

# Erection and commissioning charges not taxable as FTS

February 16, 2018

## In brief

In a recent decision,<sup>1</sup> the Chennai bench of the Income-tax Appellate Tribunal (Tribunal) held that payment made to a non-resident entity for erection and commissioning services outside India would not be taxable as fees for technical services (FTS) in India under the Income-tax Act, 1961 (the Act).

## In detail

### Facts

- The taxpayer was an Indian company. It purchased machinery and equipment from a Saudi Arabian company. For erection and commissioning it entered into agreement with a tax resident of the UAE.
- The machinery was purchased and supplied outside India, and the agreement for erection and commissioning was also made outside India.
- Subsequent to regular assessment, the tax officer (TO) issued notice under section 148 of the Act, alleging that the taxpayer had not withheld taxes on payment made towards erection and commissioning activities carried out by the non-resident entity based out of the UAE. The TO disallowed payment made towards the erection and commissioning services to the non-resident.

- On appeal, the Commissioner of Income-tax (Appeals) [CIT(A)] upheld the TO's order.
- Aggrieved by the CIT(A)'s order, the taxpayer appealed before the Tribunal.

### Issue before the Tribunal

Whether the TO has rightfully disallowed the payment made to non-resident entity towards erection and commissioning services on account of non-withholding of taxes under section 195 of the Act.

### Taxpayer's contention

The taxpayer contended that the payment was made towards erection and commissioning activities performed by the non-resident entity. The same amounts to "construction," which falls within the exclusion of FTS, as defined in explanation 2 to section 9(1)(vii) of the Act. Hence, the said payment was not liable to withholding tax.

### Revenue's contention

The Revenue contended that

the amount paid by the taxpayer towards erection and commissioning charges was in the nature of FTS under section 9 (1)(vii) of the Act, since the non-resident entity utilised its technical skill and expertise for erection and commissioning of machinery. Therefore, tax was required to be withheld.

### Tribunal's decision

The Tribunal noted that the non-resident entity was only a service provider for installation of machinery. The agreement with the non-resident entity was entered outside India, and the installation services were performed outside India. As per the agreement, the equipment, specifications, design drawing, remained the property of the taxpayer.

- In view of specific facts in the agreement, payments made to the non-resident entity could not be construed as FTS within the meaning of section 9(1)(vii) of the Act. Hence,

<sup>1</sup> ITA No.2347/Mds/2017

the taxpayer was not required to withhold tax on such payments.

***The takeaways***

Facts and the terms of an

agreement would determine tax liability of similar payments.

***Let's talk***

For a deeper discussion of how

this issue might affect your business, please contact your local PwC advisor

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