IN THE INCOME TAX APPELLATE TRIBUNAL
"L" Bench, Mumbai

Before Shri R.S. Padvekar, Judicial Member
and Shri B. Ramakotaiah, Accountant Member

ITA No. 645/Mum/2007
ITA No. 2306/Mum/2007

ADIT (International Taxation)-3(1) Scindia House, Room No. 132 2st Floor, N.M. Road Mumbai 400051	Vs.	ICICI Bank Ltd. Laxmi Commercial Bldg. 2nd Floor, C-Wing, B.K.C. Mumbai 400051 PAN - AAACI 1195 H
Appellant		**Respondent**

Appellant by: Smt. Malati Shridharan
Respondent by: Smt. Arati Vissanji

Date of Hearing: 06.09.2011
Date of Pronouncement: 16.09.2011

O R D E R

Per B. Ramakotaiah, A.M.

These two appeals are by the Revenue against the orders of the CIT(A) XXXIII, Mumbai dated 18.10.2006 and 13.12.2006 respectively on the issue of levy of interest and tax liability under sections 201(1) and 201(1A) of the I.T. Act.

2. Briefly stated, respondent bank (hereinafter referred as 'Bank') is a banking company. During A.Y. 2005-06 Bank made remittance to foreign nationals based on CA certificates and undertakings in accordance with RBI Circular No. FEX/MUMBAI/EDP.1/89/14011/Msc./2004-05 dated 07.12. 2004. These 11 CA certificates were forwarded to the A.O. vide their letter dated 14.06.2005 and another 12 CA certificates vide their letter dated 19.05.2005 and 6 CA certificates vide letter dated 15.06.2005. These 29 certificates were examined by the A.O. and an order under sections 201(1) & 201(1A) was passed determining the total tax liability under section 201(1) at ₹94,02,048/- and under section 201(1A) at ₹9,25,437/-.

3. The Bank also forwarded another 43 CA certificates vide their letter dated 19.05.2005, 5 certificates vide letter dated 26.04.2005, 84 certificates vide letter dated 23.03.2005 and 90 certificates vide letter dated 25.04.2005. Against these certificates the A.O. raised a demand under section 201(1) at ₹2,40,71,073/- and under section 201(1A) at ₹23,69,899/-. These two separate orders passed by the A.O. 28th March 2007 and 12th January 2006 were subject matter of appeal before the CIT(A) and the CIT(A) vide the above dated orders deleted the tax and interest levied under section 201(1) and 201(1A). Therefore, the Revenue is aggrieved and raised the following common grounds in respect of the above appeals: -

> *"a) On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in deleting the order passed under section 201(1) & 201(1A) of the Act, ignoring the fact that the beneficiaries of Capital Gain are not treaty subjects in UAE.*
>
> *b) On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has erred summarily ignoring the ruling given, by the Hon'ble Authority for Advance Rulings without even going into the reasoning given, by the Hon'ble Authority for Advance Ruling contained in the ruling in the case of Abdul Razak A Memon (276 ITR 306) which certainly had a persuasive value as it was rendered subsequent to the judgement of the Hon'ble Apex Court rendered in the case of Azadi Bachao Andolan (263 ITR 706)".*

4. The issue in the above appeals is with reference to the capital gains arising to various persons of Indian origin or non-resident Indians residing in UAE, who are clients of the Bank. These clients have invested in Government of India T-Bills, which has a tenure of 364 days. The T-Bills are also transferable before maturity. The clients purchased and sold these T-Bills during the year for which Bank, according to the guidelines of the RBI has opened a second subsidiary general ledger in their own name on behalf of their constituents/investors as required by the guidelines. They also have separate designated NRE account with the Bank. An agreement has been entered between the bank and the constituents/ investors for opening CSGL account. The constituents/investors purchased and sold Government Bills through the designated account maintained by the ICICI Bank. The funds in the NRE accounts were utilised for purchase of securities whereas the proceedings of sales are remitted to the same account maintained with the

bank. The contention of the Revenue is that the capital gains that has arisen to the said constituents/investors is liable to tax in India and since the Bank has not deducted tax at source the liability under section 201(1) and consequently under section 201(1A) were imposed on the said bank.

