

Group Cos negotiating/securing contracts on behalf of foreign Co. would be deemed as service PE in India

Summary – The Delhi ITAT in a recent case of Nortel Networks India International Inc., (the Assessee) held that where assessee, a US based company, entered into contract with an Indian company for supply, installation, testing and commissioning of equipment relating to GSM Cellular Radio Telephone System, in view of fact that a group company namely 'NL' India undertook responsibility for negotiating and securing contracts whereas another group company namely 'NL' Canada supplied aforesaid equipments and its LO in India rendered other services to assessee, those group concerns constituted assessee's PE in India.

Facts

- The assessee was a company incorporated in the USA. It was a group concern of 'N' Group, which was a leading supplier of hardware and software products for GSM Cellular Radio Telephones System.
- The Indian subsidiary of 'N' Group 'NL' entered into a contract with Reliance Infocom for supply of hardware equipment. Immediately after signing said contract, it was assigned by the Indian subsidiary to the assessee without any consideration. The equipments supplied by the assessee to the Indian buyer was purchased from another group company *i.e.* 'NP' Canada. The assessee thus supplied telephone hardware to Reliance Infocom.
- The assessee had not filed its return of income voluntarily for the relevant year. In the profit and loss account the assessee has booked huge gross losses.
- From the examination of the financial statement, the Assessing Officer opined that assessee did not have any manufacturing or trading infrastructure. It did not have any financial or technological capability of its own. He thus held that assessee was only a paper company incorporated for the sole purpose of evading taxes in India.
- The Assessing Officer further opined that since the assessee and 'NP' Canada were one and the same the LO building pertaining to Canadian Company constituted fixed place PE of the assessee in India. Similarly, 'NL' India would also represent PE as the business of the assessee was partly or wholly carried on through the premises of 'NL' India.
- The Commissioner (Appeals) confirmed order of Assessing Officer holding that 'NP' Canada and 'NL' India constituted assessee's PE in India in terms of article 5 of India-USA DTAA.
- The Commissioner (Appeals) further held that 50 per cent of profits arising to the assessee from supply of telecom hardware to Indian customers were attributable to alleged PE in India.
- On second appeal:

Held

- The authorities below rightly concluded that the contract entered between the assessee group and the Reliance Infocom which was a turnkey contract, indivisible contract for supply, installation,

testing, commissioning etc. 'NL' India has undertaken the responsibility for negotiating and securing the contracts. The contract for installation and commissioning was also undertaken by 'NL' India. Thus, the proposition that these arrangements show that assessee is getting its work executed through 'NL' India is correct. The assessee is merely a shadow company of 'N' Group and for all practical purposes, all the facilities and services available to the 'N' Group of Companies are equally available to the assessee. The hardware supplied through it is installed by 'NL' India. The contracts were pre-negotiated by 'NL' India. Thus, the authorities below rightly held that 'NL' India is a fixed place of the business and dependent agent PE of the assessee.

- The LO of 'NP' Canada was rendering all kinds of services to all the group companies including the assessee. The LO building pertaining to Canadian Company constitutes fixed place PE of the assessee.
- The assessee's contention that sales were completed overseas and installation was done under a separate contract cannot be accepted. The assessee through 'NL' India and LO approached the customer, negotiated the contract, bagged the contract, supplied equipment, installed the same, undertook acceptance test after which the system was accepted. The equipment remain in the virtual possession of 'N' Group till such time the equipment is set up and acceptance test is done.
- It is also an admitted fact that employees of group companies did visit in India in connection with Project in India. Thus, this indicates the employees of the group companies did carry out business of the assessee through the premise of LO or the premises of the subsidiary. Thus, the entire business enterprise activities of the assessee is managed by the subsidiary in India and the requisite supply is made from abroad. The contract does not only need loading of the equipments in the ship, but includes number of activities which are carried out in the Indian territory and the compensation/remuneration for that is also included in consideration.
- The Commissioner (Appeals) rightly held that the compensation which has been represented to a sale consideration for the equipment represent the payment for works contract where entire installation and customisation has been carried out in India. That the subsidiary has not only acted as a service provider for the assessee, but at the same time acted as a sale outlet cooperating with after sale service and also providing any assistance or service requested by the assessee.
- The assignment agreement between Indian subsidiary (assignor), the assessee-company (assignee), the parent company 'NP' Canada (the guarantor) and Reliance Infocom (the Purchaser) indicates that the contract initially signed by the Indian company gets assigned by the Indian subsidiary to the assessee and all the risk and responsibility in this regard are assumed by the parent company.
- In the background of the aforesaid discussion, the Commissioner (Appeals) rightly concluded that activities of the assessee in India constitute PE of the Assessee in terms of article 5 of the Indo-US DTAA. The activities carried out by the PE are the core activities of the assessee resulting in generation of income to the assessee and they cannot be considered to be preparatory and auxiliary and therefore, the contention of the assessee that it do not have PE in India is rejected.

- The next issue is that how much of the profits arising to the assessee from supply of telecom hardware to Indian customers is attributable to the PE in India.
- The accounts of the assessee furnished in the assessment proceedings have no sanctity. The same were not audited. The gross trading loss incurred from transaction within the group cannot be explained except for the reasons, that it has been designed as such to avoid taxation in India. Hence, for all purposes the accounts of the 'N' Group would give a true and correct picture of the profit of the assessee. Hence, Assessing Officer's reference to the global accounts of the 'N' and gross profit margin percentage as 42.6 per cent is accepted. Now the issue is as to how much of the profit is attributable to the PE.
- In this regard the Commissioner (Appeals) proposition that when profits are computed under rule 10 of Income-tax Rules, 1962 after applying the profit rate, the expenses pertaining to the PE have to be allowed as deduction is correct. Assessee has contended before the Commissioner (Appeals) that in other cases attributed profits was determined at the rate of 20 per cent in the case of Nokia and 35 per cent in the Rolls Royce. In this regard, Commissioner (Appeals) has held that income of the PE has to be computed on the facts of each case. The Commissioner (Appeals) has held that he was of the view that an attribution of 50 per cent of the profits to the activities of PE in India would be a reasonable attribution.
- It was noted from the gross profit computed by reference to the rate applicable to the global accounts of the assessee, further substantial deduction has been allowed for selling general and marketing expenses and also R&D expenses. Thereafter, 50 per cent of the resultant figure has been attributed to PE. This meets the ends of justice.
- In the background of the aforesaid discussion, it is held that Commissioner (Appeals) is justified in attributing 50 per cent of the profit to the PE i.e. assessee. Accordingly, there is no infirmity in the order of the Commissioner (Appeals) and hence, the same is upheld.