

A.P. Power Generation Vs. the Assistant Commissioner of

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Court : Income Tax Appellate Tribunal ITAT Hyderabad

Decided On : Mar-07-2006

Reported in : (2007)105ITD423(Hyd.)

Judge : D Manmohan, J S Reddy

Appellant : A.P. Power Generation

Respondent : The Assistant Commissioner of

Judgement :

1. These are cross appeals filed against the common order passed by the Commissioner of Income-tax (Appeals)-V, Hyderabad vide his order dated 29.11.2002 for the assessment years 1999-2000 to 2002-2003.
2. As the issues arising in all these appeals are common, for the sake of convenience, they are heard together and disposed of by way of this common order.
3. Brief facts of the case are given below. The assessee is a State Government undertaking, which came into existence with effect from 1.2.1999 after restructuring of the erstwhile Andhra Pradesh State Electricity Board (hereinafter referred to as APSEB). Japan Bank for International Co-operation, (hereinafter referred to as JBIC) which was formerly known as 'Overseas Economic Co-operation Fund' had signed a loan agreement with President of India on the 10th February 1988. JBIC had agreed to lend the President of India 26101 Million Yens

under the loan agreement for the purpose of implementing Srisailem Left Bank Project Power Station. The loan carried a simple interest @ 2.75 per annum. The loan amount was to be utilized for the purposes of procuring goods and services specified in the loan agreement. The loanee was to authorize the then A.P. State Electricity Board to implement the project through the Government of A.P. The project as defined in the loan agreement was Srisailem Left Bank Power Station Project. Under clause 4 of the loan agreement the borrower was to authorize APSEB to implement the project. The borrower was to furnish JBIC with the progress reports for the project on a quarterly basis until the project is completed. Two further agreements were entered into by and between JBIC and the President of India on the 28th February 1995 and 12th December 1997. Under the second loan agreement JBIC had agreed to lend a sum of 22567 Million Yen and under the third agreement a sum of 14499 Million Yen. Thus the total aggregate loan amount-agreed to be given by JBIC to the President of India was 63167 Million Yen. The Government of India lent the money in turn to the Government of Andhra Pradesh.

Government of Andhra Pradesh identified APSEB as the agency to implement Srisailem Left Bank Project Power Station, across river Krishna in Srisailem. APSEB, which was implementing the Srisailem Left Bank power Station Project on the basis of a global tender, selected Sumitomo Corporation for supply of equipment being Turbines, Generators, Gas Insulated Switchgear and XLPE Cables. Separate agreements were entered into between APSEB and Sumitomo Corporation.

3.1 APSEB entered into Contract No. CPH/OECF/LBPHDCH-31/89/1/91-92 dated 25.5.1991 with Sumitomo Corporation, Japan. The agreement was for supply of pump turbines, inlet valves, motor generator sets, associated auxiliary control and ancillary equipment. The contract price is defined in Clause 2 of the Agreement. The Yen component of the payment was 26.822 Billion and Indian rupee component Rs. 92.79 Crores. The.

contract provides for the detailed list of plant and machinery and equipment to be supplied by Sumitomo Corporation, Japan. The scope of contract clearly

envisaged that Sumitomo Corporation would supply the various items of plant and machinery and equipment specified in the contract agreement. This agreement did not envisage the erection and commissioning of the pump turbines by Sumitomo Corporation or BHEL.

This was an agreement exclusively for the sale and supply of the pump turbines and the connected equipment. The contract envisages that out of the total consideration payable to Sumitomo Corporation, a sum equivalent to 360 Million Yen relates to charges for supervisory Engineers for assembly erection, testing including field testing and commissioning as per Schedule 1, Statement 7 of the Contract. This related to the supervisory charges payable for the assembly of the turbines. Out of the total consideration, another payment of 345.6 Million Yen related to charges for Supervisory Engineers for assembly erection, testing and commissioning and field-testing of generators and controls as per Schedule 2, Statement 2 of the Agreement. APSEB entered into an independent contract with PES Engineers for the purposes of erecting and commissioning the generators, turbines and the other equipment.

3.2 The second agreement dated 7th September 1994 was entered into between APSEB and Sumitomo Corporation with respect to Gas Insulated Switch Gear. This agreement provided for contract price of Japanese Yen 4126.30 Million. The obligations of Sumitomo Corporation are specified in the said Agreement. In accordance with this agreement the contract price is for the purposes of supply of 400 KV Gas Insulated Switch Gears complete with SF6 Gas Metal annexed double gas bars and the various other items set out in the Agreement. The Agreement also envisaged a payment of 122 Million Yen only for the purposes of supervising the erection. APSEB did not get the Gas Insulated Switch Gear installed by Sumitomo Corporation. A separate contract for installation of Gas Insulated Switchgear was given to Larsen and Toubro Limited. The consideration paid for such installation was in the sum of Rs. 27 Lakhs. The assessee claimed that it was not a turnkey contract whereby the procurement and installation were both the obligation of Sumitomo Corporation; it was a pure and simple case of supply of equipment.

3.3 The third contract dated 25th April 1995 was entered into with Sumitomo Corporation for the supply of 400 KV XLPE Insulated Power Cables. The agreement envisages a consideration of Japanese Yen 2664 Million. This consideration was for the designing, manufacturing shop testing and supplying 400 KV 1000 Sq. MM XLPE Cables and its accessories. The assessee claimed that this was a supply contract, which did not involve any erection on the part of the Sumitomo Corporation. Under the local services Agreement for 400 KV XLPE Power Cables Sumitomo Corporation had a separate obligation to install the said cables. Under this contract APSEB had a separate obligation to pay a sum of Yen 1368.59 Million. There was also a rupee component payment contemplated in favour of Sumitomo Corporation in the sum of Rs. 6.87 Crores.

3.4 The fourth Agreement was executed with Electrical Power Development Company Limited, Japan (hereinafter referred to as 'EPDC'). By this agreement M/s. EPDC was awarded retainer-ship to advise the assessee on a continuous basis in the Project.

3.4(i) The Assessing Officer issued a show cause notice dated 11-03-2001 proposing to hold the assessee as a defaulter for not deducting taxes on remittances to Sumitomo Corporation and EPDC. In response to the show cause notice the assessee contended as follows.

3.5 In so far as that portion of the consideration relatable to sale of equipment is concerned, there was no question of deduction of any tax at source, inasmuch as the same was towards capital acquisition. Consequently there would be no liability to deduct taxes at source. The supply of equipment by Sumitomo Corporation to the assessee did not result in any income chargeable under the provisions of the Income-tax Act and hence the basic condition of the provision as contained in Sub-section 1 of Section 195 of the Income-tax Act was not satisfied.

The title to the equipment was transferred by Sumitomo Corporation to the assessee at the time such equipment was actually loaded free on board at the port of shipment. The equipment was imported into India by the assessee and necessary taxes and duties were paid by the assessee to the tax authorities in relation to such import. This is evidenced by the contract documents as well as

other documents like the Bills of Lading etc. In other words, no part of the sale price would form part of taxable income under the purview of the Income-tax Act. Further paragraph 1 of Article 7 of the DTAA between India and Japan clearly lays down that profits of Japanese enterprise can be taxed in India only if it carries on business in India through a Permanent Establishment. It lays down further that even if a Permanent Establishment is present, only so much of the profit as is directly or indirectly attributable to that Permanent Establishment can be taxable.

In the present case, no part of the income of Sumitomo Corporation in regard to sale of equipment under the three contracts was attributable directly or indirectly to the Permanent Establishment in India. The services were rendered by Sumitomo Corporation for which a consideration is mentioned as a part and parcel of the supply contract between Sumitomo Corporation and APGENCO. There was no supervising and erection service at project site, which was independent of supply contract. There were innumerable parts, which were shipped by Sumitomo Corporation all of which had to be assembled at site. This assembly requires the persons with technical expertise. The services being totally incidental to the supply of the machinery and equipment, there was no obligation on the part of APGENCO to deduct tax.

3.6 In so far as the erection and commissioning of generators, turbines are concerned, a separate agency viz. PES Engineers had been appointed.

A total payment of Rs. 4.9 Crores was paid to PES Engineers for the purpose of erection of the generators and turbines. This obligation was distinct from the manufacturer's obligation to assemble the unit at site. That being the case there was no obligation to deduct tax at source. In so far as the erection and commissioning of 400 KV GIS equipment is concerned a separate agency i.e., M/s. L & T Limited had been appointed at a total contract value of Rs. 27 lakhs. Sumitomo Corporation had considered income from local service contract as taxable in India and they had paid adequate tax in India in respect of the local service contract of XLPE cables by way of advance payment of tax in the relevant previous years.

3.7 The Assessing Officer did not accept the contentions of the assessee. He was of the view that the assessee had committed default by not deducting tax in respect of sums paid to Sumitomo Corporation in the financial years 1998-99 to 2001-02. He treated the assessee as an assessee in default in respect of the amounts set out in paragraph 2 of his order. The entire remittances to Sumitomo Corporation, EPDC & BHEL in these four years had been grossed up and brought to tax at 48%.

3.8 Aggrieved the assessee filed appeals before the Commissioner of Income-tax (Appeals) raising the following grounds: i) On the facts and the circumstances of the case, the ACIT erred in passing an order under Section 201(1) of the Act and in determining the appellant's liability as Rs. 166.82 crores.

ii) The order passed by ACIT is contrary to the provisions of the Act in violation of the principles of natural justice.

iii) The ACIT ought to have given an opportunity of hearing to the appellant before passing the order, and in the absence of it the order as such is void ab initio and requires to be set aside.

Further the ACIT did not provide adequate opportunity to the appellant to furnish necessary documentary evidence and submissions to show that the appellant was not liable to deduct tax at source under Section 195 of the Income tax Act.

iv) The ACIT failed to appreciate that the appellant had not made any payments to Sumitomo Corporation and as a matter of fact, Sumitomo Corporation had not been given any a edit' in the books of accounts maintained by the appellant. Consequently, there was neither a payment by the appellant nor a credit to Sumitomo Corporation in the books of accounts of the appellant as would attract the provisions of Section 195 of the Act.

v) The ACIT ought to have appreciated that in substance, the payment made by the Sumitomo Corporation was as per the instructions of Government of AP/Government of India and that the Government of India treating it as a loan in favour of Government of A.P and Government of A.P in its turn treated it as a loan

to the appellant APGENCO. vi) The ACIT ought to have appreciated that the supply of equipment by Sumitomo Corporation did not result in any income chargeable under the provisions of the Income Tax Act and hence the basic condition of the provision as contained in Sub-section (1) of Section 195 of the Income Tax Act was not satisfied. The title to the equipment was transferred by Sumitomo Corporation to the appellant at the time such equipment was imported into India by the appellant and necessary taxes and duties were paid by the appellant to the tax authorities in relation to such import. In other words, the sale of the equipment took place outside India and any income from such sale would not form part of taxable income under the purview of the Income-tax Act.

vii) The ACIT has not given due weightage to the fact that in so far as the turbines and generators are concerned, the appellant had engaged the services of M/s. PES Engineers who have been separately paid for erection of generators and equipment. The obligation of PES Engineers was distinct and different from the obligations of Sumitomo Corporation. Therefore, there was no work undertaken by Sumitomo Corporation, which would entail any liability for deduction of tax at source.

viii) Likewise, the ACIT ought to have appreciated that for erecting and commissioning 400 KV Gas Insulated Switch gear equipment, Larsen & Toubro has been appointed and that Sumitomo Corporation did not perform the job of erecting and commissioning.

ix) The ACIT erred in ignoring the terms of the double taxation avoidance agreement between India and Japan, and the fact that Sumitomo Corporation does not have a permanent establishment in India. There was no liability to tax in respect of the work undertaken by Sumitomo Corporation in India in connection with the sale of equipment.

x) The order of the ACIT is biased and prejudiced in as much as the ACIT has taken irrelevant facts into consideration in deciding the issue.

xi) The ACIT erred in finding that the appellant has claimed the benefit of Section 446BB. The appellant had only pointed out that Sumitomo Corporation had paid

tax in respect of 10% of the contract price for the erection of plant and machinery, testing and commissioning portion only. In so far as the sale of equipment is concerned, the appellant had rightly claimed that no tax is deductible as there is no element of income comprised therein as is liable for tax under the provisions of the Act.

xii) The ACIT erred in holding that in the absence of an application under Section 195(2) of the Act, there was liability to deduct tax, without appreciating that in the case of sale of equipment, the said section did not apply.

xiii) The ACIT erred in holding that the entire revenues arising out of the contracts are income chargeable to tax and further erred in grossing up the entire revenues as per the provisions of Section 195A of the Income Tax Act, 1961.

