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TAX FLASH NEWS

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Foreign tax credit is available in India on taxes deducted on commission income in Singapore

Recently, the Delhi Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Dynamic Drilling & Services Pvt. Ltd.[1] (the taxpayer) dealt with the allowability of Foreign Tax Credit (FTC) in India on taxes deducted in Singapore. The Tribunal observed that taxes were deducted at source in Singapore as per its domestic law and the same income was offered by the taxpayer in India. The Tribunal observed that the commission income was taxable in both the Countries i.e. Singapore as well as India as per the residuary article of the India-Singapore tax treaty (the tax treaty). Thus, the taxpayer was eligible for FTC in respect of taxes deducted in Singapore.

Facts of the case

The taxpayer, an Indian company, is engaged in the business of providing offshore drilling services and exploration and production of oils. The Assessing Officer (AO) noted that the taxpayer had claimed FTC under Section 90 for Assessment Year (AY) 2014-15. The AO observed that the taxpayer had received a performance guarantee commission from its overseas Joint Venture partner, Dynamic Drilling Holdco PTE Ltd. (DDHPL) based in Singapore. DDHPL had deducted tax on the commission paid to the taxpayer.

DDHPL had entered into a put/call option deed to buy 12 million shares of Dynamic Offshore Drilling Ltd (DODL) located in Cyprus. The seller/vendor was Dynamic Orion Singapore Pte Ltd (DOSPL), a Singapore based company. The taxpayer provided a performance guarantee in favour of the buyer company DDHPL to the vendor company DOSPL. A sum of USD 15 million was the consideration for which the taxpayer was to get performance guarantee commission.

[1] Dynamic Drilling & Services Pvt. Ltd. v. ACIT (ITA. Nos. 8154 AND 8155/Del/2019) – Taxsutra.com

The AO held that the commission received by the taxpayer from Singapore company was a business income of the taxpayer. Since the taxpayer did not have any PE in Singapore, the Singapore Tax Authorities could not have withheld the tax as the entire income is taxable in India.

The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO and denied FTC to the taxpayer.

Tribunal's decision

Taxpayer's main business was providing offshore drilling services and exploration and production of oil for companies in India. The taxpayer was not in the business of providing bank guarantee or performance guarantee.

The AO and the CIT (A) had misconstrued the facts and had given a finding that the provision of performance guarantee to the JV partner was for the strategic purpose in the course of business activity and it was therefore attributable to the business activity.

The AO cannot change the characteristic of one-time income by way of performance guarantee commission as business profit to bring it under the business income article of the tax treaty and hold that in order to avail tax benefit the taxpayer must have a PE.

Further the performance guarantee cannot be considered as Fees for Technical Services (FTS) as there was no rendering of technical service because there was no 'make available' of knowledge, experience, skills, know-how or process and development of any technical plant, technical design as per FTS clause of Article 12 of the tax treaty. The commission could not even fall under the provisions of Section 9(1)(vii).

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Further, it cannot be considered as interest falling under Article 11 of the tax treaty in the absence of any money borrowed or debt incurred. Neither did it fall under any other source of income elaborated in other Articles or any business income carried out from fixed place or under any of the clauses of Article 5 of the tax treaty.

Thus, it falls under residual head of income, which was covered under Article 23 of the tax treaty as per which item of income not mentioned in other Articles of the tax treaty may be taxed in accordance with the taxation laws of the contracting State. The Article 23 of the tax treaty clearly provides that the items of income which are not expressly mentioned in the foregoing Articles, same may be taxed by the respective contracting states, i.e., both under the taxation laws of Singapore as well as India.

Nowhere the AO and CIT (Appeals) had tried to find out whether this payment or the income of the taxpayer was not subjected to withholding tax under the laws of Singapore. They had presumed on the hypothesis that the commission was the business income of the taxpayer without having any PE and, therefore, as an Indian resident company the entire business is taxable in India. This hypothesis was divorced from the facts and material on record.

