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

+ ITA 1273/2018
MOSER BAER INDIA LTDAppellant
Through: Mr. Upvan Gupta, Advocate.
versus

INCOME TAX OFFICER,
WARD 75(4), & ANR.Respondents
Through: Mr. Sunil Agarwal, SSC with
Mr. Shivansh B. Pandya, Mr.
Viplav Acharya, JSCs and Mr.
Utkarsh Tiwari, Advocates.

73.
+ ITA 1280/2018
MOSER BAER INDIA LTDAppellant
Through: Mr. Upvan Gupta, Advocate.
versus

INCOME TAX OFFICER,
WARD 75(4), & ANR.Respondents
Through: Mr. Sunil Agarwal, SSC with
Mr. Shivansh B. Pandya, Mr.
Viplav Acharya, JSCs and Mr.
Utkarsh Tiwari, Advocates.

74.
+ ITA 1282/2018
MOSER BAER INDIA LTDAppellant
Through: Mr. Upvan Gupta, Advocate.
versus

COMMISSIONER OF
INCOME-TAX (TDS 1), & ANR.Respondents
Through: Mr. Sunil Agarwal, SSC with
Mr. Shivansh B. Pandya, Mr.
Viplav Acharya, JSCs and Mr.
Utkarsh Tiwari, Advocates.

75.
+ ITA 1283/2018
MOSER BAER INDIA LTDAppellant



Through: Mr. Upvan Gupta, Advocate.
versus
COMMISSIONER OF
INCOME-TAX (TDS 1), & ANR.Respondents
Through: Mr. Sunil Agarwal, SSC with
Mr. Shivansh B. Pandya, Mr.
Viplav Acharya, JSCs and Mr.
Utkarsh Tiwari, Advocates.

CORAM:
HON'BLE MR. JUSTICE YASHWANT VARMA
HON'BLE MR. JUSTICE RAVINDER DUDEJA

ORDER
29.08.2024

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1. These appeals are directed against the consolidated order of the **Income Tax Appellate Tribunal**¹ dated 14 November 2016 passed under Section 254(1) of the **Income Tax Act, 1961**², dismissing four appeals preferred by the appellant pertaining to **Assessment Years**³ 2004-05 to 2007-08.

2. By an order dated 11 October 2023, these appeals stood admitted on the following questions of law:-

“(i) Whether the Tribunal misdirected itself in law in sustaining the action of the respondents/revenue in holding the appellant/assessee as an “assessee in default” for alleged failure to deduct tax at source concerning the payments in the form of interest paid to its lender i.e., Hypo Bank?

(ii) Whether the Tribunal misdirected itself on facts and in law in denying the benefit of paragraph 3(b) of Article 11 of the Double Taxation Avoidance Agreement [in short, “DTAA”] obtaining between India and Germany, in respect of the interest paid by the appellant/assessee to Hypo Bank?

(iii) Whether in the facts and circumstances of the case, the Tribunal erred in law in not applying the DTAA with Germany in respect of the interest paid to ANZ and Standard Chartered Bank?”

3. The principal dispute emanates from a lending agreement which

¹ Tribunal

² Act

³ AYs



was entered into by the appellant-assessee with a consortium of banks and deals with the payment of interest in terms thereof. The assessee took the stand that the interest would not be taxable in India in light of Article 11(3)(b) of the **Indo-Germany Double Taxation Avoidance Agreement**⁴. This was so contended in light of the credit facilities extended being guaranteed repayment by Hermes-Deckung according to the appellant-assessee. The respondents, however, appear to have taken the position that the remittance of interest as part of the repayment of that lending facility was liable to be subjected to a withholding tax in terms of Section 195 of the Act. The respondents have also contended that Paragraph 3(b) of Article 11 would be inapplicable since the payment of interest was essentially in the nature of consideration of an insurance facility for exports which had been extended. It is this view which has been affirmed by the Tribunal.

For the purposes of examining the issues which arise, we deem it apposite to take note of the following essential facts.

