BEFORE THE HIGH COURT OF KARNATAKA

INDIA

14th Day of February 2016

W. P. No. 100000 OF 2015

Name of the Applicant: Hassleton Investment Limited, Singapore

Name of the Respondents: Director of Income Tax (International Taxation, Bengaluru)

The Authority for Advance Ruling (Income-Tax), New Delhi

JUDGEMENT

1. The current Writ Petition No. 10000 of 2015, brought before this Honourable High Court of Karnataka under Article 226 of the Indian Constitution for the issuance of *Certiorarified Mandamus* by Hassleton Investments Limited (hereinafter called 'HIL') revolves around the scope and ambit of Section 115JB of the Income Tax Act, 1961.(hereinafter called 'I-T Act').
2. It would be necessary to recount some salient fact in order to appreciate the plethora of legal contentions urged.
    a) HIL is a tax resident and registered under the Companies Act of Singapore, incorporated on 1st April, 2009. HIL is engaged in security investments in India, wherefore; it was registered with the Securities and Exchange Board of India (hereinafter called 'SEBI') as Foreign Institutional Investor (hereinafter called 'FII') under the Regulations of 1995 and was later registered as Foreign Portfolio Investor (hereinafter called 'FPI') on 01st June, 2015. The

respondents in the present case are the Director of Income Tax (International Taxation), Bengaluru (hereinafter called 'DIT') and the Authority for Advanced Rulings (Income Tax), New Delhi (hereinafter called 'AAR').

b) HIL appointed Securities Advisors India Ltd. (hereinafter called 'SAIL') as its key advisor, registered in Bengaluru under the Companies Act, 1956. HIL was the biggest client of SAIL and paid huge commissions for the assistance provided by it. In the first week of January 2015, HIL made Long Term Capital Gains while disposing off their major investments made in Indian listed securities. On 27th January, 2015, HIL filed an application with the AAR to seek clarification regarding the taxability of the said income under the Indian Taxation regime. Consequent to which, AAR served notice to the DIT asking for a response on the Petitioner's tax position.

c) In response to the application filed, the DIT recommended that HIL will fall under the ambit of Section 115JB of the Act. Relying upon the contentions of DIT, AAR ruled against HIL and ordered them to pay Minimum Alternate Tax (hereinafter called 'MAT'). Hence, the present petition has arisen.

3. The High Court, while admitting the Writ Petition has considered the following issues:

a) Whether MAT provisions will be applicable to the petitioner being a 'foreign company' as per the definition under Income Tax Act, 1961 and the Companies Act, 2013.

b) Whether the petitioner had any type of Permanent Establishment / Place of Business / Business Connection either under Income Tax Act, Companies Act or relevant tax treaty.

c) Whether the petitioner is required to prepare financials as per Companies Act, 2013 or whether it is governed by SEBI Regulations.

d) Whether the Finance Act, 2015 amendment on imposition of MAT on foreign company is prospective or retrospective as argued by both parties.

e) Whether capital gains exemption as per India – Singapore tax treaty will be applicable to the petitioner and whether imposition of MAT will be violative of the tax treaty.

f) Whether the petitioner can cherry pick the provisions of Income Tax Act and tax treaty for the purpose of definition of PE under the Act and capital gains exemption under the tax treaty.

g) Whether 115JB is equally applicable to FIIs / FPIs and Foreign Direct Investors (FDI) and the scope and nature of functioning of FIIs / FPIs and FDIs to understand the investments into India.

4. We have carefully considered the arguments addressed by the learned counsel appearing for the parties and perused the records. The learned counsel for the petitioner has assailed the order passed by the AAR on number of grounds, while the counsel for the respondent has reiterated the submissions that they had made before the AAR and prayed for dismissal of such petition.

To appreciate the arguments made, it is necessary to understand the scope, purpose and applicability of Section 115JB on FIIs/FPIs and Foreign Direct Investors.

