VODAFONE INTERNATIONAL HOLDINGS B.V.
v.
UNION OF INDIA & ANR.
(Civil Appeal No. 733 of 2012)

JANUARY 20, 2012

[S.H. KAPADIA, CJI, K.S. RADHAKRISHNAN AND SWATANTER KUMAR, JJ.]

Income Tax Act, 1961:

s.45 read with ss. 195, 201 and 201(1A) – Capital gains – Offshore transaction – Territorial tax jurisdiction of Indian tax authorities – Transaction between VIH and HTIL (both companies incorporated outside India) with regard to sale and purchase of the entire share capital of CGP, also a company incorporated outside India – Revenue seeking to tax the capital gains arising from the sale of share capital of CGP on the basis that CGP held the underlying Indian assets – Held: Indian tax authorities had no territorial jurisdiction to tax the said offshore transaction – Applying the ***look at*** *test, in order to ascertain the true nature and character of the transaction, the Offshore Transaction in the instant case, is a bonafide structured FDI investment into India which fell outside India's territorial tax jurisdiction and, as such, not taxable – The said Offshore Transaction evidences* ***participative investment*** *and not a sham or tax avoidant preordained transaction.*

s.9(1)(i) – Income deemed to accrue or arise in India – Expression, 'transfer of a capital asset situate in India" – Held: s.9(1)(i) cannot by a process of interpretation be extended to cover ***indirect transfers*** *of capital assets/property situate in India – The legislature has not used the words* ***indirect transfer*** *in s.9(1)(i) – Similarly, the words '****underlying asset'*** *do not find place in s.9(1)(i) – Further, "transfer" should be of*

*an asset in respect of which it is possible to compute a capital gain in accordance with the provisions of the Act – A legal fiction has a limited scope – It cannot be expanded by giving purposive interpretation – The question of providing "****look through"*** *in the statute or in the treaty is a matter of policy – It is to be expressly provided for in the statute or in the treaty – Similarly,* ***limitation of benefits*** *has to be expressly provided for in the treaty – Such clauses cannot be read into the Section by interpretation – Therefore, s.9(1)(i) is not a "look through" provision – Interpretation of Statutes.*

s.195 – Deduction of tax at source – Scope and applicability of – Held: The payment in question must have an element of income embedded in it which is chargeable to tax in India – If the sum paid or credited by the payer is not chargeable to tax then no obligation to deduct the tax would arise – Shareholding in companies incorporated outside India (CGP) is property located outside India – Where such shares become subject matter of offshore transfer between two non-residents, there is no liability for capital gains tax – In such a case, question of deduction of TAS would not arise – The instant case concerns the transaction of "outright sale" between two non-residents of a capital asset (share) outside India – Further, the said transaction was entered into on principal to principal basis – Therefore, no liability to deduct TAS arose –Further, in the case of transfer of the Structure in its entirety, one has to look at it holistically as one ***Single Consolidated Bargain*** *which took place between two foreign companies outside India for which a lump sum price was paid – Acquisition of CGP share which gave VIH an indirect control over three genres of companies evidences a straightforward* ***share sale*** *and not an* ***asset sale*** *– The case does not involve sale of assets on itemized basis – There was no split up of lump sum payment, asset-wise, as claimed by Revenue – There was no assignment of price for each right, considered by Revenue to be a "capital asset" in the transaction –* ***Tax presence*** *must be construed in the context, and in a manner* *that brings the non-resident assessee under the jurisdiction of the Indian tax authorities – In the instant case, Revenue has failed to establish any connection with s.9(1)(i) – Under the circumstances, s.195 is not applicable.*

ss. 163(1)(c) read with ss. 161 and 9(1)(i) – "Agent" in relation to a non-resident – Held: s.161 makes a representative assessee liable only if the eventualities stipulated in s.161 are satisfied – In the instant case, Revenue has invoked s.163(1)(c) – Both ss. 163(1)(c) and 9(1)(i) state that income should be deemed to accrue or arise in India – Both these Sections have to be read together – On facts of the instant case, s.163(1)(c) is not attracted as there is no transfer of a capital asset situated in India – Consequently, 'VIH' cannot be proceeded against even u/s 163 of the Act as a representative assessee.

Taxation:

Tax avoidance – Offshore transaction – Held: When it comes to taxation of a Holding Structure, at the threshold, the burden is on the Revenue to allege and establish abuse, in the sense of tax avoidance in the creation and/or use of such structure(s) – It is the task of the Revenue/court to ascertain the legal nature of the transaction and while doing so it has to ***look at*** *the entire transaction as a whole and not to adopt a dissecting approach – Every strategic foreign direct investment coming to India, as an investment destination, should be seen in a holistic manner – While doing so, the Revenue/courts should keep in mind: the concept of participation in investment, the duration of time during which the Holding Structure exists; the period of business operations in India; the generation of taxable revenues in India; the timing of the exit; the continuity of business on such exit – Onus will be on the Revenue to identify the scheme and its dominant purpose – Besides, there is a conceptual difference between* ***pre-ordained transaction*** *which is created for tax avoidance purposes, on the one hand, and a transaction*

which evidences ***investment to participate*** *in India – In the instant case, the sale of shares is relevant and not the sale of assets, item-wise – The Revenue has adopted a dissecting approach at the Department level –It cannot be said that the structure was created or used as a sham or tax avoidant – In such a case, where the structure has existed for a considerable length of time generating taxable revenues right from 1994 and the transaction satisfies all the parameters of "participation in investment", the court need not go into the questions such as de facto control vs. legal control, legal rights vs. practical rights, etc.*

Companies Act, 1956:

Transfer of shares of a company – Situs of shares – Held: Situs of the shares would be where the company is incorporated and where its shares can be transferred – In the instant case, transfer of CGP share was recorded in the Cayman Islands, where the register of members of CGP is maintained – In the circumstances, it cannot be said that the situs of CGP share was situated in the place (India) where the underlying assets stood situated.

ss. 2(47) and 4 – 'Holding company' and 'Subsidiary' – Held: A company is a separate legal persona and the fact that all its shares are owned by one person or by the parent company has nothing to do with its separate legal existence – The difference is between having the ***power*** *and having a* ***persuasive position –*** *The decisive criteria is whether the parent company's management has such steering interference with the subsidiary's core activities that subsidiary can no longer be regarded to perform those activities on the authority of its own executive directors – In the instant case, HTIL, as a Group holding company, had no legal right to direct its downstream companies in the matter of voting, nomination of directors and management rights – Principle of lifting the corporate veil – Doctrine of substance over form – Concept of beneficial ownership – Concept of alter ego.*

Legislation:

Need for legislation – Tax statutes – Held: FDI flows towards location with a strong governance infrastructure which includes enactment of laws and how well the legal system works – Certainty and stability form the basic foundation of any fiscal system – Tax policy certainty is crucial for taxpayers (including foreign investors) to make rational economic choices in the most efficient manner – Legal doctrines like ***"Limitation of Benefits"*** *and* ***"look through"*** *are matters of policy – It is for the Government of the day to have them incorporated in the Treaties and in the laws so as to avoid conflicting views – Investors should know where they stand – It also helps the tax administration in enforcing the provisions of the taxing laws.*

On 11.2.2007, VIH, and HTIL, both companies incorporated outside India, entered into an Agreement for Sale and Purchase of Share and Loans (SPA) under which HTIL agreed to procure for VIH the sale of the entire share capital of CGP (a company resident for tax purposes in the Cayman Islands) which it held through HTIHL. HTIHL was a wholly owned subsidiary (indirect) of HTIL. The completion of the acquisition took place on 8.5.2007. Indian Tax Authorities (Revenue) sought to tax the capital gains arising from the sale of the share capital of CGP on the basis that CGP, whilst not a tax resident in India, held the underlying Indian assets. The stand of the Revenue was that by the said transaction the stated aim of VIH was "acquisition of 67% controlling interest in "HEL", which was a company resident for tax purposes in India. On the other hand, the case of VIH was that it had agreed to acquire companies which in turn controlled a 67% interest, but not controlling interest, in HEL. On 31.5.2010, an order was passed u/ss 201 (1) and 201 (1A) of the Income Tax Act, 1961 (the Act), declaring that the "Revenue" had jurisdiction to tax the transaction,

against which VIH filed a writ petition which was dismissed by the High Court. Aggrieved, VIH filed the appeal.

Allowing the appeal, the Court

HELD:

Per S.H. Kapadia, CJI (for himself and for Swatanter Kumar, J.):

1.1. The majority judgment in *McDowell* held that "tax planning may be legitimate provided it is within the framework of law". Thus, it cannot be said that all tax planning is illegal/illegitimate/impermissible. In cases of treaty shopping and/or tax avoidance, there is no conflict between *McDowell* and *Azadi Bachao* **or between** *McDowell* and *Mathuram Agrawal*. **[Para 64] [641-G; 642-D]**

McDowell and Co. Ltd. v. CTO **1985 (3) SCR 791 = (1985) 3 SCC 230;** *Union of India v. Azadi Bachao Andolan* **2003 (4) Suppl. SCR 222 = (2004) 10 SCC 1; and** *Mathuram Agrawal v. State of Madhya Pradesh* **1999 (4) Suppl. SCR 195 = (1999) 8 SCC 667 – referred to.**

<u>International Tax Aspects of Holding Structures:</u>

1.2. It is fairly well settled that for tax treaty purposes a subsidiary and its parent are also totally separate and distinct tax payers. However, the fact that a parent company exercises shareholder's influence on its subsidiaries does not generally imply that the subsidiaries are to be deemed residents of the State in which the parent company resides. [Para 66-67] [643-B-C; 643-D]

1.3. Where the subsidiary's executive directors' competences are transferred to other persons/bodies or where the subsidiary's executive directors' decision

making has become fully subordinate to the Holding Company with the consequence that the subsidiary's executive directors are no more than puppets then the turning point in respect of the subsidiary's place of residence comes about. Similarly, if an actual controlling Non-Resident Enterprise (NRE) makes an indirect transfer through "abuse of organisation form/legal form and without reasonable business purpose" which results in tax avoidance or avoidance of withholding tax, then the Revenue may disregard the form of the arrangement or the impugned action through use of Non-Resident Holding Company, re-characterize the equity transfer according to its economic substance and impose the tax on the actual controlling Non-Resident Enterprise. [Para 67] [643-F-H; 644-A-B]

1.4. Whether a transaction is used principally as a colourable device for the distribution of earnings, profits and gains is determined by a review of all the facts and circumstances surrounding the transaction. It is in such cases that the principle of lifting the corporate veil or the doctrine of substance over form or the concept of beneficial ownership or the concept of alter ego arises. There are many other circumstances, where separate existence of different companies, that are part of the same group, will be totally or partly ignored as a device or a conduit (in the pejorative sense). [Para 67] [644-B-C]

Salomon v. Salomon **(1897) A.C. 22 – referred to.**

1.5. In the instant case, the Court is concerned with the concept of GAAR. India already has a judicial anti-avoidance rule. When it comes to taxation of a Holding Structure, at the threshold, the burden is on the Revenue to allege and establish abuse, in the sense of tax avoidance in the creation and/or use of such structure(s). In the application of a judicial anti-avoidance rule, the Revenue may invoke the "substance over form" principle or "piercing the corporate veil" test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant. [Para 68] [644-G-H; 645-A-D]

1.6. In view of the "look at" principle enunciated in *Ramsay*, the Revenue or the court must look at a document or a transaction in a context to which it properly belongs to. It is the task of the Revenue/court to ascertain the legal nature of the transaction and while doing so it has to look at the entire transaction as a whole and not to adopt a dissecting approach. The Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but it should apply the "look at" test to ascertain its true legal nature.In the instant case, the Revenue has adopted a dissecting approach at the Department level. [Para 60 and 68] [640-F-H; 645-F-G]

The Commissioners of Inland Revenue v. His Grace the Duke of Westminster **1935 All E.R. 259 and** *W.T. Ramsay Ltd. v. Inland Revenue Commissioners* **(1981) 1 All E.R. 865;** *Furniss (Inspector of Taxes) v. Dawson* **(1984) 1 All E.R. 530;** *Craven (Inspector of Taxes) v. White (Stephen)* **(1988) 3 All. E.R. 495; and** *Craven (Inspector of Taxes) v. White (Stephen)* **(1988) 3 All. E.R. 495 – referred to.**

1.7. Every strategic foreign direct investment coming to India, as an investment destination, should be seen in a holistic manner. The onus will be on the Revenue to identify the scheme and its dominant purpose. The corporate business purpose of a transaction is evidence of the fact that the impugned transaction is not undertaken as a colourable or artificial device. The stronger the evidence of a device, the stronger the corporate business purpose must exist to overcome the evidence of a device.[Para 68] [646-A-D]

<u>Section 9(1)(i) is not a look through provision:</u>

2.1. Section 9(1)(i) of the Income Tax Act, 1961 gathers in one place various types of income and directs that income falling under each of the sub-clauses shall be deemed to accrue or arise in India. Broadly, there are four items of income. The income dealt with in each sub-clause is distinct and independent of the other and the requirements to bring income within each sub-clause, are separately noted. Therefore, it is not necessary that the income falling in one category under any one of the sub-clauses should also satisfy the requirements of the other sub-clauses to bring it within the expression "income deemed to accrue or arise in India" in s.9(1)(i). In the instant case, the last sub-clause of s.9(1)(i), which refers to income arising from "transfer of a capital asset situate in India", is relevant. The fiction created by s.9(1)(i) applies to the assessment of income of non-residents. In the case of a non-resident, unless the place of accrual of income is within India, he cannot be subjected to tax. Any income that accrues or arises to a non-resident, directly or indirectly, outside India is fictionally deemed to accrue or arise in India if such income accrues or arises as a sequel to the transfer of a capital asset situate in India. Once the factum of such transfer is established by the Revenue, then the income of the non-resident arising or accruing from such transfer is made liable to be taxed by reason of s.5(2)(b) of the Act. This fiction comes into play only when the income is not charged to tax on the basis of receipt in India, as receipt of income in India by itself attracts tax whether the recipient is a resident or non-resident.Thus, the income accruing or arising to a non-resident outside India on transfer of a capital asset situate in India is fictionally deemed to accrue or arise in India, which income is made liable to be taxed by reason of s.5(2)(b) of the Act. This is the main purpose behind enactment of s.9(1)(i) of the Act. [Para 71] [647-F-H; 648-A-H]

2.2. The language of the section, when it is unambiguous and admits of no doubt regarding its interpretation, has to be given effect to, particularly when a legal fiction is embedded in that section. A legal fiction has a limited scope. It cannot be expanded by giving purposive interpretation particularly if the result of such interpretation is to transform the concept of chargeability which is also there in s.9(1)(i), when one reads s.9(1)(i) with s.5(2)(b) of the Act. [Para 71] [649-A-C]

2.3. Section 9(1)(i) cannot by a process of interpretation be extended to cover indirect transfers of capital assets/property situate in India. To do so, would amount to changing the content and ambit of s.9(1)(i). The Court cannot re-write s.9(1)(i). The legislature has not used the words indirect transfer in s.9(1)(i). If the word indirect is read into s.9(1)(i), it would render the express statutory requirement of the 4th sub-clause in s.9(1)(i) nugatory. This is because s.9(1)(i) applies to transfers of a capital asset situate in India. This is one of the elements in the 4th sub-clause of s.9(1)(i) and if indirect transfer of a capital asset is read into s.9(1)(i) then the words capital asset situate in India would be rendered nugatory. [Para 71] [649-C-F]

2.4. Similarly, the words 'underlying asset' do not find place in s.9(1)(i). Further, "transfer" should be of an asset in respect of which it is possible to compute a capital gain in accordance with the provisions of the Act. Moreover, even s.163(1)(c) is wide enough to cover the income whether received directly or indirectly. Thus, the words directly or indirectly in s.9(1)(i) go with the income and not with the transfer of a capital asset (property). [Para 71] [649-F-H]

2.5. Lastly, the Direct Tax Code (DTC) Bill, 2010 proposes taxation of offshore share transactions. This proposal indicates in a way that indirect transfers are not

covered by the existing s.9(1)(i) of the Act. In fact, the DTC Bill, 2009 expressly stated that income accruing even from indirect transfer of a capital asset situate in India would be deemed to accrue in India. These proposals, therefore, show that in the existing s.9(1)(i) the word indirect cannot be read on the basis of purposive construction. The question of providing "look through" in the statute or in the treaty is a matter of policy. It is to be expressly provided for in the statute or in the treaty. Similarly, limitation of benefits has to be expressly provided for in the treaty. Such clauses cannot be read into the Section by interpretation. Therefore, s.9(1)(i) is not a "look through" provision. [Para 71] [649-H; 650-A-D]

Transfer of HTIL's property rights by Extinguishment?

3.1. In the instant case, the Court is concerned with the sale of shares and not the sale of assets, item-wise. The facts of this case show sale of the entire investment made by HTIL, through a Top company, viz. CGP, in the Hutchison Structure. In this case, the Court needs to apply the "look at" test, and the task of the Revenue is to ascertain the legal nature of the transaction and, while doing so, it has to look at the entire transaction holistically and not to adopt a dissecting approach. [Para 73] [652-A-D]

3.2. Besides, there is a conceptual difference between preordained transaction which is created for tax avoidance purposes, on the one hand, and a transaction which evidences investment to participate in India. In order to find out the nature of the transaction one has to take into account the factors, namely, duration of time during which the holding structure existed, the period of business operations in India, generation of taxable revenue in India during the period of business operations in India, the timing of the exit, the continuity of business on such exit, etc. Applying these tests to the facts of the instant case, it is evident that the Hutchison structure has been in place since 1994. It operated during the period 1994 to 11.02.2007. It has paid income tax ranging from Rs. 3 crore to Rs. 250 crore per annum during the period 2002-03 to 2006-07. Even after 11.02.2007, taxes are being paid by VIH ranging from Rs.394 crore to Rs. 962 crore per annum during the period 2007-08 to 2010-11 (these figures are apart from indirect taxes which also run in crores). Moreover, the SPA indicates "continuity" of the telecom business on the exit of its predecessor, namely, HTIL. Thus, it cannot be said that the structure was created or used as a sham or tax avoidant. [Para 73] [652-D-H]

3.3. If one applies the look at test, without invoking the dissecting approach, then, extinguishment took place because of the transfer of the CGP share and not by virtue of various clauses of SPA. In such a case, where the structure has existed for a considerable length of time generating taxable revenues right from 1994 and where the court is satisfied that the transaction satisfies all the parameters of "participation in investment", the court need not go into the questions such as de facto control vs. legal control, legal rights vs. practical rights, etc. [Para 73] [653-A-C]

3.4. However, if HTIL did not possess a legal right to appoint directors onto the board of HEL and as such did not have "property right" in HEL, the question of such a right getting "extinguished" will not arise. A legal right is an enforceable right. Enforceable by a legal process. A company is a separate legal persona and the fact that all its shares are owned by one person or by the parent company has nothing to do with its separate legal existence. The fact that the parent company exercises share holder's influence on its subsidiaries cannot obliterate the decision-making power or authority of its (subsidiary's) directors. The difference is between having

the power and having a persuasive position. The decisive criteria is whether the parent company's management has such steering interference with the subsidiary's core activities that subsidiary can no longer be regarded to perform those activities on the authority of its own executive directors. Therefore, though it may be advantageous for a parent and subsidiary companies to work as a group, each subsidiary has to protect its own separate commercial interests. [Para 74-75] [653-D-F-G; 654-E-G; 655-E]

3.5. On the facts and circumstances of the instant case, the right of HTIL, if at all it is a right, to direct a downstream subsidiary as to the manner in which it should vote would fall in the category of a persuasive position/influence rather than having a power over the subsidiary. [Para 75] [655-E-F]

3.6. In this case, the Court is concerned with the expression "capital asset" in the income tax law. Applying the test of enforceability, influence/ persuasion cannot be construed as a right in the legal sense. [Para 76] [656-E]

3.7. Further, the concept of "de facto" control, which existed in the Hutchison structure, conveys a state of being in control without any legal right to such state. This aspect is important while construing the words "capital asset" under the income tax law. Enforceability is an important aspect of a legal right. Applying these tests, on the facts of the case and that too in the light of the ownership structure of Hutchison, this Court holds that HTIL, as a Group holding company, had no legal right to direct its downstream companies in the matter of voting, nomination of directors and management rights. [Para 76] [656-F-G]

3.8. Exit is an important right of an investor in every strategic investment. The present case concerns transfer

of investment in entirety. Exit coupled with continuity of business is one of the tell-tale important circumstance which indicates the commercial/business substance of the transaction. Thus, the need for SPA arose to re-adjust the outstanding loans between the companies; to provide for standstill arrangements in the interregnum between the date of signing of the SPA on 11.02.2007 and its completion on 8.05.2007; to provide for a seamless transfer and to provide for fundamental terms of price, indemnities, warranties etc. [Para 75] [654-H; 655-A-C]

3.9. As regards continuance of the 2006 Shareholders/Framework Agreements by SPA, one needs to keep in mind two relevant concepts, viz., participative and protective rights. This is a case of HTIL exercising its exit right under the holding structure and continuance of the telecom business operations in India by VIH by acquisition of shares. A minority investor has what is called as a "participative" right, which is a subset of "protective rights". This "exit right" comes under "protective rights". On examination of the Hutchison structure in its entirety, it becomes evident that both, participative and protective rights, were provided for in the Shareholders/ Framework Agreements of 2006 in favour of Centrino, NDC and SMMS which enabled them to participate, directly or indirectly, in the operations of HEL. Even without the execution of SPA, such rights existed in the above agreements. Therefore, it would not be correct to say that such rights flowed from the SPA. [Para 76] [656-G-H; 657-A-G]

3.10. It is impossible for the acquirer to visualize all events that may take place between the date of execution of the SPA and completion of acquisition. Therefore, there is a provision for standstill in the SPA and so also the provision for transition. But, from that, it does not follow that without SPA, transition could not ensue. Moreover, the very object of the SPA is to cover the

situations which may arise during the transition and those which are capable of being anticipated and dealt with. The rights and obligations created under the SPA had to be preserved. In any event, preservation of such rights with a view to continue business in India is not extinguishment. [Para 76] [657-G-H; 658-A-B; 660-A-B]

3.11. This Court, therefore, holds that under the HTIL structure, as it existed in 1994, HTIL occupied only a persuasive position/influence over the downstream companies *qua* manner of voting, nomination of directors and management rights; that, the minority shareholders/ investors had participative and protective rights (including RoFR/TARs, call and put options which provided for exit) which flowed from the CGP share; that, the entire investment was sold to the VIH through the investment vehicle (CGP). Consequently, there was no extinguishment of rights as alleged by the Revenue. [Para 77] [660-C-E]

<u>Role of CGP in the transaction:</u>

4.1. It is incorrect to say that CGP stood inserted at a late stage in the transaction in order to bring in a tax-free entity (or to create a transaction to avoid tax) and thereby avoid capital gains. CGP was incorporated in 1998 in Cayman Islands. It was in the Hutchison structure from 1998. The transaction in the instant case was of divestment and, therefore, the transaction of sale was structured at an appropriate tier, so that the buyer really acquired the same degree of control as was exercised by HTIL. VIH agreed to acquire companies and the companies it acquired controlled 67% interest in HEL. CGP was an investment vehicle. It is through the acquisition of CGP that VIH proposed to indirectly acquire the rights and obligations of GSPL(Indian Company) in the Centrino and NDC Framework Agreements. The advantage of transferring the CGP share enabled VIH to

indirectly acquire the rights and obligations of GSPL in the Centrino and NDC Framework agreements. This was the reason for VIH to go by the CGP route. [Para 78 and 80] [660-F; 662-A-E]

4.2. The role of CGP in the transaction is evident from two documents: one is the Report of the KPMG dated 18.10.2010 in which it is stated that through the acquisition of CGP, VIH had indirectly acquired the rights and obligations of GSPL in the Centrino and NDC Framework Agreements; and the second document is the Annual Report 2007 of HTIL. Under the caption "Overview", the Report observes that on 11.02.2007, HTIL entered into an agreement to sell its entire interests in CGP, a company which held through various subsidiaries, the direct and indirect equity and loan interests in HEL (renamed VEL) and its subsidiaries to VIH. This supports the fact that the sole purpose of CGP was not only to hold shares in subsidiary companies but also to enable a smooth transition of business, which is the basis of the SPA. Therefore, it cannot be said that the intervened entity (CGP) had no business or commercial purpose. [para 81] [663-G-H; 664-A-D]

4.3. As regards situs of the CGP share, under the Indian Companies Act, 1956, the situs of the shares would be where the company is incorporated and where its shares can be transferred. In the instant case, it has been asserted by VIH that the transfer of the CGP share was recorded in the Cayman Islands, where the register of members of the CGP is maintained. This assertion has neither been rebutted in the impugned order of the Department dated 31.05.2010 nor traversed in the pleadings filed by the Revenue nor controverted before this Court. In the circumstances, it cannot be said that the situs of the CGP share was situated in the place (India) where the underlying assets stood situated. [Para 82] [664-G-H; 665-A-C]

Did VIH acquire 67% controlling interest in HEL (and not 42%/ 52% as sought to be propounded)?

5.1. The expression "control" is a mixed question of law and fact. On perusal of Hutchison structure, it is evident that HTIL had, through its 100% wholly owned subsidiaries, invested in 42.34% of HEL (i.e. direct interest). Similarly, HTIL had invested through its non-100% wholly owned subsidiaries in 9.62% of HEL (through the pro rata route). Thus, on the basis of the shareholding test, HTIL could be said to have a 52% control over HEL. By the same test, it could be equally said that the balance 15% stakes in HEL remained with AS, AG and IDFC (Indian partners) who had through their respective group companies invested 15% in HEL through TII and Omega and, consequently, HTIL had no control over 15% stakes in HEL. At this stage, it may be stated that under the Hutchison structure shares of Plustech in the AG Group, shares of Scorpios in the AS Group and shares of SMMS came under the options held by GSPL. Pending exercise, options are not management rights. Till date GSPL has not exercised its rights under the Framework Agreement 2006 because of the sectoral cap of 74% which in turn restricts the right to vote. Therefore, the transaction in the instant case provides for a triggering event, viz. relaxation of the sectoral cap. Till such date, HTIL/VIH cannot be said to have a control over 15% stakes in HEL. It is for this reason that even FIPB gave its approval to the transaction by saying that VIH was acquiring or has acquired effective shareholding of 51.96% in HEL. [Para 83] [666-B-H]

5.2. Under the Company Law, the management control vests in the Board of Directors and not with the shareholders of the company. The Term Sheet dated 15.3.2007 entered into between VIH and Essar stated that they shall have to nominate directors on the Board of

Directors of HEL in proportion to the aggregate beneficial shareholding held by members of the respective groups. Therefore, neither from Clause 5.2 of the Shareholders Agreement nor from the Term Sheet dated 15.03.2007, one could say that VIH had acquired 67% controlling interest in HEL. [Para 84] [667-H; 668-A]

5.3. As regards the question as to why VIH should pay consideration to HTIL based on an enterprise value of 67% of the share capital of HEL, it is important to note that valuation cannot be the basis of taxation. The basis of taxation is profits or income or receipt. In this case, the Court is not concerned with tax on income/ profit arising from business operations but with tax on transfer of rights (capital asset) and gains arising therefrom. In the latter case, the conditions on which the tax becomes payable under the Income Tax Act have to be seen. In the instant case, VIH paid for 67% of the enterprise value of HEL plus its downstream companies having operational licences. VIH agreed to acquire companies which in turn controlled a 67% interest in HEL and its subsidiaries. Valuation is a matter of opinion. When the entire business or investment is sold, for valuation purposes, one may take into account the economic interest or realities. Risks as a discounting factor are also to be taken into consideration apart from loans, receivables, options, RoFR/ TAR, etc. In this case, Enterprise Value is made up of two parts, namely, the value of HEL, the value of CGP and the companies between CGP and HEL. [Para 85] [668-B-G]

5.4. In the instant case, the Revenue cannot invoke s.9 of the Income Tax Act on the value of the underlying asset or consequence of acquiring a share of CGP. The Valuation done was on the basis of enterprise value. The price paid as a percentage of the enterprise value had to be 67% not because the figure of 67% was available *in praesenti* to VIH, but on account of the fact that the

competing Indian bidders would have had *de facto* access to the entire 67%, as they were not subject to the limitation of sectoral cap, and, therefore, would have immediately encashed the call options. The expression "equity interest" came from US GAAP. The difference between the 52% figure (control) and 67% (equity interest) arose on account of the difference in computation under the Indian and US GAAP. [Para 85] [668-G-H; 669-A-C; G-H]

5.5. The instant case concerns an offshore transaction involving a structured investment. This case concerns a straight forward share sale and not an asset sale. It concerns sale of an entire investment. A "sale" may take various forms. Accordingly, tax consequences will vary. The tax consequences of a share sale would be different from the tax consequences of an asset sale. A slump sale would involve tax consequences which could be different from the tax consequences of sale of assets on itemized basis. "Control" is a mixed question of law and facts. Ownership of shares may, in certain situations, result in the assumption of an interest which has the character of a controlling interest in the management of the company. A controlling interest is an incident of ownership of shares in a company, something which flows out of the holding of shares. A controlling interest is, therefore, not an identifiable or distinct capital asset independent of the holding of shares. The control of a company resides in the voting power of its shareholders and shares represent an interest of a shareholder which is made up of various rights contained in the contract embedded in the Articles of Association. The right of a shareholder may assume the character of a controlling interest where the extent of the shareholding enables the shareholder to control the management. Shares, and the rights which emanate from them, flow together and cannot be dissected. [Para 88] [670-E; 671-A-B]

IRC v. Crossman **[1936] 1 All ER 762 – referred to**

5.6. VIH acquired Upstream shares with the intention that the congeries of rights, flowing from the CGP share, would give VIH an indirect control over the three genres of companies. Acquisition of the CGP share gave VIH an indirect control over the tier I Mauritius companies which owned shares in HEL totalling to 42.34%; CGP India (Ms), which in turn held shares in TII and Omega and which on a pro rata basis (the FDI principle), totalled up to 9.62% in HEL and an indirect control over Hutchison Tele-Services (India) Holdings Ltd. (Ms), which in turn owned shares in GSPL, which held call and put options. It is significant to note that till date options have remained un-encashed with GSPL. Therefore, even if it be assumed that the options under the Framework Agreements 2006 could be considered to be property rights, there has been no transfer or assignment of options by GSPL till date. Even if it be assumed that the options constituted capital assets, even then s.9(1)(i) of the Act was not applicable as these options have not been transferred till date. [Para 88] [671-C-H]

5.7. Call and put options were not transferred by SPA dated 11.02.2007 or under any other document whatsoever. Moreover, if, on principle, it is accepted that the transfer of the CGP share did not lead to the transfer of a capital asset in India, even if it resulted in a transfer of indirect control over 42.34% (52%) of shares in HEL, then surely the transfer of indirect control over GSPL which held options (contractual rights), would not make the transfer of the CGP share taxable in India. Acquisition of the CGP share which gave VIH an indirect control over three genres of companies evidences a straightforward share sale and not an asset sale. It is also significant to note that 67% of the economic value of HEL is not 67% of the equity capital. Further, Essar has 33% stakes in DEL out of which 22% was held by Essar Mauritius. Thus,

VIH did not acquire 67% of equity capital of HEL, as held by the High Court. [Para 88] [671-H; 672-A-C, F-H]

5.8. This case does not involve sale of assets on itemized basis. Applying the look at test, the entire Hutchison structure, as it existed, ought to have been looked at holistically. This case concerns investment into India by a holding company (parent company), HTIL through a maze of subsidiaries. CGP was treated in the Hutchison structure as an investment vehicle. As a general rule, in a case where a transaction involves transfer of shares lock, stock and barrel, such a transaction cannot be broken up into separate individual components, assets or rights such as right to vote, right to participate in company meetings, management rights, controlling rights, control premium, brand licences and so on as shares constitute a bundle of rights. [Para 88] [672-H; 673-A-D]

Charanjit Lal v. Union of India **1950 SCR 869 : AIR 1951 SC 41– relied on.**

Venkatesh (minor) v. CIT **243 ITR 367 (Mad) and** *Smt. Maharani Ushadevi v. CIT* **131 ITR 445 (MP) –referred to.**

5.9. The entire transaction has to be examined holistically. The transaction in question should be looked at as an entire package. The items like, control premium, non-compete agreement, consultancy support, customer base, brand licences, operating licences etc. were all an integral part of the Holding Subsidiary Structure which existed for almost 13 years, generating huge revenues. Merely because at the time of exit, capital gains tax becomes not payable or exigible to tax would not make the entire "share sale" (investment) a sham or a tax avoidant. The payment of US$ 11.08 bn was for purchase of the entire investment made by HTIL in India. The payment was for the entire package. The parties to the transaction have not agreed upon a separate price for the CGP share. Thus, it was not open to the Revenue to split the payment and consider a part of such payments for each of the above items. The essential character of the transaction as an alienation cannot be altered by the form of the consideration, the payment of the consideration in instalments or on the basis that the payment is related to a contingency ('options', in this case), particularly when the transaction does not contemplate such a split up. Where the parties have agreed for a lump sum consideration without placing separate values for each of the above items which go to make up the entire investment in participation, merely because certain values are indicated in the correspondence with FIPB which had raised the query, would not mean that the parties had agreed for the price payable for each of the above items. The transaction remained a contract of outright sale of the entire investment for a lump sum consideration. [Para 88] [673-E; 674-A-B]

CIT (Central), Calcutta v. Mugneeram Bangur and Company (Land Deptt.), **(1965) 57 ITR 299 (SC) – referred to.**

Commentary on Model Tax Convention on Income and Capital **dated 28.01.2003 – referred to.**

5.10. Thus, the Court needs to "look at" the entire Ownership Structure set up by Hutchison as a single consolidated bargain and interpret the transactional documents, while examining the Offshore Transaction of the nature involved in this case, in that light. [Para 88] [674-E]

6.1. Section 195 of the Act casts an obligation on the payer to deduct tax at source ("TAS") from payments made to non-residents which payments are chargeable to tax. Such payment(s) must have an element of income

embedded in it which is chargeable to tax in India. If the sum paid or credited by the payer is not chargeable to tax then no obligation to deduct the tax would arise. Shareholding in companies incorporated outside India (CGP) is property located outside India. Where such shares become subject matter of offshore transfer between two non-residents, there is no liability for capital gains tax. In such a case, question of deduction of TAS would not arise. The object of s.195 is to ensure that the tax due from non-resident persons is secured at the earliest point of time so that there is no difficulty in collection of tax subsequently at the time of regular assessment. The instant case concerns the transaction of "outright sale" between two non-residents of a capital asset (share) outside India. Further, the said transaction was entered into on principal to principal basis. Therefore, no liability to deduct TAS arose. [Para 89] [674-F-H; 675-A-D]

6.2. In the case of transfer of the Structure in its entirety, one has to look at it holistically as one Single Consolidated Bargain which took place between two foreign companies outside India for which a lump sum price was paid of US$ 11.08 bn. Under the transaction, there was no split up of payment of US$ 11.08 bn. It is the Revenue which has split the consolidated payment and it is the Revenue which wants to assign a value to the rights to control premium, right to non-compete, right to consultancy support etc. For FDI purposes, the FIPB had asked VIH for the basis of fixing the price of US$ 11.08 bn. But here also, there was no split up of lump sum payment, asset-wise as claimed by the Revenue. There was no assignment of price for each right, considered by the Revenue to be a "capital asset" in the transaction. In the absence of PE, profits were not attributable to Indian operations. [Para 89] [675-E-H; 676-A]

6.3. Moreover, tax presence has to be viewed in the context of the transaction that is subjected to tax and not with reference to an entirely unrelated matter. The investment made by Vodafone Group companies in Bharti did not make all entities of that Group subject to the Indian Income Tax Act and the jurisdiction of the tax authorities. Tax presence must be construed in the context, and in a manner that brings the non-resident assessee under the jurisdiction of the Indian tax authorities. [Para 89] [676-A-C]

6.4. Lastly, in the instant case, the Revenue has failed to establish any connection with s.9(1)(i). Under the circumstances, s.195 is not applicable. [Para 89] [676-B-C]

7.1. As regards the stand of the Revenue that VIH can be proceeded against as representative assessee u/s 163, it is significant to note that s.163 does not relate to deduction of tax. It relates to treatment of a purchaser of an asset as a representative assessee. A conjoint reading of s.160(1)(i), s.161(1) and s.163 of the Act shows that, under given circumstances, certain persons can be treated as "representative assessee" on behalf of non-resident specified in s.9(1). This would include an agent of non-resident and also who is treated as an agent u/s 163 of the Act which in turn deals with special cases where a person can be regarded as an agent. Once a person comes within any of the clauses of s.163(1), such a person would be the "agent" of the non-resident for the purposes of the Act. [Para 89] [676-C-F]

7.2. However, merely because a person is an agent or is to be treated as an agent, would not lead to an automatic conclusion that he becomes liable to pay taxes on behalf of the non-resident. It would only mean that he is to be treated as a "representative assessee". Section 161 makes a "representative assessee" liable only "as

regards the income in respect of which he is a representative assessee". Section 161 makes a representative assessee liable only if the eventualities stipulated in the said Section are satisfied. This is the scope of ss. 9(1)(i), 160(1), 161(1) read with ss. 163(1) (a) to (d). In the instant case, the Department has invoked s.163(1)(c). Both ss. 163(1)(c) and 9(1)(i) state that income should be deemed to accrue or arise in India. Both these Sections have to be read together. On facts of this case, this Court holds that s.163(1)(c) is not attracted as there is no transfer of a capital asset situated in India. Consequently, VIH cannot be proceeded against even u/s 163 of the Act as a representative assessee. [Para 89] [676-F-H; 677-A-B]

8.1. Applying the look at test in order to ascertain the true nature and character of the transaction, this Court holds, that the Offshore Transaction in the instant case is a bonafide structured FDI investment into India which fell outside India's territorial tax jurisdiction, hence not taxable. The said Offshore Transaction evidences participative investment and not a sham or tax avoidant preordained transaction. The said Offshore Transaction was between HTIL (a Cayman Islands company) and VIH (a company incorporated in Netherlands). The subject matter of the Transaction was the transfer of the CGP (a company incorporated in Cayman Islands). Consequently, the Indian Tax Authority had no territorial tax jurisdiction to tax the said Offshore Transaction. [Para 90] [677-D-E]

8.2. FDI flows towards location with a strong governance infrastructure which includes enactment of laws and how well the legal system works. Certainty is integral to rule of law. Certainty and stability form the basic foundation of any fiscal system. Tax policy certainty is crucial for taxpayers (including foreign investors) to make rational economic choices in the most efficient

manner. Legal doctrines like "Limitation of Benefits" and "look through" are matters of policy. It is for the Government of the day to have them incorporated in the Treaties and in the laws so as to avoid conflicting views. Investors should know where they stand. It also helps the tax administration in enforcing the provisions of the taxing laws. [Para 91] [677-G-H; 678-A]

8.3. The impugned judgment of the High Court is set aside. The Revenue is directed to return the sum of Rs.2,500 crores, which came to be deposited by the appellant in terms of the interim order, with interest at the rate of 4%. The interest shall be calculated from the date of withdrawal by the Revenue from the Registry of the Supreme Court up to the date of payment. [Para 92] [678-C-E]

<u>Per K.S. Radhakrishnan, J. (Concurring):</u>

<u>CORPORATE STRUCTURE/GENERAL PRINCIPLES</u>

<u>(National and Intrnational):</u>

1.1. Overseas companies are companies incorporated outside India and neither the Companies Act nor the Income Tax Act enacted in India has any control over them. They are governed by the laws in the countries where they are established. On incorporation, the corporate property belongs to the company and members have no direct proprietary rights to it but merely to their "shares" in the undertaking and these shares constitute items of property which are freely transferable in the absence of any express provision to the contrary. [para 43 and 49] [702-E-F; 705-B-C]

1.2. Domestic investments are made in the home country and meant to stay as it were, but when the trans-national investment is made overseas away from the natural residence of the investing company, provisions

are usually made for exit route to facilitate an exit as and when necessary for good business and commercial reasons, which is generally foreign to judicial review. [para 45] [703-E-F]

1.3. Multi-national companies, for corporate governance, may develop corporate structures, affiliate subsidiaries, joint ventures for operational efficiency, tax avoidance, mitigate risks etc. Revenue/courts can always examine whether those corporate structures are genuine and set up legally for a sound and veritable commercial purpose. Burden is entirely on the Revenue to show that the incorporation, consolidation, restructuring etc. has been effected to achieve a fraudulent, dishonest purpose, so as to defeat the law. [para 43 and 46] [702-E; 703-G-H]

1.4. Section 2(47) of the Indian Companies Act 1956 defines "subsidiary company" or "subsidiary", a subsidiary company within the meaning of s. 4 of the Act. The holding company does not own the assets of the subsidiary and, in law, the management of the business of the subsidiary also vests in its Board of Directors. *Holding company and subsidiary company are considered as separate legal entities, and subsidiary are allowed decentralized management. But, the business of a subsidiary is not the business of the holding company. Parent company of a WOS is not responsible legally for the unlawful activities of the subsidiary save in exceptional circumstances, such as a company is a sham or the agent of the shareholder, the parent company is regarded as a shareholder.* **[para 56, 58, 59 and 61] [708-D-E; 709-D-E; 710-A-B; F-G]**

Bacha F. Guzdar v. CIT **1955 SCR 876 = AIR 1955 SC 74;** *Carew and Company Ltd. v. Union of India* **1976 (1) SCR 379 = (1975) 2 SCC 791; and** *Carrasco Investments Ltd. v. Special Director, Enforcement* **(1994) 79 Comp Case 631 (Delhi) – referred to.**

Gramophone & Typewriter Ltd. v. Stanley, **(1908-10) All ER Rep 833– referred to.**

1.5. Shareholders' Agreement (SHA) is a private contract between the shareholders compared to Articles of Association of the Company, which is a public document. Being a private document it binds parties thereof and not the other remaining shareholders in the company. Shareholders can enter into any agreement in the best interest of the company, prvided that the provisions in the SHA do not go contrary to the Articles of Association. The essential purpose of the SHA is to make provisions for proper and effective internal management of the company. [para 62 and 64] [710-H; 711-A-B; 712-A-B]

V. B. Rangaraj v. V. B. Gopalakrishnan and Ors. **1991 (3) Suppl. SCR 1 = (1992) 1 SCC 160; and** *Gherulal Parekh v. Mahadeo Das Maiya* **(1959) SCR Supp (2) 406;** *S. P. Jain v. Kalinga Cables Ltd.* **(1965) 2 SCR 720;***Chiranjit Lal Chowdhuri v. Union of India* **(1950) 1 SCR 869 : AIR 1951 SC 41;** *Dwarkadas Shrinivas of Bombay v. Sholapur Spinning & Weaving Company* **(1954) SCR 674: AIR 1954 SC 119; and** *IRC v. V.T. Bibby & Sons* **(1946) 14 ITR (Supp) 7 – referred to.**

1.6. Shares of any member in a company is a movable property and can be transferred in the manner provided by the Articles of Association of the Company. Control, is an interest arising from holding a particular number of shares and the same cannot be separately acquired or transferred. Controlling interest forms an inalienable part of the share itself and the same cannot be treated separately unless otherwise provided by the statute. Controlling interest, therefore, is not an identifiable or distinct capital asset independent of holding of shares and the nature of the transaction has to be ascertained

from the terms of the contract and the surrounding circumstances. Controlling interest is inherently contractual right and not property right and cannot be considered as transfer of property and hence a capital asset unless the Statute stipulates otherwise. Acquisition of shares may carry the acquisition of controlling interest, which is purely a commercial concept and tax is levied on the transaction, not on its effect. [para 67, 73 and 74] [715-A-B; 717-C-H; 718-A-B]

Lifting the Corporate veil-Tax Laws:

1.7. Once the transaction is shown to be fraudulent, sham, circuitous or a device designed to defeat the interests of the shareholders, investors, parties to the contract and also for tax evasion, the court can always lift the corporate veil and examine the substance of the transaction. Lifting the corporate veil doctrine can, therefore, be applied in tax matters even in the absence of any statutory authorisation to that effect. Principle is also being applied in cases of holding company – subsidiary relationship – where in spite of being separate legal personalities, if the facts reveal that they indulge in dubious methods for tax evasion. [para 75-76] [718-C-D; 719-B]

Commissioner of Income Tax v. Sri Meenakshi Mills Ltd., Madurai, **AIR 1967 SCR 934 = 1967 SC 819;** *Life Insurance Corporation of India v. Escorts Limited and Others* **1985 (3) Suppl. SCR 909 = (1986) 1 SCC 264;** *Juggilal Kampalpat v. Commissioner of Income Tax, U.P.* , **(1969) 1 SCR 988 : AIR 1969 SC 932 – relied on.**

United States v. Bestfoods **524 US 51 (1998); and** *Adams v. Cape Industries Plc.* **(1991) 1 All ER 929 – referred to.**

Tax Avoidance and Tax Evasion:

2. The expressions tax avoidance and tax evasion are being used in different context by the Courts. Many of the offshore companies use the facilities of Offshore Financial Centres situate in Mauritius, Cayman Islands etc. Many of these offshore holdings and arrangements are undertaken for sound commercial and legitimate tax planning reasons, without any intent to conceal income or assets from the home country tax jurisdiction and India has always encouraged such arrangements, unless it is fraudulent or fictitious. [para 50 and 76] [706-A-C; 719-C-D]

IRC v. Burmah Oil Co Ltd. **(1982) 54 TC 200;** *IRC v. Plummer* **(1979) 3 All ER 775;** *Ensign Tankers (Leasing) Ltd. v. Stokes* **(1992) 1 AC 655;** *Floor v. Davis* **(1978) 2 All ER 1079 : (1978) Ch 295;** *Inland Revenue Commissioner v. McGuckian* **(1997) BTC 346;** *MacNiven v. Westmoreland Investments Limited* **(2003) 1 AC 311;** *Barclays Mercantile Business Finance Limited v. Mawson* **(2005) AC 685 (HL).;** *Inland Revenue Commissioner* v. *Scottish Provident Institution* **2004 [1] WLR 3172– referred to.**

Limitation of Benefit Clause (LOB):

3.1. Unlike Indo-US Treaty, Indo Mauritius Treaty does not contain any limitation of Benefit (LOB) clause, nor does it restrict the benefit to companies whose shareholders are non-citizens/residents of Mauritius, or where the beneficial interest is owned by non-citizens/ residents of Mauritius, in the event where there is no justification in prohibiting the residents of a third nation from incorporating companies in Mauritius and deriving benefit under the treaty. No presumption can be drawn that the Union of India or the Tax Department is unaware that the quantum of both FDI and FII do not originate from Mauritius but from other global investors situate outside

Mauritius. [para 95] [731-B-E]

3.2. In the absence of LOB Clause and the presence of Circular No. 789 dated 13.4.2000 and TRC certificate, on the residence and beneficial interest/ownership, tax department cannot at the time of sale/disinvestment/exit from such FDI, deny benefits to such Mauritius companies of the Treaty by stating that FDI was only routed through a Mauritius company, by a company/ principal resident in a third country. Setting up of a WOS Mauritius subsidiary/SPV by Principals/genuine substantial long term FDI in India from/through Mauritius, pursuant to the DTAA and Circular No. 789 can never be considered to be set up for tax evasion. [para 97] [732-D-H]

<u>TRC Whether conclusive:</u>

3.3. LOB and look through provisions cannot be read into a tax treaty. However, DTAA and Circular No. 789 would not preclude the Income Tax Department from denying the tax treaty benefits, if it is established, on facts, that the Mauritius company has been interposed as the owner of the shares in India, at the time of disposal of the shares to a third party, solely with a view to avoid tax without any commercial substance. Tax Department, in such a situation, notwithstanding the fact that the Mauritian company is required to be treated as the beneficial owner of the shares under Circular No. 789 and the Treaty is entitled to look at the entire transaction of sale as a whole and if it is established that the Mauritian company has been interposed as a device, it is open to the Tax Department to discard the device and take into consideration the real transaction between the parties, and the transaction may be subjected to tax. Thus, TRC does not prevent enquiry into a tax fraud. Nothing prevents the Revenue from looking into special agreements, contracts or arrangements made or effected by Indian resident or the role of the OCB in the entire transaction. [para 98] [733-B-E]

3.4. No court will recognise sham transaction or a colourable device or adoption of a dubious method to evade tax, but, at the same time, it cannot be said that the Indo-Mauritian Treaty will recognise FDI and FII only if it originates from Mauritius, not the investors from third countries, incorporating company in Mauritius. Facts, clearly show that almost the entire FDI and FII made in India from Mauritius under DTAA does not originate from that country, but has been made by Mauritius Companies / SPV, which are owned by companies/individuals of third countries providing funds for making FDI by such companies/individuals not from Mauritius, but from third countries. [para 99] [733-F-H; 734-A-B]

3.5. Mauritius and India have also signed a Memorandum of Understanding (MOU) laying down the rules for information, exchange between the two countries which provides for the two signatory authorities to assist each other in the detection of fraudulent market practices, including the insider dealing and market manipulation in the areas of securities transactions and derivative dealings. The object and purpose of the MOU is to track down transactions tainted by fraud and financial crime, not to target the bona fide legitimate transactions. Mauritius has also enacted stringent "Know Your Clients" (KYC) regulations and Anti-Money Laundering laws which seek to avoid abusive use of treaty. Thus, there is no reason to import the "abuse of rights doctrine" (*abus de droit*) to India. [para 100-101] [734-C-E]

A Holding Aps. **(8 ITRL) – held inapplicable.**

Round Tripping:

3.6. Large amounts can be routed back to India using TRC as a defence, but once it is established that such an investment is black money or capital that is hidden, it is nothing but circular movement of capital known as Round Tripping; then TRC can be ignored, since the transaction is fraudulent and against national interest. [para 105] [736-E]

3.7. Adequate legislative measures have to be taken to plug the loopholes, all the same, a genuine corporate structure set up for purely commercial purpose and indulging in genuine investment be recognized. [para 106] [736-F-G]

3.8. However, if the fraud is detected by the Court of Law, it can pierce the corporate structure since fraud unravels everything, even a statutory provision, if it is a stumbling block, because legislature never intends to guard fraud. Certainly TRC certificate though can be accepted as a conclusive evidence for accepting status of residents as well as beneficial ownership for applying the tax treaty, it can be ignored if the treaty is abused for the fraudulent purpose of evasion of tax. [para 106] [736-G-H; 737-A]

4.1. Revenue cannot tax a subject without a statute to support and in the course it is acknowledged that every tax payer is entitled to arrange his affairs so that his taxes shall be as low as possible and that he is not bound to choose that pattern which will replenish the treasury. It cannot be said that the ratio laid down in *McDowell* **is contrary to what has been laid down in** *Azadi Bachao Andolan;* **and, therefore, calls for no reconsideration by a larger branch. [para 117] [740-F-G]**

Union of India v. Azadi Bachao Andolan **2003 (4) Suppl. SCR 222 = (2004) 10 SCC 1;** *McDowell and Co. Ltd. v. CTO* **1985 (3) SCR 791 = (1985) 3 SCC 230;** *CIT v. A. Raman and Co.* **(1968) 1 SCC 10,** *CIT v. B. M. Kharwar* **(1969) 1 SCR 651,** *Bank of Chettinad Ltd. v. CIT* **(1940) 8 ITR 522 (PC),** *Jiyajeerao Cotton Mills Ltd.* v. *Commissioner of Income Tax and Excess Profits Tax, Bombay* **AIR 1959 SC 270;** *CIT v. Vadilal Lallubhai* **(1973) 3 SCC 17 and** *Latilla v. IRC*. **26 TC 107: (1943) AC 377;** *Sankarlal Balabhai v. ITO* **(1975) 100 ITR 97 (Guj.); and** *Mathuram Agrawal v. State of Madhya Pradesh* **1999 (4) Suppl. SCR 195 = (1999) 8 SCC 667 - referred to.**

CGP and its interposition:

4.2. Parties, it is trite, are free to choose whatever lawful arrangement which will suit their business and commercial purpose, but the true nature of the transaction can be ascertained only by looking into the legal arrangement actually entered into and carried out. Indisputedly, the contracts have to be read holistically to arrive at a conclusion as to the real nature of a transaction. [para 118] [741-B-C]

4.3. One of the tests to examine the genuineness of the structure is the "timing test" that is timing of the incorporation of the entities or transfer of shares etc. Structures created for genuine business reasons are those which are generally created or acquired at the time when investment is made, at the time where further investments are being made at the time of consolidation etc. [para 122] [742-E-F]

4.4. CGP was incorporated in the year 1998 and the same became part of the Hutchison Corporate structure in the year 2005. Facts would clearly indicate that the CGP held shares in Array and Hutchison Teleservices (India) Holdings Limited (MS), both incorporated in Mauritius. HTIL, after acquiring the share of CGP (CI) in

the year 1994 which constituted approximately 42% direct interest in HEL, had put in place various FWAs, SHAs for arranging its affairs so that it can also have interest in the functioning of HEL along with Indian partners. [para 121] [742-C-D]

4.5. HTIL structure was created over a period of time and this was consolidated in 2004 to provide a working model by which HTIL could make best use of its investments and exercise control over and strategically influence the affairs of HEL. Consolidation operations of HEL were evidently done in the year 2005 not for tax purposes but for commercial reasons and the contention that CGP was inserted at a very late stage in order to bring a pre tax entity or to create a transaction that would avoid tax, cannot be accepted. [para 124] [743-A-B; E-F]

4.6. Sale of CGP share, for exiting from the Indian Telecommunication Sector cannot be considered as pre-ordained transaction, with no commercial purpose, other than tax avoidance. Sale of CGP share was a genuine business transaction, not a fraudulent or dubious method to avoid capital gains tax. Once entry into the structure is honourable, exit from the structure can also be honourable. [para 123 and 126] [742-G-H; 744-E]

<u>**Situs of CGP:**</u>

4.7. Situs of shares situates at the place where the company is incorporated and/ or the place where the share can be dealt with by way of transfer. CGP share is registered in Cayman Islands and materials placed on record would indicate that Cayman Islands law, unlike other laws does not recognise the multiplicity of registers. The facts in this case as well as the provisions of the Caymen Islands Act would clearly indicate that the CGP (CI) share situates in Caymen Island. [para 127] [744-G-H; 745-A-B]

Brassard v. Smith **[1925] AC 371,** *London and South American Investment Trust v. British Tobacco Co. (Australia)* **[1927] 1 Ch. 107.** *Erie Beach Co. v. Attorney-General for Ontario*, **1930 AC 161 PC 10,** *R.* v. *Williams* **[1942] AC 541 – referred to.**

5.1. HTIL had the controlling interest in HEL before its exit from the Indian Telecom Sector. HTIL could, therefore, exercise its control over HEL, through the voting rights of its indirect subsidiary Array (Mauritius) which in turn controlled 42% shares through Mauritian Subsidiaries in HEL. Mauritian subsidiaries controlled 42% voting rights in HEL and HTIL could not however exercise voting rights in HEL directly but only through indirect subsidiary CGP(M) which in turn held equity interest in TII, an Indian company which held equity interest in HEL. HTIL likewise through an indirect subsidiary HTI(M), which held equity interest in Omega an Indian company which held equity interest in HEL, could exercise only indirect voting rights in HEL. [para 129] [745-E; 746-C-D]

