

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "I" MUMBAI**

**BEFORE SHRI SAKTIJIT DEY (JUDICIAL MEMBER) AND
SHRI N.K. PRADHAN (ACCOUNTANT MEMBER)**

**ITA No. 6958/MUM/2017
Assessment Year: 2013-14**

M/s Golden Bella
Holdings Ltd., Nishith
Desai Associates, 92-B
Wing, Mittal, Court,
Nariman Point, Mumbai-
400021.

PAN No. AAFCG3849R
Appellant

Vs. Deputy Commissioner of
Income Tax (International
Taxation)-2(3)(2), Room No.
1702, Air India Building,
Nariman Point, Mumbai-
400021

Respondent

Assessee by : Mr. Rajesh Simhan, AR
Revenue by : Mr. Samuel Darse, DR

Date of Hearing : 07/06/2019
Date of pronouncement: 28/08/2019

ORDER

PER N.K. PRADHAN, AM

This is an appeal filed by the assessee. The relevant assessment year is 2013-14. The appeal is directed against the assessment order dated 29.09.2017 passed by the Deputy Commissioner of Income Tax (International Taxation)- 2(3)(2), Mumbai (in short the 'AO') u/s143(3) r.w.s. 144C(13) of the Income Tax Act 1961, (the 'Act').

2. The grounds of appeal filed by the assessee read as under:

1. The AO grossly erred by taxing the entire amount of interest income of INR 15,16,43,836 received by the Appellant at 40% (plus surcharge and cess) and denying the Appellant relief of beneficial rate or interest at 10% under Article 11

of the India - Cyprus Double Taxation Avoidance Agreement ("DTAA") based on an erroneous finding that the Appellant is not the beneficial owner of the interest income.

2. The findings of the AO on the facts and in law are erroneous based on the following grounds and hence the order of the AO is liable to be set aside:
 - i. The AO erred in concluding that the Appellant was not the beneficial owner of INR 15,16,43,836 received as interest income from ADAMAS Builders Private Limited ("ABPL") on compulsorily convertible debentures ("CCD") issued by ABPL to the Appellant and has thereby erred in denying the Appellant relief under Article 11 of the India- Cyprus DTAA.
 - ii. The AO erred in fact and in law in holding that the Appellant was not the beneficial owner of the interest income by arbitrarily concluding that the Appellant did not have 'dominion and control' over the interest income, despite failing to prove that had any contractual or legal obligation to pass on the interest income to another person.
 - iii. The AO erred in fact and in law in concluding that the Appellant was merely set up as a shell or a conduit company for the passage of funds between Green World Developments Ltd ("GWDL") and ADAMAS Builders Private Limited ("ABPL") and therefore not entitled to claim benefits under Article 11 of the India - Cyprus DTAA by disregarding all the factual and legal submissions made by the Appellant during the course of the assessment proceedings.
 - iv. The AO has relied on assumptions and presumptions to conclude that the Appellant is not the beneficial owner of the interest income notwithstanding the fact that no evidence or allegation is on record stating that the Appellant acted on the instructions of GWDL.
 - v. The AO wrongly disregarded all facts furnished by the Appellant to demonstrate the independence of the Appellant company in Cyprus and wrongly concluded that the Appellant is a mere conduit without supporting such finding with any proof, particularly when the burden of furnishing such proof is on the revenue.
 - vi. The AO has incorrectly distinguished the reliance on Circular No. 789 issued by the CBDT on a mere technicality and has denied treaty relief under the DTAA to the Appellant.

