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

% *Date of Decision: 23.10.2024*

+ **ITA 792/2023**

THE COMMISSIONER OF INCOME TAX –
INTERNATIONAL TAXATION -3

.....Appellant

Through: Mr Ruchir Bhatia, SSC with Mr
Anant Mann, Advocate.

versus

ZEBRA TECHNOLOGIES ASIA PACIFIC
PET. LTD.

.....Respondent

Through: Mr Sudarshan Roy and Dr Shashwat
Bajpai, Advocates.

CORAM:

HON'BLE MR. JUSTICE VIBHU BAKHRU

HON'BLE MS. JUSTICE SWARANA KANTA SHARMA

VIBHU BAKHRU, J. (ORAL)

1. The Revenue has filed the present appeal under Section 260A of the Income Tax Act, 1961 (hereafter *the Act*) impugning an order dated 28.02.2023 (hereafter *the impugned order*) passed by the Income Tax Appellate Tribunal (hereafter *ITAT*) in ITA No.1084/Del/2022 in respect of the assessment year (AY) 2017-18.

2. The aforesaid appeal (ITA No.1084/Del/2022 captioned *Zebra Technologies Asia Pacific Pet. Ltd. v. Commissioner of Income Tax (International Taxation)-3, Delhi,*) was preferred by the respondent (hereafter *assessee*) before the learned ITAT, assailing the order dated 25.03.2022 passed by the Commissioner of Income Tax (hereafter *CIT*) under Section 263 of the Act in respect of the AY 2017-18.



3. The assessee is a company which is incorporated under the laws of Singapore and is a tax resident of Singapore. The concerned authorities in Singapore had issued a Tax Residency Certificate (TRC) in favour of the assessee. On the aforesaid basis, the assessee had sought to avail the benefit of India – Singapore Double Taxation Avoidance Agreement (DTAA). The assessee claimed that it is engaged in the business of wholesale distribution of electronic products as well as services related to after sales, repairs, and technical support services to the customers in various parts of the world including India. During the period relevant to the AY 2017-18, the assessee had received a sum of ₹19,52,78,490/- for rendition of technical support, repair, and maintenance services. In addition, it has also received the amount of USD \$2,09,19,539/- from off-shore sales of products.

4. The assessee had filed its income tax returns for the relevant assessment year, *inter alia*, claiming that it was not liable to pay tax in respect of the aforesaid receipts. According to the assessee, it did not have a permanent establishment (PE) in India and had also not made available technical knowhow, knowledge, and skill to the Communication Test Design Indian Pvt. Ltd. (CTDIPL). Therefore, the aforesaid income was not chargeable to tax in India under the Act by virtue of the DTAA.

5. The Assessing Officer (AO) issued notices under Section 142(1) and 143(2) of the Act seeking certain information. During the said proceedings, the assessee had also explained that it had entered into the agreements with the third-party channel partners as well as an Indian entity that is, CTDIPL, to carry out repairs and maintenance services in India on behalf of the assessee. The assessment proceedings culminated by the AO in its



assessment order dated 25.12.2019, whereby the income returned by the assessee was accepted.

6. The learned CIT initiated the proceedings under Section 263 of the Act by issuance of a Show Cause Notice dated 01.02.2022 (hereafter *SCN*). The said *SCN* is not on record. However, a copy of the same has been handed over to this Court. The same indicates that the learned CIT had concluded that the AO had not conducted the necessary inquiries and verified the facts for accepting the assessee's claim that its income was not chargeable to tax under the Act by virtue of the DTAA. The learned CIT noted that the AO had not called for the relevant details or taken any steps to verify whether the assessee had a PE in India during the relevant period. It was also observed that the AO had not carried out any inquiry to ascertain whether any commercial substance existed in Singapore. And, whether the assessee was merely a conduit company and used with an object to obtain the tax benefit under the DTAA.

