Payment made for package of designs and drawings couldn't be treated as royalty

Summary – The Delhi ITAT in a recent case of PB Asia Ltd., (the Assessee) held that Payment made towards an agreement for supply of package of design and drawing to enable assessee to effectively render engineering services, was not royalty

Facts

- The assessee was a company established under the laws of Thailand and was engaged in the business of providing architectural and engineering services relating to infrastructure projects throughout the Asia Pacific region. An Indian company (PBIPL) entered into an agreement with Larsen and Toubro for providing engineering consultancy services in connection with the second Tollway. In connection with the aforesaid agreement, PBIPL entered into a contract with the assessee for rendering certain services. In consequence, the assessee received payment from PBIPL.
- The assessee was asked to show-cause as to why payment received from PBIPL should not be taxed as 'Fee for Technical Services' ('FTS') under section 9(1)(*vii*) or alternatively taxable as 'Royalty' under article 12 of the DTAA read with section 9(1)(*vi*). Assessee filed detailed submissions stating that the payments received from PBIPL should be treated as business income of the assessee by applying article 7 of the relevant DTAA. Further, it was also submitted that the receipts from PBIPL, being in nature of business profits, were not to be subjected to tax in India, in the absence of assessee's PE in India under article 5 of the DTAA. The Assessing Officer rejected the contentions of the assessee and passed assessment order under section 144C/143(3) by treating the income as 'royalty'.
- The Commissioner (Appeals) called for Memorandum of Association and article of Association of the assessee-company and after examination, observed that the assessee-company was not engaged in sale/purchase of the designs and drawings. According to him, the assessee was only a service provider. The Commissioner (Appeals) was of the view that agreement between the assessee and the PBIPL was a purely service agreement and question of sale of designs by the assessee to the PBIPL would not arise. The Commissioner (Appeals) held that the payments under consideration were in the nature of royalty under provisions of Act.
- On appeal:

Held

- The present case is covered from the decision of Delhi Tribunal in *Parsons Brin Ckerhaff India (P.) Ltd.* v. *Asstt. DIT (International Taxation)* [2008] 24 SOT 341 wherein the issue in dispute has been decided in favour of PBIPL. Where the transaction has been held as outright sale of design & drawing by the assessee *i.e*. PBAT to PBIPL. It was held that though it was titled as a service agreement, it was actually an agreement for supply of a package of designs and drawings to enable the assessee to effectively render engineering consultancy services to the consortium which was found in charge of constructing Tollway. On a perusal of the decision it is that the transaction in

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question is an outright sale of design and drawings and does not constitute royalty in the hands of the assessee. The Tribunal has further observed that rather than form, substance is important and said that provision in the agreement for visit of the personal of the assessee to Kolkata and Delhi, if required, is not inconsistent with the outright sale theory. Further, the contention of the Commissioner that the intellectual property right of the design remained with assessee has been disputed by the assessee (sic). It is submitted that the assessee was bound to surrender design to PBIPL as per clause 13 of the agreement between the parties.

- Payment received by the assessee from PBIPL had been examined in detail by the Tribunal and the payment being in nature of business income, it was not taxable in India in the absence of PE in India and consequently, the amount remitted to the assessee by PBIPL was not 'royalty' within the meaning of section 9(1)(*vi*) and article 12(3).

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