IN THE INCOME TAX APPELLATE TRIBUNAL

'D' BENCH, CHENNAI

BEFORE SHRI ABRAHAM P. GEORGE, ACCOUNTANT MEMBER
AND SHRI CHALLA NAGENDRA PRASAD, JUDICIAL MEMBER

I.T.A. Nos. 1505 & 1506/Mds/2010
Assessment Years : 2006-07 & 2007-08

M/s Apollo Hospital Enterprises Ltd., Ali Towers, IV Floor, 55, Greams Road, Chennai - 600 006.	v.	The Deputy Commissioner of Income Tax, Company Circle I(1), Chennai - 600 034 .
PAN : AAACA5443N (Appellant)		(Respondent)

I.T.A. Nos. 1573 & 1574/Mds/2010
Assessment Years : 2006-07 & 2007-08

The Deputy Commissioner of Income Tax, Company Circle I(1), Chennai - 600 034 .	v.	M/s Apollo Hospital Enterprises Ltd., Ali Towers, IV Floor, 55, Greams Road, Chennai - 600 006.
(Appellant)		(Respondent)

Assessee by : Shri T. Banusekar, CA
Revenue by : Shri Anirudh Rai, CIT-DR

Date of Hearing : 12.06.2012
Date of Pronouncement : 21.06.2012

O R D E R

PER ABRAHAM P. GEORGE, ACCOUNTANT MEMBER :

These are cross appeals of assessee and Revenue respectively for assessment years 2006-07 and 2007-08, directed against the orders

dated 28.6.2010 of Commissioner of Income Tax (Appeals)-III, Chennai, for respective assessment years.

2. Except for one issue appearing in the appeal of the Revenue for assessment year 2007-08, other issues are common and therefore, these appeals are disposed of through a consolidated order.

3. For both the assessment years, assessee as well as Revenue are aggrieved against the order of CIT(Appeals) with regard to disallowance made under Section 14A of Income-tax Act, 1961 (in short 'the Act').

4. Short facts apropos are that assessee had received dividend of ₹ 6,11,76,086/- and ₹ 3,88,26,878/- for the previous years relevant to assessment years 2006-07 and 2007-08 respectively, which were claimed as exempt under Section 10(34) of the Act. As per the assessee, it had not incurred any expenditure for earning such income. However, Assessing Officer was of the opinion that assessee would have incurred routine expenditure for maintaining establishment and administrative set up as also some managerial remunerations, in relation to exempt income. Assessing Officer also noted that assessee had incurred interest expenditure of ₹ 11,56,39,871/- and ₹ 16,42,39,101/- for the respective previous years. Though the assessee had denied any borrowed capital being utilized for the investment made, resulting in dividend income, Assessing Officer did not accept this plea. For both

the years, he applied Rule 8D of Income-tax Rules, 1962 and made disallowance to the tune of ₹ 4,29,50,325/- and ₹ 6,46,48,754/- respectively.

5. In its appeals before CIT(Appeals), argument of the assessee was that no borrowed capital was utilized for making the investment and the dividend income received was directly remitted to the bank account. As per the assessee, there was no expenditure which had nexus with the utilization of funds invested for earning tax-free income. CIT(Appeals), after considering such submissions, was of the opinion that assessee itself had admitted ₹ 10,25,638/- and ₹ 14,79,568/- for the respective previous years as expenses incurred in its treasury department. As per the CIT(Appeals), there were no fresh borrowings made by the assessee during the previous year relevant to assessment year 2006-07. For the previous year relevant to assessment year 2007-08, own funds were available to the assessee which exceeded the investment. Therefore, according to him, there was no interest expenditure attributable to the earning of exempt income. Nevertheless, CIT(Appeals) was of the opinion that an addition to ₹ 10,25,638/- and ₹ 14,79,568/-, admitted by the assessee as attributable to the treasury department working was warranted. He also ruled that Rule 8D required a further ½ % disallowance on the investments yielding the exempt income. The

disallowances were thus restricted to ₹ 1,05,07,198/- and ₹ 1,63,78,457/- for the respective assessment years.

