IN THE INCOME TAX APPELLATE TRIBUNAL
"B" BENCH : BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND
SHRI JASON P. BOAZ, ACCOUNTANT MEMBER

ITA No.	A.Y.	Appellant	Respondent
209/Bang/14	2009-10	M/s. Kemwell Pvt. Ltd., Kemwell House, 11, Tumkur Road, BANGALORE [PAN: AAACK5854F]	Asst. Commissioner of Income Tax, Circle-11(5), BANGALORE
210/Bang/14	2009-10	Deputy Commissioner of Income Tax, Circle 11(5), BANGALORE	M/s. Kemwell Pvt. Ltd., Kemwell House, 11, Tumkur Road, BANGALORE [PAN: AAACK5854F]

Appellant by : Shri B.R. Renuka Prasad, Advocate
Respondent by : Shri R.N. Siddappaji, Addl.CIT

Date of hearing : 09-04-2019
Date of Pronouncement : 12-04-2019

O R D E R

Per N V Vasudevan, Vice President :

ITA No. 209/Bang/2014 is an appeal filed by the assessee while ITA No. 210/Bang/2014 is an appeal filed by the Revenue. Both these appeals are directed against the order dated 24-10-2013, of the

Commissioner of Income Tax (Appeals)-1, Bangalore, relating to Assessment Year 2009-10.

First we take up for consideration the appeal of assessee in ITA No.209/Bang/2014

2. The first issue that arises for consideration in the appeal by the assessee is with regard to addition made to the total income by rejecting the claim of assessee for deduction of a sum of Rs. 5,23,38,266/-.

3. Brief facts regarding the above issue are that the assessee is a company, engaged in the business of manufacturing of drugs and pharmaceuticals preparation. In the course of assessment proceedings for the AY. 2009-10 u/s. 143(3) of the Income Tax Act [Act], the Assessing Officer (AO) noticed that in the computation of income, the assessee had claimed deduction of a sum of Rs. 5,23,38,266/- under the head 'Foreign Currency Monetary Item Translation Difference Account'. The AO called upon the assessee to furnish the details in respect of the aforesaid claim of assessee and also to substantiate as to how the aforesaid claim is admissible.

3.1. In reply, assessee submitted that as per the provisions of Accounting Standard-11 (AS-11), issued by the Institute of Chartered Accountants of India (ICAI), the effect of changes in foreign exchange rates, insofar as they relate to the recognition of losses or gains arising on re-statement of long term foreign currency monetary items should

be recognized. In doing so, the assessee has exercised his option of adjusting to the cost of the asset, where the long-term foreign currency monetary item relate to the acquisition of a depreciable capital asset (whether purchased within or outside India), and consequently, claim depreciation over such asset's balance life. The assessee also pointed out that in the financial year ended 31-03-2018, it had a gain/profit consequent to foreign exchange fluctuation of Rs. 1,79,69,743/-, which was offered as income in that year. The assessee submitted that it was consistently offering gains on foreign exchange translation to tax. The assessee pointed out that while claiming depreciation; it had not increased the Written Down Value (WDV) of the Fixed Assets over which depreciation was claimed for income tax purposes.

4. The AO, however, did not agree with the contention of the assessee. He placed reliance on the provisions of Section 43A of the Act, which provides that *where an asset is acquired from a country outside India and consequent to change in the rate of foreign exchange, there is an increase or reduction in the liability of the assessee as expressed in Indian currency* ***at the time of making payment****, such liability or gain should go to increase or reduce the WDV of the corresponding asset on which depreciation is claimed by the assessee*. The AO therefore was of the view that only when there is an actual payment and in that year adjustment on account of fluctuation of foreign exchange currency has to be given effect. The AO accordingly disallowed the claim of assessee for deduction.

5. On appeal by the assessee, the CIT(A) concurred with the view of the AO. The CIT(A) firstly held that the fact of the gain on foreign exchange fluctuation was offered to tax by the assessee in the AYs. 2007-08 and 2008-09 should not have any bearing for AY. 2009-10 because, each assessment year is independent. Thereafter, the CIT(A) after noticing that the loan-in-question was availed for acquiring capital asset, held that the only recourse available to the assessee was as per the provisions of Section 43A of the Act. In Paras 4.7 and 4.8 the CIT(A) summed up the legal position as laid down in various decisions as follows:

"4.7. Sum and substances the aforesaid decision is that the liability expressed in foreign currency at the close of the year has to be increased/decreased based on the rates prevailing at the close of the year when corresponding increase/decrease has to be effected in the value of assets. The amendment of section 43A(1) as stated above provides for increase/decrease only for currency fluctuation at the time of payment. This will have a major implication for increase/decrease in unpaid foreign currency liability as though value of assets for the same has to be increased/decreased in he books of account. The amount of liability as stated above increased/decreased during the previous year are taken into account at the time of making payment irrespective of the method of accounting adopted by the assessee shall be added as the case may be deducted from actual cost of asset.