7. Mr Bhatia, the learned counsel appearing for the Revenue also handed over a printout of the order sheet which indicates that after issuing of the *SCN*, certain hearings were held. The said proceedings culminated in the order dated 25.03.2022 passed by the learned CIT under Section 263 of the Act. The learned CIT, *inter alia*, concluded that the assessee had been structured for the purposes of tax avoidance and for treaty shopping. The relevant extract of the learned CIT's order, setting out the conclusion and reasoning in this regard is reproduced below:

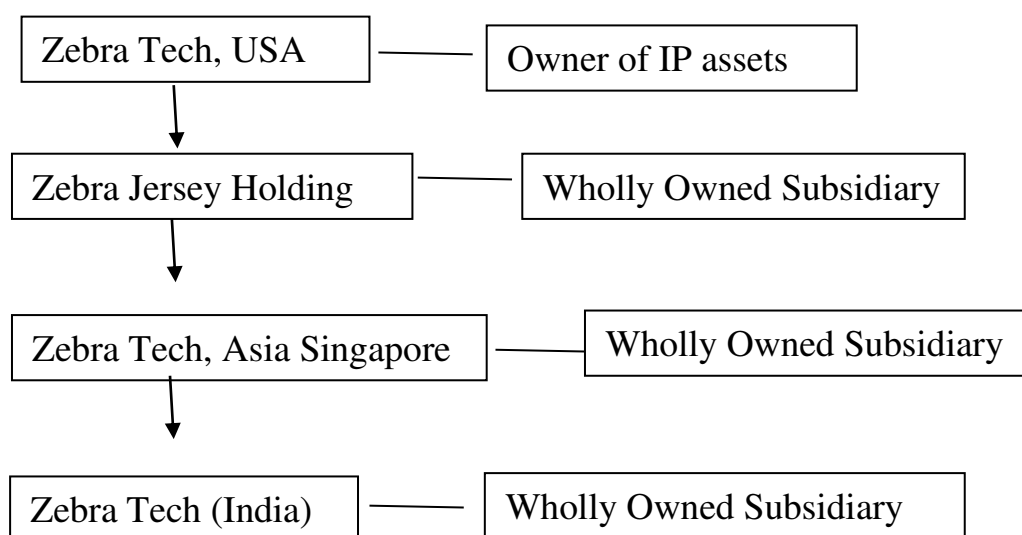
“Arrangement is a tax avoidance through treaty shopping

13.8 On this background, the examinations of facts in the



instant are conducted to ascertain as to whether the arrangement made by the assessee company is tantamount to tax avoidance. In order to understand this, the approach needed is to oversee the arrangement as a whole instead of the transaction in question. This principle has also been approved by Hon'ble SC in Vodafone case.

The Group structure reveals that Zebra Technology Inc. a tax resident of USA is the ultimate parent company who is the owner of the Intellectual property (IP) of Zebra products. It interposed two wholly owned subsidiaries: one in Jersey and other in Singapore. It formed a wholly owned subsidiary Zebra jersey Holding I Ltd in Jersey which is a tax haven. Zebra Jersey in tum interposed a wholly owned Singapore subsidiary named Zebra Technologies Asia Pte, the assessee company. The assessee company sells the Zebra products and also provides services to customer- users in India. The marketing support in India is said to be provided by Zebra Technologies India Pvt. Ltd, a wholly owned subsidiary of the assessee company.



13.9 As discussed in preceding paragraphs, the assessee provides automated services to Indian customers-users through online platforms. The moot question would be when the IP assets are owned by the USA parent, then why the



selling/services have not been made from USA as commercial outcomes in India would be identical whether it operates from USA or Singapore or Jersey or anywhere else. The whole arrangement is made to avoid payment of legitimate taxes. This is explained as follows. If the service income is received in USA, then such service would suffer source taxation in view of Article 12 of India- USA DTAA. Clause (a) of Article 12(7) deems income to arise in India if the payer is a resident in India. Even though “make available” threshold is also available under India- USA DTAA, the deeming provision under Article 12(7)(a) of India-USA DTAA would create taxation of such service income in India as in this case, the payers are Indian customers-users. Therefore, a subsidiary was interposed in Singapore with a primary objective to get the benefits of India-Singapore DTAA. India-Singapore DTAA does not have an article similar to Article 12(7) of the India-USA and at the same time it has “make available threshold” for service income to be liable for taxation in India.

13.10 In addition to the above, the transactions are characterized as sale of services instead of fees for services. This was made to the transaction the colour of business income. The business income is taxable in India only when the non-resident creates a PE in India. By this way, the income could neither be taxed in India as FTS nor as the business income. As a result, the assessee avoids payment of any tax in India year after year.

13.11 The taxpayer not only avoid payment of taxes in India but also in other jurisdictions as well. This is explained as follows. The USA parent formed a wholly owned Subsidiary in Jersey. The IP assets are transferred to Jersey entity. The jersey entity in turn licenses the IP assets to Singapore entity. It has significant tax advantages. The Singapore entity is liable to pay license fee to Jersey entity. The license fee is a tax-deductible expense and therefore, this would reduce the tax liability for Singapore entity. The financial statements furnished during the proceedings reveals that the assessee company (Singapore entity) incurs huge losses year after year.



