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DISPUTE RESOLUTION AND ARBITRATION

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DISPUTE RESOLUTION AND ARBITRATION UPDATE

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RECENT JUDGEMENTS

Union of India & Ors. v. R. Thiyagarajan

CIVIL APPEAL NO. 2229 OF 2020

Background facts

- Civil Appeal has been filed against order passed by Division Bench of High Court of Madras (**HC**) directing payment of deputation allowance to all personnel of National Disaster Response Force (**NDRF**) from date of inception of NDRF, which was constituted under Disaster Management Act, 2005, for purpose of specialized response to threatening disaster situations or disasters.
- Respondent, an employee of the Central Industrial Security Forces (**CISF**) since 1999, had been deputed to NDRF on April 18, 2008. Until September 11, 2009 i.e. date from when Disaster Management Rules (**Rules**) came into effect, Respondent drew his pay and allowances from CISF and post September 11, NDRF formed its own Battalions and control has since been vested with NDRF. Thereafter, Respondent drew his pay and allowances from NDRF.
- Tenure of Respondent with NDRF came to an end on October 07, 2011 and he was relieved of his duties in NDRF and repatriated to CISF. Subsequently, Respondent submitted a representation to Director General, NDRF requesting that he be granted 10% deputation allowance and 25% special allowance with effect from date of his deputation.
- A writ petition was filed before HC seeking payment of deputation allowance and special allowance based on his representation. Meanwhile, on January 14, 2013, Ministry of Home Affairs (MHA) issued a letter stating that deputation allowance be paid to personnel of various forces deputed with NDRF @5% if they are deputed in same station and @10% if deputed outside station, subject to certain conditions. Following orders of MHA, Director General, NDRF issued an order dated February 18, 2013 on same lines. However, said deputation allowance was made payable with effect from January 14, 2013.
- Simultaneously, Delhi High Court vide its judgment dated August 11, 2015 in *Brij Bhushan v. Union of India* (**Brij Bhushan**), held that petitioner would be entitled to deputation allowance for period he remained in service with NDRF.

- Subsequently, HC while allowing writ petition filed by Respondent, relied upon decision of Brij Bhushan and not only granted deputation allowance but also granted special allowance. Aggrieved by said decision, Union of India appealed before Division Bench of HC, which held that Respondent was only entitled to deputation allowance and not special allowance and that not only Respondent but all other personnel of NDRF drawn from other forces from January 19, 2006 up to January 13, 2013 would be entitled to a deputation allowance. Division Bench also directed Central Government to ensure that amount was paid within maximum period of six months.

Issue at hand

- Could High Court of Madras have passed an Order/direction under a writ which had a pan-India repercussion?

Findings of the Court

- Court held that up to September 10, 2009, Respondent could not be said to be on deputation since he was under control of CISF. However, when command and control of Battalions drawn from various forces was conferred to Director General, NDRF, Respondent who started drawing his pay from NDRF, would be deemed to be on deputation with NDRF.
- Further, Court was of view that HC exceeded its jurisdiction since it has territorial jurisdiction only over State(s) of which it is High Court. It was observed that HC had virtually usurped jurisdiction of other High Courts in country and granted relief to all similarly situated employees pan-India, a power only Supreme Court (**SC**) have benefit of exercising under Article 142 of Constitution of India.
- It was also stated by SC that HC may be justified in passing such an order when it only affects employees of State falling within its jurisdiction but, it could not have passed an order where an pan-India repercussion would be involved.

Our view

Though the law has been well settled on the jurisdiction of the High Courts, the Supreme Court has once again reiterated that the power to issue directions under writs having pan-India repercussion vests only with the Supreme Court. However, as matter of practice, the High Courts may pass such an order/direction under a writ when all similarly situated matters are tagged before one High Court for adjudication.

This judgment comes as a reminder to the various High Courts of their limitations on geographical jurisdictions. We may note here that the High Court derives its geographical limits/power to issue writ from Article 226 of the Constitution of India. Thus, on a combined reading of Clauses (1) and (2) of Article 226, the High Court may issue writs against a Government, person or authority if (a) its seat is within the High Court's jurisdiction and (b) the cause of action has arisen, wholly or in part, within the High Court's jurisdiction.

