WEBINAR
on Important International Tax Rulings**

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***assisted by CA Harsh Bafna**
SML tax chamber

****from January 2019 onwards**

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[2020] 116 taxmann.com 379 (SC)

RED ⇒ contention of revenue or finding of ITAT/court against

Contrary views whether an LO is/is not PE

ISSUE 1

- ***In case of a UAE entity rendering remittance services, whether the activity of dispatching cheques/drafts to beneficiaries, by a Liaison Office in India, as per the instructions of its Head Office, could be regarded as activities of preparatory or auxiliary in nature as per Article 5(3)(e) of India-UAE DTAA, and thus the LO would not be considered as a PE of the UAE entity in India?***

RELEVANT PROVISION

- **Article 5(3)(e)** of India-UAE DTAA

  *"3. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" **shall be deemed not to include** :*

  (a)……

  ……

  *(e) the **maintenance of a fixed place** of business **solely** for the purpose of carrying on, for the enterprise, any other **activity of a preparatory or auxiliary character**."*

U.A.E. Exchange Center

FACTS

- The **assessee, a tax resident of UAE**, was engaged in **provision of remittance services for transferring funds from UAE to beneficiaries in India.**

- The assessee opened **four liaison office ('LO') in India and carried activities in accordance with the conditions imposed by the RBI.** The **expenses for maintaining the LO** were met out of the funds **received** by the LO **from its Head Office in UAE** and the **LO did not charged any fee/commission** for the services rendered in India, in compliance with the conditions imposed by the RBI.

- The **assessee** entered into **contracts with customers in UAE** for provision of remittance services pursuant to which the customers handed over the funds to the assessee in lieu of one-time fees. **The funds** received from the customers were **transferred to the beneficiaries in India, in the following two ways**:-
  a) By **telegraphic transfer through bank channels**; or
  b) On **request of the customer, the assessee dispatched** instruments/**drafts/cheques through its LO to beneficiaries in India**. (while doing so, the LO remained connected with the main server in UAE for retrieving information related to the beneficiaries and the customer)

- The assessee filed an application before the AAR for determining, whether the activity in the second mode of transfer would result in a taxable presence of the assessee in India.

CONTENTION OF THE ASSESSEE

- The assessee contended that the **activities undertaken by the LO**, such as printing instruments/drafts and dispatching the same through courier to beneficiaries in India, **are only supportive and auxiliary in nature to the main work undertaken by the assessee in UAE.**

- Accordingly, the assessee contented that the activities would **not** constitute **a PE** in India **in view of Article 5(3)(e)** of the DTAA in as much as the activities are in the nature of preparatory or auxiliary character.

CONTENTION OF THE REVENUE

- The Revenue contented that **the LO assists the assessee to extend its volume of business in India** and the services rendered by the **LO is connected to the main services rendered by the assessee in UAE.**

- Accordingly, **some portion of the fees/commission** charged by the assessee pertains to the **services rendered by the LO in India** and **hence shall be deemed to accrue or arise in India.**

U.A.E. Exchange Center

DECISION OF AAR

- The AAR held that activities undertaken by the **LO would constitute a taxable presence** in India by observing without the services of the LO the assessee would not be able to render the remittance services to its customers in UAE. Further, the AAR also observed that the **commission which the assessee receives for remitting the amount covers not only the business activities carried on in UAE but also the activity undertaken by the LO.**

- The AAR further held that, the **activities** undertaken by the LO constitute a main function of the business of the assessee and hence **cannot be termed as preparatory or auxiliary in nature.**

DECISION OF HIGH COURT

- The HC reversed the **decision of the AAR**, by relying on the decision of **Supreme Court in case of Morgan Stanley & Co. [2007] 162 Taxman 165 (SC)**, and held that the **activities** undertaken by the **LO are auxiliary in nature since it supports/aids** the **execution of the main activity undertaken by the assessee in UAE** and hence the LO would not be considered as a PE of the assessee in India.

DECISION OF SUPREME COURT

- The SC placed reliance **on the approval given by the RBI for establishing the LO** in India and observed that **the LO was not allowed to enter into any contract with any person in India nor the LO was allowed to charge any fees/commission** in respect of the services rendered in India.

- The SC observed that **Article 5(3)** of the DTAA, opens with a **non-obstante clause**, which indicates that **notwithstanding the fact that a PE is constituted under Article 5(1) or 5(2)**, **if the nature of activities carried by the assessee fall within the purview of Article 5(3)**, it would be deemed that the assessee does **not** have a **PE** in the Contracting State.

- The SC referred **Black's Law and Oxford Dictionaries** to interpret the expression **'preparatory'** and **'auxiliary',** and observed that the expression **'preparatory'** has been defined as ***'Materials used in preparing the ultimate form of an agreement or statute'*** and the expression **'auxiliary'** has been defined as ***'aiding or supporting or subsidiary or supplementary'.***

- The SC observed the **LO was conducting** a **combination of virtual and physical activities** i.e. **downloading the particulars of remittances through remaining connected to the main servers of the assessee in UAE and then printing cheques/drafts drawn on the banks in India, which, in turn, are couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the NRI remitter.**

DECISION OF SUPREME COURT (……continued)

- The SC observed that the **RBI** had given **permission to the assessee** to open a **LO for conducting activities** such **responding to enquiries from correspondent banks, reconciliation of bank accounts, act as a communication center, printing INR drafts etc.**

- The SC observed that the **above mentioned conditions imply** that the **LO would not be able to undertake any commercial activities (such as charging fees/commission for its services or entering into commercial contracts)** and **hence the activities carried by the LO are in nature of preparatory or auxiliary character.**

- In view of the above observations, the SC held that the **LO was not carrying on any business activity in India as such, but only dispensing with the remittances by downloading information from the main server of respondent in UAE and printing cheques/drafts drawn in India and accordingly no income u/s 2(24) was earned by the LO in India.**

- The SC also relied on the decision of co-ordinate bench in case of **E-Funds IT Solutions Inc, [2017] 86 taxmann.com 240 (SC),** wherein the SC held that when the **Indian subsidiary company only rendered support services** which **enabled assessee** (two American companies) to **render services to their respective clients abroad, this outsourcing work to India, in nature of auxiliary operations, would not give rise to a fixed place PE in India.**

DECISION OF SUPREME COURT (……continued)

- Accordingly **the SC upheld the order of the HC** and held that the LO was not allowed to undertake any commercial activities and hence the activities were **preparatory or auxiliary in nature**, which did **not result** in constitution of a **PE of the assessee** in India and thereby not liable to tax.

RBK { JEBON CORP – 125 ITD 340 (Bang)
SOJITZ CORP – 117 TTJ (Del) 729

considerations
core, integral, revenue generation, quantum of exp'd, presence of technical experts

Hitachi High Technologies Singapore Pte Ltd v. DCIT

[2020] 113 taxmann.com 327 (Delhi - Trib.)

ISSUE 2

- ***Whether activities such as price negotiation, obtaining orders, following up on delivery and payments, ascertaining customer requirements etc. undertaken by a LO in India, would be preparatory or auxiliary in nature as per India-Singapore DTAA?***

RELEVANT PROVISION

- **Article 5(7)(e)** of India-Singapore DTAA

  "Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be ***deemed not to include*** *:*

  (a)……

  …….

  (e) the ***maintenance of a fixed place*** *of business* ***solely*** *for the* ***purpose of advertising, for the supply of information, for scientific research, or for similar activities which*** *have a* ***preparatory or auxiliary character****, for the enterprise."*

Hitachi High Technologies Singapore Pte Ltd

FACTS

- The **assessee, a Singapore Co.**, was **engaged in trading operations across Southeast Asia**. The assessee established an **LO in India for providing 'preparatory and auxiliary services, including market research and liaison activities'.**

- Based on employee statements (duly supported by e-mails exchanges) recorded in a survey conducted at the LO's premises in 2008, the **AO** initiated assessment proceedings. A draft assessment order was passed holding that the **LO was negotiating and executing contracts for the assessee in India, and was not limited to undertaking preparatory and auxiliary activities**, and hence **it was a PE of the Assessee** in India under Article 5 of the India-Singapore treaty.

- The draft order was summarily upheld by the DRP, following which the AO crystallised the final order.

Hitachi High Technologies Singapore Pte Ltd

CONTENTION OF THE ASSESSEE

- The assessee contended that the **core business activities** of the assessee comprises of **trading operations across** the ASEAN countries and **the LO was acting as a communication channel (providing logistic support)** between the assessee and its customers in India and no part of the core activities of the assessee were carried in India through the LO. Thus the assessee argued that the **LO could not be considered as a fixed place of business of assessee in India.**

- The assessee also contented that the **RBI had not found any violation in the nature of activities carried out by the LO and thus it could not be presumed that the LO was engaged in any commercial activities in India.**

CONTENTION OF THE REVENUE

- The Revenue contented that based on the evidences gathered during the course of **survey proceedings** (by way of obtaining **statements from employees supported by e-mails), it was found that the employees of the LO were engaged in advertisement, marketing, conducting market research, sales promotion, administration and activities such as price negotiation, obtaining orders, following up on delivery and payments, ascertaining customer requirements etc.**

- The activities does **not** fall within the exclusionary clause of Article 5 (**i.e. preparatory or auxiliary**) and none of the activities carried by the LO were **similar to advertising, supply of information or scientific research as required under Article 5(7)(e).**

Hitachi High Technologies Singapore Pte Ltd

DECISION OF TRIBUNAL

- The Tribunal by referring to the nature of activities undertaken by the employees of the LO i.e. advertisement, marketing, conducting market research, sales promotion and administration, observed that the **LO was undertaking the core activities of the assessee in India and hence the assessee indeed carried business in India.**

- **W.r.t Article 5(7)(e)**, the Tribunal held that the **activities would not fall within the said exclusionary clause.**

- The Tribunal analyzed the text of the PE exclusion clause in **Article 5(7)(e) of the India Singapore DTAA**, and observed that the words **'for similar activities'** used after **'advertising', 'supply of information' or 'scientific research' were noticeably different from the phrase 'for other activities' used in India's treaties with Canada, or the USA.**

- Hence the use of **'similar activities'** necessitated the application of the principle of ejusdem generis, meaning the scope of the residuary phrase had to be interpreted in light of the words preceding it, being: advertising, supply of information and scientific research. Therefore, **unless the LO was being used only for advertisement, for supply of information, for scientific research, or activities similar to these three which have preparatory or auxiliary character, they could not fall in the PE exclusion clause.**

Brown & SHARPE – 51T.com 327 (AU) – US Treaty
"negotiation"
RBI – pursuasive – rebuttable presumption
UAE ⇒ Legal interence with "core" | HITACHI – factual finding

Nagase and Company Ltd.

[2019] 109 taxmann.com 288 (Mumbai - Trib.)

ISSUE 3

- ***Whether a LO could be considered as an PE in India, when Revenue was not able to establish that the LO was carrying business activities in India, based on the documentary evidences during the course of survey proceedings?***

RELEVANT PROVISIONS

- **Article 5(7)(a)** of India Japan DTAA

  "*(a) he has and habitually exercises in that Contracting State an* ***authority to conclude contracts*** *on behalf of the enterprise, unless his activities are limited to those mentioned in paragraph 6 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph.*"

PTD

Nagase and Company Ltd.

FACTS

- The assessee, a tax resident of Japan, was allowed by the Reserve Bank of India to open a Liaison Office (LO) in India, with a condition that no business would be carried on in India and no income would be earned in India.

- Based on the **survey proceedings, the AO observed that the LO was conducting business activities in India**, by referring to the to an agreement between LG Chemicals Ltd., Korea, and Liaison Office for granting assessee an exclusive and non-transferrable right to distribute certain chemical products on commission basis. **The impounded files contained performance review reports of its employees which contained the details of the sales which the employees were expected to make and hence the AO also observed that the LO was actively pursuing potential customers in India and its activity were not limited to liaising.**

- In view of the above, the **AO** concluded that the **LO** was engaged in commercial activities and hence a PE of the assessee was constituted in India. **The Action of the AO was upheld by the CIT(A).**

Nagase and Company Ltd.

FACTS

- Before the Tribunal, the **assessee contended that the documents impounded during the course of survey proceedings, as well as the above mentioned agreement between LG Chemicals Ltd., Korea, and Liaison Office, did not pertain to the year under consideration and further** the assessee also contended **that the only two documents which pertained to the captioned year, pertained to invoices of an independent agent of the assessee,** which were kept with the **LO for the purpose of a meeting between the assessee's HO and the said independent agent.**

- Accordingly, the assessee contended that **based on the above two documents, it could not be established that the assessee's LO constituted a PE in India.**

DECISION OF THE TRIBUNAL

- The Tribunal perused the **two documents** (i.e. of **the independent agents** of the assessee), **one was with respect to achievement of sales target** and **other document was in respect to communication for a meeting** between **the employee of the assessee's HO** and the said independent agent of the assessee, with respect to achievement of the sales target covered by the first document. The said **meeting was also attended by the employees of LO** for acting as a **communication channel, since employees of HO spoke only Japanese language**.

- The Tribunal observed that the **impounded document in no way conclusively established the fact that the Liaison Office at Mumbai was acting as an agent by involving itself in concluding contracts on behalf of the Head Office or involving itself in any commercial transaction on behalf of the Head Office to constitute a PE in India.**

- The Tribunal held that based on the impounded documents, **it could not be established that the LO in India was carrying on any commercial activity on behalf of the assessee, so as to constitute a PE in India.**

CIT v. TAJ TV LIMITED

[2020] 115 taxmann.com 305 (Bombay)

ISSUE 4

- ***Whether an exclusive distributor acting independently on a principal to principal basis (for one business activity) would be considered as a dependent agent of a non-resident as per Article 5(4) of India-Mauritius DTAA, merely because he is a DAPE for another business activity.***

RELEVANT PROVISIONS

- **Article 5(4)** of India-Mauritius DTAA

  4. Notwithstanding the provisions of paragraphs (1) and (2) of this article, ***a person acting in a Contracting State*** *for* ***or on behalf*** *of an* ***enterprise of the other Contracting State*** *[****other than an agent of an independent status*** *to whom the provisions of paragraph (5) apply]* ***shall*** *be* ***deemed*** *to* ***be a permanent establishment*** *of that enterprise in the first-mentioned State if :*
  (i) he has and habitually exercises in that first-mentioned State, ***an authority to conclude contracts*** *in the name of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise ; or……*

Taj TV Limited

FACTS

- The **assessee, a tax resident of Mauritius**, was **engaged in the business of telecasting sports viz. 'Ten Sports'** channel and **earned revenue by way of advertisement and distribution of channel in India**.

- The **assessee** had entered into the following **two types of agreements** with **Taj India (a subsidiary** of the assessee, incorporated in India):
  a. **Distribution Agreement** – Through which **Taj India** was appointed as an **exclusive distributor** in India to distribute the said channel for exhibition to subscribers. The distribution revenue collected by Taj India was shared in the ratio of **60:40 between the assessee and Taj India** ; and
  b. **Advertisement Agreement** – Through which **Taj India** was appointed as **advertising sales agent** in India to sell commercial advertisements slots on the said channel.

- The **AO** concluded the assessment proceedings by holding that the **Taj India had an authority to conclude contracts w.r.t the advertisement agreement**. Further **w.r.t the distribution agreement, the AO observed that Taj India had an exclusive right to represent before the cable operators on behalf of the assessee** and hence the AO held that a **Dependent Agent PE (DAPE)** of the assessee was established in India.

Taj TV Limited

CIT(A)'S OBSERVATION

- The **CIT(A)** observed that **w.r.t advertisement agreement, Taj India was fully dependent on the assessee** for its business activities and hence **Taj India constituted a PE.**

- **W.r.t the distribution agreement**, the **CIT(A)** held that **Taj India had acquired rights of distribution of channel from the assessee on its own behalf and hence it was held that Taj India did not constitute a DAPE of the assessee as per Article 5(4) of India-Mauritius DTAA.**

TRIBUNAL'S OBSERVATION

- **Assessee's appeal w.r.t advertisement agreement was dismissed as being time barred** by the Tribunal.
- **W.r.t the distribution agreement, the Tribunal** observed that **none of the conditions as stipulated in Article 5(4) of the DTAA were applicable since Taj India was acting independently qua its distribution rights and the entire agreement was on principal to principal basis and hence DAPE in not established.**

DECISION OF THE HIGH COURT

- **The Court analyzed Article 5(4)** of the DTAA and **observed that a DAPE is constituted only if the agent habitually exercises** in the first contracting State **an authority to conclude contracts in the name of the enterprise** or **he habitually maintains** in the first contracting State **a stock of goods or merchandise belonging to the enterprise from which he regularly fulfills orders on behalf of the enterprise.**

- The **Court relied on the order of the Tribunal, wherein it was factually determined (after perusal of the distribution and the sub-distribution agreements) that Taj India was not acting as agent of the assessee but it had obtained the right of distribution of the channel for itself and subsequently, it had entered into contracts with other parties (i.e. the sub-distribution agreements) in its own name in which the assessee was not a party.**

- In view of the above, the Court held that since none of the conditions as mentioned in Article 5(4) of the India-Mauritius DTAA were fulfilled **DAPE** of the assessee **was not established** in India i.e. qua the distribution agreement.

AUDI AG v. ADIT

[2019] 111 taxmann.com 213 (Mumbai)

ISSUE 5

- ***Whether the transactions of selling cars, by a foreign assessee company to its AE, a sole distributor in India, on a principal to principal would result in constituting a business connection or PE in India of the assessee as per India-Germany DTAA?***

RELEVANT PROVISION

- **Article 5(5)** of India-Germany DTAA

  "5. Notwithstanding the provisions of paragraphs 1 and 2, where a ***person*** *-* ***other than an agent of an independent status*** *to whom paragraph 6 applies -* ***is acting in a Contracting State on behalf of an enterprise of the other Contracting State*** *that enterprise shall be* ***deemed*** *to have a* ***permanent establishment*** *in the first-mentioned State, if this person:—*

  (a). has and habitually exercises in that State ***an authority to conclude contracts on behalf of the enterprise****, unless his activities are limited to the purchase of goods or merchandise for the enterprise ;"*

Audi AG

FACTS

- **The assessee, a tax resident of Germany**, is one of the world's leading car manufacturers and has **Indian AE's, namely Volkswagen Group Sales** India Private Limited ('VW Group Sales') and Skoda India.

- The assessee appointed **VW Group Sales as a sole distributor of Audi cars in India**, who is engaged in the wholesale trading of Audi and Volkswagon car.

- VW Group Sales, purchased fully built-up cars from the assessee, Volkswagon Group AG and Skoda India and sold the same to the dealers/distributors in India.

- The **AO** concluded the assessment proceedings, by holding that the **assessee had a business connection and a PE, as per Article 5 of the India-Germany DTAA, in India in the form of VW Group Sales, since VW Group Sales was the exclusive distributor of the assessee and the activities of VW Group Sales were devoted wholly for the assessee.**

- The assesse filed objections before the DRP and the DRP rejected the objections of the assessee on the grounds that VW Group Sales has no independent authority to act on its own and is bound by the terms and conditions imposed by the assessee.

ASSESSEE'S CONTENTION

- The assessee contented that the **delivery and the title of the cars was transferred outside India** and hence **no income could be attributed in India as the income is accrued outside India.**

- The **assessee** further argued that the activities pertaining to manufacturing and sales of cars happened outside and VW Group Sales **is not selling the cars on behalf of the assessee.**

REVENUE'S CONTENTION

- The **Revenue** contended that **most of the senior officials of the VW Group Sales had come from the Audi Group abroad** and **activities such as storage, marketing, advertisement, after-sales services and support, supply of spare parts and accessories etc. were done by VW Group Sales on behalf of the assessee** and were **carried out from its fixed place of business** maintained in India.

- The Revenue contended **VW Group Sales was acting as an extended arm of the assessee in** India.

- The Revenue contended that the **aforesaid business model results in a PE. It relied on the AAR decision in case of Aramax International Logistic (P.) Ltd., In re [2012] 22 taxmann.com 74/208 Taxman 355 (AAR)**

Audi AG

DECISION

- The Tribunal observed that the **cars were manufactured outside India and were also sold outside India and accordingly the same constituted a separate and different activity.**

- The **Revenue had not provided any evidence to rebut the claim of the aseessee that the cars were not sold to VW Group Sales on principal to principal basis and thereafter, VW Group Sales sold the same on a principal to principal basis to the dealers/distributors.** In view of the same, the it could not be held that assessee had a business connection or a PE in India.