3.9 The Commissioner (Appeals), on a consideration of facts of the case held at para 12.6 of his order that the contracts in question were not contracts of works or turnkey but one of sale. He held that the goods were not in deliverable state and hence the goods were sold in India.

He applied the judgment of the Hon'ble Supreme Court in Transmission Corporation of A.P. Ltd. v. CIT reported in 239 ITR 587 and held that assessee was liable to deduct tax as it had not approached the Assessing Officer. The Commissioner (Appeals) rejected the contention of the assessee that provisions of Section 195 of the Act did not apply on the ground that there was constructive payment in favour of Sumitomo Corporation. He then considered the provisions of Double Taxation Avoidance Agreement (hereinafter referred to as DTAA) between India and Japan in para 16 of his order. He held that as per Article 7 of DTAA, the income was taxable in India and that provisions of Section 195(1) were attracted. The Commissioner (Appeals) further held that in accordance with judgment of jurisdictional High Court in Superintending Engineer, Upper Sileru (APSEB) (152 ITR 753), the liability to gross up was implicit. As far as payment to BHEI is concerned, he held that Section 195(1) did not apply, but the provisions of Section 19 4C will be applicable. The Commissioner (Appeals) applied the judgment of Hon'ble Supreme Court in Transmission Corporation of A.P. (239 ITR 587) and held that tax was to be deducted only with respect of that income that accrued in

India. The Commissioner (Appeals) rejected the alternative claim for estimation being done @ 10% of the payments made to the non-resident as relating to the services rendered in India and for determination of income thereon at 10%, based on the Board's Instruction No. 1767 dated 1.7.87. He estimated that 15% of the gross sums paid should be deemed to be the income of Sumitomo Corporation in India by virtue of the activity carried on by Sumitomo Corporation in India.

3.10 Still aggrieved, the assessee has filed the present appeals on various grounds while the Department has filed cross appeals for restoration of the orders of the Assessing Officer. The Revenue has questioned the determination by the first appellate authority that the payments made to BHEL do not attract Section 195 of the Act, but may be examined in the light of Section 194C of the Act. The Department has also filed an additional ground challenging the determination by the Commissioner (Appeals) that the contracts were not on a turnkey basis, but were contract of sale of goods.

4. The learned Senior Standing Counsel for the Revenue Shri J.V. Prasad made elaborate submission and in his written submissions at para 1 submitted that brief facts as set out above which are extracted from paras 1 to 23 of the written submissions of the assessee are undisputed facts except to the extent of the perception of the appellant that the contracts relating to: a) Pump turbines, in let valves, motor generator sets, associated auxiliary control and ancillary equipment c) 400 KV LPE Insulated Power Cables were either only sale and supply contracts related to supervision of erection, commissioning and testing or were related to third parties like BHEL, EPDC and D&T and were not turnkey projects, does not put the picture in the correct perspective.

5. We first deal with the grounds of appeal of the assessee. The first issue is whether Section 195 is applicable to the facts of the case in view of the complexity and multiplicity of agreements between various parties on terms of payment. Grounds 2, 3, 4 & 5 of the assessee's appeals dealing with the same read as follows.

2) The learned Commissioner of Income-tax (Appeals) V, erred in finding that there was an obligation on the part of the appellant to deduct taxes under the provisions

of Section 195 of the Act. In this behalf the Commissioner of Income-tax (Appeals) did not appreciate in proper perspective the submission of the appellant, that the appellant was not the payer of the amounts to non-residents and consequently there was no liability on the part of the appellant to deduct taxes.

3) The learned Commissioner of Income-tax (Appeals)-V ought to have appreciated that Japan Bank for International Corporation had given a loan to Government of India and that the Government of India in turn had given loan through Government of Andhra Pradesh to APSEB (predecessor of the appellant herein) and that the loan amount was for the purposes of implementation of Srisailem Left Bank Power Project. The payment of money having been made directly by the Bank of India, Japan Branch, against LCs opened in the said Bank by Government of India in favour of Sumitomo Corporation, the appellant had not made any payment whatsoever to Sumitomo Corporation.

4) The learned Commissioner of Income-tax (Appeals) V, ought to have further appreciated that in its books of account, any credit was not given in the name of Sumitomo Corporation. The Commissioner of Income tax (Appeals) ought to have held that the liability to deduct taxes, if any, may arise if and only if the account of Sumitomo Corporation was credited in the books of account of the appellant and not otherwise.

5) The learned Commissioner of Income-tax (Appeals) V, ought to have followed the decision of Jodhpur Bench of Income-tax Appellate Tribunal in the case of Hindustan Zinc Limited which was on all fours to the facts of the case. The payment mechanism referred to in the said decision being almost identical to the payment mechanism envisaged in the present case, the learned Commissioner of Income tax (Appeals) V, ought to have held that there was no payment by the appellant to Sumitomo Corporation so as to attract the obligation to deduct tax under Section 195 of the Act.

The learned Counsel for the assessee submitted that Section 195 of the Act is not applicable to the facts of the case as no payment was made by the assessee Corporation. He submits that Section 195 of the Act applies at the time of crediting to payee's account or alternatively at the time of actual payment to the payee only.

He submitted that in the case of the assessee no payment was made by the assessee to Sumitomo Corporation. He emphasized on the fact that the Government of India established an irrevocable letter of credit drawn on Bank of India, Japan in favour of Sumitomo Corporation. As and when Sumitomo Corporation in Japan made dispatches it used the present documents to Bank of India, Tokyo and obtained payments against irrevocable Letter of Credit established in Japan. The Japan Bank for International Co-operation (hereinafter called as 'JBIC') reimbursed the payments to Bank of India, Tokyo Branch. The Government of India treated the same as loan from JBIC. Government of India lent this money to the Government of A.P. The Government of A.P. identified APSEB as an agency to implement Srisailem Left Bank Power Station Project & directed the amount to be treated as loan owed by APSEB to the Government of Andhra Pradesh. He further submitted that the Government of A.P. after a lapse of several months used to issue Government orders giving clear instructions to the assessee as to the accounting treatment that was to be given in respect of the payments obtained by Sumitomo Corporation from Bank of India. The series of Government orders have been placed in the assessee's paper book from page 172 onwards. The learned Counsel for the assessee submitted that the assessee had no control over the time of payment, actual payment, the quantum of payment and other particulars and it was only after long lapse of time that the payments obtained from Bank of India, Tokyo were communicated to the assessee for the purpose of accounting. He submitted that the accounting entries which have been passed in the books of account are by way of journal entries which were passed pursuant to the orders of Government of A.P. He submitted that the entries would show that the amount was paid by.

Government of India to :Sumitomo Corporation though the assessee had credited the account of the Government of A.P and shown the same as being owed and payable to the Government of A.P. He vehemently contended that it is on record that during the four years in question, there was no capitalization of these assets and consequently there was no accounting entry made in the books of the assessee crediting the amount to the Sumitomo Corporation. He submitted that on these facts there is no liability to deduct tax as both limbs of Section 195(1) of the Act are not attracted as neither passing of credit entries by the assessee or

making payment by the assessee had taken place.

6. Learned Standing Counsel for the Revenue controverted submissions of the learned Counsel for the assessee and has submitted that the assessee was the person responsible for making payment to the non-resident. He submitted that tenders relating to contracts were floated by the assessee and the bids of Sumitomo Corporation were accepted by the assessee directly without the intervention of any outside agency or the Government and that a perusal of the various contracts entered into between the assessee and Sumitomo Corporation categorically established that the assessee was the payer and Sumitomo Corporation was the recipient of the amounts payable under various contracts between the parties. He contended that all the contracts referred the assessee (erstwhile APSEB) as "the buyer" and Sumitomo Corporation as "the contractor". He drew the attention of the Bench to clause 3 of the contract dated 25.5.1991 in respect of the Pump Turbines etc. wherein it is stipulated that Sumitomo Corporation is to supply goods and services in consideration of payment to be made by the assessee. Under clause 4 the assessee covenants to pay Sumitomo Corporation the contracted price at the time and in the manner mutually agreed to between them. Clause 1 of the Supplement to contract agreement states that the contract was arranged in accordance with the loan agreement between the Government of India and the Overseas Economic Co-operation Fund of Japan dated .10-2-1988. Clause 2 stipulates that payment to Sumitomo Corporation shall be made through an irrevocable letter of credit to be issued by the Bank of India, Tokyo, or as prescribed by the loan agreement dated 10-2-1988 (Yen component) and Rupees component payment to BHEL to be made through documents. Thus he submitted that the bids of Sumitomo Corporation for the various contracts were accepted by the assessee and that Sumitomo Corporation was the contractor and the assessee the buyer and further that the assessee was solely responsible for payment to the nonresident and that such payment was to be made as mutually agreed to between the parties. The contract was only arranged in terms of the loan agreement dated 10-2-1988 and the manner of payment to be made in terms of loan agreement was mutually agreed. Thus he submitted that Section 195 is clearly applicable to the facts of the case. As per the contracts between the parties, the mode or manner of payment by assessee to Sumitomo Corporation

was mutually agreed to be made as prescribed in loan agreement dated 10-2-1988 entered into between the Government and OECF of Japan (now JBC). The assessee alone issued global tenders for execution of the projects and had the sole authority to negotiate and accept the bids of various tenderers and to specify its requirements.

Neither the Government of India nor the Government of A.P. was party to any of the contracts between the assessee and M/s. Sumitomo Corporation. Thus he submitted that as far as the assessee and Sumitomo Corporation are concerned, one has to complete the works agreed to and the other has to make payment for the same. For non-payment of contract price by the assessee Sumitomo Corporation can only proceed against the assessee. He further relied on paras 13 to 15 of the order of the first appellate authority on this issue. Thus he submitted that the argument that Section 195 is not attracted is devoid of merit.

7. Rival contentions heard. On a careful consideration of the facts and circumstances of the case on this issue, we are inclined to agree with the finding of the first appellate authority in para 13.4 to para 15.1 at pages 28 to 30 of that order which is extracted below for ready reference: 13.4 However, I am not inclined to accept this argument for the simple reason that as per the appellant's own admission, the payment on behalf of the appellant was made first to the overseas suppliers and the entries in the account were made later after receipt of the Government orders. Therefore, crediting of the amount paid in the accounts and the date of making such credit is immaterial, keeping in view the fact that Section 195(1) provides for deduction of tax at source at the time of credit or at the time of payment whichever is earlier.

14. The next issue is whether the payment made as per the special procedure contained in the said loan agreement referred to above could be said to be a constructive payment made by the appellant even though there was no direct remittance by the appellant.

14.1 In this connection, the learned A.R. of the appellant argued that no payment was made by the appellant either directly or indirectly. The payment was actually made in Japan on the strength of L/C established by the Government of India with

the Japanese Bank (Bank of India, Tokyo Branch) and hence, the appellant was in no position to make a deduction of tax at source from such payment.

14.2 I have duly considered the submissions made by the appellant, but I am not inclined to accept the same. The provisions of Section 195(1) do not speak of direct or constructive payment. The fact remains that the payment was made in accordance with the terms of agreement in which a specific condition was there that JBIC would release fund only for the Power Project under consideration owned by the appellant. Therefore, irrespective of the mode of payment, the fact remained that payment was made for and on behalf of the appellant only and it was the responsibility of the appellant to ensure that in case of such payment, adequate provision is made for ensuring that the TDS as per law in force is effected before releasing such payment. If considered necessary, the appellant could have communicated with the agency of the Government of India i.e.

