

Brown and Root Inc. Vs. Commissioner of Income-tax

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Court : Authority for Advance Rulings

Decided On : Oct-27-1997

Reported in : (1999)237ITR156AAR

Judge : S Ranganathan, S C Jain

Appellant : Brown and Root Inc.

Respondent : Commissioner of Income-tax

Judgement :

For Appellant/Petitioner/Plaintiff: Dinesh Vyas and Himanshu Narayan, Advs. and Ajay Mehra, Chartered Accountant CIT v. Visakhapatnam Port Trust, [1983] 144 ITR 146; In Re: Advance Ruling Application No. P-11 of 1995, [1997] 228 ITR 55 (AAR) 1. Mazagaon Dock Limited of India (MDL) was awarded a contract by the Oil and Natural Gas Commission (ONGC) for the installation of sub-sea gas pipelines including the 12" SHG gas pipeline (SHG pipeline) to be laid down between B121 platform and the SHG platform, offshore India.

For the execution of the said contract, MDL sub-contracted a part of the installation work of the SHG pipeline to Hyundai Heavy Industries Co. Limited (HHI). For the purpose of execution of its contract with MDL, HHI sub-contracted a part of the installation work of the SHG pipeline to Brown and Root Inc. (BRI).

2. The applicant, Brown and Root Inc., is a company duly incorporated and existing under the laws of the United States of America, with its office at 1209, Orange Street, Wilmington, Delaware 19801, United States of America. During the previous year ending on March 31, 1991, BRI had entered into a contract with HHI in relation to the installation of the 12" SHG gas pipeline between the B121 platform and the SHG platform offshore India by mobilising the eight point mooring vessel "Subtec 1" and the test support vessel "Captain BO". It was completed in 39 days from the date of commencement, i.e., from November 30, 1996 to January 7, 1997.

3. An agreement for Avoidance of Double Taxation exists between India and the United States of America (hereinafter called as "DTAA"). It is contended by the applicant in its statement containing interpretation of law and facts that where there is such an agreement, the provisions of the DTAA will prevail over those contained in the domestic laws of both the countries, if the provisions of the DTAA are more favourable to the asses-see. In this connection, it has relied on a judgment of the Andhra Pradesh High Court in CIT v. Visakhapatnam Port Trust [1983] 144 ITR 146. Reliance has also been placed on section 90(2) of the Income-tax Act, 1961, inserted by the Finance (No, 2) Act, 1991, which reads as under : "Where the Central Government has entered into an agreement with the Government of any country outside India under subsection (1) for granting relief of tax, or, as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee." 4. The applicant contends that since it is a tax resident of the USA, the issue of its tax liability should be determined in accordance with the provisions of the applicable DTAA.6. According to the applicant, the work was mainly carried out at various depths of sea and it required mobilisation and demobilisation of diving personnel/equipment including the eight point mooring vessel "Subtec 1" and the

test support vessel "Captain BO" which were used by BRI to execute the work under its contract with HHI. It is stated that its duties were primarily as a work contractor and that for performing the contract, it did not require or maintain any office or fixed place of business in India or any establishment of the nature mentioned in Article 5 of the DTAA between India and USA. Accordingly, it is contended that the revenues earned by BRI under the contract fall within the scope of business profits as dealt with in Article 7 of the DTAA. Under this article, business profits arising to a US tax resident in India are taxable in India, only if the US tax resident carried on business in India through a permanent establishment (PE) and to the extent the profits are attributable to the permanent establishment of such US resident. The applicant submits that BRI could have been construed to have a permanent establishment in India as per Clause 2(k) of Article 5 of the DTAA provided its activities in India including those in relation to the projects or sites, had continued for a period of more than 120 days in any twelve month period. In the present case, the total duration of the contract executed by BRI was 39 days, i.e., from November 30, 1996 to January 7, 1997. The applicant has clarified that it has not carried out any activity in India except for the execution of the contract referred to in the application under consideration. In the light of the aforesaid, the applicant contends that revenues earned by it are not taxable in India.

7. In the background, the ruling of the authority is desired on the following question : "The taxability [in terms of Article 7 read with Article 5 of the Agreement for Avoidance of Double Taxation ('DTA') concluded between India and the United States of America which came into effect from April 1, 1991] of revenues earned by Brown and Root Inc., a tax resident of the United States of America, from its contract with Hyundai Heavy Industries Co. Limited, a company incorporated and existing under the laws of the Republic of Korea." 8. The Department, on the other hand, in its response addressed to this authority dated September 21, 1997, contends that BRI had executed only a job work, the project being that of MDL and that BRI under sub-contract with HHI had performed only a part of the installation work on SHG pipeline project of MDL. Therefore, according to the Department, BRI is not covered under Article 5(2)(k) but under Articles 5(2)(a) and 5(2)(f). Under these provisions, no time limit is prescribed for existence of permanent establishment. It is further contended that the sub-contract was managed and conducted by BRI from vessels "Subtec 1" and "Captain BO" at seabed within the territory of India which would constitute permanent establishment within the meaning of Article 5(2)(a). The Department has also taken a view that the pipeline laid by BRI under the sub-contract was connected with the gas well, and hence the pipelines were a place of extraction of natural resources and constituted permanent establishment under Article 5(2)(f) of the DTAA.9. During the arguments before the authority, learned senior counsel for the applicant, Shri Dinesh Vyas, mentioned that his client was not involved in any other work or installation and that without the work entrusted to BRI, the installation work would neither be complete nor safe. In fact, he stated that it was in the nature of foundation for installation. He also argued that vessels were the only modes of transportation for the personnel for their part of the work and this could have been done even with the help of helicopters. He countered the argument that the ship was a place of management of its work. It was, according to him, only an asset in the business.

