What *Azadi Bachao* syas about Treaty-Shopping or Round Tripping?

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A lot of studied disinformation about what ***Azadi Bachao*** (2003-TIOL-13-SC-IT) says about Treaty Shopping (or its cognate 'Round Tripping') has been circulated by the hired intellectuals through interpersonal lobbying and media. An article published in ***The Times of India*** of Jan 19, 2007 says that "all experts believe" that "classifying abuse or misuse of a treaty and even making 'treating shopping' illegal will be a very difficult task for the Indian government especially after judgments like the ***Azadi Bachao Andalon*** where Supreme Court justified treaty shopping." "Treaty shopping" is a graphic expression used to describe the act of a resident of a third country taking advantage of a fiscal treaty between two Contracting States; and the 'Round Tripping' is the round trip of black money from and the domestic jurisdiction after secret hibernation and noxious mutation in other countries. Both are, in short the device which facilitates the deflection of legitimate tax incidence, and provides scope for laundering ill-gotten or tainted wealth of the host of the waxing breed of fraudsters, scamsters, anti-national gangsters, crooks and knaves of all hues from the different lands. We get it from the Press that our Government is contemplating to revisit the Indo-Mauritius Double Taxation Avoidance Convention. Hence I consider it my moral duty to let the government and people know what the Supreme Court said as to the evil of Treaty Shopping in that case, and how that view stands now in the public domain. Our Government should now consider this aspect of the matter unless it is ready to be taken for a ride by the vested interests and the persuaders of all hues. In ***Shiva Kant Jha's Case & Anr v. Union of India & Anr.*** [2003-TIOL-04-HC-DEL-IT] the Delhi High Court said that "India had been losing crores and crores of rupees by allowing opaque system to operate", even a popular magazine the Business World of Dec. 11, 2006, on detailed analysis, shows a worrisome profile of wrongful loss to India and a wrongful gains to Mauritius and of those whose stratagems are made to succeed.

The Delhi High Court in ***Shiva Kant Jha's Case*** considered Treaty Shopping as the core point: "The core issue is as to what should be done when on investigation it is found that the assessee is a resident of a third country having only paper existence in Mauritius without any economic impact with a view to take advantage of the double taxation avoidance scheme". It held it illegal as (i) "An abuse of the treaty or Treaty Shopping is illegal and thus necessarily forbidden."; (ii) The Indo- Mauritius Avoidance of Double Taxation Convention was entered into between the Government of the Republic of India and the Government of Mauritius for avoidance of double taxation and the prevention of fiscal evasion with regard to tax on income and capital gains and for encouragement of mutual trade and investment; (iii) ***"Treaty Shopping which amounts to abuse of the Indo-Mauritius Bilateral treaty may amount to fraudulent practice and cannot be encouraged."; (iv) The company although had obtained residential certificate in Mauritius but had nothing to do therewith and factually, it got itself registered only for the purpose of tax avoidance so as to obtain benefit of the treaty; (v) "No law encourages opaque system to prevail."***

SLP before the Supreme Court was filed to which a Mauritian company became a co-appellant. Whilst the leave for appeal was sought for the Mauritian company by Shri Arun Jaitley, it was argued by Shri Salve who had argued the Government's case before the High Court as India's Solicitor-General. The Union of India's case was argued by Shri Sorabji, the then the Attorney-General. Both these learned men, who had argued the case of ***McDowell & Co*** . but had lost before the Constitution Bench, argued against ***McDowell*** = (2002-TIOL-40-SC-CT) which led the DB of two Judges to dub the Constitution Bench as "a hiccup" and "temporary turbulence".

The Division Bench of the Supreme Court reversed the decision of the High Court in ***Azadi Bachao Andolan*** , and held Treaty Shopping valid with the following seminal observations:

"There is elaborate discussion in Baker's treatise on the anti abuse provisions in the OECD model and the approach of different countries to the issue of "treaty shopping". True that several countries like the USA, Germany, Netherlands, Switzerland and United Kingdom have taken suitable steps, either by way of incorporation of appropriate provisions in the international conventions as to double taxation avoidance, or by domestic legislation, to ensure that the benefits of a treaty/convention are not available to residents of a third State. Doubtless, the treatise by Philip Baker is an excellent guide as to how a State should modulate its laws or incorporate suitable terms in tax conventions to which it is party so that the possibility of a resident of a third State deriving benefits thereunder is totally eliminated. That may be an academic approach to the problem to say how the law should be. The maxim "judicis est jus dicere, non dare" pithily expounds the duty of the court. It is to decide what the law is, and apply it; not to make it ."

