

HIGH COURT OF DELHI : NEW DELHI

+ Judgment delivered on: 13.02.2009

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WP(C) No. 14869/2004

U.A.E.EXCHANGE CENTRE LTD.

..... Petitioner

Through : Mr.H.P.Ranina and Mr.Vivek
B.Saharya, Advocates

versus

U.O.I. & ANR.

..... Respondents

Through : Mr.R.D.Jolly, Advocate

CORAM :

HON'BLE MR JUSTICE BADAR DURREZ AHMED

HON'BLE MR JUSTICE RAJIV SHAKDHER

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| 1. Whether the Reporters of local papers may be allowed to see the judgment ? | Yes |
| 2. To be referred to Reporters or not ? | Yes |
| 3. Whether the judgment should be reported in the Digest ? | Yes |

RAJIV SHAKDHER, J.

1. By this writ petition, the petitioner seeks to challenge the advance ruling of the Authority For Advance Rulings (Income Tax), New Delhi (hereinafter referred to as "the Authority") dated 26.05.2004 passed in A.A.R.No.608/2003 pursuant to an application made by the petitioner under Section 245Q(1) of the Income Tax Act, 1961 (hereinafter referred to as "the Act").

2. In the application filed under Section 245Q(1) of the Act by the petitioner before the Authority, it had sought an advance ruling by the Authority with respect to the following question :

“Whether any income is accrued/deemed to be accrued in India from the activities carried out by the Company in India?”

2.1 The aforesaid question was posed by the writ petitioner in the background of the following facts as stated in its application to the Authority.

2.2 The petitioner is a limited liability company incorporated in the United Arab Emirates ('UAE'), with its head office at Abu Dhabi. The petitioner is engaged, among others, in offering remittance services for transferring of monies from UAE to various places in India. In order to facilitate the said purpose, the petitioner had opened liaison offices in India on 01.01.1997 under a licence granted by the Reserve Bank of India ('RBI') vide its communication dated 24.09.1996. As per the RBI communication dated 24.09.1996, the petitioner's liaison offices, in India, are permitted to undertake only the following activities:-

- (i) responding to enquiries from correspondent banks with respect to drafts issued;
- (ii) undertaking reconciliation of bank accounts held in India with correspondent banks under Drafts Drawing Arrangement;
- (iii) acting as a communication centre receiving computer advices of mail transfer from UAE and transmitting to the Indian correspondent banks;
- (iv) printing drafts and dispatching the same to the addressees and;
- (v) following up with the Indian correspondent banks.

2.3 By the very same communication, the RBI has specifically prohibited the petitioner's liaison offices, in India, from charging any commission or fee or from receiving or earning any remittances from any activity undertaken by

them. Furthermore, the expenses of the liaison offices in India are required to be met exclusively out of the funds received from abroad through normal banking channels.

2.4 Pursuant to the aforesaid permission granted by the RBI, the petitioner set up its first liaison office in Cochin, in the State of Kerala, in January, 1997. At present, the petitioner has liaison offices in Cochin, Chennai, New Delhi, Mumbai and Jalandhar in India.

2.5 It is the stand of the petitioner both before the authority below, as well as, before this court, that, through its six liaison offices, in India, it provides certain 'auxiliary' services to Non-Resident Indians ('NRI') in UAE to remit funds either on their account or for the benefit of their relatives/dependents. For the said purpose, a contract between the NRI remitter and the petitioner is executed in UAE, whereupon the NRI hands over his or her funds for remittance to the petitioner at any of the centres/outlets/camps of the petitioner in UAE. Each such transaction is a separate contract between the NRI remitter and the petitioner; governed by the UAE laws. Upon funds being collected, the petitioner makes an electronic remittance of the funds on behalf of its NRI customers' in either of the two ways:

(i) funds are remitted by telegraphic transfer through banking channels; or

(ii) on the request of the NRI remitter, the petitioner sends instruments/cheques through its liaison offices to the beneficiaries in India designated by the NRI remitter.

2.6 In the second option, the liaison offices in India download the particulars of remittances through the electronic media and then print cheques/drafts drawn on the banks in India, which, in turn, are couriered/despached to the beneficiaries in India, in accordance, with the instructions of the NRI remitter. In order to facilitate downloading of the information with regard to remittances, the liaison office in India, are connected with the main server of the petitioner in UAE. This information, which is contained in the main server is accessed by the liaison offices in India for the purpose of remittances of funds to the beneficiaries in India by the NRI remitters.

2.7. However, the point to be noted, is that, in either situation, that is, whether the option exercised by the NRI remitter for remittance of the funds is through telegraphic transfer of funds to a bank in India or, through a liaison office in India; the petitioner collects a fixed charge of Dirhams 15 in UAE. There is no additional or extra charge payable by the customer to the petitioner if the customer choses the second option.

