

Assistant Commissioner of Vs. Interocean Shipping (i) (P.) Ltd.

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Court : Income Tax Appellate Tribunal ITAT Delhi

Decided On : Sep-30-1994

Reported in : (1994)51ITD582(Delhi)

Judge : A Kalyanasundharam, R Gupta

Appellant : Assistant Commissioner of

Respondent : interocean Shipping (i) (P.) Ltd.

Judgement :

1. The present appeal filed by the department is with reference to the provision of tax that should have been deducted from the payment of hire charges of ship that is contained in Section 195(2) of the Income-tax Act, 1961 ('the Act'). The objection of the department in the present appeal is on the conclusion by the CIT(A) that the hire charges is not liable to be taxed in India because of the provisions of Double Taxation Agreement between India & UK (DTA).

2. The dispute started with the assessee-company applying to the Assistant Commissioner of Income-tax (ACIT) for the issuing of 'No Objection Certificate' that was required by the Reserve Bank of India (RBI) for allowing any remittance out of India. The respondent company vide its letter dated 10-3-1993 applied for the above certificate for the remittance of US Dollars 104642.10 to M/s. Drake Maritime S.A.-London (DM) which covered the hire charges of a ship (H.V.Pelican). The respondent had stated that Oil & Natural Gas Commission (ONGC), a Government of India Undertaking had contracted with Mazagon Down

Ltd. (MDL) for various services in connection with its activities of exploration/development of Mineral Oil (MO) in Bombay Offshore area.

MDL in turn entered into a contract with the respondent for the provision of ship on hire and accordingly it had entered into Charter Party agreement with DM for hire of a ship that was effective from 7-12-1992.

3. The ACIT held that, the hire of ship to an Indian company by DM in the circumstances of the case, has to be taken to mean that service was rendered by DM in India and hence the hire charges so received by it arose and accrued in India according to the provisions of Section 5(2) of the Income-tax Act, 1961. He also noted that, since DM itself was not engaged in the business of hiring of ships for exploration of oils, the provisions of Section 44BB for determination of income from hiring of machinery for exploration/production of mineral oil does not apply.

He also noted that the Government of India had not issued any notification under Section 293A of the Act for levy of tax at a lower rate in regard to such contracts. He directed that the respondent should deduct 65% of the hire charges towards Indian Taxes and remit to UK the balance amount.

4. The respondent in its appeal before CIT(A) had contended that the situs of the contract with UK company [Non-resident company (NR)] was not in India and therefore the income derived by the UK company was not liable to tax in India. The respondent contended that in terms of Article 9 of DTA, NR is entitled to the relief from taxation in India.

It referred to the clauses of DTA, the meaning of the term 'a Contracting State' and 'other Contracting State'. It contended that the income arising to non-residents engaged in the business of shipping, etc., are governed by special Sections 44B, 44BB and 172 of the Act, which all override the provisions of computation of income from business covered by Sections 28 to 43A of the Act. It was contended that in terms of the charter party agreement any dispute that might arise was subject to the jurisdiction of English Courts. It was submitted that the agreement permitted the sub-letting of the ship during the subsistence of the agreement because from the time the agreement was entered into, it had become Disponee

Owner of the ship and it continued to enjoy the said status during the period of hire. It was accordingly contended that the payments of time hire being covered by the 'Sale of Disponee Ownership' and the situs of the contract being at UK, no income could arise to NR in India. In support of its contention it had placed reliance on (a) Lima Leita & Co. Ltd. v. Union of India (1968] 70 ITR 518 (Goa, Daman & Diu); (b) decision of the Supreme Court in Union of India v. Gosalia Shipping (P.) Ltd. [1978] 113 ITR 307; and (c) decision of the Andhra Pradesh High Cour in Addl. CIT v. Skoda Export, Praha [1988] 172 ITR 358.

5. The CIT(A) had noted that the ACIT had made no reference to DTA. He noted that paras 1 & 2 of Article 9 of DTA deal with the matter and reproduced the contents of those paras. He then referred to Section 90 of the Act that dealt with the double taxation relief wherever there was an agreement between the two countries. He observed that the present circumstance warranted examination of the provisions contained in Sections 44B, 44BB of the Act along with Article 9 of DTA. He referred to the letter from MDL to Director General of Shipping dated 25-11-1992 wherein the facility available of the ship hired from NR was indicated. This facility was 'Anchor Handling Tug to assist in Bombay High for construction of Offshore Platforms'. Considering the fact that the ship was ultimately used by ONGC in connection with oil exploration works, CIT(A) accordingly concluded that the ACIT was wrong to state that the assessee was not entitled to the benefits of Section 44BB of the Act. He therefore held that the assessee was not only entitled to the benefit under Section 44BB of the Act and was right in pleading that by virtue of Section 90 of the Act, DTA was enforceable and cancelled the order of ACIT. The CIT(A) also referred to the CBDT Circular No. 333, dated 2-4-1982 which clarified that in case of conflict between the provisions of the Act and DTA, the provisions of DTA shall prevail.

