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

RESERVED ON: 16.02.2017

% PRONOUNCED ON: 21.04.2017

\+ ITA 578/2016, CM APPL.28947/2016
ITA 579/2016, CM APPL.28948/2016

PR. COMMISSIONER OF INCOME TAX ..... Appellants
Through: Mr. Ashok Manchanda, Sr. Standing Counsel with Mr. Raghvendra Singh and Ms. Lakshmi Gurung, Advocates.

Versus

KRISHAK BHARATI COOPERATIVE LTD. ..... Respondents
Through: Mr. Arvind P. Datar, Sr. Advocate with Ms. Surekha Raman and Mr. Anuj Sarma, Advocates.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE NAJMI WAZIRI

S.RAVINDRA BHAT, J.

1. This is the revenue's appeal, under Section 260-A of the Income Tax Act ("the Act") for assessment years (AYs) 2010-2011 & 2011-12. Since the issues involved in these appeals are common and identical, these appeals were heard together. The questions of law, framed for the appeal are as follows:

(1) Did the ITAT fall into error in holding that the AO's order was not erroneous in law and prejudicial to the revenue,

(2) Did the ITAT err in deciding that dividend income was taxable but exempt under Omani law to entitle the assessee to the benefits of the Indo Oman DTAA.

2. The facts of the case are that the assessee is a multi state co-operative society registered in India, under the administrative control of the Department of Fertilizers, Ministry of Agriculture and Co-operation, Central Government. Its main business is manufacturing fertilizers such as urea and ammonia. It entered into a joint venture with Oman Oil Company to form the Oman Fertilizer Company SAOC ("OMIFCO" or "the JV"), a registered company in Oman under the Omani Laws. The assessee is 25% shareholder in the JV, which manufactures fertilizers. The fertilizers manufactured by OMIFCO are purchased by the Central Government. The assessee established a branch office in Oman to oversee its investments in OMIFCO. The branch office is independently registered as company under the Omani laws. It claims Permanent Establishment (PE) status in Oman in terms of Article 25 of the Double Taxation Avoidance Agreement ("DTAA") between India and Oman. That branch office maintains its own books of account and files, returns of income under the local income tax law of Oman.

3. The assessee filed its return of income on 24.09.2010. The return was selected for scrutiny and notices were issued along with detailed questionnaires. During the course of assessment proceedings, detailed replies were filed on behalf of the assessee; its authorized representative also attended hearings before the Assessing Officer and furnished the necessary details. The assessment was completed under Section 143 (3) through order

dated 27.02.2014. Whilst completing the assessment, the Assessing Officer allowed tax credit for a sum of ₹41.53 crores in respect of the dividend income of ₹134.41 crores received by the assessee from OMIFCO. That dividend income was simultaneously brought to the charge of tax in the assessment as per the Indian tax laws. Under the Omani Tax laws, exemption was granted to dividend income by virtue of the amendments made in the Omani Tax Laws with effect from the year 2000. The AO allowed credit for the said tax which would have been payable in Oman but for the exemption granted. After completion of assessment, the Principal Commissioner of Income Tax (hereinafter referred as "PCIT"), issued a show cause notice dated 28.09.2015, under Section 263 of the Act. The basis of the said notice is extracted below for ready reference from the notice itself:

> *"A perusal of the records indicates that in the computation of income filed by the Assessee, dividend income received from OMIFCO, Oman, of Rs.143,83,99,800 was included in the total income of the Assessee. Thereafter, tax credit of Rs. 41,44,23,149 was claimed as relief u/s 90 of the Income Tax Act 1961 read with Article 11, 7 and 25 of the India-Oman DTAA. This claim of tax credit was allowed by the Assessing Officer during the Assessment Proceedings.*
>
> *Dividend income received in Oman is exempt from taxation in as per Article 8 (bis) of the Oman Company Income Tax Law, which is reproduced below:*
>
> > *"Tax shall not apply on dividends that the company earns from its ownership of shares in the capital of any other company."*
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> *Therefore, no tax was payable by KRIBHCO on the dividend receipts of Rs.143,83,99,800 in Oman. The DTAA between India and Oman allows tax credit in India for the taxes payable in Oman. Even though no taxes were actually paid on the dividend income from OMIFCO,*

the Assessee has claimed tax credit by relying on Article 25 (4) of the India-Oman DTAA, which states -

> *"25(4) The tax payable in a Contracting State mentioned in paragraph 2 and paragraph 3 of this Article shall be deemed to include the tax which would have been payable but for the tax incentives granted under the laws of the Contracting State and which are designed to promote economic development."*

Article 25 (4) requires that in order to claim credit, tax should have been payable in Oman if not for the tax incentives granted in Oman,.

since Article 8 (bis) exempts dividend income received in Oman in totality, no tax was payable in Oman at all at any stage and thus no tax was foregone on account of tax incentives by Oman.

Article 3 (2)of the India-Oman DTAA provides that if a term used in the agreement is not defined then the term will have the meaning which it has under the Law of that Contracting State concerning the taxes to which this Agreement applies (i.e. India). The term 'tax incentive' has not been defined in the India Oman DTAA. The meaning must, therefore, be inferred from Indian Law. The term tax incentive is not defined in the Income Tax Act , 1961. The tax incentive refers to income which would otherwise be taxable but has not been taxed with a view to promote economic activity in certain sectors or in the economy as a whole. Any income which is not taxed at all as per the tax laws cannot be construed as an incentive. The Omani Companies Income Tax Law vide Article 8 (bis) exempts dividend income from taxation in Oman. this cannot be interpreted as an incentive as it exists across the board with no exceptions in Oman. It is simply a feature of Oman's Tax Law that does not tax dividend income. Hence, it cannot be construed as an incentive granted under Oman's tax laws.