5. It was the contention of the Bank that those constituents/ investors comprises of non-resident Indians as well as persons of Indian origin residing in UAE and these investors are entitled for the benefit of Article 13 of the Treaty and hence the Bank is not required to deduct tax at source on the capital gains arising from the sale of T-Bills. The bank contended that the Treaty is more beneficial to the investor and hence the Treaty should be applied. It was further contended that the Indian Government entered into a comprehensive DTAA with the Government of UAE being fully aware that there was no Income Tax or Wealth Tax on Individuals in the Emirates. It further contended that there are a number of Articles in the DTAA between India & UAE solely concerning with individuals (in particular, Article 14 to 21). If the intention was not to make the DTAA applicable to individuals, there was no need to have such Articles dealing with taxation of income in the hands of the individuals. The Bank further contended that the DTAA applies to all persons residing in UAE and there is no justification for excluding individuals from the purview of the relevant provision. The Bank contended that whenever the government intended the provisions of Treaty should not be applicable if the resident of one state is no subject to tax in that state a specific restrictive clause to that extent is included in the Treaty. In this regard the Bank has made references to the DTAA signed by India with Ukraine, Jordan and Sweden. The Bank further argued that since no such provision is available in the Indo-UAE Treaty the individuals residing in UAE cannot be taxed in India. The Bank further contended that the provisions of DTAA entered into between the Governments allocate jurisdiction between contracting states for the purpose of levy of tax and limits rate of tax leviable under the treaty. Article 13 of the DTAA between India & UAE provides that capital gains arising in India to a resident of UAE will not be subjected to tax in India. Accordingly, the jurisdiction to tax capital gains on transfer of movable property is allocated to UAE under

Article 13 of the said DTAA. The jurisdiction to tax in respect of dividend and interest is allocated to the state of residence of the recipient of such income while maintaining the jurisdiction of the source state, viz. India to tax at the specified rates under Articles 10 & 11 of the DTAA. The DTAA has granted the jurisdiction of taxing capital gains from alienation of shares, debentures, securities, etc. to the country of which the alienator is a resident. The Bank contended that its client, the alienator, is not a resident in India within the meaning of the definition of resident under the Indian I.T. laws. UAE only has the jurisdiction to tax such gains. The jurisdiction to tax capital gains solely rests with UAE and hence the capital gains cannot be taxed in India. The Bank further contended that the CBDT Circular No. 734 dated 24.01.1996 has indicated that the availability of DTAA benefit to individual residents in UAE and this Circular is clarificatory in nature. This circular supports the view that the Treaty applies to all types of income though the circular has specifically dealt with the dividend & interest. In view of the above, the appellant contended that no tax is required to be deducted at source from the capital gains arising from transfer of Government of India T-Bills. The Bank also relied on the decision of the Green Emirates Shipping and Travels 100 ITD 203. The A.O. has not accepted the contentions of the Bank. The A.O. is of the view that since the individuals are not taxable in UAE, they cannot be considered as residents within the meaning of Article 4(1) of the Treaty and hence the provisions of the Treaty are not applicable to the individuals residing in UAE. The A.O. relied on the decision of the AAR in Cyril Ugene Perera 239 ITR 650 and the A.O. has relied on the following observations of the Hon'ble AAR in that decision.

6. The learned CIT(A), following the decision of the Hon'ble Supreme Court in the case of Union of India vs. Azadi Bachao Andolan 263 ITR 706 wherein the decision of the Authority for Advance Ruling in the case of Cycil Ugene Pereia 239 ITR 650 was considered and also the decision of the Tribunal in the case of ACIT vs. Green Emirates Shipping & Travels 100 ITD 203, came to a conclusion that there is no tax liability on the capital gains on the constituents who are residents of UAE and hence the Bank is not

responsible for deducting tax. He also gave the following finding in para 5 of the order: -

"5. Before parting, I also wish to share the following views which also supports my decision:

(a) DTAA Treaty is entered into two countries to benefit the people living in these two countries from avoidance of double taxation. Just because the individuals are not an assessable entity in UAE, if we hold they are not entitled to the benefits of tax treaty, then it will amount to leaving the entire citizens living in UAE out of the tax treaty. This may not be intention of the Treaty.

