BEFORE THE AUTHORITY FOR ADVANCE RULINGS

(INCOME TAX), NEW DELHI

28th November, 2011

PRESENT

Mr Justice P.K. Balasubramanyan (Chairman)

Mr. V.K. Shridhar (Member)

A.A.R. No.846 & 847 of 2009

Name & address of the applicant	:	**Groupe Industrial Marcel Dassault** 9, round point des champs Elysees Marcel Dassault 75008, France. **[In application No. AAR/846/2009]** **Merieux Alliance** 17, rue Bougelat 69002 Lyon France. **[In application No.AAR/847/2009]**
Commissioner Concerned	:	Director of Income-tax (International Taxation) Hyderabad
Present for the applicant	:	Mr. Porus Kaka, Sr. Advocate Mr. Manish Kanth, Advocate Mr. B.M. Singh, Advocate

Mr. Dominique Tazikawa Co.Rep.

Mr. Rohan Shah, Advocate

Mr. Rohit Jain, Advocate

Mr. Parth Contractor, C.A.

Mr. Kumar Visalaksh, Advocate

Present for the Department : Mr. Girish Dave, Advocate

Mr. Gangadhar Panda,
Addl. DIT (Int. Taxation), Hyderabad

R U L I N G

[By Justice P.K. Balasubramanyan)

Murieux Alliance, hereinafter referred to as **'MA'** is said to be a part of an International Health Care Group dedicated to prevention, diagnosis and treatment of infectious diseases. It is incorporated in France. It claims that after negotiations with Groupe Industrial Marcel Dassault, hereinafter referred to as **'GIMD'**, another company incorporated in France, it formed a wholly owned subsidiary in France on 31.10. 2006 named 'ShanH'. On 6.11.2006, MA entered into a share purchase agreement acquiring the shares of an Indian company, called 'Shantha Biotechnics Ltd, ('Shantha'). ShanH was shown as a permitted assign. 599630 shares were acquired. On 12.3.2007 GIMD came into the picture by acquiring 120000 shares amounting to 20% of the shares from MA in ShanH. Further capital increase of shares on 25.3.2009 were also taken by MA and GIMD in the same proportion. In May, 2009 Mr. Georges Hiborn acquired 10400 shares from MA and 2600 shares from GIMD. Due diligence of Shantha was got done by MA. MA claims that ShanH, through its representative, also actively participated in managerial and technical issues relating to the growth of Shantha. The shares in Shantha were acquired by ShanH or in the name of ShanH. Admittedly, the original capital flowed from MA and even the stamp duty was paid by MA though it is submitted that the amount spent in that behalf by MA was subsequently made good by ShanH. MA also appointed a director on the Board of ShanH. With a view to ensuring the achievement of better progress in business by Shantha, MA and GIMD felt that Shantha needed the backing and support of a leading global vaccine company. MA and GIMD started looking for a strategic alliance in relation to their larger interest in the field of immunotherapy in developing countries and also in relation to the activities of Shantha. A commercial transaction was evolved whereby Sanofi Pasteur Holding (hereinafter,'Sanofi'), another company incorporated in France, came forward to participate actively with MA and GIMD, provided the representatives of MA continued to be Members of the Board of Directors of ShanH having a say in the policies and approach to be pursed by ShanH. With a view to further improve the business and performance, MA and GIMD sold their shares in ShanH to Sanofi in August, 2009. On 20.11.2009, MA and GIMD filed applications before this Authority under section 245Q(1) of the Income-tax Act, 1961 (hereinafter referred to as 'the Act') seeking an advance ruling on the questions raised in the applications. The application filed by GIMD was numbered as Application No. 846 of 2009 and that filed by MA was numbered as Application No. 847 of 2009.

2. The approach by the two companies to this Authority was preceeded by certain steps taken by the Revenue. On 4.8.2009, a survey under section 133A of the Act was conducted in the office premises of Shantha. This was on the

basis of information that became available that Sanofi was proposing to acquire 80% of the stakes in Shantha from MA and GIMD through their subsidiary ShanH for a consideration of Rs.2,500 crores pursuant to a share purchase agreement executed by the concerned parties on 10.7.2009. The assessing officer on 7.8.2009 informed Sanofi about its likely obligation under section 195 of the Act arising out of the share purchase agreement. The details were called for. Another notice was issued on 24.8.2009. By replies dated 27.8.2009 and 3.9.2009, Sanofi intimated the Income-tax department that the share purchase agreement had a closure with effect from 31.7.2009. This was followed by the notice to show cause under section 195 of the Act issued by the assessing officer to Sanofi. Sanofi was asked to show cause why it should not be treated as an assessee in default under section 201(1) of the Act in respect of payments made by it to MA and GIMD for acquisition of the majority controlling interest in Shantha through the transfer of the shares of ShanH, the subsidiary of MA and GIMD. The department also requested MA and GIMD to provide related documents to enable the department to ascertain their liability to tax consequent on the share transfer. It is in the face of these proceedings that MA and GIMD approached this Authority for a ruling essentially on the question whether the sale of shares by them in ShanH to Sanofi is liable to be taxed in India. The questions formulated by MA in its application are:

