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EY Tax Alert

Supreme Court of India rules on tax treaty eligibility and taxation of an indirect transfer of shares of an Indian company by a Mauritius based investment fund

Executive summary

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This Tax Alert discusses the recent landmark Supreme Court (SC) ruling in the case of Tiger Global International Holdings[1] (Taxpayer) upholding rejection of advance ruling sought by the Taxpayer seeking treaty exemption for indirect transfer. The rejection was on the ground that the application relates to a transaction or issue designed prima facie for the avoidance of income-tax.

The core fact involved was that the Taxpayer, being a Mauritian company and holding a valid Tax Residency Certificate (TRC), sold shares held in a Singapore company which derived substantial value from shares of an Indian company during the tax year 2018-19. The shares of Singapore Company were acquired prior to 1 April 2017.

The Taxpayer claimed exemption from indirect transfer source rule under Income tax Act, 1961 (ITA) on the basis of Article 13(4) of India-Mauritius Double Tax Avoidance Agreement (I-M treaty or I-M DTAA). Upon denial of nil withholding certificate by the Indian Tax Authority, the Taxpayer sought an advance ruling from the Authority for Advance Ruling (AAR) by relying upon, *inter alia*, the TRC issued by Mauritian Authority, Circular No. 789 dated 13 April 2000 issued by Central Board of Direct Taxes (CBDT) and earlier SC rulings[2] upholding the significance of TRC for treaty eligibility.

[1] Civil Appeal No. 262 of 2026
[2] For instance, UOI v. Azadi Bachao Andolan [2003] 263 ITR 706 (SC)

However, after examining the facts regarding business operations of the Taxpayer, the AAR rejected the application at threshold on the ground of prima facie tax avoidance. But on Taxpayer's writ petition, the Delhi High Court reversed the AAR ruling. The Tax Authority appealed further to the SC.

The SC ruled in Tax Authority's favor and held that the AAR had correctly rejected the application. The SC examined the legal background of I-M Treaty, various Circulars issued from time to time, ratio of earlier SC rulings and legislative developments post such rulings like introduction of indirect transfer source rule, General Anti-Avoidance Rules (GAAR) including grandfathering provisions and its treaty override effect, statutory requirement to furnish TRC and other documents/ information as also amendments in I-M treaty expanding source taxing rights of India. On a thread bare analysis of such developments, the SC held that Circular No. 789 is statutorily superseded and, hence, TRC alone is not sufficient to avail treaty benefits. The Tax Authority is now empowered to investigate the actual residential status of taxpayers by investigating the center of their management and deny treaty benefits to residents of third countries by invoking GAAR or Judicial Anti-Avoidance Rules (JAAR).

In the facts of the present case, the SC held that the Tax Authority had proved that the transaction was prima facie an impermissible tax avoidance arrangement; it was not protected by GAAR grandfathering provision; hence, the Taxpayer was not entitled to treaty benefit and the AAR had rightly rejected the advance ruling at threshold.

Background:

- Mauritius has been a preferred jurisdiction for making investments into India and has, in terms of foreign direct investments (FDI) inflow, maintained a pole position for many years. One of the often-encountered tax issue is eligibility of Mauritius entity to claim benefits under I-M treaty primarily for exemption from capital gains tax in India.

- I-M treaty first came into force on 1 April 1982 granting, *inter alia*, exemption from source taxation in India for capital gains arising from alienation of shares of Indian companies. It was subsequently amended in 2016 vide a protocol to grant taxing right to India for such capital gains for shares acquired on or after 1 April 2017. Subsequently in March 2024, both India and Mauritius have signed a protocol to amend the I-M treaty. The protocol seeks to include a "principal purpose test (PPT)"[3] but is not yet in force.

- Owing to the importance of Mauritius as an investment jurisdiction for FDIs into India, the treaty benefit for investments emanating from Mauritius has been a subject matter of various circulars issued by the CBDT from time to time viz Circular No. 682 dated 30 March 1994, Circular No. 789 dated 13 April 2000, and Circular No. 1/2003 dated 10 February 2003 (collectively referred to as Circulars). Circular No. 682 clarified that gains derived by a resident of Mauritius by sale or transfer of Indian company shares would be taxable only in Mauritius. Circular No. 789 clarified that a TRC issued by Mauritian authorities would constitute sufficient evidence of residential status as well as beneficial ownership (BO) for applying I-M treaty benefit. It further clarified that the residential status flowing from TRC would apply even in respect of capital gains arising on transfer of shares of Indian company. It may be noted that legal validity of this Circular was upheld by the SC in landmark case of UOI vs. Azadi Bachao Andolan [4]. Further, Circular No. 1/2003 clarified that where a taxpayer is a resident (other than an individual) of both India and Mauritius in accordance with Article 4(1) of the I-M treaty, then its residence is to be determined in accordance with Article 4(3), i.e. based on its place of effective management (POEM).

- Despite the administrative circulars, the issue of whether investments from Mauritius would be eligible to treaty benefits has been a matter of debate in various decisions, notable amongst them are the SC decisions in the cases of Azadi Bachao Andolan, Vodafone[5] and others[6]. Largely the controversy in these decisions have centered around whether investment through a Mauritius entity by a third state resident would qualify for I-M treaty benefits. The Indian Tax Authority's concerns were that such entities were incorporated in Mauritius solely to take advantage of treaty benefits, raising concerns on treaty shopping, tax avoidance, and the integrity of the international tax system. Additionally, significance and impact of TRC on treaty entitlement has also been a matter of high debate.

