BEFORE THE AUTHORITY FOR ADVANCE RULINGS (INCOME TAX)
NEW DELHI

17th Day of August, 2016

A.A.R. No 981 of 2010

PRESENT

Justice Mr V.S. Sirpurkar (Chairman)
Mr. A.K. Tewary, Member (Revenue)

Name & address of the applicant	MERO Asia Pacific Pte Ltd., Block 8, #05-05,51, Benoi Road, Singapore 629908
Present for the applicant	Dr. Anita Sumanth, Advocate Mr. R Venkataramani, FCA
Present for the Department	Ms Sukhvinder Khanna,CIT-DR(AAR),ND Mr. S.S Negi, JCIT-DR (AAR), ND Mr. Sachin Dhania, DCIT DR(AAR), ND Mr. J. Albert CIT(IT), Chennai Mr. Pawan Kumar, JCIT(IT), Chennai

RULING
(By A.K Tewary)

The applicant has sought ruling on the following questions:-

(1) On the facts and circumstances of the case, whether the amounts, received/receivable by the applicant from Larsen & Toubro towards offshore supply of goods and materials are liable to tax in India under the provisions of the Indian Income Tax Act read with the Agreement for the Avoidance of Double Taxation between India and Singapore?

(2) If the answer to (1) is in the affirmative, to what extent are the amounts reasonable attributable to the operations carried out in India and accordingly taxable in India by virtue of Explanation (a) to Section 9(1)(i) of the Act and / or Article 7(1) of the India-Singapore tax Treaty?

2.1 MERO Asia Pacific Pte Ltd. (MAPL) is a company registered under the Laws of Singapore and is engaged in the business of executing contracts in relation to structural glazing and wall cladding works. It has set up project Offices in India for the purpose of executing the contract works awarded to the company. Delhi International Airport Private Limited (DIAL) entered into operations, management and Development Agreement (OMDA) on 4/4/2006 with the Airports Authority of India. DIAL floated a global tender for various works in connection with the development of T3 terminal in Delhi Airport. Larsen & Toubro (L&T) won the contract involving design and construction of a state of art passenger terminal. **The main contract was awarded by DIAL (Employer) to L&T (contractor) and L&T, in turn, awarded the contract for entire external and internal façade for the glazing and cladding systems for Piers, fixed link bridges and nodes to the applicant (sub-contractor) for which an agreement was entered into on 23rd April, 2008. The applicant was to design the curtain wall and façade, supply all materials, erect, install, inspect, test and commission the entire sub contact works. The currency of the contract is in Indian Rupees and place of payment is Delhi and pursuant to an option given the payment is also made in Singapore dollar in Singapore. The contract was to be completed by 26/03/2010.**

2.2 Appendix 2A to the agreement is subcontractor's responsibilities and the scope of subcontract works is set out in Appendix 2A to the agreement. The applicant has referred to this appendix and stated that the scope of work can be broadly divided into:

(i) Off-shore supply of goods.

(ii) Installation and other works to be executed in the airport.

2.3 In the application the applicant has not specified the clause of the Appendix on the basis of which the scope of work can be broadly divided in two parts. However, during the course of arguments she mentioned that clause 1.1.4 of Appendix 2A may be treated as comprising of two different scope of work. Clause 1.1.4 reads as under:

> *1.1.4 Supply of all the materials, shipment and/or transportation, prefabrication/fabrication, erection, installation, inspection, testing and commissioning, including all the necessary enabling and allied activities for the entire subcontracts works.*

2.4 According to the applicant's counsel 'supply of all materials, shipment and/or transportation, prefabrication/fabrication' may be treated as separate and considered as part of offshore supply of goods. The applicant has heavily relied upon the judgment of Hon'ble Supreme Court in the case of Ishikawajima Harima Heavy Industries Ltd vs DIT (288 ITR 408) saying that the present contract was an offshore supply contract in respect of supply of goods, the title to the goods passed to L&T Offshore, that the payment for the same was received in Singapore and, therefore, the said judgment is applicable and no income accrues or arises or is deemed to accrue or arise in India. The applicant has further pointed out that the Hon'ble Supreme Court in the case of Ishikawajima harima has noted the following proposition of law that emerges from the decision of various Courts on the issue of offshore supplies:

"In case of sale of goods simpliciter by a non-resident in India, if the consideration for sale is received abroad and the property in the goods also passes to the purchaser outside India, no income accrues or arises or is deemed to accrue or arise to the seller in India."

Other cases relied upon by the applicant are Hysoung Corporation, In re (314 ITR 343), DIT v. Linde AG, Linde Engineering Division (2014) 44 Taxmann.com 244 (Delhi), DIT v. Nokia Networks OY (2012) 25 Taxmann.com 225 (Delhi)and Joint Stock Company Foreign Economic Association Technopromo Expert (322 ITR 409).

2.5 The applicant has further mentioned that with regard to the off-shore supply of goods, it negotiated and concluded the supply of goods and materials from various third party suppliers/manufacturers outside India and, therefore, all the activities in connection with the offshore supply were carried outside India. The suppliers/manufacturers fabricated and manufactured the goods and materials based on the specifications stipulated by the applicant. **The goods were sold by the Applicant from outside India to L & T and the consideration was paid by M/s L & T to the Applicant in Singapore Dollars by way of a transfer of funds to the bank account of the Applicant in Singapore. M/s L & T thereafter sold the consignments to DIAL on a "high sea sale" basis against transfer of bill of lading. L & T issued a high sea sale invoice and entered into an agreement with DIAL where under the ownership in the consignment was transferred to DIAL along with the bill of lading, duly endorsed. On the arrival of the goods in India, the goods were cleared by the applicant on behalf of DIAL using the services of the Project Office of the Applicant as its agent. Custom duties were paid by the applicant.**

2.6 Article 7 of the Double Taxation Avoidance Agreement between India and Singapore deals with “business profits” and sub-clause (1) read as follows:

ARTICLE 7: Business Profits – (1) The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein.