Department of Economic Affairs, prior to the release of payment. It must be mentioned in this connection that the appellant had earlier experienced difficulties in interpreting the provisions of TDS in respect of payment to overseas parties and the Hon'ble jurisdictional High Court had already interpreted such provision in its own case as far back as in 1984 as has been reported in 152 ITR 753. Further, the decision of the Hon'ble apex court in the case of Transmission Corporation of A.P. Limited, a sister undertaking, has made it absolutely clear that even in case of a trading receipt in the hands of non-resident which may or may not include pure income attracts deduction of tax at source Under Section 195 (1) of the Act. This is because, the language of Section 195(1) for deduction of tax at source by the payer is clear and unambiguous and casts an obligation to deduction appropriate tax at the rates in force.

Therefore, I am of the opinion that in the case of the appellant even though the books of accounts were not credited with the sum paid/payable to the suppliers, yet, it cannot be denied that the payment was made in a constructive manner for which the responsibility of making TDS at source or at least seeking due clarification in this regard from the Assessing Officer (TDS) no doubt, rested with the appellant.

15. The next issue is whether the payment could be said to have been covered with the meaning of the expression "any other mode" used in Section 195(1). The learned A.R. of the appellant was requested to explain as to why such special procedures for making payment could not be said to have been covered within the meaning of the words "any other mode". According to him, such payments are not covered within the meaning of the expression "any other mode". This is because, the expression "any other mode" meant payment made in kind and not in terms of money. On the contrary, Shri V. Sai Prasad Sastry, the Assessing Officer, who passed the order Under Section 201(1) of the Act who was present at the time of hearing of appeal, vehemently argued that the expression "any other mode" has been brought into statute to take care of such situations as is in the present case and the expression meant alternate procedure of payment but not payment in kind as has been submitted by the learned A.R. of the appellant. According to him, the payment could be made either in cash or by the issue of a cheque or a draft or by issue of any other instruction, method or procedure adopted with the knowledge and approval of the payer. Obviously, when APGENCO was the owner of the assets, it was the payer even though the payment was made by the Fund in pursuance of a loan agreement, which ultimately burdened the appellant with the amount paid as loan.

15.1 In this connection, one must keep in mind that the source of payment are not a matter of consideration for the purpose of effecting TDS. Hence it is not important to know as to who provided the funds or who released the payment. But what is important is for and on behalf of whom the payment was released. Moreover, the expression "any other mode", in my opinion, refers to the alternative procedure of payment rather than payment in kind. This is because, payment in cash or cheque or draft are nothing but different procedures for making the money pass from the payer to the payee. In case of cheques and drafts, the bank acts as the medium of transfer of money. In the present case, the special procedure for payment adopted is slightly different from the conventional procedure. But, it is undoubtedly a case of constructive payment covered within the expression "any other mode" contained in the provisions of Section 195(1). Therefore, the provisions of Section 195(1) of the Act are squarely attracted.

8. The agreement in question was between the assessee and Sumitomo Corporation. The duties and liabilities between the parties were governed by these agreements. The assessee is the executing agency, which ultimately, decides whether the contracting agency has complied with the terms of the agreement. The mode in which the finance has been found does not detract from the terms of the agreement. Coming to the reliance placed by the learned Counsel for the assessee on the decision of the Jodhpur Bench of the ITAT in the case of Hindustan Zinc Ltd. v.DCIT 74 TTJ (Jd) 36, we find that the "issue therein is not under Section 195 of the Act. In that case payment was actually made to the Government of India and Government of India had made payment to Crown Agent to M/s. DML having received the money from the Government of U.K.It was the case whether the payments had already been made by the Crown Agent to M/s. DML out of the grant received from U.K. Government and thus it was held that the fees for technical services was neither received no deemed to have been received during the year under consideration for and on behalf of DML and that being the position, the same cannot be said to have been covered under Clause (a) of Sub-section (2) of Section 5. In this case only financing part was undertaken at the Government level. How the assessee had financed this project is not of consequence to the applicability of Section 195. The plain and simple matter is that the assessee floated tenders and entered into agreement with the nonresident company and had in pursuance of the agreement received supply of goods as well as services and had to make payment for the same. For ready reference, we extract below some of the covenants of the contract agreement dated 25.5.91 between the assessee company which is the buyer on one hand and M/s.

Sumitomo Corporation on the other hand: 3. In consideration of the payments to be made by the Buyer to the contractor as hereinafter mentioned the contractor hereby covenants with the Buyer to provide goods and services in conformity in all respect with the provision of the contract.

4. The Buyer hereby covenants to pay the contractor in consideration of providing goods and services the contract price at the time and in the manner mutually agreed to by the contractor and the Buyer.

The fact that the contract is arranged in accordance with the Loan agreement between the Government of India and the Overseas Economic Co-operation Fund of Japan (OECF) dated 10th February 1988 concerning the Yen credit ID-P 43 (Project Aid) for Srisaillam Left Bank Power Station Project and that the fact that the payment to the contractor shall be made through an irrevocable letter of credit to be issued by the Bank of India, Tokyo or as otherwise prescribed under the Loan Agreement referred to above, does not detract from the fact that the primary liability of payment towards goods and services lie with the assessee company and it is the assessee company who has to process the claims and initiate the payment process in terms of the various agreements. The fact also remains that the payments have been made in this case for and on behalf of the assessee. It is the executing Agency which triggers the payment and while passing a bill direction for deduction of tax as per Section 195 while making a payment could be made by the assessee. No payment could have been released without the officers of the assessee company passing the bills consequent to claim made by the contractor. Delay in passing of the entries in the books of account for whatever reason does not erase the fact that the payments have been made in the impugned assessment years. Once the payment is made Section 195 of the Act is attracted. Thus we uphold the finding of the first appellate authority and dismiss this ground of the assessee.

9. The second issue is whether the equipment sold is to be considered as capital equipment and the sale having taken place outside India, for the purpose of ascertaining whether there is any liability on the assessee to deduct tax. Ground No. 6 of the assessee reads as follows: The learned Commissioner of Income-tax (Appeals) V, erred in not accepting the contention of the Appellant that in so far as the contracts for supplies of Turbines and Generators, Gas Insulated Switch Ger Equipment, and 400 KV XLPE Cables are concerned, they were pure supply contracts, that the obligation of Sumitomo Corporation was to manufacture the goods in Japan, that the risk and title in the goods passed to the Appellant on the goods being put on board the ship in Japan that the transaction of sale had taken place entirely outside the Country and accordingly there was no liability to deduct tax in respect of the same.

10. The learned Counsel for the assessee submitted that there is no break up of the figures in relation to the payments made under different contracts to Sumitomo Corporation/EPDC in the four years in question. The assessee had furnished information to the Assessing Officer but the same has not been recorded in the order of assessment.

The learned Counsel furnished the break-up in annexure I to the written submissions. He referred to salient features of the contracts and submitted that on a study of the same, following facts emerge. Three contracts, viz., the contract for procurement of turbines, generators, 400 KV Gas Insulated Switch Gear and Sale of XLPE insulated power cables are pure and simple contracts of sale in this case. He submitted that the scope of each and every contract has to be gone into and drew the attention of the Bench to pages 9 to 18 and pages 40 to 58 respectively of the relevant paper books. He submitted that Sumitomo Corporation did not install the turbines and generators and this work was done by M/s. PES Engineers for whom separate contractual payment was made. Similarly he submitted that installation of 400 KV Gas Insulated Switchgear was done by L & T. He submitted that for both these contracts supervision charges are payable to Sumitomo Corporation for supervising the erection, testing and commissioning of generators/Switch gears. The total quantum of these charges in relation to the value of these equipment is hardly 2 to 3% as furnished in Annexure I to the written submissions i.e. in the case of main generating equipment the percentage of supervision charges in contract value is 2.63% and in the case of 400 KV Gas Insulated Switchgear the percentage is 2.91%. Thus he contended that the quantum of payment made by way of supervisory charges is insignificant compared to the very value of the equipment. He relied on the jurisdictional High Court's decision in the case of C.I.T. v. Sundwiger EMFG & Co. reported in 262 ITR 110 and submitted that supervision was incidental to the sale of plant and machinery and therefore, it must be treated as part of the sale price. Reliance was also placed on the decision of the Kolkata Bench of the Tribunal in the case of DCIT v. ITC Ltd. 82 ITD 239. The proposition is that ancillary and subsidiary services linked to sale also partakes the character of sale and no part of - income is taxable in India. He contended that sale has taken place outside India inasmuch as the contract for sale of Turbines and Generators as well as Switchgear clearly'

envisage that the title to the goods has passed outside India. His contention is that the contracts are F.O.B and freights were paid outside India.

11. The learned Standing Counsel for the Revenue, on the other hand controverts this argument and submits that contracts were turnkey contracts and not one of mere sale of equipment. At this juncture it was mentioned that the revenue filed additional ground of appeal in its appeals. He disputed the finding of the first appellate authority that the contracts in question were not turnkey contracts. He pointed out that the contracts were for supply as well as for setting up of the equipment with supervision and other services related thereto. He submitted that it is essential to gather the intention of the parties by looking into the terms of the contract as a whole. Each of the contracts refer to documents that shall be deemed to form part of the contract between the parties and they include the tender documents comprising the invitation to bid, instructions to Bidder and the general terms and conditions of contract. Thus he argued that the terms and the requirements and specifications of the appellant form part and parcel of their contract with Sumitomo Corporation subject only to modifications agreed to between them by way of correspondence. Thus he submitted that any attempt to delink the contract agreements from the other documents that form part of the contract would not only be truncated but would also make the contracts un-understandable. He contended that the assessee's contract in respect of all the works was with Sumitomo Corporation alone and that no other agreements were entered into by the assessee either with BHEL, PES Engineers or L & T. The fact that Sumitomo Corporation sub-contracted some of the works to third parties is immaterial to the question at issue and that the contract of the assessee with Sumitomo Corporation was on turnkey basis. He referred to scope of the contract in respect of three works which - reads as follows: To design, manufacturing of proto type, testing at manufacturer's works before dispatch customs clearance, delivery up to the project site laying and Installation, testing and commissioning of the Equipment in accordance with the specifications and documents at the site of the proposed Power Station.

Thus he argued that it is of little consequence that separate agreements were entered into between the assessee and the non-resident after the acceptance of

the tenders spelling out the above scope of the contracts. It is the Department's case that the contracts were for execution of work on a turnkey basis and that the goods were put in a deliverable state only in India. He relied on the following judgments: *Vasantha Viswanathan and Ors. v. V.K. Elayawar and Ors.*

paa 10 at page 140 He submitted that the following points emerge from a reading of the above decisions: i) Time of transfer of property in goods depends upon the intention of the parties.

ii) Intention of the parties to be gathered from the terms of the contract iii) Bill of lading operates as transfer of goods and in FOB contracts, it passes to seller when goods are put on board unless intended otherwise by the parties or is subject to special agreement.

iv) In the case of ascertained goods in an undeliverable state, property passes only when they are put in a deliverable state.

He distinguished the decision relied on by the learned Counsel for the assessee and submitted that in the case of *CIT v. Sundwiger EMFG & Co.*

(262 ITR 110 (AP)) by stating that it was not a case where the facts or issue involved were similar to those obtaining in the present case. On the reliance placed by the learned Counsel for the assessee on the decision of the Apex Court in *CIT v. Motor General Stores (P) Ltd.* 66 ITR 692, he submitted that there is no dispute on the veracity of the contract document and the only proposition is that the contract has to be read as a whole and an analysis of the same clubbed with the circumstances showed that the title to the goods passed to the assessee on the successful testing and commissioning of each of the project works. On the decision of the Apex Court in the case of *Mahavir Commercial Co. Ltd. v. CIT* 86 ITR 417 he submitted that therein the Hon'ble Supreme Court was dealing with a case of unascertainable goods in the deliverable state. Referring to the additional ground raised by the Revenue wherein it was reiterated that the contracts in question are turnkey contracts, he submitted that the same should be admitted and stated that all the facts necessary to consider the issue were already on record and it is an issue of law requiring an analysis of the contractual agreement

between the parties involved.

12. Joining the issue, the learned Counsel for the assessee submitted that the stand of the learned Standing Counsel is not correct for the following reasons: (i) The question is what is the time at which the title to the goods passed. In this behalf contract is sacrosanct. He submitted that the clauses in contracts for supply of Turbines, Generators, XLPE cables and Switchgear record that the title has passed outside India and hence sale has taken place outside India.

