IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI E BENCH, MUMBAI

[Coram: Pramod Kumar AM and **Vijay Pal Rao JM]**

ITA No. 3941/Mum/2010
Assessment year: 2006-07

Additional Director of Income Tax
(International Taxation), Circle 2(1),Mumbai ……. ***Appellant***

Vs.

Star Cruise India Travel Services Pvt Ltd ……. ***Respondent***
[PAN : AAFCS4154H]

Appearances:
C G K Nair, *for the appellant*
Dr K Shivram, *for the respondent*

O R D E R

Per Pramod Kumar :

1. By way of this appeal, the Assessing Officer has challenged correctness of CIT(A)'s order dated 24th February 2010, in the matter of ascertainment of tax withholding liability under section 195 r.w.s. 201 of the Income Tax Act, 1961, for the assessment year 2006-07, on the following ground :

On the facts and in the circumstances of the case and in law, the learned CIT(A) erred in holding that tax is not deductible at source under section 195 of the Act, on payments made to Star Cruise Management Limited, Isle of Man, out of sale proceeds of cruise tickets booked by the assessee, and, therefore, consequential levy of tax and interest under section 201(1) and 201(1A) by the Assessing Officer was not justified, ignoring the fact:

i. **that the assessee has been appointed as an agent to provide sales and marketing services relating to cruises and holiday packages for Star Cruises and its appointment as General Sales Agent in India is mainly for the purpose of collecting money in India;**

ii. **that the entire sale proceeds received by the agents in this case were received on behalf of the SCML, and belonged to it – subject to the rights of the agents;**

iii. **that the Board circular no. 23 dated 23.07.1969 is not applicable in the assessee's case as it is withdrawn on 23.7.2009; and**

iv. **that the Assessing Officer was right in holding that the gross receipts received by the SCML as principal from agent is chargeable to tax under section 5(2) (a) of the Act.**

2. The short issue that we are required to adjudicate, set out in somewhat argumentative grounds of appeal set out above, is whether or not the Star Cruise Management Limited ('**SCML**' or '**Star Isle of Man**' – in short) was liable to income tax in India in respect of the payments received it by through this assessee ('**SCITLS**' or '**Star India**' – in short). There is no dispute that in case Star Isle of Man, had any such income tax liabilities, Star India had a corresponding vicarious tax withholding liability from the payments so made to Star Isle of Man. The core issue thus really is whether or not Star Isle of Man had, on the facts of this case, any income tax liability in India.

3. The issue in appeal lies in a rather narrow compass of material facts. Star Isle of Man is a company registered in Isle of Man and is providing sales, marketing, and promotional services for the cruise vessels owned, managed, operated or chartered through the Star Cruise Group of Companies. Star Isle of Man has appointed Star India as its canvasser in India mainly to canvass business for its operations and for marketing its cruise packages and shore excursions. As a part of this arrangement, and vide agreement dated 1st March 2005, Star India's obligations and duties are as follows:

> **i. To act as Canvasser in India for Cruise Packages, shore excursions promoted by SCML. In respect of vessels owned, chartered, managed and/or operated by Star Cruise Group of Companies from time to time.**
>
> **ii. To and remit monies received from PSAs for cruse packages, shore excursions promoted by SCML in India.**
>
> **iii. To keep SCML advised on all relevant laws and regulations and operating criteria relating to the sale of tickets with particular reference to consumer and contract legislation.**
>
> **iv. To treat as confidential all books, documents and information received from SCML and to return the same upon demand; and**
>
> **v. To keep and render to SCML fair and accurate accounts of any dealings or of all monies received by SCITS from PSAs in relations to sale, booking, confirmation for and on behalf of SCML and to pay over to SCML all monies so received from PSAs without any deductions except as may be agreed upon or authorized between SCML and SCITS.**

4. In consideration of services so rendered, the Star Isle of Man was to pay 3% of net cruise charges, remitted by the Star India, as retainer fees. The

other obligations of Star Isle of Man, as set out in the canvasser agreement, are as follows:

3.1 SCML shall provide and supply SCITS with promotional information and details of the program and itineraries in respect of the cruise vessels.