5. The considerable fact is that Section 115JB of the I-T Act was introduced by the Parliament through Finance Act 2000 w.e.f., 1.04.2001; the purpose behind this provision was to impose a minimum liability on ‘zero tax companies’, which despite having substantial book profits avoided tax liabilities by claiming several exemptions and deductions provided under the I- T Act. The two prerequisites for imposition of

MAT under Section 115JB is *firstly,* that there must be an income accruing or deemed to accrue in India and *secondly,* the enterprise must be able to prepare books of accounts in accordance with the Companies Act 1956.

On the issues regarding preparation of Books of Accounts in accordance with The Companies Act,2013

6. *ITD, Bengaluru justifiably relied on the rulings of AAR in The Timken Company case (2010) 326 ITR 193(AAR) and Praxair Pacific limited case (2010) 326 ITR 276 (AAR) in which AAR held that foreign companies having place of business in India will fall under the ambit of Section 115JB and will be required to pay Minimum Alternate Tax.*
7. We consider this submission is sound and should be accepted. It is an established principle of law that where the definition clause is preceded by the words "unless the context otherwise requires", normally the definition given in the section should be applied and given effect to but this normal rule may however be departed from if there be something in the context to show that definition should not be applied. (See Tata Consultancy Services v. State of Andhra Pradesh, AIR 2005 SC 371,see also Jagir Singh and Ors. v. State of Bihar and Anr., AIR 1976 SC 997.
8. The definition of the term 'company' under Section 2(17), The I-T Act, 1961, is also subjected to a restrictive clause "**unless the context otherwise requires**", which is to say that such definition has to be interpreted according to the circumstances.
9. The purpose of the term 'company' under 115JB is to be associated with requirement of preparation of books of accounts as per Schedule VI of Companies Act, 1956. Therefore, the context in the present case requires the definition of company to be borrowed from the Companies Act 1956.
10. It is already established that HIL is not a domestic company as it is incorporated under the laws of Singapore. The inclusion of global account of a company that does

not have a place of business in India will be contrary to the principle of territorial nexus which is the basic principle for chargeability of the I-T Act. Upon deliberation on the arguments put forth by the counsels, the court concludes that for a company to be subjected to the requirement of preparation of books of accounts under the Companies Act it must have a Place of Business in India.

11. The counsel for the respondent vehemently argued that SAIL acts as a place of business for the company HIL. However, the counsel for the petitioner argues the SAIL acts as an independent agent and is not under the control or supervision of HIL, therefore can never be considered as its place of business.

12. The ITAT, Delhi in Galileo International Inc. v. D.C.I.T., (2008) 19 S.O.T. 257 (Del) has laid down the tests for ascertaining whether or not an enterprise has a **place of business**, the test is a accumulation of three requirements, namely,

    a) Place of Business test;

    b) Right to Use test; and

    c) Business Activity test.

13. The fact that the petitioner does not qualifies the accumulated tests since there is no permanent or habitual location of business management, the office of SAIL was only used occasionally. Moreover, profit and business continuity are the most imperative base for the same which are not met in the present case. Thus, HIL does not have a Place of Business. (See Sudden Valley Inc. v. The Queen, [1976] 76 D.T.C. 6178 (F.C.T.D; CIT v. Vishakhapatnam Port Trust (1984) 38 CTR (A.P.) 1; Western Union Financial Inc. v. A.D.I.T (2007) 104 ITD 34 (Del)).

14. Section 2(42) read with Section 381 of the Companies Act, 2013 defines ‘foreign companies’ as companies having a place of business and are mandated to prepare books of accounts as per Schedule III, Companies Act, 2013.

15. Thus we are inclined to accept the contention of the petitioner that HIL does not have a place of business and hence is not subjected to the requirement of preparation of books of account under the Companies Act 2013 and are governed by SEBI (FPI) Regulations 2015.

