Reserved Judgment

IN THE HIGH COURT OF UTTARAKHAND AT NAINITAL

Income Tax Appeal No. 49 of 2005
(Assessment Year 1997-98)

1. The Commissioner of Income-tax, Dehradun.
2. Additional Commissioner of Income-tax, Special Range, Dehradun.

...……. Appellants

Versus

M/s Foramer France
(Presently known as Pride Foramer)
C/o S.P. Puri & Company, C.A.
4 / 18, Asaf Ali Road, New Delhi –02.

...……. Respondent

Mr. Arvind Vashisth, Standing Counsel for the appellants.
Mr. Kaanan Kapur, Advocate with Mr. L.K. Tiwari, Advocate for the respondent-assessee.

Along with

Income Tax Appeal No. 91 of 2006
(Assessment Year 1996-97)

The Commissioner of Income-tax, Dehradun.

...……. Appellant

Versus

M/s Pride Foramer S.A.
C/o S.P. Puri & Company,
4 / 18, Asaf Ali Road, New Delhi.

...……. Respondent

Mr. Arvind Vashisth, Standing Counsel for the appellants.
Mr. Kaanan Kapur, Advocate with Mr. L.K. Tiwari, Advocate for the respondent-assessee.

And

Income Tax Appeal No. 98 of 2006
(Assessment Year 1999-2000)

The Commissioner of Income-tax, Dehradun.

...……. Appellant

Versus

M/s Pride Foramer S.A.
C/o S.P. Puri & Company,
4 / 18, Asaf Ali Road, New Delhi.

...……. Respondent

Mr. Arvind Vashisth, Standing Counsel for the appellants.
Mr. Kaanan Kapur, Advocate with Mr. L.K. Tiwari, Advocate for the respondent-assessee.

Coram : Hon'ble Prafulla C. Pant, J.
Hon'ble B. S. Verma, J.

[Per Hon'ble Prafulla C. Pant, J.]

In all these three appeals, preferred under Section 260-A of the Income Tax Act, 1961, common questions of law are involved, as such, the appeals are being taken up together, for their disposal. At the outset, it is pertinent to mention here, that Income Tax Appeal No. 91 of 2006 and Income Tax Appeal No. 98 of 2006, are being reheard and disposed of in compliance of order dated 13th of October 2008, passed by the Apex court in Civil Appeal No. 6105 of 2008 and Civil Appeal No.

6106 of 2008. The common questions of law involved in these appeals are as under:

1) ***Whether, the assessee, a non-resident company, was entitled to claim deduction for expenses incurred by it between the period 1993-1999, particularly, when according to the Department there was no permanent establishment in existence in India during the relevant period?***

2. ***Whether, the Income Tax Appellate Tribunal has erred in law in holding that the expenses claimed by the assessee were allowable and constitute business loss to be set off under Section 71 of the Income Tax Act, 1961?***

2) Brief facts of the case relating to Income Tax Appeal No. 91 of 2006, are that the respondent / assessee, a non-resident company, entered into contract with Oil and Natural Gas Corporation (for short ONGC) in connection with the work of drilling operations in oil exploration. Business under the contract was to be completed by the end of 1993. Thereafter, the respondent / assessee made efforts for its business, but could get fresh contract only in the year 1999. The assessee M/s Pride Foramer S.A. has its office in France. The respondent / assessee filed its return for the assessment year 1996-97, showing NIL income. The return reflects that there was income of Rs. 1,69,57,395/- as receipt on account of interest

received on income tax refunds to the assessee, and against those receipts, the assessee has shown expenses of Rs. 2,40,000/- towards administrative charges; Rs. 10,000/- towards audit fee and Rs. 788/- towards depreciation in furniture and fixtures. The Assessing Officer (Deputy Commissioner of Income-tax, Dehradun) [for short A.O.] rejected the claim of the assessee on account of expenses for the year, as the assessee did not carry any business during that period in India, and held that no set off is allowable under Section 71 of the Income Tax Act, 1961 (for brevity hereinafter referred as the Act). Aggrieved by said order dated 31.12.1998, passed by the A.O., Appeal No. 413 / DDN / 2002-03 was preferred before Commissioner of Income-tax (Appeals) –I, Dehradun [for short CIT(A)]. Said appeal was dismissed by said authority vide order dated 21.02.2003. Thereafter, assessee preferred I.T.A. No. 3056 / DEL / 2003 before the Income Tax Appellate Tribunal, Delhi (for short ITAT). The said appeal was allowed by the ITAT. Hence, the appeal before this Court by the Revenue.