- Even globally, the issue of improper use of treaties has been the issue of debate with a specific Base Erosion and Profit Shifting (BEPS) Action Plan 6 targeted towards preventing such use.

[3] Refer EY Alert dated 15 April 2024 on Protocol to India-Mauritius DTAA signed to include Principal Purpose Test
[4] [2003] 263 ITR 706 (SC)
[5] UOI vs. Azadi Bachao Andolan [2003] 263 ITR 706 (SC) and Vodafone International Holdings B.V. vs. UOI [2012] 341 ITR 1 (SC)
[6] Illustratively, (1) Aditya Birla Nuvo Ltd. v DDIT [(2011) 200 Taxman 437 (Bom)]; (2) E*Trade Mauritius Ltd., In Re [(2010) 324 ITR 1], the AAR; (3) D.B. Zwirn Mauritius Trading No. 2 Ltd., In Re [(2011) 240 CTR (AAR) 6]; (4) HSBC Bank (Mauritius) [TS-460-ITAT-2018(Mum)] etc.

- Above aspects are the subject matter of discussion in the AAR[7] and Delhi High Court (HC)[8] rulings in the case of Tiger Global International Holdings wherein courts examined whether gains arising to Mauritius entity from the sale of shares held in a Singapore company (deriving substantial value from assets located in India) would be chargeable to tax in India under the provisions of ITA read with the I-M tax treaty. This Alert discusses the landmark SC ruling in the above case.

- **Relevant judicial and treaty developments**

  - **Capital gains taxation as per I-M treaty:** In the context of Mauritius-based investments in India, I-M treaty originally allowed capital gains on shares of Indian companies arising to Mauritian resident to be taxed only in Mauritius. However, as Mauritius' domestic tax laws exempted capital gains from share transfers, such gains were effectively not taxed in either India or Mauritius, which led many investors to route investments through Mauritius due to significant tax arbitrage opportunity.

  - **SC decisions in cases of Azadi Bachao Andolan and Vodafone *(supra)*:**

    (a) In Azadi Bachao Andolan, the SC upheld the legal validity of Circular No. 789 and ruled that Article 13(4)[9] of the DTAA did not require the control or BO of shares to be within India or Mauritius. Circulars issued for treaty implementation would prevail over domestic law in case of inconsistency. On the issue of treaty shopping, the SC observed that developing countries often allow treaty shopping to attract foreign capital and technology.

    (b) In case of Vodafone, the SC held that in absence of specific provisions under the ITA, indirect share transfers (i.e., where shares of foreign entity derive substantial value from assets located in India) are not taxable under the ITA. The SC also held that TRCs cannot be pierced except in cases involving fraud, sham transactions, etc.

  - **Significant amendments in ITA and DTAA post Vodafone ruling**:

    (a) **Introduction of indirect transfer provisions** – Finance Act 2012 retrospectively introduced source based taxation rights in respect of gains arising from transfer of shares or interests in a foreign entity deriving substantial value from assets located in India and imposed withholding obligation in the hands of non-resident (NR) (payer) making payments to another NR (payee), if such income is chargeable to tax in India. However, replying to the debate while moving the Finance Bill 2012, the Finance Minister stated that the clarificatory amendments pertaining to indirect transfer would not override the provisions of the DTAA.

    (b) **Introduction of GAAR provisions** – Finance Act 2012 also introduced GAAR provisions codifying substance over form approach and ensuring that real intention of the parties, actual effect of transactions, and the purpose of an arrangement are taken into account for determining tax consequences. However, the implementation of the GAAR provisions was deferred from time to time and finally made effective from 1 April 2017. The treaty benefit related provisions were also specifically amended to provide that GAAR can override treaty benefits.

    (c) **Statutory requirement for TRC** – Finance Acts of 2012 and 2013 introduced amendments mandating submission of TRC and other prescribed documents and information evidencing treaty residency. Incidentally, the Explanatory Memorandum to Finance Bill 2012 stated that TRC shall be "necessary" but not a "sufficient" condition to claim treaty relief although the text of the statute did not contain the later requirement. It was proposed by Finance Bill 2013 to amend the language to state that TRC shall not be a "sufficient" condition to claim treaty relief but it was

[7] Tiger Global International II Holdings, In re [2020] 116 taxmann.com 878 (AAR - New Delhi).
[8] Tiger Global International II Holdings, W.P.(C) 6765/2020, Judgement dated 28 August 2024; [HC was also concerned with Tiger Global International III Holdings - W.P. 6764/2020 and Tiger Global International IV Holdings - W.P. 6766/2020, since the facts and issues in all the writ petitions were similar as W.P. 6765/2020, HC proceeded to evaluate the issues basis facts in W.P. 6765/2020]
[9] Article 13(4) before amendment by 2016 protocol read as "*4. Gains derived by a resident of a Contracting State from the alienation of any property other than those mentioned in paragraphs (1), (2) and (3) of this article shall be taxable only in that State.*"

dropped at enactment stage pursuant to stakeholders' concerns and restricted to requirement of furnishing additional documents and information, as may be prescribed by the Income-tax Rules[10], 1962.