3.2 SCML shall provide and supply SCITS with all information in relation to customs, immigration and quarantine regulations in the countries where the vessels operate.

3.3 SCML shall pay a prescribed retainer fee to SCITS in accordance with Clause 4 to this agreement.

3.4 SCML shall keep SCITS informed of the rates in force and the terms and conditions of various cruise packages from time to time which SCITS is not entitled to change.

3.5 SCML shall issue the booking confirmation/statement to PSAs only upon full receipt of the monies collected on behalf.

5. On these facts, the stand of the Assessing Officer has been that Star Isle of Man is liable to be taxed in India, in respect of the cruise passage money so received from India through Star India, mainly on the ground that Star Isle of Man had a business connection in India, which is sufficient to invoke tax liability of a non resident in India – in view of the provisions of Section 9(1)(i) read with Section 5(2)(i) of the Indian Income Tax Act, 1961. The Assessing Officer also relied upon Hon'ble Supreme Court's judgments in the cases of CIT Vs R D Aggarwal & Co (56 ITR 20) and Anglo French Textile Co. Ltd Vs CIT (23 ITR 101) to come to the conclusion that the essential features of 'business connection', for the purposes of application of Section 9(1)(i) are as follows:

- **a real and intimate relation must between the trading activities by a non-resident carried on outside India and the activities within India.**

- **the relation contribution directly or indirectly to the earning of income by the non-resident in his business;**

- **a course of dealing or continuity of relationship and not a mere isolated or stay nexus between the business of the non-resident India and the activity in India, would furnish a strong indication of business connection.**

6. The Assessing Officer, based on this analysis of legal position as also taking into account the fact that **"the clients for the cruise make payment of cruise charges in India"**, was of the view that "**there exists a business connection in India, of the cruise activity of the payee** *(i.e. Star Isle of Man)* **which may be taking place outside India**". In effect, he was of the opinion that the income on account of sale of passage is deemed to accrue or arise in India, by the virtue of Star Isle of Man's business connection in India. Having thus held the taxability of Star Isle of Man's income on sale of cruise passage in India, the Assessing Officer proceeded to determine, based on certain assumptions which we need not deal with at this stage, the quantum of income taxable in India at 5% of the net cruise charges. Aggrieved by the stand so taken by the Assessing Officer, assessee carried the matter in appeal before the CIT(A). Learned CIT(A) held that **" in the present cases, services rendered by the assessee are general in nature and that cannot be interpreted to give colour of business connections as contemplated under section 9(1)(i) of the Act"**. Accordingly, it was concluded that Star Isle of Man had no tax liability in India, and, therefore, the assessee could not be faulted for not deducting tax at source from cruise passage remittances made to Star Isle of Man. The impugned tax liability was thus quashed. The Assessing Officer is not satisfied by the relief so granted by the Commissioner (Appeals) and is in appeal before us.

7. We have heard the rival contentions, perused the material on record and duly considered factual matrix of the case as also the applicable legal position.

8. Let us first look at the scheme of taxability of non-resident taxpayers under the Indian Income Tax Act, 1961, so far as relevant to issue in appeal before us. The source rule of taxation, which typically originates in domestic tax law, is based on the principle that an income earned in a tax jurisdiction, irrespective of the residential status of the person earning the said income, is liable to be taxed in the tax jurisdiction where the income is earned. Therefore, a tax object, i.e. the income which is to be taxed, as a rule attracts taxability in the source jurisdiction. On the face of it, the application of source rule in the Indian Income Tax Act, however, seems to be going little beyond this universally accepted international tax norm. The source rule embedded in our domestic tax legislation does not only cover any income of a person, de hors his residential status, which accrues or arises in India, but also such an income which is *deemed to* (emphasis supplied by us) accrue and arise in India. Section 5 (2) provides that subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which is (a) received or is deemed to be received in India in such year by or on behalf of such person; or (b) accrues or arises or is deemed to accrue or arise to him in India during such year. Section 9, which sets out the scope of expression 'income deemed to accrue or arise in India', inter alia states "all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India" will be deemed to accrue or arise in India. In effect thus, it would seem that as long as an income has 'business

connection' in India, no matter in which part of the world it accrues or arises, it can still be charged to tax in India.

