IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "L", MUMBAI

Before Shri I.P. Bansal, Judicial Member
& Shri P.M.Jagtap, Accountant Member.

I.T.A. No.2311/Mum/2007
Assessment Year : 2003-04.

Asstt. Director of Income-tax, (International Taxation)-3(2), Mumbai.	**Vs.**	M/s Mediterranean Shipping Co.,S.A., C/o MSC Agency India Pvt. Ltd., Vakil House, 3rd Floor, 18 Sprott Road, Ballard Estate, Mumbai – 400 038. PAN AABCM3905A.
Appellant.		**Respondent**.

C.O. No. 171/Mum/2007
(In ITA No. 2311/Mum/2007)
Assessment Year : 2003-04

M/s Mediterranean Shipping Co.,S.A., Mumbai.	**Vs.**	Asstt. Director of Income-tax, (International Taxation)-3(2), Mumbai.
(Cross Objector)		**Respondent.**

Department by : Shri G.C. Srivastava.
Assessee by : Shri S.E. Dastur &
Shri Nishant Thakkar.
Date of hearing : 07-09-2012
Date of pronouncement : 06-11-2012.

O R D E R

Per P.M. Jagtap, A.M. :

This appeal is preferred by the Revenue against the order of learned CIT(Appeals)-XXXIII, Mumbai dated 29-12-2006 and the same is being disposed of along with the cross objection filed by the assessee.

2. The solitary issue arising out of the appeal filed by the Revenue as well as the cross objection filed by the assessee is relating to the taxability of the profits from operation of ships in international traffic earned by the assessee (also referred to as "international shipping profits") in India.

3. The assessee in the present case is a Company incorporated in Jineva (Switzerland). It is engaged in the business of operations of ships in international waters through chartered ships. During the year under consideration, the assessee had total collection of freight amounting to Rs.295.63 crores on account of exports/imports on which a sum of Rs.9.33 crores was paid towards the tax liability. In the return of income filed for the year under consideration on 28th November, 2003, the assessee, however, declared total income at Nil on the grounds as stated in the note attached with the said return that there was no article in the Indo-Swiss treaty dealing specifically with taxability of shipping profit, that article 7 of the said treaty dealing with business profits specifically excluded profits from the operation of ships in international traffic and that article 22 of the said treaty dealing with other income subjected to tax shipping profits only in the State of residence viz. Swiss confederation in its case. The stand of the assessee thus was that the international shipping profit was not taxable in India and the entire tax of Rs.9.33 crores paid was liable to be refunded. This stand of the assessee was not found acceptable by the AO in view of the CBDT Circular No. 333 dated 02-04-1982 whereby it was clarified that where there is no specific provision in the agreement, it is the basic law i.e. the Income Tax Act which will govern the taxation of income. According to the AO, the shipping profits of the assessee company, therefore, were taxable in India u/s 44B of the Income-tax Act, 1961 which provided that not-with-standing any thing to the contrary contained in section 28 to 43A, in the case of an assessee, being a non resident engaged in the business of operation of ships, a sum equal to 7½% of the aggregate of the amounts specified in sub-section (2) shall be deemed to be the profits and gains of such business chargeable to tax under the head “Profits & Gains of business or profession”. In this regard, the assessee relied on the CBDT’s letter

dated 18-12-2003 addressed to Swiss Federal Tax Administration clarifying that the profits from operation of ships in international traffic is governed by the provisions of article 22 of the Double Taxation Avoidance Agreement. The assessee also brought to the notice of the AO that in the assessment completed in its own case for assessment year 2002-03 vide an order dated 09-03-2004 passed u/s 143(3), it was held that the profits from operations of ships in international traffic are not taxable in India as per article 22 of the DTAA. The AO did not accept this contention of the assessee relying on the letter dated 14-02-2005 issued by the Joint Secretary (FT & TR)-1,CBDT, New Delhi clarifying that the profits from operations of ships in international traffic is taxable only in accordance with the domestic law i.e. as per the provisions of section 44B of the Income-tax Act, 1961. He held that article 22 of the DTAA between India and Switzerland thus was not applicable in the assessee's case and in the absence of any specific article in the treaty dealing with taxability of international shipping profits, the said profits of the assessee were taxable in India u/s 44B of the Income-tax Act, 1961.

4. In the case of the assessee, certain information was forwarded by ACIT, Central Circle-40, Mumbai to the AO vide letter dated 21-03-2005, gist of which is as under :

> "(i) M/s Samsara Shipping Private Limited is the shipping agent for the two multinational companies namely, M/s Mediterranean Shipping Co. S.A., Switzerland and M/s orient Shipping Services, L.L.C. Dubai. Though the assessee is agent for two shipping companies, the most of the business is done for M/s Mediterranean Shipping Co. S.A.
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> (ii) From the balance sheet of M/s Samasara Shipping Private Ltd., from F.Y. 1996-97 to 2002-03, it can be seen that M/s Samsara Shipping Private Ltd. is showing sundry creditors which include the liability of Rs.9,66,53,645/- towards the principals, M/s Mediterranean Shipping Co. S.A.
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> (iii) The A.O. during the course of block assessment proceedings in the case of M/s Samasara Shipping Co. P. Ltd. has observed that it is an agent but not an independent agent of M/s Mediterranean Shipping Corporation in view of the information gathered by him.

(iv) It is seen from the return of income for A.Y. 2003-04 that M/s Samsara Shipping Pvt. Ltd. has stopped showing agency income from M/s Mediterranean Shipping Corporation S.A. M/s Mediterranean Shipping Corporation has appointed another agent namely, M/s MSC Agency India Pvt. Ltd. as their agents.

(v) It is seen from the return of income for AY 2003-04 of M/s Samsara Shipping Pvt. Ltd. and M/s MSC Agency India Pvt. Ltd., that most of the branches, which were being operated by M/s Samsara Shipping Pvt. Ltd. are transferred to M/s MSC Agency (India) Pvt. Ltd.

(vi) From the return of income and the details filed by the Samsara Shipping Pvt. Ltd.. it is seen that all the assets inclusive of furniture & fixture, computers electrical installation and vehicles are transferred from M/s Samsara Shipping Pvt. Ltd. to M/s MSC Agency India Pvt. Ltd.

(vii) From the return of income of M/s Samsara Shipping Pvt. Ltd. for the A.Y. 2002-03, it is seen that they have recruited 204 new employees during the year and the salary expenditure has been increased by more than 50%. From the return of income for A.Y. 2003-04 of M/s Samsara Shipping Pvt. Ltd. and the YDS Return of M/s MSC Agency (I) Ltd., it is seen that 122 employees have resigned from M/s Samsara Shipping Pvt. Ltd. and joined M/s MSC Agency (I) Pvt. Ltd.

(viii) Since the entire business of M/s Samsara Shipping Pvt. Ltd. has been taken over by M/s MSC Agency India Pvt. Ltd., it has been observed by the A.O. that M/s Samsara Shipping Pvt. Ltd. is not an independent agent of M/s Mediterranean shipping Corporation S.A.

(ix) From the above facts it appears that M/s Mediterranean Shipping Co., S.A. was managing and controlling their business operations in India through M/s Samsara Shipping Pvt. Ltd. from A.Y. 1998-99 to A.Y. 2002-03 and thereafter through M/s MSC Agency India Pvt. Ltd. From the information gathered by the A.O. it appears that the nature of relation between the two partakes the character of a Permanent Establishment.

(x) As per the Article 11 of the DTAA with Switzerland, the interest income earned by M/s Samsara Shipping Pvt. Ltd. from the funds of M/s Mediterranean Shipping Co. S.A. is taxable in the hands of M/s Mediterranean Shipping Co. S.A.

(xi) It is noteworthy to mention here that M/s Mediterranean Shipping Co. S.A. has drastically reduced the commission income of M/s Samsara Shipping Pvt. Ltd. w.e.f. 01-04-2001 without giving any reasons. This development shows that M/s Samsara Shipping Pvt. Ltd. has no say in the matters of income to be earned by them for the services rendered by them of dependent nature.

(xii) They have no control over the Management, Finances and Administration of their Company. Therefore, it becomes permanent establishment of M/s Mediterranean Shipping Co., S.A. of Switzerland."

The above information received by him was confronted by the AO to the assessee and the assessee was called upon to explain as to why M/s MSC Agency India P. Ltd. should not be treated as its permanent establishment in India. In reply, it was submitted by the assessee that both M/s Sansara Shipping P. Ltd. and M/s MSC Agency India P. Ltd. were independent agents and did not constitute its PE in India as per Article 5 of the treaty. This submission of the assessee was not found acceptable by the AO keeping in view the relevant clauses of the agreement dated 01-04-2002 entered into by the assessee with M/s MSC Agency India P. Ltd.. According to the AO, the said clauses made it very clear that M/s MSC Agency India P. Ltd. was legally and economically dependent agent of the assessee company inasmuch as the assessee company was managing and controlling their business operations in India through M/s MSC Agency India P. Ltd.. He, therefore, held that M/s MSC Agency India P. Ltd. constituted a permanent establishment of the assessee company in India as per Article 5(5) of the DTAA between India and Switzerland. He also held in this regard that M/s MSC Agency India P. Ltd. was carrying on the activities wholly and exclusively for the assessee company and it was merely a projection of the assessee company on the soil of India. Having held that M/s MSC Agency India P. Ltd. constituted a permanent establishment of the assessee company in India, the AO held that the shipping profits earned by the assessee company through the said PE were taxable in India u/s 44B of the Income-tax Act, 1961. Accordingly, such profits calculated at Rs.22.17 crores being 7.5% of the total collection of freight of Rs.295.63 crores was brought to tax in India by the AO in the hands of the assessee in the assessment completed u/s 143(3) vide an order dated 29-03-2006.

5. Against the order passed by the AO u/s 143(3), an appeal was preferred by the assessee before the learned CIT(Appeals) and elaborate submissions were made on its behalf before the learned CIT(Appeals) in support of the case that international shipping

profits being governed by the Article 22 of the Tax Treaty were liable to tax only in Switzerland and not in India. As regards the reliance placed by the AO on the letter dated 14-02-2005 issued by the Joint Secretary (FT & TR) of Government of India, the assessee brought to the notice of the learned CIT(Appeals) another letter written by the Joint Secretary to the DGIT (International Taxation) on 27-05-2005 wherein reference was made to the two letters dated 10th December, 2003 and 18th December, 2003 issued by his predecessor in the matter for necessary action. In the letter dated 18-12-2003, the Indian Competent Authority had accepted that only Article 22 will be applicable with regard to international shipping profits and according to the assessee, even the successor competent authority agreed with that position in his letter dated 27-05-2005 by making a reference to the letter dated 18-12-2003 for necessary action. The assessee also brought to the notice of the learned CIT(Appeals) that in the assessment completed in its own case for assessment year 2002-03, the AO had accepted the Nil return filed by it holding that Article 22 was applicable in its case. The assessee also filed the copies of double income-tax relief certificates issued by the AO for assessment years 2004-05 and 2005-05 holding the assessee to be entitled to 100% DIT relief on account of income from operations of certain ships which were also operating in the international traffic. Keeping in view this documentary evidence filed by the assessee as well as the opinion of Mr. Philip Bekar and Mr. Rahul Rohotogi, Additional Solicitor General, Supreme Court of India, the learned CIT(Appeals) accepted the claim of the assessee that Article 22 of the relevant tax treaty was applicable to the profits from shipping business of the assessee company.