4. Undisputedly, the petitioner had entered into a **Hypo Foreign Currency Loan Agreement**⁵ dated 22 May 2001. As the recitals of that Agreement bear out, the same was entered into between the appellant-assessee on the one hand and **Bayerische Hypo-Und VereinsBank AG**⁶, Australia and New Zealand Banking Group Ltd. and Standard Chartered Bank, London. The latter three entities were compendiously defined under the aforesaid Agreement as the ‘Lenders’. The Preamble of that Agreement reads as follows:-

“Preamble

Moser Baer India Ltd. a limited company incorporated and existing

⁴ Indo-Germany DTAA

⁵ Agreement

⁶ HVB



under the laws of the Republic of India with registered office at 63, Ring Road, Lajpat Nagar-III, New Delhi -110024 India, has entered into export contracts ("Export Contracts") with STEAG HamaTech AG, Ferdinand-ven-Steinbein-Ring-10, 75-7 Sternenfeis, Germany, ("Exporter") as more fully set out in Appendix A hereto.

Upto 85% of the contract values of the Export Contract will be insured with the German Export Credit Insurance Company Hermes Kreditversicherungs AG, Hamburg ("Hermes") under the rules and regulations of the official export credit insurance system of the Federal Republic of Germany and will be financed by way of a buyer's credit between the Borrower and the Lenders.

The sole purpose of this Loan Agreement is to finance the contract values of the Export Contracts up to the proportions set out in Appendix A."

As is manifest from the aforesaid extract, the principal purpose of the Agreement was to finance the contract values of the export contracts up to the proportions set out in Appendix A thereof.

5. The Agreement further defined the expression 'Facility' in the following terms:-

"Facility shall mean the amounts disbursed and/ or still to be disbursed and outstanding under the Loan Agreement."

6. The 'Interest Payment Date' was defined in the Agreement in the following terms:-

"Interest Payment Date shall mean the last day of each Interest Period. Interest Period shall mean a period of six months each unless otherwise stipulated in the Loan Agreement whereby the first day of each interest Period will not be considered for the calculation of the interest being due on the next Interest Payment Date."

7. Article 1 of the Agreement spelt out the relevant provisions of the amount which was to be disbursed and the underlying purpose of the facility. That Article is reproduced hereinbelow:-

"Article 1

Amount and Purpose of the Facility



1.1 Subject to the terms and condition of this Agreement, the Lenders will make available to the Borrower a Facility of up to a maximum of 85% of the total contract values of the Export Contract i.e. EUR 93,645,026 (in words EUR ninety three million six hundred and forty five thousand and twenty six) and each of the Lenders agrees, in the event of a disbursement pursuant to Article 3 to contribute during the Utilization Period to the amounts to be disbursed hereunder an amount corresponding to each Lender's Share, however, up to an aggregate maximum principal amount not exceeding each Lender's Commitment.

1.2 The sole purpose is the financing of up to 85 per cent of the contract values of the Export Contracts as more fully set out in Appendix A hereto, to the extent covered by the Guarantee of Finance Credit mentioned in Article 14 of this Loan Agreement.

1.3 The obligations of each Lender under this Loan Agreement are several; the failure of any Lender to perform such obligations shall not relieve the other Lender(s) or the Borrower of any of their respective obligations or liabilities under this Loan Agreement.

1.4 Notwithstanding any other term of this Loan Agreement, the interests of the Lenders are several and the amount due to each Lender is a separate and independent debt. Each Lender shall have the right to protect and enforce its rights arising out of this Loan Agreement and it shall not be necessary for the other Lender to be joined as an additional party in any proceedings for this purpose.”

As is evident from a reading of Article 1.2 thereof, the fact that the Agreement was concerned with financing of up to 85 per cent of contract values of the export contracts stood reiterated in that particular clause.

8. The terms of payment were stipulated and prescribed in Article 12 which reads as under:-

“ARTICLE 12

Payments

12.1 The Borrower shall remit all payments due from him in connection with the Loan Agreement exclusively in freely available legal currency of the federal Republic of Germany to the account of the Agent No. 700 202 70 with Landesrentalbank Munich or any other account designated by the Agent from time to time. The Borrower's payment obligations shall only be deemed fulfilled when



and to the extent that payments have been credited to these accounts and are at the free disposal of the Agent expenses shall be paid in the currency in which they have been incurred.