9. The taxability of the Star Isle of Man in India must, therefore, depend on whether or not Star Isle of Man could be said to have a business connection in India, within meanings assigned to that expression under Section 9(1)(i) of the Indian Income Tax Act, 1961, and, if so, to what extent income earned by Star Isle of Man could be said to be attributed to such business connection in India.

10. Section 9(1)(i), as it stood at the relevant point of time, is as follows:

Section 9: INCOME DEEMED TO ACCRUE OR ARISE IN INDIA

(1) The following incomes shall be deemed to accrue or arise in India:

(i) All income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India;

Explanation 1: For the purposes of this clause

(a) In the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India;

(b) In the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from

operations which are confined to the purchase of goods in India for the purpose of export;

(c) In the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India;

(d) In the case of a non-resident, being

(1) An individual who is not a citizen of India; or

(2) A firm which does not have any partner who is a citizen of India or who is resident in India; or

(3) A company which does not have any shareholder who is a citizen of India or who is resident in India, no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations which are confined to the shooting of any cinematograph film in India;

Explanation 2 : For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident unless his activities are limited to the purchase of goods or merchandise for the non-resident; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

Provided that such business connection shall not include any business activity carried out through a broker, general

commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business

Explanation 3 : Where a business is carried on in India through a person referred to in clause (a) or clause (b) or clause (c) of Explanation 2, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India.

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident unless his activities are limited to the purchase of goods or merchandise for the non-resident; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business :

11. A plain reading of the above statutory provisions makes it clear that any income directly or indirectly accruing or arising to a non-resident, through or from any 'business connection' in India, is *in principle* taxable in India. Even as the legal provision throws some light on what will, and what will not, constitute business connection, the precise connotations and scope of 'business connection' remains to be neatly defined. However, one

important principle which is clearly discernable from the statutory provision is that even when there is a business connection, by way of an agent or otherwise, the income which can be subjected to tax in India can never exceed the income attributable to operations carried out in India – by the non-resident or by the agent. Clause (a) of Explanation 1 to Section 9(1)(i) makes it clear that in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India. While Explanation 2 sets out the situations in which mere existence of an agent of the non-resident can be treated as business connection, Explanation 3 clarifies that in such situations, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India. In other words, while a business in which some part of operations are not carried out in India, taxability under section 9(1)(i) r.w.s. 5(2)(b) can not exceed income reasonably attributable to operations carried out in India, in the case of an agent, dependent or independent, taxability in India cannot exceed the income attributable to operations carried out in India. Whatever be the operations that an agent carries out for the non resident, he is compensated for the same under the agreement under which the said operations are carried out. Accordingly, in the case of business connection by the virtue of a sales agent, by whatever name called, non-resident's income deemed to accrue or arise in India can only be such income as is attributable to the operations so carried out by the agent. One way of looking at this situation is this. What can be logically deduced from these discussions is that in a case in which agent of the non-resident, which constitutes the business connection, has already been compensated for the services rendered by the agent, or, to put it differently, operations carried out for the non- resident in India, and it is not even the case of the Revenue that agent has not been paid arms-length or fair remuneration for the services so rendered, or operations so carried out in India, there cannot be

