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

+ **ITA 902/2009**

DIRECTOR OF INCOME TAX

Through: Mr.Asheesh Jain, Sr.Standing Counsel. Appellant

versus

MITSUI & CO. LTD.

Through: Mr.Mayank Nagi, Advocate. Respondent

**CORAM: JUSTICE S. MURALIDHAR
JUSTICE PRATHIBA M. SINGH**

ORDER

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12.10.2017

1. This is an appeal by the Revenue against an order dated 8th February 2008 passed by the Income Tax Appellate Tribunal ('ITAT') in ITA No. 1806/Del/2005 for the Assessment Year ('AY') 2001-02.

Questions of law

2. While admitting this appeal by the order dated 7th September 2009, the following questions were framed by the Court for consideration:-

“a) Whether the ITAT was right in holding that the Indian branches/offices of the assessee company and their activities cannot be regarded as permanent establishment of the assessee in India and income directly or indirectly attributable to these branches/offices is not taxable in India?

b) Whether the ITAT was right in law in holding that the assessee company does not have any permanent establishment

in India and its income from business turnover/imports in India was exempt in view of Agreement for Avoidance for Double Taxation between India and Japan?

c) Whether the learned ITAT erred in holding that the Assessing Officer on direction for inquiry from CIT (A) under section 250(4) could have carried out survey under section 133A of the Act?

d) Whether the ld. ITAT erred in holding that burden of proof has shifted to Revenue Authorities though Assessee is canvassing a benefit and seeking preferential treatment under the statute?”

Background facts

3. The background facts are that the Respondent-Assessee is a non-resident foreign company formed and incorporated under the laws of Japan having its Head Office (‘HO’) in Tokyo, Japan. It is an international trade house undertaking business activities in a large number of countries.

4. Admittedly, the Assessee has Liaison Offices (‘LO’) in India at Kolkata, Chennai, Mumbai and New Delhi. It also undertakes several turnkey projects. The Assessee has been regularly assessed to tax in India under the Income Tax Act, 1961 (‘Act’) as a non-resident foreign company. It has been filing reports under the Act on a consolidated basis both for the LOs as well as the projects.

5. For AY 2001-02, the Assessee filed its return on 31st October 2001 declaring an income of Rs. 8,31,14,709/-. This comprised of income of Rs. 8,29,04,578/- from the business of providing Engineering Consultancy for the various projects executed in India. However, it declared NIL income

from the LOs.

Assessment order

6. The return was picked up for scrutiny. In the assessment order dated 29th March 2004, the Assessing Officer ('AO') held that the LOs of the Assessee in India constituted its Permanent Establishment ('PE') in India in as much as the LOs were engaged in locating the customers, making offers to them, getting the terms of contract settled with them and ensuring the opening of letters of credit and other necessary follow up measures. The AO noted that the Special Bench of the ITAT had, by its judgment dated 11th October 1991 in the Revenue's appeals for AYs 1980-81 and 1981-82, held that LOs were only supplying information and, therefore, could not constitute a PE in India. The Special Bench overruled the decision of the ITAT for AYs 1978-79, 1979-80 which held to the contrary.

7. In the present assessment order, the AO highlighted what, according to him, were aspects which escaped the attention of the Special Bench of the ITAT which pronounced the aforementioned order. The AO concluded as under:

“1.4 (...) The activities of the head office and all other offices of the Assessee are more or less similar in nature. All of them locate and negotiate with vendors or customers as the case may be and effect the supply of goods or services. It may also be pointed out the Assessee apart from its affiliates or subsidiary, maintain as many as 89 such offices all over the world. Therefore it can be seen that the offices in India are undertaking more or less same or similar activities as that of its head office or other offices that constitute the principal and core activity of the Assessee. Signing of contract by the entity overseas etc. are mere formal arrangements. Substance of the matter should

have precedence over the form. Signing of a negotiated document overseas, does not mitigate the importance of negotiating and finalizing the deal. It is also interesting to note that the assessee needs to forward all its documents like performance guarantee, Letter of Credit through its office in India, but the contract is signed overseas independent of the India office.”

8. As a result, after allowing the expenses incurred by the Assessee at its offices located in India, the entire profit of the Assessee from the sale of goods in India was held to be taxable in India. The net taxable income was, therefore, determined as Rs.65,03,70,558/-.

Order of the CIT (A)

9. The Assessee then went in appeal before the Commissioner of Income Tax (Appeals) [‘CIT (A)’]. During the pendency of the appeal before it, the CIT (A) sought a remand report from the AO to examine “as to whether the facts in these two years were same as in earlier years and to offer his comments that whether the appellant had any PE in India during these years.”