2.8 On the aforesaid basis, as averred in the writ petition, the petitioner, in compliance of provisions of Section 139 of the Act, has been filing its return of income since, the assessment year 1998-99 right through till assessment year 2003-04. In all these years, returns have been filed showing 'Nil' income as according to the petitioner, no income accrued or deemed to have accrued in India both under the Act, as well as, the agreement entered into between the Government of Republic of India and the Government of UAE which is ubiquitously known as the Double Taxation Avoidance Agreement (in short 'DTAA'). The point to be noted at this stage is that the Government

of India entered into a DTAA with the government of UAE in pursuance of its powers under Section 90 of the Act, for the purposes of avoidance of 'Double Taxation and Prevention of Fiscal Evasion', with respect to, taxes and income on capital; which stood notified vide Notification No.G.S.R.No.710(E) dated 18.11.1993.

2.9 The 2nd respondent had accepted the returns for the aforesaid assessment years without demur. However, pursuant to impugned ruling of the Authority dated 26.05.2004, the 2nd respondent issued four notices of even date i.e., 19.07.2004 under Section 148 of the Act for assessment years 2000-01, 2001-02, 2002-03, 2003-04 respectively. The petitioner, being aggrieved by the action of the respondent in initiating proceedings under Section 148 of the Act on the purported ground that the respondent had reasons to believe that income for the assessment years mentioned in the aforesaid notices had escaped being taxed, preferred a writ petition before this court under Articles 226 and 227 of the Constitution of India. In the writ petition filed before us, the following reliefs have been claimed:-

- (i) Issue a Writ of Certiorari or any other Writ or Order quashing the Ruling of the AAR dated 26th May, 2004 passed at New Delhi;
- (ii) Issue a Writ of Certiorari or any other Writ or Order quashing the notice and assessment proceedings under Section 148 of the Income Tax Act, 1961, dated 19th July, 2004 for Assessment years 2000-01, 2001-02, 2002-03, 2003-04 and declare that the petitioner is not liable to tax in India;
- (iii) Issue a Writ, Order or Direction including Writ of Mandamus directing the respondents not to tax the petitioner in India because no income accrues or is deemed to accrue in India from its activities of liaison offices in India;
- (iv) Pending the disposal of this Writ petition, pass such ad-interim order as may be thought fit and proper directing Respondent No.2 not to initiate any assessment proceedings

pursuant to the notices issued under Section 148 of the Income Tax, 1961 for the assessment years 2000-01 to 2003-04;

(v) pass such other order as this Hon'ble Court may deem fit in the facts and circumstances of the case.

Submissions of petitioner's counsel

3 Learned counsel for the petitioner, Mr.H.P.Ranina has broadly made the following submissions:-

(i) the petitioner does not carry on any business/trade in India. Its business is carried out in UAE. This was sought to be demonstrated by alluding to the following facts:-

(a) after the contract for remittance of funds is executed in UAE, funds are handed over by the NRI remitter to the petitioner's collection centre/camp etc. located in UAE;

(b) the commission, which is equivalent to Dirhams 15 is received in UAE;

(c) the funds thereafter are remitted in accordance with the instructions of the customers either telegraphically through banking channels via banks nominated by the NRI remitter, or through cheques/drafts drawn on banks in India based on information downloaded by the petitioner's liaison offices in India by despatching the same through courier to the NRI remitter's beneficiaries in India.

- (ii) if the NRI remitter in UAE exercises the option of having funds transferred through the liaison office in India, no extra commission or fee is charged;
- (iii) the liaison office in India does not carry out any trading, commercial or industrial activity, in India. As a matter of fact, the RBI has specifically imposed a prohibition, while granting approval on opening liaison offices in India.
- (iv) based on the aforesaid facts, he submits, that the activity carried out in India cannot be construed as ‘business connection’ within the meaning of Section 5(2)(b) or Section 9(1)(i) – so as to hold that income is deemed to accrue or arise in India

3.1 As a necessary adjunct to his submissions above, the learned counsel for the petitioner further contended that, even if it is assumed, that the income is deemed to arise or accrue to the petitioner under the provisions of Sections 5(2) and 9(1)(i) of the Act, the business profits of the petitioner would be liable to tax, only if, it has permanent establishment within the meaning of Article 7(3) read with Articles 5(1) and (3) of DTAA .

3.2 It is the submission of the learned counsel for the petitioner, that the Authority in holding that, the income earned in UAE by the petitioner by virtue of business activity carried out in U.A.E. has a real and intimate relationship with the business activity carried out in India, has misconstrued the ratio of the judgments of the Supreme Court in the case of **CIT, Punjab vs. R.D.Aggarwal & Co;(1965) 56 ITR 20** and **Anglo French Textile Co Ltd vs. CIT;(1953) 23 ITR 101.**

3.3 It is also the contention of the petitioner that the Authority having recorded findings of fact in paragraph 6 of the impugned ruling, to the effect: that the business of the Petitioner is carried on in UAE; a contract for remitting the amounts is entered into with NRIs and is executed outside India; the commission for remitting the amounts is also earned by the Petitioner outside India, therefore no income accrues/arises or is deemed to accrue or arise in India in view of the principle that the income accrues in the country, in which, the contract is executed- it could not have, in paragraphs 7 to 11, more particularly, in paragraph 11, of the impugned ruling held that the income shall be deemed to, accrue/arise in UAE from a business connection in India.