The applicant has submitted that if the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other state but only so much of them as it is directly/ indirectly attributable to that permanent establishment. The Applicant carries on business in India through a Project Office that constitutes its Permanent Establishment in India. However, the Project Office of the Applicant is a separate taxable entity. The Applicant submits that the profits earned by way of off-shore supplies to M/s Larsen & Toubro Limited are not either directly or indirectly attributable to that Permanent Establishment, the permanent establishment (Project Office) in India oversees the installation of structural glazing works and wall cladding works for the Delhi International Airport and has no connection, whatsoever, directly or indirectly in the offshore supplies and the off-shore supplies executed by the Applicant are an independent scope of work.

3. During the course of hearings spread over a long period both the Department of Revenue and the applicant have given several submissions and counter-submissions. These are contained in Department’s letter dated 3/9/13, 2/4/14, 4/9/15 and 9/10/15. The applicant’s responses are contained in submission dated 7/2/14, 6/5/14 and 14/10/15. The comments of the Department and response of the applicant on main relevant points of fact are summarized below.

Department's comments

4. The Department of Revenue has objected to the interpretation of the applicant both on facts and in law and its comments, in brief, are as under:

(a) According to the Department, considering the number of days consumed by MAPL in executing the project works in India through the project office situated in India, a Permanent Establishment for the non-resident company MAPL in India gets established.

(b) The Department has submitted that MAPL had conducted its business operations in India through its Project Office in India and this establishes a business connection within the meaning of Explanation 2 and 3 to clause (i) of subsection 1 of Section 9 of the Income-tax Act, 1961. A Permanent Establishment of the Non- resident Company is established in India, as per Article 5(3) of the India-Singapore DTAA also.

(c) According to the Department there is no separate or exclusive contract of offshore supply of materials. The contract comprises of both supply of goods and rendering of services which includes erection, installation, commission and completion of work.

(d) The Department has submitted that the contractor did not want to split the risk and has kept the risk factor/liability for the entire sub-contract as a whole on the applicant. It means that any issue which involves risk at any part or time of the execution of the work will have the impact on the whole project. This demonstrates that the contract cannot be dissected in any way as it is a composite one and the responsibility on the sub-contractor applicant is wholesome.

(e) The Department has further submitted that payment in both currencies relate to the single composite work and is evidenced by the fact that the payment schedule does not show any such divisions. The payment schedule talks about the cost centre value and the percentage of payment at various stages. The cost centre value as said in the agreement in App 5.6.2.1 reads as follows

5.6.2.1 Cost Centre Value is the total amount of money which will become due to the subcontractor in his final account in accordance with Appendices 4 and 5, determined for the applicable Cost Centre identified in App 5.2

(f) The Department has also submitted that delivery would not be completed till the goods are supplied and commissioned on site.

(g) The Department has drawn attention to the resource material Vision No.42 2009-10 of the applicant which reads as under:

"Delhi will be hosting the Commonwealth Games in October 2010 and the modernization and expansion plans for the airport are slated for completion before the Games. The clients and main contractor for the Airport are GMR and L&T respectively. Having successfully worked with both parties on the New Hyderabad Airport, MAPL was awarded the façade contract for new domestic and international piers, fixed link bridges, nodes and apron glazing. The façade comprises of high grade steel supporting mullions and unitized aluminum curtain wall systems with aluminum cladding panels and louvers**.** The area of the façade is approximately 120,000 sqm which was to be completed within 10 months from award. To meet challenges like very tight time lines stringent specification to cater for seismic loads, planning and logistics for fabrication and installation, the MERO-team designed and engineered a system that would be completely fabricated in factory and

delivered to site as a finished product, ready to be lifted and instilled into its final position. The project is now in the completion stages. Once fully completed, the airport will be the biggest and most modern in India which will definitely impress visitors and athletes participating in the 2010 Commonwealth Games."

(h) The Department has submitted that the statement that goods have been sold on High sea and hence not taxable India is not acceptable for the reasons that the High sea sale was not a sale at all. The goods in question, though claimed as sold offshore, finally arrived at the destination in India, and were used by the applicant itself in the contract works.

(i) The Department has further submitted that there can be no dispute that there is a business connection for the applicant MAPL in India for the relevant transaction. The business connection is the subcontract awarded to MAPL by L&T and executed by it in Terminal 3 of the Delhi International Airport. Income arising directly or indirectly through this business connection is deemed to arise in India. The Department has relied on the language of expression "through" as clarified in Explanation 4 to section 9(1)(i) which is extracted below:

> ***Income deemed to accrue or arise in India.***
>
> *9.(1) The following incomes shall be deemed to accrue or arise in India:-*
>
> *(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situated in India.*
>
> *Explanation 1- For the purposes of this clause-*

(a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India;

……

Explanation 4 – For the removal of doubts, it is hereby clarified that the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

(j) The Department has pointed out that the computation of business profits of the permanent establishment is under Article 7 of the DTAA between India and Singapore. Paragraph 8 of the Article says: "For the purpose of paragraph 1, the term "directly or indirectly attributable to the permanent establishment" includes profits arising from transactions in which the permanent establishment has been involved and such profits shall be regarded as attributable to the permanent establishment to the extent appropriate to the part played by the permanent establishment in those transactions, even if those transactions are made or placed directly with the overseas head office of the enterprise rather than with the permanent establishment.

