NATIONAL JUDICIAL ACADEMY

WORKSHOP FOR HIGH COURT JUSTICES ON DIRECT TAXES
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PROGRAMME REPORT

PROGRAMME COORDINATORS: MR. RAHUL SONAWANE & MS. ANKITA PANDEY
FACULTY
NATIONAL JUDICIAL ACADEMY, BHOPAL

OVERVIEW OF THE PROGRAMME

The National Judicial Academy organized online 'Workshop for High Court Justices on Direct Taxes' on 11th and 12th September, 2021. The participants were High Court justices dealing with or likely to deal with taxation roster from across the country. Creating expertise at the High Court level was thought to be a critical factor for the judiciary in order to address the backlog and increase competencies to serve as a fair arbiter both in the domestic and international aspects. The conference was conceived to facilitate deliberations among participant justices on contemporary issues and recent developments in direct taxation in India and globally. It provided a forum for discussing normative issues pertaining to the history, basic features and evolution of direct taxes; international tax treaty and double tax avoidance agreements; Transfer Pricing: basic principles and major areas of disputes and Appellate Writ Jurisdiction of High Courts; Jurisdiction and Limitations. The workshop facilitated valuable exchange of knowledge and dissemination of best practices available for enhancing quality of adjudication in tax matters at High Court level.

DAY 1

Session 1 - History and Basic features of Tax Laws, Constitutional Provisions for Finance Bill and Treaties, Money Bills & Scheme of Income Tax Act, 1961

Session 2 - International Tax Treaty Law and Double Tax Avoidance Agreements: An Overview

DAY 2

Session 3 - Transfer Pricing: Basic Principles & Major Areas of Dispute

Session 4 - Appellate and Writ Jurisdiction of High Courts: Jurisdiction and Limitations

DAY – 1

Session 1

History and Basic features of Tax Laws, Constitutional Provisions for Finance Bill and Treaties, Money Bills & Scheme of Income Tax Act, 1961

Speakers: Mr. N. Venkataraman & Mr. Porus Kaka

Chair: Justice A. K. Sikri

Justice A. P. Sahi, Director, NJA commenced the seminar and set the theme of the session. He introduced the resource persons for the session and deliberated upon the theme of the session explaining the historical background as well as jurisprudential and philosophical aspects of taxation. Justice A. K. Sikri making his opening remarks used quotation – *"I hate paying taxes, but I love the civilization they give me"* saying this captures the entire essence of taxation law. He touched upon the philosophy of Indian Constitution explaining provisions relating to taxation viz. article 265 and so on. Doctrine of proportionality in tax matters was also explained. He explained the rationales of rights of individuals/tax payers and governments/revenues on the other hand and need to reconcile and harmonise both for betterment of society at large. He discussed about the new age problems like ecommerce, inter-country incomes, MNCs taxation, bitcoins and other forms of crypto-currency and challenge they have posed to the world tax regimes. He referred to various judicial precedents viz. ***Govind saran Gangaram case (1985), Vodafone Judgement (2012)*** etc. Mr. Porus Kaka in his presentation traced the history of taxation to Napoleonic Wars in UK in 1798. In India, income tax started in 1860 with introduction of Indian Income Tax Act. India, like UK follows the territorial model of taxation i.e. whatever related to territory of India, we choose to tax it. Speaker then explained the brief history of international tax treaties and various international conventions viz. OCED draft Treaty, UN Model Tax convention etc. He explained basic features of tax viz. Convenience *(ease of compliance and tax friendly environment)*, Certainty *(Literal Interpretation)*, Equity *(progressive taxation)*, Economic Efficiency *(tax should be transaction neutral and not influence a transaction in any manner)* and finally Simplicity *(long term fiscal policy)*. He then went on to explain various provisions relating to taxation in Constitution of India viz. Art. 265,