5.2. HTIL, by holding CGP share, got control over its WOS Hutchison Tele Services (India) Holdings Ltd (MS). HTSH(MS) was having control over its WOS 3GSPL, an Indian company which exercised voting rights in HEL. HTIL, therefore, by holding CGP share, had 52% equity interest, direct 42% and approximately 10% (pro rata) indirect in HEL and not 67% as contended by the Revenue. [para 130] [746-E-F]

5.3. Vodafone on acquisition of CGP share got controlling interest of 42% over HEL/VEL through voting rights through eight Mauritian subsidiaries, the same was the position of HTIL as well. On acquiring CGP share, CGP has become a direct subsidiary of Vodafone, but both are legally independent entities. Voting rights,

controlling rights, right to manage etc., of Mauritian Companies vested in those companies. HTIL has never sold nor did Vodafone purchase any shares of either Array or the Mauritian subsidiaries, but only CGP, the share of which situates in Cayman Islands. By purchasing the CGP share its situs will not shift either to Mauritius or to India. [para 132] [749-C-G]

5.4. Vodafone on purchase of CGP share got controlling interest in the Mauritian Companies and the incident of transfer of CGP share cannot be considered to be two distinct and separate transactions, one shifting of the share and another shifting of the controlling interest. Transfer of CGP share automatically results in host of consequences including transfer of controlling interest and that controlling interest as such cannot be dissected from CGP share without legislative intervention. Controlling interest of CGP over Array is an incident of holding majority shares and the control of Company vests in the voting power of its shareholders. [para 133] [749-H; 750-A-C]

5.5. Acquisition of shares, may carry the acquisition of controlling interest which is purely a commercial concept and tax can be levied only on the transaction and not on its effect. On transfer of CGP share, Vodafone gets controlling interest in its indirect subsidiaries which are situated in Mauritius which have equity interests in TII and Omega, Indian Companies which are independent legal entities. Controlling interest, which stood transferred to Vodafone from HTIL accompany the CGP share and cannot be dissected so as to be treated as transfer of controlling interest of Mauritian entities and then that of Indian entities and ultimately that of HEL. Situs of CGP share, therefore, determines the transferability of the share and/or interest which flows out of that share including controlling interest. Ownership of shares carries other valuable rights like, right to receive dividend, right to transmit the shares, right to vote, right to act as per one's wish, or to vote in a particular manner etc; and on transfer of shares those rights also sail along with them.Vodafone, on purchase of CGP share got all those rights, and the price paid by Vodafone is for all those rights, in other words, control premium paid, not over and above the CGP share, but is the integral part of the price of the share. On transfer of CGP share situated in Cayman Islands, the entire rights, which accompany stood transferred not in India, but offshore and the facts reveal that the offshore holdings and arrangements made by HTIL and Vodafone were for sound commercial and legitimate tax planning, not with the motive of evading tax. [para 133-135] [750-E-F-H; 751-A-F]

5.6. Vodafone, on purchase of CGP share also got control over its WOS, HTSH(M) which is having control over its WOS, 3GSPL, an Indian Company which exercised voting rights in HEL. 3 GSPL has call and put options, which are contractual rights and do not sound in property and, therefore, cannot be, in the absence of a statutory stipulation considered as capital assets. Even assuming so, they are in favour of 3 GSPL and continue to be so even after entry of Vodafone. [para 137] [752-D-E]

6.1. In none of the Agreements HTIL or Vodafone figure as parties. SHAs between Mauritian entities (which were shareholders of the Indian operating Companies) and other shareholders in some of the other operating companies in India held shares in HEL related to the management of the subsidiaries of AS, AG and IDFC and did not relate to the management of the affairs of HEL and HTIL was not a party to those agreements, and hence there was no question of assigning or relinquishing any right to Vodafone. [para 138] [752-F-G]

6.2. Controlling right over TII through TII SHAs in the form of right to appoint two Directors with veto power to promote its interest in HEL and thereby held beneficial interest in 12.30% of share capital in the HEL are also contractual rights. [para 141] [754-B-C]

6.3. Various agreements including the provisions for assignments in the SPA, indicate that all loan agreements and assignments of loans took place outside India at face value and, hence, there is no question of transfer of any capital assets out of those transactions in India, attracting capital gains tax. Right to preference shares or rights cannot be termed as transfer in terms of s.2(47) of the Act. Further, SPA contains a non-compete agreement which is a pure contractual agreement. An agreement for a non-compete clause executed offshore, by no principle of law can be termed as "property" so as to come within the meaning of capital gains taxable in India in the absence of any legislation. [para 149-151] [758-G; 759-A-F]

6.4. On transfer of CGP share, HTIL had transferred only 42% equity interest it had in HEL and approximately 10% (pro-rata) to VIH, the transfer was off-shore, money was paid off-shore, parties were no-residents and hence there was no transfer of a capital asset situated in India. Loan agreements extended by virtue of transfer of CGP share were also off-shore and hence cannot be termed to be a transfer of asset situated in India. Rights and entitlements referred to also cannot be termed as capital assets, attracting capital gains tax and even after transfer of CGP share, all those rights and entitlements remained as such, by virtue of various FWAs, SHAs, in which neither HTIL nor VIH was a party. [para 154] [760-E-G]

Commissioner of Income Tax v. Grace Collins and Others **248 ITR 323 – referred to.**

7.1. Section 9 of the Income Tax Act, 1961 extends its provisions to certain incomes which shall be deemed to accrue or arise in India. Under the general theory of nexus relevant for examining the territorial operation of the legislation, two principles that are generally accepted for imposition of tax are: (a) Source and (b) Residence. Section 5 of the Income Tax Act specifies the principle on which tax can be levied. Section 5(1) prescribes "residence" as a primary basis for imposition of tax and makes the global income of the resident liable to tax. Section 5(2) is the source based rule in relation to residents and is confined to: income that has been received in India; and income that has accrued or arisen in India or income that is deemed to accrue or arise in India. [para 160] [763-D-E]

7.2. Section 9 on a plain reading would show, it refers to a property that yields an income and that property should have the situs in India and it is the income that arises through or from that property which is taxable. Section 9, therefore, covers only income arising from a transfer of a capital asset situated in India and it does not purport to cover income arising from the indirect transfer of capital asset in India.[para 165] [767-G-H]

7.3. Source in relation to an income has been construed to be where the transaction of sale takes place and not where the item of value, which was the subject of the transaction, was acquired or derived from. HTIL and Vodafone are off-shore companies and since the sale took place outside India, applying the source test, the source is also outside India, unless legislation ropes in such transactions. [para 167] [768-C]

7.4. Substantial territorial nexus between the income and the territory which seeks to tax that income, is of prime importance to levy tax. Expression used in s.9(1)(i) is "source of income in India" which implies that income

arises from that source and there is no question of income arising indirectly from a source in India. Expression used is "source of income in India" and not "from a source in India". Section 9 contains a "deeming provision" and in interpreting a provision creating a legal fiction, the court is to ascertain for what purpose the fiction is created, but in construing the fiction it is not to be extended beyond the purpose for which it is created, or beyond the language of section by which it is created. [para 168] [768-D-F]

C.I.T. Bombay City II v. Shakuntala **(1962) 2 SCR 871,** *Mancheri Puthusseri Ahmed v. Kuthiravattam Estate Receiver* **(1996) 6 SCC 185 – relied on.**

7.5. Power to impose tax is essentially a legislative function which finds in its expression Art. 265 of the Constitution of India. Article 265 states that no tax shall be levied except by authority of law. Further, it is also well settled that the subject is not to be taxed without clear words for that purpose; and also that every Act of Parliament must be read according to the natural construction of its words. [para 169] [768-G-H; 769-A]

Cape Brandy Syndicate v. IRC **(1921) 1 KB 64, P. 71 (Rowlatt, J.) ;** *Ransom (Inspector of Tax) v. Higgs* **1974 3 All ER 949 (HL),** *Ormond Investment Co. v. Betts* **(1928) All ER Rep 709 (HL) – referred to.**

7.6. An invitation to purposively construe s. 9 applying look through provision without legislative sanction, would be contrary to the ratio of *Mathuram Aggarwal***. [para 170] [769-G]**

Mathuram Agrawal v. State of Madhya Pradesh **1999 (4) Suppl. SCR 195 = (1999) 8 SCC 667 – relied on.**

7.7. Section 9(1)(i) covers only income arising or accruing directly or indirectly or through the transfer of

a capital asset situated in India. Section 9(1)(i) cannot by a process of "interpretation" or "construction" be extended to cover "indirect transfers" of capital assets/ property situate in India. [para 171] [769-H; 770-A]

7.8. On transfer of shares of a foreign company to a non-resident off-shore, there is no transfer of shares of the Indian Company, though held by the foreign company, in such a case it cannot be said that the transfer of shares of the foreign holding company, results in an extinguishment of the foreign company control of the Indian company and it also does not constitute an extinguishment and transfer of an asset situate in India. Transfer of the foreign holding company's share off-shore, cannot result in an extinguishment of the holding company right of control of the Indian company nor can it be stated that the same constitutes extinguishment and transfer of an asset/ management and control of property situated in India. [para 172] [770-B-C]

7.9. The Legislature wherever wanted to tax the income which arises indirectly from the assets, the same has been specifically provided so. On a comparison of ss. 64 and 9(1)(i) what is discernible is that the Legislature has not chosen to extend s.9(1)(i) to "indirect transfers". Wherever "indirect transfers" are intended to be covered, the Legislature has expressly provided so. The words "either directly or indirectly", textually or contextually, cannot be construed to govern the words that follow, but must govern the words that precede them, namely the words "all income accruing or arising". [para 173] [770-D-H]

CIT v. Kothari (CM) **(1964) 2 SCR 531;***Ishikawajma-Harima Heavy Industries Ltd. v. Director of Income Tax, Mumbai* **(2007) 3 SCC 481 and** *CIT v. R.D. Aggarwal* **(1965) 1 SCR 660 – referred to.**

7.10. Section 9 has no “look through provision” and such a provision cannot be brought through construction or interpretation of a word ‘through’ in s. 9. In any view, “look through provision” will not shift the situs of an asset from one country to another. Shifting of situs can be done only by express legislation. Section 9 has no inbuilt “look through mechanism”. [para 174] [771-D-E]

Federal Commission of Taxation v. Lamesa Holdings BV (LN) **– (1998) 157 A.L.R. 290 – referred to.**

7.11. Capital gains are chargeable u/s 45 and their computation is to be in accordance with the provisions that follow s. 45 and there is no notion of indirect transfer in s.45. [para 175] [771-F]

7.12. Section 9(1)(i), therefore, will not apply to the transaction in question or on the rights and entitlements, stated to have transferred, as a fall out of the sale of CGP share, since the Revenue has failed to establish both the tests - Resident Test as well the Source Test. [para 176] [771-G]

8.1. Section 195 provides that any person responsible for making any payment to a non-resident which is chargeable to tax must deduct from such payment, the income tax at source. A reading of ss.191A, 194B, 194C, 194D, 194E, 194I, 194J read with ss.115BBA, 194I, 194J would show that the intention of Parliament was first to apply s.195 only to the residents who have a tax presence in India. It is all the more so, since the person responsible has to comply with various statutory requirements such as compliance of ss. 200(3), 203 and 203A. [para 178 and 184] [772-B-C; 775-G-H; 776-A]

8.2. The expression “any person” looking at the context in which s.195 has been placed, would mean any person who is a resident in India. [para 185] [776-B]

Ex Parte Blain; In re Sawers **(1879) LR 12 ChD 522;** *Clark (Inspector of Taxes) v. Oceanic Contractors Inc.* **(1983) 1 ALL ER 133;** *Clark (Inspector of Taxes) v. Oceanic Contractors Inc.* **(1983) 1 ALL ER 133; and** *Agassi v. Robinson* **[2006] 1 WLR 2126 – referred to.**

8.3. In the instant case, indisputedly, CGP share was transferred offshore. Both the companies were incorporated not in India but offshore. Both the companies have no income or fiscal assets in India, leave aside the question of transferring, those fiscal assets in India. Tax presence has to be viewed in the context of transaction in question and not with reference to an entirely unrelated transaction. Section 195 would apply only if payments made from a resident to another non-resident and not between two non-residents situated outside India. In the instant case, the transaction was between two non-resident entities through a contract executed outside India. Consideration was also passed outside India. That transaction has no nexus with the underlying assets in India. In order to establish a nexus, the legal nature of the transaction has to be examined and not the indirect transfer of rights and entitlements in India. Consequently, VIH is not legally obliged to respond to s. 163 notice which relates to the treatment of a purchaser of an asset as a representative assessee. [para 187] [777-E-H; 778-A]

CIT v. Eli Lilly and Company (India) P. Ltd. **(2009) 15 SCC 1 – held inapplicable.**

8.4. It can,, therefore, not be said that the sale of CGP share by HTIL to VIH would amount to transfer of a capital asset within the meaning of s.2(14) of the Indian Income Tax Act and the rights and entitlements that flow from FWAs, SHAs, Term Sheet, loan assignments, brand license etc. form integral part of CGP share attracting

capital gains tax. Consequently, the demand of nearly Rs.12,000 crores by way of capital gains tax lacks authority of law and, therefore, stands quashed. [para 188] [778-C-E]

Need for Legislation:

9. Lack of proper regulatory laws, leads to uncertainty and passing inconsistent orders by Courts, Tribunals and other forums, putting Revenue and tax payers at bay. It is often said that insufficient legislation in the countries where offshore financial centres operate gives opportunities for money laundering, tax evasion etc. and, hence, it is imperative that Indian Parliament would address all these issues with utmost urgency. Direct Tax Code Bill (DTC) 2010, proposed in India, envisages creation of an economically efficient, effective direct tax system, proposing GAAR. GAAR intends to prevent tax avoidance, what is inequitable and undesirable. [para 53 and 55] [707-C-D, H; 708-A-C]

Seth Pushalal Mansinghka (P) Ltd. v. CIT **(1967) 66 ITR 159 (SC);** *Assam Consolidated Tea Estates v. Income Tax Officer "A" Ward* **(1971) 81 ITR 699 Cal. and** *C.I.T. West Bengal v. National and Grindlays Bank Ltd*. **(1969) 72 ITR 121 Cal.** *CIT v. Grace Collis* **(2001) 3 SCC 430;** *CIT v. National Insurance Company* **(1978) 113 ITR 37(Cal.) and** *Laxmi Insurance Company Pvt. Ltd. v. CIT* **(1971) 80 ITR 575 (Delhi) – cited.**

IRC v. Duke of Westminster **(1936) AC 1 (HL),** *W. T. Ramsay v. IRC* **(1982) AC 300 (HL),** ***Craven v. White*** **(1988) 3 All ER 495,** *Furniss v. Dawson* **(1984) 1 All ER 530 - cited**

Case Law Reference:

Per S.H. Kapadia, CJI.

2003 (4) Suppl. SCR 222	referred to	para 57

1985 (3) SCR 791	referred to	para 57
1999 (4) Suppl. SCR 195	referred to	para 57
1935 All E.R. 259	referred to	para 58
(1981) 1 All E.R. 865	referred to	para 58
(1984) 1 All E.R. 530	referred to	para 62
(1988) 3 All. E.R. 495	referred to	para 62
(1897) A.C. 22	referred to	para 68
1950 SCR 869	relied on	para 88
243 ITR 367 (Mad)	relied on	para 88
131 ITR 445 (MP)	relied on	para 88
(1965) 57 ITR 299 (SC)	referred to	para 88

Per Radhakrishnan, J.

(1967) 66 ITR 159 (SC)	cited	para 38
(1971) 81 ITR 699	cited	para 38
(1969) 72 ITR 121 Cal.	cited	para 38
(2001) 3 SCC 430	cited	para 38
(1936) AC 1 (HL),	cited	para 38
(1982) AC 300 (HL),	cited	para 38
(1988) 3 All ER 495	cited	para 38
(1984) 1 All ER 530	cited	para 38
(1978) 113 ITR 37(Cal.)	cited	para 41
(1971) 80 ITR 575 (Delhi)	cited	para 41
(1908-10) All ER Rep 833	referred to	para 56
1955 SCR 876	referred to	para 56

A	**1976 (1) SCR 379**	**referred to**	**para 58**
	(1994) 79 Comp Case 631 (Delhi)	**referred to**	**para 58**
	524 US 51 (1998)	**referred to**	**para 60**
B	**1991) 1 All ER 929**	**referred to**	**para 60**
	1991 (3) Suppl. SCR 1	**referred to**	**para 63**
	(1959) SCR Supp (2) 406	**referred to**	**para 63**
	(1965) 2 SCR 720	**referred to**	**para 64**
C	**(1950) 1 SCR 869**	**referred to**	**para 70**
	(1954) SCR 674	**referred to**	**para 70**
	(1946) 14 ITR (Supp) 7 at 9-10	**referred to**	**para 73**
D	**1967 SCR 934**	**relied on**	**para 75**
	1985 (3) Suppl. SCR 909	**relied on**	**para 75**
	(1969) 1 SCR 988	**relied on**	**para 75**
E	**(1982) 54 TC 200**	**referred to**	**para 78**
	(1979) 3 All ER 775	**referred to**	**para 78**
	(1992) 1 AC 655	**referred to**	**para 81**
	(1978) 2 All ER 1079	**referred to**	**para 81**
F	**(1997) BTC 346**	**referred to**	**para 84**
	(2003) 1 AC 311	**referred to**	**para 85**
	(2005) AC 685 (HL).	**referred to**	**para 88**
G	**2004 [1] WLR 3172**	**referred to**	**para 89**
	(1968) 1 SCC 10	**referred to**	**para 107**
	(1969) 1 SCR 651	**referred to**	**para 107**
H	**1940) 8 ITR 522 (PC),**	**referred to**	**para 107**

A	**AIR 1959 SC 270**	**referred to**	**para 107**
	(1973) 3 SCC 17	**referred to**	**para 107**
	26 TC 107: (1943) AC 377	**referred to**	**para 107**
B	**AIR 1959 SC 270**	**referred to**	**para 107**
	26 TC 107: (1943) AC 377	**referred to**	**para 107**
	(1975) 100 ITR 97 (Guj.)	**referred to**	**para 109**
	1999 (4) Suppl. SCR 195	**referred to**	**para 116**
C	**2003 (4) Suppl. SCR 222**	**referred to**	**para 5 and 117**
	1985 (3) SCR 791	**referred to**	**para 5 and 117**
D	**1925] AC 371**	**referred to**	**para 127**
	1927] 1 Ch. 107	**referred to**	**para 127**
	1930 AC 161 PC 10	**referred to**	**para 127**
E	**[1942] AC 541**	**referred to**	**para 127**
	248 ITR 323	**referred to**	**para 157**
	(1962) 2 SCR 871	**relied on**	**para 168**
F	**(1996) 6 SCC 185**	**relied on**	**para 168**
	(1921) 1 KB 64, P. 71 (Rowlatt, J.)	**referred to**	**para 169**
	1974 3 All ER 949 (HL),	**referred to**	**para 170**
	(1928) All ER Rep 709 (HL)	**referred to**	**para 170**
G	**1999 (4) Suppl. SCR 195**	**relied on**	**para 171**
	(1964) 2 SCR 531	**referred to**	**para 173**
	(2007) 3 SCC 481	**referred to**	**para 173**
H			

(1965) 1 SCR 660	**referred to**	**para 173**
(1998) 157 A.L.R. 290	**referred to**	**para 174**
(1879) LR 12 ChD 522	**referred to**	**para 185**
(1983) 1 ALL ER 133	**referred to**	**para 185**
[2006] 1 WLR 2126	**referred to**	**para 185**
(2009) 15 SCC 1	**held inapplicable**	**para 186**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 733 of 2012.

From the Judgment and Order dated 08.09.2010 of the High Court of Bombay in WP in No. 1325 of 2010.

Mohan Parasaran, ASG, Aspi Chinoy, Percy Pardiwala, K.V. Vishwanathan, Anuradha Dutt, Fereshte D. Sethna, Vijayalakshmi Menon, Ekta Kapil, Anish Kapur, Pawan Sharma, Kuber Dewan, Shwetha Bidhuri, Preeti Yadav, Pratyush Miglani, Gayatri Goswami, Kamaldeep Dayal, Rook Ray, Jaiver Shergill, Anadi Chopra, Kripa Pandit, Pavitra Kacholia, D.L. Chidananda, G.C. Srivastava, Girish Dave, Gaurav Dhingra, Ritin Rai, Nakul Dewan, Arijit Prasad, C.S. Bhardwaj, B.V. Balaram Das, D.S. Mahra, Jayant Mehta, Mamta Tiwari, Sangeeta Mandal, Swati Sinha, Abhishek Kaushik, Rishabh Jain, N.B. Paonam, Zoheb Hossain (for Fox Mandal and Co.) and Sumita Hazarika for the appearing parties.

The Judgments of the Court was delivered by

S.H. KAPADIA, CJI. 1. Leave granted.

Introduction

2. This matter concerns a tax dispute involving the Vodafone Group with the Indian Tax Authorities [hereinafter referred to for short as "the Revenue"], in relation to the acquisition by Vodafone International Holdings BV [for short

"VIH"], a company resident for tax purposes in the Netherlands, of the entire share capital of CGP Investments (Holdings) Ltd. [for short "CGP"], a company resident for tax purposes in the Cayman Islands ["CI" for short] vide transaction dated 11.02.2007, whose stated aim, according to the Revenue, was "acquisition of 67% controlling interest in HEL", being a company resident for tax purposes in India which is disputed by the appellant saying that VIH agreed to acquire companies which in turn controlled a 67% interest, but not controlling interest, in Hutchison Essar Limited ("HEL" for short). According to the appellant, CGP held indirectly through other companies 52% shareholding interest in HEL as well as Options to acquire a further 15% shareholding interest in HEL, subject to relaxation of FDI Norms. In short, the Revenue seeks to tax the capital gains arising from the sale of the share capital of CGP on the basis that CGP, whilst not a tax resident in India, holds the underlying Indian assets.

Facts

A. <u>Evolution of the Hutchison structure and the Transaction</u>

3. The Hutchison Group, Hong Kong (HK) first invested into the telecom business in India in 1992 when the said Group invested in an Indian joint venture vehicle by the name Hutchison Max Telecom Limited (HMTL) – later renamed as HEL.

4. On 12.01.1998, CGP stood incorporated in Cayman Islands, with limited liability, as an "exempted company", its sole shareholder being Hutchison Telecommunications Limited, Hong Kong ["HTL" for short], which in September, 2004 stood transferred to HTI (BVI) Holdings Limited ["HTIHL (BVI)" for short] vide Board Resolution dated 17.09.2004. HTIHL (BVI) was the buyer of the CGP Share. HTIHL (BVI) was a wholly owned subsidiary (indirect) of Hutchison Telecommunications International Limited (CI) ["HTIL" for short].

5. In March, 2004, HTIL stood incorporated and listed on Hong Kong and New York Stock Exchanges in September, 2004.

6. In February, 2005, consolidation of HMTL (later on HEL) got effected. Consequently, all operating companies below HEL got held by one holding company, i.e., HMTL/HEL. This was with the approval of RBI and FIPB. The ownership of the said holding company, i.e., HMTL/HEL was consolidated into the tier I companies all based in Mauritius. Telecom Investments India Private Limited [“TII” for short], IndusInd Telecom Network Ltd. [“ITNL” for short] and Usha Martin Telematics Limited [“UMTL” for short] were the other shareholders, other than Hutchison and Essar, in HMTL/HEL. They were Indian tier I companies above HMTL/HEL. The consolidation was first mooted as early as July, 2003.

7. On 28.10.2005, VIH agreed to acquire 5.61% shareholding in Bharti Televentures Ltd. (now Bharti Airtel Ltd.). On the same day, Vodafone Mauritius Limited (subsidiary of VIH) agreed to acquire 4.39% shareholding in Bharti Enterprises Pvt. Ltd. which indirectly held shares in Bharti Televentures Ltd. (now Bharti Airtel Ltd.).

8. On 3.11.2005, Press Note 5 was issued by the Government of India enhancing the FDI ceiling from 49% to 74% in telecom sector. Under this Press Note, proportionate foreign component held in any Indian company was also to be counted towards the ceiling of 74%.

9. On 1.03.2006, TII Framework and Shareholders Agreements stood executed under which the shareholding of HEL was restructured through “TII”, an Indian company, in which Analjit Singh (AS) and Asim Ghosh (AG), acquired shares through their Group companies, with the credit support provided by HTIL. In consideration of the credit support, parties entered into Framework Agreements under which a Call Option was given to 3 Global Services Private Limited [“GSPL” for short],

a subsidiary of HTIL, to buy from Goldspot Mercantile Company Private Limited [“Goldspot” for short] (an AG company) and Scorpios Beverages Private Limited [“Scorpios” for short] (an AS company) their entire shareholding in TII. Additionally, a Subscription Right was also provided allowing GSPL a right to subscribe to the shares of Centrino Trading Company Private Limited [“Centrino” for short] and ND Callus Info Services Private Limited [“NDC” for short]. GSPL was an Indian company under a Mauritius subsidiary of CGP which stood indirectly held by HTIL. These agreements also contained clauses which imposed restrictions to transfer downstream interests, termination rights, subject to objection from any party, etc.

10. The shareholding of HEL again underwent a change on 7.08.2006 through execution of 2006 IDFC Framework Agreement with the Hinduja Group exiting and its shareholding being acquired by SMMS Investments Private Limited [“SMMS” for short], an Indian company. Hereto, the investors (as described in the Framework Agreement) were prepared to invest in ITNL provided that HTIL and GSPL procured financial assistance for them and in consideration whereof GSPL would have Call Option to buy entire equity shares of SMMS. Hereto, in the Framework Agreement there were provisions imposing restrictions on Share Transfer, Change of Control etc. On 17.08.2006, a Shareholders Agreement stood executed which dealt with governance of ITNL.

11. On 22.12.2006, an Open Offer was made by Vodafone Group Plc. on behalf of Vodafone Group to Hutchison Whampoa Ltd., a non-binding bid for US $11.055 bn being the enterprise value for HTIL’s 67% interest in HEL.

12. On 22.12.2006, a press release was issued by HTIL in Hong Kong and New York Stock Exchanges that it had been approached by various potentially interested parties regarding a possible sale of “its equity interests” (not controlling interest) in HEL. That, till date no agreement stood entered into by HTIL

with any party.

13. On 25.12.2006, an offer comes from Essar Group to purchase HTIL's 66.99% shareholding at the highest offer price received by HTIL. Essar further stated that any sale by HTIL would require its consent as it claimed to be a co-promoter of HEL.

14. On 31.01.2007, a meeting of the Board of Directors of VIH was held approving the submission of a binding offer for 67% of HTIL's interest at 100% enterprise value of US $17.5 bn by way of acquisition by VIH of one share (which was the entire shareholding) in CGP, an indirect Cayman Islands subsidiary of HTIL. The said approval was subject to:

(i) reaching an agreement with Bharti that allowed VIH to make a bid on Hutch; and

(ii) entering into an appropriate partnership arrangement to satisfy FDI Rules in India.

15. On 6.02.2007, HTIL calls for a binding offer from Vodafone Group for its aggregate interests in 66.98% of the issued share capital of HEL controlled by companies owned, directly or indirectly, by HTIL together with inter-related loans.

16. On 9.02.2007, Vodafone Group makes a revised offer on behalf of VIH to HTIL. The said revised offer was of US $10.708 bn for 66.98% interest [at the enterprise value of US $18.250 bn] and for US $1.084 bn loans given by the Hutch Group. The offer further confirmed that in consultation with HTIL, the consideration payable may be reduced to take account of the various amounts which would be payable directly to certain existing legal local partners in order to extinguish HTIL's previous obligations to them. The offer further confirmed that VIH had come to arrangements with HTIL's existing local partners [AG, AS and Infrastructure Development Finance Company Limited (IDFC)] *to maintain the local Indian shareholdings in accordance with the Indian FDI*

requirements. The offer also expressed VIH's willingness to offer Essar the same financial terms in HEL which stood offered to HTIL.

17. On the same day, i.e., 9.02.2007, Bharti conveys its no objection to the proposal made by Vodafone Group to purchase a direct or indirect interest in HEL from the Hutchison Group and/ or Essar Group.

18. On 10.02.2007, a *re-revised offer* was submitted by Vodafone valuing HEL at an enterprise value of US $18.80 bn and offering US $11.076 bn for HTIL's interest in HEL.

19. On 11.02.2007, a Tax Due Diligence Report was submitted by Ernst & Young. The relevant observation from the said Report reads as follows:

> "The target structure now also includes a Cayman company, CGP Investments (Holdings) Limited, CGP Investments (Holdings) Limited was not originally within the target group. After our due diligence had commenced the seller proposed that CGP Investments (Holdings) Limited should be added to the target group and made available certain limited information about the company. Although we have reviewed this information, it is not sufficient for us to be able to comment on any tax risks associated with the company."

20. On 11.02.2007, UBS Limited (Financial Advisors to VIH) submitted a financial report setting out the methodology for valuation of HTIL's 67% effective interest in HEL through the acquisition of 100% of CGP.

21. On 11.02.2007, VIH and HTIL entered into an Agreement for Sale and Purchase of Share and Loans ("SPA" for short), under which HTIL agreed to procure the sale of the entire share capital of CGP which it held through HTIHL (BVI) for VIH. Further, HTIL also agreed to procure the assignment of Loans owed by CGP and Array Holdings Limited ["Array" for

short] (a 100% subsidiary of CGP) to HTI (BVI) Finance Ltd. (a direct subsidiary of HTIL). As part of its obligations, HTIL undertook to procure that each Wider Group Company would not terminate or modify any rights under any of its Framework Agreements or exercise any of their Options under any such agreement. HTIL also provided several warranties to VIH as set out in Schedule 4 to SPA which included that HTIL was the sole beneficial owner of CGP share.

22. On 11.02.2007, a Side Letter was sent by HTIL to VIH inter alia stating that out of the purchase consideration, up to US $80 million could be paid to some of its existing partners. By the said Side Letter, HTIL agreed to procure that Hutchison Telecommunications (India) Ltd. (Ms) ["HTIL Mauritius" for short], Omega Telecom Holdings Private Limited ["Omega" for short] and GSPL would enter into IDFC Transaction Agreement prior to the completion of the acquisition pursuant to SPA, which completion ultimately took place on 8.05.2007.

23. On 12.02.2007, Vodafone makes public announcement to Securities and Exchange Commission ["SEC" for short], Washington and on London Stock Exchange which contained two assertions saying that Vodafone had agreed to acquire a controlling interest in HEL via its subsidiary VIH and, second, that Vodafone had agreed to acquire companies that control a 67% interest in HEL.

24. On the same day, HTIL makes an announcement on HK Stock Exchange stating that it had agreed to sell its entire direct and indirect equity and loan interests held through subsidiaries, in HEL to VIH.

25. On 20.02.2007, VIH applied for approval to FIPB. This application was made pursuant to Press Note 1 which applied to the acquisition of an indirect interest in HEL by VIH from HTIL. It was stated that "CGP owns directly and indirectly through its subsidiaries an aggregate of 42.34% of the issued share capital of HEL and a further indirect interests in 9.62%

of the issued share capital of HEL". That, the transaction would result in VIH acquiring an indirect controlling interest of 51.96% in HEL, a company competing with Bharti, hence, approval of FIPB became necessary. It is to be noted that on 20.02.2007, VIH held 5.61% stake (directly) in Bharti.

26. On the same day, i.e., 20.02.2007, in compliance of Clause 5.2 of SPA, an *Offer Letter* was issued by Vodafone Group Plc on behalf of VIH to Essar for purchase of its entire shareholding (33%) in HEL.

27. On 2.03.2007, AG wrote to HEL, confirming that he, through his 100% Indian companies, owned 23.97% of a joint venture company-TII, which in turn owned 19.54% of HEL and, accordingly, his indirect interest in HEL worked out to 4.68%. That, he had full and unrestricted voting rights in companies owned by him. That, he had received credit support for his investments, but primary liability was with his companies.

28. A similar letter was addressed by AS on 5.03.2007 to FIPB. It may be noted that in January, 2006, post dilution of FDI cap, HTIL had to shed its stake to comply with 26% local shareholding guideline. Consequently, AS acquired 7.577% of HEL through his companies.

29. On 6.03.2007, Essar objects with FIPB to HTIL's proposed sale saying that HEL is a joint venture Indian company between Essar and Hutchison Group since May, 2000. That, Bharti is also an Indian company in the "same field" as HEL. Bharti was a direct competitor of HEL in India. According to Essar, the effect of the transaction between HTIL and VIH would be that Vodafone with an indirect controlling interest in HEL and in Bharti violated Press Note 1, particularly, absent consent from Essar. However, vide letter dated 14.03.2007, Essar gave its consent to the sale. Accordingly, its objection stood withdrawn.

30. On 14.03.2007, FIPB wrote to HEL seeking

clarification regarding a statement by HTIL before US SEC stating that HTIL Group would continue to hold an aggregate interest of 42.34% of HEL and an additional indirect interest through JVCs [TII and Omega] being non-wholly owned subsidiaries of HTIL which held an aggregate of 19.54% of HEL, which added up to 61.88%, whereas in the communication to FIPB dated 6.03.2007, the direct and indirect FDI held by HTIL was stated to be 51.96%.

31. By letter of the same date from HEL to FIPB, it was pointed out that HTIL was a company listed on NY SE. Accordingly, it had to file Statements in accordance with US SEC. That, under US GAAP, HTIL had to consolidate the assets and liabilities of companies even though not majority owned or controlled by HTIL, because of a US accounting standard that required HTIL to consolidate an entity whereby HTIL had "risk or reward". Therefore, this accounting consolidation required that even though HTIL held no shares nor management rights still they had to be computed in the computation of the holding in terms of the Listing Norms. It is the said accounting consolidation which led to the reporting of additional 19.54% in HEL, which leads to combined holding of 61.88%. On the other hand, under Indian GAAP, the interest as of March, 2006 was 42.34% + 7.28% (rounded up to 49.62%). After the additional purchase of 2.34% from Hindujas in August 2006, the aggregate HTIL direct and indirect FDI stood at 51.96%. In short, due to the difference in the US GAAP and the Indian GAAP the Declarations varied. The combined holding for US GAAP purposes was 61.88% whereas for Indian GAAP purposes it was 51.96%. Thus, according to HEL, the Indian GAAP number reflected the true equity ownership and control position.

32. By letter dated 9.03.2007, addressed by FIPB to HEL, several queries were raised. One of the questions FIPB had asked was *"as to which entity was entitled to appoint the directors to the Board of Directors of HEL on behalf of TIIL*

which owns 19.54% of HEL?" In answer, vide letter dated 14.03.2007, HEL informed FIPB that under the Articles of HEL the directors were appointed by its shareholders in accordance with the provisions of the Indian company law. However, in practice the directors of HEL have been appointed pro rata to their respective shareholdings which resulted in 4 directors being appointed from the Essar Group, 6 directors from HTIL Group and 2 directors from TII. In practice, the directors appointed by TII to the Board of HEL were AS and AG. One more clarification was sought by FIPB from HEL on the credit support received by AG for his investment in HEL. In answer to the said query, HEL submitted that the credit support for AG Group in respect of 4.68% stake in HEL through the Asim Ghosh investment entities, was a standby letter of credit issued by Rabobank Hong Kong in favour of Rabo India Finance Pvt. Ltd. which in turn has made a Rupee loan facility available to Centrino, one of the companies in AG Group.

33. By letter dated 14.03.2007 addressed by VIH to FIPB, it stood confirmed that VIH's *effective shareholding* in HEL would be 51.96%. That, following completion of the acquisition HTIL's shares in HEL the ownership of HEL was to be as follows :

(i) VIH would own 42% direct interest in HEL through its acquisition of 100% CGP (CI).

(ii) Through CGP (CI), VIH would also own 37.25% in TII which in turn owns 19.54% in HEL and 38% (45.79%) in Omega which in turn owns 5.11% in HEL (i.e. pro-rata route).

(iii) These investments combined would give VIH a controlling interest of 52% in HEL.

(iv) In addition, HTIL's existing Indian partners AG, AS and IDFC (i.e. SMMS), who between them held a 15% interest in HEL (i.e. option route), agreed to retain their shareholdings with full control, including voting rights and dividend rights. In other words, none of the Indian partners exited and, consequently, there was no change of control.

(v) The Essar Group would continue to own 33% of HEL.

34. On 15.03.2007, a Settlement Agreement was signed between HTIL and Essar Group. Under the said Agreement, HTIL agreed to pay US $415 mn to Essar for the following:

(a) acceptance of the SPA;

(b) for waiving rights or claims in respect of management and conduct of affairs of HEL;

(c) for giving up Right of First Refusal (RoFR), Tag Along Rights (TARs) and shareholders rights under Agreement dated 2.05.2000; and

(d) for giving up its objections before FIPB.

35. Vide Settlement Agreement, HTIL agreed to dispose of its direct and indirect equity, loan and other interests and rights, in and related to HEL, to VIH. These other rights and interests have been enumerated in the Order of the Revenue dated 31.05.2010 as follows :

1. Right to equity interest (direct and indirect) in HEL.

2. Right to do telecom business in India

3. Right to jointly own and avail the telecom licences in India

4. Right to use the Hutch brand in India

5. Right to appoint/remove directors from the Board of HEL and its subsidiaries

6. Right to exercise control over the management and affairs of the business of HEL (Management Rights)

7. Right to take part in all the investment, management and financial decisions of HEL

8. Right over the assigned loans and advances utilized for the business in India

9. Right of subscribing at par value in certain Indian companies

10. Right to exercise call option at the price agreed in Indian companies

11. Right to control premium

12. Right to non-compete against HTIL within the territory of India

13. Right to consultancy support in the use of Oracle license for the Indian business

14. Other intangible rights (right of customer base, goodwill etc.)

36. On 15.03.2007, a Term Sheet Agreement between VIH and Essar Teleholdings Limited, an Indian company which held 11% in HEL, and Essar Communications Limited, a Mauritius company which held 22% in HEL, was entered into for regulating the affairs of HEL and the relationship of the shareholders of HEL. In the recitals, it was stated that VIH had agreed to acquire the entire indirect shareholding of HTIL in HEL, including all rights, contractual or otherwise, to acquire directly or indirectly shares in HEL owned by others which shares shall, for the purpose of the Term Sheet, be considered to be part of the holding acquired by VIH. The Term Sheet governed the relationship between Essar and VIH as shareholders of HEL including VIH's right as a shareholder of HEL:

(a) to nominate 8 directors out of 12 to the Board of Directors;

(b) nominee of Vodafone had to be there to constitute the quorum for the Board of Directors;

(c) to get a RoFR over the shares held by Essar in HEL;

(d) should Vodafone Group shareholder sell its shares in HEL to an outsider, Essar had a TAR in respect of Essar's shareholding in HEL.

37. On 15.03.2007, a Put Option Agreement was signed between VIH and Essar Group requiring VIH to buy from Essar Group Shareholders all the Option Shares held by them.

38. By letter dated 17.03.2007, HTIL confirmed in writing to AS that it had no beneficial, or legal or any other right in AS's TII interest or HEL interest.

39. On 19.03.2007, a letter was addressed by FIPB to VIH asking VIH to clarify as to under what circumstances VIH agreed to pay US $11.08 bn for acquiring 67% of HEL when the actual acquisition is only 51.96%. This query presupposes that even according to FIPB the actual acquisition was only 51.96% (52% approx.).

40. On the same day, VIH replied that VIH has agreed to acquire from HTIL, interests in HEL which included 52% equity shareholding for US $11.08 bn. That, the price included a control premium, use and rights to the Hutch Brand in India, a non-compete agreement with the Hutch Group, the value of non-voting non-convertible preference shares, various loans obligations and the entitlement to acquire a further 15% indirect interest in HEL as set out in the letter dated 14.03.2007 addressed to FIPB (see page 6117 of SLP Vol. 26). According to the said letter dated 19.03.2007, all the above elements together equated to 67% of the *economic value of HEL*.

41. Vide Agreement dated 21.03.2007, VIH diluted its stake in Bharti by 5.61%.

42. In reply to the queries raised by FIPB regarding break up of valuation, VIH confirmed as follows:

Various assets and liabilities of CGP included its rights and entitlements, including subscription rights, call options to acquire in future a further 62.75% of TII, call options to acquire in future a further 54.21% of Omega which together would give a further 15.03% proportionate indirect equity ownership of HEL, control premium, use and rights to Hutch brand in India and a non-compete agreement with HTIL. No individual price was assigned to any of the above items. That, under IFRS, consolidation included TII and Omega and, consequently, the accounts under IFRS showed the total shareholding in HEL as 67% (approx.). Thus, arrangements relating to Options stood valued as assets of CGP. In global basis valuation, assets of CGP consisted of: its downstream holdings, intangibles and arrangement relating to Options, i.e. Bundle of Rights acquired by VIH. This reply was in the letter dated 27.03.2007 in which it was further stated that HTIL had conducted an auction for sale of its interests in HEL in which HTIL had asked each bidder to name its price with reference to the enterprise value of HEL. As a consequence of the transaction, Vodafone will effectively step into the shoes of HTIL including all the rights in respect of its Indian investments that HTIL enjoyed. Lastly, the Indian joint venture partners would remain invested in HEL as the transaction did not involve the Indian investors selling any of their respective stakes.

43. On 5.04.2007, HEL wrote to the Joint Director of Income Tax (International Taxation) stating that HEL had no tax liabilities accruing out of the subject transaction.

44. Pursuant to the resolution passed by the Board of Directors of CGP on 30.04.2007, it was decided that on acquisition loans owed by CGP to HTI (BVI) Finance Ltd. would

be assigned to VIH; the existing Directors of CGP would resign; Erik de Rijk would become the only Director of CGP. A similar resolution was passed on the same day by the Board of Directors of Array.

45. On 7.05.2007, FIPB gave its approval to the transaction, subject to compliance with the applicable laws and regulations in India.

46. On 8.05.2007, consequent upon the Board Resolutions passed by CGP and its downstream companies, the following steps were taken:

(i) resignation of all the directors of Hutch Group;

(ii) appointment of new directors of Vodafone Group;

(iii) resolutions passed by TII, Jaykay Finholding (India) Private Limited, UMT Investments Ltd., UMTL, Omega (Indian incorporated holding companies) accepting the resignation of HTIL's nominee directors and appointing VIH's nominee directors;

(iv) same steps were taken by HEL and its subsidiaries;

(v) sending of a Side Letter by HTIL to VIH relating to completion mechanics;

(vi) computation of net amount payable by VIH to HTIL including retention of a certain amount out of US $11.08 bn paid on 8.05.2007 towards expenses to operationalize the Option Agreements and adjustments for breach (if any) of warranties, etc.;

(vii) assignment of loans given by HTI (BVI) Finance Ltd. to CGP and Array in favour of VIH;

(viii) cancellation of share certificate of HTIHL (BVI) and entering the name of VIH in the Register of Members of CGP;

(ix) execution of Tax Deed of Covenant indemnifying VIH in respect of tax or transfer pricing liabilities payable by Wider Group (CGP, GSPL, Mauritius holding companies, Indian operating companies).

(x) a Business Transfer Agreement between GSPL and a subsidiary of HWP Investments Holdings (India) Ltd. (Ms) for sale of Call Centre earlier owned by GSPL;

(xi) payment of US $10.85 bn by VIH to HTIL (CI).

47. On 5.06.2007, under the Omega Agreement, it was agreed that in view of the SPA there would be a consequent change of control in HTIL Mauritius, which holds 45.79% in Omega, and that India Development Fund ("IDF" for short), IDFC and SSKI Corporate Finance Private Limited ("SSKI" for short) would, instead of exercising Put Option and Cashless Option under 2006 IDFC Framework Agreement, exercise the same in pursuance of Omega Agreement. That, under the Omega Agreement, GSPL waived its right to exercise the Call Option under the 2006 IDFC Framework Agreement.

48. On 6.06.2007, a Framework Agreement was entered into among IDF, IDFC, SMMS, IDFC PE, HTIL Mauritius, GSPL, Omega and VIH by which GSPL had a Call Option to buy the entire equity shares of SMMS. Consequently, on 7.06.2007, a Shareholders Agreement was executed by which the shareholding pattern of Omega changed with SMMS having 61.6% and HTIL Mauritius having 38.4%.

49. On 27.06.2007, HTIL declared a *special dividend* of HK $6.75 per share, on account of the gains made by sale of HTIL's entire interest in HEL.

50. On 5.07.2007, a *Framework Agreement* was entered into among AG, AG Mercantile Company Private Limited, Plustech Mercantile Co. (P) Ltd ["Plustech" for short], GSPL,

Nadal Trading Company Private Limited ["Nadal" for short] and VIH. Under clause 4.4, GSPL had an unconditional right to purchase all shares of AG in AG Mercantile Company Pvt. Ltd. at any time and in consideration for such *call option*, GSPL agreed to pay to AG an amount of US $6.3 mn annually.

51. On the same day, i.e., 5.07.2007, a *Framework Agreement* was entered into among AS, his wife, Scorpios, MVH, GSPL, NDC and VIH. Under clause 4.4 GSPL had an unconditional right to purchase all shares of AS and his wife held in Scorpios at any time and in consideration for the *call option* GSPL agreed to pay AS and his wife an amount of US$ 10.2 mn per annum.

52. On 5.07.2007, TII Shareholders Agreement was entered into among Nadal, NDC, CGP India Investments Limited ["CGP India" for short], TII and VIH to regulate the affairs of TII. Under clause 3.1, NDC had 38.78% shareholding in TII, CGP India had 37.85% and Nadal had 23.57%.

53. It is not necessary to go into the earlier round of litigation. Suffice it to state that on 31.05.2010, an Order was passed by the Department under Sections 201(1) and 201(1A) of the Income Tax Act, 1961 ["the Act" for short] declaring that Indian Tax Authorities had jurisdiction to tax the transaction against which VIH filed Writ Petition No. 1325 of 2010 before the Bombay High Court which was dismissed on 8.09.2010 vide the impugned judgment [reported in 329 ITR 126], hence, this Civil Appeal.

B. Ownership Structure

54. In order to understand the above issue, we reproduce below the Ownership Structure Chart as on 11.02.2007. The Chart speaks for itself.

55. To sum up, CGP held 42.34% in HEL through 100% wholly owned subsidiaries [Mauritius companies], 9.62% indirectly through TII and Omega [i.e. pro rata route], and 15.03% through GSPL route.

56. To explain the GSPL route briefly, it may be mentioned that on 11.02.2007 AG Group of companies held 23.97% in TII, AS Group of companies held 38.78% in TII whereas SMMS held 54.21% in Omega. Consequently, holding of AG in HEL through TII stood at 4.68% whereas holding of AS in HEL through TII stood at 7.577% and holding of SMMS in HEL through Omega stood at 2.77%, which adds up to 15.03% in HEL. These holdings of AG, AS and SMMS came under the Option Route. In this connection, it may be mentioned that GSPL is an Indian company indirectly owned by CGP. It held Call Options and Subscription Options to be exercised in future under circumstances spelt out in TII and IDFC Framework Agreements (keeping in mind the sectoral cap of 74%).

<u>Correctness of Azadi Bachao case - Re: Tax Avoidance/ Evasion</u>

57. Before us, it was contended on behalf of the Revenue that *Union of India v. Azadi Bachao Andolan* (2004) 10 SCC 1 needs to be overruled insofar as it departs from *McDowell and Co. Ltd. v. CTO* (1985) 3 SCC 230 principle for the following : i) Para 46 of *McDowell* judgment has been missed which reads as under: "on this aspect Chinnappa Reddy, J. has proposed a separate opinion with which we agree". [i.e. Westminster principle is dead]. ii) That, *Azadi Bachao* failed to read paras 41-45 and 46 of *McDowell* in entirety. If so read, the only conclusion one could draw is that four learned judges speaking through Misra, J. agreed with the observations of Chinnappa Reddy, J. as to how in certain circumstances tax avoidance should be brought within the tax net. iii) That, subsequent to *McDowell*, another matter came before the Constitution Bench of five Judges in *Mathuram Agrawal v. State of Madhya Pradesh* (1999) 8 SCC 667, in which Westminster principle was quoted which has not been noticed by *Azadi Bachao*.

Our Analysis

58. Before coming to Indo-Mauritius DTAA, we need to clear the doubts raised on behalf of the Revenue regarding the correctness of *Azadi Bachao* (supra) for the simple reason that certain tests laid down in the judgments of the English Courts subsequent to *The Commissioners of Inland Revenue v. His Grace the Duke of Westminster* 1935 All E.R. 259 and *W.T. Ramsay Ltd. v. Inland Revenue Commissioners* (1981) 1 All E.R. 865 help us to understand the scope of Indo-Mauritius DTAA. It needs to be clarified, that, *McDowell* dealt with two aspects. First, regarding validity of the Circular(s) issued by CBDT concerning Indo-Mauritius DTAA. Second, on concept of tax avoidance/evasion. Before us, arguments were advanced on behalf of the Revenue only regarding the second aspect.

59. The Westminster principle states that, "given that a document or transaction is genuine, the court cannot go behind it to some supposed underlying substance". The said principle has been reiterated in subsequent English Courts Judgments as "the cardinal principle".

60. Ramsay was a case of sale-lease back transaction in which gain was sought to be counteracted, so as to avoid tax, by establishing an allowable loss. The method chosen was to buy from a company a readymade scheme, whose object was to create a neutral situation. The decreasing asset was to be sold so as to create an artificial loss and the increasing asset was to yield a gain which would be exempt from tax. The Crown challenged the whole scheme saying that it was an artificial scheme and, therefore, fiscally in-effective. It was held that Westminster did not compel the court to *look at* a document or a transaction, isolated from the context to which it properly belonged. It is the task of the Court to ascertain the legal nature of the transaction and while doing so it has to *look at* the entire transaction as a whole and not to adopt a dissecting approach. In the present case, the Revenue has adopted a dissecting

approach at the Department level.

61. Ramsay did not discard Westminster but read it in the proper context by which "device" which was colourable in nature had to be ignored as fiscal nullity. *Thus, Ramsay lays down the principle of statutory interpretation rather than an over-arching anti-avoidance doctrine imposed upon tax laws.*

62. *Furniss (Inspector of Taxes) v. Dawson* (1984) 1 All E.R. 530 dealt with the case of interpositioning of a company to evade tax. On facts, it was held that the inserted step had no business purpose, except deferment of tax although it had a business effect. *Dawson* went beyond Ramsay. It reconstructed the transaction not on some fancied principle that anything done to defer the tax be ignored but on the premise that the inserted transaction did not constitute "disposal" under the relevant Finance Act. Thus, Dawson is an extension of *Ramsay* principle.

63. After *Dawson,* which empowered the Revenue to restructure the transaction in certain circumstances, the Revenue started rejecting every case of strategic investment/ tax planning undertaken years before the event saying that the insertion of the entity was effected with the sole intention of tax avoidance. In *Craven (Inspector of Taxes) v. White (Stephen)* (1988) 3 All. E.R. 495 it was held that the Revenue cannot start with the question as to whether the transaction was a tax deferment/saving device but that the Revenue should apply the *look at* test to ascertain its true legal nature. It observed that genuine strategic planning had not been abandoned.

64. The majority judgment in *McDowell* held that "tax planning may be legitimate provided it is within the framework of law" (para 45). In the latter part of para 45, it held that "colourable device cannot be a part of tax planning and it is wrong to encourage the belief that it is honourable to avoid payment of tax by resorting to dubious methods". It is the obligation of every citizen to pay the taxes without resorting to subterfuges. The above observations should be read with para

46 where the majority holds "on this aspect one of us, Chinnappa Reddy, J. has proposed a separate opinion with which we agree". The words "this aspect" express the majority's agreement with the judgment of Reddy, J. only in relation to tax evasion through the use of colourable devices and by resorting to dubious methods and subterfuges. Thus, it cannot be said that all tax planning is illegal/illegitimate/impermissible. Moreover, Reddy, J. himself says that he agrees with the majority. In the judgment of Reddy, J. there are repeated references to schemes and devices in contradistinction to "legitimate avoidance of tax liability" (paras 7-10, 17 & 18). In our view, although Chinnappa Reddy, J. makes a number of observations regarding the need to depart from the "Westminster" and tax avoidance – these are clearly only in the context of artificial and colourable devices. Reading McDowell, in the manner indicated hereinabove, in cases of treaty shopping and/or tax avoidance, there is no conflict between McDowell and Azadi Bachao or between McDowell and Mathuram Agrawal.

International Tax Aspects of Holding Structures

65. In the thirteenth century, Pope Innocent IV espoused the theory of the legal fiction by saying that corporate bodies could not be ex-communicated because they only exist in abstract. This enunciation is the foundation of the *separate entity principle*.

66. The approach of both the corporate and tax laws, particularly in the matter of corporate taxation, generally is founded on the abovementioned *separate entity principle,* i.e., treat a company as a separate person. The Indian Income Tax Act, 1961, in the matter of corporate taxation, is founded on the principle of the independence of companies and other entities subject to income-tax. Companies and other entities are viewed as economic entities with legal independence vis-a-vis their shareholders/participants. It is fairly well accepted that a subsidiary and its parent are totally distinct tax payers.

Consequently, the entities subject to income-tax are taxed on profits derived by them on standalone basis, irrespective of their actual degree of economic independence and regardless of whether profits are reserved or distributed to the shareholders/ participants. Furthermore, shareholders/ participants, that are subject to (personal or corporate) income-tax, are generally taxed on profits derived in consideration of their shareholding/participations, such as capital gains. Now a days, it is fairly well settled that for tax treaty purposes a subsidiary and its parent are also totally separate and distinct tax payers.

67. It is generally accepted that the group parent company is involved in giving principal guidance to group companies by providing general policy guidelines to group subsidiaries. However, the fact that a parent company exercises shareholder's influence on its subsidiaries does not generally imply that the subsidiaries are to be deemed residents of the State in which the parent company resides. Further, if a company is a parent company, that company's executive director(s) should lead the group and the company's shareholder's influence will generally be employed to that end. This obviously implies a restriction on the autonomy of the subsidiary's executive directors. Such a restriction, which is the inevitable consequences of any group structure, is generally accepted, both in corporate and tax laws. However, where the subsidiary's executive directors' competences are transferred to other persons/bodies or where the subsidiary's executive directors' decision making has become fully subordinate to the Holding Company with the consequence that the subsidiary's executive directors are no more than puppets then the turning point in respect of the subsidiary's place of residence comes about. Similarly, if an actual controlling Non-Resident Enterprise (NRE) makes an indirect transfer through "abuse of organisation form/legal form and without reasonable business purpose" which results in tax avoidance or avoidance of withholding tax, then the Revenue may disregard the form of the

arrangement or the impugned action through use of Non-Resident Holding Company, re-characterize the equity transfer according to its economic substance and impose the tax on the actual controlling Non-Resident Enterprise. Thus, whether a transaction is used principally as a colourable device for the distribution of earnings, profits and gains, is determined by a review of all the facts and circumstances surrounding the transaction. It is in the above cases that the principle of lifting the corporate veil or the doctrine of substance over form or the concept of beneficial ownership or the concept of alter ego arises. There are many circumstances, apart from the one given above, where separate existence of different companies, that are part of the same group, will be totally or partly ignored as a device or a conduit (in the pejorative sense).