any further income of the non- resident which can be brought to tax under section 9(1)(i) r.w.s. 5(2)(b). Viewed thus, whether a sales agent, by whatever name called, constitutes a business connection or not is a wholly academic question – unless, of course, the very fact of such agent having been compensated fairly or at an arm's length for the work done for the non-resident is under challenge. A non-resident's tax liability under section 9 (1)(i) r.w.s. 5(2)(b) cannot come into play in a situation in which a sales agency- dependent or independent, which constitutes his 'business connection' in India, is paid a fair and arms-length remuneration for the services rendered by him, or operations carried out by him. What is perceived as Star Isle of Man's business connection in India is Star India, but given this situation it is wholly immaterial as to whether or not Star India indeed constitutes Star Isle of Man's business connection in India. Viewed from this perspective, the very foundation of the case made out by the Assessing Officer is thus devoid of legally sustainable basis, and the CIT(A) was quite justified in holding that no taxability can be imposed on the Star Isle of Man by the virtue of Section 9(1)(i) r.w.s. 5(2)(b). However, give the factual matrix of this case in which the matter is already covered by Hon'ble High Court's judgment in favour of the assessee, it is not really necessary to give a judicial adjudication on this school of thought. That must be left to be decided in a fit case. We thus make it clear that the above observations, which are somewhat academic in the above context, should not be treated as of precedence value. In the present case, the principal tax liability itself is quashed by a coordinate bench of this Tribunal.. As Star India's tax withholding liability is only a vicarious liability under section 195, once we come to the conclusion that Star Isle of Man did not have any principal tax liability in India, the impugned vicarious tax withholding liability of Star India must also be held to be not good in law. The CIT(A) was quite justified in deleting the same.

12. In the light of the above discussions, what appears to be *prima facie* an extension of the classical source rule of taxation in the scheme of the Income Tax Act, is in fact confined to the *simpliciter* taxability of an income earned in a tax jurisdiction, irrespective of the residential status of the person earning the said income, in the tax jurisdiction where the income is earned. While the main provision of the deeming fiction seems to be taking a rather aggressive view of the source rule, Explanations to the deeming fiction considerably narrow down the scope of the same. It is important to note that even this deeming provision restricts taxability of an income of the non-resident to the extent of income attributable to the operations carried out in the source jurisdiction, and that is quite in harmony with the first principles of source rule of taxation which has been embedded in the scheme of the Indian Income Tax Act as well. As a matter of fact, the provisions of Section 9(1)(i), as they stand now, are somewhat overlapping in effect inasmuch as these provisions cover only such income of the non resident as is attributable to operations carried out, by the non resident or his agent, in India, which may anyway be taxable under section 5(2)(b) as income accruing or arising in India. In other words, section 9(1)(i) does not appear to be anything more than clarificatory about the scope of first limb of Section 5(2)(b). The Direct Taxes Bill 2011 makes this overlapping effect even more glaring by providing, under section 314(40), that a business connection will include permanent establishment, and by setting out, under section 314(183), a rather exhaustive definition of 'permanent establishment' as a fixed place of business through which business of the non resident is wholly or partly carried out. When a non resident has a place of business, through which his business is wholly or partly carried out, the income of business so carried out has to be treated as 'accruing or arising' in India, and its taxability is not to depend upon a deeming fiction as 'business connection' envisages. The deeming fiction of 'business connection', in this view of the matter, does not really enlarge the scope of non resident's taxability in India,

but ends up substituting for, in a limited and somewhat ambiguous way though, the PE profit allocation rules under the domestic law.

13. While dealing with the concept of business connection under the legal position as it stands now, it is useful to also take note of the concept of 'business connection' as set out in the Income Tax Act 1922 and in the context of which several landmark judicial precedents, including in the cases of R D Aggarwal & Co. *(supra)* and Anglo French Textile Co. Ltd *(supra)* which have been relied upon by the Assessing Officer as well, were delivered.