- The Tribunal placed reliance on the decision of **Tribunal (Mumbai Bench)** in case of **Daimler Chrysler AG [2012] 21 taxmann.com 478**, wherein on similar facts the Tribunal held that the AE of the assessee could not be considered as having a fixed PE or a dependent agent of the assessee.

- The **Tribunal distinguished the case of Aramex (supra)** relied upon by the Revenue by observing that the said judgment was on **different set of facts.** In the said case, Aramex entered in to the contract with the customer outside India for delivery of parcel in India, and thus some part of the transaction was executed in India, which was not the case in the present case. **Also, the privity of contract was between the customer and Aramex outside India.**

what if sales from A to W happens in India

Linklaters LLP v. DCIT (IT)

[2019] 111 taxmann.com 198 (Mumbai - Trib.)

ISSUE 30

- ***To determine a threshold for Service PE under the India UK DTAA, whether the term 'any 12 month period' appearing in Article 5(2)(k) needs to be construed as previous/financial year for the relevant assessment year?***

RELEVANT PROVISION

- **Article 5(2)(k)** of India-UK DTAA

  "2. The term "permanent establishment" shall include especially :
  (a)…….
  …….
  (k) the furnishing of services including managerial services, other than those taxable under Article 13 (Royalties and fees for technical services), within a Contracting State by an enterprise through employees or other personnel, but only if:
  (i) activities of that nature continue within that State for a period or periods aggregating more than 90 days ***within any twelve-month period****; or*
  (ii) services are performed within that State for an enterprise within the meaning of paragraph 1 of Article 10 (Associated enterprises) and continue for a period or periods aggregating more than 30 days ***within any twelve-month period****:"*

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FACTS

- The **assessee, a tax resident of U.K.**, offers **legal consultancy services** to its **clients all over the world including India.**

- During the year under consideration, the assessee provided professional services to its Indian clients. **The employees of the assessee firm visited India to render the legal services for 42 days in the previous year relevant to assessment year 2013-14 (relevant AY).**

- During the course of assessment proceedings, the **AO** held that the **assessee had a service PE in India**, through which it was rendering legal services in India (since the **employees of the assessee firm were present in India for more than 90 days during the twelve month period**).

- The assessee raised objections against the draft assessment order, however, the DRP rejected the objections of the assessee and in terms of the directions of the DRP, the draft assessment order was finalized.

ASSESSEE'S OBJECTION BEFORE THE TRIBUNAL

- The assessee contended that it did **not** have **PE** in India in terms of **Article 5(2)(k)(i)** of the India UK DTAA, as **its employees did not stay in India more than 90 days during the relevant previous year**.

- The assesse relied on **co-ordinate bench ruling in assessee's case** wherein the expression '**any twelve months period' as used in Article-5(2)(k)(i)** of the DTAA was construed as **previous year relevant to AY under consideration.**

- The assessee contended that the **total number of days** spent by the employees in India was **42 days**, therefore, in terms of Article-5(2)(k)(i) of the DTAA, the assessee did not have PE in India during the year.

REVENUE'S OBJECTION BEFORE THE TRIBUNAL

- The **Revenue** contended that, **had it been the case, then, fiscal year which has been defined to be the previous year in Article 3(1)(d) would have been used in Article 5(2)(k)(i)** of the tax treaty. Thus, the meaning ascribed to fiscal year cannot be ascribed to the term 'any twelve months period'.

DECISION OF TRIBUNAL

- The Tribunal observed that the expression '**any 12 month period**' as used in Article 5(2)(k)(i) had **not been defined anywhere in the tax treaty, therefore, the meaning of the said expression could be taken with the aid of the provisions of the Act, since, the income is sought to be taxed in India.**

- The Tribunal observed **that section 4 of** the Act, which is the **charging section**, mandates that **a person shall be charged to income tax in respect of the total income of the previous year, which has been defined as a financial year immediately preceding the AY.**

- The Tribunal thus observed that if the provisions of **Article 5(2)(k)(i)** is read harmoniously with the provisions of the Act, it would be fair and reasonable to conclude that the expression '**any 12 month period**' mentioned in Article 5(2)(k)(i) had to be construed to mean the **previous year or financial year** as defined under the Act, since, the income is sought to be taxed in India.

Linklaters v. DDIT (IT)

[2019] 106 taxmann.com 195 (Mumbai - Trib.)

ISSUE 7

- ***While determining the threshold of 90 days for constitution of a Service PE under the India-UK DTAA, whether multiple counting of employees present on the same day (i.e. man days) is permissible and whether leaves taken by an employee is to excluded?***

RELEVANT PROVISIONS

- **Article 5(2)(k)** of India-UK DTAA

  "The term "permanent establishment" shall include especially :

  (a) a place of management

  …….

  *(k) the **furnishing of services** including managerial services, other than those taxable under Article 13 (Royalties and fees for technical services), within a Contracting State by an enterprise through employees or other personnel, but only if:*

  *(i) **activities of that nature continue** within that State for a period or periods aggregating more than **90 days** within any twelve-month period; or*

  ……."

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FACTS

- The **assessee, a tax resident of UK, was engaged in the practice of law**. The assessee **was appointed** as a **legal advisor for some of the projects in India and provided legal consultancy services to them.**

- The **assessee** filed its return of income declaring **NIL income**, by claiming that **since it had no branch office in India**, the fee received was not chargeable to tax in India **in the absence of a PE in India**, on the ground that its employees were present in India for **87 days**.

- The **AO** computed the **number of days**, during which the employees/other personnel of the assessee were present in India, **by counting the number of days employee wise (i.e. man days)** and **without excluding the leaves taken by an employee.**

- The **AO observed** that the employees/other personnel of the assessee had rendered services in India **for more than 90 days during** the relevant financial year, hence, the assessee had **a Service PE** in India **in terms of Article 5(2)(k)(i)** of the India UK DTAA. Therefore, income earned from rendering legal consultancy services in India is taxable in India.

- The assessee contended that a. **if the vacation period of one of the employee** namely Shri Narayan Iyar **was excluded**, **the period of stay of the employees of the assessee in India would be 87 days** and b. **multiple counting of employees in a single day (i.e. man days) is not permitted.**

DECISION OF TRIBUNAL

- The Tribunal observed that the **said employee had not rendered any services in India from 17 April 2001 to 4 May 2001, as he was availing a study leave** and therefore, the same period has to be **excluded for computing the period of 90 days as no other employee of the assessee was rendering services in India.**

- The Tribunal, by relying on co-ordinate bench ruling in case of **Clifford Chance** [2002] 82 ITD 106 (Mum Trib.), held that the stay of employees in India on a particular day has to be taken cumulatively and not independently. That being the case, **multiple counting of employee in a single day, as was done by the tax authorities, is not impermissible under Article 5(2)(k)(i).**

ULO Systems LLC v. ADIT (IT)

[2019] 101 taxmann.com 490 (Delhi - Trib.)

ISSUE 8

- ***Whether grouting activity, carried out for less than 9 months on various projects, to protect subsea pipelines, cables and structures, would amount to 'construction activity' so as to constitute a PE under Article 5(2)(h) of India-UAE DTAA?***

RELEVANT PROVISIONS

- **Article 5(1) and Article 5(2)(h)** of India-UAE DTAA

  "1. For the purposes of this Agreement, the term "permanent establishment" means a **fixed place** of business **through which** the business **of an enterprise** is **wholly or partly** carried on.

  2. The term "permanent establishment" includes especially :
  (a).....
  (h) ***a*** *building site or* ***construction*** *or assembly* ***project*** *or supervisory activities in connection therewith, but only where* ***such site, project or activity*** *continues for a period of more than* ***9 months"***

ULO Systems LLC

FACTS

- The **assesse, a tax resident of UAE, was engaged in providing grouting and precast solutions** for **subsea off-shore construction industry** and also provided products and solutions to support and protect subsea pipelines, cables and structures.

- During the course of assessment proceedings, the **AO contended that grouting activity is not a simple masonry work and involves complex aspects and held that the grouting activities fell within general Article 5(1)** India –UAE DTAA, whereas **the assessee contended that the grouting activities fell within 'construction activity' contemplated in specific provision of Article 5(2)(h)**, and since the number of days spent in India were **less than 9 months (i.e. 264 days), it did not had a PE in India.**

- **Assessee** also argued **that services having been rendered to different unrelated third party customers** in India, and **contracts not being inter connected**, therefore, it **could not be said that the assessee had PE in India**.

- The **DRP held** that the assessee had **an equipment PE in India**, since **the equipment through which the construction services were rendered, was in India for a period of 264 days.**

FACTS

- Further the **DRP also held** that **benefit of limitation clause (i.e. threshold of 9 months) would be applicable** only when **such activities are occasional**, however **when such activities are carried out regularly and periodically**, then it would raise a presumption that such **arrangement is done deliberately to avoid establishment of PE in India.**

DECISION OF TRIBUNAL

- The Tribunal, taking into consideration the technicalities of the **grouting activities** held that it was a settled legal principle in latin maxim "generalia specialibus non deroganf", which meant a general provision would not be applicable when specific provision is there, accordingly **the grouting activities would fall within the ambit of 'construction activity' under Article 5(2)(h) and not Article 5(1).**

- The **Tribunal rejected the plea of the Revenue** that the **services would fall under Article 5(1)** since **grouting was not a simple masonry work and involves complex aspects**, on the ground **that there is no bifurcation of simple and complex masonry/construction work under article 5(2)(h)** and any further classification would amount to rewriting DTAA.

- Further w.r.t the observations of the DRP, that the assesse had an equipment PE in India, the Tribunal **held that equipment PE is not envisaged in the India UAE DTAA.**

- Further, the Tribunal also observed that the **application of aggregation principle on all, or even connected, sites, projects or activities for computation of threshold duration test would be applicable only if there is a specific mention for it is the respective DTAA.**

may be argued for subsequent years (264 = 270)

DECISION OF TRIBUNAL (……continued)

- However, the Tribunal noted that **India-UAE DTAA used singular expressions 'a building, site or construction or assembly project' and, therefore aggregation of different projects was not allowed** by conscious legislative scheme (as adopted by the Legislature in case of DTAA's with Australia, Thailand, Canada, USA, Denmark etc.), as claimed by Revenue.

DTAA – aggregation — Australia, Thailand, Canada, U.S.A, Denmark

Equipment PE → Australia → Beneficial provisions to apply

Otherwise — Sp Vs. 4 cm.

(2009) 32 SOT 249 (mm) ← STORK Engineers

service PE Vs. Supervising

Gemological Institute of America

[2019] 109 taxmann.com 99 (Mumbai - Trib.)

ISSUE 9

- ***Whether rendition of grading services, on a revenue sharing basis by Foreign Co., to the Indian subsidiary, would result in establishment of a PE (in the form of subsidiary) of the assessee in India?***

CLIENT ← ICD ← FCD
ID : 9D

RELEVANT PROVISION

- **Article 5(1)** of India-USA DTAA

  *"1. For the purposes of this Convention, the term "permanent establishment" means a **fixed place** of business **through** which the business of an enterprise is wholly or partly carried on."*

- **Article 5(2)(l)** of India-USA DTAA

  "The term "permanent establishment" includes especially :
  (a)……..
  …….
  *(l) the **furnishing of services**, other than included services as defined in Article 12 (Royalties and Fees for Included Services), within a Contracting State by an enterprise **through employees or other personnel**, but only if)……."*

RELEVANT PROVISIONS

- **Article 5(4)** of India-USA DTAA

  *"4. Notwithstanding the provisions of paragraphs 1 and 2, where a person—**other than an agent of an independent status** to whom paragraph 5 applies - is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned State, if :*

  *(a). he has and habitually exercises in the first-mentioned State **an authority to conclude on behalf of the enterprise**, unless his activities are limited to those mentioned in paragraph 3 which, if exercised through a fixed place of business, would not make that fixed place of business a permanent establishment under the provisions of that paragraph ;"*

Gemological Institute of America

FACTS

- The **assessee, a tax resident of USA**, is engaged in the **business of diamond grading and preparation diamond dossiers**. As **per the GIA Gem Grading Services Agreement** (which had been **entered into by** the **various entities of the Group, including the assessee and its Indian subsidiary**), **whenever any member** of the Group faced **capacity and/or technical constraints for grading diamonds**, it **send stones for grading to other entities** of the Group across the globe, including the assessee. **Further, two graders who were earlier employed with the assessee were currently employed with its Indian subsidiary and working under the control and supervision of the Indian subsidiary.**

- As per the above mentioned agreement, there was a **uniform pricing mechanism of 90:10** for grading services i.e. the **entity of** the Group which was **requesting for the grading services** retains **10% of the fees** it collects from its customer and **90% of the said fees** was **paid** to the **entity which provided the grading activity.**

- The **AO** during the course of assessment proceedings, viewed this agreement as an agreement through which the **assessee was carrying its business in India through its subsidiary as a JV**. Accordingly, the AO concluded, that the **assessee has a PE in the form of its subsidiary**. Further the AO **attributed 50% of the grading fees received by the assessee from its subsidiary to the said PE.**

- **The assessee contented that in terms of the relevant DTAA provisions, a PE would be constituted only when, there exist a place of business in India or a service PE or an agency PE, which was lacking in the present case.**

DECISION OF TRIBUNAL

- **Fixed Place PE:**
  - The Tribunal observed that the **mere fact that a company has controlling interest in the other company** does **not** by itself construe the other company to be its **PE**.
  - Further, the Tribunal perused the above mentioned agreement and observed that the transaction of grading services between the assessee and its subsidiary **could not be considered** to be in the nature of a **joint venture**. The **subsidiary bore all the risk** including credit risk, client facing risk, risk of all damage of articles in transit **i.e. all economic risks**.
  - Since the **subsidiary had** its own **independent expertise but only due to its technology/capacity constraints, it forward the stones to the assessee for** grading **purposes**.
  - Accordingly, the subsidiary could not be treated as Fixed place PE of the assesses.

- **Service PE:**
  - The Tribunal held that, **Service PE** was **not constituted** since **the graders (i.e. employees)** were **working under the control and supervision of its subsidiary and were on its payroll**.
  - The Tribunal relied on the decision of **Supreme Court** which affirmed the decision of the Delhi **High Court in E-funds IT Solutions** Inc., wherein it was held that **two employees deputed to e-Fund India did not create a service PE as the entire salary cost was borne by e-fund India and they were working under control and supervision of e-fund India.**

DECISION OF TRIBUNAL

- **Agency PE:**
  - The Tribunal observed that the **subsidiary was bearing all the client facing risk vis-à-vis the stones sent to the assessee for grading purposes** and the **subsidiary did not have any authority to conclude any contract in India on behalf of the assessee.**

Reliance Jio Infocomm Ltd

[2019] 111 taxmann.com 371 (Mumbai - Trib.)
[2019] 108 taxmann.com 325 (Mumbai - Trib.)

ISSUE 10

- ***Whether payment made for bandwidth services (with respect to telecommunication services) amounts to 'royalty' under the India – Singapore DTAA?***
- ***Scope of Article 3(2) of the India – Singapore DTAA?***

RELEVANT PROVISIONS

- **Explanation 2 to section 9(1)(vi)**

*"Explanation 2.—For the purposes of this clause, **"royalty"** means **consideration** (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") **for**—*

*(i) the **transfer of all or any rights** (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or **process** or trade mark or similar property ;*

*(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret **formula or process** or trade mark or similar property ;*

*(iii) the use of any patent, invention, model, design, **secret formula or process** or trade mark or similar property ;"*

RELEVANT PROVISIONS

- **Article 12(3)** of India-Singapore DTAA

  *"3. The term **"royalties"** as used in this Article means payments of any kind received as a consideration **for the use of, or the right to use :***
  *(a) any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, **secret formula or process**, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right, property or information ;*
  (b) any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraph 4(b) or 4(c) of Article 8."

- **Article 3(2)** of the India – Singapore DTAA

  *"as regards the application of the Agreement by a Contracting State, any **term not defined** therein shall, unless the context otherwise requires, have, the **meaning** which it has under the **law** of that State concerning the taxes to which the Agreement applies".*

- **Explanation 6 to Section 9(1)(vii)**

  *"for the removal of doubts, it is hereby clarified that the expression **"process"** includes and shall be deemed to have always included **transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre** or by any other similar technology, **whether or not such process is secret**".*

Reliance Jio Infocomm Ltd.

FACTS

- Reliance Jio Infocomm Ltd. ('RJIL' or 'the **Assessee**'), an Indian company, was in the business of rolling out **telecom services in India**.

- Assessee entered into a **bandwith services agreement** with **Reliance Jio** Infocomm Pte Ltd., **Singapore** ('I Co.') which enabled it to establish, install, maintain, operate and provide telecommunication services in Singapore and also provide bandwith services to service recipients across the globe.

- In pursuance of the agreement, assessee remitted a certain sum to RJIPL.

- **Assessee** approached **CIT(A) u/s 248** of the Indian Income Tax Act, 1961 and **claimed** that it was not obliged to deduct tax at source under section 195 of the Income Tax Act, 1961 as **I Co.'s income** was in the nature of **business profits** which in **absence of PE** in India could **not be taxed in India**.

CIT(A)'s FINDING

FTS

1. Services were **standard telecom services** - did not require any **human intervention** – could not be 'technical services' – could **not** be **FTS under S.9(1)(vii)**
2. Article 12(3) of the tax treaty – bandwith services did not **'make available'** any technical knowledge, experience, skill, knowhow or process to the assessee which was simply availing the said standard facility

ROYALTY

3. Assessee did **not** have **access** to any **process**
4. **Infrastructure and process** required was used and had remained under **control of RJIPL** and was not given to the assessee
5. **Process** involved was **not 'secret'** – IPR was not owned/registered in the name of RJIPL
6. Standard commercial process followed by industry players – could not be classified as 'secret process' as required under the DTAA
7. Amount paid by assessee was **not** towards **use of** (or for obtaining right to use) industrial, commercial, scientific **equipment** nor towards use of (or for obtaining right to use) any **secret formula or process**
8. Not Royalty both under treaty as well under the Act

BUSINESS PROFITS/PE

9. Business Profit – No PE – Not taxable

REVENUE'S CONTENTION BEFORE HON'BLE TAX TRIBUNAL [I.T.A.T]

FTS

- The Revenue accepted that the payment for bandwith services was not FTS

ROYALTY

- The revenue contended that the **payment for bandwith services** amounted to **royalty** under **Article 12** of the India-Singapore DTAA as well **as Explanation 6 to Section 9(1)(vi)** of the Act**.**

SCOPE OF ARTICLE 3(2)

- As per Article 3(2) of the India-Singapore DTAA and Explanation 6 to Section 9(1)(vi) in interpretation of Article 12 of the DTAA the payment made by the assessee to I Co. for providing bandwith services was royalty and could not be classified as business profits.
- CIT v. Siemens Aktiongesellschaft had upheld ambulatory approach to domestic law meaning of undefined terms under article 3(2).

Reliance Jio Infocomm Ltd.

DECISION UNDER THE TREATY

ROYALTY

1. Assessee received **standard facilities**
2. Assessee did **not** have **access to any equipment**
3. Assessee did **not** have **access to any process**
4. **Infrastructure and process** required for provision of bandwith services was always used and **under control of Co.**
5. **Process** was **not 'secret**' i.e. **IPR was not owned**/registered in the name of **RJIPL**
6. **Amount paid** by assessee was **not** towards use of (or **for** obtaining right to use) **industrial, commercial, scientific equipment** nor towards use of (or for obtaining right to use) any **secret formula or process**
7. 'Royalty' under Article 12 of **India-Hungary DTAA (unlike India-Singapore DTAA)** takes **within its sweep "...transmission by satellite, cable, optic fibre or similar technology..."**
8. Royalty defined in the Indian Income Tax Act **was amended vide Finance Act 2012** to include the definition of **"process". Subsequently, India-Singapore tax treaty was amended by Notification No. SO 935(E), dated 23.03.2017, however, the definition of royalty therein envisaged had not been tinkered with and remained as such**
9. **Amendment in section 9(1)(vi) will not have any bearing on definition of 'royalty'.** [CIT v. Reliance Infocomm Ltd, CIT v. Siemens Aktiongesellschaft

SCOPE OF ARTICLE 3(2)

10. Provisions of **Article 3(2)** come into play for domestic law meaning of **"any term not defined"** in the tax treaty.

