourg company. Since by that date, the value of the shares has decreased to an extent, no Luxembourg capital gains tax was payable.
- Canadian Revenue relied upon the domestic general anti-avoidance rule (GAAR) to ignore the transfer toLuxembourg as being a tax avoidant transaction. Revenue argued that the deliberate selection of a low tax jurisdiction was itself abusive and/or there was an anti-avoidance rule inherent in the Convention. Bell, J allowed the appeal by the taxpayer, holding:

  (a) *The tax benefit had arisen from the sale of the shares. To find that the sale was one of a series oftransactions it had to be shown that the series was preordained and that there was a strong nexus between them. On the facts it could not be shown that the sale was intended at the time at which the previous transactions had been entered into;*

  (b) *There was nothing inherently proper or improper in selecting one foreign regime over another. The selection of a low tax jurisdiction might be evidence that a transaction had a tax purpose but treaty shopping, or selection of a jurisdiction to minimize tax could not on its own be viewed as abusive;*

  (c) *A purely commercial transaction conceived by business persons without any tax motivation and carried out with the assistance of tax professionals in a manner designed to achieve that result with the least unfavorable tax consequences was per se not an avoidance transaction;*

  (d) *One of the driving forces of the transactions was the taxpayer's desire to sell its shares in a tax efficient manner. How this was done was subordinate to the purpose of the transaction which was a bona fide commercial reason;*

  (e) *There was nothing in the Convention that could be construed as containing an inherent anti-avoidance rule especially in view of the fact that both Canada and Luxemburg had domestic general anti-avoidance rules and had not included one in the carefully negotiated Convention; Canada has negotiated a broad net-work of carefully negotiated Tax Conventions with many different nations; and* *prior to negotiating the treaty (Convention), Canada undoubtedly had knowledge of Luxembourg's treatment of capital gains;*

(f) In the light of OECD commentary and the decision by Canada and Luxembourg not to include an explicit reference to anti-avoidance rules in their carefully negotiated treaty (Convention), no ambiguity in the treaty is discernible permitting it to be construed as containing an inherent anti-abuse rule; consequently the ordinary meaning of the treaty allowing the appellant to claim the exemption must be respected.

In *MIL (Investments) SA v. Canada*[105] the Federal Court of Appeal dismissed the appeal by the Canadian Revenue. The appellate Court held: *Canadian Tax Legislation exempted non-residents from taxation on the gains from the disposition of treaty-exempt property; the Taxpayer's shares were treaty-exempt property; had the intention been to limit the exemption to portfolio investments, or to non-controlling interests in immoveable property it could easily have been provided so; and there was no object or purpose to be found which would justify departure from the plain words of the disposition. The Federal Court of Appeal further observed that the argument of Revenue that tax treaty should not be interpreted so as to permit double non-taxation does not commend acceptance, since the issue raised by GAAR is the incidence of Canadian taxation and not the foregoing of revenues by the Luxemburg Fiscal authorities.*

In the present case (as earlier adverted to), France is neither a tax haven nor a low tax jurisdiction; and in fact the liability of the transaction in issue (to capital gains tax) is said to be higher in the French jurisdiction than in India. The *ratio* of *MIL (Investments)* therefore (though persuasive), commends acceptance, *a fortiori*.

Is Article 25 of DTAA relevant ?

Revenue alternatively contended that in any event petitioners would not suffer any prejudice by way of double-taxation, in view of provisions of Article 25(1) r/w (2)(a)(i) thereof.

The above contention, in the facts and circumstances of the present *lis*, is stated to be rejected. Provisions of the DTAA including Article 25 have been extracted *supra*. On a true and fair construction, absent a grammatical ambiguity and the literal meaning of the text corresponding to its legal meaning, it is clear that only income arising and taxable in India, *in accordance with the provisions of this Convention* (DTAA) i.e., Article [14(5)], would be taken into account for computation of the French tax, to the extent of the amount of tax paid in India, in accordance with the provisions of the said Article [14(5)], so however that it shall not exceed the amount of French tax attributable to such income. Article 25(2)(a)(i) applies only where the income is taxable in India *in accordance with the provisions of the DTAA*.

As earlier noticed, Revenue predicates its claim to tax the transaction in issue on a *purposive construction* of Article 14(5) and ascription of a *see through* therein, to treat alienation of ShanH shares (the subject matter of the transaction in issue) as involving deemed transfer of control over the management and the underlying assets, of SBL. This proposition by Revenue, we have noticed, is premised over other substrating assumptions, viz., that ShanH is an entity of no commercial substance and the legal and beneficial owner of SBL shares is MA/GIMD, not ShanH.

In our conclusions recorded on Issues 1 and 2 and in the preceding analyses on Issues 3 and 4, we have rejected the above contentions by Revenue and concluded that:

(i) ShanH is an entity of commercial substance and business purpose; is not a mere nominee of MA/GIMD; is the true and beneficial owner of SBL shares; and Article 14(5) neither incorporates nor accommodates a *see through*;

(ii) the transaction in issue is of alienation of ShanH shares and not transfer of the shares or of the control, management or underlying assets of SBL;

(iii) retrospective amendments to provisions of the Act are neither relevant nor operate to impact in any manner the good faith interpretation of DTAA provisions; and

(iv) that the tax (on capital gain) on the transaction in issue, is allocated exclusively to France under Article 14(5) of the DTAA, not to India.

In the light of aforesaid analyses of the provisions of Article 25 of the DTAA and our conclusions on Issues 1 to 4 (summarized *supra*), the income accruing to MA/GIMD consequent on the transaction in issue neither arises nor is taxable in India in accordance with provisions [Art.14(5)] of the DTAA and is hence outside the province of Article 25. The transaction in issue is clearly liable to French Tax. Therefore, Indian tax if paid, notwithstanding the immunity to Indian tax liability, would not be entitled to tax credit against the French tax attributable to the income accrued on the transaction in issue.