- **Recommendations/guidelines from Shome Committee[11] report on implementation of GAAR (dated 30 September 2012):**

  (a) Grandfather all "investments" (but not "arrangements") made by residents or non-residents existing as on date of commencement of GAAR provisions so that GAAR provisions are not invoked on sale of such investments on or after such date for denial of tax benefit. The rationale in the report was that grandfathering a tax avoidance structure itself will grant permanent immunity. For instance, if a conduit company (say, a letter box company) is incorporated in a favorable jurisdiction in pre-GAAR period and this arrangement is grandfathered, then, all future investments made by it would also enjoy tax exemption for an indefinite future. Hence the intention should be to grandfather "investments" rather than "arrangements". This recommendation was implemented by inserting Rule 10U in the Income-tax Rules, 1962.

  Rule 10U(1)(d) provides that GAAR shall not apply to income, *inter alia*, arising from transfer of "investments" made before 1 April 2017. However, Rule 10U(2) provides that without prejudice to Rule 10U(1)(d), GAAR shall apply to any "arrangement", irrespective of the date on which it has been entered into, in respect of the tax benefit obtained from the arrangement on or after 1 April 2017. The term "arrangement" is defined in GAAR provisions to, *inter alia*, mean any transaction, operation, scheme, arrangement or understanding and includes alienation of any property in such transaction, operation, scheme, arrangement or understanding.

  (b) Restrain applying GAAR provisions where Circular No. 789 of 2000 in respect of Mauritius is applicable. Revisit Mauritius treaty if required, rather than challenging it indirectly under GAAR. However, this recommendation was not implemented.

- **I-M Treaty amendment** – Article 13 of I-M treaty was amended[12] w.e.f. 1 April 2017 to address long-pending issues of Treaty abuse, round-tripping of funds associated with DTAA and curb revenue loss, prevent double non-taxation, streamline investment flows and enhance the exchange of information between the countries. As per the said amendment:

  (a) Source state to have taxing rights on capital gains arising from transfer of shares of company resident in source state acquired on or after 1 April 2017 (Article 13(3A)).

  (b) If capital gain is derived on above referred shares (acquired on or after 1 April 2017) between 1 April 2017 and 31 March 2019, it would be taxed at concessional tax rate of 50% of the prevailing rate in source State, subject to the fulfilment of Limitation of Benefits (LOB) conditions (Article 13(3B)).

  (c) Further, Article 13(4), residuary clause for taxation of capital gains of any other property, was consequentially amended to provide the taxing rights of any other property (not captured in earlier provisions of Article 13) to resident country.

  The above amendments implied that India as a source country got taxing rights over capital gains arising to Mauritian resident from shares of Indian companies acquired on or after 1 April 2017 but such shares acquired till 31 March 2017 was treaty grandfathered and not taxable in India.

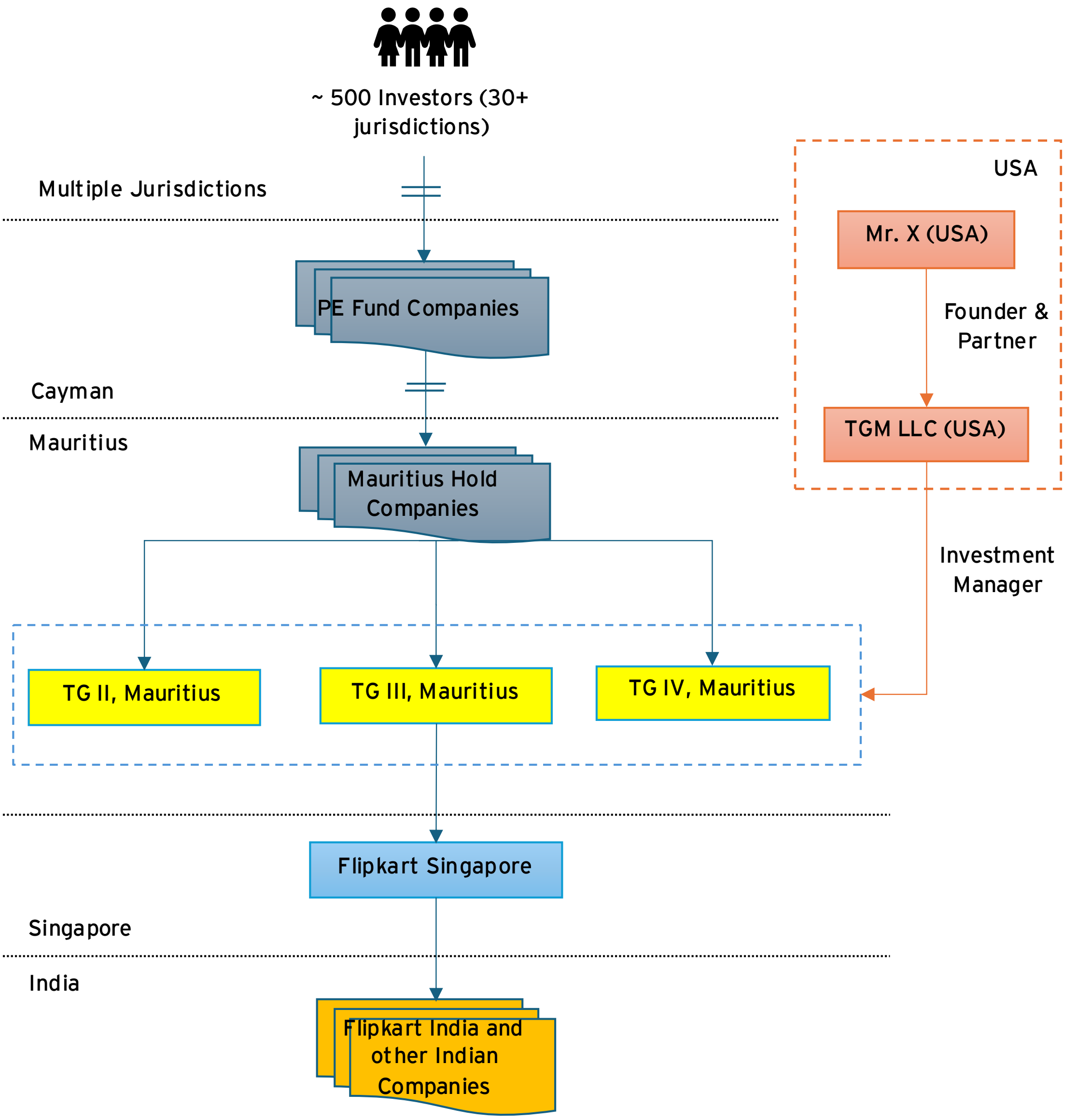
Facts of the case:

- The Taxpayer[13] was a Mauritian private limited company incorporated in year 2011. The immediate shareholders of the Taxpayer were also Mauritian Companies, which in turn were held by private equity funds organised in Cayman, which raised funds from around 500 investors residing in as many as 30 jurisdictions.

[10] Form 10F
[11] Expert Committee constituted to review and analyze GAAR provisions before its implementation.

[12] Through a Protocol signed on 10 May 2016
[13] Tiger Global International II, III, IV Holdings, Civil Appeal No. 262, 263 and 264 of 2026, Decision dated 15 January 2026

- The Taxpayer was set up with primary objective of undertaking investment activities and earning long term capital appreciation and investment income. The Taxpayer held Category 1 Global Business License (Cat. 1 GBL) in Mauritius and activities were regulated by Financial Services Commission (FSC) of Mauritius.
- The Taxpayer's Board of Directors (BOD), consisted three directors of whom two were Mauritian residents and one was a resident of the United States. They maintained their principal bank accounts and accounting records in Mauritius. Their statutory financial statements were prepared and audited in Mauritius and also held office premises in Mauritius with two employees on-board since incorporation. Further, the Taxpayer held a valid TRC issued by Mauritian tax authorities.
- Tiger Global Management LLC (TGM LLC), a US entity, was appointed as the investment manager of the Taxpayer. Services provided by TGM LLC were subject to review of Taxpayer's BoD and final approval was provided by the BOD.
- The organizational structure is diagrammatically represented below:



- During the period October 2011 to April 2015, the Taxpayer acquired shares of Flipkart Singapore (Singapore company) by way of capital contribution.

- Singapore company invested in multiple companies in India and qualifies as an entity covered by Explanation 5 to S.9(1)(i) of ITA deriving more than 50% value from assets located in India. In May 2018, the Taxpayer entered into a share purchase agreement with Walmart Inc (a third party) to sell its stake in Singapore company.

- The Taxpayer made an application to Indian Tax Authority in August 2018 to obtain a nil tax withholding certificate14. In response thereto, the Indian Tax Authority held that the Taxpayer was not eligible to avail benefit under the I-M Tax Treaty as they were not independent in their decision making and the control over the decision making of the purchase and sale of the shares did not lie with them. Accordingly, the Tax Authority issued a certificate prescribing a tax withholding rate in the range of 6-8.5% of the consideration received. The transaction was, accordingly, executed in August 2018.

- Subsequently, in February 2019, the Taxpayer preferred an application before Advance Ruling Authority (AAR) for obtaining tax ruling on taxability of the Singapore company share transfer transaction. The Taxpayer sought exemption from capital gains tax under Article 13 of I-M treaty.

- The Indian advance ruling provisions permits the AAR to reject the application at threshold if the question raised in the application, *inter alia*, relates to a transaction or issue which is designed prima facie for the avoidance of income-tax (barring certain exceptions).

- AAR[15] held as follows:

  (a) The AAR noted the Taxpayer's contention that it was entitled to benefit of Article 13(4) of I-M DTAA. The subject matter of transfer was Singapore company shares and not Indian company shares; the intent of the I-M DTAA as amended is only to protect transfer of Indian company shares.

  (b) The founder and partner of TGM LLC, an US entity, is the beneficial owner of the Taxpayer. The AAR concluded that since such individual had control over funds of the Taxpayer and was the signatory to the bank accounts of the Taxpayer, the real control of Taxpayer was lying with him (who was not based in Mauritius), while the Board of Directors (BOD) of the Taxpayer in Mauritius were merely puppets. Further, the Taxpayer made no investments other than in Singapore company. In absence of any strategic FDI in India, there was neither any business operation in India nor any taxable revenue generated by the Taxpayer. Prima facie, the Taxpayer was a conduit/ see-through entity set up for tax avoidance by availing the benefits under I- M treaty. Hence AAR rejected the advance ruling application made by the Taxpayer at threshold.

- Being aggrieved, the Taxpayer filed a writ petition before Delhi HC challenging the AAR ruling. The HC held that Taxpayers were entitled to treaty benefits and the capital gains income would not be chargeable to tax in India as it is duly grandfathered under Article 13(3A) of the DTAA.