(k) The Department has relied upon on the judgement by Hon'ble Madras High Court in the case of Ansaldo Energia SPA [310 ITR 237 (Mad)] saying that, "*it is not just where the title passed, but also whether*

there was a crucial and intimate relation, whether there was an element of continuity between the business of the non-resident and the activity within the taxable territories". It has been pointed out that the case of Ishikawajima harima was discussed in detail in the judgment and the court held that the decision in Ishikawajima harima cannot be torn from its context and there are obviously situations where profits from offshore supply cannot be totally excluded from tax. The High Court held that passing of title is not the sole determinant to decide taxability. The Hon'ble High court has held *we do not think that the Tribunal has ignored the decision in Ishikawajima harima Heavy Industries Ltd.'s case (supra). On the other hand, it has applied the ratio in that case, but, has held, for reasons given in its order that the entire profits of Contact No.1 cannot be segregated and dealt with as if they arose outside India. For the reasons given above, we confirm the findings that,*

(a) the foreign company and the activities rendered by it under contract No.1 and the other three contracts are inextricably linked and it was a composite contract,

(b) all responsibility from the beginning to the end rested on the assessee,

(c) there is an intimate, real and continuous relationship with the subsidiary company, and

(d) that the price of other contract was loaded on to Contract No.1.

During the course of arguments, the Department was asked by us to compare the rates of goods involved in offshore supply with other similar parties to see if there is a possibility of loading the so called offshore supply with disproportionately higher value in order to avoid taxation in India. The Department has mentioned that despite issuing letters to

some international parties and making repeated attempts, no response was received from them. They are of the view that since the applicant is seeking the ruling, the onus is on the applicant to substantiate that the price of the contract was not loaded to its offshore supply of materials. Having said this, the Department of Revenue has compared the prices obtained from domestic/Indian companies for supply of same or similar materials by the applicant and has concluded that *prima facie* it appears that there is a possibility of loading of value towards offshore supply of materials. The Department has further stated that after the judgment in 341 ITR 1, the Authority for Advance Rulings in Roxar Maximum Reservoir Performance WLL [349 ITR 189 (AAR)] and Alstom Transport SA [349 ITR 292 (AAR)] has held that Ishikawajima Harima Heavy Industries Ltd [288 ITR 408 (SC)] stood disapproved and overruled, though not expressly, and that composite contracts should not be dissected, and they must be 'looked at' and not 'looked through'. The AAR held that a contract had to be read as a whole and the purpose of the contract is to be ascertained from the terms of the contract.

(l) According to the Department the factual matrix in Ishikawajima harima case is contrasted with the facts of the applicant's case as under:

(i) In Ishikawajima Harima case, there is a consortium of various entities each with distinct responsibilities to execute parts of the turnkey project. Role and responsibility of each member of the consortium was specified separately. In the applicant's case, MAPL is the single subcontractor with the full responsibility of executing the work called "Façade and Associated Works".

(ii) The contract document in Ishikawajima Harima case specified the various components of the project distinctly as offshore supply and onshore supply of materials and services. The price for each

component was also specified separately. In the applicant's contract with L&T there is no such specification. The division of the total value of contract into Indian rupees and Singapore dollars is not spelt out in the contract as attributable to different distinct components of the contract and no basis for the division into two currencies is available in the contract document itself.

(iii) The contract document in Ishikawajima Harima categorically spells out that title to goods supplied offshore pass to the contractee ('owner') on the high seas. There is no such mention in the applicant's case.

(iv) In the Ishikawajima Harima case, the goods supplied from offshore are insured in the name of the contractee as the contractee obtains insurable interest in the goods along with the title. In the applicant's case, the materials imported are insured in the name of the subcontractor applicant and it is required to bear the risk and responsibility for the goods at all times. Although a paper trail is created to appear as if the materials are transferred to the contractee on the high seas, in effect there is no change to the risk and responsibility of the subcontractor applicant.

(v) In Ishikawajima Harima case, it was found that the PE of the foreign company had no role to play in the offshore supply of equipments, materials, etc. In the applicant's case, the procurement of material outside India to suit the specific requirement of the subcontract work in India could not have been done without technical, engineering inputs from the MAPL's personnel at its project office in India, which is its PE. Thus, there was an organic link between the activities in India and outside India.

5. The applicant, in its response, emphasized as under:

a. Two transactions and its consideration have been bifurcated contractually into supplies effected and services rendered. The aspect of supply is dealt with separately in the agreement.

b. Para 5.1.4.5 shows that payment towards shipment of goods is effected upon receipt of shipment. The transaction of supply is complete upon the consignment leaving the factory of manufacture. As regards continuance of risk, the applicant assumes risk towards quality, quantity and standard of materials supplied, the risk assumed towards the aspect of service is assumed by parties rendering the service.

c. As regards comparison of prices of offshore supply of goods, the applicant submits that the revenue has obtained comparable quotes from certain parties in an attempt to prove that the prices were loaded to the supply portion. This exercise of comparing the prices of the applicant with that of a third party itself is fundamentally incorrect since the goods differ in quality and various other parameters. Also the revenue has compared wrong goods in wrong geographical location.

d. As regards reliance of the Revenue on the decision of the Madras High Court in the case of Ansaldo Energia SPA [310 ITR 237 (Mad)], the applicant has mentioned that this decision is distinguishable on facts and is pending before the Hon'ble Supreme Court for final hearing.