Rajasthan State Electricity Board, Jaipur v. DCIT (Assessment) & Anr

CA No. 8590 of 2010

Background facts

- Petitioner (**Assessee**) was entitled to claim 100% depreciation on the loss incurred as per his IT return filed on December 30,1991 for AY 1991-92. Through an amendment in 1991, depreciation value was lowered to 75%; however, the Assessee erroneously claimed 100% depreciation on written down value of assets instead of 75%.
- Assessee received a notice issued by Assessing Officer (**AO**) disallowing 25% of depreciation, restricting it to 75% and demanded additional tax. Aggrieved by the same, Assessee filed application for rectification of demand and a petition before the Commissioner of Income Tax (**CIT**) praying for demand of additional tax to be quashed. CIT dismissed the Petition against which Assessee filed a writ petition before Rajasthan High Court. The demand for additional tax was upheld. Being aggrieved by the same, Assessee filed a civil appeal before Supreme Court (**SC**), which was allowed.

Issues at hand

- Whether demand of additional tax under Section 143(1-A) was justified?
- Whether there should be a levy of additional tax under Section 143(1-A) in all cases where loss is reduced?
- Whether 100% depreciation as mentioned in return filed by the Assessee was a result of an attempt to evade tax lawfully payable by the Assessee?

Findings of the Court

- SC relied on *K.P. Varghese v. ITO*[1], in which it had upheld the constitutional validity of Section 143(1-A) and stated that the section can be invoked only in cases where it is found on facts that lesser amount stated in return filed by an assessee is result of an attempt to evade tax.
- SC examined the object and purpose of this Section and held that burden of proving that Assessee has attempted to evade tax is on Revenue, which may be discharged by establishing facts and circumstances from which a reasonable inference can be drawn that Assessee has attempted to evade tax lawfully payable by him.
- The Court also placed reliance on *CIT v. Sati Oil Udyog Ltd & Anr*.[2] where it was held that Section 143(1-A) cannot be applied mechanically and can only be invoked where real intent to evade tax is found. Based on above, it found that Assessee's claim of 100% depreciation was not with an intent to evade tax and thereby quashed the order of High Court.

Our view

Considering the fact that many businesses have faced difficulties whilst dealing with revenue matters due to their hyper-technical/mechanical approach, this is indeed a welcome judgment that will encourage tax authorities to give due consideration to facts and satisfy the ingredients of a provision, as per ,guidelines laid down by courts before prosecuting an assessee.

Banyan Tree Growth Capital L.L.C. v. (1) Axiom Cordages Ltd; (2) Responsive Industries Ltd; (3) Wellknown Business Ventures LLP