(b) As per DTAA article 13, the capital gains on immovable property will be taxed in the country in which the property is situated. Similarly, for the movable assets forming part of business assets, the capital gains arises where the Permanent Establishment is situated. Hence, in these two cases, the capital gains are taxable in the country in which the property is situated. It appears to me that for all other properties, the treaty intends to keep the fiscal residence of the person in mind in taxing the capital gains. In this case, all such clients of the appellant bank are not residents of India and hence capital gains cannot be taxed in India.

(c) In case, if we hold that the treaty is not applicable to the NRI living in UAE, then the same individual will not be resident of India and also not a resident of UAE and hence the capital gains arising from sale of such securities cannot be taxed in any of the country because Article 13(3) of the treaty says that capital gains <u>shall be taxable only in the Contracting State of which the alienator is a resident</u>. In this case, as per the interpretation advocated by the assessing officer, the individual will not be a resident of UAE as well as India. In view of this also, the appellant should succeed.

(d) In many of the other treaties it is specifically provided that the capital gains are taxable in the country in which the alienation of the property takes place in case such gains is not taxable in the country in which the alienator is a resident.

Firstly, Article 13(5) of the tax treaty with Sweden reads as follows:

"Gains from the alienator of any property other than that referred to in paragraphs (1), (2), (3) and (4), shall be taxable only in the Contracting State of which the alienator is a resident, provided that such resident is subject to tax thereon in that state. ***<u>If the resident is not subject to tax thereon, then such gains may be taxed in the other Contracting State.</u>****" (emphasis supplied)*

Article 13(6) of the tax treaty with Ukraine reads as follows:

"Gains from the alienation of any property other than that mentioned in paragraphs 1,2,3,4 and 5, shall be taxable only in the Contracting State of which the alienator is a resident ***<u>provided that those gains are subject to tax in that Contracting State</u>****." (emphasis supplied).*

Secondly, Article 13(5) of the tax treaty with Jordan reads as follows:

"Gains from the alienation of any property other than that referred to in paragraphs 1,2,3 and 4 shall be taxable only in the Contracting State of which the alienator is a resident, provided that such resident is subject to tax thereon in that State. ***If the resident is not subject tax thereon, then such gains may be taxed in the other Contracting State****.´(emphasis supplied)*

Since no such provision is available in the UAE treaty, the contentions put forth by the appellant is acceptable.

5.1 In view of the decision of the Hon'ble Supreme Court in the case of Azadi Bacaho Andolan 263 ITR 706; & also the Hon'ble ITAT's decision in the case of Asstt. DIT vs. Green Emirates Shipping & Travels 100 ITD 203 and also in view of my above observations I am fully convinced that the capital gains arising out of the transfer of T Bills in the hands of the residents of UAE is not taxable in India in view of DTAA. I direct the A O to cancel the demand raised u/s. 201 and u/s. 201(1A) of the I.T. Act."

Revenue is aggrieved on the above and raised the grounds accordingly.

7. It was the contention of the learned D.R. that the Tribunal has taken a decision already but the proof that these constituents are residents of UAE is required to be verified and made request that the matter be examined afresh. She relied on the order of the A.O. in submitting that there is no tax liability on the constituents/investors in UAE, therefore, they are liable to be taxed in India as held by the A.O.