DECISION (...continued)

11. The expression **"term"** is defined as **"a word or phrase used to describe a thing or to express a concept, especially in a particular kind of language or branch of study"**. A "term" is thus a word that has meaning and refers to objects, ideas, events or a state of affair. **A term is thus, in addition** to being **a word,** some kind of a point of reference, whereas a word is only a constituent of language.
12. **Article 3(2)** will come into play only in respect of the **undefined treaty terms**, which are in the nature of reference points and which have some peculiar significance, and not in respect of all the **undefined words** and expressions used in a treaty.
13. **The expression 'process' is not a treaty term *per se***, or a reference point, used in the treaty, **rather it is an expression or word used in defining the treaty term 'royalty'.** The expression **"process"** is used in the treaty in that limited context and it **does not have an independent existence**.
14. The domestic law meaning under article 3(2) is relevant only when the treaty term itself is undefined, as noted by Hon'ble Delhi High Court in the case of **DIT v. New Skies Satellite BV**. When the expression **'royalty' is a defined** expression under the applicable **tax treaty**, there cannot be any occasion to invoke **article 3(2) for further dissecting** the issue and exploring the **domestic law** meaning of each expression used in this definition for coming to the conclusions about connotations of royalty.
15. It could not, therefore, be open to invoke article 3(2) to import domestic law meaning, even partly, when the treaty term has received a definition under the treaty. It was for this reason that **Explanation 6 to Section 9(1)(vi)**, had **no role**, **under article 3(2)** of the treaty, in **explaining the expression "process"**, in the context of defining royalty under the Indo Singaporean tax treaty.

DECISION (...continued)

16. The next fundamental question, was whether assignment of the domestic law meaning under article 3(2), to an undefined treaty term, was to be done by way of **static interpretation or** by way of dynamic or **ambulatory interpretation.**

(a) The expression **"process" was not, at the point of time** relevant to static interpretation, **statutorily defined.**

(b) (i) The Court dealt with the case of **CIT v. Siemens Aktiongesellschaft** cited by Revenue, which had upheld ambulatory approach. However, in that case the treaty in question was the **Indo-German DTAA**. The relevant article [**II(2)**] of the said treaty stated "in the application of the provisions of this agreement in one of the territories any **term not** otherwise **defined** in this agreement shall unless the context otherwise requires, **have the meaning which it has under the laws in force in that territory**." The **Indo-Singapore treaty**, however, states "As regards application of the agreement by contracting state, any **term not defined** therein **shall have the meaning** which it has **under the law of that state**. Thus, the Indo-Singapore DTAA was differently worded from the German DTAA as the words 'law in force' were not found in it. Thus, ambulatory approach would not apply in the present case.

(ii) In the case of **Her Majesty The Queen v. Melford Developments Inc.** it was observed **by the Supreme Court of Canada** that unilateral amendment it is not possible for one nation which is party to an agreement to tax income which otherwise was not subject to tax. Whatever be the approach adopted, for the purpose of article 3(2) i.e. static or ambulatory, **a unilateral treaty override, is not permissible**.

DECISION (...continued)

17. (a) **Article 26 of Vienna Convention on Law of Treaties** provides that, "Pacta sunt servanda: **Every treaty in force is binding on the parties to it and must be performed by them in good faith ".**

(b) What it implies is that whatever be the provisions of the treaties, these provisions are to be given effect in good faith. **If a tax jurisdiction is allowed to amend the settled position with respect to a treaty provision, by an amendment in the domestic law, it cannot be treated as performance of treaties in good faith.**

(c) Held by the Delhi High Court in the case of **DIT v. New Skies Satellite BV**, **"the "VCLT" is universally accepted as authoritatively laying down the principles governing the law of treaties".**

(d) Held by the Supreme Court in the case of **Ram Jethmalani v. Union of India**, that "it **(VCLT) contains many principles of customary international law".**

(e) Therefore, the **additional test that is required** to be put, while **adopting the ambulatory interpretation** in such a situation, is **whether the amendment in domestic law ends up unsettling a conclusion arrived at under the pre domestic law amendment position** i.e. reversing the judicial rulings in favour of the residence jurisdiction, and, **if the answer is in the positive, the ambulatory interpretation is to be discarded** because **that approach would** patronise, and **legitimise, a unilateral treaty override**, and the outcome of ambulatory interpretation in such a case will be **incompatible with the fundamental principles of treaty interpretation under the Vienna Convention.**

(f) The approach is justified on the first principles on the ground that **when two approaches are possible** for incorporation of domestic law provisions in the tax treaties and one of these approaches is compatible with Article 26 of the VCLT while the other is incompatible with the same, **the approach compatible with the VCLT provisions is to be adopted.**

DECISION (...continued)

18. **These observations regarding ambulatory** or dynamic **approach** being inappropriate in the context of article 3(2) is **confined to the peculiar facts discussed above**, and, are not, therefore, of general application.

AAR ⇒ Bharti Airtel – 47 ITR(1) 418 (Del-Trib)

CIT v. MSM Satellite (Singapore) Pte. Ltd

[2019] 106 taxmann.com 353 (Bombay)

Compare with Taj TV (DAAE) case

ISSUE 11

- ***Whether distribution charges received by the assessee (a Singapore Co.) for telecasting TV Channels in India would constitute 'royalty' under the Act as well as India-Singapore DTAA?***

RELEVANT PROVISIONS

- **Explanation 2 to section 9(1)(vi)**

"For the purposes of this clause, **"royalty"** means **consideration** (including any lump sum consideration …… **for-**

(v) the **transfer** *of all or* ***any rights*** *(****including the granting of a licence****) in respect of* ***any copyright****, literary, artistic or scientific work including films or video tapes* ***for use in connection with television*** *or tapes for use in connection with radio broadcasting,* ***but not including consideration for the sale, distribution or exhibition of cinematographic films****…*
…."

MSM Satellite (Singapore) Pte. Ltd

FACTS

- The **assessee, a tax resident of Singapore, engaged in the business of operation of TV Channels for exhibition of various programs.**

- An **Indian Co. (namely SET India Private Limited) through layers of multi system operators and cable operators collects subscription charges from individual customers to view the channels and the programs telecasted on such channels. The said subscription charges collected is paid to the assessee after adjustment of intermediary charges paid to the different agencies.**

- The **AO held that these payments made to the assessee are in the nature of royalty for use of copyright**, however **the assessee contended that the same is not in nature of 'royalty, since the assessee had not given any rights to the copyrights'. The plea of the assesse was accepted by the CIT(A) and ITAT.**

DECISION OF THE HIGH COURT

- The Court **referred the definition of copyright defined under Copyright Act, 1957,** and observed that the **term 'copyright' means exclusive right**, subject to the provisions of this Act, **to do or authorise the doing of any of the following acts** specified in the said provision **in respect of a *work* or any substantial part thereof.** Further the **term 'work'** is defined under section 2(y) of the Copyright Act, 1957, as to mean any of the works, namely, a **literary, dramatic, musical or artistic work or a cinematograph film and a sound recording. In view of the above, the Court held that the assessee was not parting with any of the copyrights for which payment can be considered as royalty payment.**

- The **Court rejected the plea of the Revenue that clause (v) of Explanation (2) would be applicable** in the present case, **on the ground that the captioned payment was not for granting any copyrights in any literary, artistic or scientific work.**

- **Further, the Court held that payment would not be 'Royalty' under Article 12 of India-Singapore DTAA.**

EPRSS Prepaid Recharge Services India (P.) Ltd. v. ITO

[2018] 100 taxmann.com 52 (Pune - Trib.)

ISSUE 12

- ***Whether the assessee was liable to withhold taxes at the time making payments to Amazon for 'web hosting charges'?***

RELEVANT PROVISIONS

- **Article 12(3)(b)** of India-USA DTAA

  *"(b) **payments** of any kind received as consideration* **for the use of**, *or* **the right to use**, *any industrial,* **commercial**, *or scientific equipment, other than payments derived by an enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(c) or 3 of Article 8.*

- **Explanation 2 to section 9(1)(vi)**

  "Explanation 2.—For the purposes of this clause, ***"royalty"*** *means* ***consideration*** *(including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains")* ***for*** *–*

  (i)…….

  (iva) the **use** *or* ***right to use*** *any industrial,* ***commercial*** *or scientific* ***equipment*** *but not including the amounts referred to in section 44BB*

RELEVANT PROVISIONS (….. continued)

- Explanation 5 to section 9(1)(vi) inserted by Finance Act, 2012 w.r.e.f 01.06.1976

  "***For the removal of doubts**, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, **whether or not**—*

  *(a) the **possession or control** of such right, property or information is with the payer;*

  *(b) **such** right, property or information **is used directly by the payer**;*

  *(c) the **location** of such right, property or information **is in India**.*

EPRSS Prepaid Recharge Services India (P.) Ltd.

FACTS

- The **assessee, an Indian company,** was engaged in the distribution of recharge pens of various DTH providers. **The assessee made payments to Amazon Web Services (AWS), a tax resident of USA, for web hosting services, without withholding any taxes u/s 195.** Since the **purchase/maintenance and its upkeep of servers required skilled manpower**, which the assessee didn't have, hence **the servers were taken on hire from AWS**, in its cold units.

- During the course of assessment proceedings, the **AO** disallowed the said payment **u/s 40(a)(i)**, o the ground that these **charges were in the nature of use of commercial equipment's (i.e. a server) within the meaning of amended section 9(1)(vi) read with Explanation 2 and Explanation 5 having retrospective effect and thus took the nature of royalty**.

- The **CIT (A) upheld the order of AO in holding that the payment made by assessee** is covered by the term **"Royalty"** as per amended provisions of **Explanation 2 clause (iva) of section 9(1)(vi).**

EPRSS Prepaid Recharge Services India (P.) Ltd.

DECISION OF TRIBUNAL

- The Tribunal **held that the fees paid by assessee was for use of the technology driven services and cannot be said to be for use of infrastructure/servers (i.e. a equipment)**, which stands proven by the fact that charges being not fixed but variable i.e. it varies with the use of technology driven services and also use of such **services does not give rise to any rights in property of AWS and consequently, Explanation under section 9(1)(vi) of the Act is not attracted.**

- The Tribunal observed that **even if the retrospective amendment is held to be applicable, the case of assessee of payment to Amazon being outside the scope of said Explanation 2 (iva) to section 9(1)(vi),** cannot make the assessee liable to deduct tax at source.

- The Tribunal held that **once the payments were released in FY 2009-10 and 2010-11**, or shown to have been accrued to Amazon, then even though there was a **retrospective amendment by insertion of Explanation 5 to section 9(1)(vi), payments already made could not be withdrawn as this would be an impossible act to perform.** Reliance was placed on the decision of Bombay HC in case of **NGC Networks (India) (P.) Ltd.** [IT Appeal No. 397 of 2015, dated 29-1-2018] and **Cello Plast** [2012] 209 Taxman 617.

- The Tribunal held that **retrospective amendment to the definition of "royalty" would not affect the provisions of the India USA DTAA** and hence **Explanation 5 would not have any bearing while interpreting the provisions of the DTAA**. Reliance was placed on the decision of Madras HC in case of Skycell Communications Ltd. [2001] 119 Taxman 496 (Mad.) (para 20)

EPRSS Prepaid Recharge Services India (P.) Ltd.

DECISION OF TRIBUNAL

TREATY - MERITS

- The Tribunal observed that any **payment for use of right to use any commercial equipment would be taxed as per the DTAA, only if the position and control of server/ server space (i.e. equipment) was possessed by the assessee, which was not the case in the present situation**. Hence the Tribunal held that as per the DTAA, **the assessee would not be required to withhold taxes at the time of making payment for web hosting charges.**

Note:- Similar view has been adopted by the Tribunal (Mumbai Bench) in case of Rackspace, US Inc. [2020] 113 taxmann.com 382 (Mumbai - Trib.)

Kingfisher Airlines Ltd. v. DDIT (IT)

[2019] 110 taxmann.com 311 (Bangalore - Trib.)

ISSUE 13

- ***Whether payment made by Indian Airlines Co. to foreign aviation academies (in Dubai, Germany and Singapore) for training its pilots and cockpit crews outside India (which also include training through airplane simulators), could be taxed as FTS/Royalty?***

RELEVANT PROVISION

READ ALL ROYALTY & ALL FTS

- **Explanation 2 to section 9(1)(vi)**

*"For the purposes of this clause, **"royalty" means consideration** (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") **for**—*
(i)…….
…….
*(iv) **the imparting of any information concerning technical**, industrial, **commercial** or scientific knowledge, experience or skill*
*(iva) the **use or right to use any industrial, commercial or scientific equipment** but not including the amounts referred to in section 44BB;….."*

RELEVANT PROVISION

- **Explanation 2 to section 9(1)(vii)**

  *For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the **rendering of any managerial, technical or consultancy services** (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".*

- **Article 12(3) and Article 12(4)** of India-Germany DTAA

  *"3. The term **"royalties"** as used in this Article means **payments** of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematograph films or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, **or for the use of**, or the **right to use**, industrial, **commercial or scientific equipment**, or for information concerning industrial, commercial or scientific experience.*

  *4. The term "fees for technical services" as used in this Article means **payments of any amount** in **consideration** for the **services of managerial, technical or consultancy nature**, including the provision of services by technical or other personnel, but does not include payments for services mentioned in Article 15 of this Agreement."*

no more available

Kingfisher Airlines Ltd.

RELEVANT PROVISION

- **Article 12(3) and Article 12(4)** of **India-Singapore DTAA**

  *"3. The term **"royalties"** as used in this Article means **payments** of any kind received as a consideration for **the use of, or the right to use** :*

  (a) …….;

  *(b) any **industrial, commercial or scientific equipment**, other than payments derived by an enterprise from activities described in paragraph 4(b) or 4(c) of Article 8.*

  *4. The term **"fees for technical services"** as used in this Article **means payments** of any kind to any person in **consideration for services** of a **managerial, technical or consultancy nature** (including the provision of such services through technical or other personnel) if such services :*

  (a)……..

  *(b) **make available** technical knowledge, experience, skill, know-how or processes, which enables the person acquiring the services to apply the technology contained therein ; or*

  (c)……..

- **Article 12(3)** of India-UAE DTAA

  *"3. The term **"royalties"** as used in this Article means **payment** of any kind received as a **consideration for the use of**, or the right to use, any copyright of literary, artistic or scientific work, including cinematography films, or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or **for the use of, or the right to use, industrial, commercial or scientific equipment**, or for information concerning industrial, commercial or scientific experience but do not include royalties or other payments in respect of the operation of mines or quarries or exploitation of petroleum or other natural resources.*

NO FTS ARTICLE

Kingfisher Airlines Ltd.

FACTS

- The **assessee, an Indian Co. engaged in airlines business, made payment to certain foreign companies (based in UAE, Germany and Singapore) for training its pilots and cockpit crews outside India (which also include training through airplane simulators), without deducting taxes u/s 195**.

- The **training facilities** were located **outside India** and the **training and payment were made outside India.** The **assessee** claimed that the **training given by these foreign Co. were part of their normal business routine and the training did not entail any transfer of technology** and by relying on the **Supreme Court** ruling in case **of Ishikawajima Harima Heavy Industries Ltd.** v. DIT [2007] 158 Taxman 259/288 ITR 408 (SC), the assessee further contended that **there was no territorial nexus between the service rendered and India as the services were neither rendered in India nor utilized in India**, and hence the services rendered by the foreign academies were not taxable in India.

- During the course of the **survey proceedings**, the **AO observed** that the **payments consist of two components**, namely a. **Charges for usage of simulators** and b. **Charges for trainers, instructors etc**. The AO observed that the **main purpose of the agreements**, was to **lease the simulators to the assessee**, which also includes the charges of instructors and trainers. The AO thus held that payments for **usage of simulators and the charges for imparting training/instructions would be in nature of royalty under clause (iva) and (iv) of Explanation 2 to section 9(1)(vi)**. Further, with respect **to payment for instructors and trainers** the **AO also held** that the same would be in nature of **fees for technical services under the Act as well under the DTAA.**

Kingfisher Airlines Ltd.

FACTS (…….continued)

- The AO observed that as per **Explanation to section 9(2),** income in nature of **FTS/Royalty would be taxable in India notwithstanding the fact** that the **non-resident service provider** did not have a **place of business in India or the services had been rendered outside India. Further the AO also observed that the services were utilized in India. Accordingly he passed the order's u/s 201 and 201(1A) for AY 2007-08 and AY 2008-09.**

- **Observation of CIT(A) – W.r.t Dubai Entity**
- The **CIT(A)** held that **charges for usage of simulators could not be treated as royalty since the usage of simulator could not really be regarded as usage of a 'scientific equipment'.** The CIT(A) opined that the term 'scientific equipment', has to be interpreted in the context in which it is used. The CIT(A) also observed that though when considered in isolation, the payment **can loosely be regarded** as usage of scientific equipment, for considering payment as **towards royalty**, **however tests such as the uniqueness and non-availability elsewhere etc. of the scientific equipment, needs to be taken into consideration, otherwise even payment outside India towards purchase of a mobile, laptop or usage of internet will also have to be regarded as usage of scientific equipment which ultimately require it to be considered under payment towards royalty.**

- **W.r.t Charges for trainers, instructors etc. the CIT(A) held that the same would be in nature of FTS** and thus the business income which could not be taxed in absence of a PE in India. and FTS article in the Treaty

FACTS (…….continued)

- **Observation of CIT(A) – W.r.t Singapore & German Entity**
- The CIT(A) by relying on the **decision of AAR in case of Intertek Testing Services India (P.) Ltd., (307 ITR 418) (AAR),** held that payment for training of pilots and cabin crew was FTS since **it was in nature of imparting skills, knowledge and technical know how to the crew members of the assessee.**

Kingfisher Airlines Ltd.

DECISION OF TRIBUNAL

- **Departmental Appeal – W.r.t Dubai entity**
  - The **Tribunal upheld the order of CIT(A) w.r.t charges for simulator fees**, by observing that **flight simulator was an essential part of the training** and **the fact that separate hourly fees for using the same is charged did not mean that the assessee was hiring the same** or getting a right to use the same.
  - **W.r.t charges for trainers, instructors** the Tribunal held that in **absence of any specific clause governing FTS**, the same would be construed as business income and hence **would not be taxed** in India in **absence of a PE. The Tribunal relied on the decision of ABB FZ-LLC [2016] 75 taxmann.com 83 (Bang. -Trib.)**
- **Assessee Appeal - W.r.t German and Singapore Entity for payments in nature of training charges**
  - The Tribunal observed that CIT(A) **upheld the order of the AO** solely on the ground of **insertion of an explanation for retrospective amendment to the section 9 from 1.6.1976.**
  - The Tribunal held that **tax withholding obligation cannot be fastened on the assessee on the basis of a retrospective amendment to the law**, which was not in force when the payments were made by the assessee.
  - The **Tribunal relied on the decision in case of Delhi HC in case of Asia Satellite Telecommunications Co. Ltd v. DIT [2011] 9 taxmann.com 168, Tribunal - Mumbai Bench in case of Sonata Information Technology Ltd v. Dy. CIT [2012] 25 taxmann.com 125 and Channel Guide India Ltd. v. Asstt. CIT [2012] 25 taxmann.com 25, Hyderabad Bench in case of Infotech Enterprises Ltd. v. Addl. CIT [2014] 41 taxmann.com 364 and Bangalore Bench in case of TTK Prestige Ltd. v. ACIT [IT Appeal No. 1257 (Bang) of 2011.**

Majestic Auto Ltd. v. CIT

[2019] 110 taxmann.com 261 (Punjab & Haryana)

ISSUE 14

- ***Whether payment made to a foreign company for supply of technical designs, drawings and specification would be taxable as Royalty as per the Act as well as under the erstwhile India-Austria DTAA?***

RELEVANT PROVISIONS

- **Article VI** of erstwhile **India-Austria DTAA**

  "(2) In this Article, the term ***"royalty"*** *means any royalty of other like* ***amount received as consideration*** *for the* **right to use** *copy-rights, artistic or scientific works, cinematographic films, patents,* ***models, designs, plans,*** *secret processes or formulae, trademarks* ***and other like properties or rights.***

- **Explanation 2 to section 9(1)(vi)**

  For the purposes of this clause, **"royalty" means consideration** (including any lump sum consideration …… for—……

  (i) the **transfer of all or any rights** *(including the granting of a licence) in respect of … model,* **design***….*

  (iii) **the use** *of any patent, invention, model,* **design***, secret formula or process or trade mark or similar property ;*

Majestic Auto Ltd.