4.8. In view of the discussion made above the action of the AO is upheld. However, as per ruling of the Hon'ble ITAT in the case of JSW Steel Ltd., Vs. ACIT (supra) depreciation is to be allowed on the enhanced value of the capital assets."

5.1. Aggrieved by the aforesaid order of CIT(A), assessee preferred an appeal before the Tribunal.

6. Before the Tribunal, the assessee has filed an application for admission of the following additional evidences:

Sl. No.	Particulars of documents
1	Loan sanction letter dated 31.12.2005, issued by ICICI Bank addressed to the appellant.
2	Loan sanction letter dated 15.12.2005, issued by the State Bank of India addressed to the appellant.
3	Audited Financial Statements of the Appellant along with Auditor's Report, for the year ending 31st March 2007.
4	Audited Financial Statements of the Appellant along with Auditor's Report, for the year ending 31st March 2008.
5	Audited Financial Statements of the Appellant along with Auditor's Report, for the year neding 31st March 2009.
6	Audit Report issued in Form 3CA, of the Appellant, for the year ended 31st March 2007.
7	Audit Report issued in Form 3CA, of the Appellant, for the year ended 31st March 2008.
8	Audit Report issued in Form 3CA, of the Appellant, for the year ended 31st March 2009
9	Assessment order of the Appellant dated 26.10.2009, relevant to the Assessment Year 2007-08, along with the submissions of the Appellant made during the assessment proceedings.
10	Assessment order of the Appellant dated 26.10.2009 relevant to the Assessment Year 2008-09, along with the submissions of the Appellant made during the assessment proceedings.
11	Audited Financial Statements of M/s. Rubtech Exports Pvt. Ltd , along with Auditor's Report, for the year ending 31st March 2009.
12	Audited Financial Statements of M/s. Kemwell Biopharma Pvt. Ltd., along with Auditor's Report, for the year ending 31st March 2009.

6.1. In an affidavit filed in support of the above additional evidences, the assessee has explained the reasons for filing additional evidence, in paras 2 to 4, which reads as under:

"2. I affirm that the issue in the above appeal relates to (a) disallowance of foreign currency fluctuation difference under Section 43A and (b) disallowance of interest u/s. 36(1)(iii) r.w. Sec. 37 of the Income Tax Act.

3. I affirm that both during the assessment proceedings as well as during the first appellate proceedings, allowance or otherwise of foreign currency fluctuation difference in terms of Sec.43A of the Act was examined on the angle of whether it requires to be capitalized and whether it is allowable only on cash basis i.e., as and when the difference is actually paid.

4. I affirm that during the course of preparation for addressing the Arguments before this Hon'ble Tribunal by our Counsel in the recent past, our Counsel examined the said issue on a different angle altogether, as to whether the capital assets were purchased indigenously or were imported from abroad, since, the application of Sec. 43 A of the Act would depend on the said fact and if the capital assets are purchased indigenously, invoking of Sec. 43 A of the Act and disallowance thereof would not arise at all. This particular angle was not gone into either during the course of assessment or the first appellate proceedings both by the Appellant as well as by the Department. Therefore, the said additional documents which are required to substantiate the said fact, could not be produced during the course of assessment or the first appellate proceedings. Likewise, in respect of the disallowance interest U/s. 36 (1) (iii) r w. Sec. 37 of the Income Tax Act, the said issue in the Appellant's case in respect of the earlier Assessment Years were raised by the Assessing Officer, and the proposal to disallow the same was dropped based on the submissions of the Appellant and the Audited Financial Statements of the Companies to which Advances were made by the Appellant. Neither the Counsel nor the Appellant realised the necessity of relying and producing these documents either during the assessment proceedings or first appellate proceedings, by sheer inadvertence".