68. The common law jurisdictions do invariably impose taxation against a corporation based on the legal principle that the corporation is "a person" that is separate from its members. It is the decision of the *House of Lords in Salomon v. Salomon* (1897) A.C. 22 that opened the door to the formation of a corporate group. If a "one man" corporation could be incorporated, then it would follow that one corporation could be a subsidiary of another. This legal principle is the basis of *Holding Structures.* It is a common practice in international law, which is the basis of international taxation, for foreign investors to invest in Indian companies through an interposed foreign holding or operating company, such as Cayman Islands or Mauritius based company for both tax and business purposes. In doing so, foreign investors are able to avoid the lengthy approval and registration processes required for a direct transfer (i.e., without a foreign holding or operating company) of an equity interest in a foreign invested Indian company. However, taxation of such Holding Structures very often gives rise to issues such as double taxation, tax deferrals and tax avoidance. In this case, we are concerned with the concept of GAAR. In this case, we are not concerned with treaty-shopping but with the anti-avoidance rules. The concept of GAAR is not

new to India since India already has a judicial anti-avoidance rule, like some other jurisdictions. Lack of clarity and absence of appropriate provisions in the statute and/or in the treaty regarding the circumstances in which judicial anti-avoidance rules would apply has generated litigation in India. Holding Structures are recognized in corporate as well as tax laws. Special Purpose Vehicles (SPVs) and Holding Companies have a place in legal structures in India, be it in company law, takeover code under SEBI or even under the income tax law. When it comes to taxation of a Holding Structure, at the threshold, the burden is on the Revenue to allege and establish abuse, in the sense of tax avoidance in the creation and/or use of such structure(s). In the application of a judicial anti-avoidance rule, the Revenue may invoke the "substance over form" principle or "piercing the corporate veil" test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant. To give an example, if a structure is used for circular trading or round tripping or to pay bribes then such transactions, though having a legal form, should be discarded by applying the test of fiscal nullity. Similarly, in a case where the Revenue finds that in a Holding Structure an entity which has no commercial/business substance has been interposed only to avoid tax then in such cases applying the test of fiscal nullity it would be open to the Revenue to discard such inter-positioning of that entity. However, this has to be done at the threshold. In this connection, we may reiterate the *"look at"* principle enunciated in *Ramsay* (supra) in which it was held that the Revenue or the Court must *look at* a document or a transaction in a context to which it properly belongs to. It is the task of the Revenue/Court to ascertain the legal nature of the transaction and while doing so it has to look at the entire transaction as a whole and not to adopt a dissecting approach. The Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but that it should apply the "look at" test to ascertain its true legal nature [See *Craven v. White* (supra) which further observed that

genuine strategic tax planning has not been abandoned by any decision of the English Courts till date]. Applying the above tests, we are of the view that every strategic foreign direct investment coming to India, as an investment destination, should be seen in a holistic manner. While doing so, the Revenue/Courts should keep in mind the following factors: the concept of participation in investment, the duration of time during which the Holding Structure exists; the period of business operations in India; the generation of taxable revenues in India; the timing of the exit; the continuity of business on such exit. In short, the onus will be on the Revenue to identify the scheme and its dominant purpose. The corporate business purpose of a transaction is evidence of the fact that the impugned transaction is not undertaken as a colourable or artificial device. The stronger the evidence of a device, the stronger the corporate business purpose must exist to overcome the evidence of a device.

Whether Section 9 is a "look through" provision as submitted on behalf of the Revenue?

69. According to the Revenue, if its primary argument (namely, that HTIL has, under the SPA, directly extinguished its property rights in HEL and its subsidiaries) fails, even then in any event, income from the sale of CGP share would nonetheless fall within Section 9 of the Income Tax Act, 1961 as that Section provides for a *"look through"*. In this connection, it was submitted that the word "through" in Section 9 inter alia means "in consequence of". It was, therefore, argued that if transfer of a capital asset situate in India happens "in consequence of" something which has taken place overseas (including transfer of a capital asset), then all income derived even indirectly from such transfer, even though abroad, becomes taxable in India. That, even if control over HEL were to get transferred in consequence of transfer of the CGP Share outside India, it would yet be covered by Section 9.

70. We find no merit in the above submission of the

Revenue. At the outset, we quote hereinbelow the following Sections of the Income Tax Act, 1961:

> Scope of total income.
>
> 5. (2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which—
>
>> (a) is received or is deemed to be received in India in such year by or on behalf of such person ; or
>>
>> (b) accrues or arises or is deemed to accrue or arise to him in India during such year.
>
> Income deemed to accrue or arise in India.
>
> 9. (1) The following incomes shall be deemed to accrue or arise in India :—
>
>> (i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

71. Section 9(1)(i) gathers in one place various types of income and directs that income falling under each of the sub-clauses shall be deemed to accrue or arise in India. Broadly there are four items of income. The income dealt with in each sub-clause is distinct and independent of the other and the requirements to bring income within each sub-clause, are separately noted. Hence, it is not necessary that income falling in one category under any one of the sub-clauses should also satisfy the requirements of the other sub-clauses to bring it within the expression "income deemed to accrue or arise in India" in Section 9(1)(i). In this case, we are concerned with the last sub-clause of Section 9(1)(i) which refers to income arising

from "transfer of a capital asset situate in India". Thus, charge on capital gains arises on transfer of a capital asset situate in India during the previous year. The said sub-clause consists of three elements, namely, transfer, existence of a capital asset, and situation of such asset in India. All three elements should exist in order to make the last sub-clause applicable. Therefore, if such a transfer does not exist in the previous year no charge is attracted. Further, Section 45 enacts that such income shall be deemed to be the income of the previous year in which transfer took place. Consequently, there is no room for doubt that such transfer should exist during the previous year in order to attract the said sub-clause. The fiction created by Section 9(1)(i) applies to the assessment of income of non-residents. In the case of a resident, it is immaterial whether the place of accrual of income is within India or outside India, since, in either event, he is liable to be charged to tax on such income. But, in the case of a non-resident, unless the place of accrual of income is within India, he cannot be subjected to tax. In other words, if any income accrues or arises to a non-resident, directly or indirectly, outside India is fictionally deemed to accrue or arise in India if such income accrues or arises as a sequel to the transfer of a capital asset situate in India. Once the factum of such transfer is established by the Department, then the income of the non-resident arising or accruing from such transfer is made liable to be taxed by reason of Section 5(2)(b) of the Act. This fiction comes into play only when the income is not charged to tax on the basis of receipt in India, as receipt of income in India by itself attracts tax whether the recipient is a resident or non-resident. This fiction is brought in by the legislature to avoid any possible argument on the part of the non-resident vendor that profit accrued or arose outside India by reason of the contract to sell having been executed outside India. Thus, income accruing or arising to a non-resident outside India on transfer of a capital asset situate in India is fictionally deemed to accrue or arise in India, which income is made liable to be taxed by reason of Section 5(2)(b) of the Act. This is the main purpose behind enactment of Section 9(1)(i) of the Act. We have to give effect to the language of the section when it is unambiguous and admits of no doubt regarding its interpretation, particularly when a legal fiction is embedded in that section. A legal fiction has a limited scope. A legal fiction cannot be expanded by giving purposive interpretation particularly if the result of such interpretation is to transform the concept of chargeability which is also there in Section 9(1)(i), particularly when one reads Section 9(1)(i) with Section 5(2)(b) of the Act. What is contended on behalf of the Revenue is that under Section 9(1)(i) it can "look through" the transfer of shares of a foreign company holding shares in an Indian company and treat the transfer of shares of the foreign company as equivalent to the transfer of the shares of the Indian company on the premise that Section 9(1)(i) covers direct and *indirect transfers* of capital assets. For the above reasons, Section 9(1)(i) cannot by a process of interpretation be extended to cover *indirect transfers* of capital assets/property situate in India. To do so, would amount to changing the content and ambit of Section 9(1)(i). We cannot re-write Section 9(1)(i). The legislature has not used the words indirect transfer in Section 9(1)(i). If the word indirect is read into Section 9(1)(i), it would render the express statutory requirement of the 4th sub-clause in Section 9(1)(i) nugatory. This is because Section 9(1)(i) applies to transfers of a capital asset situate in India. This is one of the elements in the 4th sub-clause of Section 9(1)(i) and if indirect transfer of a capital asset is read into Section 9(1)(i) then the words *capital asset situate in India* would be rendered nugatory. Similarly, the words underlying asset do not find place in Section 9(1)(i). Further, "transfer" should be of an asset in respect of which it is possible to compute a capital gain in accordance with the provisions of the Act. Moreover, even Section 163(1)(c) is wide enough to cover the income whether received directly or indirectly. Thus, the words directly or indirectly in Section 9(1)(i) go with the income and not with the transfer of a capital asset (property). Lastly, it may be mentioned that the Direct Tax Code (DTC) Bill, 2010 proposes to tax income from transfer of shares of a foreign company by

a non-resident, where at any time during 12 months preceding the transfer, the fair market value of the assets in India, owned directly or indirectly, by the company, represents at least 50% of the fair market value of all assets owned by the company. Thus, the DTC Bill, 2010 proposes taxation of offshore share transactions. This proposal indicates in a way that *indirect transfers* are not covered by the existing Section 9(1)(i) of the Act. In fact, the DTC Bill, 2009 expressly stated that income accruing even from indirect transfer of a capital asset situate in India would be deemed to accrue in India. These proposals, therefore, show that in the existing Section 9(1)(i) the word indirect cannot be read on the basis of purposive construction. The question of providing *"look through"* in the statute or in the treaty is a matter of policy. It is to be expressly provided for in the statute or in the treaty. Similarly, *limitation of benefits* has to be expressly provided for in the treaty. Such clauses cannot be read into the Section by interpretation. For the foregoing reasons, we hold that Section 9(1)(i) is not a "look through" provision.

Transfer of HTIL's property rights by Extinguishment?

72. The primary argument advanced on behalf of the Revenue was that the SPA, commercially construed, evidences a transfer of HTIL's property rights by their extinguishment. That, HTIL had, under the SPA, directly extinguished its rights of control and management, which are property rights, over HEL and its subsidiaries and, consequent upon such extinguishment, there was a transfer of capital asset situated in India. In support, the following features of the SPA were highlighted: (i) the right of HTIL to direct a downstream subsidiary as to the manner in which it should vote. According to the Revenue, this right was a property right and not a contractual right. It vested in HTIL as HTIL was a parent company, i.e., a 100% shareholder of the subsidiary; (ii) According to the Revenue, the 2006 Shareholders/ Framework Agreements had to be continued upon transfer of control of HEL to VIH so that VIH could step

into the shoes of HTIL. According to the Revenue, such continuance was ensured by payment of money to AS and AG by VIH failing which AS and AG could have walked out of those agreements which would have jeopardized VIH's control over 15% of the shares of HEL and, consequently, the stake of HTIL in TII would have stood reduced to minority; (iii) Termination of IDFC Framework Agreement of 2006 and its substitution by a fresh Framework Agreement dated 5.06.2007, as warranted by SPA; (iv) Termination of Term Sheet Agreement dated 5.07.2003. According to the Revenue, that Term Sheet Agreement was given effect to by clause 5.2 of the SPA which gave Essar the right to Tag Along with HTIL and exit from HEL. That, by a specific Settlement Agreement dated 15.03.2007 between HTIL and Essar, the said Term Sheet Agreement dated 5.07.2003 stood terminated. This, according to the Revenue, was necessary because the Term Sheet bound the parties; (v) the SPA ignores legal entities interposed between HTIL and HEL enabling HTIL to directly nominate the Directors on the Board of HEL; (vi) Qua management rights, even if the legal owners of HEL's shares (Mauritius entities) could have been directed to vote by HTIL in a particular manner or to nominate a person as a Director, such rights existed dehors the CGP share; (vii) Vide clause 6.2 of the SPA, HTIL was required to exercise voting rights in the specified situations on the diktat of VIH ignoring the legal owner of CGP share [HTIHL (BVI)]. Thus, according to the Revenue, HTIL ignored its subsidiaries and was exercising the voting rights qua the CGP and the HEL shares directly, ignoring all the intermediate subsidiaries which are 100% held and which are non-operational. According to the Revenue, extinguishment took place dehors the CGP share. It took place by virtue of various clauses of SPA as HTIL itself disregarded the corporate structure it had set up; (viii) As a holder of 100% shares of downstream subsidiaries, HTIL possessed *de facto control* over such subsidiaries. Such *de facto control* was the subject matter of the SPA.

73. At the outset, we need to reiterate that in this case we are concerned with the sale of shares and not with the sale of assets, item-wise. The facts of this case show sale of the entire investment made by HTIL, through a Top company, viz. CGP, in the Hutchison Structure. In this case we need to apply the *"look at"* test. In the impugned judgment, the High Court has rightly observed that the arguments advanced on behalf of the Department vacillated. The reason for such vacillation was adoption of *"dissecting approach"* by the Department in the course of its arguments. *Ramsay* (supra) enunciated the *look at* test. According to that test, the task of the Revenue is to ascertain the legal nature of the transaction and, while doing so, it has to *look at* the entire transaction holistically and not to adopt a dissecting approach. One more aspect needs to be reiterated. There is a conceptual difference between *preordained transaction* which is created for tax avoidance purposes, on the one hand, and a transaction which evidences *investment to participate* in India. In order to find out whether a given transaction evidences a preordained transaction in the sense indicated above or *investment to participate,* one has to take into account the factors enumerated hereinabove, namely, duration of time during which the holding structure existed, the period of business operations in India, generation of taxable revenue in India during the period of business operations in India, the timing of the exit, the continuity of business on such exit, etc. Applying these tests to the facts of the present case, we find that the Hutchison structure has been in place since 1994. It operated during the period 1994 to 11.02.2007. It has paid income tax ranging from Rs. 3 crore to Rs. 250 crore per annum during the period 2002-03 to 2006-07. Even after 11.02.2007, taxes are being paid by VIH ranging from `394 crore to Rs. 962 crore per annum during the period 2007-08 to 2010-11 (these figures are apart from indirect taxes which also run in crores). Moreover, the SPA indicates "continuity" of the telecom business on the exit of its predecessor, namely, HTIL. Thus, it cannot be said that the structure was created or used as a sham or tax avoidant. It

cannot be said that HTIL or VIH was a "fly by night" operator/ short time investor. If one applies the *look at* test discussed hereinabove, without invoking the dissecting approach, then, in our view, extinguishment took place because of the transfer of the CGP share and not by virtue of various clauses of SPA. In a case like the present one, where the structure has existed for a considerable length of time generating taxable revenues right from 1994 and where the court is satisfied that the transaction satisfies all the parameters of "participation in investment" then in such a case the court need not go into the questions such as de facto control vs. legal control, legal rights vs. practical rights, etc.

74. Be that as it may, did HTIL possess a legal right to appoint directors onto the board of HEL and as such had some "property right" in HEL? If not, the question of such a right getting "extinguished" will not arise. A legal right is an enforceable right. Enforceable by a legal process. The question is what is the nature of the "control" that a parent company has over its subsidiary. It is not suggested that a parent company never has control over the subsidiary. For example, in a proper case of "lifting of corporate veil", it would be proper to say that the parent company and the subsidiary form one entity. But barring such cases, the legal position of any company incorporated abroad is that its powers, functions and responsibilities are governed by the law of its incorporation. No multinational company can operate in a foreign jurisdiction save by operating independently as a "good local citizen". A company is a separate legal persona and the fact that all its shares are owned by one person or by the parent company has nothing to do with its separate legal existence. If the owned company is wound up, the liquidator, and not its parent company, would get hold of the assets of the subsidiary. In none of the authorities have the assets of the subsidiary been held to be those of the parent unless it is acting as an agent. Thus, even though a subsidiary may normally comply with the request of a parent company it is not just a puppet of the parent

company. The difference is between having power or having a persuasive position. Though it may be advantageous for parent and subsidiary companies to work as a group, each subsidiary will look to see whether there are separate commercial interests which should be guarded. When there is a parent company with subsidiaries, is it or is it not the law that the parent company has the "power" over the subsidiary. It depends on the facts of each case. For instance, take the case of a one-man company, where only one man is the shareholder perhaps holding 99% of the shares, his wife holding 1%. In those circumstances, his control over the company may be so complete that it is his alter ego. But, in case of multinationals it is important to realise that their subsidiaries have a great deal of autonomy in the country concerned except where subsidiaries are created or used as a sham. Of course, in many cases the courts do lift up a corner of the veil but that does not mean that they alter the legal position between the companies. The directors of the subsidiary under their Articles are the managers of the companies. If new directors are appointed even at the request of the parent company and even if such directors were removable by the parent company, such directors of the subsidiary will owe their duty to their companies (subsidiaries). They are not to be dictated by the parent company if it is not in the interests of those companies (subsidiaries). The fact that the parent company exercises shareholder's influence on its subsidiaries cannot obliterate the decision-making power or authority of its (subsidiary's) directors. They cannot be reduced to be puppets. The decisive criteria is whether the parent company's management has such steering interference with the subsidiary's core activities that subsidiary can no longer be regarded to perform those activities on the authority of its own executive directors.

75. Before dealing with the submissions advanced on behalf of the Revenue, we need to appreciate the reason for execution of the SPA. Exit is an important right of an investor in every strategic investment. The present case concerns

transfer of investment in entirety. As stated above, exit coupled with continuity of business is one of the important tell-tale circumstance which indicates the commercial/business substance of the transaction. Thus, the need for SPA arose to re-adjust the outstanding loans between the companies; to provide for standstill arrangements in the interregnum between the date of signing of the SPA on 11.02.2007 and its completion on 8.05.2007; to provide for a seamless transfer and to provide for fundamental terms of price, indemnities, warranties etc. As regards the right of HTIL to direct a downstream subsidiary as to the manner in which it should vote is concerned, the legal position is well settled, namely, that even though a subsidiary may normally comply with the request of a parent company, it is not just a puppet of the parent company. The difference is between having the *power* and having a *persuasive position*. A great deal depends on the facts of each case. Further, as stated above, a company is a separate legal persona, and the fact that all the shares are owned by one person or a company has nothing to do with the existence of a separate company. Therefore, though it may be advantageous for a parent and subsidiary companies to work as a group, each subsidiary has to protect its own separate commercial interests. In our view, on the facts and circumstances of this case, the right of HTIL, if at all it is a right, to direct a downstream subsidiary as to the manner in which it should vote would fall in the category of a persuasive position/influence rather than having a power over the subsidiary. In this connection the following facts are relevant.

76. Under the Hutchison structure, the business was carried on by the Indian companies under the control of their Board of Directors, though HTIL, as the Group holding company of a set of companies, which controlled 42% plus 10% (pro rata) shares, did influence or was in a position to persuade the working of such Board of Directors of the Indian companies. In this connection, we need to have a relook at the ownership structure. It is not in dispute that 15% out of 67% stakes in HEL was held by AS, AG and IDFC companies. That was one of

the main reasons for entering into separate Shareholders and Framework Agreements in 2006, when Hutchison structure existed, with AS, AG and IDFC. HTIL was not a party to the agreements with AS and AG, though it was a party to the agreement with IDFC. That, the ownership structure of Hutchison clearly shows that AS, AG and SMMS (IDFC) group of companies, being Indian companies, possessed 15% control in HEL. Similarly, the term sheet with Essar dated 5.07.2003 gave Essar the RoFR and Right to Tag Along with HTIL and exit from HEL. Thus, if one keeps in mind the Hutchison structure in its entirety, HTIL as a Group holding company could have only persuaded its downstream companies to vote in a given manner as HTIL had no power nor authority under the said structure to direct any of its downstream companies to vote in a manner as directed by it (HTIL). Facts of this case show that both the parent and the subsidiary companies worked as a group since 1994. That, as a practice, the subsidiaries did comply with the arrangement suggested by the Group holding company in the matter of voting, failing which the smooth working of HEL generating huge revenues was not possible. In this case, we are concerned with the expression “capital asset” in the income tax law. Applying the test of enforceability, influence/ persuasion cannot be construed as a right in the legal sense. One more aspect needs to be highlighted. The concept of “de facto” control, which existed in the Hutchison structure, conveys a state of being in control without any legal right to such state. This aspect is important while construing the words “capital asset” under the income tax law. As stated earlier, enforceability is an important aspect of a legal right. Applying these tests, on the facts of this case and that too in the light of the ownership structure of Hutchison, we hold that HTIL, as a Group holding company, had no legal right to direct its downstream companies in the matter of voting, nomination of directors and management rights. As regards continuance of the 2006 Shareholders/Framework Agreements by SPA is concerned, one needs to keep in mind two relevant concepts, viz., participative and protective rights. As stated, this is a case of HTIL exercising its exit right under the holding structure and continuance of the telecom business operations in India by VIH by acquisition of shares. In the Hutchison structure, exit was also provided for Essar, Centrino, NDC and SMMS through exercise of Put Option/TARs, subject to sectoral cap being relaxed in future. These exit rights in Essar, Centrino, NDC and SMMS (IDFC) indicate that these companies were independent companies. Essar was a partner in HEL whereas Centrino, NDC and SMMS controlled 15% of shares of HEL (minority). *A minority investor has what is called as a "participative" right, which is a subset of "protective rights".* These participative rights, given to a minority shareholder, enable the minority to overcome the presumption of consolidation of operations or assets by the controlling shareholder. These participative rights in certain instances restrict the powers of the shareholder with majority voting interest to control the operations or assets of the investee. At the same time, even the minority is entitled to exit. This "exit right" comes under "protective rights". On examination of the Hutchison structure in its entirety, we find that both, participative and protective rights, were provided for in the Shareholders/ Framework Agreements of 2006 in favour of Centrino, NDC and SMMS which enabled them to participate, directly or indirectly, in the operations of HEL. Even without the execution of SPA, such rights existed in the above agreements. Therefore, it would not be correct to say that such rights flowed from the SPA. One more aspect needs to be mentioned. The Framework Agreements define "change of control with respect to a shareholder" inter alia as substitution of limited or unlimited liability company, whether directly or indirectly, to direct the policies/ management of the respective shareholders, viz., Centrino, NDC, Omega. Thus, even without the SPA, upon substitution of VIH in place of HTIL, on acquisition of CGP share, transition could have taken place. It is important to note that "transition" is a wide concept. It is impossible for the acquirer to visualize all events that may take place between the date of execution of the SPA and completion of acquisition.

Therefore, we have a provision for standstill in the SPA and so also the provision for transition. But, from that, it does not follow that without SPA, transition could not ensue. Therefore, in the SPA, we find provisions concerning Vendor's Obligations in relation to the conduct of business of HEL between the date of execution of SPA and the closing date, protection of investment during the said period, agreement not to amend, terminate, vary or waive any rights under the Framework/ Shareholders Agreements during the said period, provisions regarding running of business during the said period, assignment of loans, consequence of imposition of prohibition by way of injunction from any court, payment to be made by VIH to HTIL, giving of warranties by the Vendor, use of Hutch Brand, etc. The next point raised by the Revenue concerns termination of IDFC Framework Agreement of 2006 and its substitution by a fresh Framework Agreement dated 5.06.2007 in terms of the SPA. The submission of the Revenue before us was that the said Agreement dated 5.06.2007 (which is executed after the completion of acquisition by VIH on 8.05.2007) was necessary to assign the benefits of the earlier agreements of 2006 to VIH. This is not correct. The shareholders of ITNL (renamed as Omega) were Array through HTIL Mauritius and SMMS (an Indian company). The original investors through SMMS (IDFC), an infrastructure holding company, held 54.21% of the share capital of Omega; that, under the 2006 Framework Agreement, the original investors were given Put Option by GSPL [an Indian company under Hutchison Teleservices (India) Holdings Limited (Ms)] requiring GSPL to buy the equity share capital of SMMS; that on completion of acquisition on 8.05.2007 there was a change in control of HTIL Mauritius which held 45.79% in Omega and that changes also took place on 5.06.2007 within the group of original investors with the exit of IDFC and SSKI. In view of the said changes in the parties, a revised Framework Agreement was executed on 6.06.2007, which again had call and put option. Under the said Agreement dated 6.06.2007, the Investors once again agreed to grant call option to GSPL to buy the shares of SMMS and to enter into a

Shareholders Agreement to regulate the affairs of Omega. It is important to note that even in the fresh agreement the call option remained with GSPL and that the said Agreement did not confer any rights on VIH. One more aspect needs to be mentioned. The conferment of call options on GSPL under the Framework Agreements of 2006 also had a linkage with intra-group loans. CGP was an Investment vehicle. It is through the acquisition of CGP that VIH had indirectly acquired the rights and obligations of GSPL in the Centrino and NDC Framework Agreements of 2006 [see the report of KPMG dated 18.10.2010] and not through execution of the SPA. Lastly, as stated above, apart from providing for "standstill", an SPA has to provide for transition and all possible future eventualities. In the present case, the change in the investors, after completion of acquisition on 8.05.2007, under which SSKI and IDFC exited leaving behind IDF alone was a situation which was required to be addressed by execution of a fresh Framework Agreement under which the call option remained with GSPL. Therefore, the June, 2007 Agreements relied upon by the Revenue merely reiterated the rights of GSPL which rights existed even in the Hutchison structure as it stood in 2006. It was next contended that the 2003 Term Sheet with Essar was given effect to by clause 5.2 of the SPA which gave Essar the Right to Tag Along with HTIL and exit from HEL. That, the Term Sheet of 5.07.2003 had legal effect because by a specific settlement dated 15.03.2007 between HTIL and Essar, the said Term Sheet stood terminated which was necessary because the Term Sheet bound the parties in the first place. We find no merit in the above arguments of the Revenue. The 2003 Term Sheet was between HTIL, Essar and UMTL. Disputes arose between Essar and HTIL. Essar asserted RoFR rights when bids were received by HTIL, which dispute ultimately came to be settled on 15.03.2007, that is after the SPA dated 11.02.2007. The SPA did not create any rights. The RoFR/TARs existed in the Hutchison structure. Thus, even without SPA, within the Hutchison structure these rights existed. Moreover, the very object of the SPA is to cover the situations which may arise

during the transition and those which are capable of being anticipated and dealt with. Essar had 33% stakes in HEL. As stated, the Hutchison structure required the parent and the subsidiary to work together as a group. The said structure required the Indian partners to be kept in the loop. Disputes on existence of RoFR/ TARs had to be settled. They were settled on 15.03.2007. The rights and obligations created under the SPA had to be preserved. In any event, preservation of such rights with a view to continue business in India is not extinguishment.

77. For the above reasons, we hold that under the HTIL structure, as it existed in 1994, HTIL occupied only a persuasive position/influence over the downstream companies qua manner of voting, nomination of directors and management rights. That, the minority shareholders/investors had participative and protective rights (including RoFR/TARs, call and put options which provided for exit) which flowed from the CGP share. That, the entire investment was sold to the VIH through the investment vehicle (CGP). Consequently, there was no extinguishment of rights as alleged by the Revenue.

Role of CGP in the transaction

78. The main contention of the Revenue was that CGP stood inserted at a late stage in the transaction in order to bring in a tax-free entity (or to create a transaction to avoid tax) and thereby avoid capital gains. That, in December, 2006, HTIL explored the possibility of the sale of shares of the Mauritius entities and found that such transaction would be taxable as HTIL under that proposal had to be the prime mover behind any agreement with VIH – prime mover in the sense of being both a seller of shares and the recipient of the sale proceeds therefrom. Consequently, HTIL moved upwards in the Hutchison structure and devised an artificial tax avoidance scheme of selling the CGP share when in fact what HTIL wanted was to sell its property rights in HEL. This, according to the Revenue,

was the reason for the CGP share being interposed in the transaction. We find no merit in these arguments.

79. When a business gets big enough, it does two things. First, it reconfigures itself into a corporate group by dividing itself into a multitude of commonly owned subsidiaries. Second, it causes various entities in the said group to guarantee each other's debts. A typical large business corporation consists of sub-incorporates. Such division is legal. It is recognized by company law, laws of taxation, takeover codes etc. On top is a parent or a holding company. The parent is the public face of the business. The parent is the only group member that normally discloses financial results. Below the parent company are the subsidiaries which hold operational assets of the business and which often have their own subordinate entities that can extend layers. If large firms are not divided into subsidiaries, creditors would have to monitor the enterprise in its entirety. Subsidiaries reduce the amount of information that creditors need to gather. Subsidiaries also promote the benefits of specialization. Subsidiaries permit creditors to lend against only specified divisions of the firm. These are the efficiencies inbuilt in a holding structure. Subsidiaries are often created for tax or regulatory reasons. They at times come into existence from mergers and acquisitions. As group members, subsidiaries work together to make the same or complementary goods and services and hence they are subject to the same market supply and demand conditions. They are financially inter-linked. One such linkage is the intra-group loans and guarantees. Parent entities own equity stakes in their subsidiaries. Consequently, on many occasions, the parent suffers a loss whenever the rest of the group experiences a downturn. Such grouping is based on the principle of *internal correlation*. Courts have evolved doctrines like piercing the corporate veil, substance over form etc. enabling taxation of underlying assets in cases of fraud, sham, tax avoidant, etc. However, genuine strategic tax planning is not ruled out.

80. CGP was incorporated in 1998 in Cayman Islands. It was in the Hutchison structure from 1998. The transaction in the present case was of divestment and, therefore, the transaction of sale was structured at an appropriate tier, so that the buyer really acquired the same degree of control as was hitherto exercised by HTIL. VIH agreed to acquire companies and the companies it acquired controlled 67% interest in HEL. CGP was an investment vehicle. As stated above, it is through the acquisition of CGP that VIH proposed to indirectly acquire the rights and obligations of GSPL in the Centrino and NDC Framework Agreements. The report of Ernst & Young dated 11.02.2007 inter alia states that when they were asked to conduct due diligence by VIH, it was in relation to Array and its subsidiaries. The said report evidences that at the negotiation stage, parties had in mind the transfer of an upstream company rather than the transfer of HEL directly. The transfer of Array had the advantage of transferring control over the entire shareholding held by downstream Mauritius companies (tier I companies), other than GSPL. On the other hand, the advantage of transferring the CGP share enabled VIH to indirectly acquire the rights and obligations of GSPL (Indian company) in the Centrino and NDC Framework agreements. This was the reason for VIH to go by the CGP route. One of the arguments of the Revenue before us was that the Mauritius route was not available to HTIL for the reason indicated above. In this connection, it was urged that the legal owner of HEL (Indian company) was not HTIL. Under the transaction, HTIL alone was the seller of the shares. VIH wanted to enter into an agreement only with HTIL so that if something goes wrong, VIH could look solely to HTIL being the group holding company (parent company). Further, funds were pumped into HEL by HTIL. These funds were to be received back in the shape of a capital gain which could then be used to declare a special dividend to the shareholders of HTIL. We find no merit in this argument. Firstly, the tier I (Mauritius companies) were the indirect subsidiaries of HTIL who could have influenced the

former to sell the shares of Indian companies in which event the gains would have arisen to the Mauritius companies, who are not liable to pay capital gains tax under the Indo-Mauritius DTAA. That, nothing prevented the Mauritius companies from declaring dividend on gains made on the sale of shares. There is no tax on dividends in Mauritius. Thus, the Mauritius route was available but it was not opted for because that route would not have brought in the control over GSPL. Secondly, if the Mauritius companies had sold the shares of HEL, then the Mauritius companies would have continued to be the subsidiaries of HTIL, their accounts would have been consolidated in the hands of HTIL and HTIL would have accounted for the gains in exactly the same way as it has accounted for the gains in the hands of HTIHL (CI) which was the nominated payee. Thus, in our view, two routes were available, namely, the CGP route and the Mauritius route. It was open to the parties to opt for any one of the two routes. Thirdly, as stated above, in the present case, the SPA was entered into inter alia for a smooth transition of business on divestment by HTIL. As stated, transfer of the CGP share enabled VIH to indirectly acquire the rights and obligations of GSPL in the Centrino and NDC Framework Agreements. Apart from the said rights and obligations under the Framework Agreements, GSPL also had a call centre business. VIH intended to take over from HTIL the telecom business. It had no intention to acquire the business of call centre. Moreover, the FDI norms applicable to the telecom business in India were different and distinct from the FDI norms applicable to the call centre business. Consequently, in order to avoid legal and regulatory objections from Government of India, the call centre business stood hived off. In our view, this step was an integral part of transition of business under SPA.

81. On the role of CGP in the transaction, two documents are required to be referred to. One is the Report of the KPMG dated 18.10.2010 in which it is stated that through the acquisition of CGP, VIH had indirectly acquired the rights and

obligations of GSPL in the Centrino and NDC Framework Agreements. That, the said two agreements were put in place with a view to provide AG and AS with downside protection while preserving upside value in the growth of HEL. The second document is the Annual Report 2007 of HTIL. Under the caption "Overview", the Report observes that on 11.02.2007, HTIL entered into an agreement to sell its entire interests in CGP, a company which held through various subsidiaries, the direct and indirect equity and loan interests in HEL (renamed VEL) and its subsidiaries to VIH for a cash consideration of HK $86.6 bn. As a result of the said Transaction, the net debt of the Group which stood at HK $37,369 mn as on 31.12.2006 became a net cash balance of HK $25,591 mn as on 31.12.2007. This supports the fact that the sole purpose of CGP was not only to hold shares in subsidiary companies but also to enable a smooth transition of business, which is the basis of the SPA. Therefore, it cannot be said that the intervened entity (CGP) had no business or commercial purpose.

82. Before concluding, one more aspect needs to be addressed. It concerns situs of the CGP share. According to the Revenue, under the Companies Law of Cayman Islands, an exempted company was not entitled to conduct business in the Cayman Islands. CGP was an "exempted company". According to the Revenue, since CGP was a mere holding company and since it could not conduct business in Cayman Islands, the situs of the CGP share existed where the "underlying assets are situated", that is to say, India. That, since CGP as an exempted company conducts no business either in the Cayman Islands or elsewhere and since its sole purpose is to hold shares in a subsidiary company situated outside the Cayman Islands, the situs of the CGP share, in the present case, existed "where the underlying assets stood situated" (India). We find no merit in these arguments. At the outset, we do not wish to pronounce authoritatively on the Companies Law of Cayman Islands. Be that as it may, under the Indian Companies Act, 1956, the situs of the shares would be where

the company is incorporated and where its shares can be transferred. In the present case, it has been asserted by VIH that the transfer of the CGP share was recorded in the Cayman Islands, where the register of members of the CGP is maintained. This assertion has neither been rebutted in the impugned order of the Department dated 31.05.2010 nor traversed in the pleadings filed by the Revenue nor controverted before us. In the circumstances, we are not inclined to accept the arguments of the Revenue that the situs of the CGP share was situated in the place (India) where the underlying assets stood situated.

Did VIH acquire 67% controlling interest in HEL (and not 42%/ 52% as sought to be propounded)?

83. According to the Revenue, the entire case of VIH was that it had acquired only 42% (or, accounting for FIPB regulations, 52%) is belied by clause 5.2 of the Shareholders Agreement. In this connection, it was urged that 15% in HEL was held by AS/ AG/ IDFC because of the FDI cap of 74% and, consequently, vide clause 5.2 of the Shareholders Agreement between these entities and HTIL downstream subsidiaries, AS/ AG/IDFC were all reigned in by having to vote only in accordance with HTIL's dictates as HTIL had funded the purchase by these gentlemen of the HEL shares through financing of loans. Further, in the Term Sheet dated 15.03.2007, that is, between VIH and Essar, VIH had a right to nominate 8 directors (i.e. 67% of 12) and Essar had a right to nominate 4 directors which, according to the Revenue, evidences that VIH had acquired 67% interest in HEL and not 42%/52%, as sought to be propounded by it. According to the Revenue, right from 22.12.2006 onwards when HTIL made its first public announcement, HTIL on innumerable occasions represented its direct and indirect "equity interest" in HEL to be 67% - the direct interest being 42.34% and indirect interest in the sense of shareholding belonging to Indian partners under its control, as 25%. Further, according to the Revenue, the purchase price

paid by VIH was based on an enterprise value of 67% of the share capital of HEL; this would never have been so if VIH was to buy only 42.34% of the share capital of HEL and that nobody would pay US $2.5 bn extra without control over 25% in HEL. We find no merit in the above submissions. At the outset, it may be stated that *the expression "control" is a mixed question of law and fact.* The basic argument of the Revenue is based on the equation of "equity interest" with the word "control". On perusal of Hutchison structure, we find that HTIL had, through its 100% wholly owned subsidiaries, invested in 42.34% of HEL (i.e. direct interest). Similarly, HTIL had invested through its non-100% wholly owned subsidiaries in 9.62% of HEL (through the pro rata route). Thus, in the sense of shareholding, one can say that HTIL had an *effective shareholding* (direct and indirect interest) of 51.96% (approx. 52%) in HEL. On the basis of the shareholding test, HTIL could be said to have a 52% control over HEL. By the same test, it could be equally said that the balance 15% stakes in HEL remained with AS, AG and IDFC (Indian partners) who had through their respective group companies invested 15% in HEL through TII and Omega and, consequently, HTIL had no control over 15% stakes in HEL. At this stage, we may state that under the Hutchison structure shares of Plustech in the AG Group, shares of Scorpios in the AS Group and shares of SMMS came under the options held by GSPL. Pending exercise, options are not management rights. At the highest, options could be treated as potential shares and till exercised they cannot provide right to vote or management or control. In the present case, till date GSPL has not exercised its rights under the Framework Agreement 2006 because of the sectoral cap of 74% which in turn restricts the right to vote. Therefore, the transaction in the present case provides for a triggering event, viz. relaxation of the sectoral cap. Till such date, HTIL/VIH cannot be said to have a control over 15% stakes in HEL. It is for this reason that even FIPB gave its approval to the transaction by saying that VIH was acquiring or has acquired effective shareholding of 51.96% in HEL.

84. As regards the Term Sheet dated 15.03.2007, it may be stated that the said Term Sheet was entered into between VIH and Essar. It was executed after 11.02.2007 when SPA was executed. In the Term Sheet, it has been recited that the parties have agreed to enter into the Term Sheet in order to regulate the affairs of HEL and in order to regulate the relationship of shareholders of HEL. It is also stated in the Term Sheet that VIH and Essar shall have to nominate directors on the Board of Directors of HEL in proportion to the aggregate beneficial shareholding held by members of the respective groups. That, initially VIH shall be entitled to nominate 8 directors and Essar shall be entitled to nominate 4 directors out of a total Board of Directors of HEL (numbering 12). We must understand the background of this Term Sheet. Firstly, as stated the Term Sheet was entered into in order to regulate the affairs of HEL and to regulate the relationship of the shareholders of HEL. It was necessary to enter into such an agreement for smooth running of the business post acquisition. Secondly, we find from the letter addressed by HEL to FIPB dated 14.03.2007 that Articles of Association of HEL did not grant any specific person or entity a right to appoint directors. The said directors were appointed by the shareholders of HEL in accordance with the provisions of the Indian Company Law. The letter further states that *in practice* the directors were appointed pro rata to their respective shareholdings which resulted in 4 directors being appointed from Essar group, 6 directors being appointed by HTIL and 2 directors were appointed by TII. One such director was AS, the other director was AG. This was the practice even before the Term Sheet. The Term Sheet continues this practice by guaranteeing or assuring Essar that 4 directors would be appointed from its Group. The above facts indicate that the object of the SPA was to continue the “practice” concerning nomination of directors on the Board of Directors of HEL which in law is different from a right or power to control and manage and which practice was given to keep the business going, post acquisition. Under the Company Law, the management control vests in the Board of

Directors and not with the shareholders of the company. Therefore, neither from Clause 5.2 of the Shareholders Agreement nor from the Term Sheet dated 15.03.2007, one could say that VIH had acquired 67% controlling interest in HEL.

85. As regards the question as to why VIH should pay consideration to HTIL based on an enterprise value of 67% of the share capital of HEL is concerned, it is important to note that valuation cannot be the basis of taxation. The basis of taxation is profits or income or receipt. In this case, we are not concerned with tax on income/ profit arising from business operations but with tax on transfer of rights (capital asset) and gains arising therefrom. In the latter case, we have to see the conditions on which the tax becomes payable under the Income Tax Act. Valuation may be a science, not law. In valuation, to arrive at the value one has to take into consideration the business realities, like the business model, the duration of its operations, concepts such as cash flow, the discounting factors, assets and liabilities, intangibles, etc. In the present case, VIH paid US $11.08 bn for 67% of the enterprise value of HEL plus its downstream companies having operational licences. It bought an upstream company with the intention that rights flowing from the CGP share would enable it to gain control over the cluster of Indian operations or operating companies which owned telecom licences, business assets, etc. VIH agreed to acquire companies which in turn controlled a 67% interest in HEL and its subsidiaries. Valuation is a matter of opinion. When the entire business or investment is sold, for valuation purposes, one may take into account the economic interest or realities. Risks as a discounting factor are also to be taken into consideration apart from loans, receivables, options, RoFR/ TAR, etc. In this case, Enterprise Value is made up of two parts, namely, the value of HEL, the value of CGP and the companies between CGP and HEL. In the present case, the Revenue cannot invoke Section 9 of the Income Tax Act on the value of the underlying asset or consequence of acquiring a share of CGP. In the present case, the Valuation done was on the basis

of enterprise value. The price paid as a percentage of the enterprise value had to be 67% not because the figure of 67% was available in praesenti to VIH, but on account of the fact that the competing Indian bidders would have had de facto access to the entire 67%, as they were not subject to the limitation of sectoral cap, and, therefore, would have immediately encashed the call options. The question still remains as to from where did this figure/ expression of 67% of equity interest come? The expression "equity interest" came from US GAAP. In this connection, we have examined the Notes to the Accounts annexed to the Annual Report 2006 of HTIL. According to Note 1, the ordinary shares of HTIL stood listed on the Hong Kong Stock Exchange as well as on the New York Stock Exchange. In Note No. 36, a list of principal subsidiaries of HTIL as on 31.12.2006 has been attached. This list shows the names of HEL (India) and some of its subsidiaries. In the said Annual Report, there is an annexure to the said Notes to the Accounts under the caption "Information for US Investors". It refers to Variable Interest Entities (VIEs). According to the Annual Report, the Vodafone Group consisting of HTIL and its subsidiaries conducted its operations inter alia in India through entities in which HTIL did not have the voting control. Since HTIL was listed on New York Stock Exchange, it had to follow for accounting and disclosure the rules prescribed by US GAAP. Now, in the present case, HTIL as a listed company was required to make disclosures of potential risk involved in the investment under the Hutchison structure. HTIL had furnished Letters of Credit to Rabo Bank which in turn had funded AS and AG, who in turn had agreed to place the shares of Plustech and Scorpios under Options held by GSPL. Thus, giving of the Letters of Credit and placing the shares of Plustech and Scorpios under Options were required to be disclosed to the US investors under the US GAAP, unlike Indian GAAP. Thus, the difference between the 52% figure (control) and 67% (equity interest) arose on account of the difference in computation under the Indian and US GAAP.

Approach of the High Court (acquisition of CGP share with "other rights and entitlements")

86. Applying the "nature and character of the transaction" test, the High Court came to the conclusion that the transfer of the CGP share was not adequate in itself to achieve the object of consummating the transaction between HTIL and VIH. That, intrinsic to the transaction was a transfer of other *"rights and entitlements"* which rights and entitlements constituted in themselves "capital assets" within the meaning of Section 2(14) of the Income Tax Act, 1961. According to the High Court, VIH acquired the CGP share with other rights and entitlements whereas, according to the appellant, whatever VIH obtained was through the CGP share (*for short "High Court Approach"*).

87. At the outset, it needs to be mentioned that the Revenue has adopted the abovementioned *High Court Approach* as an alternative contention.

88. We have to view the subject matter of the transaction, in this case, from a commercial and realistic perspective. The present case concerns an offshore transaction involving a structured investment. This case concerns *"a share sale" and not an asset sale*. It concerns sale of an entire investment. A "sale" may take various forms. Accordingly, tax consequences will vary. The tax consequences of a *share sale* would be different from the tax consequences of an *asset sale*. A slump sale would involve tax consequences which could be different from the tax consequences of sale of assets on itemized basis. "Control" is a mixed question of law and fact. Ownership of shares may, in certain situations, result in the assumption of an interest which has the character of a *controlling interest* in the management of the company. A controlling interest is an incident of ownership of shares in a company, something which flows out of the holding of shares. A controlling interest is, therefore, not an identifiable or distinct capital asset independent of the holding of shares. The control of a company resides in the voting power of its shareholders and shares

represent an interest of a shareholder which is made up of various rights contained in the contract embedded in the Articles of Association. The right of a shareholder may assume the character of a controlling interest where the extent of the shareholding enables the shareholder to control the management. Shares, and the rights which emanate from them, flow together and cannot be dissected. In the felicitous phrase of Lord MacMillan in *IRC v. Crossman* [1936] 1 All ER 762, shares in a company consist of a "congeries of rights and liabilities" which are a creature of the Companies Acts and the Memorandum and Articles of Association of the company. Thus, control and management is a facet of the holding of shares. Applying the above principles governing shares and the rights of the shareholders to the facts of this case, we find that this case concerns a straightforward *share sale*. VIH acquired Upstream shares with the intention that the congeries of rights, flowing from the CGP share, would give VIH an indirect control over the three genres of companies. If one looks at the chart indicating the Ownership Structure, one finds that the acquisition of the CGP share gave VIH an indirect control over the tier I Mauritius companies which owned shares in HEL totalling to 42.34%; CGP India (Ms), which in turn held shares in TII and Omega and which on a pro rata basis (the FDI principle), totalled up to 9.62% in HEL and an indirect control over Hutchison Tele-Services (India) Holdings Ltd. (Ms), which in turn owned shares in GSPL, which held call and put options. Although the High Court has analysed the transactional documents in detail, it has missed out this aspect of the case. It has failed to notice that till date options have remained *un-encashed* with GSPL. Therefore, even if it be assumed that the options under the Framework Agreements 2006 could be considered to be property rights, there has been no transfer or assignment of options by GSPL till today. Even if it be assumed that the High Court was right in holding that the options constituted capital assets even then Section 9(1)(i) was not applicable as these options have not been transferred till date. Call and put options were not transferred vide SPA dated

11.02.2007 or under any other document whatsoever. Moreover, if, on principle, the High Court accepts that the transfer of the CGP share did not lead to the transfer of a capital asset in India, even if it resulted in a transfer of indirect control over 42.34% (52%) of shares in HEL, then surely the transfer of indirect control over GSPL which held options (contractual rights), would not make the transfer of the CGP share taxable in India. Acquisition of the CGP share which gave VIH an indirect control over three genres of companies evidences a straightforward *share sale* and not an *asset sale*. There is another fallacy in the impugned judgment. On examination of the impugned judgment, we find a serious error committed by the High Court in appreciating the case of VIH before FIPB. On 19.03.2007, FIPB sought a clarification from VIH of the circumstances in which VIH agreed to pay US$ 11.08 bn for acquiring 67% of HEL when actual acquisition was of 51.96%. In its response dated 19.03.2007, VIH stated that it had agreed to acquire from HTIL for US$ 11.08 bn, interest in HEL which included a 52% equity shareholding. According to VIH, the price also included a control premium, use of Hutch brand in India, a non-compete agreement, loan obligations and an entitlement to acquire, subject to the Indian FDI rules, a further 15% indirect interest in HEL. According to the said letter, the above elements together equated to 67% of the economic value of HEL. This sentence has been misconstrued by the High Court to say that the above elements equated to 67% of the equity capital (See para 124). 67% of the economic value of HEL is not 67% of the equity capital. If VIH would have acquired 67% of the equity capital, as held by the High Court, the entire investment would have had breached the FDI norms which had imposed a sectoral cap of 74%. In this connection, it may further be stated that Essar had 33% stakes in HEL out of which 22% was held by Essar Mauritius. Thus, VIH did not acquire 67% of the equity capital of HEL, as held by the High Court. This problem has arisen also because of the reason that this case deals with *share sale* and not *asset sale*. This case does not involve sale of assets on itemized basis. The High Court ought to have applied the *look at* test in which the entire Hutchison structure, as it existed, ought to have been looked at holistically. This case concerns investment into India by a holding company (parent company), HTIL through a maze of subsidiaries. When one applies the "nature and character of the transaction test", confusion arises if a dissecting approach of examining each individual asset is adopted. As stated, CGP was treated in the Hutchison structure as an investment vehicle. As a general rule, in a case where a transaction involves transfer of shares lock, stock and barrel, such a transaction cannot be broken up into separate individual components, assets or rights such as right to vote, right to participate in company meetings, management rights, controlling rights, control premium, brand licences and so on as shares constitute a bundle of rights. [See *Charanjit Lal v. Union of India* AIR 1951 SC 41, *Venkatesh (minor) v. CIT* 243 ITR 367 (Mad) and *Smt. Maharani Ushadevi v. CIT* 131 ITR 445 (MP)] Further, the High Court has failed to examine the nature of the following items, namely, non-compete agreement, control premium, call and put options, consultancy support, customer base, brand licences etc. On facts, we are of the view that the High Court, in the present case, ought to have examined the entire transaction holistically. VIH has rightly contended that the transaction in question should be looked at as an entire package. The items mentioned hereinabove, like, control premium, non-compete agreement, consultancy support, customer base, brand licences, operating licences etc. were all an integral part of the Holding Subsidiary Structure which existed for almost 13 years, generating huge revenues, as indicated above. Merely because at the time of exit capital gains tax becomes not payable or exigible to tax would not make the entire *"share sale"* (investment) a sham or a tax avoidant. The High Court has failed to appreciate that the payment of US$ 11.08 bn was for purchase of the entire investment made by HTIL in India. The payment was for the entire package. The parties to the transaction have not agreed upon a separate price for the CGP share and for what the High Court calls as "other rights and entitlements" (including options, right to non-

compete, control premium, customer base etc.). Thus, it was not open to the Revenue to split the payment and consider a part of such payments for each of the above items. The essential character of the transaction as an alienation cannot be altered by the form of the consideration, the payment of the consideration in instalments or on the basis that the payment is related to a contingency ('options', in this case), particularly when the transaction does not contemplate such a split up. Where the parties have agreed for a lump sum consideration without placing separate values for each of the above items which go to make up the entire *investment in participation*, merely because certain values are indicated in the correspondence with FIPB which had raised the query, would not mean that the parties had agreed for the price payable for each of the above items. The transaction remained a contract of outright sale of the entire investment for a lump sum consideration [see: Commentary on Model Tax Convention on Income and Capital dated 28.01.2003 as also the judgment of this Court in the case of *CIT (Central), Calcutta v. Mugneeram Bangur and Company (Land Deptt.),* (1965) 57 ITR 299 (SC)]. Thus, we need to *"look at"* the entire Ownership Structure set up by Hutchison as a *single consolidated bargain* and interpret the transactional documents, while examining the Offshore Transaction of the nature involved in this case, in that light.

Scope and applicability of Sections 195 and 163 of IT Act

89. Section 195 casts an obligation on the payer to deduct tax at source ("TAS" for short) from payments made to non-residents which payments are chargeable to tax. Such payment(s) must have an element of income embedded in it which is chargeable to tax in India. If the sum paid or credited by the payer is not chargeable to tax then no obligation to deduct the tax would arise. Shareholding in companies incorporated outside India (CGP) is property located outside India. Where such shares become subject matter of offshore transfer between two non-residents, there is no liability for

capital gains tax. In such a case, question of deduction of TAS would not arise. If in law the responsibility for payment is on a non-resident, the fact that the payment was made, under the instructions of the non-resident, to its Agent/Nominee in India or its PE/Branch Office will not absolve the payer of his liability under Section 195 to deduct TAS. Section 195(1) casts a duty upon the payer of any income specified therein to a non-resident to deduct therefrom the TAS unless such payer is himself liable to pay income-tax thereon as an Agent of the payee. Section 201 says that if such person fails to so deduct TAS he shall be deemed to be an assessee-in-default in respect of the deductible amount of tax (Section 201). Liability to deduct tax is different from "assessment" under the Act. Thus, the person on whom the obligation to deduct TAS is cast is not the person who has earned the income. Assessment has to be done after liability to deduct TAS has arisen. The object of Section 195 is to ensure that tax due from non-resident persons is secured at the earliest point of time so that there is no difficulty in collection of tax subsequently at the time of regular assessment. The present case concerns the transaction of "outright sale" between two non-residents of a capital asset (share) outside India. Further, the said transaction was entered into on principal to principal basis. Therefore, no liability to deduct TAS arose. Further, in the case of transfer of the Structure in its entirety, one has to look at it holistically as one *Single Consolidated Bargain* which took place between two foreign companies outside India for which a lump sum price was paid of US$ 11.08 bn. Under the transaction, there was no split up of payment of US$ 11.08 bn. It is the Revenue which has split the consolidated payment and it is the Revenue which wants to assign a value to the rights to control premium, right to non-compete, right to consultancy support etc. For FDI purposes, the FIPB had asked VIH for the basis of fixing the price of US$ 11.08 bn. But here also, there was no split up of lump sum payment, asset-wise as claimed by the Revenue. There was no assignment of price for each right, considered by the Revenue to be a "capital asset" in the transaction. In the absence of PE, profits were not

attributable to Indian operations. Moreover, *tax presence* has to be viewed in the context of the transaction that is subjected to tax and not with reference to an entirely unrelated matter. The investment made by Vodafone Group companies in Bharti did not make all entities of that Group subject to the Indian Income Tax Act, 1961 and the jurisdiction of the tax authorities. *Tax presence* must be construed in the context, and in a manner that brings the non-resident assessee under the jurisdiction of the Indian tax authorities. Lastly, in the present case, the Revenue has failed to establish any connection with Section 9(1)(i). Under the circumstances, Section 195 is not applicable. Alternatively, the Revenue contended before us that VIH can be proceeded against as *"representative assessee"* under Section 163 of the Act. Section 163 does not relate to deduction of tax. It relates to treatment of a purchaser of an asset as a *representative assessee*. A conjoint reading of Section 160(1)(i), Section 161(1) and Section 163 of the Act shows that, under given circumstances, certain persons can be treated as *"representative assessee"* on behalf of non-resident specified in Section 9(1). This would include an *agent* of non-resident and also who is treated as an *agent* under Section 163 of the Act which in turn deals with special cases where a person can be regarded as an agent. Once a person comes within any of the clauses of Section 163(1), such a person would be the *"Agent"* of the non-resident for the purposes of the Act. However, merely because a person is an agent or is to be treated as an agent, would not lead to an automatic conclusion that he becomes liable to pay taxes on behalf of the non-resident. It would only mean that he is to be treated as a "representative assessee". Section 161 of the Act makes a "representative assessee" liable only "as regards the income in respect of which he is a representative assessee" (See: Section 161). Section 161 of the Act makes a representative assessee liable only if the eventualities stipulated in Section 161 are satisfied. This is the scope of Sections 9(1)(i), 160(1), 161(1) read with Sections 163(1) (a) to (d). In the present case, the Department has invoked Section 163(1)(c). Both Sections

163(1)(c) and Section 9(1)(i) state that income should be deemed to accrue or arise in India. Both these Sections have to be read together. On facts of this case, we hold that Section 163(1)(c) is not attracted as there is no transfer of a capital asset situated in India. Thus, Section 163(1)(c) is not attracted. Consequently, VIH cannot be proceeded against even under Section 163 of the Act as a representative assessee. For the reasons given above, there is no necessity of examining the written submissions advanced on behalf of VIH by Dr. Abhishek Manu Singhvi on Sections 191 and 201.