Contract

6.1 Before taking up these issues, it is necessary to set out the important portions of the contract/appendices for two reasons: one, the issues can be considered only on the basis of contracts, clauses and respective contentions and, second, quoting one portion of the clause from here and one from there on selective basis is not appropriate way to consider the issues involved. To recall the facts, DIAL floated the global tender and contract for development of Delhi Airport was awarded to L&T, which, in turn, gave sub-contract to the applicant. The sub-contract agreement is titled 'sub-contract –T3 – 04.1 Façade & Associated Works' and comprises of special conditions of contract (SCD), sub-contract data (SD) & Appendices 1 to 12 (App).

6.2 Appendix 2A to the agreement is regarding "sub-contractors responsibilities" which are as under:-

<u>App 2A1 Sub Contract works</u>

1.1.1 The entire external and internal Façade for the glazing and cladding systems for Piers, fixed link bridges and nodes as indicated below to provide a watertight and weather proof enclosure & all the associated works forming part of the Works including without limitation of all double and/or single skinned factory prefabricated exterior cladding and curtain walling, metal baking panels, vision and spandrel panels, shadow box for spandrel panels, modular metal panels, fire/smoke stops, composite metal panels, louvered panels, external entrance doors, windows & other openings, all

hardware & fixtures, miscellaneous metal claddings (like cornices, copings, fascias, casings, etc.), acoustic attenuation, thermal insulation, flashings and all necessary fittings & accessories and the like to complete the system, with all the appropriate provisions for MEP and other services.

1.1.2 Design and engineering of the curtain wall, façade, accommodating subcontract works (the subcontractor shall interpret the drawings & specification supplied as App 1.1 as minimum performance requirement and formulate his own functional, efficient & preeminent design and engineering to meet the functional, aesthetic, structural, utility, interfacing and performance requirements.)

1.1.4 Supply of all the materials, shipment and/or transportation, prefabrication/fabrication, erection, installation, inspection, testing and commissioning, including all the necessary enabling and allied activities for the entire subcontracts works.

1.1.5 Interfacing with other elements without limitation to roof, steel roofing, finishing works, MEP penetrations and ensuring weather tight and waterproof curtain wall and cladding system and the Subcontractor shall be fully responsible for the overall performance of the entire system.

1.1.10 The subcontract works include without limitation to all the supporting structural steel framing work including design, engineering, supply, fabrication, assembly, surface treatment, storage, delivery and erection of all the steelwork required to support the building envelope as part of the subcontract works and also incorporation of all the supply and installation of all cast-in items used to support the steelwork, the grouting of base plates, the provision of cleats and drilling of holes for the attachment of the glazing and cladding system, and repairs to damage surfaces during constrictions, etc.

6.3 Clause 1.2.7 of this Appendix 2A further provides subcontractor's responsibilities as under:-

Selection of materials, components suppliers; procurement, manufacture, assembly, shipping to Site, profiling at Project Site, multiple handling on Site and installation into the Works, commissioning and placing into service, including all protection and cleaning of the subcontract works therefor.

6.4 Clause 2.3 of this Appendix reads as under:-

The Subcontractor is responsible for the general arrangement, detailed design, technical specification, adequacy and contractual and legal compliance of the whole subcontract works, including all of their interfaces, and leading the design and specification aspects of their testing, commissioning, trials and defect remediation, and including

obtaining the endorsement of the Employer's Representative and the consent/approval of all Relevant Authorities thereto.

6.5 Appendix 2B, Clause 2.2.4 provides that '*subcontractor, at his own expenses schedules his deliveries of Materials to Site such that he can store them and work upon them within the working areas assigned to the Subcontractor by the Contractor, without inconveniencing or endangering Interfacing over workers of the Contractor, Other Subcontractors or the Employer.*'

6.6 Appendix 5 is in respect of prices, rates and tax and the relevant provisions are as under:-

5.1.1 *The currency of this subcontract in the Indian rupee (INR) and the place of payment is Delhi, India. Pursuant to option X3, the Contractor also pays the Subcontractor:*

1.1.1 In S$ paid in Singapore

5.1.4 *The Subcontractor pays all other Taxes including all duties and like Government impositions arising from this Subcontract, and indemnifies the Contractor and the Employer against same. For Indian Customs Duty upon Plant and Materials imported into India for the subcontract works:*

5.1.4.1 *prior to Subcontract Key Dates T3-04.1-07, the Subcontractor provides to the Contractor priced lists of the corresponding Plant and Materials to*

be imported into India for the subcontract works, being consistent with Appendix 5s.App5.7

5.1.4.2 within 6 Business Days of any such Plant and/or Materials leaving the port of shipment outside of India, the Subcontract provides to the Contractor all of the following documents for the shipment:

1.4.2.1 Clean (on board) Bill of Lading

1.4.2.2 Commercial Invoice

1.4.2.3 Packing List

1.4.2.4 Certificate of Origin at source (if required)

5.1.4.3 within 6 Business Days of the Subcontractor having complied with s.App5.1.4.2 in relation to a shipment:

1.4.3.1 <u>The Contractor and the Employer execute a "high seas purchase contract" for that shipment pursuant to MCoC 30.1.1,</u> at the price shown on the Subcontractor's Commercial Invoice plus a Loading Fee Margin.