6.2. As can be seen from the aforesaid contentions, in the affidavit filed in support of admission of additional evidences, the assessee seeks to contend that Section 43A of the Act would apply only when capital assets are acquired outside India from and out of foreign currency loan and consequent to fluctuation of foreign currency, the liability to repay the said loan would either increase or

decrease. It is being claimed by the assessee that the foreign exchange fluctuation in question did not relate to acquisition of a capital asset from outside the country. This stand is totally contradictory to the stand taken before the Revenue authorities. Apart from the above the allowability of loss on account of fluctuation in foreign currency as a revenue expenditure is dependent on the question whether the foreign currency loan was availed for meeting capital expenditure or revenue expenditure. If the foreign currency loan is availed for acquiring capital assets whether in India or outside India, would not make any difference, since acquiring capital asset in India would also be a capital item and therefore the claim of loss as expenditure and allowable deduction while computing total income would become inadmissible.

7. Ld. Counsel for th assessee could not explain as to what is the basis on which such a claim is being made nor the documents that are sought to be filed as an additional evidence establish the claim made in the affidavit filed in support of leave to file additional evidence before Tribunal. The learned Counsel for the Assessee could not bring to our notice any other evidence on the claim of the assessee as made in the application for admission of additional evidence.

8. In these circumstances, we refuse to entertain the request for admission of additional evidence as we are of the view that the additional evidences are to be filed is not necessary for adjudication of the issue in dispute before the Tribunal. In this regard, Ld. Counsel for

the assessee was also filed an application under Rule 11 for raising the following additional ground of appeal:

"a. The Appellant submits that both the Respondent as well as the First Appellate Authority failed to examine the applicability of Sec.43A r.w. Sec.37 of the Income Tax Act, since the Appellant has purchased capital assets indigenously, which are substantial in nature".

8.1. The application for raising additional ground is also dismissed for the very same reasons. Ld. Counsel for the assessee submitted that Shri Harish, Advocate who was handling the matter, could not make appearance and sought for time This request was made after hearing of the appeal commenced Further, this appeal filed in the year 2014 and has been adjourned on several occasions at the request of the assessee. In these circumstances, we are of the view that no useful purpose will be served by granting adjournment.

8.2. We find that the claim made by the assessee was contrary to the provisions of Section 43A of the Act and in the circumstances, the Revenue au horities were justified in rejecting the claim of assessee. The argument that *similar gain was offered to tax in the earlier assessment years* will not be a ground to accept the claim of assessee in the present assessment year. We therefore concur with the view of the CIT(A) and dismiss the relevant ground of appeal of assessee.

9. The next grievance projected by the assessee in its appeal is with regard to disallowance of interest u/s. 36(1)(iii) of the Act.

9.1. As far as this issue is concerned, the facts are that the assessee had borrowed funds and on such borrowing, the assessee had paid interest of Rs. 3,33,99,162/-. The assessee had given interest free loans and advances of Rs. 5,52,44,519/- to M/s. Rubtech Exports Pvt. Ltd., and M/s. Kemwell Biopharma Pvt. Ltd., Rs. 10,36,815/-. The AO was of the view that borrowed funds on which interest was paid had been diverted for non-business purposes and he accordingly worked out proportionate disallowance of interest claimed a deduction by the assessee at the sum of Rs. 37,37,461/- and added the same to the total income of the assessee.

10. Before the CIT(A), the assessee submitted that the interest free loans and advances were given to the aforesaid companies, who were of sister concerns (wholly owned subsidiary companies), for business purposes and owing to commercial expediency. Therefore, no interest was charged. The submissions were as follows:

"C.2.2 The Appellant submits that during the relevant year, only a sum of Rs.36.20 Lacs was advanced to Rubtech Exports. The Respondent has considered the entire sum of Rs.5.52 Crores and Rs.10.36 Lacs as the sums advanced during the relevant year as against only a sum of Rs.36.20 Lacs advanced during the relevant year and determined the disallowance, which is incorrect.

C.2.3 The Appellant submits that there is no presumption available in Law for the Respondent to presume that the advances are made out of interest bearing funds. The Respondent ought to have given a specific finding and clearly pointed out by way of calculation to arrive at the conclusion that the advances were out of interest bearing funds. The Respondent has seriously erred in presuming that the advances were out of interest bearing funds, which is nothing but a mere imagination.