6. After arriving at a conclusion that Article 22 of the relevant tax treaty was applicable for deciding the taxability of shipping profits of the assessee company in India, the learned CIT(Appeals) proceeded to examine as to whether the case of the assessee was covered under Article 22(2) or not which provided that the provisions of Article 22(1) shall not apply to income, other than income from immovable property as defined in Article 6(2), if the recipient of such income, being a resident of contracting State,

carries on business in the other contracting State through a permanent establishment therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the income is paid is effectively connected with such permanent establishment or fixed base. It was provided that in such a case, the provisions of Article 7 or Article 14, as the case may be, shall apply. In this regard, the learned CIT(Appeals) referred to the agreement between the assessee company and M/s MSC Agency India P. Ltd. and held that as per the relevant clauses of the said agreement, the agent had the authority to negotiate and enter into contracts for and on behalf of the assessee company. He also noted that there was nothing brought on record to prove that M/s MSC Agency India P. Ltd. was rendering any services to any other shipping company. He held that M/s MSC Agency India P. Ltd. thus was an independent shipping agency exclusively doing the services for the assessee company and it constituted a permanent establishment of the assessee company in India.

7. After having held that M/s MSC Agency India P. Ltd. constituted a permanent establishment of the assessee company in India, the learned CIT(Appeals) proceeded to examine as to whether any income could be considered as arising out of any right or property in respect of which the income paid was effectively connected with such PE. In this regard, he referred to the opinion of Shri Mukul Rohotogi filed by the assessee wherein it was stated that the term "effectively connected" must be understood to mean that there is a powerful, complete or thorough control of the ship by the agency. It was stated that in the case of the assessee, it was simply akin to an agent who made bookings and performed other ancillary services and it, therefore, could not be said that the ships had any effective connection with the agency where such agency performed limited activities. It was further stated that Article 22(2) brings profit of the PE within the scope of Article 7 only if the relevant income of the PE arises from a right or property effectively connected with such PE. It was stated that the right or property must necessarily refer to the ship itself since the property which generates the income is the ship and since these ships clearly did not form part of the assets of PE in India but where

the assets of the assessee company, the same could not be said to be effectively connected to such PE. The learned CIT(Appeals) also referred to the opinion of Mr. Philip Baker filed by the assessee wherein it was stated that the property in respect of which the shipping income was paid is the ships which are operated by the shipping company and since these ships clearly do not form of the assets of the PE in India, the same cannot be said to be effectively connected to the PE in India. It was stated that the ships are the assets of the assessee company having no connection with agency PE in India save that the PE may clear inbound cargo and book outbound cargo which is carried on those ships. It was stated that the ships thus are clearly not assets of the PE nor are they in some other way effectively connected with a PE.

8. Relying on the opinion of Mr. Rohotogi and Mr. Philip Baker filed by the assessee as well as other relevant aspect of the matter, the learned CIT(Appeals) held that although the assessee company had a PE in India in the form of M/s MSC Agency India P. Ltd., the right or property in respect of which the income was paid i.e. ships was not effectively connectively with such permanent establishment as envisaged in Article 22(2) and, therefore, Article 22(1) was applicable in the case of the assessee by which the profits from shipping business was taxable in Switzerland and not in India. Accordingly, the addition made by the AO on account of shipping profits in the hands of the assessee was deleted by the learned CIT(Appeals). Aggrieved by the order of the learned CIT(Appeals), the Revenue has preferred this appeal before the Tribunal while the assessee has also filed the cross objection disputing the decision of the learned CIT(Appeals) that M/s MSC Agency India P. Ltd. constituted its PE in India.

9. The learned standing counsel for the Revenue Shri. G.C.Srivastava submitted that the income derived by the assessee from the business of operation of ships in international traffic in India is chargeable to tax under section 44B (read with sections 4 and *5)* of the IT Act, 1961 and the claim of the assessee that such income being covered under Article 22(1) of the Indo-Swiss DTAA is chargeable to tax only in Switzerland is

wholly untenable. He submitted that the profits from shipping and air transport are specifically dealt with under Article 8 of OECD model convention, but India and Switzerland negotiated and reached an agreement that while profits from their air transport would be taxed in the country of residence but shipping profits would be left to be taxed according to the domestic laws of each contracting state. Accordingly, Article 8, as given in the model convention, was modified to exclude shipping profits from its scope. He submitted that Para (1) of Article 7 as given in the model convention was also modified to exclude shipping profits from the scope of Article 7 to deny the exclusive right of taxation to the country of residence. He contended that the combined effect of modifications in Article 8 and Article 7 thus made it clear that the profits from the operation of ships in international traffic was left to be taxed by each contracting state according to its domestic law and this was the undisputed position and understanding of the true import of the Indo-Swiss DTAA till the year 2001 according to which all the assessment of the assessee and other Swiss residents were made for and upto A.Y 2001-2002.

10. Shri Srivastava submitted that although amendment was brought about in the Indo- Swiss DTAA in the year 2001 by introducing Article 22 to allocate taxing rights to the country of residence in respect of certain kinds of income which were not hitherto dealt with in the Treaty, neither the terms of the amended provision nor the protocol signed on 10th February 2000 make any indication to the effect that it altered the undisputed position that income from shipping business was liable to be taxed in either or both contracting states depending upon the domestic laws of each state. He submitted that Prof. Klaus Vogal in his book "Interpretation of Tax Treaties" has explained the scope of Article 22 which suggests that the scope of the Article is very narrow to apply to income like annuity, maintenance payment, damages, accident benefit, payment from business plan, scholarships, awards etc. and as asserted by the said author, Article 22 does not apply to items of income classifiable as business profits within the meaning of Article 7 and the term used therein "Not dealt with" must not, therefore, be taken to mean "not unmistakably dealt with". It is also opined that the said Article is neither

designed to remove difficulties of interpretation nor even less to settle them, in favour of the state of residence."

11. Shri Srivastava pointed out that the taxing rights in respect of shipping profits are now allocated in favour of resident state (Switzerland, in this case) by a second amendment of the DTAA in 2011 only after a prolonged negotiation between the two states by amending Article 8 to include profits from operation of ships in international traffic and Article 7 to drop the words and phrase " other than the profits from the operation of ships in international traffic". He submitted that the amendments made in 2011 thus have brought the Treaty provision in tune with model conventions and allocated taxing rights to Switzerland in this case. According to him, the shipping profits till 2011, however, continued to be taxed in accordance with domestic laws of each state and any suggestion to the contrary is a complete misreading of the terms of the DTAA as originally entered into and of the amendments carried thereto from time to time.

12 As regards the reliance of the learned CIT (A) on the order of assessment for A.Y 2002-03 and the T.D.S. certificate given under section 197, Shri Srivastava contended that the learned CIT(A) has committed a grave error in drawing support from the same for the following reasons:

i. It is a settled jurisprudence that each year is a separate and independent unit of assessment and the principles of res judicata do not apply to Income Tax proceedings.

ii. In the order of assessment for A.Y 2002-03, the A.0 was led to a mistaken belief by the letter 30.01.2004 from Swiss competent Authority filed by the assessee before him that the competent Authority of India had agreed to the position that the provisions of Article 22 were applicable to shipping profits.

iii. Apart from the fact that the Swiss competent Authority departed from the established procedure of making public only the final decision arrived at and not the correspondence entered into to reach the decision, the fact remains that the Indian competent Authority had categorically stated in his letter dated 10th December 2003 addressed to the Swiss Competent Authority that "We are not in agreement that income from shipping business in international traffic shall be covered

under Article 22."

iv. A clarification was sought by the Director of International taxation, Mumbai from the Indian competent Authority who responded to say that " India has not accepted that income from operation of ships in international traffic accruing to a resident of Switzerland will not be taxable in India in view of applicability of Article 22 of Indo-Swiss Treaty. The profits from operation of ships in international traffic will be taxable only in accordance with the domestic law of each state.

v. However, Since the Indian Competent Authority did not prefer to issue instructions in individual cases, he enclosed copies of previous correspondence vide his letter dated 27th may 2005. But his assertion that the Govt. of India had not agreed to the position held the field.

vi. It is unmistakably evident that India never accepted the position that prior to 2011, Article 22 was applicable to shipping profits.

vii. Hence the error committed in the order of assessment for AY 2002-03 or in the order U/s 197 was caused due to wrong communication from the competent Authority of Switzerland that such agreement was reached.

viii. In any case, it was an error of law in the order of assessment for that year and it would always open to correction by the A.O.

ix. Hon'ble Supreme Court quoted with approval the observations of Lord Denning- "The doctrine of precedent does not compel your Lordships to follow the wrong path until you fall over the edge of the cliff.

13. Reliance was placed by Shri Srivastava on the decision of Authority for Advance Ruling in the case of Gearbulk AG reported in (2009) 184 Taxman 383 wherein while dealing with a similar issue it was held that income derived from operations of ships in international traffic is liable to tax in India in terms of the DTAA between India and Switzerland. He submitted that The Authority rejected the contention of the applicants in the said case that Article 22 of the DTAA applied to allocate taxing rights to the country of residence on the basis of the following reasoning:

i. There was no dispute that such profits were taxable as per the domestic

law of each state and there is nothing in the amendments made in 2001 to indicate that this position was intended to be changed.

ii. Article 22 can not be made applicable by implication. The language of Article 8 and Article 7 would militate against such a view.

iii. The retention of the exclusionary clause in Article 7 very clearly demonstrates that the pre-amendment position was not intended to be charged.

iv. A particular species of income (Shipping profits) which is specially referred to in Article 7 and deliberately left out of its genus, namely business profits, can not be said to an item of income not dealt with under Article 7.The expression "dealt with" is a comprehensive expression having different shades of meanings. The exclusion clause refers to the conscious decision of the authors of the Treaty to deal with this kind profit and exclude it from the application of Article 7 and allocate taxing jurisdiction to each sate according to its domestic law. It is not an uncovered or untreated item of income.(Para 9)

iv. The argument that an item of income can be said to have been "dealt with" in an Article only if it defines the scope as well allocates the taxing rights and mere exclusion is not dealing with the income is devoid of substance and deserves to be rejected.

v. The comparison of the expression "dealt with" with other expression" not expressly mentioned" in some other DTAAs India has entered into with other countries like Malaysia, Australia, Singapore etc is again of no consequence in the light of clear expression of the intent in Article 7 by way of exclusion of shipping profits.

vi. Whenever it was intended to cover the shipping income under the provision of the DTAA, a separate provision has been made therefor as would be evident from India's treaty with countries like USA, UK, Australia, Uganda, Kazakhstan, Mongolia, Oman, Russia or Pakistan and UAE.