6. Now before us, learned D.R., strongly assailing the order of CIT(Appeals), submitted that Rule 8D was correctly applied by the Assessing Officer for the respective assessment years and interest disallowance were correctly made. The CIT(Appeals) had without any reason, deleted such interest disallowances based on the workings given by the assessee. According to him, the disallowances, which were correctly worked out by the A.O., were disturbed by the CIT(Appeals) and such disallowances were to be reinstated in full.

7. Per contra, learned A.R., assailing the order of CIT(Appeals) insofar as he sustained disallowance of ½% of the investment yielding exempt income, submitted that though CIT(Appeals) was correct in his finding that there were no interest expenses relatable to investment yielding the dividend income, he had erroneously applied Rule 8D and made a disallowance of ½% of investment yielding exempt income, which was not warranted. According to him, contention of the assessee all along was that no expenditure whatsoever was incurred for the purpose of earning the exempt income and this was not considered by the lower authorities.

8. We have perused the orders and heard the rival submissions. We find that the A.O. as well as CIT(Appeals) had applied Rule 8D for the purpose of determining disallowance to be made under Section 14A of the Act. Hon'ble Bombay High Court in the case of Godrej and Boyce Mfg. Co. Ltd vs. Dy. CIT (328 ITR 81), has clearly held that Rule 8D applied only prospectively with effect from assessment year 2008-09. Therefore, Rule 8D was not applicable for the impugned assessment years. Nevertheless, their Lordship in that decision also held that though the said rule was not applicable for the earlier years, Assessing Officer was duty bound to compute the disallowance by applying reasonable method having regard to the facts and circumstances of the case. Since the disallowances were made applying a rule which was not applicable for the impugned assessment years, we are of the opinion that the matter requires a re-visit by the Assessing Officer. We, therefore, set aside the orders of authorities below on this issue and remit the matter back to the file of the A.O. for consideration afresh in accordance with law.

9. Thus, Ground No.2 of the Revenue for assessment year 2006-07, Ground No.3 of the Revenue for assessment year 2007-08 as well as the sole ground raised by the assessee in their cross appeals are allowed for statistical purposes.

10. This leaves us with the only other ground raised by the Revenue for assessment year 2007-08. This ground relates to an issue regarding taxing capital gains arising out of sale of certain shares held by the assessee-company in a company incorporated in Sri Lanka.

11. Short facts apropos are that assessee was holding shares in a company called M/s The Lanka Hospitals Corporation Ltd., incorporated in Sri Lanka. The said shares were sold by the assessee during the relevant previous years. This resulted in a profit of ₹ 32,50,68,449/-. The amount was accounted by the assessee under the head "Extraordinary items". However, while computing the taxable income, assessee excluded such profits. The A.O., during the course of assessment proceedings, required the assessee to explain why the income from sale of shares should not be taxed in India as capital gains. Reply of the assessee was that the said sale of shares in the Sri Lankan company were governed by Article 13(4) of Double Taxation Avoidance Agreement (DTAA) between India and Sri Lanka, and such gains were taxable only in Sri Lanka. As per the assessee, Section 13(t) of the Inland Revenue Act No.10 of 2006 of Sri Lanka exempted the profits derived from sale of shares where such sale had attracted share transaction levy. Reliance was placed by the assessee on the decision of Hon'ble Apex Court in the case of Union of India v. Azadi Bachao Andolan (263 ITR 706). As per the assessee, the provisions of DTAA

