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Case Comment on Ruling of AAR in the case of Tiger Global International Holdings, Mauritius

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ABSTRACT

This case comment is situated within the domain of taxation law and examines the intricate issues of international taxation and treaty shopping in the Tiger Global-Flipkart case, focusing on India's Double Taxation Avoidance Agreement (DTAA) with Mauritius. To address double taxation, India has established DTAAs, such as the 1983 India-Mauritius DTAA, which exempts Mauritius residents from capital gains tax on Indian assets. In this case, Mauritius-based subsidiaries of a U.S. corporation sold Flipkart shares, generating substantial capital gains. India's tax authorities contended that these subsidiaries lacked independent control and functioned merely as "see-through entities," with control residing in the U.S., thereby denying DTAA benefits and withholding tax exemptions. The Authority of Advance Rulings (AAR) invoked anti-avoidance provisions, emphasizing that the corporate structure aimed to exploit the DTAA for tax benefits. The AAR's ruling diverged from prior decisions that upheld DTAA exemptions in similar scenarios, sparking debate on consistency and the persuasive value of AAR decisions. This case underscores India's commitment to preventing treaty shopping, reinforcing that capital gains exemptions under the DTAA are not absolute and are subject to scrutiny on economic substance grounds. The ruling has notable implications for multinational corporations employing intermediary holding structures to minimize tax liabilities and signals India's increasing reliance on anti-avoidance doctrines, such as General Anti-Avoidance Rules (GAAR). This examines the arguments put forth by the counsels and the parameters inadequately perused by the adjudicating authorities and examines the correctness of the Ratio Decidendi. It also provides a Comparative Assessment with Other Judgments and highlights the Jurisprudential Contribution of this case.

***Keywords**: International Taxation, DTAA, Authority of Advanced Ruling, Capital Gains, Tiger Global, Flipkart.*

I. INTRODUCTION

International taxation essentially refers to a set of rules and regulations relating to the taxation

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procedures of income and assets across the territorial borders of a nation. In India, the most critical tax provision is Article 265 of the Constitution, which states that no tax shall be levied or collected except by authority of law. When it comes to international taxation, there are different sets of national rules and international conventions to govern it. The most relevant issue in international taxation is the problem of double taxation, which refers to when countries of two different jurisdictions seek to tax the same amount of money of the same legal person[2].

Thus, to avoid such issues, many countries have drawn up Double Taxation Avoidance Agreements ("DTAA") to facilitate trade and investments by voluntarily restricting their taxing jurisdictions. Currently, India has signed the DTAA with more than 80 countries and protects its non-residents from paying taxes to the source and resident country. The current case is based on the DTAA signed between India and Mauritius on 6th December 1983. This agreement has six chapters, which further sub-divides into 29 articles. Under this treaty, Individuals living in Mauritius who earn income from selling shares of Indian companies will be subject to capital gains tax exclusively in Mauritius and will not be obligated to pay any capital gains tax in India. The term tax avoidance is not defined statutorily. Still, OCED represents tax avoidance as "an arrangement of a taxpayer's affairs that is intended to reduce his liability, and that although the arrangement could be strictly legal is usually in contradiction with the intent of the law, it purports to follow.[3]"

The Authority of Advanced Ruling (AAR), which ruled for this case, came into effect in 1993 through the Finance Act. Section 254N of the Income Tax Act, 1961 states that a ruling can be obtained by an applicant, either non-resident or resident, who is involved in a transaction with a non-resident for any question of law or fact regarding the tax liability of non-resident out of a transaction that has already taken place or is to be undertaken. This authority is an independent adjudicatory body headed by a retired Supreme Court judge[4]. It is empowered to issue a ruling, and it only applies to any question of law or fact under the Income Tax Act, 1961, and the authority has to give the ruling within six months of receipt of the application.

II. FACTS OF THE CASE AND PROCEDURAL HISTORY

Tiger Global was one of the earliest investors in Flipkart. Tiger Global II Holdings, Tiger Global III Holdings and Tiger Global International IV Holdings, which are Mauritian subsidiary

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[2] CMA Mrityunjay Acharjee, International Taxation In India - Recent Developments & Outlook (Part - II), 23 TBS 7, 7 (2018)

[3] OECD, Glossary of Tax Terms

[4] Anonymous, Authority for advanced rulings, INDIALIAISON, (n.d), https://indialiaison.com/authority_for_advance_rulings.htm#:~:text=Advance%20Ruling%2C%20means%20written%20opinion,amended%20from%20time%20to%20time.

companies of a US corporation, sold about 17% out of the 22% of their shares of Flipkart (a Singapore company) to Walmart (US Company). This transaction was valued at over 14 Crores. Tiger Global had made most of its investments during the first half of the decade (before 2016), so the amendment made to the DTAA did not apply to them. The applicant filed the case when the tax department stated that they were not eligible for tax benefits under the DTAA as they were not independent in their decision-making and that the purchasing power and control of shares did not lie with them. Thus, the tax department refused to grant the applicant 'nil' withholding certificates under Section 197 of the Income Tax Act and prescribed an appropriate withholding rate for the sale of shares. Following this, the applicant (Tiger Holdings) filed an application before the AAR.

