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INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1. No substantial question of law arose against the Tribunal's order excluding comparable companies which (i) had substantial related party transaction (ii) were performing clinical research trials in-house while the assessee – company had outsourced its clinical research activities

Pr. CIT vs. M/s. Pfizer Limited– [TS-130-HC-2019-TP (Bom)] – Income Tax Appeal No. 1731 of 2016

Facts

(i) The assessee was engaged in manufacturing and sale of pharmaceutical products. It had adopted TNMM for benchmarking its clinical study management and monitoring supporting services and selected 6 comparables and concluded the price charged to be at ALP as margin of comparables was 12.61% i.e. within +5% range from its margin of 11.11%.

(ii) The TPO rejected 4 of the companies selected by the assessee as he was of the view that the assessee was providing specialized skill services in area of clinical trials and not merely routine support services whereas the said companies were functionally different (engaged in consultancy and management services). He proceeded to select additional comparable companies and accordingly made an upward adjustment.

(iii) The CIT(A) accepted assessee's plea for exclusion of TPO's comparable i.e., Syngene International Pvt. Ltd on ground that the company had substantial Related Party Transactions (RPT). However it rejected assessee's plea for exclusion of two other comparables viz. *SIRO Clinpharm Pvt. Ltd. and Choksi Laboratory Ltd.*

(iv) The Tribunal confirmed CIT(A)'s order with respect to exclusion of Syngene International Pvt. Ltd. noting that Revenue was not able to controvert CIT(A)'s finding of substantial RPT and further agreed with assessee's contention that it had two streams of income viz., contract research fees and sale of compounds however there was no separate segmental information available.

(v) The Tribunal also excluded the comparables contested by assessee viz., *SIRO Clinpharm Pvt. Ltd. and Choksi Laboratory Ltd.* on

ground that the business models of the aforesaid companies were different as they conducted research trials whereas the assessee company was outsourcing its entire activity of clinical research trials to hospitals.

(vi) Aggrieved, the Revenue filed an appeal before the High Court.

Held

(i) With respect to Revenue's plea to consider *Syngene International Ltd.* as a comparable, the Court held that the Revenue had not shown as to how the findings of facts by CIT(A) and Tribunal that the said company had substantial RPT was perverse.

(ii) With respect to *SIRO Clinpharm Pvt. Ltd.,* at the outset, the Court held that merely because assessee had selected the said comparable could not estop it from contesting its exclusion.

(iii) Further, with respect to exclusion of *SIRO Clinpharm Pvt. Ltd.* and *Choksi Laboratories Ltd.,* it relied on its own decision in the case of *CIT vs. Aptara Technology P. Ltd. (2018) 92 taxmann.com 240 (Bom)* wherein it was held that the company which outsources it work is not comparable for ALP determination with a company that does the activity in house and thus held that no fault could be found with the Tribunal's order.

(iv) Accordingly, it held that no substantial question of law arose and dismissed Revenue's appeal.

2. As regards transaction which are not referred to the TPO by the AO, the TPO can make *suo motu* adjustment only with respect to international transactions and not with respect to specified domestic transaction

Times Global Broadcasting Company Ltd. vs. UOI [2019] 103 taxmann.com 388 (Bom) – Writ Petition No. 3386 of 2018

Facts

(i) The assessee was engaged in the business of distribution of television channels owned by Times Group entities including BCCL and retained 8% of its fees as its service income received upon distribution and remitted the balance to the aforesaid entities according to their revenue share. With effect from 1.04.2014, the assessee demerged one of its business undertakings into BCCL.

(ii) For AY 2015-16, the assessee reported two specified domestic transactions ("SDTs") in its Form 3CEB (a) payment of subscription fees earned from distribution services (b) Payment to key management personnel. The AO made a reference to TPO to determine ALP of said SDTs reported.

(iii) The TPO held the assessee to be in default for not reporting in Form 3CEB SDT with respect to payment of creditors in demerger process (where TPO contended that by transferring creditors of the demerged company to the AE under demerger, the assessee had made a payment which would fall within ambit of any expenditure under section 92BA and thus a SDT) and made an ALP adjustment with respect to the same. He also made an adjustment with respect to the SDT of payment of subscription fees.