14. Shri Srivastava submitted that although the decision of AAR is not binding on the ITAT, there being no decision of ITAT, High Court or the Supreme Court on the issue, the decision of AAR in the case of Gearbulk AG which deals the similar issue as arising in the present appeal exhaustively, has to be followed by the Tribunal having a great persuasive value. He contended that there are no distinguishing features to suggest that the said decision is not applicable to the facts of the case and there is also no perversity in the reasoning given by AAR for coming to the finding.

15. Without prejudice to his main argument that the international shipping profits are chargeable to tax in India as the same are not covered by Article 22 of the treaty and as an alternative, Shri. Srivastava contended that Para (2) of Article 22 provides that such profits can be taxed in the source country if the business operations are carried out by the foreign enterprise in the source country through a PE and the income from rights or property is effectively connected to the PE. He submitted that the learned CIT(A) in the present case has confirmed the finding of the A.O. that assessee had a PE in India which was based on the following:

i. The entire business operations of the assessee are being carried out in India through its agent MSC Agency (India) Pvt Ltd. The said Indian Co. is doing business only for the -assessee and is, therefore, fully covered as a dependent agent under Para(6) of Article *5* of the Indo-Swiss DTAA, which provides that it the activities of the agent are devoted wholly or almost wholly for the enterprise, he would not be regarded as an agent of independent status.

ii. The scope of operations of the agent are defined in the Agreement entered into by MSC Agency (India) Ltd with the assessee. (Kindly refer to Agency agreement on Page 18 of the Paper Book).

a) Clause 2 (Page 18) refers to sales and marketing, Bookings, Documentation, Equipment control, Inland transportation, vessel operation! husbandry, System/IT, disbursements etc. All aspects of operations in India are covered in the agreement.

b) Clause 3.12 calls upon the agent to announce sailing or arrivals and to quote freight rates and announce tariffs, subject to freight policy and instructions of the principals.

The agent is, therefore, negotiating the freight rates within the broad Policy Framework. Policy framework will obviously lay down broad guidelines. The individual rates are not predetermined. In any case, he is negotiating contracts which bind the Principal and the contract with third parties will not only include rates but a host of other obligations like loading, unloading, delivery etc. The agent has to undertake many other obligations with third parties which bind the Principal as he has been given the task of entire

business operations in India.

c) Clauses 3.14, 3.21, 3.22, 3.23, 3.24, 3.25 (Page 20) and 3.28 (on Page 21) need specifically to be referred to understand the scope of agent's activities in India. Clause 4.01 (Page 22) and 4.02 are equally relevant.

d) Clauses 5.02 and 5.03 also indicate how the agent is acting on behalf of the Principal.

e) Schedule A on Page 25 shows how all expenses of the agent are borne by the assessee.

f) In the light of the aforesaid clauses it can not be asserted that the agent is not contracting on behalf of the assessee.

Shri Srivastava submitted that on the basis of above reasons, the A.O has rightly concluded that the agent is both legally and economically dependent on the assessee and hence Agency PE gets triggered under Article 5(4) of the DTAA and the learned CIT(A) has affirmed the conclusion of the A.O. after making a detailed discussion which runs from Para 3.14 to Para 3.32 of his impugned order. Shri Srivastava contended that the learned CIT(A), however, has erroneously come to the conclusion that the right or property is not effectively connected to the PE and hence income would not fall under Para(2) of Article 22. According to him, the learned CIT(A) and the assessee both have proceeded on a wrong premise that the expression "effectively connected" would mean that the property (Ship in this case) must necessarily be owned by the PE (The Agent). If that were the intention, the language in the Treaty (Article 22(2)) would have been" right or property" " owned" by the PE and not " effectively connected" to the PE. He contended that "Effectively connected" is a much wider -expression than "owned". The effective connection could be by way of ownership or by the operation or maintenance of the property. It is not in dispute that the operation of ships and its repair and maintenance is done in India by the agent. Clause 3.20 clearly brings out this import. He contended that the agent thus is involved not only in the marketing and booking of the Cargo but also in the operation of the ships in India and it can not be said that the ship is

not effectively connected to the PE (Agency PE).

16. As regards the reliance of the learned CIT(A) on the opinion of Sri Mukul Rohtagi and Mr. Phillip Baker, Shri. Srivastava contended that the same is clearly misplaced. He contended that both the learned experts have proceeded on a totally wrong premise that 'effectively connected' means the same as ownership. They have not taken into account the role of the agency PE into the operations of the ships. He also contended that the income is received not "from the ship" but from the "operation of ship" and the Agent is effectively connected with the operation of ship. The assessee is not deriving lease rentals from the ship. If that were the case, possibly the learned experts would have been right in their opinions but not in this case where the income is arising from the operation of ships. The "effective connection" here would mean not the ownership of the ship but connection with income generating activities of the ship. He contended that the international shipping income thus is alternatively liable to tax in India in terms of Article 22(2) of the DTAA.

17. The learned counsel for the assessee Shri S.E.Dastur submitted that the Indo-Swiss treaty did not contain a residuary ("Other Income") article until assessment year 2002-03 and the profits from operation of ships in international traffic were taxable in India as per section 44B of the Income-tax Act, 1961 (hereinafter referred to as "the Act"). He submitted that it was so not because the exclusion of international shipping profits from the scope of article 7 vested India with the authority to tax such international shipping profits, but because there was no other article in the Indo-Swiss treaty which could have applied to international shipping profits and as such, in terms of section 90(2) of the Act, provisions of Act (section 44B) could not be overridden by any more beneficial provision contained in the Indo-Swiss treaty. He contended that as a result of introduction of Article 22, the position that prevailed until March 31, 2001 stood altered, in that, international shipping profits which until then were not covered by any of the then

existing articles, and hence not "dealt with", came to fall within the scope of the residuary article 22. He submitted that this position was accepted for assessment year 2002-03 by the Revenue vide a reasoned order passed under section 143(3) of the Act dated 9 March 2004 and the international shipping profits of the Respondent were not subjected to tax in India in view of Article 22 which finding was in line with the specific understanding reached between the competent authority of Switzerland (SFTA) and of India (CBDT) as contained in the former's letter dated 29 October 2003 and the latter's final concurrence dated 18 December 2003.

18. Shri Dastur submitted that the assessing officer for assessment year 2003-04 however has declined to follow his order for assessment year 2002-03 by relying on letter of the DGIT (Mt. Taxation) dated February 14, 2005 which stated that international shipping profits are not covered by Article 22 of the Indo Swiss Treaty and were taxable as per the domestic laws of India. Accordingly the assessing officer denied treaty benefit and held that international shipping profits of the Respondent are taxable under section 44B of the Act and that such profits are not entitled to any treaty benefit. He contended that the learned CIT(A) however has rightly allowed the claim of the assessee by inter alia placing reliance on the aforementioned letters exchanged between the competent authorities of the two countries. He submitted that in order to be covered by Article 22 of the Indo Swiss Treaty, the item of income must be such as has not been "dealt with" in the foregoing articles of Indo Swiss Treaty. IN this regard, his contention was that insofar as Assessment Years 2002-03 to 2012-13 are concerned, international shipping profits, having been excluded from the scope of Article 7 and are not "dealt with" either in Article 7 or any other article preceding Article 22, would fall within the scope of Article 22.

19. Shri. Dastur contended that the words "dealt with" used in Article 22 have to be read in the context of purpose of a double tax avoidance agreement, which is, allocation of taxing jurisdiction and hence, for an item of income to be regarded as "dealt with" by

an article of the double tax avoidance agreement, such article must positively vest the powers to tax such item of income in one or both states. In support, the Respondent submits as follows. He submitted that the words "dealt with" in Article 22 by employing purposive construction imply a positive dealing with, in that, the articles in the treaty must unequivocally provide for the allocation of tax jurisdiction in favor of either one or both contracting states with respect to the subject item of income. He contended that vesting of jurisdiction cannot be imputed or inferred, it must be positively stated and the mere exclusion of international shipping profits from Article 7 cannot be regarded as vesting India with a right to tax international shipping profits.

20. Referring to the meaning of the words "dealt with" given in the Advanced Law Lexicon by Ramanathan Aiyar and several other dictionaries, Shri. Dastur submitted that the words "dealt with" mean a positive action and not a lack of action. He contended that a positive action in the context of a tax treaty would be when an article categorically states whether the source country or the country of residence or both have a right to tax an item of income. In support of this contention, he relied on the decision of Hon'ble Supreme Court in case of Union of India *v.* Azadi Bachao Andolan 263 ITR 706 (SC) wherein it was held at Pgs.715, 723 and 724 of the report that the purpose of tax treaties is to allocate taxing jurisdiction. He also relied on the Commentary on Double Taxation Conventions (Third Edition) by Klaus Vogel wherein he has explained that article 21 of the OECD model convention (which is equivalent to article 22 of the Indo-Swiss treaty) is a part of the "distributive rules" contained in double tax avoidance agreements, meaning thereby that double tax avoidance agreements distribute jurisdiction. Further reliance was also placed by him on the book titled "Taxation of Cross-border Services" by Rawal wherein he has observed that in the context of tax treaty "when an article provides for tax treatment (distribute taxing right) of a particular type of income, the article can be said to be dealing with such item of income".

21. Shri Dastur then referred to Article 7(1) of the treaty and submitted that when the underlined words in the opening sentence - "The business profits of an enterprise of a Contracting State, other than the profits from the operation of ships in international traffic, ..." appear before the statement of allocation of jurisdiction in favor of state of residence, it only means that international shipping profits do not enter Article 7 at all. His contention was that when business profits for the purposes of Article 7 mean other than international shipping profits, distributive rules of taxation prescribed in article 22 would apply to international shipping profits and not some distributive rules which can allegedly be imputed by virtue of exclusion from article 7. According to him, when a right had to be vested in the source state (India) to tax it, it has been specifically provided, how then can a mere exclusion from Article 7 be said to have conferred such a right. He also supported this contention by relying on the law laid down by the Special Bench in the case of Mahindra & Mahindra's case 313 ITR (AT) 263 and explained how the proposition laid down therein supports the stand of the assessee. He also explained how the interpretation sought to be placed by the department in this context will lead to an absurd situation by pointing out that accepting the Revenue's contention means that profits of the Respondent from operation of ships in domestic traffic, for example, freight earned for carriage from Goa to Mumbai, will be accorded treaty benefit and will not be taxable in India (if the Respondent has no PE), but whole of the freight earned for example, for carriage from Colombo to Mumbai will be taxable in India under section 44B of the Act.

22. Shri Dastur emphasized that a mere reference to international shipping profits in Article 7 of the Indo-Swiss treaty does not mean that such profits have been dealt with there as India has, in several double tax avoidance agreements used the word "mentioned" as against "dealt with" in the "Other Income" article which demonstrates that the words "dealt with" must mean something more than a mere mentioning of such income in the article. He submitted that where the Contracting States intended to provide for taxability of a particular item under the domestic laws

of both states in treaties having a residuary clause (i.e. "Other Income" Article), they have specifically said so, for example, when the negotiators wanted both states to have a right to tax capital gains as per their domestic laws, Article 13 of Indo-US and Article 14 Indo-UK treaty positively stated so. He contended that if the Revenue is right that by merely not having any article providing for taxability of capital gains in a treaty having a "Other Income" Article, both states were automatically vested with the right to tax capital gains as per their domestic laws, then providing for such dual right of taxation in Article 13 of Indo-US and Article 14 Indo-UK treaty was not necessary.