(ii) As far as the supply part of XLPE contract is concerned, it is submitted that clause 9 of the agreement between APSEB and Sumitomo Corporation envisaged the passing of title on FOB basis and so the title has passed outside India. From this there is no question of erection and commissioning of XLPE cables as the cables were fully manufactured when they were put on board and nothing further was to be done. He pointed out that unlike the other two contracts in the case of XLPE cables, there is no fee for supervision and commissioning and thus they were in deliverable state when they have been put on ship and nothing was required to be done.

(iii) He once again referred to the decision of the Hon'ble Supreme Court in the case of Mahabir Commercial Co. Ltd. (86 ITR 417) and submitted that therein it was held that in the case of contract for sale, the mere fact that the seller does certain acts even after the sale or retains certain amount of control over the assets sold even after the sale, it does not mean that the sale has not taken place earlier. He specifically referred to page 423 of the judgment which reads as follows: But, where however, the seller exercises a right of disposal or where he agrees to deliver the goods at their destination, the carrier is the seller's agent and the delivery is not a final appropriation. The intention of the parties is, therefore, one of the important elements in determining the situs where the property passes to the buyer in pursuance of the contract.

He distinguished the case law relied on by the learned Standing Counsel and submitted that these are contracts of sale pure and simple and the same had taken place outside India.

12.1 On the issue whether the contract is work contract or turnkey contract, and on the additional ground raised by the department, he submitted that the ground itself was belatedly raised and the Standing Counsel sought to rely upon the pre-contract documents, tender document, quotations by different parties and correspondence with parties to show that it was a works contract and not a contract for sale. He referred to paragraph 12.6 at page 24 of the order of the first appellate authority wherein a finding was given that it was a contract for sale and not a works contract. He strongly disputed the admission of the additional ground and on merits submitted that: a) It was not the case of the Assessing Officer who made the assessment that it was a turnkey contract. On the contrary he rejected the claim for estimation of income under Section 44BBB of the Act on the ground that it was not a turnkey contract. He vehemently contended that the learned standing counsel cannot alter the stand of the department and seek to establish a totally new case before the Hon'ble Tribunal. At any rate, he submitted that these documents are of no assistance or relevance.

b) While submitting that the agreement does state that the contract shall include various documents, which are annexed that is not to say that for understanding the plain and obvious terms of the agreement one must look at the tender documents or the correspondence thereafter. He submitted that the correspondence between the parties shows the manner in which the contract was negotiated and at best these can be the background material for understanding the contract as it has fructified and has eventually emerged. The final contract that emerged as a result of negotiation between the parties is what is relevant. To fortify his stand he submits that if the offer was at variance with the contract then only the contract would survive and thus, the process through which the parties passed through which ultimately resulted in the contract being reduced to writing and override the agreement itself. He referred to the Indian Contract Act and Specific Relief Act to support the view that where there is no ambiguity in the terms of a contract it is impermissible to look into the documents exchanged during negotiations. Thus he submitted that the contract does not envisage any type of works contract but it is a case of simple sale contract.

13. We have carefully considered the rival submissions. The principles that emerge from the various case laws relied upon by both the parties can be summarized as follows: (1) In the case of FOB contracts, the property in the goods passes on to the seller when the goods are put on board unless it is intended otherwise by the parties.

(2) Intention of the parties has to be gathered from the terms of the contract.

In this case there are three contracts. The first relates to pump - turbines, inlet valves, motor generator sets, associated auxiliary control and ancillary equipments. The second contract relates to 400 KV Gas Insulated Switchgear. The last contract relates to 400 KV XLPE Insulated Power Cables.

14.1 As far as 400 KV XLPE Power Cables are concerned, the question of them being brought to India in knocked down condition does not arise.

The question of assembling or erection also does not arise. Section 44BBB of the Act applies only in so far as local service contract for installation of these cables is concerned. M/s. Sumitomo Corporation estimated the income from such activity and has already paid taxes thereof. The contract agreement dated 25.4.95 is for the production and supply of such goods and the assessee is termed a buyer. In clause 4 of the covenant, the buyer agrees to pay the contractor for providing goods, the term services is conspicuously absent. Coming to the other two contracts, the machinery in question has been put on board at a Japanese Port FOB in knocked down condition. It was the assessee company which brought these goods into India and thereafter, they were assembled. Though contract documents provide that the custom duty etc.

have to be borne by the assessee company, in further modification it is given that whatever amount is paid by Sumitomo Corporation would have to be reimbursed by the assessee. For ready reference clauses 20.1 & 20.2 are extracted below: It is understood that this Contract is Supply Contract (delivery CIF Indian Port) and that the customs clearance to the port of entry in India and transportation to site from the said port of entry shall be made by the buyer.

Accordingly, this Clause shall not be applied to the Contractor and all Custom Duties, Taxes, Port charges and etc. shall be paid by the Buyer directly to the authorities concerned.

Clause 20.2: Custom Duties, Tax & Port Charges and etc. It is understood that this Contract is Supply Contract (delivery CIF Indian Port). Consequently this Clause shall not be applied to the Contractor.

It is understood that the equipment under scope of supply shall be delivered on CIF Basis at Visakhapatnam Port (India) The deliveries of the cargo was done at Indian Port as it is mentioned as CIF delivery port in the agreement.

15. The first question is whether the contract in question can be termed as a turnkey contract. As already stated the Revenue has filed additional ground wherein it submits that both the Assessing Officer and the first appellate authority have committed an error by coming to a conclusion that the contracts in question are supply contracts and not turnkey contracts. The learned Standing Counsel finds fault with the Assessing Officer's findings. Before we go into the question of admissibility of this additional ground the word turnkey in Oxford Concise Dictionary is termed as "of or involving a complete product or service ready for immediate use." Going by the literal meaning, it appears that purchase of any machinery or even a small item like ceiling fan would tantamount to turnkey contract for it is to be a complete product which is ready for immediate use. Taking the example of a ceiling fan, once the ceiling fan is purchased it is at a place where the buyer requires the same to be installed and after fixing the blades to the motor and the pipe on which the motor is hung the product becomes completely operational on operating the switch. Thus purchasing a plant and machinery in this sense of the term can be called a turnkey job. Definitely it is distinct from the term works contract. The issue for consideration should be whether it is a "contract of work" or a contract of sale". We do not see any merit in the argument of the learned Standing Counsel on this issue as it is the assessee company, which has put up the power plant and only certain plant and machinery, were being purchased. Such purchase of plant and machinery just because they have to be handed over in a ready to function manner, does not make a supply contract into a

turnkey contract in the sense that turnkey is used to mean that the entire power project from the beginning to the end is constructed and handed over in a ready to use manner.

In Black's Law Dictionary, seventh edition, under, the head engineering, procurement and construction contract, turnkey contract is termed as: a fixed-piece, schedule-intensive construction contract-typically used in the construction of single purpose projects such as energy plants-in which the contractor agrees to a wide variety of responsibilities, including the duties to provide for the design, engineering, procurement, and construction of the facility; to prepare start-up procedures; to conduct performance tests to create operating manuals; and to train people to operate the facility-Abbr.

EPC contract. - Also termed as turnkey contract.

Going by this definition, the contract on hand cannot be described as a turnkey contract but just a contract for supply of goods as held by the Assessing Officer as well as by the Commissioner of Income-tax (Appeals). This is not a contract of work, but only a contract of sale for the reasons specified hereinafter in this order. We examine the nature of services involved in these contracts.

15.1 In this case, the power project is being constructed by the assessee company and certain plant and machinery have been purchased by them from M/s. Sumitomo Corporation. Page 22 of the assessee's paper book, Attachment Sheet No. 1 to Statement No. 7, is the statement of man-day rate of the services of Japanese supervisory personnel. At page 32 of the assessee's paper book Sl. No. 5 which is clause 14.0 Contractor's Site Office Establishment it is given as follows: As the contract does not involve the erection work at site, it is understood that the establishment of the contractor's site office is at the contractor's option.

The contract agreement for local service is at page 66 of the assessee's paper book. Payments for this contract are under the following heads: Clearance & Handling charge, Inland transportation, Inland transit Insurance and Unloading & stacking at Buyer's site/warehouse, Storage/and supervision at site laying, termination, testing and commissioning of 5 circuits of 400 KV 1,000 sq mm XLPE

cables (3 cables per circuit with the connected accessories) as set out in detail in these contract documents.

In the agreement No. 1/88-89 between APSEB and EPDC International Ltd. executed on 10.2.1988, reference to the scope of services under Article 3 which is as follows: 3.1 SCOPE OF SERVICES OF RETAINER CONSULTANT FOR TRANSFER OF TECHNOLOGY & KNOW-HOW FOR ENGINEERING AND PROJECT IMPLEMENTATION OF 990 MW, SRISAILAM LEFT BANK POWER STATION PROJECT. The Retainer Consultant shall perform the SERVICES under this contract in accordance with the technical bid and terms of reference set forth as follows: 3.2.1 The Retainer Consultant shall review the Project Report prepared by APSEB/CEA/CWC and advise the APSEB/CEA/CWC on the layout of water conducting system and underground caverns as well as that of equipments covering pump turbines, motor generators, transformers, processor based control and relaying equipment, EHV cable system, Bus ducts, Gas insulated/AIR insulated/Oil insulated indoor and outdoor switchgear and ancillary and auxiliary equipment for efficient operation of power house etc., or any specific problems which may be referred by APSEB/CEA/CWC. 3.2.2 To advise on any clauses of technical nature of the tender documents prepared by APSEB/CEA/CWC. 3.2.3 To advise and render assistance in technical evaluation of bids, as stipulated in Appendix "D" hereto wherever considered necessary by APSEB/CEA/CWC. 3.2.4 The Retainer Consultant shall assist APSEB/CEA/CWC on the review of vendor drawings and related calculation-sheets of fundamental or basic design drawings of electrical equipment as specified in Appendix 'D' hereto, whenever considered necessary by APSEB/CEA/CWC by mutual consent.

3.2.5 The Retainer Consultant shall assist APSEB/CEA/CWC on the performance guarantee tests of the first generating unit at the site.

3.2.6 To advise the APSEB in working out implementation programme and establish monitoring systems to watch the progress of works and expenditure, and preparing norms and systems for the performance.

3.2.7 To advise fixing priorities and sequence of construction with specific time schedule.

- 3.2.8 To advise on proper techniques and methodologies in the various fields of construction.
- 3.2.9. To advise on blasting pattern and support system for ground excavation.
- 3.2.10 To assist the APSEB/CEA/CWC in choice and design of starting method of pumping mode.
- 3.2.11 To advice in organization and placement of various construction supervision units and provision of "quality control facilities like testing, instrumentation, and training and suggest general procedures for review and improvement on project implementation.
- 3.2.12 To accept engineers of APSEB/CEA/CWC for a total 12 (Twelve) man months consisting of Six (6) Engineers for two months each to visit stations in Japan both under Construction and in operation to study, design, construction and operation/maintenance.
- 3.2.13 The Retainer Consultant shall furnish monthly reports of the services carried out by him for the project.
- The Retainer Consultant shall provide 8 (Eight) copies of his reports and drawings, if any prepared by him as part of his service.
- 3.2.14 The Retainer Consultant shall also review progress reports prepared by APSEB covering various areas of work with reference to scheduled programmes pinpoint slippages and suggest corrective action required for restoring the schedule.
- 3.2.15 The Retainer Consultant shall also supply typical design memoranda relating to similar type of pumped storage Hydro Electric Schemes of comparable size for reference in APSEB/CEA/CWC as supplemental consultancy service subject to mutual consent.
- 3.2.16 The Retainer Consultant shall undertake other design and Engineering works which may be entrusted to him by APSEB/CEA/CWC as supplemental consultancy services, subject to mutual consent.

3.2.17 The Retainer Consultant shall provide the latest technical know-how to CEA/CWC in design and Engineering of pumped storage projects in addition to Srisailem Left Bank Power Station, if so desired by these organizations, as supplemental Consultancy Service subject to mutual consent.