(iv) Aggrieved, the assessee filed a writ petition before High Court challenging the adjustments made by TPO on ground (a) TPO could not examine any SDT if not referred by AO, thus it could not make a suo moto adjustment in case of payment of creditors in demerger process and (b) so far as the payment of subscription fees was concerned, the same was made without proper notice to the assessee.

Held

(i) The Court rejected the preliminary objection of Revenue raised against the maintainability of writ petition holding that its powers under Article 226 of the Constitution of

India were wide and if found that TPO's action were without jurisdiction, it could strike down the order irrespective of alternative statutory remedies of appeal available with the assessee.

(ii) With respect to payment of creditors in demerger process:-

(i) The Court held that the TPO had no jurisdiction to make any such adjustment as the said SDT was not referred to him by the AO.

(ii) It rejected the reliance placed by the Revenue on provisions of sub-section (2A) and (2B) of section 92CA inserted w.e.f. 1-6-2011 with retrospective effect from 1-6-2002 which empower the TPO to examine any international transaction which come to his notice during proceedings before him without reference being made by AO. The Court held that the legislature while expanding the scope of TP study by TPO to transaction not referred to him or not reported by assessee has confined the applicability thereof only to international transaction and not SDT.

(iii) It held that in case of SDTs, TPO could determine ALP only on reference by AO in terms of section 92CA(1) and further, AO would have to obtain prior approval of Principal Commissioner or Commissioner before making a reference and such requirement could not be jettisoned by TPO exercising *suo motu* jurisdiction over the transaction not referred to him.

(iv) However, the Court clarified that as per the CBDT Instructions dated 20-5-2013, it was always open to TPO who notices such transactions during the course of proceedings to call for reference by the AO.

(iii) With respect to payment of subscription fee earned from distribution services:-

(i) The Court noted that assessee's contention on merits required minute examination of documents and materials on record.

(ii) Further with regard to assessee's contention of breach of natural justice, it held that it was not possible to consider the said contention in brief since the TPO had issued a number of notices and it would have to be examined whether in any of such notice he had raised precise query in relation to the adjustment for payment of subscription fee.

(iii) Accordingly, it held that since the Act provides for statutory appeals and further appeal to High Court on substantial question of law, the Court would not undertake this ground in writ petition.

(iv) Thus, it quashed TPO's order to the extent it provided for adjustment of ALP towards payment of creditors in demerger process and let the ALP adjustment on payment of subscription fees stand as it is.

3. Two companies having fundamental difference in the profiles cannot be comparable to each other, irrespective of the fact the assessee itself had included such a comparable in the TP study report

PCIT vs. Lionbridge Technologies Ltd. [TS-176-HC-2019 (Bom)-TP] – ITA No 1815 of 2016

Facts

(i) The Assessee-company was *inter alia* engaged in calling of localisation and software services. Before Tribunal, for the first time, the assessee contended for exclusion of comparable i.e., Bodhtree Consulting, which the assessee itself had included in the TP study report for determining arm's length price.

(ii) The Tribunal excluded Bodhtree Consulting as comparable on the ground of functional dissimilarity as it was a software product manufacturer as against assessee who was found to be in the calling of localisation and software services.

(iii) Aggrieved, the Revenue filed an appeal before the High Court against the Tribunal's order excluding Bodhtree Consulting as a comparable.

Held

(i) The Court held that it did not find any error in the Tribunal's finding as two companies having fundamental difference in the profiles could not be comparable to each other.

(ii) Further, it also rejected Revenue's contention that the assessee could not change its stand regarding comparability *vis-à-vis* a company having included the said company in its TP-analysis. It relied on the own decision in the case of *Tata Power Solar Systems Ltd. (2017) 77 taxman.com 326 (Bom HC)* wherein it was held that assessee was not barred from withdrawing a comparable if the same was included on account of mistake and was not comparable.

(iii) Accordingly, the Court concluded that the Tribunal's finding was not shown to be perverse in any manner and, thus, dismissed Revenue's appeal.

B. TRIBUNAL

4. India-USA DTAA Lease line reimbursements to US parent, not royalty – Not Taxable in India – In favour of the assessee

T-3 Energy Services vs. JCIT [TS-70-ITAT-2018(PUN)] Assessment Year: 2010-11

Facts

(i) T-3 Energy Services India Pvt. Ltd. ('assessee') engaged in the manufacturing of Industrial Valves & Valve Components used in the Oil Field Service Industry, had incurred expenditure on account of reimbursement of lease line charges to its parent company in AY 2010-11.

