

Joint Cit, Vs. Essar Oil Ltd.

Joint Cit, Vs. Essar Oil Ltd.

SooperKanoon Citation : sooperkanoon.com/369449

Court : Mumbai

Decided On : Nov-30-2005

Reported in : [2006]7SOT216(NULL)

Appeal No. : It Appeal No. 168 (Mum.) of 2000 , A.Y. 1996-97 , 30 N

Appellant : Joint Cit,

Respondent : Essar Oil Ltd.

Advocate for Pet/Ap. : R.N. Parbat, *for the Assessee* , Dinesh Vyas and P.C. Tripathi, *for the Revenue*.

Judgement :

ORDER

G.E. Veerabhadrappe, V.P.

This appeal by the revenue arises out of the order of the Commissioner (Appeals)-XIV, Mumbai, dated 29-11-1999 for assessment year 1996-97. The revenue has raised the following grounds of appeal :

'1. On the facts and in the circumstances of the case and in law, the learned Commissioner (Appeals) has erred in holding that the services provided by the assessee do not fall within the category of fees for technical services and, therefore, are not assessable under section 44D of the Income Tax Act, 1961 read with section 115A of the Income Tax Act and further erred in directing assessing

officer to compute the income of the assessee as business income as per provisions of Indo-UK DTAA.

2. On the facts and in the circumstances of the case and in law, the learned Commissioner (Appeals) has erred in directing the assessing officer to consider the claim of the assessee for carry forward of the loss for set off against profits in subsequent years.'

2. The facts in brief are that M/s. ABB Lummus Crest Ltd., U.K. (hereinafter referred to as 'U.K. Company') is a company incorporated in the United Kingdom. The said U.K. Company entered into a contract with M/s. Essar Oil Ltd., the assessee before us, for supervision of construction and commissioning activities in India for the refinery complex being built at Vadanar near Jamnagar in Gujarat by the assessee. India and United Kingdom have entered into and their subsists between them an Agreement for the Avoidance for Double Taxation ('DTAA' for short). For the year under consideration the assessee returned a loss of Rs. 66,20,690 which was accepted under section 143(1)(a) of the Act. Subsequently, this case was selected for scrutiny assessment. During the course of such assessment proceedings the assessing officer has discussed in detail the nature of services provided by the U.K. Company. The main services to be provided are as under:

(i) Construction supervisory services of the project.

(ii) Supervision of start up and commissioning of the project.

(iii) Material and warehouse management of the project.

(iv) Any other services incidental to the scope of PMC-1 services as defined and as may be required with a view of achieving realization of the project.

According to the assessing officer, services were provided by highly qualified technical personnel and, therefore, they fall within the ambit of 'fee for technical services'. As the receipts are assessable as fees for technical services, no deduction of expenses is to be allowed, in view of section 44D of the Act, even though the receipt may be assessable under article 7 of DTAA between India and

U.K. The assessing officer has taken this view keeping in mind the provision of article 7(5) of DTAA. The assessing officer, therefore, did not allow any expenditure while computing the income. Therefore, he has not allowed the assessee's claim for carry forward of the loss to be set off against profit in subsequent years. Aggrieved the assessee filed an appeal before the Commissioner (Appeals).

3. Before the Commissioner (Appeals) the assessee submitted that as per the agreement, no receipts had accrued to it in the current year but expenditure had been incurred which would result in income/receipts in the subsequent years. Therefore, it had claimed carry forward of expenditure amounting to Rs. 66,20,690. However, the assessing officer was of the opinion that the expenses are not to be considered for computation of income and, therefore, did not allow the assessee's claim for carry forward the expenses. The main arguments of the assessee before the Commissioner (Appeals) have been summarized at pages 4 and 5 of the impugned order. It was further contended that the definition of 'Fees for technical services' has been explained in a protocol on India-US Treaty, where also similar words have been used to define 'Fees for technical services'. In the said protocol it is stated that technology will be considered as made available when the person acquiring the service is enable to apply the same. The fact that the provision of the service may require technical input by the person providing the service does not per se mean that technical knowledge, skill, experience, etc., are made available to the person purchasing the service. In view of the above, supervisory work does not enable the company personnel to carry out similar activity later by the assessee's personnel and as such, supervisory services do not constitute 'Fees for technical services'. It was also pointed out before the Commissioner (Appeals) that the Tribunal in the case of General Electric Technical Services Co. Inc. in (IT Appeal No. 3328 (Bom.) of 1986) for assessment year 1981-82 and for subsequent years took a view that when major part of the expenses are incurred by the recipient on payment of wages (salary of labour) and/or on purchase of material, income is to be assessed as business income after allowing deduction of expenses incurred in connection with such business. The further arguments of the assessee, as mentioned by the Commissioner (Appeals), were as under :

