

TAX FLASH NEWS

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To determine a threshold for Service PE under the India-UK tax treaty 'any 12 month period' is to be construed as previous/financial year

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Linklaters LLP¹ (the taxpayer) dealt with issue of whether the expression 'any 12 month period' as used in the Service Permanent Establishment (PE) clause of the India-U.K. tax treaty (tax treaty) could be construed as 'previous year' or 'financial year'. The Tribunal observed that if the provisions of Service PE clause of the tax treaty is read harmoniously with the provisions of the Income-tax Act, 1961 (the Act), it would be fair and reasonable to conclude that the expression 'any 12 month period' has to be construed to mean the 'previous year' or 'financial year'. Accordingly, the Tribunal directed the AO to verify as to whether the employees of the taxpayer were situated in India for rendering services for a period not exceeding ninety days during the previous year and if it is found to be so, then, it has to be held that the taxpayer did not have a PE in India under the tax treaty.

Facts of the case

The taxpayer, a Limited Liability Partnership, is a tax resident of U.K. and it offers legal consultancy services to its clients all over the world including India. During the Assessment Year (AY) 2013-14, the taxpayer provided professional services to its Indian clients.

The taxpayer contended that it did not have PE in India in terms of Article 5(2)(k)(i) of the tax treaty as its employees did not stay in India more than 90 days during the relevant year. The expression 'any twelve months period' as used in Article-5(2)(k)(i) of the tax treaty has to be construed as previous year relevant to AY under consideration. The aforesaid ratio has been laid down by the Tribunal² while deciding its own case. The taxpayer contended that the total number of days spent by the employees in India was 42 days. Therefore, in terms of Article-5(2)(k)(i) of the tax treaty, the taxpayer did not have PE in India during the year.

The tax department contended that the expression 'any twelve months period' as used in Article-5(2)(k)(i) of the tax treaty would not mean the previous year as defined in Section 3 of the Act. The tax department contended that, had it been the case, then, like Article-5(2)(k)(i) of the tax treaty, fiscal year which has been defined to be the previous year would have been used in Article 5(2)(k)(i) of the tax treaty. Thus, the meaning ascribed to fiscal year cannot be ascribed to the term 'any twelve months period'.

Tribunal decision

The Tribunal relied on taxpayer's own case for the AY 2012-13. The Tribunal in earlier case observed that the AO referring to Article 5(2)(k)(i) of the tax treaty had concluded that the taxpayer had a PE in India, since, its employees or personnel have rendered services in India for a period of 90 days or more within any 12 month period. However, the Tribunal observed that the expression 'any 12 month period' as used in Article 5(2)(k)(i) of the tax treaty had not been defined anywhere in the tax treaty. Therefore, the meaning of the said expression could be taken with the aid of the provisions of the Act, since, the income is sought to be taxed in India. Section 5 of the Act which defines scope of total income refers to the total income of any previous year of a person who is a resident. Similarly, Section 6 of the Act postulates that an individual or a HUF or a company or any other person can be considered to be a resident in India in any previous year if it satisfies the condition mentioned therein.

Thus, for the purpose of being considered as a resident in India a reference had been made to the previous year. Section 4 of the Act, which is the charging section, mandates that a person shall be charged to income tax in respect of the total income of the previous year. The expression 'previous year' has been defined under Section 3 of the Act to mean the financial year immediately preceding the AY. Thus, as per the

¹ Linklaters LLP v. DCIT [2019-TII-172-ITAT-Mum-INTL]

² Linklaters LLP v. DCIT [2018-TII-348-ITAT-MUM-INTL]

provisions of the Act, the 12 month period would mean the previous year or the financial year which is the unit for which the income of a person is taxable. If the provisions of Article 5(2)(k)(i) of the tax treaty is read harmoniously with the provisions of the Act, it would be fair and reasonable to conclude that the expression 'any 12 month period' mentioned in Article 5(2)(k)(i) of the tax treaty had to be construed to mean the previous year or financial year as per Section 3 of the Act, since, the income is sought to be taxed in India.

Therefore, the Mumbai Tribunal in the instant case directed the AO to verify as to whether the employees /personnel of the taxpayer were situated in India for rendering services for a period not exceeding ninety days during the previous year and if it is found to be so, then, it has to be held that the taxpayer did not have a PE in India during the year under consideration.

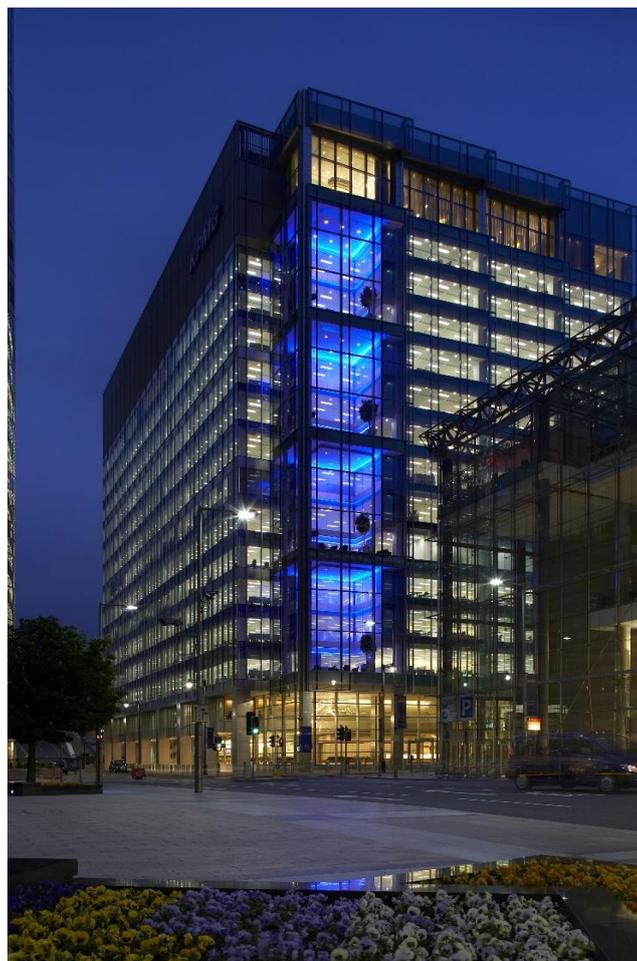
Our comments

The issue with respect to determination of service PE based on calculation of a relevant period for presence of employees in a particular jurisdiction, has been a matter a matter of debate before the courts.

The issue for consideration was whether the threshold has to be calculated on the basis of the 'entire period' for which services have been furnished in a source state although such period may span across various years. The Supreme Administrative Court of Austria³ held that the threshold has to be calculated on the basis of the 'entire period' of services rendered even though it may span across various years.

However, the Madras High Court in the case of Bangkok Glass Industry Co. Ltd.⁴ observed that the '183-day' threshold has to be determined based on the relevant fiscal year of source state⁵.

The Mumbai Tribunal in the instant case read the provisions of Service PE clause of the tax treaty harmoniously with the provisions of the Act and held that the expression 'any 12 month period' has to be construed to mean the 'previous year' or 'financial year'.



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³ IBFD Case No. 95/13/0137 (Supreme Administrative Court of Austria)

⁴ Bangkok Glass Industry Co. Ltd. v. ACIT [2013] 34 taxmann.com 77 (Mad)

⁵ 1 April to 31 March in the case of India

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