

**INTERNATIONAL TAX
UPDATE**

**Delhi Tax Tribunal upholds
the validity of TRC, allows
DTAA benefit**



Delhi Tribunal Upholds TRC Validity for DTAA Benefits

Facts of the Case

- SC Lowy P.I. (LUX) S.A.R.L. is a company incorporated in Luxembourg on March 6, 2015, as a Limited Liability Company (LLC).
- It is registered as a Category II Foreign Portfolio Investor with SEBI (Indian Securities Market Regulator) and primarily invests in bonds and pass-through certificates issued by Indian companies and securitization trusts.
- For the Assessment Year (AY) 2021-22, the company declared an income of ₹10.63 crores in its tax return, filed on January 31, 2022.

- The company claimed benefits under the India-Luxembourg Double Taxation Avoidance Agreement (DTAA), asserting:
 - Business income was exempt from tax in India under Article 7 due to the absence of a permanent establishment in India.
 - Capital gains on the sale of securities were exempt under Article 13(6).
 - Interest income was taxable at a reduced rate of 10% under Article 11.
- The Tax Assessing Officer (AO) denied DTAA benefits, raising the following objections:
 - The company was allegedly a conduit entity engaging in treaty shopping for tax avoidance purposes.
 - It was argued that the company lacked economic substance and was not the

beneficial owner of the income, as it is step down subsidiary of a company incorporate in Cayman Islands.

- The Tax Residency Certificate (TRC) provided by Luxembourg was deemed insufficient to establish its claim of residency for tax purposes.
- Consequently, the AO taxed the company's income as per the Indian Income Tax Act:
 - Business income was taxed as interest income.
 - Capital gains were taxed at 30% under Section 115AD of the Indian Income Tax Act ("IT Act").
 - Interest income was taxed at 40% under Section 115UB of the IT Act.

- The Dispute Resolution Panel (DRP) upheld the AO's findings, leading the company to file an appeal before the Delhi Tax Tribunal.

Key Issues

- Whether the TRC issued by Luxembourg authorities is sufficient to establish the company's residency and entitlement to DTAA benefits.
- Whether the incorporation of the company in Luxembourg was primarily aimed at obtaining DTAA benefits, violating the Principal Purpose Test under the Multilateral Instrument (MLI).
- Whether the company had adequate economic substance to justify its claims of beneficial ownership and treaty benefits.
- Whether the company's income streams (business income, capital gains, and interest

income) were correctly taxed by the AO under Indian domestic law.

- Whether the AO and DRP were justified in denying the application of DTAA provisions based on their findings.

Judgment of the Court

- The Delhi Tribunal ruled in favour of the company, allowing it to claim DTAA benefits.
- The Tribunal observed that:
 - The TRC is a valid and conclusive document for establishing tax residency, as upheld in the *Tiger Global International III Holdings* [TS-624-HC-2024(DEL)] case by the Delhi's High Court.
 - The AO had not provided cogent evidence to prove that the company was a mere conduit

for tax avoidance or lacked economic substance.

- The Delhi Tribunal noted that the company demonstrated substantial economic activity in Luxembourg, including:
 - Paying taxes on its global income, including income from Indian investments.
 - Incurring operational expenses related to consulting, legal, and administrative services in Luxembourg.
 - Maintaining control and dominion over its investments, which supported its claim of beneficial ownership.
- The Delhi Tribunal rejected the Revenue's argument that the company's incorporation in Luxembourg was intended to exploit DTAA benefits, emphasizing:

- The company was established in 2015, before the MLI (Multilateral Instrument) provisions came into effect.
- Its investment portfolio was diversified across multiple jurisdictions, with only 14% of investments in India.
- The Delhi Tribunal placed reliance on various judicial precedents, including:
 - *Union of India v. Azadi Bachao Andolan* [263 ITR 706], where the Apex Court of India upheld treaty shopping unless it involved fraud or sham transactions.
 - *Bid Services Division (Mauritius)*, which recognized the sanctity of TRCs and required stringent evidence to question their validity.
 - The *Tiger Global* case, which clarified that TRCs and Limitation of Benefits (LOB)

clauses are sufficient to establish eligibility for treaty benefits unless there is evidence of fraud or tax evasion.

- Regarding the tax treatment of income, the Delhi Tribunal directed the following:
 - Business income from pass-through certificates was non-taxable under Article 7, as the company had no permanent establishment in India.
 - Capital gains from the sale of securities were exempt under Article 13(6).
 - Interest income was taxable at a reduced rate of 10% under Article 11, as the company was the beneficial owner of the income.
- The Tribunal emphasized that any allegation of fraud, sham transactions, or treaty abuse must be

substantiated with compelling evidence, not mere conjecture or assumptions.

For Complete details, please refer the judgement:

<https://itat.gov.in/public/files/upload/1736242639-rznf24-1-TO.pdf>

DISCLAIMER: - The information herein is based on ITAT Delhi's ruling in the case of SC Lowy P.I. (LUX) S.A.R.L. vs. ACIT (International tax) [ITA No.3568/DEL/2023] on 30th December 2024. While the information is believed to be accurate, we make no representations or warranties, express or implied, as to the accuracy or completeness of it. Readers should conduct and rely upon their own examination and analysis and are advised to seek their own professional advice. This note is not an offer, advice or solicitation. We accept no responsibility for any errors it may contain, whether caused by negligence or otherwise or for any loss, howsoever caused or sustained, by the person who relies upon it.