3.4 It may be noted here that, apart from the above submission in the writ petition, one of the grounds which has been taken to challenge the ruling of the Authority, is that, the Authority has rendered its ruling beyond the period of six months as prescribed under Section 245R(6) of the Act. It is averred that the petitioner had filed the application with the Authority on 10.01.2003; while the ruling was rendered by the Authority on 26.05.2004 well beyond the period prescribed under the said provision. It may, however, be noted that at the stage of arguments, this ground was not pressed before us. We have taken note that the petitioner has given up the said ground of challenge.

Submission of the Respondent

4. As against this, the learned counsel for the respondent, Mr.R.D.Jolly, has raised a preliminary objection, which is that, in view of Section 245S, which provides, that the advance ruling pronounced by the Authority under the provisions of Section 245R shall be binding on the petitioner/applicant,

the Commissioner and the Income Tax authorities subordinate to him in respect of the application and the transactions on which ruling has been sought – this Court ought not to exercise its extra ordinary jurisdiction under Article 226 of the Constitution of India as, there is no case made out by the petitioner that the Authority has acted either without jurisdiction or in breach of the principles of natural justice.

4.1 As regards merits, the learned counsel for the Revenue, has largely placed reliance on the ruling of the Authority, by reiterating, that the activity undertaken by the liaison offices had a ‘real and intimate’ connection with business activity of the petitioner in UAE and hence, the business connection was established in terms of Section 9(1)(i) read with Section 5(2)(b) of the Act. He further contended that the liaison offices of the petitioner, in India, also represented the permanent establishment of the petitioner in India in terms of Articles 5(1) and 7 of the DTAA, and that, in respect of the second mode of remittance, whereby the liaison offices in India performed the function of downloading information in India, which was, stored in the main server in UAE for the purposes of printing cheques which were then, despatched/couriered to the NRI remitter’s beneficiaries, in India, has a crucial link, which enabled fulfillment of obligation undertaken by the petitioner under the contract with the NRI remitter in UAE and hence, could not be termed as an activity of an ‘auxiliary’ character, so as to, fall within the ambit of an exclusionary clause contained in Article 5(3) (e) of DTAA

Our reasoning with respect to preliminary objection of the respondent

5. The provisions for advance ruling are contained in chapter XIX-B of the Act, which was introduced in the Act, by virtue of the Finance Act, 1993

with effect from 01.01.1993. The said chapter consists of Sections commencing from Section 245N to Section 245V. Section 245N deals with definitions of various terms used in the chapter which, in sum and substance, define as to who can approach the Authority and, the kind of transactions on which the Authority can render its advance ruling. Section 245-O deals with the constitution of the Authority. The said Section provides for a three member authority, with the Chairman being a retired Judge of the Supreme Court and the other two members from Indian Revenue Service and Indian Legal Service respectively. Section 245P provides that no proceedings before, or pronouncement of advance ruling by the authority shall be questioned or become invalid on the ground of any vacancy or defect in the constitution of the authority. Section 245Q provides for the procedure for filing of an application before the authority, in the manner prescribed, stating the question, on which the advance ruling is sought by the applicant. Section 245R, significantly, provides for the procedure which the authority is required to adopt in deciding the question posed before it by the applicant. Under sub-section (1) of Section 245R, on receipt of an application, the Authority is required to forward a copy of the same to the Commissioner and, if necessary, call upon him to furnish the relevant records. After examining the application and the records, the Authority is empowered to allow or reject the application. Under the first proviso, the authority's jurisdiction to allow the application is excluded, with respect to issues which are also pending before Income Tax Authority or the Appellate Tribunal or involves determination of fair market value of any property or relates to a transaction or an issue, which is designed prima facie to avoid income-tax except in the case of a resident applicant falling in sub-clause (iii) of clause (b) of Section

245N. The second proviso to Section 245R clearly mandates that the Authority shall not reject any application unless the applicant has been given an opportunity of being heard. Under the third proviso, the said section, specifically, provides that where the application is rejected, reasons for rejection shall be given in the order. Under sub-sections (4) and (5) of the said Section, the Authority is required to give its advance ruling after examining the material placed before it by the applicant or that obtained by the Authority and after providing an opportunity to the applicant of being heard in person or his duly authorised representative. Section 245S specifies that the advance ruling pronounced by the Authority under Section 245R shall be binding both, on the applicant, as well as the Commissioner and the Authority below, in respect of, the applicant and the transaction with regard to which a ruling has been sought. Section 245T provides that the authority may declare its ruling as void ab initio based on the representation by the Commissioner or otherwise that the same has been obtained by fraud or misrepresentation of facts. Significantly, under Section 245U, the authority has been conferred with all the powers of the Civil Court under the Civil Procedure Code, 1908 (CPC) as referred to in Section 131 of the Act, while exercising its power under this chapter. Sub-section 245U(2) provides that the Authority is deemed a Civil Court for the purposes of Section 195 of the Criminal Procedure Code, 1973 (Cr. P.C.) and every proceeding before the Authority shall be deemed to be a judicial proceedings within the meaning of Sections 193 and 228 and also, for the purpose of Section 196 of the Indian Penal Code (IPC). The last Section in the Chapter being Section 245V. Under this Section, the Authority has been conferred with the power to

regulate its own procedure in all matters arising out of the exercise of its power under this Act.