6. The department has thus come up in appeal before us. The learned departmental representative contended that Article 9 of DTA covered movement of ships in international waters. The notification was issued extending the rights of water territory of India to the Exclusive Economic Zone extending the territorial waters to the Offshore mining for oil exploration to 200 nautical miles. He made extensive reference to the provisions of Sections 6(6), 7(7) and 7(a) of the

Territorial Waters, Continental Shelf, Exclusive Economic Zone and Other Maritime Zones Act, 1976. He contended that by the above Act the Indian territory had got extended and therefore any type of commercial operation that is carried out within this extended territory, is liable to be taxed in India. He referred to the book on Constitutional Law by H.M. Seervai, 3rd edition Volume 1, Chapter VI to emphasise the point that once an extension to the territory of India is made by means of any notification, it remains in effect for all purposes including for taxation in India. He contended that in view of this extension the plying of the ship of NR has to be considered as plying within India and therefore Article 9 of DTA is inapplicable. He relied on the decision of the Tribunal in ONGC v. IAC [1989] 29 ITD 422 for his proposition of territorial waters. He contended that the ship was required to be delivered at Bombay at the start of the contract and it was to be released from Bombay on the conclusion of the contract and therefore it is a clear case of the contract being effected in India.

He pleaded that, the ship was required to ply between the Offshore platform to the various ports in India which also established that the plying was within India. He contended that Article 7 of DTA are inapplicable to the facts of the case. He also referred to the definition of UK as contained in DTA. He pleaded that since DTA did not cover the present contract of hire and therefore, tax needs to be deducted from the hire charges payable to NR.7. The learned Senior Advocate Mr. Dastur contended that; the Territorial Waters Act, 1976 that was referred to by the departmental representative only provided the rights to explore for oil, its extraction but, it could never extend the territory of India because, such an Action required amendment to the Constitution of India. In support of this argument he relied upon the decision of the Tribunal in IAC v. Donald William Rickard [1988] 26 ITD 434 (Mad.), specifically to the observation made in para 35 in this regard.

He contended that, the ship was required for the construction of the Offshore platforms because it satisfied the technical specifications as had been noted by the CIT(A) in his order. He submitted that, the extension of the rights on water that permitted the oil exploration is with regard to water, the oil under it, etc. and has been so made keeping in line with the International understanding. He submitted that, the ship had to be brought from Sharjah where it was used for similar work of

oil exploration & extraction. He contended that the ship was required for the construction of the Offshore platforms is not in dispute, that it is also not disputed that it satisfied the technical specifications for the nature of the work and that it was used solely to enable the construction of the Offshore platform. He submitted that, provisions of Section 44BB is relevant only to the limited extent of appreciating the various actions that would be treated as in the nature of oil exploration. He contended that, it covered all those services that assisted in the ultimate aim of exploration or extraction. He contended that the prospecting for the mineral oil required the special platform is not in dispute and since NR had only assisted in the construction of the platform which is to be used for the prospecting for, extraction of the oil, it is part of the entire process of oil exploration & extraction.

He contended that DTA is an understanding between UK and India with the sole view of providing recognition of areas of work & income which are agreed to be allowed to be carried in both the countries by both of them and the manner in which the income are liable to be taxed and both the countries have accepted that they would honour the agreement to its letter. He contended that, DTA therefore had come to be regarded as a mini code in itself and overrides whatever that is contained in the taxing statutes.

He pleaded that, the hire had to be treated as in the nature of shipping income arising out of plying in International waters and therefore Article 9 of DTA squarely apply. He pleaded that, in the event of the hire income not being treated as not falling within Article 9 of the DTA then the general clause on business viz., Article 6 would come into operation and since, NR has no permanent establishment in India, the business income from hire would be liable to be taxed only in UK. He also placed reliance on the Bombay High Court decision in McDermott International Inc. v. Union of India [1988] 173 ITR 155.

8. The rival submissions and the materials that have been emphasised upon by the parties have been very carefully considered. In the instant case before us we are called upon to decide whether the income from hire of the ship M.V. Pelican by NR to the assessee which has been contracted by MDL in connection with its

contract with ONGC for the project of construction of Offshore platform in the Bombay High Seas is liable to tax in India or not. In order to decide this issue it is necessary to appreciate the nature of the ship, the use which it is capable of being put to and for what purpose it is used.