Consequently, reliance on Article 25 (4) of the India Oman DTAA was erroneous in this case and no tax credit was due to the Assessee under Section 90 of the IT Act. The Assessment Order passed, accepting the contentions of the Assessee and allowing tax credit is erroneous as well as prejudicial to the interest of the Revenue. You are, therefore, in terms of provisions of sub-section (1) of Section 263 hereby given

an opportunity to furnish justification as to why the tax credit of Rs.41,44,23,149 should not be withdrawn for A.Y. 2010-11."

4. The assessee resisted the notice contending that the specific issue relating to allowing tax credit for the deemed tax paid on dividend income in Oman, was allowed at the time of original assessment, after considering the detailed reply filed before the AO. It was pointed out that in the letter issued under Section 142 (1) of the Act during the course of assessment proceedings, the assessee was specifically queried about the tax credit claimed by it in respect of dividend income received from OMIFCO. The Assessee had filed a letter dated 11.12.2013 which enclosed the complete details to the AO and explained the factual and legal position with reference to the provisions of Section 90 of the Act and Article 25 (4) of the DTAA. As to the merits of allowing credit of the deemed tax also, detailed submissions were made. The provisions of DTAA read with the relevant provisions of Omani Tax Laws, as clarified by the Ministry of Finance, Secretary General for Taxation, Muscat, Sultanate of Oman, were also referred to and copies of all relevant documents were filed before the Assessing Officer. It was contended in this reply that the tax credit has been allowed by the Assessing Officer after duly considering the merits of the claim made by the Assessee.

5. The revisional Commissioner by order under Section 263 rejected all of the assessee's submissions. The CIT extracting Article 25 of the DTAA which states that, tax payable in a 'contracting state' shall be deemed to include the tax which would have been payable but for the tax incentive granted under the Law of the Contracting State and which are designed to

promote economic development. The CIT observed that Article 115 of the Omani Tax Laws exempts from tax dividends received by the establishment, Omani Oil Company or Permanent Establishment from shares, allotments or shareholding it owns in the capital of any Omani Company. It was also observed that Article 116 specifically exempts various business activities from the charge of Omani tax. It was held by the CIT that under the Omani Tax Laws dividend is absolutely exempt and is not includible in the total income and, therefore, it cannot be said that any specific exemption was granted for the purpose of tax incentives for economic development. Regarding the assessee's argument with respect to exercise of jurisdiction under Section 263 of the Act it was held that to fall within the benefit of the decision of the Supreme Court, the assessee had to clearly show that the view taken by the AO was a possible view in law. However according to the CIT, that was not the case in the present instance. The CIT held that:

> *"This from the plain and simple reading of both the Oman Tax Law as applicable from 01-01-2010 (Royal Decree No. 28/2009) or the earlier law (Royal Decree 68/2000) effective from the tax year 2000, there is no tax payable on dividend in Oman and accordingly, no tax has been paid. Further, the exemption is not available because of any economic incentive for economic development as the case of the Assessee is not covered under the exemption. The Royal Decree 28/2009, which came into force w.e.f. 01-01-2010 makes the position very clear and reiterates the position of exemption of dividend income provided for in the Article 8 of old Royal Decree 68/2000. The Royal Decree of 2009 also provides for incentive only for a period of five years. In case of Assessee that period has elapsed long back."*

6. The PCIT did not confine himself to the particular issue referred to in the show cause notice issued by him under Section 263 but also ordered in regard to a new issue (which was not referred to in the show cause notice).

The CIT here held that the assessee had credited more income than the dividend received by it and further that in P&L Account written in India in terms of Indian laws and accounting standards and submitted to the Department. The accretion and addition to its opening capital in terms of the profit on account of its PE audited and submitted during the proceedings were *"not disclosed in its accounts in India. This makes it abundantly clear that the dividend declared or received only is being shown in its income in India and thus confirming that the income received by the Assessee by its own admission is its dividend income and not business income as claimed by the Assessee."*

The directions issued to the AO were to modify the assessment order as follows:

> *" 1. That the tax credit allowed by the A. O. in respect of dividend income in the Assessment Order is not available to Assessee in terms of either para (1) or para (4) of the Article 25 of the Indo-Oman DTAA.*
>
> *2. The share of profit of its investment in Oman (to the extent it is not declared as dividend) is to be included in the global income of the resident tax payer India as per Sections 4 & 5 of the I.T. Act. This part of income would be eligible for allowance of tax credit as per para (4) of Article 25 of the Indo-Oman DTAA to the extent of taxes which would have been payable but for the incentive provided by the Royal Decree No. 28/2009 w.e.f. 01-01-2010 on any other notification,. The Assessee shall provide it to the A. O. if there is any such notification prior to this Royal Decree 28/2009 and still applicable for the current year. The income shall be computed in terms of notes to account of the financial statement of the branch office of the Assessee is Oman. the tax credit would be available for income earned after this date and tax credit shall be computed accordingly. However, the A.O. shall ensure that the Assessee has*

been granted exemption by the Oman Tax Authority as provided in Article 118 of Royal Decree No. 28/2009.] It is also seen that the Assessee has not furnished complete and true income or particulars of income and, therefore, the A.O. shall also frame a view thereon and take action as per laws."