Reliance was also placed by Shri. Dastur on the opinion of Mr. Philip Baker dated *25* June 2003 wherein Mr. Baker (an internationally acclaimed authority) has categorically opined that article 7 cannot be regarded as having dealt with international shipping profits and that such profits would be covered within the purview of article 22 of the Indo-Swiss treaty. He submitted that the letter written by the competent authority of Switzerland dated 29 October 2003 and the final response from the competent authority of India vide letter dated 18 December 2003 unequivocally demonstrate that international shipping profits fall within the purview of Article 22 of the Indo-Swiss Treaty. He contended that the double tax avoidance agreement is nothing but a contract between two states, required to be interpreted in good faith and any subsequent clarification/understanding between the contracting parties must be given effect to. Reliance in this regard was also placed by him on the decision of the Hon'ble Calcutta High Court in case of CIT v. Arun Dua (186 ITR 494) wherein at Page 496 the High Court has held that if an agreement between two parties has been understood in a certain way and has been acted upon by them, it was not open to the tax officer to give another interpretation to the agreement.

23. As regards the Revenue's contention that the reason for exclusion of international shipping profits from the Indo-Swiss treaty is that Switzerland is a landlocked

country and if the Indo-Swiss treaty were to provide for taxability of such profits it would result into treaty shopping, Shri. Dastur pointed out that India has entered into tax treaties with several other landlocked countries such as Uganda, Kazakhstan, Turkmenistan, etc. which have a shipping income article. He contended that if this contention of the Revenue is correct, then India and Switzerland would not have amended the Indo-Swiss treaty in 2012 whereby Article 8 has been amended to include international shipping profits thereby giving the state of residence the sole right to tax such profits. He also contended that the amendment to the Indo-Swiss treaty with effect from April 1, 2012 has given additional relief to residents of both countries, in that, it has amended Article 8 to include international shipping profits thereby giving the state of residence the sole right to tax such profits irrespective of whether its resident has a PE in the other state or not and whether the rights or property are effectively connected with such PE. He contended that it is therefore wrong to say that accepting the assessee's stand would render the 2012 amendment a fruitless exercise.

24. Shri Dastur explained the effect of letters exchanged between the competent authorities in the light of Article 25 of the Treaty. He submitted that the understanding arrived at between the competent authority of Switzerland and that of India vide exchange of letters dated 29 October 2003 and 18 December 2003 constituted an understanding employing the mutual agreement procedure as provided for in Article 25 of the Indo-Swiss treaty and hence is binding on the Revenue. He submitted that the letter dated 14 February 2005 relied upon by the assessing officer to deny treaty benefit to the assessee, on the other hand, has been superseded by letter dated 27 May 2005 and reliance of the assessing officer there is wholly misplaced. He pointed out that applicability of Article 22(1) of the Indo-Swiss treaty to international shipping profits has been accepted by the Revenue in the order passed under section 143(3) of the Income-tax Act, 1961 for Assessment Year 2002-03 in assessee's own case based on the bilateral letters exchanged between the competent authorities of India and Switzerland mentioned

above. He submitted that the Revenue has also passed a voyage assessment order dated 10 June 2005 under section 172(4) of the Act for Assessment Year 2005-06 wherein it was held that international shipping profits are covered by Article 22(1) of the Indo--Swiss treaty and hence freight collected was allowed to be remitted without deduction / payment of any taxes.

In this regard, he relied on the decision of the Hon'ble Supreme Court in case of Radhasoami Satsang v. CIT (193 ITR 321) wherein it was held at Page 329 that where a fundamental aspect permeating through the different assessment years has been found as a fact one way or the other and parties have allowed that position to be sustained by not challenging the order, it would not be at all appropriate to allow the position to be changed in a subsequent year. He contended that the availability of benefit under a double taxation avoidance agreement is a fundamental aspect permeating through different assessment years.

25. As regards the applicability of Article 22(2), Shri Dastur submitted that the same is applicable only if the two conditions are satisfied i.e. *t*he Respondent must have a PE in India and the income paid must be with respect to a right or property which is effectively connected to such PE. In this regard, he submitted that MSC Agency (India) Pvt. Ltd. does not constitute a PE of the assessee in India, neither in the form of a fixed place PE nor as an agency PE. *He* submitted that the assessee has no interest in MSC Agency (India) Pvt. Ltd. which is owned and controlled by the Sharaf Group based out of Dubai. It also has no control or dominion over any place from which MSC Agency (India) Pvt. Ltd. carries on its business and hence MSC Agency (India) Pvt. Ltd. cannot constitute a fixed place PE of the assessee. Insofar as MSC Agency (India) Pvt. Ltd. constituting an agency PE is concerned, he submitted that MSC Agency (India) Pvt. Ltd. did not have any blanket powers / rights to negotiate contracts with shippers but only had a limited right to perform its activities within the terms and conditions prescribed by the assessee. He contended that MSC Agency (India) Pvt. Ltd. therefore cannot be regarded as being covered by Article 5(4)(i) so

it cannot be regarded as habitually exercising " ... an authority to negotiate and enter into contracts for or on behalf of the enterprise ...". He also contended that the assessee in any case having no control over MSC Agency (India) Pvt. Ltd., the later at the most would be an independent agent which cannot be regarded as a PE in view of Article 5(5) of the Indo-Swiss treaty.

26. As regards condition no. 2 for applicability of Article 22(2), Shri Dastur submitted that even where there is an agency PE, for international shipping profits to be hit by Article 22(2) of the Indo-Swiss treaty, not only must there be a PE of the assessee in the source state (India, in the present case), but the "right or property" in respect which the income is paid (viz, freight earned on operation of ships in international traffic) must be effectively connected with such PE. He contended that even if MSC Agency (India) Pvt. Ltd. Is treated as a PE of the assessee in India, the "right or property" in respect which the income is paid viz. the ships cannot be regarded as being effectively connected to such PE and hence remain outside the purview of Article 22(2) of the Indo-Swiss treaty. He contended that for the "right or property" viz. the ships, to be effectively connected to the PE, the PE must economically own the ships, in that the PE must have full control over the ships, for example. the PE should be in a position to decide the route that the vessel takes or where it will stop in transit etc. He submitted that no such control in the present case can be or is exercised by MSC Agency (India) Pvt. Ltd. on any of the vessels owned by the assessee and as a matter of fact, the captain of the vessel and the crew are all employees of the assessee and not of MSC Agency (India) Pvt. Ltd. Reliance in support of his contention on this aspect was placed by Shri. Dastur on the decision of the Special Bench Mumbai, in case of Sumitomo Mitsui Banking Corporation & Ors. v. DDIT (136 ITD 66) at Pages 687 and 688 of the report and the opinion of Mr. Philip Baker dated 23 December as well as that of Mr. Mukul Rohotgi, Additional Solicitor General of India, dated 25 February 2004.

27. As regards the decision of the Authority of Advance Ruling (Authority) in the case of Gearbulk AG In Re (184 Taxman 383) relied upon by Shri. Srivastava in support of the Revenue's case, Shri. Dastur submitted that the same is not a good law and does not deserve to be followed for the following reasons:

- The Authority was not made aware of and hence has not considered the letters exchanged between the Competent Authorities (referred to above) on applicability of Article 22 to shipping profits in international traffic.

- In Para 8, the Authority admits that prior to 2001 shipping profits in international traffic were "untouched" under the Indo-Swiss Treaty. The Authority therefore accepts that prior to 2001 the Indo-Swiss Treaty did not "deal with" such shipping profits. Having so admitted and proceeded on that basis, the Authority could not have come to the conclusion that Article 22 does not apply to international shipping profits.

- The basis on which the Authority proceeds (in Para 8) that there would be no point in excluding shipping profits from Article 7 and including it in Article 22, when both Articles 7 and 22 prescribe PE based taxation, is incorrect. Article 22 is narrower than Article 7, as under Article 22 the income paid must be in respect of a right or property "effectively connected" to the PE, whereas, under Article 7 the profits must be attributable to the PE.

- The observations of the Authority (in Para 9) that a particular specie of income which is specifically referred to in Article 7 and deliberately left out of its genus, namely, business profits, cannot be said to be an item of income not dealt with under Article 7 is, with due respect, incorrect since there are certain types of income which are governed by Article 22 even if they are referred to in the specific Articles. For e.g., Interest paid on a borrowing by a US branch of a Swiss Co. from an Indian lender will not be covered by Article 11 as the interest would arise in US and not in Switzerland or India. Thus, the aforementioned incomes would be covered under Article 22 *(see **Annexure** M of the Index giving the extract of the US Technical Explanation)*

- The Authority has not considered the definition of 'deal with' given in the *Advanced* Law Lexicon *and other meanings of the term referred to above (refer **Annexure C** of the Index)* which clearly states that it means a positive

action and not lack of action.

- The Authority has not considered the impact of definitions cited in the context of Azadi Bachao Andolan's case (supra) when it says that the object of tax treaties is to allocate jurisdiction, and in that context 'dealt with' must mean dealt with by allocating jurisdiction.

- In Para 9.2, the Authority has referred to the argument of the difference between "dealt with" and "mentioned in" but has not give any reasoning for rejecting the submissions.

- In Para 10, the Authority has observed that tax treaties entered into by Indiawith various countries show that whenever shipping profits was to be covered by the tax treaty a separate article was provided, hence in case of Switzerland, shipping profits are not meant to be covered by the Indo-Swiss treaty. This observation of the Authority is again incorrect since a foreign shipping company's income from domestic /coastal traffic is covered under Article 7(1), and therefore it would not be correct to say that "shipping profits" *per se* are not covered.

- In any event, the ruling of the Authority is merely persuasive and not binding as is evident from section 245S and as has in fact been held by the Tribunal in case of ADIT v. Green Emirates Shipping and Travels (100 **ITD** 203)

28. Without prejudice to his main argument that Article 22(2) of the Treaty is applicable in the case of the assessee and not Article 22(2) and as an alternative, Shri. Dastue contended that even if Article 22(2) is held to be applicable in the case of the assessee, no portion of the international shipping profits earned by the assessee can be taxed in India inasmuch as the commission paid to MSC Agency (India) Pvt. Ltd. is admittedly at an arm's length. He submitted that this fact is borne out from the transfer pricing assessments of the assessee as also MSC Agency (India) Pvt. Ltd. for the year under consideration. Reliance in support of this contention was placed by him on the decision of Hon'ble Delhi High Court in the case of DIT vs. BBC Worldwide

Ltd. 203 Taxman 554 (Delhi) and the decision of the Hon'ble Bombay High Court in the case of Set Satellite (Singapore) Pte Ltd. vs DDIT 218 CTR 452.