overrode the provisions of the Act. Assessee also pointed out to the A.O. that Notification No.90 of 2008 dated 28th August, 2008 defining the scope of words "may be taxed" would not be applicable to it, since the right to tax capital gains solely rested with Sri Lanka. However, the A.O. was not impressed. According to him, Section 5 of the Act clearly stipulated that income of a resident included all income from whatever source derived. As per the A.O., assessee was resident in India and therefore, it had to be subjected to tax in India for the global income. Nevertheless, assessee could take benefit of DTAA. A.O. observed that there were two methods provided for elimination of double taxation, namely, Income Exclusion Method and Tax Credit Method. In DTAA, the words "shall be taxed" and "may be taxed" were used with different meaning and Notification No.90 of 2008 (supra) would clearly apply when dealing with the income of a resident in India. The expression used in Article 13(4) of DTAA was "may be taxed" and therefore, according to the A.O., both the countries had the right to tax such income. Hence, according to him, Income Exclusion Method would not be applied for mitigating the double taxation effect. Only the other method namely, Tax Credit Method could be applied. According to him, Article 24 of DTAA specified only Tax Credit Method and under the Tax Credit Method, the tax credit had to be given to the assessee, for the tax paid in Sri Lanka on such capital gains. Since no tax was paid, there

was no scope for any tax credits. In other words, according to A.O., the profit arising out of capital gains arising on sale of shares was to be taxed in India in full. As for the reliance placed by the assessee on the decision of Hon'ble Apex Court in the case of Azadi Bachao Andolan (supra), view of the A.O. was that treaty provisions did override the provisions of the Act. However, when the words used in the treaty where such that 'Income Exclusion Method' could not be used, then it was well within his power to tax such income in India after giving due credit for the tax paid in the country where the capital gains arose. For taking this view, reliance was placed on the decision of co-ordinate Bench of this Tribunal in the case of CIT v. Data Software Research Co. Ltd. in I.T.A. No. 2072(Mds)/2006 dated 27.11.2007. Thus, he worked out the capital gains arising out of the sale of shares, which came to ₹ 32,46,30,249/- as long term and ₹ 4,38,200/- as short term.

12. In its appeal before CIT(Appeals), argument of the assessee was that Article 13(4) of the DTAA stood in favour of assessee. As per the assessee, Notification No.90 of 2008 (supra) relied on by the Assessing Officer was not at all applicable in its case. Shares of The Lanka Hospitals Corporation Ltd., which were sold, was issued in Sri Lanka and therefore, the gains from transfer was taxable only in Sri Lanka. For trading done thorugh the Colombo Stock Exchange, the turnover was subjected to a levy called "share transaction levy" by the Finance Act

No.5 of 2005 of Sri Lanka. On account of imposition of the share transaction levy, by virtue of Section 13(t) of the Inland Revenue Act No.10 of 2006 of Sri Lanka, the profits derived from sale of share on which such share transaction levy was charged, became exempt. Thus, the gains on transfer of share of The Lanka Hospitals Corporation Ltd. was exempt in the hands of the assessee-company in Sri Lanka. As per the assessee, the phrase "liable to taxation" was not same as "pay tax". Liability for taxation was not to be determined on the basis of exemption granted in respect of any particular source of income but, taking into account the totality of the provisions of the tax laws prevailing in contracting States. Just because the entity was not to pay any tax due to an exemption provision, it would not mean that the sale amount will be taxed in the other contracting State. As for the reliance placed by the A.O. on the decision of co-ordinate Bench of this Tribunal in the case of Data Software Research Co. Ltd. (supra), argument of the assessee before the CIT(Appeals) was that the said decision was rendered in the context of taxability of business income of an overseas branch under Article 7 of DTAA between India and USA. As per this Article, profits were taxable in contracting State of residence unless there was a permanent establishment in the other contracting State. Here, on the other hand, the income was neither business income nor the assessee had any permanent establishment in Sri Lanka. The Sri Lankan