  Considering the holistic facts of the case, the HC concluded that the Taxpayer had sufficient economic substance in Mauritius, and its BoD was not merely a puppet or subservient to the wishes of its parent company, rather it had competence and independent autonomy over the decision-making process. The HC noted various facts evidencing the BoD making deliberative and collective decisions. Recognizing the advantages of choosing Mauritius as a preferred investment destination, the HC noted that routing investments through Mauritius cannot by itself lead to an adverse inference.

  Further, presence of TRC as well as the satisfaction of LOB test provide sufficient evidence of legitimate tax residency, BO and treaty eligibility. Further, it was held that GAAR provisions cannot override or dilute the treaty protection.

- The HC noted that both Taxpayer and Tax Authority conceded that Article 13(3A) was of critical importance for the purposes of adjudging whether the transaction stood grandfathered and placed in safe harbor vis-à-vis application of GAAR. The HC held that AAR's interpretation of I-M treaty not intending to protect capital gains arising from Singapore company shares deriving substantial value from assets in India was incorrect. Article 13(3A) of the I-M treaty clearly embodies intent of both countries to safeguard and provide safe passage to all transactions which had consummated prior to 1 April 2017 considering that India had introduced provisions for taxing indirect transfers.

- Aggrieved by the HC order, Revenue filed an appeal before the SC.

[14] Section 197 read with Section 195 of ITA

[15] Refer EY Tax Alert titled as "AAR rules that investment of a Mauritius company in a Singapore company deriving substantial value from assets in India is prima facie designed for avoidance of tax not eligible for treaty benefits and rejects the application filed by Mauritius company", dated 5 June 2020

- On 24 January 2025, the SC stayed the order of HC from its operation, implementation and execution. Subsequently, the SC also stayed the assessment proceedings initiated against the Taxpayer, by order dated 4 February 2025, with a view to protect the interest of the revenue and obviate the difficulty of the notices getting time barred. Thereafter, the appeals before SC were taken up for hearing by 2 judge bench (Division bench).

Issue for consideration framed by SC:

Whether AAR was right in rejecting the application for Advance Ruling on the ground of maintainability, by prima facie treating the capital gains arising out of a transaction of sale of shares of a Singapore Company which holds the shares of an Indian company, by a Mauritian company controlled by a US company, to be prima facie a tax avoidance arrangement, and hence, whether it can be inquired into to ascertain whether such capital gains is taxable in India under ITA read with the relevant provisions of the I-M Treaty?

SC ruling:

Basis reasoning elaborated in ensuing paragraphs, the SC reversed the Delhi HC ruling and ruled in favor of Tax Authority as follows in the main judgement authored by Justice R. Mahadevan:

- Once it is factually found that the subject sale of shares of Singapore company giving rise to capital gains were transferred pursuant to an impermissible avoidance arrangement as per GAAR under Indian domestic tax law, the Taxpayer is not entitled to claim treaty exemption under Article 13(4).

- The Tax Authority has proved that the transaction in the instant case are prima facie impermissible tax-avoidance arrangements attracting GAAR.

- The AAR rightly rejected the application under the bar for transaction designed prima facie for tax avoidance.

- Accordingly, capital gains arising from transfer effected on or after 1 April 2017 are taxable in India read with applicable provisions of the treaty.

  <u>**Legal Background:**</u>

  - The SC elaborately traced the history and evolution of the I-M DTAA, various Circulars including Circular No. 789, SC rulings in Azadi Bachao Andolan and Vodafone *(supra)* followed by following developments:

    - Introduction of indirect transfer source rule in ITA

    - Introduction of GAAR in ITA which can override treaty benefit along with grandfathering rule for "investments" made before 1 April 2017

    - Mandatory TRC and stricter documentation requirements for claiming treaty benefits

    - Amendment of I-M treaty to grant source taxing rights to India on capital gains arising from shares of Indian companies acquired on or after 1 April 2017

<u>**Applicability of Article 13 of India-Mauritius (I-M) Treaty:**</u>

- Article 13 of the DTAA lays down detailed rules with regard to taxation of capital gains.

- Article 13(2) covers cases of gains arising from sale of movable property forming part of permanent establishment (PE) or fixed base of Mauritian resident company in India and gives source taxing right to India. It applies to such movable property directly owned by Mauritian company in India. The present transaction does not fall within this para.

- Article 13(3A), inserted in 2016, applies to sale of shares of company resident in India acquired on or after 1 April 2017 and provides for taxation in India. This applies to shares directly held and sold by Mauritian entity.

- Under Article 13(4), all transactions not covered by earlier paras are taxable in state of residence.

- On a combined reading, it becomes clear that for claiming benefit of Article 13(4), the person seeking to avail treaty protection must, not only qualify as a "resident" of the other state i.e., Mauritius, but also establish that movable property or shares forming subject matter of the transaction are directly held by such resident entity. In all other cases, the transaction is taxable in India where the capital gains arise out of the disposition of movable property, including movable property forming part of the business property held by a PE in India. Thus, an indirect sale of shares would not, at the threshold, fall within the treaty protection contemplated by Article 13 (Para 18 of SC ruling).