(1) *In terms of the provisions of the double taxation avoidance treaty dated 6th September, 1994 as amended from time to time, entered between the Republic of India with the Government of French Republic ("Indo-French Tax Treaty") read with section 90 of the Income-tax Act, 1961, whether the Capital gains arising from the sale of shares of ShanH (French incorporated Entity) by the Applicant (French Incorporated Entity) to Sanofi (French Incorporated Entity) is liable to tax in France or in India?*

(2) *Without prejudice to the above, whether controlling interest (assuming while denying that it is a separate asset) is liable to be taxed in France under Article 14(6) of the Indo-French Tax Treaty?*

GIMD has raised only the first question indicated above, in its application.

3. To recapitulate the facts, MA a French company, possibly after arriving at an understanding with GIMD, another French company, decided to invest in Shantha by purchasing 80% of the shares of Shantha. With that in view while entering into an agreement with the sharesholders of Shantha for purchase of its shares, it got the due diligence of Shantha done, and also formed a 100% subsidiary, ShanH. The shares in Shantha were acquired in the name of ShanH or by ShanH. The consideration and stamp duty proceeded from MA. Thereafter, GIMD acquired 20% of the shares of ShanH from MA. Mr. Hebon also purchased some of the shares of ShanH. Thereafter, for business reasons, according to the applicants, they decided to sell their shares in ShanH to Sanofi. The case of MA and GIMD in a nutshell is that what was involved in the transaction of the two applicants selling their shares in ShanH to Sanofi, was only the sale of shares held in a French company and that had nothing to do with the shares of Shantha, the Indian company, the sale of which might or might not attract liability under the Indian Income-tax Act. MA and GIMD, therefore, claim that any attempt to tax in India the sale of shares of ShanH by them to Sanofi, was not sanctioned by the Income-tax Act and certainly not by the Double Taxation Avoidance Agreement (DTAA) between India and France. The essential contention of the Revenue, as we understand it, is that ShanH was only a front, a paper company, having no office and no employee. The Director of MA was also its director. What was involved in the alleged sale of shares of ShanH by MA and GIMD to Sanofi was the transfer of the assets of an Indian

company and certainly the controlling interest in the Indian company, Shantha. In reality, the sale of shares in ShanH held by MA and GIMD to Sanofi, attracted capital gains tax in India and the transaction was liable to be taxed in India. This stand of the Revenue is met by MA and GIMD by pointing out that the tax authorities in India could not ignore the incorporation of the Company ShanH, the Tax Residency Certificate produced and the recognition of the transaction even by the Government of India and proceed to tax what it calls the underlying transaction. In the light of the principle settled by the decision in *Azadi Bachao Andolan(263 ITR 706)*, there is no question of attempting to pierce the veil and attempting to go behind the existence of ShanH in the eye of law and ignoring the tax residency certificate issued to it by the French Authorities. It is pointed out that there was no treaty shopping or evasion of tax involved since the capital gain, if any, was taxable in France under the French law and all that was being sought for, was a ruling on the interpretation of the relevant article in the DTAA between India and France.

4. Facts in detail and the incidents relating to the transaction have been presented before us. The attempt of the Revenue was to persuade us to invoke the proviso to Section 245R(2) of the Act to find that what was involved was the devising of a scheme to avoid tax payable in India and in such a context, no ruling ought to be given by this Authority under section 245R(4) of the Act. The pendency of the proceedings under section 201 as against Sanofi was also put forward as a bar to the entertaining of this application. Originally, this Authority had admitted the applications on 17.12.2009 for giving a ruling under section 245R(4) of the Act on the basis that no valid objection in terms of Section 245R(2) of the act had been put forward. The Revenue came forward with an