3.2.18 The Retainer Consultant shall assist APSEB/CEA/CWC in submitting and reporting various kinds of documents to OECF and in applying for their approval.

3.2.19 To attend the co-ordination meetings and any other meetings at site of work and other places in India by mutual consent.

15.2 We have taken the above extracts as a sample for enabling us to come to a conclusion as to whether the contract in question can be considered as turn key contract or a supply contract. The nature of services contemplated in these contracts are vital for the decision. In our considered opinion a combined reading of the terms and conditions of these agreements fortify the view of the Assessing Officer as well as the first appellate authority that the contracts in question are not turnkey contracts as being claimed by the learned Standing Counsel but were contracts for supply. The Hon'ble jurisdictional High Court in the case of C.I.T. v. Sundwinger EMFG & Co. 262 ITR 110 (AP) had considered an identical issue. In that case also, separate agreements were entered into for supply of capital equipment as well as for supervision of installation of capital equipment. The Hon'ble High Court concluded as follows: A plain and cumulative reading of the terms and conditions of the contract entered into between the principal to principal, i.e.

foreign company and Midhani, i.e. preamble of the contract, Parts I and II of the contract and also the separate agreement, as referred to above, would clearly show that it was one and the same transaction. One cannot be read in isolation of the other. The services rendered by the experts and the payments made towards the same were part and parcel of the sale consideration and the same cannot be severed and treated as a business income of the non-resident company for the services rendered by them in erection of the machinery in Midhdni unit at Hyderabad. Therefore the contention of the Revenue that as the amounts were reimbursed by Midhani under a separate contract for the technical services

rendered by a non-resident company, it must be deemed that there was a "business connection", and it attracts the provisions of Section 9(1)(vii) of the Income-tax Act cannot be accepted and the judgments relied upon by the Revenue are cases where there was a separate agreement for the purpose of technical services to be rendered by a foreign company, which is not connected with the fulfillment of the main contract entered into principal to principal. This is not one such case and thus the contention of the Revenue cannot be accepted in the circumstances and nature of the terms of the contract of this case.

The Hon'ble jurisdictional High Court in the case of C.I.T. v. Visakhapatnam Port Trust 144 ITR 146 considered the following points: The assessee, the Visakhapatnam Port Trust, exported a large amount of iron ore. In order to speed up export operations it decided to install a plant known as "bucket wheel reclaimer." A German company tendered the contract for the supply of the equipment. An agreement was entered into between the German company and the Port Trust whereby the German company understood to supply the equipment and to delegate an engineer to supervise its installation. A company in Poona was employed to fabricate a steel plate (boom). The equipment supplied by the German company was to be imbedded on the steel plate and delivered at Visakhapatnam. The assembling at the Visakhapatnam Port was to be done at the expense of the Port Trust. The term "erection" used in the contract meant payment of wages to the German supervising engineer and his travel expenses. Under Clause 12(a) of the contract, the purchase price for the equipment was payable in German currency in Germany. Part of it was payable on conclusion of the contract and the balance was payable in twenty semi annual installments.

(ii) that the agreement providing for supervision of the installation work did not amount to business connection nor did the agreement with the Poona company amount to business connection between the non-resident and resident within the meaning of Section 9 of the Indian I.T. Act. Even assuming that all the profits of the German company were to be deemed to have accrued or that all the profits of the German company were to be deemed to have accrued or arise in India by virtue of Section 9 the terms of art. III of the Indo-German Agreement would prevail over Section 9; (iii) that there was nothing in the contract between the German

company and the Port Trust which contemplated that the German company was to set up in India any establishment of a permanent or enduring nature either wholly or substantially, which would amount to a virtual projection of the German company in India. Nor had any evidence been let in this behalf. The agreement was purely for the supply of parts of equipment and for sending of an expert engineer to supervise the erection of the reclaimer by the Port Trust. The contract between the German Company and the Port Trust made it clear that the Port Trust was in charge of installation of the plant.

There was no evidence that the German company reimbursed the expenditure of the Port Trust in this regard. The word "erection" was specifically described in the contract as meaning "wages and traveling expenses". Therefore, the erection of equipment did not.

amount to the German company having a "permanent establishment" in India.

The agreement between the German company and the Poona company did not also amount to the German company having a permanent establishment in India. The original contract between the German company and the Port Trust completed the employment of a sub-contractor or sub-supplier. The Poona company was so employed later. There was neither any identify of interest nor identity of character nor of personality, nor was there any unify in profit-making between the Poona company and the German company so that the former may be treated as an Indian agent of the latter.

In this case the value of supervisory charges is just. 2.63% of the total cost of the main generating equipment and 2.91% of the cost of 400 KV Gas Insulated Switchgear. As the jurisdictional High Court has considered a number of judgments and had come to a conclusion and as we are applying the ratio of that judgment to the facts of this case, we do not wish to go into the various other judgments quoted by both the parties in this regard.

15.3 As regards the test to be applied for ascertaining the situs, the Hon'ble Gujarat High Court in the case of C.I.T. v. Saurashtra Cement & Chemical Industries Ltd. 101 ITR 502 has relied on the judgment of the Hon'ble Supreme

Court in the case of Delhi Cloth & General Mills Co.

Ltd. v. Harnam Singh Court In view of this clear-cut pronouncement of the Supreme Court, it is obvious that the amount of the unpaid price cannot be said to be a loan advanced by the non resident company to the assessee-company nor can the nonresident company be said to be a lender to the assessee-company so far as that amount was concerned. Since the non-resident company cannot be said to have lent the amount of unpaid purchase price to the assessee-company either in cash or in kind, there is no question of interest payable by the assessee-company to the non-resident being deemed to be "income" accruing or arising from any money lent at interest and brought into India in kind. Hence, the alternative argument urged on behalf of the revenue must be rejected since there was no money lent by the non-resident company to the assessee-company. Though the amount of the unpaid price was undoubtedly a liability which the assessee-company owed to the non-resident company.

After extracting several authorities on the point, the Court observed in para 48 thereof, as under: But when all is said and done, we find that in every one of these cases the proper law of the contract was applied, that is to say, the law of the country in which its elements were most densely grouped and with which factually the contract was most closely connected. It is true the judges purported to apply the 'lex situs' but in determining the 'situs' they apply rules (and modify them where necessary to suit changing modern conditions) which in fact are the very rules which in practice would be used to determine the proper law of the contract.

The English judges say that when the intention is not express, one must be inferred and the rules they have made come to this, that as reasonable men they must be taken to have intended that the proper law of the contract should obtain. The other view is that the intention does not govern even when express and that the proper law must be applied objectively. But either way, the result is the same when there is no express term.

The 'proper law' is in fact applied and for present purposes it does not matter whether that is done for the reasons given by Cheshire or because the fluid English rules that centre round the 'lex situs' lead to the same conclusion in this

class of case.

Therefore, the correct test, according to the Supreme Court to be applied is the law of the country in which the elements were most densely grouped and with which factually the contract was most closely connected. That is the test to apply, whether one applies the test of "lex situs" as done by the English judges or whether one applies the proper law of the contract. In view of the terms of the contract which we have set out in this case, it is obvious that so far as the non-resident company, Messrs. Ansaldo of Genoa was concerned, all that the company did was to send a representative when the contract was signed in India. Barring that action so far as the performance of the contract was concerned, the non-resident company nowhere came near the shores of India or territories of India. It puts the goods on board the ship concerned at a port in Europe. It received all the price in Europe and that too in terms of foreign currency. The plant was not to be erected or put up by the nonresident company but the assessee company was to set up the plant in India. Even the installments were to be paid in foreign currency.

So far as the unpaid price was concerned, the amount was to be paid by bills of exchange drawn in a foreign country and accepted by the assessee-company in India. Thus, most of the elements of this contract are found to be most densely grouped with the country, namely, Italy, where the non-resident company, Messrs Ansaldo is carrying on its business of supplying plant and machinery and hence the debt which the assessee-company owed to the non-resident company was not an asset held by the non-resident company in India.

Therefore, the interest which was payable in respect of this debt was not income arising from or through any asset held by the non-resident company in India. Since the non-resident company had no income accruing or arising in India, it cannot be said that there was any liability of the non-resident company to pay income-tax on the amount of interest of the three installments and, consequently there cannot be said to be any liability of the assessee company as the agent of the non-resident company so far as this aspect of income accruing or arising through or from any asset held by the non-resident company in India was concerned.

Applying these tests, we have to necessarily conclude that most of the elements of this contract were found to be most densely grouped in Japan, and thus the situs of the contract, though signed in India, has to be held as one which is Japan.

16. Thus in our considered opinion the judgments relied on by the learned Standing Counsel for the revenue, to drive home the point that the intention of the parties as can be gathered from the agreements and other documents is that the property in the goods passed to the buyer only in India though it is a C.I.F. contract, does not advance the case of the Revenue. The mere fact that more than 80% of the contract value pertains to activities that have been undertaken in Japan clearly points out that the element of contract was most densely grouped in Japan and not in India. Just because equipment has been purchased and it is made operational by assembling the same at the buyer's place of work and supervising the erection of such machinery does not make a supply contract into a turnkey contract or work contract. We emphasize the fact that in all the documents the supplier was obliged to depute personnel to supervise the erection, commissioning and testing all these equipments. Thus in our considered opinion, this is a pure sale contract and not a works contract.

17. Now we deal with ground Nos. 11 & 12 which relate to XLPE cables contract. The ground reads as follows: 11) Without prejudice the learned Commissioner of Income-tax (Appeals) V, ought to have accepted that then provisions of Section 44BBB of the Income tax Act, 1961, applies only in so far as local services contract for installation of 400 KV XLPE Cables is concerned.

12) The learned Commissioner of Income-tax (Appeals)V, ought to have taken into consideration the fact that Sumitomo Corporation had estimated the income from such activity, paid taxes thereof and that there was no liability on the Appellant.

The case of the assessee is that Sumitomo Corporation has recognized that it is liable to tax in respect of the installation work undertaken and has estimated its income under Section 44BBB of the Act and filed its returns. It is, therefore, the case of the assessee that if the quantum was wrongly assessed then it is a matter for the Assessing Officer of Sumitomo Corporation to deal with the same and reliance is placed on the judgment of the Gujarat High Court in the case of C.I.T.

v.Rishikesh Apartments Co-operative Housing Society Ltd. 253 ITR 310. His submission is that as the assessee has already paid the taxes, there is no liability on the appellant. The Revenue submits that the payment of advance tax by Sumitomo Corporation does not come to the rescue of the assessee as the impugned order is one passed under sc. 201 of the Act and not one which is passed under any regular assessment.

17.1 The judgment of the Hon'ble Gujarat High Court in the case of Rishikesh Apartments Co-operative Housing Society Ltd. (supra) is not applicable to the facts of the case as per the learned Standing Counsel as there was no regular assessment in the case of Sumitomo Corporation.

It was further submitted that the Hon'ble Gujarat High Court had not considered the judgment of the Hon'ble Supreme Court in the case of Transmission Corporation of A.P. Ltd. v. CIT 239 ITR 587 as well as the jurisdictional High Court's decision in the case of C.I.T., A.P. v. Superintending Engineer, Upper Sileru 152 ITR 753.

18. After hearing both the parties, we are of the considered opinion, that the assessee definitely had obligation in this case to deduct tax under Section 195 of the Act. This is also not disputed by the assessee. The only claim of the assessee is that there was no question of levying any interest on the assessee under Section 201(1 A) as the amounts which were payable to the Revenue have been duly paid directly.

The Hon'ble Gujarat High Court in the case of Rishikesh Apartments (supra) at page 315 para 2 observed as follows: If one looks at the fact whether Ravi Builder had in fact paid the amount of tax payable by it on the amount which was paid to it by the assessee, one finds that Ravi Builder had paid the tax. In fact for both the years, it had paid more advance tax than what was payable by it. Thus, the entire amount of tax which was payable by it had been duly paid. Had Ravi Builder not paid tax on the amount which it had received from the assessee, the Revenue could surely saddle the assessee with the liability of payment of interest under the provisions of Section 201(1A) of the Act. But in the instant case, as Ravi Builder had already paid the tax on the income, in our opinion, there was no question of

levying any interest on the assessee as the amount which was payable to the Revenue had been duly paid. In other words, we may say that the liability of the assessee-society to make deduction at source and pay the tax to the Revenue is not independent of the liability of the contractor or Ravi Builder to pay tax. If assessment in relation to income of Ravi Builder, i.e., the contractor, had become final and no further tax was found due from Ravi Builder, that would put an end to the liability of the assessee-society and as the assessee-society was not liable to make any payment of tax on behalf of the contractor, no amount of interest could be leviable under the provisions of Section 201(1A) of the Act.