23. Conclusions on Issues 3 and 4 :

On analyses of the relevant facts and attendant circumstances, duly considered in the light of curial and other authority referred to, we conclude:

(a) that the transaction in issue (pursuant to the SPA dated 10-07-2009 between MA/GIMD and Sanofi) is for alienation of 100% ShanH shares held by MA, GIMD and Mr. Georges Hibon in favor of Sanofi (falling within Article 14(5) of the DTAA); and constitutes neither the transfer nor deemed transfer of shares or of the control, management, or underlying assets of SBL (i.e., not a transfer, within the meaning of the expression as defined in Section 2(47) of the Act);

(b) the consequent tax on the capital gain accrued to MA/GIMD, is clearly and exclusively allocated to France under the provisions of Article 14(5) of the DTAA;

(c) retrospective amendments to provisions of the Act (by the Finance Act, 2012) *per se* do not operate to deflect, modify; or subject DTAA provisions to provisions of the Act (interpreted on good faith principle and construed in the light of applicable principles of statutory construction). There is no ambiguity in the Article 14(5) expressions - *alienation* or *participation*; and since these terms (identical, not synonymous) are neither employed nor defined in the Act, there is no warrant for invoking provisions of Article 3(2) of the DTAA; and thereby provisions of the Act to the transaction in issue; and in transgression of provisions of the DTAA; and

(d) the transaction in issue is not liable to tax in India, under the provisions of the Act read in conjunction with provisions of the DTAA.

24. Alternative Submission: Since computation provisions of the Act cannot apply, the charging provisions would also not apply :

Petitioners contended that the cost of acquiring the controlling rights and underlying assets in and of SBL and the date of acquisition of each of these 'assets' cannot be determined nor is it possible to determine the exact or rationally approximate consideration (out of the total consideration for the transaction in issue), apportionable to these assets/rights. According to the petitioners, computation provisions being inextricably integrated with the charging provision (Section 45 of the Act), inapplicability/failure of one component would render the other inapplicable as well. Reliance for this contention is placed on the decisions in *CIT v. BC Srinivasa Shetty*[106]; *PNB Finance Ltd. v CIT*[107]; and the AAR ruling dated 30-11-2009 in *Dana Corporation v. DIT*[108]. This contention by petitioners is integrated with other cognate contentions, *viz*., that the assets of SBL cannot be treated as the assets of ShanH or MA/GIMD even under domestic law; and controlling interest over a distinct corporate entity is not a separate asset, independent of the shareholding. The later contentions and the precedential authority marshaled in support thereof have already been considered in the analyses on Issues 1 and 2, *supra*.

Revenue however contended that evaluation of the transaction is capable of computation. According to Revenue, the long-term capital gain on the transaction in issue is the value of the sale of ShanH shares by MA/GIMD to Sanofi less the cost of acquisition of SBL shares by ShanH.

Conclusion :

In the light of the relevant precedential authority, considered in Issues 1 and 2 and the conclusions recorded, the controlling interest of ShanH over the affairs, assets and management of SBL being incidental to its shareholding and not a separate asset cannot be considered or computed as a distinct value, of ShanH shares. The assets of SBL in the light of binding precedential authority cannot be considered as belonging to a shareholder (even if a majority shareholder) – ShanH. The value of the controlling rights over SBL attributable to the ShanH shareholding is also incapable of determination and computation. There is also the issue of the value of Shanta West, a subsidiary of SBL. For these reasons, the computation component which is inextricably integrated to the charging provision (in Sec. 45 of the Act) fails, and consequently the charging provision would not apply.

25. Issue No.5 :

There are two facets to this issue, *viz*., :

(a) Whether the AAR may review its order, admitting the applications for advance ruling, for consideration on merits ?

To restate the relevant facts : On 17-12-2009 applications for advance ruling (by MA and GIMD) were allowed by the AAR u/S.245R(2), recording a clear finding that the applications are not hit by Clause(iii) of the proviso to the provision. Revenue challenged this order before this Court. On 08-07-2010, AAR by another order considered representations/objections (of Revenue to admissibility of the applications), found no reason to revoke its earlier order dated 17-12-2009 and posted the applications for hearing on merits, u/S.245R(4) of the Act. On 15-07-2011 writ petitions by Revenue were dismissed by this Court. AAR (at paragraphs 30 and 31 of the impugned ruling) declined to rule on the questions raised in the applications, invoking Clause (iii) of the proviso u/S.245R(2) of the Act.

AAR's observations on this aspect signal the clear inference that the learned Authority was revisiting its decision dated 17-12-2009 (admitting the applications, for eventual determination on merits), reiterated on 08-07-2010; and reviewed the earlier decision. No other interpretation of the observations by AAR is proffered by Revenue. Petitioners' contention that AAR reviewed its earlier decision to admit the applications appears to be the only possible construction of the relevant AAR observations.

Revenue contended that AAR, a *quasi-judicial* tribunal exercising adjudicatory jurisdiction under Chapter XXI - B of the Act, is neither expressly granted nor has inherently, the power to review its earlier decision (admitting the applications).

Revenue does not contest petitioners' submission that AAR has no jurisdiction, of review; a submission for which reliance is placed on the following decisions (rendered in various factual, legal and statutory contexts).