FACTS

- The **assessee, a Indian Co.,** entered into an **agreement** with an **Austrian Co.** whereby the **assessee** was **granted an exclusive individual right and a license to use manufacturing related information to be supplied by the said Austrian Co. for the purpose of manufacturing and selling vehicles in India.**

- As per the agreement, **the Austrian Co. supplied the requisite drawings, designs, specifications, processes, schedule and all other relevant technical details and documents to the assessee** for which the assessee paid an amount of 3 Million Austrian Schilling.

- Further **the agreement contained another clause**, whereby the **assessee would pay royalty to the Austrian Co. once the production started**, the quantification of the said amount **was based on the quantum of the vehicles produced by the assessee.**

- **The assessee sought an income tax clearance certificate u/s 195(2), from the AO for making the lump sum consideration without deducting any taxes on the ground that the captioned payment was made for 'supply' of drawings, designs etc., and not for their 'use',** which was **denied by the AO on the ground that even payment for supply of designs, drawings specifications etc. would be in nature of royalty and hence tax was liable to be deducted.**

Majestic Auto Ltd.

FACTS

- The **CIT(A) held that the said payments would not be in nature of royalty**, on the ground that the payments made to the Austrian Co**. were only in respect of drawings and designs and not for any services rendered in India** and accordingly upheld the plea of the assessee.

- However, the **Tribunal** held that there is **no difference between the term 'supply' and 'use' of designs, drawings, specifications etc. and accordingly held that the captioned payments were 'royalty' liable for tax withholding.**

DECISION OF THE HIGH COURT

- The Court held that the term royalty **would mean payments made to an owner for the ongoing use of its assets or property such as patents or natural resources for its business purposes.**

- The Court placed reliance on the decision **of Supreme Court in case of Entertainment Network (I) Ltd. v. Super Cassette Industries Ltd.,** [2008] 13 SCC 30, wherein the Supreme Court had defined the term 'royalty' as ***"the remuneration paid to an author in respect of the exploitation of a work, usually referring to payment on a continuing basis rather than a payment consisting of a lump sum in consideration of acquisition of rights.".***

- The Court also placed reliance on the decision of Supreme Court in case of **State of H. P. v. Raja Mahendra Pal, [1999] 4 SCC 43** which defined the term 'royalty' as "***a payment reserved by the grantor of a patent****, lease of a mine or similar right, and payable proportionately to the use made of the right by the grantee, which shall on payment of money, but may be a payment in kind being the part of the produce of the exercise of the right.'(excerpts taken from the Supreme Court on Words, Phrases and Legal Expressions (Judicially defined) 1950-2015 Volume III."*

- Further the Court also placed reliance on the Oxford Advanced Learner's Dictionary, whereby the term 'royalty' was defined to *'**a sum of money** that is paid by an oil or mining company **to the owner** of the land **that they are working on**'.*

DECISION OF THE HIGH COURT

- The High Court observed that **the Austrian Co. had merely authorized its use to the taxpayer, however its actual use would arise only on commencement of production and that would be the stage at which royalty would become payable.**

- Further, **the Court also observed that the Tribunal had given an unnatural meaning to the term 'supply', (i.e. there is no difference between 'supply' and 'use').** The Court also held that based on the agreement, **the actual use of the said drawings, designs etc. would start only when the only when production and sale commenced** and at that point of time it would be construed as 'use' of drawings, designs etc.

- Accordingly, the **Court held that payments for supply of designs, drawings, specifications etc. was not in nature of royalty.**

NOT ON 2 considerations but favourable on tut/supply of design

- Davy Ashmore India – 190 ITR 626 (Cal) (UK)
- Creative Industry – 827.com 356 (Guj) (US)
- Parsons Brinkerhoff – 24 SOT 341 (Del) [THAILAND ACT]
- Other ITAT

John Deere India (P.) Ltd. v. DDIT (IT)

[2019] 102 taxmann.com 267 (Pune - Trib.)

ISSUE 15

- ***Whether web-based training services provided to assessee's employees by its foreign associate company, which did not involve transfer of any technical knowledge, experience, skill, know-how, would be in nature of FTS under the Act as well under the India-USA DTAA?***

RELEVANT PROVISIONS

- Explanation 2 to section 9(1)(vii)

"For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) ***for the rendering of any managerial, technical or consultancy services*** *(including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries"."*

John Deere India (P.) Ltd.

FACTS

- Relevant extracts from Memorandum of Understanding to the India-USA DTAA

  "Typical categories of services that generally involve either the development and transfer of technical plants or technical designs, or making technology available as described in paragraph 4(b), include :

  1. Engineering Services…

  2. ……

  9. Technical Training

John Deere India (P.) Ltd.

FACTS

- The **assessee, an Indian Co., is engaged in software development services and IT support services.**

- During the year under consideration, the assessee had made **various payment to its U.S.A. based associate company Deere & Co**. for SAP License, email facility, disk storage and other system expenses, software charges and system updating charges, **training charges etc.**

- During the course of assessment proceedings, the **AO** held that the payment made by the assessee for obtaining **training fees was in nature of FTS under** the Act as well as under the India USA DTAA and accordingly the assessee **disallowed the said expenses for non-deduction of taxes u/s 40(a)(i).**

- The **assessee** contented that the **training fees were not FTS**, since nothing was being **made available** by way of technical knowledge, experience, skill, know-how or process.

DECISION OF THE TRIBUNAL

- The **Tribunal observed that the training fees paid by the assessee, was not case of interactive session and it was akin to reading an article or book and even if the person availing services had a query, there was no facility to answer the same on web.**

- The Tribunal held that since the **training availed by employees of assessee were web based services available on internet and no technical knowledge was being imparted by service provider** and the Revenue has failed to demonstrate that the services did involve transfer of technology, **it cannot be said to be payments in the nature of FTS under the India-USA DTAA.**

Spencer Stuart International BV v. DCIT

[2019] 108 taxmann.com 47 (Mumbai)

ISSUE 16

- ***In case of a Dutch company, who had entered into two separate agreements with its Indian subsidiary, i.e. a) for granting a right to use software owned by it and b) to render executive search services, whether the payment for executive search services could be considered as fees for technical services under Article 12(5)(a) of India-Netherlands DTAA, being ancillary and subsidiary to the rights to use software (the income from which was offered to tax as Royalty income)?***

RELEVANT PROVISION

- **Article 12(5)** of India-Netherlands DTAA

  *"5. For purposes of this Article, **"fees for technical services"** means payments of any kind to any person in consideration for the rendering of any **technical or consultancy services** (including through the provision of services of technical or other personnel) if such services :*
  *(a) are **ancillary and subsidiary** to the **application** or enjoyment of the **right, property or information** for which a payment described in paragraph 4 of this Article is received; **or***
  *(b) **make available** technical knowledge, experience, skill, know-how or processes, or consist of the development and transfer of a technical plan or technical design."*

FACTS

- **Article 12(4)** of India-Netherlands DTAA

  "4. The term "royalties" as used in this Article means payments of any kind received as a ***consideration for the use of, or the right to use****,* ***any copyright*** *of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience."*

Spencer Stuart International BV

FACTS

- **The assessee, a tax resident of Netherlands, had a wholly owned subsidiary in India.** The **assessee was engaged in the business of executive search services as well as providing Spencer Stuart Technology software and related services to its group concerns worldwide and third party franchisees.**

- The **assessee** had entered into the following **two types of agreements**, which generated income by way of **executive fees and license fees to the assessee**:
  a. **Service Agreement –** Pursuant to which, the assessee agreed to provide **support services in relation to executive search assignments** to the subsidiary company (i.e. Indian Co.); and
  b. **License Agreement** – Pursuant to which, the **subsidiary had been granted license to use trademark, trade name, logos** and the right to use the **software** owned by the assessee.

- **Income from License Agreement** was **offered to tax as royalty** under the Act as well as under the tax treaty.

- **W.r.t Service agreement**, the assessee treated the same as **business income not taxable in India in absence of a PE in India**. The assessee claimed that the said income was **not** taxable as **FTS** under **Article 12(5)** of the tax treaty since the said services neither '**made available**' any technical knowledge, experience, skill, know-how or process nor did it constitute development and transfer of a technical plan or technical design. The assesse also contented that **executive search services were not ancillary or subsidiary to the property rights for which license fees was paid.**

FACTS (…..continued)

- The **AO** concluded the assessment proceedings by holding that **executive search fee** was to be treated as **FTS u/s 9(1)(vi)**. Further, the AO also held that such **fee was for services which are ancillary and for the application or enjoyment of the right for which the 'license agreement' was entered into (income from which was offered to tax as Royalty)** and, **therefore, though it was in terms of a separate 'service agreement' yet it constituted FTS in terms of Article 12(5)(a)** of the DTAA.

- **Alternatively**, the AO also held that it **was to be treated as royalty under Article 12(4) of the DTAA read with clause (iv) of Explanation 2 to Section 9(1)(vi) of the Act on the alleged ground that the executive search fee was paid for using SS's (Spencer Stuart's) worldwide client list database, SS's mailing list database, SS's knowledge management resources pages, SS's Board of Director's database and other data base and consequently it was for information concerning industrial commercial scientific experience.**

- The Dispute Resolution Panel (DRP) upheld the order of the AO.

Spencer Stuart International BV

DECISION OF TRIBUNAL

- The **Tribunal, by relying on co-ordinate bench ruling in assessee's own case and the APA entered by the subsidiary**, held that **License Agreement** and **Service Agreement** were **separate and distinct** agreement **constituting different sources of income**, and **hence income from service agreement** could **not** be considered as **ancillary or subsidiary to the license agreement**.

- The **principal business** of the **subsidiary** was to **carry out** or execute the mandate of **executive searches** and **thus** the **executive search fee** generating activities **could not be treated as ancillary or subsidiary to the license agreement.**

- Accordingly the **income from service agreement** would **not** be considered as **fees for technical services under the DTAA.**

- The **Tribunal also rejected the plea of the Revenue** that the executive search fee **could be treated as 'Royalty',** on the ground that the payment has been made for **obtaining a whole range of services for performing the executive search.**

- Further the Tribunal also **rejected the plea of the Revenue** that the said **payments were for using SS's (Spencer Stuart's) worldwide client list database, SS's mailing list database, SS's knowledge management resources pages, SS's Board of Director's database and other data base**, by **observing** that the **said items were part of the License Agreement** for which the TPO has already held to be at arm's length **and hence no further amount be attributed to the License Agreement.**

wrg: principal bus. not as critical as separate & distinct agreement [even if no APA]

Buro Happold Limited v. DCIT

[2019] 103 taxmann.com 344 (Mumbai - Trib.)

ISSUE 17

- ***Whether payment received for development and transfer of a technical plan or technical design would be in the nature of FTS as per Article 13 of the India UK DTAA, irrespective of the fact, whether it 'makes available' technical knowledge, experience, skill, knowhow, etc. or not?***

RELEVANT PROVISION

- **Article 13(4)** of India-UK DTAA

  "4. For the purposes of paragraph 2 of this Article, and subject to paragraph 5, of this Article, the term "fees for technical services" means payments of any kind of any person in consideration for the rendering of any technical or consultancy services (including the provision of services of a technical or other personnel) which :

  (a)……

  …….

  (c) ***make available*** *technical knowledge, experience, skill know-how or processes****, or*** *consist of the* ***development and transfer*** *of a technical plan or technical design."*

Buro Happold Limited

FACTS

- The **assessee, a tax resident of the UK**, is engaged in the **business of providing consulting** and **engineering services** in relation to structural and MEP (Mechanical, Electrical and Public health) designs for buildings.

- The **assessee had a subsidiary in India** (referred as **Buro India**), **which rendered consulting engineering services to its clients**. **However, in areas**, such as master planning, acoustics engineering, environmental engineering, etc., for **which they lacked the expertise, the said services were availed from the assessee.**

- During the year under consideration, the **taxpayer** had **received income for the provision of consulting and engineering services and income on account of cost recharge to Buro India.**

- The **assessee** claimed the **receipt** from provision of consulting and engineering services as **not taxable** in India as per **Article 13** of India UK DTAA **as the consulting and engineering services did not made available technical skills, knowledge etc. to Buro India.**

- However the **AO** held that as per **Article-13(4)(c)**, **payment received for development and transfer of a technical plan or technical design would be** in **the nature of FTS, irrespective of the fact, whether it satisfied the condition of 'make available'** technical knowledge, experience, skill, knowhow, etc., which was **upheld by the CIT(A) on appeal**.

ASSESSEE'S CONTENTION

- The taxpayer contended that the income received for the rendering of consulting and engineering services could be charged to tax as **FTS under Article 13 only** if it **makes available** technical knowledge, experience, skill, know-how or processes **or** consists of the **development and transfer of a technical plan or technical design.**

- The taxpayer alternatively also argued that **even if the amount received from rendering of the consultancy services was attributed to the supply of technical design and drawings, the same could not be treated as FTS** under Article 13 as the second limb of Article 13(4) (c) "**consist of the development and transfer of technical plan or technical design**" cannot be **read disjunctively** from the phrase **"make available technical knowledge, experience, skill know-how or processes"**. Thus, the **condition of making available has to be applied even for the second limb**.

REVENUE'S CONTENTION

- The revenue contented that '**make available**' clause goes with technical knowledge, experience, skill, know-how, etc., but **does not go with the second limb of Article 13(4) (c), i.e., the development and transfer of technical plan or a technical design**. Hence, the amount received for consulting and engineering services would be taxable as FTS.

DECISION OF TRIBUNAL

- The Tribunal perused **Article 13(4) (c)** of India-UK Tax Treaty and held that the words "**or consists if the development and transfer of a technical plan or technical design**," appearing in the second limb **has to be read in conjunction with "make available technical knowledge, experience, skill, know-how or processes**."

- The Tribunal further observed that as per rule of '***ejusdem generis***', the words "**or consists of the development and transfer of a technical plan or technical design" will take color from "make available technical knowledge, experience, skill, know-how or processes.**"

- Accordingly, the Tribunal held that the **supply of project-specific designs/drawings/plans did not make available technical knowledge, experience, skill, know-how or process (since the designs were project specific and cannot be used by Buro India subsequently)** and hence, the same was not taxable in India.

HSBC Bank Plc v. DCIT

[2019] 109 taxmann.com 434 (Mumbai - Trib.)

ISSUE 18

- ***Whether receipt of referral fees from a Group concern in India, by a UK Group entity (i.e. assessee), for referring its client to the said Indian Group concern, would be FTS under the Act as well under the India-UK DTAA?***

RELEVANT PROVISIONS

- Explanation 2 to section 9(1)(vii)

"For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) ***for the rendering of any managerial, technical or consultancy services*** *(including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries"."*

skip

RELEVANT PROVISIONS

- **Article 13(4)** of India-UK DTAA

  4. For the purposes of paragraph 2 of this Article, and subject to paragraph 5, of this Article, the term "fees for technical services" means payments of any kind of any person in consideration for the rendering of any technical or consultancy services (including the provision of services of a technical or other personnel) which :

  (a).....

  .....

  (c) **make available** technical knowledge, experience, skill know-how or processes, or consist of the development and transfer of a technical plan or technical design.

HSBC Bank Plc

FACTS

- The **assessee, a tax resident of UK, is engaged in the business of providing banking and financial services** to individuals and commercial organizations across the world.

- During the year under consideration, **the assessee received referral fees from its Group Co. in India, which was not offered to tax**, as **the assessee contended that the said fees was neither FTS under the Act as well under the India-UK DTAA.**

- The **assessee contented that the said fees** was received for referring its client to a group concern and there was **no element of managerial, technical or consultancy function** discharged by the assessee to be construed as **'FTS'** as canvassed by the AO.

DECISION OF THE TRIBUNAL

- The Tribunal upheld the plea of the assesse by observing that the **referral fees** has been received by the assessee on account of the referral made by assessee for the potential rendering of services by a group concern to the prospective client so referred and **the said activity does not require any managerial, technical or consultancy function to be discharged by assessee.**

- The Tribunal also observed that **the services are akin to commercial services and hence cannot be construed as FTS under the Act.**

Note:- The Tribunal also ruled on the following issues:

a) When the assessee received certain amount from its Indian group entities as reimbursement of expenses, the said receipt cannot be taxed as Fees for Technical Services, since the reimbursement received by assessee was in respect of specific and actual expenses incurred by assessee and it did not involve any mark up.

b) When the assessee received certain amounts as protection fees from its Indian group entities, for a guaranteed portfolio performance, the said receipt cannot be taxed as Fees for Technical Services, since the assessee did not make available the technical knowledge, skills etc. under the India-UK DTAA

Panasonic Corporation v. DCIT (IT)

[2018] 99 taxmann.com 183 (Chennai - Trib.)

ISSUE 19

- ***Whether reimbursement pertaining to salary cost of seconded employees of a Japanese Co. would be FTS?***

RELEVANT PROVISIONS

- Article 12(4) of India-Japan DTAA

*4. The term **'fees for technical services'** as used in this article means **payments** of any amount to any person other than payments to an employee of a person making payments and to any individual for independent personal services referred to in article 14, in **consideration for the services of a managerial, technical or consultancy nature,** **including the provisions of services of technical or other personnel.**"*

Panasonic Corporation

FACTS

- The **assessee, a tax resident of Japan, was engaged in the business of development, production and sale of electrical and electronic products**, systems and components for a wide range of consumer, business and industrial uses.

- The assessee **deputed some of its employees to its subsidiary in India**. The **salary of the employees** of the assessee, who were working for its subsidiary, **were reimbursed by its subsidiary**.

- The **assessee did not offer the receipts of reimbursement it to tax since it was only reimbursement. The TPO held that no adjustment was required on the reimbursable expenditure received by the assessee.**

- The **AO** while passing the draft assessment order held that the assessee rendered services in nature of FTS since the **deputed employees held senior positions who reported to the Vice-Presidents and Presidents, who in turned reported to the assessee and hence the assessee had ultimate responsibility and the direction, control and supervision of the personnel.**

- Further the AO also observed that the **assessee had a lien marked on the deputed employees and the deputed employees would go back to the assessee after employment with the subsidiary.**

Panasonic Corporation

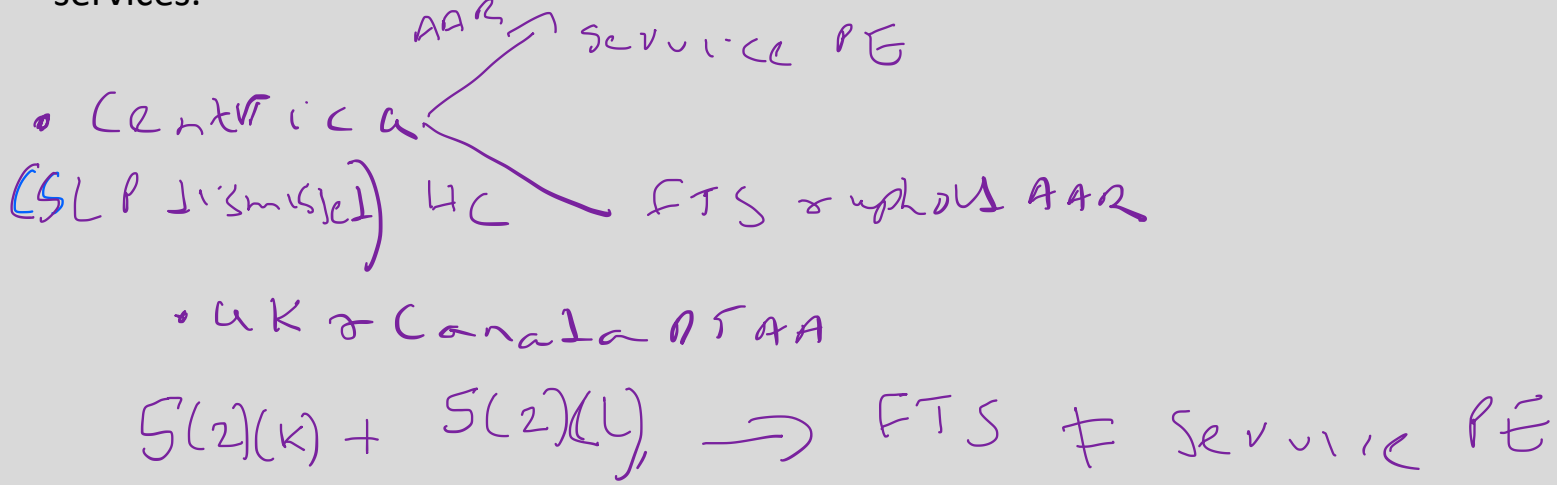
FACTS

- The **DRP upheld the action of the AO** by relying on the decision of Delhi HC in case of **Centrica India Offshore (P.) Ltd.** [2014] 44 taxmann.com 300, wherein it was held that **secondment of employees by a foreign group company would constitute a Service PE** of the foreign group company in India and the services rendered by the seconded empoyees would be in **nature of fees for technical services which** would make available technical skills, knowledge under the India-UK DTAA.