company also did not have any permanent establishment in India. Insofar as reliance on Article 24 of the DTAA was concerned, argument of the assessee was that the Tax Credit Method for elimination of double taxation could be used only where both the countries had a right to tax the income. The terms "may be taxed" did not mean that the income was taxable in both the countries. Ld. CIT(Appeals) was appreciative of the these contentions of the assessee. According to him, the share transaction levy on shares transacted through the Colombo Stock Exchange in Sri Lanka, was akin to security transaction tax in India. According to him, Section 10(38) of the Act gave exemption for the gains arising out of transfer of shares on which security transaction tax was levied. Similarly, in Sri Lanka on transaction of shares, where share transaction levy was charged, the surplus arising out of such transaction was exempt under Inland Revenue Act of that country. According to him, the interpretation given by the Assessing Officer to Article 13(4) of DTAA was not in consonance with the language and spirit of the Treaty. Ld. CIT(Appeals) was of the opinion that only Sri Lanka had the right to tax capital gains on sale of shares of The Lanka Hospitals Corporation Ltd., since the latter company was incorporated in Sri Lanka. According to him, the scheme of the DTAA clearly substantiated the contention of the assessee that the country of a resident did not get the right or mandate to tax capital gains arising in the other country, namely, Sri Lanka.

Reliance was placed by the CIT(Appeals) on the decision of Hon'ble Apex Court in the case of CIT v. P.V.A.L. Kulandagan Chettiar (267 ITR 654) and also the decision of Hon'ble Madhya Pradesh High Court in the case of DCIT v. Turquoise Investment & Finance Ltd. (299 ITR 143), which was later affirmed by Hon'ble Supreme Court in 300 ITR 1. He approved the contention of the assessee that Article 24 of DTAA could be invoked only when income was taxable in both the countries. As for the reliance placed on the decision of co-ordinate Bench of this Tribunal in the case of Data Software Research Co. Ltd. (supra), CIT(Appeals) was of the opinion that the Indo-US Treaty was not at par with Indo-Sri Lanka Treaty on double taxation. In Indo-US Treaty, both the countries were empowered to tax business income, subject to certain conditions, while this was not the case in Indo-Sri Lanka Treaty. In this view of the matter, he held that capital gains on sale of shares of The Lanka Hospitals Corporation Ltd. was not taxable in India.

13. Now before us, learned D.R., strongly assailing the order of CIT(Appeals), submitted that Article 13 of DTAA did not exclude the power of India to tax a long term capital gains arising to an assessee, which was a resident in India, on account of transaction in Sri Lanka. According to him, the term used was "may be taxed" and it could not be interpreted to mean that the other contracting State was excluded completely from considering such income. As per the learned D.R., from

Section 5 of the Act, it was clear that the total income of a resident had to be considered for the purpose of charging of income-tax. Relying on Notification No.90 of 2008 (supra), learned D.R. submitted that the words “may be taxed” were clearly interpreted by the CBDT. As per this interpretation, the income coming within the purview of Article 13 of DTAA has to be included in the total income chargeable to tax in India, in accordance with provisions of Indian Income-tax Act. The relief that could be granted to the assessee was based on the method of elimination by giving tax credit relief. According to learned D.R., the A.O. had applied Article 24 of DTAA, finding that ‘NIL’ tax was charged on the capital gains in Sri Lanka and therefore, no tax credit was available to the assessee in India. According to him, capital gains in the case of a resident in India on account of transaction arising outside India, had to be considered as a part of its income based on Section 5 of the Act. Relying on the decision of co-ordinate Bench of this Tribunal in the case of Data Software Research Co. Ltd. (supra), learned D.R. submitted that even though it related to Indo-US Double Taxation Avoidance Agreement, profits of an assessee who was a resident in India, was held to include profits acquired in its US Branch also. As per the learned D.R., this Tribunal had clearly considered the two methods for elimination of double taxation, namely, exemption method and tax credit method and, thereafter, came to a conclusion that the said double

taxation treaty did not anywhere prescribed that the profits arising in USA for a resident would be exempt from taxation in India. Therefore, according to him, the Assessing Officer rightly relied on the said decision and applied Tax Credit Method for eliminating the double taxation. Here, in the case of assessee, there being no capital gains arising in Sri Lanka on account of the share transaction levy, there was nothing whatsoever given as tax credit. Hence, the learned D.R. submitted that the addition made by the A.O. under the head "capital gains" had to be sustained.