Summary of Findings

90. Applying the *look at* test in order to ascertain the true nature and character of the transaction, we hold, that the Offshore Transaction herein is a bonafide structured FDI investment into India which fell outside India's territorial tax jurisdiction, hence not taxable. The said Offshore Transaction evidences participative investment and not a sham or tax avoidant preordained transaction. The said Offshore Transaction was between HTIL (a Cayman Islands company) and VIH (a company incorporated in Netherlands). The subject matter of the Transaction was the transfer of the CGP (a company incorporated in Cayman Islands). Consequently, the Indian Tax Authority had no territorial tax jurisdiction to tax the said Offshore Transaction.

Conclusion

91. FDI flows towards location with a strong governance infrastructure which includes enactment of laws and how well the legal system works. Certainty is integral to rule of law. Certainty and stability form the basic foundation of any fiscal system. Tax policy certainty is crucial for taxpayers (including foreign investors) to make rational economic choices in the most efficient manner. Legal doctrines like *"Limitation of Benefits"* and *"look through"* are matters of policy. It is for the Government of the day to have them incorporated in the

Treaties and in the laws so as to avoid conflicting views. Investors should know where they stand. It also helps the tax administration in enforcing the provisions of the taxing laws. As stated above, the Hutchison structure has existed since 1994. According to the details submitted on behalf of the appellant, we find that from 2002-03 to 2010-11 the Group has contributed an amount of Rs. 20,242 crores towards direct and indirect taxes on its business operations in India.

Order

92. For the above reasons, we set aside the impugned judgment of the Bombay High Court dated 8.09.2010 in Writ Petition No. 1325 of 2010. Accordingly, the Civil Appeal stands allowed with no order as to costs. The Department is hereby directed to return the sum of Rs. 2,500 crores, which came to be deposited by the appellant in terms of our interim order, with interest at the rate of 4% per annum within two months from today. The interest shall be calculated from the date of withdrawal by the Department from the Registry of the Supreme Court up to the date of payment. The Registry is directed to return the Bank Guarantee given by the appellant within four weeks.

K.S. RADHAKRISHNAN, J. 1. The question involved in this case is of considerable public importance, especially on Foreign Direct Investment (FDI), which is indispensable for a growing economy like India. Foreign investments in India are generally routed through Offshore Finance Centres (OFC) also through the countries with whom India has entered into treaties. Overseas investments in Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS) have been recognised as important avenues of global business in India. Potential users of off-shore finance are: international companies, individuals, investors and others and capital flows through FDI, Portfolio Debt Investment and Foreign Portfolio Equity Investment and so on. Demand for off-shore facilities has considerably increased owing to high growth rates of cross-border investments and a number of rich global investors have come forward to use high technology and communication infrastructures. Removal of barriers to cross-border trade, the liberalisation of financial markets and new communication technologies have had positive effects on global economic growth and India has also been greatly benefited.

2. Several international organisations like UN, FATF, OECD, Council of Europe and the European Union offer finance, one way or the other, for setting up companies all over the world. Many countries have entered into treaties with several offshore companies for cross-border investments for mutual benefits. India has also entered into treaties with several countries for bilateral trade which has been statutorily recognised in this country. United Nations Conference on Trade and Development (UNCTAD) Report on World Investment prospects survey 2009-11 states that India would continue to remain among the top five attractive destinations for foreign investors during the next two years.

3. Merger, Amalgamation, Acquisition, Joint Venture, Takeovers and Slump-sale of assets are few methods of cross-border re-organisations. Under the FDI Scheme, investment can be made by availing the benefit of treaties, or through tax havens by non-residents in the share/convertible debentures/preference shares of an Indian company but the question which looms large is whether our Company Law, Tax Laws and Regulatory Laws have been updated so that there can be greater scrutiny of non-resident enterprises, ranging from foreign contractors and service providers, to finance investors. Case in hand is an eye-opener of what we lack in our regulatory laws and what measures we have to take to meet the various unprecedented situations, that too without sacrificing national interest. Certainty in law in dealing with such cross-border investment issues is of prime importance, which has been felt by many countries around the world and some have taken

adequate regulatory measures so that investors can arrange their affairs fruitfully and effectively. Steps taken by various countries to meet such situations may also guide us, a brief reference of which is being made in the later part of this judgment.

4. We are, in the present case, concerned with a matter relating to cross-border investment and the legal issues emanate from that. Facts have been elaborately dealt with by the High Court in the impugned judgment and also in the leading judgment of Lord Chief Justice, but reference to few facts is necessary to address and answer the core issues raised. On all major issues, I fully concur with the views expressed by the Lord Chief Justice in his erudite and scholarly judgment.

5. Part-I of this judgment deals with the facts, Part-II deals with the general principles, Part-III deals with Indo-Mauritian Treaty, judgments in *Union of India v. Azadi Bachao Andolan and Another* (2004) 10 SCC 1 and *McDowell and Company Limited v. Commercial Tax Officer* (1985) 3 SCC 230, Part-IV deals with CGP Interposition, situs etc, Part-V deals with controlling interest of HTIL/Vodafone and other rights and entitlements, Part-VI deals with the scope of Section 9, Part-VII deals with Section 195 and other allied provisions and Part-VIII is the conclusions.

Part – I

6. Hutchison Whampoa is a multi-sectional, multi-jurisdictional entity which consolidates on a group basis telecom operations in various countries. Hutchison Group of Companies (Hong Kong) had acquired interest in the Indian telecom business in the year 1992, when the group invested in Hutchison Max Telecom Limited (HTML) (later known a Hutchison Essar Limited (HEL), which acquired a cellular license in Mumbai circle in the year 1994 and commenced its operation in the year 1995. Hutchison Group, with the

commercial purpose of consolidating its interest in various countries, incorporated CGP Investments Holding Limited (for short “CGP”) in Cayman Islands as a WOS on 12.01.1998 as an Exempted Company for offshore investments. CGP held shares in two subsidiary companies, namely Array Holdings Limited (for short Array) and Hutchison Teleservices (India) Holding Ltd. [for short HTIH(M)] both incorporated in Mauritius. CGP(India) Investment (for short CGPM) was incorporated in Mauritius in December 1997 for the purpose of investing in Telecom Investment (India) Pvt. Limited (for short TII), an Indian Company. CGPM acquired interests in four Mauritian Companies and entered into a Shareholders’ Agreement (SHA) on 02.05.2000 with Essar Teleholdings Limited (ETH), CGPM, Mobilvest, CCII (Mauritius) Inc. and few others, to regulate shareholders’ right inter se. Agreement highlighted the share holding pattern of each composition of Board of Directors, quorum, restriction on transfer of ownership of shares, Right of First Refusal (ROFR), Tag Along Rights (TARs) etc.

7. HTIL, a part of Hutchison Whampoa Group, incorporated in Cayman Islands in the year 2004 was listed in Hong Kong (HK) and New York (NY) Stock Exchanges. In the year 2005, as contemplated in the Term Sheet Agreement dated 05.07.2003, HTIL consolidated its Indian business operations through six companies in a single holding company HMTL, later renamed as Hutchison Essar Ltd. (HEL). On 03.11.2005, Press Note 5 of 2005 series was issued by the Government of India enhancing the FDI ceiling from 49% to 74% in the Telecom Sector. On 28.10.2005, Vodafone International Holding BV (VIHBV) (Netherlands) had agreed to acquire 5.61% of shareholding in Bharati Tele Ventures Limited (Bharati Airtel Limited) and on the same day Vodafone Mauritius Limited (Subsidiary of VIHBV) had agreed to acquire 4.39% shareholding in Bharati Enterprises Pvt. Ltd. (renamed Bharati Infotel Ltd.), which indirectly held shares in Bharati Airtel Ltd.

8. HEL shareholding was then restructured through TII and an SHA was executed on 01.03.2006 between Centrino Trading Company Pvt. Ltd. (Centrino), an Asim Ghosh (Group) [for short (AG)], ND Callus Info Services Pvt. Ltd. (for short NDC), an Analjit Singh (Group) [for short (AS)], Telecom Investment India Pvt.Ltd. [for short (TII)], and CGP India (M). Further, two Framework Agreements (FWAs) were also entered into with respect to the restructuring. *Credit facilities were given to the companies controlled by AG and AS*. FWAs called, Centrino FWA and N.D. FWA were executed on 01.03.2006. HTIL stood as a guarantor for Centrino, for an amount of ‘ 4,898 billion advanced by Rabo Bank. HTIL had also stood as a guarantor for ND Callus, for an award of ‘ 7.924 billion advanced by Rabo Bank.

9. Following the credit support given by HTIL to AG and AS so as to enable them to acquire shares in TII, parties entered into separate agreements with 3 Global Services Pvt. Ltd. (India) [for short 3GSPL], a WOS of HTIL. FWAs also contained *call option* in favour of 3GSPL, a right to purchase from Gold Spot (an AG company) and Scorpios (an AS company) their entire shareholding in TII held through Plustech (an AG company) and MVH (an AS company) respectively. *Subscription right* was also provided allowing 3GSPL a right to subscribe 97.5% and 97% of the equity share capital respectively at a pre-determined rate equal to the face value of the shares of Centrino and NDC respectively exercisable within a period of 10 years from the date of the agreements. Agreements also restricted AG companies and AS companies from transferring any downstream interests leading to the shareholding in TII.

10. HEL shareholding again underwent change with Hinduja Group exiting and its shareholding being acquired by an Indian company called SMMS Investments Private Limited (SMMS). SMMS was also a joint venture company formed by India Development Fund (IDF) acting through IDFC Private

Equity Company (IDFCPE), Infrastructure Development Finance Company Limited (IDFC) and SSKI Corporate Finance Pvt. Ltd. (SSKI) all the three companies were incorporated in India. Pursuant thereto, a FWA was entered into on 07.08.2006 between IDF (through IDFCPE), IDFC, SSKI, SMMS, HTIL (M), 3GSPL, Indus Ind Telecom Holding Pvt. Ltd. (ITNL) (later named as Omega Telecom Holding Pvt. Ltd. (Omega) and HTIL. 3GSPL, by that Agreement, had a *call option* and a right to purchase the entire equity shares of SMMS at a pre-determined price equal to ‘ 661,250,000 plus 15% compound interest. A SHA was also entered into on 17.08.2006 by SMMS, HTIL (M), HTIL(CI) and ITNL to regulate affairs of ITNL. Agreement referred to the presence of at least one of the directors nominated by HTIL in the Board of Directors of Omega. HTIL was only a *confirming party* to this Agreement since it was the parent company.

11. HTIL issued a press release on 22.12.2006 in the HK and NY Stock Exchanges announcing that it had been approached by various potentially interested parties regarding a possible sale of *"its equity interest" in HEL* in the Telecom Sector in India. HTIL had adopted those measures *after procuring all assignments of loans, facilitating FWAs, SHAs, transferring Hutch Branch, transferring Oracle License etc*.

12. Vodafone Group Plc. came to know of the possible exit of Hutch from Indian telecom business and on behalf of Vodafone Group made a non-binding offer on 22.12.06, for a sum of US$ 11.055 million in cash for HTIL's shareholdings in HEL. The offer was valued at an *"enterprise value"* of US$ 16.5 billion. Vodafone then appointed on 02.01.2007 Ernst and Young LLP to conduct due diligence, and a Non-Disclosure (Confidentiality) Agreement dated 02.01.2007 was entered into between HTIL and Vodafone. On 09.02.2007 Vodafone Group Plc. wrote a letter to HTIL making a "revised and binding offer" on behalf of a member of Vodafone Group (Vodafone) for HTIL's shareholdings in HEL together with interrelated company

loans. Bharati Infotel Pvt. Limited on 09.02.2007 expressed its 'no objection' to the Chairman, Vodafone Mauritius Limited regarding proposed acquisition by Vodafone group of direct and / indirect interest in HEL from Hutchison or Essar group. Bharati Airtel also sent a similar letter to Vodafone.

13. Vodafone Group Plc. on 10.02.2007 made a final binding offer of US$ 11.076 billion "in cash over HTIL's interest", based on an *enterprise value* of US$ 18.800 billion of HEL. Ernst and Young LLP, U.K. on 11.02.2007 issued due diligence report in relation to operating companies in India namely HEL and subsidiaries and also the Mauritian and Cayman Island Companies. Report noticed that CGP(CI) *was not within the target group* and was later included at the instance of HTIL. On 11.02.2007, UBS Limited, U.K. issued fairness opinion in relation to the transaction for acquisition by Vodafone from *HTIL of a 67% effective interest in HEL* through the acquisition of 100% interest in CGP and granting an option by Vodafone to Indian Continent Investment Ltd. over a 5.6% stake in Bharati Airtel Limited. Bharati Infotel and Bharati Airtel conveyed their no-objection to the Vodafone purchasing direct or indirect interest in HEL.

14. Vodafone and HTIL then entered into a Share and Purchase Agreement (SPA) on 11.02.2007 whereunder HTIL had agreed *to procure the transfer of share capital of CGP by HTIBVI, free from all encumbrances and together with all rights attaching or accruing together with assignments of loan interest*. HTIL on 11.02.2007 issued a side letter to Vodafone inter alia stating that, out of the purchase consideration, up to US$80 million could be paid to some of its Indian Partners. HTIL had also undertaken that Hutchison Telecommunication (India) Ltd. (HTM), Omega and 3GSPL, would enter into an agreed form "IDFC Transaction Agreement" as soon as practicable. On 11.02.2007, HTIL also sent a disclosure letter to Vodafone in terms of Clause 9.4 of SPA – Vendor warranties relating to consents and approvals, wider group companies,

material contracts, permits, litigation, arbitration and governmental proceedings to limit HTIL liability.

15. Vodafone on 12.02.2007 made a public announcement to the Securities and Exchange Commission, Washington (SEC), London Stock Exchange and HK Stock Exchange stating that *it had agreed to acquire a Controlling Interest in HEL for a cash consideration of US$ 11.1 billion*. HTIL Chairman sent a letter to the Vice-Chairman of Essar Group on 14.02.2007 along with a copy of Press announcement made by HTIL, setting out the principal terms of the *intended sale of HTIL of its equity and loans in HEL, by way of sale of CGP share and loan assignment to VIHBV*.

16. Vodafone on 20.02.2007 filed an application with Foreign Investment Promotion Board (FIPB) requesting it to take note of and grant approval under Press note no.1 *to the indirect acquisition by Vodafone of 51.96% stake in HEL through an overseas acquisition of the entire share capital of CGP from HTIL*. HTIL made an announcement on HK Stock Exchange regarding the intended use of proceeds from sale of HTIL's interest in HEL viz., declaring a special dividend of HK$ 6.75 per share, HK$ 13.9 billion to reduce debt and the remainder to be invested in telecommunication business, both for expansion and towards working capital and general policies. Reference was also made to the sale share and sale loans as being the entire issued share capital of CGP and the loans owned by CGP/Array to an indirect WOS. AG on 02.03.2007 sent a letter to HEL confirming that he was the *exclusive beneficial owner of his shares and was having full control over related voting rights. Further, it was also stated that AG had received credit support, but primary liability was with his Companies. AS also sent a letter on 05.03.2007 to FIPB confirming that he was the exclusive beneficial owner of his shares and also of the credit support received*.

17. Essar had filed objections with the FIPB on 06.03.2007

to HTIL's proposed sale and on 14.03.2007, Essar withdrew its objections.

18. FIPB on 14.03.2007 sent a letter to HEL pointing out that in filing of HTIL before the U.S. SEC in Form 6K in the month of March 2006, it had been stated that HTIL Group would continue *to hold an aggregate interest of 42.34% of HEL* and an additional indirect interest through JV companies being non-wholly owned subsidiaries of HTIL which hold an aggregate of 19.54% of HEL and, hence, the combined holding of HTIL Group would then be 61.88%. Reference was also made to the communication dated 06.03.2007 sent to the FIPB wherein it was stated *that the direct and indirect FDI by HTIL would be 51.96%* and, hence, was asked to clarify that discrepancy. Similar letter dated 14.03.2007 was also received by Vodafone. On 14.03.2007, HEL wrote to FIPB stating that the discrepancy was because of the difference in U.S. GAAP and Indian GAAP declarations and that the combined holding for U.S. GAAP purposes was 61.88% and for Indian GAAP purposes was 51.98%. *It was pointed out that Indian GAAP number accurately reflected the true equity ownership and control position*. On 14.03.2007 itself, HEL wrote to FIPB confirming that *7.577% stake in HEL was held legally and beneficially by AS and his wife and 4.78% stake in HEL was held legally and beneficially by AG*. Further, it was also pointed out that *2.77% stake in HEL through Omega and S.M.M.S. was legally and beneficially owned by IDFC Limited*, IDFC Private Equity Limited and SSKI Corporate Finance Limited. Further, it was also pointed out that Articles of Association of HEL did not give any person or entity any right to appoint directors, however, in practice six directors were from HTIL, four from Essar, two from TII and TII had appointed AG & AS. On credit support agreement, it was pointed out that no permission of any regulatory authority was required.

19. Vodafone also wrote to FIPB on 14.03.2007 confirming that *VIHBV's effective shareholding in HEL would*

be 51.96% i.e. Vodafone would own 42% direct interest in HEL through its acquisition of 100% of CGP Investments (Holdings) Limited (CGPIL) and through CGPIL Vodafone would also own 37% in TII which in turn owned 20% in HEL and 38% in Omega which in turn owned 5% in HEL. It was pointed out that both TII and Omega were Indian companies and those investments combined would give Vodafone a *controlling interest of 52% in HEL. Further, it was pointed out that HTIL's Indian partners AG, AS, IDFC who between them held a 15% interest in HEL on aggregate had agreed to retain their shareholding with full control including voting rights and dividend rights*.

20. HTIL, Essar Teleholding Limited (ETL), Essar Communication Limited (ECL), Essar Tele Investments Limited (ETIL), Essar Communications (India) Limited (ECIL) signed a settlement agreement on 15.03.2007 regarding Essar Group's support for completion of the proposed transaction and covenant not to sue any Hutchison Group Company etc., in lieu of payment by HTIL of US$ 373.5 million after completion and a further US$ 41.5 million after second anniversary of completion. In that agreement, HTIL had agreed to dispose of its direct and indirect equity, loan and other interests and rights in and related to HEL, to Vodafone pursuant to the SPA. HTIL had also agreed to pay US$ 415 million to Essar in return of its acceptance of the SPA between HTIL and Vodafone. On 15.03.2007 a Deed of Waiver was entered into between Vodafone and HTIL, whereby Vodafone had waived some of the warranties set out in paragraphs 7.1(a) and 7.1(b) of Schedule 4 of the SPA and covenanted that till payment of HTIL under Clause 6.1(a) of the Settlement Agreement of 30.05.2007, Vodafone should not bring any claim or action. On 15.03.2007 a circular was issued by HTIL including the report of Somerley Limited on the Settlement Agreement between HTIL and Essar Group.

21. VIHBVI, Essar Tele Holdings Limited (ETH) and ECL entered into a Term Sheet Agreement on 15.03.2007 for

regulating the affairs of HEL and the relationship of its shareholders including setting out VIHBVI's right as a shareholder of HEL to nominate eight persons out of twelve to the board of directors, requiring Vodafone to nominate director to constitute a quorum for board meetings and get ROFR over shares owned by Essar in HEL. Term Sheet also stated that Essar had a TAR in respect of Essar's shareholding in HEL, should any Vodafone Group shareholding sell its share or part thereof in HEL to a person not in a Vodafone Group entity. VIHBV and Vodafone Group Plc.(as guarantor of VIHBV) had entered into a *'Put Option'* Agreement on 15.03.2007 with ETH, ECL (Mauritius), requiring VIHBV to purchase from Essar Group shareholders' all the option shares held by them.

22. The Joint Director of Income Tax (International Taxation), in the meanwhile, issued a notice dated 15.03.2007 under Section 133(6) of the Income Tax Act calling for certain information regarding sale of stake of Hutchison group HK in HEL, to Vodafone Group Plc.

23. HTIL, on 17.3.2007, wrote to AS confirming that HTIL *has no beneficial or legal or other rights in AS's TII interest or HEL interest*. Vodafone received a letter dated 19.3.2007 from FIPB seeking clarifications on the circumstances under which Vodafone had agreed to pay consideration of US$ 11.08 billion *for acquiring 67% of HEL when the actual acquisition was only 51.96%* as per the application. Vodafone on 19.03.2007 wrote to FIPB stating that it had agreed to acquire from *HTIL interest in HEL which included 52% equity shareholding for US$ 11.08 billion which price included control premium, use and rights to Hutch brand in India, a non-compete agreement with Hutch group, value of non-voting, non-convertible preference shares, various loans obligations and entitlement and to acquire further 15% indirect interest in HEL*, subject to Indian foreign investment rules, which together equated to about 67% of the *economic value of HEL*.

24. VIHBVI and Indian continent Investors Limited (ICIL) had entered into an SHA on 21.03.2007 whereby VIHBVI had to sell 106.470.268 shares in Bharati Airtel to ICIL for a cash consideration of US$ 1,626,930.881 (which was later amended on 09.05.2007)

25. HEL on 22.3.2007 replied to the letter of 15.03.2007, issued by the Joint Director of Income Tax (International Taxation) furnishing requisite information relating to HEL clarifying that it was neither a party to the transaction nor would there be any transfer of shares of HEL.

26. HEL received a letter dated 23.3.2007 from the Additional Director Income Tax (International Taxation) intimating that both Vodafone and Hutchison Telecom Group announcements/press releases/declarations had revealed that HTIL *had made substantive gains and consequently HEL was requested to impress* upon HTIL/Hutchison Telecom Group to discharge their liability on gains, before they ceased operations in India. HEL attention was also drawn to Sections 195, 195(2) and 197 of the Act and stated that under Section 195 obligations were both on the payer and the payee.

27. Vodafone, in the meanwhile, wrote to FIPB on 27.03.2007 confirming that in determining the bid price of US$ 11.09 billion it had taken into account various assets and liabilities of CGP including:

(a) its 51.96% direct and indirect equity ownership of Hutch Essar;

(b) Its ownership of redeemable preference shares in TII and JKF;

(c) Assumption of liabilities of various subsidiaries of CGP amounting to approximately US$630 million;

(d) subject to Indian Foreign Investment Rules, its rights and entitlements, including subscription rights at par value and call options to acquire in future a further 62.75% of TII and call options to acquire a further 54.21% of Omega Telecom Holdings Pvt. Ltd, which together would give Vodafone a further 15.03% proportionate indirect equity ownership of Hutch Essar, various intangible features such as control premium, use and rights of Hutch branch in India, non compete agreement with HTIL.

HEL on 5.4.2007 wrote to the Joint director of Income Tax stating that it has no liabilities accruing out of the transaction, also the department has no locus standi to invoke Section 195 in relation to non-resident entities regarding any purported tax obligations. On 09.04.2007 HTIL submitted FWAs, SHAs, Loan Agreement, Share-pledge Agreements, Guarantees, Hypothecations, Press Announcements, Regulatory filing etc., charts of TII and Omega Shareholding, note on terms of agreement relating to acquisition by AS, AG and IDFC, presentation by Goldman Sachs on fair market valuation and confirmation by Vodafone, factors leading to acquisition by AG and AS and rationale for put/call options etc.

28. Vodafone on 09.04.2007 sent a letter to FIPB confirming that valuation of N.D. Callus, Centrino, would occur as per Goldman Sach's presentation in Schedule 5 to HTIL's letter of 09.04.2007 with a minimum value of US$ 266.25 million and US$164.51 million for the equity in N.D. Callus and Centrino respectively, which would form the basis of the future partnership with AS & AG. Vodafone also wrote a letter to FIPB setting out details of Vodafone Group's interest worldwide. On 30.04.07 a resolution was passed by the Board of Directors of CGP pertaining to loan agreement, resignation and appointment of directors, transfer of shares; all to take effect on completion of SPA. Resolution also accorded approval of entering into a Deed of Assignment in respect of loans owed to HTI(BVI) Finance Limited in the sums of US$

132,092,447.14 and US$ 28,972,505.70. Further resolution also accorded approval to the resignations of certain persons as Directors of the Company, to take effect on completion of SPA. Further, approval was also accorded to the appointment of Erik de Rjik as a sole director of CGP. Resolution also accorded approval to the transfer of CGP from HTI BVI to Vodafone. On 30.04.2007 a board of resolution was passed by the directors of Array for the assignment of loans and resignation of existing directors and appointment of new directors namely Erik de Rjik and two others. On 30.04.2007, the board of directors of HTI BVI approved the transfer documentation in relation to CGP share capital in pursuance of SPA and due execution thereof. On 04.05.2007 HTI BVI delivered the share transfer documentation to the lawyers in Caymen Islands to hold those along with a resolution passed by the board of directors of HTI BVI to facilitate delivery of instruments of transfer to Vodafone at closing of the transaction.

29. *Vodafone on 07.05.2007 received a letter from FIPB conveying its approval to the transaction subject to compliance of observation of applicable laws and regulations in India.* On 08.05.2007 a sum of US$10,854,229,859.05 was paid by Vodafone towards consideration for acquisition of share capital of CGP. On 08.05.2007 Vodafone's name was entered in the register of members of CGP kept in Caymen Islands and the share certificate No.002 of HTI BVI relating to CGP share capital was cancelled. On the same day a Tax Deed of Covenant was entered into between HTIL and Vodafone in pursuance of SPA indemnifying Vodafone in respect of taxation or transfer pricing liabilities payable or suffered by wider group companies (as defined by SPA i.e., CGP, 3 GSPL, Mauritian holding and Indian Companies) on or before completion, including reasonable costs associated with any tax demand.

30. HTIL also sent a side letter to SPA on 08.05.2007 to Vodafone highlighting the termination of the brand licences and brand support service agreements between HTIL and 3GSPL

and the Indian Operating Companies and stated that the net amount to be paid by Vodafone to HTIL would be US$ 10,854,229,859.05 and that Vodafone would retain US$ 351.8 million towards expenses incurred to operationalize the option agreements with AS and AG, out of the total consideration of US$11,076,000,000. On 08.05.2007 loan assignment between HTI BVI Finance Limited, Array and Vodafone of Array debt in a sum of US$ 231,111,427.41 was effected, whereby rights and benefits of HTI BVI Finance Limited to receive repayment was assigned in favour of Vodafone as part of the transaction contemplated vide SPA. On the same day loan assignment between HTI BVI Finance Limited, CGP and Vodafone, of CGP debt in the sum of US$ 28,972,505.70 was effected, whereby rights and benefits of HTI BVI Finance Limited to receive the repayment was assigned in favour of Vodafone as part of the transactions contemplated vide SPA. On 08.05.2007, business transfer agreement between 3GSPL and Hutchison Whampoa Properties (India) Limited, a WOS of HWP Investments Holdings (India) Limited, Mauritius, for the sale of business to 3GSPL of maintaining and operating a call centre as a going concern on slump-sale-basis for a composite price of ‘ 640 million. On 08.05.2007, as already stated, a Deed of Retention was executed between HTIL and Vodafone whereunder HTIL had agreed that out of the total consideration payable in terms of Clause 8.10(b) of the SPA, Vodafone would be entitled to retain US$ 351.8 million by way of HTIL's contribution towards acquisition cost of options i.e., stake of AS & AG. On 08.05.2007 Vodafone paid US$ 10,854,229,859.05 to HTIL.

31. Vodafone on 18.05.2007 sent a letter to FIPB confirming that VIHBV had no existing joint venture or technology transfer/trade mark agreement in the same field as HEL except with Bharati as disclosed and since 20.02.2007 a member of Bharati Group had exercised the option to acquire a further 5.6% interest from Vodafone such that Vodafone's direct and indirect stake in Bharati Airtel would be reduced to 4.39%.

32. An agreement (Omega Agreement) dated 05.06.2007 was entered into between IDF, IDFC, IDFC Private Equity Fund II (IDFCPE), SMMS, HT India, 3GSPL, Omega, SSKI and VIHBV. Due to that Agreement IDF, IDFC and SSKI would instead of exercising the *'Put option'* and *'cashless option'* under 2006 IDFC FWA could exercise the same in pursuance of the present Agreement. Further, 3GSPL had waived its right to exercise the *'call option'* pursuant to 2006 IDFC FWA. On 06.06.2007 a FWA was entered into between IDF, IDFC, IDFCPE, SMMS, HT India, 3GSPL, Omega and VIHBV. By that Agreement 3GSPL had a *'call option'* to purchase the equity shares of SMMS. On 07.06.2007 a SHA was entered into between SMMS, HTIL(M), Omega and VIHBV to regulate the affairs of Omega. On 07.06.2007 a Termination Agreement was entered into between IDF, IDFC, SMMS, HTIL, 3GSPL, Omega and HTL terminating the 2006 IDFC FWA and the SHA and waiving their respective rights and claims under those Agreements. On 27.06.2007 HTIL in their 2007 interim report declared a dividend of HK$ 6.75 per share on account of the gains made by the sale of its entire interest in HEL. On 04.07.2007 fresh certificates of incorporation was issued by the Registrar of Companies in relation to Indian operating companies whereby the word "Hutchison" was substituted with word "Vodafone".

33. On 05.07.2007, a FWA was entered into between AG, AG Mercantile Pvt. Limited, Plustech Mercantile Company Pvt.Ltd, 3GSPL, Nadal Trading Company Pvt. Ltd and Vodafone as a confirming party. In consideration for the unconditional 'call option', 3GSPL agreed to pay AG an amount of US$ 6.3 million annually. On the same day a FWA was signed by AS and Neetu AS, Scorpio Beverages Pvt. Ltd.(SBP), M.V. Healthcare Services Pvt. Ltd, 3GSPL, N.D. Callus Info Services Pvt. Ltd and Vodafone, as a *confirming party*. In consideration for the 'call option' 3GSPL agreed to pay AS & Mrs. Neetu AS an amount of US$ 10.02 million annually.

TII SHA was entered into on 05.07.2007 between Nadal, NDC, CGP (India), TII and VIHBV to regulate the affairs of TII. On 05.07.2007 Vodafone entered into a Consultancy Agreement with AS. Under that Agreement, AS was to be paid an amount of US$ 1,050,000 per annum and a one time payment of US$ 1,30,00,000 was made to AS.

34. Vodafone sent a letter to FIPB on 27.07.2007 enclosing undertakings of AS, AG and their companies as well as SMMS Group to the effect that they would not transfer the shares to any foreign entity without requisite approvals.

35. The Income Tax Department on 06.08.2007 issued a notice to VEL under Section 163 of the Income Tax Act to show cause why it should not be treated as a representative assessee of Vodafone. The notice was challenged by VEL in Writ Petition No.1942 of 2007 before the Bombay High Court. The Assistant Director of Income Tax (Intl.) Circle 2(2), Mumbai, issued a show cause notice to Vodafone under Section 201(1) and 201(1A) of the I.T. Act as to why Vodafone should not be treated a assessee-in-default for failure to withhold tax. Vodafone then filed a Writ Petition 2550/2007 before the Bombay High Court for setting aside the notice dated 19.09.2007. Vodafone had also challenged the constitutional validity of the retrospective amendment made in 2008 to Section 201 and 191 of the I.T. Act. On 03.12.2008 the High Court dismissed the Writ Petition No.2550 of 2007 against which Vodafone filed SLP No.464/2009 before this Court and this Court on 23.01.2009 disposed of the SLP directing the Income Tax Authorities to determine the jurisdictional challenge raised by Vodafone as a preliminary issue. On 30.10.2009 a 2nd show cause notice was issued to Vodafone under Section 201 and 201(1A) by the Income Tax authorities. Vodafone replied to the show cause notice on 29.01.2010. On 31.05.2010 the Income Tax Department passed an order under Section 201 and 201(1A) of the I.T. Act upholding the jurisdiction of the Department to tax the transaction. A show

cause notice was also issued under Section 163(1) of the I.T. Act to Vodafone as to why it should not be treated as an agent / representative assessee of HTIL.

36. Vodafone then filed Writ Petition No.1325 of 2010 before the Bombay High Court on 07.06.2010 challenging the order dated 31.05.2010 issued by the Income Tax Department on various grounds including the jurisdiction of the Tax Department to impose capital gains tax to overseas transactions. The Assistant Director of Income Tax had issued a letter on 04.06.2010 granting an opportunity to Vodafone to address the Department on the question of quantification of liability under Section 201 and 201(1A) of the Income Tax Act. Notice was also challenged by Vodafone in the above writ petition by way of an amendment. The Bombay High Court dismissed the Writ Petition on 08.09.2010 against which the present SLP has been filed.

37. The High Court upheld the jurisdiction of the Revenue to impose capital gains tax on Vodafone as a representative assessee after holding that the transaction between the parties attracted capital gains in India. Court came to the following conclusions:

(a) Transactions between HTIL and Vodafone were fulfilled not merely by transferring a single share of CGP in Cayman Islands, but the commercial and business understanding between the parties postulated that what was being transferred from HTIL to VIHBV was the "controlling interest" in HEL in India, which is an identifiable capital asset independent of CGP share.

(b) HTIL had put into place during the period when it was in the control of HEL a complex structure including the financing of Indian companies which in turn had holdings directly or indirectly in HEL and hence got controlling interest in HEL.

(c) Vodafone on purchase of CGP got indirect interest in HEL, controlling right in certain indirect holding companies in HEL, controlling rights through shareholder agreements which included the right to appoint directors in certain indirect holding companies in HEL, interest in the form of preference share capital in indirect holding companies of HEL, rights to use Hutch brand in India, non-compete agreement with Hutch brand in India etc., which all constitute capital asset as per Section 2(14) of the I.T. Act.

(d) The price paid by Vodafone to HTIL of US$ 11.08 billion factored in as part of the consideration of those diverse rights and entitlements and many of those entitlements are relatable to the transfer of CGP share and that the transactional documents are merely incidental or consequential to the transfer of CGP share but recognized independently the rights and entitlements of HTIL in relation to Indian business which are being transferred to VIHBV.

(e) High Court held that the transfer of CGP share was not adequate in itself to achieve the object of consummating the transaction between HTIL and VIHBV and the rights and entitlements followed would amount to capital gains.

(f) The Court also held that where an asset or source of income is situated in India, the income of which accrues or arises directly or indirectly through or from it shall be treated as income which is deemed to accrue or arise in India, hence, chargeable under Section 9(1)(i) or 163 of the I.T. Act.

(g) Court directed the Assessing Officer to do apportionment of income between the income that has deemed to accrue or arise as a result of nexus with India and that which lies outside. High Court also concluded that the provisions of Section 195 can apply to a non-resident provided there is sufficient territorial connection or nexus between him and India.

(h) Vodafone, it was held, by virtue of its diverse agreements has nexus with Indian jurisdiction and, hence, the proceedings initiated under Section 201 for failure to withhold tax by Vodafone cannot be held to lack jurisdiction.

38. Shri Harish Salve, learned senior counsel appearing for Vodafone explained in detail how Hutchison Corporate Structure was built up and the purpose, object and relevance of such vertical Transnational Structures in the international context. Learned Senior counsel submitted that complex structures are designed not for avoiding tax but for good commercial reasons and Indian legal structure and foreign exchange laws recognize Overseas Corporate Bodies (OCB). Learned senior counsel also submitted that such Transnational Structures also contain exit option to the investors. Senior counsel also pointed out that where regulatory provisions mandate investment into corporate structure such structures cannot be disregarded for tax purposes by lifting the corporate veil especially when there is no motive to avoid tax. Shri Salve also submitted that Hutchison corporate structure was not designed to avoid tax and the transaction was not a colourable device to achieve that purpose. Senior counsel also submitted that source of income lies where the transaction is effected and not where the underlying asset is situated or economic interest lies. Reference was made to judgment in *Seth Pushalal Mansinghka (P) Ltd. v. CIT* (1967) 66 ITR 159 (SC). Learned counsel also pointed out that without any express legislation, off-shore transaction cannot be taxed in India. Reference was made to two judgments of the Calcutta High Court *Assam

Consolidated Tea Estates v. Income Tax Officer "A" Ward* (1971) 81 ITR 699 Cal. and *C.I.T. West Bengal v. National and Grindlays Bank Ltd.* (1969) 72 ITR 121 Cal. Learned senior counsel also pointed out that when a transaction is between two foreign entities and not with an Indian entity, source of income cannot be traced back to India and nexus cannot be used to tax under Section 9. Further, it was also pointed out that language in Section 9 does not contain "look through provisions" and even the words "indirectly" or "through" appearing in Section 9 would not make a transaction of a non-resident taxable in India unless there is a transfer of capital asset situated in India. Learned Senior counsel also submitted that the Income Tax Department has committed an error in proceeding on a "moving theory of nexus" on the basis that economic interest and underlying asset are situated in India. It was pointed out that there cannot be transfer of controlling interest in a Company independent from transfer of shares and under the provisions of the Company Law. Acquisition of shares in a Company entitles the Board a right of "control" over the Company. Learned Senior Counsel also pointed out the right to vote, right to appoint Board of Directors, and other management rights are incidental to the ownership of shares and there is no change of control in the eye of law but only in commercial terms. Mr. Salve emphasized that, in absence of the specific legislation, such transactions should not be taxed. On the situs of shares, learned senior counsel pointed out that the situs is determined depending upon the place where the asset is situated. Learned senior counsel also pointed out that on transfer of CGP, Vodafone got control over HEL and merely because Vodafone has presence or chargeable income in India, it cannot be inferred that it can be taxed in some other transactions. Further, it was also pointed out that there was no transfer of any capital asset from HTIL to Vodafone pursuant to Option Agreements, FWAs, executed by the various Indian subsidiaries. Learned Senior Counsel also pointed out that the definition of "transfer" under Section 2(47) which provides for "extinguishment" is attracted for a transfer of a legal right and not a contractual right and there was no extinguishment of right by HTIL which gave rise to capital gains tax in India. Reference was made to judgment *CIT v. Grace Collis* (2001) 3 SCC 430**.** Learned senior counsel also submitted that the acquisition of "controlling interest" is a commercial concept and tax is levied on transaction and not its effect. Learned senior counsel pointed out that to lift the corporate veil of a legally recognised corporate structure time and the stage of the transaction are very important and not the motive to save the tax. Reference was also made to several judgments of the English Courts viz, *IRC v. Duke of Westminster* (1936) AC 1 (HL)**,** *W. T. Ramsay v. IRC* (1982) AC 300 (HL)**,** *Craven v. White* (1988) 3 All ER 495**,** *Furniss v. Dawson* (1984) 1 All ER 530 etc. Reference was also made to the judgment of this Court in *McDowell, Azadi Bachao Andolan* cases (supra) and few other judgments. Learned senior counsel point out that Azadi Bachao Andolan broadly reflects Indian jurisprudence and that generally Indian courts used to follow the principles laid down by English Courts on the issue of tax avoidance and tax evasion. Learned Senior counsel also submitted that Tax Residency Certificate (for short TRC) issued by the Mauritian authorities has to be respected and in the absence of any Limitation on Benefit (LOB Clause), the benefit of the Indo-Mauritian Treaty is available to third parties who invest in India through Mauritius route.

39. Mr. Salve also argued on the extra territorial applicability of Section 195 and submitted that the same cannot be enforced on a non-resident without a presence in India. Counsel also pointed out that the words "any person" in Section 195 should be construed to apply to payers who have a presence in India or else enforcement would be impossible and such a provision should be read down in case of payments not having any nexus with India. Senior counsel also submitted that the withholding tax provisions under Section 195 of the Indian Income Tax Act, do not apply to offshore entities making off-

shore payments and the said Section could be triggered only if it can be established that the payment under consideration is of a "sum chargeable" under the Income Tax Act (for short IT Act). Senior counsel therefore contended that the findings of the Tax Authorities that pursuant to the transaction the benefit of telecom licence stood transferred to Vodafone is misconceived and that under the telecom policy of India a telecom licence can be held only by an Indian Company and there is no transfer direct or indirect of any licence to Vodafone.

40. Mr. R.F. Nariman, Learned Solicitor General appearing for the Income Tax Department submitted that the sale of CGP share was nothing but an artificial avoidance scheme and CGP was fished out of the HTIL legal structure as an artificial tax avoidance contrivance. Shri Nariman pointed out that CGP share has been interposed at the last minute to artificially remove HTIL from the Indian telecom business. Reference was made to the Due Diligence Report of Ernst and Young which stated that target structure later included CGP which was not there originally. Further, it was also pointed out that HTIL extinguished its rights in HEL and put Vodafone in its place and CGP was merely an interloper. Shri Nariman also pointed out that as per Settlement Agreement, HTIL sold direct and indirect equity holdings, loans, other interests and rights relating to HEL which clearly reveal something other than CGP share was sold and those transactions were exposed by the SPA. Learned Solicitor General also referred extensively the provisions of SPA and submitted that the legal owner of CGP is HTIBVI Holdings Ltd., a British Virgin Islands Company which was excluded from the Agreement with an oblique tax motive.

41. Mr. Nariman also submitted the situs of CGP can only be in India as the entire business purpose of holding that share was to assume control in Indian telecom operations, the same was managed through Board of Directors controlled by HTIL. The controlling interest expressed by HTIL would amount to property rights and hence taxable in India. Reference was made

to judgments of the Calcutta High Court in *CIT v. National Insurance Company* (1978) 113 ITR 37(Cal.) and *Laxmi Insurance Company Pvt. Ltd. v. CIT* (1971) 80 ITR 575 (Delhi). Further, it was also pointed out the "call and put" options despite being a contingent right are capable of being transferred and they are property rights and not merely contractual rights and hence would be taxable. Referring to the SPA Shri Nariman submitted that the transaction can be viewed as extinguishment of HTILs property rights in India and CGP share was merely a mode to transfer capital assets in India. Further, it was also pointed out that the charging Section should be construed purposively and it contains a look through provision and that the definition of the transfer in Section 9(1)(i) is an inclusive definition meant to explain the scope of that Section and not to limit it. The resignation of HTIL Directors on the Board of HEL could be termed as extinguishment and the right to manage a Company through its Board of Directors is a right to property. Learned Solicitor General also extensively referred to Ramsay Doctrine and submitted that if business purpose as opposed to effect is to artificially avoid tax then that step should be ignored and the courts should adopt a *purposive construction* on the SPA. Considerable reliance was placed on judgment of this Court in *Mc.Dowell* and submitted that the same be followed and not *Azadi Bachao Andolan* which has been incorrectly decided. Further, it was also pointed out that Circular No.789 as regards the conclusiveness of TRC would apply only to dividend clause and as regards capital gains, it would still have to satisfy the twin tests of Article 13(4) of the treaty namely the shares being "alienated and the gains being derived" by a Mauritian entity. Learned Solicitor General also submitted that the Department can make an enquiry into whether capital gains have been factually and legally assigned to a Mauritian entity or to third party and whether the Mauritian Company was a façade.

42. Learned counsels, on either side, in support of their

respective contentions, referred to several judgments of this Court, foreign Courts, international expert opinions, authoritative articles written by eminent authors etc. Before examining the same, let us first examine the legal status of a corporate structure, its usefulness in cross-border transactions and other legal and commercial principles in use in such transactions, which are germane to our case.

Part – II

CORPORATE STRUCTURE / GENERAL PRINCIPLES (National and International)

43. Corporate structure is primarily created for business and commercial purposes and multi-national companies who make offshore investments always aim at better returns to the shareholders and the progress of their companies. Corporation created for such purposes are legal entities distinct from its members and are capable of enjoying rights and of being subject to duties which are not the same as those enjoyed or borne by its members. Multi-national companies, for corporate governance, may develop corporate structures, affiliate subsidiaries, joint ventures for operational efficiency, tax avoidance, mitigate risks etc. On incorporation, the corporate property belongs to the company and members have no direct proprietary rights to it but merely to their "shares" in the undertaking and these shares constitute items of property which are freely transferable in the absence of any express provision to the contrary.

44. Corporate structure created for genuine business purposes are those which are generally created or acquired: at the time when investment is being made; or further investments are being made; or the time when the Group is undergoing financial or other overall restructuring; or when operations, such as consolidation, are carried out, to clean-defused or over-diversified. Sound commercial reasons like

hedging business risk, hedging political risk, mobility of investment, ability to raise loans from diverse investments, often underlie creation of such structures. In transnational investments, the use of a tax neutral and investor-friendly countries to establish SPV is motivated by the need to create a tax efficient structure to eliminate double taxation wherever possible and also plan their activities attracting no or lesser tax so as to give maximum benefit to the investors. Certain countries are exempted from capital gain, certain countries are partially exempted and, in certain countries, there is nil tax on capital gains. Such factors may go in creating a corporate structure and also restructuring.

45. Corporate structure may also have an exit route, especially when investment is overseas. For purely commercial reasons, a foreign group may wind up its activities overseas for better returns, due to disputes between partners, unfavourable fiscal policies, uncertain political situations, strengthen fiscal loans and its application, threat to its investment, insecurity, weak and time consuming judicial system etc., all can be contributing factors that may drive its exit or restructuring. Clearly, there is a fundamental difference in transnational investment made overseas and domestic investment. Domestic investments are made in the home country and meant to stay as it were, but when the trans-national investment is made overseas away from the natural residence of the investing company, provisions are usually made for exit route to facilitate an exit as and when necessary for good business and commercial reasons, which is generally foreign to judicial review.

46. Revenue/Courts can always examine whether those corporate structures are genuine and set up legally for a sound and veritable commercial purpose. Burden is entirely on the Revenue to show that the incorporation, consolidation, restructuring etc. has been effected to achieve a fraudulent, dishonest purpose, so as to defeat the law.

CORPORATE GOVERNANCE

47. Corporate governance has been a subject of considerable interest in the corporate world. The Organisation for Economic cooperation and Development (OECD) defines corporate governance as follows :-

> "Corporate governance is a system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation and other stake holders and spells out rules and procedures for making decisions on corporate affairs. By doing this, it also provides a structure through which the company objectives are set and the means of attaining those objectives and monitoring performance."

The Ministry of Corporate Affairs to the Government of India, has issued several press notes for information of such global companies, which will indicate that Indian corporate Law has also accepted the corporate structure consisting of holding companies and several subsidiary companies. A holding company which owns enough voting stock in a subsidiary can control management and operation by influencing or electing its Board of Directors. The holding company can also maintain group accounts which is to give members of the holding company a picture of the financial position of the holding company and its subsidiaries. The form and content of holding company or subsidiary company's own balance sheet and profit and loss account are the same as if they were independent companies except that a holding company's accounts an aggregated value of shares it holds in its subsidiaries and in related companies and aggregated amount of loss made by it to its subsidiaries and to related companies and their other indebtedness to it must be shown separately from other assets etc.

48. Corporate governors can also misuse their office, using

fraudulent means for unlawful gain, they may also manipulate their records, enter into dubious transactions for tax evasion. Burden is always on the Revenue to expose and prove such transactions are fraudulent by applying *look at principle*.

OVERSEAS COMPANIES AND FDI

49. Overseas companies are companies incorporated outside India and neither the Companies Act nor the Income Tax Act enacted in India has any control over those companies established overseas and they are governed by the laws in the countries where they are established. From country to country laws governing incorporation, management, control, taxation etc. may change. Many developed and wealthy Nations may park their capital in such off-shore companies to carry on business operations in other countries in the world. *Many countries give facilities for establishing companies in their jurisdiction with minimum control and maximum freedom. Competition is also there among various countries for setting up such offshore companies in their jurisdiction*. Demand for offshore facilities has considerably increased, in recent times, owing to high growth rates of cross-border investments and to the increased number of rich investors who are prepared to use high technology and communication infrastructures to go offshore. *Removal of barriers to cross-border trade, the liberalization of financial markets and new communication technologies have had positive effects on the developing countries including India*.

50. Investment under foreign Direct Investment Scheme (FDI scheme), investment by Foreign Institutional Investors (FIIs) under the Portfolio Investment Scheme, investment by NRIs/OBCs under the Portfolio Investment Scheme and sale of shares by NRIs/OBCs on non-repatriation basis; Purchase and sale of securities other than shares and convertible debentures of an Indian company by a non-resident are common. Press Notes are announced by the Ministry of Commerce and Industry

and the Ministry issued Press Note no. 2, 2009 and Press Note 3, 2009, which deals with calculation of foreign investment in downstream entities and requirement of ownership or control in sectoral cap companies. Many of the offshore companies use the facilities of Offshore Financial Centres situate in Mauritius, Cayman Islands etc. *Many of these offshore holdings and arrangements are undertaken for sound commercial and legitimate tax planning reasons, without any intent to conceal income or assets from the home country tax jurisdiction and India has always encouraged such arrangements, unless it is fraudulent or fictitious*.

51. Moving offshore or using an OFC does not necessarily lead to the conclusion that they involve in the activities of tax evasion or other criminal activities. The multi-national companies are attracted to offshore financial centres mainly due to the reason of providing attractive facilities for the investment. Many corporate conglomerates employ a large number of holding companies and often high-risk assets are parked in separate companies so as to avoid legal and technical risks to the main group. *Instances are also there when individuals form offshore vehicles to engage in risky investments, through the use of derivatives trading etc. Many of such companies do, of course, involve in manipulation of the market, money laundering and also indulge in corrupt activities like round tripping, parking black money or offering, accepting etc., directly or indirectly bribe or any other undue advantage or prospect thereof*.

52. OECD (Organisation for Economic Co-operation and Development) in the year 1998 issued a report called "Harmful Tax Competition: An Emerging Global Issue". The report advocated doing away with tax havens and offshore financial canters, like the Cayman Islands, on the basis that their low-tax regimes provide them with an unfair advantage in the global marketplace and are thus harmful to the economics of more developed countries. OECD threatened to place the Cayman

Islands and other tax havens on a "black list" and impose sanctions against them.

53. OECD's blacklist was avoided by Cayman Islands in May 2000 by committing itself to a string of reforms to improve transparency, remove discriminatory practices and began to exchange information with OECD. *Often, complaints have been raised stating that these centres are utilized for manipulating market, to launder money, to evade tax, to finance terrorism, indulge in corruption etc.* All the same, it is stated that OFCs have an important role in the international economy, offering advantages for multi-national companies and individuals for investments and also for legitimate financial planning and risk management. *It is often said that insufficient legislation in the countries where they operate gives opportunities for money laundering, tax evasion etc. and, hence, it is imperative that that Indian Parliament would address all these issues with utmost urgency*.

Need for Legislation:

54. Tax avoidance is a problem faced by almost all countries following civil and common law systems and all share the common broad aim, that is to combat it. Many countries are taking various legislative measures to increase the scrutiny of transactions conducted by non-resident enterprises. Australia has both general and specific anti-avoidance rule (GAAR) in its Income Tax Legislations. In Australia, GAAR is in Part IVA of the Income Tax Assessment Act, 1936, which is intended to provide an effective measure against tax avoidance arrangements. South Africa has also taken initiative in combating impermissible tax avoidance or tax shelters. Countries like China, Japan etc. have also taken remedial measures.

55. Direct Tax Code Bill (DTC) 2010, proposed in India, envisages creation of an economically efficient, effective direct

tax system, proposing GAAR. GAAR intends to prevent tax avoidance, what is inequitable and undesirable. Clause 5(4)(g) provides that the income from transfer, outside India of a share in a foreign company shall be deemed to arise in if the FMV of assets India owned by the foreign company is at least 50% of its total assets. Necessity to take effective legislative measures has been felt in this country, but we always lag behind because our priorities are different. Lack of proper regulatory laws, leads to uncertainty and passing inconsistent orders by Courts, Tribunals and other forums, putting Revenue and tax payers at bay.

HOLDING COMPANY AND SUBSIDIARY COMPANY

56. Companies Act in India and all over the world have statutorily *recognised subsidiary company as a separate legal entity*. Section 2(47) of the Indian Companies Act 1956 defines "subsidiary company" or "subsidiary", a subsidiary company within the meaning of Section 4 of the Act. For the purpose of Indian Companies Act, a company shall be subject to the provisions of sub-section 3 of Section 4, be deemed to be subsidiary of another, subject to certain conditions, which includes holding of share capital in excess of 50% controlling the composition of Board of Directors and gaining status of subsidiary with respect to third company by holding company's subsidization of third company. A holding company is one which owns sufficient shares in the subsidiary company to determine who shall be its directors and how its affairs shall be conducted. Position in India and elsewhere is that the holding company controls a number of subsidiaries and respective businesses of companies within the group and manage and integrate as whole as though they are merely departments of one large undertaking owned by the holding company. *But, the business of a subsidiary is not the business of the holding company* (See *Gramophone & Typewriter Ltd. v. Stanley,* (1908-10) All ER Rep 833 at 837).

57. Subsidiary companies are, therefore, the integral part of corporate structure. Activities of the companies over the years have grown enormously of its incorporation and outside and their structures have become more complex. *Multi National Companies having large volume of business nationally or internationally will have to depend upon their subsidiary companies in the national and international level for better returns for the investors and for the growth of the company*. When a holding company owns all of the voting stock of another company, the company is said to be a WOS of the parent company. Holding companies and their subsidiaries can create pyramids, whereby subsidiary owns a controlling interest in another company, thus becoming its parent company.

58. Legal relationship between a holding company and WOS is that they are two distinct legal persons and the holding company does not own the assets of the subsidiary and, in law, the management of the business of the subsidiary also vests in its Board of Directors. In *Bacha F. Guzdar v. CIT* AIR 1955 SC 74, this Court held that shareholders' only rights is to get dividend if and when the company declares it, to participate in the liquidation proceeds and to vote at the shareholders' meeting. Refer also to *Carew and Company Ltd. v. Union of India* (1975) 2 SCC 791 and *Carrasco Investments Ltd. v. Special Director, Enforcement* (1994) 79 Comp Case 631 (Delhi).

59. Holding company, of course, if the subsidiary is a WOS, may appoint or remove any director if it so desires by a resolution in the General Body Meeting of the subsidiary. Holding companies and subsidiaries can be considered as single economic entity and consolidated balance sheet is the accounting relationship between the holding company and subsidiary company, which shows the status of the entire business enterprises. Shares of stock in the subsidiary company are held as assets on the books of the parent company and can be issued as collateral for additional debt

financing. *Holding company and subsidiary company are, however, considered as separate legal entities, and subsidiary are allowed decentralized management. Each subsidiary can reform its own management personnel and holding company may also provide expert, efficient and competent services for the benefit of the subsidiaries*.

60. U.S. Supreme Court in *United States v. Bestfoods* 524 US 51 (1998) explained that it is a general principle of corporate law and legal systems that a parent corporation is not liable for the acts of its subsidiary, *but the Court went on to explain that corporate veil can be pierced and the parent company can be held liable for the conduct of its subsidiary, if the corporal form is misused to accomplish certain wrongful purposes, when the parent company is directly a participant in the wrong complained of*. Mere ownership, parental control, management etc. of a subsidiary is not sufficient to pierce the status of their relationship and, to hold parent company liable. In *Adams v. Cape Industries Plc.* (1991) 1 All ER 929, the Court of Appeal emphasized that it is appropriate to pierce the corporate veil where special circumstances exist indicating that it is mere façade concealing true facts.

61. *Courts, however, will not allow the separate corporate entities to be used as a means to carry out fraud or to evade tax. Parent company of a WOS, is not responsible, legally for the unlawful activities of the subsidiary save in exceptional circumstances, such as a company is a sham or the agent of the shareholder, the parent company is regarded as a shareholder.* Multi-National Companies, by setting up complex vertical pyramid like structures, would be able to distance themselves and separate the parent from operating companies, thereby protecting the multi-national companies from legal liabilities.