1.4.3.2 The Contractor provides to the Subcontractor such documentation from the Employer as is needed for the Subcontractor to import that shipment into India, and pay the

Indian Customs duty thereon, as the agent of the Employer.

1.4.3.3 Should the Employer have established with all Relevant Authorities its entitlement to any concessional rate of Customs duty regarding any such shipment, but not otherwise, the Contractor provides to the Subcontractor such additional documentation from the Employer as is needed for the Subcontractor to import such shipment at such concessional rate of Customs duty.

5.1.4.5 The Subcontractor pays the Indian Customs duty upon that shipment and clears it through Indian Customs, as the agent of the employer; subject to all additional Employer's documentation regarding any concessional rate of Customs duty as App5.1.4.3.3 complying with all Applicable Law:-

1.4.5.1 the Subcontractor pays only that concessional Rate of Customs duty upon that shipment.

1.4.5.2 the Total Value of the Subcontract is reduced by the amount of Customs duty so saved.

5.1.4.6 subject to s.App5.1.4.3 and to s.App5.1.4.4.3 if applicable, the Subcontractor remains responsible for

the timeliness, cost and risk of the shipmen's delivery to the Project Site and of the subcontract works as a whole.

6.7 App5.2 gives the value of the contract as under:

Cost Centre	***Description***	***Amount, INR***	***Amount, SGS***
T4. 1-Ci	*Pier AB*	*349,365,709*	*167,54,444*
T4.1C2	*Pier CD*	*333,018,384*	*15,686,842*
T4.1-C3	*Fixed Link Bridges and Nodes & Reminder of subcontract works*	*165,377,817*	*89,24,118*
	Sub-Total		*41,365,405*
	Conversion to INR	*1*	*28*
	INR Equivalent	*847,761,910*	*1,158,231,343*
	Total Value, INR	*2,005,993,253*	
	Two thousand and five million, Nine hundred and ninety three Thousand Two hundred and fifty three INR only		

6.8 Appendix 3C to the agreement is Subcontractor's deployment schedule which shows that it deployed one design manager, one design team leader, 3 designers on site full time with effect from May 2008, i.e. much before goods and materials started being delivered to the site.

6.9 Appendix 5.6 is the payment schedule according to which payment in respect of the contract started in June 2008 without any separate reference to offshore supply and onshore services.

6.10 The import of Plant and Materials as per Appendix 5.7 is according to INCOTERMS 2000. The payment schedule shows that the payments are to be made as per overall schedule of key dates and Appendix 5.6.2.1 shows that when the Subcontractor has achieved the stated Subcontract Key Date, it becomes eligible for payment of the corresponding percentage of that Cost Centre's Value stated in s.App5.6.

6.11 Sample invoices & other documents furnished by the applicant show that :

a. Invoice dated 10/10/2009 has been issued by Mero Asia Pacific Pte Ltd to L&T for sale of Aluminum glass panels – for shipment from Shanghai to New Delhi on CIF basis.

b. Bills of Lading show Mero Asia Pacific Pte Ltd as shipper and L&T as consignee.

c. Certificate of Insurance dated 12/10/2009 issued by Axa Insurance Singapore Pte Ltd shows that insured person is Mero Asia Pacific Pte Ltd till the goods reach delivery site in India.

d. High sea sale invoice dated 22/10/2009 shows that L&T has made high sea sale for same Aluminum glass panels to DIAL.

6.12 The applicant made an application with the Income Tax Department u/s 197 (1) of the Act on 2/4/2009 for issue of lower tax deduction certificate on the ground that portion of the contract relating to supply of plant and materials would not generate any tax liability in India.

The order u/s 195 of the Act passed on 16/4/2009 in which it was held that the supply of plant and materials form part of the composite contract and the request for a certificate for NIL deduction of tax was not acceptable.

Inferences & Conclusions

7.1 The contentions of both the applicant and the department have been broadly summarized in earlier paragraphs. The question revolves around the fact as to whether the amount received by the applicant from L&T pursuant to the contract can be bifurcated into offshore supply of goods and materials and services rendered and to consider this question the following issues arise for consideration before us:

I. Whether the contract is divisible into offshore supply of goods and materials and services rendered, whether obligations under the work as per the contract are distinct, i.e. whether off shore supply is an independent scope of work in the contract?

II. Whether all parts of transaction relating to sale of goods to L & T, i.e. transfer of property in goods as well payments, were carried outside India and sale of goods can be treated as completed outside India?

III. Whether price of goods supplied by way of offshore supply and separate payments for that are specified in the contract?

IV. Whether PE has a role in execution of supply, procurement of goods and materials from abroad into India?

V. Whether fact pattern is identical or almost identical to the case of Ishikawajima Harima and the law as enunciated by

the Hon'ble Supreme Court in the said case will squarely apply to the facts of the present case?