application to have the question re-examined and this Authority re-examined the question and found no reason to change the position earlier adopted that there was no valid objection to the entertaining of the application for giving a ruling. But considering the persistence with which the Revenue questioned the original allowing of the application under section 245R(2) of the Act without actually hearing it, this Authority specified that the question of avoidance of tax and the bar created by the pendency of other proceedings under the Act, would be considered again while giving the ruling under section 245R(4) of the Act in terms of the order already passed under section 245R(2) of the Act. This Authority recorded in its order dated 3.8.2010, "Having been prima facie satisfied that there was no compelling reason to revoke the earlier order of admission and to refuse hearing on merits and that a comprehensive final order could be passed as regards the grounds made out for revoking the admission as well as on the merits, this case was posted for hearing on merits under section 245R(4) of the Act on the specified date." Not satisfied, the Revenue chose to challenge the order of this Authority in Writ Petition Nos. 18132 and 18133 of 2010 in the High Court of Andhra Pradesh. The original order challenged was the one allowing the application under section 245R(2) of the Act, without hearing the Revenue, since the Revenue had not appeared and later by amendment, the subsequent order on the application of the Revenue to re-consider the question, an order passed after hearing the Revenue. The Division Bench of the High Court considered the Writ Petitions. In the meanwhile, this Authority had listed the matter for final hearing to render the ruling under section 245R(4) of the Act. The hearing was spread over for days and was very elaborate. In view of the request made by the High Court of Andhra Pradesh to this Authority to withhold the ruling since they were entertaining the Writ Petitions against the orders under section 245R(2) of the Act and were to render a decision on the question whether the applications were rightly allowed under section 245R(2) of the Act or not, the ruling was withheld. Subsequently, the Division Bench heard the writ petitions finally. But the learned Judges differed in their conclusions – one of them taking the view that there was no warrant for interference with the order allowing the application under section 245R(2) of the Act, since the final ruling was yet to be rendered and this Authority had itself clarified that the question sought to be raised by the Revenue would again be considered while giving the final ruling. But the other learned Judge took the view that it was a question of jurisdiction of this Authority to entertain an application under section 245Q of the Act. Since according to him, there was violation of natural justice in that the Revenue was not given a proper opportunity of being heard, the orders of this Authority were liable to be quashed. A post decision hearing would not suffice and was not authorised since it was a question of jurisdiction. The Writ Petitions were then placed before a third Judge who found that there was no reason to interfere with the orders under section 245R(2) of the Act passed by this Authority. The learned Judge concluded that the Revenue had failed to substantiate an infringement of any legal right conferred on it under the Statute while allowing the application under section 245R(2) of the Act. Since the request not to render a ruling continued all this while, this Authority could not give a ruling under section 245R(4) of the Act. By the time, the path became clear for this Authority to give its ruling, one of the Members - Member(Law) - had retired and this resulted in the application having to be posted again for a hearing under Section 245R(4) of the Act. The parties took full advantage of that opportunity and re-argued the matter in detail. The ruling is being given after such fresh hearing.

5. Before proceeding to deal with the various contentions, it appears to be proper to observe that the object of creating this Authority for Advance Ruling is likely to be defeated if parties are given the opportunity to challenge the rulings either at the first stage or at the subsequent stage before High Courts. We may clarify that this has nothing to do with the composition of this Authority being presided over by a retired Judge of the Supreme Court. But permitting a challenge in the High Court would become counter productive since writ petitions are likely to be pending in High Courts for years and in the case of some High Courts, even in Letters Patent Appeals and then again in the Supreme Court. It appears to be appropriate to point out that considering the object of giving an advance ruling expeditiously, it would be consistent with the object sought to be achieved, if the Supreme Court were to entertain an application for Special Leave to appeal directly from a ruling of this Authority, preliminary or final, and render a decision thereon rather than leaving the parties to approach the High Courts for such a challenge. It is for the legislature to consider whether an appeal directly to the Supreme Court should not be provided against a ruling rendered by this Authority to ensure that the delay in procedure is minimised and the object of creating this Authority is achieved.

6. Persisting in its objection based on the proviso to section 245R(2) of the Act, in spite of the dismissal of the Writ Petitions by the High Court of Andhra Pradesh, but taking advantage of the observation of the Authority that the objection will be considered while giving a Ruling under section 245R(4) of the Act, the representative for the Revenue again reiterated before us the contention that the hearing of the applications and the giving of a ruling under section 245R(4) of the Act was barred by clause (i) of the proviso to Section 245R(2) of

the Act. He pointed out that in its second order rejecting the application made by the Revenue for reconsideration of the question this Authority had agreed to re-consider the question while giving the ruling under section 245R(4) of the Act. Counsel for the applicant submitted that the High Court of Andhra Pradesh having dismissed the writ petition challenging the order of this Authority allowing the application under section 245R(2) of the Act, there remained nothing for the Revenue to contend on this objection. There may be some force in the submission of learned Senior counsel for the applicant. But, in view of this Authority leaving open that question for consideration afresh in its second order and an objection based on clause (iii) of the proviso is not necessarily confined to the stage of a hearing under section 245R(2) of the Act, we think it appropriate to deal with the question.

7. What is contended on behalf of the Revenue is that the issue regarding taxability of the transaction is being examined by the DDI(IT), Hyderabad, during the course of the proceedings against Sanofi under section 201 of the Act. He submitted that an order dated 25.5.2010 was passed overruling the contentions of Sanofi and treating it as an assessee in default in respect of the payments made by it for purchasing the shares of ShanH. A proceeding has also been taken against ShanH relating to the transaction. The Revenue, therefore, submitted that the hearing of the application was squarely barred by clause (i) of the proviso to Section 245R(2) of the Act.

8. This Authority has consistently taken the view that the initiation of proceedings under section 195 or 197 of the Act and even a final order passed

therein, would not create a bar to entertaining an application for advance ruling. This was based on the scope and object of enacting Section 195 of the Act. The Supreme Court has also indicated the scheme of and the nature of the proceedings under section 195 of the Act. [See Transmission Corporation of Andhra Pradesh v. CIT (239 ITR 587) and GE Indian Technology Centre P. Ltd. v. CIT (327 ITR 456)].