12.2 The Borrower shall not be entitled to exercise any rights of retention or any set off or counterclaim against arising from the Loan Agreement.

12.3 As least 10 calendar days before the due date of any payment obligation of the Borrower under the Loan Agreement the Agent shall inform the Borrower and the other Lender(s) by telex or telefax of :

- a) the total amount due.
- b) its due date
- c) the nature of the claim and is composed by several amounts their respective individual amounts and nature.
- d) its computation in case of commitment fee and interest.
- e) the account to which the payment has to be effected.

Provided that no failure by the Agent so to inform the Borrower shall relieve the Borrower of any of its obligations under the Loan Agreement.

In case such notice is given with respect to an interest payment and a disbursement under the Facility shall occur after the giving of such notice and before the due date specified in such notice, interest on such disbursed amounts accruing during the period beginning on the disbursement day and ending on such due date shall contrary to the stipulations in Article 4 hereof not be payable in the Interest Payment Date subsequent to the disbursement day but on the next following Interest Payment Date.”

Article 12.1 placed the borrower under an obligation to remit all payments due from it in connection with the Agreement in the legal currency prevalent in the Federal Republic of Germany to the account of the agent i.e. HVB.

9. Article 14 comprised the guarantee conditions for repayment of the loan which had been extended. Articles 14.1 and 14.2 are reproduced hereinbelow:-



“ARTICLE 14

Guarantee of Finance Credit

14.1 The Lender’s claims under the facility are the subject of an export credit insurance cover in form of a Guarantee of Finance Credit issued by the Federal Republic of Germany, represented by Hermes Kreditversicherungs-AG under its rules and regulations for export credit insurance as the case may be.

14.2 In view of the above, the Lenders are entitled to allow the competent bodies of the aforementioned government to inspect any records which may relate to the Loan Agreement and to furnish copies thereof.”

10. In order to understand the nature of the Hermes guarantee, it would also be apposite to refer to the relevant parts of the Export Guarantee Scheme as formulated by the Federal Republic of Germany. The relevant parts thereof are extracted hereunder:-

“A. PRINCIPLES

1. The purpose of the Export Guarantees provided by the Federal Government (HERMES cover) is to support German exports. It is one of the main goals to create a level playing field for German exporters towards their competitors from other countries on an international market with keen competition.

Legal framework

2. The promotion of German exports forms an important part of Germany’s foreign trade and payments policy and can only be carried out within the provisions of the framework of currently valid Foreign Trade and Payments Law, in particular the export control regulations. In other respects the general laws (e.g. the provisions for criminal law) as well as the legal provisions of intergovernmental institutions and relevant international arrangements with direct binding effects in the Federal Republic of Germany should apply (e.g. regulations to safeguard against hazardous chemicals). In addition to this the Political Principles of the Federal Government, effective 19th January 2000 and the decisions of the Federal Security Council apply for the export of war arms and other military supplies.

Exports of nuclear technology designed for the building of new or conversion of existing nuclear power plants are excluded from support by the Federal Government. Depending on the individual transaction, measures and equipment related to the decommissioning



of existing plants or the improvement of their safety standards may be eligible for support, provided they are not classified nuclear technology.

Export is eligible for support under normal circumstances

3. Eligibility for support and justifiability of risk are basic criteria for the granting of cover by the Federal Government. German exports are of vital importance for the Federal Republic of Germany. Therefore, they are – within the legal framework pointed out in 2. – in general eligible for support. Nevertheless, in the decision making process aspects that go beyond economic policy objectives will be taken into account as well and given careful consideration.”

As is manifest from a reading of the fundamental principles underlying that scheme, the same appears to have been formulated in order to give an impetus to German exports and to ensure repayment to parties which may enter into such arrangements.

