

# Income from rendering of marine logistic services taxable under section 44BB of the Act

February 28, 2015

## In brief

In a landmark decision in the case of SBS Marine Limited (SBS or the taxpayer), the Delhi Bench of the Income-tax Appellate Tribunal (Tribunal) has held that the income arising to the taxpayer from the rendering of marine logistic services to drilling companies was covered by the provisions of section 44BB of the Income-tax Act, 1961 (the Act).

## In detail

### Facts

The taxpayer<sup>1</sup>, a non-resident company based in the United Kingdom, was engaged in the business of providing marine logistic services to its customers (Transocean group companies) in India through the charter party of Platform Supply Vessels (vessels or PSV). The taxpayer's scope of work under charter party included transportation of personnel and materials between base and offshore installations, carrying out standby and rescue operations, etc.

The taxpayer filed the return of income for the assessment year (AY) 2008-09, offering the income earned from the charter party of vessels under section 44BB of the Act. The tax officer (TO) rejected the taxpayer's claim on the following grounds:

- The rental earned by the taxpayer was not covered under section 44BB of the Act, since they were not used for prospecting for, or exploration and production of, mineral oil, but were used for services connected to these activities.
  - The taxpayer was not undertaking the activities specified under section 44BB of the Act, as it was merely hiring vessels to its customers, who were further leasing them to operators for prospecting for, or extraction or production of, mineral oil.
  - There was no scope in the statute for extending the provisions of section 44BB of the Act beyond the hirers for the benefit of sub-hirers.
- The TO passed the final assessment order holding that:
- charter party receipts received by the taxpayer
  - were in nature of royalties under section 9(1)(vi) of the Act.
  - Since the taxpayer was rendering services through its permanent establishment, section 44DA of the Act was applicable, and as per section 115A, the gross receipts were taxable at the rate of 10%.

### Issue before Tribunal

Was the income earned by the taxpayer assessable under section 44BB of the Act?

### Taxpayer's contention

The taxpayer contended that income earned from charter party of the PSV was covered by section 44BB of the Act for the following reasons:

- The taxpayer referred to various terms of the charter party agreements and contended that the primary nature of the charter party agreement

<sup>1</sup> SBS Marine Ltd v. ADIT (ITA No.107/Del/ 2012, AY 2008-09, ITAT Delhi)

entered into with Transocean group companies was for the provision of marine logistic services or facilities. Since these services were inextricably linked to the drilling operations carried out by Transocean group companies, they were in connection with prospecting for, or extraction or production of, mineral oil, and therefore covered by the first limb of section 44BB of the Act.

- Even if the nature of the charter party agreement was considered as for hire of the vessels, it would be covered by the second limb of section 44BB of the Act.
- The definition of the term ‘plant’ provided in Explanation to section 44BB included vehicles and aircraft. These equipment could never be used directly in the prospecting, extraction or production of mineral oil, and therefore the phrase ‘used or to be used in prospecting, ....’ did not envisage the direct use of plant or machinery for these activities.
- In relation to the revenue’s contention that the hire charges were based on each day of use, it was contended that the measure and method of payment was not decisive of the character of the payment. In this regard, reliance was placed on the decision of the Supreme Court (SC) in case of *Senairam Doongarmall*<sup>2</sup>.

### Section 44DA and section 115A

The provisions of section 44DA and section 115A of the Act were not applicable in view of the following:

- The income earned by the taxpayer did not constitute

<sup>2</sup> *Senairam Doongarmall v. CIT* [1961] 42 ITR 392 (SC)

‘royalty’ of ‘fees for technical services’

- The contracts had been entered into with Transocean group companies (who were non-residents) and not with the Government of India or an Indian concern.

Reliance was placed on various judicial precedents including the ruling of Authority for Advance Ruling (AAR) in case of *Lloyd Helicopters*<sup>3</sup>, *Wavefield*<sup>4</sup> and *Siem Offshore*<sup>5</sup>.