9. The proceedings under section 201 of the Act is a consequence of the failure to comply with the requirement of Section 195 of the Act. Even earlier, this Authority had noticed that such a proceeding cannot stand in the way of an application being considered for a ruling under section 245R(4) of the Act. We do not find any reason to depart from that position adopted by this Authority earlier. If so, the pendency of the proceedings or the order passed under section 201 of the Act against Sanofi cannot stand in way of our proceeding to give a ruling. The main thrust of the argument in the earlier round on alleged violation of natural justice, stands concluded by the decision of the Andhra Pradesh High Court. Even otherwise it has lost its steam since all the facts are now before this Authority at the instance of the Revenue and we are in a position to render a satisfactory decision on the bar claimed to have been created by of the proviso to Section 245R(2) of the Act. Suffice it to say, we overrule the objection of the Revenue that giving of a ruling under section 245R(4) of the Act was barred by clause (i) in the proviso to Section 245R(2) of the Act.

10. Counsel for the applicants contended that having initiated proceedings against Sanofi on the purchase of the shares of ShanH by it and also against ShanH based on the sale, the Revenue was not entitled to question the transfer

of shares of ShanH by its shareholders to Sanofi or the reality of that transaction or take up the theme of tax avoidance. The representative for the Revenue submitted that adequate facts were not disclosed by the applicants and could not be gathered by the Revenue at the time of initiation of proceedings against Sanofi and ShanH and now that the facts are clear, this Authority has to consider the nature of the transaction and the effect of the transaction in the context of the ruling sought for. The proceeding against ShanH is also under section 201 of the Act. We do not think that it would be proper for us to decline to consider the rival claims in the context of these applications based on the effect of the proceedings initiated against Sanofi and/or ShanH canvassed for by Counsel for the applicant. As we have noticed, the nature of the proceedings based on section 195 of the Act, is not conclusive and is only preliminary in nature. It cannot stand in the way of our considering this objection also even while we consider the main application for a ruling.

11. We may here notice the ruling of this Authority in Canaro Reources Ltd. (313 ITR 2) relied on. Therein an objection based on clause (iii) of the proviso to Section 245R(2) of the Act was not taken when the application was being allowed under section 245R(2) of the Act for giving a Ruling. But at the hearing under Section 245R(4) of the Act, the objection was taken. The applicant objected to the question being considered. This Authority overruled that plea on the basis that it was an objection "pertaining to the maintainability of the application". Subsequently in ABC In re (AAR No.840/2010), this Authority has indicated that the consideration of such an objection at the stage of hearing under Section 245R(4) of the Act was not taboo and had to be dealt with on

merits. It is really an objection to the jurisdiction to give a ruling. We cannot keep out a consideration of the objection and clutch at a jurisdiction; we may or may not have. We, therefore, proceed to consider the objection that the transaction is designed to avoid tax in India.

12. Before doing so, we have to notice the argument of counsel for the applicant that the stand of the applicants was only that the transaction was taxable in France and not in India in terms of the DTAA and that no avoidance of tax was involved. What this Authority is entrusted with, is a jurisdiction to rule in advance, whether a transaction is taxable in India, going by the Act or the overriding DTAA. Therefore, the question of avoidance of tax that has to be considered is the avoidance, if any, of the tax in India. Therefore, the argument on behalf of the applicants that tax on this transaction has to be paid in France where the companies involved were incorporated and of which they were tax residents and hence no avoidance of tax was involved, even if acceptable to the extent it goes, cannot stand in the way of this Authority considering whether designing of a scheme for avoidance of payment of tax in India has been resorted to. Hence, this aspect raised by the Revenue has to be considered.

13. On behalf of the Revenue, it was submitted that the prior transactions leading to the present transaction relied upon by the applicants were only transactions on paper and it was part of an elaborate scheme to avoid tax in India. The Revenue submits that ShanH was created merely for the purpose of dealing with the assets of Shantha and its creation was merely to avoid the tax that may be due while dealing with the shares of Shantha. Counsel for the

Revenue submitted that on 6.11.2006, MA had entered into an agreement for purchase of the shares of Shantha. It was MA that got the due diligence done. Though it is claimed that ShanH was formed as a 100% subsidiary of MA on 31.10.2006, it was not ShanH that entered into the share purchase agreement on 6.11.2006. ShanH had no office, no staff and the director of MA was also its director. Only in March, 2007, GIMD came into the picture by acquiring 20% shares in ShanH. Subsequently one Mr. Hebon also acquired some shares in Shan H. ShanH had no other business and it held no assets other than the shares in Shantha. The Revenue, therefore, submits that ShanH was merely a front created for avoiding the liability to tax that may arise on dealing with the shares of Shantha by MA which still held the controlling interest in Shantha through ShanH. What was now being done was to sell the shares of ShanH to Sanofi virtually handing over the assets and control of Shantha. It is also pointed out that MA assumed the right to nominate the Members of the Board of Shantha and the entire transaction now put forward was a clear attempt to avoid tax by way of capital gains. Even on a *prima facie* scrutiny, this was clear and hence the objection that the giving of a ruling under section 245R(4) was barred by clause (iii) of the proviso to sub-section (2) of Section 245R of the Act, was liable to be upheld.

