* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 8th October, 2012.
% **Date of Decision**: 12th December, 2012.

\+ **WP(C) No.6468/2010**

CONVERGYS CUSTOMER MANAGEMENT .... Appellant
Through Ms. S. Ganesh, Sr. Adv. with Mr. Anand Sukumar and Mr. Bhupesh Kumar Pathak, Advs.

VERSUS

ASSISTANT DIRECTOR OF INCOME TAX & ANR. ..Respondents
Through Mr. Sanjeev Sabharwal, sr. standing counsel with Mr. Puneet Gupta and Ms. Gayatri Verma, Advs.

CORAM:
MR. JUSTICE S. RAVINDRA BHAT
MR. JUSTICE R.V. EASWAR

R.V. EASWAR, J.:

This petition under Article 226/227 has been filed in the following circumstances. The petitioner is a company incorporated in USA. It is engaged in the business of providing business process outsourcing services to its clients located worldwide. It has a subsidiary in India which is known as Convergys India Services Pvt. Ltd. (hereinafter referred to as "CISPL"). CISPL renders back office services exclusively to the petitioner-company.

2. In respect of the assessment years 2002-03 and 2004-05, notices for reopening the assessments were issued by the first respondent on 30.3.2007.

There were three broad grounds upon which the assessments were sought to be reopened. The first was that the financial statements of CISPL, the subsidiary company of the petitioner, showed that the petitioner received certain payments which in substance represented "fees for technical services" within the meaning of Section 9(1)(vii) of the Income Tax Act, 1961 ('Act', for short) paid in the guise of reimbursement of salary of its employees rendering services to CISPL. It was the view of the first respondent that these payments made to the petitioner by its subsidiary were taxable in the hands of the petitioner. The second reason given in the reasons recorded was that the petitioner had advanced an interest-free loan to CISPL, which was not at arm's length because on the loan taken by the petitioner from City Bank, NA, the bank was charging interest from the petitioner. According to the first respondent no interest was charged by the petitioner from CISPL only because they were associated enterprises. The interest was chargeable under Section 9(1)(b) of the Act as well as under Article 11 of the Agreement for the Avoidance of Double Taxation entered into between India and USA. The third and last reason was that the petitioner had a "business connection" in India within the meaning of Section 9(1)(i) of the Act. Not only was there a business connection because of CISPL, but CISPL was also the petitioner's "permanent establishment" in India within the meaning of Article 5 of the Double Tax Treaty.

3. On the basis of the aforesaid three reasons, the first respondent sought to reopen the assessments. The petitioner challenged the notices in WP(C) No.2991/2007 before this Court and by order dated 23.11.2009, this Court directed the petitioner to file returns and simultaneously ask for the reasons for issuance of the reassessment notices upon which the assessing officer would

grant an opportunity to the petitioner of being heard; the petitioner was permitted to file objections to the reopening of the assessments, which were directed to be decided by a speaking order including the preliminary issue of jurisdiction. The writ petition was disposed of in these terms.

4. The petitioner thereafter filed detailed objections to the notices issued under Section 148 raising various contentions, the summary of which is this:

a) the petitioner was not liable to file any returns of income in India since no income accrued or arose to it in India under the Act read with the Indo-US Tax Treaty. The first respondent therefore did not have any jurisdiction to issue the notices to the petitioner;

b) CISPL had withheld the applicable taxes on the interest income and therefore the petitioner had no obligation to file returns in India;

c) the transfer pricing officer, in the course of the assessment made on CISPL had examined the international transactions between the petitioner and CISPL and after due examination the arm's length price stood accepted, pursuant to the orders of the CIT(Appeals) for both the years. In any case, even if any addition is to be made, it can be made only in the hands of the CISPL and not in the hands of the petitioner; and

d) there was no reason to believe that income chargeable to tax had escaped assessment nor was there any tangible material on the basis of which the reopening notices could be issued.