'In the present case, out of total expenses of UKF2,53,101,30, the expenses on manpower deployed in India amounted to UKF 1,65,043 out of which UKF 1,25,755 were not borne by the permanent establishment and, therefore, were not claimed as expenses in India. The other major expenses related to travel. Thus, the major costs were incurred on manpower deployment in India. In view of the foregoing, the income should be assessed after allowing deduction of expenses.

(x) The Non-Discriminatory clause article 26 of India-U.K. Double Taxation Avoidance Agreement provides that taxation of a permanent establishment of a Contracting State shall not be less favourably assessed to tax in the other State compared to their own enterprise under the same conditions. Engineers India Limited, Tata Consulting Engineers etc., are providing services, some of which are definitely 'Fees for technical services', yet their income is assessed to tax on net basis and not on gross basis. Therefore, the permanent establishment should also be assessed to tax accordingly. The Non-Discriminatory Clause, itself provides that rate of tax in the case of permanent establishment could be different from the rate of tax charged on enterprise of the State itself. The Non-Discriminatory clause also provides that where income is assessed on the basis of estimated allocation of expenses, it will not be treated as discriminatory. Thus wherever a permanent establishment could be treated in a manner different from what the enterprise of the State is to be treated, the Non-Discriminatory clause has specifically provided for it.

(xi) India-U.K. Double Taxation Avoidance Agreement is on the Model Convention of Treaties. Detailed commentaries were issued along with the Model Convention. In the book of Double Taxation Avoidance Agreements by Mr. K. Srinivasan, on page 294, it has been stated that income arising to the permanent establishment under the heads, dividend, interest and royalties should be treated on par with income arising to a resident enterprise and the income of the two should be subject to tax on profit only.

2. In view of the aforesaid submission, Authorised Representative pleads that the assessing officer may be directed to allow the expenditure claimed by the appellant and also its carry forward for set off against profits in subsequent years.'

After considering the above arguments of the assessee the Commissioner (Appeals) partly allowed the assessee's appeal observing as under:

'3. I have considered the above submissions the assessment order as well as the legal position brought to my notice. The case laws cited supra have also been perused by me. After having done so, I am of the view that decisions taken by assessing officer that the services provided by the appellant fall within the category of 'Fees for technical services' and assessable under section 44D read with section 115A of the Act cannot be sustained. Considering the facts and circumstances of the case and also the legal position, I agree with the views of Authorised Representative that the provisions of Indo-UK DTAA are applicable in computing the total income of 'ABB Lummus Crest Ltd., UK in India including the tax thereon.

4. The assessing officer is directed to compute the income (loss) arising to the above concern during the year as business income as laid down in Article 7 of the Indo-UK DTAA. He is also directed to consider the claim of appellant for carry forward of loss (to be determined) for set off against profits in subsequent years.'

4. Before us the learned Departmental Representative strongly relied on the observations of the assessing officer. The learned counsel for the assessee, on the other hand, relied on the order of the Commissioner (Appeals). It was also contended that the issue stands covered in favour of the assessee by the decisions of the Tribunal in the case of Dy. CIT v. Boston Consulting Group P. Ltd. (IT Appeal No. 447 (Mum.) of 2001) for the assessment year 1997-98, order dated 4-2-2005 in Dy. CIT v. Boston Consulting Group P. Ltd. (2005) 93 TTJ (Mum.) 293 and Dy. CIT v. Boston Consulting Group P. Ltd. .

5. We have considered the rival submissions and have gone through the record as also the Tribunal decision relied upon by the learned counsel for the assessee. There is no dispute as to the facts and circumstances of the case as mentioned above. The core of controversy before us is that whether or not the limitation on deduction for expenses as set out in section 44D of the Income Tax Act will apply in a case where the related income is not in the nature of fees for technical

services so far as the meaning of the said expression under the applicable bilateral tax treaty is concerned, but on the test laid down under Explanation 2 to section 9(1)(vii) of the Act, such an income could be treated as fees for technical services. For resolving this controversy it is necessary to refer to article 7 of the DTAA which reads as under:

'Article 7. Business profits- 1. The profits of an enterprise of a Contracting State shall be taxable only in the State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is directly or indirectly attributable to that permanent establishment.