(ii) The parent company of assessee T-3, USA had entered into an agreement with service provider Qwest Communications Inc. for providing of bandwidth services and the parent company in turn, provided bandwidth services to its subsidiaries. The assessee availed lease line services from its parent company and reimbursed the lease line charges to it. The assessee contended that the reimbursement was on cost to cost basis and there was no profit element involved in it, therefore, tax was not required to be deducted.

(iii) The AO contended that the said payment was not reimbursement of expenses to the associated enterprises for any services provided by them to the assessee, but it was payment made to third party Qwest Communication Inc., through associated enterprise of assessee. The AO contended that in the absence of associated enterprise, if the assessee intended to take services of Qwest Communications, Inc, services would be provided to him at the same rates as charged by associated enterprise and it was veil to shadow profit element (income) in the hands of recipient i.e., third party.

(iv) The AO held that the said payment was covered within the definition of royalty due to retrospective amendment in Section 9 by Finance Act 2012, on which the assessee should have deducted tax u/s. 195. The AO further contended that the amended clarificatory definition of royalty under Act will be applicable to DTAA. Therefore, the ITO disallowed the payment of ₹ 20.47 lakh u/s. 40(a)(i). CIT(A) upheld the disallowance of AO.

Decision

On appeal, the Tribunal held in favour of the assessee as follows:

(i) The Tribunal relied on Delhi HC decision in the case of *New Skies Satellite BV & Ors.* to hold that amendment made under the Act does not affect the terms of DTAA unless and until the same is amended by two Contracting States. Therefore, it held that even though the definition of royalty under the Act has been amended, however, the term 'Royalty' under the DTAA between India and USA is not amended. Accordingly, it held that the assessee is not liable to withhold tax on the payments made to its associated enterprise on account of lease line charges.

(ii) The Tribunal also relied on the Bombay HC decision in the case of Siemens Aktiongesellschaft to hold that once a term has been defined in DTAA, then the said term is to be applied unless and until the parties to the DTAA amends the same. Thus, the Tribunal held that the amended provisions of section 9(1)(vi) of the Act brought into force by the Finance Act, 2012 are applicable to domestic laws and the said amended definition cannot be extended to DTAA, where the term has been defined originally and not amended.

(iii) The Tribunal further noted that the privity of contract is between Qwest Communications Inc, the service provider and T-3, USA, who in turn had received bandwidth and passed on the services to various entities of group on cost to cost basis. Qwest Communications Inc had raised charges upon T-3, USA and the portion allocable to the assessee was charged on cost to cost basis. Therefore, it held that it cannot be said that there was any income element which has arisen in the case and consequently where the assessee had reimbursed the expenses having no income element, there is no requirement to withhold tax out of such payments. It rejected the Revenue's contention that it is not case of reimbursement but is a case of payment to third party through its associated enterprise and hence, the need for withholding tax on the ground that the said payment was not royalty under DTAA.

(iv) Further, the Tribunal noted that the assessee had declared the reimbursement of lease line charges in its TP study report and the TPO had accepted the nature of expenses i.e., reimbursement of lease line charges to be at arm's length price. Therefore, the Tribunal held that once the TPO has accepted the nature of expenses, the AO cannot sit in judgment of the TPO order since under the provisions of the Act, the order passed by the TPO is binding upon the AO. It further held that at best AO could have invoked the provisions of Income-tax Act *per se* and not question the nature of expenditure contending it to be royalty.

5. India-UAE DTAA – No PE for *Booz* UAE; Revenue's reliance on AAR in group concern's case, misplaced

Booz & Company (ME) FZ-LLC vs. DDIT [TS-27-ITAT-2018(Mum)] Assessment Year 2011-12

Facts

(i) Booz & Company (ME) FZ-LLC ('assessee'), company incorporated in UAE and engaged in the business of providing management and technical consultancy services, provided technical/professional personnel to its Indian associated enterprise named Booz & Company India Private Limited (Booz India).

(ii) The assessee received a fee of ₹ 112.83 lakh from Booz India during AY 2011-12. The assessee did not offer the said income to tax contending that since India-UAE DTAA does not have any specific clause on taxability of fees for technical services and hence the said receipt is taxable as business income. However, since it did not have Permanent Establishment (PE) in India, above said fee is not taxable in India.