CIT & Anr. vs Income Tax Appellate Tribunal & Anr[109]; *Patel Narshi Thakershi vs Pradyumansinghji Arjunsinghji*[110]; *Grinland Bank Ltd. vs Central Garment Industrial Tribunal & Anr.*[111]; *Appropriate Authority vs Rasiklal M. Dhariwal*[112]; *Jose T. Mooken vs CIT, Kerala*[113]; *CIT vs Radha Swami Satsang*[114]; *CIT vs Suresh Kumar*[115]; *Shew Paper Exchange vs Income Tax Officer "C" Ward, Dist. V(1), Calcutta & Ors*[116]; *A.P. Kuruvilla and Co. and Ors vs Central Board of Direct Taxes and Ors.*[117]; *Laherchand Dhanji vs Union of India & Ors*[118]; *CIT vs Income Tax Appellate Tribunal & Anr* [119]; *CIT vs Globe Transport*

Corporation[120]; *CIT & Anr vs Income Tax Appellate Tribunal & Anr*[121]; *Chandrakant Butalal Shah vs Union of India*[122]; *J.K. Synthetics Ltd. vs. Collector of Central Excise*[123].

From the catena of referred authority, persuasive and binding, it is clear that judicial and *quasi-judicial*authorities exercising jurisdiction under a legislative grant have no inherent power to review their decision. Since the several precedents cited reiterate an established norm, we avoid an idle parade and detailed analyses of familiar authority.

In view of the settled position, the decision of the learned AAR (in the impugned ruling – set out in paragraphs 30 and 31 thereof), reviewing its earlier decision (admitting the applications) dated 17-12-2009, reiterated on 08-07-2010, is unsustainable and so declared.

We hasten to add that the above declaration is formally recorded on petitioners' invitation for a determination on this aspect. However, nothing substantial turns on this issue or *qua* our declaration thereon. The AAR has also ruled on the merits of the applications. Counsel for respective parties are agreed and have urged this Court to adjudicate on the validity of the AAR decision, as well. The substantive validity of the AAR ruling is the second facet of this issue, which we now proceed to consider.

(b) Is the AAR ruling misconceived, contrary to settled legal principles and hence unsustainable ?

In para-9 (*supra*), we have summarized the relevant conclusions of the AAR ruling. In the context of our analyses on this aspect of Issue No.5, the relevant factual assumptions, observations and conclusions in the AAR ruling are summarized:

(i) *AAR is required to consider whether a transaction is designed prima facie for avoidance of income tax; and the avoidance in issue would thus be avoidance, if any, of tax in India;*

(ii) *SBL shares were acquired in the name of or by, ShanH;*

(iii) *It is not necessary to ignore ShanH existence to come to the conclusion that what is put up is a façade in the context of tax law and would amount to a scheme for avoidance of tax; and in the view, the fact that GIMD and George Hibon held shares in ShanH, makes no difference; transfer of ShanH shares may have a commercial and business efficacy and validity. The transaction as conceived and executed is commercially real and taken step by step, valid. A permissible commercial scheme was adopted to acquire the shares, the underlying assets and control of SBL. Thereafter, under the guise of dealing with shares of a subsidiary firm (ShanH) for such acquisition, the underlying assets, business and control of an Indian company (SBL) is passed from one hand to another;*

(iv) *On a literal construction of Article 14(5) of DTAA, transfer of ShanH shares can be taxed only in France (where the companies involved were incorporated and are tax residents); and hence no avoidance of tax per se is involved;*

(v) *What is involved in the sale of ShanH shares (by MA/GIMD to Sanofi), is however, the alienation of the assets, control and interest of the Indian company – SBL;*

(vi) *The legal validity of a transaction or the adoption of a series of transactions commonly used, like creating a fully owned subsidiary for making such investments in another country, cannot hinder the query whether it is acceptable in the context of a taxing statute. The aspect of underlying assets and control over affairs of the Indian company passing from one hand to another cannot be ignored;*

(vii) *The series of transactions from commencement of ShanH formation suggests a pre-ordained scheme to produce a given result, viz., to deal with the assets and control of SBL without actually dealing with its shares, assets and business. The scheme adopted must be seen as one for avoiding payment of capital gains, which would otherwise arise if the shares of an Indian company had been transferred, leading to the same result as now achieved. So considered, it is a scheme for avoidance of tax in India;*

(viii) Though the transaction does not involve alienation of shares of an Indian company on a literal interpretation of Article 14(5), on a purposive construction of the said provision however, it must be concluded that the capital gains arising out of the transaction is taxable in India; and the essence of the transaction takes within its sweep various rights including a change in the controlling interests of the Indian company - SBL, having assets, business and income in India. Therefore, the transaction is taxable in India in terms of Article 14(5). This ruling is without prejudice to the rights, if any, of MA and GIMD to the benefits, if any, available under Article 25(2) of the DTAA; and

(ix) In view of above ruling, the second question posed by MA does not arise, since Article 14(6) would apply only if Article 14(5) has no application. The question whether controlling interest is an asset that would be taxable in France under Article 14(6), is therefore not considered.

Conclusions on Issue No.5 :-

Consistent with our analyses on issues 1 to 4 (of the relevant facts); the transactional documents and surrounding circumstances; the appropriate principles relevant to interpretation of tax treaties and to convergent application of a duly notified tax treaty and domestic tax legislation; and our conclusions that:

(i) ShanH is the true, legal and beneficial owner of SBL shares since inception;

(ii) ShanH is not either a sham, an artificially interposed entity with no commercial or business purpose or a tax-avoidant contrivance;

(iii) the transaction in issue is of transfer of ShanH shares and not of SBL shares or of its underlying assets and controlling interests; and

(iv) the resultant gain is allocated to France (not India) under Article 14(5) of the DTAA, the impugned AAR ruling is declared misconceived and as premised on flawed interpretation of relevant facts, provisions of the Act, the DTAA and applicable legal and interpretive norms relevant to the questions presented for advance ruling by the AAR.