6. At this point, it would be important to note that the powers given under Section 131 of the Act are the same powers which are vested in a Court under the CPC when trying a suit in respect of discovery, production of evidence, enforcing attendance of persons, issue of commission etc. A perusal of Section 245S of the Act shows that, while it is binding on the applicant, the transaction in relation to which the ruling is sought, the Commissioner and the Income Tax authorities subordinate to him, in respect of, the applicant and the transaction, it does not exclude the jurisdiction of the Courts either expressly or by implication. There is no provision which gives finality to the decision of the Authority. In our view, even though the provisions of Section 245S provide that the orders of the Authority would be binding, this, by itself, cannot exclude the jurisdiction of the Courts by implication or otherwise, as it does not provide for any adequate remedy to mitigate or deal with the grievance of the aggrieved party. Therefore, in our view the Courts would have jurisdiction to entertain actions under Article 226 of the Constitution impugning the ruling given by the Authority under Section 245R of the Act. [See : **Dhulabhai vs. State of MP; AIR 1969 SC 78 at page 89 (para 32)** and **Gurbax Singh vs. Financial Commissioner and Anr; 1991 Supp (1) SCC 167 at pages 174-175 (para 19)**]. The principles enunciated in the aforementioned judgments clearly point to the fact that Section 245S in Chapter XIX-B of the Act cannot be construed as an ouster clause, ousting the jurisdiction of the Courts.

7. This brings us to a question as to whether the Authority is a Tribunal within the meaning of Article 227 of the Constitution. The broad test which has been laid down by the Courts are that an Authority shall be construed to be a Tribunal within the meaning of Article 227 of the Constitution of India if it is invested with the judicial power of the State, which is, that it should act judicially after ascertaining the facts placed before it and upon application of the relevant law applicable to the facts obtaining in a case. Broadly, the expression used in various judgments rendered by various Courts is that an Authority would be a Tribunal if it has the 'trappings of a Court'. What are the indices of the expression 'trappings of a court' are best illustrated in the judgment of the Supreme Court in the case of Jaswant Sugar Mills Ltd, Meerut vs. Lakshmi Chand & Ors; AIR 1963 SC 677, Justice Shah (as he then was) at page 685 (paras 19 & 20) observed as follows:-

"Their primary function is administrative and not judicial. In deciding whether an authority required to act judicially when dealing with matters affecting rights of citizens may be regarded as a tribunal, though not a court, the principle incident is the investiture of the "trappings of a court" - such as authority to determine matters in cases initiated by parties, sitting in public, power to compel attendance of witnesses and to examine them on oath, duty to follow fundamental rules of evidence (though not the strict rules of the Evidence Act), provision for imposing sanctions by way of imprisonment, fine, damages or mandatory or prohibitory orders to enforce obedience to their commands. The list is illustrative; some, though not necessarily all such trappings will ordinarily, make the authority which is under a duty to act judicially, a 'tribunal'.

20. Mahajan, J., in *Bharat Bank Ltd. v. Employees of Bharat Bank Ltd.* [(1950) S.C.R. 459] observed at p. 476 :

*"As pointed out in picturesque language by Lord Sankey L.C. in *Shell Co. of Australia v. Federal Commissioner of Taxation* [[1931] A.C. 275], there are tribunals with many of the "trappings of a Court" which, nevertheless, are not Courts in the strict sense of exercising judicial power. It seems to me that such*

tribunals though they are not full-fledged Courts, yet exercise quasi-judicial functions and are within the ambit of the word 'tribunal' in article 136 of the Constitution. It was pointed out in the above case that a tribunal is not necessarily a Court in this strict sense because it gives a final decision, nor because it hears witnesses on oath, nor because two or more contending parties appear before it between whom it has to decide, nor because it gives decisions which affect the rights of subjects, nor because there is an appeal to a Court, nor because it is a body to which a matter is referred by another body. The intention of the Constitution by the use of the word 'tribunal' in the article seems to have been to include within the scope of article 136 tribunals adorned with similar trappings as Court but strictly not coming within that definition."

