Tenet Tax & Legal Private Limited

Tenet Tax Daily
October 3, 2013

Business income of NR not taxable if its dependent agent is remunerated on ALP basis and is charged to tax

Summary – The Mumbai ITAT in a recent case of ANL Singapore Pte. Ltd., (the Assessee) held that where associated enterprise of an assessee that also constituted its PE was remunerated on ALP, then nothing further was left to attribute to PE and, therefore, in such a case, income from business operations could not be included in hands of non-resident assessee.

- This appeal by the assessee is directed against the order passed by the Assessing Officer u/s 143(3) read with section 144C(13) of the Income-tax Act, 1961 (hereinafter also called as 'the Act') in relation to the assessment year 2007-08.

- Briefly stated the facts of the case are that the assessee is shipping company incorporated in and tax resident of Singapore. Gross receipts of freight amounting to Rs. 13.34 crore were shown and after application of section 44B of the Act, income was declared at the rate of 7.5% amounting to Rs. 1.00 crore and odd. The Assessee claimed exemption of this income as per Article 8 of the Double Taxation Avoidance Agreement between India and Singapore (hereinafter also called 'the DTAA'). A copy of Tax residency certificate was furnished to indicate that the assessee was tax resident of Singapore. The Assessing Officer noticed that the assessee earned shipping income from pool arrangement with Noratia and CMA CGM China in respect of 37 voyages, which in his opinion did not qualify for relief under Article 8 of the DTAA because of the absence of any evidence of the proof about the assessee having any pool arrangement. Similarly, the AO noticed that the assessee had shown freight receipts in respect of slot hiring charges from 61 voyages amounting to Rs. 3.65 crore. Since, the slots were hired from CMA CGM as sub-charterer, who had an arrangement with other shipping companies, the Assessing Officer held that the relief in respect of such 61 voyages was also not available under Article 8 of the DTAA.
- The AO refused the benefit of Article 8 in respect of 98 voyages, out of total of 178 voyages, on a sum of Rs. 8.09 crore (inclusive of detention charges). Thereafter, he proceeded to determine as to whether the assessee has a permanent establishment in India in the form of M/s CMA CGM Global (India) Pvt. Ltd. (hereinafter also called 'CMA'). On a perusal of the agency agreement with CMA, the Assessing Officer came to hold that CMA was assessee's dependent agent and hence it constituted its permanent establishment in India as per the terms of Article 5 of the DTAA. In that view of the matter, he computed income at Rs. 89.01 lacs u/s 44B of the Act by applying rate of 10% in respect of the 98 voyages. As regards the remaining 80 voyages, he computed income u/s 44B at the rate of 7.5% at Rs. 33.35 lacs and allowed exemption under Article 8 of the DTAA.

- The Draft assessment order was challenged by the assessee before the Dispute Resolution Panel (hereinafter also called 'the DRP'). Vide its Direction dated 16.09.2010, the DRP directed the Assessing Officer to examine fresh evidence in respect of 98 voyages and allow similar benefit if the conditions of Article 8 were fulfilled. Vide the final order passed by the AO u/s 144C(13), the Assessing Officer noticed that the assessee failed to furnish any details in respect of 21 shipments. He, therefore, granted relief in respect of 77 voyages and proportionately determined receipts in relation to 21 voyages at Rs. 26.31 lacs. Rate of 10% was applied for determining total income at Rs. 2.63 lacs.

- The ITAT after having heard the rival submissions and perused the material on record, held that before going into the first question of the availability of the benefit of Article 8 of the DTAA in respect of such 21 voyages, it would be important to examine as to whether the amount is chargeable to tax as per Article 7 of the DTAA. The ld. AR was fair enough to accept that CMA may be considered as the dependent agent of the assessee. Thus, it satisfies the requirement of Article 5 of the DTAA. We therefore, hold that CMA was the agent of the assessee and hence constitutes its permanent establishment in India.

- The next question is determination of the 'Business profits' as per Article 7 of the DTAA. The ld. Counsel for the assessee contended that CMA was given commission, container controller fees and detention collection fees in respect of total 178 voyages which include 21 voyages in respect of which the instant addition has been made. He took us through relevant documents of CMA, copies placed on pages 77, 84 and 85 of the paper book, for indicating that the assessee made a payment of such commission etc. to CMA which was declared by the latter in its report in Form No. 3CEB, being international transactions, *inter alia,* with the assessee. It was submitted that in the draft assessment order passed by the relevant AO in the case of CMA, a transfer pricing adjustment of Rs. 3.00 crore was proposed. However, the DRP vide its direction dated 23.09.2011, in the case of CMA, held that the transfer pricing adjustment was not warranted. In the final assessment order passed u/s 144C(13) in respect of CMA, the Assessing Officer did not make any transfer pricing adjustment. It was submitted that since commission etc. to CMA was paid at arm's length price (ALP), there were no question of taxing further 'business profits' in the hands of the assessee under Article 7. In support of this contention, he relied on the judgment of the Hon'ble jurisdictional High Court in *Set Satellite(Singapore) Pte Ltd*. v. *Dy. DIT(IT)* [2008] 307 ITR 205/173 Taxman 475 (BOM). Similar view was shown to have been taken by the Mumbai Bench of the Tribunal in the case of *Delmas, France* v. *Asstt. DIT(IT)* [2012] 49 SOT 719/17 taxmann.com 91.

- Opposing the contention advanced on behalf of the assessee, the ld. DR submitted that commission paid to the dependent agent at arm's length price cannot have the effect of

obliterating the profit earned by the assessee from the shipping income. She stated that commission is simply one of the costs incurred by the assessee in earning the overall income. If one expense has been incurred at market price, it does not mean that there remains no profit from the overall business activity in the hands of the assessee. When the assessee has a permanent establishment in India and business income is attributable to such permanent establishment, then apart from the commission income earned by such agent in its individual capacity, the income from carrying on the business activity of the assessee relatable to the PE in India should also be taxed. She argued that the subject matter of taxation in India under Article 7 of the DTAA is 'Business profits' earned by the enterprise of the other State through a PE in India. As the taxable entity *qua* such 'business profits' is not the PE in its individual capacity but the enterprise of the other State represented by such PE, it is the income earned by the assessee through its PE which is chargeable to tax, which in the present context is from the shipping activity. The fact that such agent, representing PE, has been taxed distinctly in its individual capacity, *inter alia*, from the commission earned at arm's length price, does not mean that the business profits of the assessee attributable to the PE stand automatically erased.

- It is observed that the income in respect of 21 voyages which has been considered as chargeable to tax in India as per Article 7 of the DTAA is the amount on which the assessee paid commission etc. to CMA, which is its AE and also a dependent agent. The receipt in the hands of the CMA has been determined at ALP under due process of law. Though we do not find the submissions of the ld. DR recorded above as absolutely devoid of any force, but the cases of *Set Satellite* (*Singapore*) *Pte. Ltd.* (*supra*) and *Delmas France* (*supra*) stand in the way. In these decisions, it has been held that where the associated enterprise (that also constitutes a PE) is remunerated on ALP, then nothing further would be left to attribute to the PE. In that view of the matter and respectfully following the precedents, we uphold the contention of the ld. AR. We, therefore, hold that income in respect of 21 voyages cannot be included in the hands of the assessee.

- In view of our above decision on the exclusion of income in respect of 21 voyages, there remains no need to consider the taxability or otherwise of the amount as per Article 8 of the DTAA. The main issue raised through various grounds is, therefore, decided in assessee's favour.