If the Revenue is permitted to levy interest under the provisions of Section 201(1A) of the Act, even in a case where the person liable to pay the tax has paid the tax on the date due for the payment of the tax, the Revenue would derive undue benefit or advantage by getting interest on the amount of tax which had already been paid on the due date. Such a position in our opinion cannot be permitted.

18.1 The contention of the learned Counsel for the Revenue that the statutory provisions do not support the contentions of the assessee, in our considered opinion, is also not correct.

18.2 What is to be understood is that tax deduction at source is only provisional payment. The jurisdiction High Court in the case of CIT v. Superintending Engineer, Upper Sileru 152 ITR 753 had brought out this view at page 776 which reads as follows: It should also be borne in mind that whatever tax is deducted at source under Section 195 from out of the gross sum is not irretrievably lost to the recipient. It is only a provisional payment which will be made to the Central Government to the credit of the recipient. The provisions of the Act enable the recipient, whether such recipient is a resident or non-resident, to file a return of income in the regular course and prove to the satisfaction of the ITO the income chargeable under the Act. After such determination, if the tax provisionally deducted at source under any of the provisions contained in Part B of Chapter XVII is in excess of what is required to be paid, the ITO is bound to grant refund of the excess tax deducted at source with interest to the recipient.

Thus, the interests of the recipients are fully protected under the scheme of the Act. We do not see any ground for the person responsible for making the payment to object to the deduction of tax at source provisionally either from sums which represent wholly income or from sums which represent only a part of the income chargeable under the provisions of the Act, so long as the recipient is clearly told that the tax deducted at source from out of the sums paid are liable to be refunded by the Income-tax Department to the recipient if, by any chance, the tax deducted at source is more than the tax properly chargeable on the total income of the recipient.

Thus if the deductee has made a direct payment and has filed his return of income, dehors Explanation to Section 191, it cannot be said that default continues. The term default has not been defined in the Act. As per Black's Law Dictionary, Seventh Edition, default means 'the omission or failure to perform a legal or contractual duty; esp., the failure to pay a debt when due. In K.J. Aiyer's Judicial Dictionary 8th Edition the meaning of default is given as 'Neglect, omission or failure to do something.' 18.3 Going by these definitions, default occurs on the failure on the part of the assessee to deduct tax. It continues as long as the assessee or the deductee do not pay the tax which is due. But once the deductee pays tax and files its return, the default comes to an end. It can not be said that the default continues when no money whatsoever is due to the Government, the deductee having paid the tax and having filed his return of income. Once there is no amount legally assessed as due from the deductee and when nobody requires to pay any sum to the Central Government on this assessment, then to hold a person as an assessee in default at a posterior point of time would be illogical.

The primary thing is that there is no sum due which has remained unpaid. At best, the default could be from the date on which tax has to be deducted to the date on which the deductee filed his return of income and paid tax thereon. Otherwise, if after deductee filed his return and the assessments are completed or barred by limitation or accepted without any further demand then, to ask the tax deductor to deduct tax now and remit it to the Government and issue the certificate to the deductee and the deductee again going before the Department for refund of this

tax with interest is nothing but an idle formality which is not contemplated under the scheme of the Act. TDS is termed as provisional payment by the jurisdictional High Court and once the interest of the revenue has been protected by the factum of the deductee filing the return and paying the taxes, it cannot be said that any person continues to be in default. The proposition that when no portion of the gross sums estimated can be considered as income accrued or arisen in India then liability to deduct tax under Section 195 does not arise, is supported by the decision of the ITAT reported in 90 ITD 793 as well as in the case of Raymond's v. ACIT 203 TTJ 120. Our view is further supported by the order of the Mumbai Bench 'B' of the Tribunal in the case of DCIT, TDS Circle v. EXCEL Industries (2006) 5 SOT 235 (Mum.) wherein it has been held as follows: Section 201, read with Sections 17(2) and 221 of the Income-tax Act -Deduction of tax at source - Consequence of failure to deduct or pay -Assessment Year 1996-97 - Whether levy of interest under Section 201(1 A) is a posterior action to declaring an assessee-employer as deemed to be in default and where no fault can be found with employer for not deducting tax on some controversial addition or deducting and paying tax on an honest and fair estimation, he cannot be declared as an assessee deemed to be in default, and, therefore, question of levy of interest under Section 201(1A) would not arise - Held, yes - Whether default in Section 201 is for non-deduction and not for short deduction, and since Section 201 is a penal section, it has to be strictly construed, and it cannot be assumed that there is a duty to deduct tax strictly in accordance with computation under Act and for any shortfall as compared to such strict computation, employer can be declared as assessee-in-default, i.e. it cannot be assumed that due to difference of opinion as to taxability of an item, employer has to be declared to be an assessee-in-default - Held, yes- Whether in absence of any specific order declaring assessee as 'deemed to be in default', order of Assessing Officer under Section 201(1) is liable to be quashed - Held, yes - Assessing Officer having considered that conveyance allowance paid to staff was taxable as perquisite under Section 17(2), ordered collection of deficient tax under Section 201(2) for non-deduction of tax at source on payment of conveyance allowance - He also charged interest under Section 201 (1 A) for failure to deduct tax on payment of conveyance allowance to salaried employees - Whether since assessment of employees to whom conveyance

allowance was paid must have been completed before date when order under Section 201(1) and 201 (1A) was passed, shortfall in tax, if any, in deduction of tax at source had to be paid back by employees while filing their returns - Held, yes - Whether, therefore, Assessing Officer was incorrect in directing to recover deficient tax from employer after expiry of limitation period for completion of assessment of employees - Held, yes - Whether employer-assessee could be faulted for holding an honest opinion that conveyance allowance was not to be included in computation of income of employees while deducting tax at source so as to be declared as an assessee deemed to be in default and charged interest under Section 201 (1 A) - Held, no.

In the case of Gwalior Rayon Silk Co. Ltd. v. C.I.T. 140 ITR 832 it is held as follows: Held also, that where the regular assessment of an employee had been completed and the amount of tax was fully paid, the ITO (TDS) had no jurisdiction under Section 201 to demand further tax from the employer in respect of tax sort deducted relates to such employee.

In C.I.T. v. M.P. Agro Morarji Fertilizers Ltd. 176 ITR 282 (M.P) it was held that: Where the regular assessment of an employee had been completed and the amount of tax fully paid by him, the Income-tax Officer (TDS) has no jurisdiction under Section 201 of the Income-tax Act, 1961, to demand further tax from the employer in respect of tax short-deducted relating to such employee.

18.4 In case the Revenue feels that during the period of default i.e.

the actual date on which the tax is due for deduction and remittance and the date of payment by the deductee, it had lost some interest thus calling for levy of interest for that period under Section 201(1 A), we find that the Act provides that the deductee pay interest under Section 234C and in case the pre-paid tax falls short of requirement of advance tax payments. The interest, of the Revenue is well taken care of by interest levied under Section 234B i.e. interest for default in payment of tax and 234C being interest for deferment of advance tax. The section, i.e. Section 201, in our considered opinion, can be enforced if the deductee has not filed his return of income, or if the deductee is an assessee in default for reason of non-payment of taxes.

18.5 On the other hand, if such levy is permitted it would cause prejudice to the Revenue because it might have to refund the money with interest to the deductee as there is no payment whatsoever due from the deductee in such cases. This would cause loss of revenue. In cases, where a deductee has not paid his taxes or filed his return, the period of default continues and the deductor shall be deemed to be an assessee in default and the liability has to be discharged.

191. In the case of income in respect of which provision is not made under this Chapter for deducting income-tax at the time of payment, and in any case where income-tax has not been deducted in accordance with the provisions of this Chapter, income-tax shall be payable by the assessee direct.

Explanation - For the removal of doubts, it is hereby declared that if any person referred to in Section 200 and in the cases referred to in Section 194. the principal officer and the company of which he is the principal Officer does not deduct the whole or any part of the tax and such tax has not been paid by the assessee direct then, such person, the principal officer and the company shall, without prejudice to any other consequences which he or it may incur be deemed to be an assessee in default as referred to in Sub-section (1) of Section 201 in respect of such tax.

The explanation is inserted by Finance Act with effect from 1.6.2003 and speaks of removal of doubts. Thus the same is retroactive in nature and thus retrospective as it only clarifies the intention of the Legislature, as it always was, as held by the Hon'ble Supreme Court in the case of C.I.T. v. Plantation Corporation of Kerala Ltd. 247 ITR 155(SC). As per the Explanation the Principal Officer and the Company of which he is the Principal Officer, which does not deduct tax shall be deemed to be an assessee in default if such tax has not been paid by the assessee direct. The word "then" clearly denotes the intention of the Legislature that the Principal officer and the Company shall not be considered to be assessee in default if the tax due is paid directly.

The use of the word "and" denotes cumulative conditions one of which is direct payment by deduction. Even under Section 201(1 A), simple interest at the rate of 12% is leviable from the date on which the tax was deductible to the date on which the tax is paid. The payment herein may be a direct payment by the assessee

concerned. The word 'paid' does take into its fold the payment made directly by the assessee concerned.

The revenue's contention that it is not possible for it to ascertain the assessment details of the deductee and that the T.D.S. Officer cannot verify whether the deductee offered this turnover/income to tax is not tenable for the reason that, the information can be easily obtained by requisition of the details from the concerned Assessing Officer as he is also from the department, and by directing the assessee to furnish the same. Even otherwise, if the T.D.S. Officer apprehends underassessment, the same may be brought to the notice of the Jurisdictional Assessing Officer of the deductee for suitable action. The T.D.S. Officer cannot plead helplessness especially when the entire resources of the Dept. are available with him and when the statute confers power on him. Thus in our considered opinion, the assessee cannot be held to be an assessee which is deemed to be in default, when the deductee has filed its return of income and the revenue has accepted the same.

18.7. We find that the issue is as to whether the T.D.S. has to be made on purchase of goods covered against the assessee and in favour of the Revenue by the judgment of the jurisdictional High Court in the case of C.I.T. v. Superintending Engineer, Upper Sileru 152 ITR 753. At page 767 it is held as follows: It is next contended that the obligation to deduct tax at source under s: 195 cannot be held to extend to sums paid to non-residents during the course of regular trading operations, that is to say, where the sums paid to the nonresidents represented value or cost of goods purchased in the course purchased in the course of regular trade. It is urged that, if the provisions contained in Section 195 should be interpreted as sanctioning the deduction of tax at source from out of gross sums paid to non-resident by way of cost of goods, it would lead to serious hardships in the course of international trade. While we agree that some amount of inconvenience and hardship is bound to be felt by the non-residents by reason of deduction of fax at source from sums referable to trading operations, that cannot be a ground for arriving at an interpretation of the provisions of Section 195 to exclude sums paid to non-resident during trading operations. The language of the section is very clear and unambiguous and effect must be given to the clear

provisions of law irrespective of hardships and inconveniences. We are conscious of the fact that the process of making regular assessments on non-residents, after deduction of tax at source under Section 195, may take time and the non-residents may not be able to get back refund of excess tax deducted at source, if any, till the regular assessment is completed determining the tax payable by the non-residents on the total income chargeable under the provisions of the Act. We can only express the hope that the Central Board of Direct Taxes gives instructions to all the ITOs to expedite regular assessments on non-residents, from whom tax is deducted at source, giving top priority and facilitate smooth course of international trade involving large magnitude of trading operations. The tax authorities will do well to make an accelerated assessment on nonresidents under Section 194 of the Act, should circumstances require such a course in order to ensure that the non-residents get back expeditiously excess amounts of tax, if any, deducted at source under Section 195.

