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IN ABSENCE OF SPECIFIC PROVISION, CONCEPT OF BENEFICIAL OWNERSHIP CANNOT BE READ INTO ARTICLE 13 OF THE INDIA-MAURITIUS TAX TREATY

May 30, 2022

INTRODUCTION

The Mumbai bench of the Income Tax Appellate Tribunal ("**ITAT**" or "**the Tribunal**") in its recent ruling in *Blackstone FP Capital Partners v. DCIT*[1], set aside the assessment order wherein the Assessing Officer (**"AO"**) had declined the treaty benefit under article 13(4) of India-Mauritius DTAA (**"the Treaty"**) to the appellant on the ground that the beneficial owners of shares were in a different jurisdiction, i.e., Cayman Islands. While remitting the matter to the AO, the ITAT noted that unlike Article 10 or Article 11 of the Treaty, which specifically provides for beneficial ownership of interest or dividend to be entitled to treaty protection, there is no such provision in Article 13, thus, the AO's reading of beneficial ownership test in Article 13 is an impermissible interpretation and amounted to rewriting of the treaty provision itself.

[1] ITA Nos. 981 and 1725/Mum/2021.

FACTS

Blackstone FP Capital Partners Mauritius V Ltd (**"the appellant"**) was a company fiscally domiciled in Mauritius and had been issued a 'tax residency certificate' ("**TRC**") by the Mauritian Revenue Authority. The Taxpayer had earned long-term capital gains amounting to Rs 904,98,16,345 in the relevant previous year, i.e., 2015-16, arising from the transfer of shares it held in an Indian company, i.e., CMS Info Systems Limited, to a Singaporean company, i.e., Sion Investment Holdings Pte Ltd. The Taxpayer sought relief under Article 13(4) of the Treaty which grants residuary taxing rights solely to the country of residence. This is where the dispute arose, as the AO based on the information received from the tax authorities of Mauritius and Cayman Islands, concluded that the appellant is a wholly-owned subsidiary of the Cayman Island entity and had no independent existence. The AO further noted that the appellant's entire activity was controlled as per the directions of its affiliates including the entire scheme of purchase and sale of shares which was designed for the benefit of the entities in Cayman Islands. On this basis he decided that the appellant was not entitled to the Treaty benefit.

The AO relied on the Bombay High Court's ("**HC**") ruling in *Aditya Birla Nuvo Limited v. DDIT*[2] and the decision of the Authority for Advance Ruling ("**AAR**") in the case of *AB Mauritius, In Re*[3] to deny benefit of Article 13(4) of the Treaty to the appellant on the basis that the beneficial ownership of the shares did not rest with the Mauritian company. The AO's decision was confirmed by the Dispute Resolution Panel (**"DRP"**), following which, the appellant approached the ITAT in appeal.

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[2] [(2011) 12 taxmann.com 141 (Bom)].
[3] [(2018) 90 taxmann.com 182 (AAR)].

RULING BY THE TRIBUNAL

The Tribunal ruled that the AO had proceeded based on a flawed fundamental assumption, that the concept of beneficial ownership of the capital gains can indeed be read into the scheme of Article 13 of the Treaty.

The Tribunal further noted that, unlike Article 10 and Article 11 of the Treaty which specifically provides for beneficial ownership of interest or dividend in order to be entitled for treaty protection, there is no such provision in article 13 of the Indo Mauritius tax treaty. It ruled that the concept of beneficial ownership is a *sine qua non* to entitlement to treaty benefits, therefore, in the absence of specific provision to that effect, it cannot be inferred or assumed in the scheme of Article 13 of the Treaty as had been done by the AO.

The tribunal delved into international tax literature, based on which it decided that unless a condition is specifically set out in the treaty provision itself, it cannot possibly be inferred. Consequently, the ITAT stated that the concept of beneficial ownership is utterly foreign to the scheme of Article 13 of the Treaty. Therefore, the reading of beneficial ownership in to the scheme of Article 13 of the Treaty amounted to rewriting of the treaty provision itself.