5. The objections were considered and disposed of by the first respondent by order passed on 07.09.2010. In these orders the first respondent rejected all the objections of the petitioner and directed it to participate in the reassessment

proceedings and submit the details/information called for by the notices issued by him.

6. It is against the notices issued under Section 148 of the Act on 30.03.2007 and the orders passed on 07.09.2010 disposing of the petitioner's objections that the petitioner has filed the present petition seeking quashing of the notices and the orders for both the years.

7. The main arguments put forward on behalf of petitioner are that (a) there is no nexus between the materials which were present before the assessing officer (the first respondent herein) and his belief that income chargeable to tax had escaped assessment; (b) no case has been made out in the reasons recorded to show escapement of income chargeable to tax; (c) no dealings between the petitioner and CISPL have been pointed out in the reasons recorded nor was there anything to justify the finding of business connection. With reference to the fees for technical services, it was submitted that just because one employee was seconded by the petitioner to CISPL and was paid salary by CISPL it cannot be assumed, without anything more, that the salary paid to that employee represented fees for technical services in the hands of the petitioner and in support of this submission a copy of the circular No.5 issued by the CBDT on 28.9.2004 was relied upon. With regard to the interest it was submitted that in the assessment year 2002-03, there was no loan given by the petitioner to CISPL and therefore there was no question of charging any interest and that in the assessment year 2004-05 the loan was not given interest-free but interest was charged. As regards the existence of business connection it was contended that there was no material brought out in the reasons recorded to

sustain even a prima facie the belief that there was a business connection within the meaning of Section 9(1)(i). It was contended that even proceeding on the basis that CISPL was a permanent establishment of the petitioner in India, the reopening notices cannot be justified because there was no income attributable to the PE.

9. These contentions were resisted by the revenue and the learned standing counsel submitted that the petitioner did not even file returns of income which default *per se* attracted the provisions of Section 147 read with Explanation 2(a), that at the stage of recording reasons on the basis of the materials available before the assessing officer he is expected to only reach a prima facie belief of the escapement of income, that there were materials before the assessing officer to show that there was another subsidiary of the petitioner in Hyderabad, India, which was not subjected to transfer pricing study and thus there was failure on the part of the petitioner to disclose the source of income in India and all these constituted relevant material for reopening the assessments on the ground of escapement of income. Reliance was placed on the judgment of this Court in ***Reach Cable Networks Ltd. Vs. Deputy Director of Income Tax*** (2008) 299 ITR 316. It was accordingly contended that the notices issued under Section 148 were valid and the first respondent was justified in rejecting the objections of the petitioner.

10. On a careful consideration of the matter we are of the opinion that there is no merit in the petition. It is a well settled proposition that at the time of issuance of the notices under Section 148, the Assessing Officer is not expected to form any definite or conclusive opinion about the taxability of the disputed

amounts and that he is only expected to form a tentative or prima facie belief regarding the escapement of income chargeable to tax. The mere failure to file the return of income (though liable to) would invite action to reopen the assessment on the ground of escapement of income and this has been provided in Explanation 2(a) below Section 147. It is also well-settled that there should be material before the assessing officer which should afford a live link or nexus with the formation of the belief regarding escapement of income; the material should not be mere hearsay, gossip or rumour.

11. The reasons recorded by the first respondent have to be scrutinized by the application of the aforesaid tests.

12. The first respondent has brought out in the reasons recorded, that at least prima facie there is a case for the application of Section 9(1)(i) of the Act on the footing that the petitioner had a business connection in India. CISPL is admittedly a subsidiary of the petitioner in India and it renders services exclusively to the petitioner. This prima facie indicates that there is business connection. The role of the subsidiary is to provide customer management services in fulfillment of contracts negotiated by the petitioner for its US based clients. The Assessing Officer further observed in the reasons recorded that when the core business of the petitioner is business process outsourcing and the core business itself was outsourced to CISPL, there is prima facie material to hold that CISPL is a fixed place of business which is at the disposal of the petitioner. This would also mean that apart from the prima facie existence of a business connection there is also material to entertain the belief that CISPL is a permanent establishment of the petitioner in India. It has been held in

