IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL (IT) NO.1169 OF 2018

Commissioner of Income Tax (IT)-2 ...Appellant

Versus

M/s. HSBC Bank (Mauritius) Ltd. ...Respondent

Mr. Suresh Kumar with Ms. Mohinee Chougule, for Appellant.
Mr. P. F. Kaka, Senior Advocate, with Mr. Niraj Sheth, i/b. Mr. Atul K. Jasani, for Respondent.

CORAM: K. R. SHRIRAM &
DR. NEELA GOKHALE, JJ.
DATED: 24th January 2024

PC:-

1. Appellant has preferred this Appeal under Section 260A of the Income Tax Act, 1961 ("**the Act**") impugning an order pronounced on 16th December 2016 by the Income Tax Appellate Tribunal ("**ITAT**"). The appeal pertains to Assessment Year 2011-12.

2. Respondent-Assessee is a Limited Liability Company incorporated and registered in and tax resident of Mauritius. It is admittedly a Foreign Institutional Investor ("**FII**") duly licensed by the Securities and Exchange Board of India ("**SEBI**"). During the course of assessment proceedings, the Assessing Officer ("**AO**") noticed that assessee earned an amount of Rs.94,57,45,856/- as interest income on securities. Assessee claimed the same as Exempt Income under Article 11(3) of the Indo-Mauritius Double Taxation Avoidance

Agreement ("**DTAA**"). The AO did not accept assessee's claim that the interest income from securities in India was exempt from tax in India as per clause (c) of Article 11(3) of the DTAA. The AO, however, had accepted that assessee's income from External Commercial Borrowings ("**ECB**") was exempt under Section 90 of the Act read with Article 11 of the DTAA as the company was carrying on *bona fide* banking business in Mauritius.

3. Against the order disallowing the interest income from securities in India, assessee filed objections with the Dispute Resolution Panel ("**DRP**") under Section 144C of the Act. The DRP upheld the findings of the AO based on which the AO passed the assessment order under sub-section (13) of Section 144C of the Act r/w 143(3) of the Act. The matter was carried in appeal to the ITAT and the ITAT allowed assessee's appeal and by the impugned order held that the interest income on securities was exempt from tax in India under Clause (c) of Article 11(3) of the DTAA.

4. It is this order, which is impugned in the Appeal and the following five substantial questions of law are proposed:

> *(a) "Whether on the facts and the circumstances of the case and in law, Hon'ble Tribunal has erred in holding that assessee in involved in bonafide banking activity, whereas on the other hand Hon'ble Tribunal has accepted that the assessee has failed to prove beneficial ownership of funds which have bearing on establishment of bonafide banking activity of assessee and has already set-aside on this issue?"*
>
> *(b) "Whether on the facts and the circumstances of the case*

and in law, Hon'ble Tribunal has erred in holding that the assessee is involved in bonafide banking activities ignoring the fact that assessee has even not furnished the financials e.g. Annual reports etc during the course of assessment proceedings, whereas Hon'ble ITAT has itself held that onus is on assessee to demonstrate that assessee is not conduit company for the benefit of third person?"

(c) "Whether on the facts and the circumstances of the case and in law, Hon'ble Tribunal has erred in holding assessee is involved in bonafide banking activities, ignoring the fact that in India, the assessee is involved in only FII activity and no banking license has been granted by the RBI to the assessee for banking activities in India?"

(d) "Without prejudice to the above, whether on the facts and the circumstances of the case and in law, Hon'ble Tribunal has erred in holding assessee is entitled to the benefit of Article 11(3)(c) of the India Mauritius Treaty, whereas, the interest income derived by assessee in India not derived from its banking activity in India?"

(e) "Whether on the facts and the circumstances of the case and in law, "Hon'ble ITAT has erred in holding that assessee has interest income derived from bonafide banking activity ignoring the fact that assessee is not involved in any banking activities in India. This is in contravention to the ratio of Hon'ble Supreme Court in the case of Liberty India."

5. As regards questions (a) and (b), Mr. Kaka points out will not arise inasmuch as this has been subsequently recalled by the ITAT in a Miscellaneous Application filed by assessee where the ITAT has held that assessee satisfies the beneficial ownership requirement.

Therefore, what we need to consider are the remaining three questions proposed.

6. Revenue's case in short is Clause (c) of Article 11 of the DTAA will not apply to assessee. This is because assessee does not have a banking business license from the Reserve Bank of India. In our view, to fall under Clause 3(c) of Article 11 of the DTAA, assessee need not

have to be carrying on banking business in India. Assessee should only be a resident of Mauritius and must be carrying on *bona fide* banking business in Mauritius. We have to note that in the draft assessment order dated 30th March 2015 passed under Section 144C (1) r/w Section 143(3) of the Act, the AO while granting exemption to the interest on ECB has accepted that assessee is carrying on *bona fide* banking business in Mauritius. So also in the final assessment order dated 28th January 2016. Therefore, the fact that assessee is carrying on a *bona fide* banking business in Mauritius is not disputed. Would such an assessee be entitled to exemption from tax in India is what we need to consider. Article 11(3) of the DTAA reads as under:

> "Interest arising in a Contracting State shall be exempt from tax in that State provided it is derived and beneficially owned by:
>
> (a) the Government or a local authority of the other Contracting State;
>
> (b) any agency or entity created or organised by the Government of the other Contracting State; or
>
> (c) any bank carrying on a bona fide banking business which is a resident of the other Contracting State."

Under the said Article, therefore, interest arising in a contracting state (in this Case India) shall be exempt from tax in that State (in India) provided it (the Income) is derived and beneficially owned by any bank carrying on a *bona fide* banking business which is a resident of the other contracting State (Mauritius). Therefore, so long as assessee is carrying on *bona fide* banking business in

Mauritius being a resident of Mauritius, the interest that assessee would earn in India shall be exempt from tax in India.

7. If we have to accept, what Mr. Suresh Kumar submitted, that assessee should have had a banking license from the Reserve Bank of India, then what would be applicable is Clause 6 of Article 11 of the DTAA and that has not been relied upon by the AO. Moreover, the AO has, as noted earlier, granted exemption to the interest on FCB by accepting that assessee is carrying on *bona fide* banking business in Mauritius.

8. In the circumstances, we do not find any infirmity in the order passed by the ITAT. No substantial question of law arises. Appeal dismissed.

(DR. NEELA GOKHALE, J.) (K. R. SHRIRAM, J.)