Object and purpose of treaty:

- The object of treaty is to prevent double taxation and not to facilitate avoidance or evasion of tax. Therefore, for the treaty to be applicable, the taxpayer must prove that the transaction is taxable in its state of residence. The subsequent amendments to treaty were introduced to prevent abuse. Hence a taxpayer has to establish that it is a resident of a Contracting State covered by DTAA by producing all relevant documents

- Considering the object and purpose of treaty, it must be read harmoniously with other provisions of ITA including charging provisions which levy tax on global income of residents. Treaties are entered to resolve anomalies of double or multiple taxation in multiple jurisdictions due to adoption of one or more connect factors for taxing income like situs of transaction, source of income, residence of taxable entity, maintenance of PE and so on. The power to enter into treaties is an incident of sovereign authority of the state.

- Different countries have varying procedures for implementing treaty obligations. In India, Central Government is authorized to enter into treaties and make provisions for implementing it through notification in Official Gazette.

- Treaties are entered not only for avoiding double taxation but also for exchange of information for prevention of evasion or avoidance of taxes on income, for investigation of cases involving tax evasion or avoidance, or for recovery of taxes in foreign countries in a reciprocal basis.

Impact on CBDT circulars on TRC post statutory amendments:

- In general, Circulars issued by CBDT in exercise of power granted by ITA are binding on the Tax Authority even when they depart from the correct statutory interpretation [16]. However, such Circulars operate only within the legal regime in which they were issued and cannot override subsequent statutory amendments. It is equally settled law that Parliament is well within its right to bring in a law, either by amendment, substitution, or introduction so as to remove the basis of a judicial decision.

- After the amendments to ITA subsequent to Vodafone decision like indirect transfer source rule, GAAR, Rule 10U and treaty changes, TRC alone is not sufficient to avail the benefits under the DTAA, and reliance upon earlier SC rulings[17] dealing with Circulars issued in the pre-amendment regime cannot be relied upon. Rather, the facts which need to be independently analyzed are the facts to decide on the applicability of GAAR provisions under the ITA.

- Thus, the relevant steps are (i) examine whether transaction falls within source rule of ITA (including indirect transfer) (ii) whether such taxability is curtailed or overridden by DTAA,

- For the second step regarding DTAA applicability, it is necessary to examine (a) whether taxpayer is "resident" of Mauritius as per Article 4(1) (b) whether the transaction falls under Articles 13(3A), 13(3B) or residuary rule of 13(4) and (c) whether LOB under Article 27A applies to deny treaty protection.

- Basis the amendments referred earlier, Indian Tax Authority is now empowered to investigate the actual residential status of taxpayers by investigating the center of their management and thereafter apply the charging provisions of the ITA. Further, amendments to the ITA, the Rules, and the treaty terms which have enabled strict scrutiny cannot be ignored and tax relief cannot be ipso facto granted. In the present case, the Tax Authority was seeking to examine whether the taxpayers were in fact residents of third country on the basis of alleged control and management being exercised from that country. The treaty residence is to be construed as per connect factors provided in the treaty like domicile, residence, place of management, or any other criterion of a similar nature.

- While Article 13(4) provides exclusive taxing right to Mauritius, the term of "resident" of Mauritius has to be construed as per Article 4 of the I-M treaty. If person other than individual is found to be resident of both Contracting States, the treaty benefit

[16]K.P. Varghese v. Income-Tax Officer, Ernakulam (AIR 1981 SC 1922). Similar view was held by SC in the case of Anjum M.H. Ghaswala and Others (2001 INSC 519)

[17] Union of India v Azadi Bachao Andolan (2004) 10 SCC 1; Vodafone International Holdings BV v. Union of India (2012) (6 SCC 613).

cannot be availed. The benefit of exemption available to a resident by virtue of the treaty is not available if the transaction is taxable in the source state.

Limited evidentiary value of TRC:

- The ITA makes TRC only an "eligibility" requirement and not "sufficient" evidence of residency which is a higher threshold. Thus, TRC cannot by itself prevent an enquiry, if it is established that the interposed entity was a device to avoid tax.

- TRC is not binding on any statutory authority or court unless its contents are independently examined by the authority or Courts.

- In the present case, TRCs relied upon by the Taxpayer is non-decisive, ambiguous and ambulatory, merely recording futuristic assertions without any independent verification. Thus, the TRC lacks the qualities of a binding order issued by an authority.

- Treaty related amendments in the present case through Protocol entered in 2016 resulting in change in rules of source taxation, LOB conditions, sharing of information, etc. make it clear that merely holding of TRC cannot, by itself, prevent an enquiry subsequent to such amendments like GAAR, if it is established that the interposed entity was a device to avoid tax. The SC reiterated that Circulars, having since been superseded by statutory amendments, will not come to the aid of the taxpayers.

SC's observation on AAR ruling:

- Given the settled anti-avoidance principles, Parliament has statutorily empowered the AAR to reject applications at the threshold where the transaction appears prima facie tax-avoidant.

- In the present case, the AAR rejected the Taxpayer's applications mainly on two grounds, i.e. (i) prima facie the transaction was for tax avoidance and (ii) shares sold were those of Singapore company and not of an Indian company, and any exemption in respect of shares of the company not resident in India was not intended by the Legislature.

- The AAR concluded that the Taxpayer's effective control and management was not in Mauritius but in USA having regard to method of bank account operation. Having so concluded, the AAR's inquiry whether the shares were of Indian company pale into insignificance. Once taxability was established under indirect transfer rule, rejection of exemption only on the ground that sale of shares was not of Indian company may be an enquiry in the wrong direction. But validity of rejection has to be tested on "prima facie" tax avoidance criteria.