29. In the rejoinder, Shri Srivastava submitted that the reliance of Shri. Dastur on certain definitions of the expression "dealt with" given in some of the dictionaries such as Shorter oxford Dictionary, Law Lexicon by Sri Ramanathan Aiyer, Macmillion Dictionary, Oxford English Dictionary etc. is clearly misplaced and the same does not advance the case of the assessee. He contended that the said expression has different meanings like the shorter Oxford Dictionary gives one meaning of the expression as "be concerned with" while Law Lexicon of the Sri Aiyer gives one such meaning as "to take the action that is necessary" and Oxford Dictionary has one meaning as " to have to do in any way." He contended that the meaning " Positive dealing with property and not lack of dealing" extracted by Mr. Ramanthan Aiyar is in the context of particular dealing with property and such a meaning can not be of universal application. He contended that when the treaty negotiators excluded the shipping profits from Article 7, they were concerned with it and took action that was necessary in this regard which itself was a positive dealing with the subject of shipping profits. According to him, there may be several ways of dealing with an item of income and one such way is to exclude the income from the operation of the Article and leaving it to be addressed by domestic law. He contended that the Subject was regarded as "dealt with" without any shadow of doubt till the year 2001 and it can not become" Not dealt with" by mere introduction of Article 22 in the DTAA. He also contended that if the resident country was denied exclusive taxing rights under Article 7 and Article 8, it would be absurd to suggest that exclusive rights were given to the resident country under Article 22. As regards the opinions of Philip Baker and Mukul Rohtagi filed by the assessee, he submitted that the same have proceeded on fallacious assumptions and the opinions expressed by them being contrary to the decision of a judicial authority like AAR can not be accepted.

30. As regards the alternative plea of Shri Dastur that the PE in India having been remunerated at Arms' Length for the services rendered, no further income can be brought to tax in the hands of the assessee under Article 22(2) of the DTAA, Shri. Srivastava contended that the risk in the present case is entirely borne by the assessee which aspect has obviously not been captured in the remuneration of the agent. He pointed out that this contention of the assessee has been rejected by the learned CIT(A) on the ground that unlike other treaties, Indo-Swiss DTAA has not incorporated the words "and the transaction between the agent and the enterprise are not made under arm's length conditions". He also pointed out that the tested party before the T.P.0. was the agent and even if the payment made to the agent may be at arm's length, it cannot go to suggest that the arm's length price for the risks undertaken by the assessee is also captured in the remuneration paid to the agent.

31. We have considered the rival submissions and also perused the relevant material on record. It is observed that the profits from operation of ships in international traffic were claimed to be taxable only in Switzerland by the assessee i.e. in the State of its residence and not in India and accordingly Nil income was declared by it in the return of income filed for the year under consideration. This claim of the assessee was based on Article 22 of the DTAA between India and Switzerland (Indo-Swiss treaty) especially paragraph 1 of that article. According to the AO, the said Article 22 dealing with other income not specifically dealt with by any article of the treaty, however, was not applicable in respect of profits from operation of ships in international traffic as the same was dealt with in Article 7 by exclusion whereby such profits were excluded from the purview of Article 7(1). According to him, the said profits thus were taxable in India as per the domestic law i.e. Income-tax Act, 1961 and accordingly he brought the same to tax in the hands of the assessee in India by applying the provisions of section 44B at the rate of 7.5% of gross receipts. In this regard, he held that the assessee was having a permanent establishment in India in the form of M/s MSC Agency India P. Ltd.. The

learned CIT(Appeals) agreed with the AO to the effect that the assessee company was having a PE in India during the year under consideration. He, however, held that the taxability of the profits of the assessee company from operation of ships in international traffic is governed by Article 22 of Indo-Swiss treaty and although the assessee was having a PE in India, the right or property in respect of which the income was paid i.e. ships not being effectively connected with such PE, profits from operation of ships in international traffic is taxable only in Switzerland as per paragraph 1 of Article 22 of Indo-Swiss treaty. The first and foremost issue that is to be considered and decided thus is whether the taxability of profits from operation of ships in international traffic of the assessee company is governed by Article 22 of the Indo-Swiss treaty or not.

32. The learned Special Counsel for Revenue Shri G.C. Srivastava, has contended that the profits from shipping and air transport are specifically dealt with under Article 8 of OECD model convention according to which profits of an enterprice of a contracting State from the operation of ships or aircraft in international traffic is taxable only in that State. He has contended that India and Switzerland, however, have agreed to modify Article 8 to exclude shipping profit from its scope. He has submitted that the shipping profits are also excluded from Article 7(1) which provides that the business profits of an enterprise of a contracting State shall be taxable only in that State unless the enterprise carries on business in the other contracting State through a PE constituted therein. He has contended that the combined effect of these modifications in Articles 7 and 8 makes it clear that the profits from the operation of ships in international traffic were left to be taxed by each contracting State according to its domestic law. He has contended that this was an undisputed position and understanding of the true import of the Indo-Swiss treaty till the year 2001 and the introduction of Article 22 in the treaty in 2001 did not alter this position.

33. The provisions of Article 22 introduced in the Indo-Swiss treaty in 2001 being relevant in the present context are reproduced hereunder :

"1. Items of income of a resident of a Contracting State, wherever arising, not dealt with in the foregoing Articles of this Agreement shall be taxable only in that State.

2. The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the income is paid is effectively connected with such permanent establishment or fixed base. In such the provisions of Article 7 or Article 14, as the case may be, shall apply.

3. Notwithstanding the provisions of paragraph 1, if a resident of a Contracting State derives income from sources within the other Contracting State in the form of lotteries, crossword puzzles, races including horse races, card games and other games of any sort or gambling or betting of any form or nature whatsoever, such income may be taxed in that other Contracting State."

A reading of Article 22 especially paragraph 1 thereof makes it clear that the items of income of a resident of a contracting State i.e. Switzerland which are not dealt with in the foregoing Articles of the Indo-Swiss treaty shall be taxable only in that State. In the present case, the assessee company being a resident of Switzerland, the income, wherever arising, would fall within the scope of the residuary Article 22 if the same is not dealt with in any other Articles of the treaty. The question, therefore, is whether the shipping profits are dealt with in any other articles of the Indo-Swiss treaty or not. The contention raised by Shri Srivasava on behalf of the Revenue is that by agreeing to exclude the shipping profits from Article 8 as well as Article 7 of the Indo-Swiss treaty, India and Switzerland had agreed to leave the shipping profits to be taxed by each State according to its domestic law and this undisputed position prevailing upto 2001 did not change as a result of introduction of Article 22 of the treaty with effect from 01-04-2001. We are unable to agree with this contention of Shri Srivastava. In our opinion, as a result of introduction of Article 22, the items of income not dealt with in the other articles of the Indo-Swiss treaty are covered in the residuary Article 22 and their taxability is governed by the said Article with effect from 01-04-2001. Articles 7 and 8 of the treaty therefore cannot be relied upon to say that by agreeing to exclude the shipping profits from said

Articles, the shipping profits are left to be taxed by each contracting State according to its domestic law. It is no doubt true that this was the position prior to introduction of Article 22 in the Indo-Swiss treaty in the year 2001 but the same was altered as a result of introduction of the said article inasmuch as it became necessary to find out as to whether shipping profits have been dealt with in any other article of the treaty. Mere exclusion of shipping profits from the scope of treaty could have resulted in leaving the same to be taxed by the concerned contracting State according to its domestic law prior to introduction of Article 22. However, such exclusion alone will not take it out of the scope of Article 22 unless it is established that the shipping profits have been dealt with in any other article of the treaty. The language of Article 22(1) in this regard is plain and simple and the requirement for application of the said Article is explicitly clear.

34. It is pertinent to note here that the purpose of tax treaties is to allocate taxing jurisdiction as held, inter alia, by the Hon'ble Supreme Court in the case of Union of India vs. Azadi Bachao Aandolan 263 ITR 706 and only when an Article provides for tax treatment i.e. to distribute taxing right of a particular type of income, then it can be said that it deals with such item of income. If there is no article providing for such tax treatment to distribute jurisdiction to tax a particular income like the shipping profits the present case, then it cannot be said that such income is dealt with by the articles of the treaty. When Article 7 provides for taxability of business profits other than international shipping profits, it prescribes distributive rules in respect of business profits other than international shipping profits and it can, therefore, be said that such business profits are dealt with by Article 7. It is, however, not true in respect of international shipping profits as it does not prescribe distributive rules with respect to such profits. By exclusion of such profits from Article 7, it can be said that the same are left to be taxed by the contracting State as per their domestic laws as there was no article upto 01-04-2001 dealing with such income. However, as a result of introduction of the residuary Article 22 with effect from 01-04-2001, the items of income not dealt with by any other article are specifically covered in that article and since the taxability of such other income is now

governed by Article 22, the same has to be dealt with reference to the said article. This conclusion gets support from the opinion of Mr. Philip Bekar dated 25th June, 2003 filed by the assessee wherein he has opined that Article 7 cannot be regarded as having dealt with international shipping profit and such profits would be covered within the perview of Article 22 of the Indo-Swiss treaty.

35. In support of his action in bringing to tax the profits from shipping to tax in India as per domestic law, the AO has relied upon the letter dated 14th February, 2005 issued by the Joint Secretary. However, as rightly contended by the learned counsel for the assessee, the said letter has been impliedly superseded by another letter dated 27th May, 2005 issued subsequently wherein reference was made to two letters written earlier dated 29th October, 2003 and 18th December, 2003 accepting that the taxability of shipping profits was governed by Article 22 of the Indo-Swiss treaty. As a matter of fact, this position was accepted by the AO himself in the assessment completed in assessee's own case for assessment year 2002-03 wherein the claim of the assessee that the shipping profit is chargeable to tax only in Switzerland and not in India as per Article 22 of the treaty was allowed by the AO. Even in the voyage assessment order passed on 10th June, 2005 u/s 172(4), the AO accepted that the international shipping profits of the assessee company for assessment year 2005-06 were governed by Article 22(1) of the Indo-Swiss treaty.

In order to say that a particular item of income has been dealt with, it is necessary that the relevant article must state whether Switzerland or India or both have a right to tax such item of income. Vesting of such jurisdiction must positively and explicitly stated and it cannot be inferred by implication as sought to be contended by Shri. Srivastava relying on Articles 7 and 8 of the treaty. As rightly contended by the learned counsel for the assessee, the mere exclusion of international shipping profit from Article 7 cannot be regarded as an item of income dealt with by the said article as envisaged in Article 22(1). The expression "dealt with" contemplates a positive action and such positive action in the present context would be when there is an article categorically stating the source of

country or the country of residence or both have a right to tax that item of income. The fact that the expression used in Article 22(1) of the Indo-Swiss treaty is "dealt with" viz-a-viz the expression "mentioned" used in some other treaties clearly demonstrates that the expression "dealt with" is some thing more than a mere mention of such income in the article and as rightly contended by the learned counsel for the assessee, the international shipping profits can at the most be said to have mentioned in Article 7 but the same cannot be said to have been dealt with in the said article.