2. Where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, the profits which that permanent establishment might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment shall be treated for the purpose of paragraph 1 of this article as being the profits directly attributable to that permanent establishment.

3. Where a permanent establishment takes an active part in negotiating, concluding or fulfilling contracts entered into by the enterprise, then notwithstanding that other parts of the enterprise have also participated in those transactions, that proportion of profits of the enterprise arising out of those contracts which the contribution of the permanent establishment of those transactions bears to that of the enterprise as a whole shall be treated for the purposes of paragraph 1 of this article as being the profits indirectly attributable to that permanent establishment.

4. Insofar as it has been customary in a Contracting State according to its law to determine the profits to be attributed to a permanent establishment on the basis of an apportionment of the total profits of the enterprise to its various parts, nothing in paragraphs 1 and 2 of this article shall preclude that Contracting State from

determining the profits to be taxed by such an apportionment as may be necessary, the method of apportionment adopted shall, however, be such that the result shall be in accordance with the principles laid down in this Article.

5. Subject to paragraphs 6 and 7 of this Article, in the determination of the profits of a permanent establishment, there shall be allowed as deduction expenses which are incurred for the purposes of the business of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere, which are allowed under the provisions of and subject to the limitations of the domestic law of the Contracting State in which the permanent establishment is situated.

6. Where the law of Contracting State in which the permanent establishment is situated imposes a restriction on the amount of the executive and general administrative expenses which may be allowed, and the restriction is relaxed or overridden by any Convention between that Contracting State and a third State which is a member of the Organisation for Economic Co-operation and Development or a State in a comparable stage of development and that Convention enters into force, after the date of entry into force of this Convention, the competent authority of that Contracting State shall notify the competent authority of the other Contracting State of the terms of the relevant paragraph in the Convention with that third State immediately after the entry into force of that Convention and, if the competent authority of the other Contracting State so requests, the provisions of this Convention shall be amended by protocol to reflect such terms.

7. Paragraph of this article shall not apply to amounts, if any, paid (otherwise than towards reimbursement of actual expenses) by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents or other rights, or by way of commission, for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on monies lent to the permanent establishment, nor shall account be taken in the determination of the

profits of a permanent establishment of amounts charged (otherwise than towards reimbursement of actual expenses) by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents or other rights, or by way of commission for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on monies lent to the head office of the enterprise or any of its other offices.

8. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

9. Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provision of this Article.'

It is an admitted position that the terms of article 7 of the DTAA between India and UK is similar to the terms of article 7 of the DTAA between India and Singapore considered by the Tribunal in the case of Boston Consulting Group P. Ltd. (supra). In that case, the assessee was receiving income through its permanent establishment in India by providing strategy consultancy services such as marketing and sales strategy, business strategy and portfolio strategy, etc. to its clients in India and abroad. The Tribunal, after discussing the terms of article 7 of the DTAA and referring to the provisions of sections 44D and 115A of the Income Tax Act, has held that such services clearly rule out the applicability of clauses (a) and (c) to article 12(4) of the DTAA. As regards clause (b) of article 12(4) the Tribunal held that only such services as are technical in nature are covered which may enable the recipient of services to apply the technology and not consultancy services. In case receipts through permanent establishment in respect of which profits are computed under article 7(3) of the DTAA are not fee for technical services, section 44D is not to be applied for purposes of deduction of expenses. Tribunal held that receipts by assessee- Singapore -company through its permanent establishment in India chargeable to tax under article 7(3) of the DTAA between India and Singapore, being from strategy consultancy services, were not

from technical services as referred to in article 12(4)(d) of the DTAA. Hence section 44D, and for that matter, Explanation 2 to section 9(1)(vii) did not apply and, therefore, the limitation for deduction under section 44D was not attracted. The Tribunal also held that even if a contrary view was possible the one favourable to the assessee has to be preferred. Similar is the view taken by the Tribunal in the case of Raymond Ltd., (supra). Facts and circumstances being similar following the detailed discussions contained in the order of the Boston Consulting Group Pte. Ltd., we are of the opinion that the Commissioner (Appeals) has come to a right conclusion and his order does not call for any inference. It is accordingly upheld and the revenue's grounds are rejected.

6. In the result, the appeal is dismissed.

SooperKanoon - India's Premier Online Legal Search - sooperkanoon.com