

TAX FLASH NEWS

2 May 2019

Income earned by a foreign company as a member of consortium/projects for providing technical assistance is taxable as business income under the India-Russia tax treaty

Recently, the Delhi Bench of the Income-tax Appellate Tribunal (The Tribunal), in the case of PJSC Stroytransgaz¹ (taxpayer) held that income earned by a foreign company as a member of consortium/projects for providing technical assistance is taxable as business income under the India-Russia tax treaty (the tax treaty).

Background and facts of the case

The taxpayer, a non-resident company, had a liaison office (LO) in India which assisted in identifying the business potential in India. The taxpayer also opened a branch office in India. During the financial year 2003-04, the taxpayer participated in three projects. The taxpayer was a member in all three projects/consortium. The taxpayer bifurcated its income into two parts i.e. royalty income earned by the head office which was offered to tax on the gross basis under Article 12 of the tax treaty and fees for technical services (FTS) earned by the branch office in India. The taxpayer had a PE in India under Article 5 of the tax treaty. The Assessing Officer (AO) held that the income of the taxpayer earned from the projects had been earned through PE in India. Therefore, the profits of the taxpayer were attributable to its PE in India. The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

Tribunal's decision

On a perusal of the contracts read with the supplementary agreement, it indicates that the taxpayer was one of the partners in all the three projects. Further, the contracts indicate that each member was assigned specific jobs to be executed by them and since the taxpayer had the expertise in the implementation of the oil and gas industry, it was assigned the principal job of preparation of

technical bid and because of this specialty, the taxpayer had laid emphasis that the payment received by it was for providing technical know-how and, therefore, was to be considered as royalty.

However, the Tribunal did not agree with the claim of the taxpayer since the taxpayer was one of the members of the consortium of all the three projects, this amounts to paying a royalty to oneself. The shares which the taxpayer received from the execution of the three projects was to be considered as the business profit of the taxpayer. However, the taxpayer chose to bifurcate the same into the royalty income of the head office and FTS for its branch office. Since there was no transfer of any technical know-how and even if the services were rendered in India by the head office and not by the branch office, then also, the revenue of the taxpayer cannot be bifurcated as royalty and FTS. The entire payment received by the taxpayer has to be attributable to the PE in India, and, therefore, the same is taxable as business profit.

Our comments

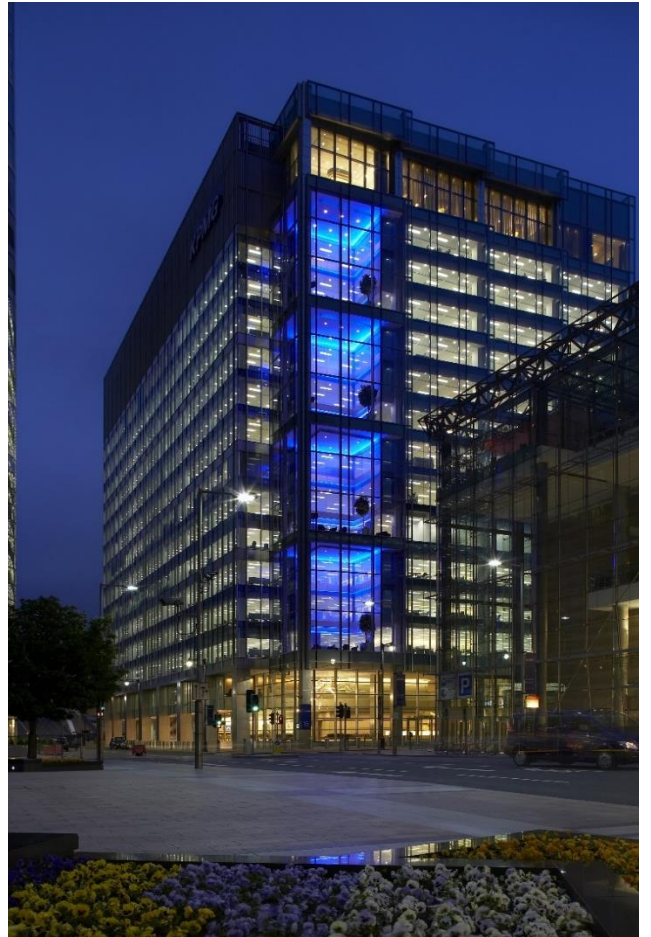
The issue with respect to treatment of income earned by a foreign company as a member of consortium/projects has been a subject matter of debate before the courts/Tribunal.

The Ahmedabad Tribunal in various cases² held that income earned by a foreign company as a member of consortium for providing technical guidance and consultancy for project management was liable to be taxed as FTS under the India-Russia tax treaty.

¹ PJSC Stroytransgaz v. DDIT (ITA No. 2942/Del/2010) – Taxsutra.com
² Joint Stock Company Zangas v. ADIT [2011] 13 taxmann.com 223 (Ahd), ADIT v. Joint Stock Company Zangas [2014] 44 taxmann.com 429 (Ahd)

¹ PJSC Stroytransgaz v. DDIT (ITA No. 2942/Del/2010) – Taxsutra.com

However, the Tribunal in the present case has held that income earned by a foreign company as a member of consortium/projects for providing technical assistance is taxable as business income under the India-Russia tax treaty.



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