Further, it was reiterated by the ITAT that tax treaties are consciously entered into by two willing partners based on minutely laid out terms and the same cannot be unilaterally nullified on the basis of underlying notions of what would constitute good public policy. It ruled that *"respect for negotiated bargains between contracting states is fundamental to ensure tax certainty and predictability and to uphold the principle of pacta sunt servanda, which is specifically referred to in Article 26 of the Vienna Convention on the Law of Treaties. Any violation of this approach, no matter how well-intended, can only be at a huge cost of tax unpredictability- something tax administrations can ill afford."*

Based on the above, the ITAT decided that the AO had fallen in error and wrongfully proceeded without addressing the fundamental question as whether the concept of beneficial ownership can be read into the scheme of Article 13 of the Treaty. Therefore, the matter was remanded back to the AO to decide whether the concept of "beneficial ownership" is inbuilt in the scheme of Article 13 and, if so, what are the connotations of "beneficial ownership" in the context of the present matter.

AMICUS COMMENTS

ITAT's literal interpretation of the Treaty provisions is a step in the right direction and would bring certainty to investors and bolster confidence in the Indian tax regulatory framework. Having said that, the decision to remand the matter back to the AO is likely to evoke mixed feelings. The tribunal's refrain from delving into the merits of the case and examining the concept of beneficial ownership seems like an opportunity passed considering the limited jurisprudence on the same in the Indian context. The remand back to the AO would prolong unwarranted litigation and add to the debate with no end in sight.

Further, the tribunal did not merit discussing Circular No. 789 of 2000[4], which provided the clarification that TRC would be applicable in respect of income from capital gains on sale of shares and accordingly, capital gains arising in India on sale of shares would not be taxable as per Article 13(4) of the Treaty. Despite the clarificatory circular, the revenue has often challenged availability of treaty benefits on the ground of beneficial ownership. However, the validity of Circular 789 of 2000 was upheld by the Supreme Court of India in *Azadi Bachao Andolan v. Union of India*[5] and the same has been relied upon by various judicial and quasi-judicial forums in due course. Considering the tribunal's decision to remand back the matter to the AO, it would have been pertinent to discuss the circular as it would have lent further decisiveness to the tribunal's directions to AO.

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[4] Circular No. 789 of 2000, Dated April 13, 2000

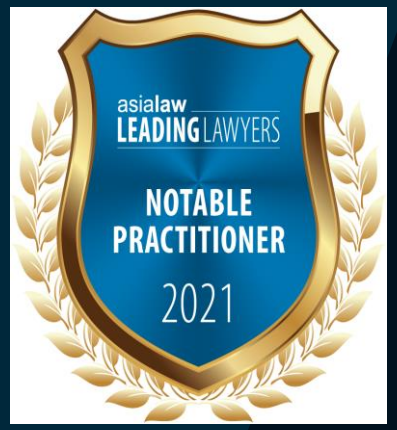
[5] [2003] 263 ITR 706 (SC).

The ruling evokes a mixed response. On one hand it restores faith in the Indian judicial system for its look-at (as against look-through) approach towards interpreting tax treaties. On the other hand, the facts signal a biased approach of revenue authorities at the ground level towards Mauritius as an intermediary jurisdiction for holding companies. More often than not tax authorities proceed with a predetermined mindset of suspicion in respect of companies set up in Mauritius as special purpose vehicles lacking substance. This case also belongs to the same class of cases wherein the tax authorities have stretched the fabric of law to challenge transactions despite express treaty provisions and protected administrative circulars (Circular 789 of 2000). The ruling would undoubtedly have been a landmark ruling had it closed the issue of beneficial ownership on its own rather than delegating to the AO.

ABOUT AMICUS

Amicus is legal and tax consulting firm with focus on corporate finance, re- structuring, private equity, international taxation, transfer pricing and goods and services tax. The Firm's tax team also represents clients in assessments and litigation including Tax Tribunal and Higher Courts.

The Firm focuses on providing efficient, effective, solution- oriented advice and representation based on specialist knowledge and experience. Amicus' boutique tax practice has been consistently ranked as a leading practice by Legal 500, Asia Law and World Tax (ITR).



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