- vii. The conclusions of the AO are contrary to the Income Tax Act and the DTAA. The denial of treaty benefits sought to be made by the AO is contrary to Section 90 of the Income Tax Act and Article 11 of the Treaty.
- viii. The AO has not discharged the burden of proof and has made incorrect findings based on surmises and conjecture.
- ix. The AO has disregarded the fact that the board of directors of the Appellant had the requisite expertise and knowledge to take informed business decisions and that the decision to make investments were made unanimously thereby demonstrating substance and independence.
- x. The AO has ignored the fact all important commercial decisions were made at the Appellant's office in Cyprus which shows commercial operations in Cyprus.
- xi. It is grossly erroneous on part of the AO to record a finding that the Appellant was unable to disprove any of the findings of the AO and unlawfully shift the burden of proof when additionally such findings were baseless and unsupported by proof.
- xii. The AO erred in finding the Appellant to be a conduit and does not possess the CCD in its own right when no evidence is on record to support a finding that GWDL had legal control or had otherwise exercised such control in the upstreaming of interest income.
- xiii. The AO and CIT(A) has erred in law and has levied interest under Section 234A, Section 234B and Section 234C of the Income Tax Act mechanically without due application of mind.

3. Briefly stated, the facts are that the appellant is a company incorporated on 01.08.2011 under the laws of Cyprus with the objective of undertaking business activities of an investment holding company. It filed its return of income for AY 2013-14 on 29.11.2013 showing a total income of Rs.15,16,43,840/- from interest on Compulsorily Convertible Debentures (CCDs) in Adams Builders Private Limited (ABPL), an Indian private limited company and such interest was duly offered to tax @ 10% in accordance with the beneficial provisions of Article 11 of the DTAA

between India and Cyprus (“Cyprus Treaty”). The AO has denied the benefit of the Cyprus Treaty on the basis that the appellant was not the “beneficial owner” of interest income and brought to tax the interest income earned at the rates in force (approximately 42%).

The AO held that the investment in CCDs is a mere back-to-back loan transaction. Accordingly, the AO passed a draft assessment order u/s 144C(1) of the Act denying the benefit of the Cyprus Treaty on the basis that the appellant was not the “beneficial owner” of interest income and sought to tax the interest income earned by the appellant at the rates in force (approximately 42%). The appellant filed objections against the draft assessment order before the Dispute Resolution Panel-1, Mumbai (DRP).

The DRP observed that the appellant is a 100% subsidiary of M/s Green World Development Ltd. (GWDL) of Mauritius. Further, GWDL had remitted a sum of USD 2,15,00,000 to the assessee on 20.10.2011. And on 27.10.2011 the appellant invested a sum of USD 2,01,450,000 in the CCDs of ABPL. As per the AO this back-to-back receipt and investment indicates that the investment made in ADPL had actually been made by GWDL. The DRP thus observed that the AO was correct in his finding that the appellant only served as a mere conduit for the passage of funds and an agent or nominee or a conduit company acting as a fiduciary on behalf of the interested party and therefore cannot be regarded as a beneficial owner.

During the course of assessment proceedings, the assessee filed before the AO an organization chart stating that GWDL holds 100% equity

in the assessee-company and it also holds 99.5% equity in M/s ABPL. The AO held that the routing of funds from GWDL to ABPL through the assessee is only a device. The AO further observed that GWDL is itself 100% subsidiary of M/s Mapletree Mauritius Ltd. which is 100% subsidiary of M/s Mapletree Hinjewadi (Mauritius) Ltd. and which in turn is 100% subsidiary of M/s Mapletree India China Fund Ltd. based in Cayman Island and no further detail was available about the ultimate beneficiary behind that entity.

The AO held that the investment made by the appellant in ABPL is back-to-back loan, on the basis that it had used a shareholder loan raised from its immediate shareholder to invest in ABPL ; the appellant was acting as a mere conduit for the passage of funds between the appellant's immediate shareholder and ABPL; the appellant had outsourced its corporate secretariat and management function to an institutional service provider; the appellant did not carry out any business activities in Cyprus and was merely a "name plate" company ; the appellant did not exercise dominion and control over the CCDs as "most of the companies" incorporated in Cyprus and other "tax havens" did not have any independent office or qualified employees to carry out any business or investment activities ; the appellant was not the "beneficial owner" of the interest income on CCDs and therefore, denied the benefit of Article 11 of the Cyprus Treaty.

The AO also noted that the Fair Market Value(FMV) of share of ABPL was Rs.1,17,717/- and the CCDs were issued for Rs.1,99,900/- which is 70% higher than the FMV. The assessee also went into

liquidation in the subsequent year and CCD of Rs.100 crores were sold for nearly Rs.77.71 crores to one of its affiliated concern namely M/s Mapletree BG Pte Ltd.