14. Section 42(1) of the 1922 Act, in so far as it material in this context, *inter alia* provided that " all incomes, profits and gains accruing or arising, whether directly or indirectly, through or from any taxable territories *(i.e. territories under direct control of British India and excluding princely states)* shall be deemed to be income accruing or arising within the taxable territories…". This provision existed at a time when a part of India was under direct British rule in which Indian Income Tax Act had application and which were termed as 'taxable territories' and a part of India was under princely states to which the provisions of Indian Income Tax Act did not extend. In many cases, the *situs* of business was intermingled in the sense that some activities of a business were carried out in the taxable territories and some operations of the same business were carried outside taxable territories. It was in this backdrop that the legislation saw an extended source rule, arguably typical of colonial approach to extend its area of jurisdiction, which laid down that as long as there is a business connection in the taxable territories, the income of a person living outside taxable territories was also subject to taxation in British India. Once this provision was attracted, Rule 33 provided the method of computation of income deemed to accrue or arise in India, which ranged from "(a) a percentage of

turnover considered reasonable; (b) a proportion of the total profits (computed according to the provisions of the Indian IT Act) of the business of the assessee equal to the proportion which the receipts accruing or arising bear to the total receipts of the business; and (c) in such other manner as the ITO may deem suitable" *[see Netherlands Steam Navigation Co Ltd Vs CIT 74 ITR 72 SC].* These legal provisions were so judicially interpreted that "a company resident outside British India, which received goods from branches within British India, was assessable to Indian Income Tax in respect of sale of those goods outside British India". Taking note of these results, , Chief Justice Beaumont, with dignified restraint which was hallmark of judicial conduct in the good old days anyway, observed thus:

> **"…These decisions show that in the case of a non-resident, income which neither accrues or arises nor is received, within British India, may be liable to tax under the combined operation of Ss. 3,4, and 42; that is to say, a non- resident may be liable to tax in respect of sources of income, which would not be liable to tax in the case of a resident. The proposition is no doubt a somewhat startling one, but it is desirable that decisions of Courts in India under the Income Tax Act should be uniform as far as practicable, and I think we ought to follow these two cases without pausing to inquire whether we should ourselves have arrived at the same conclusion…"**
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> CIT Vs. National Mutual Life Association of Australasia
> (1 ITR 350)

15. It is thus clear that under the scheme of the domestic law, as it then stood; a mere business connection was enough to attract taxability of a business subject, i.e. business itself. The quantum of taxability was then determined on the basis of the provisions of the domestic law i.e. percentage of turnover, proportion of profits or such other residual method as the

Assessing Officer may adopt. These apparently harsh provisions resulted in situations, as was noted by Hon'ble Bombay High Court in the observations extracted above, that what was not even taxable in the hands of a resident, ended up being taxable when the same activity was carried out by a non-resident. Contrast this with the present scheme of law, which refers to business connection but expressly restricts the taxability to business object, i.e. business activity carried out in India, and restricts the same only to such operations as are performed in India. Therefore, when business activity is not carried out in India, there cannot be any taxability in India at all. These two set of provisions, i.e. in the Indian Income Tax Act 1922 and in the Income Tax Act 1961, are in a way different in scope and character and what has been held in the context of the former will not necessarily hold good in the context of the latter. Having said that, we may add that in the later cases, most notably in R D Aggarwal's case (supra), Hon'ble Supreme Court has held restricted application of taxability as a result of 'business connection', but we will deal with that aspect of the matter a little later.

16. In Anglo French Textile Co. Ltd's case *(supra),* for example, Hon'ble Surpeme Court were *in seisin* of a situation in which entire sourcing of raw material was done from British India, while manufacturing activity was carried out in French India (i.e. Pondicherry) and also sales was entirely outside British India. It was in this context that Their Lordships, *inter alia*, observed that the assessee had a business connection in India by the virtue of having sourcing operations in India, and, accordingly, income in respect of the same in deemed to accrue or arise in British India. Souring of raw material is an integral part of the business activity, but then if these facts are to be examined on the touchstone of legal position as it stands now, in view of the provisions of Explanation 1(b) to Section 9(1)(i) which provides that "**no income shall be deemed to accrue or arise in India to him through**

or from operations which are confined to the purchase of goods in India for the purpose of export", merely because raw material is purchased from India and exported outside India for processing, taxability can not arise. The legal provisions are thus not in *pari materia* vis-à-vis the legal provisions as they stood at the relevant point of time. When legal provisions are not in *pari materia*, the judicial precedent ceases to be relevant in the present context.