11. The appellant has also drawn our attention to a certificate which came to be issued in furtherance of that scheme and which reads thus:-

“EULER HERMES Kreditversicherung
Christian Schumilas
Tel. +49 (0) -40/88 34-91 48 Fax +49 (0) 40/88 34-90 29
Christian.schulilars@eulerhermes.com

Hamburg. 20.03.2007

Bayerische Hypo- und Vereinsbank AG
MJS3R3
Brau Choo-Ludwig
Am Eisbach 4
80538 Monchen
DN 163337/MFA 902291/FKG/Indien
Finanzkreditgarantie
a/ Moser Baer India Limited, New Delhi (664/12196)

TO WHOMSOEVER IT MAY CONCERN

This is to certify that the loan agreement dated May 22, 2001 entered among Moser Baer India Limited, Bayerische Hypo- und Vereinsbank Aktengesellschaft, Australia and New Zealand Banking Group. Ltd., Niederiassung Frankfurt am Main and Standard Chartered Bank, London is the subject of one export Insurance cover in the form of a Guarantee of Finance Credit issued by the Federal Republic of Germany (also referred to as HERMES-Deckung),



represented by Euler Hermes Kreditversicherungs-AG (formerly known as Hermes Kreditversicherungs-AG).

We further confirm that Euler Hermes Kreditversicherungs-AG (formerly known as Hermes Kreditversicherungs -AG) to authorized to manage the Export Credit Guarantee Scheme of the Government of the Federal Republic of Germany.

Best Regards

Sd/-”

This certificate too speaks of the Agreement noticed above and the same being subject to an export insurance cover in the form of a Guarantee of Finance Credit titled Hermes-Deckung. Although the certificate does allude to export insurance cover, it proceeds further to underscore the same being concerned with guaranteeing the finance credit issued.

12. Article 11 of the Indo-Germany DTAA reads as under:-

“11 – INTEREST

“(1) Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

(2) However, such interest may also be taxed in the Contracting State in which it arises and according to the laws of that State, but if the recipient is the beneficial owner of the interest, the tax so charged shall not exceed 10 per cent of the gross amount of the interest.

(3) Notwithstanding the provisions of paragraphs 1 and 2-

XX XX XX XX XX XX

(b) interest arising in the Republic of India and paid to the Government of the Federal Republic of Germany, the Deutsche Bundesbank, the Kreditanstalt für Wiederaufbau or the Deutsche Investitions-und Entwicklungsgesellschaft (DEG) and interest paid in consideration of a loan guaranteed by HERMES-Deckung shall be exempt from the Indian tax.

4. The term "interest" as used in this Article means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits,



and in particular, income from Government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest for the purpose of this Article.

5. The provisions of paragraphs 1, 2 and 3 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of Article 7 or Article 14, as the case may be, shall apply.

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13. As we construe Paragraph 3(b) of that Article, it becomes apparent that as long as the payment remitted was interest paid in consideration of a loan guaranteed by Hermes-Deckung, it would fall within the exclusionary clause of Article 11. Regard must be had to the fact that Paragraph 3 of Article 11 commences with a non-obstante clause and overrides the provisions contained in the preceding Paragraphs of that Article of the DTAA. Paragraph 3(b) thus clearly exempted all interest payments from Indian tax liabilities, provided it could be characterized as interest paid in consideration of a loan duly guaranteed by Hermes-Deckung.

14. We also take note of similar provisions in treaties which India has entered into with other countries and which aspect has been succinctly captured in the form of a table which is reproduced hereinbelow:-

S. No.	Country	Article of the DTAA	Text of the Article
1.	Canada	Article 11(3)(b)	(b) (i) interest arising in India and paid to a resident of Canada shall be taxable only in Canada if it is paid in



			respect of a loan <u>made, guaranteed or insured, or a credit extended, guaranteed or insured</u> by the Export Development Corporation;
2.	Hungary	Article 11(3)(b)	3. Notwithstanding the provisions of paragraph 2, interest arising in a Contracting State shall be exempt from tax in that State provided it is derived and beneficially owned by: (iii) (a) the Hungarian Exim Bank; or (b) a resident of Hungary if the interest is paid in respect of a loan <u>made, guaranteed or insured or a credit extended, guaranteed or insured by the Hungarian Exim Bank</u>;
3.	Israel	Article 11(3)(b)	3. Notwithstanding the provisions of paragraphs 1 and 2, interest arising in a Contracting State and paid to a resident of the other Contracting State shall be taxable only in that other State, if the interest is paid in respect of— (b) a loan made, refinanced, guaranteed or insured, or a credit extended, refinanced, guaranteed or insured by— (i) in the case of India, the Reserve Bank of India,
4.	Japan	Article 11(3)(b)	“3. Notwithstanding the provisions of paragraph 2, interest arising in a Contracting State shall be taxable only in the other Contracting State if: (b) the interest is derived and beneficially owned by a resident of that other Contracting State with respect to <u>debt-claims guaranteed, insured or indirectly financed by the Government of that other Contracting State</u>, a political sub-division or local authority thereof, or the central bank of that other Contracting State or any financial institution wholly owned by