14. On behalf of the applicant it is submitted that the setting up of a subsidiary company for making fresh acquisitions was a legal, permissible and known method of business and there was nothing illegal in MA and GIMD forming a subsidiary ShanH for the purpose of acquiring shares in Shantha. He submitted that ShanH had three shareholders including the two applicants and

the shares of ShanH are now acquired by Sanofi. ShanH being a French company and a tax resident of France was entitled to claim the protection of the DTAA between India and France. What was involved was the transfer of shares of Shan H held by the two applicants to another French company Sanofi and the capital gains, if any, arising out of the transaction to the applicants, was taxable in France. This was not a case of an attempt to avoid the payment of tax. This was not a case of treaty shopping. The tax had to be paid in France in terms of the DTAA and as a matter of fact, the tax payable would be more in France since treatment of long term capital gains in France was to the disadvantage of the applicants, where shares had to be held for two years before sale, for qualifying as long term capital gains whereas it was only one year in India. All the companies were within the tax jurisdiction of France and the transaction was taxable in France. By virtue of Article 13 of the India-France treaty, the power to tax rested with France and not with India. The applicants were only claiming the benefit of a Treaty, and were not attempting to avoid tax. The argument that what was really being transferred, were the assets of Shantha, the Indian company, had no substance. The shares of Shantha were not being dealt with, though the consequence of the buying of shares of ShanH by Sanofi might be to give control of the affairs of Shantha to Sanofi. But then, it was a legal and legitimate business route taken by the applicants and the transaction did not attract taxability as capital gains in India.

15. Counsel for the applicant submitted that in the light of the decision of the Supreme Court in *Azadi Bachao Andolan*[1], there was no question of going

[1] 263 ITR 706

behind the transaction to ascertain its so-called real nature especially in cases governed by agreements for avoidance of double taxation. Here, the applicants were claiming the benefit of DTAA between India and France to be taxed in France. He also submitted that Tax Residency Certificates have been produced and it was not open to the Revenue or this Authority to go behind them in the light of the position settled in *Azadi Bachao Andolan.* It was also not open to ignore the existence of properly incorporated companies under relevant laws of the country to which the parties belonged. There is no substance in the contention raised by the Revenue in the light of the decision in *Azadi Bachao Andolan.*

16. We may straightaway notice, that the decision in Azadi Bachao Andolan, obviously binding on this Authority, may not be the final word in a given situation, when this Authority is approached for an advance ruling. The proviso to Section 245R(2) of the Act mandates that this Authority shall not allow the application for pronouncing a ruling where the question raised in the application relates to a transaction or issue which is designed, *prime facie*, for the avoidance of income-tax. This obviously means that this Authority has to decline jurisdiction when it finds that the ruling sought for relates to a transaction which is designed *prime facie* for the avoidance of income-tax. In considering that question what this Authority is doing is not piercing the veil of the corporate entity, but is only asking itself the question whether there was a step taken or a series of steps taken, that may have business purpose but was clearly a device to avoid the liability to tax and look at the transaction within the confines of the proviso.

17. We also find some difficulty in accepting the arguments based on Azadi Bachao Andolan. Azadi Bachao Andolan was inter alia considering the effect of the ratio of the earlier constitution bench decision of the Supreme Court in McDowell and Co. Ltd. v. Commercial Tax Officer (154 ITR 148). One of the main aspects involved was whether a tax avoidance scheme or attempt at avoidance of tax was liable to be accepted by the Court once it was shown that it was not an objectionable evasion. Four of the learned judges speaking through Ranganath Misra J. are seen to have left it to the other learned judge, Chinnappa Reddy, J. to deal with this aspect. The four learned judges referred to some of the earlier decisions on the subject and did observe:

> "The planning may be legitimate provided it is within the frame work of law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges."

But, they did not stop there. They proceeded to say:

> "On this aspect, one of us, Chinnappa Reddy, J. has proposed a separate and detailed opinion <u>with which we agree</u>" **[emphasis supplied].**

18. With respect, Azadi Bachao Andolan seems to proceed on the basis that the views expressed by Chinnappa Reddy, J. are his own and do not represent the view of the Court as a whole. This, with respect, does not appear to be correct. An analysis of the Ramasay principle as discussed and adopted in later decisions of the House of Lords show that much water had flowed under the bridge since IRC v. Duke of Westminister was rendered. In IRC v. Burmah Oil