SHAREHOLDERS' AGREEMENT

62. hareholders' Agreement (for short SHA) is essentially

a contract between some or all other shareholders in a company, the purpose of which is to confer rights and impose obligations over and above those provided by the Company Law. *SHA is a private contract between the shareholders compared to Articles of Association of the Company, which is a public document. Being a private document it binds parties thereof and not the other remaining shareholders in the company*. Advantage of SHA is that it gives greater flexibility, unlike Articles of Association. It also makes provisions for resolution of any dispute between the shareholders and also how the future capital contributions have to be made. Provisions of the SHA may also go contrary to the provisions of the Articles of Association, in that event, naturally provisions of the Articles of Association would govern and not the provisions made in the SHA.

63. The nature of SHA was considered by a two Judges Bench of this Court in *V. B. Rangaraj v. V. B. Gopalakrishnan and Ors.* (1992) 1 SCC 160. In that case, an agreement was entered into between shareholders of a private company wherein a restriction was imposed on a living member of the company to transfer his shares only to a member of his own branch of the family, such restrictions were, however, not envisaged or provided for within the Articles of Association. This Court has taken the view that provisions of the Shareholders' Agreement imposing restrictions even when consistent with Company legislation, are to be authorized only when they are incorporated in the Articles of Association, a view we do not subscribe. This Court in *Gherulal Parekh v. Mahadeo Das Maiya* (1959) SCR Supp (2) 406 held that freedom of contract can be restricted by law only in cases where it is for some good for the community. Companies Act 1956 or the FERA 1973, RBI Regulation or the I.T. Act do not explicitly or impliedly forbid shareholders of a company to enter into agreements as to how they should exercise voting rights attached to their shares.

64. *Shareholders can enter into any agreement in the best interest of the company, but the only thing is that the provisions in the SHA shall not go contrary to the Articles of Association. The essential purpose of the SHA is to make provisions for proper and effective internal management of the company*. It can visualize the best interest of the company on diverse issues and can also find different ways not only for the best interest of the shareholders, but also for the company as a whole. In *S. P. Jain v. Kalinga Cables Ltd.* (1965) 2 SCR 720, this Court held that agreements between non-members and members of the Company will not bind the company, but there is nothing unlawful in entering into agreement for transferring of shares. Of course, the manner in which such agreements are to be enforced in the case of breach is given in the general law between the company and the shareholders. A breach of SHA which does not breach the Articles of Association is a valid corporate action but, as we have already indicated, the parties aggrieved can get remedies under the general law of the land for any breach of that agreement.

65. SHA also provides for matters such as restriction of transfer of shares i.e. *Right of First Refusal (ROFR), Right of First Offer (ROFO), Drag-Along Rights (DARs) and Tag-Along Rights (TARs), Pre-emption Rights, Call option, Put option, Subscription option etc*. SHA in a characteristic Joint Venture Enterprise may regulate its affairs on the basis of various provisions enumerated above, because Joint Venture enterprise may deal with matters regulating the ownership and voting rights of shares in the company, control and manage the affairs of the company, and also may make provisions for resolution of disputes between the shareholders. Many of the above mentioned provisions find a place in SHAs, FWAs, Term Sheet Agreement etc. in the present case, hence, we may refer to some of those provisions.

(a) <u>Right of First Refusal (ROFR)</u>: ROFR permits its holders to claim the transfer of the subject of the right with a unilateral declaration of intent which can either be contractual or legal. No statutory recognition has been given to that right either in the Indian Company Law or the Income Tax Laws. Some foreign jurisdictions have made provisions regulating those rights by statutes. Generally, ROFR is contractual and determined in an agreement. ROFR clauses have contractual restrictions that give the holders the option to enter into commercial transactions with the owner on the basis of some specific terms before the owner may enter into the transactions with a third party. Shareholders' right to transfer the shares is not totally prevented, yet a shareholder is obliged to offer the shares first to the existing shareholders. Consequently, the other shareholders will have the privilege over the third parties with regard to purchase of shares.

(b) Tag Along Rights (TARs): TARs, a facet of ROFR, often refer to the power of a minority shareholder to sell their shares to the prospective buyer at the same price as any other shareholder would propose to sell. In other words, if one shareholder wants to sell, he can do so only if the purchaser agrees to purchase the other shareholders, who wish to sell at the same price. TAR often finds a place in the SHA which protects the interest of the minority shareholders.

(c) Subscription Option: Subscription option gives the beneficiary a right to demand issuance of allotment of shares of the target company. It is for that reason that a subscription right is normally accompanied by ancillary provisions including an Exit clause where, if dilution crosses a particular level, the counter parties are given some kind of Exit option.

(d) Call Option: Call option is an arrangement often seen in Merger and Acquisition projects, especially when they aim at foreign investment. A Call option is given to a foreign buyer by agreement so that the foreign buyer is able to enjoy the

permitted minimum equity interests of the target company. Call option is always granted as a right not an obligation, which can be exercised upon satisfaction of certain conditions and/or within certain period agreed by the grantor and grantee. The buyer of Call option pays for the right, without the obligation to buy some underlying instrument from the writer of the option contract at a set future date and at the strike price. Call option is where the beneficiary of the action has a right to compel a counter-party to transfer his shares at a pre-determined or price fixed in accordance with the pre-determined maxim or even fair market value which results in a simple transfer of shares.

(e) Put Option: A put option represents the right, but not the requirement to sell a set number of shares of stock, which one do not yet own, at a pre-determined strike price, before the option reaches the expiration date. A put option is purchased with the belief that the underlying stock price will drop well before the strike price, at which point one may choose to exercise the option.

(f) Cash and Cashless Options: Cash and Cashless options are related arrangement to call and put options creating a route by which the investors could carry out their investment, in the event of an appreciation in the value of shares.

66. SHA, therefore, regulate the ownership and voting rights of shares in the company including ROFR, TARs, DARs, Preemption Rights, Call Options, Put Options, Subscription Option etc. in relation to any shares issued by the company, restriction of transfer of shares or granting securities interest over shares, provision for minority protection, lock-down or for the interest of the shareholders and the company. *Provisions referred to above, which find place in a SHA, may regulate the rights between the parties which are purely contractual and those rights will have efficacy only in the course of ownership of shares by the parties*.

SHARES, VOTING RIGHTS AND CONTROLLING INTERESTS:

67. Shares of any member in a company is a moveable property and can be transferred in the manner provided by the Articles of Association of the company. Stocks and shares are specifically included in the definition of the Sale of Goods Act, 1930. A share represents a bundle of rights like right to (1) elect directors, (2) vote on resolution of the company, (3) enjoy the profits of the company if and when dividend is declared or distributed, (4) share in the surplus, if any, on liquidation.

68. Share is a right to a specified amount of the share capital of a company carrying out certain rights and liabilities, in other words, shares are bundles of intangible rights against the company. Shares are to be regarded as situate in the country in which it is incorporated and register is kept. Shares are transferable like any other moveable property under the Companies Act and the Transfer of Property Act. Restriction of Transfer of Shares is valid, if contained in the Articles of Association of the company. Shares are, therefore, presumed to be freely transferable and restrictions on their transfer are to be construed strictly. Transfer of shares may result in a host of consequences.

Voting Rights:

69. Voting rights vest in persons who names appear in the Register of Members. Right to vote cannot be decoupled from the share and an agreement to exercise voting rights in a desired manner, does not take away the right of vote, in fact, it is the shareholders' right. Voting rights cannot be denied by a company by its articles or otherwise to holders of shares below a minimum number such as only shareholders holding five or more shares are entitled to vote and so on, subject to certain limitations.

70. Rights and obligations flowing from voting rights have

been the subject matter of several decisions of this Court. In *Chiranjit Lal Chowdhuri v. Union of India* (1950) 1 SCR 869 at 909 : AIR 1951 SC 41, with regard to exercise of the right to vote, this Court held that the right to vote for the election of directors, the right to pass resolutions and the right to present a petition for winding up are personal rights flowing from the ownership of the share and cannot be themselves and apart from the share be acquired or disposed of or taken possession of. In *Dwarkadas Shrinivas of Bombay v. Sholapur Spinning & Weaving Company* (1954) SCR 674 at 726 : AIR 1954 SC 119, this Court noticed the principle laid down in *Chiranjit Lal Chowdhuri* (supra).

71. Voting arrangements in SHAs or pooling agreements are not "property". Contracts that provide for voting in favour of or against a resolution or acting in support of another shareholder create only "contractual obligations". A contract that creates contractual rights thereby, the owner of the share (and the owner of the right to vote) agrees to vote in a particular manner does not decouple the right to vote from the share and assign it to another. *A contract that is entered into to provide voting in favour of or against the resolution or acting in support of another shareholder, as we have already noted, creates contractual obligation.* Entering into any such contract constitutes an assertion (and not an assignment) of the right to vote for the reason that by entering into the contract: (a) the owner of the share asserts that he has a right to vote; (b) he agrees that he is free to vote as per his will; and (c) he contractually agrees that he will vote in a particular manner. Once the owner of a share agrees to vote in a particular manner, that itself would not determine as a property.

Controlling Interest:

72. Shares, we have already indicated, represent congeries of rights and controlling interest is an incident of holding majority shares. Control of a company vests in the

voting powers of its shareholders. Shareholders holding a controlling interest can determine the nature of the business, its management, enter into contract, borrow money, buy, sell or merge the company. Shares in a company may be subject to premiums or discounts depending upon whether they represent controlling or minority interest. Control, of course, confers value but the question as to whether one will pay a premium for controlling interest depends upon whether the potential buyer believes one can enhance the value of the company.

73. The House of Lords in *IRC v. V.T. Bibby & Sons* (1946) 14 ITR (Supp) 7 at 9-10, after examining the meaning of the expressions “control” and “interest”, held that controlling interest did not depend upon the extent to which they had the power of controlling votes. Principle that emerges is that where shares in large numbers are transferred, which result in shifting of “controlling interest”, it cannot be considered as two separate transactions namely transfer of shares and transfer of controlling interest. *Controlling interest forms an inalienable part of the share itself and the same cannot be traded separately unless otherwise provided by the Statute.* Of course, the Indian Company Law does not explicitly throw light on whether control or controlling interest is a part of or inextricably linked with a share of a company or otherwise, so also the Income Tax Act. In the impugned judgment, the High Court has taken the stand that controlling interest and shares are distinct assets.

74. Control, in our view, is an interest arising from holding a particular number of shares and the same cannot be separately acquired or transferred. Each share represents a vote in the management of the company and such a vote can be utilized to control the company. *Controlling interest, therefore, is not an identifiable or distinct capital asset independent of holding of shares and the nature of the transaction has to be ascertained from the terms of the contract and the surrounding circumstances. Controlling*

interest is inherently contractual right and not property right and cannot be considered as transfer of property and hence a capital asset unless the Statute stipulates otherwise. Acquisition of shares may carry the acquisition of controlling interest, which is purely a commercial concept and tax is levied on the transaction, not on its effect.

A. <u>LIFTING THE VEIL – TAX LAWS</u>

75. Lifting the corporate veil doctrine is readily applied in the cases coming within the Company Law , Law of Contract, Law of Taxation. Once the transaction is shown to be fraudulent, sham, circuitous or a device designed to defeat the interests of the shareholders, investors, parties to the contract and also for tax evasion, the Court can always lift the corporate veil and examine the substance of the transaction. This Court in *Commissioner of Income Tax v. Sri Meenakshi Mills Ltd., Madurai,* AIR 1967 SC 819 held that the Court is entitled to lift the veil of the corporate entity and pay regard to the economic realities behind the legal façade meaning that the court has the power to disregard the corporate entity if it is used for tax evasion. In *Life Insurance Corporation of India v. Escorts Limited and Others* (1986) 1 SCC 264, this Court held that the corporate veil may be lifted where a statute itself contemplates lifting of the veil or fraud or improper conduct intended to be prevented or a taxing statute or a beneficial statute is sought to be evaded or where associated companies are inextricably as to be, in reality part of one concern. Lifting the Corporate Veil doctrine was also applied in *Juggilal Kampalpat v. Commissioner of Income Tax, U.P.* , AIR 1969 SC 932 : (1969) 1 SCR 988, wherein this Court noticed that the assessee firm sought to avoid tax on the amount of compensation received for the loss of office by claiming that it was capital gain and it was found that the termination of the contract of managing agency was a collusive transaction. Court held that it was a collusive device, practised by the managed

company and the assessee firm for the purpose of evading income tax, both at the hands of the payer and the payee.

76. Lifting the corporate veil doctrine can, therefore, be applied in tax matters even in the absence of any statutory authorisation to that effect. Principle is also being applied in cases of holding company – subsidiary relationship- where in spite of being separate legal personalities, if the facts reveal that they indulge in dubious methods for tax evasion.

B. <u>Tax Avoidance and Tax Evasion:</u>

Tax avoidance and tax evasion are two expressions which find no definition either in the Indian Companies Act, 1956 or the Income Tax Act, 1961. But the expressions are being used in different contexts by our Courts as well as the Courts in England and various other countries, when a subject is sought to be taxed. One of the earliest decisions which came up before the House of Lords in England demanding tax on a transaction by the Crown is *Duke of Westminster* (supra). In that case, Duke of Westminster had made an arrangement that he would pay his gardener an annuity, in which case, a tax deduction could be claimed. Wages of household services were not deductible expenses in computing the taxable income, therefore, Duke of Westminster was advised by the tax experts that if such an agreement was employed, Duke would get tax exemption. Under the Tax Legislation then in force, if it was shown as gardener's wages, then the wages paid would not be deductible. Inland Revenue contended that the *form of the transaction* was not acceptable to it and the Duke was taxed *on the substance of the transaction*, which was that payment of annuity was treated as a payment of salary or wages. Crown's claim of *substance doctrine* was, however, rejected by the House of Lords. Lord Tomlin's celebrated words are quoted below:

> "Every man is entitled if he can to order his affairs so that

> the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax. This so called doctrine of 'the substance' seems to me to be nothing more than an attempt to make a man pay notwithstanding that he has so ordered his affairs that the amount of tax sought from him is not legally claimable."

Lord Atkin, however, dissented and stated that "the substance of the transaction was that what was being paid was remuneration."

The principles which have emerged from that judgment are as follows:

> (1) A legislation is to receive a strict or literal interpretation;
>
> (2) An arrangement is to be *looked at* not in by its economic or commercial substance but by its legal form; and
>
> (3) An arrangement is effective for tax purposes even if it has no business purpose and has been entered into to avoid tax.

The House of Lords, during 1980's, it seems, began to attach a *"purposive interpretation approach"* and gradually began to give emphasis on *"economic substance doctrine"* as a question of statutory interpretation. In a most celebrated case in *Ramsay* (supra), the House of Lords considered this question again. That was a case whereby the taxpayer entered into a circular series of transactions designed to produce a loss for tax purposes, but which together produced no commercial result. Viewed that transaction as a whole, the series of transactions was self-canceling, the taxpayer was in precisely the same commercial position at the end as at the beginning of the series of transactions. House of Lords ruled that, notwithstanding the rule in *Duke of Westminster's* case, the series of transactions should be disregarded for tax purposes and the manufactured loss, therefore, was not available to the taxpayer. Lord Wilberforce opined as follows:

> "While obliging the court to accept documents or transactions, found to be genuine, as such, it does not compel the court to *look at* a document or a transaction in blinkers, isolated from any context to which it properly belongs. If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine to prevent it being so regarded; to do so in *not to prefer form to substance, or substance to form*. It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions intended to operate as such, it is that series or combination which may be regarded."

(emphasis supplied)

House of Lords, therefore, made the following important remarks concerning what action the Court should consider in cases that involve tax avoidance:

> (1) A taxpayer was only to be taxed if the Legislation clearly indicated that this was the case;
>
> (2) A taxpayer was entitled to manage his or her affairs so as to reduce tax;
>
> (3) Even if the purpose or object of a transaction was to avoid tax this did not invalidate a transaction unless an anti-avoidance provision applied; and

> (4) If a document or transaction was genuine and not a sham in the traditional sense, the Court had to adhere to the form of the transaction following the Duke Westminster concept.

77. In *Ramsay* (supra) it may be noted, the taxpayer produced a profit that was liable to capital gains tax, but a readymade claim was set up to create an allowable loss that was purchased by the taxpayer with the intention of avoiding the capital gains tax. Basically, the House of Lords, cautioned that the technique of tax avoidance might progress and technically improve and Courts are not obliged to be at a standstill. In other words, the view expressed was that that a subject could be taxed only if there was a clear intendment and the intendment has to be ascertained on clear principles and the Courts would not approach the issue on a mere literal interpretation. *Ramsay* was, therefore, seen as a new approach to *artificial tax avoidance scheme*.

78. *Ramsay* was followed by the House of Lords in another decision in *IRC v. Burmah Oil Co Ltd.* (1982) 54 TC 200. This case was also concerned with a self-cancelling series of transactions. Lord Diplock, in that case, confirmed the judicial view that a development of the jurisprudence was taking place, stating that *Ramsay* case marked a significant change in the approach adopted by the House of Lords to a *pre-ordained* series of transactions. *Ramay* and *Burmah* cases, it may be noted, were against self-cancelling artificial tax schemes which were widespread in England in 1970's. Rather than striking down the self-cancelling transactions, of course, few of the speeches of Law Lords gave the impression that the tax effectiveness of a scheme should be judged by reference to its commercial substance rather than its legal form. On this, of course, there was some conflict with the principle laid down in *Duke of Westminster. Duke of Westminster* was concerned with the "single tax avoidance step". During 1970's, the Courts in England had to deal with several pre-planned avoidance

schemes containing a number of steps. In fact, earlier in *IRC v. Plummer* (1979) 3 All ER 775, Lord Wilberforce commented about a scheme stating that the same was carried out with "*almost military precision*" which required the court to look at the scheme as a whole. The scheme in question was a "circular annuity" plan, in which a charity made a capital payment to the taxpayer in consideration of his covenant to make annual payments of income over five years. The House of Lords held that the scheme was valid. Basically, the *Ramsay* was dealing with "*readymade schemes*".

79. The House of Lords, however, had to deal with a non self-cancelling tax avoidance scheme in *Dawson* (supra). Dawsons, in that case, held shares in two operating companies which agreed in principle in September 1971 to sell their entire shareholding to Wood Bastow Holdings Ltd. Acting on advice, to escape capital gains tax, Dawsons decided not to sell directly to Wood Bastow, rather arranged to exchange their shares for shares in an investment company to be incorporated in the Isle of Man. Greenjacket Investments Ltd. was then incorporated in the Isle of Man on 16.12.1971 and two arrangements were finalized (i) Greenjacket would purchase Dawsons shares in the operating company for £152,000 to be satisfied by the issue of shares of Greenjacket and (ii) an agreement for Greenjacket to sell the shares in the operating company to Wood Bastow for £152,000.

80. The High Court and the Court of Appeal ruled that *Ramsay* principle applied only where steps forming part of the scheme were *self-cancelling* and they considered that it did not allow share exchange and sale agreements to be distributed as steps in the scheme, because they had an enduring legal effect. The House of Lords, however, held that steps inserted in a *preordained* series of transactions with no commercial purpose other than tax avoidance should be disregarded for tax purposes, notwithstanding that the inserted step (i.e. the introduction of Greenjacket) had a business effect. Lord

Brightman stated that inserted step had no business purpose apart from the deferment of tax, although it had a business effect.

81. Even though in *Dawson*, the House of Lords seems to strike down the transaction by the taxpayer for the purpose of tax avoidance, House of Lords in *Craven* (supra) clarified the position further. In that case, the taxpayers exchanged their shares in a trading company (Q Ltd) for shares in an Isle of Man holding company (M Ltd), in anticipation of a potential sale or merger of the business. Taxpayers, in the meanwhile, had abandoned negotiations with one interested party, and later concluded a sale of Q Ltd's shares with another. M Ltd subsequently loaned the entire sale proceeds to the taxpayers, who appealed against assessments to capital gains tax. The House of Lords held in favour of the taxpayers, dismissing the crown's appeal by a majority of three to two. House of Lords noticed that when the share exchange took place, there was no certainty that the shares in Q Ltd would be sold. Lord Oliver, speaking for the majority, opined that *Ramsay, Burmah and Dawson* did not produce any legal principle that would nullify any transaction that has no intention besides tax avoidance and opined as follows:

> "My Lords, for my part I find myself unable to accept that Dawson either established or can properly be used to support a general proposition that any transaction which is effected for avoiding tax on a contemplated subsequent transaction and is therefore planned, is for that reason, necessarily to be treated as one with that subsequent transaction and as having no independent effect."

Craven made it clear that: (1) Strategic tax planning undertaken for months or possible years before the event (of-sale) in anticipation of which it was effected; (2) A series of transactions undertaken at the time of disposal/sale, including an intermediate transaction interposed into having no independent life, could under *Ramsay* principle be *looked at* and treated as a composite whole transaction to which the fiscal results of the single composite whole are to be applied, i.e. that an intermediate transfer which was, at the time when it was effected, so closely interconnected with the ultimate disposition, could properly be described as not, in itself, a real transaction at all, but merely an element in some different and larger whole without independent effect.

81. Later, House of Lords in *Ensign Tankers (Leasing) Ltd. v. Stokes* (1992) 1 AC 655 made a review of the various tax avoidance cases from *Floor v. Davis* (1978) 2 All ER 1079 : (1978) Ch 295 to *Craven* (supra). In *Ensign Tankers*, a company became a partner of a limited partnership that had acquired the right to produce the film “Escape to Victory”. 75% of the cost of making the film was financed by way of a non-recourse loan from the production company, the company claimed the benefit of depreciation allowances based upon the full amount of the production cost. The House of Lords disallowed the claim, but allowed depreciation calculated on 25% of the cost for which the limited partnership was at risk. House of Lords examined the transaction as a whole and concluded that the limited partnership had only ‘incurred capital expenditure on the provision of machinery or plant’ of 25% and no more.

83. Lord Goff explained the meaning of “unacceptable tax avoidance” in *Ensign Tankers* and held that unacceptable tax avoidance typically involves the creation of *complex artificial structures* by which, as though by the wave of a magic wand, the taxpayer conjures out of the air a loss, or a gain, or expenditure, or whatever it may be, which otherwise would never have existed. This, of course, led to further debate as to what is “unacceptable tax avoidance” and “acceptable tax avoidance”.

84. House of Lords, later in *Inland Revenue*

Commissioner v. McGuckian (1997) BTC 346 said that the substance of a transaction may be considered if it is a tax avoidance scheme. Lord Steyn observed as follows:

> “While Lord Tomlin’s observations in the Duke of Westminster case [1936] A.C. 1 still point to a material consideration, namely the general liberty of the citizen to arrange his financial affairs as he thinks fit, they have ceased to be canonical as to the consequence of a tax avoidance scheme.”

McGuckian was associated with a tax avoidance scheme. The intention of the scheme was to convert the income from shares by way of dividend to a capital receipt. Schemes’ intention was to make a capital receipt in addition to a tax dividend. *Mc.Guckian* had affirmed the *fiscal nullity* doctrine from the approach of United Kingdom towards tax penalties which emerged from tax avoidance schemes. The analysis of the transaction was under the principles laid down in *Duke of Westminster*, since the entire transaction was not a tax avoidance scheme.

85. House of Lords in *MacNiven v. Westmoreland Investments Limited* (2003) 1 AC 311 examined the scope of Ramsay principle approach and held that it was one of purposive construction. In fact, Ramsay’s case and case of *Duke of Westminister* were reconciled by Lord Hoffmann in *MacNiven*. Lord Hoffmann clarified stating as follows

> ‘if the legal position is that tax is imposed by reference to a legally designed concept, such as stamp duty payable on a document which constitute conveyance or sale, the court cannot tax a transaction which uses no such document on the ground that it achieves the same economic effect. On the other hand, the legal position is that the tax is imposed by reference to a commercial concept, then to have regard to the business “substance” of the matter is not to ignore the legal position but to give effect to it.”

86. In other words, Lord Hoffmann reiterated that tax statutes must be interpreted "in a purposive manner to achieve the intention of the Legislature". *Ramsay* and *Dawson* are said to be examples of these fundamental principles.

87. Lord Hoffmann, therefore, stated that when Parliament intended to give a legal meaning to a statutory term or phrase, then Ramsay approach does not require or permit an examination of the commercial nature of the transaction, rather, it requires a consideration of the legal effect of what was done.

88. *MacNiven* approach has been reaffirmed by the House of Lord in *Barclays Mercantile Business Finance Limited v. Mawson* (2005) AC 685 (HL). In *Mawson, BGE,* an Irish Company had applied for a pipeline and it sold the pipeline to (BMBF) taxpayer for ? 91.3 Million. BMBF later leased the pipeline back to BGE which granted a sub-lease onwards to its UK subsidiary. BGE immediately deposited the sale proceeds as Barclays had no access to it for 31 years. Parties had nothing to loose with the transaction designed to produce substantial tax deduction in UK and no other economic consequence of any significance. Revenue denied BMBF's deduction for depreciation because the series of transactions amounted to a single composite transaction that did not fall within Section 24(1) of the Capital Cost Allowance Act, 1990. House of Lords, in a unanimous decision held in favour of the tax payer and held as follows" *driving principle in Ramsay's line of cases continues to involve a general rule of statutory interpretation and unblinked approach to the analysis of facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to a transaction, viewed realistically*.

89. On the same day, House of Lords had an occasion to consider the Ramsay approach in *Inland Revenue Commissioner v. Scottish Provident Institution* (2004 [1] WLR 3172). The question involved in *Scottish Provident Institution*

was whether there was "a debt contract for the purpose of Section 150A(1) of the Finance Act, 1994." House of Lords upheld the Ramsay principle and considered the series of transaction as a composite transaction and held that the composite transaction created no entitlement to securities and that there was, thus, no qualifying contract. The line drawn by House of Lords between *Mawson* and *Scottish Provident Institution* in holding that in one case there was a composite transaction to which statute applied, while in the other there was not.

90. Lord Hoffmann later in an article *"Tax Avoidance"* reported in (2005) BTR 197 commented on the judgment in BMBF as follows:

> "the primacy of the construction of the particular taxing provision and the illegitimacy of the rules of general application has been reaffirmed by the recent decision of the House in "BMBF". Indeed, it may be said that this case has killed off Ramsay doctrine as a special theory of revenue law and subsumed it within the general theory of the interpretation of statutes".

Above discussion would indicate *that a clear-cut distinction between tax avoidance and tax evasion is still to emerge in England and in the absence of any legislative guidelines, there bound to be uncertainty, but to say that the principle of Duke of Westminster has been exorcised in England is too tall a statement and not seen accepted even in England*. House of Lords in *McGuckian* and *MacNiven*, it may be noted, has emphasised that the *Ramsay* approach as a principle of *statutory interpretation* rather than an *over-arching anti avoidance doctrine* imposed upon tax laws. *Ramsay approach ultimately concerned with the statutory interpretation of a tax avoidance scheme and the principles laid down in Duke of Westminster, it cannot be said, has been given a complete go by Ramsay, Dawson or other judgments of the House of Lords*.

PART-III

INDO-MAURITIUS TREATY – AZADI BACHAO ANDOLAN

91. The Constitution Bench of this Court in *McDowell* (supra) examined at length the concept of tax evasion and tax avoidance in the light of the principles laid down by the House of Lords in several judgments like *Duke of Westminster, Ramsay, Dawson* etc. The scope of Indo-Mauritius Double Tax Avoidance Agreement (in short DTAA)], Circular No. 682 dated 30.3.1994 and Circular No. 789 dated 13.4.2000 issued by CBDT, later came up for consideration before a two Judges Bench of this Court in *Azadi Bachao Andolan*. Learned Judges made some observations with regard to the opinion expressed by Justice Chinnappa Reddy in a Constitution Bench judgment of this Court in *McDowell*, which created some confusion with regard to the understanding of the Constitution Bench judgment, which needs clarification. Let us, however, first examine the scope of the India-Mauritius Treaty and its follow-up.

92. India-Mauritius Treaty was executed on 1.4.1983 and notified on 16.12.1983. Article 13 of the Treaty deals with the taxability of capital gains. Article 13(4) covers the taxability of capital gains arising from the sale/transfer of shares and stipulates that "Gains derived by a resident of a Contracting State from the alienation of any property other than those mentioned in paragraphs 1, 2 and 3 of that Article, shall be taxable only in that State". Article 10 of the Treaty deals with the taxability of Dividends. Article 10(1) specifies that "Dividends paid by a company which is a resident of a Contracting State to a resident of other contracting State, may be taxed in that other State". Article 10(2) stipulates that "such dividend may also be taxed in the Contracting State of which the company paying the dividends is a resident but if the recipient was the beneficial owner of the dividends, the tax should not exceed; (a) 5% of the gross amount of the dividends if the recipient of the dividends holds at least 10% of the capital

of the company paying the dividends and (b) 15% of the gross amount of the dividends in all other cases.

93. CBDT issued Circular No. 682 dated 30.03.1994 clarifying that capital gains derived by a resident of Mauritius by alienation of shares of an Indian company shall be taxable only in Mauritius according to Mauritius Tax Law. In the year 2000, the Revenue authorities sought to deny the treaty benefits to some Mauritius resident companies pointing out that the *beneficial ownership* in those companies was outside Mauritius and thus the foremost purpose of investing in India via Mauritius was tax avoidance. Tax authorities took the stand that Mauritius was merely being used as a conduit and thus sought to deny the treaty benefits despite the absence of a limitation of benefits (LOB) clause in the Treaty. CBDT then issued Circular No. 789 dated 13.04.2000 stating that the Mauritius Tax Residency Certificate (TRC) issued by the Mauritius Tax Office was a sufficient evidence of tax response of that company in Mauritius and that such companies were entitled to claim treaty benefits.

94. Writ Petitions in public interest were filed before the Delhi High Court challenging the constitutional validity of the above mentioned circulars. Delhi High Court quashed Circular No. 789 stating that inasmuch as the circular directs the Income Tax authorities to accept as a certificate of residence issued by the authorities of Mauritius as sufficient evidence as regards the status of resident and beneficial ownership, was ultra vires the powers of CBDT. The Court also held that the Income Tax Office was entitled to lift the corporate veil in India to see whether a company was a resident of Mauritius or not and whether the company was paying income tax in Mauritius or not. The Court also held that the "Treaty Shopping" by which the resident of a third country takes advantage of the provisions of the agreement was illegal and necessarily to be forbidden. Union of India preferred appeal against the judgment of the Delhi High Court, before this Court. This Court in *Azadi Bachao*

Andolan allowed the appeal and Circular No. 789 was declared valid.

Limitation of Benefit Clause (LOB)

95. India Mauritius Treaty does not contain any Limitation of Benefit (LOB) clause, similar to the Indo-US Treaty, wherein Article 24 stipulates that benefits will be available if 50% of the shares of a company are owned directly or indirectly by one or more individual residents of a controlling state. LOB clause also finds a place in India-Singapore DTA. Indo Mauritius Treaty does not restrict the benefit to companies whose shareholders are non-citizens/residents of Mauritius, or where the beneficial interest is owned by non-citizens/residents of Mauritius, in the event where there is no justification in prohibiting the residents of a third nation from incorporating companies in Mauritius and deriving benefit under the treaty. *No presumption can be drawn that the Union of India or the Tax Department is unaware that the quantum of both FDI and FII do not originate from Mauritius but from other global investors situate outside Mauritius*. Maurtius, it is well known is incapable of bringing FDI worth millions of dollars into India. If the Union of India and Tax Department insist that the investment would directly come from Mauritius and Mauritius alone then the Indo-Mauritius treaty would be dead letter.

96. Mr. Aspi Chinoy, learned senior counsel contended that in the absence of LOB Clause in the India Mauritius Treaty, the scope of the treaty would be positive from Mauritius Special Purpose Vehicles (SPVs) created specifically to route investments into India, meets with our approval. We acknowledge that on a subsequent sale/transfer/disinvestment of shares by the Mauritian company, after a reasonable time, the sale proceeds would be received by the Mauritius Company as the registered holder/owner of such shares, such benefits could be sent back to the Foreign Principal/100% shareholder of Mauritius company either by way of a declaration of special

dividend by Mauritius company and/or by way of repayment of loans received by the Mauritius company from the Foreign Principal/shareholder for the purpose of making the investment. Mr. Chinoy is right in his contention that apart from DTAA, which provides for tax exemption in the case of capital gains received by a Mauritius company/shareholder at the time of disinvestment/exit and the fact that Mauritius does not levy tax on dividends declared and paid by a Mauritius company/ subsidiary to its Foreign Shareholders/Principal, there is no other reason for this quantum of funds to be invested from/ through Mauritius.

97. *We are, therefore, of the view that in the absence of LOB Clause and the presence of Circular No. 789 of 2000 and TRC certificate, on the residence and beneficial interest/ ownership, tax department cannot at the time of sale/ disinvestment/exit from such FDI, deny benefits to such Mauritius companies of the Treaty by stating that FDI was only routed through a Mauritius company*, by a company/principal resident in a third country; or the Mauritius company had received all its funds from a foreign principal/company; or the Mauritius subsidiary is controlled/managed by the Foreign Principal; or the Mauritius company had no assets or business other than holding the investment/shares in the Indian company; or the Foreign Principal/100% shareholder of Mauritius company had played a dominant role in deciding the time and price of the disinvestment/sale/transfer; or the sale proceeds received by the Mauritius company had ultimately been paid over by it to the Foreign Principal/ its 100% shareholder either by way of Special Dividend or by way of repayment of loans received; or the real owner/beneficial owner of the shares was the foreign Principal Company. Setting up of a WOS Mauritius subsidiary/SPV by Principals/genuine substantial long term FDI in India from/through Mauritius, pursuant to the DTAA and Circular No. 789 can never be considered to be set up for tax evasion.

TRC whether conclusive

98. LOB and *look through* provisions cannot be read into a tax treaty but the question may arise as to whether the TRC is so conclusive that the Tax Department cannot pierce the veil and *look at the* substance of the transaction. DTAA and Circular No. 789 dated 13.4.2000, in our view, would not preclude the Income Tax Department from denying the tax treaty benefits, if it is established, on facts, that the Mauritius company has been interposed as the owner of the shares in India, at the time of disposal of the shares to a third party, solely with a view to avoid tax without any commercial substance. *Tax Department, in such a situation, notwithstanding the fact that the Mauritian company is required to be treated as the beneficial owner of the shares under Circular No. 789 and the Treaty is entitled* to *look at* the entire transaction of sale as a whole and if it is established that the Mauritian company has been interposed as a device, it is open to the Tax Department to discard the device and take into consideration the real transaction between the parties , and the transaction may be subjected to tax. *In other words, TRC does not prevent enquiry into a tax fraud, for example, where an OCB is used by an Indian resident for round-tripping or any other illegal activities, nothing prevents the Revenue from looking into special agreements, contracts or arrangements made or effected by Indian resident or the role of the OCB in the entire transaction*.

99. *No court will recognise sham transaction or a colourable device or adoption of a dubious method to evade tax, but to say that the Indo-Mauritian Treaty will recognise FDI and FII only if it originates from Mauritius, not the investors from third countries, incorporating company in Mauritius, is pitching it too high, especially when statistics reveals that for the last decade the FDI in India was US$ 178 billion and, of this, 42% i.e. US$ 74.56 billion was through Mauritian route*. Presently, it is known, FII in India is Rs.450,000 crores, out of which Rs. 70,000 crores is from Mauritius. Facts, therefore,

clearly show that almost the entire FDI and FII made in India from Mauritius under DTAA does not originate from that country, but has been made by Mauritius Companies / SPV, which are owned by companies/individuals of third countries providing funds for making FDI by such companies/individuals not from Mauritius, but from third countries.

100. Mauritius, and India, it is known, has also signed a Memorandum of Understanding (MOU) laying down the rules for information, exchange between the two countries which provides for the two signatory authorities to assist each other in the detection of fraudulent market practices, including the insider dealing and market manipulation in the areas of securities transactions and derivative dealings. The object and purpose of the MOU is to track down transactions tainted by fraud and financial crime, not to target the bona fide legitimate transactions. Mauritius has also enacted stringent “Know Your Clients” (KYC) regulations and Anti-Money Laundering laws which seek to avoid abusive use of treaty.

101. Viewed in the above perspective, we also find no reason to import the *“abuse of rights doctrine”* (abus de droit) to India. The above doctrine was seen applied by the Swiss Court in A Holding Aps. (8 ITRL), unlike Courts following Common Law. That was a case where a Danish company was interposed to hold all the shares in a Swiss Company and there was a clear finding of fact that it was interposed for the sole purpose of benefiting from the Swiss-Denmark DTA which had the effect of reducing a normal 35% withholding tax on dividend out of Switzerland down to 0%. Court in that case held that the only reason for the existence of the Danish company was to benefit from the zero withholding tax under the tax treaty. On facts also, the above case will not apply to the case in hand.

102. Cayman Islands, it was contended, was a *tax heaven* and CGP was a *shell company*, hence, they have to be looked at with suspicion. We may, therefore, briefly examine what those

expressions mean and how they are understood in the corporate world.

TAX HAVENS, TREATY SHOPPING AND SHELL COMPANIES

103. Tax Havens" is not seen defined or mentioned in the Tax Laws of this country Corporate world gives different meanings to that expression, so also the Tax Department. The term "tax havens" is sometime described as a State with nil or moderate level of taxation and/or liberal tax incentives for undertaking specific activities such as exporting. The expression "tax haven" is also sometime used as a "secrecy jurisdiction. The term "Shell Companies" finds no definition in the tax laws and the term is used in its pejorative sense, namely as a company which exits only on paper, but in reality, they are investment companies. Meaning of the expression 'Treaty Shopping' was elaborately dealt with in *Azadi Bachao Andolan* and hence not repeated.

104. Tax Justice Network Project (U.K.), however, in its report published in September, 2005, stated as follows:

> "The role played by tax havens in encouraging and profiteering from tax avoidance, tax evasion and capital flight from developed and developing countries is a scandal of gigantic proportions".

The project recorded that one per cent of the world's population holds more than 57% of total global worth and that approximately US $ 255 billion annually was involved in using offshore havens to escape taxation, an amount which would more than plug the financing gap to achieve the Millennium Development Goal of reducing the world poverty by 50% by 2015. ("Tax Us If You Can" September 2005, 78 available at http:/www.taxjustice.net). Necessity of proper legislation for charging those types of transactions have already been emphasised by us.

Round Tripping

105. India is considered to be the most attractive investment destinations and, it is known, has received $37.763 billion in FDI and $29.048 billion in FII investment in the year to March 31, 2010. FDI inflows it is reported were of $ 22.958 billion between April 2010 and January, 2011 and FII investment were $ 31.031 billions. Reports are afloat that million of rupees go out of the country only to be returned as FDI or FII. Round Tripping can take many formats like under-invoicing and over-invoicing of exports and imports. Round Tripping involves getting the money out of India, say Mauritius, and then come to India like FDI or FII. Art. 4 of the Indo-Mauritius DTAA defines a 'resident' to mean any person, who under the laws of the contracting State is liable to taxation therein by reason of his domicile, residence, place of business or any other similar criteria. An Indian Company, with the idea of tax evasion can also incorporate a company off-shore, say in a Tax Haven, and then create a WOS in Mauritius and after obtaining a TRC may invest in India. Large amounts, therefore, can be routed back to India using TRC as a defence, but once it is established that *such an investment is black money or capital that is hidden, it is nothing but circular movement of capital known as Round Tripping; then TRC can be ignored, since the transaction is fraudulent and against national interest*.

106. *Facts stated above are food for thought to the legislature and adequate legislative measures have to be taken to plug the loopholes, all the same, a genuine corporate structure set up for purely commercial purpose and indulging in genuine investment be recognized*. However, if the fraud is detected by the Court of Law, it can pierce the corporate structure since fraud unravels everything, even a statutory provision, if it is a stumbling block, because legislature never intents to guard fraud. *Certainly, in our view, TRC certificate though can be accepted as a conclusive evidence for accepting status of residents as well as beneficial ownership*

for applying the tax treaty, it can be ignored if the treaty is abused for the fraudulent purpose of evasion of tax.

McDowell - WHETHER CALLS FOR RECONSDIERATION:

107. *McDowell* has emphatically spoken on the principle of Tax Planning. Justice Ranganath Mishra, on his and on behalf of three other Judges, after referring to the observations of Justice S.C. Shah in *CIT v. A. Raman and Co.* (1968) 1 SCC 10, *CIT v. B. M. Kharwar* (1969) 1 SCR 651, the judgments in *Bank of Chettinad Ltd. v. CIT* (1940) 8 ITR 522 (PC), *Jiyajeerao Cotton Mills Ltd. v. Commissioner of Income Tax and Excess Profits Tax, Bombay* AIR 1959 SC 270; *CIT v. Vadilal Lallubhai* (1973) 3 SCC 17 and the views expressed by Viscount Simon in *Latilla v. IRC.* 26 TC 107 : (1943) AC 377 stated as follows:

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

108. Justice Shah in *Raman* (supra) has stated that avoidance of tax liability by so arranging the commercial affairs that charge of tax is distributed is not prohibited and a tax payer may resort to a device to divert the income before it accrues or arises to him and the effectiveness of the device depends not upon considerations of morality, but on the operation of the Income Tax Act. Justice Shah made the same observation in *B.N. Kharwar* (supra) as well and after quoting a passage from the judgment of the Privy Council stated as follows :-

> "The Taxing authority is entitled and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of the relationship. But the legal effect of a transaction cannot be displaced by probing into the "substance of the transaction".

In *Jiyajeerao* (supra) also, this Court made the following observation:

> "Every person is entitled so to arrange his affairs as to avoid taxation, but the arrangement must be real and genuine and not a sham or make-believe."

109. In *Vadilal Lalubhai* (supra) this Court re-affirmed the principle of strict interpretation of the charging provisions and also affirmed the decision of the Gujarat High Court in *Sankarlal Balabhai v. ITO* (1975) 100 ITR 97 (Guj.), which had drawn a distinction between the legitimate avoidance and tax evasion. *Lalita's* case (supra) dealing with a tax avoidance scheme, has also expressly affirmed the principle that genuine arrangements would be permissible and may result in an assessee escaping tax.

110. Justice Chinnappa Reddy starts his concurring judgment in McDowell as follows:

> "While I *entirely agree* with my brother Ranganath Mishra, J. in the judgment proposed to be delivered by me, I wish to add a few paragraphs, particularly to *supplement* what he has said on the "fashionable" topic of tax avoidance."

(emphasis supplied)

Justice Reddy has, the above quoted portion shows, entirely *agreed* with Justice Mishra and has stated that he is only *supplementing* what Justice Mishra has spoken on tax avoidance. Justice Reddy, while agreeing with Justice Mishra and the other three judges, has opined that in the very country of its birth, the principle of Westminster has been given a decent burial and in that country where the phrase "tax avoidance" originated the judicial attitude towards tax avoidance has changed and the Courts are now concerning themselves not merely with the genuineness of a transaction, but with the intended effect of it for fiscal purposes. Justice Reddy also opined that no one can get away with the *tax avoidance project* with the mere statement that there is nothing illegal about it. Justice Reddy has also opined that the ghost of Westminster (in the words of Lord Roskill) has been exorcised in England. *In our view, what transpired in England is not the ratio of McDowell and cannot be and remains merely an opinion or view*.

111. Confusion arose (see Paragraph 46 of the judgment) when Justice Mishra has stated after referring to the concept of tax planning as follows:

> "On this aspect, one of us Chinnappa Reddy, J. has proposed a separate and detailed opinion with which we agree."

112. Justice Reddy, we have already indicated, himself has stated that he is entirely agreeing with Justice Mishra and has only supplemented what Justice Mishra has stated on Tax Avoidance, therefore, we have go by what Justice Mishra has spoken on tax avoidance.

113. Justice Reddy has depreciated the practice of setting up of Tax Avoidance Projects, in our view, rightly because the same is/was the situation in England and *Ramsay* and other judgments had depreciated the Tax Avoidance Schemes.

114. In our view, the ratio of the judgment is what is spoken by Justice Mishra for himself and on behalf of three other judges, on which Justice Reddy has agreed. Justice Reddy has clearly stated that he is only supplementing what Justice Mishra has said on Tax avoidance.

115. Justice Reddy has endorsed the view of Lord Roskill that the ghost of Westminster had been exorcised in England and that one should not allow its head rear over India. If one scans through the various judgments of the House of Lords in England, which we have already done, one thing is clear that it has been a cornerstone of law, that a tax payer is enabled to arrange his affairs so as to reduce the liability of tax and the fact that the motive for a transaction is to avoid tax does not invalidate it unless a particular enactment so provides (Westminster Principle). Needless to say if the arrangement is to be effective, it is essential that the transaction has some economic or commercial substance. Lord Roskill's view is not seen as the correct view so also Justice Reddy's, for the reasons we have already explained in earlier part of this judgment.

116. A five Judges Bench judgment of this Court in *Mathuram Agrawal v. State of Madhya Pradesh* (1999) 8 SCC 667, after referring to the judgment in *B.C. Kharwar* (supra) as well as the opinion expressed by Lord Roskill on *Duke of Westminster* stated that the subject is not to be taxed by inference or analogy, but only by the plain words of a statute applicable to the facts and circumstances of each case.

117. *Revenue cannot tax a subject without a statute to support and in the course we also acknowledge that every tax payer is entitled to arrange his affairs so that his taxes shall be as low as possible and that he is not bound to choose that pattern which will replenish the treasury*.Revenue's stand that the ratio laid down in McDowell is contrary to what has been laid down in *Azadi Bachao Andolan*, in our view, is unsustainable and, therefore, calls for no reconsideration by a larger branch.

PART-IV

CGP AND ITS INTERPOSITION

118. CGP's interposition in the HTIL Corporate structure and its disposition, by way of transfer, for exit, was for a commercial or business purpose or with an ulterior motive for evading tax, is the next question. *Parties, it is trite, are free to choose whatever lawful arrangement which will suit their business and commercial purpose, but the true nature of the transaction can be ascertained only by looking into the legal arrangement actually entered into and carried out*. Indisputedly, that the contracts have to be read holistically to arrive at a conclusion as to the real nature of a transaction. Revenue's stand was that the CGP share was a mode or mechanism to achieve a transfer of control, so that the tax be imposed on the transfer of control not on transfer of the CGP share. Revenue's stand, relying upon *Dawson* test, was that CGP's interposition in the Hutchison structure was an arrangement to deceive the Revenue with the object of hiding or rejecting the tax liability which otherwise would incur.

119. Revenue contends that the entire corporate structure be looked at as on artificial tax avoidance scheme wherein CGP was introduced into the structure at the last moment, especially when another route was available for HTIL to transfer its controlling interest in HEL to Vodafone. Further it was pointed out that the original idea of the parties was to sell shares in HEL directly but at the last moment the parties changed their mind and adopted a different route since HTIL wanted to declare a special dividend out of US $ 11 million for payment and the same would not have been possible if they had adopted Mauritian route.

120. Petitioner pointed out that if the motive of HTIL was only to save tax it had the option to sell the shares of Indian companies directly held Mauritius entities, especially when there is no LOB clause in India-Mauritius Treaty. Further, it was pointed out that if the Mauritius companies had sold the shares of HEL, then Mauritius companies would have continued to be

the subsidiary of HTIL, their account could have been consolidated in the hands of HTIL and HTIL would have accounted for the accounts exactly the same way that it had accounted for the accounts in HTIL BVI/nominated payee. Had HTIL adopted the Mauritius route, then it would have been cumbersome to sell the shares of a host of Mauritian companies.

121. CGP was incorporated in the year 1998 and the same became part of the Hutchison Corporate structure in the year 2005. Facts would clearly indicate that the CGP held shares in Array and Hutchison Teleservices (India) Holdings Limited (MS), both incorporated in Mauritius. HTIL, after acquiring the share of CGP (CI) in the year 1994 which constituted approximately 42% direct interest in HEL, had put in place various FWAs, SHAs for arranging its affairs so that it can also have interest in the functioning of HEL along with Indian partners.

122. Self centred operations in India were with 3GSPL an Indian company which held options through various FWAs entered into with Indian partners. *One of the tests to examine the genuineness of the structure is the "timing test" that is timing of the incorporation of the entities or transfer of shares etc. Structures created for genuine business reasons are those which are generally created or acquired at the time when investment is made, at the time where further investments are being made at the time of consolidation etc.*

123. HTIL preferred CGP route rather than adopting any other method (why ?) for which we have to examine whether HTIL has got any justification for adopting this route, for sound commercial reasons or purely for evasion of tax. In international investments, corporate structures are designed to enable a smooth transition which can be by way of divestment or dilution. Once entry into the structure is honourable, exits from the structure can also be honourable.

124. HTIL structure was created over a period of time and this was consolidated in 2004 to provide a working model by which HTIL could make best use of its investments and exercise control over and strategically influence the affairs of HEL. HTIL in its commercial wisdom noticed the disadvantage of preferring Array, which would have created problems for HTIL. Hutchison Teleservices (India) Mauritius had a subsidiary, namely 3GSPL which carried on the call centre business in India and the transfer of CGP share would give control over 3GSPL, an indirect subsidiary which was incorporated in the year 1999. It would also obviate problems arising on account of call and put options arrangements and voting rights enjoyed by 3GSPL. If Array was transferred, the disadvantage was that HTIL had to deal with call and put options of 3GSPL. In the above circumstances, HTIL in their commercial wisdom thought of transferring CGP share rather than going for any other alternatives. Further 3GSPL was also a party to various agreements between itself and the companies of AS, AG and IDFC Group. If Array had been transferred the disadvantage would be that the same would result in hiving off the call centre business from 3GSPL. Consolidation operations of HEL were evidently done in the year 2005 not for tax purposes but for commercial reasons and the contention that CGP was inserted at a very late stage in order to bring a pre tax entity or to create a transaction that would avoid tax, cannot be accepted.

125. The Revenue has no case that HTIL structure was a device or an artifice, but all along the contention was that CGP was interposed at the last moment and applying the *Dawson* test, it was contended that such an *artificially interposed device* be ignored, and applying *Ramsay* test of *purposive interpretation*, the transaction be taxed for gain. CGP, it may be noted, was already part of the HTIL's Corporate Structure and the decision taken to sell CGP (Share) so as to exit from the Indian Telecom Sector was not the fall out of a tax exploitation scheme, but a genuine commercial decision taking

into consideration the best interest of the investors and the corporate entity.

126. Principle of *Fiscal nullity* was applied by Vinelott, J. in favour of the assessee in *Dawson*, where the judge rejected the contention of the Crown that the transaction was hit by the *Ramsay* principle, holding that a transaction cannot be disregarded and treated as *fiscal nullity* if it has enduring legal consequences. Principle was again explained by Lord Brightman stating that the *Ramsay* test would apply not only where the steps are *pre-contracted*, but also they are *pre-ordained,* if there is no contractual right and in all likelihood the steps would follow. On *Fiscal nullity,* Lord Brightman again explained that there should be a *pre-ordained* series of transactions and there should be steps inserted that have no commercial purpose and the inserted steps are to be disregarded for fiscal purpose and, in such situations, Court must then *look at* the end result, precisely how the end result will be taxed will depend on terms of the taxing statute sought to be applied. *Sale of CGP share, for exiting from the Indian Telecommunication Sector, in our view, cannot be considered as pre-ordained transaction, with no commercial purpose, other than tax avoidance. Sale of CGP share, in our view, was a genuine business transaction, not a fraudulent or dubious method to avoid capital gains tax*.

SITUS OF CGP

127. Situs of CGP share stands where, is the next question. Law on situs of share has already been discussed by us in the earlier part of the judgment. Situs of shares situates at the place where the company is incorporated and/ or the place where the share can be dealt with by way of transfer. CGP share is registered in Cayman Island and materials placed before us would indicate that Cayman Island law, unlike other laws does not recognise the multiplicity of registers. Section 184 of the Cayman Island Act provides that the company may

be exempt if it gives to the Registrar, a declaration that "operation of an exempted company will be conducted mainly outside the Island". Section 193 of the Cayman Island Act expressly recognises that even exempted companies may, to a limited extent trade within the Islands. Section 193 permits activities by way of trading which are incidental of off shore operations also all rights to enter into the contract etc. The facts in this case as well as the provisions of the Caymen Island Act would clearly indicate that the CGP (CI) share situates in Caymen Island. The legal principle on which situs of an asset, such as share of the company is determined, is well settled. Reference may be made to the judgments in *Brassard v. Smith* [1925] AC 371, *London and South American Investment Trust v. British Tobacco Co. (Australia)* [1927] 1 Ch. 107. *Erie Beach Co. v. Attorney-General for Ontario,* 1930 AC 161 PC 10, *R. v. Williams* [1942] AC 541. Situs of CGP share, therefore, situates in Cayman Islands and on transfer in Cayman Islands would not shift to India.

PART-V

128. Sale of CGP, on facts, we have found was not the fall out of an artificial tax avoidance scheme or an artificial device, pre-ordained, or pre-conceived with the sole object of tax avoidance, but was a genuine commercial decision to exit from the Indian Telecom Sector.

129. HTIL had the following controlling interest in HEL before its exit from the Indian Telecom Sector:-

1. HTIL held its *direct equity interest* in HEL amounting approximately to 42% through eight Mauritius companies.

2. HTIL indirect subsidiary CGP(M) held 37.25% of equity interest in TII, an Indian Company, which in turn held 12.96% equity interest in HEL. CGP(M), as a result of its 37.25% interest in TII had an interest in several downstream companies which held interest in HEL, as a

result of which HTIL obtained indirect equity interest of 7.24% in HEL.

3. HTIL held in Indian Company Omega Holdings, an Indian Co., interest to the extent of 45.79% of share capital through HTIM which held shareholding of 5.11% in HEL, resulting in holding of 2.34% interest in the Indian Company HEL.

HTIL could, therefore, exercise its control over HEL, through the voting rights of its indirect subsidiary Array (Mauritius) which in turn controlled 42% shares through Mauritian Subsidiaries in HEL. Mauritian subsidiaries controlled 42% voting rights in HEL and HTIL could not however exercise voting rights as stated above, in HEL directly but only through indirect subsidiary CGP(M) which in turn held equity interest in TII, an Indian company which held equity interest in HEL. HTIL likewise through an indirect subsidiary HTI(M), which held equity interest in Omega an Indian company which held equity interest in HEL, could exercise only indirect voting rights in HEL.

130. HTIL, by holding CGP share, got control over its WOS Hutchison Tele Services (India) Holdings Ltd (MS). HTSH(MS) was having control over its WOS 3GSPL, *an Indian company which exercised voting rights in HEL. HTIL, therefore, by holding CGP share, had 52% equity interest, direct 42% and approximately 10% (pro rata) indirect in HEL and not 67% as contended by the Revenue*.

131. HTIL had 15% interest in HEL by virtue of FWAs, SHAs Call and Put Option Agreements and Subscription Agreements and not controlling interest as such in HEL. HTIL, by virtue of those agreements, had the following interests:-

(i) Rights (and Options) by providing finance and guarantee to Asim Ghosh Group of companies to exercise control over TII and indirectly over HEL through TII Shareholders Agreement and the

Centrino Framework Agreement dated 1.3.2006;

(ii) Rights (and Options) by providing finance and guarantee to Analjit Singh Group of companies to exercise control over TII and indirectly over HEL through various TII shareholders agreements and the N.D. Callus Framework Agreement dated 1.3.2006.