DECISION OF TRIBUNAL

- The **Tribunal upheld the action of the AO by observing that the deputed employees were reporting to the assessee through the Vice Presidents and Presidents and the deputed employees had to work under the direction, control and supervision of the assessee** under the Act as well under the India-Japan DTAA as **it made available technical knowledge to the subsidiary in India**.

- The Tribunal upheld the order of the DRP and also held **since the employees deputed by the assessee were of high level technical executives** and they are **rendering highly technical services to the subsidiary**, the payments for such services would fall within the ambit of fee for technical services.



DCIT (IT) v. IBM India Private Limited

[2018] 100 taxmann.com 230 (Bangalore - Trib.)

ISSUE 20

- ***In absence of a specific Article governing taxation of FTS, whether income in nature of technical services (from provision of IT services) would be taxable under Article 7 or Article 23 or Article 24 of India Philippines DTAA r.w section 9(1)(vii) of the Act?***

RELEVANT PROVISIONS

- **Article 24(1)** of India-Philippines DTAA

  "1. The **laws in force in either of the Contracting States shall continue to govern the taxation of income** *in the respective Contracting States* **except where provisions to the contrary** *are made* **in this Convention.**"

- **Article 23** of India-Philippines DTAA

  "Items of income of a resident of a Contracting State, ***wherever arising, not dealt with*** *in the* ***foregoing Articles*** *of this Convention shall be taxable only in that State."*

IBM India Private Limited

FACTS

- The **assessee company, an Indian Co.,** was **engaged in the business of selling computers, software,** besides rendering software development and information technology services.

- The **assessee required services of expatriate employees of the IBM Business Services, Philippines** (IBM Philippines) for its business projects. The **assessee reimbursed the salary cost of the seconded expatriate employees to the IBM Philippines, without deducting any taxes since it was in nature of reimbursement of expenses.**

- A notice under sec 201(1) and 201(1A) was issued to the assessee, seeking clarification as to why tax was not deducted at source from above mentioned payments made to IBM Philippines.

- The **assessee** contended that **in absence of an article for "FTS" in India Philippines DTAA**, payments **constituted 'business profits' under article 7 of the DTAA and as IBM Philippines did not have PE in India such payments were not taxable in India.** Further, the **assessee also contended that as per Article 23 dealing with 'Other Income' of the DTAA, income of IBM Philippines was taxable only in Philippines and not in India.**

- The **AO,** after considering assessee's contentions held the assessee as **'assessee in default'** for not deducting tax at source **on the basis that** in the **absence of an Article dealing with FTS under the tax treaty, the provisions of Act would apply.**

DECISION OF TRIBUNAL

- The Tribunal **relied** on the decision of Tribunal (Mumbai Bench) in case of **BNB Paribas SA [2013] Tax Corp (AT) 32700**, which dealt with identical clause (i.e. Article 25(1)) India-UAE DTAA which is similar to Article 24(1) of India Philippine DTAA, wherein at was held that the **object of the said provision** was to:
  - **(i) Eliminate double taxation** and it is for this purpose, it has been provided that the 'laws in force' in either of the Contracting States shall continue to govern the taxation of the income unless express provision to the contrary are made in this Agreement.
  - **(ii) To provide for deductions or credit of the taxes paid** in either of the states based on either exemption method or providing for credit for taxes paid in the other country and that Article 25 by itself does not provide any rules on the mechanism for computing relief.

  It is only for such purposes the domestic laws may have to be referred and it cannot be extended to tax business income falling under Article 7 as per domestic law.

- The **Tribunal held that Article 23 begins with the words items of 'income not expressly covered' by provisions of Article 6 to Article 22**. Therefore, the Tribunal held that **if an items of income can be classified under Article 6 to Article 22, whether or not taxable under these articles, would not be covered by Article 23.**

DECISION OF TRIBUNAL

- The Tribunal held that **since the reimbursement received by the assessee, were in the ordinary course of its business, the said receipt is dealt with Article 7** and not Article 23.

- Accordingly , the Tribunal held that **in absence of a PE**, the **reimbursement of salary was not taxable in India.**

NO FTS ARTICLE

1. NEPAL
2. BANGLADESH
3. BRAZIL
4. THAILAND
5. KENYA
6. LIBYA
7. UAE

Morgan Stanley Asia (Singapore) Pte. V. DDIT (IT)

[2018] 95 taxmann.com 165 (Mumbai - Trib.)

ISSUE 21

- ***Whether reimbursement, by an Indian Co., pertaining to salary cost of seconded employees of a Singapore Co. (assessee) would be taxable as FTS under the Act as well as under the India Singapore DTAA?***

FACTS

RELEVANT PROVISIONS

- **Explanation 2 to section 9(1)(vii)**

  "Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) **but does not include** *consideration for any construction, assembly, mining or like project undertaken by the recipient or* **consideration** *which* **would** ***be income of the*** **recipient** ***chargeable under the head*** **"Salaries".”**

RELEVANT PROVISIONS

- Article 12(4) of India-Singapore DTAA

> *"4. The term "fees for technical services" as used in this Article means payments of any kind to any person in consideration for* **services of a managerial, technical or consultancy nature (including the provision of such services through technical or other personnel)** *if such services :*
> *(a) ……. ; or*
> *(b**) make available** technical knowledge, experience, skill, know-how or processes, which enables the person acquiring the services to apply the technology contained therein ; or*
> *……."*

Morgan Stanley Asia (Singapore) Pte.

FACTS

- The **assessee, a resident of Singapore, deputed one of its Director/employee to India for the period from May 2004 to April 2007 to set up Morgan Stanley Advantage Services Private Limited (MSAS) i.e. Indian Co., an associate concern in India.**

- The assessee, as per the terms of contract, agreed to continue paying salary of the employee in Singapore and **cross charged Indian Co. for the same.**

- The **assessee before the AO** claimed that the amount received by the assessee was in the nature of **pure reimbursement of cost** incurred by assessee on behalf of MSAS and **hence no income arose in its hands.**

- The **AO** rejected the assessee's explanation by contenting that the **employee deputed to India was highly qualified and had technical experience and the role of the assessee was more than employer.**

- Hence the **AO** held that amount received by the assessee **was in nature of FTS**. **The TPO made an adjustment on account of the ALP of the mark-up to be charged, computed @ 23.30% on the amount of reimbursement of salaries.**

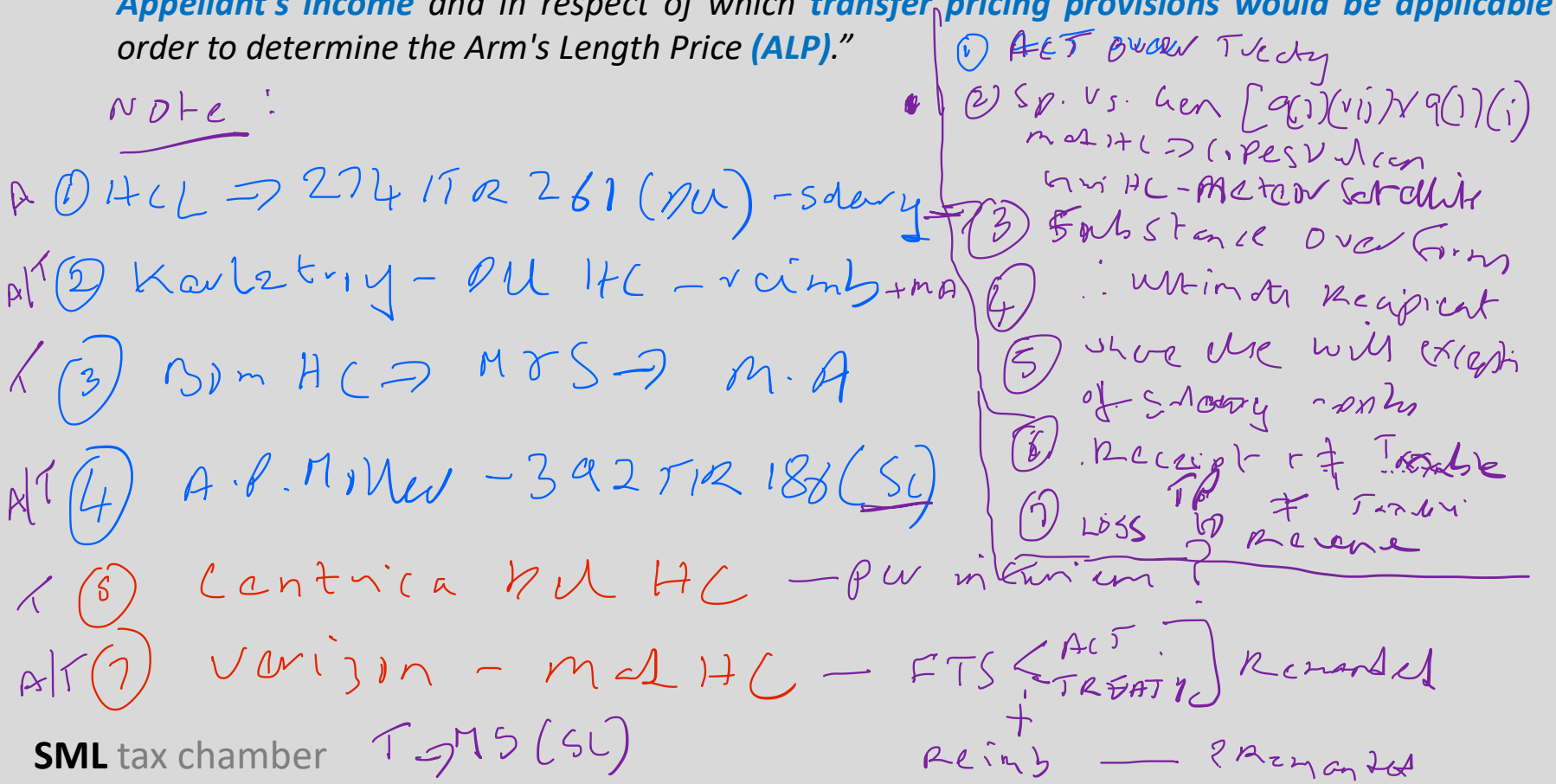
- The CIT(A) upheld the AO's order.

Morgan Stanley Asia (Singapore) Pte.

FACTS

- The following **main ground** was raised by the assessee before the Tribunal:

*"1. Ground No.1: In upholding that the **reimbursement of personnel costs** amounting to Rs. 57,825,175 by Morgan Stanley Advantage Services Private Limtied (MSAS) to the Appellant is the **Appellant's income** and in respect of which **transfer pricing provisions would be applicable** in order to determine the Arm's Length Price **(ALP)**."*



Morgan Stanley Asia (Singapore) Pte.

DECISION OF TRIBUNAL

- The Tribunal held that **payment by India Co. being a pure reimbursement of salary cost**, **would be covered under exception mentioned in explanation 2 to section 9(1)(vii)** and **would not be taxable as fees for technical service under the domestic law.**

- The Tribunal **relied** on **Delhi Tribunal ruling in United Hotels Ltd.** [2005] 2 SOT 0267 (Delhi) wherein it was held that for each deputed person, the amount received by it **is income chargeable under the head "salary"** and therefore, **it cannot be termed as "fees for technical services".**

- Further, the Tribunal observed that **receipt had been taxed as salary in the hands of the employee in India.**

- The Tribunal **relied** on the decision of Tribunal (Mumbai Bench) in case of Mark & Spencer Reliance India (P) Ltd. [2013] 38 taxmann.com 190 (Mumbai – Trib.), wherein it was held that when the seconded employees were deputed for providing assistance in management and set up of business, and worked under direct control, management and supervision of the taxpayer, **the services would not be in nature of FTS under the India-UK DTAA and further the said services would not make available technical skills, know how to the taxpayer.**

- The Tribunal **allowed the main grounds** of the appeal in favor of the assessee and did not adjudicate the balance grounds which had become academic (**once the reimbursement of salaries was not taxable, the corresponding TP adjustment/markup could not be taxed**).

Sofina S.A. v. ACIT

[TS-129-ITAT-2020(MUM)] - ITA No.7241/Mum/2018

ISSUE 22

- ***Whether capital gains on transfer of shares of a Singapore Co. (holding 99.99% shares of an Indian Co.) by a Belgian resident would be taxable in India or Belgium?*** [Spore Co has no other asset]
- ***Whether indirect transfer provision in Explanation 5 to section 90(1)(i) can be read into the DTAA, in absence of similar provisions in the DTAA itself?***

RELEVANT PROVISIONS

- **Section 9(1)(i) and Explanation 5** of the Act

"9(1) The following incomes shall be deemed to accrue or arise in India :—

(i) ***all income accruing or arising, whether directly or indirectly****, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or* ***through the transfer of a capital asset situate in India."***

Explanation 5.—For the removal of doubts, it is hereby clarified that an asset or a capital asset being any ***share or interest in a company*** *or entity registered or* ***incorporated outside India*** *shall be* ***deemed*** *to be and shall always be deemed to have been* ***situated in India****, if the* ***share or interest derives****, directly or indirectly,* ***its value substantially*** *from the assets located in India"*

Sofina S.A.

RELEVANT PROVISION

- **Article 13** of India-Belgium DTAA

  *"1. **Gains derived** by a resident of a Contracting State from the **alienation of immovable property** referred to in Article 6 and situated in the other Contracting State may be taxed in that other State.*

  *2. **Gains from the alienation of movable property** forming **part of the business property of a permanent establishment** which an enterprise of a Contracting State has in the other Contracting State or of movable property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or together with the whole enterprise) or of such fixed base, may be taxed in that other State.*

  *3. **Gains from the alienation of ships or aircraft** operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State of which the alienator is a resident.*

  *4. Gains from the **alienation of shares of the capital stock of a company**, the **property of which consists directly or indirectly principally of immovable property** situated in a Contracting State may be taxed in that State.*

  *5. Gains from the **alienation of shares other than those mentioned in paragraph 4**, forming part of a participation of **at least 10 per cent of the capital stock of a company which is a resident of a Contracting State** may be taxed in that State.*

  *6. Gains from the alienation of any **property other than that** mentioned in paragraphs 1, 2, 3, 4 **and 5 shall be taxable only in the Contracting State of which the alienator is a resident.**"*

Belgium

Sofina S.A.

FACTS

- The **assessee, a tax resident of Belgium**, subscribed to the **preference shares of a Singapore Co.** totalling to **11.34%** of its total shareholding. Further, **Singapore Co. in turn held 99.99%** of the total shareholding of an **Indian Co.**

- The **assessee sold its entire stake in Singapore Co. (i.e. 11.34%) to Jasper Infotech Pvt. Ltd. (a tax resident of India). Jasper Infotech Pvt. Ltd.** while discharging the consideration for the above mentioned transaction, **withheld taxes u/s 195. The assessee filed its return of income declaring NIL income as per the provisions of Article 13(6) of India-Belgium DTAA. As per Article 13(6), gains from alienation of the said shares would be taxable in the state of the alienator i.e. Belgium.**

- The **AO** concluded the assessment proceedings by holding that the Singapore Co. did not had any other assets except for its investment in the Indian Co. and thus the **shares of Singapore Co. derived their value substantially from the shares of Indian Co. and hence the transfer of shares of Singapore Co. would be taxable in India in terms of explanation 5 to section 9(1)(i).**

- Further, the AO held that by virtue of the deeming fiction created by explanation 5 to section 9(1)(i), the shares of Singapore Co. were deemed to be situated in India and **consequently the Singapore Co. was deemed to be a tax resident of India. In view of the same, the AO applied Article 13(5) of the relevant DTAA to conclude that the transfer would be taxed in India.** The assessee filed objections before the DRP, however the DRP upheld the order of the AO.

ASSESSEE'S CONTENTION BEFORE THE TRIBUNAL

- The assessee contended that deeming fiction created by **Explanation 5 to section 9(1)(i) deems shares of a foreign company to be situated in India and does not deem that the company itself becomes a resident in India.**
- The assessee also contended that Explanation 5 to section 9(1)(i) was inserted in the statute by Finance Act, 2012 w.r.e.f 01.04.1962, **however in absence of any similar amendments in the India-Belgium DTAA or India-Singapore DTAA, such amendments cannot be read into the said DTAA's.**
- Accordingly, it was argued that the **Article 13(5) would not be applicable as it explicitly provides that the company whose shares are to be transferred should be a resident of either of a contracting states i.e. either Belgium or India.**

REVENUE'S CONTENTION BEFORE THE TRIBUNAL

- The **Revenue placed reliance on the order of the AO** and argued that **the fact pattern** of the captioned transaction **bought the transaction within the ambit of Article 13(5)** read with Explanation 5 to section 9(1)(i)

Sofina S.A.

DECISION

- The Tribunal relied on the decision of **Andhra Pradesh HC in case of Sanofi Pasteur holding SA (2013) 30 taxmann.com 222 (Andhra Pradesh) and observed that as per Article 13(5) gains from alienation of shares in a company can be taxed in the State in which the said company is resident** only if the following two conditions are satisfied viz.
  a. **participation of at least 10%** in the capital stock of company; and
  b. the **company whose** shares are transferred **should be a resident of a contracting state**

- Since the **shares transferred** by the assessee in the present case were of **Singapore Co.**, the pre-condition that the shares transferred should form part of the capital stock of a company which is a resident of a **Contracting State i.e. India was not fulfilled** and hence **Article 13(5) would not be applicable in the present case**.

- **Explanation 5 of section 9(1)(i) incorporates a 'see through' approach** i.e. if a person holds shares outside India, which, directly or indirectly, derives its value substantially from the assets located in India, the legislation deems such shares located outside India to be located in India for taxation purposes. However a similar '**see through' approach is not envisaged in Article 13(5) of the relevant DTAA** and hence it cannot be deemed that the above mentioned transaction results in the transfer of shares of Indian Co.

JCIT v. Merrill Lynch Capital Market Espana SA SV

[2019] 112 taxmann.com 119 (Mumbai - Trib.)

ISSUE 23

- ***Whether gains on transfer of shares of an Indian company engaged in real estate development business would be taxed in India as per Article 14(4) of India-Spain DTAA, which inter alia provides that gains on alienation shares of company, which results in transfer of rights/control over the underlying immovable property, would be taxed in the State where the immovable is situated?***

RELEVANT PROVISION

- **Article 14(4)** of India-Spain DTAA

  *"4. Gains from the **alienation of shares** of the capital stock of a **company the property of which consists**, directly or indirectly, **principally of immovable property** situated in a Contracting State may be taxed **in that State**."*

  *5. Gains for the **alienation of shares** of the capital stock of a company **forming part of a participation of at least 10 per cent** in a company which is a resident of a Contracting State may be taxed in that Contracting State.*

  *6. Gains from the **alienation of any property other than that mentioned in paragraphs 1, 2, 3, 4 and 5** shall be taxable only in the Contracting State of which the **alienator is a resident.***

Merrill Lynch Capital Market Espana SA SV

FACTS

- The **assessee, a tax resident of Spain held ~7% stake in six Real Estate companies** in India forming part of the BSE realty index. During the year under consideration, the assessee **earned capital gains on sale of ~2% stake in such companies**.

- The **AO** concluded the assessment proceedings by holding that the **said companies were dealing** in **real estate sector** including development of properties, residential as well as commercial, **and the share value was derived from the immovable properties held by it.**

- Accordingly the **AO** held that **gains on transfer of shares** of the said companies **would be taxable in India as per Article 14(4)** of the India Spain DTAA, which inter alia provides that that gains on alienation shares of company, which results in transfer of rights/control over the underlying immovable property, would be taxed in the State where the immovable is situated.