7.2 **At the outset we must say that as regards Department's strong reliance on judgment of Hon'ble Madras High Court in the case of Ansaldo (supra), it was pointed out by the applicant's counsel that this decision is pending before Hon'ble Supreme Court and has not become the law of the land so far. The Department was asked by us to establish if the price of offshore supply was loaded in this case also, by comparing the rates of goods involved in offshore supply with that of other similar parties. The Department could not obtain rates from offshore suppliers located abroad although they have compared the prices obtained with that of Indian companies for similar materials and has concluded that *prima facie* loading of value towards offshore supply cannot be ruled out. However, such conclusion is flawed because rates from offshore suppliers located abroad could not be obtained. Since no reply to the letters sent by them to offshore suppliers abroad has been received, their conclusion cannot be relied upon. In these circumstances the reliance of the Department on Ansal do cannot be accepted by us.**

7.3 Therefore, we have to address the issues formulated by us as above on the basis of the facts from the contract agreement and appendices as under:

(a) There is only one contract agreement (T3-04.1 Façade & Associated Works) for the contract to be executed by the applicant for the entire external and internal façade for the glazing and cladding systems for Piers, fixed link bridges

and nodes. The design, engineering, supply, fabrication, assembly, erection and installation are interlinked and everything culminates into one system.

(b) The applicant has to formulate its own design and engineering based on which plants and materials are procured.

(c) The permanent establishment, which is its project office, had come into existence long before the design of materials and equipments for offshore supply started. The project office had already one design manager, one design team leader and three designers working full time for this purpose with effect from May, 2008.The project office is admittedly PE and there is no dispute about the fact that this came into being much before the supply of goods and materials started. The contract document shows that it was being manned by personnel deployed for design of goods and materials to be selected and procured. The goods have been cleared from customs in India by the project office and customs duty has also been paid by the project office. In these circumstances, to say that PE had no role in respect of supply of goods and materials is incorrect.

(d) There is no bifurcation between supply and erection/installation in the contract. In fact, in the entire contract there is no such bifurcation, either in the context of sub-contractor's works and responsibilities or with reference to cost center where cost of Pier AB, Pier CD etc is mentioned or with reference to payments required to be made. The applicant is relying on one portion of clause 1.1.4 of Appendix 2A. Such artificial bifurcation is flawed.

Appendix 2A describes the complete work without any bifurcation.

(e) The applicant is responsible for selection and supply of materials, shipping to site and installation in all works, commissioning and placing into services. Even though invoices show sale of materials to L&T in Singapore, the agreement shows that the applicant at its own expenses delivers the materials to the site in India.

(f) The applicant is to ensure deliveries of materials at site and store them there.

(g) The invoices show sale of materials by the applicant to L&T outside India by raising invoice on L&T and L&T, in turn, has made high sea sale to DIAL. The High Sea Sale contract is between L&T and DIAL and the applicant is not involved in this.

(h) Even though the sale of materials was completed by the applicant outside India it remains responsible for delivery of materials to the site, acts as an agent of DIAL for the purpose of payments of customs duty and makes payment of customs duty and gets the goods cleared from customs. These activities are performed by the applicant in India. If the sale to L&T is complete in Singapore and it is L&T which is making high sea sale to DIAL as claimed by the applicant, then how the applicant is paying customs duty in India and delivering the same to its project site?

(i) SD 8 – Risks & Inference - show that the applicant is bearing risk & insurance in respect of plants and materials until completion and insurance covers entire replacement cost, including the removal of debris and making good of

affected works. If the sale in Singapore is considered to be complete, there is no reason to provide such insurance cover until the completion of entire sub-contract works. Marine cargo insurance is also in the name of applicant and not in the name of L&T or DIAL.

(j) The currency to this contract is Indian rupees and the place of payment is Delhi. It is only as an option given to the applicant to receive certain payments in Singapore dollars as a result of which certain payment has been made in Singapore dollar. Such payment amounting to Singapore $ 41365405 (INR 1158231343/-) is for total cost of Pier AB, Pier CD and fixed link bridges & nodes & remainder of sub-contract works as clearly mentioned in App. 5.2. This is not relatable to offshore supply of plant & materials as being projected by the applicant. Nowhere in the contract is it specified that payment for supply of goods & materials will be in Singapore dollars and in Singapore. The cost centre, which shows cost in Singapore dollars & Indian Rupees, is only for working of the cost and conversion in Indian rupees thereof and it says that total amount (shown in Indian rupees) will become due to the applicant in his final account.

(k) Payments in the contract are not related with sale of goods and materials to L & T outside India. Payments are linked with the different stages of design, drawing, supply and commissioning of the entire networks and have been made at different stages as under:-

2% - on submission of detailed working programme

2% - shop drawing & detailed fabrication

1% - whole of subcontract works

27% - all bought on materials & components documented as being in sub-contractor's premise

3% - Prototype complete

7% - on plants and materials shipped to site

26% - on plant & materials assembled and/or Fabricated units delivered to site with Custom Duties paid.

27% - on plant & materials assembled and/or Fabricated units installed at site.

3% - Test being successful.

2% - On obtaining completion certificate.

(l) The major milestone schedule in Appendix 3A1 does not mention about supply/sale of plant and materials and recognizes architectural works, testing of IT and other systems, complete BHS installation & initial testing and commissioning, furnishing of O&M manuals, complete integration, testing & commissioning and obtaining terminal operation trials certificate only as major milestones. This further shows the nature of contract being one and indivisible as no separate supply/sale of plant and materials is recognized as a milestone.