7. Therefore, the CIT issued directions to the AO regarding the following issues:

(i) Tax credit on dividend is not allowable.

(ii) Profits pertaining to undistributed dividend should be brought to charge of tax.

(iii) The AO was also to frame a view with regard to the default of not furnishing complete and true income or particulars of income on the part of the Assessee.

8. The assessee appealed to the ITAT contending that the AO's order was neither erroneous nor prejudicial to the revenue and was in fact based on a consistent view taken for several previous years, with respect to the applicability of provisions of the DTAA. It was also contended that having regard to the law applicable to Section 263, the CIT could not have travelled beyond the show cause notice and the issues covered by it. To say so, the assessee relied on *CIT Vs. Ashish Rajpal* 320 ITR 674.

9. The ITAT decided the merits of the DTAA claim as follows:

"18. With regard to allowing credit for deemed dividend tax which would have been payable in Oman, we have gone through the relevant provisions of the DTAA between the Republic of India and the Sultanate of Oman read with section 90 of the I.T. Act. Clause (4) of Article 25 of DTAA lays down that the tax payable shall be deemed

to include the tax which would have been payable but for the tax incentive granted under the laws of the contracting State and which are designed to promote economic developments. Thus, the crucial issue to be examined is whether the dividend income was granted exemption in Oman with the purpose of promoting economic development. The exemption has been granted under Article 8 (bis) of the Omani Tax Laws. The said provision has been clarified and explained vide letter dated 11.12.2000 issued by the Sultanate of Oman, Ministry of Finance, Secretariat General for Taxation, Muscat. The text of this letter has already been reproduced (supra). From this letter, the following points emerge:-

(a) Under Article 8 of the Omani Tax Laws, dividend forms part of gross income chargeable to tax.

(b) As a result, investors in tax exempt companies that undertake activities considered essential for the country's economic development suffered a tax cost which had the negative impact.

(c) The Company Income-tax Law of 1981 was therefore amended by Royal Decree No.68/2000 by insertion of a new Article 8 (bis).

(d) Thereby the Government of Oman would achieve its main objective of promoting economic development by attracting investments.

(e) Tax would be payable on dividend income if not for the tax exemption provided under Article 8 (bis).

(f) As the introduction of Article 8 (bis) is to promote economic developments in Oman, the Indian investors should be able to obtain relief in India under Article 25 (4) of the Agreement for Avoidance of Double Taxation.

19. From the above clarifications there remains no doubt regarding the purpose of granting exemption to dividend income. The interpretation of Omani Tax Laws can be clarified only by the highest tax authorities of Oman and such interpretation given by them must be adopted in India. Further, in the tax assessments made in Oman in respect of the PE of the assessee-society it is clearly mentioned that the dividend income which is included in the gross total income is, however, exempt in accordance with Article 8 (bis) and such

exemption is granted with the objective of promoting economic developments within Oman by attracting investments. In view of the facts stated above, we are of the considered view that on merits also the assessee-society is entitled to tax credit in respect of deemed dividend tax which would have been payable in Oman. Therefore, we hold that on merits also the learned PCIT was not justified in directing the Assessing Officer to withdraw the aforesaid tax credit. Further such credit was allowed by the Assessing Officer during several preceding assessment years and, therefore, when there is no change in the facts and the relevant provisions of law, following the well settled principle of consistency of approach, as emerging from a chain of decisions referred to above, credit for deemed dividend tax is clearly allowable in respect of the assessment year under appeal.

20. We note that in his impugned order passed u/s. 263 of the I.T. Act, the Ld. PCIT has given directions to the AO on another issue which did not find any mention in the show cause notice issued. The Ld. PCIT has directed the AO to add the amount of undistributed dividend from Omani Company as reflected in the Profit and Loss Account of the PE of the assessee in Oman. We have already recorded a finding that the Ld. PCIT has no jurisdiction whatsoever to issue any directions with regard to any issue on which no show cause notice was issued and on that account even the order of the ld. PCIT gets vitiated. Coming to the merits, from the factual position discussed, as aforesaid, it is seen that the annual accounts of the PE are prepared in accordance with the International Financial Reporting Standards (IFRS). As per IFRS-28 the share of PE in the profit / loss in OMIFCO at 25% has to be accounted as income in the Profit and Loss account of the PE even though such income received is only to the extent of dividend declared and distributed. Out of the total distributable profit, OMIFCO is required to transfer a specified amount to reserves under the Omani law and only the remaining profits are distributed to the shareholders. Therefore, even under the Omani Tax Laws, the PE offers for taxation only the dividend income actually received and not the total share of the PE in the profits of OMIFCO. On the other hand, books of account of the assessee in India are required to be prepared in consonance with the Indian Accounting Standards. Obviously, the undistributed share of profit

reflected in the books of P.E. cannot be said to partake the character of income under the provisions of the Income Tax Act. It is settled position that accounting entries are not determinative of taxability under the Income Tax Act and further only the real income can be brought to the charge of tax. In the present case even the undistributed profits reflected in the books of the P.E. are not brought to the charge of tax under the Omani Tax Laws. In our view having regard to the above mentioned facts the said income by assuming undistributed profit cannot be taxed under the I.T. Act. Therefore, on merits also the directions issued by the learned PCIT on this issue are not justified and the same are hereby vacated.

21. In view of the above, we hold that the impugned order passed by the learned PCIT u/s.263 of the I.T. Act is without jurisdiction and not sustainable in law. Accordingly, the said order is hereby quashed and as a result, the Assessee's Appeal No. 6785/Del/2015 (AY 2010-11) stands allowed."