The transaction in issue does not involve tax avoidance. The core issue (substrating the questions presented for advance ruling) is regarding allocation of the tax to one or the other contracting States – India or France, under DTAA provisions. France is neither a low tax jurisdiction nor a tax haven, and is the natural jurisdiction of all entities involved in the transaction – MA, GIMD, ShanH and Sanofi.

The learned AAR had concluded that:

(a) SBL shares were acquired by ShanH (not by MA or MA/GIMD) and ShanH is an entity of commercial substance and a business purpose;

(b) the transaction involves alienation of ShanH shares by MA/GIMD to Sanofi (and not SBL shares);

(c) a permissible commercial scheme was adopted (through an inter-positioned ShanH JV) to acquire SBL shares;

(d) the transaction in issue is taxable in France; no avoidance of tax per-se is thus involved and the series of transactions are commercially real and taken step by step, valid;

(e) the capital gain consequent on the transaction in issue is taxable in France (not in India) on a literal interpretation of Article 14(5) of the DTAA; but

(f) since the transaction results in no tax liability (to India) under provisions of the Act, it must be considered an Indian tax-avoidant devise; and the several legitimate stages/steps/transactions leading to the transaction in issue must nevertheless be ignored.

In the light of our prefatory observations, analyses on issues 1 to 4, and the conclusions recorded by AAR (adverted to *supra*), processed in the light of the catena of textual and precedential authority, the AAR ruling that the capital gain arising out of the transaction in issue is liable to tax in India is, in our respectful view, unsustainable.

As we perceive, the fallacy in Revenue assumptions which resonates through the impugned ruling as well, is a sub-liminal perception that administering provisions of the Act requires prioritizing levy and collection of Indian income tax, subordinating the dominant signals of DTAA provisions, by resort, if need be, to artificial and strained construction; of the transaction and DTAA provisions as well.

In our considered view, provisions of the DTAA (truly and fairly construed) applied to the transaction in issue (neutrally identified with forensic integrity) leads to the singular conclusion - that the consequent tax is allocated toFrance; and there is no question of avoidance of tax under the provisions of the Act. In the facts and circumstances of the case, the provision [Clause(iii) of the proviso to Sec. 245R(2)], i.e., the clause: *relates to a transaction ... ... which is designed prima facie for the avoidance of income-tax* would not apply where the claim of immunity to Indian income-tax is predicated upon the fact of allocation of the tax (chargeable on the transaction in issue) to France under DTAA provisions.

As a result of the preceding analyses, the ruling dated 28-11-2011 of the Authority for Advance Ruling, is quashed.

26. Issue No. 6 :

The order dated 25-05-2010 (impugned in Writ Petition No. 14212 of 2010) determined Sanofi to be an assessee in default for failure to deduct tax on the payment to MA/GIMD on the transaction in issue, u/Sec. 195 of the Act. A consequent demand notice of even date and the subsequent Rectification order dated 15-11-2011 by Revenue are also challenged. The petitioner (Sanofi) adopts the contentions advanced on behalf of the other petitioners, without reservation.

Conclusions on Issue No. 6 :

The liability of Sanofi to deduct tax at source, while remitting payment to MA/GIMD towards consideration for the ShanH shares transferred to it under the transaction in issue is contingent on the consequent gain being*chargeable under the provisions of the Act* - Sec. 195(1). If the income (the gain) is not so chargeable, the corresponding obligation does not arise. see - *GE India Technology Centre Pvt. Ltd v. CIT and another*[124]

We have carefully considered the order dated 25-05-2010. Interpretation of the several transactional documents and the surrounding circumstances, provisions of the Act and the DTAA; and reasons set out for the conclusions recorded in the order dated 25-05-2010, are *in pari materia* those proffered by and on behalf of Revenue.

Since the tax on the capital gain on the transaction in issue is not allocated to India and is exclusively allocated to France, under provisions of the Act read with DTAA provisions (as concluded earlier *vide our* analyses on Issues (1) to (5) *supra*), Sanofi has transgressed no provision of the Act (Sec.195 included) in not deducting tax on payments made to MA/GIMD on the transaction in issue.

It was alternatively contended that since there is no allegation of tax avoidance by Sanofi, even if ShanH were considered a tax avoidant device Sanofi cannot be treated an assessee in default, for proceeding u/Sec. 201 of the Act. This contention is misconceived. If the capital gain accruing from the transaction in issue is chargeable to tax under the Act, Sanofi is obligated to deduct the income tax thereon in accordance with the provisions of Sec. 195.

As a consequence of the preceding analysis, the impugned order, assessing Sanofi as an assessee in default; the notice of demand, also dated 25-05-2010 and the Rectification order dated 15-11-2011 are invalid and unsustainable.

27. We place on record our appreciation and gratitude, for the valuable assistance rendered by the learned counsel for the respective parties, whose commitment, fair and professional advocacy and forensic integrity, greatly assisted us in the discharge of our functions.

28. Summary of conclusions :

Our conclusions on Issues (1) to (6) are:

a) ShanH is an independent corporate entity, registered and resident in France. It has a commercial substance and a purpose (FDI in SBL); and is neither a mere nominee of MA and/or MA/GIMD, nor is a contrivance/device for tax avoidance;

b) since inception (in 2006) till date, ShanH (not MA or MA/GIMD) had acquired and continues to hold the SBL shares;

c) there is no warrant for lifting the corporate veil of ShanH; and even on looking through the ShanH corporate *persona* there is no material to conclude that there is a design or stratagem to avoid tax;

d) the capital gain arising as a consequence of the transaction in issue is chargeable to tax; and the resultant tax is allocated to France (not to India) under the DTAA;

e) the retrospective amendments to the Income Tax Act, 1961 (*vide* the Finance Act, 2012) have no impact on interpretation of the DTAA; the transaction in issue falls within Article 14(5) of the DTAA; and the tax resulting there from is allocated exclusively to France;

f) the ruling dated 28-11-2011 of the Authority for Advance Rulings is unsustainable; and

g) the order of assessment dated 25-05-2010 (determining Sanofi to be an assessee in default, u/Sec. 201 of the Act) is unsustainable. The consequent demand notice dated 25-05-2010 and the Rectification order dated 15-11-2011, being orders/proceedings consequent to the order dated 25-05-2010, are unsustainable.