7.4 As against the factual position mentioned above, the assertions of the applicant are tested as under:-

a) The applicant asserts that two transactions and its considerations have been bifurcated contractually into supplies effected and services rendered. Nowhere in the agreement is such contractual

bifurcation available. There is no mention of two transactions. According to the applicant Clause 1.1.4 of appendix 2A is the scope of work and is divisible into two portions. The fact is that appendix 2A.1, in full, describes sub- contract works and clause 1.1.1 is the main sub-contract works descriptions. It is incorrect to pick up one portion of a clause (1.1.4) selectively to show that it represents independent scope of work. This clause is not divisible in two parts. The applicant is relying on one portion of one sentence of the clause. Such division is imaginary and artificial.

b) The applicant further states that para 5.1.4.5 shows that payment towards shipment of goods is effected upon the receipt of the shipment. This para does not even mention this as it talks about payment of customs duty by the applicant and clearing of goods through customs in India. In fact as mentioned elaborately above, the payment schedule depends upon stages of completion of the project and not at all on shipment of goods or completion of services.

c) According to the applicant's assertion, the parties agree that the cost relating to the aspect of supply would be incurred in foreign currency. Nowhere such agreement between parties is found. The cost center value shown in Appendix 5.2 is for working out the cost. There is indeed an option that has been given to receive payments in foreign currency even though the currency of the entire contract is Indian rupees and the place of payment is in India. However, the option to receive payment in foreign currency is not linked with shipment of goods but it is with reference to entire contract value, i.e. option has been given to receive part payment in foreign currency without reference to offshore supply.

d) The applicant further asserts that the transaction of supply is completed upon the consignment leaving the factory. The applicant has stated that the sale to L&T was done outside India. This leads to a major question whether on the basis of facts the sale to L & T could be considered to be completed outside India. Under the Sale of Goods Act, Section 19 of the Sale of Goods Act makes it clear that property in goods passes when the parties intend it to pass. Section 19 is reproduced as under:

(1) Where there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.

(2) For the purpose of ascertaining the intention of the parties regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case.

(3) Unless a different intention appears, the rules contained in sections 20 to 24 are rules for ascertaining the intention of the parties as to the time at which the property in goods is to pass to the buyer.

Clause (2) of this section states that for the purpose of ascertaining the intention of the parties, regard shall be had to the terms of the contract, the conduct of the parties and the circumstances of the case. In any sale transaction, risk passes with property. Thus, the goods agreed to be sold remain at the seller's risk until the property in goods passed to the buyer. When property or risk is to pass is, therefore, a question that depends on the intention of the contracting parties. If a contract provides for a specific method, place or time of passing of

property or risk or both, it has to be concluded accordingly. In the present case the intention of the applicant is that the property in goods will pass only when the installation and erection of entire works will be completed. If this is not so, then there would be no question of retaining effective control over the goods till it reaches the contract site, paying customs duty for that, bearing the risk and covering insurance till completion of sub-contract works. DIAL and L & T never intended to buy materials on standalone basis. The undertaking of all these responsibilities, even after making sale to L&T outside India, shows the intention. In this case there is continuity from preparation of invoice in the name of L&T of the goods supplied till the same reached the contract site. The buying of insurance in the name of the applicant instead of L& T till it reaches the site in India is a clear proof that risk does not pass to L&T/DIAL till the goods are not used for the works as per the contract.

7.5 The applicant has relied on the judgments in the case of Ishikawajma harima (supra), Linde AG (supra), Nokia Networks (supra) as regards the facts relating to the contract, responsibilities of suppliers, and role of PE. The facts involved, in brief, in these cases are as under:-

A. In the case of Ishikawajma harima the supply segment and service segment were specified in different parts of the contract. The equipment supplied stood transferred upon delivery thereof outside India on high sea basis. All parts of the transaction in question, i.e. the transfer of property in goods as well as the payments, were carried outside India. The permanent establishment was not involved in the transactions. As regards offshore supply it was held that since all parts of the transaction in question, i.e., the transfer of property in goods as well as the

payment, was carried outside the Indian soil, the transaction could not have been taxed in India. In this case the Hon'ble Court had reproduced all relevant clauses of the contract to show that clause 14.8 showed separate payment in US dollars and Indian rupees depending on the nature of supply viz. offshore supply and offshore services and onshore supply and onshore services. Exhibit D-2.1 mentioned that offshore supply was the price of Equipment & Material (including cost of engineering, if any, involved in the manufacturing of such Equipment & Material) supplied from outside India on CFR basis. Exhibit D-2.2 was for offshore services, Exhibit D-2.3 was for onshore supply and Exhibit D-2.4 was for onshore services. Article 13.3.2 specifically referred to the cost and offshore supplies. The insurance was in owner's name. Then the Court concluded "*obligations under the contract are distinct one. Supply obligation is distinct and separate from service obligation. Price for each of the component of the contract is separate. Similarly, offshore supply and offshore services have separately been dealt with. Prices in each of the segment are also different. The very fact that in the contract, the supply segment and the service segment have been specified in different parts of the contract is a pointer to show that the liability of the appellant there under would also be different*." The Court had identified two basic issues for consideration: (a) the taxation of price of goods supplied, by way of offshore supply price of which is specified in Ex. D, clause 2.1; and (b) the taxation of consideration paid for rendition of services in the contract as offshore services at Ex. D. There was clear and distinct bifurcation in the contract between offshore and onshore works based on which issues were decided. The Hon'ble Court had also noticed that in CIT vs. Mitsui

Engineering and Shipping Building Company (2003) 259 ITR 2458 Delhi it was held that it was not possible to apportion the consideration design on one part and the other activities on the other part as the prices paid to the assessee was not the total price which covered all the stages involved in the supply of machinery. The Hon'ble Court noted that the case of Ishikawajima harima was clearly distinguishable from the facts of Mitsui since the payments for offshore and on shore supply of goods and services was in itself clearly demarcated and cannot be held to be a complete contract that had to be read as a whole and not in parts.