Company Ltd [1982 STC 30(HL)] Lord Diplock stated that no one can assume that Ramasay did not mark a significant change in the approach adopted by the House of Lords in its judicial role into preordained transactions (whether or not they include the achievement of a legitimate commercial end) into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax; which in the absence of those particular steps would have been payable. The learned Law Lord continued, "The difference is in approach. It does not necessitate the overruling of any earlier decisions of this House; but it does involve recognizing that Lord Tomlin's oft quoted dictum in IRC v. Duke of Westminister, 'Everyman is entitled, if he can, to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be,' tells us little or nothing as to what methods of ordering one's affairs will be recognized by the courts as effective to lessen the tax that would attach to them if business transactions were conducted in a straight forward way." Furniss v. Dawson [(1984) AC 474] took the concept forward followed by Ensign Tankers [(1992) 2 WLR 469 HL] and Moodi (1993) 1 WLR 266 HL. An attempt was made to confine the operation of the doctrine in Cravan V. White [(1988) 3 WLR 423 HL] by the majority therein, and some decisions that followed it. But, recently in HMRC v. Tower MCashback LLC [(2011 UK SC 19] the Supreme Court of England has reiterated and applied the Ramasay principle to find a transaction found to be genuine to be part of a tax avoidance scheme to deny the full relief to the assessee therein. As we understand it, the view that has emerged is that notwithstanding the legal validity of a transaction or a set of transactions, if the purpose was to create a legal smoke screen to avoid the payment of tax that would legitimately be due as having arisen on the basis of a transaction or an event, the legal effect of the transaction in the context of the taxing statute, has to be considered, notwithstanding its reality or validity. As observed by Lord Hoffman in Macniven v. Westmoreland Investments [(2001) UKHL 6], “The point to hold on to is that something may be real for one purpose, but not for another.”

19. What is it that is happening in this case? A company in France, invests in acquiring shares in an Indian company. Ultimately it acquires a controlling interest. For this purpose, it creates a fully owned subsidiary. The shares are taken in the name of the subsidiary. Subsequently, another company also comes in and acquires a part of the shares (20%) in the subsidiary. The only asset of the subsidiary is the shares in the Indian company. It has no other business. Now the two shareholders of the subsidiary are selling the shares of the subsidiary to another company. By that process, what really passes is the underlying assets and the control of the Indian company. A gain is generated by this transaction. By repeating the process, the control over the Indian assets and business can pass from hand to hand without incurring any liability to tax in India, if the transaction is accepted at face value.

20. This type of attempt is what is frowned upon by the McDowell decision. This is the line of reasoning adopted by the English Courts in Ramasay and the subsequent decisions. The payment of tax on capital gains over the shares of Shantha can be perpetually avoided by dealing with the shares of ShanH earlier with MA and GIMD, but now with Sanofi, but passing effective control over the assets and the business of Shantha. It is the adoption of such devices that is not accepted at face value by courts and treated as ineffectual for the purpose of averting payment of tax due under the statute.

21. It is argued on behalf of the applicant that what is taxed by the taxing statute is the gain arising out of the sale of the shares of an Indian company and that taxing event has not taken place. He also submitted that the concept of underlying assets and controlling interest are not concepts that can come into reckoning while interpreting the taxing statute. A taxing statute is to be construed strictly and nothing is to be added or subtracted. Nor can it be interpreted in such a manner that transactions not directly hit by it, are also roped in based on presumed intention or purpose. Counsel for the Revenue submitted that what we are concerned with, is to see whether there is an attempt to avoid payment of tax in India for declining a ruling and in arriving at that conclusion, nothing is being added to or subtracted from the section. Section 9 of the Income-tax Act and the DTAA permit a see through of the transaction to ascertain its true purpose and that is all that is needed to be done in this case.

22. The whole endeavour on the side of the applicants was to show that the coming into being and existence of ShanH as a commercial and corporate entity cannot be ignored. It is emphasized that ShanH is the shareholder in Shantha, that in the books of account of ShanH, the investment originally made in the purchase of shares of Shantha is shown as a loan from MA, that the stamp duty has also been accounted for by ShanH, that the French Tax Authorities and the Indian authorities have accepted the existence of ShanH as the investor in Shantha and that the legal and valid existence of ShanH cannot be ignored. It is not necessary to ignore the existence of ShanH to come to a conclusion that what is put up is a facade in the context of the tax law and would amount to a scheme for avoidance of tax. In that view, the fact that GIMD and George Hiborn held shares in ShanH would not make a difference.

23. The legal validity of a transaction or the adoption of a series of transactions commonly used, like creating a fully owned subsidiary for making such investments in another country, cannot stand in the way of the question being asked whether it is acceptable in the context of the taxing statute. When we ask ourselves that question in this case, we get the answer that by accepting it in the context of the taxing statute we would be opening the door for the passing of the assets and control of an Indian company repeatedly without the shares of the Indian company being touched, though in reality it is only by acquiring shares of the Indian company, that control over it and its assets can otherwise be acquired. When dealing with such a question we cannot ignore the aspects of underlying assets and control over the affairs of the company, passing from one hand to another.