			that Government.
5.	Latvia	Article 11(3)(b)	3. Notwithstanding the provisions of paragraph 2, interest arising in a Contracting State shall be exempt from tax in that State provided it is derived and beneficially owned by: (d) a resident of India, if the interest is paid in respect of a loan made, guaranteed or insured or a credit extended, guaranteed or insured by the Government, a political subdivision or a local authority of India or by any of the bodies mentioned in sub-paragraph (b) (i) or (c)
6.	Netherlands	Article 11(3)(b)	3. Notwithstanding the provisions of paragraph 2 (b) interest arising in one of the States and paid in respect of a loan guaranteed or insured by the Government of the other State shall be exempted from tax in the first-mentioned State.
7.	Swiss Confederation	Article 11(3)(b)	[3.] Notwithstanding the provisions of paragraph 2 (b) interest arising in India and paid to a resident of Switzerland shall be taxable only in Switzerland if it is paid in respect of a loan made, guaranteed or insured, or credit extended, guaranteed or insured under the Swiss provisions regulating the Export or Investment Risk Guarantee or by any institution specified and agreed in letters exchanged between the competent authorities of the Contracting States;

15. As would be evident from a reading of those clauses, various tax conventions use the expressions “guaranteed” or “insured”. However, insofar as the Indo-Germany DTAA is concerned, it restricts and confines itself only to interest in respect of a loan which is guaranteed by Hermes-Deckung. That guarantee was one extended to the lenders under the Agreement as would be evident from a



reading of Article 14 of the Agreement and was independent of the liability of the writ petitioner to make repayments.

16. Viewed in that light, and bearing in mind the obligation which was taken over by Hermes-Deckung by virtue of Article 14 of the Agreement, in our considered opinion, the payment could have only answered to the description of interest paid in consideration of a loan and clearly did not partake the character of insurance.

17. The Agreement itself was concerned with financing and extending credit facilities to the appellant to the extent of 85% of the Export Contract value. The consortium of banks had undertaken to provide credit facilities to the appellant-assessee to the aforesaid extent. The Agreement placed a corresponding obligation upon the appellant to repay the lenders and it was the lenders' claims which were guaranteed by Hermes-Deckung.

18. Regard must also be had to the fact that the Agreement was not concerned with providing a risk cover to the appellant-assessee in respect of a default event or any other contingency which could have formed the subject matter of an insurance contract. It was concerned solely with the ability of the appellant to repay the loans extended and to abide by the repayment conditions as contained therein.

19. The expression "insurance" has been defined by the *Black's Law Dictionary*, 8th Edn. in the following terms:-

- "insurance. 1.** A contract by which one party (the *insurer*) undertakes to indemnify another party (the *insured*) against risk of loss, damage, or liability arising from the occurrence of some specified contingency, and usu. to defend the insured or to pay for a defense regardless of whether the insured is ultimately found liable.
- An insured party usu. pays a premium to the insurer in exchange for the insurer's assumption of the insured's risk. Although indemnification provisions are most common in insurance policies, parties to any type of contract may agree on indemnification



arrangements. [Cases: Insurance 1001. C.J.S. *Insurance* § 2.] **2.** The amount for which someone or something is covered by such an agreement. — **insure**, *vb.*

"Insurance, or as it is sometimes called, assurance, is a contract by which one party for a consideration, which is usually paid in money either in one sum or at different times during the continuance of the risk, promises to make a certain payment of money upon the destruction or injury of something in which the other party has an interest. In fire insurance and in marine insurance the thing insured is property; in life or accident insurance it is the life or health of the person." 1 George J. Couch, *Couch on Insurance* § 1.2, at 4-5 (2d ed. 1984). "