8. The learned counsel, however, submitted that there is no dispute with reference to residence of constituents/ investors in UAE and referred to para 3 of the order of the A.O. whereas it was stated that the beneficiaries of the remittance by the ICICI Bank were residents of UAE. Therefore the question of verifying the residential status on the basis of the subsequent protocol entered into by the Government of India with the Government of UAE vide Portfolio dated 15th June 2006, notified with No. 282 of 2007 dated 28th November 2007 cannot be considered, at this stage. Further it was placed on record the protocol made effective subsequently where the liability to capital gains by Article 4 of the Protocol amending the DTAA, to submit that there is no tax liability in the impugned years on the capital gains and, therefore, Bank is not liable to deduct any tax. She relied on the order of the CIT(A). She also relied on the orders of the ITAT in Green Emirates Shipping

& Travel 100 ITD 203 and ITO vs. Ramesh Kumar Goenka 39 SOT 132 (Mum).

9. We have considered the issue. As briefly stated above the issue is of liability to capital gains in the case of the individual residents of UAE who transacted in the government T-Bills through the account maintained with the Bank. There is no dispute with reference to the fact that all these constituents/investors are residents of UAE. The A.O. also gives a finding that they are residents of UAE. There is also no dispute that during the year the various constituents/investors earned short term capital gains as stated in the Annexure to the AO's order by transacting in government T-Bills. It was the contention that those residents of UAE are not liable to tax in view of Article 13(3) of the Indo-UAE DTAA. Since the constituents were residents of UAE, it is only the UAE which has right to tax capital gains and not India. Article 13 of the agreement for avoidance of double taxation between India and the UAE (hereinafter referred to as the 'India-UAE Treaty) provides an exemption from capital gains tax in India to the residents of UAE. It reads as under: -

Article 13: Capital gains:

(1) Gains derived by a resident of a contracting State form the alienation of immovable property referred to in paragraph 2 of Article 6 and situated in the other contracting State may be taxed in that other State.

(2) Gain from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a contracting State has in the other contracting State or of movable property pertaining to a fixed base available to a resident of the contracting State in the other contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or together with the enterprise) or of such fixed base may be taxed in that other State.

(3) Gains from the alienation of any property other than that mentioned in paragraphs 1 and 2 shall be taxable only in the contracting State of which the alienator is a resident.

Article 4 of the India-UAE DTAA defines resident of a contracting State as any persons who under the laws of the State is liable to tax therein.

10. Vide Article 13(3) it is very clearly stated that gains from alienation of any property other than mentioned in paragraphs 1 and 2 shall be taxable only in the contracting state of which the alienator is a resident. Paragraph 1 refers to alienation of immovable property and paragraph 2 refers to alienation of movable property forming part of business property and permanent establishment. The property in question is government T-Bills, which are movable property not covered by Article 13(1) & (2). Therefore under Article 13(3) it is taxable only in the contracting state of which alienator is a resident. There is no dispute in this case as to the fact that the constituents are residents of UAE, therefore, the right to tax the amount, by the virtue of DTAA, is with the country in which the alienator is a resident and in this case the constituents/investors being alienators are residents of UAE, therefore, with UAE.

11. By virtue of DTAA the right was arising to the country in which alienator is a resident. Since the alienators are residents of UAE there is no right to tax the capital gains from alienation of T- Bills in India. This being the case we are unable to understand on what basis the A.O. raised the demand holding that the capital gain is taxable in India.

12. The case of revenue is that there is no tax liability on this in UAE. This issue was already decided by the Coordinate Bench in the case of Green Emirates Shipping and Travels 100 ITD 203 wherein the Tribunal had an occasion to deal with an identical issue and held as under: -

> *"8. Although the Assessing Officer's objection to applicability of India-UAE tax treaty was only on the ground that the provisions of double taxation avoidance agreements do not come into play unless it is established that the appellant bank is paying tax in both the countries in respect of the same income, in the ground of appeal before us it is also contended that the assessee-company failed to produce any evidence to the effect that it was 'liable to pay taxes' in UAE. The question then arises whether an existing liability to pay taxes in UAE is a sine qua non to avail the benefit of India-UAE tax treaty in India. On this issue also, we find guidance from the judgement of Hon'ble Supreme Court in the case of Azadi Bachao Andolan (supra). Referring to the Klaus Vogel's Commentary on Double Taxation Conventions, Their Lordships, inter alia, observed as follows:*