### Revenue’s contentions

- The nature of the contract was for the hire of equipment, and in this regard, heavy reliance was placed on the SC decision in the case of *Gosalia Shipping*<sup>6</sup> and Madras High Court (HC) decision in the case of *Poompuhar Shipping*<sup>7</sup>.
- The taxpayer was neither providing any service or facility, nor undertaking the activities specified in section 44BB of the Act. The taxpayer was only supplying ‘plant and machinery’ on hire to a person, who further leased it to the operators for putting to use for the purposes as specified in section 44BB of the Act.
- The intention of section 44BB was to provide benefit to the persons supplying ‘plant and machinery’ on hire directly to the entities involved in the business of prospecting for, or extracting or production of mineral oil exploration itself. Thus, the provisions of section 44BB of the Act would apply only if the taxpayer had

<sup>3</sup> *Lloyd Helicopters International Pty Ltd v. CIT* [2001] 249 ITR 162(AAR)

<sup>4</sup> *Wavefield Inseis ASA, In re* [2010] 320 ITR 290 (AAR)

<sup>5</sup> *Siem Offshore Inc., In re* [2007] 337 ITR 207 (AAR)

<sup>6</sup> *UOI v. Gosalia Shipping Private Limited* [1978] 113 ITR 307 (SC)

<sup>7</sup> *Poompuhar Shipping Corporation Limited v. ITO* [2014] 360 ITR 257 (Madras)

entered into a direct contract with ONGC.

- The words “in the” in the expression “supplying of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils” have much limited scope as compared to the words in “in connection with” in the expression “providing services or facilities in connection with prospecting for, or extraction or production of, mineral oils”.

### Tribunal’s ruling

The Tribunal held that the income received by the taxpayer from the rendering of marine logistic services was taxable under the provisions of section 44BB of the Act. The relevant observations of the Tribunal were as follows:

- The taxpayer was engaged in providing services or facilities in connection with prospecting, extraction and production of mineral oil, along with the hire of vessel:
  - The entire operation, navigation and management of the vessel was under the exclusive control and command of the taxpayer, including the responsibility for obtaining security clearances, etc..
  - The taxpayer provided the services of carrying personnel and materials between base and offshore installations as well as other field operations as per the instructions of its customers, and ensured that the vessel was available round the clock every day during the term of contract.
  - Relying on the SC decision, it was held that the day rate spelt out in the charter party contract

did not mean that it was a case of hiring.

- The services/ facilities and the vessels provided by the taxpayer were used in offshore drilling operations as the location of operation of vessel was mentioned as ONGC Deepwater blocks, East and West Coast of India and ONGC locations in coastal India.
- Even if it was considered that the taxpayer was engaged in simple hire of vessels, the same would be covered within the scope of section 44BB of the Act since:
  - o The definition of the term 'plant' provided in Explanation to section 44BB included vehicles and aircraft. These equipment can never be used directly in the prospecting, extraction or production of mineral oil, and therefore the phrase "used in prospecting, ...." did not envisage direct use of plant or machinery for these activities.
  - o It was sufficient if the plant or machinery was used for the purposes of the business of

prospecting for, or extraction or production of, mineral oil.

- There was no requirement of a direct contract or agreement with the person actually engaged in prospecting for, or extraction or production of, mineral oils for section 44BB, unlike as required under sections 42 and 80-IA.
- Sections 115A and 44DA of the Act were not applicable in the present facts, since the said sections dealt with the taxability of royalty received from the Government or an Indian concern, whereas the taxpayer had received charter party payments from non-residents.
- The SC decision in *Gosalia Shipping*<sup>6</sup> dealt with the issue of whether the payment made by its customers was on account of carriage of goods, and the said issue did not arise in the present facts. Similarly, the Madras HC decision in case of *Poompuhar*<sup>7</sup> did not deal with applicability of section 44BB of the Act.

### **The takeaways**

This is a landmark decision rendered by the Tribunal since it has shed light on many points of

litigation being faced by non-resident oil and gas service providers, especially the following:

- The applicability of section 44BB is not restricted to only those taxpayers (first leg contractors) who have directly entered into a contract with the person who is engaged in prospecting for or extraction or production of, mineral oils.
- Section 44BB does not envisage direct use of the plant or machinery in the prospecting for, or extraction or production of, mineral oil. It is sufficient if the plant or machinery is used for the purposes of the business of prospecting for or extraction or production of mineral oil.
- The terms of the contract have to be read as a whole and cannot be interpreted selectively.

### **Let's talk**

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

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