17. We must at this stage briefly deal with a very illuminating judgment of Hon'ble Supreme Court which deserves to be noted as much for its binding nature as much for a very erudite and pragmatic analysis of the concept of 'business connection' in the light of commercial realities. In this judgment, i.e. R D Aggarwal's case *(supra)*, Hon'ble Supreme Court had an occasion to deal with a situation in which the assessee was carrying on the business as commission agents for two non-resident exporters of worsted woollen yarn. The question which came up for consideration of Hon'ble Supreme Court was whether the non-resident exporters could be said to have business connection in India, on account of their sale agency arrangements with the Indian concern, and, whether, on that basis, a part of income of the non-resident exporters could be brought to tax in India. Their Lordships took note of the fact that the assessee was not an agent of the non-resident inasmuch as assessee merely communicates the orders canvassed by them to the non-residents for acceptance, and final decision to accept or not to accept the order rests with the principals. Their Lordships noted that that "the only question that falls to be determined in these appeals is whether there was, in two cases between the non-residents and the assessee, such a relation as may be called 'business connection' in the taxable territories" and proceeded to observe that "if the answer to this question be in affirmative, the assessee would, as statutory agent, be chargeable to tax on behalf of the non-resident companies, on profits and gains reasonably attributable to

those parts of operations which were carried out in India". It was in this backdrop that Their Lordships, *inter alia*, observed as follows:

> **12. Turning to the facts of the present case, as found by the Revenue authorities, contracts for the sale of goods took place outside the taxable territories, price was received by the non-residents outside the taxable territories, and delivery was also given outside the taxable territories. No operation such as procuring raw materials, manufacture of finished goods, sale of goods or delivery of goods against price took place within the taxable territories : the assessee merely procured orders from merchants in Amritsar for purchase of goods from the non-resident companies. The orders were offers which the assessees had no authority to accept on behalf of the non-residents. Some commercial activity was undoubtedly carried on by the assessees in the matter of procuring orders which resulted in contracts for sale by the non-residents of goods to merchants at Amritsar. But on this account no business connection of the assessees with the non-residents within the taxable territories resulted. The activity of the assessees in procuring orders was not as agents of the non-residents in the matter of sale of goods manufactured by the latter, nor of procuring raw materials in the taxable territories for their manufacturing process. Their activities led to the making of offers by merchants in the taxable territories to purchase goods manufactured by the non-residents which the latter were not obliged to accept. The expression "business connection" postulates a real and intimate relation between trading activity carried on outside the taxable territories and trading activity within the territories, the relation between the**

two contributing to the earning of income by the non-resident in his trading activity. In this case was such a relation is absent.

18. In essence thus, Their Lordships have held that the expression 'business connection' does not cover, in its scope, mere canvassing for business by an agent in India as is the situation that we are *in seisin* of in this case. Their Lordships also observed that the expression 'business connection' **postulates a real and intimate relation between trading activity carried on outside the taxable territories and trading activity within the territories, the relation between the two contributing to the earning of income by the non-resident in his trading activity"** which suggested that the business operations carried out outside taxable territories and inside taxable territories must have such a relationship as to contribute to business operations as a whole. It suggested greater nexus of the core business operations. Considering that this decision, though delivered in 1964 i.e. after Indian Income Tax Act 1961 came into effect, was dealing with the provisions in Indian Income Tax Act, 1922, it marked quite a paradigm shift in judicial perceptions about the concept of business connection. As a matter of fact, as we have noted above, this is a decision in which Hon'ble Supreme Court has in a way indicated a greater nexus of operation in taxable territories with core operations of the business in order that the non-resident can be said to have business connection in taxable territories. Viewed thus, this decision, if anything, supports the case of the assessee. As we make these observations, we are alive to the fact that, as held by Hon'ble Calcutta High Court, in the case of Biyani & Sons Vs CIT (120 ITR 887), it is appreciation of agreement as a whole which is decisive of the nature of relationship between Indian associate and the non-resident, and in effect whether or not such relationship constitutes 'business connection' but

then Revenue has not even questioned bonafides of nomenclature of the agreement. .