Two broad comments are worthwhile:

(i) The reason for non-intervention to reject the evil of Treaty Shopping is the Supreme Court's perception of judicial role stated with reference to a Latin maxim. In ***Assistant Commissioner of Income-tax v. Velliappa Textiles & Ors*** (2003-TIOL-12-SC-IT***)***
in a one-sentence paragraph the three judges Bench of our Supreme Court in its majority judgment reiterated the above quoted view as to the judicial role: but the minority view of Justice G.P. Mathur struck a contrary note. But in ***Standard Chartered Bank***
our Supreme Court (Coram: N. Santosh Hegde, K.G. Balakrishnan, D.M. Dharmadhikari, Arun Kumar and B.N. Srikrishna, JJ.) (2005-TIOL-79-SC-FERA-Constitution) reversed the view, taken in ***Assistant Commissioner of Income-tax v. Velliappa Textiles & Ors*** , on the role of judiciary. Hon'ble Justice B.N. Srikrishna in his dissenting Judgment (on behalf of Justice N. Santosh Hegde and himself) acknowledged it in these telling words:

"The interpretation suggested by the learned counsel arguing against the majority view taken in Velliappa, which has appealed to our learned brothers Balakrishnan, Dharmadhikari and Arun Kumar, JJ., would result in the Court carrying out a legislative exercise thinly disguised as a judicial act."

Velliappa Textiles Ltd. and Anr, decided by adopting the judicial role perception succinctly stated in the maxim
'judicis est just dicere, non dare', was overruled by the majority decision in ***Standard Chartered Bank*** .

As a larger Bench in a subsequent decision has departed from the role perception which led the Division Bench to say what it has said on Treaty Shopping, the view of the Division Bench in ***Azadi Bachao***
becomes incompatible with the subsequent larger Bench Decision. As a matter of logic it can be assumed that a decision on a point is bound to be wrong if it is arrived if it is arrived under erroneous role perception. I may mention, in passing for the information of my countrymen, that the ambit of the Circular Making power of the CBDT, as declared in ***Azadi Bachao,***
was disapproved in the minority judgment of Justice Reddy in ***Commissioner of Customs, Calcutta v. Indian OIL Corporation Ltd*** (2004-TIOL-23-SC-CUS). After considering ***Azadi Bachao,*** it suggested reconsideration of the correctness of ***Dhiren Chemical Industries (*** 2002-TIOL-83-SC-CX***),*** in the light of which a major point had been decided in ***Azadi Bachao.*** And now we find that in ***Commissioner of Central Excise , Bolpur (Appellant) v. Ratan Melting & Wire Industries, Calcutta (Respondents)*** [2005-TIOL-41-SC-CX-LB] this matter stands referred to a Constitution Bench. In the meanwhile a 3-Judges Bench in ***Pahwa Chemicals Pvt Ltd vs the Commissioner of Central Excise*** (2005-TIOL-43-SC-CX-LB
) has said what, in effect, Delhi High Court had said in ***Shiva Kant Jha's Case*** on circular-making power.

(ii) The tenor of the exposition of principles, culled from Phillip Baker, tells clearly that the Division Bench was convinced that Treaty Shopping is an abuse of a tax treaty which deserved to be stopped, but it felt that under its role perception it could not provide an appropriate remedy. The improper narrowing of the role perception was so dominant that the Division Bench missed the examples of cases in Phillip Baker wherein judiciary in exercise of its common law jurisdiction provided remedy. In short, no superior court in any of the major country world over has justified Treaty Shopping. Prof Ray August (Professor of Business Law Washington State University), in his ***International Business Law*** (4th ed. 2004) points out:

"In countries that do not have specific anti-abuse legislation, the problem of treaty shopping is attacked using general principles of equity. Common law countries (including Australia, Canada, and the United Kingdom) use a "substance over form" approach. That is, their tax authorities attempt to determine if the movement of income between foreign affiliated companies is based on legitimate commercial reasons or if it is merely a sham set up in order to obtain treaty benefits. Civil law countries (including France and Germany) use an "abuse" approach. In

other words, their tax authorities ask whether a particular arrangement of companies constitutes an abuse, a misuse, or an improper use of a tax treaty."

