

Authority for Advance Rulings: Still Not Advanced Enough!

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The Hon'ble Authority for Advance Ruling (“**AAR**”) in Notice No. F. No./105/AAR/1999(PT)/21 dated April 12, 2017 has stated that in view of the directions given by the Hon'ble Authority, the cases listed before the Hon'ble Authority are hereby adjourned until further orders. Future dates in the cases will be intimated in due course. The above order was passed by the AAR due to the adjournments that revenue department was seeking in all matters pursuant to recent development in relation to an approval for appointment of a Vice-Chairman of the AAR. This has resulted in, yet again, stalling the work of the AAR and making it effectively non-existent.

BACKGROUND

The AAR is a Tax Tribunal constituted under the Income Tax Act, 1961 (“**ITA**”) which has been set up to decide the taxability of non-resident / foreign companies in India in relation to a transaction which the non-resident / foreign company proposes to carry out or for a transaction which has been completed. Notably, the AAR has gained significant importance with the number of applications made to it for obtaining tax certainty on transactions.

Under the ITA, a bench^[1] of the AAR shall consist of the Chairman (who has to be a retired Judge of the Supreme Court of India) or a Vice-Chairman (who has been a High Court judge) and one Revenue Member (who is a high ranking officer from the Indian Revenue Service) and a law member (a high ranking officer from the Indian Legal Service). The Advance Ruling (Procedure) Rules, 1996^[2] provide that a hearing can take place by a Bench consisting of at least two members, one of whom is the Chairman. Further, in case no other member is available, the Bench will consist of only the Chairman who will carry out the function of the AAR.

As stated above, the Chairman of the AAR needs to be a retired judge of the Supreme Court of India. The AAR in the recent past has gone through considerable amount of turmoil as the Government has always been delayed in appointing a Chairman. Further, with every Chairman retiring from the AAR, there have been times where the AAR has not functioned at all for months – again due to non-appointment by the Government of a Chairman. It should be noted that under the ITA, the AAR is bound to pronounce its ruling within 6 months from the date of receipt of the application. However, considering the current situation, it may be safely assumed that one can expect a ruling not before at least 18 - 24 months after filing the application.

JUDGMENT OF THE PATNA HIGH COURT

Considering the above situation, a writ petition in the form of a Public Interest Litigation was filed by Mr. Rajeev Kumar in the High Court of Patna^[3]. The petitioner challenged the *vires* of Section 245-O (2) of the ITA as well as Rule 27 of the Advance Rulings (Procedure) Rules, 1996.

Section 245O(2) of the ITA provides that “*The Authority shall consist of a Chairman and such number of Vice-Chairman, revenue Members and law Members as the Central government may, by notification, appoint.*” Rule 27, as discussed above, permits a decision to be taken only by Chairman or by only two Members, if one of them is a Chairman.

The petitioner grieved that since the post of Chairman and Vice Chairman are vacant, the AAR has become non-functional and, as a result thereof, Rule 27 would be rendered unconstitutional unless it is read down by applying the “doctrine of necessity” by the respondent - Union of India. The High Court ruled the following:

- The AAR forms an integral part of the administration of justice and cannot be allowed to remain effectively non-existent for a long time;
- The respondent - Union of India needs to consider the grievance expressed and need to decide if the AAR and/or the qualifications prescribed for Chairman need any change. The Court provided the Union of India a time of 8 weeks to take appropriate measures in this regard.
- As an interim measure, that until a decision is taken on the issues raised by the Union of India, and till a new Chairman is appointed, all the pending cases before the AAR shall be dealt with by the Judicial Member, at the Principal Bench, who shall carry out the functions of the AAR as its in-charge Chairman, so that the functioning of the Authority does not remain completely stopped.

FINANCE ACT, 2017

Pursuant to the judgment of the Patna High Court, the Finance Act, 2017 made amends to the provisions of the ITA which deal with the AAR. The amendments, *inter alia*, include:

(i) The Chairman of the AAR can be either a retired judge of the Supreme Court or the Chief Justice of a High Court or a judge of a High Court who has been a judge of a High Court for atleast 7 years.

(ii) If the Chairman is unable to discharge his functions owing to absence, illness, etc. or if his office is vacant, the Vice-chairman will discharge the functions of the Chairman of AAR.

The above changes come into effect from April 1, 2017.

RECENT DEVELOPMENTS & CONCLUSION

As per an information note^[4] dated April 5, 2017, the Appointments Committee of the Cabinet (ACC) has approved the proposal for appointment of Justice K.K. Trivedi, Retired Judge, Madhya Pradesh High Court, to the post of Vice-Chairman of AAR in the apex scale in the newly created Bench at National Capital Region for a period of 03 years from the date on which he enters office, or till he attains the age of 65 years, or until further orders, whichever is the earliest.

As stated above, by virtue of the above approval for appointment, the Revenue Department has sought an adjournment in all cases which the current bench of the AAR has to hear. The AAR after considerable deliberation has passed a general order applying to all cases before it stating that till further orders, all cases before the AAR are adjourned.^[5]

The reason for the above is that the Judicial Member is only an 'in-charge Chairman' and by virtue of the approval for appointment of the Vice-Chairman read with the new provisions relating to vacancy of the office of the Chairman, the Vice-Chairman needs to discharge the functions of the Chairman. Thus, the current bench of the AAR should comprise of the newly appointed Vice-Chairman who would be the acting Chairman till a permanent Chairman is appointment along with the members. Thus, leaving the current bench with no locus to hear any matters.