Considering the above facts, the AO held that the assessee is not the beneficial owner of the interest on the CCDs and the interest was sought to be taxed under the domestic law @ 40% along with applicable surcharge and education cess.

The DRP observed that the financials did not indicate that the assessee was doing anything else other than merely routing the funds from GWDL to ABPL. Incidentally GWDL owns 100% shares in the assessee-company and 99.5% share in ABPL. The investment by the assessee in ABPL as per the DRP is a back-to-back transaction which leaves no doubt that the legal control over the investment is with GWDL. It further held that the assessee did not possess the CCDs in its own right and its power of disposal is also not unhindered. Further observing that the investment has been made by the assessee without considering the FMV of the CCDs or the financials of ABPL and the assessee has not given the details of the ultimate beneficiary, the DRP confirmed the finding of the AO that the assessee is not the beneficial owner of the interest received on CCDs and therefore, denied the benefit of the provisions of Article 11 of the Cyprus Treaty.

The DRP further observed that Circular 789 issued by CBDT does not apply to Cyprus treaty and as per the case-laws Tax Residency Certificate(TRC) is not the final answer to the question of beneficial ownerships.

Following the direction of the DRP, the AO assessed the interest on CCDs at normal rates i.e. without benefit of DTAA i.e. @ 40% + surcharge + education cess.

4. Before us, the Ld. counsel of the assessee submits that the appellant is a company incorporated on 01.08.2011 under the laws of Cyprus with the objective of undertaking business activities of an investment holding company. As at 31.03.2012, the appellant's capital base consisted of equity share capital of USD 7,200 and debt capital of USD 21,500,000 in the form of unsecured interest-free shareholder loans from its immediate shareholder. It is stated that the appellant is a tax resident of Cyprus and has been issued a TRC by the tax authorities in Cyprus. The Ld. counsel explains that *vide* a Board Resolution dated 21.10.2011 the appellant applied for 5000 CCDs in ABPL, an Indian Pvt. Ltd. company each having a face value of Rs.10, at a premium of Rs.1,99,990/- per CCD and carrying a coupon of 15% on the face value, for an aggregate consideration of Rs.100,00,00,000/-. The premium at which the appellant proposed to apply for such CCDs was determined based on a valuation report dated 21.10.2011 obtained by ABPL valuing its equity shares at Rs.1,17,717/- per share using the Discounted Cash Flow (DCF) Method. It is explained that the appellant applied for such CCDs on its own account using a portion of the share capital and the interest-free shareholder loan raised from its immediate shareholder and even after the investment was made, the appellant continued to have cash balances of USD 1,354,761 available to it. The said CCDs were allotted to the appellant w.e.f. 28.03.2012 and it held such CCDs as a capital asset for its own benefit and not on behalf of, or as an agent or nominee of any other person. The Ld. counsel argues

that no documents or evidence has been put forth by the AO to show otherwise, other than making vague and unsubstantiated allegations and statements.

The Ld. counsel submits that neither the Act nor the Cyprus treaty defines the term “beneficial owner”. It is stated that internationally, the term is used to mean the entity which is the legal owner of a property (in this case, being interest income) and who has dominion and control over the property (i.e. an owner who holds the property for its own benefit and not as an agent, trustee, or nominee for some other person, who has the right to deal with the property as its own). Thereby it is stated by him that the appellant in the present case invested in CCDs and received interest income thereon for its own exclusive benefit, and not for or on behalf of any other entity, in that sense, the appellant is the ‘true’ owner of the interest income as it had complete control on the application or use of the income it received. In that sense the appellant did not exercise any agency or mandate over the CCDs or the interest income other than for its own exclusive benefit.