36. In the case of Mahindra & Mahindra 313 ITR (AT) 263, the issue before the Special Bench of the Tribunal was relating to taxability of fees paid by Mahindra & Mahindra Ltd. to merchant bankers on account of services rendered by the merchant bankers in relation to a GDR issue floated by Mahindra & Mahindra Ltd. in U.K. In this regard, the Special Bench took a view that since the services rendered by the merchant bankers did not "make available" any technical knowledge etc. to Mahindra & Mahindra Ltd., such technical services would travel from Article 7 to Article 13. The Special Bench, however, took note of Article 7(9) of the DTAA between India and United Kingdom which provided that "where profits include items of income which are dealt with separately in other articles of this convention, then the provisions of those articles shall not be affected by the provisions of this article" and held in view of the said article that technical services would have to go back to article 7 for determination of whether India can tax fees from such technical services. The stand of the Revenue that exclusion of an item of income from an article means that such item has been "dealt with" thus was not accepted by the Special Bench of ITAT by implication in the case of Mahindra & Mahindra.

37. As already observed, the expression "dealt with" used in Article 22 have to be read in the context of purpose of double tax avoidance agreement which is allocation of taxing jurisdiction. From this angle, an item of income can be regarded as "dealt with" by an article of DTAA only when such article provides for and positively vests the powers to tax such income in one or both States. The mere exclusion of international shipping

profits from Article 7, therefore, cannot be regarded as vesting India with a right to tax international shipping profits and such profit, in our opinion, cannot be regarded as "dealt with" by the said article as envisaged in Article 22.

38. The stand of the Revenue is that by excluding the profits from the operation of ships in international traffic from Article 7(1), the same has to be regarded as dealt with by Article 7(1) and it, therefore, cannot fall under Article 22. It is contended that such profit, therefore, will be taxable in India as per the domestic law by applying the provisions of section 44B of the Income-tax Act, 1961. If this contention of the Revenue is accepted, the same, in our opinion, will lead to absurdity as rightly contended by the learned counsel for the assessee inasmuch as the profits from the operation of ships in domestic traffic, for example, freight earned for carriage from Goa to Mumbai will be eligible for treaty benefit and will not be taxable in India whereas profits from the operation of ships in international traffic will be taxable in India u/s 44B of the Act. In our opinion, this cannot be the intention of the legislature or even of the parties to the Indo-Swiss treaty i.e. India and Switzerland and the contention of the Revenue resulting in such absurdity cannot be accepted.

39. One of the contentions raised by Shri Srivastava is that the reason for exclusion of international shipping profits from the Indo-Swiss treaty is that the Switzerland is a Land locked country and if the Indo-Swiss treaty were to provide taxability of such profit, it would result into treaty shopping. However, as pointed out by the learned counsel for the assessee, India has entered into tax treaties with several other Land locked countries such as Uganda, Kazakhstan Turkmenistan etc. which have not excluded shipping income. Moreover, even the Indo-Swiss treaty has now been amended in the year 2012 whereby the shipping income has been included in Article 8. We, therefore, find it difficult to accept the contention of Shri Srivastava that the international shipping profit were excluded from Indo-Swiss treaty for the reason that Switzerland is a land locked country. We are also unable to agree with the contention of Shri Srivastava that if the stand of the assessee for international shipping profits are not taxable in India but are taxable in

Switzerland after the introduction of Article 22 in the Indo-Swiss treaty with effect from 01-04-2001 is to be accepted, the amendment with effect from 1st April, 2012 whereby such income is included in Article 8 thereby giving the State of residence the sole right to tax the same would render a futile exercise, because as a result of the said amendment made in the year 2012, the international shipping profits shall be taxable in the State of residence irrespective of whether the resident has a PE in the other State or not and whether the rights or property are effectively connected with such PE or not which was not the position earlier prior to 2012 even after insertion of Article 22.

40. Shri Srivastava has relied on the commentary of Professor Klaus Vogal wherein while explaining the scope of Article 22, the learned Commentator has stated that the said article does not apply to the items of income classifiable as business profits within the meaning of Article 7. It is, however, to be noted that the international shipping profits have been excluded from business profits within the meaning of Article 7. He has also relied on the comments of Professor Klaus Vogal that the expression "not dealt with" used in the said article must not be taken to mean "not unmistakably dealt with" as the said article is neither designed to remove difficulties of interpretation nor even lays to settle them in favour of the State of residence. In this regard, we have already referred to the correspondence exchanged with the competent authorities of India and Switzerland whereby it was mutually agreed to assign a certain specific interpretation to Article 22 in the context of international shipping profits and keeping in view this agreement arrived at between the two competent authorities, we are of the view that the Revenue authorities are not free to take any contrary view relying on the commentary of Professor Klaus Vogal. As regards the contention of Shri Srivastava that there is nothing in Article 22 to suggest that the position that existed till assessment year 2001-02 got altered or modified by the introduction of Article 22 in the Indo-Swiss treaty, we are of the view that the mutual agreement arrived at by the competent authorities of two countries, is good enough to suggest that the position as regards the taxability of international shipping profits got changed by the introduction of Article 22.

41. Upto assessment year 2001-02, international shipping profits no doubt were being taxed under the domestic laws as per the provisions of section 44B. However, it was not because of the exclusion contained in Article 7 that India was vested with the authority to tax such international shipping profit but it was because there was no other article in the Indo-Swiss treaty dealing with international shipping profits which could override the provisions of section 44B of the Act in terms of section 90(2) of the Act being more beneficial to the assessee. This position, however, has changed as a result of introduction of Article 22 in the Indo-Swiss treaty which now governs the international shipping profits not being dealt with specifically by any other article of the treaty and if the provisions of Article 22 are beneficial to the assessee, the same are bound to prevail over the provisions of section 44B of the Act. In this regard, a reference can usefully be made to the DTAA between India and Libya which has no clause prescribing the tax treatment for capital gains nor any residuary clause such as other income clause. The capital gains earned by a resident of Libya in India thus is taxable in India if exigible as per the domestic laws in view of the absence of a more beneficial clause in the relevant treaty. This position can be further understood by reference to DTAA between India and Malaysia which has no clause prescribing a tax treatment for capital gains but has a residuary clause i.e. other income clause in Article 22 which prescribes distributive rules with respect to items of income for which no rules have been prescribed in the earlier articles of the agreement. The taxability of capital gains earned by a resident of Malaysia in India thus will be governed by the distributive rules contained in Article 22 if they are more beneficial to the assessee than the relevant provisions contained in the Indian Income-tax Act. These examples will further support and substantiate the view that international shipping profits were being taxed in India under the domestic law upto assessment year 2001-02 not because of the exclusion contained in Article 7 but because of absence of any article prescribing specifically a tax treatment i.e. distributive rules in the Indo-Swiss treaty. This position, however, has changed as a result of introduction of residuary article 22 prescribing tax treatment or distributive rules for other income which

has not been dealt with by any earlier articles of the treaty like the international shipping profits.

42. In assessee's own case, a similar issue came up for consideration for the first time in assessment year 2002-03 when Article 22 introduced in the Indo-Swiss treaty from 01-04-2001 became operative and applicable. For that year, the return was filed by the assessee declaring Nil income making a similar claim that under the beneficial provisions of Article 22 of Indo-Swiss treaty, it was not liable to tax in India on its international shipping profits. The stand of the assessee was that in the absence of any specific article in the DTAA dealing with taxability of profits derived from the operation of ships in international traffic, paragraph 1 of Article 22 of the DTAA was applicable and its shipping profits were taxable only in Switzerland. It was submitted that even Article 7 of the treaty which excluded international shipping profits from its ambit did not deal with such profit up to 31/03/2001 and in the absence of any other article in the treaty dealing with such profit, the same was chargeable to tax as income under the Indian Income-tax Act. It was submitted that this position, however, got changed as a result of introduction of Article 22 in the treaty with effect from 01-04-2001 which governs the taxability of all other income which have not been dealt with in other articles of the treaty and since as per the said Article 22, all other income not specifically dealt with in the other articles of the treaty is taxable only in the State of residence i.e. Switzerland, the shipping income from international traffic was not taxable in India and was taxable only in Switzerland. In support of this claim, a letter dated 30th January, 2004 issued by Swiss Tax Authorities to the foreign consultant of the assessee was filed which clearly stated that the profits from operation of ships in international traffic was not covered specifically by any of the articles and, therefore, Article 22 would govern the taxability of such profits. The stand of the assessee was accepted by the AO and in the assessment completed u/s 143(3) vide an order dated 09-03-2004 for assessment year 2002-03 , he held that with the introduction of new Article 22 in the treaty, the income of the assessee from profits from

shipping operation in international traffic were taxable only in the State of residence i.e. Switzerland and not in India.

43. There is no dispute that the issue involved in the year under consideration as well as all the material facts relevant thereto are similar to assessment year 2002-03 wherein the claim of the assessee was accepted by the AO. In the year under consideration, he, however, has taken a different view relying on the letter dated 14th February, 2005 issued by the Joint Secretary. As pointed out by the learned counsel for the assessee, the said letter has been superseded by another letter issued on 27th May, 2005 wherein the Joint Secretary has made a reference to the letters exchanged between the competent authority of India and that of Switzerland dated 29th October, 2003 and 18th December, 2003. Copies of the said letters are placed on record. The first letter dated 29th October, 2003 was sent by Professor Dr. R. Waldburger, Vice Director, Division for International Fiscal Law and Double Taxation Matters, Swiss Federation Tax Administration to the Joint Secretary (FT & TR), Ministry of Finance, Government of India, the contents of which are reproduced below :

> "We write this letter to you in order to agree on the taxation of profits arising from operation of ships in international traffic in our respective countries in accordance with the provisions of our double taxation agreement.
>
> During our negotiation both contracting States decided to tax enterprises that operate in the shipping business according to the internal law of each Contracting State. The term "international traffic" in paragraph 1 subparagraph i) of Article 3 therefore was limited to transport by an aircraft operated by an enterprises of a Contracting State. Consequently we have excluded shipping profits in Article 8 DTA-IND (which normally deals with profits arising from shipping and operation of aircrafts). According to paragraph 1 of Article 7 DTA-IND profits from the operation of ships in international traffic are not treated under the general concept of business profit attribution between the company and its permanent establishment. As the double taxation agreement concluded in 1994 did not contain a general provision attributing the taxing right for other income to the states of residence, shipping profits could be taxed by each Contracting State according to its internal law.

During the renegotiation we inserted Article 22 into our agreement that deals with all items of income not dealt with specifically under the other Articles of our agreement. As paragraph 1 subparagraph i) of Article 3, Article 7 and Article 8 DTA-IND did not undergo any changes, business profit arising from shipping activities consequently falls under Article 22.

Paragraph 1 and 2 of Article 22 DTA-IND, which is relevant for this purpose, reads as follows:

"Article 22 Other income

1.Items of income of a resident of a Contracting State, wherever arising, not dealt with in the foregoing Articles of this Agreement shall be taxable only in that State.

2.The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein, or performs in the other State independent personal services from a fixed base situated therein, and the right or property in respect of which the income is paid is effectively connected with such permanent establishment or fixed base. In such case the provisions of Article 7 or Article 14, as the case may be, shall apply."