C.2.4 The Appellant submits that during the relevant year, the Appellant had an accumulated reserves and surplus of Rs. 42.18 Crores. The Appellant raised a sum of Rs.3.45 Crores by allotting Equity and Preference shares. The Appellant submits that the advances for the earlier years were met by the Appellant out of money raised for that specific purpose and also out of the huge accumulated Reserves and Surplus of the Appellant. The money advanced during the relevant year is just Rs.36.20 Lakhs as against the available accumulated reserves and surplus of Rs.42.18 Crores and capital raised during the year to an extent of Rs.3.45 Crores. This itself clearly proves beyond doubt that the same were out of interest free funds.

C.2.5 The Appellant submits that there was no necessity for the Appellant to borrow funds for interest and advance the same without any interest. As a matter of fact, not only the Appellant, but any prudent businessman or a Corporate entity would ever opt to borrow money for interest and lend it for no gain / profit. It is also to be appreciated that the Appellant has availed Working Capital facility from its Bankers. Such being the case, the Bankers would not permit diversion of funds other than for business purposes".

10.1. The CIT(A) on a consideration of the above submissions, accepted the fact that the assessee had sufficient own funds. The following were the relevant observations of the CIT(A):

"6.4 I have considered the appellant's submission and it is true that the appellant having tax free fund of Rs. 50,19,32,748/- as on 31/03/2009. It is also true that the appellant borrowed fund of Rs. 50,29,48,224/- on which interest and bank charges claimed for Rs. 3,33,99,162/- and utilization of borrowed fund under common pool since no separate accounts were maintained in respect of interest free funds and interest bearing funds. Further, the appellant made payment to its subsidiary concerns by way of loans and advance. The loan and advances appears against Rubtech Export Pvt Ltd., year-wise as under:

Financial Year	*Asst. Year*	*Outstanding loan and advances (In Rs.)*
2005-06	*2006-07*	*3,72,44,519*
2006-07	*2007-08*	*4,55,24,519*
2007-08	*2008-09*	*5,16,24,519*
2008-09	*2009-10*	*5,52,44,570*

6.5. Thus it may be seen that loan and advance to Rubtech Export Pvt. Ltd., in increased traced since assessment year 2006-07, it indicate that advanced amount not utilized for business purpose and parked since long. As discussed above, since the appellant has not maintained separate account, obviously part of the interest bearing fund was given to the said company.

10.2. The CIT(A), however, proceeded to confirm the order of AO on the basis that firstly there was nothing on record to show that the interest free loans were given to the sister concern for business purposes or owing to commercial expediency. He also proceeded to hold that if the claim of assessee was that it had own funds, then, assessee ought not to have borrowed and paid interest at all. On that line of reasoning, the CIT(A) rejected the claim of assessee.

10.3. Aggrieved by the order of Ld.CIT(A), assessee preferred the present appeal before the Tribunal.

11. We have heard the rival submissions. It is clear from the facts of the case that the assessee had tax free funds to the tune of Rs. 50,19,32,748/-. It has been held by the Hon'ble Bombay High Court in the case of CIT Vs. Reliance Utilities & Power Ltd., (2009) [313 ITR 340] (Bom) that *if the own funds of the assessee are more than the*

interest free advances given to the sister concern, then, there is a presumption that interest free funds were used for giving loans to sister concerns and therefore no disallowance of interest paid on borrowings can be made. As we have already stated in the application filed for admission of additional evidence, which has been rejected by us, the assessee has sought to file evidence to show that funds given to the sister concern were out of own funds. Without going into the correctness of that claim, we are satisfied that in the given facts and circumstances of the case, the interest free funds available with assessee was sufficient at all material point of time when loans were advanced to the subsidiary company and hence di allowance of interest u/s. 36(1)(iii) of the Act cannot be sustained and the same is directed to be deleted.

12. In the result, the appeal of assessee is partly allowed.

ITA No. 210/Bang/2014 (Revenue's appeal):

13. As far as the appeal of Revenue is concerned, the Ground Nos. 1, 5 & 6 raised by the Revenue are general in nature and calls for no adjudication.