3) The facts in Income Tax Appeal No. 98 of 2006 are similar to the facts in Income Tax Appeal No. 91 of 2006. The same respondent / assessee Pride Foramer S.A., a non-resident company, having its office in France, in the assessment year 1999-2000 submitted its return before the A.O. (Dy. Commissioner of Income-tax, Dehradun) showing income of Rs. 11,29,957/- on

account of interest received from the refund of income tax. The assessee has shown profit and loss expenses such as legal & professional charges, salary & administrative charges and depreciation. It further claimed unabsorbed depreciation amounting to Rs. 4,44,04,337/- pertaining to the years 1987-88 and 1988-89, on the ground that after the period of contract was over, since, the assessee was not in business the A.O. disallowed the claim and assessed the income at Rs. 11,29,957/-. Said order dated 26.02.2002, passed by the A.O., was challenged before the CIT(A) by filing Appeal No. 415 / DDN / 2002 –03, but said appeal was allowed partly by the CIT(A), vide its order dated 21.02.2003. Thereafter, the assessee filed I.T.A. No. 3057 / DEL / 2003 before the ITAT, Delhi, which was allowed. Hence, the appeal by the Revenue.

4) The facts in connection with Income Tax Appeal No. 49 of 2005, are that the respondent / assessee Foramer France, another non-resident company, also having its office in France, had a contract with ONGC in the year 1983, which expired in the year 1991-92, and thereafter there was no business activity till 1998, and fresh contract was awarded to the assessee only in the year 1999. The assessee submitted its return before the A.O. (Jt. Commissioner of Income-tax, Dehradun) for the assessment year 1997-1998, showing income to the tune of Rs. 5,49,628/- on account of interest received from the refund of income tax. As against

this, expenses were claimed on various heads, such as, legal & professional charges, salary and administrative charges, vehicle maintenance, travelling expenses, miscellaneous expenses and depreciation. After processing the return under Section 143(1)(a) of the Act, the A.O. assessed total income of the assessee at Rs. 5,49,648/-, refusing to allow the expenses claimed on the ground that that assessee company did not carry out any business relating to work of oil exploration in India during the period the same are said to have been incurred. Also, penalty proceedings were directed to be initiated under Section 271(1)(C) of the Act. Aggrieved by said order dated 13.01.2000, the assessee preferred Appeal No. 352 / DDN / 1999-2000, before the CIT(A), Dehradun. Said authority, after hearing the parties, partly allowed the appeal to the extent the A.O. charged interest under Section 234 of the Act. Thereafter, the assessee filed I.T.A. No. 1442 / DEL / 2001 (Assessment Year 1997-98) before the ITAT, Delhi. After hearing the parties, the ITAT partly allowed the appeal and directed the A.O. to give due effect to set off and carry forward in accordance with law. Hence, this appeal by the Revenue.

Answers to questions of law No. 1 and 2:

5) Before further discussion, we think it just and proper to quote Article 5 of the Double Taxation Avoidance Agreement entered into by the Republic of

India with French Republic. The same is being reproduced below:

Article 5 : Permanent Establishment

"For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term "permanent establishment" includes especially:

- *(a) a place of management;*
- *(b) a branch;*
- *(c) an office;*
- *(d) a factory;*
- *(e) a workshop;*
- *(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources;*
- *(g) a warehouse in relation to a person providing storage facilities for others;*
- *(h) a premises used as a sales outlet;*
- *(i) an installation or structure used for the exploration of natural resources provided that the activities continue for more than 183 days.*

3. A building site or construction, installation or assembly project constitutes a permanent establishment only where such site or project continues for a period of more than six months.

4. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include;

(a) the use of facilities solely for the purpose of storage or display of goods or merchandise belonging to the enterprise;

(b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display;

(c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;

(e) the maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research, or for other activities which have a preparatory or auxiliary character, for the enterprise;

(f) the maintenance of a fixed place of business solely for any combination of activities mentioned in sub-paragraphs (a) to (e), provided that the overall activity of the fixed place of business resulting from this combination is of preparatory or auxiliary character.

5. Notwithstanding the provisions of paragraphs 1 and 2 where a person other than an agent of an independent status to whom paragraph 6 applies is acting in one of the Contracting States on behalf of an enterprise of the other Contracting State, the enterprise shall be deemed to have a permanent establishment in the first-mentioned Contracting State, if:

(a) he has and habitually exercises in that Contracting State an authority to conclude contracts on behalf of the enterprise, unless, his activities are limited to the purchase of goods or merchandise for the enterprise; or

(b) he has no such authority, but habitually maintains in the first mentioned Contracting State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise.

6. An enterprise of one of the Contracting States shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other Contracting State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph if it is shown that the transactions between the agent and

the enterprise were not made under at arm's length conditions.

7. The fact that a company which is resident of one of the Contracting States controls or is controlled by a company, which is a resident of the other Contracting State, or which carries on business in that other Contracting State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other."

6) Admittedly, the assessee in these appeals are non-resident companies having no permanent establishment in India. It is also not disputed that after the contract received by the assessee companies in the year 1983 and before, fresh contract was given to them by the ONGC only in the year 1999. Learned counsel for the appellant (revenue) argued that since the respondent / assessee did no business in India between 1993 to 1998, as such, they cannot claim any set off under Section 71 of the Act. It is further argued on behalf of the appellant (revenue) that since during the relevant period the assessee were not doing any business in India, as such, the A.O. had rightly disallowed the expenses and the claims of depreciation, which were upheld by the CIT(A). On the other hand, learned counsel for the respondent / assessee argued that the assessee were very much in business and were making attempt to get a new contract, but they could get fresh contract only in 1999.