(iii) The AO noted that the Booz group is a global network group of companies having subsidiaries all over the world. He noted that AAR in case of some of the group companies [TS-76-AAR-2014] had ruled that these companies had PE in India and income received

by them from Indian companies are taxable as business profit under Article 7 of Tax agreement of India and respective countries. Therefore, relying on AAR the AO held that 'Booz India' (Indian AE) to whom services were provided is the PE of the assessee. Accordingly the AO held that the income of ₹ 112.83 lakhs is taxable as business income of the assessee.

(iv) The CIT(A) confirmed the AO's order.

Decision

On Appeal, the Tribunal held in favour of the assessee as follows:

(i) The Tribunal accepted the assessee's contention that the tax authorities were incorrect in merely placing reliance on the ruling of AAR without examining the facts available in the present case and that AAR has given a common ruling with reference to all the group companies without making specific reference to the provisions of respective DTAA.

(ii) The Tribunal noted that the employees of the assessee has worked for only 156 solar days only (on all projects taken together), meaning thereby, the period of working is less than 9 months. Therefore, there is no Service PE also in terms of Article 5 of DTAA.

(iii) The Tribunal further noted that M/s. Booz India has also not earmarked any specific place under the control or disposal of the assessee. Hence, it held that there was no fixed place of business in India. Further, it held that since the assessee has provided service to M/s. Booz India and did not receive any service, the question of dependent agent PE also does not arise in India.

(iv) Therefore, the Tribunal holds that there is no PE of the assessee in India and the business income in absence of PE would not be taxable in India. Accordingly, it set aside the order of the AO.

6. India-Singapore DTAA – Salary reimbursement for Morgan Stanley's seconded employee not taxable as FTS – Held in favour of the assessee.

Morgan Stanley Asia (Singapore) Pte. vs. DDIT TS-384-ITAT-2018 (Mum.) Assessment Year 2007-08

Facts

(i) Morgan Stanley Asia (Singapore) Pte. ('assessee'), resident of Singapore deputed one of its Director/employee to India for the period from May 2004 to April 2007 to set up Morgan Stanley Advantage Services Private Limited (MSAS), an associate concern in India.

(ii) The assessee, as per the terms of contract, agreed to continue paying salary of the employee in Singapore and cross charging India for the same. The assessee received an amount of ₹ 5.78 lakh as reimbursement from the Indian company.

(iii) The AO rejected the assessee's explanation that it was in the nature of reimbursement of salary and contended that Director/employee deputed to India was highly qualified and technical experience having vast experience and expertise in this area and the role of the assessee was more than employer. The AO held that amount of ₹ 5.78 lakh received by the assessee was FTS and charged markup of 23.3% on the reimbursement received by the assessee. The CIT(A) upheld the AO's order

Decision

The Tribunal held in favour of the assessee as under:

(i) The Tribunal noted that there was contractual agreement between MSAS and assessee, which clearly provides that salary is paid by assessee on behalf of MSAS and the same is recharged by assessee to MSAS. The Tribunal held that payment by MSAS being a pure reimbursement of salary cost incurred by the assessee and would be covered under exception mentioned in *explanation 2* to Sec. 9(1)(vii) and will not be taxable as fees for technical service under the domestic law. Further, the

Tribunal noted that receipt has been taxed as salary in the hands of the employee in India.

(ii) The Tribunal relied on Delhi Tribunal ruling in *United Hotels Ltd.* wherein it was held that for each deputed person, the amount received by it is income chargeable under the head "salary" and therefore, it cannot be termed as "fees for technical services". The Tribunal also relied on the Co-ordinate Bench ruling in *Mark & Spencer Reliance India (P) Ltd. [TS-449-ITAT-2013 (Mum.)]* wherein it was held that expatriation of employee under secondment agreement without transfer of technology would not fall under the term " make available" and will not be taxable under the treaty.

(iii) Therefore, the Tribunal held that reimbursement of salary was not FTS under Act as well as India-Singapore DTAA. It further held that as per the agreement, there was no profit element involved in the impugned payment. The Tribunal held that even otherwise, the salary was taxed in the hands of the employee and accordingly, it cannot be taxed in the hands of the assessee.