268, 269, 270 etc. He also explained as to when tax becomes "unconstitutional" and what the *vires* are. He touched upon the importance of Directive Principles of State Policy in constitution and its importance in deciding tax cases. He also explained provisions relating to international tax treaties in Indian Constitution. He referred to various case-laws like ***Pepsi Foods case, Maganbhai Ishwarbhai Patel case (1970), Azadi Bachao Andolan case (2004), Engineering Analysis co. case (2021)*** etc. Speaker then went on to explain the scheme of the Income Tax Act and new concepts introduced recently like faceless assessment, faceless appeals etc. Mr. N. Venkataraman then took over explaining the constitutional provisions relating to money bills and controversies surrounding it. He suggested that money bills are not only federal/union issue, but rather it is also a state issue as even state legislatures also can pass money bills. He explained the modalities and nuances of passing money bills and upper hand given to the Lok-Sabha over Rajya-Sabha in cases of money bill by Constitution itself. He referred to the judgement of Supreme Court in Aadhaar Judgement where the Aadhaar Act was held to be a money bill. He emphasized that Constitution clearly says that Speaker of Lok-Sabha is the only authority to decide whether a bill is money bill or not. This decision of Speaker, Lok-Sabha is final. Here he raised an issue as whether this decision of speaker is subject to judicial review and if yes, to what extent. He then stressed upon the Constitutional Supremacy and urged the judges to always keep in mind. Many participants expressed their views on the money bills as well as tax treaties and challenge to it in the courts of law. Panel tried to clear their doubts.

Session 2

International Tax Treaty Law and Double Tax Avoidance Agreements: An Overview

Speakers: Mr. N. Venkataraman & Mr. Porus Kaka
Chair: Justice A. K. Jayasankaran Nambiar

Justice AKJ Nambiar commenced session with quote of Benjamin Franklin saying, *"There are only two certainties in life; one is death and the other is Taxes"*. He stressed the importance of international taxes for high court judges saying economic activities have now crossed the boundaries and every country wants its share by way of taxes in economic activities in their countries. It sometimes involves sovereign rights and decision has to be taken by high courts.

He dealt with concepts like tax avoidance, tax invasion, multi-lateral international treaties, bilateral international treaties, double tax avoidance agreements etc. He explained the rationale behind the foreign investments and bilateral treaties alongwith tax issues involved therein. Earlier bilateral or multilateral treaties did not contain tax provisions as it was considered to be sovereign function, but off recently, tax issues have made their way into the treaties, albeit indirectly. Mr. N. Venkataraman then took over talked about the constitutional basis of international treaties. Treaties are left to the job of Executive by the Constitution of India. But it doesn't translate into a legislation/law directly. He referred to Art. 253 of Constitution saying Parliament only has power to give effect and implement the treaty entered into by the executive. He also referred to various provisions of Income Tax Act to make his point clear. He suggested that bilateral investment treaties (BITs) are things of past and proved to be a failure. He referred to the judgements of Supreme Court in cases of ***McDowells, Azadi Bachao Andolan, Vodafone tax case*** etc. He explained the functioning of international arbitration forum in tax cases as well as relating to bilateral investment treaties and criticized it saying that it directly comes into the way of sovereign powers of a state. He vehemently defended the decision of Union of India to bring retrospective amendment in tax law to overcome the judgement of Supreme Court in Vodafone case. Mr. Porus Kaka then presented his thoughts on international treaty law. As opposed to Mr. N. Venkataraman, Mr. Porus vehemently supported the International Arbitration Forum in tax matters. He suggested that International Arbitration has made tax officers of sovereign state to act fairly and in case of their aggression, there is an international forum. As regards issue of sovereign power of state, he suggested that the moment state enters into bilateral or multilateral treaty it surrenders its sovereign power and assures to investors that they will be treated fairly. He suggested that extremely aggressive executive undermines judiciary. In 2012 executive of India has undermined 17 judgments including of Supreme Court. He then dwelled into the history and evolution of international tax treaties and double tax avoidance agreements. He explained the 'exemption' and 'credit' method of double tax avoidance globally. He also drew attention of floor to the fact that amended provisions of tax law does not only take care of double taxation, but also of "Double Non Taxation". No investor or entity can be allowed to take benefit of tax exemption in both countries. He then went on to discuss various adjudicating forums in international tax and double tax avoidance agreement

related cases. He said India shares more than 70 percent international tax law cases in the world. He then explained basic principles of bilateral or multi-lateral tax treaties viz. commitment in treaty must be honoured, treaty should be interpreted in good faith etc. He also talked about synergy between international treaties and domestic laws. He referred to various cases on treaty law and DTAA viz. ***Azadi Bachao Andolan, Ram Jethmalani case, Emirates Shipping case, Sanofi Pasteur Holdings case, Honda Motor Ltd co., Vijay Drolia case*** etc. He also discussed heads of income under treaty viz. income from immovable property, business income, dividend, airline, interest and royalty etc. Justice AKJ Nambiar then concluded the session addressing the questions the raised by participants.