20. Similarly, Eastern Book Company's *The Law Lexicon and Maxims* defines the word "insurance" as under:-

"Insurance – The act of providing against a possible loss, by entering into a contract with one who is willing to give assurance — that is, to bind himself to make good such loss should it occur. In this contract, the chances of benefit are equal to the insurer and the insured. The first actually pays a certain sum and the latter undertakes to pay a larger, if an accident should happen. The one renders his property secure; the other receives money with the probability that it is clear gain. The instrument by which the contract is made is called a policy; the stipulated consideration a premium. As to what is known as a coupon policy, i.e. a coupon cut out of a diary, etc., *Assce. Corpn. v. Robertson*, [1909] AC 404. Insurances generally provide either against risks at *sea* or losses by *fire* or *death* or *accident*; but losses by burglary or by default of clerks are also insured against. Insurances are effected sometimes by companies or societies and sometimes by individuals, the risk being in either case diffused amongst a number of persons. Companies formed for carrying on this business have generally a large subscribed but uncalled capital, so as to enable them to raise large sums to make good extraordinary losses. [Whart.]"

21. We also take note of the definition of "insurance" in P. Ramanatha Aiyar's *Advanced Law Lexicon*, 7th Edn., Vol. 2, and which reads as follows:-

"Insurance. A contract by which one party in consideration of a premium, engages to pay agreed sum on a certain event or indemnify another against a contingent loss.

A contract under which the insurer agrees to pay compensation to



the insured in the event of a specified occurrence, such as the loss of or damage to property. In return, the insured pays the insurer a premium, usually at fixed intervals, which the insurer invests to finance the business and to make a profit. The premium varies according to the insurer's estimate of the probability that the event insured against will actually occur (a calculation carried out by an actuary). Insurance of a person's life is called assurance.

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"Insurance is a contract by which the one party in consideration of a price (called the premium) paid to him adequate to the risk becomes security to the other that he shall not suffer loss, damage or prejudice by the happening of the perils specified to certain things which may be exposed to them." LAWRENCE J. in *Lucena v Graufurd*, (1806) 2 Bos & PNR 269 at p. 301 : 127 ER 42 HL."

22. As is manifest from the above, insurance is concerned with indemnifying against risk, loss or liability that may arise on account of a specified contingency. Insurance, as is explained by those lexicons, is concerned with an assurance that may be proffered to make good a loss that may be suffered. Tested on the aforesaid precepts, it is apparent that the liability taken over by the appellant was to pay interest on the lending facility that stood extended. That liability was continuous and indelibly connected with the debt owed. The mere fact that the export transactions were subject to a Hermes-Deckung guarantee provided to the lenders, would not detract from the liability being construed as interest per se or justify the same being recharacterized as insurance.

23. Viewed in light of the aforesaid, we find ourselves unable to sustain the view taken by the authorities that the repayments effected by the appellant would not fall within the scope of Paragraph 3(b) of Article 11.

24. Although it was also sought to be contended that HVB, which was acting as the agent of the consortium members, was merely the



beneficial owner and thus the appellant would have been liable to comply with the withholding tax obligations comprised in Section 195 of the Act, we find ourselves unable to sustain that submission bearing in mind the unequivocal command of Paragraph 5 of Article 11.

25. As is evident from a reading of the aforesaid Paragraph, the exemption provisions comprised in Paragraphs 1, 2 and 3 of Article 11 would have become inapplicable only if the beneficial owner (and if we were to proceed on the assumption that HVB was one) were carrying on business in the other Contracting State (India) in which the interest arose through a permanent establishment situate therein. It was never the case of the respondents that the HVB had a permanent establishment in India.

26. It is thus apparent that Article 11(3)(b) was clearly applicable and the interest would consequently be exempt from Indian tax liabilities.

27. Consequently, we allow the instant appeal and answer the questions framed for our consideration in favour of the appellant-assessee.

28. The appellant-assessee shall be entitled to consequential reliefs.

YASHWANT VARMA, J.

RAVINDER DUDEJA, J.

AUGUST 29, 2024/vp