- On appeal, the **CIT(A)** upheld the contention of the assessee, that provision of **Article 14(4)** would **not** be **applicable in** the present case, **since there is no indirect transfer of ownership of immovable properties by transfer of these shares.**

Merrill Lynch Capital Market Espana SA SV

CONTENTION OF THE ASSESSEE

- The assessee contended that the **stake** in such companies was **~7%,** hence there was **no effective rights/control to occupy the immovable properties of such companies. As per UN Model Convention commentary, the provisions of Article 14(4) come into play only in case of indirect transfer of ownership of immovable property by transfer of shares owning these properties, which was not the case in the present situation.**

CONTENTION OF THE REVENUE

- The Revenue contended that the **listed companies were dealing in real estate sector** including development of properties, residential as well as commercial, and **the share value was derived from the immovable properties held by it, hence the transfer would be taxable under Article 14(4).**

- Whether such immovable properties are held by such companies as investments or stock-in-trade was immaterial for bring the said transactions under the ambit of Article 14(4).

Merrill Lynch Capital Market Espana SA SV

DECISION OF TRIBUNAL

- The Tribunal held that interpretation of **Article 14(4)** must essentially remain **confined to the shares effectively leading to control or which gives the right to enjoy the underlying immovable property owned by the company, and such property is what the company principally holds.**

- The Tribunal also observed that all these **listed companies were engaged in the business of real estate development** rather than in the business of holding real estate as investments and **their business model is focused on gains from real estate development rather than gains from holding the immovable properties.**

- The Tribunal observed that the expression **"principally" is not specifically defined in the DTAA**, and drawing support from **various commentaries of Model Convention**, interpreted threshold for the term **"principally" as 50% or more of the aggregate value of assets.**

- Further, the Tribunal also observed that the AO **did not** bring any **material to prove that such companies were "principally" holding the immovable properties.** The Tribunal also mentioned that **merely because a company is dealing in real estate development, it does not imply that over 50% of its aggregate assets consist of immovable properties.**

Merrill Lynch Capital Market Espana SA SV

DECISION OF TRIBUNAL

- In view of the above, the Tribunal held that **since the assessee held ~7% (and transferred ~2%)** stake in the companies, **the question of holding controlling interest or even significant interest in these companies does not arise, and hence Article 14(4) would not be applicable in the present situation.**

- Note:- The Tribunal also ruled on the following issue:-
  a. Where an assessee, a FII, earned gains on account of transaction in foreign exchange, and the said gains were not taxable under Article 7 or under Article 14 of the India-Spain DTAA, the AO cannot tax the said profits under Article 23 i.e. Other Income, since the said gains is expressly dealt with in Article 7 or Article 14.

? what if FCO holds 70% in ICO-vedanta development

GO TO ISSUE SLIDE

DCIT (IT) v. Sri. K.E.Faizal

[2019] 108 taxmann.com 545 (Cochin - Trib.)

ISSUE 24

- ***Whether gains from transfer of units of equity oriented mutual funds listed in India, by a resident of UAE would be taxable in India in light of provisions of Article 13 of India UAE DTAA?***

RELEVANT PROVISION

- **Article 13(3) and 13(4)** of India-UAE DTAA

  "3. Gains from the alienation of shares of the capital stock of a company the property of which consists directly or indirectly principally of immovable property situated in a Contracting State may be taxed in that State.

  4. ***Gains*** *from the alienation of* ***shares*** *other than those mentioned in paragraph 3* ***in a company which is a resident of a Contracting State may be taxed in that State.***

  5. Gains from the alienation of any property ***other than that referred to in paragraphs 1, 2, 3 and 4*** *above shall be taxable only in the Contracting State of which* ***the alienator is a resident.****"*

Sri. K.E.Faizal

FACTS

- The assessee, a tax resident of UAE, transferred units of equity oriented mutual funds listed in India.

- The **assesse** filed return of income in India by claiming **gains** from transfer of units of equity oriented mutual fund as **not taxable in India by virtue of Article 13(5)** of the India UAE DTAA, which inter alia provides that **gains on alienation of any property (other than gains resulting from alienation of shares of a company) would be taxable in the state in which the alienator is a resident i.e. UAE** in the present case.

- The **AO** concluded the assessment proceedings by holding that that the underlying **instrument of an equity oriented mutual fund was a share** and consequently, as per **Article 13(4)** of the DTAA, which inter alia provides that **gains from alienation of the shares would be taxed in the State in which, the company whose shares are sold, is a resident, i.e. India** in the present case.

- On appeal, the CIT(A), by relying on the decision of Tribunal (Mumbai Bench) in case of **Satish Beharilal Raheja [2013] 37 taxmann.com 296/145 ITD 29 (Mum. - Trib.)**, held that gains would not be taxable in India as the equity oriented mutual funds are not shares and therefore Article 13(5) of the Treaty (and not Article 13(4)) would be applicable.

DECISION OF TRIBUNAL

- The Tribunal observed that the term, **'share' is not defined under the DTAA** and accordingly the term needs to be understood from a **domestic law** of the contracting state.

- As per the provisions of **Securities and Exchange Board of India (Mutual Funds) Regulations, 1995, mutual funds in India can be established only in the form of 'trusts' and 'not companies' and hence it can be inferred that shares and units of mutual funds are two different types of securities.**

- The Tribunal upheld the order of the CIT(A) and held that **gains arising from sale of units of mutual funds (and not shares) are not liable to tax in India in view of Article 13(5)** of the DTAA.

BID SERVICES DIVISION (MAURITIUS) LTD., In Re

[2020] 114 taxmann.com 434 (AAR-Mumbai) (AAR No. 1270/2011)

ISSUE 25

- ***Whether capital gains exemption under the India-Mauritius DTAA could be denied to a Mauritius Co., when it was formed just 2 weeks before making a bid resulting in purchase of shares of an Indian Co., which subsequently resulted to the impugned capital gains?***

NB: Shares acquired prior to 2017

RELEVANT PROVISION

- **Article 13 of India-Mauritius DTAA**

"1. Gains from the alienation of immovable property, ……

2. Gains from the alienation of movable property forming part of the business property ……

3. Notwithstanding the provisions of paragraph (2) of this article, gains from the alienation of ships and aircraft operated in international traffic……

*3A. Gains from the **alienation of shares acquired on or after 1st April 2017** in a company which is resident of a Contracting State may be taxed in that State.*

3B. However, the tax rate on the gains referred to in paragraph 3A of this Article …….

*4. Gains from the alienation **of any property other than that referred to in paragraphs 1, 2, 3 and 3A** shall be taxable only in the Contracting State of which the alienator is a resident.]*

5. For the purposes of this article, the term "alienation" means the sale, exchange, transfer, or relinquishment of the property or the extinguishment of any rights therein or the compulsory acquisition thereof under any law in force in the respective Contracting States.

***Paragraph 4 substituted** by Notification No. SO 2680(E) {NO.68/2016 (F.No.500/3/2012-FTD-II)}, dated 10-8-2016, **w.e.f. 1-4-2017 (Assessment Year 2018-19)**. **Prior to its substitution**, said paragraph read as under :*

*"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."*

Bid Services Division (Mauritius) Ltd.

FACTS

- The **assessee, a wholly owned subsidiary of a South African Co.**, was a **tax resident of Mauritius** and a part of the **Bidvest Group (based out in South Africa)**.

- **Airports Authority of India ('AAI') floated a tender inviting bids** for undertaking development, **operation and maintenance of Mumbai Airport.**

- **Initially,** a **consortium consisting** of **GVK Industries Limited, Airports Company South Africa (ACSA) Limited, Old Mutual Life Assurance Company and Bidvest Group Limited made a joint bid against the said tender.**

- In the above backdrop, **subsequently the assessee was incorporated in Mauritius** and **two weeks thereafter**, a **final binding bid** was submitted by the **assessee in consortium** with **GVK Airports** Holding Pvt. Ltd. ('GAHPL') and **ACSA** Global Limited ('AGL') and **the said bid was selected by AAI on 4th February, 2006 whereby each parties to the consortium were joint venture partners.**

- A **shareholders agreement** dated **4th April, 2006 between AAI and the JV partners** was executed for governing the rights, obligations and shareholding pattern in the JV (an Indian Co.). The **assessee** agreed to **subscribe and acquire 27 %** of the paid up share capital of the said JV.

FACTS (…continued)

- **Subsequently**, the **assessee** entered into a **share purchase agreement** on **1st March, 2011 with GAHPL** for transferring its shares, held in the JV, to GAHPL in **AY 2012-13**.

- The assessee sought **ruling from the AAR** in respect of its **tax exemption** claim on capital gains arising on transfer of shares held in the JV (i.e. the Indian Co.), in light of the provisions of **Article 13(4) of the India-Mauritius DTAA** ('DTAA'), since it was a **tax resident of Mauritius and held a valid TRC.**

Finding @ pg 125

Bid Services Division (Mauritius) Ltd.

ASSESSEE'S CONTENTION

- The assessee contented that capital gains would not be taxable in India in view of **Article 13(4)** of the DTAA which inter alia provides that gains from alienation of shares would be taxable in the contracting state in which the alienator is a resident i.e. Mauritius in the present case.

- The assessee placed reliance on **Circular No. 789 dated 13th April, 2000** issued by the Central Board of Direct Taxes ('CBDT') which clarified that **companies resident of Mauritius would not be taxable on income arising from transfer of capital assets, being shares of a domestic company, in India as per Article 13(4) of the DTAA.**

REVENUE'S CONTENTION

- The **Revenue** predominantly contended **that the entire arrangement lacked commercial substance and was aimed towards avoiding payment of taxes** in India in view of benefit of Article 13(4), **since at the time of bidding for the tender, the consortium did not include the assessee as a joint venture partner**; the assessee was acting as a **conduit company for routing the funds** for its Group and further the **assessee was incorporated just two weeks prior to the submission of the final** binding bid by the consortium (i.e. after the final screening of all the bidders to the tender).

DECISION

- The **AAR** held that the **assessee was not entitled to the benefit under Article 13(4)** of the India-Mauritius DTAA **since the entire arrangement lacked commercial substance and its dominant purpose was to avoid taxes.**

- The AAR relied on the **OECD Commentary** (2014 version), wherein it has been provided that benefits of **DTAA should not be available where the main purpose of the arrangement is to secure a more favorable tax position or for obtaining tax benefits**, to observe that assessee was interposed in order to obtain the India-Mauritius DTAA and the main purpose of the arrangement was to obtain a tax benefit.

- Further the AAR also **relied** on the **decision of Supreme Court in case of Vodafone Holdings International v. UOI [2012] 17 taxmann.com 202 (SC)**, to observe that **DTAA benefits could be denied if the main purpose of the arrangement is tax avoidance, notwithstanding the fact that the assessee produces a valid TRC for availing DTAA benefits.**

DECISION (……continued)

- The **AAR relied on the following factual matrix**, while coming to the above conclusion:-

  - **Assessee was incorporated just two weeks before the final bid** was submitted to the AAI.
  - **All the pre-bidding activities** such as site visits, discussion with Government agencies, filing of technical and financial bids etc. **were done by consortium (the assessee was not in existence at that point in time).**
  - Assessee didn't provide any **cogent reasons or commercial rationale for incorporating it in Mauritius.**
  - **Assessee** was a **shell company without** any **tangible assets, employees, office space, financial background, experience or other skills** to facilitate the business venture of the JV.
  - **Assessee** was used as a **conduit for routing the funds for its holding company (i.e. company incorporated in South Africa) and the beneficial owner of the shares of the JV was the holding company of the Applicant.**

Indostar Capital v. ACIT (IT)

[2019] 105 taxmann.com 96 (Bombay)

FROM PAYER'S PERSPECTIVE

ISSUE 26

- ***Whether an application u/s 197, for NIL withholding certificate, could be denied to a Mauritius Co. merely on the surmise that the transaction of transferring shares of an Indian Co. (shares purchased prior to 01.04.2017) is a scheme for avoidance of taxes under the garb of India-Mauritius DTAA?***

FACTS @ PG. 129

RELEVANT PROVISIONS

- **Article 13** of India-Mauritius DTAA

  "1. Gains from the alienation of immovable property, …….

  2. Gains from the alienation of movable property …….

  3. Notwithstanding the provisions of paragraph (2) of this article, gains from the alienation of ships and aircraft …….

  *3A. Gains from the **alienation of shares acquired on or after 1st April 2017** in **a company which is resident** of a Contracting State **may be taxed in that State.***

  *3B. However, the tax rate on the gains referred to in paragraph 3A of this Article and arising during the period beginning on **1st April, 2017** and ending **on 31st March, 2019** shall* not exceed 50% *of the tax rate applicable on such gains in the State of residence of the company whose shares are being alienated;]*

RELEVANT PROVISIONS (……continued)

*4. Gains from the **alienation of any property** other than that referred to in paragraphs 1, 2, 3 and 3A shall be taxable only in the Contracting State of which the **alienator is a resident.***

***Paragraph 4 substituted by** Notification No. SO 2680(E) {NO.68/2016 (F.No.500/3/2012-FTD-II)}, dated 10-8-2016, w.e.f. 1-4-2017 **(Assessment Year 2018-19)**. **Prior to its substitution**, said paragraph read as under :*

*"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**.*

Indostar Capital

FACTS

- The assessee, **a tax resident of Mauritius** holding a Category-1 Global Business License issued by the Financial Services Commission of Mauritius to act as an investment holding company. It was **formed to promote an Indian non-banking financial company namely Indostar Capital Finance Limited ('ICFL')** and **made investment in 7.13 crore equity shares of ICFL** (which was 97.30% of its share capital) **prior to 01-04-2017** in a span of 4 years.

- The assessee sought to sell **1.85 crore shares of ICFL through an IPO for a total consideration of more than INR 1000 crore**. The made any **application** before the AO for the grant of a **NIL withholding certificate** under section **197**. **In this application**, the assessee **placed before** the AO its **corporate structure**, **the source of funds for acquisition of the shares and several documents including a copy of its TRC.**

- The **AO** carried out a **detailed inquiry** and passed an order **rejecting the said application**, on the **ground that transaction was not genuine**, created to avoid taxes, considering the **following factors**:
  - **No business activities had been carried apart from making the above mentioned investment in ICFL and advancing a loan to Everstone Capital Limited.**
  - **The assessee did not maintain any establishment / incur any administrative expenses and it did not had any employees in Mauritius.**
  - **The shares of the assessee were held by eight equity funds and no details of the same, including TRC's, were provided to demonstrate the genuiness of the transaction.**

FACTS(…..continued)

- An order was passed authorizing the payment after deducting tax at source. Aggrieved, the assessee filed a writ petition before the Bombay High Court.

DECISION OF HIGH COURT

- The Court held that **as per Article 13(4) of the India-Mauritius DTAA** as it stood at the relevant time, the **capital gain arising out of the sale of shares of Indian company acquired on or before 31.3.2017 could be taxed, if at all, in Mauritius i.e. it could not be taxed in India**. The Court also took note of the **CBDT Circular, which had clarified that TRC will constitute sufficient evidence for accepting status of the residence as well as beneficial ownership for applying the DTAA. Further the Court held that the said CBDT circular issued in exercise of powers u/s 119(2) would bind the Revenue.**

- The HC observed that the **Revenue is not precluded from denying tax treaty benefits, if it is established, on facts, that the transaction was an artificial tax avoidance scheme or an artificial device, pre-conceived with the sole object of tax avoidance.**

- The Court observed that the **AO did not have any sufficient prima facie material to demonstrate that the entire transaction from the inception was sham, colorable device and a bogus transaction to simply avoid tax** and held that **mere fact that the assessee had not transacted any other business by itself may not be conclusive proof to accept AO's contention.**

- The Court further observed that the **extent of administrative expenditure and the employment structure may be some of the factors to determine whether a transaction is sham or not**, **however by themselves they may not be sufficient, and such held that all these aspects could and need to be dealt at the time of assessment proceedings.**

DECISION OF HIGH COURT (…… continued)

- The Court also noted that a **mere fact that the assessee has not transacted any other business by itself, non-production of TRC of the companies which hold shares in the assessee company, would not be conclusive that the transaction is sham or colorable**, but the same also cannot be a ground against the assessee **unless there was adverse material on record**.

- The Court observed that a **certificate issued u/s 197, provides an immunity to the payer** from being declared a deemed defaulter, **however, the proceedings u/s 197 would not decide the taxability of the certain receipts in the hands of the payee** and the **Revenue can always in normal assessment bring the income to tax if otherwise permissible in law.**

- The **Court observed that the question of deducting tax at source would arise only if the income in the hands of the payee is taxable**.

- Accordingly, the Court (i) q**uashed the order rejecting the application** filed by the asssessee (ii) **directed the AO to issue certificate under section 197 stating that there is no requirement to deduct TDS** (iii) gave **direction to release the TDS amount already deposited** by the payer and (iv) directed the assesse to **continue to hold minimum 50 lakhs shares of ICFL (having valuation of 200% of the disputed tax amount), so as to protect the interest of Revenue.**

Poddar Pigments Ltd. v. ACIT

[2019] 107 taxmann.com 422 (Delhi - Trib.)

individuals

ISSUE 27

- ***Whether scientific services rendered by Swiss scientists to assessee-company, would be covered under Article 14 which deals with independent personal activities, read with Article 12(5)(b) of India Swiss DTAA?***

RELEVANT PROVISIONS

- **Article 12(4)** of India-Swiss Confederation DTAA

  "4. For purposes of this Article the term "fees for technical services" means ***payments*** *of any kind to any person in consideration for the* ***rendering of any managerial, technical or consultancy services****, including the provision of services by technical or other personnel."*

ND MFN clause

- ***Article 14(1)*** *of India-Swiss Confederation DTAA*

  "1. Income derived by a ***resident*** *of a Contracting State in respect of* ***professional services or other activities of an independent character*** *shall be taxable* ***only in that State*** *except in the following circumstances, when such income may also be taxed in the other Contracting State :"*

- Fixed base – regularly available or
- his stay in India > 183 days in 12 month period

14(2) ⇒ prof. services include... scientific activity

Poddar Pigments Ltd.

FACTS

- The **assessee, an Indian Co.,** is engaged in the **business of manufacturing** of master batches and engineering plastics compounds.

- During the year under consideration, the **assessee had** made **payment of technical fees to non-resident scientists**, namely, Dr. Werner Stibal and Mr. Hans Peter Meyer, **without withholding any taxes as per Article 14** of India-Swiss Confederation DTAA.

- During the course of assessment proceedings, the **AO** held that the payment made by the assessee were in nature of **FTS covered by Article 12 of the DTAA** and accordingly disallowed the said expenditure u/s 40(1)(i) of the Act. The action of the AO was upheld by the CIT(A)

- Before the Tribunal, the Revenue relied on the decision of Supreme Court in case of GVK Industries Ltd. v. ITO [2015] 54 taxmann.com 347, Delhi HC decision in case of DIT v. Rio Tinto Technical Services [2012] 17 taxmann.com 70 and Centrica India Offshore (P.) Ltd. v. CIT [2014] 44 taxmann.com 300, in support of its contention that the payments were FTS.

DECISION OF THE TRIBUNAL

- The Tribunal observed that as per Article 12(5)(b) of the DTAA, professional services which are covered in Article 14 i.e. Independent Personal Services and Article 15 i.e. Dependent Personal Services, would not be covered under Article 12 governing FTS.

- Article 12(5) of India Swiss Confederation DTAA is reproduced as under:

  "(5) Notwithstanding paragraph 4, "fees for technical services" does not include amounts paid:
  (a) for teaching in or by educational institutions;
  *(b) for **services covered by Article 14** or Article 15, as the case may be.."*

- The Tribunal distinguished the three precedents relied by the Revenue, as in the present case (unlike in the precedents relied by Revenue), the scientific services rendered were independent in nature, which would specifically fall under Article 14 of the DTAA.

- The Tribunal accordingly held that since the services being scientific services would be considered as professional services, covered by Article 14.

∴ specific vs General

Hydrosult Inc.

[2019] 103 taxmann.com 193 (Ahmedabad - Trib.)