10. The revenue argues that the ITAT fell into error in holding that the CIT's order and approach was incorrect. It is urged that the exercise of jurisdiction under Section 263 was warranted and justified. Elaborating on this, learned counsel, Mr. Ashok Manchanda argued that the ITAT overlooked material terms of the treaty as well as the fact that without proper authorization, the income could not be treated as arising from a project relating to the economic development of Oman. It was submitted that merely because the AO had previously in some other year considered or discussed the matter, did not mean that those views had to be considered plausible. Even otherwise, the principle of *res judicata* does not apply to Income-tax proceedings and an error in the preceding year need not be repeated or ignored in the subsequent years as held by this Court in *Thomson Press (India) Ltd. v. CIT* (2015) 379 ITR 222 (Del).

11. On the merits, it was urged that the ITAT fell into a fundamental error of law in proceeding on the assumption that the dividend income in this case was entitled to the benefit of the DTAA. It was submitted that the character of the income underwent a change at the stage of reporting it in the returns. Learned counsel pointedly argued that the exemption sought could not be said to have been validly given, because in terms of the Royal decree of 1994, only a ministerial committee could issue the certificate with respect to a project promoting economic development of Oman. Since the certificate relied on in the present case was not issued by the Ministerial office or authority, but by a lower ranking body, i.e the Secretary it could not be considered competent. Furthermore, counsel argued that the relevant provision was Article 115 and not Article 8 (bis) which was never seen.

12. Mr. Manchanda argued that the Tribunal failed to appreciate that the AO did not consider and apply his mind whether the dividend exempt under Article 8 of Omani Income Tax Law was covered under Article 25(4) of the Indo Oman DTAA as incentive designed to promote economic development. In this context, it is urged that the Tribunal erred in accepting the letter from the Secretary General of Taxation, Sultanate of Oman dated 11.12.2000 as conclusive proof of the fact that exemption was indeed granted as an incentive designed to promote economic development and allowed tax credit as per Article 25(4) of India-Oman DTAA. Counsel submitted that the ITAT could not have accepted the letter at face value without proof that it was issued under proper authority.

13. It was argued that the assessee does not fulfill the conditions of Article 5 of the DTAA. The assessee does not carry on business through any

permanent establishment situated or performs in Oman independent personal services from its fixed base situated there. Moreover, the investment made by the assessee in OMIFCO is the decision of the KRIBHCO-India and was done through its own funds and likely even before KRIBHCO-Muscat came into existence. Thus the dividend paid from such investment cannot be 'effectively connected' with the KRIBHCO-Muscat, as is contended by it. It is highlighted that the branch office carries no effective work and in fact functions as a mail receiving and forwarding unit which also remits the dividends received. The learned counsel urged that ITAT was wrong in law in holding the revenue had accepted the position that the branch office of the assessee constituted Permanent Establishment (PE) in Oman in terms of Article 25 of the Indo-Omani DTAA. The CIT had not observed this and clearly stated that the income is not connected to it as the role of a PE is only preparatory and auxiliary as is evident from the final accounts of the assessee as there are no tangible expenses which could indicate activities of any kind so as to justify the role of an income earning unit; it had only one employee working.

14. It is argued that even if the assessee's contention that Article 7 applies to them, is accepted, it has to either treat the dividend income as business profits under Article 7 and cannot claim dividend exemption under Article 8 (bis) of Omani Tax Law and should show the dividend income as business profits in Oman. If the assessee treats it as dividend under Article 8 (bis) of Omani Tax Law, dividend income under Article 11 (1) provides tax at the rate of 10%, subsequently tax credits only to the extent of 10%, i.e., approximately ₹14.4 crores and not ₹41.8 crores, as claimed by the assessee. In effect, the assessee is picking provisions between Omani Tax Law and the

DTAA at its convenience to suit its expediency. It is therefore not entitled to the benefits of the DTAA as claimed.

15. It is contended by Mr. Arvind Datar, learned senior counsel for the assessee that only one issue arose, that the CIT issued notice under Section 263 and that reliance on and claim for benefit under Section 25 (4) of the DTAA was not justified. However he has passed the order on three issues and directed the Assessing Officer to tax the assumed profits on account of the undistributed dividends by OMIFCO as reflected in the Books of Account of the PE. He has also directed the Assessing Officer to frame a view regarding the non-furnishing of complete details or furnishing inaccurate particulars by the Assessee. On these two issues, there was complete denial of natural justice on the part of the PCIT for the reason that the Assessee Society was not allowed any opportunity whatsoever to present its case on these issues. In these circumstances, the entire order passed by the Ld. PCIT under Section 263 was vitiated in law. There was no nexus between the reasons or grounds indicated in the show cause notice issued under Section 263 and the final order passed under that provision. The judgment in *Ashish Rajpal* (*supra*) is relied on.

16. It was urged that the issue sought to be revisited had been considered threadbare in past years and relief granted. In these circumstances, it could not be said that the view of the AO was erroneous. The assessment under Section 143 (3) by the Additional CIT for AY 2006-07 was relied upon. In that order, the issue was discussed as follows:

> *"9. Tax credit as per DTAA with Oman:*

The Assessee has claimed a tax credit of Rs.6,00,49,920 on the dividend income of Rs.20,01,66,440 received from Oman India Fertilizer Company SAOC (herein after referred as OMIFCO). It has been submitted that the Assessee is a joint venture partner in the above company. It has received dividend of Rs.20,01,66,400 during the previous year which has been included in its income under the head Misc. Income under Schedule 7 - 'Other Revenue'. The Assessee has referred to Section 90 of the Income Tax Act and claimed benefit of deemed tax paid in Oman by its PE in Oman. a reference has further been made to Article 25 of DTAA, Article 7,11 and 25 of the DTAA between India and Oman.