Remarks

Bombay HC in *Marks & Spencer Reliance India Pvt. Ltd. [TS-178-HC-2017 (Bom.)]* held that reimbursement of salary to non-resident for seconded employee was not FTS.

7. No PE trigger for UAE Co. undertaking 'grouting' masonry work in India

ULO Systems LLC vs. Assistant D.I.T [TS-741-ITAT-2018(Del.)] Assessment Year 2007-08

Facts

(i) ULO Systems LLC (assessee) is engaged in providing grouting and precast solutions for subsea off-shore construction industry and also provides products and solutions to support and protect subsea pipelines, cables and structures.

(ii) The Revenue contended that the grouting activities fell within Article 5(1) India–UAE DTAA whereas assessee contended that the grouting activities fell within construction activity contemplated in specific provision of Article 5(2)(h).

(iii) The DRP had determined the number of days spent in India at 264 days on which the assessee contended that the same was less than the stipulated period of 9 months/duration test in India as per Article 5(2)(h) India-UAE DTAA and therefore no PE came into existence.

(iv) Assessee also argued that services having been rendered to different unrelated third party customers in India, and contracts not being inter connected, therefore, it cannot be said that the assessee had PE in India. However, Revenue relied on Co-ordinate Bench ruling in *Fugro Engineers* BV to support its stand.

Decision

On Appeal, the Tribunal held in assessee's favour as under:

(i) The Revenue contended that by keeping the number of days less than nine months, the assessee has circumvented the provision of the Act by manipulating the stay of number of day in India, since assessee's equipment was in India for at least 264 days on which work for execution of construction was carried on, assessee had equipment PE in India. Revenue also submitted that even movables place of business constituted a PE even if they were temporary in location but permanent in time.

(ii) Revenue contended that a place of business would constitute a PE even if it exists only for a very short period, if time and nature of business is such that it is carried on for that period of time. Revenue submitted that the assessee should be allowed benefit of limitation clause only when activities carried on are occasional but when activities are carried on from year to year regularly and periodically, then it does raise a presumption that it is being

done deliberatively to avoid establishment of PE in India.

(iii) Distinguishing Revenue's reliance on Co-ordinate Bench ruling in *Fugro Engineers* BV, the Tribunal stated that the specific provisions were not applicable on the facts of the aforementioned case whereas in the case in hand, specific Article 5(2)(h) was squarely applicable. The Tribunal held that it was a settled legal principle in latin maxim *"generalia specialibus non deroganf'*, which means a general provision would not be applicable when specific provision is there.

(iv) The Tribunal also denied Revenue's concept of 'Equipment PE' in India as such a concept was nowhere mentioned. The Tribunal opined that it is the settled principle of interpretation in view of Vienna Convention of 1969, that DTAA needed to be interpreted *"uberrimae fidei"* which meant 'with utmost good faith'. Thus, the Tribunal held that Revenue was rewriting DTAA by contending that assessee deliberately manipulated length of projects to always keep it under 270 days and hence was an ill-placed allegation only.

(v) The Tribunal rejected Revenue's observation that grouting was not a simple masonry work and involved complex aspects on the ground that there was no bifurcation of simple and complex masonry/construction work under Article 5(2)(h) and any further classification would amount to rewriting DTAA. In view of the above, the Tribunal also denied Revenue's reliance on AAR ruling in *Sea Bird Exploration FZ LLC* by stating that when there was no option, the general Article 5(1) would get attracted which meant that when there was an option, specific article would prevail.

(vi) The Tribunal stated that few DTAAs like Australia, Thailand, Canada, USA, Denmark etc., the PE clauses are so worded that there is a specific mention for application of aggregation principle on all, or even connected, sites, projects or activities for computation of threshold duration test. However, the Tribunal noted that India-UAE DTAA used singular expressions 'a building, site or construction or assembly project' and, therefore aggregation of different projects was not allowed by conscious legislative scheme.

(vii) Regarding Revenue's contention that since assessee indulged in on-going projects, it cannot be said that the stay was less than nine months, the Tribunal opined that the establishment of PE in India is with respect to each AY only and there was no bar in carrying on the activities year after year. The Tribunal remarked that "The determination of existence of PE in India is to be made by reference to provision in DTAA." The Tribunal stated that Revenue was trying to set up a new case which was not permissible by the decision of the Special Bench in the case of Mahindra & Mahindra.

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