On the issues of Capital Gains Exemption under Article 13 of the India-Singapore Tax Treaty

16. The subsequent point of determination is whether there is any income accruing to the petitioner in India. It is to be noted that the scope of 115JB is such that the total book profits of an enterprise is to be taken into assessment for computation of MAT under Section 115JB. For the applicability of the said provision, accrual of income in India is a pre-requisite as mandated by the legislation.
17. It is to be noted that the petitioner in the present case is covered under the India-Singapore Double Taxation Avoidance Agreement, thus, to determine whether there is any income accruing to the petitioner it must first be determined whether such income is exempted under the said Agreement or not.
18. We are in consonance with the contention made by the counsel for the petitioner that imposition of MAT by ITD will be violation of the India- Singapore tax treaty.
19. The fact that the petitioner in the present case is a resident company of Singapore registered under the relevant laws is undisputed. India-Singapore entered into a DTAA with the objective as specified in the preamble to be such –

    "Agreement for avoidance of double taxation and prevention of fiscal evasion with Singapore for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income has entered into force on 27th May, 1994.

20. The essential principle which is to be ruminated while interpreting an international treaty is that such treaties/agreements are contracted at a political level and have

diplomatic and severe consideration as their bases. David R. Davis in *Principles of International Double Taxation Relief, Pg.4 (London Sweet & Maxwell, 1985)*, says that the primary function of Double Taxation Avoidance Agreements should be interpreted in the background of facilitating economical relations between contracting parties and being a negotiation between two countries as to the right of taxability of income falling under the tax jurisdiction of both countries.

21. Taking into consideration, the objective and purpose of the said agreement, we can wisely conclude that imposition of any such tax that has been exempted specifically in the agreement would be a violation of the DTAA.

    However, the counsel for the respondents has argued that the exemption provided to the petitioner by virtue of the DTAA shall not be applicable since the petitioner has a permanent establishment in India.

    It is therefore significant to determine the presence of a permanent establishment in the present case for the ascertainment of the Income of the petitioner.

22. The counsel for the petitioner pleaded to take definition of Capital Gains from the Tax Treaty while borrowing the definition of Permanent Establishment from the Income Tax Act, 1961.

23. The said issue has been significantly dealt by the Apex Court in the case of Union of India v. Azadi Bachao Andolan (263 ITR 706 (SC)), wherein, the court enunciated the nuances of Section 90(2) of the Income Tax Act that provides an Assessee with the discretion of opting for provisions that are beneficial to him for the purpose of Assessment.

24. The counsel for the petitioner has vehemently argued that the definition under the Tax Treaty much not be applicable on them, however, the counsel for the respondent contended otherwise saying that since the petitioner is claiming capital gain

exemption according to the definition given in tax treaty, the same should be done for the definition of permanent establishment too. However, we have already established that Section 90(2) provides for beneficial opting of provisions by an assessee**.**

25. Regardless, for the definition of Permanent Establishment the petitioner cannot venture into the Income Tax Act, 1961. The definition provided in Section 92F (iiia) of the Income Tax Act is in relation to Arm's length transaction only. Thus, the well-established principle of *'expression unius est exclusion alterius'* must be applicable here which establishes that something that is expressly mentioned in one place but not in another must be taken to have been deliberately omitted by the legislature.
26. In our view, definition of Permanent Establishment can therefore only be taken from the Tax Treaty and hence we reject the contention of the petitioner of taking the definition of Permanent Establishment from I-T Act, 1961.
27. For the determination of the primary issue, as to whether any income is accruing to the petitioner in India, it is necessary to venture into the definition of Capital Gains in the Tax Treaty.
28. Article 13 of the India-Singapore DTAA provides for Capital Gain Exemption, Article 13(2) specifically provides that Capital Gains exemption over movable property will only be accrued to the resident country if there is no Permanent Establishment in the other contracting state. It is therefore essential to ascertain whether or not the petitioner has a permanent establishment in India.
29. The counsel for the respondent has fallaciously argued that SAIL is acting as an Agency PE of the petitioner in India and therefore they must not be given Capital Gains Exemption under the Tax Treaty and must rather be subjected to the Income Tax Act.