(iii) Controlling rights over TII through the TII Shareholder's Agreement in the form of rights to appoint two directors with veto power to promote its interest in HEL and thereby hold beneficial interest in 12.30% of the share capital of the in HEL.

(iv) Finance to SMMS to acquire shares in ITNL (formerly Omega) with right to acquire the share capital of Omega in future.

(v) Rights over ITNL through the ITNL Shareholder's Agreement, in the form of right to appoint two directors with veto power to promote its interests in HEL and thereby it held beneficial interest in 2.77% of the share capital of the Indian company HEL;

(vi) Interest in the form of loan of US$231 million to HTI (BVI) which was assigned to Array Holdings Ltd.;

(vii) Interest in the form of loan of US$ 952 million through HTI (BVI) utilized for purchasing shares in the Indian company HEL by the 8 Mauritius companies;

(viii) Interest in the form of Preference share capital in JKF and TII to the extent of US$ 167.5 million and USD 337 million respectively. These two companies hold 19.54% equity in HEL.

(ix) Right to do telecom business in India through joint venture;

(x) Right to avail of the telecom licenses in India and right to do business in India;

(xi) Right to use the Hutch brand in India;

(xii) Right to appoint/remove directors in the board of the Indian company HEL and its other Indian subsidiaries;

(xiii) Right to exercise control over the management and affairs of the business of the Indian company HEL (Management Rights);

(xiv) Right to take part in all the investment, management and financial decisions of the Indian company HEL;

(xv) Right to control premium;

(xvi) Right to consultancy support in the use of Oracle license for the Indian business;

Revenue's stand before us was that the SPA on a commercial construction brought about an *extinguishment* of HTIL's rights of *management and control* over HEL, resulting in transfer of capital asset in India. Further, it was pointed out that the assets, rights and entitlements are property rights pertaining to HTIL and its subsidiaries and the transfer of CGP share would have no effect on the Telecom operations in India, but for the transfer of the above assets, rights and entitlements. SPA and other agreements, if examined, as a whole, according to the Revenue, leads to the conclusion that the *substance* of the transaction was the transfer of various property rights of HTIL in HEL to Vodafone attracting capital gains tax in India. Further, it was pointed out that moment CGP share was transferred offshore, HTIL's right of control over HEL and its subsidiaries *stood extinguished,* thus leading to *income indirectly earned,* outside India through the medium of sale of the CGP share. All these issues have to be examined without forgetting the fact that we are dealing with a taxing statute and the Revenue has to bring home all its contentions within the four corners of taxing statute and not on assumptions and presumptions.

132. Vodafone on acquisition of CGP share got controlling interest of 42% over HEL/VEL through voting rights through eight Mauritian subsidiaries, the same was the position of HTIL as well. On acquiring CGP share, CGP has become a direct subsidiary of Vodafone, but both are legally independent entities. Vodafone does not own any assets of CGP. Management and the business of CGP vests on the Board of Directors of CGP but of course, Vodafone could appoint or remove members of the Board of Directors of CGP. On acquisition of CGP from HTIL , Array became an indirect subsidiary of Vodafone. Array is also a separate legal entity managed by its own Board of Directors. Share of CGP situates in Cayman Islands and that of Array in Mauritius. Mauritian entities which hold 42% shares in HEL became the direct and indirect subsidiaries of Array, on Vodafone purchasing the CGP share. *Voting rights, controlling rights, right to manage etc., of Mauritian Companies vested in those companies. HTIL has never sold nor Vodafone purchased any shares of either Array or the Mauritian subsidiaries, but only CGP, the share of which situates in Cayman Islands*. By purchasing the CGP share its situs will not shift either to Mauritius or to India, a legal issue, already explained by us. Array being a WOS of CGP, CGP may appoint or remove any of its directors, if it wishes by a resolution in the general body of the subsidiary, but CGP, Array and all Mauritian entities are separate legal entities and have de-centralised management and each of the Mauritian subsidiaries has its own management personnels.

133. Vodafone on purchase of CGP share got controlling

interest in the Mauritian Companies and the incident of transfer of CGP share cannot be considered to be two distinct and separate transactions, one shifting of the share and another shifting of the controlling interest. *Transfer of CGP share automatically results in host of consequences including transfer of controlling interest and that controlling interest as such cannot be dissected from CGP share without legislative intervention. Controlling interest of CGP over Array is an incident of holding majority shares and the control of Company vests in the voting power of its shareholders*. Mauritian entities being a WOS of Array, Array as a holding Company can influence the shareholders of various Mauritian Companies. Holding Companies like CGP, Array, may exercise control over the subsidiaries, whether a WOS or otherwise by influencing the voting rights, nomination of members of the Board of Directors and so on. On transfer of shares of the holding Company, the controlling interest may also pass on to the purchaser along with the shares. *Controlling interest might have percolated down the line to the operating companies but that controlling interest is inherently contractual and not a property right unless otherwise provided for in the statue.* Acquisition of shares, may carry the acquisition of controlling interest which is purely a commercial concept and the tax can be levied only on the *transaction* and not on its *effect.* Consequently, on transfer of CGP share to Vodafone, Vodafone got control over eight Mauritian Companies which owned shares in VEL totalling to 42% and that does not mean that the situs of CGP share has shifted to India for the purpose of charging capital gains tax.

134. Vodafone could exercise only indirect voting rights in VEL through its indirect subsidiary CGP(M) which held equity interests in TII, an Indian Company, which held equity interests in VEL. Similarly, Vodafone could exercise only indirect voting rights through HTI(M) which held equity interests in Omega, an Indian Company which in turn held equity interests in HEL. On

transfer of CGP share, Vodafone gets controlling interest in its indirect subsidiaries which are situated in Mauritius which have equity interests in TII and Omega, Indian Companies which are independent legal entities. *Controlling interest, which stood transferred to Vodafone from HTIL accompany the CGP share and cannot be dissected so as to be treated as transfer of controlling interest of Mauritian entities and then that of Indian entities and ultimately that of HEL.* Situs of CGP share, therefore, determines the transferability of the share and/or interest which flows out of that share including controlling interest. Ownership of shares, as already explained by us, carries other valuable rights like, right to receive dividend, right to transmit the shares, right to vote, right to act as per one's wish, or to vote in a particular manner etc; and on transfer of shares those rights also sail along with them.

135. Vodafone, on purchase of CGP share got all those rights, and the price paid by Vodafone is for all those rights, in other words, *control premium* paid, not over and above the CGP share, but is the integral part of the price of the share. On transfer of CGP share situated in Cayman Islands, the entire rights, which accompany stood transferred not in India, but offshore and the facts reveal that the offshore holdings and arrangements made by HTIL and Vodafone were for sound commercial and legitimate tax planning, not with the motive of evading tax.

136. Vodafone, on purchase of CGP share also got control over its WOS, HTSH(M) which is having control over its WOS, 3GSPL, an Indian Company which exercised voting rights in HEL. 3GSPL, was incorporated on 16.03.99 and run call centre business in India. The advantage of transferring share of CGP rather than Array was that it would obviate the problems arising on account of the <u>call</u> and <u>put</u> agreements and *voting rights* enjoyed by 3GSPL. 3GSPL was also a party to various agreements between itself and Companies of AS, AG and IDFC Groups. AS , AG & IDFC have agreed to retain their

shareholdings with full control including voting rights and dividend rights. In fact, on 02.03.2007 AG wrote to HEL confirming that his indirect equity or beneficial interest in HEL worked out to be as 4.68% and it was stated, *he was the beneficiary of full dividend rights attached to his shares and he had received credit support and primarily the liability for re-payment was of his company*. Further, it was also pointed out that he was the exclusive beneficial owner of his shares in his companies, enjoying full and exclusive rights to vote and participate in any benefits accruing to those shares. On 05.03.2007 AS also wrote to the Government on the same lines.

137. Vodafone, on acquisition of CGP, is in a position to replace the directors of holding company of 3GSPL so as to get control over 3GSPL. 3GSPL has call option as well as the obligation of the put option. Rights and obligations which flow out of call and put options have already been explained by us in the earlier part of the judgment. *Call* and *put options* are contractual rights and do not sound in property and hence they cannot be, in the absence of a statutory stipulation, considered as capital assets. Even assuming so, they are in favour of 3GSPL and continue to be so even after entry of Vodafone.

138. We have extensively dealt with the terms of the various FWAs, SHAs and Term Sheets and in none of those Agreements HTIL or Vodafone figure as parties. SHAs between Mauritian entities (which were shareholders of the Indian operating Companies) and other shareholders in some of the other operating companies in India held shares in HEL related to the management of the subsidiaries of AS, AG and IDFC and did not relate to the management of the affairs of HEL and HTIL was not a party to those agreements, and hence there was no question of assigning or relinquishing any right to Vodafone.

139. IDFC FWA of August 2006 also conferred upon 3

GSPL only call option rights and a right to nominate a buyer if investors decided to exit as long as the buyer paid a fair market value. June 2007 Agreement became necessary because the composition of Indian investors changed with some Indian investors going out and other Indian investors coming in. On June 2007, changes took place within the Group of Indian investors, in that SSKI and IDFC went out leaving IDF alone as the Indian investor. Parties decided to keep June 2007 transaction to effectuate their intention within the broad contours of June 2006 FWA. On *06.06.2007 FWA has also retained the rights and options in favour of 3GSPL but conferred no rights on Vodafone and Vodafone was only a confirming party to that Agreement*. Call and put options, we have already mentioned, were the subject matter of three FWAs viz., Centrino, N.D. Callus, IDFC and in Centrino and N.D. Callus FWAs, neither HTIL was a party, nor was Vodafone. HTIL was only a confirming party in IDFC FWA, so also Vodafone. Since HTIL, and later Vodafone were not parties to those SHAs and FWAs, we fail to see how they are bound by the terms and conditions contained therein, so also the rights and obligations that flow out of them. HTIL and Vodafone have, of course, had the interest to see the SHAs and FWAs, be put in proper place but that interest cannot be termed as property rights, attracting capital gains tax.

140. We have dealt with the legal effect of exercising call option, put option, tag along rights, ROFR, subscription rights and so on and all those rights and obligations we have indicated fall within the realm of contract between various shareholders and interested parties and in any view, are not binding on HTIL or Vodafone. Rights (and options) by providing finance and guarantee to AG Group of Companies to exercise control over TII and indirectly over HEL through TII SHA and Centrino FWA dated 01.03.2006 were only contractual rights, as also the revised SHAs and FWAs entered into on the basis of SPA. Rights (and options) by providing finance and guarantee to AS

Group of Companies to exercise control over TII and indirectly over HEL through various TII SHAs and N.D. Callus FWA dated 01.03.2006 were also contractual rights, and continue to be so on entry of Vodafone.

141. Controlling right over TII through TII SHAs in the form of right to appoint two Directors with veto power to promote its interest in HEL and thereby held beneficial interest in 12.30% of share capital in the HEL are also contractual rights. Finance to SMMS to acquire shares in ITNL (ultimately Omega) with right to acquire share capital of Omega were also contractual rights between the parties. On transfer of CGP share to Vodafone corresponding rearrangement were made in the SHAs and FWAs and Term Sheet Agreements in which Vodafone was not a party.

142. SPA, through the transfer of CGP, indirectly conferred the benefit of put option from the transferee of CGP share to be enjoyed in the same manner as they were enjoyed by the transferor and the revised set of 2007 agreements were exactly between the parties that is the beneficiary of the put options remained with the downstream company 3 GSPL and the counter-party of the put option remained with AG/AS Group Companies.

143. Fresh set of agreements of 2007 as already referred to were entered into between IDFC, AG, AS, 3 GSPL and Vodafone andin fact, those agreements were irrelevant for the transfer of CGP share. FWAs with AG and AS did not constitute transaction documents or give rise to a transfer of an asset, so also the IDFC FWA. All those FWAs contain some adjustments with regard to certain existing rights, however, the options, the extent of rights in relation to options, the price etc. all continue to remain in place as they stood. Even if they had not been so entered into, all those agreements would have remained in place because they were in favour of 3GSPL, subsidiary of CGP.

144. The High Court has reiterated the common law principle that the controlling interest is an incident of the ownership of the share of the company, something which flows out of holding of shares and, therefore, not an identifiable or distinct capital asset independent of the holding of shares, but at the same time speaks of change in the controlling interest of VEL, without there being any transfer of shares of VEL. Further, the High Court failed to note on transfer of CGP share, there was only transfer of certain off-shore loan transactions which is unconnected with underlying controlling interest in the Indian Operating Companies. The other rights, interests and entitlements continue to remain with Indian Operating Companies and there is nothing to show they stood transferred *in law*.

145. The High Court has ignored the vital fact that as far as the put options are concerned there were pre-existing agreements between the beneficiaries and counter parties and fresh agreements were also on similar lines. Further, the High Court has ignored the fact that Term Sheet Agreement with Essar had nothing to do with the transfer of CGP, which was a separate transaction which came about on account of independent settlement between Essar and Hutch Group, for a separate consideration, unrelated to the consideration of CGP share. The High Court committed an error in holding that there were some rights vested in HTIL under SHA dated 5.7.2003 which is also an agreement, conferring no right to any party and accordingly none could have been transferred. The High Court has also committed an error in holding that some rights vested with HTIL under the agreement dated 01.08.2006, in fact, that agreement conferred right on Hutichison Telecommunication (India) Ltd., which is a Mauritian Company and not HTIL, the vendor of SPA. The High court has also ignored the vital fact that FIPB had elaborately examined the nature of call and put option agreement rights and found no right in presenti has been transferred to Vodafone and that as and

when rights are to be transferred by AG and AS Group Companies, it would specifically require Government permission since such a sale would attract capital gains, and may be independently taxable. We may now examine whether the following rights and entitlements would also amount to capital assets attracting capital gains tax on transfer of CGP share.

Debts/Loans through Intermediaries

146. SPA contained provisions *for assignment of loans either at Mauritius or Cayman Islands* and all loans were assigned at the face value. Clause 2.2 of the SPA stipulated that HTIL shall procure the assignment of and purchaser agrees to accept an assignment of loans free from encumbrances together with all rights attaching or accruing to them at completion. Loans were defined in the SPA to mean, all inter-company loans owing by CGP and Array to a vendor group company including accrued or unpaid interest, if any, on the completion date. HTIL warranted and undertook that, as on completion, loans set out in Part IV of Schedule 1 shall be the only indebtedness owing by the Wider group company to any member of the vendor group. Vendor was obliged to procure that the loans set out in Part IV of Schedule 1 shall not be repaid on or before completion and further, that any loan in addition to those identified will be non-interest bearing. Clause 7.4 of the SPA stipulated that any loans in addition to those identified in Part IV of Schedule 1 of the SPA would be non-interest bearing and on terms equivalent to the terms of those loans identified in Part IV of Schedule 1 of the SPA. The sum of such indebtedness comprised of:

(a) US$ 672,361,225 (Loan 1) – reflected in a Loan Agreement (effective date of loan: 31 December 2006; date of Loan Agreement: 28 April 2007);

(b) HK$ 377,859,382.40 (Loan 2) – reflected in a Loan Agreement (effective date of Loan 31st December 2006; date of Loan Agreement: 28 April 2007) [(i)

+ (ii): US$ 1,050,220,607.40]

(c) US$ 231,111,427.41 (Loan 3) – reflected in a Receivable Novation Agreement i.e. HTM owed HTI BVI Finance such sum, which Array undertook to repay in pursuance of an inter-group loan restructuring, which was captured in such Receivable Novation Agreement dated 28 April 2007.

HTI BVI Finance Limited, Array and Vodafone entered into a Deed of Assignment on 08.05.2007 pertaining to the Array indebtedness. On transfer of CGP shares, Array became a subsidiary of VIHBV. The price was calculated on a gross asset basis (enterprise value of underlying assets), the intra group loans would have to be assigned at face value, since nothing was payable by VIHBV for the loans as they had already paid for the gross assets.

147. CGP had acknowledged indebtedness of HTI BVI Finance Limited in the sum of US$161,064,952.84 as at the date of completion. The sum of such indebtedness was comprised of:

(a) US$ 132,092,447.14, reflected in a Loan Agreement (effective date of loan: 31 December 2006; date of Loan Agreement: 28 April 2007)

(b) US$ 28,972,505.70, reflected in a Loan Agreement (effective date of loan: 14 February 2007; date of Loan Agreement: 15 February 2007).

HTI BVI Finance Limited Limited, CGP and the Purchaser entered into the Deed of Assignment on 08.05.2007 pertaining to the CGP indebtedness.

148. In respect of Array Loan No. 3 i.e. US$ 231,111,427.41, the right that was being assigned was not the

right under a Loan Agreement, but the right to receive payment from Array pursuant to the terms of a Receiveable Novation Agreement dated 28.04.2007 between Array, HTIL and HTI BVI Finance Limited. Under the terms of the Receiveable Novation Agreement, HTIL's obligation to repay the loan was novated from HTI BVI Finance to Array, the consideration for this novation was US$ 231,111,427.41 payable by Array to HTI BVI Finance Limited. It was this right to receive the amount from Array that was assigned to VHI BV under the relevant Loan Assignment. It was envisaged that, between signing and completion of the agreement, there would be a further loan up to US$ 29.7 million between CGP (as borrower) from a Vendor Group Company (vide Clause 6.4 of the SPA) and the identity of the lender has not been identified in the SPA. The details of the loan were ultimately as follows:

Borrower	Lender	Amount of Loan	Date of Agreement	Effective date of Agreement
CGP	HTI (BVI) Finance Limited	US$28,972,505.70	15 February 2007	14 February 2007

Array and CGP stood outside of obligation to repay an aggregate US$ 1,442,396.987.61 to HTI BVI Finance Limited and VHIBV became the creditor of Array and CGP in the place and stepped off a HTI BVI Finance Limited on 8.5.2007 when VHIBV stepped into the shoes of HTI BVI Finance Limited.

149. Agreements referred to above including the provisions for assignments in the SPA, indicate that all loan agreements and assignments of loans took place outside India at face value and, hence, there is no question of transfer of any capital assets out of those transactions in India, attracting capital gains tax.

Preference Shares:

150. Vodafone while determining bid price had taken into consideration, inter alia¸ its ownership of redeemable preference shares in TII and JFK. Right to preference shares or rights thereto cannot be termed as transfer in terms of Section 2(47) of the Act. Any agreement with TII, Indian partners contemplated fresh investment, by subscribing to the preference shares were redeemable only by accumulated profit or by issue of fresh capital and hence any issue of fresh capital cannot be equated to the continuation of old preference shares or transfer thereof.

NON COMPETE AGREEMENT

151. SPA contains a Non Compete Agreement which is a pure Contractual Agreement, a negative covenant, the purpose of which is only to see that the transferee does not immediately start a compete business. At times an agreement provides that a particular amount to be paid towards non-compete undertaking, in sale consideration, which may be assessable as business income under Section 28(va) of the IT Act, which has nothing to do with the transfer of controlling interest. However, a non-compete agreement as an adjunct to a share transfer, which is not for any consideration, cannot give rise to a taxable income. In our view, a non-compete agreement entered into outside India would not give rise to a taxable event in India. An agreement for a non-compete clause was executed offshore and, by no principle of law, can be termed as "property" so as to come within the meaning of capital gains taxable in India in the absence of any legislation.

HUTCH BRAND

152. HTIL did not have any direct interest in the brand. The facts would indicate that brand/Intellectual Property Right were held by Hutchison Group Company based in Luxemburg. SPA

only assured Vodafone that they would not have to overnight cease the use of the Hutch brand name, which might have resulted in a disruption of operations in India. The bare license to use a brand free of charge, is not itself a "property" and, in any view, if the right to property is created for the first time and that too free of charge, it cannot give rise to a chargeable income. Under the SPA, a limited window of license was given and it was expressly made free of charge and, therefore, the assurance given by HTIL to Vodafone that the brand name would not cease overnight, cannot be described as "property" rights so as to consider it as a capital asset chargeable to tax in India.

ORACLE LICENSE:

153. Oracle License was an accounting license, the benefit of which was extended till such time VEL replaced it with its own accounting package. There is nothing to show that this accounting package, which is a software, was transferred to Vodafone. In any view, this license cannot be termed as a capital asset since it has never been transferred to the petitioner.

154. We, therefore, conclude that on transfer of CGP share, HTIL had transferred only 42% equity interest it had in HEL and approximately 10% (pro-rata) to Vodafone, the transfer was off-shore, money was paid off-shore, parties were no-residents and hence there was no transfer of a capital asset situated in India. Loan agreements extended by virtue of transfer of CGP share were also off-shore and hence cannot be termed to be a transfer of asset situated in India. Rights and entitlements referred to also, in our view, cannot be termed as capital assets, attracting capital gains tax and even after transfer of CGP share, all those rights and entitlements remained as such, by virtue of various FWAs, SHAs, in which neither HTIL nor Vodafone was a party.

155. Revenue, however, wanted to bring in all those rights and entitlements within the ambit of Section 9(1)(i) on a liberal construction of that Section applying the principle of purposive interpretation and hence we may examine the scope of Section 9.

PART VI

SECTION 9 AND ITS APPLICATION

156. Shri Nariman, submitted that this Court should give a purposive construction to Section 9(1) of the Income Tax Act when read along with Section 5(2) of the Act. Referring extensively to the various provisions of the Income Tax Act, 1922, and also Section 9(1)(i), Shri Nariman contended that the expression "transfer" in Section 2(47) read with Section 9 has to be understood as an inclusive definition comprising of both direct and *indirect transfers* so as to expand the scope of Section 9 of the Act. Shri Nariman also submitted that the object of Section 9 would be defeated if one gives undue weightage to the term "situate in India", which is intended to tax a non-resident who has a source in India. Shri Nariman contended that the effect of SPA is not only to effect the transfer of a solitary share, but transfer of *rights and entitlements* which falls within the expression "capital asset" defined in Section 2(14) meaning property of any kind held by the assessee. Further, it was stated that the word "property" is also an expression of widest amplitude and would include anything capable of being raised *including beneficial interest*. Further, it was also pointed out that the SPA extinguishes all the rights of HTIL in HEL and such extinguishment would fall under Section 2(47) of the Income Tax Act and hence, a capital asset.

157. Shri Harish Salve, learned senior counsel appearing for the petitioner, submitted that Section 9(1)(i) of the Income Tax Act deals with taxation on income "deemed to accrue or arise" in India through the transfer of a capital asset situated in

India and stressed that the source of income lies where the transaction is effected and not where the economic interest lies and pointed out that there is a distinction between a legal right and a contractual right. Referring to the definition of "transfer" in Section 2(47) of the Income Tax Act which provides for extinguishment, it was submitted, that the same is attracted for transfer of a legal right. Placing reliance on the judgment of this Court in *Commissioner of Income Tax v. Grace Collins and Others,* 248 ITR 323, learned senior counsel submitted that SPA has not relinquished any right of HTIL giving rise to capital gains tax in India.

158. Mr. S.P. Chenoy, senior counsel, on our request, argued at length, on the scope and object of Section 9 of the Income Tax Act. Learned senior counsel submitted that the first four clauses/parts of Section 9(1)(i) deal with taxability of revenue receipts, income arising through or from holding an asset in India, income arising from the transfer of an asset situated in India. Mr. Chenoy submitted that only the last limb of Section 9(1)(i) deals with the transfer of a capital asset situated in India and can be taxed as a capital receipt. Learned senior counsel submitted to apply Section 9(1)(i) the capital asset must situate in India and cannot by a process of interpretation or construction extend the meaning of that section to cover *indirect transfers* of capital assets/properties situated in India. Learned senior counsel pointed out that there are cases, where the assets/shares situate in India are not transferred, but where the shares of foreign company holding/owning such shares are transferred.

159. Shri Mohan Parasaran, Additional Solicitor General, submitted that on a close analysis of the language employed in Section 9 and the various expressions used therein, would self-evidently demonstrate that Section 9 seeks to capture income arising directly or indirectly from direct or indirect transfer. Shri Parasaran submitted, if a holding company

incorporated offshore through a maze of subsidiaries, which are investment companies incorporated in various jurisdictions indirectly contacts a company in India and seeks to divest its interest, by the sale of shares or stocks, which are held by one of its upstream subsidiaries located in a foreign country to another foreign company and the foreign company step into the shoes of the holding company, then Section 9 would get attracted. Learned counsel submitted that it would be a case of indirect transfer and a case of income accruing indirectly in India and consequent to the sale of a share outside India, there would be a transfer or divestment or extinguishment of holding company's rights and interests, resulting in transfer of capital asset situated in India.

160. Section 9 of the Income Tax Act deals with the incomes which shall be deemed to accrue or arise in India. Under the general theory of nexus relevant for examining the territorial operation of the legislation, two principles that are generally accepted for imposition of tax are: (a) Source and (b) Residence. Section 5 of the Income Tax Act specifies the principle on which tax can be levied. Section 5(1) prescribes "residence" as a primary basis for imposition of tax and makes the global income of the resident liable to tax. Section 5(2) is the source based rule in relation to residents and is confined to: income that has been received in India; and income that has accrued or arisen in India or income that is deemed to accrue or arise in India. In the case of Resident in India, the total income, according to the residential status is as under:

(a) Any income which is received or deemed to be received in India in the relevant previous year by or on behalf of such person;

(b) Any income which accrues or arises or is deemed to accrue or arise in India during the relevant previous year; and

(c) Any income which accrues or arises outside India during the relevant previous year.

In the case of Resident but not Ordinarily Resident in India, the principle is as follows:

(a) Any income which is received or deemed to be received in India in the relevant previous year by or on behalf of such person;

(b) Any income which accrues or arises or is deemed to accrue or arise in India to him during the relevant previous year; and

(c) Any income which accrues or arises to him outside India during the relevant previous year, if it is derived from a business controlled in or a profession set up in India.

In the case of Non-Resident, income from whatsoever source derived forms part of the total income. It is as follows:

(a) Any income which is received or deemed to be received in India during the relevant previous year by or on behalf of such person; and

(b) Any income which accrues or arises or is deemed to accrue or arise to him in India during the relevant previous year.

161. Section 9 of the Income Tax Act extends its provisions to certain incomes which are deemed to accrue or arise in India. Four kinds of income which otherwise may not fall in Section 9, would be deemed to accrue or arise in India, which are (a) a business connection in India; (b) a property in India; (c) an establishment or source in India; and (d) transfer of a capital asset in India.

Income deemed to accrue or arise in India

Section 9

(1) The following incomes shall be deemed to accrue or arise in India :-

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through orfrom any asset or source of income in India, or through the transfer of a capital asset situate in India.

[Explanation 1] – For the purposes of this clause –

(a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India ;

(b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export;

(c) in the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India;]

(a) in the case of a non-resident, being –

(1) an individual who is not a citizen of India; or

(2) a firm which does not have any partner who is

a citizen of India who is resident in India; or

(3) a company which does not have any shareholder who is a citizen of India or who is resident in India."

162. The meaning that we have to give to the expressions "either directly or indirectly", "transfer", "capital asset" and "situated in India" is of prime importance so as to get a proper insight on the scope and ambit of Section 9(1)(i) of the Income Tax Act. The word "transfer" has been defined in Section 2(47) of the Income Tax Act. The relevant portion of the same is as under:

"**2(47)** "Transfer", in relation to a capital asset, includes.-

(i) the sale, exchange or relinquishment of the asset; or

(ii) the extinguishment of any rights therein; or

(iii) the compulsory acquisition thereof under any law; or

(iv) in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment; or

xxx xxx xxx

xxx xxx xxx"

The term "capital asset" is also defined under Section 2(14) of the Income Tax Act, the relevant portion of which reads as follows:

"**2(14)** "Capital asset" means property of any kind held by an assessee, whether or not connected with the business or profession, but does not include-

(i) any stock-in-trade, consumable stores or raw materials held for the purposes of his business or profession;

xxx xxx xxx

xxx xxx xxx"

163. The meaning of the words "either directly or indirectly", when read textually and contextually, would indicate that they govern the words those precede them, namely the words "all income accruing or arising". The section provides that all income accruing or arising, whether directly or indirectly, would fall within the category of income that is deemed to accrue or arise in India. Resultantly, it is only where factually it is established that there is either a business connection in India, or a property in India, or an asset or source in India or a capital asset in India, the transfer of which has taken place, the further question arises whether there is any income deeming to accrue in India from those situations. In relation to the expression "through or from a business connection in India", it must be established in the first instance that (a) there is a non-resident; (b) who has a business connection in India; and (c) income arises from this business connection.

164. Same is the situation in the case of income that "arises through or from a property in India", i.e. (a) there must be, in the first instance, a property situated in India; and (b) income must arise from such property. Similarly, in the case of "transfer of a capital asset in India", the following test has to be applied: (a) there must be a capital asset situated in India, (b) the capital asset has to be transferred, and (c) the transfer of this asset must yield a gain. The word 'situate', means to set, place, locate. The words "situate in India" were added in Section 9(1)(i) of the Income Tax Act pursuant to the recommendations of the 12th Law Commission dated 26.9.1958.

165. Section 9 on a plain reading would show, it refers to a property that yields an income and that property should have the situs in India and it is the income that arises through or from that property which is taxable. *Section 9, therefore, covers only income arising from a transfer of a capital asset situated in India and it does not purport to cover income arising from the indirect transfer of capital asset in India*.

SOURCE

166. Revenue placed reliance on "Source Test" to contend that the transaction had a deep connection with India, i.e. ultimately to transfer control over HEL and hence the source of the gain to HTIL was India.

167. Source in relation to an income has been construed to be where the transaction of sale takes place and not where the item of value, which was the subject of the transaction, was acquired or derived from. HTIL and Vodafone are off-shore companies and since the sale took place outside India, applying the source test, the source is also outside India, unless legislation ropes in such transactions.

168. Substantial territorial nexus between the income and the territory which seeks to tax that income, is of prime importance to levy tax. Expression used in Section 9(1)(i) is "source of income in India" which implies that income arises from that source and there is no question of *income arising indirectly* from a source in India. Expression used is "source of income in India" and not "from a source in India". Section 9 contains a "deeming provision" and in interpreting a provision creating a legal fiction, the Court is to ascertain for what purpose the fiction is created, but in construing the fiction it is not to be extended beyond the purpose for which it is created, or beyond the language of section by which it is created. [See *C.I.T. Bombay City II v. Shakuntala* (1962) 2 SCR 871, *Mancheri Puthusseri Ahmed v. Kuthiravattam Estate Receiver*

(1996) 6 SCC 185].

169. Power to impose tax is essentially a legislative function which finds in its expression Article 265 of the Constitution of India. Article 265 states that no tax shall be levied except by authority of law. Further, it is also well settled that the subject is not to be taxed without clear words for that purpose; and also that every Act of Parliament must be read according to the natural construction of its words. Viscount Simon quoted with approval a passage from Rowlatt, J. expressing the principle in the following words:

> "In a taxing Act one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used. [Cape Brandy Syndicate v. IRC (1921) 1 KB 64, P. 71 (Rowlatt,J.)]"

170. In *Ransom (Inspector of Tax) v. Higgs* 1974 3 All ER 949 (HL), Lord Simon stated that it may seem hard that a cunningly advised tax-payer should be able to avoid what appears to be his equitable share of the general fiscal burden and cast it on the shoulders of his fellow citizens. *But for the Courts to try to stretch the law to meet hard cases (whether the hardship appears to bear on the individual tax-payer or on the general body of tax-payers as represented by the Inland Revenue) is not merely to make bad law but to run the risk of subverting the rule of law itself*. The proper course in construing revenue Acts is to give a fair and reasonable construction to their language without leaning to one side or the other but keeping in mind *that no tax can be imposed without words clearly showing an intention to lay the burden and that equitable construction of the words is not permissible* [*Ormond Investment Co. v. Betts* (1928) All ER Rep 709 (HL)], a principle entrenched in our jurisprudence as well. In *Mathuram Aggarwal* (supra), this Court relied on the judgment

in *Duke of Westminster* and opined that the charging section has to be strictly construed. An invitation to purposively construe Section 9 applying *look through* provision without legislative sanction, would be contrary to the ratio of *Mathuram Aggarwal***.**

171. Section 9(1)(i) covers only income arising or accruing directly or indirectly or through the transfer of a capital asset situated in India. Section 9(1)(i) cannot by a process of "interpretation" or "construction" be extended to cover "*indirect transfers*" of capital assets/property situate in India.

172. *On transfer of shares of a foreign company to a non-resident off-shore, there is no transfer of shares of the Indian Company, though held by the foreign company, in such a case it cannot be contended that the transfer of shares of the foreign holding company, results in an extinguishment of the foreign company control of the Indian company and it also does not constitute an extinguishment and transfer of an asset situate in India*. Transfer of the foreign holding company's share off-shore, cannot result in an extinguishment of the holding company right of control of the Indian company nor can it be stated that the same constitutes extinguishment and transfer of an asset/ management and control of property situated in India.

173. The Legislature wherever wanted to tax income which arises indirectly from the assets, the same has been specifically provided so. For example, reference may be made to Section 64 of the Indian Income Tax Act, which says that in computing the total income of an individual, there shall be included all such income as arises *directly or indirectly*: to the son's wife, of such individual, from *assets transferred directly or indirectly* on and after 1.6.73 to the son's wife by such individual otherwise than for adequate consideration. The same was noticed by this Court in *CIT v. Kothari (CM),* (1964) 2 SCR 531. Similar expression like "from asset transfered directly or indirectly", we find in Sections 64(7) and (8) as well. On a comparison of Section 64 and Section 9(1)(i) what is

discernible is that the Legislature has not chosen to extend Section 9(1)(i) to *"indirect transfers"*. Wherever "indirect transfers" are intended to be covered, the Legislature has expressly provided so. The words "either directly or indirectly", textually or contextually, cannot be construed to govern the words that follow, but must govern the words that precede them, namely the words "all income accruing or arising". The words "directly or indirectly" occurring in Section 9, therefore, relate to the relationship and connection between a non-resident assessee and the income and these words cannot and do not govern the relationship between the transaction that gave rise to income and the territory that seeks to tax the income. In other words, when an assessee is sought to be taxed in relation to an income, it must be on the basis that it arises to that assessee directly or it may arise to the assessee indirectly. In other words, for imposing tax, it must be shown that there is specific nexus between earning of the income and the territory which seeks to lay tax on that income. Reference may also be made to the judgment of this Court in *Ishikawajma-Harima Heavy Industries Ltd. v. Director of Income Tax, Mumbai* (2007) 3 SCC 481 and *CIT v. R.D. Aggarwal* (1965) 1 SCR 660.

174. *Section 9 has no "look through provision" and such a provision cannot be brought through construction or interpretation of a word 'through' in Section 9. In any view, "look through provision" will not shift the situs of an asset from one country to another. Shifting of situs can be done only by express legislation*. *Federal Commission of Taxation v. Lamesa Holdings BV (LN)* – (1998) 157 A.L.R. 290 gives an insight as to how "look through" provisions are enacted. Section 9, in our view, has no inbuilt "look through mechanism".

175. Capital gains are chargeable under Section 45 and their computation is to be in accordance with the provisions that follow Section 45 and there is no notion of indirect transfer in Section 45.

176. Section 9(1)(i), therefore, in our considered opinion, will not apply to the transaction in question or on the rights and entitlements, stated to have transferred, as a fall out of the sale of CGP share, since the Revenue has failed to establish both the tests, Resident Test as well the Source Test.

177. Vodafone, whether, could be proceeded against under Section 195(1) for not deducting tax at source and, alternatively, under Section 163 of the Income Tax Act as a representative assessee, is the next issue.

SECTION 195 AND OFFSHORE TRANSACTIONS

178. Section 195 provides that any person responsible for making any payment to a non-resident which is chargeable to tax must deduct from such payment, the income tax at source. Revenue contended that if a non-resident enters into a transaction giving rise to income chargeable to tax in India, the necessary nexus of such non-resident with India is established and the machinary provisions governing the collection of taxes in respect of such chargeable income will spring into operation. Further, it is also the stand of the Revenue that the person, who is a non-resident, and not having a physical presence can be said to have a presence in India for the purpose of Section 195, if he owns or holds assets in India or is liable to pay income tax in India. Further, it is also the stand of the Revenue that once chargeability is established, no further requirements of nexus needs to be satisfied for attracting Section 195.

179. Vodafone had "presence" in India, according to the Revenue at the time of the transaction because it was a Joint Venture (JV) Partner and held 10% equity interest in Bharti Airtel Limited, a listed company in India. Further, out of that 10%, 5.61% shares were held directly by Vodafone itself. Vodafone had also a right to vote as a shareholder of Bharati Airtel Limited and the right to appoint two directors on the Board of Directors of Bharti Airtel Limited. Consequently, it was stated

that Vodafone had a *presence* by reason of being a JV Partner in HEL on completion of HEL's acquisition. Vodafone had also entered into Term Sheet Agreement with Essar Group on 15.03.2007 to regulate the affairs of VEL which was restated by a fresh Term Sheet Agreement dated 24.08.2007, entered into with Essar Group and formed a JV Partnership in India. Further, Vodafone itself applied for IFPB approval and was granted such approval on 07.05.2007. On perusal of the approval, according to the Revenue, it would be clear that Vodafone had a *presence* in India on the date on which it made the payment because of the approval to the transaction accorded by FIPB. Further, it was also pointed out that, in fact, Vodafone had presence in India, since by mid 1990, it had entered into a JV arrangement with RPG Group in the year 1994-95 providing cellular services in Madras, Madhya Pradesh circles. After parting with its stake in RPG Group, in the year 2003, Vodafone in October, 2005 became a 10% JV Partner in HEL. Further, it was pointed out that, in any view, Vodafone could be treated as a *representative assessee* of HTIL and hence, notice under Section 163 was validly issued to Vodafone.

180. Vodafone has taken up a specific stand that "tax presence" has to be viewed in the context of the transaction that is subject to tax and not with reference to an entirely unrelated matter. Investment made by Vodafone group in Bharti Airtel would not make all entities of Vodafone group of companies subject to the Indian Law and jurisdiction of the Taxing Authorities. "Presence", it was pointed out, be considered in the context of the transaction and not in a manner that brings a non-resident assessee under jurisdiction of Indian Tax Authorities. Further, it was stated that a "tax presence" might arise where a foreign company, on account of its business in India, becomes a resident in India through a permanent establishment or the transaction relates to the permanent establishment.

181. Vodafone group of companies was a JV Partner in Bharti Airtel Limited which has absolutely no connection whatsoever with the present transaction. The mere fact that the Vodafone group of companies had entered into some transactions with another company cannot be treated as its presence in a totally unconnected transaction.

182. To examine the rival stand taken up by Vodafone and the Revenue, on the interpretation of Section 195(1) it is necessary to examine the scope and ambit of Section 195(1) of the Income Tax Act and other related provisions. For easy reference, we may extract Section 195(1) which reads as follows:

> "**Section 195. OTHER SUMS.-** (1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest or any other sum chargeable under the provisions of this Act (not being income chargeable under the head "Salaries" shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force :
>
> Provided that in the case of interest payable by the Government or a public sector bank within the meaning of clause (23D) of section 10 or a public financial institution within the meaning of that clause, deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode:
>
> Provided further that no such deduction shall be made in respect of any dividends referred to in section 115-O.
>
> Explanation: For the purposes of this section, where any interest or other sum as aforesaid is credited to any account, whether called "Interest payable account" or "Suspense account" or by any other name, in the books

of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly."

Section 195 finds a place in Chapter XVII of the Income Tax Act which deals with collection and recovery of tax. Requirement to deduct tax is not limited to deduction and payment of tax. It requires compliance with a host of statutory requirements like Section 203 which casts an obligation on the assessee to issue a certificate for the tax deducted, obligation to file return under Section 200(3), obligation to obtain "tax deduction and collection number" under Section 203A etc. Tax deduction provisions enables the Revenue to collect taxes in advance before the final assessment, which is essentially meant to make tax collection easier. The Income Tax Act also provides penalties for failure to deduct tax at source. If a person fails to deduct tax, then under Section 201 of the Act, he can be treated as an assessee in default. Section 271C stipulates a penalty on the amount of tax which has not been deducted. Penalty of jail sentence can also be imposed under Section 276B. Therefore, failure to deduct tax at source under Section 195 may attract various penal provisions.

183. Article 246 of the Constitution gives Parliament the authority to make laws which are extra-territorial in application. Article 245(2) says that no law made by the Parliament shall be deemed to be invalid on the ground that it would have extra territorial operation. Now the question is whether Section 195 has got extra territorial operations. It is trite that laws made by a country are intended to be applicable to its own territory, but that presumption is not universal unless it is shown that the intention was to make the law applicable extra territorially. We have to examine whether the presumption of territoriality holds good so far as Section 195 of the Income Tax Act is concerned and is there any reason to depart from that presumption.

184. A literal construction of the words "any person responsible for paying" as including non-residents would lead to absurd consequences. A reading of Sections 191A, 194B, 194C, 194D, 194E, 194I, 194J read with Sections 115BBA, 194I, 194J would show that the intention of the Parliament was first to apply Section 195 only to the residents who have a tax presence in India. It is all the more so, since the person responsible has to comply with various statutory requirements such as compliance of Sections 200(3), 203 and 203A.

185. The expression "any person", in our view, looking at the context in which Section 195 has been placed, would mean any person who is a resident in India. This view is also supported, if we look at similar situations in other countries, when tax was sought to be imposed on non-residents. One of the earliest rulings which paved the way for many, was the decision in *Ex Parte Blain; In re Sawers* (1879) LR 12 ChD 522 at 526, wherein the Court stated that "if a foreigner remain abroad, if he has never come into this country at all, it seems impossible to imagine that the English Legislature could ever have intended to make such a person subject to particular English Legislation." In *Clark (Inspector of Taxes) v. Oceanic Contractors Inc.* (1983) 1 ALL ER 133, the House of Lords had to consider the question whether chargeability has ipso facto sufficient nexus to attract TDS provisions. A TDS provision for payment made outside England was not given extra territorial application based on the principle of statutory interpretation. Lord Scarman, Lord Wilberforce and Lord Roskill held so on behalf of the majority and Lord Edmond Davies and Lord Lowry in dissent. Lord Scarman said :

> "unless the contrary is expressly enacted or so plainly implied as to make it the duty of an English court to give effect to it, United Kingdom Legislation is applicable only to British subjects or to foreigners who by coming into this country, whether for a long or short time, have made themselves during that time subject to English jurisdiction."

The above principle was followed in Agassi v. Robinson [2006] 1 WLR 2126.

186. This Court in *CIT v. Eli Lilly and Company (India) P. Ltd.* (2009) 15 SCC 1 had occasion to consider the scope of Sections 192, 195 etc. That was a case where Eli Lilly Netherlands seconded expatriates to work in India for an India-incorporated joint venture (JV) between Eli Lilly Netherlands and another Indian Company. The expatriates rendered services only to the JV and received a portion of their salary from the JV. The JV withheld taxes on the salary actually paid in India. However, the salary costs paid by Eli Lilly Netherlands were not borne by the JV and that portion of the income was not subject to withholding tax by Eli Lilly or the overseas entity. In that case, this Court held that the chargeability under Section 9 would constitute sufficient nexus on the basis of which any payment made to non-residents as salaries would come under the scanner of Section 192. But the Court had no occasion to consider a situation where salaries were paid by non-residents to another non-resident. Eli Lilly was a part of the JV and services were rendered in India for the JV. In our view, the ruling in that case is of no assistance to the facts of the present case since, here, both parties were non-residents and payment was also made offshore, unlike the facts in Eli Lilly where the services were rendered in India and received a portion of their salary from JV situated in India.

187. In the instant case, indisputedly, CGP share was transferred offshore. Both the companies were incorporated not in India but offshore. Both the companies have no income or fiscal assets in India, leave aside the question of transferring, those fiscal assets in India. Tax presence has to be viewed in the context of transaction in question and not with reference to an entirely unrelated transaction. *Section 195, in our view, would apply only if payments made from a resident to another non-resident and not between two non-residents situated outside India. In the present case, the transaction was*

between two non-resident entities through a contract executed outside India. Consideration was also passed outside India. That transaction has no nexus with the underlying assets in India. In order to establish a nexus, the legal nature of the transaction has to be examined and not the *indirect transfer of rights and entitlements* in India. Consequently, Vodafone is not legally obliged to respond to Section 163 notice which relates to the treatment of a purchaser of an asset as a representative assessee.

PART-VIII

CONCLUSION:

188. I, therefore, find it difficult to agree with the conclusions arrived at by the High Court that the sale of CGP share by HTIL to Vodafone would amount to transfer of a capital asset within the meaning of Section 2(14) of the Indian Income Tax Act and the rights and entitlements flow from FWAs, SHAs, Term Sheet, loan assignments, brand license etc. form integral part of CGP share attracting capital gains tax. Consequently, the demand of nearly Rs.12,000 crores by way of capital gains tax, in my view, would amount to imposing capital punishment for capital investment since it lacks authority of law and, therefore, stands quashed and I also concur with all the other directions given in the judgment delivered by the Lord Chief Justice.

R.P. Appeal allowed.

IMTIYAZ AHMAD
v.
STATE OF UTTAR PRADESH & ORS.
(Criminal Appeal Nos. 254-262 of 2012)

FEBRUARY 1, 2012

[ASOK KUMAR GANGULY AND T.S. THAKUR, JJ.]

Administration of Justice

Stay by High Courts of investigations and trials - Resulting in pendency of such cases for long - Held: The fact finding exercise directed by Supreme Court has revealed a problem of serious concern - It is simply unacceptable for a case to remain pending for three decades under any circumstances, and more so when the pendency is a consequence of the stay proceedings granted by High Court - Unduly long delay has the effect of bringing about blatant violation of the Rule of Law and adverse impact on the common man's access to justice - A person's access to justice is a guaranteed fundamental right under the Constitution and, particularly, Article 21 - Access to Justice must be defined in terms of ensuring that legal and judicial outcome is just and equitable - The steps taken by the Government of India to ensure speedy justice and to reduce delay, brought to the notice of the Court - Directions given by Supreme Court with regard to exercise of extra-ordinary power by High Courts to grant stay of investigations and trials - Directions also given to the Law Commission which itself is seized with the issue and is making investigation having regard to its terms of reference - Matter to appear before the appropriate Bench for consideration of the recommendations of the Law Commission and for further directions - Constitution of India, 1950 - Articles 21, 136 and 142.

R. Ramachandra Rav v. State of Karnataka, **(2002) 4 SCC 578 - referred to.**

Delcourt v. Belgium **[1970] ECHR 1 - referred to.**

14th Report of the Law Commission and Nature of Judicial Process **by Justice D.M. Dharmadhikari (2002) 6 SCC (Jour) 1 - referred to.**

United Nations Development Programme, **Access to Justice - Practice Note (2004);** *William H. Taft, The Delays of the Law, Yale Law Journal.* **Vo1.18. No.1 (Nov., 1908, p.28);** *Belekar Memorial Lecture Series,* **Lecture delivered on August 31, 2002;** *Roscoe Pound, Social Justice and Legal Justice* **(Address delivered to the Allegheny County Bar Association, April 5, 1912;** *The Rule of Law* **by Tom Bingham, p. 85 - referred to.**

International Covenant on Civil and Political Rights **(ICCPR), Article 14(3);** *European Charter on Fundamental Rights,* **Article 47;** *European Convention on Human Rights and Fundamental Freedoms,* **Article 6; ECHR Article 6(1);** *Universal Declaration of Human Rights,* **Articles 8 and 16 and** *South Africa's Constitution* **- referred to.**

Report of Lord Woolf submitted to Lord Chancellor in England: *Final Report to the Lord Chancellor on the Civil Justice System in England and Wales (Lord Woolf's Report),* **1996, Chapter 21, para 1 - referred to.**

Case Law Reference:

[1970] ECHR 1	**referred to**	**para 46**
(2002) 4 SCC 578	**referred to**	**para 51**

CRIMINAL APPELLATE JURISDICTION : Criminal Appeal No. 254-262 of 2012.

From the Judgment & Order dated 09.4.2003, 29.4.2003, 30.4.2003, 10.10.2003, 7.5.2004, 26.5.2005, 19.9.2006, 27.9.2006, 6.10.2006 and 18.12.2008 of the High Court of Judicature at Allahabad in CRLWP No. 1786 of 2003.

H.P. Raval, ASG, Gopal Subramaniam, Ratnakar Dash, T.A. Khan, Padma Laxmi Nigam, B.V. Balram Das, Sandeep S. Karhail, B.P. Singh Dhakray, Shakti Singh Dhakray, D.B. Raj Vohra, Rajeev K. Dubey, Kamlendra Mishra, T.G. Narayanan Nair, K.N. Madhusoodhanan, Krishanand Pandeya, Amrendra Kr. Choubey, Anitha Shenoy for the appearing parties.

The Order of the Court was delivered by

O R D E R

GANGULY, J.

Leave granted.

1. Heard learned counsel for the parties, including the learned Amicus Curiae.

2. In these appeals, this Court is concerned with a case where orders were passed by the High Court on several dates after the registration of FIR and on stay order being granted, investigation, and framing of charges or trial thereafter in the matter remained pending in the High Court for a long period of time. The stay order dated 9.4.03 and several orders dated 29.4.03, 30.4.03, 10.10.03, 7.5.04, 26.5.05, 19.9.06, 27.9.06, 6.10.06 & 18.12.08 of the High Court passed thereafter have been impugned in these appeals.

3. The questions which crop up in this case are of serious magnitude and transcend the immediate facts in the appeal and are of great national importance.

4. These appeals are directed against a batch of interlocutory orders passed by a learned Single Judge of

Allahabad High Court in Criminal Writ Petition No. 1786/2003 pending before the learned Judge.

5. It appears that by order dated 9.4.2003, the learned Single Judge admitted the writ petition filed by respondent Nos. 2 and 3 herein and also stayed the order dated 7.12.2002 passed by the Additional Chief Judicial Magistrate, Gautam Budh Nagar whereby direction had been given for registration of case against the said respondents. Thereafter, the matter has been listed on various days before the High Court but the matter was getting adjourned. As on the date of filing of the SLP, the writ petition had been kept pending for six years.

6. The SLP came up for hearing before this Court on 8.1.2010. This Court was very greatly concerned about the manner in which criminal investigation and trial have been stayed by the High court and also being aware of the fact that similar cases are happening in several High Courts in India wanted a serious consideration of the issues and appointed Mr. Gopal Subramanium, Senior Advocate (at that time Solicitor General of India) to assist the Court as Amicus Curiae.

7. The Court also issued a direction dated 8.1.2010 to the Registrars General/Registrars of all the High Courts in the country to furnish a report containing statistics of cases pending in the respective High Courts in which the proceedings have been stayed at the stage of registration of FIR, investigation, framing of charges and/or trial in exercise of power under Article 226 of the Constitution or Sections 482 and/or 397 of the Code of Criminal Procedure. The report was to deal with the following types of cases:

(a) murder,

(b) rape,

(c) kidnapping, and

(d) dacoity.

8. In response to the above direction, most of the High Courts submitted their reports. Two High Courts, Sikkim and Himachal Pradesh, reported that they do not have any such pending criminal cases of the types mentioned above. The reports submitted by different High Courts disclosed that altogether there were large number of such cases pending. Such pendency of cases was analyzed by the Amicus Curiae with the valuable assistance of Dr. Pronab Sen, Secretary and Dr. G.C. Manna, Deputy Director in the Ministry of Statistics and Programme Implementation.

9. The important findings arrived at after the analysis of the data are as under:

(a) Out of the four categories of cases, murder cases were found to be the most common type, accounting for 45% of all the cases.

(b) About one-fourth of all the cases pending are for 2 to 4 years from the date of stay order. Nearly 8% of the cases are, however, pending for 6 years or more.

(c) In most of the cases in different High Courts, the duration for which the case is pending varies from 1 to 4 years. It is seen that 34 out of 201 cases in Patna High Court and 33 out of 653 cases in Allahabad High Court are pending for 8 years or more.

10. About total pendency, in the report dated 12.4.10 filed by the Amicus, the following position emerges. Table 1 below shows the total number of cases pending in each High Court and the percentage share of the total pendency.

TABLE 1: TOTAL PENDENCY

High Court	Number of criminal cases by type					% share of High Court in total number of cases
	Murder	Rape	Kidna-napping	Dac-oity	All	
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Allahabad	144	100	341	68	653	28.6
Andhra Pradesh	46	8	2	4	60	2.6
Bihar	92	36	42	31	201	8.8
Bombay	14	5	4	6	29	1.3
Chhattisgarh	4	0	0	1	5	0.2
Delhi	4	5	2	0	11	0.5
Gauhati	6	5	2	8	21	0.9
Gujarat	56	9	34	16	115	5.0
J & K	4	4	6	0	14	0.6
Jharkhand	18	11	12	0	41	1.8
Karnataka	11	4	4	3	22	1.0
Kerala	12	2	5	1	20	0.9
Kolkata	431	209	21	48	709	31.1
Madhya Pradesh	10	14	1	5	30	1.3
Madras	0	1	2	0	3	0.1
Orissa	111	40	26	10	187	8.2

Punjab & Haryana	17	9	5	1	32	1.4
Rajasthan	23	11	17	5	56	2.5
Uttarakhand	18	19	24	10	71	3.1
All	1021	492	550	217	2280	100

11. It may be seen that the Hon'ble Calcutta High Court has the highest percentage share (31.1%) in total number of cases. It is followed by the Hon'ble High Courts of Allahabad (28.6%), Patna (8.8%) and Orissa (8.2%). Thus, these four High Courts taken together account for 76.9% of all the pendency.

12. Table 2 gives the distribution of all cases and the period for which the cases are pending in each High Court.

TABLE 2: DURATION OF PENDENCY

High court	Duration for which pending								
	Nil	<6m	6m–1y	1-2y	2-4y	4-6y	6-8y	≥8y	All
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Allahabad	1	38	126	190	158	90	17	33	653
Andhra Pradesh	0	16	16	17	11	0	0	0	60
Bihar	70	14	11	33	27	8	4	34	201
Bombay	0	1	6	8	6	3	2	3	29
Chhattisgarh	0	1	0	0	0	1	2	1	5
Delhi	0	1	2	4	0	3	1	0	11
Gauhati	0	3	5	4	3	0	6	0	21
Gujarat	0	8	6	34	46	20	1	0	115
J & K	0	5	2	3	4	0	0	0	14
Jharkhand	0	7	4	2	9	3	9	7	41
Karnataka	9	4	3	5	0	1	0	0	22
Kerala	0	1	0	1	5	13	0	0	20
Kolkata	7	40	104	135	209	176	38	0	709
Madhya Pradesh	0	2	6	2	12	6	1	1	30
Madras	0	1	0	1	1	0	0	0	3
Orissa	0	9	37	52	60	18	4	7	187
Punjab & Haryana	0	10	9	4	6	1	1	1	32
Rajasthan	0	8	8	11	22	6	0	1	56
Uttarakhand	0	7	10	9	21	20	3	1	71
All	87	176	355	515	600	369	89	89	2280

13.The category wise distribution is as follows:

TABLE 3: CATEGORYWISE DISTRIBUTION

Type of Case	Duration for which pending								
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	Nil	<6m	6m–1y	1-2y	2-4y	4-6y	6-8y	≥8y	All
Murder	25	65	132	182	309	211	43	54	1021
Rape	25	46	83	111	127	68	21	11	492
Kidnapping	16	51	120	156	116	67	12	12	550
Dacoity	21	14	20	66	48	23	13	12	217
All	87	176	355	515	600	369	89	89	2280

14. It is clear from the above that out of the four categories, murder cases account for nearly 45% of the total pendency. This

share increases if only the oldest pending cases are considered. Out of the 178 cases pending for 6 years or more, 97 are murder cases – i.e. a share of almost 55%.

