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No TDS on sum paid for repairing of aircraft as same was leased to foreign Co and running on international routes

Summary – The High Court of Delhi in a recent case of Lufthansa Cargo India., (the Assessee) held that Payment made by assessee, engaged in wet leasing of aircrafts to foreign companies on international routes only, for carrying out overhaul repairs to aircrafts was FTS under section 9(1)(vii); but it could not be taxed in India owing to exclusionary clause (b) of section 9

Facts

- The assessee was engaged, in wet leasing of aircrafts to foreign companies, on international routes only. The assessee entered into an overhaul agreement with a German Co. (Technik) to carry out maintenance repairs without providing technical assistance by way of advisory or managerial services and these repairs, therefore, did not constitute 'managerial', 'technical' and 'consultancy services' as defined under *Explanation* 2 to section 9(1)*(vii)(b)* as per the assessee.
- The Assessing Officer held that the said payments were in the nature of 'fees for technical services' defined in *Explanation* 2 to section 9(1)*(vii)(b)*, and were, therefore, chargeable to tax on which tax should have been deducted at source under section 195(1). The Assessing Officer passed orders under section 201 deeming the assessee to be an assessee in default, and levied tax as well as interest under section 201(1A). The assessee's alternate plea that in any case the payments made to residents of USA, UK, Israel, Netherlands, Singapore and Thailand could be taxed as business profits only and not as fees for technical services keeping in view the relevant provisions of the DTAAs with those countries, too was rejected.
- According to the Commissioner (Appeals), the repairs constituted 'technical services' and therefore, were subject to TDS. With reference to payments made to residents of UK and USA, the Commissioner (Appeals) held that they were not in the nature of 'fees for technical or included services' under article 12 of the DTAA but were 'business profits' and since those companies did not have a PE in India, their income was not chargeable to tax.
- The Tribunal held that the payments made to Technik and other foreign companies for maintenance and repairs were not in the nature of fees for technical services as defined in *Explanation* 2 to section 9(1)*(vii)(b)*. Further, in any event these payments were not taxable for the reason that they had been made for earning income from sources outside India and, therefore, fell within exclusionary clause of section 9(1)(vii)(b).
- On appeal :

Held

Component overhaul or repair is technical service

- The Tribunal, concluded that the services provided by Technik did not fall within the expression "technical service" and that section 9(1)*(vii)* did not apply at the threshold. To arrive at this conclusion, the Tribunal held that the assessee had no say in the work done by Technik and did not know what kind of repairs were carried out and that none of its employees ever visited Technik's facility in connection with such work. The Tribunal surmised that since what the assessee asserted is that the overall components are returned duly certified by Technik that it had carried out the prescribed repairs, alongwith warranty and tax, there was no technical assistance by providing managerial, consultancy or technical services. It concluded that Technik performed the entire work on "an inanimate body without any involvement or participation of assessee's personnel". It also held that managerial or physical exertion by Technik's engineers on the assessee's components did not render such services managerial, technical and consultancy services within the meaning of section 9(1)*(vii)(d)*.
- This Court is of the opinion that the Tribunal was unduly influenced by all the regulatory compulsions which the assessee had to face. Besides international convention and domestic law that mandated aircraft component overhaul, the manufacturer itself – as a condition for the continued application of its warranty, and in order to escape any liability for lack of safety, required periodic overhaul, maintenance and repairs. Unlike normal machinery repair, aircraft maintenance and repairs inherently are such as at no given point of time can be compared with contracts such as cleaning *etc.* Component overhaul and maintenance by its very nature cannot be undertaken by all and sundry entities. Level of technical expertise and ability required in such cases is not only exacting but specific, in that aircraft supplied by manufacturer has to be serviced and its components maintained, serviced or overhauled by designated centres. It is this specification which makes the aircraft safe and airworthy because international and national domestic regulatory authorities mandate that certification of such component safety is a condition precedent for their airworthiness. The exclusive nature of these services cannot but lead to the inference that they are technical services within the meaning of section 9(1)*(vii)*. The Tribunal findings on this point are, therefore, erroneous.

Payment fell under exclusionary clause of section 9

- As regards treatment of expenditure incurred by the assessee (*i.e.* the payments made) towards its activities outside India, the assessee's submission was that the payment made fell within the exclusionary part of section 9(1)*(vii)(b)* and was not affected by the *Explanation* to section 9(2). The assessee stressed upon the fact that no foreign technician was deputed to work in India. The assessee's submission is that the source of its income is wet-leasing activity to non-resident companies and consequently the source of income is outside India.

- The revenue's contention, was that the materials did not show that entire income was earned from sources outside India and consequently, the payment made to Technik could not be excluded. The revenue also relied on the retrospective amendment to section 9(2) made in 2010 to say that regardless of the question as to whether the expenditure is towards income earned abroad, the payee is deemed to have earned income in India by virtue of the amendment.
- "The revenue urges that the fiction created by the said amendment is to do away with the requirement of the non-resident having a place of business, or business connection, irrespective of whether "..the non-resident has rendered services in India." Did this amendment make any difference to payments made to such companies – even in relation to income accruing abroad? The revenue grounds its arguments in the assumption that the later, 2010 retrospective amendment, overrides the effect of section 9(1)*(vii)(b)* exclusion. While no doubt, the Explanation is deemed to be clarificatory and for a good measure retrospective at that, nevertheless there is nothing in its wording which overrides the exclusion of payments made under section 9(1)*(vii)(b)*.
- In the present case, the Tribunal held that the overwhelming or predominant nature of the assessee's activity was to wet-lease the aircraft to, a foreign company. The operations were abroad, and the expenses towards maintenance and repairs payments were for the purpose of earning abroad. In these circumstances, the Tribunal's factual findings cannot be faulted.