29. Declarations :

In the light of our conclusions (summarized in paragraph 28 above), the ruling dated 28-11-2011 of the Authority for Advance Rulings, the order of the Sanofi assessment dated 25-05-2010, the consequent notice of demand, also dated 25-05-2010 and the Rectification order dated 15-11-2011 are quashed.

30. The Writ Petitions are allowed as above. No costs however.

JUSTICE GODA RAGHURAM

JUSTICE M.S. RAMACHANDRA RAO

Dated : 15-02-2013
NDR/VA/PVSN

LR copy to be marked : YES

A N N E X U R E

Relevant provisions of the Income Tax Act, 1961 : Pre and Post – amendments *qua* The Finance Act, 2012 :

Pre-Finance Act, 2012	Post-Finance Act, 2012
Section 2(14)	
"capital asset" means property of any kind held by an assessee, whether or not connected with his business or profession, but does not include –	"capital asset" means property of any kind held by an assessee, whether or not connected with his business or profession, but does not include –

(i) any stock-in-trade, consumable stores or raw materials held for the purposes of his business or profession;	(i) any stock-in-trade, consumable stores or raw materials held for the purposes of his business or profession;
(ii) Personal effects, that is to say, movable property (including wearing apparel and furniture) held for personal use by the assessee or any member of his family dependent on him, but excludes -	(ii) personal effects, that is to say, movable property (including wearing apparel and furniture) held for personal use by the assessee or any member of his family dependent on him, but excludes --
(a) jewellery; (b) archaeological collections; (c) drawings; (d) paintings; (e) sculptures; or (f) any work of art.	(a) jewellery; (b) archaeological collections; (c) drawings; (d) paintings; (e) sculptures; or (f) any work of art.
Explanation – For the purposes of this sub-clause, "jewellery" includes –	Explanation – For the purposes of this sub-clause, "jewellery" includes –
(a) ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stone, and whether or not work or sewn into any wearing apparel;	(a) ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stone, and whether or not worked or sewn into any wearing apparel;
(b) precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel;	(b) precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel;
(iii) agricultural land in India, not being land situate --	(iii) agricultural land in India, not being land situate --
(a) in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year; or	(a) in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year; or
(b) in any area within such distance, not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a), as the Central Government may, having regard to the extent of, and scope for,	(b) in any area within such distance, not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a), as the Central Government may, having regard to the extent of, and scope for, urbanization of that area and other relevant considerations, specify in this behalf by notification in the Official

urbanization of that area and other relevant considerations, specify in this behalf by notification in the Official Gazette; (iv) 6 ½ per cent Gold Bonds, 1977, or 7 per cent Gold Bonds, 1980, or National Defence Gold Bonds, 1980, issued by the Central Government; (v) Special Bearer Bonds, 1991, issued by the Central Government; (vi) Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 notified by the Central Government;	Gazette; (iv) 6 ½ per cent Gold Bonds, 1977, or 7 per cent Gold Bonds, 1980, or National Defence Gold Bonds, 1980, issued by the Central Government; (v) Special Bearer Bonds, 1991, issued by the Central Government; (vi) Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 notified by the Central Government; *Explanation – For the removal of doubts, it is hereby clarified that "property" includes and shall be deemed to have always included any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever; (inserted by the Finance Act 2012 w.e.f. 1st April, 1962)*
Section 2(47)	
(47) "transfer", in relation to a capital asset, includes, -- (i) the sale, exchange or relinquishment of the asset; or (ii) the extinguishment of any rights therein; or (iii) the compulsory acquisition thereof under any law; or (iv) in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment; or (iva) the maturity or redemption of a zero coupon bond; or (v) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882); or (vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any	(47) "transfer", in relation to a capital asset, includes, -- (i) the sale, exchange or relinquishment of the asset; or (ii) the extinguishment of any rights therein; or (iii) the compulsory acquisition thereof under any law; or (iv) in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment; or (iva) the maturity or redemption of a zero coupon bond; or (v) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882); or (vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in

agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, any immovable property. Explanation – For the purposes of sub-clauses (v) and (vi), "immovable property" shall have the same meaning as in clause (d) of section 269 UA;	any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, any immovable property. Explanation 1. – For the purposes of sub-clauses (v) and (vi), "immovable property" shall have the same meaning as in clause (d) of section 269UA; *Explanation 2. – For the removal of doubts, it is hereby clarified that "transfer" includes and shall be deemed to have always included disposing of or parting with an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or directly, absolutely or conditionally, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterized as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India; (Inserted by the Finance Act 2012 w.e.f. 1^{st} April, 1962)*
Section 9 – Income deemed to accrue or arise in India.	
9. (1) The following incomes shall be deemed to accrue or arise in India :-- (i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India. Explanation 1 – For the purposes of this clause – (a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India; (b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in Indiafor the purpose of export; (c) in the case of a non-resident, being a person	9. (1) The following incomes shall be deemed to accrue or arise in India : -- (i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India. Explanation 1 – For the purposes of this clause -- (a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India; (b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in Indiafor the purpose of export; (c) in the case of a non-resident, being a person

engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India;	engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India;
(d) in the case of a non-resident, being --	(d) in the case of a non-resident, being --
(1) an individual who is not a citizen ofIndia; or	(1) an individual who is not a citizen ofIndia; or
(2) a firm which does not have any partner who is a citizen of India or who is resident in India; or	(2) a firm which does not have any partner who is a citizen of India or who is resident inIndia; or
(3) a company which does not have any shareholder who is a citizen of India or who is resident in India, no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations which are confined to the shooting of any cinematograph film in India.	(3) a company which does not have any shareholder who is a citizen of India or who is resident in India, no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations which are confined to the shooting of any cinematograph film in India.
Explanation 2 – For the removal of doubts, it is hereby declared that “business connection” shall include any business activity carried out through a person who, acting on behalf of the non-resident, --	Explanation 2. – For the removal of doubts, it is hereby declared that “business connection” shall include any business activity carried out through a person who, acting on behalf of the non-resident, --
a. has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or	(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or
b. has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or	(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or
c. habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident :	(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident :
Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the	Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the

ordinary course of his business :

Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

Explanation 3. – Where a business is carried on in India through a person referred to in clause (a) or clause (b) or clause (c) of Explanation 2, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India;

(ii) income which falls under the head “Salaries”, if it is earned in India.

Explanation. – For the removal of doubts, it is hereby declared that the income of the nature referred to in this clause payable for –

(a) service rendered in India; and

(b) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment,
shall be regarded as income earned in India;

(iii) income chargeable under the head “Salaries” payable by the Government to a citizen of India for service outside India;

(iv) a dividend paid by an Indian company outside India;

(v) income by way of interest payable by –

(a) the Government; or

(b) a person who is a resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the

ordinary course of his business :

Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

Explanation 3. – Where a business is carried on in India through a person referred to in clause (a) or clause (b) or clause (c) of Explanation 2, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India;

Explanation 4. – For the removal of doubts, it is hereby clarified that the expression “through” shall mean and include and shall be deemed to have always meant and included “by means of”, “in consequence of” or “by reason of”.

Explanation 5. – For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India. (inserted by the Finance Act 2012 w.e.f. 1st April, 1962)

(ii) income which falls under the head “Salaries”, if it is earned in India.
Explanation – For the removal of doubts, it is hereby declared that the income of the nature referred to in this clause payable for –

(a) service rendered in India; and

(b) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment, purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India;

(vi) income by way of royalty payable by –

(a) the Government; or

(b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person in Indiaor for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1^{st} day of April, 1976, and the agreement is approved by the Central Government :

Provided further that nothing contained in this shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a licence) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software

shall be regarded as income earned inIndia;

(iii) income chargeable under the head "Salaries" payable by the Government to a citizen of India for service outside India;

(iv) a dividend paid by an Indian company outside India;

(v) income by way of interest payable by --

(a) the Government; or

(b) a person who is a resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India;

(vi) income by way of royalty payable by --

(a) the Government; or

(b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person in Indiaor for the purposes of making or earning any income from any source in India :
Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to

Export, Software Development and Training, 1986 of the Government of India.

Explanation 1.—For the purposes of the first proviso, an agree-ment made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date; so, however, that, where the recipient of the income by way of royalty is a foreign company, the agreement shall not be deemed to have been made before that date unless, before the expiry of the time allowed under sub-section (1) or sub-section (2) of section 139 (whether fixed originally or on extension) for furnishing the return of income for the assessment year commencing on the 1st day of April, 1977, or the assessment year in respect of which such income first becomes chargeable to tax under this Act, whichever assessment year is later, the company exercises an option by furnishing a declaration in writing to the Assessing Officer (such option being final for that assessment year and for every subsequent assessment year) that the agreement may be regarded as an agreement made before the 1st day of April, 1976.

Explanation 2. – For the purposes of this clause, “royalty” means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head “Capital gains”) for –

(i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;

(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;

(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;

(iva) the use or right to use any industrial,

any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April, 1976, and the agreement is approved by the Central Government :

Provided further that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a licence) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development and Training, 1986 of the Government of India.

Explanation 1. – For the purposes of the first proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date; so, however, that, where the recipient of the income by way of royalty is a foreign company, the agreement shall not be deemed to have been made before that date unless, before the expiry of the time allowed under sub-section (1) or sub-section 92) of section 139 (whether fixed originally or on extension) for furnishing the return of income for the assessment year commencing on the 1st day of April, 1977, or the assessment year in respect of which such income first becomes chargeable to tax under this Act, whichever assessment year is later, the company exercises an option by furnishing a declaration in writing to the (Assessing) Officer (such option being final for that assessment year and for every subsequent assessment year) that the agreement may be regarded as an agreement made before the 1st day of April, 1976.

Explanation 2.—For the purpose of this clause, “royalty” means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head “Capital gains”) for –

(i) the transfer of all or any rights (including the commercial or scientific equipment but not including the amounts referred to in section 44BB;

(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films; or

(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v).

Explanation 3. – For the purposes of this clause, "computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data;

(vii) income by way of fees for technical services payable by --

(a) the Government; or

(b) a person who is a resident except where the fees are payable in respect of services utilized in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the fees are payable in respect of services utilized in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1^{st} day of April, 1976, and approved by the Central Government.

Explanation 1. -- For the purposes of the foregoing proviso, an agreement made on or after the 1^{st} day of April, 1976, shall be deemed to have been made before that date if the agreement is made in

granting of a licnece) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;

(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;

(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;

(va) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;

(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films; or

(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v).