The Assessee has submitted that it has filed its return for the year ended 31-3-2006 under Oman's Income Tax Law for its branch namely KRIBHCO Musket Branch PE. Reference has further been made to Article 8 (bis) under Oman's Income Tax Law. A copy of the Assessment Order as made in Oman for its PE has been filed to support its contention that the dividend income has been exempted in Oman in accordance with Article 8 (bis) of Income 'fax Law of Oman. The Assessee's claim of tax sparing @ 30 as per the Royal Decree No. 68/2000 read with Royal Decree No. 48/81 under Company's Income Tax Law, appears to be justified. The credit for Rs.6,00,49m,920 as deemed tax paid under DTAA in addition to the prepaid taxes as claimed in Return of income is allowed."

17. The assessee, by virtue of being a joint venture partner in OMIFCO received during the year, dividend US$30.2325 equivalent to Indian ₹143,83,99,800. The dividend was received by the Permanent Establishment (PE) namely the Branch Office of the assessee. The dividend was received in Oman and was deposited in the bank account maintained by the (PE) branch office, with Bank of Baroda, London, on 21.08.2009, 04.01.2010 and 16.03.2010. Later the dividend was remitted through banking channel into the State Bank of India, NOIDA, INDUSIND Bank, Nehru Place, and ICICI Bank, New Delhi, account of the assessee. It is submitted that dividend is

43.51% of the equity share capital held by the assessee in the JV. The Director's Report of OMIFCO, Oman, and the Minutes of 12th Annual General Meeting of OMIFCO, Oman, held on 10th March 2010 in support of the amount of dividend declared by OMIFCIO were shown to the AO and were part of the record. The dividend income of ₹143,83,99,800 was included in the profit taken as starting point of computation. The dividend income from OMIFCO is included under the Schedule 7 - "Other Revenue" under the item "Dividend". The said dividend is considered as part of the total income of the Assessee Society. The tax liability has been computed on such total income.

18. Learned counsel submitted that the assessee claimed deemed tax credit of ₹41,44,23,149 because the said dividend income is subject matter of taxation in both the countries, one has to read Section 90 of the Act along with the provisions of DTAA between India and Oman. Article 11 (4) of DTAA provides that the provisions of Article 11 (1) shall not apply if the beneficial owner of the dividends being a resident of a contracting state carries on business in the other Contracting States of which the company is paying the dividends is a resident, through a permanent establishment situated therein, then in such a case the provisions of Article 7 of DTAA would apply. Since the assessee has a permanent establishment, these provisions would apply. It is urged that Article 7 of DTAA deals with business profits and it provides that where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein profits attributed to that permanent establishment to the extent they are attributable directly or indirectly to that

permanent establishment may be taxed in the other Contracting State. The assessee in the return of income under the Omani Income Tax Law included the said dividend income as part of its total income. The dividend thus received in Oman by the assessee's PE, therefore, could be taxed only by the Omani Tax Law. However, Royal Decree 68/2000 issued by the Omani Authorities, provides that no tax is leviable on dividends, which a company earns from its ownership of shares. This tax exemption is, therefore, granted by the Omani Tax Authorities as an incentive for promoting economic development. The letter dated 11th December, 2000 by the Secretary General of Taxation, Ministry of Finance, Oman, addressed to the joint venture partner, clarified that Article 8 (bis) under the Omani Income Tax Law was for achieving the main objective of promoting economic development with Oman by attracting investment. The CIT could not have doubted the effect of such certificate.

19. It was argued that under Article 25 (4) of the DTAA tax payable in a Contracting State (i.e. Oman) shall be deemed to include the tax which would have been payable but for the tax incentive granted under the laws of Oman and which are designed to promote economic development. Tax treaties provide for such deemed tax credit with respect to tax forgone by the developing countries so that the benefit is retained by the investor. Such credit is known as tax sparing. If the credit is given only to actual tax paid and not for the tax which would have been payable then the benefit which the developing country intended to offer to the concerned tax payer would be nullified. The country's sacrifice of the revenue would ultimately accrue to the state of residence. Mr. Datar argues that therefore, by virtue of Article

25 (4) of the DTAA and Article 8 (bis) off the Omani Tax Law and the Royal Decree 68/2000 and the letter dated 11 December, 2000 of the Secretary General of Taxation, Ministry of Finance, during the year, the assessee received a dividend income of ₹143,83,99,800 on its equity investment in Oman India Fertilizer Company SAOC (OMIFCO) which was entitled and correctly given tax credit.