10. Pursuant to the said direction of the CIT (A), the AO undertook a survey of the LO of the Assessee in Delhi under Section 133A of the Act and submitted a detailed report dated 31st January 2005 in which he observed that the Assessee was carrying on business in a regular way from the LOs in India. The AO also recorded the statement of Mr. Yuki Morata, Administrative Head of the LO on oath and also obtained copies of various documents found on the said premises. The AO in his remand report submitted as under:

“During the survey it was found that the Assessee was operating from a full-fledged office comprising of 3 floors with staff strength of approximately 100 people including 6 expatriates. The LO is modelled in the same fashion as its head office is modelled. The LO had various different Deptts Viz Machinery Deptt, Energy Deptt, Information, Electronics and Telecommunication business unit, Automobile Unit, lease for aeroplane Unit, Organic Chemical Business Unit, Consumer Services Business Unit. However, after incorporation of an Indian subsidiary since March 2003, only two departments i.e. Machinery Department and Energy Department are being handled by LO.”

11. By the order dated 18th February 2005, the CIT (A) dismissed the appeal by concurring with the AO that the LOs of the Assessee in India constituted PEs. The CIT (A) referred to the following materials to arrive at a conclusion that the Assessee was carrying on activities in its LOs which were not merely preparatory or auxiliary in nature:-

“(i) Business report for the month of February 2003 ((placed at pages 53 to 61 of the Paper Book of the Revenue).

(ii) E-mail dated 07.11.2002 sent by Mr. Aswani Bhagwan from Bombay office to Mr. Haga, Head of machinery Division of on textile business (placed at pages 51 to 52 of the Paper Book of the Revenue).

(iii) Report of the meeting on 01.04.04 with M/ s Tata Tele Services Ltd. (placed at pages 48 to 50 of the Paper Book of the Revenue).

(iv) Copy of MOU Between Balmer Lawrie & Co. Ltd. and Yanmar Co. Ltd. for supply of cool container (placed at pages 27 to 33 of the Paper Book of the Revenue).

(v) Copy of successor report submitted by an employee of LO to three expatriates of New Delhi LO along with a MOU ((placed at pages 93 to 110 of the Paper Book of the Revenue).

(vi) Statement of Mr. Yuki Morata, Director and, Chief Financial Officer recorded on date of survey on 25.01.2005 (placed at pages 1 to 7 of the paper book of the Revenue).”

12. The CIT (A) concluded:

“7. (...) Considering the total activities of the appellant in India and business model it will be appropriate and justifiable that 50% of the total net income as computed in para 6.1 is attributable to Indian operations. Accordingly, 50% of the net income as determined in para 6.1 should be taken as the income of the appellant attributable to the P.E. in India. AO should re-compute & determine the income attributable to PE in India accordingly. Therefore, this ground is partly allowed.”

Impugned order of the ITAT

13. The Assessee then went before the ITAT which, by the impugned order, allowed its appeal. The ITAT noticed that under Article 5 (6) (e) of the Double Taxation Avoidance Agreement (‘DTAA’) between India and Japan, “a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character” was excluded from the definition of a PE.

14. The ITAT took note of the decision of the Special Bench of the ITAT for AYs 1980-81 and 1981-82 holding that the LOs of the Assessee were only carrying on the work of supply of information and liaison work. They were not carrying on any trade in India and therefore, could not be considered to be a PE. It was further noticed that the Special Bench decision was

consistently followed by the ITAT in all succeeding AYs up to AY 1998-99.

15. The ITAT then discussed each of the materials referred to by the CIT (A) in its order and came to the following conclusions:-

(a) The document at para 10 (i) above was merely a business report prepared at Tokyo and forwarded to the General Manager in Delhi which gave a summary of activities undertaken and business done by the HO. There was nothing to suggest from the said document that any business was done by the LO. The main test was whether the LO could independently take a business decision to undertake trading and commercial activity. It was held that the said document did not indicate or suggest so. Further the said report dated March, 2003 was for the month of February, 2003, i.e. a period beyond the previous year relevant to the AY in question and therefore was not relevant. The CIT(A), therefore, had erred in relying on such a document.

(b) The document at (ii) above was an e-mail sent by an employee of the LO at Bombay to Mr. Haga, Head of Machinery Division, of the LO relating to textile business. It was dated 7th November 2002 and, therefore, did not relate to the AY in question. However, it only suggested passing information from one person to another at the LO in Bombay in respect of the cotton yarn for various customers in Philippines. The said e-mail could not be read to conclude that the contract was either negotiated or concluded in India by the LO.

(c) The document at (iii) above was a report of the meeting between

Tata Teleservices Limited and the Assessee. It was a normal practice of the LO to receive delegations from abroad and arrange meetings. The said document also did not suggest that the employees were concluding contracts in India on behalf of the HO.