15. In that report indications were also given about the frequency of listing of cases by different High Courts.

16. On the hypothesis that if a case is listed frequently, it indicated that the matter was being actively considered by the High court, data was also called for on the number of times the case was listed after the grant of the stay order.

17. The following table gives the average number of times a matter was listed for hearing after the grant of stay order.

High Court	Total number of cases	Average number of times the matter was listed per case
Allahabad	653	4.0
Andhra Pradesh	60	3.4
Bihar	201	21.7
Bombay	29	5.1
Chhattisgarh	5	4.3
Delhi	11	12.2
Gauhati	21	17.0
Gujarat	115	13.4
J & K	14	7.7
Jharkhand	41	3.5
Karnataka	22	5.0
Kerala	20	11.4
Kolkata	709	N/A
Madhya Pradesh	30	3.0
Madras	3	2.3
Orissa	187	5.8
Punjab & Haryana	32	8.8
Rajasthan	56	7.9
Uttarakhand	71	3.1
All	2280	6.1

18. However, the above analysis was not pursued any further, since there was no way of ascertaining which of the hearings were effective and which were non-effective. Hence, it could be misleading to draw any conclusions from this data.

19. On the basis of the aforesaid data it is clear that problems which the administration of justice faces today is of serious dimensions. Pendency is merely a localized problem, in the sense that it affects some High Courts far more than others. As seen above, just four High Courts in this country amount for 76.9% of the pendency. This may well be because of various social, political and economic factors, which are beyond the scope of the current enquiry by this Court.

20. It is a matter of serious concern that 41% of the cases have been pending for 2-4 years, and 8% (approximately 1 out of every 12 cases) have been pending for more than six years.

21. After considering the first report by the Amicus, this Court passed the following order on 3.5.2010:-

"The suggestions given by the Solicitor General have been considered. But before passing any order, we deem it proper to request learned counsel representing Allahabad High Court to place before the Court total number of cases in which power under Article 226 of the Constitution of India or Section 482 of the Code of Criminal Procedure has been exercised and the proceedings of the criminal case have been stayed at the stage of investigation or trial."

22. Pursuant to the above order, the Allahabad High Court furnished information of a total of 10,541 cases where power under Article 226 of the Constitution of India or Section 482 of the Code of Criminal Procedure has been exercised and the proceedings of the criminal case have been stayed at the stage of investigation or trial. Pursuant to a request of the Amicus Curiae, the Allahabad High Court also furnished the above data in electronic form.

23. The data was then analyzed by the Amicus Curiae with the help of Dr. T.C.A. Anant (the current Secretary) and Dr. G.C. Manna, Deputy Director General in the Ministry of Statistics and Programme Implementation. Then a second report was prepared and placed for the consideration of this Court.

24. Important findings from the second report are:-

"Out of the data for 10,541 cases received, data for 10,527 cases could be meaningfully analysed (as the rest had some missing elements). The important findings in respect of these are:

(a) As high as 9% of the cases have completed-more than twenty years since the date of stay order.

(b) Roughly 21 % of the cases have completed more than ten years.

(c) Average pendency per case (counted from the date of

stay order till July 26, 2010) works out to be around 7.4 years.

(d) Charge-sheet was found to be the most prominent stage where the cases were stayed with almost 32% of the cases falling under this category. The next two prominent stages are found to be "appearance" and "summons", with each comprising 19% of the total number of cases. (If "appearance" and "summons" are considered interchangeable, then they would collectively account for the maximum of stay orders."

25. Table below gives the duration for which cases have been pending since the date of the stay order:

No. of years passed	**Number of cases**	**Percentage of cases**
0	763	7.2
1	1250	11.9
2	1272	12.1
3	1024	9.7
4-5	2003	19.0
6-7	1125	10.7
8-10	920	8.7
11-15	577	5.5
16-20	648	6.2
21-25	631	6.0
More than 25	314	3.0
All	**10527**	**100.0**

26. A perusal of that information reveals that shockingly thirty-two cases have been pending for thirty years or more.

27. The data was also analyzed to ascertain the stage of the proceedings at which stay order was granted. Table below may be seen:-

Stage at which proceeding stayed	**Number of cases**	**Percentage of cases**
Chargesheet	3365	32.0
Appearance	2016	19.2
Summons	1951	18.5
"Further proceedings stayed"	563	5.3
Before charge	380	3.6
Trial	330	3.1
Evidence	323	3.1
Complaints	315	3.0
Cognizance	245	2.3
Disposal	237	2.3
Issue of notice	178	1.7
Others	624	5.9
All	**10527**	**100.0**

28. As stated in the First Report and Second Report, the fact-finding exercise directed by this court has revealed a problem of serious concern. It is respectfully submitted that it is simply unacceptable for a case to remain pending for three

decades under any circumstances, and more so when the pendency is a consequence of the stay proceedings granted by the High Court.

29. Thereafter, vide Order dated 26.08.2010, this Court was of the view that the existing infrastructure in the High Court's and District Court's must be improved and had directed that a comprehensive exercise should be undertaken to prepare the system in which all the cases instituted in the Court are listed for hearing without undue delay and some arrangement be made for monitoring of the listing and disposal of the cases. As a pilot project, the system is to be first implemented in the Allahabad High Court.

30. Thereafter, meetings were held between the officers of NIC, the Ministry of Statistics, the Allahabad High Court and the Amicus Curiae and efforts were made to develop the comprehensive system that the Court has directed. Another Report was filed by the Amicus Curiae setting out the steps taken by the Allahabad High Court, the Central Government and also certain suggestions given by Dr. G.C. Manna, Director General, Ministry of Statistics, who had been requested to visit the High Court to interact with the officials there to see how a better system of listing and tracking cases could be developed.

31. Thereafter, vide Orders dated 14.07.2011 and 17.08.2011, this Court again called for status reports from all the High Courts as to what steps had been taken specifically in the context of this case, in order to expeditiously dispose of matters where proceedings are stayed at the stage of registration of FIR, investigation, framing of charges or trial. Status reports were furnished by some of the High Courts and reports from other High Courts were awaited.

32. Then, vide Order dated 29.09.2011, this Court observed that considering the larger issues which are involved in this case which virtually have a direct impact on administration of justice, it was fit and proper to implead the

Central Government in this proceeding.

33. It is submitted that the issues being considered in this case have far reaching implications for maintaining of rule of law. Where investigation/trial is stayed for a long time, even if the stay is ultimately vacated, the subsequent investigation/trial may not be very fruitful for the simple reason, that evidence may no longer be available. Witnesses may not be able to recall the events properly, and some may have moved away or even died. Even the parties to the litigation may not survive. Unduly long delay has the effect of bringing about blatant violation of the rule of law and adverse impact on the common man's access to justice. A person's access to justice is a guaranteed fundamental right under the Constitution and particularly Article 21. Denial of this right undermines public confidence in the justice delivery system and incentivises people to look for short-cuts and other fora where they feel that justice will be done quicker. In the long run, this also weakens the justice delivery system and poses a threat to Rule of Law.

34. It may not be out of place to highlight that access to justice must not be understood in a purely quantitative dimension. Access to justice in an egalitarian democracy must be understood to mean qualitative access to justice as well. Access to justice is, therefore, much more than improving an individual's access to courts, or guaranteeing representation. It must be defined in terms of ensuring that legal and judicial outcomes are just and equitable (See United Nations Development Programme, Access to Justice - Practice Note (2004)].

35. The present case discloses the need to reiterate that 'Access to Justice' is vital for the Rule of Law, which by implication includes the right of access to an Independent Judiciary. It is submitted that the stay of investigation or trial for significant periods of time runs counter to the principle of Rule of Law, wherein the rights and aspirations of citizens are intertwined with expeditious conclusion of matters. It is further

submitted that delay in conclusion of criminal matters signifies a restriction on the right of access to justice itself, thus amounting to a violation of the citizens' rights under the Constitution, in particular under Article 21.

36. In a very important address to the Virginia Bar Association in 1908, William H. Taft observed that one reason for delay in the lower courts is the disposition of judges to wait an undue length of time in the writing of their opinions or judgments. [See William H. Taft, The Delays of the Law, Yale Law Journal. Vo1.18. No.1 (Nov., 1908), pp.28-39)]. The Judge should deliver the judgment immediately upon the close of the argument. It is almost of as much importance that the court of first instance should decide promptly as that it should decide right. It should be noted that everything which tends to prolong or delay litigation between individuals, or between individuals and State or Corporation, is a great advantage for that litigant who has the longer purse. The man whose rights are involved in the decision of the legal proceeding is much prejudiced in a fight through the courts, if his opponent is able, by reason of his means, to prolong the litigation and keep him for years out of what really belongs to him.

37. Dispatch in the decision making process by Court is one of the great expectations of the common man from the judiciary. A sense of confidence in the Courts is essential to maintain a fabric of order and liberty for a free people. Delay in disposal of cases would destroy that confidence and do incalculable damage to the society; that people would come to believe that inefficiency and delay will drain even a just judgment of its value; that people who had long been exploited in the small transactions of daily life come to believe that courts cannot vindicate their legal rights against fraud and overreaching; that people would come to believe that the law - in the larger sense cannot fulfil its primary function to protect them and their families in their homes, at their work place and on the public streets. [See Belekar Memorial Lecture Series, organized by High

Court Bar Association, Nagpur. Lecture delivered on August 31, 2002]

38. Merely widening the access to justice is not enough to secure redress to the weaker sections of the community. Post Independence, it was evident that litigation in India was getting costlier and there was agonizing delay in the process. After the adoption of the Constitution and creation of a Welfare State, the urgency of some structural changes in the justice delivery system was obviously a major requirement. In the 14th Report of the Law Commission under the Chairmanship of the first Attorney General for India, Shri M.C. Setalvad, it was observed as under:-

> "In so far as a person is unable to obtain access to a court of law for having his wrongs redressed.... Justice becomes unequal and laws which are meant for his protection fail in their purpose."

39. In a very important discourse Roscoe Pound argued that by responding to the doctrine of social justice, the concept of justice has advanced through various stages. [See Roscoe Pound, Social Justice and Legal Justice (Address delivered to the Allegheny County Bar Association, April 5, 1912]. At the first stage justice was equated with dispute settlement. At the second stage justice was equated with maintenance of harmony and order. In the third stage, justice was equated with individual freedom. Pound argued that a fourth stage had developed in society, but had not yet been fully reflected in the courts, and that was what Pound called 'social justice'. That is the ideal form of justice where the needs of the people are satisfied, apart from ensuring that they have freedom.

40. Despite complicated social realities, it is submitted that Rule of Law, independence of the judiciary and access to justice are conceptually interwoven. All the three bring to bear upon the quality of aspirations which are guaranteed under our Constitution. In order to fulfil the aspiration, it is important that

the system must be a successful legal and judicial system. This would involve improvement of better techniques to manage courts more efficiently, cutting down costs and duration of proceedings and to ensure that there is no corruption in the judiciary and the establishment of the judiciary and would also require regular judicial training and updating.

41. The memorable words of Lord Devlin (as quoted by D.M. Dharmadhikari, J.) are pertinent to note:

> "... The prestige of the judiciary and their reputation for stark impartiality is not at the disposal of any government; it is an asset that belongs to the whole nation ... "
>
> [See Justice D.M. Dharmadhikari, Nature of Judicial Process, (2002) 6 SCC (Jour) 1.

42. Under the principle of the Rule of Law, adequate protection of the law must be given to all persons and to give meaning to it, there must exist an unimpeded right of access to justice. In the 'Words of Lord Bingham:

> "It would seem to be an obvious implication of the principle that everyone is bound by and entitled to the protection of law that people should be able, in the last resort, to go to court to have their civil rights and claims determined. An unenforceable right or claim is a thing of little value to anyone."
>
> [See Tom Bingham, The Rule of Law, p. 85]

43. The right of access to justice has been recognised as one of the fundamental and basic human rights in various international covenants and charters. [See Article 14(3) of the International Covenant on Civil and Political Rights (ICCPR)]

44. The right of access to justice is also recognised under Article 67 of the Statute of the International Criminal Court (Rome Statute).

45. In the context of the European Union, Article 47 of the European Charter on Fundamental Rights provides for the right to an effective remedy and to fair trial. With respect to the Council of Europe, the European Convention on Human Rights and Fundamental Freedoms, Article 6 significantly protects this right to access justice.

46. The European Court of Human Rights has held that a broader interpretation must be given to Article 6(1) of the ECHR laying emphasis on 'right to a fair administration of justice' in the case of *Delcourt v. Belgium.*

> "…In a democratic society within the meaning of the Convention, the right to a fair administration of justice hold such a prominent place that a restrictive interpretation of Article 6(1) would not correspond to the aim and purpose of that provision."
>
> [See [1970] ECHR 1.]

47. Article 8 of the Universal Declaration of Human Rights provides that:

> "Everyone has the right to an effective remedy by the competent national tribunals for acts violating the fundamental rights granted him by the constitution or by law."

48. Article 16 of the Principles of Freedom from Arbitrary Arrest and Detention provides that:

> "To ensure that no person shall be denied the possibility of obtaining provisional release on account of lack of means, other forms of provisional release than upon financial security shall be provided."

49. The principle of 'Access to Justice or Courts' is recognized as a right in South Africa's Constitution as well:

> "Access to Courts.
>
> 34. Everyone has the right to have any dispute that can be resolved by the application of law decided in a fair public hearing before a court or, where appropriate, another independent and impartial tribunal or forum."

50. The learned Amicus urged that having regard to the paramount importance of the right to access, the Court which he argues is a basic fundamental right specially the Central Government and the State Governments have a duty to ensure speedy disposal of cases for proper maintenance of rule of law and for sustaining peoples' faith in the judicial system. He further argued that with the present infrastructure it is not possible for Courts, whether it is District Courts or the State High Courts or this Court to effectively dispose of cases by just and fair orders within a reasonable timeframe. The learned Amicus also urged that the problem is huge and the considerations are momentous. To understand the magnitude of the problem, the Government must appoint a permanent commission to make continuous recommendation on measures which are necessary to streamline the existing justice delivery system. In support of his submission, he referred to the Report of Lord Woolf submitted to Lord Chancellor in England:

> "…It will not only assist in streamlining and improving our existing systems and process; it is also likely, in due course, itself to be a catalyst for radical change as well…"
>
> [Final Report to the Lord Chancellor on the Civil Justice System in England and Wales (Lord Woolf's Report), 1996, Chapter 21, para 1]

51. The learned Amicus submitted that this huge pendency of cases operates as a burden on the mindset of a Judge. He submitted rightly that the inner charter of the judge is constantly under a pressure to somehow decide the case and the quality of justice suffers. Therefore, according to him, it is

the constitutional duty of both the Central Government and the State Government to provide adequate infrastructure to the judiciary and only an independent commission which functions on a permanent basis can assess the necessity of the required infrastructure and make recommendations to the Government for providing necessary steps which the Government should take to make the Constitutional promise of justice a reality. The learned Amicus developed his argument by referring to various decisions of this Court and also various provisions of the Constitution. He further submitted that the plea of the Government that in view of financial crunch it cannot provide the necessary infrastructure cannot be countenanced by this Court and in support of the said submission he referred to the decision of this Court in the case of *R. Ramachandra Rav v. State of Karnataka,* reported in (2002) 4 SCC 578. The relevant observations made in the said judgment are as follows:-

> "…The law does not permit any government to deprive its citizens of constitutional rights on a plea of poverty or administrative inability…"

52. As the Central Government has been impleaded in this proceeding it was represented by Mr. Harin P. Raval, the learned ASG.

53. The learned ASG very fairly submitted that the questions debated in this case, by and large, are not adversarial. The learned ASG submitted that the Government also accepts that right of access to Court is a fundamental and constitutional right. The learned ASG also accepted that if right to access justice is denied to the citizens then most of the rights given under the Constitution virtually become a rope of sand. The learned ASG submitted that the Government is aware of the importance of these rights and are taking several steps to make these rights vibrant. In the counter affidavit, which has been filed by the Under Secretary, Ministry of Law and Justice dated 9.1.2012 several steps which have been taken by the

Government to ensure speedy justice and to reduce delay are as follows:-

I. Appointment of Court Managers in High Courts and Sub-ordinate Courts.

II. Vision Statement and Action Plan adopted by the National Consultation for Strengthening the Judiciary towards Reducing Pendency and Delays.

III. To prepare National Arrear Grid

IV. National Mission for Justice Delivery and Legal Reforms.

V. National and State Legal Service Authorities constituted under Legal Service Authorities Act, 1987.

VI. National Court Management System (as proposed by Hon'ble Chief Justice of India).

54. The learned ASG referred to the agenda notes and the minutes of the meeting of the Advisory Council of the National Commission for Justice Delivery and Legal Reforms. He submitted that the National Mission spanning from 2011 to 2016 would focus on two major goals envisaged in the Vision document, namely, (i) increasing access by reducing delays and arrears in the system, and (ii) enhancing accountability through structural changes and by setting performance standards and capacities.

55. It was also pointed out that the tentative action plan covers five strategic initiatives and one of them is improving infrastructure of the District and Subordinate Courts and creation of special and additional courts like morning and evening courts etc. He referred to various pages of the Meeting of the Advisory Council of the National Mission held on

18.10.2011 in Vigyan Bhawan, New Delhi to show that the Government is aware of the problem and is seeking to address the same. However, in the course of his arguments the learned ASG took the leave of this Court and filed another affidavit dated 18.1.2012 by Dr. S.S. Chahar, Joint Secretary and Legal Advisor, Ministry of Law and Justice.

56. By filing the said affidavit the learned ASG wanted to urge before this Court that even though the Government is aware of the urgency of the problem and the immediate necessity of addressing it, Government is not willing to accept the suggestion of the learned Amicus for setting-up of a permanent commission for the purposes suggested by the learned Amicus.

57. The learned ASG on the other hand submitted in view of the stand taken by the Central Government in its affidavit dated 18.1.2012 that the existing terms of reference of the 19th Law Commission are wide enough to include within its ambit the question of setting up additional courts for the purpose of tackling the arrears so that access to justice is ensured. In this connection, he referred to the terms of reference of the 19th Law Commission. The said terms of reference are as follows:-

"A. Review/Repeal of obsolete laws:

i. To identify laws which are no longer needed or relevant and can be immediately repealed.

ii. To identify laws which are in harmony with the existing climate of economic liberalization which need no change.

iii. To identify laws which require changes or amendments and to make suggestions for their amendment.

iv. To consider in a wider perspective the suggestions for revision/amendment given by Expert Groups in various Ministries/Departments with a view to coordinating and harmonizing them.

v. To consider references made to it by Ministries/ Departments in respect of legislation having bearing on the working of more than one Ministry/Department.

vi. To suggest suitable measures for quick redressal of citizens grievances, in the field of law.

B. Law and Poverty

i. To examine the Law which affect the poor and carry out post-audit for socio-economic legislation.

ii. To take all such measures as may be necessary to harness law and the legal process in the service of the poor.

C. To keep under review the system of judicial administration to ensure that it is responsive to the reasonable demands of the times and in particular to secure: -

i. Elimination of delays, speedy clearance of arrears and reduction in costs so as to secure quick and economical disposal of cases without affecting the cardinal principle that decisions should be just and fair.

ii. Simplification of procedure to reduce and eliminate technicalities and devices for delay so that it operates not as an end in itself but as a means of achieving justice.

iii. Improvement of standards of all concerned with the administration of justice.

D. To examine the existing laws in the light of Directive Principles of State Policy and to suggest ways of improvement and reform and also to suggest such legislation as might be necessary to implement the Directive Principles and to attain the objective set out in the Preamble to the Constitution.

E. To examine the existing laws with a view to promoting gender equality and suggesting amendments thereto.

F. To revise the Central Acts of General Importance so as to simplify them and to remove anomalies, ambiguities and inequities.

G. To recommend to the Government measure for bringing the statute book up-to-date by repealing obsolete laws and enactments or parts thereof which have outlived their utility.

H. To consider and to convey to the Government its views on any subject relating to law and judicial administration that may be referred to it by the Government through Ministry of Law and Justice (Department of Legal Affairs).

I. To consider the requests for providing research to any foreign countries as may be referred to it by the Government through Ministry of Law and Justice (Department of Legal Affairs).

J. To examine the impact of globalization on food security, unemployment and recommend measures for the protection of the interests of the marginalized.

The Commission shall devote, its time bound attention to all issues relating to item (A) of the terms of reference as indicated above, viz., review/repeal of obsolete laws and shall make its recommendations to Government for repeal of obsolete laws and for appropriate amendments in others as may be found necessary ON TOP PRIORITY basis.

The Commission shall submit its reports in Hindi and English with sufficient number of copies for being placed on Tables of both houses of Parliament. The Law Commission shall also make its reports available through website or otherwise as soon as reports are submitted to the Government.

Various Law Commissions have given about 234 Reports so far. Many of them are made available on the website of Law Commission. Since many of the Reports are voluminous it will be difficult for researchers to read entire Report online. To facilitate the researchers to choose the topics of their area and to create awareness amongst Judges, Lawyers, Law Teachers and Students on the various recommendations of the Law Commission, a brief summary of all the Reports of the Law Commission shall be made available by the Law Commission, online."

58. The learned ASG submitted that in view of Clause 'H' of the terms of reference of the 19th Law Commission, the present Law Commission can go into the question of making a proper research and a scientific and empirical study to assess the requirement of setting up additional courts and making available additional infrastructures for ensuring free access to court and speedier disposal of cases. The learned ASG submitted that the pendency of cases cannot be tackled by only setting up additional courts. Various other factors are also involved including the cooperation of the members of the Bar, the quality of legal education, policy of legislation, recruitment of quality manpower and such other issues which the Law Commission should urgently address and make recommendations on.

59. The learned ASG also submitted that having regard to the provision of Article 235 of the Constitution the control over district and subordinate courts rests with the respective High Courts in each State. In assessing the requirement of setting up of additional courts and creating additional benches, the opinion of the High Court and the State Government have to be ascertained including the question of budget allocation to each State Government. The learned ASG also submitted that since the Government is keenly interested to address these problems it is open to any suggestion. It was submitted that any direction from this Court will help the Government and the Law

Commission to tackle this problem in a very effective way.

60. The Court, upon a detailed and very anxious consideration of the aforesaid issues and specially huge pendency of arrears in different High Courts and considering the stand of the Central Government in its affidavit dated 18.1.2012 is giving the following directions.

I. Certain directions are given to the High Courts for better maintenance of the Rule of Law and better administration of justice:

While analyzing the data in aggregated form, this Court cannot overlook the most important factor in the administration of justice. The authority of the High Court to order stay of investigation pursuant to lodging of FIR, or trial in deserving cases is unquestionable. But this Court is of the view that the exercise of this authority carries with it the responsibility to expeditiously dispose of the case. The power to grant stay of investigation and trial is a very extraordinary power given to High Courts and the same power is to be exercised sparingly only to prevent an abuse of the process and to promote the ends of justice. It is therefore clear that:

(i) such an extraordinary power has to be exercised with due caution and circumspection.

(ii) Once such a power is exercised, High Court should not lose sight of the case where it has exercised its extraordinary power of staying investigation and trial.

(iii) High Court should make it a point of finally disposing of such proceedings as early as possible but preferably within six months from the date the stay order is issued.

61. It is true that this Court has no power of superintendence over High Court as the High Court has over District Courts under Article 227 of the Constitution. Like this

Court, High Court is equally a Superior Court of Record with plenary jurisdiction. Under our Constitution High Court is not a Court subordinate to this Court. This Court, however, enjoys appellate powers over High Court as also some other incidental powers. But as the last court and in exercise of this Court's power to do complete justice which includes within it the power to improve the administration of justice in public interest, this Court gives the aforesaid guidelines for sustaining common man's faith in the rule of law and the justice delivery system, both being inextricably linked.

II. Certain directions are also given to the Law Commission which are as follows:

a) Since the Law Commission itself is seized with the problem and is making investigation having regard to its terms of reference specially clause 'H', thereof, this Court requests the Law Commission, which is headed by a distinguished retired judge of this Court, to undertake an enquiry and submit its recommendation in relation to the following matters:-

I. Keeping in view that timely justice is an important facet to access to justice, the immediate measures that need to be taken by way of creation of additional courts and other allied matters (including a rational and scientific definition of "arrears" and delay, of which continued notice needs to be taken), to help in elimination of delays, speedy clearance of arrears and reduction in costs. It is trite to add that the qualitative component of justice must not be lowered or compromised; and

II. Specific recommendations whenever considered necessary on the above aspects in relation to each State be made as a product of consultative processes involving the High Courts and other stake holders, including the Bar.

b) In doing so, the Commission may take such assistance from the Central Government and the State Governments as it thinks fit and proper.

c) Accordingly, it is directed that on the Commission's request for assistance both the Central Government and the State Governments shall render all possible assistance to the Commission to enable it to discharge its functions, as directed by this Court in its order. The Commission shall at the discretion of its Chairman be free to co-opt purposes of the enquiry to be undertaken by it. Such legal & technical, experts as may be considered necessary by it for an effective and early completion of the assignment hereby made.

d) The Commission is requested to submit its report within six months from the date of this order.

e) Such recommendations be sent to the Registrar General of this Court in sealed covers.

62. The matter may appear before the appropriate Bench after being nominated by the Hon'ble the Chief Justice on the 7th August, 2012 for further consideration by this Court of the recommendations by the Law Commission and if necessary for further directions to be passed in these appeals.

R.P. Matter adjourned.

M/S HOTEL ASHOKA (INDIAN TOUR.DEV.COR.LTD.)
v.
ASSISTANT COMMISSIONER OF COMMERCIAL TAXES & ANR.
(Civil Appeal No. 2560 of 2010)

FEBRUARY 03, 2012

[D.K. JAIN AND ANIL R. DAVE, JJ.]

CENTRAL SALES TAX ACT, 1956:

s.. 5(2) r/w Art. 286 of the Constitution and s.2(ii) of Customs Act - Goods sold at duty free shops at the International Airport - Held: State Government has no right to tax any such transaction which takes place at the duty free shops which are not within the customs frontiers of India - Karnataka value Added Tax, 2003 - Customs Act, 1962 - s.2(ii) - Constitution of India, 1950 - Art. 286 -Arts.226 and 136 - Alternative remedy.

The appellant, a dealer registered under the Karnataka Value Added Tax Act, 2003 and the Central Sales Tax Act, 1956, filed returns stating that no tax was payable by it in respect of the goods sold directly to the passengers at the duty free shops at the International Airport, Bengaluru. However, the Assistant Commissioner of Commercial Taxes directed the appellant to pay a sum of Rs. 4,20,70,900/- by way of sales tax. The writ petition filed by the appellant was dismissed by the Single Judge of the High Court on the ground that it had not exhausted the alternative remedy under the Act. The Division Bench of the High Court declined to interfere. Aggrieved, the Assessee filed the appeals.

Allowing the appeals, the court

HELD : 1. It is true that the appellant had rushed to

the High Court without exhausting equally efficacious alternative statutory remedy. The Single Judge of the High Court was also right when he directed the appellant to move the statutory appellate authority. In normal circumstances, even this Court would have expressed the same opinion, but looking to the fact that the special leave petition has already been admitted and the matter pertains to the assessment year 2004-2005, it would not be in the interest of justice to relegate the appellant to the statutory authorities especially when the legal position is very clear and the law is also in favour of the appellant. [Para 28] [819-H; 820-A-B]

2.1 In the instant case, admittedly, the goods brought from foreign countries by the appellant had been kept in bonded warehouses and, as such, the said goods are deemed to have been kept outside the customs frontiers of the country. Before the goods were imported in the country, they had been sold at the duty free shops of the appellant situated at the International Airport of Bengaluru which are also beyond the customs frontiers of India. [Para 18-19 & 23] [817-E; 818-A-B; 819-A-B]

2.2 No tax on the sale or purchase of goods can be imposed by any State when the transaction of sale or purchase takes place in the course of import of goods into or export of goods out of the territory of India. Thus, if any transaction of sale or purchase takes place when the goods are being imported in India or they are being exported from India, no State can impose any tax thereon. In view of the provision of sub.s. (2) of s.5 of the Central Sales Tax Act, 1956, it is clear that a sale or purchase of goods shall be deemed to take place in the course of import of the goods into the territory of India only if sale or purchase takes place before the goods have crossed the customs frontiers of India. [Para 20 and 22] [818-B-C; G]

2.3 When any transaction takes place outside the customs frontiers of India, the transaction would be said to have taken place outside India. Though the transaction might take place within India but technically, looking to the provisions of s. 2(11) of the Customs Act and Article 286 of the Constitution, the said transaction would be said to have taken place outside India. It cannot be said that the goods are imported into the territory of India till the goods or the documents of title to the goods are brought into India. Admittedly, in the instant case, the goods had not been brought into the customs frontiers of India before the transaction of sales had taken place and, therefore, the transactions had taken place beyond or outside the custom frontiers of India. [Para 30] [820-E-G]

2.4 It is not disputed that in the instant case the goods were sold by giving physical possession at the duty free shops to the customers. Simply because the sales had not been effected by transfer of documents of title to the goods and the sales were effected by giving physical possession of the goods to the customer, it would not mean that the sales were taxable under the Act. [Para 31] [821-B-C]

2.5 Looking to the provisions of Article 286 of the Constitution, the State of Karnataka has no right to tax any such transaction which takes place at the duty free shops owned by the appellant which are not within the customs frontiers of India. The order of assessment so far as the transactions, which are the subject matter of this litigation, are concerned, is quashed. [Para 24 and 32] [819-B-C; 821-D]

State of Travancore-Cochin and others v. Bombay Company Ltd. Alleppey **1952 SCR 1112 = AIR 1952 SC 366;** *State of Travancore-Cochin and others v. Shanmugha Vilas Cashewnut Factory Quilon* **1954 SCR 53= AIR 1953 SC 333;** *J.V. Gokal & Co. (Private) Ltd. v. Assistant Collector of Sales*

Tax (Inspection) and Others **1960 SCR 852=AIR 1960 SC 595;** *Kiran Spinning Mills v. Collector of Customs* **AIR 2000 SC 3448;** *K. Gopinathan Nair and Others v. State of Kerala* **1997 (3) SCR 226 = (1997) 10 SCC 1;** *Binani Bros. (P) Ltd. v. Union of India and Others* **1974 (2) SCR 619 = (1974) 1 SCC 459;** *Mohd. Serajuddin & Ors. v. State of Orissa* **1975 (0) Suppl. SCR 169 (1975) 2 SCC 47 - cited.**

Case Law Reference:

1952 SCR 1112	**Cited**	**Para 11**
1954 SCR 53	**Cited**	**Para 11**
1960 SCR 852	**Cited**	**Para 11**
AIR 2000 SC 3448	**Cited**	**Para 11**
1997 (3) SCR 226	**Cited**	**Para 11**
1974 (2) SCR 619	**Cited**	**Para 11**
1975 (0) Suppl. SCR 169	**Cited**	**Para 11**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2560 of 2010.

From the Judgment & Order dated 9.6.2009 of the High Court of Karnataka at Bangalore in Writ Appeal No. 881 of 2009.

WITH

C.A. No. 10404-10412 of 2010.

Joseph Vellapally, Randhir Chawla, Renu Sehgal, Kumar Rajesh Singh, Praveen Kumar for the Appellant.

K.N. Bhat, K.K. Sharma, Anantarayana M.G., V.N. Raghupahy, S. Wasim A. Qadri Khanna, Suchismita, Zaid Ali, Anil Katiyar for the Respondents.

The Judgment of the Court was delivered by

ANIL R. DAVE, J.

CIVIL APPEAL NO. 2560 OF 2010

1. In this appeal, an order dated 9th June, 2009 passed by the High Court of Karnataka, in Writ Appeal No. 881 of 2009 (T-CST) is challenged by the appellant, who is an assessee and registered as a dealer under the provisions of the Karnataka Value Added Tax Act, 2003 (hereinafter referred to as 'the Act'). Facts giving rise to the present litigation in a nutshell are as under:

2. The appellant, M/s Hotel Ashoka, is managed by India Tourism Development Corporation Limited (hereinafter referred to as 'the Corporation'). The Corporation is having its duty free shops at all major International Airports in India. At the said duty free shops, the appellant sells several articles including liquor to foreigners and also to Indians, who are going abroad or coming to India by air. We are concerned with a duty free shops situated at an International Airport at Bengaluru. The appellant is registered as a dealer under the Act as well as under the Central Sales Tax Act, 1956 (hereinafter referred to as 'the Central Act'). In the return filed under the Act as well as under the Central Act for the relevant period, the appellant had stated that though liquor, cigarettes, perfumes and food articles were sold at the duty free shops at the Bengaluru International Airport, no tax was payable by the appellant as the goods which had been sold at the duty free shops were sold directly to the passengers and even the delivery of goods at the duty free shops was made before importing the goods or before the goods had crossed the customs frontiers of India.

3. According to the appellant, no tax can be levied under the Act or under the Central Act when the goods are sold in the course of import or before the goods have crossed the customs frontier of India as per the provisions of Section 5 of the Central Act and so far as the Act is concerned, no tax can be levied, if the sale takes place before the goods crosses the customs frontiers of India as no State can tax the sale or

purchase of goods which are outside the concerned State i.e. the State of Karnataka in the instant case, as per the provisions of Article 286 of the Constitution of India. In spite of the above stand of the appellant, the Assistant Commissioner of Commercial Taxes (Transition -12) Bengaluru, by an assessment order dated 28th May, 2008 directed the appellant to pay a sum of Rs.4,20,70,900/- by way of sales tax.

4. Being aggrieved by the assessment order passed by the Assistant Commissioner of Commercial Taxes Bengaluru, the appellant filed W.P.(C) No. 10989 of 2008 in the High Court of Karnataka which was rejected on 11th February, 2009, on the ground that the appellant had not exhausted equally efficacious alternative remedy available to it under the provisions of the Act. The learned Single Judge did not consider merits of the case for the aforestated reason.

5. Being aggrieved by the view expressed by the learned Single Judge, the appellant preferred Writ Appeal No. 881 of 2009(T-CST) before the Division Bench of the High Court which was also dismissed on 9th June, 2009 as the Division Bench found substance in the observations made by the learned Single Judge, hence the appellant has filed this appeal before this Court.

6. Learned counsel appearing for the appellant drew our attention to the provisions of Article 286 of the Constitution and Section 5 of the Central Act. He submitted that the Constitution does not permit any State to impose tax on sale or purchase of goods where such sale or purchase takes place outside the State or in the course of the import of the goods into or export of the goods out of the territory of India.

7. He further submitted that in the instant case, all sales had taken place at the duty free shops of the appellant before the goods had crossed the customs frontiers of India. He stated that the goods, which are the subject matter of the present litigation were brought in India and had been kept at bonded

warehouses and thereafter they were transported to duty free shops which were outside the customs frontiers of India.

8. He further submitted that till the goods cross the customs frontiers of India, technically the goods are considered to have remained outside India and once the sale or purchase of the goods which takes place in the course of import or export or outside the concerned State, according to the provisions of Article 286 of the Constitution, no State can impose any tax on such a sale or purchase. As the duty free shops of the appellant are outside the customs frontiers of India, as per legal fiction, the sale of goods cannot be said to be in any State but technically such a sale would be considered to be in the course of import of the goods and, therefore, the sale effected at the duty free shops of the appellant cannot be taxed under the Act.

9. He further submitted that all the duty free shops of the appellant are in customs area as defined under Section 2(11) of the Customs Act, 1962 (in short the ‘Customs Act’). According to the said definition, ‘customs area’ is the area of a customs station and it includes any area in which imported goods or export goods are ordinarily kept before clearance by Customs Authorities. According to him, the goods can be said to have been imported only after sale of the goods at duty free shop to a passenger, if the passenger brings the goods in India, after crossing the customs frontiers of India and not before that, because import means bringing of goods into India from a place outside India and as the duty free shops are in customs area, and as the goods are sold before clearance of Customs Authorities, it cannot be said that the goods sold by the duty free shops were sold after they were imported or in Karnataka State.

10. For the aforestated reasons, according to him, the assessment order passed by the Assistant Commissioner of Commercial Taxes, Bengaluru dated 28th May, 2008 is bad in law. According to the learned counsel, the said officer had

committed a grave error by treating the sale at duty free shops as sale after import of the goods in the State of Karnataka.

11. He further submitted that the learned Single Judge as well as the Division Bench of the High Court ought not to have passed orders against the appellant as the appellant had not exhausted equally efficacious alternative statutory remedy. He submitted that the issue involved in the litigation had already been decided by this Court and other High Courts and the legal position was so clear that the appellant ought not to have been asked to exhaust alternative statutory remedy. He submitted that when facts were not in dispute and the law had been settled by this Court in several other cases, it was not proper on the part of the learned Single Judge to dispose of the petition only on the ground that the alternative remedy had not been exhausted. He also submitted that the Division Bench also committed an error by confirming the order passed by the learned Single Judge of the High Court. So as to substantiate his submission, the learned counsel relied upon several judgments including the judgments delivered in the cases of *State of Travancore-Cochin and others v. Bombay Company Ltd. Alleppey* [AIR 1952 SC 366], *State of Travancore-Cochin and others v. Shanmugha Vilas Cashewnut Factory Quilon* [AIR 1953 SC 333], *J.V. Gokal & Co. (Private) Ltd. v. Assistant Collector of Sales Tax (Inspection) and Others* [AIR 1960 SC 595] and in *Kiran Spinning Mills v. Collector of Customs* [AIR 2000 SC 3448].

12. On the other hand, learned senior counsel Shri Bhat and Shri Sharma, assisted by learned counsel Shri Qadri appearing for the respondent-State, mainly submitted that the orders passed by the learned Single Judge as well as by the Division Bench of the High Court are just and proper. They submitted that the High Court rightly did not entertain the petition as the appellant had not challenged the validity of the order before the appellate authority appointed under the Act. They submitted that the Act has set up appellate authorities and

according to the provisions of the Act, an order passed by the assessing officer should be first challenged before the first appellate authority and only after all the remedies under the Act are exhausted, the appellant should have approached the High Court. As the statutory remedies had not been exhausted by the appellant, according to the learned counsel, the High Court had rightly dismissed the appeal by confirming the order passed by the learned Single Judge.

13. On merits they submitted that purchase of the goods at the duty free shops of the appellant would be taxable under the provisions of the Act. They submitted that after purchase of the goods at the duty free shops, passengers enter the country by crossing the customs frontiers. The goods were actually delivered to the customers and sales were not effected by transfer of documents of title to the goods and, therefore, it can not be said that no tax could have been levied on the sales effected at the duty free shops. According to them, crossing of customs frontiers had no significance because once the goods are brought into our country and especially in the State of Karnataka, all sales effected in the State of Karnataka would be subject to tax as per the provisions of the Act. The duty free shops situated at Bengaluru International Airport are situated in the State of Karnataka and, therefore, sales effected at the said shops would be taxable under the provisions of the Act.

14. They further submitted that according to Section 5 of the Central Act, the sales which caused import or which occasioned import would not be subject to tax under the Act. According to them, all these transactions referred to in the assessment order had not taken place in the course of import or they had not caused or occasioned import, and, therefore, they would be subject to tax under the Act. They further submitted that the goods had not been sold by transferring the documents of title to the goods. According to them, before the goods had crossed the customs frontiers, they ought to have been transferred by transfer of documents of title to the goods, but

as it was not done so, it cannot be said that the sales had taken place in the course of import of the goods before crossing the customs frontiers of our country. So as to substantiate the aforestated submissions, they relied upon the judgments in *K. Gopinathan Nair and Others v. State of Kerala* [(1997) 10 SCC 1], *Binani Bros. (P) Ltd. v. Union of India and Others* [(1974) 1 SCC 459], *Mohd. Serajuddin & Ors. v. State of Orissa* [(1975) 2 SCC 47].

15. In the circumstances, they submitted that the appeal be dismissed with costs and the stay granted by this Court be vacated.

16. We heard the learned counsel at length and considered the impugned order of assessment as well as the orders passed by the High Court of Karnataka and the judgments referred to by the learned counsel.

17. In our opinion, the facts stated by the counsel are not much in dispute.

18. It is an admitted fact that the goods which had been brought from foreign countries by the appellant had been kept in bonded warehouses and they were transferred to duty free shops situated at International Airport of Bengaluru as and when the stock of goods lying at the duty free shops was exhausted. It is also an admitted fact that the appellant had executed bonds and the goods, which had been brought from foreign countries, had been kept in bonded warehouses by the appellant. When the goods are kept in the bonded warehouses, it cannot be said that the said goods had crossed the customs frontiers. The goods are not cleared from the customs till they are brought in India by crossing the customs frontiers. When the goods are lying in the bonded warehouses, they are deemed to have been kept outside the customs frontiers of the country and as stated by the learned senior counsel appearing for the appellant, the appellant was selling the goods from the

duty free shops owned by it at Bengaluru International Airport before the said goods had crossed the customs frontiers.

19. Thus, before the goods were imported in the country, they had been sold at the duty free shops of the appellant.

20. In view of the aforestated factual position and in the light of the legal position stated hereinabove, it is very clear that no tax on the sale or purchase of goods can be imposed by any State when the transaction of sale or purchase takes place in the course of import of goods into or export of the goods out of the territory of India. Thus, if any transaction of sale or purchase takes place when the goods are being imported in India or they are being exported from India, no State can impose any tax thereon.

21. Section 5 of the Central Act deals with the transaction which is said to have taken place in the course of import or export. Relevant portion of Section 5 of the Central Act reads as under:

> "5(1) xxx xxx xxx
>
> (2) A sale or purchase of goods shall be deemed to take place in the course of the import of the goods into the territory of India only if the sale or purchase either occasions such import or is effected by a transfer of documents of title to the goods before goods have crossed the customs frontiers of India."

22. Upon perusal of the aforestated provision of Section 5 of the Central Act, it is clear that a sale or purchase of goods shall be deemed to take place in the course of import of the goods into the territory of India only if sale or purchase takes place before the goods have crossed the customs frontiers of India.

23. Looking to the aforestated legal position, it cannot be disputed that the goods sold at the duty free shops, owned by

the appellant, would be said to have been sold before the goods crossed the customs frontiers of India, as it is not in dispute that the duty free shops of the appellant situated at the International Airport of Bengaluru are beyond the customs frontiers of India i.e. they are not within the customs frontiers of India.

24. If this is the factual and legal position, in our opinion, looking to the provisions of Article 286 of the Constitution, the State of Karnataka has no right to tax any such transaction which takes place at the duty free shops owned by the appellant which are not within the customs frontiers of India.

25. Looking to the aforestated simple and factual legal position, in our opinion, it would not be much useful to discuss the judgments which have been referred to by the learned counsel appearing for the appellant. In our opinion, the legal position is so clear that it was not necessary for the learned counsel to refer to any judgment and merely by showing the aforestated factual aspects and legal provisions to the concerned authority, the appellant could have convinced the concerned authority that the sale effected at the duty free shops of the appellant could not have been taxed by the State of Karnataka.

26. Learned counsel appearing for the respondent-Authorities had vehemently submitted that the appellant had not exhausted equally efficacious alternative statutory remedy and, therefore, the Single Judge of the High Court had rightly not entertained the petition filed by the appellant.

27. According to them, the Division Bench had also rightly dismissed the appeal for the same reason. According to them, this Court also should not entertain this appeal.

28. It is true that the appellant had rushed to the High Court without exhausting equally efficacious alternative statutory remedy. In our opinion, the learned Single Judge of the High

Court was also right when he directed the appellant to move the statutory appellate authority. In normal circumstances, even we would have expressed the same opinion but looking to the fact that the special leave petition has already been admitted and the matter pertains to the assessment year 2004-2005, it would not be in the interest of the justice to relegate the appellant to the statutory authorities especially when the legal position is very clear and the law is also in favour of the appellant.

29. The learned counsel appearing for the respondent had submitted that the sale would not be subject to tax under the Act only if it occasions in the course of import but the transactions of sale, which are subject matter of this litigation had not taken place in the course of import and, therefore, they would not be exempted under the provisions of Section 5 of the Central Act. In our opinion, the aforestated submission cannot be sustained.

30. They again submitted that ‘in the course of import’ means ‘the transaction ought to have taken place beyond the territories of India and not within the geographical territory of India’. We do not agree with the said submission. When any transaction takes place outside the customs frontiers of India, the transaction would be said to have taken place outside India. Though the transaction might take place within India but technically, looking to the provisions of Section 2(11) of the Customs Act and Article 286 of the Constitution, the said transaction would be said to have taken place outside India. In other words, it cannot be said that the goods are imported into the territory of India till the goods or the documents of title to the goods are brought into India. Admittedly, in the instant case, the goods had not been brought into the customs frontiers of India before the transaction of sales had taken place and, therefore, in our opinion, the transactions had taken place beyond or outside the custom frontiers of India.

31. In our opinion, submissions with regard to sale not

taking effect by transfer of documents of title to the goods are absolutely irrelevant. Transfer of documents of title to the goods is one of the methods whereby delivery of the goods is effected. Delivery may be physical also. In the instant case, at the duty free shops, which are admittedly outside the customs frontiers of our country, the goods had been sold to the customers by giving physical delivery. It is not disputed that the goods were sold by giving physical possession at the duty free shops to the customers. Simply because the sales had not been effected by transfer of documents of title to the goods and the sales were effected by giving physical possession of the goods to the customers, it would not mean that the sales were taxable under the Act. Thus, we do not agree with the aforestated submissions made by the learned counsel appearing for the Revenue.

32. Looking to the aforestated clear and settled legal position, we allow the appeal and quash the order of assessment so far as the transactions which are the subject matter of this litigation are concerned. There shall be no order as to cost.

CIVIL APPEAL NOs. 10404-10412 OF 2010

33. As issues involved in the aforestated appeals and in Civil Appeal No.2560 of 2010 are same, for the reasons recorded in the judgment rendered in Civil Appeal No. 2560 of 2010, these appeals also stand allowed and the assessment orders, so far as they pertain to the subject matter of these appeals are concerned, are quashed. There shall be no order as to costs.

R.P. Appeals allowed.

BAVO @ MANUBHAI AMBALAL THAKORE
v.
STATE OF GUJARAT
(Criminal Appeal No. 309 of 2012)

FEBRUARY 3, 2012

[P. SATHASIVAM AND J. CHELAMESWAR, JJ.]

Penal Code 1860 - ss. 376 and 506 (2) - Commission of rape by accused aged 18/19 years on victim aged about 7 years - Conviction of accused for commission of offence u/ss. 376 and 506 (2) - Sentence of life imprisonment with a fine of Rs. 20,000/- in default, to further undergo rigours imprisonment for three years imposed - On appeal held: In view of the age of victim and accused; and that the incident occurred nearly 10 years ago, sentence of life imprisonment modified to RI for 10 years with fine of Rs. 1,000/-.

Appellant committed rape on a girl aged about 7 years. At the time of the incident appellant was 18/19 years. The courts below convicted the appellant-accused for the offence punishable under Sections 376 and 506 (2) of the Penal Code, 1860 and sentenced him to undergo imprisonment for life with a fine of Rs.20,000/-, in default, to further undergo RI for three years. Therefore, the appellant filed the instant appeal questioning the quantum of sentence only.

Disposing of the appeal, the Court

HELD: 1.1 For the offence of rape on a girl under 12 years of age, punishment shall not be less than 10 years but which may extend to life and also to fine shows that the legislature intended to adopt strictness in awarding sentence if the victim is below 12 years of age. No doubt, the proviso to Section 376(2) IPC lays down that the Court

A **may, for adequate and special reasons to be mentioned in the judgment, impose a sentence of imprisonment of either description for a term of less than 10 years. The courts are obliged to respect the legislative mandate in the matter of awarding of sentence in all such cases. In**
B **the absence of any special and adequate reasons, recourse to proviso to Section 376(2) cannot be applied in a casual manner. [Para 8] [826-E-G]**

1.2 Considering the fact that the victim, in the instant case was aged about 7 years on the date of the incident
C **and the accused was in the age of 18/19 years and also of the fact that the incident occurred nearly 10 years ago, the award of life imprisonment which is maximum prescribed is not warranted and also in view of the mandate of Section 376(2)(f) IPC, the ends of justice**
D **would be met by imposing RI for 10 years. Furthermore, the appellant had already served nearly 10 years. [Para 11] [827-E-F]**

1.3 In view of the fact that the accused hails from a poor family and was working as an agricultural labourer
E **and is not in a position to pay such a huge amount as fine , the fine of Rs. 20,000/- is reduced to Rs. 1,000/-, in default, to further undergo RI for one month. The conviction imposed on the appellant is upheld. However, the sentence of life imprisonment is modified to RI for 10**
F **years with a fine of Rs.1,000/-, in default, to further undergo RI for one month. [Paras 12 and 13] [827-G-H; 828-A]**

Narayanamma (Kum) vs. State of Karnataka and Ors.
G **(1994) 5 SCC 728: 1994 (2) Suppl. SCR 799;** *Rajendra Datta Zarekar vs. State of Goa* **(2007) 14 SCC 560: 2007 (12) SCR 840 - referred to.**

Case Law Reference:

H	**1994 (2) Suppl. SCR 799**	**Referred to**	**Para 9**

A	**2007 (12) SCR 840**	**Referred to**	**Para 10**

CRIMINAL APPELLATE JURISDICTION : Criminal Appeal No.309 of 2012.

From the Judgment & Order dated 28.8.2009 of the High
B Court of Judicature of Gujarat at Ahmedabad in Criminal Appeal No. 505 of 2004.

K.S. Bahl, Merusagar Samantaray for the Appellant.

Hemantika Wahi, Jesal for the Respondent.

C

The Judgment of the Court was delivered by

P. SATHASIVAM, J. 1. Leave granted.

2. This appeal is directed against the final judgment and
D order dated 28.08.2009 passed by the Division Bench of the High Court of Gujarat at Ahmedabad in Criminal Appeal No. 505 of 2004 whereby the High Court while affirming the conviction and sentence awarded by the trial Court dismissed the appeal of the appellant herein.

E

3. **Brief facts:**

(a) According to the Complainant-Ramilaben, on 02.05.2002 in the morning, when her husband had gone to
F work, she was in her house along with her three children. At that time, her daughter – Smita, aged seven years, was having pain in her finger, therefore, she called her distant relative Bavo @ Manubhai Ambalal Thakore - the appellant herein for taking her to the doctor.

G (b) Thereafter, the appellant herein took Smita to a doctor at about 10:00 a.m. and at about 11:30 a.m. she returned home alone limping and crying. When the complainant asked her daughter as to what had happened, she narrated the whole incident that how the appellant herein over-powered her and the
H Complainant finally came to know that he has committed rape

on her daughter which was also evident from her condition. Thereafter, the Complainant went to the house of the appellant, but he was not present there. When her husband returned home in the evening, she informed him about the incident and, on 05.05.2002, a complaint was lodged at Umreth Police Station.

(c) On 07.07.2002, the police, after conducting the investigation, filed a charge sheet before the Judicial Magistrate, First Class, Umreth. Since the case was exclusively triable by the Court of Sessions, the Judicial Magistrate committed the case to the Court of Additional Sessions Judge, Anand. On 18.03.2004, the Addl. Sessions Judge, convicted the appellant for the offence punishable under Sections 376 and 506(2) of the Indian Penal Code, 1860 (in short "the IPC") and sentenced him to undergo imprisonment for life with a fine of Rs.20,000/-, in default, to further undergo RI for three years.

(d) Being aggrieved by the order of conviction and sentence, the appellant herein preferred an appeal before the High Court. The High Court, by order dated 28.08.2009, dismissed the appeal and confirmed the conviction and sentence awarded by the Addl. Sessions Judge.

(e) Being aggrieved, the appellant herein has preferred this appeal by way of special leave before this Court.

4. Heard Mr. Merusagar Samantaray, learned counsel for the appellant herein and Ms. Hemantika Wahi, learned counsel for the respondent-State.

5. Learned counsel appearing for the appellant fairly states that he is not challenging the conviction but questioning the quantum of sentence only. According to him, taking note of various factors including the age of the appellant-accused being 18-19 years at the time of the incident and hailing from a poor family, award of life imprisonment and a fine of Rs.20,000/-, in default, to further undergo RI for three years is excessive. Learned counsel appearing for the respondent-State fairly

submitted that the Court is free to impose appropriate sentence in terms of Section 376(2)(f) of the IPC.

6. In view of the limited submission, there is no need to go into the finding regarding conviction under Sections 376 and 506(2) of the IPC. The only question to be considered is whether the sentence of life imprisonment and a fine of Rs.20,000/- is reasonable or excessive.

7. Section 376 speaks about the punishment for rape. Sub-section(2)(f) makes it clear that whoever commits rape on a woman when she is under 12 years of age shall be punished with RI for a term which shall not be less than 10 years but which may be for life and shall also be liable to fine. Proviso appended to sub-section (2) makes it clear that the Court may, for adequate and special reasons to be mentioned in the judgment, impose a sentence of imprisonment of either description for a term of less than 10 years.

8. It is clear from the above statutory provision that for the offence of rape on a girl under 12 years of age, punishment shall not be less than 10 years but which may extend to life and also to fine shows that the legislature intended to adopt strictness in awarding sentence if the victim is below 12 years of age. No doubt, the proviso to Section 376(2) lays down that the Court may, for adequate and special reasons to be mentioned in the judgment, impose a sentence of imprisonment of either description for a term of less than 10 years. It is settled law that courts are obliged to respect the legislative mandate in the matter of awarding of sentence in all such cases. In the absence of any special and adequate reasons, recourse to proviso mentioned above cannot be applied in a casual manner.

9. Learned counsel for the appellant relied on a decision of this Court in *Narayanamma (Kum) vs. State of Karnataka and Others,* (1994) 5 SCC 728 and contended that the life imprisonment is not warranted and sentence may be reduced

to the period already undergone. The said decision relates to the rape on a minor girl aged 14 years. While the trial Judge convicted and sentenced the accused to three years RI, the High Court reversed the same and acquitted the accused. It was challenged before this Court. After considering the entire materials, this Court set aside the order of the High Court and affirmed the conclusion arrived at by the trial Court. Though this Court expressed displeasure in awarding only three years RI for the crime of rape, taking note of length of time, not inclined to enhance it and confirmed the sentence awarded by the trial Court.

10. Counsel for the appellant relied on another decision of this Court in *Rajendra Datta Zarekar vs. State of Goa,* (2007) 14 SCC 560. The said case also relates to the offence under Section 376. The victim was aged about 6 years and the accused was aged about 20 years. Ultimately, this Court confirmed the conviction and sentence of 10 years as awarded by the High Court. However, the fine amount of Rs. 10,000/- awarded under Section 376(2)(f) being found to be excessive reduced to Rs. 1,000/-.