Analysis and Findings

20. Since the decision in these appeals hinges upon provisions of the DTAA, it would be useful to extract them. Article 7 talks of business profits and prescribes as follows:

> *"The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carried on business in the other Contracting State through a Permanent Establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other Contracting State but only so much of them as is attributable directly or indirectly to that Permanent Establishment."*

Article 11 of the DTAA, which deals with dividends, reads as follows:

> *"ARTICLE 11 DIVIDENDS*
>
> *1. Dividends paid by a company which is resident of a Contracting State to a resident of the other Contracting State may be taxed in that other Contracting State.*
>
> *2. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of the State, but if the recipient is the beneficial owner of the dividends, the tax so charged shall not exceed:*

(a)		*10 per cent of the gross amount of the dividends if the beneficial*

		owner is a company which owns at least 10 per cent of the shares of the company paying the dividends ;
(b)		*12½ per cent of the gross amount of the dividends in all other cases.*

This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term "dividends" as used in this Article means income from shares or other rights, not being debt-claims, participating in profits as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the Contracting State of which the company making the distribution is a resident.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident, through a permanent establishment situated therein or performs in that other Contracting State independent personal services from a fixed base situated therein, and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of Article 7 or Article 16, as the case may be, shall apply.

5. Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other Contracting State may not impose any tax on the dividends paid by the company except insofar as such dividends are paid to a resident of that other Contracting State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or a fixed base situated in that other Contracting State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other Contracting State."

Article 25 deals with avoidance of double taxation and reads as follows:

"25. Avoidance of Double Taxation (1) The law in force in either of the Contracting States will continue to govern the taxation of income in the respective Contracting States except where provisions to the contrary are made in this Agreement.

(2) Where a resident of India derives income which, in accordance with the provisions of this Agreement, may be taxed in the Sultanate of Oman, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income-tax paid in the Sultanate of Oman, whether directly or by deduction. Such deduction shall not, however, exceed that part of the income-tax (as computed before the deduction is given) which is attributable to the income which may be taxed in the Sultanate of Oman.

(3) Where a resident of the Sultanate of Oman derives income which, in accordance with the provisions of this Agreement, may be taxed in India, the Sultanate of Oman shall allow as a deduction from the tax on the Income of the resident an amount equal to the income-tax paid in India, whether directly or by deduction. Such deduction shall not, however, exceed that part of the income-tax (as computed before the deduction is given) which IS attributable to the income which may be taxed in India.

(4) The tax payable in a Contracting State mentioned in paragraph 2 and paragraph 3 of this Article shall be deemed to include the tax which would have been payable but for the tax incentive granted under the laws of the Contracting State and which are designed to promote development.

(5) Income which, in accordance with the provisions of this Agreement, is not to be subjected to tax in a Contracting State, may be taken into account for calculating the rate of tax to be imposed In that Contracting State."

The relevant provision relied on by the assessee, of the Omani Tax law, reads as follows:

"Article 8 (bis) In exception to the provisions of Article 8 of this Law, tax shall not apply on the following:

1. Dividends received by the company against equity shares, portions or stocks in the capital of any other company.

2. Profits or gains realized by the Company from the sale of securities listed in Muscat Securities Market or from their disposal."

The CIT had relied on the following provision:

"SECTION ONE: EXEMPTION FOR CERTAIN CATEGORIES OF INCOME:
Article 115: In determining the taxable income for any tax year, the following shall be exempted from tax:
1. Dividend received by the establishment, Omani company or permanent establishment from shares, allotments or shareholding it owns in the capital of any Omani company.
2. Profits and gains from the disposal of securities listed in the Muscat Capital market."

Findings on the first question: Did the ITAT fall into error in holding that AO's order was not erroneous in law and prejudicial to the revenue

21. What impelled the CIT to hold that the AO had erred was *inter alia*, his interpretation of "tax incentive" under Article 25. The word ""tax incentive" is undefined in the DTAA; the CIT stated that consequently the definition, in terms of Article 3 (2) of the DTAA was to be in accord with Indian law. It was therefore held that in domestic law, a tax incentive is a deduction from income which is otherwise taxable as per law. So, he reasoned that income which does not fall in the total income cannot be the subject matter of tax incentive for economic development. Furthermore, the CIT revisited the issue of PE and held that the assessee had no PE, but a

small branch which carried out auxiliary and preparatory activities, not business.

22. The first question which this court addresses itself to is the order under Section 263 as to the issues which were not covered by the show cause notice issued to the assessee. On this *Ashish Rajpal* is categorical. It was held in that ruling that:

> *"The provisions of Section 263 mandate that an order for enhancing, or modifying the assessment, or cancelling the assessment and directing a fresh assessment can only be passed after giving the assessee an opportunity of being heard and after making or causing to be made such enquiry as is deemed necessary. The threshold condition for reopening the assessment is that before passing an order an opportunity has to be granted to the assessee and, such an opportunity granted to the assessee is a necessary concomitant of the enquiry the Commissioner is required to conduct to come to a conclusion that an order for either an enhancement or modification of the assessment or, as in the present case, an order for cancellation of the assessment is called for, with a direction to Assessing Officer to make a fresh assessment. This defect cannot be cured by first reopening the assessment and then granting an opportunity to the assessee to respond to the issues raised before Assessing Officer during the course of fresh assessment proceedings. To buttress his submission the learned counsel for the Revenue has relied upon the judgment of the Supreme Court in the case of Rampyari Devi Saraogi v CIT, West Bengal & Ors. (1968) 67 ITR 84. This is a case in which, the order issued by the Commissioner, itself revealed that the assessment was being reopened based on an additional supporting material. The Supreme Court in such fact situation thus ruled that non supply of additional supporting material would not effect the basic issue of assessment being carried out without adequate investigation. In the instant case the Order-in-Revision refers to issues and discrepancies which did not find mention in the initial notice dated 11.05.2006 and not to additional or supporting material as in the case of Rampyari Devi (supra). Therefore, to suggest that it would be sufficient compliance of the provisions of Section 263of the Act, if an*

opportunity to respond to the discrepancies mentioned in the Order-in-Revision is given to the assessee in reassessment proceedings before the Assessing Officer, is according to us is completely untenable. It is the requirement of Section 263 of the Act that the assessee must have an opportunity of being heard in respect of those errors which the Commissioner proposes to revise. To accord an opportunity after setting aside the assessment order, would in our view not meet the mandate the Section 263 of the Act. If such an interpretation is accepted it would make light of the finality accorded to an assessment order which cannot be reopened unless due adherence is made to the conditionalities incorporated in the provisions of the Act in respect of such powers vested in the Revenue."