Explanation 3. – For the purposes of this clause, "computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data;

(vii) income by way of fees for technical services payable by --

(a) the Government; or

(b) a person who is a resident, except where the fees are payable in respect of services utilized in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India;

accordance with proposals approved by the Central Government before that date. Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries". (2) Notwithstanding anything contained in sub-section (1), any pension payable outside India to a person residing permanently outside India shall not be deemed to accrue or arise in India, if the pension is payable to a person referred to in article 314 of the Constitution or to a person who, having been appointed before the 15th day of August, 1947, to be a Judge of the Federal Court or of a High Court within the meaning of the Government of India Act, 1935, continues to serve on or after the commencement of the Constitution as a Judge in India. Explanation . – For the removal of doubts, it is hereby declared that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India under clause 9v) or clause (vi) or clause (viii) of sub-section (1) and shall be included in the total income of the non-resident, whether or not, -- (i) the non-resident has a residence or place of business or business connection in India; or (ii) the non-resident has rendered services in India.	or (c) a person who is a non-resident, where the fees are payable in respect of services utilized in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India : Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government. Explanation 1. – For the purposes of the foregoing proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date. Explanation 2. – For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries". (2) Notwithstanding anything contained in sub-section (1), any pension payable outside India to a person residing permanently outside India shall not be deemed to accrue or arise in India, if the pension is payable to a person referred to in article 314 of the Constitution or to a person who, having been appointed before the 15th day of August, 1947, to be a Judge of the Federal Court or of a High Court within the meaning of the Government of India Act, 1935, continues to serve on or after the commencement of the Constitution as a Judge in India. Explanation -- For the removal of doubts, it is hereby declared that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India under clause (v) or clause (vi) or clause (vii) of sub-section (1) and

	shall be included in the total income of the non-resident, whether or not, -- (i) the non-resident has a residence or place of business or business connection in India; or (ii) the non-resident has rendered services in India.
Section 195 – Other sums	
195. (1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest or any other sum chargeable under the provisions of this Act (not being income chargeable under the head "Salaries") shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force: Provided in the case of interest payable by the Government or a public sector bank within the meaning of clause (23D) of section 10 or a public financial institution within the meaning of that clause, deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode : Provided further that no such deduction shall be made in respect of any dividends referred to in section 115-O. Explanation. – For the purposes of this section, where any interest or other sum as aforesaid is credited to any account, whether called "Interest payable account" or "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly (2) Where the person responsible for paying any such sum chargeable under this Act (other than salary) to a non-resident considers that the whole of such sum would not be income chargeable in the case of the recipient, he may make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of such	195. (1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company, *any interest (not being interest referred to in section 194LB or section 194LC)* or any other sum chargeable under the provisions of this Act (not being income chargeable under the head "Salaries") shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force : Provided that in the case of interest payable by the Government or a public sector bank within the meaning of clause (23D) of section 10 or a public financial institution within the meaning of that clause, deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mod : Provided further that no such deduction shall be made in respect of any dividends referred to in section 115-O. Explanation 1. – For the purposes of this section, where any interest or other sum as aforesaid is credited to any account, whether called "Interest payable account" or "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly. *"Explanation 2 – For the removal of doubts, it is hereby clarified that the obligation to comply with sub-section (1) and to make deduction thereunder applies and shall be deemed to have always applied and extends and shall be deemed to have always extended to all persons, resident or non-resident, whether or not the non-resident person*

sum so chargeable, and upon such determination, tax shall be deducted under sub-section (1) only on that proportion of the sum which is so chargeable.

(3) Subject to rules made under sub-section (5), any person entitled to receive any interest or other sum on which income-tax has to be deducted under sub-section (1) may make an application in the prescribed form to the Assessing Officer for the grant of a certificate authorizing him to receive such interest or other sum without deduction of tax under that sub-section, and where any such certificate is granted, every person responsible for paying such interest or other sum to the person to whom such certificate is granted shall, so long as the certificate is in force, make payment of such interest or other sum without deducting tax thereon under sub-section (1).

(4) A certificate granted under sub-section (3) shall remain in force till the expiry of the period specified therein or, if it is cancelled by the Assessing Officer before the expiry of such period, till such cancellation.

(5) The Board may, having regard to the convenience of assesses and the interests of revenue, by notification in the Official Gazette, make rules specifying the cases in which, and the circumstances under which, an application may be made for the grant of a certificate under sub-section (3) and the conditions subject to which such certificate may be granted and providing for all other matters connected therewith.

(6) The person referred to in sub-section (1) shall furnish the information relating to payment of any sum in such form and manner as may be prescribed by the Board.

has –

(i) a residence or place of business or business connection in India; or

(ii) *any other presence in any manner whatsoever in India: (inserted by the Finance Act 2012 w.e.f. 1st April, 1962)*

(2) Where the person responsible for paying any such sum chargeable under this Act (other than salary) to a non-resident considers that the whole of such sum would not be income chargeable in the case of the recipient, he may make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of such sum so chargeable, and upon such determination, tax shall be deducted under sub-section (1) only on that proportion of the sum which is so chargeable.

(3) Subject to rules made under sub-section (5), any person entitled to receive any interest or other sum on which income-tax has to be deducted under sub-section (1) may make an application in the prescribed form to the Assessing Officer for the grant of a certificate authorizing him to receive such interest or other sum without deduction of tax under that sub-section, and where any such certificate is granted, every person responsible for paying such interest or other sum to the person to whom such certificate is granted shall, so long as the certificate is in force, make payment of such interest or other sum without deducting tax thereon under sub-section (1).

(4) A certificate granted under sub-section (3) shall remain in force till the expiry of the period specified therein or, if it is cancelled by the Assessing Officer before the expiry of such period, till such cancellation.

(5) The Board may, having regard to the convenience of assesses and the interest of revenue, by notification in the Official Gazette, make rules specifying the cases in which, and the circumstances under which, an application may be made for the grant of a certificate under sub-section (3) and the conditions subject to which such certificate may be granted and providing for all other matters connected therewith.