ISSUE 28

- ***Whether payments in nature of technical/consultancy services, paid to independent contractors from Canada and other countries would fall under Article governing Fees for Technical Services (i.e. Article 12 or 13 of the respective DTAA's) or would fall under Article 14 i.e. dealing with Independent Personal Services?***

RELEVANT PROVISION — INDEPENDENT PERSONAL SERVICES

- **Article 14(1)** of India-Canada DTAA

  *"1. Income derived by an individual or a firm of individuals (other than a company) who is a resident of a Contracting State in respect of **professional services** or **other independent activities** of a similar character shall be taxable only in that State. However, in the following circumstances, such income may be taxed in the other Contracting State, that is to say :*
  *(a) if he has or had **a fixed base regularly available** to him in the other Contracting State for the purpose of performing his activities; in that case only so much of the income as is attributable to that fixed base may be taxed in that other Contracting State; or*
  *(b) if his **stay in the other Contracting State** is for a period or periods amounting to or exceeding in the **aggregate 183 days** in the relevant fiscal year; or*

RELEVANT PROVISIONS

*(c) if the **remuneration for the services** in the other Contracting State is **either derived from residents of that other Contracting State** or is borne by a permanent establishment which a person not resident in that other Contracting State has in that other Contracting State and such remuneration exceeds two thousand five hundred Canadian dollars ($2,500) or its equivalent in Indian currency in the relevant fiscal year."*

- Article dealing with Independent Personal Services in DTAA's with **Germany** (threshold of **120 days**), **Philippines** (threshold of **183 days**), **UK** (threshold of **90 days**), **Australia** (threshold of **183 days**) and **New Zealand** (threshold of **183 days**) is materially the same (except for the threshold and other condition for the short stay exemption) with India-Canada DTAA.

- **Article 12(5)(e)** of India-Canada DTAA

  "*5. Notwithstanding paragraph 4, 'fees for included services' **does not include amount paid** :*
  (a)…….
  *(e) to an employee of the person making the payments or to any individual or firm of individuals (other than a company) **for professional services as defined in Article 14.***

- **Similar exclusion** clause i.e. Article 12(5)(e) of India-Canada DTAA, is present in **DTAA's with Philippines, UK, Australia and New Zealand.**

Hydrosult Inc.

FACTS

- The **assessee, a foreign company incorporated in Canada, was engaged in providing technical consultancy for development of irrigation** and water resources in **India in the State of Chhattisgarh and Orissa.**

- The **assessee** was awarded **contract by Chhattisgarh Government** for providing consultancy services under the **Chhattisgarh Irrigation Development Project**. It **had its PE in Raipur.**

- During the year under consideration, the **AO** noted that the **assessee had claimed consultancy expenses on which taxes were not withheld.**

- **Assessee** contended that the **consultancy fees were paid to several independent professionals of foreign origin hired for technical services and the services were in the nature of independent personal services (IPS) governed by Article 14 of the respective DTAA** and not taxable in India **since the conditions for taxability under Article 14 were not fulfilled.**

- The **AO** concluded that taxes should have been withheld since the contractors **were not independent** and thus the said **expenses were disallowed**.

Hydrosult Inc.

ASSESSEE'S CONTENTION

- The assessee contended that that the **professionals rendering services** had **neither fixed base in India (source country) nor had any of the professionals stayed in India more than the threshold limit in terms of number of days (aggregate 90/183 days) of stay provided in the respective DTAA and they are independent professionals of foreign origin.**

REVENUE'S CONTENTION

- The AO contented that the **services rendered were admittedly technical/consultancy services by the professionals who are stated to be specialists in their respective domains and therefore,** the services were in the nature of technical and consultancy services and would thus fall in the article related to **FTS**.

- The AO also contended that the **professionals rendering consultancy services were not independent per se and their scope of work and activities were regulated by contractual obligations or other form of employment.**

- Thus, the **services** were in the nature of **FTS** and **not IPS.**

DECISION OF TRIBUNAL

- the **Tribunal perused the specimen agreement** entered into between the assessee and one of the consultants and observed that, the **contractors has been contracted as an 'Advisor' for providing consulting services related to the project to the assessee.**

- The Tribunal noted that the **responsibility or the risk for the results of the work was with the contractors** to a greater degree, moreover the **obligations arising from the contract could not be assigned to some other persons unlike in the case of an employer.**

- The Tribunal upheld the plea of the assessee, that the **contractors providing IPS did not have a fixed base** available to them in **India** and **none** of them have **stayed in India** for a period **exceeding** aggregate **183 days** in the AY concerned, and **hence** would **not be taxable in India** by virtue of Article 14 of DTAA with the respective country (i.e. Canada and other countries) where the respective contractors were residents.

ACIT v. Grant Thornton

[TS-10-ITAT-2019(DEL)]

ISSUE 29

- ***Whether Article 15 dealing with Independent Personal Services would be applicable to partnerships also?***

RELEVANT PROVISIONS

- **Article 15(1) of India-UK DTAA**

"1. Income derived by an **individual**, **whether** *in his own capacity or as a* **member of a partnership**, ***who is a resident of a Contracting State*** *in respect of* ***professional services*** *or* ***other independent activities of a similar character*** *may* ***be taxed in that State***. ***Such income may also be taxed in the other Contracting State if such services are performed in that other State and if*** *:*

(a) ***he is present in that other*** *State* ***for a*** *period or periods aggregating to* ***90 days*** *in the relevant fiscal year ; or*

(b) ***he****, or the* ***partnership****,* ***has a fixed base regularly available to him****, or it, in that other State for the purpose of performing his activities;*

but in each case only so much of the income as is attributable to those services."

RELEVANT PROVISIONS

- **Article 15(1) of India-USA DTAA**

  *"1. Income derived by a person who is an **individual** or* **firm of individuals** *(other than a company) who is a resident of a Contracting State from the performance in the other Contracting State of professional services or other independent activities of a similar character shall be taxable only in the first-mentioned State except……."*

- **Article 14(1)** of **India-Netherlands DTAA**

  *"1. Income derived by a **resident** of one of the States in respect of professional services or other activities of an independent character shall be taxable only in that State except in the following circumstances,……."*

- **Article 4(1)** of **India-Netherlands DTAA**

  *"1. For the purposes of this Convention, the term "resident of one of the States" means any **person** who, under the laws of that State, is liable to tax therein by reason of his domicile, residence,……."*

- **Article 3(1)(e)** of **India-Netherlands DTAA**

  *"the term "person" **includes** an individual, a company, any other body of persons and **any other entity** which is treated as a taxable unit, under the taxation laws in force in the respective States……."*

covers P-ship also

RELEVANT PROVISIONS

- **Article 15** of **India-France DTAA**
  *"1. Income derived by an individual or a **partnership of individuals** who is a resident of a Contracting State from the performance of professional services or other independent activities of a similar character shall be taxable only in that Contracting State……."*

FACTS

- The **assessee a partnership firm was engaged in providing international accountancy and advisory services to various clients in India and abroad**. The assessee had made **payments for professional fees to non-residents firms, without withholding any taxes on the same.**

- During the course of assessment proceedings, **the AO sought to disallow the said payments u/s 40(a)(i) on the premise that services rendered is in the nature of Fees for technical services and would not be covered under Article 15 i.e. Independent Personal Services on the ground that this Article would be applicable only to individuals and not to partnership firms.**

- It was contended by the **assessee** that the said payments are covered by **Article 15 "Independent Personal Services"** of respective DTAA and **in absence of any fixed base of the recipient in India, income was not chargeable to tax in India.**

- The **CIT(A)** held that the payments would be covered by **Article 15** of the respective DTAA and accordingly **payments received by individual or partnerships would be taxed in country of residence.**

DECISION OF TRIBUNAL

- The Tribunal **upheld the CIT(A)'s observation** that in the case of **DTAA's with USA, UK and France**, it is unambiguously provided that **Article 15** on "Independent Personal Services" **would be applicable to the following:**
  - **an individual or firm of individuals;**
  - **an individual, whether in his own capacity or as a member of a partnership**
  - **an individual or partnership of individuals.**

- Further, w.r.t **India-Netherlands DTAA**, the Tribunal **upheld the order of the CIT(A)**, that Article on "Independent Personal Services" would be applicable **to any person** (which included a partnership firm) **who is a resident of a Contracting State**.

- The term '**resident**' under India-Netherlands DTAA would mean any **person who**, under the laws of that State, **is liable to tax** therein by reason of his domicile, **residence** etc.

- Further, '**person**' has been defined to include an **individual**, a company, any other body of persons and any **other entity** which is treated as a taxable unit, under the taxation laws in force in the respective States."

Golden Bella Holdings Ltd. v. DCIT

[2019] 109 taxmann.com 83 (Mumbai - Trib.)

ISSUE 30

- ***Whether an assessee, who had entered into a back-to-back arrangement whereby it received funds from its Parent Co. for making investment, in the form of CCD's, in another Group Co., would be considered as a 'beneficial owner' of interest income under the India-Cyprus DTAA?***

RELEVANT PROVISION

- **Article 11(2)** of India-Cyprus DTAA

  "2. However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, ***but if the beneficial owner*** *of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 percent of the gross amount of the interest."*

Golden Bella Holdings Ltd.

FACTS

- The **assessee, a tax resident of Cyprus**, was **incorporated** with the objective of undertaking business activities of an **investment holding company**. The assessee was a **wholly owned subsidiary of a Mauritius Co.** and further the **Mauritius Co. also held 99.5% in an Indian Co.**

- The **assessee** had made **investments**, in the form of **CCD's, in Indian Co.** and had **earned interest** income on such CCD's. **The investment were made by the assesse from its own funds (i.e. share capital infused by the Mauritius Co.) and from the unsecured interest free loan received from Mauritius Co. (loan received a week before making the investments in Indian Co.)**

- The assessee filed its tax return and the said interest income was offered to tax at a reduced rate of 10% in accordance with Article 11 of the India Cyprus DTAA.

- The **AO** passed a draft order by denying benefit of reduced rate of tax under the DTAA on the ground that the **assessee was not the 'beneficial owner' of the interest income received from Indian Co. The AO observed that, the assessee was acting as a conduit for the passage of funds between its shareholder i.e. Mauritius Co. and Indian Co.**

- The DRP upheld the order of the AO and following the same, the AO crystallized the assessment proceedings

Golden Bella Holdings Ltd.

CONTENTION OF THE ASSESSEE

- The assesse contented that the **assessee was the sole owner of the interest income and was under no contractual, legal, or economic obligation to pass on the interest income** it received to its immediate shareholder, **or to its ultimate parent**, or to any other entity.

- The assesse further contented that, **the fact that the investment was funded using shareholder loan and equity does not ipso facto, mean that corporate status may be disregarded.**

- The assessee further **relied on CBDT Circular No. 789** to content that **TRC issued by the tax authorities of Cyprus** in its name would be a **sufficient basis** for determining **'beneficial ownership'**, of interest income.

CONTENTION OF THE REVENUE

- The Revenue contended that **investment made** by the assessee in the Indian Co. **is a back-to-back loan transaction** out of the funds received from its immediate parent company, i.e., the Mauritius Co. and hence **the assessee was a conduit company incorporated for passing the funds from the Mauritius Co. to the Indian Co.**

- The assesse was not carrying any business activities other than the investment made and hence was just a name plate company.

DECISION OF TRIBUNAL

- The Tribunal held that the **assesse would** be **eligible for the DTAA benefits** on the following grounds:-

  - The **assessee applied for CCD's using a portion of the share capital and the interest free loan and was still left with a reasonable cash balance.**

  - The **assessee** invested in CCD's and **received interest for its own exclusive benefit** and not on behalf of any other entity. **The transactions between the parties could not be considered as a back-to-back transaction lacking economic substance.**

  - The **AO could not establish that the assessee was constrained by a contractual, legal or economic arrangement with any third party with respect to the interest income received.**

  - The **assessee maintained the foreign exchange risk on CCD's (as they were denominated in INR), and counter-party risk on interest payment arising on the CCD's**.

M.CD ⇒ Int Income as per India tax rate ie 40% in this case
Ltd Cyprus – Beneficial owner
Today M.CD_INDIA Intact tax rate – 7.5%.

40%
LIBYA
GREECE
EGYPT

Mohinder Singh Sanghera v. ADIT (IT)

[2019] 101 taxmann.com 274 (Chandigarh - Trib.)

ISSUE 31

- ***Whether an assessee who made advance payments for a real estate property with an assured return on the said advance payment till possession is received, was a financial transaction and thus whether the assured return would be 'interest' under Article 12 of India UK DTAA?***

RELEVANT PROVISIONS — INTEREST

- **Article 12(2) and Article 12(5)** of India UK DTAA

  "2. However, **such interest may also be taxed in the Contracting State** in which it arises and accordingly to the law of that State, provided that where the resident of the other Contracting State is the beneficial owner of the interest **the tax so charged shall not exceed 15 per cent of the gross amount of the interest**……."

  *"5. The term **"interest"** as used in this Article means income from **debt-claims of every kind**, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from Government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures but, subject to the provisions of paragraph 9 of this Article, shall not include any item which is treated as a distribution under the provisions of Article 11 (Dividends) of this Convention."*

Vs. Other Income

Mohinder Singh Sanghera

FACTS

- The **assessee, a tax resident of UK, had invested in a real estate project by making 95% of the sale consideration as advance payment. In lieu of the said advance payment, the assessee was assured a monthly return till the time the possession of the commercial space was handed over. Taxes @15% on the said monthly return was withheld by the developer as per India-UK DTAA** at the time of making payment to the assessee.

- The **AO** sought to **reopen the assessment** for the captioned year and asked the assessee to file the return of income. **The assessee filed its return of income, by offering the assured return as interest income taxable @ 15% as per Article 11 of the DTAA.**

- The **AO held that the assured return is akin to return on investment made in the property and hence not in nature of interest income and accordingly the same would be taxed as 'income from other sources'. The Action of the AO was upheld by the CIT(A).**

DECISION OF THE TRIBUNAL

- The Tribunal perused **the allotment letter issued by the developer and observed that until and unless the conveyance deed was registered in the name of the assessee, the assessee would not have any rights in the property and the amounts paid by the assessee would be a token payment which shall not be construed as having any interest or lien over the property.**

- In view of the, the tribunal observed that **the assured return would not be in nature of return on investment, but the advance payment would be in nature of a debt claim** and consequently any returns on the said debt would be in **nature of interest income**, which has been rightly offered to tax by the assessee.

AGR Matthey of Western Australia

[TS-356-ITAT-2019(Mum)]

ISSUE 32

- ***In a case where Letter of Credit (LC's) is issued by Indian Co. to Foreign Co. (i.e. the assessee) who receives interest on the same, whether the said interest received by the Foreign Co. would be taxable as income from other sources without allowing deduction for discounting charges paid by the Foreign Co. on the said LC's or would the same be business income and not taxable in the absence of a PE in India?***

RELEVANT PROVISION

- **Section 2(28)**

  *"(28A) "interest" means **interest** payable in any manner in respect of any **moneys borrowed** or **debt incurred** (including a deposit, claim or other similar right or obligation) and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised "*

  GO TO FACTS

- **Article 11(1), Article 11(2) and Article 11(3)** of India-Australia DTAA

  "1. Interest arising in one of the Contracting States, being interest to which a resident of the other Contracting State is beneficially entitled, may be taxed in that other State.

RELEVANT PROVISION (…….continued)

*2. Such interest **may also be taxed in the Contracting State** in which it arises**, and according to the law of that State,** but the tax so charged shall not **exceed 15 per cent of the gross amount of the interest.”***

*3. The **term "interest"** in this Article **includes** interest from Government securities or from bonds or debentures, whether or not secured by mortgage and whether or not carrying a right to participate in profits, and **interest from any other form of indebtedness as well as all other income assimilated to income from money lent by the law**, relating to tax, of the Contracting State in which the income arises, but does not include interest referred to in paragraph (1) of Article 8.*

- **Section 56(1)**

  *“56. (1) **Income of every kind** which is **not to be excluded from the total income under this Act** shall be chargeable to income-tax under the head **"Income from other sources", if it is not chargeable to income-tax under any of the heads specified in section 14, items A to E.***

- **Section 57(iii)**

  “The income chargeable under the head "Income from other sources" shall be computed after making the following deductions, namely :—

  (i)……

  *(iii) any other **expenditure** (not being in the nature of capital expenditure) **laid out or expended wholly and exclusively** for the **purpose of making or earning such income**;*

AGR Matthey of Western Australia

FACTS

- The **assessee, a tax resident of Australia, sold gold/bullion to PEC Ltd. ('PEC'), an Indian Government entity, against issuance of letters of credit (LC).**

- During the year under consideration, **PEC issued LC's against the supply of gold** by the assessee, which are accepted through the assessee's bankers in Australia. **The assessee was entitled to charge an interest on the LC's at the rate LIBOR +0.5% margin p.a. Further, the assesse discounted the said LC's (within a day or two) with the bankers in Australia and paid discounting charges which were equivalent to the interest earned on LC's from PEC.**

- The return of income was filed by PEC, as a representative assessee of the assessee, and **declared the interest on LC's** issued by PEC as **"interest income"** and **claimed an equivalent amount of discounting charges paid to bankers in Australia as deduction** against the said interest income.

- The **AO disallowed the claim of the discounting charges on the LC's** discounted and **taxed the entire interest income under the head "Income from Other Sources" under the Act and under Article 11(2) of the India-Australia DTAA, which was upheld by the CIT(A)** on further appeal.

ASSESSEE'S CONTENTION

- The assessee contended that the **interest on LC is a notional interest income**, as the **said interest was never received by the assessee**, but the same is received by its bank through which the assessee discounted the LC.

- The assesse contended that **usance and discounting of LC pertained to the sale transaction undertaken by the assessee** and the interest cost is always considered as a **part of purchase cost since it facilitates the transaction of sale of bullion**. Accordingly, the assessee argued that the same **would be considered as the business income** of the assessee, **not taxable in India in absence of a PE**, as opposed to the action of AO and CIT(A) wherein the said notional interest has been taxed as income from other sources.

- The assesse placed **reliance on the decision of Supreme Court in case of Cocanada Radhaswami Bank Ltd. (1965) 57 ITR 306 (SC) and the decision of Delhi HC in case of Cargill Global Trading (P.) Ltd. (2011) 11 Taxmann.com 219 (Del.)** to press the claim that such interest partakes of the character of the purchase price itself and could not have been put to tax under the residual head of income from other sources.

- The assessee also contended that, in order **invoke Article 11(2),** the interest income has **to first satisfy the taxation under the domestic laws (i.e. referring to the phrase 'and according to the law of that State' appearing in Article 11(2))**. Since the said interest was not taxable under the domestic laws as interest income u/s 2(28A), Article 11(2) cannot be invoked.

REVENUE'S CONTENTION

- The Revenue contented that the **nature of income would be 'income from other sources'** and not as "Profits and gains of Business and Profession", **as the assessee itself has claimed the same as interest income in the return of income.**

- The Revenue contended that the **assessee would not be entitled to claim deduction of discounting charges under Article 11(2)**, as the said Article i.e. 11(2) prescribes that the interest income would be taxed on a **gross basis and not on a net basis (by referring to phrase "15 per cent of the gross amount of the interest.").**

- The Revenue further contended that the assessee would not be **eligible to claim the deduction u/s 57** for discount charges under the Act also, since the said **expenses are incurred in Australia i.e. outside India.**

- The Revenue also contended that **in the absence of a PE**, neither the assessee is eligible to be taxed **on a net basis nor the expenses incurred by it outside India are allowable as expenses.**

DECISION OF TRIBUNAL

- The Tribunal noted that there was **no interest credit arising to the assessee as the LC's were discounted with the bankers at Australia within two days of issuing the LC**, and hence the interest itself was notional since it was never received by assessee.

- The Tribunal further observed that **the interest was in the context of a transaction of high-seas sale of bullion, a part of the cost of such bullion itself,** and could **not** be taxed under the head '**income from other sources**' as contended by the Revenue. Reliance in this regards was placed on the decision of **SC in case of Cocanada Radhaswami Bank (supra) and Delhi HC in case of Cargill Global Trading (supra).** The Tribunal held that the **relevant receipt was not covered under the definition of interest u/s 2(28A)** and hence, could not be taxed as income from other sources under the Act.

- Further the Tribunal also observed that the **Revenue had conveniently relied upon the Assessee's own claim of declaring the impugned interest as 'interest income'', without noting** that this is a case where the **claim were made not by the assessee but by a representative assessee.**

- The Tribunal also observed that the **Revenue had failed to point out as to how the condition prescribed under Article 11(2) (i.e. referring to the phrase 'and according to the law of that State') was fulfilled, since the impugned interest was not interest u/s 2(28A) of the Act as held above.**

- Further, the Tribunal held that as per Article 7 of India Australia DTAA, **no tax liability** can be determined **in the absence of a permanent establishment** in India.