On the other hands, the income by way of license fee is not taxable in Jersey. The jersey entity being a subsidiary of USA parent may repatriate the income in the form of dividend. However, under USA domestic law, the dividend income is taxed in USA once the same is received by the shareholders. Therefore, if the Jersey entity defers the payment of dividend, then there is no taxation even in USA. Therefore, in reality the whole income does not suffer any taxation.

13.12 The point that is made out here is the whole arrangement is a tax avoidance arrangement including treaty shopping. The Zebra USA has resorted to treaty shopping by interposing of a subsidiary in Singapore to get the favorable tax position under India-Singapore DTAA. As a result, **the assessee is not entitled to the benefits under India-Singapore DTAA.** In that case, **the taxability would be decided only under the provisions of Income-tax Act.** As discussed in preceding paragraphs, the service income is taxable as FTS under the section 5(2) read with section 9(1)(vii) of the Act.”

8. Aggrieved by the order dated 25.03.2022, the assessee preferred an appeal (ITA No.1084/Del/2022), which was allowed by the learned ITAT in terms of the impugned order.
9. The learned ITAT had faulted the learned CIT for not affording the assessee an opportunity to rebut the allegations that it was merely a conduit without any substance and had entered into an agreement for the purposes of taking an advantage of the DTAA.
10. In the aforesaid context, the Revenue has projected several questions for consideration including the following question:

“2.3 Whether on the facts and in the circumstances of the case, the Ld. ITAT has erred in not appreciating the fact that availing the treaty benefit is dependent upon the fact of each year and, therefore, passing an order by allowing the benefits



of Indian-Singapore DTAA by following the order of earlier assessment year without making detailed enquiry to find out that the Assessee is involved in treaty shopping thereby making it ineligible to chain DTAA benefits which makes the assessment order erroneous being prejudicial to the interest of revenue in view of legal provision under Explanation (2) in clause (a) and (b) of section 263 of the I.T. Act, which deems an order erroneous and prejudicial to the interest of revenue if passed without enquiry?”

11. Mr Bhatia, fairly states that if the Revenue does not succeed in the aforesaid question, the other questions as projected would not arise.

12. Mr Bhatia referred to the SCN and submitted that the same clearly mentioned the issue regarding the assessee being a conduit company. He relied on the following statement made in the said SCN:

“...AO had not carried out any inquiry to ascertain whether there existed any commercial substance in Singapore and whether any tax avoidance arrangement was made where in the form of a conduit company with an objective to obtain tax benefits under the India-Singapore DTAA.”

13. A plain reading of the SCN indicates that the learned CIT had called upon the petitioner to show cause why the proceedings under Section 263 of the Act not be taken in view of what was stated to be the failure on part of the AO to conduct the necessary enquiries.

14. The learned CIT had faulted the AO for not undertaking certain enquiries including verifying whether the assessee has a PE in India; whether in terms of Section 9(1)(vii) of the Act, the income is chargeable as fees for technical services (FTS); whether TDS at the rate of 10% on all the remittances made to the assessee were deducted; whether the condition as set out in Article 12 of the DTAA in regard to taxation of FTS were



satisfied. In a similar vein, the learned CIT had also faulted the AO for not making enquiries regarding the commercial substance of the assessee in Singapore and whether it was a conduit company form for obtaining the tax benefits under the DTAA. The said observations were made only for the purposes of calling upon the assessee to show cause why the proceedings not be initiated under Section 263 of the Act. However, thereafter, the learned CIT had not put the issue regarding treaty shopping to the assessee. Undisputedly, the tentative opinion formed by the learned CIT that the assessee was a conduit company for the reasons as articulated in the order dated 25.03.2022, was not put to the assessee. Clearly in the circumstances, the assessee had not given any opportunity to satisfy the learned CIT regarding its view, which has found its way in the aforesaid order of the learned CIT's conclusion.

15. In the given facts, we are unable to find any fault with the decision of the learned ITAT in setting aside the order dated 25.03.2022 on the ground that the assessee was not afforded an opportunity to counter the allegation that it was a conduit company without any substance.

16. In our view, no question of law arises in the present appeal. The same is, accordingly, dismissed.

VIBHU BAKHRU, J

SWARANA KANTA SHARMA, J

OCTOBER 23, 2024

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Click here to check corrigendum, if any