24. When can an usually adopted business scheme be treated as an attempt at avoidance of tax liable to be not accepted by the tax regime? It appears to us that it will depend on the effect of the scheme as a whole on the liability of the entity to be taxed. In this case, a permissible commercial scheme has been adopted to acquire the shares, the underlying assets and control of an Indian company. But thereafter, in the guise of dealing with the shares of a subsidiary formed for such acquisition, the underlying assets, business and control of an Indian company is passed from one hand to another. By repeating this process, without touching the shares of the Indian company, the right and dominant control over its assets and business can pass from hand to hand. On a look at the series of transactions from the commencement of the formation of ShanH, it appears to us to be a pre-ordained scheme to produce a given result, viz., to deal

with the assets and control of Shantha without actually dealing with the shares of Shantha or its assets and business. This scheme adopted, has to be seen as one for avoiding payment of capital gains which would otherwise arise if the shares of the Indian company had been transferred, leading to the same result as now achieved. We are satisfied that a scheme of the nature cannot be accepted simply for the reason that "upon the true construction of the Statute, the transaction which was designed to avoid the charge to tax, actually comes within it." [See Norglen Ltd. v. Reeds Rains Prudential Ltd. [1999 2 AC 1 at 14).

25. It is pointed out that ShanH would continue to exist inspite of the sale of shares in it by the applicants to Sanofi. The question may also arise as to what would happen if Sanofi were to sell the shares of ShanH, it has acquired, to another. We do not consider it proper to go into that question since our ruling is invited only on the transaction involved herein, namely, transfer of the shares of ShanH by MA and GIMD to Sanofi. Our ruling can only relate to that transaction on the scheme of the Act. May be, a subsequent transaction by Sanofi of the shares in ShanH may have to be considered based on all the facts then available including the assets and line of business then held by ShanH and the reasons put forward in support of that transaction.

26. We are, therefore, of the view that the transaction involved is not one to be taken at face value by the Taxing Statute since it is one intended to avoid payment of tax on capital gains in India. The questions posed have to be answered in this context.

27. The object of the Double Taxation Avoidance Convention between India and France is not only to avoid double taxation but also to prevent fiscal evasion with respect to taxes on Income and capital. This is clear from the preamble to the convention itself. The said preamble reads:

> "The Government of the Republic of India and Government of the French Republic, desiring to conclude a convention for avoidance of double taxation and the <u>prevention of fiscal evasion with respect to taxes on Income and capital</u>".**(emphasis supplied)**.

Have agreed to its terms: To test whether a scheme adopted is with the object of avoidance of tax which would have been otherwise payable an enquiry in that behalf is contemplated by the very tax convention relied on by the applicant. This is in addition to the power available to this Tribunal under the proviso to Section 245R(2) of the Act and the law settled by courts in decisions like the one in McDowell. Therefore, when a plea of attempt at tax avoidance is raised by the Revenue in a proceeding before this Authority for a Ruling on the question of liability to tax of an applicant in respect of a transaction, an enquiry in that behalf cannot be avoided. This can be done even while we consider the application under section 245R(4) of the Act, when all the facts relevant, are available before us or ought to be made available to us.

28. It is the case of the applicant that the transaction in question is governed by Article 14 of the DTAA. Under Article 14.5 gains from alienation of shares representing a participation of atleast 10% in a company which is a resident of France, may be taxed in France. It is the contention that the capital gain arising

out of the sale of the shares of ShanH in France, can be taxed only in France. It is pointed out that neither the applicants nor Sanofi are tax residents of India.

29. On behalf of the Revenue, it is reiterated that what is really sold is the property and the controlling interest in Shantha and so considered, the capital gains arising out of the sale of shares is liable to be taxed in India. The whole case of the Revenue depends upon the plea that what is really being dealt with by virtue of the transaction in question is the underlying assets, business and controlling interest of an Indian company and consequently, any transfer for a consideration giving rising to a gain could be taxed in India. The further argument is that the payments made by Sanofi for the purchase to the shares of the applicants is for acquisition of control and management and other bundle of rights in Shantha and consequently, the transaction would give rise to capital gains in India, as Shantha is a company incorporated in India and located in India. The transfer of shares of ShanH would amount to the transfer of the assets of Shantha, if not of its shares formally.

30. In view of our conclusion that the transaction must not be taken at face value since it amounts to a scheme for avoidance of tax in India, the logical stand this Authority has to adopt on the scheme of the Act is to decline a ruling on the questions posed for our ruling. Therefore, invoking the ratio of the decision of the Supreme Court in McDowell and in the light of clause (iii) of the proviso to Section 245R(2) of the Act, we decline to rule on the questions raised.

31. This Authority had allowed the application under Section 245R(2) of the Act but had clarified that the bar created by Section 245R(2) of the Act will be reconsidered while giving a ruling under section 245R(4) of the Act. This

behaves us to consider the questions on merits and to give rulings on them. A ruling is also necessary for a completion of this proceeding and to avoid a remit of this matter to this Authority, in case, on the question of tax avoidance, the Supreme Court were to disagree with our conclusion. It will be unjust to leave open the question raised and argued.