Glencore International AG v. Dalmia Cement (Bharat) Ltd.

[2019] 110 taxmann.com 48 (Delhi)

ISSUE 33

- ***Whether damages for breach of contract and interest thereon, paid to a Swiss Co. in consequence of an international arbitral award are taxable in India?***

RELEVANT PROVISIONS

- Article 22 India-Swiss Confederation DTAA

"1. Items of income of a resident of a Contracting State, **wherever arising**, **not dealt** *with in the foregoing Articles of this Agreement* ***shall*** *be taxable only in that State*

…….

3. ***Notwithstanding the provisions of paragraph 1****, if a* ***resident*** *of a Contracting State* ***derives income from sources within the other Contracting State*** *in the form of lotteries, crossword puzzles, races including horse races, card games and other games of any sort or gambling or betting* ***of any form or nature whatsoever, such income may be taxed in that other Contracting State****."*

Glencore International AG v. Dalmia Cement (Bharat) Ltd.

FACTS

- **Glencore International AG ("Glencore"), a Swiss Co., initiated international arbitration proceedings against Dalmia Cement ("Dalmia"), a Indian Co., for breach of contract and received an award in its favour.**

- The **Award comprised** of (i) **damages for breach of contract**; (ii) **legal costs** incurred by Glencore, (iii) the **costs of the arbitration** proceedings and (iv) **interest on the above** amounts.

- The **Court** passed a decree **directing Dalmia to deposit the full amount of the award**, **subject to certain amounts to be retained while the views of the Income Tax Department were sought on whether the payments made to Glencore would be liable for tax in India** and consequently Dalmia was required to withheld taxes at the time of making the award.

- The **Income Tax Department vide an affidavit** asserted that **damages for breach of contract would be taxed u/s 56 of the Act**. Further under the India-Swiss Confederation DTAA, **the said receipts would fall under Article 22(3) and accordingly would be taxed in India**. With respect to the **legal cost and cost of arbitration**, the same would be **taxable as FTS since the predominantly the expenses include fees paid to lawyers and other professional expenses.**

- In this background, **Glencore approached the Court for the release of the balance amount of the award and contented that no taxes should be withheld.**

DECISION OF THE HIGH COURT

- The Court held that **amounts comprising damages for breach of contract, along with interest thereon would not fall within Article 22(3), since the said clause is applicable only for specific nature of income viz. lotteries, crossword puzzles etc. and hence the income would therefore not be taxable in India as per Article 22(1).**

- The Court further held that the amounts comprising **reimbursement of legal costs and arbitration costs could not be regarded as income of Glencore**, and therefore **would not be taxable in India**.

- Thus, having determined that the amounts would not be taxable in the hands of Glencore, it ruled that there was **no requirement for Dalmia to withhold tax on the same.**

A.P. Moller Maersk v. DCIT - [2019] 111 taxmann.com 195 (Mumbai - Trib.)

ISSUE 34

- ***Whether Inland Haulage Charges (IHC) would be regarded as part of operations of ships?***

RELEVANT PROVISIONS

- **Article 9** of India-Denmark DTAA

*"1. Profits derived from the **operation of ships** in international traffic shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated."*

FACTS - A.P. Moller Maersk

- **The assessee, a tax resident of Denmark, was engaged in chartering and other related activities of shipping in international traffic.** During the year under consideration the assessee filed a return of income **declaring NIL income as per Article 9 of India Denmark DTAA.**

- After verifying the return of income and other details furnished by the assessee, **the AO held that Inland Haulage Charges would not be considered as revenue earned from shipping in international traffic.**

DECISION OF THE TRIBUNAL - A.P. Moller Maersk

- **The Tribunal relied on the OECD Commentary** and observed that Paragraph 4 of the commentary indicates that Article dealing with **Shipping Income, applies to profits directly obtained from the transportation of passengers or cargo by ships owned**, leased or otherwise at the disposal of a person **as well as the profits from the activities which are not directly connected with the acquisition of the assessee 's ships. In the latter case however, the activities must be ancillary to such operations** viz, the operation of ships owned, leased or otherwise at the disposal of the assessee in international traffic. **It indicates that the provision also applies to the activities that permit, facilitate or support the international traffic operations.**

- The Tribunal upheld the plea of the assessee by relying on Hon'ble Bombay High Court decision in the case of **Balaji Shipping (UK) Ltd. (2012) 253 CTR 460 (Bom.),** wherein it has been held that the that **IHC is necessarily in connection with transport of containers either discharged or loadable at Indian ports for the purpose of delivery through international waters and is directly connected with such transportation will always be included within the term "operations of ships".**

DCIT v. KLM Royal Dutch Airlines LB - [2019] 101 taxmann.com 9 (Delhi - Trib.)

ISSUE 35

- ***Whether ground handling and the technical handling services rendered by the assessee to the other airlines in India forms part operation of aircraft in international traffic.***

RELEVANT PROVISIONS

- **Article 8** of India-Netherlands DTAA

  "*1.* ***Profits from the operation of aircraft*** *in international traffic shall be taxable only in the State in which the place of effective management of the enterprise is situated.*"

FACTS - KLM Royal Dutch Airlines LB

- The **assessee, a tax resident of Netherlands**, was into the **business of operations of aircraft in international traffic** and derives income from providing air services for the carriage of the passengers, freight and mail in international traffic. **Apart from business of air transport operation, the assessee is also rendering technical handling services to other airlines in India, the payments of which are settled through IATA clearance.**

- The **Assessee** claimed the **said technical handling receipt as exempt under Article 8 of India – Netherlands DTAA**. However, **the AO held** that the said **technical handling charges** are required to be taxed in accordance with **the provisions of Act and not under Article 8**.

DECISION OF THE TRIBUNAL

- The Tribunal upheld the plea of the assessee **by relying on the decision of Delhi HC in assessee's own case**, held that **Article 8 is categoric enough in its meaning of expression "profit from the operation of ship or aircraft in international traffic" which includes the activities carried out by the assessee company by rendering technical handling services to the other airlines in India and has certainly connected with its activity of transportation by way of operating the aircraft.**

R.A.K. Ceramics UAE v. DCIT - [2019] 104 taxmann.com 380 (Hyderabad - Trib.)
Soregam SA v. DDIT - [2019] 101 taxmann.com 94 (Delhi - Trib.)

ISSUE 36

- ***Whether the expression 'tax' as provided in the respective clauses of the DTAA subsumes within itself education cess and surcharge as applicable under the Act.***

RELEVANT PROVISIONS

- **Article 12(2)** of India-Belgium DTAA

  "[2. However, such royalties and fees for technical services may also be taxed in the Contracting State in which they arise and, according to the laws of that State, but if the beneficial owner of the royalties or fees for technical services is a resident of the other Contracting State, the tax so charged ***shall not exceed 10 per cent of the gross amount*** *of the* ***royalties or fees for technical services.****]"*

- **Article 12(2)** of India-UAE DTAA

"2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the recipient is the beneficial owner of the royalties the tax so charged ***shall not exceed 10 per cent of the gross amount*** *of such* ***royalties.****"*

RELEVANT PROVISIONS

- **Article 2(2)** of India-Belgium DTAA

  *"'The **existing taxes to which the Agreement shall apply** are.*

  (a) in the case of India :

  *(i) the **income-tax including any surcharge thereon**, and*

  (ii) the surtax,

  (hereinafter referred to as "Indian tax")'"

- **Article 2(2)** of India-UAE DTAA

  *"2. The **existing taxes** to which the Agreement shall apply are :*

  "(a) In United Arab Emirates…… :

  (b)In India :

  *(i) the **income-tax including any surcharge thereon** ;*

  (ii.)the surtax ; and

  (iii)the wealth-tax

  (hereinafter referred to as "Indian tax").”

R.A.K. Ceramics, UAE & Soregam SA

FACTS - R.A.K. Ceramics, UAE

- The **assessee, a tax resident of Belgium, is engaged in the business of providing Information Technology Support Services to various group entities.**

- During the course of assessment proceedings, the **AO** held that the services rendered by the assessee **were in nature of FTS** and accordingly taxed the same **@10% as per Article 12 of India-Belgium DTAA**. While passing the assessment order, **the AO levied cess and surcharge over an above the rates as prescribed under Article 12 of the DTAA**.

- The **assessee contended** Article 2 states that **surcharge is included in income tax** and the tax rate of **10%** as prescribed in **Article 12 shall have to be deemed to include surcharge and since cess is nothing but an additional surcharge, the tax prescribed under DTAA at the rate of 10% shall be deemed to included surcharge and education cess.**

Note :- Similar view has been adopted in case of Soregam SA v. DDIT [2019] 101 taxmann.com 94 (Delhi - Trib.)

DECISION OF THE TRIBUNAL

- The Tribunal upheld the plea of the assessee by relying on the decision of **Delhi Tribunal in case of Elektrobit Automotive GmbH [IT Appeal No. 678/Delhi of 2013],** wherein the Tribunal held that **education cess is only a surcharge and inturn surcharge is only a tax clarified by the Hon'ble Apex Court in case of K. Srinivasan ([1972] 83 ITR 346)**

Aditya Khanna v. ITO - [2019] 105 taxmann.com 323 (Delhi - Trib.)

ISSUE 37

- ***Whether states taxes paid in USA would be available as tax credit in India u/s 91?*** YES

RELEVANT PROVISIONS

- **Section 91(1)**

  "91. (1) ***If any person who is resident in India*** *in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India),* ***he has paid in any country with which there is no agreement*** *under section 90 for the relief or avoidance of double taxation,* ***income-tax****, by deduction or otherwise,"*

FACTS - Aditya Khanna

- Assessee, an individual 'not ordinarily resident in India', filed a return of income **declaring salaries for the proportionate period for which he was employed with his employer in USA and claimed the credit for New York State taxes and local state taxes, besides federal taxes as foreign tax credit claim u/s 91 of the Act.**

- **The AO denied the credit of state taxes by adopting a view that taxes for foreign tax credit would include only federal taxes.**

DECISION OF THE TRIBUNAL

- The Tribunal upheld the plea of the assessee **by relying on Karnataka High Court decision in case of Wipro Ltd. (62 taxmann.com 26)**, wherein it has been held that the **Income Tax in relation to any country includes Income-tax paid not only to the Federal Government of that country, but also any Income-tax charged by any part of that country meaning a State or a local authority, and the assessee would be entitled to the relief of double taxation benefit with respect to the latter payment also.**

Bank of Tokyo Mitsubishi Ltd. v. CIT

[2019] 108 taxmann.com 242 (Calcutta)

ISSUE 38

- ***Whether by virtue of Article 24(2) of India Japan DTAA, permanent establishment of a Japanese entity in India cannot be charged tax at a rate higher than comparable Indian assesses carrying on same activities?***

RELEVANT PROVISIONS

- **Article 24(2)** of India Japan DTAA

  "2. The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State **shall not be less favorably levied** in that other Contracting State **than the taxation levied on enterprises of that other Contracting State carrying on the same activities."**

- **Article 24(2)** of India Netherlands DTAA

  "2. Except where the provisions of paragraph 3 of Article 7 apply, **the taxation on a permanent establishment** which an enterprise of one of the States has in the other State **shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State** carrying on the same activities."

Bank of Tokyo Mitsubishi Ltd.

FACTS

- The taxpayer, **a Japanese Bank, had a permanent establishment**, in India.

- For AY 1991-92, the Tribunal vide order dated 31 March 1997 **held that that rate of tax applicable to the taxpayer should be 65 percent and not the rate of tax applicable to the domestic company in India as the CBDT had not issued a circular as was issued in the case of ABN Amro Bank** (Letter No. D.O. No. 500/45/94-FTD, dated 21st. Nov., 1994).

Netherland Entity

- The **assessee contended** that as per **Article 24(2)** of India Japan DTAA, **the rate of tax of its PE would be the same as applicable to a domestic company carrying on similar activities in India.**

DECISION OF THE HIGH COURT

- The Court held that **as per Article 24(2) a permanent establishment of a foreign origin in the other contracting State, would not be taxed on less favorable terms than enterprises carrying on the same activities in the relevant contracting State.**

- The Court also held that the **stand taken in the Tribunal's order could not be appreciated or accepted merely becuase a similar clause** in the DTAA between **India and the Netherlands was interpreted by the Central Board for Direct Taxes and a circular issued thereupon (and no circular was issued for the India-Japan DTAA).**

- Accordingly the Court held that the **Tribunal was incorrect** in holding that the rate of tax applicable to the taxpayer **was 65 percent**. The Tribunal ought to have held that the rate applicable to the assessee was such rate as applicable to a domestic company carrying on similar activities.

- NA Amendment in s. 90 → Expl by F.A 2001 w.r.e.f 1-4-62 Tax Rate of FCO ⊃ Tax rate of ICO cannot be considered as "less favourable" — lang in A. 24(2)
- Chohung Bank – 102 ITD 45 (mum)
- St. Bank of Mauritius 11 T.com 331 (mum) → unilateral Treaty override not permissible
- Abu Dhabhi commercial Bank – 18 SOT 169 (mum)

DCIT v. Shri Kumar Sanjeev Ranjan

[2019] 104 taxmann.com 183 (Bangalore - Trib.)

LAW TO FACTS

ISSUE 39

- ***Which factors would be germane in deciding as to which state the personal and economic relations (i.e. center of vital interest) of a person are closer for determining his residential status under the India-USA DTAA?***

RELEVANT PROVISIONS

- **Article 4(1)** of India-USA DTAA

  *"1. For the purposes of this Convention, the term "**resident of a Contracting State**" means **any person who**, under the laws of **that State**, is **liable to tax therein by reason** of his domicile, **residence, citizenship**……."*

- **Article 4(2)** of India-USA DTAA

  *"(2) **Where by** reason of the provisions of paragraph 1,* **an individual** *is a* **resident of both** ***Contracting States**, then his **status** shall be determined as follows :*

  (a) he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, **he shall be deemed** *to be a* **resident of the State** *with which his* **personal and economic relations are closer** *(centre of vital interests) ; ……*

FACTS

- The **assessee, a US citizen, was on a temporary cross-border assignment to India, from June 2006 until 10 August, 2012, and thereafter, returned to USA with his family.**

- For the **AY 2013-14**, the **assessee was a Resident and Ordinarily Resident (ROR) of India and resident of USA under the domestic tax law of the respective countries.**

- The **assessee filed** his India tax return and **offered salary income earned till August 2012 to tax in India** and **salary for the remaining period, which was earned in USA, was claimed as not taxable in India** on account of him being a resident of USA under the provisions of **Article 16(1)** of India-USA DTAA for the remaining part of the year.

- The **AO denied the benefit of Article 16(1) for want of TRC from US Tax Authorities and alternatively also held that the condition of 'Centre of Vital Interest' was not in USA in the instant case as the assessee had been in India for six years and hence his economic and personal relations, developed over a period of time, were closer in India than in the USA.**

- The **CIT(A)** analyzed the personal and economic relations of the assessee and allowed assessee's appeal. It noted that the **assessee's family members, personal belongings, voting right, driving license, social ties, investments, settlement, social security etc. are in USA** and hence, it concluded that the taxpayer had his **center of vital interest in the USA** during the remaining part of the year. **Further the assessee also produced the TRC from US Tax Authorities before the CIT(A).**

ASSESSEE'S CONTENTION

- The assessee contended that for the period 11 August, 2012 to 31 March, 2013, he tie-broke his residency to the USA, as his center of vital interests was in the USA, based on the following factors:
  - **Family members were citizens of USA**
  - **House properties, car and other personal belongings were in USA**
  - **Voting rights and driving license were in USA**
  - **Investments and social security were in USA**

REVENUE'S CONTENTION

- The **AO** contended that the **personal and economic relations refer to a long and continuous relation** that an individual nurtures with a place. Therefore, **the assessee could not claim that after the end of his assignment (i.e. from 11 August 2012) his economic and personal relations were suddenly closer to the USA than India.**

For ITAT - see slide 185
finding (last slide)

Sreenivasa Reddy Cheemalamarri v. ITO

[TS-158-ITAT-2020(HYD)] - ITA No. 1463/Hyd/2018

ISSUE 40

- ***Whether DTAA benefit could be denied merely on the ground of non-furnishing of TRC u/s 90(4) of the IT Act, if circumstantial evidences demonstrates that the assessee is eligible for DTAA benefit?***

RELEVANT PROVISIONS

- **Section 90(4)** of the Act — TRC ↓

  "(4) An assessee, not being a resident, to whom an agreement referred to in sub-section (1) applies, ***shall*** *not be entitled to claim any relief under such agreement* ***unless a certificate of his being a resident in any country outside India*** *or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory."*

- **Article 4** of India-Austria DTAA — TRC NOT REQUIRED ↓

  "1. For the purposes of this Convention, the ***term "resident of a Contracting State"*** *means* ***any person*** *who,* ***under the laws of that State****,* ***is liable to tax*** *therein* ***by reason*** *of* ***his domicile, residence****, place of management or any other criterion of a similar nature, and also includes that State and any political sub-division or local authority thereof."*

SML tax chamber — GO TO CONTENTION BEFORE TRIBUNAL

Sreenivasa Reddy Cheemalamarri

FACTS

- **The assessee, a tax resident of Austria**, filed return of income in India for AY 2014-15, **by claiming the salaries received** from **IBM India Pvt. Ltd.** (on which taxes u/s 192 were withheld) **as exempt in India under Article 15(1) of India-Austria DTAA.**

- **Article 15(1)** of **India-Austria DTAA** provides that **income in nature of salaries**, wages and other similar remuneration **derived by a resident of a Contracting State(i.e. Austria)** in respect of an **employment shall be taxable only in that State(i.e. Austria)** unless the employment is exercised in the other Contracting State (i.e. India).

- During the course of assessment proceedings, **the AO required the assessee** to provide the **TRC issued by the Austrian Tax Authorities** in support of its claim under Article 15(1). However **the assessee, despite best possible efforts, was not able to obtain the TRC** from the Austrian Tax Authorities.

- The **AO** concluded the assessment proceedings by **denying DTAA benefit on the grounds that as per section 90(4), the assesse should obtain a TRC in order to claim DTAA benefit.** On appeal by the assessee before the CIT(A), the CIT(A) upheld the order of the AO.

CONTENTIONS BEFORE THE TRIBUNAL

- The assessee argued that he qualified as a tax resident of Austria ; **the said salary income had also been duly taxed in Austria which resulted in double taxation of the** same income and **accordingly the assessee was eligible of benefit of DTAA u/s 90.**
- The Revenue supported the view of the AO, that DTAA benefit u/s 90 cannot be granted unless a TRC is obtained.

DECISION

- The Tribunal observed that **obtaining a TRC from foreign tax authorities is generally a herculean task and hence the assessee cannot be obligated to perform an impossible task** (i.e. obtaining the TRC from Austrian tax authorities, despite best possible efforts, in the present case).

- In view of the same, the Tribunal held that **if the assessee with circumstantial evidences** (i.e. the fact that the said income has also been taxed in Austria) **demonstrates that he is a resident of the other state**, the provisions of **section 90(4) ought to be relaxed** and accordingly the claim of the assessee should not be rejected merely on the grounds of non-furnishing of TRC.

- Further, the Tribunal, by **relying on the decision of Tribunal (Ahmedabad Bench) in case of Skaps Industries Pvt. Ltd. [2018] 94 taxmann.com 448 (Ahmedabad - Trib.)**, held that the provisions of **section 90(4) cannot override the provisions of the DTAA** and accordingly **if the conditions prescribed under the relevant DTAA are fulfilled, then the assessee cannot be denied benefit of the DTAA.**

THIS SLIDE IS TO BE READ AFTER SLIDE NO 180

DECISION OF TRIBUNAL

- The **Tribunal noted** the entire factual matrix of the assessee and **upheld the order of CIT(A)** in holding that the assessee **had his center of vital interest in USA**.

- Further, the **Tribunal upheld the action of the CIT(A) in accepting TRC directly in the first instance without remanding the matter back to the tax officer** for fresh examination, since the CIT(A) arrived at the conclusion of center of vital interest taking into consideration the entire facts of the case and only a passing reference were made to the TRC.

THANK YOU

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