Accordingly, any income derived by a resident of one of the Contracting States not specifically dealt with in any of the other Articles of our agreement falls under Article 22. According to paragraph 1 of Article 22 such income is taxable only in the country of residence, unless the beneficial owner carries on business in the other Contracting State through a permanent establishment and the right or property in respect of such income is effectively connected with such permanent establishment (paragraph 2 of Article 22).

Considering these provisions, we are of the opinion, that income derived by a resident of Switzerland from India out of operation of ships in international traffic, shall fall under Article 22. Further, it is our understanding that such income would be liable to tax only in Switzerland unless the beneficial owner carries on business in India through a permanent establishment situated therein and the right or property in respect of such income is effectively connected with such permanent establishment.

We hope that you interpret these provisions of our double taxation agreement in the same way and therefore will be able to confirm your agreement to us by returning a countersigned copy of this letter. (emphasis supplied in bold letters)

We thank you for your cooperation in this matter and look forward to receiving your soon answer."

44. The immediate reply to the above letter was sent by Joint Secretary (FT & TR) by a letter dated 10th December, 2003 communicating that India was not in agreement that income from shipping business in international traffic would be covered under Article 22 and reasons for the same were also given. However, immediately thereafter, a letter dated 18th December, 2003 was sent by the Joint Secretary (FT & TR) to Shri Wardbarger clarifying the matter as under :

> " As regards the query raised in your letter dated 29.10.2003, I have already handed over a written reply to Ms. Silvia Frohofer. **However, to clarify the matter further, I may submit that profit from operation of ships in international traffic is not covered specifically by any of the Articles of the amended DTAA (Article 8 only refers to air transport). Accordingly, Article 22 of the DTAA dealing with other income would fall to be applicable in respect of income from operation of ships in international traffic. As per paragraph 1 of the said Article, such income is taxable only in the state of residence of the taxpayer.** However, paragraph 2 of the Article provides that if the enterprise engaged in operation of ships in international traffic has a Permanent Establishment in another country, then the provisions of Article 7 of the DTAA would apply and not Article 22. But paragraph 1 of Article 7 of the Treaty categorically says that the said Article is not applicable to profits from operation of ships in international traffic. Accordingly, if a Swiss shipping enterprise engaged in operation of ships in international traffic has a Permanent Establishment in India or if an Indian shipping enterprise engaged in operation of ships in international traffic has a Permanent Establishment in Switzerland then the income attributable to the activities carried out in the other country will be taxable in accordance with domestic tax laws of the said country." (emphasis supplied in bold letters).

As is clearly evident, it was agreed by the Indian Competent Authority that profit from operation of ships in International traffic is not governed specifically by any of the articles of the treaty and that Article 22 of the DTAA dealing with other income would fall to be applicable in respect of such income. The AO, however, relied on the letter dated 14th February, 2005 written by Joint Secretary (FT & TR) to DGIT, International Taxation clarifying that India has not accepted that income from operations of ships in international traffic accruing to a resident of Switzerland will not be taxable in India in

view of applicability of Article 22 of Indo-Swiss treaty and such income will be taxable only in accordance with the domestic law of the State. As pointed out by the learned counsel for the assessee, another letter dated 27th May, 2005 thereafter was written by Joint Secretary (FT & TR) to the DGIT, International Taxation enclosing the letters dated 10th December, 2003 and 18th December, 2003 issued in the matter for necessary action. As already noted by us, letter dated 18th December,2003 was written by the Joint Secretary (FT & TR) after 10th December, 2003 clarifying the matter further to the Competent Authority of Switzerland whereby it was agreed that profits from operation of ships in international traffic is not covered specifically by any of the articles of the treaty and that Article 22 of the treaty dealing with other income would fall to be applicable in respect of such income. The letter dated 14th February, 2005 of Joint Secretary (FT & TR) relied upon by the AO to deny the treaty benefit to the assessee company thus was superseded by the letter dated 27th May, 2005 and the reliance of the AO on the letter dated 14th February, 2005 to deny the treaty benefit to the assessee company was clearly misplaced.

45. In Article 3 of Indo-Swiss treaty giving general definitions, the term "competent authority" is defined to mean in the case of India, the Central Government in the Department of Revenue or their authorized representative and in the case of Switzerland, Director of Federal Tax Administration or his authorized representative. Article 25 of the said treaty prescribes the mutual agreement procedure whereby if a resident of a contracting State considers that the action of one or both of the contracting States result or will result for him in taxation not in accordance with this agreement, he may notwithstanding the remedies provided by the national laws of those States, present his case to the competent authority of the contracting States of which he is a resident. As per paragraph 2 of Article 25, the competent authority then shall endeavor, if the objection appears to it to be justified and if it is not itself able to arrive at an appropriate solution, to resolve the case by mutual agreement with the competent authority of the other contracting State, with a view to avoidance of taxation which is not in accordance with

the agreement. As per paragraph 3 of Article 25, the competent authorities of the contracting States shall endeavor to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the agreement. In the present case, such endeavor was made by the competent authorities of Switzerland and India and the doubt arising as to the interpretation of Article 22 was resolved by mutual agreement whereby both the competent authorities agreed that international shipping profits of the assessee company are covered by Article 22.

46. In the case of CIT vs. Arun Dua 186 ITR 494, it was held by the Hon'ble Calcutta High Court at page 496 of the report that if an agreement between two parties has been understood in a certain way and has been acted upon by them, it would not be open to the Tax Officer to give another interpretation to the agreement. In the present context, the Indo-Swiss treaty especially the scope of Article 22 thereof was understood in a certain way as expressed and clarified in the letter dated 29th October, 2003 issued by the Competent Authority of Switzerland and reply thereto given by the Indian Competent Authority by letter dated 18th December, 2003 agreeing that there being no other article of the treaty dealing with profits derived from shipping operations in international traffic, the taxability thereof was governed by Article 22. We are of the view that the revenue authorities in India therefore are not justified to take a different view by assigning different interpretation to the relevant clauses of the treaty than the one understood by both the parties to the said agreement.

47. In support of the Revenue's case on the issue under consideration, Shri Srivastava has heavily relied on the decision of Authority for Advance Ruling in the case of Gearbulk AG (supra) wherein a similar issue has been stated to be decided in favour of the Revenue holding that income derived from operations of ships in international traffic is liable to tax in India as per domestic law rejecting the contention of the assessee that Article 22 of the Indo-Swiss treaty applies to such income and allocates taxing rights to the country of residence i.e. Switzerland. He has contended that although the said decision of Authority for Advance Ruling is not strictly binding on the Tribunal, it has a

grate persuasive value and their being no decision of the Tribunal, High Court or the Supreme Court directly on the issue, the decision of Authority for Advance Ruling deserves to be followed by the Tribunal. We are unable to accept this contention of Shri Srivastava. A perusal of the judgment of the Authority for Advance Ruling passed in the case of Gearbulk AG (supra) shows that the letters exchanged between the Competent Authority of India and Switzerland explaining their understanding as regards the applicability of Article 22 to the international shipping profits were not brought to the notice of the Authority. Moreover, having held at one place that prior to 01-04-2001, such profits were untouched under the Indo-Swiss treaty, the Authority still proceeded to arrive at a conclusion that Article 22 did not apply to such profits which, in our opinion, with due respect, is self contradictory. It is also observed that the Authority while holding that there was no point in excluding shipping profits from Article 7 and including it in Article 22 when both Articles 7 and 22 prescribed PE based taxation, has overlooked the fact that the scope of Article 22 is narrower than the scope of Article 7 inasmuch as Article 22 covers the income which is in respect of a right or property effectively connected to the PE whereas Article 7 covers the profits attributable to the PE. The authority has also not considered the meaning of expression "dealt with" used in Article 22 of the treaty in the context of the purpose of tax treaties which is to allocate jurisdiction as held by Hon'ble Supreme Court in the case of Azadi Bachao Andolan. It has also not appreciated the different expressions i.e. "dealt with" and "mentioned in" used in different treaties and the effect thereof, although the said difference was specifically brought to its notice.

48. In the case of ADIT (International Taxation) vs. Green Emirate Shipping & Travels 100 ITD 203 (Mum.), reliance was placed on behalf of the Revenue on the ruling given by the Authority for Advance Ruling in the case of Abdul Razak A. Meman 276 ITR 306 which was directly applicable to the issue under consideration. The Tribunal, however, declined to treat it as a covered matter relying on the decision of Hon'ble Supreme Court in the case of Azadi Bachao Andolan (supra) wherein it was held that the

ruling given by the Authority for Advance Ruling is not even binding on the Commissioner of Income Tax and authorities sub-ordinate thereto in any case except in the case of the very assessee in which such a ruling was given and that too in respect of transaction in respect of which such ruling was given. It was held by the Tribunal that whatever be the respect and deference judicial authorities indeed have for the rulings given by the authority, the Authority for Advance Ruling not being a part of judicial hierarchy cannot lay down a binding precedence. It was held that the ruling given by the Hon'ble Authority for Advance Ruling, therefore, has no precedence value in general. We are, therefore, unable to accept the plea of Shri Srivastava that the issue under consideration be decided in favour of the Revenue following the decision of the Authority for Advance Ruling in the case of Gearbulk AG (supra) . In our opinion, the item of income in question i.e. international shipping profit cannot be said to be dealt with in any other articles of the Indo-Swiss treaty and the taxability of the said income thus is governed by residuary Article 22 introduced in the treaty with effect from 01-04-2002.

49. Having held that the taxability of international shipping profits is covered by Article 22, it is necessary to ascertain whether the assessee company which received such income being a resident of Switzerland carried on the shipping business in India through a permanent establishment situated therein and whether the property in respect of which such income was paid i.e. ships is effectively connected with such permanent establishment. If both these conditions are satisfied, the international shipping profits will be taken out of Article 22 and will fall in Article 7 as per paragraph 2 of Article 22.

50. As regards the issue as to whether M/s MSC Agency India Pvt. Ltd. constituted permanent establishment of the assessee company in India, it is observed that certain specific information was received by the AO from ACIT, Central Circle-40, Mumbai vide letter dated 31-03-2005 showing that M/s Samasara Shipping P. Ltd. was working as dependant agent of the assessee company in India upto assessment year 2002-03 and the business of the said concern was taken over and continued by M/s MSC Agency India

Pvt. Ltd. from assessment year 2003-04. The said information, gist of which is already given in the foregoing portion of this order, was confronted by the AO to the assessee who took a stand that both M/s Samsara Shipping P. Ltd. and M/s MSC Agency India Pvt. Ltd. were independent agents and did not constitute its PE in India. There was, however, nothing brought on record on behalf of the assessee to support and substantiate its stand. The AO, therefore, did not accept the stand of the assessee and treated M/s MSC Agency India Pvt. Ltd. as dependant agent of the assessee in India on the basis of the following clauses of the agreement dated 01-04-2002 between the assessee company and M/s MSC Agency India Pvt. Ltd. :

"2.00 General Conditions:-

2.01 The agreement covers all ports in the Region and /or inland agency work within the Region nominated in clause 11 and covers the following duties:-

* Sales and Marketing
* Bookings
* Documentation
* Equipment Control
* Equipment Control
* Inland Transportation
* Operations cost control
* Vessel Operations / Husbandry
* Disbursements
* Systems/IT

2.02 The Agents undertake not to accept the representation in the Region of any other Principals for the service in direct competition or with direct conflict of interest with the Principal's activities in section, without written consent, which shall not be unreasonably withheld by the Principals.