10. Articles 5 and 7 of the DTAA between India and USA to the extent relevant for the present discussion are reproduced below (see [1991] 187 ITR (St.) 102, 106) : (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.

(f) a mine, an oil or gas well, a quarry, or any other place of extraction of natural resources ; (g) a warehouse, in relation to a person providing storage facilities for others ; (h) a farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on ; (j) an installation or structure used for the exploration or exploitation of natural resources, but only if so used for a period of more than 120 days in any twelve-months period ; (k) a building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities (together with other such sites, projects or activities, if any) continue for a period of more than 120 days in any twelve-month period ; (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 : (i) activities of that nature continue within that State for a period or periods aggregating more than 90 days within any twelve-months period ; or (ii) the services are performed within that State for a related enterprise (within the meaning of paragraph 1 of Article 9 (associated enterprises)).

3. Notwithstanding the preceding provisions of this article, the term 'permanent establishment' shall be deemed not to include any one or more of the following ; (a) the use of facilities solely for the purpose of storage, display, or occasional delivery of goods or merchandise belonging to the enterprise ; (b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or occasional delivery ; (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise ; (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise ; (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 other activities which have a preparatory or auxiliary character, for the enterprise.

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 contracts 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 ; (b) he has no such authority but habitually maintains in the first-mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise, and some additional activities conducted in that State on behalf of the enterprise have contributed to the sale of the goods or merchandise ; or (c) he habitually secures orders in the first-mentioned State, wholly or almost wholly for the enterprise.

5. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent, or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise and the transactions between the agent and the enterprise are not made under arm's-length conditions, he shall not be considered an agent of independent status within the meaning of this paragraph.

6. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other. Article 7-Business profits : 1. The profits of an enterprise of a Contracting State shall be taxable only in that 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 attributable to, (a) that permanent establishment ; (b) sales in the other State of goods or merchandise of the same or similar kind as those sold through that permanent establishment ; or (c) other business activities carried on in the other State of the same or similar kind as those effected through that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly at arm's length with the enterprise of which it is a permanent

establishment and other enterprises controlling, controlled by or subject to the same common control as that enterprise. In any case where the correct amount of profits attributable to a permanent establishment is incapable of determination or the determination thereof presents exceptional difficulties, the profits attributable to the permanent establishment may be estimated on a reasonable basis. The estimate adopted shall, however, be such that the result shall be in accordance with the principles contained in this article.

3. In the determination of the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the business of the permanent establishment, including a reasonable allocation of executive and general administrative expenses, research and development expenses, interest, and other expenses incurred for the purposes of the enterprise as a whole (or the part thereof which includes the permanent establishment), whether incurred in the State in which the permanent establishment is situated or elsewhere, in accordance with the provisions of and subject to the limitations of the taxation laws of that State. However, no such deduction shall be allowed in respect of 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, know-how or other rights, or by way of commission or other charges for specific services performed or for management, or, except in the case of banking enterprises, by way of interest on moneys lent to the permanent establishment. Likewise, no account shall be taken, in the determination of the profits of a permanent establishment, for amounts charged (otherwise than toward 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, know-how or other rights, or by way of commission or other charges for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on moneys lent to the head office of the enterprise or any of its other offices.

4. 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.

5. For the purposes of this Convention, the profits to be attributed to the permanent establishment as provided in paragraph 1(a) of this Article shall include only the profits derived from the assets and activities of the permanent establishment and shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

6. Where profits include items of income which are dealt with separately in other articles of the Convention, then the provisions of those articles shall not be affected by the provisions of this article.

7. For the purposes of the Convention, the term 'business profits' means income derived from any trade or business including income from the furnishing of services other than included services as defined in Article 12 (royalties and fees for included services) and including income from the rental of tangible personal property other than property described in paragraph 3(b) of Article 12 (royalties and fees for included services)".