(iii) This narrowed role perception led the Division Bench to rely on the three long paragraphs from book on International Taxation, written whilst the matter was ***sub judice***
before the High Court and the Supreme Court. It is most unfortunate that neither the Bench, nor the Attorney General noticed (i) that book was written by an interested person during the matter was ***sub judice***
before the High Court; (ii) that the author is a Chartered Accountant who had been a partner in infamous Arthur Anderson for 25 years, was on the website of the legal firm which represented the Mauritian company before the Bench, and had close connection with Mauritius in his professional capacity, and was the First Academic Director in an institute under/associated with the Financial Services Promotion Agency in Mauritius ; (iii) that the author was neither one who held a judicial office, nor was he an advocate of any eminence: he described himself on his website as "a strategy and International Tax Consultant to several Indian and Overseas Companies."; (iv) that the author is himself " is at pains to point out that any information he gives should not be used as the basis for providing advice without further consultation and research."; (v) the exposition in the three paragraphs show only selective materials culled from the areas of darkness as can be considered in a brief for the tax havens.; (v) that we are told to accept the doctrine of toleration of Evil "in the interest of long term development. The author is at pains to point out in the Preface itself that any information he gives should not be used as the basis for providing advice without further consultation and research. Never in the past any lawyer would have tried to persuade a court with a book of this sort going against all the principles governing the reliance on text-books [vide ***Cordell v. Second Clanfield Properties***
((1969) 2 Ch. 10). If the A-G found this o.k. where were the respondents asleep? Will you believe if I tell you they had not seen the book, nor had been invited to have their say on this book of not much worth. Lord Bridge L.J. in ***Goldsmith v. Perrings Ltd (***
(1977) 1 W.L.R. 487) observed that a judgment based on the Judge's "judicial research", the result of which has not been put to counsel, violates the rules of ***audi alteram partem***
since that rule applies both to facts and law. Dissenting from Lord Denning, Scarman L.J. said [1977] 2 All ER 720 C.A.] that wherever a point is decided against someone the must should be taken up and the court should put the point to the opposite party as a matter of compliance with the rule of ***audi alteram partem.***
Besides the holding on the doctrine of necessary evil seems to be incompatible with scores of cases highlighting creativity with an evident factor of constitutional morality: to mention one, the 9 judges Bench in ***Coelho (Dead) By LRs. vs. State of Tamil Nadu & Ors (*** 2007-TIOL-05-SC-Constitution-LB
) : "It is the duty of this Court to uphold the constitutional values and enforce constitutional limitations as the ultimate interpreter of the Constitution".

The purpose of highlighting the aforementioned facts is to inform our people as it is their executive government and Parliament who are now to act responding to the judicial ***cri de Coeur***
. A distinguished citizen and former dean of the faculty of law of Calcutta University, Dr M L Upadhyaya has perceptively observed in his Opinion on ***Azadi Bachao:***

> ***"Let us assume that two states have entered into a bilateral beneficial treaty securing certain benefits and advantages for their nationals only. There is no express or implied provision or suggestion to extend the benefits arising out of such treaty to the nationals of third States. In reality, the nationals of the third states pretending to be national entities of one of the contracting states claim such benefits. Objections are raised to such claims. If one of the Contracting States wants to condone this apparent illegal or unethical practice, how should it go about it. There are two courses open. One either the two states by consent amend the terms of the treaty and provide for by an express term in the treaty and then amend its laws, if the said amendments have financial implications affecting its revenues. But if the executive without amending the laws give a clarification of the provision of the treaty and the law and by executive fiat condones the manifestly illegal practice and does what was not initially intended by the treaty, it would certainly be a fraud on the Constitution and a colourable exercise of power. This is clearly an attempt to do indirectly what it could not do directly."***

Those who want to know a lot about the evil of 'Treaty Shopping' and 'Round Tripping' may go through the chapters on 'An Opaque System', 'Treaty Shopping', 'Supreme Court on Treaty Shopping', 'The CAG on Treaty Shopping', and 'A Morbid Story of the Indo-Mauritius DTAC' in my book on ***Judicial Role in Globalised Economy*** (published by the Wadhwa & Co.).

Now it is for our Parliament to act. I had put this fact in public domain in my interview to the Frontline which published it in its issue Volume 20 - Issue 23, November, 08 - 21, 2003 under the heading `Parliament has a role to play now'. It is good that our government wants to do something to give effect to one of its Common Minimum Programme to stop the misuse of the tax treaties. It is further suggested that in this pursuit let it not deplete the Consolidated Fund of India by unwarranted assistance to a tax haven with per capita income many times more

than that of our country with starving millions. This Fund is not meant for granting undeserved dole or largesse. The specious pleading for more of foreign funds is no good for the common men who shudder at the emerging two Indias in this phase of Economic Globalization when the political realm is subjugated to the economic realm led ruthlessly by, to borrow the words of Edmund Burke, "sophisters, economists, and calculators' working for a ***Sone ki Lanka***.

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(The views expressed are strictly personal)