Thus even for the payment which is made for value of cost of goods purchased in the course of regular trade, tax should be deducted at source under Section 195 of the Act.

18.8 The learned Standing Counsel has rightly pointed out that the very same assessee was party to the judgment in the case before the Hon'ble A.P. High Court as well as the Hon'ble Supreme Court on the issues and despite suffering adverse decision in these cases has been careless in the present issues also.

19. Now we come to ground Nos. 7 & 8 of the assessee, which read as follows: 7. Alternatively without prejudice as directed by the Central Board of Direct Taxes in its Instruction No. 176, the learned Commissioner of Income Tax (Appeals)V, ought to have estimated the income accruing to Sumitomo Corporation in India on account of the transaction of sale could not exceed 10% of 10% of 1% of the sale consideration, which alone should have been subjected to tax under Section 195 of the Act.

8. At any rate and without prejudice the estimation of income from , the said contracts at 15% is excessive, arbitrary and unreasonable having regard to the fact that in the case of APTRANSCO from identical activities the income had been

estimated at 10% of the contract value, and that therefore the appellant ought to get the benefit of the same.

19.1 The learned Counsel for the assessee submitted that if the Hon'ble Tribunal does not agree with the assessee's contention that the contract in question is sale contract and the sale has taken place outside India, and no portion of income accrues in India even then the assessee is entitled to relief on the following grounds: 1) The Double Taxation Avoidance Agreement between India and Japan (DTAA for short) in Article 7 clearly contemplates that only so much of the income as is attributable to permanent establishment in India can be charged to tax in India. In this context the first question is what is permanent establishment for the purposes of Article 5 of the double taxation avoidance agreement. It is the contention of the learned Standing Counsel was that Sumitomo Corporation had offices in Delhi, Calcutta, Chennai and Mumbai that it had extensive businesses in India and that apart from the Srisailem Left Bank Project Power Station it has also executed various other projects.

It is, therefore the submission of the learned Standing Counsel that Sumitomo Corporation with its permanent establishment in India has carried on the business.

2) The learned Counsel for the assessee, disputing this argument of the Revenue, submitted that the Assessing Officer has not made any efforts to discover what is the extent of activity the so-called permanent establishment of Sumitomo Corporation carried on in India.

The belated efforts on the part of the department to establish that the permanent establishment carried all the business is futile.

Referring to the letters shown by the learned Standing Counsel, he submitted that the offices of Sumitomo Corporation at Chennai and Delhi merely acted as post office. The letters of transmittal and Power of Attorney executed show that it is a convenient location for dispatch of the notices etc.

3) The learned Counsel for the assessee's case is that the contract envisaged designing, drawing and manufacturing of various sophisticated equipment and the

question was whether the Liaison office has undertaken any of these activities. His case is that as no part of the manufacturing activity was done in India and as the liaison offices did not carry out any managerial function and thus they did not constitute a permanent establishment. He referred to the correspondence on which Department relied on to show that all the processes of decision making which is key in any managerial function had taken place outside India and application of mind was entirely outside India. The mere act of receiving letters from the appellant and others and transmitting the same to Japan or receiving communication from other places and forwarding the same to the assessee, as per the learned Counsel, did not constitute an income generating activity of the permanent establishment.

4) Alternatively, without prejudice to his contention that Sumitomo Corporation had no permanent establishment in India, he submitted that even if it is assumed that there is a permanent establishment, the same did not do any tangible work in India and thus no part of the income which was accrued to Sumitomo Corporation under these contracts in India can be attributable to the permanent establishment.

5) Referring to the EPDC contract, he submitted that though there is a finding by the Commissioner (Appeals) that they have a permanent establishment in India, there is no finding by the Assessing Officer or the Commissioner (Appeals) as to what is the work done by the permanent establishment in India. He submitted that at any rate there is no material to conclude that the permanent establishment did any work in India. He emphasized that EPDC never established any office in India though the same was contemplated. Thus he submitted that in the absence of any finding about the extent of work done by EPDC in India through its permanent establishment, there cannot be any liability to deduct tax.

6) Without prejudice to the above contention it is further submitted that even if the act of supervising the erecting and commissioning resulted in any income for Sumitomo Corporation, it is essentially a question of estimation of the income. While pointing out that the contracts specifically provided for supervision of erection and commissioning, he submitted that at best this is the component which is chargeable to tax in India and not the whole. Only the profit element embedded

in the fee for supervision of erection and commissioning, which was payable during the years in question, according to the learned Counsel, can be taxed as per the double taxation avoidance agreement.

7) An alternative contention has been raised that the Central Board of Direct Taxes had issued Instruction No. 1767 F. No. 484/3/87-FTD dated 1.7.1987 wherein only 10% of the consideration paid was directed to be taken as which is deemed to relate to work done in India. Thus he submitted that the profit element thereon is to be estimated at 10%, which can be said to have accrued to Sumitomo Corporation. Thus he argued that only 1% of the total receipts could be treated as profit element which can be said to have been accrued to Sumitomo Corporation which is attributable to work done in India.

He further relied on the judgement of the Hon'ble Supreme Court in the case of Union of India v. Azadi Bachao Andolan 263 ITR 706 and submitted that the instruction issued by the CBDT is binding on the Revenue. While conceding that in that circular the Board was considering the case of oil exploration companies, he submitted that the instructions analogous principle is applicable and at any rate the facts of the present case show that the value of supervision work in India is only between 2% to 3% of the total contract value which is much less than what is assumed in the Instruction i.e. 10%.

20. The learned standing counsel for the Revenue, on the other hand, disputed the contention of the assessee and submitted that the first appellate authority has erred in scaling down the estimation to the rate of 15%. He vehemently contended that the Commissioner (Appeals) has failed to give any basis for restricting and adopting the said rate especially when it is not a case of regular assessment. He contended that the T.D.S. Officer has no jurisdiction to assess the income in its pure, simple and strict sense. Whatever liability raised by the TDS Officer is only temporary in nature and any excess TDS is liable to be adjusted or refunded at the time of final assessment on production of the TDS certificate.

20.1 On the point of Art. 5 & Art. 7 of the DTAA between India and Japan, the learned Standing Counsel submitted that the definition of "Permanent Establishment" as occurring in Art. 5 considered in the light of the documents

annexed under the heading "Permanent Establishment in India" in Book I, II and III, as per the learned Counsel, clearly and clinchingly establishes that Sumitomo Corporation has a permanent establishment in India and that the profits earned by the non-resident are attributable to the permanent establishment. He submitted that it is apparent from the documents that the P.Es in India were headed by senior managerial functionaries of Sumitomo Corporation of the rank of Deputy General Managers and who not only signed the contracts as powers of attorney but were also actively involved in negotiations with the assessee as is evident from the minutes of the meetings and the other correspondence between the assessee and Non-resident. Further he submitted that given the huge nature of the works undertaken by the non-resident in India, the work being attributable to the P.Es cannot be of any doubt as otherwise it would only be pushing the issue under the rug. He submitted that the P.Es were not post offices and the expression 'attributable to' itself puts the issue in a wide perspective. He relied on the orders of the Commissioner of Income-tax (Appeals) in so far as EPDC is concerned and on specific findings at paras 16.4, 18.2 and 21.2. He contended that the assessee had not come out with any contra positive evidence to come to a different conclusion.

20.2 On the CBDT Instruction in question, he submitted that it was issued in relation to exploration of oil and natural gas and the nature of the work in this case being different, the instruction cannot be generalized.

20.3 On the departmental appeal, he submitted that it is not for the TDS Officers who has no jurisdiction over the non-resident to be convinced especially when no details of the gross receipts etc. are given by the non- resident. He submitted that in the absence of an appropriate application under sec, 195(2) of the Act with the relevant documentary evidence, the action of the TDS Officer cannot be found fault with on this score.

21. The first question that arises for our consideration is whether the non- resident has a permanent establishment in India and if so, any part of the and profit thereon is attributable to the said permanent establishment. Before we go into these facts, we extract below for ready reference Art. 5 and Art. 7 of the Double Taxation

Avoidance Agreement between India and Japan.

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 a 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 of natural resources, built only if so used for a period of more than six months.

3. A building site or construction, installation or assembly project constitutes permanent establishment only if it lasts for more than six months.

4. An enterprise shall be deemed to have a permanent establishment in a Contracting state and to carry on business through that permanent establishment if it carries on supervisory activities in that Contracting State for more than six months in connection with a building site or construction, installation or assembly project, which is being undertaken in that Contracting State.

5. Notwithstanding the provisions of paragraphs 3 and 4 an enterprise shall be deemed to have a permanent establishment in a Contracting State and to carry on business through that permanent establishment if it provides services or facilities in that Contracting State for more than six months in connection with the exploration, exploitation or extraction of mineral oils in that Contracting State.

6. Notwithstanding the provisions of the preceding paragraphs of this article, the term "permanent establishment" shall be deemed not to include: (a) the use of facilities solely for the purpose of storage or display 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 or display; (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 carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.

7. Notwithstanding the provisions of paragraphs 1 and 2, where a person other than an agent of an independent status to whom paragraph 8 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 Contracting State, if (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; (b) he has no such authority, but habitually maintains in the first-mentioned Contracting State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise: or (c) he habitually secures orders in the first-mentioned Contracting State, wholly or almost wholly for the enterprise itself or for the enterprise and other enterprises controlling, controlled by, or subject to the same common control as that enterprise.

8. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that Contracting 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.

9. 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 Contracting State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

1. The profits of an enterprise of a Contracting State shall be taxable only in that Contracting 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 that other Contracting State but only so much of them as is directly or indirectly attributable to 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 separate enterprise engaged in the same or similar activities under the same or other similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.

3. In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the Contracting State in which the permanent establishment is situated or elsewhere.

4. In so far as it has been customary in a Contracting State 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 paragraph 2 shall preclude that Contracting State from determining the profits to be taxed by such an apportionment as may be customary; the method of apportionment adopted shall, however, be such that the result shall be in accordance with the principles contained in this article.

5. 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.

6. For the purpose of the provisions of the preceding paragraphs of this article, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

7. 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 provisions of this article.

The undisputed fact is that the non-resident Sumitomo Corporation has filed its return in India and has paid advance tax and assessments were made. While so, we do not understand as to how the learned Counsel for the assessee argues stating that there was no permanent establishment in this country. A plain reading of the Double Taxation Avoidance Agreement at any rate does not contemplate that each and every work has to have a separate and independent permanent establishment. 'Permanent Establishment' is an inclusive definition and under Article 5 (4) there is a deeming provision which in our view applies to this case. The deductee had a place of management as well as a building site for more than six months, and it suo motu filed its returns of income. Thus on this sole fact itself, we uphold the contention of the learned standing counsel. Thus the finding of the first appellate authority that the assessee has permanent establishment in India in terms of Art. 5 of the DTAA is upheld: 22. This brings us to the question whether any part of the transaction should be attributable to the permanent establishment in India. Various correspondences filed by the parties show that the permanent establishment in India was not merely post office but was something more than that. The supervisory personnel of the non-resident company have spent a number of years i.e. beyond the period of six months in this country and this factor goes against the claim made by the assessee. Thus we uphold the findings of the first appellate authority on this issue also. The argument of the assessee that no proof or, evidence has been brought out by the Assessing Officer to prove that the permanent establishment has in fact income which is attributable to it in this transaction is devoid of merit. The correspondence filed by the learned Standing Counsel speaks otherwise.

23. This brings us to Art.7 of DTAA. A plain reading of Art. 7 show that only that portion of income which is attributable to the permanent establishment in this country is taxable in this country. Definitely the entire contract cannot by any stretch of imagination be treated as income which is attributable to the permanent establishment. At best, the supervisory charges which formed less than 3% of the

total value of the contract can be said to be attributable to the permanent establishment. The profit arising out of these service contracts, if any, has to be considered as taxable income in the hands of the non-resident company.