COMMERCIAL ARBITRATION PETITION NO. 476 OF 2019

Background facts

- Petitioner, Banyan Tree Growth Capital L.L.C. (**Banyan**), is a company incorporated under laws of Mauritius. Respondent number 1, Axiom Cordages Ltd (**Axiom**), and Respondent number 2, Responsive Industries Ltd (**Responsive**), are companies incorporated under laws of India. Respondent number 3, Wellknown Business Ventures LLP (**Wellknown**), is a limited liability partnership registered under laws of India.
- On September 12, 2008, Banyan, Axiom, Responsive and Wellknown entered into a share subscription agreement (**SSA**) under terms of which Banyan invested approximately USD 7.5 million in Axiom in form of equity shares (**Subscription Shares**) and convertible debentures. In order to provide for a timebound exit from Axiom, a Put Option deed (**Put Option**) and an Escrow Agreement (**Escrow**) were also entered into by all four parties on same date as SSA. Put Option and Escrow formed part of larger investment transaction that was consummated under SSA.
- SSA provided three options for Banyan's exit from Axiom. One of these options permitted Banyan to exercise its rights under Put Option by obligating the Promoters to purchase convertible debentures (and/or equity shares issued upon their conversion) and Subscription Shares. Under terms of Escrow, Wellknown agreed to keep equity shares it held in Responsive or its cash equivalent in an escrow account which acted as security – if Promoters failed to honour terms of Put Option, shares held in escrow account were to be sold and proceeds used to settle Put Option.
- After failed attempts to orchestrate Banyan's exit and a subsequent plan to merge Axiom with Responsive that did not fructify, the convertible debentures were converted into equity shares in Axiom (**Equity Shares**). Disagreements ensued when Banyan discovered that Wellknown had transferred shares held in escrow account to a new account and closed escrow and cash accounts unlawfully. Subsequently, Wellknown refused to reinstate shares previously held in escrow account on the ground that Escrow and Put Option were both unlawful under Indian law. High Court of Bombay was persuaded to pass an interim order directing the Promoters to maintain status quo with regard to the equity shares that Wellknown held in Responsive.
- Banyan subsequently served a notice on Responsive under Put Option requiring Responsive and Wellknown to buy Subscription Shares and Equity Shares (**Put Shares**). Banyan also communicated to Promoters fair market value of Put Shares, calculated using discounted cash flow method, as arrived at by a firm of chartered accountants. Promoters refused to purchase Put Shares on ground that Put Option was unlawful under Indian law.
- In Singapore-seated arbitration proceedings instituted by Banyan and conducted under rules of Singapore International Arbitration Centre, arbitral tribunal declared that Put Option was valid under Indian law and that Promoters were in breach of their obligations under it. It awarded damages of USD 11.14 million along with interest and costs and ordered Banyan to transfer Put Shares to Promoters upon receipt of payment from them (**Award**).

[1] (1981) 4 SCC 173
[2] (2015) 7 SCC 304

- In proceedings instituted by Banyan before High Court of Bombay (**Court**), Promoters and Axiom (collectively, **Respondents**) asserted that recognition and enforcement of the Award would be contrary to public policy of India because it would contravene fundamental policy of Indian law under Section 48(2) of Arbitration and Conciliation Act, 1996 (**Act**).
- The particulars of the Respondents' arguments were that Put Option was inadequately stamped and cannot, therefore, be relied upon. The Respondents also submitted that the Put Option was unlawful under Securities Contracts (Regulation Act), 1956 (**SCRA**) and Foreign Exchange Management Act, 1994 (**FEMA**) and secondary legislations promulgated under them and was, therefore, unenforceable.

Findings of the court

Stamp Duty

- The Court held that on merits the Put Option was, in fact, adequately stamped. In any event, the Respondents had always maintained that Put Option was adequately stamped and had not raised issue of inadequate stamping during arbitral proceedings. Furthermore, in proceedings under Section 48 of Act, the Court is precluded from reopening this issue.

SCRA

- The Court observed that purpose of SSA was for Banyan to invest significant sums of money so that Axiom was able to fund capacity expansion of its plants and granting of Put Option was consideration for Banyan's subscription of convertible debentures. Therefore, the transaction contemplated by Put Option was not one of speculation in securities, which would have been a legitimate reason to attract regulatory and penal measures under SCRA.
- Put Option was not a derivatives contract and did not attract SCRA and, therefore, could not have fallen foul of its requirements regarding type of settlement or being traded on regulated exchanges. In order to clear any lingering doubts, Court drew attention to subsequent notification issued by SEBI on October 3, 2013 under SCRA that exempted persons entering into shareholders' agreements for purchase of securities pursuant to an exercise of an option from requiring permission of SEBI – that date is significant because Banyan's purported exercise of its rights under Put Option that would have resulted in contract for purchase of securities occurred subsequently in 2015.

FEMA

- The Court reiterated that legislative regime under FEMA is concerned with regulation and management of India's foreign exchange. A process of approvals and permissions has been put in place to act as a gateway to cross-border remittances involving Indian entities. FEMA is not concerned with invalidating underlying transactions and violation of provisions of FEMA cannot render Put Option unlawful or Award unenforceable.
- The Put Option did not grant to Banyan an open-ended assured return in contravention of FEMA – the effect of SSA was that if fair market value of Put Shares represented a return that was less than return agreed in SSA, only fair market value will have been remitted overseas to Banyan with balance amount being paid into an Indian Rupee account as nominated by Banyan. In such event, prohibition in FEMA against payment to a person resident outside India of a sum greater than fair market value will not have been contravened. In any event, arbitral tribunal held that consideration payable to Banyan for Put Shares was less than their fair market value and therefore, the added complication of Promoters being required to make payment to Banyan overseas and in India did not arise.

