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**The Delhi High Court in the case of Krishak Bharati Cooperative Ltd.(the taxpayer)<sup>1</sup> held that foreign tax credit ('FTC') is available in respect of dividend income received from Oman company even though no taxes thereon have been paid in Oman under its domestic law.**

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<sup>1</sup> CIT v. Krishak Bharati Cooperative Ltd. [TS-160-HC-2017 (Del)]

## Background/ Facts

- The taxpayer is a multistate co-operative society registered in India and engaged in the business of manufacturing fertilizers. It entered into a joint venture with Oman Oil Company to form the Oman Fertilizer Company SAOC ('OMIFCO' or 'JV'), a registered company in Oman, under Omani laws.
- The taxpayer also established a branch office in Oman which was claimed to be an admitted Permanent Establishment ('PE') in Oman.
- The taxpayer received a dividend income of INR 134.41 crores from OMIFCO (for being 25% equity stakeholder in the company) through its PE in Oman. Such dividend was duly offered to tax in India under Article 7 read with Article 11 of the India-Oman tax treaty. No taxes were paid in Oman on such income owing to <sup>2</sup>specific exemption under the domestic tax law of Oman.
- FTC of INR 41.53 crores was claimed on such dividend income under Article 25(4) of the India-Oman tax treaty (which provides for a tax sparing clause) which was duly allowed by the assessing officer ('AO').
- The Principal Commissioner of Income Tax ('PCIT') exercised its revisionary powers under Section 263 of the Income-tax Act, 1961 ('Act'). The FTC claim was disallowed on the ground that subject dividend income has not suffered double taxation and thus, not eligible to relief under Section 90 of the Act.
- Key observations of the PCIT were as under:
  - Article 25(4) of the India-Oman tax treaty states that tax payable in Oman shall be deemed to include the tax which would have been payable but for the tax incentive granted under the law of Oman and which are designed to promote economic development.
  - The term 'tax incentive' has not been defined in the India-Oman tax treaty. Hence, taking recourse to Article 3(2) of the tax treaty, the domestic tax law of India is required to be referred to. Under India's tax law, tax incentive is a deduction from income, which is otherwise taxable as per law<sup>3</sup>. Under the domestic tax laws of Oman, the dividend income is absolutely exempt, therefore, it cannot be said that any specific exemption was granted for the purpose of tax incentives for economic development.
  - <sup>4</sup>Share of profit recorded in the books of PE should be included in the global income of the taxpayer as per Section 4 & 5 of the Act<sup>5</sup>.
- The tribunal quashed the order passed by PCIT and held that the taxpayer is entitled to claim FTC of INR 41.53 crores. It was also held that the undistributed profits booked in the books of the PE in accordance with International Financial Reporting Standards ('IFRS') cannot partake the character of income under the provisions of the Act. It is a settled position that accounting entries are not determinative of taxability under the Act, and only the real income can be brought to tax.
- Aggrieved by the order of the Tribunal, the revenue filed an appeal before the High Court.

<sup>2</sup> Article 8(bis) of the Oman Company Income Tax Law

<sup>3</sup> The term 'tax incentive' has not specifically been defined under the Act also.

<sup>4</sup>As per International Financial Reporting Standards ('IFRS'), the share of PE in the profits/loss of OMIFCO at 25% was to be accounted as income in the Profit and Loss account of the PE even though such income received is only to the extent of dividend declared and distributed.

<sup>5</sup> This issue was not covered in the show cause notice issued by PCIT to the taxpayer.

## Ruling of the High Court

### On Technical grounds

- An opportunity to be heard must be given to the taxpayer in respect of those errors which the commissioner proposed to revise. <sup>6</sup>He could not go beyond the show cause notice and issues covered by it.
- <sup>7</sup>An order is erroneous when it is contrary to law or proceeds on an incorrect assumption of facts or is in breach of principles of natural justice or is passed without application of mind. In the present case, neither the AO overlooked the relevant facts nor did he fail in making inquiries. Hence, CIT's view that the assessment orders were erroneous, requiring revision under Section 263, is not sustainable in law.

### On Merits

- The Court took note of the clarification issued by the <sup>8</sup>highest tax authorities of Oman that the purpose of introduction of exemption for dividend income under Oman tax laws is to promote economic developments in Oman and Indian investors should be able to obtain relief under Article 25(4) of the India-Oman tax treaty.

- Against the contention of the PCIT that the clarification has not been issued by a proper authority, the court concluded that the clarification is conclusive.

It took note of the findings of the ITAT that it is an accepted position of interpretation that if there is some doubt about the interpretation of a particular provision of law, the competent authority to clarify that provision is only the government of that particular country. The Income Tax department of India has no locus standi in this matter. A clarification issued by the highest authority of the Sultanate of Oman, through the Secretariat General of Taxation, was to be so considered.

- The court thus upheld the order of the ITAT and the appeal filed by revenue was dismissed.

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<sup>6</sup> 'CIT Vs. Ashish Rajpal' 320 ITR 674.

<sup>7</sup> Followed its earlier ruling in 'Gee Vee Enterprises vs. ACT, Delhi-I & Ors.' [1975] 99 ITR 375 (Del. H.C.) and 'CIT vs. Gabriel India' [1993] 203 ITR 108 (Bom. H.C.)'

<sup>8</sup>Sultanate of Oman, Ministry of Finance, Secretariat General for Taxation, Muscat.

## Conclusion

This is an important decision by the High Court on interpretation of tax treaty provisions. The court has recognised that interpretation to the tax treaty provisions as accorded by tax authorities of the foreign country play a significant role in deciding tax claims in India.

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