

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI 'I' BENCH, MUMBAI**

**[Coram: Pramod Kumar (Vice President),
and Ravish Sood (Judicial Member)]**

IT (TP) A Nos. 1518/Mum/16 and 560/Mum/2017
Assessment years: 2011-12 and 2012-13

Ampacet Cyprus Limited**Appellant**
*Plot No D 267, 277 and 283, Rajangaon Industrial Area,
Pune 412 220 [PAN: AAACL6740M]*

Vs

Dy Commissioner of Income Tax
International Taxation Circle 1(1)(1), Mumbai**Respondent**

Appearances by

M P Lohia *for the appellant*
Avaneesh Tiwari *for the respondent*

SPECIAL BENCH REFERENCE

Per Pramod Kumar, VP:

1. In both of these appeals, the assessee-appellant has raised two separate, but materially identical, petitions seeking additional grounds of appeal which are materially similar, except for the variation is in respect of the quantum of amount involved. The additional ground so sought to be raised, so far as the assessment year 2012-13, is as follows:

On the facts and in the circumstances of the case and in law, the Hon'ble DRP, the learned Assessing Officer and the learned Transfer Pricing Officer have:

2. Erred in making transfer pricing adjustment of Rs 2,62,69,721 as notional interest and charging it to tax, disregarding the provisions of Article 11 of India Cyprus DTAA

2.1 Erred in imputing and charging notional interest of Rs 2,62,69,721 by applying transfer pricing provisions (under chapter X of the Act) to tax in India disregarding the provisions of Article 11 of India-Cyprus DTAA, which provides for taxability of interest only on paid basis;

2.2 Ought to have considered the fact that assessee is a resident of Cyprus and liable to be taxed on interest income as per Article 11 of Indo Cyprus DTAA, which states that interest is chargeable to tax only when it is arising and paid to non-resident.

2. The additional ground of appeal for the assessment year 2011-12 is exactly the same but the amount of interest adjustment involved, impugned in this appeal, is Rs 55,08,678.

3. On a perusal of petitions seeking admission of additional grounds, and having heard the rival contentions on the same, these additional grounds were admitted by us. These additional grounds were, accordingly, taken up for hearing.

4. When the hearing commenced on merits, on 11th August 2020 and, thereafter, on 13th August, 2020, it was pointed out that in the event of the additional grounds of appeal being allowed, all other issues raised in the appeals will be rendered infructuous. Our attention was invited to the wordings of Article 11(1) and (2) of India Cyprus Double Taxation Avoidance Agreement (**Indo Cyprus tax treaty, in short**) which are as follows:

Article 11- Interest

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 percent of the gross amount of the interest.

[3 to 7-not relevant in the present context and, therefore, not reproduced here]

[Emphasis, by underlining, supplied]

5. Learned counsel submits that a plain reading of the above provision shows that the twin conditions of (a) interest arising in a contracting state, and (b) the interest being paid to the resident of the other contracting state are required to be satisfied for brining the interest to tax under article 11. He submits that it is an admitted position that no interest was paid in the relevant period as the said period was covered by the moratorium under the loan agreement with its Indian subsidiary Ampacet Speciality Products Pvt Ltd, India [**Ampacet India, in short**] and it is for this reason, i.e. treating moratorium as is said to be influenced by the intra AE relationship, that the impugned arm's length price adjustment is made. In effect thus, learned counsel's submission is that when the interest is not actually paid by the Indian subsidiary company to the parent company, i.e. assessee before us, there cannot be any question of any taxability of interest income in the hands of the assessee, and, since there is no taxability of income in the hands of the assessee, there cannot be any question of an arm's length price adjustment to such an income. Our attention is then invited to a series of decisions of the coordinate benches holding so.

6. In response to a question from the bench whether the expression 'paid' is defined under the treaty, and, if not, why should the meanings of expression 'paid', as assigned under section 43(2) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') be considered under article 3(2) of Indo Cyprus tax treaty, learned counsel submitted that there are direct decisions of the coordinate benches on the issues which hold that taxability of interest under Indo Cyprus tax treaty could only be done on cash basis. When he was asked whether these decisions have dealt with the implications of article 3(2), read with definition under section 43(2), and whether, in the absence of such an analysis- which is relevant in the present context, these decisions could be treated as *per incuriam*, learned counsel submitted that answering this question will need reference to a lot of papers. He then withdrew his consent for the virtual court and prayed that the matter be adjourned for hearing before a physical court.