Public policy

- With regard to Respondents' argument that enforcement of Award would be contrary to public policy of India, Court cited *Renusagar Power Co. Ltd. v. General Electric Co.* where Supreme Court of India held that "public policy of India" in context of Foreign Awards (Recommendation and Enforcement) Act, 1961 meant that "something more than violation of law of India" would be required if enforcement of a foreign award was to be refused.
- Court held that no part of test for determining whether enforcement of Award would be contrary to public policy of India was satisfied. Court declared that the Award was binding and enforceable as a decree of the Court.

Our view

The decision of court is laudable for its pro-arbitration stance, but it would seem that the court went about its task in a long-winded way.

While the Court's ability to reject speculative and opportunistic interpretation of statutory provisions is indeed welcome, proceedings were effectively reduced to a first appeal, which is a gross violation of tenets of proceedings for enforcement of foreign arbitration awards.

Halliburton Offshore Services Inc. v. Vedanta Ltd & Anr

O.M.P. (I) (COMM) & I.A. 3697/2020

Background facts

- Halliburton Offshore (**Petitioner**) and Vedanta Ltd & Anr (**Respondent**) entered into a contract for development of three oil and gas blocks. Various bank guarantees were furnished by the Petitioner to the Respondent as security. The Petitioner had requested for extension of time for completing the contract works by March 31, 2020, which Respondent claimed to have not accepted at any point during the subsistence of the contract.
- On March 18, 2020 and on March 25, 2020, petitioner invoked force majeure under contract due to ongoing global Coronavirus pandemic and consequent restriction on movement and travel in country. The Petitioner apprised that it was unable to continue performing contract works because its workers from overseas and various parts of country were restricted from traveling. By a letter dated March 31, 2020, the Respondent wrote to the Petitioner, refusing to accommodate the Petitioner's recourse to the force majeure clause under the contract and reserved its rights to terminate the contract and complete the balance work through a new contractor at the cost of the Petitioner.
- The Petitioner filed an application under Section 9 of the Arbitration and Conciliation Act, 1996 (**Act**) before the High Court of Delhi (**HC**) seeking interim protection in the form of restraint against the Respondent for invocation of the bank guarantees.

Issue at hand

- Whether encashment of the bank guarantees can be stayed?

Findings of the Court

- The Court made reference to the Respondent's letter dated March 31, 2020 and observed that the Respondent had acknowledged the Petitioner's endeavour to complete the contract works by March 31, 2020. Thereafter, the Court held that the Respondent is deemed to have extended the time for completion of the contract till March 31, 2020.
- The court then examined the narrow test of law with regard to restraining invocation of bank guarantees. The Court made reference to *Himadri Chemicals Industries Ltd. v. Coal Tar Refining Co.*[3] and *Standard Chartered Bank Ltd. v. Heavy Engineering Corporation*[4] and reiterated that the grounds under which invocation of bank guarantees can be stayed are the following only: (i) existence of fraud, of which the beneficiary of the bank guarantee may take advantage of; and (ii) existence of circumstances which would result in irretrievable harm or injustice to one of the parties in case bank guarantees or a letters of credit are encashed.
- The Court stated that the countrywide lockdown, which came into place on March 24, 2020, was, prima facie, in the nature of force majeure. It noted that the lockdown and government restrictions on movement and travel were unpredictable and held that special circumstances existed during the time which restricted the Petitioner from performing the activities under the contract after 24 March 2020 and if in these circumstances the Respondent is allowed to encash the bank guarantees, the Petitioner will suffer irretrievable injury.
- As a result, Court granted interim injunction in favour of Petitioner against invocation of bank guarantees until next date of hearing that was scheduled for May 11, 2020 (at the time of publishing this note, there is no publicly available information on the status of the case).