It is contended on behalf of the respondent / assessee that merely for the reason that there was ‘lull in business’ it cannot be said that the assessee were ‘not in business’ during the relevant period.

7) Learned counsel for the respondent / assessee drew attention of this Court to Annexure –1 filed with the counter affidavit in Income Tax Appeal No. 49 of 2005, showing that in October 1996, the assessee was making correspondence with ONGC relating to hiring of manpower services in respect of export key personnel for drilling in deep waters. On perusal of said letter we find that this letter has been issued from Dubai office of the assessee in aforesaid appeal. In our opinion, this does not reflect that the business was being done in India as the earlier contract had long been expired and new contract by then had not been given to the assessee. Merely for the reason that the assessee sent some letters and made some offer from Dubai to ONGC does not amount doing business in India. We do agree that ‘lull in business’ does not mean that the assessee has ceased its business. But, when the assessee has neither permanent office, nor any other office in India, nor any contract was in execution during the relevant period, it cannot be said that they were in business in India, as such, it cannot be said that assessee was entitled to set off claimed by it under Section 71 of the Act.

8) Learned counsel for the respondent / assessee drew attention of this Court to sub-section (3) of Section 176 of the Act, and submitted that the assessee had not given any notice of discontinuance of business to the Income-tax Department, as such, it cannot be said that the business had stopped. We have examined the issue raised by learned counsel for the respondent / assessee. We are of the view that the respondent / assessee cannot take benefit of his own wrong. Apart from this, what is relevant is that from the record it is clear that in one of the assessment proceedings in question, the assessee company itself has given an affidavit to the Department that it has stopped business in India. Thereafter, it is not open for the assessee to say that it was doing business in India between the period 1993 to 1999. In our considered opinion, the ITAT has erred in law in holding that the assessee was in business and passing through a lean period, as such, entitled to deduction on account of expenses, depreciation and set off, claimed by them.

9) On behalf of respondent / assessee our attention is drawn to the case of ***Union of India and another Vs. Azadi Bachao Andolan and another; 2003 ITR (263) 706 (at page 722)***, and it is argued that the provision of Section 90 of the Act relating to double taxation relief under Agreement with foreign countries is a beneficial provision and should be interpreted to favour the assessee. Having gone through the said case law, we

are of the view that the principle laid down in aforesaid case would help the assessee only when he was in business in India and not during the period he had done no business. Also, learned counsel for the respondent / assessee drew attention of this Court to the case of **Sayaji Iron and Engineering Company Vs. Commissioner of Income-tax; 2002 ITR (253) 749 (at page 752)**, and it is argued that any expenditure incurred by officers of the company in India amount to the expenditure incurred by the company in doing its business. On perusal of said case law we find that the facts of said case were different and it was not a case where the company was not in business in India. Similarly, para 99 in ***Ishikawajima-Harima Heavy Industries Ltd. Vs. Director of Income-tax, Mumbai; 2007 ITR (288) 408 (at page 446)***, which was read out before us by learned counsel for the respondent / assessee, in our opinion does not help the respondent / assessee in this case for the reason that in that case the assessee company registered in Japan had its business activities in India during the relevant period, and in that situation the Apex court observed - 'there exists a distinction between a business connection and a permanent establishment. As the permanent establishment cannot be said to be involved in the transaction, the aforementioned provision will have no application. The permanent establishment cannot be equated to a business connection, since the former is for the purpose of assessment of income of a non-resident

under a Double Taxation Avoidance Agreement, and the latter is for the application of Section 9 of the Income Tax Act.'

10) Lastly, it is argued on behalf of the respondent / assessee that the finding of fact recorded by the ITAT cannot be disturbed by the High Court in an appeal under Section 260-A of the Act. Having heard learned counsel for the parties and after going through the impugned orders, we do not find that it is a case where the finding of fact has been challenged by the Revenue, but it is a question of law which has been raised as to whether, when the assessee had its permanent business establishment outside India (with no office in India) and the contract under which it worked had expired long back in that situation can it be said that it was in business in India, thereafter, till it received a new contract after a gap of some more than five years, and is it entitled to set off under Section 71 of the Act (for the period it did not work in India). We have already discussed above that in such a case it cannot be said that the assessee was in business in India and expenditure shown by him in India are not liable to be allowed, or set off. Therefore, we find that the A.O. and CIT(A) have committed no error of law, and the ITAT has erred in law in taking the view that even in the situation mentioned above, the assessee had been in business in India, and as such, entitled to the set off.

Accordingly, both the questions of law stand answered, in favour of the Revenue.

11) For the reasons as discussed above, all the three appeals are allowed. The impugned orders passed by the ITAT are hereby set aside. The orders passed by the CIT(A) are upheld.

(B.S. Verma, J.) **(Prafulla C. Pant, J.)**

Dt. June 12, 2009.
H. Negi