8. Seen in the light of the principles enunciated above, it is clear that the Authority constituted under Chapter XIX-B of the Act is a Tribunal as it is invested with powers of a civil court by virtue of provisions of Section 131 of the Act; which includes all such powers a court is vested with under the CPC when trying a suit in respect of matters relating to discovery, inspection, enforcing attendance of persons including officials of banking company and examining such persons on oath, compelling production of books of accounts, summons of accounts etc. Under the provisions of 245R, there is a requirement to give an opportunity of hearing to the applicant and to give reasons for rejecting an application. The cumulative effect of the powers invested and the attributes of the Authority, when gleaned from the provisions of Chapter XIX-B, leave no doubt in our minds that it has the 'trappings of a court' and hence, would undoubtedly qualify as a Tribunal within the meaning of Article 227 of the Constitution of India. Thus, the Authority would be amenable to the jurisdiction of this court under Article 227, and more so, under Article 226 of the Constitution of India which, without doubt, has a wider reach being conferred with jurisdiction to issue

appropriate writ order or direction to any “person or Authority” for enforcement of fundamental rights under Part-III of the Constitution as also for any other purpose. [See: **Kihoto Hollohan vs. Zachillhu and Ors; 1992 Supp (2) Supp 651 at 706 to 712 (paras 98 to 111)**]

9. This brings us to the next limb of the preliminary objection as to whether in the facts and circumstances of the present case, we should exercise our writ jurisdiction. This would require us to look at the merits of the case. Before we do that, we would like to touch upon the well engrafted principles, with respect to, the exercise of writ jurisdiction by Courts, in such like, matters. Essentially, when superior courts exercise the power of judicial review in respect of orders, decisions or, as in the instant case, a ruling of administrative quasi-judicial authority or a judicial authority, it looks at the decision making process and not at the decision itself. A superior court is not expected to substitute its view with that of the authority whose decision is impugned before it as long as the view taken by the authority, is a plausible view which is free from errors of jurisdiction or errors apparent on the face of the record. The statement of law on this aspect of the matter, in respect of a quasi judicial authority, has been very aptly enunciated in the judgment of seven Judges of the Supreme Court in the case of **Ujjam Bai vs. State of U.P.; AIR 1962 SC 1621 at page 1629 (para 15)** reads as follows:-

“where a quasi-judicial authority has jurisdiction to decide a matter, it does not lose its jurisdiction by coming to a wrong conclusion, whether it is wrong in law or in fact.”

9.1 It is now fairly well settled that superior courts can issue a writ of certiorari where there is an error of law which is apparent on the face of record as these are akin to errors of jurisdiction as against mere errors of law.

The statement of law in Halsbury's Laws of England [4th Edition Vol. 1(1)

Para 73 Page 127] best captures the accepted position in law.

“Where upon the face of the proceedings themselves it appears that the determination of an inferior tribunal is wrong in law, certiorari to quash will be granted. Thus, it will be granted where a charge laid before magistrates, as stated in the information, does not constitute an offence punishable by the magistrates, or where it does not amount in law to the offence of which the accused is convicted, or where an order is made which is unauthorized by the findings of the magistrates, or is materially defective in form. Most of these cases are to be regarded as usurpations of jurisdiction; but it is settled that certiorari will also be granted to quash a determination for error of law on the face of the record although the error does not go to jurisdiction.”

9.2 This again brings us to the question as to what would be an error apparent on the face of record. The Supreme Court in the case of *Hari Vishnu Kamath vs. Ahmad Ishaque*; AIR 1955 SC 233 at page 244 (paras 22 & 23) has laid down a litmus test, that is, it should be one which is ‘manifest error apparent on the face of the record’. This brings us to another quintessential question as to what constitutes a ‘record’. In the case of *R. vs. Northumberland Compensation*; (1952) 1 All.E.R. 122 at page 131 Lord Justice Denning has opined that the record must contain “at least the document which initiates the proceedings, the pleadings if any, and the adjudication, but not the evidence, nor the reasons, unless the Tribunal chose to incorporate them.” We may also note the decision in *MMB Catholicos vs. M.P. Athanasius*; AIR 1954 SC 526 at page 543 (para 36) wherein the Supreme Court expanded the scope of what would constitute a ‘record’.

9.3 The difficult part is as to how to differentiate between the error of law as against the error of jurisdiction as in most cases errors of law impinge upon the jurisdiction of the court. However, this distinction has disappeared with the judgment of House of Lords in the case of *Anisminic vs. Foreign*

Compensation Commission; (1969) 2 AC 247 as also in **O' Reelly vs. Mackman; (1983) 2 AC 237 at Page 278.** The position which has emerged is that, in so far as, errors of fact are concerned the Courts will quash a decision which is based on an erroneous but a decisive fact which goes to the root of jurisdiction, or is based on no evidence or is wrong, misunderstood or ignored. Similarly Courts would also quash decisions of the Tribunal which is a decisive error of law since all errors of law are considered as errors of jurisdiction (See: *Administrative Law 8th Edition by H.W.R.Wade and C.F.Forsyth at Page 286*). What has, however, been accepted, is that, the Writ Courts in India have power to issue the writ of certiorari, in respect of, errors apparent on the face of the record committed by a subordinate Court or a Tribunal.

10 In the light of the aforesaid well entrenched principles of law it would be appropriate to consider the decision of the Authority in the facts of the present case.