14. Ground Nos. 2 & 3 raised by the Revenue are with regard to disallowance of expenses made by the Revenue authorities invoking the provisions of Section 14A of the Act. As far as this issue is concerned, the facts are that the assessee earned dividend income on its

investments in the shares of M/s. Kemfin Holdings Pvt. Ltd., Cyprus no other dividend income was earned from any investment. The dividend income earned from M/s. Kemfin Holdings Pvt. Ltd., Cyprus was chargeable to tax and was not an item of income, which does not form part of total income under Chapter-III of the Act. In the given circumstances, the question of re-consideration is as to whether disallowance can be made u/s. 14A of the Act in the absence of exempt income. The law in this regard is now fairly well settled. The Bangalore Bench of ITAT in the case of M/s UB Infrastructure Projects Ltd., Vs. DCIT, ITA No. 2098/Bang/2016 (AY.2012-13) order dated 22-12-2017, this Tribunal took the view that there can be no disallowance of expenses u/s 14A of the Act, if there is no exempt income earned during the relevant previous year. The following are the relevant observations of the Tribunal in this regard.

> *"3. Having carefully examined the orders of authorities below, we find that undisputedly the assessee has not earned any exempted income. Now it is settled position of law that whenever assessee did not earn any exempt income, no disallowance could be made u/s. 14A of the Act. The Hon'ble Delhi High Court in the case of Cheminvest Ltd. v. CIT, 378 ITR 33 (Del) has categorically held that section 14A envisages that there should be actual receipt of income which was not includible in the total income during the relevant previous year for the purpose of disallowing any expenditure in relation to the said income. Wherever there is no exempt income includible in the total income of the assessee, the provisions of section 14A cannot be invoked. The relevant observations of the judgment of the Hon'ble Delhi High Court are extracted hereunder:-*

"15. Turning to the central question that arises for consideration, the court finds that the complete answer is provided by the decision of this court in CIT v. Hololcim India (P) Ltd. (decision dated 5th September 2014, in I.T. A. No. 486 of 2014). In that case, a similar question arose, viz., whether the Income-tax Appellate Tribunal was justified in deleting the disallowance under section 14A of the Act when no dividend income had been earned by the assessee in the relevant assessment year ? The court referred to the decision of this court in Maxopp Investment Ltd. (supra) and to the decision of the Special Bench of the Income-tax Appellate Tribunal in this very case, i.e., Cheminvest Ltd. v. CIT [2009] 317 !TR (AT) 86 (Delhi) [SB]. The court also referred to three decisions of different High Courts which have decided the issue against Revenue. The first was the decision in CIT v. Lakhani Marketing Incl. (decision dated April 2, 2014, of the High Court of Punjab and Haryana in I. T. A. No. 970 of 2008)--since reported in [2015] 4 ITR-OL 246 (P&H)--which in turn referred to two earlier decisions of the same court in CIT v. Hero Cycles Ltd. [2010] 323 ITR 518 (P&H) and CIT v. Winsome Textile Industries Ltd. [2009] 319 ITR 204 (P&H). The second was of the Gujarat High Court in CIT v. Corrtech Energy (P.) Ltd. [2014] 223 Taxmann 130 (Guj) ; [2015] 372 1TR 97 (Guj) and the third of the Allahabad High Court in CIT v. Shivam Motors (P) Ltd. (decision dated 5th May, 2014, in T.A. No. 88 of ITA No 1 1071Bang12016 2014). These three decisions reiterated the position that when an assessee had not earned any taxable income in the relevant assessment year in question "corresponding expenditure could not be worked out for disallowance."

4. This was also examined by the Tribunal in the assessee's own case for assessment year 2010-11 and held that when there is no exempt income, provision of section 14 of the Act cannot be applied.

5. In the light of the aforesaid judgment, the provisions of section 14A cannot be invoked as there is no exempt income in the hands of the assessee. Accordingly, we find no infirmity in the order of the CIT(Appeals) who has rightly deleted the addition."

14.1. In view of the aforesaid decision of the Tribunal, we are of the view that the disallowance of expenditure u/s 14A of the Act was rightly deleted by the CIT(A). In view of the above legal position, there is no merit in Ground Nos. 2 & 3 raised. Hence, these two grounds are dismissed.

15. Ground No. 4 raised by the Revenue reads as follows:

"4. The CIT(A) erred in directing the AO to allow rebate of Rs. 68,60,902 without appreciating the fact that as per the Indo-Cyprus DTAA credit could be claimed in India only when the exemptions or incentives granted in Cyprus were designed to promote economic development as the treaty with Cyprus starts with a rider that the exemption is an incentive for economic development and hence this has to be followed strictly".