23. Besides, the assessee is also justified in complaining that the CIT could not have branded the AO's order as erroneous in the facts and circumstances of this case. As noticed previously, in the earlier years, the AO had finalized the scrutiny assessment, considered the impact of Articles 11 and 25 of the Indo Omani DTAA, and issued pointed queries on the issue of dividends earned. He had also considered whether a PE had earned dividend income. In such circumstances, the CIT could not have stated that another view rendered the AO's plausible view erroneous. In this regard, the decision in *Commissioner of Income Tax v Gabriel India* (1993) 203 ITR 108 (Bom) had stated this about Section 263:

"This section does not visualise a case of substitution of the judgment of the Commissioner for that of the Income-tax Officer, who passed the order, unless the decision is held to be erroneous. Cases may be visualised where the Income-tax Officer while making an assessment examines the accounts, makes enquiries, applies his mind to the facts and circumstances of the case and determines the income either by accepting the accounts or by making some estimate himself. The Commissioner, on perusal of the records, may be of the opinion that the estimate made by the officer concerned was on the lower side and left to the Commissioner he would have estimated the income at a

figure higher than the one determined by the Income-tax Officer. That would not vest the Commissioner with power to re-examine the accounts and determine the income himself at a higher figure. It is because the Income-tax Officer has exercised the quasi-judicial power vested in him in accordance with law and arrived at a conclusion and such a conclusion cannot be termed to be erroneous simply because the Commissioner does not feel satisfied with the conclusion.....

..... We may now examine the facts of the present case in the light of the powers of the Commissioner set out above. The Income-tax Officer in this case had made enquiries in regard to the nature of the expenditure incurred by the assessee. The assessee had given detailed explanation in that regard by a letter in writing. All these are part of the record of the case. Evidently, the claim was allowed by the Income-tax Officer on being satisfied with the explanation of the assessee. Such decision of the Income-tax Officer cannot be held to be "erroneous" simply because in his order he did not make an elaborate discussion in that regard."

This court has ruled in *Gee Vee Enterprises v ACIT, Delhi-I & Ors* (1975) 99 ITR 375 that an order is erroneous when it is contrary to law or proceeds on an incorrect assumption of facts or is in breach of principles of natural justice or is passed without application of mind, that is, is stereo-typed, in as much as, the Assessing Officer, accepts what is stated in the return of the assessee without making any enquiry called for in the circumstances of the case, that is, proceeds with undue haste. In the facts of this case, neither did the AO overlook the relevant facts; nor did he not make inquiries. In fact the queries were specifically with respect to dividend income, the exemption etc and had also considered the explanation of the Omani authorities on the subject. Therefore, the CIT's view that the assessment orders were erroneous requiring revision was not sustainable in law.

The second question: Did the ITAT err in deciding that dividend income was taxable but exempt under Omani law to entitle the assessee to the benefits of the Indo Oman DTAA

24. The rival contentions on this aspect are whether dividend income is at all taxable or if it taxable, but exempt. This is relevant in the context of the assessee's contention that under Article 25 (2) of the treaty, it is entitled to benefit of whatever was the tax treatment it received in Oman. The relevant part of the said provision states *"..Where a resident of India derives income which, in accordance with the provisions of this Agreement, may be taxed in the Sultanate of Oman, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income-tax paid in the Sultanate of Oman, whether directly or by deduction."* Article 25 (4) further clarifies one eventuality, i.e. if dividend is not tax as a result of incentive for economic development of Oman:

> *"(4) The tax payable in a Contracting State mentioned in paragraph 2 and paragraph 3 of this Article shall be deemed to include the tax which would have been payable but for the tax incentive granted under the laws of the Contracting State and which are designed to promote development."*

The relevant portions of Article 11, which deals with dividend income in the DTAA, reads as follows:

> *"11.1. Dividends paid by a company which is resident of a Contracting State to a resident of the other Contracting State may be taxed in that other Contracting State.*
>
> *2. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of the State, but if the recipient is the beneficial owner of the dividends, the tax so charged shall not exceed:..."*

Naturally, the revenue's argument is that Article 11 (1) applies, to say so, it urges that the dividend income is not taxed, at least as far as co-operative societies are concerned and that in any event, the certificate relied upon by the assessee to claim the benefit of Article 25 (2) was not issued by a competent Omani authority.