The Ld. counsel submits that there are no facts or documents that have been produced by the revenue in support of its claim that the appellant is not the “beneficial owner” of interest income received ; that the mere fact that the investment in CCDs was partly funded using an interest-free shareholder loan and share capital does not *ipso facto* mean that the appellant’s corporate status may be disregarded so as to consider the appellant’s immediate shareholder to be the “beneficial owner” of the appellant’s assets, including the interest income earned by the appellant ;

the revenue has failed to prove even a single fact showing that the appellant did not exercise full dominion and control over the interest income. In these circumstances, it is submitted by him the appellant should be considered the “beneficial owner” for the purposes of Article 11 of the Cyprus treaty.

The Ld. counsel submits that in the present case, the appellant has been duly incorporated as a limited liability company in Cyprus, and holds a TRC issued by the tax authorities of Cyprus certifying it to be tax resident in Cyprus. Relying on Circular No. 789 dated 13.04.2000 issued by CBDT, the Ld. counsel argues that a mere TRC will constitute sufficient evidence for accepting the status of residence as well as beneficial ownership for applying the provisions of a tax treaty. In this context, reliance is placed by him on the decision in *DIT v. Universal Music International B.V.* (2013) 214 Taxman 19 (Bombay). It is argued that the revenue has not challenged the validity of the TRC held by the appellant either at the assessment stage or during the course of present proceedings.

Concluding his arguments, the Ld. counsel submits that

- (i) the Appellant was under no contractual, legal, or economic compulsion to invest those funds to Adamas, but chose to do so of its own volition, after due deliberation and independent application of mind and approval by the Appellant's Board of Directors;
- (ii) the Appellant did not merely on-lend those funds to Adamas, but re-characterized the funds into an INR denominated convertible debt instrument that was compulsorily convertible into equity shares of Adamas at a pre-defined ratio at a pre-defined point in time, unlike a pure loan which

is not convertible into equity. In so altering the character of the transaction, the Appellant displayed sole and absolute control over the funds received from its immediate shareholder;

- (iii) while the interest free shareholder loan was denominated in USD, the CCDs and the interest income thereon were denominated in INR, thereby further illustrating that the Appellant was not acting as a mere conduit for the passage of funds between its immediate shareholder and Adamas but was actually a risk bearing entity.;
- (iv) while the interest free shareholder loan received by the Appellant was repayable on demand, the CCDs in Adamas were in effect blocked capital since they could not be repaid but only be converted into equity shares, and was therefore not repayable on demand. For this reason also, the transaction was not a mere back-to-back arrangement;
- (v) the Appellant was the sole owner of the interest income received on CCDs, and was under no contractual, legal, or economic obligation to pass on the interest income received by it to its immediate shareholder, or to its ultimate parent, or to any other entity;
- (vi) the Appellant earned interest income from the CCDs; and finally,
- (vii) the rate of interest payable on the CCDs was accepted to be at arm's length by the Revenue itself, and no adjustment was proposed to the investment by the Appellant in Adamas.

5. *Per contra*, the Ld. Departmental Representative (DR) explains that the AO had made inquiries from the assessee and had also obtained bank statement thereof ; the assessee is a 100% subsidiary of GWDL of Mauritius and GWDL had remitted a sum of USD 2,15,00,000 to the assessee on 20.10.2011 and thereafter on 27.10.2011, the assessee invested a sum of USD 2,01,450,000 in the CCDs of ABPL ; this back-to-back receipt and investment indicates that the investment made in ABPL

has actually been made by GWDL ; therefore, the AO was correct in observing that the appellant has only served as a mere conduit for the passage of the funds.

The Ld. DR further relies on the order of the DRP and submits that the appellant does not possess the CCDs in one's own right and its power of disposal is also not unhindered; the investment has been made by the appellant without considering the FMV of the CCDs or the financials of ABPL, which is a clear indicator that the decisions have been taken somewhere else; the assessee has not given the details of the ultimate beneficiary i.e. M/s Mapletree India China Fund Ltd., Cayman Islands or even of M/s Greenworld Development Ltd., Mauritius. Thus the Ld. DR argues that the assessee is not the beneficial owner of the interest received on CCDs and the AO has rightly denied the benefit of provisions of Article 11 of the Cyprus treaty.