3.10 Marketing Sales and Documentation:-

3.11 To provide marketing and sales activities for the services of the Principals in the Region, to canvass for and book cargo, to publicise the services and to maintain contact with Shippers, Consignees, Forwarding Agents, Port and other Authorities and trade organizations.

3.12 To provide statistics and information, and to report on cargo bookings and use of space allocations. To announce sailing and / or arrivals and to quote freight

rates and announce freight traffic and amendments, subject to the freight policies and instructions of the Principals. To provide regular reports and information concerning latest market trends and competition advice developments.

3.13 To arrange for public relations work (including advertising, press…….agreed by the principles.

3.14 To issue, sign and stamp on behalf of the Principals …… to perform these duties.

5.00 Principals' Duties:

5.02 The Principals will provide the Agents with any necessary funds to cover creditors and any advance disbursements in respect of the Principal's business within the region, which may be specifically agreed as items not subtracted from the freight account.

5.03 To pay all statutory charges and taxes (as required by Law) levied by countries in the Region, payable by ship owners / operators / charterers whose ships call at ports in the Region.

6.00 Remuneration:

6.01 The Principals agree to pay the Agents, for the above services rendered by them, the commission set forth in Schedule A to this agreement.

7. Duration:

The Agent confirms that if their current Agency name includes any of the names listed below, or any variation of these names, then, on termination of this agreement, the existing name of their agency shall also cease, and they will no longer have any entitlement to use the following names, or variations thereof:-

MSC
M.S.C.
Mediterranean Shipping Company (or Mediterranean Shipping Co.)

Medite
Medship."

51. After having perused the relevant clauses of the agreement between assessee company and M/s MSC Agency India Pvt. Ltd. as given above, we find ourselves in

agreement with the view of the AO and the learned CIT(Appeals) that M/s MSC Agency India Pvt. Ltd. was legally and economically dependent agent of the assessee company and since the assessee company was managing and controlling some of its business operations in India through the said dependant agent, it constituted the permanent establishment of the assessee company in India in terms of the Indo-Swiss treaty. We are unable to accept the contention raised by Shri Dastur in this regard that M/s MSC Agency India Pvt. Ltd. had limited right to perform its activities and it, therefore, cannot be regarded as habitually exercising an authority to negotiate and enter into contracts for and on behalf of the assessee company which, in our opinion, is contrary to the relevant clauses of the agreement between the assessee company and M/s MSC Agency India Pvt. Ltd. defining the scope and authority of M/s MSC Agency India Pvt. Ltd. and its commitment to work exclusively for the assessee company and not to accept the representation of any other principle for the same services in the same region without the written consent of the assessee company.

52. The next issue that arises for our consideration in this context is whether the property in respect of which international shipping income was received by the assessee company through shipping business carried on in India through the P.E. situated therein i.e. ships was effectively connected with such permanent establishment. The expression "effectively connected" used in this context in the Article 22(2) of the Indo-Swiss treaty is not defined either in the said treaty or even in the domestic law i.e. Income-tax Act. The said term, therefore, has to be understood using the general principles of common law keeping in mind the common uses associated with the phrase. The assessee has filed opinion of Shri Mukul Rohotogi, Additional Solicitor General, Supreme Court of India wherein after referring to the meaning given in the "Webstors Revised Unabridged dictionary" and in the words and phrases, permanent edition, Shri Mukul Rohotogi has opined that the expression "effectively connected" must be understood to mean that there is a powerful, complete or thorough control of the ship by the agency. In his view, the shipping company, however, has no such control whatsoever over the ship and since it is

only working as an agent who makes bookings and perform other ancillary services, it cannot be said that the ship has any effective connection with the agency. He has stated that to say that the ships are effectively connected with the agency would lead to absurd results inasmuch as the agency will be liable to pay tax whenever the ships are plied on international waters even if they do not come to or depart from Indian shores which would result in extending the territorial jurisdiction of Indian Tax Laws. According to him, Article 22(2) brings profits of the PE within the scope of Article 7 only if the relevant income of the PE arises from a right or property effectively connected with such PE which necessarily refers to the ship itself as the property which generates the income is the ship. In the circumstances, when the ships clearly do not form part the assets of the PE in India but are the assets of the non-resident shipping company abroad, the same cannot be said to be effectively connected to such PE. Where the ships are owned or chartered by the non-resident shipping company abroad and the agency PE merely clears inbound cargo and books outbound cargo and carries out similar functions, the ships are clearly not the assets of the PE nor are they any other way effectively connected with the PE. He has thus concluded that the provisions of Article 22(1) of the treaty would be applicable and the profits of shipping operations in international traffic in the case of non-resident shipping company would be taxable in the country of residence i.e. Switzerland and not in India.

53. The assessee has also filed the opinion of Mr. Philip Baker where he has expressed a similar view saying that the property in respect of which the shipping income is paid is the ships which do not form part of the assets of the permanent establishment in India nor can they be said to be otherwise effectively connected with the permanent establishment in India. They are the assets of the shipping company and have no connection with any agency PE in India save that the PE may clear inbound cargo and book outbound cargo which is carried on those ships. Where the ships are owned or chartered by a non-resident shipping company and the agency PE merely clears inbound cargo and books outbound cargo and carries out similar ancillary functions, the ships are clearly not the assets of the

PE nor are they in some other way effectively connected with a permanent establishment. According to him, the concept of "effectively connected" can be applied in practical terms where branch accounts are drawn up for the PE based upon the correct accounting principles where the ships are shown as assets of the branch.

54. In the case of Sumitomo Mitsui Banking Corporation (supra), the Special Bench of this Tribunal had an occasion to consider and interpret the meaning of the term "effectively connected" used in paragraph No. 6 of Article 11 of the Indo-Japanese treaty which reads as under :

> "The provisions of para 1, 2 and 3 shall not apply if the beneficial owner of the interest, being a resident of the contracting State carries on business in the other contracting State in which the interest arises, through a PE situated therein or performs in that other contracting State independent personal services from a fixed base situated therein and the debt claimed in respect of which the interest is paid is effectively connected with such PE or fixed base. In such a case, the provision of Article 7 or Article 4 as the case may be shall apply."

55. The Special Bench in this context noted that the provisions of Article 11(6) of the Indo-Japanese convention were pari-materia to that of Article 11(4) of the OECD Model Convention and after taking into consideration the purpose and scope of Article 11(4) of the OECD Model Convention as explained in paragraph No. 24 and 25.1 of the OECD commentary on Model Tax Convention on Income Tax and on Capital (condensed version) issue in July, 2010, the Special Bench held that the economic ownership of the debt claim not being allocated to the PE, it cannot be said that such debt claim is effectively connected with that PE. The Special Bench thus has taken the economic ownership as the basis or criteria to apply the concept of "effectively connected with". Since the economic ownership of the ships in the present case cannot be said to be allocated to the PE but the same has always remained with the assessee company, we are of the view that it cannot be said that the property in the said ships is effectively connected with the PE in India on the basis of criteria adopted by the Special Bench of this Tribunal in the case of Sumitomo Mitsui Banking Corporation (supra). Shri Srivastava has contended that the expression "effectively connected" is much wider than

the expression "owned". He has contended that effective connection could be by way of ownership or by the operation or maintenance of the property. We are unable to agree with this contention of Shri Srivastava in view of the decision of Special Bench of this Tribunal in the case of Sumitomo Mitsui Banking Corporation (supra) wherein the similar expression has been interpreted as to mean economic ownership. In any case, it cannot be said that the ships owned by the assessee company were exclusively operated or maintained by the PE in India and going by the scope of work to be done by the said PE which was limited.

56. In the OECD commentary on Model Tax Convention on Income and on Capital (condensed version) published in July, 2010, the term used in paragraph 21(1) of the Model Convention, (similar to Article 22(1) of the Indo-Swiss Treaty) viz. a right or property in respect of which income paid will be effectively connected with a permanent establishment has been explained. It is stated that for the purposes of paragraph 21(1), a right or property in respect of which income paid will be effectively connected with a PE if the economic ownership of that right or property is allocated to that PE. It is stated that the economic ownership of a right or property in this context means the equivalent of ownership for income-tax purposes by a separate enterprise with the attended benefits and burdens (e.g. the right to the income attributable to the ownership of the right or property, the right to any available depreciation and judicial exposer to gains or losses from the appreciation or depreciation of that right or property).

57. Keeping in view the relevant portion of the OECD commentary on Model Tax Convention on Income and on Capital (condensed version) published in July, 2010 and the ratio of the decision of Special Bench of this Tribunal in the case of Sumitomo Mitsui Banking Corporation (supra) as also the opinion of Philip Baker and Mr. Mukul Rohotogi which conforms to the said ratio, we are of the view that the right or property in respect of which the shipping income is earned by the assessee i.e. ships cannot be said to be effectively connected with the permanent establishment in India . Such income, therefore, will not fall under Article 22(2) but will fall under Article 22(1) and accordingly shall be

taxable only in the State of residence of the assessee company i.e. Switzerland and not in India. In that view of the matter, we uphold the impugned order of the learned CIT(Appeals) holding that the international shipping profits of the assessee company are covered by Article 22 of the Indo-Swiss treaty and although the assessee company had a PE in India in the year under consideration, the ships i.e. the property in respect of which shipping income was paid to the assessee company being not effectively connected with that PE, the case of the assessee will be out of paragraph No. 2 of Article 22 and will fall in paragraph 1 of the said article. Consequently, the same will be taxable in the country of residence of the assessee company i.e. Switzerland and not in India.

58. As regards the alternative contention of Shri Dastur that no portion of the international shipping profits earned by the assessee in any case can be taxed in India as the commission paid to M/s MSC Agency India Pvt. Ltd. which constituted its PE is admittedly at an arm's length, it is observed that this alternative claim of the assessee has now become academic in view of our decision accepting the main contention of the assessee that the international shipping profits are chargeable to tax only in Switzerland as per Article 22(1) and not in India. We, therefore, do not deem it necessary or expedient to dwell upon this alternative claim of the assessee.

59. In the result, the appeal of the Revenue and the cross objection of the assessee are dismissed.

Order pronounced on this 6th day of Nov., 2012.

Sd/-	Sd/-
(I.P. Bansal)	(P.M. Jagtap)
Judicial Member	Accountant Member

Mumbai,
Dated: 6th Nov., 2012.

Copy to :

1. Appellant
2. Respondent
3. C.I.T.
4. CIT(A)
5. DR, L-Bench.

(True copy)

By Order

Asstt. Registrar,

ITAT, Mumbai Benches, Mumbai.

Wakode