32. The primary and common question raised in these applications is whether the capital gains arising to the applicants from the sale of their shares in ShanH to Sanofi, another company incorporated in France is taxable in France alone or in India. Looked at blandly, the transaction in the manner put through, is taxable in France. We have earlier concluded that the fact that the transactions are commercially real and taken step by step valid, does not preclude us from considering the scheme or the scope of the transaction as a whole from the point of view of taxation and so looked at, it is a scheme for avoidance of tax in India. We have held that what is involved is a preordained scheme for avoidance of tax and it cannot be given effect to in the context of the taxing statute. In substance, what is dealt with are the underlying assets and the controlling interest in Shantha, a consequence that would naturally spring out of the sale of shares of Shantha itself. The transfer of shares of ShanH may have commercial and business efficacy or validity. But that does not prevent us from looking at the transaction in the context of the Income-tax Act and/or the DTAA between the countries and assessing its efficacy from the point of view of taxation.

33. Article 14 of the Convention between India and France deals with capital gains. It is the case of the applicants that paragraph 5 of the said Article is attracted and since the shares being sold are of a company incorporated in

France, which is a tax resident of France, to another tax resident of France, the gain therefrom is taxable in France. Article 14.5 reads:

> "5. Gains from the alienation of shares other than those mentioned in paragraph 4 representing a participation of atleast 10 per cent in a company which is a resident of a contracting state may be taxed in that contracting state."

It is the contention that ShanH, the shares of which are being sold is a company incorporated in France in which the applicants have a participation above 10 per cent and since the gains is that of a resident of France, it is liable to be taxed only in France. It is contended that unlike paragraph 1 of Article 14 relating to immoveable property, paragraph 5 does not permit a see through and the transaction has to be accepted as it is. The fact that the asset is located in another country is irrelevant. The option to provide for a 'see through' has not been exercised while entering into the Treaty with France.

34. Alternatively, it is submitted that even if paragraph 5 is held to be not applicable to bring about the above result, in terms of paragraph 6 of the Convention, the transaction is taxable only in France. Article 14.6 reads:

> "6. Gains from the alienation of any property other than that mentioned in paragraphs 1, 2, 4 and 5 shall be taxable only in the contracting state of which the alienator is a resident."

It is submitted that the applicants, the alienators are resident of France and going by paragraph 6 of Article 14, the transaction would be taxable in France. By no stretch of imagination can the alienator be deemed to be a resident of India.

35. On behalf of the Revenue, it is submitted that alienation is a word of wide import and read with the words participation of atleast 10 per cent in a company, it would mean that conveying of such rights of participation would also attract tax in India, if the interest of participation is of an Indian company. It is submitted that transfer of the right of participation in an Indian company even by a non-resident, outside India which allows the transfer of participation interest in an Indian company would be taxable in India as per paragraph 5 of Article 14 of the Convention. Participation in a company, according to the Revenue would mean, the right to vote, the right to nominate Directors, control and management, day to day decision making and right to get distribution of profits. It is submitted that all these rights in respect of the Indian company, Shantha are with MA or with MA and GIMD, the applicants and hence the transfer now being effected is taxable in India in terms of paragraph 5 of Article 14.

36. It is true that a Double Taxation Avoidance Convention has to be construed on its terms. On a literal construction paragraph 5 would lead to the position that the transfer of shares of ShanH in this case, can be taxed only in France. But the contention of the Revenue is that the situs of the underlying assets cannot be ignored and the underlying assets and controlling interest are that of a company incorporated in India and a resident of India. We have found that what is involved in this transaction, is an alienation of the assets and controlling interest of an Indian company. It will logically follow from our finding that the transactions gone through are part of a scheme for avoidance of tax and the scheme has to be ignored, that the gain from the transaction is taxable in India. Even then, it is not an alienation of the shares of an Indian company, on a

literal interpretation of paragraph 5 of Article 14 of the treaty. But a purposive construction of the said paragraph of the treaty leads us to the conclusion that the capital gains arising out of the transaction is taxable in India. The essence of the transaction takes within its sweep various rights including a change in the controlling interest of an Indian company having assets, business and income in India.

37. We, therefore, rule on question no. 1 in the application by MA and on the question in the application by GIMD, that the transactions of sale of shares by them in ShanH to Sanofi are taxable in India in terms of paragraph 5 of Article 14 of the Double Taxation Avoidance Convention between India and France.

38. This ruling is obviously without prejudice to the right, if any, of the applicants to the benefits, if any, available to them under Article 25.2 of the DTAA.

39. Since we have ruled on question no.1 that the transaction is liable to be taxed in India in terms of Article 14.5 of the DTAA, the second question posed in application No. 847 of 2009 filed by MA does not arise. Article 14.6 has application only if Article 14.5 has no application. Hence, we are not inclined to consider the question whether controlling interest is an asset that would be taxable in France under Article 14.6 of the Treaty.

40. Accordingly, the ruling is pronounced on this 28th day of November, 2011.

(V.K. Shridhar) **(P.K. Balasubramanyan)**

Member **Chairman**