"In other words, Contracting States mutually bind themselves not to levy taxes or to tax only to a limited extent in cases when the treating reserves taxation for the other contracting State either entirely or in part. Contracting States are said to waive 'tax claims' or more illustratively to divide 'tax sources', 'taxable objects', amongst themselves. Double taxation avoidance treaties were in vogue even from the time of the League of Nations. The experts appointed in the early 1920s by the League of Nations describe this method of classification of items and their assignments to the Contracting States. While the English lawyers called it 'classification and assignment rule', the German jurists called it 'the distributive rule' (Vertei-lungsnorm). To the extent that an exemption is agreed to, its effect is in principle independent of both whether the Contracting State imposes a tax in the situation to which the exemption applies, and irrespective of whether the State actually levies the tax. Commenting particularly on the German Double Taxation Convention with the United States, Vogel comments: Thus, it is said that the treaty prevents not only 'current' but also merely 'potential' double taxation'." [Emphasis supplied]

It is, thus, clear that a tax treaty not only prevents 'current' but also 'potential' double taxation. Therefore, irrespective of whether or not the UAE actually levies taxes on non-corporate entities, once the right to tax UAE residents in specified circumstances vests only with the Government of UAE, that right, whether exercised or not, continues to remain exclusive right of the Government of UAE. As noted above, the exemption agreed to under the 'assignment' or 'distributive' rule, is independent of whether the Contracting State imposes a tax in the situation to which exemption implies'. In the case of John N. Gladden v. Her Majesty the Queen 85 TC 5188, which was quoted with approval by the Hon'ble Supreme Court in Azadi Bachao Andolan's case (supra), Federal Court of Canada was observed that "the non-resident can benefit from the exemption (under the treaty) regardless of whether or not he is taxable on that capital gain in his own country. If Canada or the US were to abolish the capital gains tax completely, while the other country did not, a resident of the country which has abolished the capital gains would still be exempt from capital gains in that other country". It is, thus, clear that taxability in one country is not sine qua non for availing relief under the treaty from taxability in the other country. All that is necessary for this purpose is that the person should be 'liable to tax in the Contracting State by reason of domicile, residence, place of management, place of incorporation or any other criterion of similar nature' which essentially refers to the fiscal domicile of such a person. In other words, if fiscal domicile of a person is in a Contracting State, irrespective of whether or not that person is actually liable to pay tax in that country, he is to be treated as resident of that Contracting State. The expression 'liable to tax' is not to read in isolation but in conjunction with the words immediately following it, i.e., 'by reason of domicile, residence, place of management, place of incorporation or

> *any other criterion of similar nature'. That would mean that merely a person living in a Contracting State should not be sufficient, that person should also have fiscal domicile in that country. These tests of fiscal domicile which are given by way of examples following the expression 'liable to tax by reason of', i.e., domicile, residence, place of management, place of incorporation, etc., are no more than examples of locality related attachments that attract residence type taxation. Therefore, as long as a person has such locality related attachments which attract residence type taxation, that 'person' is to be treated as resident and this status of being a 'resident' of the Contracting State is independent of the actual levy of tax on that person. Viewed in this perspective, we are of the considered opinion that being 'liable to tax' in the Contracting State does not necessarily imply that the person should actually be liable to tax in that Contracting State by the virtue of an existing legal provision but would also cover the cases where that other Contracting State has the right to tax such persons – irrespective of whether or not such a right is exercised by the Contracting State. In our humble understanding, this is the legal position emerging out of Hon'ble Supreme Court's judgement in Azadi Bachao Andolan's case (supra). The plea taken by the revenue that the assessee was not 'liable to tax', which was anyway not taken by the Assessing Officer or before the CIT(A), is also not sustainable in law either."*

13. In our view the decision in the case of Green Emirates Shipping and Travels (supra) is clearly applicable to the facts of the case. As held in the aforesaid case the expression 'liable to tax in the contracting state' as used in Article 4.1 of Indo-UAE DTAA does not necessarily imply that the person should actually be liable to tax in the contracting sate but would also cover the cases where that other Contracting State has the right to tax such person whether or not such a right is exercised.