14. Per contra, learned A.R. submitted that the question here was whether the terms "may be taxed" appearing in Article 13(4) gave an exclusive right to the contracting State, excluding the other contracting State or give right to both the States for taxing the income. Relying on the decision of Hon'ble Apex Court in the case of P.V.A.L. Kulandagan Chettiar (supra), learned A.R. pointed out that the issue there was regarding taxing of income from immovable property in Malaysia. According to him, the terminology used in Double Taxation Avoidance Agreement with Malaysia was also "may be taxed" and Hon'ble Apex Court clearly held that the treaty had to be interpreted as though it prevailed over Section 4 and 5 of the Act. According to learned A.R., Hon'ble Apex Court held that residency in India would become irrelevant when DTAA applied. Placing reliance on the decision of Hon'ble Madhya Pradesh High Court in the case of Turquoise Investment &

Finance Ltd. (supra), learned A.R. submitted that provisions regarding tax credit for elimination of double tax, would be applicable only if tax was payable in both the countries. Being exempt from tax would not render the assessee not liable to tax. The moment Section 13(t) of the Inland Revenue Act of Sri Lank was deleted, the gains arising on transfer of shares would be taxed in Sri Lanka. The gains were always liable to tax in Sri Lanka, but, by virtue of exemption provision, it was not taxed. In such a situation, according to him, exclusion method had to be given preference over the Tax Credit Method. Relying on the decision of Indore Bench of this Tribunal in the case of ACIT v. Turquoise Investment & Finance Ltd. (89 ITD 155), which was affirmed by Madhya Pradesh High Court, learned A.R. submitted that long term capital gains arising in Sri Lanka would not be taxable in India at all. Once such income was considered to be not taxable because of specific exclusion clause in the taxing enactment of Sri Lanka, there was no question of any credit being given, but on the other hand, the whole of the income had to be excluded while computing the total income of the resident-assessee in India. Specific attention was invited to Article 7 of DTAA with Sri Lanka, by virtue of which business profits could be taxed in the contracting State only to the extent it was attributable to the permanent establishment or sales through such permanent establishment or other business activities carried on similar nature. According to him, Article 7

gave rise to a situation where the income could be taxed in both contracting States. Article 24 which provided for tax credit for taxes paid in one contracting country, would be applicable in such a situation. On the other hand, according to him, Article 13 clearly established that capital gains arising on sale of shares was to be taxed in the contracting State in which such stock or share were issued. Coming to the aspect of Notification No.90 of 2008 (supra) relied on by the learned D.R., it was submitted that the said Notification was with reference to Section 90A of the Act. As per the learned A.R., the said Notification was, undisputedly issued under sub-section (3) of Section 90A of the Act. A notification given under the said Section would be applicable only to a type of agreement mentioned in sub-section (1) of Section 90A of the Act and it could not be applied to a Double Taxation Avoidance Agreement between countries. In any case, according to him, the said notification was issued only on 28th August, 2008 and could be applied retrospectively.

15. We have perused the orders and heard the rival submissions. There is no dispute that assessee is a resident of India as per Income-tax Act. Assessee had capital gains which arose in Sri Lanka. Such capital gains arose on account of sale of shares of one company which was incorporated in Sri Lanka. Such sale of shares effected in Sri Lanka was subjected to share transaction levy imposed in that country, as per

Finance Act 5 of 2005 of that country. It is also not disputed that under Section 13(t) of Inland Revenue Act No.10 of 2006 of that country, profits and income derived from sale of any share on which share transaction levy was charged, was exempt from income-tax. The question to be resolved is whether in such a situation, based on the DTAA between India and Sri Lanka, the capital gains arising to the assessee on account of sale of such shares, could be considered as part of its income for the purpose of Income-tax Act or whether it was to be excluded in toto. Stand of the Assessing Officer was that such capital gains had to be included as a part of income of the assessee in view of Section 5 of Income-tax Act, 1961, but nevertheless, assessee was entitled to tax credit for the taxes, if any paid in Sri Lanka. Stand of the assessee is that capital gains was solely taxable in Sri Lanka as per the DTAA and therefore, such income automatically stood excluded from its income as per the Income-tax Act in India. Relevant Article relied on by the assessee is Article 13 of the DTAA which reads as under:-