15.1. Before we deal with the aforesaid ground of appeal, we need to understand what tax sparing credit is. Tax Sparing Credit, in the context of Double Tax Avoidance Conventions, refers to the provisions in the DTAA's between Contracting States which give enjoin the Residence Country to give credit not only for Taxes actually *paid* in the Source Country but also for Taxes which would have been paid but for the Tax *Incentives* granted in the Source Country's Domestic Law. The OECD's Glossary of Tax Terms defines Tax Sparing Credit as "*Term used to denote a special form of double taxation relief in tax treaties with developing countries. Where a country grants tax incentives to encourage foreign investment and that company is a resident of another country with which a tax treaty has been concluded, the other country may give a credit against its own tax*

for the tax which the company would have paid if the tax had not been "spared (i.e. given up)" under the provisions of the tax incentives" The purpose is clear, to ensure that the Domestic Law Tax Incentive in the Source Country is not made ineffective in the Foreign Investor's hand if the Country of Residence were to deny the Tax Credit to the extent of the taxes "spared" but not paid in the Source Country.

15.2. As far as this ground of appeal raised by the Revenue is concerned, the facts are that assessee received dividend from M/s. Kemfin Holdings Pvt. Ltd., Cyprus during the previous year. In accordance with Article 25 of the Double Taxation Avoidance Agreement (DTAA) between India and Cyprus, the assessee claimed tax relief to the extent of tax payable in Cyprus but which was not paid because of tax incentive given by the Cyprus Government on dividend. Article 25 of the DTAA which deals with avoidance of double taxation of income, in *Para 1 of Article 25 provides that the taxation of income would be governed by the laws of the respective contracting states. Para 2 of Article 25 of the Double Taxation Avoidance Agreement (DTAA) between India – Cyprus allows credit for taxes paid in Cyprus, directly or by deduction in computing the income tax payable in India. Para 3 is not relevant in the present case. Para 4 of Article 25 allows credit on taxes deemed to have been paid in Cyprus. As per para 4, tax payable in Cyprus shall be deemed to include the tax which would have been payable but for the tax incentives granted under the laws of Cyprus and which are designed to promote economic development. Para 4 quantifies the quantum of tax that shall be deemed to have been paid in respect of certain streams of*

income. This is popularly termed as the "tax sparing" credit. The following table captures the said information.

Sl.No.	*Article*	*Particulars of income*	*Tax deemed to have been paid*
1	*10*	*Dividend*	*10% of gross amount of dividends*
2	*11*	*Interest*	*10% of gross amount of interest*
3	*12*	*Royalties and fees for included services*	*15% of gross amount of royalties and fees for included services*
4	*13*	*Technical fees*	*10% of gross amount of technical fees*

15.3. The Assessee therefore claimed credit for deemed to have been paid in Cyprus under Article 25(4) of the DTAA between India and Cyprus. The AO, however, did not accept the claim of assessee and he held as follows:

"The Contention of the assessee is not acceptable.

a) Para 4 of Article 25 of the Indo-CyPrus DTAA, makes it abundantly clear that credit could be claimed in India for tax payable in Cyprus only when the exemptions or incentives granted in Cyprus were 'designed to promote economic development' The assessee has failed to prove that this requisite condition has been fulfilled.

b) The evidence relied upon by the assessee indicates the general conditions congenial to foreign investments. It fails to prove that the exemption for dividend income was provided as an incentive for economic development.

c) It is noted that Section 8 of the Cyprus Income Tax Act is akin to Section 10 of the Indian Income Tax Act and the exemptions granted u/s. 8 of the CyPrus Income Tax Act mainly concerned emoluments of the President, etc., Gratuity, Pension, income of charitable institutions, etc. As the dividend is also bracketed u/s. 8, it cannot be said that it was designed for economic development. Hence it is seen that a direction connection has not been established between the exemption for dividends and economic development.

d) Though tax sparing credit is commonly seen in the double taxation avoidance agreements, the treaty with Cyprus adds a rider stating that the exemption is an incentive for economic development and hence this has to be followed strictly. It is also noted that the tax rate for dividends was essential for the reason that without the rate tax credit cannot be computed. Reliance is also placed on the decision of the Hon'ble AAR in the case of Cyril Eugene Pereira in 239 ITR 0650 (AAR) wherein it was held that if no tax was payable in the foreign country there was no question of availing tax credit in India.

e) Reliance is also placed on the following case laws.

i. Tarulata Sham and other 108 ITR 345 (SC)
ii. Keshavji Raoji and Company 183 ITR 1 (SC)
iii. Budharaja and Company 204 ITR 412 (SC)

Wherein it has been held that when the wordings in the Statute are clear and specific, it has to be followed strictly without importing or assessing any other meaning or intention.