- For AAR to be able to reject the Taxpayer's application, it is sufficient if on "prima facie" examination of the documents it is satisfied that the transaction is for avoidance of income tax.

- The level of satisfaction required to arrive at a prima facie conclusion is much less when compared to a case where a fact has to be proved. "Prima facie" does not mean proving to the hilt but a case which can be said to be established if the evidence which is led in support of the same is accepted18.

- All that is required for the AAR, in the case of an application by a NR, is to see whether the contents of the application and the documents disclose a transaction by which an attempt is made to avoid payment of tax, if it is otherwise taxable under law. The language of the provision has to be read in tandem with the object of the respective provisions of the ITA and the Rules as applicable to the facts of the case.

- The Delhi HC was not right in observing that merely because the taxpayers have been in existence from 2011 onwards, the presumption of tax avoidance cannot be made by relying upon an SC ruling rendered prior to statutory amendments by which the mere existence of TRC is insufficient to establish the resident status of applicant in the other State.

- The SC emphasized that a TRC has only limited evidentiary value in proceedings for advance ruling, considering that after legislative amendments the earlier circulars and

[18] Reliance placed on SC rulings in the case of Balvir Singh v State of Uttarakhand (AIR 2023 SC 5551) and Martin Burn Ltd v. R. N. Banerjee (AIR 1958 SC 79)

pre-amendment case laws [19] cannot override the current legal position.

- Every nation has a sovereign right to tax based on internationally recognized residence and source principles. The judgements relied upon by the Taxpayer in the present case rendered prior to TRC related amendment, the SC had not totally shut out the Revenue's case when it comes to a fraudulent or fictitious transaction. Each case has to be evaluated on its own facts.

Applicability of GAAR and JAAR:

- It is undisputed that the transaction in the present case has been undertaken post 1 April 2017. While investment in shares was made before 1 April 2017, but the proposal for sale of investments commenced in 2018 through discussions with various parties to the agreement, board resolutions etc, i.e. after the cut-off date of 1 April 2017.

- The provisions of GAAR are applicable in the present case which empowers the revenue to declare the subject transaction to be an impermissible arrangement [20]. Further, exemptions or concessions provided under GAAR provisions are available only to genuine entities resident in the Contracting State with commercial interest and without tax avoidance as their main object in order to prevent treaty abuse.

- Rule 10U grants GAAR grandfathering for "investments" made before 1 April 2017 but not for "arrangement" entered prior to that date. For this purpose, the duration of such "arrangement" is irrelevant.

- Further, even if GAAR is held to be inapplicable, SC agreed with revenue's contention, JAAR grounded on "substance over form" principle could be invoked to deny treaty benefits in cases involving treaty abuse or conduit structures consistently recognized in Indian jurisprudence, including the cases of McDowell & Company Ltd v Commercial Tax Officer[21] and Vodafone *(supra)*. The SC accepted the Tax Authority's contentions that JAAR continues to operate in parallel with GAAR and empowers Indian Tax Authority to deny treaty benefits in cases involving treaty abuse or conduit structures. The Taxpayer in the present case did not dispute this proposition by furnishing detailed documentation regarding control and management, thereby conceding that mere possession of TRC is not sufficient. In the present case, the taxability under domestic source rule was established, treaty relief was contested by Tax Authority by challenging the residency claim in view of prima facie finding that effective management and control was not in Mauritius, the scope of Article 13, Circular No. 789 and Azadi Bachao Andolan in current factual context, GAAR and in the alternative JAAR are invoked to pierce the structure and deny treaty benefits where the transaction lacks genuine commercial interest.

- The SC decision in Vodafone ruling (*supra*) supports that commercial intent of a transaction is a strong indicator of whether a transaction is genuine or merely an artificial device. The fact that the Taxpayer claimed tax exemption both in India and Mauritius is contrary to the spirit of the DTAA and strongly supports the Tax Authority's case that the arrangement is impermissible.

- The GAAR provisions shifts the burden onto the taxpayer to disprove the presumption of tax avoidance. In the present case, there is a clear and convincing prima facie evidence to demonstrate that the arrangement was designed with sole intent of evading tax and the Taxpayer failed to furnish sufficient material to rebut this presumption.

- It is lawful for the taxpayer to structure transactions to avoid or reduce the burden of tax, however the mechanism must be legitimate and compliant with the provisions of the Act, rules, and notifications. If the structure is found to be sham or illegal, it ceases to be "permissible avoidance" and becomes "impermissible avoidance" or evasion. Thus, the Tax Authority is entitled to examine the transaction and verify whether the claim made by the Taxpayer is lawful or not.

[19] Union of India v Azadi Bachao Andolan (2004) 10 SCC 1, Vodafone International Holdings BV v. Union of India (2012) (6 SCC 613).

[20] An arrangement, the main purpose of which is to obtain a tax benefit, and which, *inter alia*, is entered into or carried out by means or in a manner which is not ordinarily employed for bona fide purposes

[21] (1985) 3 SCC 230

Additional observations by Justice J.B. Pardiwala:

Justice J.B. Pardiwala fully concurred with the judgment authored by Justice R. Mahadevan and in addition thereto provided below key observations in the context of tax sovereignty and safeguards to be borne in mind while entering into tax treaties.