24. The next contention is whether the act of not making application under Section 195(2) to the Income-tax Officer does empower the ITO to enforce deduction of tax from the gross sums of money. This issue has been decided by the jurisdictional High Court in favour of the assessee in the case of CIT v. Superintending Engineer, Upper Sileru 152 ITR. We are unable to accept the contention of the learned Counsel for the Revenue that, because the assessee did not file an application under Section 195(2), the ITO is empowered to call upon the assessee to pay tax under Section 195 in respect of the entirety of the gross sum. It should be borne in mind that a person may be honestly under the impression that no part of the gross sum payable to the non-resident is chargeable to tax as income under the Act and, hence, he does not find it necessary to make an application under Section 195(2). The ITO, on the other hand, may be again honestly under the impression that the gross sum of money includes some portion chargeable under the I.T. Act. Could it be said that, under such circumstances, the person responsible for making the payment could be punished or penalized by requiring him to pay the tax deductible on the entirety of the gross sum? The answer is clearly negative. We cannot accede to the contention of the learned Counsel for the Revenue that the ITO is entitled to call upon the Electricity Board, to pay tax deductible under Section 195 in respect of the entirety of the payments made to M/s. Charmilles Engineering Works Ltd. in R.C. 203 and to M/s. Oerlikon Engineering Company in R.C. 205. It must be remembered that the order was passed under Section 201 of the Act. For the purpose of determining the tax in respect of which the person responsible for making the payment could be deemed to be in default, the ITO must determine the tax only on the appropriate proportion of income chargeable under the Act. There is no prohibition in Section 201 of the act. In the face of the ITO's own acquiescence that, in respect of erection charges paid to the other companies, the net profit could not exceed 25%, it is not possible to uphold the ITO's action in determining the tax with reference to the gross sums of money in R.C.203 and R.C.205. As already mentioned, the power to determine the appropriate amount of tax is referable to Section 201 of the Act and the fact

that the assessee did not file an application under Section 195(2) for determination of such appropriate proportion is not relevant for the purpose. In any event, this is the only way the provisions contained in Section 195 and Section 201 can be harmoniously interpreted. We, therefore, hold that the power of the ITO under Section 201 of the Act to deem the person responsible for paying any sum to the non-resident under Section 195 as being in default extends only to the proportion of income chargeable under the Act and forming part of the gross sum of money.

The obligation of the respondent-assessee to deduct tax under Section 195 is limited only to the appropriate proportion of the income chargeable under the Act forming part of the gross sums of money paid to the three nonresidents above referred.

Approving of this decision, the Hon'ble Supreme Court in the case of Transmission Corporation of A.P. Ltd. v. CIT 239 ITR 587 at 596 answered question No. 2 as follows: the obligation of the respondent-assessee to deduct tax under Section 195 is limited only to the appropriate proportion of income chargeable under the Act.

24.1 A combined reading of these two judgments clearly indicate that when there is no portion of income chargeable under the Act from out of gross sums of money paid, then Section 195 is not attracted. This view is fortified by the following Board's Circulars: The following clarifications would be found useful in deciding questions regarding the applicability of the provisions of Section 9 in certain specific situations: 1. Non-resident exporter selling-goods from abroad to Indian importer - No liability will arise on accrual basis to the non-resident on the profits made to him where the transactions of sale between the two parties are on a principal to principal basis.

In all cases, the real relationship between the parties has to be looked into on the basis of an agreement existing between them but where: (a) the purchases made by the resident are outright on his own account.

(b) the transactions between the resident and the non-resident are made at arm's length and at prices which would be normally chargeable to other customers, (c) the non-resident exercises no control over the business of the resident and sales

are made by the latter on his own account, or (d) the payment to the non-resident is made on delivery of documents and is not dependent in any way of the sales to be effected by the resident.

It can be inferred that the transactions are on the basis of principal to principal.

2. Non-resident company selling goods from abroad to its Indian subsidiary -(i) A question may arise whether the dealings between a non-resident parent company and its Indian subsidiary can at all be regarded as on a principal to principal basis since the former would be in a position to exercise control over the affairs of the latter.

In such a case, if the transactions are actually on a principal to principal basis and are at arm's length and the subsidiary company functions and carries on business on its own, instead of functioning as an agent of the parent company, the mere fact that the Indian company is a subsidiary of the non-resident will not be considered a valid ground for invoking Section 9 for assessing the non-resident.

3. Sale of plant and machinery to an Indian importer on installment basis -Where the transaction of sale and purchase is on a principal to principal basis and the exporter and the importer have no other business connection the fact that the exporter allows the importer to pay for the plant and machinery in installments will not, by itself render the exporter liable to tax on the ground that the income is deemed to arise to him in India. The Indian importer will not, in such a case, be treated as an agent of the exporter for the purpose of assessment.

7. Extent of the profit assessable under Section 9 - Section 9 does not seek to bring into the tax net the profits of a non-resident which cannot reasonably be attributed to operations carried out in India. Even if there be a business connection in India, the whole of the profit accruing or arising from the business connection is not deemed to accrue or arise in India. It is only that portion of the profit which can reasonably be attributed to the operations of the business carried out in India, which is liable to income-tax.

2. The deduction of tax at source under Section 195 would arise if the payment of commission to the non-resident agent is chargeable to tax in India. In this regard attention to CBDT Circular No. 23 dated 23rd July 1969 is drawn, where the taxability of "Foreign Agents of Indian Exporters" was considered along with certain other specific situations. It had been clarified then that where the non-resident agent operates outside the country no part of his income arises in India. Further, since the payment is usually remitted directly abroad it cannot be held to have been received by or on behalf of the agent in India. Such payments were therefore held to be not taxable in India. The relevant sections namely Section 5(2) and Section 9 of the Income-tax Act, 1961 not having undergone any change in this regard, the clarification in Circular No. 23 still prevails. No tax is therefore, deductible under Section 195 and consequently the expenditure on export commission and other related charges payable to a non-resident for services rendered outside India becomes allowable expenditure. On being apprised of this position the Comptroller & Auditor General have agreed to drop the objection referred to above.

The jurisdictional High Court has made it abundantly clear that the requirements for treating the assessee as being in default extends only to the portion of income chargeable under the Act. Thus the issue is answered in favour of the assessee by applying the ratio of the judgment of the jurisdictional High Court. Thus the argument of the learned Counsel for the assessee that at best, certain percentage of the amount received towards services which is 2.68% in the case of main generation equipment and 2.91% in the case of 400KV Gas Insulated Switchgear can only be considered as income attributable to permanent establishment and this alone can form the basis for holding that the person is liable in terms of Section 195 of the Act is upheld. ix) The learned Commissioner of Income-tax (Appeals)V, erred in holding that the provisions of Section 195A of the Act applies to all the contracts, and that therefore grossing up had to be done for deduction of tax.

x) Having regard to the clear provisions in the contract, appellant had no liability to bear tax in so far as the Gas Insulated Switch Gear Equipment and 400 KV XLPE Cables are concerned. Even in so far as the Generators and Turbines are

concerned, the appellant had declined to accept the liability with respect to payment of Indian taxes. The fact that the parties had agreed to negotiate at a future date, would not mean that there was a liability in present on the part of the Appellant to deduct taxes and therefore the learned Commissioner of Income-tax (Appeals)-V, ought to have held that grossing up is impermissible on the facts of the case.

25.1 The learned Counsel for the assessee submitted that the view of the Commissioner of Income-tax (Appeals) that in the absence of definite agreement between the parties, not to pass on the burden of tax to Sumitomo Corporation, the assessee must be deemed to have undertaking the said liability and that grossing up has to be done is not correct. The learned Counsel submitted that this clearly showed that there was no obligation on the part of the assessee to remit the amount net of taxes and thus there was no liability on the assessee to pay taxes on behalf of Sumitomo Corporation. Reliance is placed on clauses in the relevant contracts: (i) Clause 20.4 at page 24 in respect of contract for supply of Turbines and Generation sets.

(ii) Clause 20.4 at page 46 in respect of contract for supply of 400 KV Gas Insulated Switchgear (iii) Clause 20.4 at page 59 in respect of contract for 400 KV XLPE Insulated Power Cables (iv) Clause 20.4 at page 74 & 75, in respect of contract for 400 KV XLPE Insulated Power Cables.

25.2 The assessee filed additional ground in respect of grossing up by relying on sec, 10(6A) and 10(6B) of the Act and submitted that the contract in question should be considered as one which is approved by the Government of India as the very genesis of the contract was an agreement between the Government of India and JBIC. He submitted that that the APSEB was a nominee of the Government of India through GOAP to execute the contract. The contract was with the approval of the Government of India. He submitted that Section 10(6A) clearly exempts the grossing up in such cases.

25.3 The learned Standing Counsel for the Revenue submitted that the reliance on Section 10(6A) and 10(6B) is not relevant or is not applicable to the facts of the case as no evidence was filed by the assessee that the agreement between the

assessee and the foreign company was approved by the Central Government and it is not shown that the tax payable by the Foreign Company is the responsibility of the Government or the Indian concern under the terms of agreement under the terms of agreement.

26. Considering the rival submissions as well as the additional ground filed by the assessee, we find that the agreed position is that there is no categorical covenant whereby it is stipulated that either the Government of India or the assessee has undertaken the liability to pay taxes of the deductees on to themselves. On the contrary, the assessee has specifically denied that it would undertake the liability to pay the taxes. When there is no specific agreement then it follows that only the non-resident company is responsible for paying the income tax on the transaction or the income that accrued to it and none else. Thus the case of grossing up simply does not arise. Reference to Section 10(6A) or Section 10(6B) does not arise. Thus the issue of grossing up is decided in favour of the assessee.

26.1 As all the issues were argued at length over a period of time and as the writ/en submissions have been filed by both the parties, we have decided to give our findings on each of the issues though the appeals could have been disposed of by just giving a finding on the issue as to whether the contracts in question are simple sale contracts and not works contracts and as to whether any income can be said to have been deemed to accrue or arise in India to the assessee company on these contracts. Applying the ratio of the , judgment of the jurisdictional High Court in the cases of C.I.T. v. Visakhapatnam Port Trust 144 ITR 146 (A.P) and C.I.T. v. Sundwiger EMFG & Co. and Ors. 262 ITR 110(A.P), we have held that this is a contract of sale and that no portion of income is chargeable to tax in India. When no portion of the gross remittances is liable to charge under the Indian Income-tax Act, there is no liability for deduction of tax under Section 195 as per the Board Circular No. 786 dated 7.2.2000 and it is well settled that the circulars are binding. Even otherwise for the reason that Sumitomo Corporation has filed its return of income and paid taxes thereon, it cannot be said that default, if any, that has occurred, still continues in the present case thus warranting levy of interest under Section 201(1 A). We follow the judgment of the Hon'ble Gujarat High Court in the case of C.I.T. v. Rishikesh Apartments Co-op. Housing Society Ltd. 253 ITR

310(Guj). Thus we hold that the plant and machinery purchased by the assessee were manufactured outside India and is exported to India and the supply of the material is a transaction involving trading with India and not trading in India and thus the profits if any arising in the manufacture and export of the material to India are not attributable to the permanent establishment of Sumitomo Corporation. It is an international transaction on principle to principle basis and therefore, the profits, if any, - arising from manufacture and export of such material are not chargeable to tax under the Indian Income-tax Act. Hence there is no liability on the part of the assessee to deduct tax in terms of Section 195. For all these reasons, the appeals of the assessee are hereby allowed.

27. Now we take up ground No. 3 of the departmental appeals which -reads as under: The CIT (Appeals) erred in considering the payments made to BHEL as payments made as per Section 194C of the Act.

27.1 After hearing both parties on this issue, we find that the ratio of the judgment of the jurisdictional High Court in the case of Visakhapatnam Port Trust (supra) is in favour of the assessee. Relevant extracts are already given above. In that case the jurisdictional High Court held that the agreement between the German Company and the Poona Company did not also amount to the German Company having permanent establishment in India as there was neither any identity of interest nor identity of character nor of personality nor was there any unit for profit making between the Poona Company and the German Company so that the former maybe treated as the Indian agent of the latter. In any event BHEL is a public sector company and there is no allegation by the Revenue that it has not filed its returns of income or that it is an assessee in default for that particular assessment year. Thus we uphold the order of the first appellate authority though not only for reasons mentioned by him but also for the reasons given by us in our order above.

28. In the result, while the appeals of the assessee are allowed, the appeals filed by the Revenue are dismissed.