7. While we refrain from making any observations on the manner in which, and stage at which, the consent for virtual hearing was withdrawn, we see merits in this matter being referred to a bench of three or more Members under section 255(3) of the Act. The reason is this. In all the coordinate bench decisions, there is no discussion whatsoever to the connotations of the expression 'paid' and these decisions simply proceed on the basis that because the expression 'paid' is used article 11(1) of Indo Cyprus tax treaty, the taxability of interest can only be on cash basis. The expression "paid" is admittedly not defined in the treaty but article 3(2) of Indo Cyprus tax treaty provides that **"As regards the application of the Agreement at any time by a Contracting State any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Agreement applies and any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State"**. What essentially follows is that unless the context otherwise requires, the definition of the undefined treaty term, under the domestic law of the source country i.e. India- and preferably under the domestic tax laws, is to be adopted. It is in this context, Section 43(2) of the Income Tax Act, 1961 may perhaps be relevant because it provides that **"paid" means actually paid or incurred according to the method of accounting upon the basis of which the profits or gains are computed under the head "Profits and gains of business or profession" (Emphasis, by underlining, supplied by us)**. While it is indeed true that this meaning cannot be imported in the tax treaty mechanically, without any application of mind and as a sort of automated process, undoubtedly a call is to be taken by the bench as to whether or not this domestic law meaning of the expression 'paid' will be relevant. There could possibly be a school of thought that a decision rendered in this context, without specifically dealing with the implications of section 43(2) read with article 3(2), could possibly be *per incuriam*. A conscious call is required to be taken on these aspects. While on this issue, we may further add that one will have to see whether Hon'ble Supreme Court's judgment in the case of **Standard Triumph Motor Co Pvt Ltd Vs CIT [(1993) 201 ITR 391 (SC)]** which, inter alia, observes that **"it must be held in this case that the credit entry to the account of the assessee in the books of the Indian company does amount to its receipt by the assessee and is accordingly taxable and that it is immaterial when did it actually receive it in UK"**, will have any bearing on the connotations of expressions "paid" appearing in the Indo Cyprus tax treaty. As a corollary to these discussions, connotations of the expression "paid" appearing in article 11 of Indo Cyprus tax treaty are required to be examined in some detail, and that exercise can at best be conducted by a bench of three or more members so that the decision is unfettered by the decisions of the division benches in this regard. The issue raised in these appeals needs to be decided in a holistic manner, unfettered by the decisions of the division benches, examining all the relevant facets, including the facets which are germane in the present context have remained to be examined by the coordinate benches.

8. Having said that we may add that we are alive to the fact that there is a decision of Hon'ble jurisdictional High Court, in the case of Director of Income Tax Vs Siemens AG which does observe as follows:

As regards first question is concerned, the Income Tax Appellate Tribunal referred to para 1 to 3 of Article IIX-A of the Double Taxation Avoidance Treaty with the Federal German Republic, as per notification dated 26th August 1985, held that the assessment or royalty or any fees for technical services should be made in the year in which amounts are received and not otherwise. Counsel for the revenue relied upon the Special

Bench decision in assessee's own case, which, in our opinion, has no relevance to the facts of the present case, as it relates to the period prior to the issuance of notification dated 26th August 1985. In this view of the matter the decision of the Income Tax Appellate Tribunal in holding that the royalty and fees for technical services should be treated on receipt basis cannot be faulted.

9. A plain reading of the above decision shows, even though the issue in this case was materially similar inasmuch in this case also it was inferred that since the expression used is “paid” it refers to the taxation on receipt basis, apart from the fact that this decision is in respect of royalty and fees for technical services, that it pertains to the another DTAA, i.e. old double taxation avoidance agreement between India and the Federal Republic of Germany (as it then was) which came to an end on 1st April 1997 and incidentally it was with effect from the same date that hybrid method of accounting also came to an end. Considering that essentially business concerns prepare their accounts on the basis of mercantile method of accounting in general, even accounting of any income, such as interest and royalties, on cash basis was no longer permissible. To suggest, therefore, that interest or royalty income could be taxed in the hands of the foreign company on cash basis on the first principles is no longer permissible, and, as for the connotations of the expressions “paid” in the light of article 2(2), as it was numbered in the old Indo German tax treaty, read with section 43(2), this issue never came up for consideration at any stage at all. As article 2(2) was not even discussed, the relevance of section 43(2) or of Hon’ble Supreme Court’s decision in the case of **Standard Triumph Motor** (*supra*) did not come up for Their Lordships’ kind consideration at all. It is also important to note that so far as article 3(2) of the Indo Cyprus treaty is concerned, it uses the expression “**the meaning that it (i.e. the undefined treaty term) has at that time under the law of that State (i.e. under the Indian law)**”. It is also worth examining whether, in this context, the scope of ‘Indian law’ will include not only the law legislated by the Parliament but also the law laid down by Hon’ble Courts above. A view is thus indeed worth exploring as to whether the meaning assigned to the expression “received by an assessee”, which essentially corresponds to and has to be treated as equivalent to “paid to the payee”, by Hon’ble Supreme Court is to be assigned to the treaty of the undefined treaty expression “paid”. Obviously, this exercise was not done by the coordinate bench, nor this aspect of the matter was pointed out by the learned counsel appearing before Their Lordships, and thus Their Lordships had no occasion to examine this aspect of the matter either. To this extent, the impact of judgment of Hon’ble Supreme Court’s judgment in the case of **Standard Triumph Motor** (*supra*) remained unexamined. That aspect of the matter is thus, *de hors* the judgment of Hon’ble jurisdictional High Court, does seem to be in an uncharted territory on which call may indeed be taken by the Tribunal.