- On tax sovereignty:
    - A nation's strength comes from its ability to make independent decisions, especially regarding tax matters, for the benefit of its citizens. While countries have the right to exercise sovereignty within their borders and internationally, global politics often require negotiation and compromise. Historically, developing nations like India had to concede some sovereign rights to more powerful countries. However, India has now emerged as a respected global economic force, driven by its demographic advantages.
    - In today's world, marked by political uncertainty and trade disputes, it is crucial for India to uphold its tax sovereignty and maintain control over taxing rights on domestic profits. While international treaties offer benefits such as stability and consistency, India should periodically review these agreements to ensure they serve national interests. Outdated treaties should not restrict India, especially when addressing cross-border issues like tax evasion and illicit financial flows. Ultimately, India must prioritize its people's welfare by making independent choices in treaty negotiations.
- Following safeguards may be undertaken by India while entering into international treaties:
    - Include **LOB clause** to prevent treaty shopping (e.g. amended India-Mauritius DTAA)
    - Explicitly allow **GAAR to override treaty in case** of tax avoidant and artificial transactions
    - Ensure **right to tax digital economy** by recognizing significant economic presence (SEP), equalization levy, digital services tax provisions
    - Preserve **source-based taxation rights**[22] and avoid residence-based taxation models favoring tax havens and developed countries
    - **Inclusion of tax credit mechanism** and not exemption mechanism to avoid double non taxation.
    - **Include 'Exit or Renegotiation Clause'** if treaty is misused, diverges from India's economic goals (e.g. India's renegotiation with Mauritius, Cyprus, Singapore)
    - **Avoid Most Favoured Nation (MFN)** clause as it may undermine India's flexibility in future negotiations.
    - Ensure **clear, broad and updated Permanent Establishment (PE) definition** to prevent avoidance through commissionaire arrangements and fragmentation of business activities
    - Align treaty provisions with **India's domestic laws and constitution**
    - Conduct **Cost-Benefit Analysis** in terms of India's revenue loss, impact on domestic industry, long-term strategic impact etc. before signing a tax treaty
    - **Build treaty monitoring and review mechanism** to review treaty abuse, relevance and changing business and legal trends
    - **Consult stakeholders**[23] before signing to ensure treaties reflect broader economic and public interest, not just bureaucratic or diplomatic goals.

[22] Especially for capital gains, interest, royalties, technical fees, business profits

[23] Namely tax experts, legal professionals, industry bodies, parliament committees

Comments

Over the past two decades, treaty eligibility under the India-Mauritius tax treaty has been among the most contentious and litigated issues in Indian international tax jurisprudence. The interplay between form and substance, the evidentiary value of TRC, and the role of anti-avoidance doctrines have been shaped by a series of judicial pronouncements, legislative amendments, and administrative circulars, reflecting the evolving approach of Courts and the Indian tax administration of balancing investor certainty with the protection of India's taxing rights.

Against this backdrop, the Supreme Court's ruling in the Tiger Global case may transform India's approach to tax treaty eligibility and taxation of cross-border transactions, especially those investing through jurisdictions that provide treaty benefits.

The SC has effectively recast the TRC from being near-conclusive to merely prima facie. Further, SC's remark that the TRC in present case was "futuristic" underscores a clear shift away from reliance on formal documentation towards a deeper inquiry into where real control, management and decision-making lie. The decision also appears to dilute the long-standing principles laid down by the SC in Azadi Bachao Andolan, particularly in light of subsequent amendments to both domestic law and the DTAA framework post that ruling.

It is important to highlight that the Protocol incorporating the Principal Purpose Test (PPT) clause into the India-Mauritius DTAA has not yet come into effect. Once the PPT becomes operative under the treaty, scrutiny of treaty benefits is likely to become even more rigorous. Notably Circular 1/2025, clarifies investments that have been grandfathered will remain outside the purview of the PPT and PPT in general will apply only prospectively.

The validity of TRC and the limits of GAAR grandfathering are likely to be evaluated in light of SC ruling by field officers including in various ongoing assessments and by appellate authorities to appeals at various stages. It also raises questions on whether past assessments may be reopened through rectification, revision or reassessment. The mode in which SC ruling may be applied whether by invoking GAAR or JAAR may also need to be seen (including in the present case). This is because GAAR applies only from 1 April 2017 onwards and requires reference to GAAR approval panel. It may be good for the Government to clarify its stand as early as possible to provide clarity and remove uncertainty for the stakeholders.

Furthermore, the observations of SC on application of Article 13 to indirect transfers has raised some ambiguity. It may be recollected that the Finance Minister had clarified in 2012 while introducing indirect transfer source rule that it would not override the treaties. The Tax Authority's arguments before the SC also acknowledged that indirect transfers are covered by residuary Article 13(4). It would be prudent for the Government to reaffirm the clarification issued in 2012, stating that indirect transfers are not subject to tax under tax treaties, provided treaty eligibility is established in line with the current Supreme Court judgment.

At a broader level, the judgment could impact a significant number of investment structures that rely on tax treaty benefits, particularly as GAAR grandfathering is no longer a blanket shield. Further, even if GAAR is held to be inapplicable, Tax Authority may invoke JAAR to pierce the structure and potentially deny treaty benefits. Multinational groups might therefore need to reassess their holding and transaction structures where treaty benefits have been availed. Arrangements grounded in demonstrable commercial substance, rather than primarily in treaty benefits, are more likely to withstand sustained scrutiny over time.

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ED None.