Our view

Court took a sympathetic approach in present instance. Perhaps extraordinary conditions brought about by the pandemic persuaded Court to invoke its equitable jurisdiction to conclude that irretrievable harm would result if at least a temporary injunction until the next date of hearing were not granted. It will be interesting to see whether a more thorough adjudication of the merits of the dispute changes the Court's mind.

[3] (2007) 8 SCC 110
[4] 2019 SCC Online SC 1638

Triloki Nath Singh v. Anirudh Singh (D) through LRs & Ors

2020 SCC ONLINE SC 444

Background facts

- Plaintiff purchased a disputed parcel of land by registered sale deed. However, Defendants started interfering in possession of property by relying on a compromise decree, which was filed in second appeal before High Court of Patna (**HC**).
- Plaintiff contended that compromise decree was obtained by fraud and misrepresentation, in addition to concealing facts from HC and submitted that since the sale deed was executed much prior to date of compromise, the compromise decree was, therefore, void.
- Defendants contested the maintainability of the suit under Section 34 of Specific Relief Act and Order 23 Rule 3A of Code of Civil Procedure, 1908, claiming that the plaintiff should have filed an application before HC which passed the compromise decree and, as such, have no right to seek injunction. They further claimed that any transfer of property was also barred by Section 52 of Transfer of Property Act.
- Plaintiff filed a civil suit seeking a declaration that compromise decree is illegal, inoperative and obtained by fraud and misrepresentation and also prayed for injunction against respondents restraining him from entering into peaceful possession of the suit property. The suit was dismissed in both first and second appeal before High Court, after which the Plaintiff approached SC for seeking relief.

Issue at hand

- Whether Plaintiff, being a third party, could challenge the compromise decree?

Findings of the Court

- SC relied on its earlier judgements in matters of *Pushpa Devi Bhagat (Dead) through LR Sadhna Rai (Smt) v. Raiinder Singh*[5] and *R. Rajanna v. S.R. Venkataswamu*[6] wherein it held that only remedy available to party challenging a compromise decree is to approach the court which recorded the compromise and establish that there was no compromise.
- In present case, sale deed was executed during pendency of first appeal in respect of partition suit on issue regarding right, title and interest in respect of land, which was subject matter of sale deed dated January 06, 1984 and was still inchoate and not finally decided.
- Apex Court held that compromise decree passed by High Court in second appeal would relate back to date of institution of suit between parties. As such Appellant cannot question compromise decree being not a party to compromise and, at best could file a civil suit against seller of property for protection of his right, title or interest devolved on basis of stated sale deed. The Apex Court held that in any event, even assuming it well within the rights of Appellant, any challenge to validity of compromise could lie only in High Court which had passed decree basis such compromise and not by way of a separate civil suit.

Our view

The Apex Court has reiterated the settled legal position of rights of a third party against a compromise decree while at the same time offering protection to such third party to protect its rights by way of an independent suit in respect of its rights flowing from a separate executed instrument. The possibility, however, of such third party being denied any relief contrary to the terms of a compromise or a decree based on such compromise is imminent, especially when such decree is passed by a higher court. This question has been left unanswered by the Apex Court and also goes against its own observation of avoidance of multiplicity of litigation, much less a litigation with an imminent result.

Quippo Construction Equipment Ltd v. Janardan Nirman Pvt Ltd

CIVIL APPEAL NO. 2378 OF 2020 (ARISING OUT OF SPECIAL LEAVE PETITION (C) NO. 11011 OF 2019)

Background facts

- The parties had entered into an agreement for supply of construction equipment. Out of four agreements that were executed, venue for holding arbitration under one agreement was New Delhi and under another was Kolkata. Dispute arose between the parties and Appellant invoked arbitration for proceedings to be conducted at New Delhi. Respondent denied claim of Appellant and did not take any steps to participate in Arbitration proceedings, following which the Arbitrator proceeded ahead with arbitration and passed an *ex-parte* order in favour of Appellant encompassing all four agreements.