"Article 13: CAPITAL GAINS

1. Gains derived by a resident of a Contracting State from the alienation of immovable property referred to in paragraph 2 of Article 6 and situated in the other Contracting State may be taxed in that other State.
2. Gains from the alienation of immovable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in other Contracting State, including such gains from the alienation of such a permanent

establishment (alone or with the whole enterprise), may be taxed in that other State.

3. Gains from the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.
4. Gains from the alienation of stocks and shares of a company may be taxed in the Contracting State in which they have been issued.
5. Gains from the alienation of any property other than that referred to in paragraphs 1 to 4 of this Article, shall be taxable only in the Contracting State of which the alienator is a resident.
6. The term "alienation" means the sale, exchange, transfer, or relinquishment of the property or the extinguishment of any rights therein or the compulsory acquisition thereof under any law in force in the respective Contracting State."

Case of the assessee falls under clause 4. It says that gains from alienation of shares "may be taxed" in the State of issue. Argument of the assessee is that the term "may be taxed" give exclusive power to tax such income only to Sri Lanka and such income could not be considered as part of income, under Indian Income-tax Act. No doubt, if we consider the term "may be taxed" as not excluding the power to tax such amount in India, then assessee would have to be given benefit of tax credit for taxes if any paid in Sri Lanka for elimination of double taxation. So, the entire issue hinges on the meaning to be attached to the words "may be taxed". If such term excluded the power of India to tax the amount of capital gains, arising out of transfer of shares of a company in Sri Lanka, then there was no question of application of Tax Credit Method. This is because such gain, by virtue of such an interpretation,

will automatically get out of the ambit of "income" as per Income-tax Act, though Section 5 of the Act mandates otherwise. Hon'ble Apex Court in the case of Azadi Bachao Andolan (supra), as relying on Philip Baker's commentary on OECD Double Taxation Convention, noted that a person did not need to be actually paying tax to be "liable to tax". At para 64 of the judgment, their Lordship agreed with the view that merely because an exemption was granted in respect of taxability of a particular income, it cannot be postulated that the entity concerned was not "liable to tax". A person, who would have been otherwise subject to capital gains tax but, who enjoyed specific exemption from tax in the income originating country, was nevertheless, liable to tax in such country, since if such exemption was repealed, the person would automatically become liable to tax there. Co-ordinate Bench of this Tribunal in the case of Ms.Pooja Bhatt v. DCIT (2009) 22 DTR 458 had an occasion to consider the meaning of the term "may be taxed" as relevant to Indo-Canada Double Taxation Avoidance Agreement. Para 7 of the order dated 20th October, 2008, is reproduced hereunder:-

> "7. After giving our due consideration to the above rival contentions, we are of the humble view that income derived by the assessee from the exercise of her activity in Canada is taxable only in source country, i.e. Canada for the reasons given hereafter. The scheme of taxation of income is contained in Chapter III of DTAA/Indo-Canada Treaty. On an analysis of various articles contained in Chapter III, we find that the scheme of taxation is divided in three categories. The first category includes art. 7

