

ITAT: Absolves German Co. from taxability of offshore supplies & inextricably linked services

Nov 30, 2023

DSD Noell GMBH [TS-714-ITAT-2023(DEL)]

Conclusion

Delhi ITAT deletes the addition on account of consideration received by a German entity for offshore supplies and holds *"no part of consideration received outside India for offshore supplies of plant and equipment and spares could be deemed to accrue or arise in India as per section 9 in the hands of the assessee"*; Further observes that admittedly, the Assessee has no Permanent Establishment (PE) in India and *"such consideration would only be in the nature of business income not attributable to PE in India and hence not taxable under Article 5 read with Article 7 of the India-Germany DTAA"*; ITAT notes that plant and equipment supplied to Hindustan Construction Company Ltd. (HCC) were designed and manufactured outside India, title was duly passed on to the customer outside India on FOB basis, consideration for such offshore supplies was also received outside India in foreign currency either through letter of credit or through bank transfer and all activities such as manufacturing, fabrication, designing etc. of plant & equipment was undertaken outside India; Relies on SC judgment in [Ishikawajima-Harima](#) and jurisdictional HC judgment in [National Petroleum](#) to observe *"where the property in respect of the goods is transferred to the buyer outside India, the sale of such goods has to be regarded as having completed outside the taxable territories of India, hence, the income from such sale is not liable to tax in India"*; Regarding offshore services of drawing and designs, ITAT observes that the drawings and design supplied are inextricably linked with the plant and equipment supplied by the Assessee; Relies on Jurisdictional HC judgment in [Linde AG](#) and co-ordinate bench ruling in [SMS Concast](#) to observe, *"if design and engineering is inextricably linked with the manufacture and fabrication of the material and equipment to be supplied from overseas, and form an integral part of the said supply, then the services rendered would not be amenable to tax as FTS"*; Further relies on SC judgment in [ONGC](#) and observes that the dominant object of the contract entered with HCC was to supply a plant manufactured according to the designs developed, thus, the character of the offshore services must be that of the supply of the equipment; :ITAT DEL

Decision Summary

The ruling was delivered by the Division Bench of Delhi ITAT comprising Shri Challa Nagendra Prasad, Judicial Member and Shri M. Balaganesh, Accountant Member

Advocate Rajan Bhatia and CA. Shruti Srivastava appeared for the Assessee while the Revenue was represented by Mr. Sanjay Kumar, Senior D.R.

Assessee-Company, incorporated in Germany, is engaged in the business of engineering, designing, manufacturing and installing plants for the hydro electric power projects and entered into agreement with HCC for carrying out hydro-mechanical works in relation to setting up of Kishanganga Hydro Electric Power Project of NHPC; For AY 2011-12, 2012-13 and AY 2014-15 to AY 2018-19, Assessee received consideration from HCC towards offshore supply of plant & equipment as well as for offshore services (involving supply of related drawings design) which were not offered to tax in India and the same was disputed by the Revenue as well as CIT(A); ITAT observes that the Assessee submitted copy of invoices, bill of lading, shipping documents etc. to substantiate that transfer of title and risk happened outside India; ITAT finds that custom clearances though was Assessee's responsibility, however, all the plant & machinery and materials received remained absolute property of the owner; Rejects Revenue's argument that the Assessee was responsible for insurance by observing that HCC was also the co-insurer in the insurance policy and it was clearly specified that plant and equipment shall remain absolute property of HCC; Regarding, Revenue's argument that title and custody of equipment passed only after successful commissioning of the plant at project site in India, ITAT notes that separate agreement for onshore services such installation, erection, commissioning and supervision at project site in India was entered

and consideration received separately for the same was offered to tax which is not disputed in the instant case; Relies on jurisdictional HC judgment in case of [LG Cables](#) to observe, “*none of the stipulations of the onshore contract could conceivably postpone the transfer of property of the equipment supplied under the offshore contract, which, in accordance with the agreement, had been unconditionally appropriated at the time of delivery, at the port of shipment*”.

Regarding Revenue’s observation that 100% supply of machinery is not preceded to the formation of Project Office in India

ITAT observes that it is inconclusive to hold that the offshore supply is taxable in India; Further opines that several machineries were supplied at different point of time from outside India and for all the machineries that were supplied, the title was transferred outside India; With respect to Revenue’s finding that ownership in the equipment was transferred subsequent to the Defects Liability Period, ITAT states that Defects Liability Clause would be incorporated in every contract to take care of a contingent event and this has got nothing to do with the passing of title to the equipment; On the issue of retention of consideration till the functional demonstration of equipment in India, ITAT observes that this is a normal clause which is incorporated in any contract especially the nature of contract undertaken in the instant case.

Regarding taxability of offshore services

Assessee entered into contract with HCC for rendering offshore services which mainly comprised of ‘Planning, designing and Engineering’ of Hydro Mechanical Plant and Machinery; Assessee submitted that considering the nature, size and specific purpose of the plant and equipment to be supplied, it is necessary to first prepare the drawing, design of the plant and equipment to be manufactured/fabricated and get the same approved by the customer; ITAT notes that offshore services involve supply of drawings and design that are required for the manufacturing of the imported plant & equipment, proper installation of such equipment and synchronisation of the same with civil construction as well as with the locally procured equipment and parts; Revenue argued that these services are purely technical in nature and hence taxable as ‘Fee for Technical Services’; ITAT observes that Assessee supplied offshore drawings and designs together with the supply of plant and equipment; ITAT notes that both of them are inextricably connected because the supply cannot be made without the drawing and similarly, the drawings and designs could not be utilised by HCC to get the manufacturing of plant from another manufacture since drawings are tailor made to suit the requirements of the Plant and equipment supplied by the Assessee; Rejects Revenue’s reliance on Karnataka HC judgment in [AEG Aktiengesellschaft](#) observing that Karnataka HC judgment is contrary to the decision of the Jurisdictional HC in Linde AG which is binding on the bench; Thus, concludes that supply of drawings and designs coupled with supply of equipment, which is manufactured in accordance with the designs supply, is not taxable as FTS; Opines that such consideration qualifies as business profits which cannot be attributed to PE in India.

Case Law Information

Taxpayer Name

- DSD Noell GMBH

Judicial Level & Location

- Income tax Appellate Tribunal Delhi

Appeal Number

- ITA No.3186/Del/2016

Date of Ruling

- 2023-11-21

Ruling in favour of

- Assessee

Section Reference Number

- 9(1)(i)
- 9(1)(vii)

Nature of Issue

- Offshore supplies
- Fees for Technical Services (FTS)

Judges

- Challa Nagendra Prasad, Judicial Member
- M. Balaganesh, Accountant Member

Counsel for Tax Payer

- Mr. Rajan Bhatia
- Shruti Srivastava

Counsel for Department

- Adv. Sanjay Kumar