B. In the case of LG Cables there were two separate contracts, one for offshore supply and other for onshore services. The property in the goods would pass on to the buyer as and when the seller loads the equipment on to the mode of transport for transportation from the country of origin. The PE had no role to play in the execution of offshore supply contract and as a matter of fact was set up for sole purpose of enabling the purpose of the onshore services contract, which was a separate one.

C. In the case of Nokia GSM equipment manufactured in Finland was sold to Indian Telecom Operators from outside India on a principle to principle basis, under independent buyers and sellers arrangement. Installation activities were undertaken by Indian subsidiary under its independent contracts with Indian Telecom Operators.

D. In the case of Linde AG, Linde and Samsung were responsible for performing separate items of work. The scope of work to be

performed under the contracts by both the parties was clearly demarcated and separately identified. The considerations payable to Linde and Samsung for the respective items of work to be performed by them were separately specified and the amounts payable by Opal under the contract were also paid directly to each member of the consortium. The permanent establishment of Linde did not come into existence till the commencement of installation stage which was subsequent to Linde providing a basic and detailed engineering and drawings and offshore supply of equipment and material.

7.6 The common facts in all above mentioned decisions as compared to the facts in the present case are:

(a) In these cases there were separate contracts for offshore supply and onshore services or such distinction was specific with supply obligation being distinct from service obligation. There is no such distinction in the present case.

(b) In these cases price for each component was separately specified. However, cost value centre in the present case mentions the price of entire contract.

(c) In all these cases all parts of transactions were completed outside India but in the present case the sale was not completed outside India.

(d) In Ishikawajima Harima the insurance for goods supplied was in owner's name whereas in this case the insurance was in applicant's name, covering the risk till completion.

(e) In all these cases PE had no role to play in offshore supply whereas in this case PE played significant role in design, selection and procurements of materials to be used in the

façade related work in India, clearance of goods through customs in India and payment of customs duty in India.

7.7 The present contract is clearly a composite one for providing services. Appendix V describes the nature of work in detail and a simple reading of work and responsibilities of the applicant shows that contract is one. In this context, the following observations of Hon'ble Supreme Court in the case of BSNL Vs Union of India & Oths (2006) 3 SCC are relevant.

The reason why these services do not involve a sale for the purposes of Entry 54 of List - II is, as we see it, for reasons ultimately attributable to the principles enunciated in Gannon Dunkerley case, namely, if there is an instrument of contract which may be composite in form in any case other than the exceptions in Article 366(29-A), unless the transaction in truth represents two distinct and separate contracts and is discernible as such, then the State would not have the power to separate the agreement to sell from the agreement to render service, and impose tax on the sale. The test therefore for composite contracts other than those mentioned in Article 366 (29-A) continues to be: Did the parties have in mind or intend separate rights arising out of the sale of goods? If there was no such intention there is no sale even if the contract could be disintegrated. The test for deciding whether a contract falls into one category or the other is to as what is "the substance of the contract". We will, for the want of a better phrase, call this the dominant nature test.

(Emphasis supplied)

7.8 The substance of the present contract very clearly shows that it is composite in form as there is no division in the contract on the basis of supply and services, payment is not separately linked with services and supply but is to be made on the basis of stages of

completion of the contract irrespective of goods and materials brought in the premise.

7.9 This Authority in the case of Roxar Maximum (supra), wherein also the applicant had relied upon the judgment in Ishikawajima Harima, also held as under-

"A contract has to be read as a whole. The purpose for which the contract is entered into by the parties is to be ascertained from the terms of the contract. In the case on hand, ONGC clearly called for a contract for "services for supply, installation and commissioning of 36 manometer gauges". The purpose of the contract is the installation of the gauges at site to enable ONGC to carry out its operations. I have quoted earlier the relevant portion of the contract. On a reading of the same, there cannot be any doubt that that the contract in question was for erection and commissioning of 36 manometer gauges for the use of ONGC. The contract is clearly not one for sale of equipment. Nor is it one for mere erection of the equipment. It is a composite contract for supply and erection at sites within the territory of India. What is paid for by ONGC is for the supply and erection done in India. The payment is received by the applicant for the performance of the contract as a whole in India. It is, therefore, clear that the income to the applicant accrued in India."

7.10 The discussion as above clarifies the issues formulated by us as under:

I. The contract is a composite one and offshore supplies are not an independent scope of work.

II. All parts of the transaction relating to sale of goods to L & T were not completed outside India.

III. No separate price of goods supplied by way of offshore supply or sale of goods to L & T outside India is specified in the contract.

IV. PE played a role in design, selection and procurement of materials to be used in the façade related work.

V. The fact pattern of this case is not at all similar to that of Ishikawajima Harima and the law as enunciated by the Hon'ble Supreme Court does not apply to the facts of the present case.

8. In view of above, we hold that the contract in this case is a composite one and the entire amount received by the applicant from L&T is taxable in India.

The Ruling is accordingly given and pronounced on this 17th day of August, 2016.

(VS Sirpurkar)
Chairman

(A.K. Tewary)
Member