(business profits without PE in the other State), art. 8 (air transport), art. 9 (shipping), art. 14 (capital gains on alienation of ships or aircrafts operated in international traffic), art. 15 (Professional services), art. 19 (pensions) which provide that income shall be taxed only in the State of residence. The second category includes art. 6 (income from immovable property), art. 7 (business profits where PE is established in other Contracting State), art. 15 (income from professional services under certain circumstances), art. 16 (income from dependent personal services where employment is exercised in other Contracting State), art. 17 (director's fees), art. 18 (income of artists and athletes), art. 20 (Government service) which provide that such income may be taxed in the other Contracting State, i.e. State of income source. The third category includes art. 11 (dividends), art. 12 (interest), art. 13 (royalty and fee for technical services), art. 14 (capital gains on other properties) and art. 22 (other income) which provide that such income may be taxed in both the Contracting States. For example, para 1 of art. 11 provides that dividend income may be taxed in other Contracting State while para 2 provides that dividend income may also be taxed in the State of residence. Similarly, art. 14(2) and art. 22 provide that income may be taxed in both the countries. The above analysis clearly shows that intention of parties to the DTAA is very clear. Wherever the parties intended that income is to be taxed in both the countries, they have specifically provided in clear terms. Consequently, it cannot be said that the expression "may be taxed" used by the contracting parties gave option to the other Contracting States to tax such income. In our view, the contextual meaning has to be given to such expression. If the contention of the Revenue is to be accepted then the specific provisions permitting both the Contracting States to levy the tax would become meaningless. The conjoint reading of all the provisions of articles in Chapter III of Indo-Canada treaty, in our humble view, leads to only one conclusion that by using the expression "may be taxed in the other State", the contracting parties permitted only the other State, i.e. State of income source and by implication, the State of residence was precluded from taxing such income. Wherever the contracting parties intended that income may be taxed in both the countries, they have specifically so provided. Hence, the contention of the Revenue that the expression "may be taxed in other State" gives the option to the other State and the State of residence is not precluded from taxing such income cannot be accepted."

While coming to this view, co-ordinate Bench had considered the decision of Hon'ble Apex Court in the case of P.V.A.L. Kulandagan Chettiar (supra) as well as the decision of Hon'ble jurisdictional High Court in the case of CIT v. VR.S.R.M. Firm (208 ITR 400) where the terms "may be taxed" were analysed. Thus, what comes out of the above analysis is that when the term "may be taxed" is used in a treaty, there is an automatic exclusion of other State. Wherever both the countries are having right to tax a particular income, the DTAA had clearly spelt it out. As pointed out by the learned A.R., in the case of business income, there is a possibility that the income could be taxed in both Contracting States vide Article 7. In such a situation, Article 24 would apply and will call for application of Tax Credit Method for avoiding double taxation. Assessing Officer himself had admitted that only two methods were available for elimination of double taxation – (i) Income Exclusion Method, and (ii) Tax Credit Method. According to him, there is nothing whatever in the treaty for applying an Income Exclusion Method, since Article 24 thereof dealt with only Tax Credit Method. In our opinion, this view of the Assessing Officer was incorrect. It is for the reason that such exclusion is built-in to the words "may be taxed" appearing in Article 13(4) of the DTAA. When there is total exclusion, it would not be necessary to have a separate article prescribing a method for avoiding double taxation. That when there is a

beneficial provision available to an assessee under a treaty, it could rely on such provision is a position of law which stands more or less accepted though various rulings which now have attained finality.

16. Now coming to Notification No.90 of 2008 (supra) relied on by the learned D.R., the term "may be taxed" of course has been interpreted in such notification. The said Notification is reproduced hereunder:-

> NOTIFICATION NO. 90 OF 2008, DT. 28TH AUGUST, 2008
>
> 28/08/2008
>
> Scope of words "may be taxed"
>
> DOUBLE TAXATION RELIEF
>
> SECTION 90A
>
> In exercise of the powers conferred by sub-section (3) of section 90A of the Income-tax Act, 1961(43 of 1961), the Central Government hereby notifies that where an agreement entered into by any specified association in India with any specified association in the specified territory outside India and adopted by the Central Government by way of notification in the official Gazette, for granting relief of tax, or as the case may be, avoidance of double taxation, provides that any income of a resident of India "may be taxed" in the other country, such income shall be included in his total income chargeable to tax in India in accordance with the provisions of the Income-tax Act, 1961 (43 of 1961), and relief shall be granted in accordance with the method of elimination or avoidance of double taxation provided in such agreement.