DAY – 2

Session 3

Transfer Pricing: Basic Principles & Major Areas of Dispute

Speakers: Mr. V. Lakshmikumaran & Mr. Sujit Ghosh

Chair: Justice Vineet Kothari

The session began with the assertion that transfer pricing is a major area of concern and under the corporate structure the cobweb of the shell companies is created to adjust the prices in such a manner that profits are shifted to tax havens where they are taxed at a beneficial rate. Transfer pricing is the price charged in a transaction between two related parties. Under the income tax regime the attempt is not only to trap revenue but also to ensure that illegal or erroneous expenses are not claimed. In this regard, it was pointed out that while expenses are a 'state of fact' transfer pricing tends to go beyond this to a 'state of acceptable fact'. That is to say, transfer pricing is inherently a fact intensive exercise and extremely subjective in nature. It involves hypothetical considerations and comparisons, and reasonable minds may differ on interpretation of hypothetical facts. Therefore, to make an objective assessment of a subjective law is a challenge before the courts. In this regard, India has adopted the Arm's Length Price approach whereby transaction price is determined based on the functions, assets and risk analysis of parties and the members of MNE group are treated as separate entities rather than inseparable part of single unified business.

Section 92 of the Income Tax Act and Rules 10A to 10E of the Income Tax Rules dealing with the transfer pricing provisions were briefly discussed. The issue was dealt with the aid of illustrations. For instance, if the transaction value of raw material is $100. Now, higher the cost of raw material lower will be the profit and as a result India will get lesser amount as income tax. Therefore, by applying the Arm's Length Principle the income tax authorities arrive at the value of $95 to be the transaction value of the raw material thereby suppressing the cost of the raw material. This, in turn increases the profit and consequently the income tax collected is much more. On the other hand, the custom authorities are interested in collecting tax on the transaction value and therefore the endeavour is to arrive at an estimated valuation higher than the base value. The method of valuation adopted by income tax authorities and customs authorities appears to be conflicting. In this context, it was remarked that there is no need for any formal convergence on the assumption that the

subjective satisfaction of the customs authorities and income tax authorities should be exercised in the most honest manner and that commercial transactions eventually have a bearing on economic realities. However, another school of thought proposed for some form of convergence in order to bring in more objectivity in the otherwise subjective nature of the transfer pricing law.

It was further clarified that there is a difference between entrepreneurs and service providers as the former incurs a gamut of risk including profit/loss, market, capital, bad debt, technology obsolescence etc. In terms of economics, the entity that bears the maximum risk should make greater profit/margin and the one that takes lesser risk must get a proportionate reward. Transfer pricing is all about gearing to ascertain the risk taker. In this regard, the session delved into the six methods to arrive at an Arm's Length Price as specified under Section 92C of the Act which are (i) Comparable Uncontrolled Price (ii) Resale Price Method (iii) Cost Plus Method (iv) Profit Split Method and (v) Transactional Net Margin Method and (vi) such other method as may be prescribed by the Board. Most of the disputes relating to the transfer pricing arise with respect to the choice of the method and the choice of comparable by the assesse. It was stressed that courts are expected to see if the most appropriate method has been followed and the comparables have been properly adopted based on the circumstances of the particular case.

The session deliberated upon the pertinent issue of whether selection of comparables amounts to substantial question of law. Under Section 260 A of the Income Tax Act, 1961 appeal lies to the High Court where substantial question of law can only be entertained. It was pointed out that unless the findings of the tribunal are found to be perverse the interference by the High Court in such cases should be minimal. However, under writ jurisdiction High Court can venture into broader concerns relating to transfer pricing in international taxation. It was pointed out that insofar as transfer pricing is concerned the jurisdiction of writ and appellate court is blurred. That is to say, 'perversity' in the methodology adopted or decision making process and 'jurisdictional fact' can be a ground for appeal as well as writ jurisdiction. However, where a conclusion taken by a tribunal does not admit of a view that is eminent from the reading of the law the appellate court will have exclusive jurisdiction and a writ would not lie. In this regard the Karnataka High Court in ***Principal Commissioner of Income Tax, Bangalore & Another v. M/S Softbrands India (Pvt.) Ltd.***[1] observed that in transfer pricing matters aspects related to choice of comparable companies, choice