11. Considering the fact that the victim, in the case on hand, was aged about 7 years on the date of the incident and the accused was in the age of 18/19 years and also of the fact that the incident occurred nearly 10 years ago, the award of life imprisonment which is maximum prescribed is not warranted and also in view of the mandate of Section 376(2)(f) IPC, we feel that the ends of justice would be met by imposing RI for 10 years. Learned counsel appearing for the appellant informed this Court that the appellant had already served nearly 10 years.

12. Coming to the quantum of fine, in the case on hand, the learned trial Judge has imposed Rs.20,000/-, in default, to undergo RI for three years, learned counsel for the appellant submitted that the accused hails from a poor family and was working as an agricultural labourer and is not in a position to pay such a huge amount as fine which is not disputed by the

State. Taking note of all these aspects, we reduce the fine of Rs. 20,000/- to Rs. 1,000/-, in default, to further undergo RI for one month.

13. In view of the above discussion, the conviction imposed on the appellant herein is confirmed. However, the sentence of life imprisonment is modified to RI for 10 years with a fine of Rs.1,000/-, in default, to further undergo RI for one month.

14. With the above modification of sentence, the appeal stands disposed of.

N.J. Appeal disposed of.

SUSANTA GHOSH

v.

STATE OF WEST BENGAL

(Criminal Appeal No. 310 of 2012)

FEBRUARY 03, 2012

[ALTAMAS KABIR AND GYAN SUDHA MISRA, JJ.]

Bail:

Death of seven persons - Three FIRs lodged earlier - Appellant, a member of Legislative Assembly not named in the three FIRs - Named in the fourth FIR lodged after 9 years - Allegation against appellant that he entered into a criminal conspiracy with other accused persons in order to cause deaths of seven victims who were allegedly members of political party - Bail application - Rejected by High Court - On appeal, held: Appellant's prayer for bail is allowed - There was no mention of the appellant's name or alleged role in the incident in the three FIRs - Appellant was arrested in connection with a FIR lodged 9 years after the incident - During all these years there was no allegation that he had interfered with the investigation - Furthermore, in connection with this case he was also granted anticipatory bail - There was nothing to indicate that such privilege was either abused or misused by the appellant - Tampering with the evidence or the investigation is no longer relevant since charge-sheet has already been filed in the case - Since appellant is a sitting MLA, the possibility of his absconding is remote - Appellant be released on bail to the satisfaction of the trial Court subject to conditions as imposed by trial court.

CRIMINAL APPELLATE JURISDICTION : Criminal Appeal No. 310 of 2012.

From the Judgment & Order dated 29.9.2011 of the High Court of Calcutta in C.R.M. No. 7982 of 2011.

Ajay Sharma for the Appellant.

Kalyan Bandopadhyay, Abhijit Sengupta for the Respondent.

The Order of the Court was delivered by

O R D E R

ALTAMAS KABIR, J. 1. Leave granted.

2. This Appeal is directed against the judgment and order dated 29th September, 2011, passed by the Division Bench of the Calcutta High Court in C.R.M. No.7982 of 2011, which was an application for grant of bail under Section 439 of the Criminal Procedure Code, hereinafter referred to as “Cr.P.C.”, in connection with Anandapur Police Station Case No.36 of 2011, dated 6th June, 2011, under Sections 147, 148, 149, 448, 326, 307, 302, 506, 201 and 120-B of the Indian Penal Code read with Sections 25 and 27 of the Arms Act, corresponding to G.R. Case No.1364 of 2011, pending before the learned Chief Judicial Magistrate, Paschim Medinipur. The Appellant had moved the High Court for bail against the order dated 20th August, 2011, passed by the Chief Judicial Magistrate, Paschim Medinipur, rejecting his prayer for bail and remanding him to jail custody.

3. The Appellant is an elected Member of the West Bengal Legislative Assembly. His prayer for bail is based mainly on the ground that on account of political vendetta he has been named as an accused in a First Information Report which was lodged on 5th June, 2011, in respect of an incident which occurred on 22nd September, 2002, and in respect whereof three separate FIRs had been lodged, two on the date of incident itself and one on 26th September, 2002, in which he had not been named. The first FIR was lodged by one Nemai

Ch. Sarkar, which was recorded as FIR No.59 dated 22nd September, 2002 of Keshpur PS, Paschim Medinipur, under Sectio s 148, 149, 307 and 302 IPC read with Sections 25, 27 and 35 of the Arms Act as also Section 9(b) of the Indian Explosives Act.

4. The second FIR was lodged by one Shri Debashish Roy, the Station House Officer of Keshpur Police Station, on the same day and in respect of the same incident, which was recorded as FIR No.60 dated 22nd September, 2002, under similar provisions.

5. The third FIR was lodged by the daughter of the deceased, Smt. Chandana Acharya, which was recorded as Keshpur PS Case No.61 dated 26th September, 2002, under Sections 148, 149, 448, 326, 307, 364 and 506 IPC read with Sections 25 and 26 of the Arms Act.

6. As will be apparent from the three FIRs, the first two related to the incident in which seven persons, including the father of the third complainant, Ajoy Acharya, were killed at Piyasala Village and their bodies were removed to and buried at Daser Bandh, Keshpur. As indicated hereinabove, in none of the above FIRs was the Appellant named, nor was he included in the charge-sheets which were filed.

7. The cases which arose out of the first two FIRs in which charge-sheets were filed under Sections 148, 149, 302 IPC and also under Sections 448, 364 and 506 IPC, ended in acquittal of the accused persons who were alleged to have committed the offences complained of. The third case is, however, still pending trial before the learned Additional Sessions Judge, Paschim Medinipur.

8. From amongst a number of skeletons which were recovered from a grave in Daser Bandh, Keshpur, one of the skeletons was identified by one Shyamal Acharya, the younger son of the deceased, on the strength of the clothes which were

recovered, together with a set of teeth, which were identified to be that of the deceased, Ajoy Acharya. It is thereafter that the fourth FIR was lodged by Shri Shyamal Acharya, being Anandapur P.S. Case No.36 of 6th June, 2011, in which 40 persons were named as accused and the name of the Appellant was shown at serial No.2 and it was alleged that he had entered into a criminal conspiracy with the other accused persons in order to cause the deaths of the seven victims, who were allegedly members of the Trinamool Congress. It was further alleged that a peace meeting had been held prior to the incident and the victims were returning to their homes upon the assurance that had been given in the meeting that peace would be maintained by the local villagers. The further allegation was that under the directions of the Appellant, the seven victims were targeted and dragged out of their homes and were killed upon his instructions. Thereafter, the bodies were carried to different places and ultimately buried at Daser Bandh in Keshpur, from where the skeletons were recovered.

9. Mr. Ranjit Kumar, learned Senior Advocate, who appeared on behalf of the Appellant, Mr. Susanta Ghosh, urged that with the change in the Government in the State of West Bengal, the Appellant, who is a M.L.A. of the Communist Party of India (Marxist) and a former Minister, is being targeted after an interval of nine years in order to discredit and humiliate him and to adversely affect his political career. It was further submitted that nothing prevented the prosecution or even the heirs of the victim, including his daughter, Smt. Chandana Acharya, who had earlier lodged FIR No.61 dated 25th September, 2002, or the younger son, Shri Shyamal Acharya, who had lodged the fourth FIR, from coming out with the allegation against the Appellant earlier. Mr. Ranjit Kumar submitted that not only was the delay in lodging the FIR, in which the Appellant was indicted, fatal to the prosecution case, but gave rise to a strong suspicion that it was motivated. Mr. Ranjit Kumar also submitted that before the Division Bench of the Calcutta High Court, the Appellant had been granted the benefit

of anticipatory bail which was subsequently not extended by the learned trial Judge, who remanded the Appellant to police custody, and, thereafter, bail has been refused.

10. Mr. Ranjit Kumar submitted that the parameters for grant of bail have been laid down by this Court in various cases and this Court has indicated as to when bail could be refused in respect of cognizable offences, such as, if there were :

(i) chances of tampering with the evidence;

(ii) chances of interfering with the investigation; and

(iii) chances of absconsion;

11. Mr. Ranjit Kumar submitted that as far as the first two instances are concerned, since charge-sheet has already been filed, the same do not survive. Furthermore, since the Appellant is a sitting MLA and a former Minister in the West Bengal Government, there was no chance of his absconsion.

12. Mr. Ranjit Kumar submitted that this is a fit case for grant of bail to the Appellant.

13. Strongly opposing the Appellant's prayer for bail, Mr. Gopal Subramanium, learned Senior Advocate, submitted that the offences alleged to have been committed by the accused, including the Appellant, were highly disturbing and had caused a serious law and order situation and had also spread panic amongst the people of the area. Mr. Subramanium submitted that apart from being grievous, as well as heinous in nature, the crimes were committed pursuant to a well-conceived conspiracy which had been hatched under the leadership of the Appellant herein. Mr. Subramanium submitted that although the name of the Appellant had not figured in the earlier FIRs, his complicity in the murder of the seven victims had been subsequently established by witnesses who had witnessed the incident and had maintained that the Appellant had been

present throughout, until the dead bodies were buried, giving rise to an additional charge under Section 201 IPC.

14. Mr. Subramanium submitted that having regard to the grievous and appalling nature of the crime, right from when the murders were committed, till the concealment of the bodies by burying them, the question of granting bail to the Appellant does not arise, especially when charge-sheet has been filed against him and the matter is ready for trial. Learned counsel submitted that the prayer made on behalf of the Appellant for grant of bail was liable to be rejected.

15. Having considered the submissions made on behalf of the respective parties, we are inclined to allow the Appellant's prayer for bail. Admittedly, two FIRs in respect of the same incident were lodged on the same day, while the third FIR was lodged a few days later. The first FIR was lodged by one Nemai Ch. Sarkar, a local man. The second FIR was lodged by the S.H.O. of the Keshpur Police Station and the third FIR was lodged by the daughter of the deceased Ajoy Acharya.

16. There is no mention of the Appellant's name or alleged role in the incident. There was nothing to prevent at least Smt. Chandana Acharya, the daughter of the deceased, from naming him. Whether the investigating authorities took notice of the same is an entirely different matter. At this stage it will not be proper for us to dilate any further on the factual aspect of the matter, but at least for the purpose of considering the Appellant's prayer for bail it does merit consideration that the Appellant has been arrested in connection with a FIR lodged 9 years after the incident. During all these years there is no allegation that the Appellant has interfered with the investigation. Furthermore, in connection with this case he was also granted anticipatory bail. There is nothing to indicate that such privilege was either abused or misused by the Appellant.

17. As indicated hereinabove, the parameters laid down by this Court for considering grant of bail to an accused include

the likelihood of his absconsion and tampering with the evidence or the witnesses or even the investigation. Tampering with the evidence or the investigation is no longer relevant since charge-sheet has already been filed in the case. As far as absconsion is concerned, the Appellant being a sitting MLA, even such a possibility is remote. There is, of course, the possibility that the Appellant may tamper with the witnesses. However, considering the fact that the matter has been reopened as far as the Appellant is concerned, after an interval of about 10 years, even such a possibility appears to be remote. However, in order to prevent such an eventuality, the Appellant can be put on terms, as was done by the High Court while allowing his prayer for Anticipatory Bail.

18. We, therefore, allow the appeal and direct that the Appellant be released on bail to the satisfaction of the trial Court. The trial Court may impose such conditions as may be necessary to secure the Appellant's presence during the trial. In addition to the above, except for Garhbeta, which is his Assembly Constituency, the Appellant shall not enter other areas of Paschim Medinipur District, West Bengal, without the permission of the trial Court and shall report to the local police station where he will be residing, once on the last Sunday of each month, between 11.00 a.m. and 1.00 p.m. The Appellant shall make himself available before the trial Court at all stages of the trial, unless for any special reason he is exempted from doing so by the trial Court on any particular occasion.

19. The appeal is disposed of accordingly.

D.G. Appeal disposed of.

RAJENDRA PRASAD BAGARIA
v.
PHARMACY COUNCIL OF STATE OF RAJASTHAN & ANR.
(Civil Appeal No. 6895 of 2008)

FEBRUARY 06, 2012

[P. SATHASIVAM AND H.L. GOKHALE, JJ.]

Pharmacy Act, 1948 - ss 36, 31, 32 and 33 - Cancellation of registration as pharmacist upon review - Challenge to - Appellant obtained registration as pharmacist in the State of Rajasthan on basis of being a registered pharmacist in Sikkim - Cancellation of registration as pharmacist upon review by the Executive Committee constituted by the Pharmacy Council of the State of Rajesthan since the registration was found to be irregular - High Court upheld the decision of the Executive Committee - On appeal, held: Section 36(1)(i) gives sufficient power to the Executive Committee to recall its decision - It provides for removing the name of a registered pharmacist in the event there is an error in his registration, or where it is registered on account of misrepresentation or suppression of a material fact - On facts, there was an error on the part of the Pharmacy Council of Rajasthan (first respondent) in accepting the registration from Sikkim as a valid registration for transfer of the appellant as a pharmacist in Rajasthan - On receiving complaint that appellant was functioning as ineligible pharmacist in the State, the appellant was given a notice affording him a personal opportunity as required u/s. 36(1) but he did not avail the opportunity nor produced any evidence as to how his registration in Sikkim was a valid registration - He stayed in Sikkim just for a few months, and he himself contended that he did not have any documentary evidence to prove that he stayed in Sikkim for five years or that he had the necessary experience of not less than five years of work in *dispensing medicines in Sikkim - First respondent did not have any opportunity to examine as to whether the appellant did have the experience of five years in Rajasthan - Thus, the Executive Committee considered the material on record and cancelled the appellant's registration in Rajasthan and not in Sikkim - It cannot be said that the Executive Committee had exercised the power of review without being empowered for the same under the statute or that it had exercised it erroneously - Welfare statute cannot be permitted to be defeated by the methods such as one employed by the appellant - Requirement of five years experience in the registering State would be defeated if any such method are permitted - Thus, there was no error in the decision of the first respondent in canceling registration of the appellant nor the decision of the High Court in upholding the same.*

Object of the Act - Held: Is to make better provisions for the regulation of the profession and practice of pharmacy.

It is the case of the appellant that after passing Secondary School Examination, he worked in a Medical Shop in Rajasthan for more than five years and on basis of his experience, he was eligible to be enrolled as a pharmacist in Rajasthan but could be enrolled since he did not apply on time. Thereafter, the appellant shifted to Sikkim, worked there with a medical shop for two months and applied for registration as pharmacist and was registered. Subsequently, he returned to Rajasthan and applied for registration on basis of the registration obtained in Sikkim and he was enrolled as a registered pharmacist by their registration in Rajasthan.

The Authorities in Rajasthan received some complaints as regards the functioning of large number of ineligible pharmacists in the State. On enquiry they found that the registration of the appellant was irregular and issued him notice to explain as to why his name should not be removed. However, the appellant did not file any

reply and the Executive Committee cancelled his registration. Aggrieved, the appellant filed a writ petition challenging the decision of the first respondent and the Single Judge of the High Court dismissed the same. The Division Bench of the High Court also held that the decision of the Executive Committee of the first respondent could not be faulted. Therefore, the appellant filed the instant appeal.

Dismissing the appeal, the Court

HELD: 1.1 The Preamble of the Pharmacy Act, 1948, states that it is an Act to make better provisions for the regulation of the profession and practice of pharmacy, and for that purpose to constitute the Pharmacy Councils. The qualifications for entry in the first register are provided under Section 31 of the Act, that to be a pharmacist, importance is given to have a degree or diploma in pharmacy, failing which any other degree is permitted with three years experience of dispensing medicines, or passing of an examination recognised by the State Government, or having an experience of not less than five years of working in a hospital or dispensary in which drugs are regularly dispensed on prescriptions of medical practitioners. Section 32 of the Act provides for subsequent registration, which also includes amongst the qualified categories, a registration on the basis of being a registered pharmacist in another State. [Paras 8 and 9] [846-B-C; 847-F-H; 848-A]

Patel Narshi Thakershi and Ors. Vs. Shri Pradyumansinghji Arjunsinghji **1971(3) SCC 844 - referred to.**

1.2 Section 36 (1)(i) provides for removing the name of a registered pharmacist in the event there is an error in his registration, or where it is registered on account of misrepresentation or suppression of a material fact. This

sub-section gives sufficient power to the Executive Committee to recall its decision. In the instant case, obviously, there was an error on the part of the first respondent in accepting the registration from Sikkim as a valid registration for transfer of the appellant as a pharmacist in Rajasthan. Ultimately, it is the State Pharmacy Council which is responsible for having well-equipped pharmacists in the State who have the requisite qualifications and/or experience. The fact is that the second respondent had received complaints with respect to a large number of in-eligible persons functioning as pharmacists. Therefore, when this fact was brought to the notice of the first respondent, a notice was given to the appellant affording him a personal opportunity as required under Section 36 (1) of the Act. However, the appellant did not avail of this opportunity. Thus, all that the Executive Committee had done was to consider the material on record and to cancel his registration in Rajasthan. The Executive Committee of the first respondent had not cancelled his registration in Sikkim. It cannot, therefore, be said that the Executive Committee had exercised the power of review without being empowered for the same under the statute or that it had exercised it erroneously. [Para 11] [850-F-H; 851-A-C]

1.3 There is no dispute that the appellant was given a notice of hearing; and that the appellant did not produce any evidence as to how his registration in Sikkim was a valid registration. This is because there was no dispute that he stayed in Sikkim just for a few months, and he himself contended that he did not have any documentary evidence to claim that he stayed in Sikkim for five years, or that he had the necessary experience of not less than five years of work in dispensing medicines in Sikkim. This is because at the highest, his case with respect to his qualification was one under Section 31 sub-clause (d) of the Act. [Para 12] [851-D-E]

1.4 Section 32 of the Act does entitle a registered pharmacist in one State to have his name entered in the register of another State. Section 33 of the Act, however, gives the power of scrutiny to the State Council and every enrolment is subject to the scrutiny. Thereafter, if the State Council receives any complaint concerning the eligibility of a person to function as a pharmacist, the Executive Committee of the Council does have the power to make necessary enquiry under Section 36 of the Act, and if satisfied, to remove the name of such a registered pharmacist though after giving him a reasonable opportunity of being heard. Sub-section (i) of Section 36 (1) gives the grounds on which a name can be removed from the register. In the instant case, the Executive Committee was satisfied that there was an error in enrolling the appellant as a registered pharmacist. At that stage, the appellant was called upon to give his explanation. In this enquiry, one State Council can certainly look into the prima-facie material on the basis of which registration was granted in another State. This is because the State Council is given the power to scrutinize such applications, and if such registration has been permitted by any error to that extent, it can certainly take the corrective step. Such a decision cannot amount to sitting in appeal over the decision of another State's Council. This is because the concerned State Council is answerable to the persons purchasing the medicines from the pharmacists in the State. It is its duty to see that pharmacists do have necessary educational qualifications or the experience as required. In a country where there is so much illiteracy, the requirements concerning educational qualifications or experience of the pharmacist have to be scrupulously scrutinized. If the registration of the concerned pharmacist obtained from another State does not appear to be a justified registration, the transferee State Council can certainly decline to accept that registration for the purpose of carrying on the profession of a pharmacist in the

transferee State, or cancel such registration once effected. Such scrutiny is permissible at the time of initial registration, and also later when complaints are received, leading to the enquiry for the purpose of removal from their register. [Para 13] [851-F-H; 852-A-F]

1.5 The purpose of a welfare statute cannot be permitted to be defeated by the methods such as the one employed by the appellant. The Act is passed for making better provisions for the regulation of the profession and practice of pharmacy. The primary qualification for such a person is to have a degree or diploma in pharmacy. It is only as an alternative qualification that some other degree with three years experience is permitted. The last alternative qualification is that of five years experience in dispensing drugs which has to be in the concerned State. This is because under Section 31 of the Act, the person who wants to be registered as a pharmacist has to be of 18 years of age, and he has to reside and carry on the business or profession of pharmacy in that particular State. The State Pharmacy Council which issues the certificate of registration ought to satisfy itself that the person concerned did have atleast five years of experience, and which experience has obviously to be in that State for the State Council to assess it. [Para 15] [853-B-F]

1.6 In the instant case, the appellant did not reside or carry the business or profession of pharmacy or dispensing of drugs in Sikkim for more than five years. If any such method, as adopted by the appellant is permitted, persons who claim to have experience of five years in one State, would go to another State for a few months only to obtain registration in that State, and thereafter, seek transfer of that registration to their own state. The first respondent did not have any opportunity to examine as to whether the appellant did have the experience of five

years in Rajasthan. The only submission of the appellant is that the papers which concerned the so-called experience were submitted to the Sikkim Tribunal alongwith the certificate of employer of the appellant in Sikkim where he worked for just two months. The consequences of accepting appellant's plea would mean that the transferee State would have to accept a person as a pharmacist when it did not have the opportunity to examine the material with respect to his experience of more than five years. The requirement of five years experience in the registering State would be defeated if any such methods are permitted. Thus, there is no error in the decision of the first respondent in canceling registration of the appellant, nor the decision of the Single Judge as well that of the Division Bench approving the same. [Paras 15 and 16] [853-F-H; 854-A]

Maruti Wire Industries Pvt. Ltd. Vs. S.T.O. 1st Circle, **Mattancherry 2001 (3) SCC 735: 2001 (2) SCR 829 - referred to.**

Case Law Reference:

1971(3) SCC 844	**Referred to**	**Para 9**
2001 (2) SCR 829	**Referred to**	**Para 14**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 6895 of 2008.

From the Judgment & Order dated 8.8.2006 of the High Court of Judicature for Rajasthan, Jaipur Bench, Jaipur, in D.B. Special Appeal (Writ) No. 507 of 2006 in S.B. Civil Writ Petition No. 4309 of 2005.

Anurag Sharma, Prashant Kumar, Ap & J Chambers for the Appellant.

Pramod Swarup, Vikrant Yadav, Tapan Masta, Sushma Verma, Pooja Sharma, Akshay Verma, M.C. Dhingra, Vivek Gupta for the Respondents.

The Judgment of the Court was delivered by

H.L. GOKHALE, J. 1. This appeal by special leave is directed against the judgment and order dated 8.6.2006 passed by a Division Bench of the High Court of Rajasthan, Jaipur Bench, in D.B. Special Appeal (Writ) No. 507/2006 arising out of S.B. Civil Writ Petition No. 4309/2005, whereby the Writ Petition filed by the appellant was dismissed.

Short facts leading to this appeal are as follows:-

2. The appellant claims that after passing the Secondary School Examination in 1986, he worked in a Medical Store named as 'Todi Medicals' at Sikar in the state of Rajasthan from October 1991 to March 1997. It is his case that though on the basis of his experience, he was otherwise eligible to be enrolled as a pharmacist in Rajasthan, he could not get so enrolled since by the time he could apply, the registration of pharmacists in Rajasthan was closed. He claims that thereafter he shifted to Sikkim in August, 2001, where he worked for about two months in a medical store at Gangtok. On the basis of the certificate issued by his employer in Sikkim, he applied for registration as a pharmacist with the Sikkim State Pharmacy Tribunal (Sikkim Tribunal for short), and he was so registered over there on 5.12.2001.

3. The purpose of his sojourn to Sikkim having been achieved, the appellant returned to Kherli in the State of Rajasthan towards the beginning of January 2002. On the basis of this registration from Sikkim, he applied on 8.4.2002 for his registration with the Pharmacy Council of the State of Rajasthan (respondent No.1 herein – 'Rajasthan Council' for short) under Section 32 of The Pharmacy Act, 1948 (hereinafter referred to as 'the Act').

4. It is the further case of the appellant that the Rajasthan Council made necessary enquiries with the Sikkim Tribunal, and thereafter enrolled him as a registered pharmacist by their registration certificate dated 4.6.2002. It however, appears that some complaints were received by the Government of Rajasthan (respondent No.2) with respect to functioning of a large number of in-eligible pharmacists in the State. Consequently, on being informed about the same, the Rajasthan Council decided to look into such cases. On 22.7.2004, a notice was issued by the first respondent to the appellant informing him that Enquiry Committee constituted by the Rajasthan Council had found his registration to be irregular, and therefore, he should appear before the Executive Committee of the Council on 2.8.2004, to explain as to why his name should not be removed from the Register of Pharmacists of Rajasthan by invoking its powers under Section 36 of the Act. The appellant did not care either to reply, or to remain present before the Executive Committee. The Executive Committee, therefore, considered the material on record, and took the decision to cancel his registration. This decision was approved by the Full Council on 16.3.2005 and the appellant was informed to surrender his certificate of registration by the Council by its further communication dated 12.4.2005.

5. The appellant filed a Writ Petition to challenge this decision of the first respondent. The said Writ Petition bearing No. 4309/2005 was heard by a Single Judge of the Rajasthan High Court. The appellant did not dispute the fact that he did not appear before the Executive Committee, nor did he dispute any of the aforesaid facts. The learned Single Judge accepted the submission of the respondents that the appellant had an alternative remedy to file an appeal under section 36(4) of the Act which he had not exhausted. That apart, he also noted that though the appellant was given an opportunity of personal hearing by the Executive Committee, he did not place any convincing proof of his registration having been done as per provisions of the Act by the Sikkim Tribunal. The learned Single Judge also

noted that no such documents were produced before him also, which would indicate that the appellant had acquired necessary experience in Sikkim, before obtaining the registration over there. The learned Single Judge therefore, dismissed the said Writ Petition by his judgment and order dated 7.4.2006.

6. Aggrieved by this decision, the appellant filed a D.B. Special Appeal (Writ) No. 507/2006. It was submitted on behalf of the appellant that the State Government had no business to make an enquiry about the validity of appellant's registration, nor the Executive Committee had any authority to cancel his registration with the Rajasthan Council which had issued the same to him on the basis of his registration in another State. As far as the first submission is concerned, the Division Bench took the view that the State Government did have the authority to look into the complaints, which it received from the citizens. It had merely brought those complaints to the notice of the Rajasthan Council. Ultimately, it is the Executive Committee of the Rajasthan Council which had taken necessary decision after calling upon the appellant to attend an enquiry, which he did not. As far as the decision of the Rajasthan Council is concerned, it was held that the appellant had failed to prove that his registration in Sikkim could be considered to be a valid one for Rajasthan since he had not worked for requisite period in Sikkim. The Division Bench, therefore, held that the decision of the Executive Committee of the first respondent could not be faulted. The appeal was accordingly dismissed.

7. Being aggrieved by this judgment and order, the present appeal has been filed. The principle submission of the appellant's counsel is that the first respondent having granted registration to the appellant after making an initial enquiry with the Sikkim Tribunal, could not review its decision, and secondly, in any case, the appellant had the necessary qualification for his registration with the first respondent under Section 31 of the Act, and therefore the orders of the Executive Committee, as well as the two judgments and orders, are required to be set aside. The

counsel for the respondents, on the other hand, defended the decision of the first respondent as well the two judgments and orders, as being perfectly justified.

Consideration of the rival submissions

8. Now, if we see the Preamble of The Pharmacy Act, 1948, it states, that it is an Act to make better provisions for the regulation of the profession and practice of pharmacy, and for that purpose to constitute the Pharmacy Councils. The Act provides for entry of the names in the Register of Pharmacists in three stages:

(i) The first stage is entry of names in the first register under Section 30 of the Act. Qualifications for such entry are given in Section 31 of the Act. Under Section 30(2), the State Government is required to fix a date by notification, and applications for registration must be made by the appointed date.

(ii) The second stage is where people fail to apply for entry in First register, they can apply for registration u/s 32(1) if they satisfy the requisite qualifications.

(iii) The third stage is for registration u/s 32 (2) of the Act as per education regulations, or as a registered pharmacist in another state.

The qualifications for entry in the first register are provided under Section 31 of the Act which reads as follows:-

"31 - *Qualifications for entry on first register*

[A person who has attained the age of eighteen years shall be entitled] on payment of the prescribed fee to have his name entered in the first register if he resides, or carries on the business or profession of pharmacy, in the State and if he—

(a) holds a degree or diploma in pharmacy or pharmaceutical chemistry or a chemist and druggist diploma of an Indian University or a State government as the case may be, or a prescribed qualification granted by an authority outside {The words "the Provinces of" omitted by the A.O.1950.} India, or

(b) holds a degree of an Indian University other than a degree in pharmacy or pharmaceutical chemistry, and has been engaged in the compounding of drugs in a hospital or dispensary or other place in which drugs are regularly dispensed on prescriptions or medical practitioners for a total period of not less than three years, or

(c) has passed an examination recognised as adequate by the State Government for compounds or dispensers, or

(d) has been engaged in the compounding of drugs in a hospital or dispensary or other place in which drugs are regularly dispensed on prescriptions of medical practitioners for a total period of not less than five years prior to the date notified under sub-section (2) of section 30."

As the Section itself shows, that to be a pharmacist, importance is given to have a degree or diploma in pharmacy, failing which any other degree is permitted with three years experience of dispensing medicines, or passing of an examination recognised by the State Government, or having an experience of not less than five years of working in a hospital or dispensary in which drugs are regularly dispensed on prescriptions of medical practitioners.

9. Section 32 of the Act provides for subsequent registration, which also includes amongst the qualified categories, a

registration on the basis of being a registered pharmacist in another State. The submission of the appellant was that he was already registered in Sikkim, which registration was accepted by the first respondent, and therefore, the first respondent issued him its registration certificate on 5.12.2001. The Executive Committee of the first respondent could not review the decision once taken, since there was no provision for review in the Act. In support of this proposition, he relied on the judgment of this Court in *Patel Narshi Thakershi and Ors. Vs. Shri Pradyumansinghji Arjunsinghji* reported in 1971(3) SCC 844.

10. In this behalf, what is material to note is that the first respondent has taken the action against the appellant under Section 36 of the Act. This Section reads as follows:-

"36 - *Removal from register*

(1) Subject to the provisions of this section, the Executive Committee may order that the name of a registered pharmacist shall be removed from the register, where it is satisfied, after giving him a reasonable opportunity of being heard and after such further inquiry if any, as it may think fit to make.—

(i) that his name has been entered in the register by error or on account of misrepresentation or suppression of a material fact, or

(ii) that he has been convicted of any offence or has been guilty of any infamous conduct in any professional respect which in the opinion of the Executive Committee, renders him unfit to be kept in the register, or

(iii) that a persons employed by him for the purposes of his business of pharmacy. {Ins. by s.13, ibid.(w.e.f.1-5-1960).} [or employed to work under him in connection with any business of pharmacy] has been convicted of any such offence or has been guilty of any such infamous conduct as would, if such person were a registered pharmacist, render him liable to have his name removed from the register under clause (ii):

Provided that no such order shall be made under clause (iii) unless the Executive Committee is satisfied—

(a) that the offence or infamous conduct was instigated or connived at by the registered pharmacist, or

(b) that the registered pharmacist has at any time during the period of twelve months immediately preceding the date on which the offence or infamous conduct took place committed a similar offence or been guilty of similar infamous conduct, or

(c) that any person employed by the registered pharmacist for the purposes of his business of pharmacy [or employed to work under him in connection with any business of pharmacy] has at any time during the period of twelve months immediately preceding the date on which the offence or infamous conduct took place, committed a similar offence or been guilty of similar infamous conduct, and that the registered pharmacist had, or reasonably ought to have had, knowledge of such previous offence or infamous conduct, or

(d) that where the offence or infamous conduct continued over a period, the registered pharmacist had, or reasonably ought to have had, knowledge of the continuing offence or infamous conduct, or

(e) that where offence is an offence under the.{ Substitute. by Act 70 of 1976, s.18, for "Drugs Act, 1940" (w.e.f.1-9-1976).} [Drugs and Cosmetics Act, 1940] (23 of 1940), the registered pharmacist has

not used due diligence in enforcing compliance with the provisions of that Act in his place of business and by persons employed by his [or by persons under his control]

(2) An order under sub-section (1) may direct that the person whose name is ordered to be removed from the register shall be ineligible for registration in the State under this Act either permanently or for such period as may be specified.

(3) An order under sub-section (1) shall be subject to confirmation by the State Council and shall not take effect until the expiry of three months from the date of such confirmation.

(4) A person aggrieved by an order under sub-section (1) which has been confirmed by the State Council may, within thirty days from the communication to him of such confirmation, appeal to the State Government, and the order of the State Government upon such appeal shall be final.

(5) A person whose name has been removed from the register under this section or under sub-section (2) of section 34 shall forthwith surrender his certificate or registration to the Registrar, and the name so removed shall be published in the Official Gazette."

11. Section 36 (1) (i) provides for removing the name of a registered pharmacist in the event there is an error in his registration, or where it is registered on account of misrepresentation or suppression of a material fact. In our view, this sub-section gives sufficient power to the Executive Committee to recall its decision. In the instant case obviously, there was an error on the part of the first respondent in accepting the registration from Sikkim as a valid registration for transfer of the appellant as a pharmacist in Rajasthan. Ultimately, it is the State Pharmacy Council which is responsible for having well-equipped pharmacists in the State who have the requisite

qualifications and/or experience. The fact is that the second respondent had received complaints with respect to a large number of in-eligible persons functioning as pharmacists. Therefore, when this fact was brought to the notice of the first respondent, a notice was given to the appellant affording him a personal opportunity as required under Section 36 (1) of the Act. However, the appellant did not avail of this opportunity. Hence, all that the Executive Committee had done was to consider the material on record and to cancel his registration in Rajasthan. The Executive Committee of the first respondent had not cancelled his registration in Sikkim. It cannot, therefore, be said that the Executive Committee had exercised the power of review without being empowered for the same under the statute or that it had exercised it erroneously.

12. There is no dispute that the appellant was given a notice of hearing. There is also no dispute that the appellant did not produce any evidence as to how his registration in Sikkim was a valid registration. This is because there was no dispute that he stayed in Sikkim just for a few months, and he has himself contended that he did not have any documentary evidence to claim that he stayed in Sikkim for five years, or that he had the necessary experience of not less than five years of work in dispensing medicines in Sikkim. This is because at the highest, his case with respect to his qualification was one under Section 31 sub-clause (d) of the Act.

13. It is true that section 32 of the Act does entitle a registered pharmacist in one State to have his name entered in the register of another State. Section 33 of the Act, however, gives the power of scrutiny to the State Council and every enrolment is subject to the scrutiny. Thereafter, if the State Council receives any complaint concerning the eligibility of a person to function as a pharmacist, the Executive Committee of the Council does have the power to make necessary enquiry under Section 36 of the Act, and if satisfied, to remove the name of such a registered pharmacist though after giving him a

reasonable opportunity of being heard. Sub-section (i) of Section 36 (1) gives the grounds on which a name can be removed from the register. In the instant case, the Executive Committee was satisfied that there was an error in enrolling the appellant as a registered pharmacist. At that stage, the appellant has been called upon to give his explanation. In this enquiry, one State Council can certainly look into the prima-facie material on the basis of which registration was granted in another State. This is because the State Council is given the power to scrutinize such applications, and if such registration has been permitted by any error to that extent, it can certainly take the corrective step. Such a decision cannot amount to sitting in appeal over the decision of another State's Council. This is because the concerned State Council is answerable to the persons purchasing the medicines from the pharmacists in the State. It is its duty to see that pharmacists do have necessary educational qualifications or the experience as required. In a country where there is so much illiteracy, the requirements concerning educational qualifications or experience of the pharmacist have to be scrupulously scrutinized. If the registration of the concerned pharmacist obtained from another state does not appear to be a justified registration, the transferee State Council can certainly decline to accept that registration for the purpose of carrying on the profession of a pharmacist in the transferee State, or cancel such registration once effected. Such scrutiny is permissible at the time of initial registration, and also later when complaints are received, leading to the enquiry for the purpose of removal from their register.

14. It was submitted on behalf of the appellant that in the instant case, the act did not provide a solution to this type of problem. The appellant relied upon the judgment of this Court in *Maruti Wire Industries Pvt. Ltd. Vs. S.T.O. 1st Circle, Mattancherry* reported in 2001 (3) SCC 735 to submit that where the Legislature was silent about any particular aspect, the same could not be supplied by judicial interpretative process. As seen above, in the instant case, the provisions of the Act are sufficiently

clear, and therefore, the actions of the respondent could not be faulted.

15. The purpose of a welfare statute cannot be permitted to be defeated by the methods such as the one employed by the appellant. As stated earlier, the Act is passed for making better provisions for the regulation of the profession and practice of pharmacy. As is seen, the primary qualification for such a person is to have a degree or diploma in pharmacy. It is only as an alternative qualification that some other degree with three years experience is permitted. The last alternative qualification is that of five years experience in dispensing drugs which has to be in the concerned State. This is because under Section 31 of the Act, the person who wants to be registered as a pharmacist has to be of 18 years of age, and he has to reside and carry on the business or profession of pharmacy in that particular state. The State Pharmacy Council which issues the certificate of registration ought to satisfy itself that the person concerned did have atleast five years of experience, and which experience has obviously to be in that State for the State Council to assess it. In the instant case, the appellant did not reside or carry the business or profession of pharmacy or dispensing of drugs in Sikkim for more than five years. If any such method, as adopted by the appellant is permitted, persons who claim to have experience of five years in one State, will go to another State for a few months only to obtain registration in that State, and thereafter seek transfer of that registration to their own state. In the instant case, the first respondent did not have any opportunity to examine as to whether the appellant did have the experience of five years in Rajasthan. The only submission of the appellant is that the papers which concerned the so-called experience were submitted to the Sikkim Tribunal alongwith the certificate of employer of the appellant in Sikkim where he worked for just two months. The consequences of accepting appellant's plea will mean that the transferee State will have to accept a person as a pharmacist when it did not have the opportunity to examine the material with respect to his experience of more than five years.

The requirement of five years experience in the registering State will be defeated if any such methods are permitted.

16. In the circumstances, we do not find any error in the decision of the first respondent in canceling registration of the appellant, nor the decision of the Single Judge as well that of the Division Bench approving the same.

17. We therefore, pass the following order:

(a) The Civil Appeal is, hereby dismissed.

(b) There will be no order as to costs.

N.J. Appeal dismissed.

RATTAN BAI & ANR.
v.
RAM DASS & ORS.
(Civil Appeal No. 1614 of 2012)

FEBRUARY 06, 2012

[P. SATHASIVAM AND J. CHELAMESWAR, JJ.]

SUIT: Withdrawal of - Suit for specific performance by respondent 1 to 3 - Application P-2 filed by Advocate on behalf of respondents that in view of compromise with defendants, suit be dismissed - Trial court did not pass any order - Application (P-4) made by Advocate on behalf of respondent 1 and 3 that they intended to withdraw the suit - Respondent 1 gave another affidavit (P-5) that the said suit was not filed by him - The counsel of the respondents made statement that he did not press the applications P-2 and P-4 - In view of the said statement, trial court disposed of the said two applications and posted the matter for evidence - Revision petition by appellant dismissed by High Court - On appeal, held: The issue was not whether the trial court has the power to permit the withdrawal of the applications filed earlier to the withdrawal of the suit but whether such power was exercised in accordance with law and for the purpose for which it is meant - The mere existence of a power did not justify the exercise of the power - The fact situation on hand did not justify permitting the respondents 1 and 3 to withdraw their earlier application (P-2) and the statement P-4 as a matter of course in the background of the content of the affidavit (P-5) - The professional conduct of the counsel apart from anything else amounted to the abuse of the process of the court - High Court erred in dismissing the revision petition of the appellants - Matter remitted to High Court for consideration afresh.

Respondents 1 to 3 instituted a suit for specific

performance of an agreement of sale of immovable property and for the possession of the said property against the appellants and others. The appellants filed a written statement on 2.12.2006. On 18.12.2007, an application (Annexure P-2) was filed on behalf of respondents 1 to 3 but signed only by respondents 1 and 3 alone. The application was accompanied by an affidavit of respondent 3, wherein he made a statement that he had compromised the suit with defendants and he did not wish to continue the suit, and, therefore the same be dismissed. Annexure P-3, purportedly a vakalatnama in favour of one 'S', advocate in the said suit was executed on the same day, i.e. 18.12.2007 by the respondents 1 to 3. However, Annexure P-2, application was signed by an advocate by name 'AK' along with respondents 1 and 3. The trial court did not pass any order either accepting or rejecting the application. On 4.8.2010, a joint statement (Annexure P-4) of respondent 1 and the advocate 'AK' allegedly representing respondents 1 and 3 was recorded by the trial court stating that they intended to withdraw the suit.

On 7.8.2010, respondent 1 gave another affidavit (Annexure P-5) before the trial court to the effect that the said suit was neither filed by him nor the said suit bore his signatures. Thereafter, the appellants filed an application praying that the suit be dismissed in so far as it pertained to respondents Nos. 1 and 3. Another application (Annexure P-8) was filed on 16.9.2010 purportedly on behalf of respondent 1 stating that application dated 18.12.2007 (annexure P-2) and the statement dated 4.8.2010 (annexure P-4) was wrongly submitted by the Advocate 'AK' and, therefore, respondent 1 be allowed to withdraw the same and pursue the suit.

On 1.2.2011, the trial court recorded the statement by

one 'MS', Advocate said to be appearing for the respondents that he did not press the application dated 18.12.2007 and 4.8.2010. Thereupon the trial court passed an order that in view of the statement of the advocate, the applications dated 18.12.2007 and 4.8.2010 were disposed of. Aggrieved by the said order, the appellants filed revision petition before the High Court. The said revision was dismissed. The instant appeal was filed challenging the order of the High Court.

Allowing the appeal and remitting the matter to the High Court, the Court

HELD: 1. The issue was not whether the trial court has the power to permit the withdrawal of the applications filed earlier to the withdrawal of the suit but whether such power was exercised in accordance with law and for the purpose for which it is meant. The mere existence of a power did not justify the exercise of the power. In the context of the powers of the judicial bodies, all powers are required to be exercised with a view to secure ends of justice. The fact situation on hand did not justify permitting the respondents 1 and 3 to withdraw their earlier applications (p.2) dated 18.12.2007 and the statement of respondent 1 dated 04.08.2010 as a matter of course in the background of the content of the affidavit (p.5) dated 7.8.2010. If the content of P.5 is proved to be false, appropriate legal action against the 1st respondent must be taken. The professional conduct of the counsel 'AK' apart from anything else amounts to the abuse of the process of this Court. The High Court erred in dismissing the revision of the appellants. [Paras 23, 25, 26] [864-F-H; 866-B-F]

Jet Ply Wood (P) Ltd. and anr. v. Madhukar Nowlakha & Ors. **(2006) 3 SCC 699: 2006 (2) SCR 761;** *Rajendra Prasad Gupta v. Prakash Chandra Mishra & Ors.* **(2011) 2 SCC 705: 2011 (1) SCR 321- Distinguished.**

Case Law Reference:

2006 (2) SCR 761	**Distinguished**	**Para 22, 24**
2011 (1) SCR 321	**Distinguished**	**Para 22**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 1614 of 2012.

From the Judgment & Order dated 8.3.2011 of the High Court of Punjab & Haryana at Chandigarh in C.R. No. 1075 of 2011.

Brijender Chahar, K.R. Anand, Jyoti Chahar, Jagbir S. Malik, Vinay Garg for the Appellants.

Uday U. Lalit, S. Padhi, Siddhesh Kotwal, Nirnimesh Dube, Sandeep Phogat, Jayant Kumar Mehta for the Respondents.

The Judgment of the Court was delivered by

CHELAMESWAR, J. 1. Leave granted.

2. This appeal arises out of the final order dated 8th March, 2011 of the Punjab and Haryana High Court in Civil Revision No. 1075 of 2011 under Article 227 of the Constitution of India. By the said order, the High Court dismissed the Revision filed by the appellants herein.

3. Respondent Nos.1 to 3 herein instituted a Civil Suit No. RBT 124/22.05.2006 on the file of Civil Judge, Senior Division (S.D.) Jhajjar, against the two appellants herein and two others.

4. Respondents 4 to 7 herein are the legal representatives of one Kanta Bai, who died during the pendency of the suit and

the said Kanta Bai was one of the other two defendants in the suit.

5. Unfortunately, copy of the plaint is not available on record but it appears that the suit was filed for the specific performance of an agreement of sale of immovable property and for the possession of the said property.

6. The defendants (appellants herein) contested the suit. They filed a written statement on 2.12.2006.

7. On 18.12.2007, an application (Annexure P-2) came to be filed purportedly on behalf of the three plaintiffs (respondents 1 to 3 herein), but signed only by respondents 1 and 3 alone. The relevant portion reads as follows:-

> "Aforementioned titled case is fixed for 4.8.2010 for defendants evidence and in the afore-stated case the applicant plaintiff has compromised with the defendant in the suit I have neither any claim against the defendant nor I intend to continue the suit.
>
> Therefore, it is prayed that file be summoned and the suit on behalf my self plaintiff no.3 be dismissed and file be consigned, I will be highly grateful."

The application was accompanied by an affidavit of the third respondent herein, wherein he made a statement that he had compromised the suit with defendants and he did not wish to continue the suit, and, therefore the same be dismissed.

8. Annexure P-3, purportedly a vakalatnama in favour of one Shri A.K. Saini, advocate in the above mentioned civil suit, came to be executed on the same day, i.e. 18.12.2007 by the respondents 1 to 3. However, it must be mentioned herein that Annexure P-2, application was signed by an advocate by name Shri Arun Kumar along with two plaintiffs mentioned above.

9. The trial court did not pass any order either accepting or

rejecting the application. (Annexure P-2)

10. On 4.8.2010, a joint statement (Annexure P-4) of first respondent and the above-mentioned advocate Shri Arun Kumar allegedly representing respondents 1 and 3 herein was recorded by the Trial Court. The relevant portion reads as follows:-

> "…….stated that we do not intend to continue with the suit and withdraw the suit on behalf of plaintiff no.1 and 3."

11. On 7.8.2010, the first respondent herein gave another affidavit (Annexure P-5) before the Trial Court. The relevant portion reads as follows:-

> "1. That above noted suit has neither filed by me nor above noted suit bears my signatures.
>
> 2. That pertaining to the agreement to sell we were not having sufficient funds within limitation and my compromise with Rattan Bai, Ram Phool took place in the year 1999.
>
> 3. That in the afore-stated case I have neither furnished any power of attorney as plaintiff nor any General Power of Attorney has been given by me.
>
> 4. That in the afore-stated suit I have falsely been impleaded as plaintiff and my signatures are also forged.
>
> 5. That in the aforesaid suit I have neither engaged any counsel nor purchased any stamp nor any witness has been produced by me on my behalf. The entire proceedings in this case carried out on my behalf are false and forged."

12. In the background mentioned above, an application, Annexure P-7, came to be filed on behalf of the appellants herein. It does not contain any date. But in the opening paragraph of the said application it is stated as follows:-

> "That the above noted civil bearing no.124 of 2006 is pending in this Hon'ble Court and the same is fixed for hearing on 28.1.2010."

13. The normal inference of the above extracted statement should be that the application was filed sometime prior to 28th January, 2007. However, the remaining paragraphs referred to events which took place on 4.8.2010 i.e. the date of joint statement (exhibit P-4). It is not clear from the record whether the Annexure P-7 is a true copy of certified copy of the application filed by the appellant herein. The appellant herein owes an explanation with regard to the discrepancy of the dates referred to above. Para 4 of the said application reads as follows:-

> "That the defendants applicants are not alleging any malafide intention on the part of the learned presiding officer inspite of the fact that some undesirable persons are claiming that they have approached the learned presiding officer and the order for withdrawal and dismissal of the suit qua the claim and relief claimed by plaintiffs nos.1 and 3 will not be passed nor the suit will be dismissed. But it appears that inadvertently and due to oversight the orders for dismissal of the suit filed by plaintiffs nos.1 and 3 has not been passed inspite of the statement dated 4.8.2010 made by their counsel along with Ram Dass plaintiff read with the application moved earlier by Jawahar plaintiff No.3.
>
> It is, therefore, prayed necessary orders for dismissal of civil suit on behalf of plaintiffs 1 and 3 may kindly be passed keeping in view the above said circumstances as they have already withdrawn the same and have sought the dismissal of their suit."

In substance, praying that the suit be dismissed in so far as it pertains to respondents Nos. 1 and 3 herein.

14. As the matter stood, thus, another application (Annexure

P-8) came to be filed on 16.9.2010 purportedly on behalf of the first respondent herein. The substance of the application is that annexure P-2 application dated 18.12.2007 and the statement dated 4.8.2010 (annexure P-4) had been wrongly submitted by the above-mentioned Advocate Shri Arun Kumar and, therefore, the first respondent herein be allowed to withdraw the same and pursue the suit. The prayer portion is as follows:-

> "It is therefore prayed that the application dated 4.8.10/18.12.07 has been wrongly submitted before the Hon'ble Court by Sh. Arun Kumar Advocate. Hence applicant may please be allowed to withdraw the said application dated 4.8.10/18.12.07 and further be retained as a plaintiff in the said suit in the interest of justice."

15. It is also stated in para 3 of the affidavit as follows:-

> "That the applicant never engaged Sh. Arun Kumar as his advocate and further never intended to submit such applicant. The applicant/plaintiff has not reached to a compromise with defendants."

16. The said application was supported by an affidavit of the first respondent herein wherein the first respondent reiterated the various allegations made in the application portions of which are extracted earlier. An identical application and affidavit (Annexure P-9) also came to be made by the third respondent herein on the same date i.e. on 16.9.2010.

17. Such applications were contested by the appellants herein by filing a counter.

18. On 1.2.2011 the trial court recorded the statement by one Shri M.S. Gulia, Advocate said to be appearing for the plaintiffs. The statements as follows:-

> "....Stated that I do not press the application dated 18.12.2007 and 4.8.2010."

19. Thereupon the trial court passed an order on the same date which reads as follows:-

> " Sh. M.S. Gulia Ld. Counsel for plaintiff has made a statement that he does not press the application order dated 18.12.2007 & 4.8.2010, accordingly. Both the applications is disposed off accordingly. Now come upon 8.2.2011 for rebuttal evidence, if any and arguments."

20. Aggrieved by the said order, the appellants herein carried the matter by way of Revision under Article 227 of the Constitution of India to the Punjab and Haryana High Court by the order under appeal. The said revision was dismissed. The High Court held -

> "The learned trial Court was well within its jurisdiction to allow the withdrawal of application dated 18.12.2007 and statement dated 4.8.2010 under its inherent powers and this view can be supported by way of the latest judgment of Hon'ble Supreme Court in *Rajinder Prasad Gupta v. Prakash Chandra Mishra* (2011) 2 Supreme Court Cases 705 ……………."

The High Court after examining four paragraphs of the above-mentioned judgment finally held –

> "In my considered opinion, the impugned order is innocuous and no prejudice will be caused to the defendants-petitioners as they will have full opportunity to present their case before the learned trial Court at the relevant stage.
>
> Keeping in view the facts and circumstances discussed hereinabove, this Court finds no illegality or perversity in the impugned order dated 1.2.2011 (P.16) passed by the learned Civil Judge (Sr. Division), Jhajjar warranting interference under Article 227 of the Constitution."

21. Learned senior counsel for the appellant Mr. Brijender Chahar argued that the High Court erred in dismissing the Revision. He further submitted that the question is not whether the trial Court had the inherent power to permit the respondent-plaintiffs to go back on their earlier "applications" dated 4.8.2010 and 18.12.2007 but in the circumstances of the case particularly in the background of the reasons given in the affidavit dated 7.8.2010 (p.5) wherein the 1st respondent herein made a categoric allegation that he had been "falsely impleaded as a plaintiff" and his signatures are "forged" etc. whether the inherent power of the Court was exercised in accordance with the well established principles of law.

22. On the other hand, learned senior counsel for the respondent Mr. Uday U. Lalit argued that even in cases where an application for withdrawal of the suit is allowed, it is held by this Court that nothing prevents the plaintiffs to go back upon the withdrawal. Therefore, nothing in law prevents the respondents/ plaintiffs to withdraw their applications for the withdrawal of the suit. The learned counsel relied upon *Jet Ply Wood (P) Ltd. and anr. Vs. Madhukar Nowlakha & Ors.,* (2006) 3 SCC 699 and *Rajendra Prasad Gupta Vs. Prakash Chandra Mishra & Ors.,* (2011) 2 SCC 705 in support of his submissions.

23. As rightly contended by the learned counsel for the appellant, the issue is not whether the trial court has the power to permit the withdrawal of the applications filed earlier to the withdrawal of the suit but whether such powers was exercised in accordance with law and for the purpose for which it is meant. The mere existence of a power does not justify the exercise of the power. In the context of the powers of the judicial bodies, all powers are required to be exercised with a view to secure ends of justice. In neither of the above-mentioned two cases this Court had an occasion to examine whether the inherent power of the Civil Court under Section 151 CPC was properly exercised. In the 1st case, the suit had been withdrawn by the plaintiffs and the plaintiffs subsequently sought to go back upon the withdrawal

and reopen the suits on the ground that they were induced to withdraw the suit on a misrepresentation made by the defendants. In the 2nd case, the plaintiff "changed his mind" after filing the applications for withdrawal of the suit and sought to withdraw the said application even before a formal order permitting the withdrawal was passed the Court. The argument in both the cases was the trial Court lacked the jurisdiction to permit the course of action undertaken by the plaintiffs. This Court only laid down the principle that Section 151 of CPC recognises* the existence of ample power on the Civil Court to permit the plaintiffs to pursue the course of action undertaken by them.

24. In *Jet Ply Wood* (supra), the trial Court rejected the application of the plaintiffs "recalling the order by which the suit had been permitted to be withdrawn". The High Court recalled the order and restored the suit. Dealing with the case, this Court held at para 24 -

> "……………… which indicates that the court did not find any scope to exercise its inherent powers under Section 151 of the Code of Civil Procedure for recalling the order passed by it earlier. In the circumstances set out in the order of 24..2004, the learned trial court felt that no case had been made out to recall the order which had been made at the instance of the plaintiff himself. It was, therefore, not a question of lack of jurisdiction but the conscious decision of the court not to exercise such jurisdiction in favour of the plaintiff."

This Court did not examine the question whether "the conscious decision of the Court not to exercise such jurisdiction" was justified. This Court only held that the High Court's decision to reverse the trial Court's order - not to permit the recall of the earlier order permitting the withdrawal of the suit - does not call for interference.

> "27. We are of the view that the law having been correctly stated in the aforesaid case, the learned Singl Judge of the Calcutta High Court in making an order on the same lines did not commit any error of jurisdiction which calls for any interference in these appeals."

25. But the fact situation on hand does not, in our opinion, justify permitting the respondents 1 and 3 to withdraw their earlier applications (p.2) dated 18.12.2007 and the statement of the 1st respondent dated 04.08.2010 as a matter of course in the background of the content of the affidavit (p.5) dated 7.8.2010. If the content of p.5 is proved to be false, there is no validly constituted suit at least on behalf of the 1st respondent. Secondly, the professional conduct of the counsel Mr. Arun Kumar may require an examination in the interest of the purity of a justice delivery system. If the content of P.5 is proved to be false, appropriate legal action against the 1st respondent must be taken. His conduct apart from anything else amounts to the abuse of the process of this Court.

26. In the circumstances, we are of the view that the High Court erred in dismissing the revision of the appellants herein.

27. We allow the appeal and remit the matter to the High Court for an examination of the factors indicated above and any other relevant factor which the High Court may deem appropriate, if necessary even by taking evidence, and pass appropriate orders in accordance with law. The trial of the suit shall stand stayed until the High Court takes a final decision as indicated above.

D.G. Appeal allowed.