19. The approach of the Assessing Officer finds support from an interesting quarter in academics, which in turn relies upon a ruling given by the learned Authority for Advance Ruling. Prof Michael Lang, a well-known contemporary commentator on international taxation and renowned international tax academician, has made following interesting observations, in the context of Section 9(1)(i), in his book 'Introduction to the Law of Double Taxation Conventions' (an IBFD publication by Linde, Austria; ISBN 978-90-8722-082-2):

> **In international law practice, there are no significant limits on the tax sovereignty of states. In designing the domestic personal tax law, the national legislator can even tax situations when, for example, only a "*genuine link*" exists. It is only when neither the person nor the transaction has any connection with the taxing state that tax cannot be levied**.

> Example: *According to the Indian legal tax system, tax is levied when a "genuine link" exists. Pursuant to Se.9(1)(i) of the Income tax At, tax is levied on all income earned outside India which accrues, whether directly or indirectly, through or from any business connection in India. This principle formed the basis for the opinion of the Indian Authority for Advance Rulings (AAR) that a commission paid to a non-resident agent may be taxable in India even if the services are rendered outside India. Those services consisted of pursuing and soliciting the participation of foreign concerns, undertakings and government departments in the International Food and Wine Show (IFOWS) in India. Although the activity of the agent was carried on abroad, the AAR observed that the agent's right to receive commissions arose in India the when the foreign concerns, undertakings and government departments participated in the IFOWS. Therefore, the AAR considered*

that the agent's income accrued from a business connection in India (cf. IN. AAR 3July, 2006, Rajiv Malhotra, AAR/671/2005)

20. However, the observations so made by Prof Lang, and the ruling rendered by Authority for Advance Ruling in the case of Rajiv Malhotra (284 ITR 564), did not have the benefit of examining the impact of Explanation 1 (a) to Section 9(1)(i) of the Act. As a matter of fact, in Rajiv Malhotra's case *(supra),* the Authority for Advance Ruling does observe that "**the facts that the agent renders services abroad in the form of pursuing and soliciting the participants and that the commission is remitted to him abroad are wholly irrelevant for the purpose of determining the *situs* of his income**" but then this observation overlooks the fact that in terms of Explanation 1(a) to Section 9(1)(i), "in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India" but then since no part of the operations was carried out in India, no part of assessee's income could have been thus taxable in India. It would thus seem to us that when no business operations are carried out in India, even if a non resident has a business connection in India, no part of income of such business can be deemed to have accrued or arisen in India. The views expressed by the learned Authority for Advance Ruling, which do not fetter our independent opinion anyway in view of its limited binding force under section 245 S of the Act, do not impress us, and we decline to be guided by the same. Revenue thus derives no support from these observations either. In view of these discussions, and bearing in mind entirety of the case, we uphold the relief granted by the learned Commissioner (Appeals) and decline to interfere in the matter. This conclusion is also in harmony with the conclusions arrived at by a coordinate bench in assessee's own case for the

assessment years 2002-03 to 2005-06, reported in 134 TTJ at page 204 as DDIT Vs Star Cruise India Travel Services Pvt Ltd and *vice versa*.

21. In the result, the appeal is dismissed. Pronounced in the open court today on 22nd day of July, 2011.

Sd/xx
(Vijay Pal Rao)
Judicial Member

Sd/xx
(Pramod Kumar)
Accountant Member

*Mumbai; **22nd** day of **July** , **2011**.*

Copy forwarded to :

1. *The appellant*
2. *The respondent*
3. *Director of Income Tax (International Taxation) , Mumbai*
4. *Commissioner (Appeals) II , Mumbai*
5. *Departmental Representative, E bench, Mumbai*
6. *Guard File*

True Copy

By Order etc.

Assistant Registrar
Income Tax Appellate Tribunal
Mumbai benches, Mumbai