Technical and supervisory services does not create a PE in the absence of an independent site operation

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In brief

The Hyderabad Bench of the Income-tax Appellate Tribunal (Tribunal), in the case of **GFA Anlagenbau Gmbh** (the taxpayer) held that rendition of supervisory services cannot constitute a permanent establishment (PE), if such services are not in connection with building, construction or assembly activities of the taxpayer.

In detail

Facts

- The taxpayer[1], a foreign company incorporated in Germany, was engaged in the activities of supervision, construction and commissioning of plant and machinery for steel and allied plants in India.
- The taxpayer rendered services to multiple clients in India by engaging foreign technicians at the work sites in India. The total stay of technicians on one of the projects exceeded 183 days. The taxpayer categorised the receipts from such activities as 'fees for technical services' (FTS) under the provisions of section 9(1)(vii) of the Income-tax Act, 1961 (the Act), read with Article 12 of the India–Germany Double Taxation Avoidance Agreement (tax treaty).
- The taxpayer's technicians stayed in India until the completion of the work, exceeding 183 days, and their income tax returns were also filed in India. Considering this, the Tax Officer (TO) was of the view that the taxpayer had a PE in India, according to Article 5 of the tax treaty, and concluded that its income was liable to be taxed under the head 'business profits', in accordance with Article 7 of the tax treaty. The TO disallowed all the expenditure and taxed all receipts.
- On appeal the Dispute Resolution Panel (DRP) did not accept the contentions of the taxpayer. Pursuant to the DRP's instructions, the TO allowed a 50% deduction from the gross receipts as expenditure in connection with the execution of contracts.
- The TO, applying the provisions of section 44DA of the Act, applied a 40% tax rate (excluding surcharge and cess), treating the income as business profits.

Issues before the Tribunal

- Did the TO err in holding that the taxpayer has a PE in India and that the amount received by rendering technical and supervision services was chargeable under Article 7 of the tax treaty ?
- Did the TO err in rejecting the contention of the taxpayer that the amount received was chargeable to tax as FTS under the provisions of section 9(1)(vii) of the Act read with Article 12 of the tax treaty ?

[1] GFA Anlagenbau Gmbh *v.* DDIT/ ADIT [TS-383-ITAT-2014(Hyd)]

Taxpayer's contentions

- The taxpayer contended that fixed place of business according to Article 5(2)(i) should be owned by the taxpayer and should not be a place where supervisors attend work, which was provided by the contractee.
- Furthermore, mere accommodation provided to technicians could not be considered as a fixed place of business for a non-resident[2].
- It was also argued that the provisions of Article 7 could be invoked only when the taxpayer carried on business in India through a PE. Merely because the stay of technical personnel exceeded six months, a PE could not be said to have been established[3].
- Mere supervisory activities carried out would not merit the definition of PE and consequent taxation as *"business income"*[4].
- The taxpayer also contended that all the project receipts could not be assessed at a higher rate where the duration of stay of the technicians exceeded the threshold only in one project.

Revenue's contention

The revenue relied on the DRP's order.

Tribunal's ruling

Under the Act

- The Tribunal relied on the decision of the jurisdictional High Court[5] and concluded that the supervisory activities fell within the ambit of section 9(1)(vii) of the Act as FTS.
- It was observed that the concept of "fixed place of business" was no different from the general provision of Article 5(1) of Model Conventions and tax treaties. Hence, it was also held that such supervisory activities did not constitute a fixed place of business under section 92F(iiia) of the Act, as the taxpayer rendered its services at the project sites of its clients and did not own or operate such sites independently.

Under the tax treaty

- Relying on the Delhi Tribunal Special Bench decision[6] where it held that technicians were not operating from a fixed place in the taxpayer's custody and hence, it could not be said that the taxpayer had a fixed place of business in India for its supervisory activities under Article 5(1).
- The Tribunal also held that supervisory activities by themselves could not constitute a PE under Article 5(2)(i), if they were not in connection with the taxpayer's building, construction or assembly activities. In the given case, the taxpayer was only providing supervisory services, which were technical in nature and hence, was taxable as FTS under Article 12 of the tax treaty.
- While adjudicating on the above issues, the Tribunal observed that unless the contracts were otherwise linked with each other, they had to be individually assessed with respect to the duration of stay test.

The takeaway

This ruling once again re-iterates the position on PEs, which is in line with International Tax commentaries and the OECD Model Convention.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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[2] CIT *v.* Visakhapatnam Port Trust [1983] 144 ITR 146 (AP)
[3] Reliance placed on commentary of Klause-Vogel & ACIT *v.* Enron Global Exploration & Production Ltd [2009] 120 TTJ 774 (Delhi)
[4] Motorola Inc *v.* DCIT [2005] 95 ITD 269 (Delhi)(SB)
[5] Clouth Gummiwerke Akrineqesellschaft *v.* CIT [1999] 238 ITR 861 (AP)
[6] Motorola Inc *v.* DCIT [2005] 95 ITD 269 (Delhi)(SB)

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