10. As we part with this note recommending constitution of a special bench, we may add that, in our humble understanding, such a reference is not contrary to the principles of judicial discipline. In the event of a doubt about the correctness of the earlier decision or, extending that logic a little further, correctness of the path the earlier decisions have traversed to come to a conclusion, it is open to the bench to make a reference to for constituting a larger bench for considering the same. In the case of **Union of India v. Paras Laminates (P.) Ltd. [(1990) 186 ITR 722 @ p 726 (SC)]**, Hon’ble Supreme Court recognized the right of the President to constitute Special Benches, and observed that “**It is true that a Bench of two members must not lightly disregard the decision of another Bench of the same Tribunal on an identical question..... The rationale of this rule is the need for continuity, certainty and predictability in the administration of justice. Persons affected by**

decisions of Tribunals or courts have a right to expect that those exercising judicial functions will follow the reason on ground of the judicial decision in the earlier cases on identical matters. It is, however, equally true that it is vital to the administration of justice that those exercising judicial power must have the necessary freedom to doubt the correctness of an earlier decision if and when subsequent proceedings bring to light what is perceived by them as an erroneous decision in the earlier case. In such circumstances, it is but natural and reasonable and indeed efficacious that the case is referred to a larger Bench. This is what was done by the Bench of two members who, in their reasoned order, pointed out what they perceived to be an error of law in the earlier decision and stated the points for the President to make a reference to a larger Bench." It is not sinful either, and is perfectly natural- as we will see in a short while, to entertain doubts about correctness of the path that the coordinate benches have traversed. On this aspect, one may usefully refer to the observations of Justice Cardozo, in his classic book 'The Nature Of Judicial Process', (first published by Yale University Press, United States, in December 1921; also available online at http://www.constitution.org/cmt/cardozo/jud_proc.htm) that, "I own that it is a good deal of a mystery to me how judges, of all persons in the world, should put their faith in dicta. A brief experience on the bench was enough to reveal to me all sorts of cracks and crevices and loopholes in my own opinions when picked up a few months after delivery, and reread with due contrition. The persuasion that one's own infallibility is a myth leads by easy stages and with somewhat greater satisfaction to a refusal to ascribe infallibility to others." That is equally, and perhaps much more, true for many of us too. As Hon'ble Supreme Court has said, in the case of **Distributors (Baroda) (P.) Ltd. v. Union of India [(1985) 155 ITR 120 1 (SC)]**, "To perpetuate an error is no heroism. To rectify it is the compulsion of the judicial conscience. In this, we derive comfort and strength from the wise and inspiring words of Justice Bronson in *Pierce v. Delameter* (A.M.Y. at page 18) : 'a judge ought to be wise enough to know that he is fallible and, therefore, ever ready to learn : great and honest enough to discard all mere pride of opinion and follow truth wherever it may lead : and courageous enough to acknowledge his errors'." There is, thus, no heroism in perpetuating an error in approach to a judicial exercise. The conclusions, even after the exercise of detailed analysis as discussed earlier is conducted, may or may not be the same as the coordinate benches have arrived, even if rather serendipitously, but that does not really matter. Once we realize that there was something lacking in our approach last time, there cannot be any justification in continuing to adopt the same approach yet again. It is, after all, one of the fundamental duties, under article 51A(h) of the Constitution of India, of every citizen to have, *inter alia*, the "spirit of inquiry of reform". It is in this backdrop, and without making any observations on correctness or otherwise of the conclusions arrived at by the coordinate benches, we deem it fit and proper to refer the additional grounds of appeal raised before us to a special bench of three or more Members.

11. Let the matter be placed before Hon'ble President for his kind consideration, and appropriate orders. In the meantime, as also prayed for by the learned counsel, the matter stands adjourned, and, in the light of this special bench reference, it stands adjourned *sine die*.

Sd/xx

Ravish Sood

(Judicial Member)

Mumbai, dated the 13th day of August, 2020

Sd/xx

Pramod Kumar

(Vice President)