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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Decided on: 17.08.2016

+ **ITA 461/2008**

+ **ITA 638/2008**

DIRECTOR OF INCOME TAX

..... Appellant

Through: Mr. Dileep Shivpuri, Sr. Standing
Counsel along with Mr. Sanjay
Kumar, Jr. Standing Counsel.

versus

TOKIO MARINE & FIRE INSURANCE CO. LTD. Respondent

Through: Mr. Siddharth Bawa and Mr. Shyamal
Anand, Advocates.

CORAM:

HON'BLE MR. JUSTICE S. RAVINDRA BHAT

HON'BLE MR. JUSTICE NAJMI WAZIRI

MR. JUSTICE S. RAVINDRA BHAT (OPEN COURT)

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1. The assessee is a non-resident company, incorporated in Japan; it opened a liaison office (LO) in India in 1997, with permission of the Reserve Bank of India (RBI). It entered into a joint venture agreement with IFFCO; the JV was called IFFCO-Tokio General Insurance Business Co. Ltd and was incorporated on 17th January, 2000 for the purpose of insurance business in India. The LO was opened to assist in the formation of the JV. The assessee took the stand that the LO was set-up to finalize preparation of the JV agreement and also for applying for license from the regulating authorities to conduct the general insurance business, for the purpose of which four expatriate officers were deputed to the LO. It was claimed that the work of the LO was preparatory in nature and, therefore, it did not constitute a permanent establishment (PE). The AO negated this contention and held that the LO did constitute a business connection, leading to a PE

which rendered the assessee liable to tax in India. The CIT(A), on appeal, reversed this finding, upon a factual analysis of the various circumstances. The Revenue's appeal to the Income Tax appellate Tribunal (ITAT) was rejected by the impugned order.

2. In the above circumstances, the questions of law formulated for these appeals – at the time of admission- were firstly whether the said offices (LOs) could be regarded as PE and secondly whether its income from imports in India were not taxable by reason of the Indo-Japan Double Taxation Avoidance Agreement (Indo-Japan DTAA).

3. In the opinion of the Court, both questions can be taken together for consideration. The Revenue's complaint is that four expatriates were employed by the LO, who did all the necessary work and followed up with lawyers, consultants, chartered accountants and regulatory authorities in connection with the assessee's business. Though they did not *per se* enter into any agreement on behalf of the company, they did all that was necessary for the purpose of business, i.e making extensive survey, identifying the JV partner most suited for the purpose, negotiating with the concerned parties and most importantly was incurring considerable expenditure. All these factors clearly pointed to a deep and intimate commercial connection between the assessee and the foreign entity, demonstrating that it was the latter's PE. These arguments were contested on behalf of the respondent assessee. It was argued that all those steps taken by the four expatriates were for laying the groundwork for the assessee to start business in India; even the agreement signed between the parties was merely witnessed by the said four officials and could not be said to be a PE.

4. Article 5 of the Indo-Japan DTAA governs this case. If indeed the office in question- the LO results in profit or income generation, it can be said to be a PE. The question is whether the activities undertaken can warrant such a conclusion. The evidence on record- concurrently found shows that four expatriate employees were there at the relevant time. The task of this office was to identify a proper JV partner; involve in the negotiation, identify and engage all manner of consultants, lawyers, accountants, etc. Its incurring expenditure (a factor taken into consideration by the Courts) did not *ipso facto* satisfy the requisite test.

5. The *ratio* of the judgments of the Supreme Court in *Anglo French Textile Co Ltd v. Commissioner of Income Tax* (1953) 23 ITR 101 and *Commissioner of Income Tax, Punjab v. R.D. Aggarwal & Co.* (1965) 56 ITR 20 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.

6. In the present case, both the CIT(A) and ITAT have found that the four expatriate employees posted in India performed purely preparatory functions: identifying a JV partner, negotiating with parties, seeking regulatory approvals and clearances, consulting management experts, lawyers and accountants toward setting up of the JV, towards entering into agreements, etc. They did not even enter into agreements on behalf of the assessee; instead they merely signed them as witnesses. These could not *per se* or by themselves amount to a business connection as to create a PE in India.

7. The DTAA clearly envisions that offices that perform auxiliary and preparatory services are not to be treated as business connection. Black's Law Dictionary defines the word 'auxiliary' to mean as "aiding or supporting, subsidiary". The word 'auxiliary' owes its origin to the Latin word 'auxiliarius' (from *auxilium* meaning 'help'). The Oxford Dictionary defines the word 'auxiliary' to mean "providing supplementary or additional help and support". In the present context, the expression means carrying on activities, other than the main business functions, that aid and support the assessee. In the context of the contracts in question, where the main business is insurance business - coverage of industries and others who are subject to general insurance policies by entering into contracts of insurance, collecting *premia*, setting up networks of distributors or offices for that purpose etc., the functions performed by the expatriates in the liaison office were of auxiliary character - an activity which aids and supports the Assessee in carrying on its

main business, but not the business itself. The findings of the authorities below, therefore, were warranted and call for no interference.

8. In view of the above conclusions, the questions framed are answered against the Revenue and in favour of the assessee; these appeals are, therefore, dismissed.

S. RAVINDRA BHAT
(JUDGE)

NAJMI WAZIRI
(JUDGE)

AUGUST 17, 2016
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