The notification having been issued under Section 90A(3) of the Act, it calls for a look at Section 90A. Said Section reads as under:

Adoption by Central Government of agreement between specified associations for double taxation relief.

90A. (1) Any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for adopting and implementing such agreement—

(*a*) for the granting of relief in respect of—

(*i*) income on which have been paid both income-tax under this Act and income-tax in any specified territory outside India; or

(*ii*) income-tax chargeable under this Act and under the corresponding law in force in that specified territory outside India to promote mutual economic relations, trade and investment, or

(*b*) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that specified territory outside India, or

(*c*) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that specified territory outside India, or investigation of cases of such evasion or avoidance, or

(*d*) for recovery of income-tax under this Act and under the corresponding law in force in that specified territory outside India.

(2) Where a specified association in India has entered into an agreement with a specified association of any specified territory outside India under sub-section (1) and such agreement has been notified under that sub-section, for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette[76] in this behalf.

Explanation 1.—For the removal of doubts, it is hereby declared that the charge of tax in respect of a company incorporated in the specified territory outside India at a rate higher than the rate at

which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such company.

Explanation 2.—For the purposes of this section, the expressions—

(*a*) "specified association" means any institution, association or body, whether incorporated or not, functioning under any law for the time being in force in India or the laws of the specified territory outside India and which may be notified[76] as such by the Central Government for the purposes of this section;

(*b*) "specified territory" means any area outside India which may be notified[76] as such by the Central Government for the purposes of this section.]

It is clear that the above section enabled the Central Government to adopt an agreement entered into between specified associations, for according double tax relief. In other words, it was a methodology for giving official stamp to a private agreement entered between two parties. The agreement mentioned in sub-section (3) of said Section is that which is referred in sub-section (1). Sub-section (1) only deals with agreements between a specified association in a specified territory outside India and a specified association in India. Sub-section (3) gives the power to the Central Government to notify the meanings assigned to any term in such an agreement. The power given in sub-section (3) is limited to defining the terms in an agreement between specified persons. This power cannot be expanded or interpreted in such a way that it would include a power to define terms in a DTAA between countries as well. When a notification is issued exercising the powers conferred under sub-section (3) of Section 90A of the Act, it can have effect only

on those types of agreement mentioned in sub-section (1) thereof. If such a notification goes beyond that mandate, it will have to be ignored to the extent it goes overboard. Even if the term “may be taxed” has been given a meaning by the Government through a Notification No.90A(3) of the Act, so as to extend such meaning to terms used in a Double Taxation Avoidance Agreement, it will have to be ignored. We are, therefore, of the opinion that the said Section 90A cannot come to the aid of the Revenue in any manner at all.

17. For the reasons mentioned above, we are of the opinion that Exclusion Method was the appropriate one and this was rightly used by the CIT(Appeals). The capital gains arising on account of transfer of share in Sri Lanka would not exigible to tax in India in the given circumstances. We do not find any reason to interfere with the order of CIT(Appeals).

18. Ground No.2 of the Revenue for assessment year 2007-08 stands dismissed.

19. To summarize results, appeals of the assessee for assessment years 2006-07 and 2007-08 are allowed for statistical purposes. Appeal of the Revenue for assessment year 2006-07 is allowed for statistical purposes. Appeal of the Revenue for assessment year 2007-08 is partly allowed for statistical purposes.

The order was pronounced in the Court on Thursday, the 21st of June, 2012, at Chennai.

sd/-	sd/-
(Challa Nagendra Prasad)	(Abraham P. George)
Judicial Member	Accountant Member

Chennai,
Dated the 21st June, 2012.

Kri.

Copy to:
(1) Assessee
(2) Assessing Officer
(3) CIT(A)-III, Chennai
(4) CIT, Chennai-I, Chennai
(5) D.R.
(6) Guard file