In view of Singapore Taxation Laws, commission income was taxable in Singapore even if the taxpayer had no PE in Singapore, on account of the fact that commission was deductible expense to the entity paying in Singapore.

If the source country which here in this case was Singapore, had held that amount was taxable under the Singapore Income Tax Laws and tax was withheld, then the tax credit was to be given on the same income offered by the taxpayer in India.

The Tribunal relied on the decision of Mumbai Tribunal in the case of Amarchand Mangaldas and Suresh K Shroff & Co[2] held that in all cases in which interpretation of residence country about applicability of a treaty provision is not the same as that of source jurisdiction about the provision and yet the source country levied taxes whether directly or by way of tax withholding, tax credit cannot be declined.

Further, the AO was obliged to allow tax deducted in Singapore as FTC under Rule 128 read with Section 295(2)(ha), even though this rule was introduced from 1 April 2017.

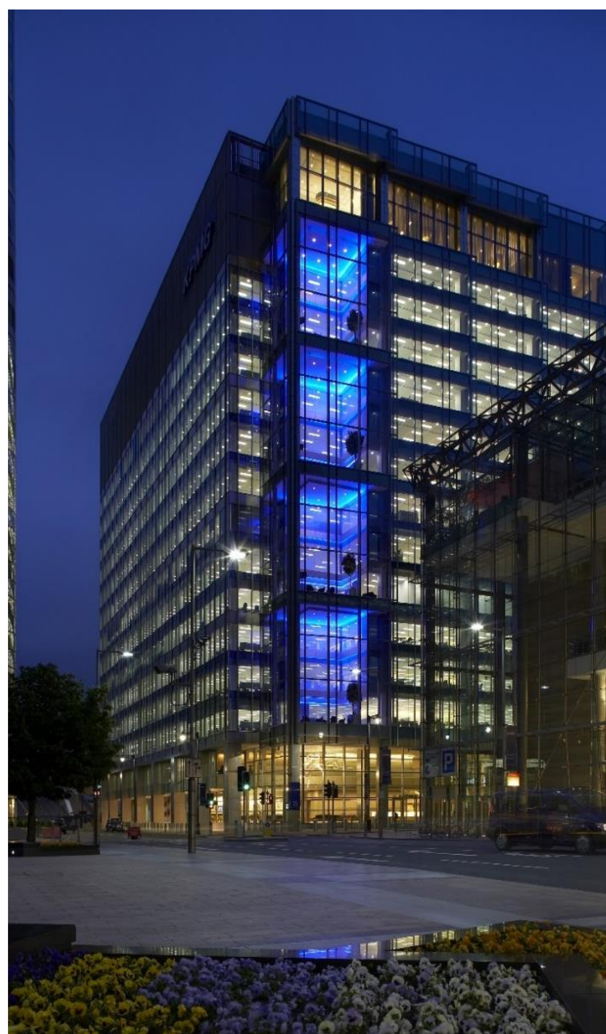
[2] Amarchand Mangaldas and Suresh K Shroff & Co v. ACIT (ITA No.2613/Mum/2019, dated 18 December 2020)

Our comments

Increase in cross border transactions posed various challenges with respect to taxation of foreign income and availability of credit of taxes paid in a source country.

While in some cases, the Courts/Tribunal have allowed[3] the foreign tax credit, in some of the cases, the credit has been denied[4].

The Tribunal in the present case has observed that taxes were deducted at source in Singapore as per its domestic law and the same income was offered to tax by the taxpayer in India. Therefore, FTC was allowed to the taxpayer in India.



[3] ITTIAM Systems Pvt Ltd. v. ITO [2021] 86 ITR(T) 611 (Bang), Amarchand Mangaldas and Suresh K Shroff & Co v. ACIT (ITA No.2613/Mum/2019, dated 18 December 2020), Promac Engineering Industries Ltd. v. ACIT (ITA No.501/Bang/2018)
[4] Bank of India v. ACIT [2021] 125 taxmann.com 155 (Mum)

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