Commissioner of Income Tax, Punjab Vs. R D Aggarwal and Co. and Anr. (1964) 56 ITR 20 as under :

> *"The expression "business" is defined in the Act as any trade, commerce, manufacture or any adventure or concern in the nature of trade, commerce or manufacture, but the Act contains no definition of the expression "business connection" and its precise connotation is vague and indefinite. The expression "business connection" undoubtedly means something more than 'business". A business connection in section 42 involves a relation between a business carried on by a non-resident which yields profits or gains and some activity in the taxable territories which contributes directly or indirectly to the earning of those profits or gains. It predicates an element of continuity between the business of the non-resident and the activity in the taxable territories: a stray or isolated transaction is normally not to be regarded as a business connection. Business connection may take several forms : it may include carrying on a part of the main business or activity incidental to the main business of the non-resident through an agent, or it may merely be a relation between the business of the non-resident and the activity in the taxable territories, which facilitates or assists the carrying on of that business. In each case the question whether there is a business connection from or through which income, profits or gains arise or accrue to a non-resident must be determined upon the facts and circumstances of the case."*

In the light of the above observations, where the existence of a business connection was held to depend on the facts of each case, we are of the view that there was prima facie material in the possession of the Assessing Officer to form a tentative belief that Section 9(1)(i) was attracted. This reason by itself constituted a relevant ground to reopen the petitioner's assessments.

13. On the question of the existence of a permanent establishment, it was made clear on behalf of the petitioner in the course of the arguments that the

argument against the notices would proceed on the basis that the petitioner had a PE in India. If that much is admitted, the tax implications of having a PE in India both under the Act and under the Double Tax Avoidance Agreement would fall to be examined. The assessing officer was therefore justified in taking the prima facie view that CISPL constituted the petitioner's permanent establishment in India.

14. So far as the assessability of the interest under Section 9(1)(v) is concerned it would appear that clause (b) of Section 9(1)(v) is applicable. Under this clause income by way of interest payable by a resident is taxable in the hands of the non-resident, except under specific circumstances, as for example, where the interest was payable in respect of the monies borrowed and used for the purpose of a business carried on by the resident outside India. Prima facie the Section can said to be attracted, at least for the assessment year 2004-05, for which year admittedly the petitioner had charged interest on the loan advanced to CISPL.

15. As far as fees for technical services are concerned, we do not find any material in the reasons recorded to show that the salary paid to the employees seconded by the petitioner to CISPL and who were rendering services, represented fees for technical services paid in the guise of salary. The conclusion to the contrary found in the reasons recorded seems to us to be based on conjecture.

16. In the course of the submissions, it was submitted on behalf of the petitioner that for the two assessment years under consideration before us, the transfer pricing officer, in the course of the assessments of CISPL had gone into

the question of arm's length price in detail and for the assessment year 2002-03 had accepted the price declared by CISPL and has not made any adjustments; for the assessment year 2004-05 he made an adjustment of ₹27.58 crores. The addition made for the assessment year 2004-05 was deleted by the CIT(Appeals) but an appeal to the Tribunal is pending at the instance of the revenue. These facts have no relevance to the present petition since there is no reference to the assessments of CISPL in the reasons recorded. If anything, these facts may impinge on the merits or additions, if any, proposed to be made in the reassessments. It is neither necessary nor proper for us to comment upon those facts or their impact on the reassessment of the petitioner.

17. for the above reasons we see no merit in the writ petition which is dismissed. All interim orders stand vacated. The petitioner shall pay the cost of the revenue which we assess at ₹75,000/-

We clarify that we have not expressed any opinion on the merits of the petitioner's objections.

(R.V. EASWAR)
JUDGE

(S. RAVINDRA BHAT)
JUDGE

DECEMBER 12, 2012
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