The nature of the ship can be derived from the purpose for which it is hired. The purpose of its hire is delineated by the CIT(A) in his order from the letter dated 25-11-1992 from MDL to Director General of Shipping. This is reproduced for the sake of facility : 2. M/s. Interocean have offered a substitute vessel "M.V. Pelican" as Anchor Handling Tug in lieu of "M.V. Gomes Defender" which is technically acceptable to us.

3. "M.V. Pelican" is very versatile and technically more suitable for our Offshore operations. The day rate for the Charter hire are the same as day rate of "M.V. Gomes Defender" and lowest as compared to rates quoted by other bidders. Our requirement for Charter hire of this vessel is approx. 170 days.

4. We are in the process of issuing the letter of Intent to M/s.

Interocean Shipping (P.) Ltd., Bombay on a condition that they will obtain the necessary approval from the D.G. Shipping prior to mobilization of the vessel. In order to mobilize this vessel we request you to kindly grant them necessary permission/approval, clearance etc., at your earliest as Anchor Handling Tug is urgently required by us to assist our DB Mahavir in Bombay High for construction of Offshore platforms.

The reading of the above indicates that the ship supplied by NR is not a shipment for passenger or cargo or a trailer vessel but a sort of machinery which assists in the construction of Offshore platforms for the Oil exploration/extraction. The vessel that is hired is stated to be technically superior for the anchor handling. The word 'anchor' means to hold and the word 'tug' means to pull hard. This indicates that, the vessel is meant to assist in the construction of the platform by providing such facility so that the platform remains stationary at one place. In our view therefore the ship so supplied by NR placing it in the same category as a passenger or a cargo or a trailer would be wrong because it is the usage for which it is put to that

would determine its nature. Since, it is an undisputed fact that the ship was so hired because of its technical viability and utility especially for Offshore Platform constructions and has been exclusively used only for the construction of Offshore Platform that too in connection with the Oil exploration/extraction, its hire is directly related to oil exploration/extraction.

Section 44BB is an exclusive section that deals with the income arising from the exploration, extraction, ship or machinery used or to be used in connection with such exploration. The said section in unambiguous term states that it includes in its purview the usage of any ship or machinery for the purpose of extraction or exploration and therefore the hire charges paid to NR by the assessee for the Charter hire of the ship M.V. Pelican is squarely covered by the provisions of the said section.

We have earlier observed that the ship hired out by NR is not a ship but is a specially designed vessel of the nature of a machinery which would ply in the ocean and assist in the construction of Offshore platforms that are used for the exploration of mineral oil. Therefore, the claim of the appellant that the hire charges received by NR is taxable in the Contracting State because of Article 9 of the DTA, is rejected because the said article covers shipping income arising from the operation of ships.

The alternative submission of the learned Senior Advocate Mr. Dastur that Article 7 of DTA would cover this feature as of business in our view gains weight in the light of the special nature of the vessel and its usage. Article 7 of DTA covers business profits to be taxed in the Contracting and the Contracted State, i.e., the Other State only when the enterprise who is a resident of the Contracting State has a permanent establishment in India such as maintaining of an office etc.

In the instant case it is undisputed that NR is a resident enterprise in UK, it has as its business hiring out its vessel for Offshore operations and that it is not the case of the department that NR has any permanent establishment in India. Therefore, we are of the opinion that, the hire charges paid to NR would be liable to be taxed in UK in view of the provisions contained in Article 7 of DTA. Since, the hire charges are not subjected to Indian Taxation, question of deducting any tax from

the hire charges payable to NR does not arise. We accordingly uphold the order of the CIT(A).

The other alternative submission that the ship should be treated to have plied in international waters and that the Territorial Waters Act, 1976 only permitted rights of exploration and did not extend the Indian territory, in our opinion would be a mere academic discussion that need not be gone into and therefore we do not express our opinion on those submissions of the parties. Before we part we may observe that the Tribunal in ONGC's case (supra) was concerned with a hire of a vessel for transportation of men and machine to its work site and such hire was considered as not covered by shipping activity. In Donald William Rickard's case (supra), the Tribunal was concerned with the effective of the notification issued in regard to the exclusive economic zone it was held that it would be applicable for the financial year commencing from 1-4-1983 relevant for the assessment year 1984-85. Similar was the view of the Bombay High Court decision in McDermott International Inc.'s case (supra). In Donald William Rickard's case (supra), the extension of territory of India by the Territorial Waters Act, 1976 was examined, but we do not feel it necessary to go into this aspect because it is found that the present facts of the case squarely falls within the purview of Article 7 of DTA. Therefore, none of these decisions have any bearing to the present facts of the case. In the result, the appeal of the revenue fails and is dismissed.

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