14. We are also in agreement with the observation of the CIT(A) vide para 5(c). If the treaty is not applicable to the individual persons living in UAE then the same individual will not be resident of India and also not a resident of UAE and hence capital gains arising from sale of such serucities cannot be taxed in any of the country because Article 13(3) of the Treaty says that capital gains shall be taxable only in the contracting state of which the alienator is a resident. In this case, as per the interpretation advocated by the A.O. the individual will not be a resident of UAE as well as India. In view of this also the case of the Revenue fails on this point.

15. Be that as it may, the Government of India entered into a further protocol vide 15th day of June 2006, which was notified vide Notification No. 282 of 2007 dated 28th November 2007. This Protocol amended the DTAA and vide Article 4 of the Protocol the following were modified: -

> *"Article 4*
>
> *Paragraph 3 of article 13 (Capital Gains) of the Agreement shall be replaced by the following:*
>
> *"3. Gains from the alienation of shares of the capital stock of a company the property of which consists directly or indirectly principally of immovable property situated in a Contracting State may be taxed in that State.*
>
> *4. Gains from the alienation of shares other than those mentioned in paragraph 3 in a company which is a resident of a Contracting State may be taxed in that State.*
>
> *5. Gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4 above shall be taxable only in the Contracting State of which the alienator is a resident."*

16. As can be seen from the above the amended Article 13 (after insertion of modified Article 13(3), 13(4) and 13(5)) gives rise to a situation where the gains from alienation of shares of the capital stock of a company is also taxed in the contracting state where the property of which consists directly or indirectly of immovable property situated in a Contracting State. Therefore the earlier uncertainty in taxing the capital gains arising from alienation of shares on the capital stock of the company or alienation of shares are permitted to be taxed in the state where the property is situated or the company is a resident of the Contracting State. But as seen from the facts of the case, the constituents/investors did not alienate any property covered by even the amended Article 13(3) and 13(4) as the transaction is with reference to Government of India T-Bills. Government T-Bills are not shares in a company. These are sovereign bonds issued by Government of India through RBI. Therefore, it is again covered by Article 13(5) wherein the power to tax was with the Contracting State of which the alienator is a resident. Even after the amended Protocol, the capital gains in the case of Government T-Bills are not taxable in India as the power to tax them has

been assigned to UAE by virtue of amended protocol, wherein those persons are residents.

17. The term 'resident' has been defined in the notification as 'individual who is present in that UAE for a period or periods totalling in the aggregate at lease 183 days in the calendar year concerned". In this case there is no dispute with reference to the fact that these persons are residents of UAE. Therefore, we are of the opinion that there is no liability to tax the capital gains arising to the individual constituents/investors on the transactions in Government Treasury Bills undertaken through the Bank. Since there is no liability to tax in India, obviously the Bank is not covered by the provisions of TDS. In view of this, the order of the CIT(A) is upheld and the Revenue grounds are dismissed.

18. In the result, Revenue's appeals are dismissed.

Order pronounced in the open court on 16th September 2011.

Sd/-	Sd/-
(R.S. Padvekar)	**(B. Ramakotaiah)**
Judicial Member	**Accountant Member**

Mumbai, Dated: 16th September 2011

<u>Copy to:</u>

1. *The Appellant*
2. *The Respondent*
3. *The CIT(A) – XXXIII, Mumbai*
4. *DIT (International Taxation) 3(2), Mumbai*
5. *The DR, "L" Bench, ITAT, Mumbai*

By Order

//True Copy//

Assistant Registrar
ITAT, Mumbai Benches, Mumbai

n.p.