(d) The document at (iv) above was a Memorandum of Understanding ('MOU') signed by the representative of the LO wherein the name of the LO was appearing as a witness. The MOU was between Balmer Lawrie & Co. Limited and Yanmar Co. Limited and it was unsigned and undated. It did not establish that the LO was party in any trading or commercial activities.

(e) The document at (v) above was an MOU between Yanmar Diesel Engine Co. Limited, Japan, the Assessee and Transport Corporation of India Limited. The MOU is dated 29th January 2002 and, therefore, was not relevant for the AY in question. There was no consideration or revenue involved in the MOU and it was only for exploring new business of collecting information/responses. This document also did not establish that the LO was engaged in any activity other than those which were preparatory and auxiliary in nature.

16. The ITAT concluded that there was no clinching evidence to establish that the LO finalized and transacted a business deal on its own or in the name of the HO. The ITAT also discussed in detail the statement of Mr. Yuki Morata recorded during the survey undertaken on 25th January 2005. Whatever he explained of the role and activities of the LO did not show that the LO was undertaking any trade or commercial

activities by itself. It was noted that in response to Questions 9 and 11, Mr. Yuki Morata specifically noted that the pre-contract negotiations were done by the HO personnel with Indian clients and after the award of the contract, the LO did not take part in follow-up of payments for supplies transacted by the HO. Further, in answer to Question 10, it was stated that the LO had no role to play in the logistical aspects of the contract undertaken by the HO. Again, in response to Question 14, it was stated that the LO had no role to play in after sales service. In response to Question 15, it was stated that the LO did not have any technical personnel on its rolls.

17. The ITAT then discussed the power of the CIT (A) under Section 250 (4) of the Act to direct the further enquiry by the AO and submit a report. Further, the ITAT found that the order of the CIT (A) did not refer to any such direction being issued to the AO under Section 250 (4) of the Act. The ITAT found that, in the circumstances, the CIT (A) had “entertained an evidence produced by the Assessing Officer which was hitherto not available during the assessment proceedings and such evidence was therefore not the basis for making the assessment which was in challenge.” It had further not been established that such evidence was collected at the behest of the CIT (A) in terms of Section 250 (4) of the Act. It was held that the AO could not have produced such evidence before the CIT (A). Further, Rule 46A was not applicable in the present case as no application had been made for leading additional evidence. It was accordingly concluded that such evidence collected by the AO by undertaking a survey after completion of the assessment could not be considered in the appellate proceedings in the absence of an order of the

CIT (A) under Section 250 (4) of the Act.

Analysis and reasons

18. Mr. Asheesh Jain, the learned Senior Standing Counsel for the Revenue, has placed before the Court the remand report dated 31st January 2005 prepared by the AO for submission to the CIT (A) in the course of the appellate proceedings. The Court has also been taken through the statement recorded by Mr. Yuki Morata and the answers given by him to specific queries. The Court is unable to be persuaded that the ITAT erred in its conclusion that the evidence produced by the AO does not show that the LOs of the Assessee carried on any activity which was not incidental and auxiliary in nature.

19. It is urged by Mr. Jain that the ITAT had merely gone by the fact that the Reserve Bank of India ('RBI') had not found the Assessee to be in violation of any of the conditions subject to which it was permitted to operate its LOs in India. The Court finds that, independent of the above factor, the ITAT has in fact examined in detail all the materials referred to by the AO in its remand report as well as the order of the CIT (A) and has given detailed reasons why none of these materials establish that the LOs were used by the Assessee to carry on any business or trading activity in India. The said factual finding by the ITAT has not been shown to be perverse.

20. The Court further notes that there was no basis for the AO to conclude that the Special Bench of the ITAT had erred in its conclusion in favour of the Assessee that the LOs were not carrying on any activity which was either incidental and auxiliary in nature. With the consistent position in this regard

continuing since 1977-78, in the absence of any evidence to suggest a change in the circumstances, there was no warrant for the AO and the CIT (A) to take a different view of the matter.

Conclusion

21. Accordingly, the Court answers Questions (a) and (b) in the affirmative, i.e. in favour of the Assessee and against the Revenue. Question (d) is answered in the negative, i.e. in favour of the Assessee and against the Revenue.

22. In view of the above conclusions, the Court does not consider it necessary to answer Question (c). It is left open for consideration in an appropriate case.

23. For the aforementioned reasons, the appeal is dismissed but, in the circumstances, with no orders as to costs.

S. MURALIDHAR, J.

PRATHIBA M. SINGH, J.

OCTOBER 12, 2017
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