11. Shri Vyas contended that Clauses (j) and (k) of Article 5(2) of the DTAA are the closest to the applicant's fact situation. Clause (f) of Article 5(2) laid emphasis on one point for an activity whereas installation work involved activity from one point to another point. As such, Clause (f) of Article 5(2) was not applicable to it. He argued that it was the assessee's choice to opt for the most beneficial provision. Shri Vyas also relied upon ruling of this authority dated February 9, 1996, in Advance Ruling Application No. P-11 of 1995, In re [1997] 228 ITR 55 (MR) (hereinafter referred to as the Singapore case) where interpretation of Articles 5(3) and 7 of the DTAA between India and Singapore was involved. Shri Vyas argued that this ruling was squarely applicable in the instant case since Articles 5(3) and 7 of the DTAA between India and Singapore are *pari materia* with Article 5(2)(k) and Article 7 of the DTAA between India and the U.S.A. In the Singapore case [1997] 228 ITR 55 (AAR), this Authority held as under (page 60) : "From a perusal of the scope of the work carried on by the applicant, it is clear that the applicant was engaged in an installation and assembly project which pertained to the burial

of pipelines in the seabed. Such activities are covered by para. 3 of Article 5 of the Agreement for Avoidance of Double Taxation and not by Clause (f) of para. 2 of Article 5 as claimed by the Department.

But para. 3 permits such project to be treated as a permanent establishment only if the duration of the project exceeds 183 days in any fiscal year, which is not the case here. It, therefore, follows that the applicant has no permanent establishment in India within the meaning of Article 5 and since Article 7 of the DTA permits the taxation, in the hands of a resident of Singapore, only of the profits attributable to a permanent establishment in India, no part of the profits earned by the applicant from its activities under the contract can be charged to Indian income-tax even though such activities took place within Indian territory and the profits there from would have been chargeable to tax in India but for the DTA." 12. Shri Braj Lal, Additional Commissioner of Income-tax, Special Range, Dehradun, arguing on behalf of the Department asserted that the vessels were not used only for transportation of personnel as contended by the applicant's counsel but were used for radio and communication, sending telex and fax, etc., and as such were fit to be used as office premises and for the purpose of management of the work. It was pointed out by Shri Braj Lal that the sub-contract was signed on behalf of the applicant by the manager (India) who was receiving instructions at the vessels from BRI to function as per their advice and such vessels were being used as workshop/office premises for purposes of management of their part of the project. Shri Braj Lal also referred to the definition of the expression "site" in Article 17 of the agreement for performance of contract works and said the applicant had some site from where it could supervise the work. Some other technical issues were also raised by Shri Braj Lal, namely, failure to furnish the identity of the company, failure to furnish the balance-sheet to indicate whether it was capable of executing the contract, etc. He even suggested that BRI may be acting as an agent or in benami capacity and that the real company behind the transaction may be having permanent establishment in which case the applicant could not deny that it had a permanent establishment. Further, it was contended that the certificate of completion of work from HHI, which was an interested party, could not be treated as authentic and that a certificate from the customs authorities would have carried better authenticity. An alternate argument was made by Shri Braj Lal that the case of the applicant could be brought under Article 12(3)(b) of the DTAA, namely, "royalties" towards "payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial or scientific equipment" since, according to him, it was a contract to provide commercial equipment. Shri Braj Lal stated that in a case covered by Article 12(3)(b), the period or duration of the work was not relevant.

Refuting the contention of Shri Vyas that the work of BRI was covered by Article 5(2)(k) of the DTAA, Shri Braj Lal argued that BRI performed only an insignificant part of the contract awarded by ONGC to MDL and that it may be a construction activity for MDL but not for the applicant.

13. Shri Vyas countered the arguments put forward by Shri Braj Lal and reiterated his interpretation of the provisions of the DTAA. 14. As far as some technical issues raised by the Department are concerned, we do not consider it necessary to go into these aspects as the assessing authority can always satisfy itself as to the facts of a case before applying the ruling of this Authority. The question raised before us is legal and we have prima facie no reason to doubt the basic facts given by the applicant for the purpose of giving our ruling.

15. We do not find much force in the argument of the Department that the activity of installation of the pipeline could be brought under other Clauses of the DTAA such as Clause (a), (e) or (f) of Article 5(2) or under Article 12(3)(b) of the DTAA. In our opinion, to hold that installation of the gas pipeline clearly falls within the scope of other Clauses such as (a) would militate against the well-established principles that a specific provision will override a general one and that the assessee/subject is entitled to invoke, the provision most beneficial to him, be they the provisions of a treaty or statute. Since the activity falls short of 120 days, the applicant could not be said to have a permanent establishment in India. The element of permanence in relation to an establishment, if any, would be attracted under Article 5(2)(k) only if the installation project continues for a period of more than 120 days and that condition is not satisfied here. It is not disputed that earnings from the work performed by BRI constitute business profits. However, in the absence of a permanent establishment, Article 7 of the DTAA would not be attracted. As such, there is no tax liability on BRI

for the business profits earned by it. In the circumstances, the ruling of the authority in the Singapore case [1997] 228 ITR 55 (AAR), referred to earlier is equally applicable in the facts of the present case.

16. In the light of the above discussion, the Authority pronounces the following ruling on the question raised in the application before it ; 17. The revenue earned by the applicant from the contracts with Hyundai Heavy Industries Co. Ltd., Ulsan, Korea, and performed offshore India, during the previous year ended on March 31, 1997, will not be liable to tax in India, as it had no permanent establishment in India.

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