[5] (2005) 5 SCC 566
[6] (2014) 15 SCC 471

- Respondent challenged *ex-parte* order before Alipore District Court which dismissed the same and held that only Courts at Delhi have jurisdiction to entertain the proceedings since New Delhi was the venue chosen as per the agreements.
- Respondent thereafter filed petition challenging said order before Calcutta High Court (**HC**), which allowed the same. Thereafter, Appellant filed Special Leave Petition before SC against the said order of HC.

Issue at hand

- Whether Respondent has waived his right to raise objections by not participating in the arbitration proceedings and letting the same conclude and culminate?

Findings of the Court

- SC held that 'place of arbitration' may have special significance in an International Commercial Arbitration, where this phrase may determine which curial law would apply. However, in the present case, the applicable substantive as well as curial law would remain the same.
- SC therefore allowed the appeal and restored order of Alipore Court holding that Respondent is precluded from raising any submission or objection as to venue of arbitration.

Our view

The view taken by Apex Court follows section 4 of Arbitration & Conciliation Act. Thus, Respondent in instant case who chose not to participate in arbitration proceedings and did not raise its objections at relevant time before arbitrator was deemed to have waived his right to raising such objections subsequently and was estopped by his own actions from doing so in appeal.

IFCI Ltd v. Lucknow Municipal Corporation

MISC. BENCH NO. - 4517 OF 2013 & MISC. BENCH NO. - 2397 OF 2013 (ALLAHABAD HC)

Background facts

- Lucknow Nagar Nigam (**LNN or Lessor**) leased a property to Uptron India Ltd (**Uptron or Lessee**) for a period of 30 years with two rights of renewal for a similar term of 30 years on each renewal on the same terms and conditions.
- Uptron, due to its financial needs, mortgaged the property with IFCI Ltd (**IFCI**) and took financial assistance. Upon committing default in payment of its dues of loan, IFCI proceeded under SARFAESI Act, 2002 for recovery of its outstanding dues from Uptron. During auction of said property, bid of M/s. Shalimar Corporation Ltd. was accepted and 25% of bid amount was deposited with IFCI.
- LNN terminated lease of the land that was leased out to Uptron on grounds of non-payment of rent. IFCI being aggrieved by action of termination of lease by LNN filed the writ petition.

Issues at hand

- Whether writ petition filed by LNN challenging auction proceedings initiated and carried out by IFCI Ltd is entertainable and maintainable before the Court or LNN should be relegated to avail remedy available under Section 17 of the Act of 2002?
- Whether determination of lease by alleged order/notice by LNN is just and proper?
- Whether auction proceedings in relation to the property under the provisions of the SARFAESI Act, 2002 are sustainable in the eyes of law?
- Whether mortgagee IFCI, for the purposes of recovery of dues, was empowered to sell property or was empowered to sell only lease hold rights available to Uptron under the lease deed?
- Whether, as per facts of case, a direction can be issued to lessor to renew the lease?
- Whether M/s. Shalimar is entitled for refund of 25% of bid amount with interest w.e.f. the date of passing of interim order dated May 27,2013?

Findings of the Court

- Issue 1 – It was held that writ petition filed by LNN challenging auction proceedings carried out by IFCI is maintainable.
- Issue 2 – The court held that determination of lease by LNN was as per terms laid down in the lease and was just and proper. Court rightly held that IFCI was liable to pay rent, as it had stepped into the shoes of Uptron Ltd. in terms of the section 108(j) of the Transfer of Property Act, 1882.
- Issue 3 – The court referred to the judgment in the case of *Rakesh Kumar Kaushal v. State of U.P. & Ors*[7], where sections 13, 14 and 17 of SARFAESI Act, 2002 were considered and it was held that writ petition is maintainable and also that responsibility of bank does not get diluted by merely inserting a clause "as is where is and as is what is" and further held that secured creditor is under a mandate to disclose every aspect of property to be auctioned under provisions of SARFAESI Act of 2002 and Rules, 2002. Therefore, in present case, the auction proceedings in relation to property carried out by IFCI are not sustainable.
- Issue 4 – The court held that lessee can only mortgage or sub-lease whole or any part of his interest in property and any transferee of such interest or part may again transfer it. It further provides that lessee shall not, by reason of such transfer, cease to be subject to any liabilities attaching to lease and, therefore, only lease hold rights could have been auctioned.
- Issue 5 – The court held that tenant was not in breach of terms of the lease and is entitled for renewal of lease. As per terms of lease deed, the right of renewal can be exercised during the term of lease and not after determination of lease. In the instant case, lease was terminated by LNN and till that date right of renewal was not exercised by lessee or any other person, who entered in shoes of lessee. Court held that no direction can be issued to the lessor to renew the lease.
- Issue 6 – The court held that M/s. Shalimar was entitled to refund of 25% of bid amount from IFCI with interest.