However, is the above interpretation correct? This leaves us with a couple situations:

(i) Can an approval for appointment be treated as an appointment itself? The information note only provides that the ACC has approved the appointment of the Vice-Chairman. There is no letter of appointment appointing, Justice K.K. Trivedi as the Vice-Chairman of the AAR Bench at National Capital Region. In such a situation, can it be concluded that the approved for appointment Vice-Chairman is the new acting Chairman, resulting in the current Bench of the AAR to not function.

(ii) Is the office of the Chairman really vacant? By virtue of the order of the Patna High Court, the Judicial member was appointed as the in-charge Chairman till a new Chairman is appointed. Thus, the office of the Chairman cannot be considered to be vacant as the very essence of the judgment of the Patna High Court was to provide immediate relief for administration of justice for which an in-charge Chairman was appointed. Now by stating that since a Vice-Chairman has been approved for appointment (not appointed yet), the office of the Chairman has been vacated would not be a correct reading of the law laid down by the Patna High Court. In fact, such a reading of the law would tantamount to nullifying the judgment of the Patna High Court which could not have been the intention of the legislature.

(iii) Even assuming that the Vice-Chairman has been appointed, does it still make the office of the Chairman vacant? This too would result in an incorrect reading of the judgment of the Patna High Court. The reading of the approval note along with the new provisions cannot result in the office of the Chairman being considered to be vacant even though an order of a High Court provides the AAR

with an in-charge Chairman. Let's assume a situation where the new provisions did not come into effect and the Bench was functioning as is due to the judgment of the Patna High Court. This would mean that by the current reading of the new provisions, the Revenue Department always considered the office of the Chairman to be vacant even though the High Court order specifically appointed an in-charge Chairman. Note also should be made of the fact that no appeal was preferred by the respondents against the order of the Patna High Court which means that the order was accepted and the Revenue Member should continue to be the in-charge Chairman till a new Chairman is appointed. Therefore, there was an acknowledgement of the fact that a Chairman has been appointed who will continue in office till such time a new Chairman is appointed. By reading the law as is being done today is also departing from the view that was impliedly taken earlier by the department.

(iv) Section 245P of the ITA provides that a proceeding or pronouncement of an advance ruling by the AAR shall not be questioned or shall not be invalid on the ground merely of the existence of any vacancy or defect in the Constitution of the AAR. By virtue of these provisions, even a defect in the Constitution of the AAR should not result in invalidating proceedings before it. Therefore, even if the AAR continued to hear matters pending before it, it should not have resulted in invalidating such proceedings and orders passed by the AAR would be binding on the parties. In fact, wouldn't the general order of the AAR for all matters, be against the provisions of Section 245P? The approval for appointment should not have come in the way of the AAR delivering justice.

(v) Rule 26 of the Advance Ruling (Procedure) Rules, 1996 provides that every order of the Authority shall be duly signed by the members and bear official seal of the Authority. Therefore, the question that arises is whether the AAR can pass a general order in respect of all the cases pending before itself. Further, the question that also arises is whether by passing such an order which was due to the reading of the new provisions, is the AAR reviewing the order of the Patna High Court which under the ITA it does not have the power to do. Ideally, the appropriate method should have been to go back to the Patna High Court and ask for directions and putting before the High Court all facts, new provisions instead of *suo-moto* passing a general order concerning the validity of the Bench which it did not have the power to do.

It should also be noted that the Patna High Court in its order observed that the AAR forms an integral part of the administration of justice and cannot be allowed to remain effectively non-existent for a long time. The order of the Court was so that the functioning of the Authority does not remain completely stopped. But the result of an (flawed) interpretation has resulted in doing exactly opposite of what the High Court wanted to do.

As per data available, there are more than 400 cases (some filed as early as in the year 2009) pending before the AAR which under the ITA need to be disposed within 6 months from the date of filing of application. The fate of the transactions in these cases remain in the hands of an authority which currently is non-functional and may not function at all until clarification is received. Interestingly, in February of 2015, the Cabinet had approved the setting up of two more benches

of the AAR in Mumbai and in New Delhi. However, it's been more than two years but neither has been set up. Considering that currently there is effectively no AAR, the Government needs to set up not just two benches but three.

Tax certainty is the key for foreign investment into India. The AAR is one of those mediums which allows taxpayers the tax certainty that they require. The number of cases in the AAR is evident of the certainty that the taxpayer is looking for before making investment into India. However, such kind of functioning only results in loss of faith in the judicial system and results in being seen as a mockery of the justice system.

[1] Section 245O of the ITA

[2] Rule 27 of the Advance Ruling (Procedure) Rules, 1996

[3] CWJ Case No. 17261 of 2016 decided on September 18, 2016

[4] No.18/68/2016-EO(SM-II) Information Note (05.04.2017)

[5] http://aarrulings.in/cause_list_it.pdf