[1] ILR 2018 KAR 3959

of filters used, correctness of application of filters etc. are factual exercises and it does not give rise to any substantial question of law. However, the Delhi High Court in ***Rampgreen Solutions (Pvt.) Ltd. v. Commissioner of Income Tax***[2] admitted and allowed the appeal filed by the assesse for rejection of comparable companies. The issue is pending before the Hon'ble Supreme Court in the matter of ***Principal Commissioner of Income Tax v. M/S Sap Labs India Pvt. Ltd.***[3]

The session also dealt with the issue of AMP expense which contemplates that if a domestic company is incurring significant expenses to push the brand value of the foreign parent company the former must earn a certain amount of consideration. This principle is etched in the OECD guidelines as well. However, it was pointed out that it is not the factor but the factorial of compensation which must be deliberated upon. The Delhi High Court in ***Principal Commissioner of Income Tax v. Sony Mobile Communications India (Pvt.) Ltd.***[4] held AMP to be an international transaction and the same cannot be disputed for the reason assesse itself contended that it has been remunerated as part of the distribution function. The Court however, rejected BLT as a method to benchmark the transaction or determine the compensation receivable by the assesse. It was held that distribution function and ALP function are closely linked and should therefore be benchmarked together. In ***Maruti Suzuki India Ltd. v. Commissioner of Income Tax***[5] the court followed the decision in Sony Ericsson and held that BLT is not a prescribed method under the Income Tax Act to determine compensation for AMP function. In order to determine compensation Revenue must show the existence of an international transaction on account of AMP function.

Session 4

Appellate and Writ Jurisdiction of High Courts: Jurisdiction and Limitations

Speakers: Mr. S. Ganesh & Mr. Sujit Ghosh

Chair: Justice Manmohan

The session commenced with the assertion that the power of the High Court under statutory appellate provisions or writ remedies under Article 226 of the Constitution is very wide. It was highlighted that as a writ court while exercising power under Article 226 judge must be concerned

[2] (2015) 377 ITR 533 (Delhi)
[3] Diary No(s). 26872/2019
[4] 2021 SCC OnLine Del 2465
[5] (2016) 381 ITR 117

with the decision making process and not the conclusion or the correctness of the decision. Such process could be vitiated in multiple ways such as perversity, error of jurisdiction, non-consideration of relevant material etc. However, the High Court has limited appellate jurisdiction to interfere with findings of fact recorded by the tribunal.

The appellate jurisdiction is enshrined in Section 260A of the Income Tax Act, 1961 which provides for appeal to the High Court against the decision of the Income Tax Appellate Tribunal only on substantial question of law. It was opined that in order to be 'substantial' a question of law must be debatable and not previously settled. While dealing with the appellate jurisdiction of the High Courts, five tests as to what constitutes 'substantial question of law' based on the decision in ***Santosh Hazari v. Purushottam Tiwari***[6] were discussed: (a) It directly or indirectly affects substantial rights of the parties; (b) It is of general public importance; (c) It is an open question in the sense that the issue has not been settled by the Supreme Court; (d) It is not free from difficulty; or (e) It calls for a discussion of an alternate view.

In ***Naresh Shridhar Mirajkar and Ors. v. State of Maharashtra and Anr.***[7]**,** it was held that an alternative statutory remedy does not operate as a bar to maintainability of a writ petition in at least four contingencies, namely: (i) violation of fundamental rights; (ii) violation of principle of natural justice; (iii) order or notice is wholly without jurisdiction; or (iv) vires of act is challenged. The decision in ***Assistant Commissioner of State Tax and Others v. M/s Commercial Steel Limited***[8] has reiterated this principle. Similarly, ***in A.V. Venkateswaran, Collector of Customs, Bombay v. Ramchand Sobhraj Wadhwani and Another***[9]**,** it was observed that writ jurisdiction is equitable and discretionary and its object and purpose is to redress injustice wherever it may be found. Therefore, it is not desirable to lay down inflexible rules to be applied with rigidity in every case which comes up before the court. That is to say, plea of alternative remedy is closely and inextricably interconnected to the discretionary aspect of the exercise of writ jurisdiction. Consequently, the fact that an assessment order has been passed and it is open to challenge by way of an appeal does not denude the right of the petitioner to challenge the notice of assessment if it is without jurisdiction. In ***Calcutta Discount Company Limited v. Income Tax Officer,***

[6] (2001) 3 SCC 179
[7] 1966 SCR (3) 744
[8] 2021 SCC OnLIne SC 884
[9] AIR 1961 SC 1506

Companies District and Another*[10]*, the Supreme Court held that if the Assessing Officer had no jurisdiction to initiate jurisdiction proceedings the mere fact that subsequent orders have been passed would not render the challenge to jurisdiction infructuous.