III. Assessing the appropriateness

The main issue in this case was

"*Whether the capital gains arising out of the sale of shares held by Tiger Holdings in Flipkart Pvt Ltd., which derives its value substantially from the assets located in India, would be taxable under the Income Tax Act, 1961 when read along with the Indian and Mauritius DTAA*[5]?"

This issue is framed appropriately since most companies tend to take advantage of this particular provision of the DTAA and base their companies solely in Mauritius so that they could claim tax benefits. Thus, the ruling on this issue would answer a lot of confusion and restrict the mischievous use of the DTAA by the companies.

The Clause (i) of the proviso to Section 245R (2), which states that AAR shall not entertain any application which involves the determination of the Fair Market Value of a property, was not attracted in this case because the issue raised before AAR does not include the valuation of shares or computation of Capital Gains on the transfer of shares since the issues are only about the taxability of capital gains.

Clause (ii) of the proviso to Section 245R (2) states that an application on a pending matter before any IT department shall not be allowed. This proviso is not applicable in this case since the proceedings under Section 197 were already reviewed and concluded. No further proceeding was pending on the said date. The AAR rightly relied on precedents like ***Hyosung Corpn v. AAR*[6], *Burmah Castrol Pic v. AAR*[7], *and Asgarali Nazarali Singaporawalla v. State of***

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[5] Anonymous, Analysis of AAR Ruling in Tiger Global Holdings' Transfer Of Flipkart's Shares, TAXAARAM, (19th August, 2020), https://www.taxaaram.com/articles/analysis-of-aar-ruling-in-tiger-global-international-holdings-transfer-of-flipkarts-shares
[6] Hyosung Corpn v. AAR [2016] 382 ITR 371 (Del)
[7] Burmah Castrol Pic v. AAR [2008]174 Taxman 95

Bombay[8].

The Court, in this case, relied on clause (iii) of the proviso to section 245R (2) of the Income Tax Act, 1961, which states that applications which are prima facie related to transactions involving tax avoidance shall not be admitted.

The AAR was proper to reject the application at the admission stage based on this proviso clause because the applicants, as mentioned before, are subsidiary companies of a US group of companies. The main objective/motive of the applicants is to act as holding companies for any investment made by the parent company outside Mauritius. In this case, the applicants invested in Flipkart, an Indian Subsidiary, with the primary purpose of obtaining tax benefits through the DTAA signed between the two countries. As pointed out by the tax department, the decision-making authority and financial control were not with the applicants, and the applicants were only 'see-through entities'. The head and brains behind the transfer of shares were situated in the USA with Mr. Charles P. Coleman.

The applicants placed reliance on the percentage of the ruling given in Moody's Analysis Inc. by AAR, which was subsequently upheld by Delhi HC in 2013. That case was regarding the sale of shares of an Indian Company (Copal Research India Pvt Ltd) by a Mauritian company (Copal Research Ltd) to Moody's Analytics Inc. In this case, the AAR only looked at the central issue of whether the capital gains arising from the said transaction were taxable. It overlooked that in the same ruling, the AAR allowed tax benefit to be claimed on the transfer of shares of Exevo India by Exevo USA through CRML Mauritius to Moody Inc, USA. This situation is quite similar to the present case. But AAR rejected reliance on the present and denied tax benefits in the current case, going against the law which was previously established by it.

IV. ANALYSIS OF ARGUMENTS

The applicant claimed exception under Clause 4 of Article 13, which provides that any gains from the transfer of any property he referred to in paragraphs 1, 2, 3 and 3A shall be taxable only in the Contracting State of which the alienator is a resident. The applicants argued that it must be proven that the transaction about the final sale of shares itself was designed to avoid taxes. So, the Income Tax Department had failed to discharge its burden of proof. AAR counter-argued this by stating, “You don’t just compute taxes by looking at the final transaction. Instead, you look at the transaction as a whole.”

The stand taken by AAR is more appropriate, as held in Ramsay’s principle, where the

[8] Asgarali Nazarali Singaporawalla v. State of Bombay, 1957 AIR 503

transaction as a whole has to be examined to know whether it was made for tax avoidance or not.

V. Review of parameters inadequately perused

It is further essential to note that the DTAA provides an exemption from capital gains tax on the transfer of shares of an Indian Company, and such an exemption shall not apply to a company not resident in India, which is Flipkart - a Singapore-based Company. This conclusive statement made by AAR is quite contradictory because if the applicants are considered to have transferred shares of a Singapore company, the question of taxing such capital gains should not arise in the first place. This shows that AAR while making the above statement, disregarded that the Singapore Company substantially derived its assets from India. In this case, the retrospective amendment made to section 9 of the Income Tax Act, which enables the taxing of capital gains of a foreign company which derives its substantial value from assets located in India, based on the judgment given by the Supreme Court in ***Vodafone International Holding v. UOI***[9] has been overlooked by AAR. This indicates that AAR has relied on the theory of legal ownership rather than the theory of beneficial ownership of shares. Although the ruling mentioned the Vodafone case, it did not look into the details of it.