	(6) The person referred to in sub-section (1) shall furnish the information relating to payment of any sum in such form and manner as may be prescribed by the Board.
Validation of demands, etc., under Income-tax Act, 1961 in certain cases	
	Notwithstanding anything contained in any judgment, decree or order of any Court or Tribunal or any authority, all notices sent or purporting to have been sent, or taxes levied, demanded, assessed, imposed, collected or recovered or purporting to have been levied, demanded, assessed, imposed, collected or recovered under the provisions of Income-Tax Act, 1961, in respect of income accruing or arising through or from the transfer of a capital asset situate in India in consequence of the transfer of a share or shares of a company registered or incorporated outside India or in consequence of an agreement, or otherwise, outside India, shall be deemed to have been validly made, and the notice, levy, demand, assessment, imposition, collection or recovery of tax shall be valid and shall be deemed always to have been valid and shall not be called in question on the ground that the tax was not chargeable or any ground including that it is a tax on capital gains arising out of transactions which have taken place outside India, and accordingly, any tax levied, demanded, assessed, imposed or deposited before the commencement of this Act and chargeable for a period prior to such commencement but not collected or recovered before such commencement, may be collected or recovered an appropriated in accordance with the provisions of the Income-tax Act, 1961 as amended by this Act, and the rules made thereunder and there shall be no liability or obligation to make any refund whatsoever.

Note : Highlighted portions of the text are relevant amendments to provisions of the Act *qua* the Finance Act, 2012.

Other provisions of the Act :

- Chapter IX of the Act sets out provisions pertaining to double-taxation relief. Prior to its substitution by Finance Act, 2009, (with effect from 01-10-2009), Section 90 bore the marginal heading "agreement with foreign countries" and after the substitution *qua* the Finance Act, 2009 the marginal heading reads "agreement with foreign countries or specified territories". For purposes of this *lis* nothing substantial turns upon amendment of the marginal heading of Section 90, by the Finance Act, 2009 or of its text. We set out the relevant provisions of Section 90 of the Act, as substituted by the Finance Act, 2009.

90. (1) The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India, -

(a) for the granting of relief in respect of –

(i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or

(ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or

(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory, as the case may be, or

(c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be,

and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

(2) Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

Amendments to Sec.90 by Finance Act, 2012 :

Sub-sections (2A) and (4) were inserted after Sub-section (2) and (3) of Section 90, by the Finance Act, 2012, (with effect from 01-04-2013). Post the amendatory exercise, sub-sections (2A) to (4) read :

(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee, even if such provisions are not beneficial to him.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

(4) An assessee, not being a resident, to whom an agreement referred to in sub-section (1) applies, shall not be entitled to claim any relief under such agreement unless a certificate, containing such particulars as may be prescribed, of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory.

Explanation 1.—For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

Explanation 2.---- For the purposes of this section, “specified territory” means any area outside India which may be notified as such by the Central Government.

Explanation 3.---- For the removal of doubts, it is hereby declared that where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued thereunder being in force, then, the meaning assigned to such term shall be deemed to have effect form the date on which the said agreement came into force.

Section (2)(A) (inserted by the Finance Act, 2012 with effect from 01-04-2013) enacts that the provisions of Chapter X-A shall apply to the assessee, even if such provisions are not beneficial to him and this provision is fortified by a *non-obstante* clause, to operate notwithstanding anything contained in Section 90(2).

Chapter X-A of the Act :

Sections 95 to 102 were inserted in a separate Chapter X-A by the Finance Act, 2012, *with effect from 01-04-2014*. This Chapter sets out the General Anti-Avoidance Rule (GARR). Section 95 delineates contours of the applicability of GARR and provides that notwithstanding anything contained in the Act, an arrangement entered into by an assessee may be declared to be an impermissible avoidance arrangement and the consequences in relation to tax arising therefrom may be determined subject to the provisions of this Chapter (X-A); and the explanation thereto declares (for the removal of doubts) that the provisions of the Chapter may be applied to any step in, or a part of the arrangement as they are applicable to the arrangement. Section 96 - defines an impermissible avoidance arrangement. Section 97 - delineates when an arrangement shall be deemed to lack commercial substance. Section 98 - sets out the consequences of an impermissible avoidance arrangement and Section 99 – the treatment of “connected person” and “accommodating party”. Section – 100 enacts that the provisions of this Chapter shall apply in addition to, or in lieu of any other basis for determination of tax liability; Section – 101 enacts that the provisions of this Chapter shall be applied in accordance with such guidelines and subject to such conditions and the manner as may be prescribed; and Section 102 defines expressions used in the several provisions in Chapter X-A.

Chapter XVII B of the Act :

S.201. (1) Where any person, including the principal officer of a company, --

(a) who is required to deduct any sum in accordance with the provisions of this Act; or

... … …

does not deduct, or does not pay, or after so deducting fails to pay, the whole or any part of the tax, as required by or under this Act, then, such person, shall, without prejudice to any other consequences which he may incur, be deemed to be an assessee in default in respect of such tax:

… … …

… … …

(1A) Without prejudice to the provisions of sub-section (1), if any such person, principal officer or company as is referred to in that sub-section does not deduct the whole or any part of the tax or after deducting fails to pay the tax as required by or under this Act, he or it shall be liable to pay simple interest, --

(i) at one per cent for every month or part of a month on the amount of such tax from the date on which such tax was deductible to the date on which such tax is deducted; and

(ii) at one and one-half per cent for every month or part of a month on the amount of such tax from the date on which such tax was deducted to the date on which such tax is actually paid,

and such interest shall be paid before furnishing the statement in accordance with the provisions of sub-section (3) of section 200.

… … …

Dated : 15-02-2013

JUSTICE GODA RAGHURAM

JUSTICE M.S. RAMACHANDRA RAO

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