

Revenue allocated to German HO by Indian BO not taxable in India as India-Germany DTAA allows “fee splitting arrangement”.

Summary – The Mumbai bench of the ITAT has recently pronounced a decision in the case of Germanischer Lloyd A.G., (the Assessee) and held that where fee split arrangement was fully backed by the India Germany DTAA, revenue allocated to German head office by the Indian branch office could not be taxed in India.

Facts

- The assessee company (having its head office in Germany) was engaged in providing inspection and certification services to the maritime industry. The assessee had submitted that it had been following a “Fee splitting mechanism” with its head office and the fee retained or remitted to the HO was the income of the head office and same could not be taxed in the hands of the assessee.
- The revenue however submitted that with regard to the functions of the head office and branch office the job was conducted in India and only the intimation was forwarded to the head office. Therefore, since the assessee and the head office were part of the same organization, the question of splitting of fee could not arise.
- However, the assessee submitted that the fee splitting mechanism fell within the protocol to the India Germany DTAA and the said mechanism had been devised way back in 1973 and similar attribution was followed globally. It was further submitted that the head office provided continuous assistance to its branch offices.

Held

- The ITAT held that it was an undisputed fact that India Branch Office undertakes inspection and validation of ocean fairing vessels by physically examining the vessels. After physical examination, the reports are sent to the HO located in Germany and the HO issues a validation certificate regarding the fitness of the vessel thereafter.
- Under the business model followed by the assessee and its HO, ships and vessels in order to operate in the sea are required to be classified by a classification society approved by an authority – this classification is done at the insistence of the ship owner on their own behalf or on behalf of the respective governments. In either case, the post examination approval reports are submitted to the respective government/ship owners.

- The Indian activities are carried out with the technical assistance and cooperation of its HO in Germany which is available for assistance 24x7. Once the classification work is completed, an invoice is raised by the Indian BO or the German HO, as the case may be, and the receipts are assigned as per the agreed module followed globally, whereby the HO retains 30 per cent and the BO retain 70 per cent as per fee splitting arrangement.
- While interpreting the India Germany DTAA it was held that as per Article 7, the business profits of only the permanent establishment in India are offered to tax.
- Accordingly, strictly following the DTAA, the split of fee which is attributed to the German HO, become non-taxable under the Indian tax regime.
- The ITAT followed the decision of *Intergrafia Print & Pack GMBH* where after following the India German DTAA, the Delhi ITAT had approved of the fee split arrangement. The ITAT also agreed to the decision of the assessee's own case in penalty proceedings, wherein, the CIT(A) came to a factual finding that, "following a well defined system, the revenue earned from the activities of the HO cannot be taxed in India", which ultimately has been attributed to the HO and fully backed by the India German DTAA and Para1(b) of the Protocol.