In this case, the AAR explicitly stated that the arrangement made by the applicants was entirely made to claim tax benefit, and such shall intention was not intended by the lawmakers. Although this statement looks legally sound when read alone, it contradicts already settled legal propositions. Supreme Court, in the case of ***Union of India vs Azadi Bachao Andolan***, states that "treaty shopping doesn't tant-amounts to avoidance of tax", - which means that arrangements done within legal restrictions to avail tax benefit under treaties don't mean it amounts to tax avoidance prima facie.

VI. Ratio decidendi and Obiter dictum - examination of correctness

In this case, the AAR denied the tax benefit under Article 13(4) of India-Mauritius DTAA for exemption of capital gains tax on two grounds

- The India-Mauritius DTAA's goal was to exempt capital gains on the transfer of shares only belonging to Indian companies; the legislator never intended for any such exemption on the transfer of shares belonging to companies not resident in India. The applicants are not eligible for the treaty benefit because they transferred shares of a Singaporean company rather than an Indian one.

[9] *Vodafone International Holding v. UOI*, [2012] 341 ITR 1(SC)

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- Mr. Charles P. Coleman, the beneficial owner of the entire group structure, was in charge of the applicants' absolute control and management, not in Mauritius but in the United States. Therefore, the applicants' entire plan was to use the India-Mauritius DTAA to claim benefits, which was not what the lawmakers had in mind. This plan was essentially an attempt to avoid paying taxes in India.

I stand by the grounds for denying the tax benefit as stated by the AAR since treaty shopping is becoming a trend, and it affects the tax base of any country. And giving out rulings like these would contribute to restricting treaty shopping by multinational corporations through shell companies. However, the AAR has not been consistent with its ruling since its previous ruling stands contradictory to the grounds of denial of tax benefit in this ruling. Thus, it proves to be detrimental to the persuasive value and credibility of this ruling.

[In this case, there were no passing remarks or comments made by the authority that were not directly relevant and were persuasive]

VII. Comparative assessment with other judgments

In the case of ***Sanofi Pasteur Holding***[10], the AP High Court has ruled to avail tax benefits in the indirect transfer of shares in India- France DTAA. Mumbai IT Tribunal, in the case of ***Sofina S.A***[11]**,** has allowed the same as the AP High Court ruling concerning the India- Belgium Tax Treaty. In the case of ***GEA Refrigeration Technologies GmBH***[12], even AAR has ruled to availing tax benefits under the India-Germany tax treaty regarding the indirect transfer of shares. These judgments stand in contrast to the ruling of AAR in the current case, where it has denied tax benefits under the India-Mauritius Tax treaty regarding the indirect transfer of shares.

VIII. Jurisprudential contribution

This ruling has reignited controversy surrounding intermediary holding structures and indirect transfer of shares. Later, on May 10, 2016, the Amendment Protocol to the Agreement for the Prevention of Double Taxation between India and Mauritius was signed. This protocol specified that starting from the financial year 2017-18, capital gains resulting from the sale of shares acquired on or after April 1, 2017, in an Indian-resident company would be subject to source-based taxation. Simultaneously, investments made before April 1, 2017, were exempt from capital gains tax in India, as they were considered grandfathered.

The growing scrutiny from tax authorities emphasises the actual economic reality over legal

[10] Sanofi Pasteur Holding SA V. Dept of Revenue [2013] 354 ITR 316 (AP)
[11]Sofina S.A, ITA N0. 7241/MUM/2018
[12] GEA Refrigeration Technologies GmBH, Application No. 1232 of 2012

technicalities. It has led to the denial of advantages granted by the India-Mauritius tax treaty, even for investments that were previously exempt. While the decision and rationale put forth by the AAR may raise questions, it serves as a timely reminder for global investors to assess their existing structures and ensure that legitimate business reasons substantiate these multi-tier arrangements. Furthermore, given the broad scope of General Anti-Avoidance Rules (GAAR) and the Principal Purpose Test under the Multilateral Instrument (MLI), corporations will need to engage in thorough and precise planning to access treaty benefits and avoid being penalised under anti-avoidance regulations.

In September 2020, Tiger Global moved to Delhi HC against the ruling given by AAR by stating that "There is enough substance and decision making in the deal structure to get India-Mauritius treaty benefits[13]" and that AAR has failed in looking through all aspects of the transaction before delivering the ruling.

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[13] Kriti Bhalla, Tiger Global Moves Delhi HC Against Flipkart Double Tax Ruling, INC42,)22nd September, 2020), https://inc42.com/buzz/after-aar-rejection-tiger-global-moves-delhi-hc-against-flipkart-tax-ruling/