10.1 The admitted facts in this case are that the petitioner is offering remittance services to NRIs in UAE. The contracts pursuant to which funds are handed over by the NRIs to the petitioner in UAE are entered into between the petitioner and the NRI remitter in UAE. The funds are collected from the NRI remitter by the petitioner in UAE. A one time fee of Dirhams 15 is levied and collected by the petitioner from the NRI remitter in UAE. The funds are transmitted to the beneficiaries of the NRI remitter, in India, either by telegraphic transfer through normal banking channels via banks in India or are remitted by involving the liaison offices of the petitioner in India, who in turn, download the information and particulars necessary for

remittance by using computers in India which are connected to the servers in UAE, by drawing cheques on banks in India in couriering/despaching the same to the beneficiaries of the NRI remitter in India.

11 The Authority in paragraph 11 of the impugned ruling held that downloading of information by the liaison offices in India with regard to the beneficiaries of the NRI remitters in India and thereupon the act of the cheques or drafts being drawn on banks in India, in the name of beneficiaries and their despatch through couriers to the beneficiaries constitutes an activity, which enabled the petitioner to complete the transaction of remittance, in terms of the contract entered into with the NRIs. From this the Authority has concluded, that there is, therefore, a real and intimate relationship between the business carried on by the petitioner, for which, it receives commission in UAE. Furthermore, the Authority has held that the activities of the liaison offices of downloading of information, printing and preparation of cheques and drafts, and sending the same to the beneficiaries in India, contribute directly or indirectly to the earning of income by the petitioner by way of commission. It also held that there is continuity between the business of the petitioner in UAE and the activities carried on by the liaison offices in India. On this basis, the Authority concluded that the income shall be deemed to accrue or arise to the petitioner in UAE from 'business connection' in India.

11.1 In our view, the Authority has misconstrued the provisions of Section 90 of the Act which empowers the Central Government to enter into an agreement with the Government outside India for the purposes of granting relief in respect of aspects referred to in sub-section (1) clauses (a) to (d). It

is well settled that where India has entered into a treaty for avoidance of double taxation as also in respect of purposes referred to in Section 90 of the Act, the contracting parties are governed by the provisions of the treaty. The treaty overrides the provisions of the Act. The answer with respect to the same is clearly evident from a reading of Sections 4 and 5 of the Act. Section 4 which relates to the chargeability and Section 5 which encapsulates what would constitute the total income which would be chargeable under the Act are provisions, which are, both subject to other provisions of the Act. Therefore, a treaty entered into by the Government of India, which is, notified under Section 90 of the Act will govern the liability to tax, in respect of, those to whom the treaty applies. In this regard, the observations of the Supreme Court in the case of **Union of India vs. Azadi Bachao Andolan;** (2003) 263 ITR 706 at page 724 are apposite:-

“A survey of the aforesaid cases makes it clear that the judicial consensus in India has been that Section 90 is specifically intended to enable and empower the Central Government to issue a notification for implementation of the terms of a double taxation avoidance agreement. When that happens the provisions of such an agreement, with respect to cases to which where they apply, would operate even if inconsistent with the provisions of the Income Tax Act. We approve of the reasoning in the decisions which we have noticed. If it was not the intention of the Legislature to make a departure from the general principle of chargeability to tax under Section 4 and the general principle of ascertainment of total income under Section 5 of the Act, then there was no purpose in making those sections “subject to the provisions” of the Act. The very object of granting the said two sections with the said clause is to enable the Central Government to issue a notification under Section 90 towards implementation of the terms of the DTA’s which would automatically override the provisions of the Income-Tax Act in the matter of ascertainment of chargeability to income-tax and ascertainment of total income, to the extent of inconsistency with the terms of the DTAC.

The contention of the respondents, which weighted with the High Court, viz, that the impugned Circular No.789 (see [2000] 243 ITR (St.) 57) is inconsistent with the provisions of the Act, is a

total non sequitur. As we have pointed out, Circular No.789 (see [2000] ITR(St.) 57) is a circular within the meaning of section 90; therefore, it must have the legal consequences contemplated by sub-section 2 of the Section 90. In other words, the circular shall prevail even if inconsistent with the provisions of the Income-tax Act, 1961, in so far as assesses covered by the provisions of the DTAC are concerned.”

11.2 In the present case, the liability to tax under the DTAA is governed by Article 7. Sub-section (1) of Article 7 of the DTAA categorically provides that profits of an enterprise of a contracting State shall be taxable only in that State, unless the enterprise carries on business, in the other State, through a permanent establishment situated thereof. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State, but only so much of that, as is attributable to the permanent establishment. Therefore, the liability on account of tax, of an enterprise of either of the contracting State, in India, would arise if the enterprise in issue, i.e., the petitioner, had a permanent establishment in India. The provisions of Section 5(2) (b) and Section 9(1)(1) of the Act would have, in our view, no applicability. Discussion with respect to the ‘business connection’ in the impugned ruling was, in our view, unnecessary. The Authority had to determine only whether the petitioner carried on business in India through a permanent establishment. For this purpose it was required to examine the definition of permanent establishment as contained in Article 5 of DTAA read with Article 5(3)(e). There is no dispute raised by the petitioner that it maintains liaison offices in India and hence, would fall within the definition of permanent establishment in accordance with the provisions of Article 5(2)(c). The petitioner, however, has contended both before the Authority and before us that it falls within the exclusionary clause contained in Article