Based on the above, the rebate u/s. 90 of Rs. 68,60,892/- claimed by the assessee is disallowed and added back to income".

15.4. On appeal by the assessee, the Ld.CIT(A) noticed that similar claim made in AY. 2008-09 was allowed by the CIT(A) and the Revenue did not prefer appeal before the ITAT on the aforesaid order. Ld.CIT(A) agreed with the conclusions of his predecessor with the following observations:

"7.3 I have gone through the appellant's submission. Similar issue arose during the assessment year 2008-09 and my predecessor in the appellate order in ITA No. 39/DCIT-LTU/CIT(A)LTU/10-11 dated 29/03/2011 analysed the similar issue in details and decided in favour of the appellant, the relevant part of the decision is reproduced below :-

> *"5.1 Based on a careful consideration of the appellant's arguments as well as the AO's contentions, I am inclined to conclude that the*

appellant has rightly sought credit of 16% of the dividend income earned by it in accordance with the provisions of Article 25 (4) of the India - Cyprus DTAA which is reproduced as under:-

> *"The tax payable in a Contracting State mentioned in paragraph 2 and paragraph 3 of this Article shall be deemed to include the tax which would have been payable but for the tax incentives granted under the Laws of the Contracting States and which are designed to promote economic development. For the purpose of paragraph 2 of Article 10 the amount of tax shall be deemed to be 10 per cent or 15 per cent as the case may be, of the gross amount of dividend, for the purpose of paragraph 2 of Article 11, the amount of tax shall be deemed to be 10 per cent of the gross amount of interest and for the purpose of paragraph 2 of Article 12, the amount of tax shall be deemed to be 15 per cent of the gross amount of royalties and fees for included services and for the purpose of paragraph 2 of Article 13, the amount of tax shall be deemed to be 10 per cent of the gross amount of technical fees."*

It is crystal clear from a plain reading of para 4 of Article 25 that the first phase of the said Article lays down a criterion that credit would be given for tax which would have been payable but for the tax incentives granted under the laws of the Contracting States and which are designed to promote economic development. In other words, the tax amount eligible for credit would need to be computed having regard to the tax incentives designed to promote economic development. It is also evident that no mechanism or yardstick has been prescribed for either qualifying or quantifying economic development as a pre-condition for allowing tax sparing credit. It appears that in none of the Treaties certification from the authorities of the source country as regards economic development was made a pre-condition for allowing tax sparing credit by the residence country since no system/mechanism was available in any source country for issue of such Certificates. None of the Treaties cast the burden of proving that the tax exemption was in r/o economic development on the claimant let alone establishing that the tax exemption is in r/o "special" economic development. I am of the considered opinion that

the insistence by the AO of such proof as a pre-condition for allowing tax sparing credit negates the very scheme of tax sparing. Moreover as regards the implication of the phrase 'to promote economic development' economic development in ordinary parlance refers to sustainable increase in living standards that delivers increase per capital income, better education and health as well as environmental protection. The public policy of any Stat aims at continuous and sustained economic growth and expansion of national economics so that 'developing countries' become 'developed countries'. Hence the phrase 'to promote economic development' would imply measures undertaken to further/bolster the cause of increasing the standard of living of the people by means of sustained growth. Attracting and encouraging new businesses is definitely a took to implement the cause of economic development and giving incentives in the nature of exemption from liability to tax in r/o dividends is a very elementary method by which resources could be garnered to be invested in new business etc., thereby promoting economic growth and development. In my view, no other specific evidence is mandated either by law or common sense to establish that the exemption in question is designed to promote economic development. In fact, to my mind there is no alternative plausible conclusion possible as the rationale for the providing of the said exemption other than to promote economic activity and hence economic development. To sum up, it seems as if the AO is indirectly imposing a pre-condition not mandated in Article 25(4). I am of the firm view that in the absence of specific words no requirement/cond tion can be read into a statutory provision as held by the Apex Court in the case of CIT Vs Virmani Industries P . Ltd (1995) 216 ITR 607). In other words, the AO cannot adduce any special requirements where there was none for the purpose of affording the exemption which is explicitly provided under the Treaty or import additional adjectives such as 'general' or 'special' etc. when such a requirement has not been specifically laid down in the DTAA. By giving exemption/ tax incentive in r/o dividend income, Cyprus was definitely contributing to the promotion of its economic development. It is pertinent to note that by giving exemption in r/o dividend income, more and more entities etc. were sufficiently incentivized to invest in shares of companies based in Cyprus resulting in companies having more and more capital to invest further in the setting up of organization/industries thereby contributing to its economic development. Consequently s increased

employment and the increased standards of living resulting from increased business investments would necessarily further the cause of economic development.