Further referring to the order of the DRP, the Ld. DR submits that mere nominees or agents, who are not treated as owners of income in the country of residence cannot be treated as beneficial owner of interest. Similarly, any other conduit company, cannot be treated as beneficial owner of income even if it has formal ownership of the income, if it is seen to have very narrow powers over the income and thus is reduced to being a mere fiduciary or administrator acting on behalf of other interested parties. Thus the Ld. DR argues that in the present case the assessee has no dominion and control over the funds invested in or the interest received on the CCDs and that it is a conduit company set up for passage of funds only.

Arguing the above, the Ld. DR submits that the order passed by the AO be confirmed.

6. We have heard the rival submissions and perused the relevant materials on record. The reasons for our decisions are given below.

The appellant-company was incorporated on 01.08.2011 under the laws of Cyprus. Its objective was to undertake business activities of an investment holding company. As at 31.03.2012, the appellant's capital base consisted of equity share capital of USD 7,200 and debt capital of USD 21,500,000 in the form of unsecured interest-free shareholder loans from its immediate shareholder. The appellant has been issued a TRC by the tax authorities in Cyprus. The appellant applied for 5000 CCDs in ABPL, an Indian Pvt. Ltd. company, each having a face value of Rs.10 at a premium of Rs.1,99,990/- per CCD, and carrying a coupon of 15% on the face value, for an aggregate consideration of Rs.100,00,00,000/-. The premium at which the appellant proposed to apply for such CCDs was determined based on a valuation report dated 21.10.2011 obtained by ABPL valuing its equity shares at Rs.1,17,717/- per share using DCF method. The appellant applied for such CCDs on its own account, using a portion of the share capital and the interest-free shareholder loan raised from its immediate shareholder. Even after, the investment was made, the appellant continued to have cash balance of USD 1,354,761 available to it. The said CCDs were allotted to the appellant w.e.f. 28.03.2012. The above details were filed by the assessee before the AO.

We find that the appellant invested in CCDs and received interest income thereon for its own exclusive benefit, and not for or on behalf of

any other entity. The mere fact that the investment was funded using a portion of an interest-free shareholder loan and share capital does not affect the appellant's status as the "beneficial owner" of interest income, as the entire interest income was the sole property of the appellant. In this context, we may refer to para 10.2 of the OECD Commentary (2017) on Article 11 (Interest) of the 'Model Tax Convention' to appreciate the meaning of "beneficial owner" and the same reads as under :

"Where the recipient of interest does have the right to use and enjoy the interest unconstrained by a contractual or legal obligation to pass on the payment received to another person, the recipient is the 'beneficial owner' of that interest".

The issue is simple because the mere fact that the CCDs were funded using monies received by the appellant from its immediate shareholder does not make the arrangement a back-to-back transaction. The appellant had the absolute control over the funds received from its immediate shareholder. Further, in the instant case the appellant wholly assumed and maintained the foreign exchange risk on the CCDs (as they were INR denominated), and the counter party risk on interest payments arising on the CCDs.

In the instant case, the AO/DRP have failed to prove that (i) the appellant did not have exclusive possession and control over the interest income received, (ii) the appellant was required to seek approval or obtain consent from any entity to invest in ABPL, or to utilize the interest income received at its own discretion and (iii) the appellant was not free to utilize the interest income received at its sole and absolute discretion,

unconstrained by any contractual, legal, or economic arrangements with any other third party.

In view of the above factual scenario, the transaction between the appellant and ABPL cannot be considered a mere back-to-back transaction lacking economic substance.

Therefore, we direct the AO to accept the return of income filed by the appellant for the impugned assessment year disclosing a total income of Rs.15,16,43,840/- from interest on CCDs in ABPL, wherein it has offered such interest to tax @ 10%.

7. In the result, the appeal is allowed.

Order pronounced in the open Court on 28/08/2019.

Sd/-
(SAKTIJIT DEY)
JUDICIAL MEMBER

Sd/-
(N.K. PRADHAN)
ACCOUNTANT MEMBER

Mumbai;

Dated: 28/08/2019

Rahul Sharma, Sr. P.S.

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. The CIT(A)-
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

//True Copy//

BY ORDER,

(Sr. Private Secretary)
ITAT, Mumbai