5(3)(e) in as much as the activity carried on by the liaison offices in India, has an ‘auxiliary’ character. On this aspect of the matter the discussion and reasoning by the Authority is contained in paragraphs 12 to 15 of the impugned ruling. The Authority came to the conclusion that the activity carried on by the liaison offices in India did not have an ‘auxiliary’ character in terms of Article 5(3)(e) of the Act as the option of remitting of funds through the liaison offices in India was exercised by the NRI remitter which was *“nothing short of, as in the words of the parties, performing contract of remitting the amounts”*. The Authority, thus, held that while, in respect of all remittances of funds by telegraphic transfer through banking channels, the role of the liaison offices in India of an ‘auxiliary’ character, the same was not true in respect of remittance of funds through liaison offices in India. This was based on the reasoning that without remittances of funds to the beneficiaries in India performance under the contract would not have been complete and thus, the downloading of data, preparation of cheques for remitting the amount, despatching the same through courier by the liaison offices, constituted an important part of the main work, which was, remitting the amount to the beneficiaries as desired by the NRIs. Based on this reasoning, the Authority came to the conclusion that the work of the liaison offices in India, being a significant part of the main work of UAE establishment, the liaison office of the petitioner, in India, would constitute a ‘permanent establishment’ within the provisions of the DTAA.

12 In our opinion, this view is clearly erroneous. We are living in an era where the world is described euphemistically as ‘flat’ or even a global village. Organisations and companies operate transnationally. There is an

eagerness to bring to tax by States income, by employing deeming fictions so that incomes which ordinarily do not accrue or arise within the taxing State are brought within the States' tax net. It is in this context that the expression 'permanent establishment' appearing in the DTAA has to be viewed. In the case of DTAA under consideration in the present case under Article 5 read with Article 7, profits of an enterprise are liable to tax in India if an enterprise were to carry on business through permanent establishment, meaning thereby fixed place of business through which business of an enterprise is wholly or partly carried on. Under Article 5(2)(c), amongst others, permanent establishment includes an office. However, Article 5(3) which opens with a non-obstante clause, is illustrative of instances where-under the DTAA various activities have been deemed as ones which would not fall within the ambit of the expression 'permanent establishment'. One such exclusionary clause is found in Article 5(3)(e) which is: maintenance of fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character. The plain meaning of the word 'auxiliary' is found in Black's Law Dictionary 7th Edition at page 130 which reads as "aiding or supporting, subsidiary". The only activity of the liaison offices in India is simply to download information which is contained in the main servers located in UAE based on which cheques are drawn on banks in India whereupon the said cheques are couriered or despatched to the beneficiaries in India, keeping in mind the instructions of the NRI remitter. Can such an activity be anything but auxiliary in character. Plainly to our minds, the instant activity is in 'aid' or 'support' of the main activity. The error into which, according to us, the Authority has fallen is in reading Article 5(3)(e) as a clause which permits making a value judgment as to

whether the transaction would or would not have been complete till the role played by liaison offices in India was fulfilled as represented by the petitioner to their NRI remitter. According to us, what has been lost sight of, is that, by invoking the clause with regard to permanent establishment, we would, by a deeming fiction tax an income which otherwise neither arose nor accrued in India – when looked at from this point of view, the exclusionary clause contained in Article 5(3) and in this case in particular, sub-clause (e) have to be given a wider and liberal play. Once an activity is construed as being subsidiary or in aid or support of the main activity it would, according to us, fall within the exclusionary clause. To say that a particular activity was necessary for completion of the contract is, in a sense saying the obvious as every other activity which an enterprise undertakes in earning profits is with the ultimate view of giving effect to the obligations undertaken by an enterprise vis-a-vis its customer. If looked at from that point of view, then, no activity could be construed as preparatory or of an ‘auxiliary’ character. On this aspect of the matter, the Supreme Court in the case of **DIT(International Taxation) vs. Morgan Stanley & Co; 2007(7) SCC 1** amongst other issues was called upon to decide as to whether back office operations carried on by Morgan Stanley Company for one of its Morgan Stanley Advantages Services Pvt. Ltd would qualify as having a permanent establishment in India. The Supreme Court, while holding that back office operations fall within the exclusionary clause Article 5(3) (e) of Indo-US Double Taxation DTAA, which is, identical to DTAA under consideration in the present case, came to the conclusion that back office operations came within the purview of Article 5(3)(e). It is laid down by the Supreme Court in the case of **Morgan Stanley (supra)** that in ascertaining what would

constitute a ‘permanent establishment’ within the meaning of Article 5(1) of the Indo-US DTAA, one had to undertake what is called a functional and factual analysis of each of the activities undertaken by an establishment. In that case the Supreme Court came to the conclusion that the entity located in India which was engaged in only supporting the front office functions of Morgan Stanley & Co., a non-resident, in fixed income and equity research and information technology enabled services such as data processing support centre, technical services and reconciliation of accounts being back office operators would not fall with Article 5(1) of the Indo-US DTAA.