5.1.1 It is of relevance to note that several High Courts as well as the Hon'ble supreme Court have held that provisions of tax statutes granting incentives and benefits for promoting, growth and development of the industry are required to be construed liberally so as to advance the objective of the provision viz., the Apex Court in the case of CIT Vs Gwallor Rayon Silk Manufacturing Co. Ltd. (1992) 196 ITR 149 and P.R. Prabhkar Vs CIT (2006) 284 ITR 548, the jurisdictional High Court in the case of A. S. Mani Vs Union of India and others [20031 204 ITR 5 and the Hon' ble ITAT, Mumbai Bench in the case of Hindalco Industries Ltd. Vs. Asst. CIT (2005) 94 ITO 242 etc. Similarly, the view that a strict and literal construction should be avoided in interpreting a clause in the Treaty and the intention and purpose behind the provisions incorporated in the Treaty should be given due weight has been taken by the Authority of Advance Ruling in the case of Cal Dive Marine construction (Mauritius) Ltd. in re [2009] 315 ITR 334 (AAR) and the Hon'ble ITAT, Delhi Bench in the case of Ensco Maritime Ltd. Vs Dy. CIT [2004] 91 ITD 459 (pages 476-477) which has enunciated the principles of interpretation of treaties. It is noteworthy that the Hon'ble ITAT, Mumbai Bench in the case of Dy. DIT (International Taxation) Vs Balaji Shipping (UK) Ltd. (2009) 315 ITR (AT) 62: (2008) 117 TTJ 865 (Mumbai) also held that the rules of interpretation for interpreting a statue were not applicable for interpreting the covenants of tax Treaties between contracting States. Further the Tribunal has observed that the words or expressions used in the Treaties, if not defined in the treaties themselves, should be understood in the sense in which the contracting States understood them at the time the Treaty was executed; i.e., contemporaneous thinking. In view of the foregoing analysis, I am inclined to uphold the appellant's claim for credit for double taxation relief amounting to Rs.342,532/- and direct the AO to allow the same. Grounds 2.1 to 2.5, therefore, succeed."

7.4. Since the issue is identical for this year and in order to maintain rule of consistency, I hold similar view. The AO is therefore directed to allow rebate of Rs. 68,60,902/ -. The appeal in this ground thus succeeds".

15.5. Aggrieved by the order of Ld.CIT(A), Revenue raised Ground No.4 before the Tribunal.

15.6. Ld.DR reiterated the stand of the Revenue as contained in the grounds of appeal.

15.7. We are of the view that the conclusions of the Ld.CIT(A) in AY. 2008-09 are correct and does not call for any interference. As rightly held by the CIT(A) in the order for AY 2008-09, the implication of the phrase 'to promote economic development' in ordinary parlance refers to sustainable increase in living standards that delivers increase per capital income, better education and health as well as environmental protection. The public policy of any State aims at continuous and sustained economic growth and expansion of national economics so that 'developing countries' become 'developed countries'. Hence the phrase to promote economic development' would imply measures undertaken to further/bolster the cause of increasing the standard of living of the people by means of sustained growth. Attracting and encouraging new businesses is definitely a took to implement the cause of economic development and giving incentives in the nature of exemption from liability to tax in r/o dividends is a very elementary method by which resources could be garnered to be invested in new business etc., thereby promoting economic growth and development. The rationale for providing exemption by itself is proof that it was for no other purpose other than to promote economic activity and hence economic development. We

agree with the foresaid reasoning and find no grounds interfere with the order of CIT(A). Consequently, Ground No. 4 raised by the Revenue is dismissed.

16. In the result, this appeal of Revenue is dismissed.

17. To sum-up, the appeal of assessee is partly allowed and the appeal of Revenue is dismissed.

Pronounced in the open court on this 12th day of April, 2019

Sd/-	Sd/-
(JASON P. BOAZ)	(N.V. VASUDEVAN)
ACCOUNTANT MEMBER	VICE PRESIDENT

Bangalore,
Date: 12th April, 2019.

TNMM

Copy to:

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

By order

Assistant Registrar,
ITAT, Bangalore