30. Article 5, clause 8 of the India Singapore DTAA provides the definition of Permanent Establishment. The primary tests for ascertaining Agency PE are the extent of dependency of the Agent on the foreign company and the acts beyond the ordinary course of business. To establish Agency PE there must be substantial dependency of the agent upon the foreign company.

31. The court taking into consideration the ruling given in the case of Western Union Financial Services Inc. v. Additional Director of Income Tax, (2007) 104 I.T.D. 34 (Del) where the Income Tax Department (Delhi) had enunciated that an agent of independent status having other clients does not constitute Permanent Establishment.

32. Thus, after taking into consideration the fact of this case, we reject the contention of the respondent and conclude that SAIL is acting as an independent agent and hence does not constitute Permanent Establishment.

33. Establishing the above view, we have reached the conclusion that HIL can avail the benefits of the Tax Treaty under Article 13 which provides for Capital Gains Exemption.

On the issue of Retrospective applicability of the Amendment vide Finance Act, 2015 to Section 115JB

34. One of the primary and substantial question of determination that has been put forth in this court is regarding the applicability of the Amendment vide the Finance Act, 2015 to Section 115JB of the Income Tax Act. The counsel for the petitioner has contested that the functioning of this amendment must be made retrospectively, whereby exempting all existing FIIs/FPIs from the purview of the MAT provisions. The counsel for the respondent argued vehemently against the said proposition of the petitioner's counsel, relying heavily upon the principle of ***lex prospicit non respicit*** meaning that the law should look forward and not backward.

35. It is our view that the doctrine of literal interpretation is subjected to certain exceptions. The Apex court, in a plethora of cases, has established that the doctrine of literal interpretation must not be employed when such literal interpretation would lead to injustice and would vitiate the purpose of the law in question. (B.Premanand v. Mohan Koikal, AIR 2011 SC 1925; S.Mehta v. State of Maharashtra, 2001 (8) S.C.C. 257; CIT v. Keshavchandra Mandal, AIR 1950 SC 265)

36. The Apex Court through a five judge bench has laid down the test to determine whether the amendment vide finance act must be applied retrospectively or not. The test laid down in this case is that if the amendment is clarificatory in nature which has to be examined in the light of the purpose of such amendment, if it is conferring some benefit rather than imposing a liability then it has to be treated retrospectively. (CIT v. Vatika Township (2015) 1 S.C.C. 1)

37. In the history of MAT regime, during all the past 19 years since the introduction of MAT in 1996, the authorities have never put up such liability upon FIIs/FPIs, instead such investors have been subjected to the beneficial tax scheme as provided under Section 115AD. Thus, we are of the opinion that it is imperative that the said amendment be given a constructive interpretation since the nature of the amendment is clarificatory in nature that is to say that by bringing such amendment the legislation has attempted to bring more clarity to an existing provision of law.

38. The amendment vide Finance Act 2015 is a clarification that is conferring a benefit upon the FIIs/FPIs in question; therefore, imposing a liability upon them would vitiate the purpose of such amendment and would lead to injustice. Hence, accepting the petitioners contention we conclude that the amendment in question has to be interpreted retrospectively so as to fulfil the intention of the legislature.

39. We would conclude as follows for the reasons stated above –

a) HIL does not have a permanent establishment in India.

b) HIL is not covered under the Companies Act and need not prepare Books of Accounts as per Schedule VI of the said Act.

c) HIL is not liable to pay Minimum Alternate Tax under Section 115JB.

d) The amendment vide the Finance Act, 2015 on applicability of Minimum Alternate Tax should have retrospective operation.

40. Accordingly, we declare this judgment on this, 14th day of February, 2015.