The session went on to explore liberal and pragmatic approaches adopted by the Supreme Court while entertaining writ jurisdiction in cases where alternative remedy is available. In this regard, the Supreme Court in ***Paradip Port Trust v. Sales Tax Officer and Others***[11] held that even though an alternative remedy is available against the assessment order there are appropriate pristine questions of law involved which should be decided at the earliest and remanded the matter to the respective High Courts to be decided on merits. In contrast, the Supreme Court in ***Commissioner of Income Tax & Ors. v. Chhabil Dass Agarwal***[12] held that a writ can never lie against an assessment order.

The discussion also pertained to jurisdictional error including instances of lack of jurisdiction and assumption of jurisdiction where it does not exist. In this regard the decision in ***Nusli Nieville Wadia v. Ivory Properties & Ors.***[13] was referred wherein the Supreme Court addressed the blurred line between lack of jurisdiction and error of jurisdiction. Further, the discussion explored the contours of jurisdictional fact. It was pointed out that in ***Raza Textiles Ltd. v. Income Tax Officer, Rampur***[14] it was held that the question whether the jurisdiction fact has been rightly decided or not is open for examination by the High Court in a writ of Certiorari. Also, in ***Carona Ltd. v. Parvathy Swaminathan & Sons***[15] it was observed that it is well settled that by erroneously assuming existence of a jurisdictional fact a subordinate court or tribunal cannot confer upon itself jurisdiction which it otherwise does not possess.

Typically, in most tax matters Certiorari or Prohibition are the most sought after writs. It was stressed that the writ of prohibition is most appropriate in such cases. Where the lower authority does not have jurisdiction a challenge can be made at the stage of show cause notice itself. In such a case alternate remedy shall not be a bar.[16] The discussion highlighted major litigation area in this

[10] AIR 1961 SC 372
[11] (1998) 4 SCC 90
[12] (2014) 1 SCC 603
[13] AIR 2019 SC 5125
[14] AIR 1973 SC 1362
[15] (2007) 8 SCC 559
[16] Isha Beevi v. TRO (1976) 1 SCC 70

regard to be the reopening of assessment. The judgment of ***GKN Driveshafts v. ITO***[17] was referred to wherein the Supreme Court stated that issuance of notice under section 148 must be adhered to before reassessment proceedings to which the assesse is entitled to object and only after disposal of the objections the authority can proceed further. Therefore, at the stage of objections the writ court may be approached.

The discussion also reflected upon the doctrine of imminent threat which permits maintainability of writ petitions without there being any overt act of the revenue. In this regard, the Constitution Bench judgment of ***State of Bombay v. United Motors***[18] was discussed wherein challenge to the Bombay Sales Tax Act, 1952 on grounds of violation of Article 19 (1) (g) on its mere passing without there being any notice, assessment or demand was held to be maintainable. In another decision of ***Himmatlal Harila Mehta v. State of MP***[19] it was held that anticipatory threat by the authority of law using coercive machinery under the impugned legislation was sufficient infringement of one's fundamental rights and therefore gives the petitioner right to seek relief under Article 226.

Lastly, it was pointed out that High Courts ordinarily do not interfere in writs against assessment orders unless it is wholly without jurisdiction. However, recently the Delhi High Court has quashed a number of assessment orders owing to the newly introduced faceless assessment provision (Section 144B). Providing ease of tax compliance and opportunity to tax payers before finalizing the assessment orders are core features of the faceless assessment. The system allows for dynamic jurisdiction, team based assessment, functional specialization and does away with human interface altogether. It was reflected that the dynamic jurisdiction seem to be unsettling the otherwise settled principles of territorial jurisdiction.

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[17] (2003) 1 SCC 72
[18] AIR 1953 SC 252
[19] 1954 SCR 1122