13 In view of the fact that the ruling rendered by the Authority proceeded on a wrong premise, inasmuch as, it firstly examined the case from the point of view of Section 5(2)(b) and Section 9(1)(1) of the Act, while it was required to look at the provisions of DTAA for ascertaining the petitioner’s liability to tax and, secondly, it ignored the plain meaning of the terms of exclusionary clause, i.e., Article 5(3)(e), while examining as to whether by setting up a liaison office in India would result in setting up a permanent establishment within the meaning of DTAA, the decision of the Authority in these circumstances, being contrary to, the well established principles, as well as, provisions of law, would amount to an error apparent on the face of the record and hence, amenable to a writ of certiorari. In these circumstances, we are inclined to quash and set aside the impugned ruling of the Authority dated 26.05.2004. In this matter, even though, as discussed above, we are not required to discuss as to whether the activity carried on by the liaison offices of the petitioner in India resulted in a ‘business connection’ so as to bring the income earned by the petitioner within the ambit of Section

9(1)(1) and Section 5(2)(b) of the Act, we are of the opinion that the Authority has misconstrued the ratio of the judgments of the Supreme Court in the case of *Anglo French Textile Co Ltd vs. CIT; (1953) 23 ITR 101* and *CIT, Punjab vs. R.D. Aggarwal & Co; (1965) 56 ITR 20*. The ratio in both the judgments is that the non-resident entity could be taxed only if there was business connection between the business carried on by a non-resident which yields profits or gains and some activity in the taxable territory which contributes directly or indirectly to the earning of those profits or gains. The acid test for determination of a business connection as laid down in the aforementioned judgments is that there must be a real and intimate relationship between the activity of a non-resident outside the taxable territory with that of activity in the taxable territory. Therefore, the profit or gains earned by the non-resident should accrue or arise due to direct or indirect contribution of the activity carried out in the taxable territory entailing an element of continuity. A fortiori every such activity would not come within the purview of the expression 'business connection'. According to accepted business notions and usages, a particular activity may be a well defined business operation. Activities which are not well defined or are of casual or isolated character would not fall within the ambit of this aforementioned test.

13.1 In our view, the activity carried on by the liaison offices in India did not, in any manner, whatsoever, contribute directly or indirectly to the earning of profits or gains by the petitioner in UAE. As indicated above, every aspect of the transaction was concluded in UAE. The commission for the services of remittances offered by the petitioner was also earned in UAE.

The activity performed by the liaison offices in India was only supportive of the transaction carried on in UAE. It did not contribute to the earning of profits or gains by the petitioner in UAE. The reasoning of the Authority in paragraph 11 of the impugned order does not commend to us.

13.2 This is made even more clear if a reference is made to explanation 2 to Section 9(1). The said explanation reads as follows:-

“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 contact 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*
- (c) habitually secures orders in India, mainly or wholly for the non-resident or that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident.”*

13.3 The explanation is a pointer to the fact that in order to have a business connection, in respect of a business activity carried on by non-resident through a person situated in India it should involve more than what are supportive or subsidiary to the main function. Illustratively, clauses (a) to (c) includes activities such as habitually concluded contracts on behalf of non-resident, maintaining of all stocks and goods and merchandises from which he regularly delivers goods or habitually secures orders in India mainly or wholly for the non-resident.

13.4 Curiously, while the Authority has returned a finding of fact that none of the activities mentioned in explanation (2) to Section 9(1)(1) is carried on

by the petitioner in India, it then went on to apply the ratio of the judgment of the Supreme Court in the case of ***R.D.Aggarwal*** (*supra*) to hold that the activity carried on by the liaison offices of the petitioner, in India, constituted a ‘business connection’ in India and hence, income shall be deemed to accrue/arise in India, to the petitioner, situated in UAE, from business connection in India. In our opinion, the Authority has clearly erred in applying the ratio of the judgments of Supreme Court in the case of ***R.D.Aggarwal*** (*supra*) and ***Anglo French Textile Co*** (*supra*) which was not applicable in the present case.

14 In the circumstances, we quash the impugned order of the Authority. In so far as the other prayers are concerned we refrain from examining the matter, in respect of the same as in either situation it would be incumbent upon respondent to consider withdrawal of the notices under Section 148 of the Act if the only ground available for reopening the assessments of earlier years was the impugned ruling rendered by the Authority. In the event the respondent has additional grounds which are sustainable in law, it would be open to the petitioner to resist the re-opening of assessment by taking recourse to the remedies available under the Act.

15 The writ petition is disposed of in the aforesaid terms.

RAJIV SHAKDHER, J

BADAR DURREZ AHMED, J

February 13, 2009

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