25. The Tribunal noticed- in this court's opinion, correctly- that the expression "incentive" is neither defined in the Omani Tax Laws nor in the Income Tax Act, 1961. Due to this, OMIFCO wrote in November 2000 to Oman Oil Company SAOC seeking authentic clarification, regarding purpose of Article 8 (bis) of the Omani tax law. The Omani Ministry of Finance, Secretariat General for Taxation, Muscat, by letter dated 11th December, 2000 addressed to Oman Oil Company SAOC stated as follows:

> *"We refer to your letter dated 2 December, 2000 and our previous letter dated 6 August, 2000 on the above subject.*
>
> *Under Article 8 of the Company Income Tax Law of Oman, dividend forms part of the gross income chargeable to tax. The tax law of Oman provides income tax exemption to companies undertaking certain identified economic activities considered essential for the country's economic development with a view to encouraging investments in such sectors.*
>
> *Before the recent amendments to the Profit Tax Law on Commercial and Industrial Establishments, Article 5 of this law provided for exemption of dividend income in the hands of the recipients if such dividends were received out of the profits on which Omani income tax was paid by distributing companies. It meant that Omani income tax was payable by the recipients on any dividend income received out of the exempt profits from tax exempt companies. As a result, investors in tax exempt companies that undertake those activities considered essential for the country's economic development suffered a tax cost on their return on investments. the tax treatment under the above*

mentioned Article 5 had the negative impact on investments in tax exempt project.

The Company Income Tax Law of 1981 was, therefore, recently amended by Royal Decree No. 68/2000 by the insertion of a new Article 8 (bis) which is effective as from the tax year 2000.

As per the newly introduced Article 8 (bis) of the Company Income Tax Law, dividend distributed by all companies, including the tax exempt companies would be exempt from payment of income tax in the hands of the recipients. In his manner, the Government of Oman would achieve its aim objective of promoting economic development within Oman by attracting investments.

We presume from our recent discussions with you that the Indian investors in the above Project would be setting up Permanent Establishment in Oman and that their equity investments in the Project would be effectively connected with such Permanent establishments.

On the above presumption, we confirm that tax would be payable on dividend income earned by the Permanent Establishments of the Indian Investors, as it would form part of their gross income under Article 8, if not for the tax exemption provided under Article 8 (bis) .

As the introduction of Article 8 (bis) is to promote economic development in Oman, the Indian Investors should be able to obtain relief in India ITA NOS. 6785&6786/DEL/2015 (AYRS. 2010-11 & 2011-12) KRISHAK BHARATI CO-OPERATIVE LIMITED VS. ACIT under Article 25 (4) of the Agreement for Avoidance of Double Taxation in India.

All other matters covered in our letter No. FT/13/92/, dated 6th August, 2000 remained un-changed. "

26. The Tribunal concluded that the above clarification showed that the amendment of the law was to promote Omani economic development and to

encourage investment in Omani companies. The Sultanate of Oman itself therefore clarified the issue regarding interpretation of Article 8 (bis). The tribunal held, in the light of this letter as follows:

> *"It is an accepted position of interpretation that if there is some doubt about the interpretation of a particular provision of Law, the Competent Authority to clarify that provision is only the Government of that particular country. The Income Tax Department of India has no locus standi in this matter. The issue has been clarified by the highest Authority of the Sultanate of Oman through the Secretariat General of Taxation."*

The ITAT also noticed Article 6 of Omani Income Tax Law of Companies No.47 /1981, which spells out functions of the Secretariat General Article 3 (3) states that:

> "*3 - Any form or notification of document issued or published or delivered by the Secretary General in accordance with this Law shall be considered an official document if it carries the name or description of the Secretary General or the responsible officer who is designated by virtue of Paragraph (2) of Article (3) and this shall be whether the name or description is printed, stamped or written."*

In view of the above, it is held that the clarification has to be regarded as conclusive; if the tax authorities had any doubts, they could not have proceeded to elevate them into findings, but rather addressed them to Omani authorities- if not directly, then through Indian diplomatic channels. In not doing so, but proceeding to interpret the laws and certificate of Omani authorities, the revenue, especially the Commissioner fell into error.

27. As far as the submission of the revenue, that the assessee did not have a Permanent Establishment in Oman is concerned, this court is of opinion

that admittedly, for about 5 years, i.e 2002 to 2006, a common order was made under Article 26 (2) (b) of the Income Tax Law of Oman. The opening para of this order reads as under:

> *"We refer to the returns of income and determine the taxable income as under:*
>
> *Kribhco Muscat is a permanent establishment supported by M/s. Krishak Bharati Cooperative Limited, a multi- state cooperative society registered in India. As per the accounts, Kribhco-Muscat is in receipt of dividend income from Omifco, a joint stock company registered in Oman, and that dividend income is connected with the investment of Kribhco-Muscat. The dividend income is, however, exempt from tax in accordance with Article 8 (bis) (1) of the Company Income Tax Law.*
> *The tax exemption on dividend is granted with the objective of promoting economic development within Oman by attracting investments."*

That order first included dividend income (in the total income determined) and thereafter granted deduction. For later years as well, assessments were made similarly. The ITAT also noticed as follows:

> *"Up to the tax year 2011 dividend has been first included in the total income and thereafter deduction has been granted. The facts mentioned above clearly establish that the Assessee Society is entitled to getting credit for the deemed dividend tax by virtue of the provisions of DTAA read with Section 90 of the Income Tax Act, 1961 together with the clarifications issued by the Sultanate of Oman and the assessment made under the Omani Laws. In view of the above it is respectfully submitted that on merits also Assessee Society is entitled for the tax credit which has been rightly allowed by the Assessing Officer and, therefore, the Ld. PCIT has completely erred in giving directions to the Assessing Officer under Section 263 to withdraw the said tax credit."*

These findings are, in this court's opinion, in consonance with logic and reason and do not call for interference. Both questions of law are answered in favour of the assessee; the appeals fail and are, therefore, dismissed.

S. RAVINDRA BHAT
(JUDGE)

NAJMI WAZIRI
(JUDGE)

APRIL 21, 2017