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Delhi HC remanded case back as ITAT failed to examine taxability of technical service charge in terms of FTS

Summary – The High Court of Delhi in a recent case of Modiluft Ltd., (the Assessee) held that Taxability of technical service charges payable to foreign company in Germany to be determined in terms of article VIIIA of DTAA between India and Germany as there existed a 'Fees for Technical Services' clause in lease agreement with said company

Facts

- The assessee leased three aircrafts (aircraft lease agreement) from a german company, Deutsche Lufthansa Aktienge sells chaft (Lufthansa). Before the lease agreement, the assessee had entered into agreement for technical support (technical support agreement). In addition, another agreement for provision for flight deck crews (flight deck agreement) was also entered into. The aircraft lease agreement was approved by the CBDT under section 10(15A).
- The Assessing Officer declined the assessee's request for withholding tax certificate in respect of crew lease payments for engineers by holding that:
  (a) crew lease payment was not covered under section 10(15A);
  (b) technical support agreement for providing engineers on lease was not approved under section 10(15A);
  (c) Under the DTAA between India and Germany, payments to a non-resident for providing technical personnel is fee for technical service (FTS) and the same is taxable in the country in which they arise.
- On appeal, the Commissioner (Appeals) by a consolidated order, dismissed the appeals in limine on the ground that the same were barred by limitation.
- On further appeal, the Tribunal firstly condoned the delay in filing the appeal and following the previous order dated 18-9-1998 in IT Appeal No. 2648 of 1998 held that:
  (i) Payments under technical support and crew lease agreements were not entitled to exemption under section 10(15A) because no approval under section 10(15A) was granted to these agreements.
  (ii) Both the lease rent and the fee for technical services were business profits of Lufthansa, inasmuch as the lease of the aircrafts was with the operational staff.
  (iii) Having held that lease rent and fee for technical services was business profits, the Tribunal relying upon *Tekniskil (Sendirian) Berhard* v. *CIT* [1996] 88 Taxman 439/222 ITR 551 (AAR - New Delhi) held that payment made for provision for technical personnel was not taxable in India within the meaning of article III of the DTAA between India and Germany.
- On revenue's appeal to the High Court:

Held

- During the hearing of the appeals, great emphasis was laid on the fact that the Tribunal had recorded independent findings with regard to the non-taxability -as FTS and under the DTAA, of the assessee's payments and the finding that Lufthansa had no PE in India. The fact that the findings of the Tribunal, as is evident, were influenced by the decision of the AAR in *Tehniskil (Sendirian)* (*supra*) were rendered in an entirely different context, and in that case the relevant Double Taxation Avoidance Agreement between India and Malaysia as applicable at the relevant time did not contain the clause for 'Fee for Technical Services'. In that context it was held by the AAR, that the fee for technical services arising out of supply of skilled labour were not liable to tax in India in terms of article 7 as 'business profits' on the ground that the assessee did not have a permanent establishment in India in terms of article 5 of the Double Taxation Avoidance Agreement. In the facts of the instant case in terms of the DTAA, payments made to Lufthansa may not be liable to tax in India in terms of article III of the DTAA, yet their taxability in terms of article VIIIA of the DTAA, as there exists a 'Fee for Technical Services' clause in the Agreement, was not examined in proper perspective.
- Thus, the issue of technical fee has to be examined from the point of view of article VIIIA introduced by the amending protocol, which to the extent it is relevant, states (by clause (4)) that: 'fees for technical services' as used in this Article means payments of any kind to any person, other than payments to an employee of the person making the payments, in consideration for services of a managerial, technical or consultancy nature, including the provision of services of technical or other personnel. The facts of this case also reveal that only one agreement, *i.e.*, the lease agreement, was approved under section 10(15A). The other two agreements, *i.e.*, the crew lease and technical support agreements were not approved. There is no discussion in the orders of the Tribunal whether the payments made under the technical support agreement or the crew lease agreements were not payment for technical services, apart from an a priori assumption that the question of taxation does not arise if there is no PE. With respect to payment for services of personnel under the crew lease agreement, both the statute (*Explanation 2* to section 9(1)(vii)) and the DTAA talk of taxability of payments for services that are managerial, technical or consultative in nature 'including provision of services of technical or other personnel.'
- In the absence of the agreements and a fuller discussion by the Tribunal which seems to have decided only on the applicability of the AAR's ruling, it is opined that the appeals need to be reconsidered and specific findings rendered in the context of section 9 (1)(vii) and provisions of the DTAA.
- For the above reasons, the appeals are allowed to the extent that the impugned orders are set aside; the issue is restored to the file of the Tribunal which shall proceed to hear the cases and render its findings in the light of the provisions of DTAA and the other provisions of the Act, in accordance with law.