Union of India v. UAE Exchange Centre

CA No/9775/11

Background facts

- UAE Exchange Centre (**Respondent**) is a limited company incorporated in UAE and is engaged in offering, among others, remittance services for transferring amounts from UAE to various places in India. The Respondent set up its first liaison office in Cochin, in January, 1997 and thereafter, in other parts of India, in line with permission granted to it by RBI on September 24, 1996.
- The contract to remit such sums were entered between the Respondent and NRI remitter in the UAE and the funds were collected from the NRI remitter by the Respondent in UAE by charging one-time fee, post which the Respondent used to electronically remit funds either by telegraphic transfer through bank channels or through instruments/cheques issued by its liaison offices to beneficiaries in India.
- The Respondent sought in 2003[8] ruling of the Authority for Advance Rulings (Income Tax), (**AAR**) on the following question: 'Whether any income is accrued/deemed to be accrued in India from the activities carried out by the Company in India?'
- AAR, vide its ruling dated May 26, 2004, answered the question in affirmative and held that 'income shall be deemed to accrue in India from the activity carried out by the liaison offices in India, as per the provisions Sections 5 and 9 (1)(i) of Income Tax Act (**ITA**), as Respondent had a Permanent Establishment (**PE**) India.'
- The department issued four notices dated July 19, 2004 under Section 148 of ITA pertaining to AY 2000-04. The Respondent impugned the said order and challenged these notices before the Delhi High Court (**HC**) by way of a writ.[9] The HC vide its order dated quashed the notices and set aside the AAR ruling.
- The said order of the HC was challenged before Supreme Court (**SC**) in SLP.

[7] 2019 (1) ADJ 689

[8] AAR No. 608/2003

[9] Writ Petition No. 14869/2004

Issue at hand

- Whether the stated activities of the respondent would qualify the expression "of preparatory or auxiliary character"

Findings of the Court

- While dismissing appeal filed by Revenue, SC interpreted term PE as mentioned in Article 5 of India-UAE DTAA dated November 18, 1993. Court held that PE would normally be a fixed place of business through which the business of an enterprise is wholly or partly carried on, provided it passes the functional test regarding its activity in question and is out of contours of Article 5(3) of the DTAA. It further held that the stated activities of the liaison offices of the respondent in India were of preparatory or auxiliary character as per Article 5(3)(e) of the DTAA & therefore, it cannot be regarded as a PE within the sweep of Article 7 of DTAA
- The SC affirmed the view of HC & reliance placed upon the dictum in the case of E-Funds IT Solution Inc[10]. It held that the for taxing a PE, Revenue should travel beyond ITA provisions such as Section 5 r/w Section 9(1)(i), especially when there is a DTAA between India and Assessee's country, to establish that that all ingredients of the DTAAs are satisfied.
- The court adverted to its own judgment *of Morgan Stanley & Co Inc*[11] wherein it was held that in order to decide whether a PE stood constituted, one has to undertake a functional and factual analysis of each of the activities to be undertaken by an establishment.

Our view

Time and again we have seen the SC act as a guardian of the foreign investors and tax payers. The Court has affirmed the lower courts' view of interpreting the tax laws and the need to ascertain their applicability & inter-lay with DTAA, if any. The Revenue department should be mindful of directions & precedents set by Leonhardt Andra Und Partner, GmbH and Azadi Bachao Andolan & Anr , wherein courts have held that that where a DTAA exists, the provisions of DTAA will apply even if inconsistent with the provisions of ITA.

[10] (2018) 13 SCC 294
[11] (2007) 7 SCC 1

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