

*

IN THE HIGH COURT OF DELHI AT NEW DELHI

2

+

ITA No.706 of 2011
ITA No.704 of 2011
ITA No.707 of 2011

%

Reserved on: 13th September, 2011.
Pronounced on: 30th September, 2011

(1) ITA No.706/2011

DIRECTOR OF INCOME TAX . . . APPELLANT

Through: Mr. Abhishek Maratha, Sr.
Standing Counsel.

VERSUS

L.S. CABLES LTD. . . .RESPONDENT

Through: Mr. R. Satish Kumar,
Advocate.

(2) ITA No.704/2011

DIRECTOR OF INCOME TAX . . . APPELLANT

Through: Mr. Abhishek Maratha, Sr.
Standing Counsel.

VERSUS

L.S. CABLES LTD. . . .RESPONDENT

Through: Mr. R. Satish Kumar,
Advocate.

(3) ITA No.707/2011

DIRECTOR OF INCOME TAX . . . APPELLANT

Through: Mr. Abhishek Maratha, Sr.
Standing Counsel.

VERSUS

ITA No.706, 704, 707/2011

Page 1 of 14

Signature Not Verified

Digitally Signed By: AMULYA
Certify that the digital file and
physical file have been compared and
the digital data is as per the physical
file and no page is missing.

Through: Mr. R. Satish Kumar,
Advocate.

CORAM :-**HON'BLE MR. JUSTICE A.K. SIKRI****HON'BLE MR. JUSTICE SIDDHARTH MRIDUL**

1. Whether Reporters of Local newspapers may be allowed to see the Judgment?
2. To be referred to the Reporter or not?
3. Whether the Judgment should be reported in the Digest?

A.K. SIKRI, J.

1. The assessee is a company incorporated in Korea and as per the notes attached to the statement of the total income, during the year under consideration, the company was engaged in the execution of the following four projects:
 - (i) Fibre Optic Cabling Project – Eastern India for Power Grid Corporation of India Limited (hereinafter referred to as the PGCIL).
 - (ii) Fibre Optic Cabling Project – PDA – 2A for PGCIL.
 - (iii) Fibre Optic Cabling Project – Western India for PGCIL.
 - (iv) Fibre Optic Cabling Project – PDT – 1B for PGCIL.
2. The Assessing Officer (AO) after going through all the four contracts and even interacting in details with the assessee company and PGCIL and perusing the documents on record

(4)

found out that the assessee had performed various activities in India during the relevant assessment year and thereby attributed 50% of the income relatable to the operations carried out in India, both as per the provisions of Section 9 of the Income Tax Act (hereinafter referred to as 'the Act') and Article 7 of Double Taxation Avoidance Agreement ('DTAA' for brevity) between India and Korea. The AO while considering the offshore supply, attributed income for the taxation in India vide letter dated 05.07.2006, the details of payments received on originating the territory of India in respect of the offshore supplies during the period 01.04.2003 to 31.03.2004 are of US\$ 25,705,837/-. The TT buying rate as on 31.03.2004 was ₹1,127,458,025/-. The profit taxable in India on this amount @ 10% is computed at ₹11,27,45,802/-. The AO, therefore, vide Assessment Order dated 26.12.2006 assessed the income of the assessee at ₹7,85,16,943/-.

3. Being aggrieved by the assessment order passed by the AO, the assessee filed three separate appeals, i.e. Appeal No.179/06-07, 380/06-07 & 127/07-08 for the Assessment Years 2003-04, 2004-05 & 2005-06 respectively before the CIT (A). The CIT (A) vide the consolidated order dated 06.07.2009 dismissed the appeal of the assessee.

- (5)
4. Not satisfied with the order of the CIT (A), the assessee preferred three separate appeals, i.e., ITA Nos.3634/Del/2009, 3635/Del/2009 & 3636/Del/2009 before the Income Tax Appellate Tribunal (hereinafter referred to as 'the Tribunal'). Learned Tribunal, however, vide common orders dated 13.08.2010 partly allowed the appeals of the assessee.
5. In these appeals preferred by the Revenue against the aforesaid orders of the Tribunal, we are concerned with the taxability of offshore supply of the equipments. From the brief narrations of the events stated above, it is clear that the assessee, a company (earlier known as LG Cables Ltd.) incorporated in Republic of Korea, is engaged in the business of manufacture and sale of power transmission cable and related equipments. It had entered into a series of contracts with Power Grid Corporation (A Government of India Undertaking) (for short 'PGCI') with the approval of Reserve Bank of India since 2001 for off-shore supply and on-shore erection testing, commissioning, etc. of Fiber Optic Cabling System for power transmission in different geographical regions of India. Four contracts, particulars whereof are already given above, were entered into between the assessee and the PGCI. Insofar as on-shore erection testing, commissioning, etc. are concerned, the assessee has been filing income tax returns and paying

(9)

taxes. As per as off-shore supply is concerned, the admitted facts are that the cables are manufactured in Korea and shipped from a port in the said country.

6. We may mention at this stage that for each project two contracts were entered into, viz., a contract for off-shore supply of equipments and separate supply for on-shore supply, viz., custom clearance of imported equipments at Indian port, inland transportation insurance, erection and testing, commissioning and related activities. We may also point out here itself that for on-shore activities, the assessee had appointed Indian agent, viz., M/s. Alpasso Industries Pvt. Ltd. This Indian agent was concerned only with execution of contract in India.
7. The AO as well as CIT (A), however, took the view that the issue relating to off-shore contract and on-shore contract between the assessee and PGCI had been carried out by the agent in India, income on sale of equipment has accrued in India and on that basis, Section 9 of the Act was attracted in this case.
8. In respect of off-shore supplies also, it was held that the assessee had a business connection in India and M/s. Alpasso Industries Pvt. Ltd. was a permanent establishment.

(2)

It is on this ground that income from off-shore contracts had accrued in India and was held liable for tax. It is a matter of record that the Assessment Year 2002-03, identical issue had cropped up and the Tribunal had taken the view that off-shore/overseas contract was totally incumbent on on-shore service contract and in respect of off-shore contract, no work was entrusted by the assessee to its Indian agent, M/s. Alpasso Industries Pvt. Ltd. On this basis, it was held that Section 9 of the Act had no application and in respect of those off-shore supplies, the Indian agent did not constitute a business connection and the following two conditions which are necessary for invocation of Section 9 of the Act are not satisfied:

- (i) Business connection in India; or
- (ii) Attributing income earned by the assessee from the said supplies, were not satisfied.

9. Following the decision rendered in respect of Assessment Year 2002-03, the Tribunal has allowed the appeals partly.
10. It would be relevant to point out that against the order of the Tribunal pertaining to Assessment Year 2002-03, the Revenue had preferred appeal under Section 260A of the Act, which was

(2)

registered as ITA No.703 of 2009. It was admitted on the following substantial question of :

"(1) Whether the Income Tax Appellate Tribunal is justified in not holding that the contract in question is not a composite one and, therefore, the assessee is not liable to pay tax in India in respect of offshore service?

(2) Whether the levy of interest under Section 234B for short deduction of TDS is mandatory and is leviable automatically?"

11. The aforesaid appeal was finally heard and decided on 24.12.2010, deciding the question of law (1) in favour of the assessee and against the Revenue and question of law (2) was rendered as infructuous. In the aforesaid judgment delivered by this Court, the terms and conditions of the two contracts for each project, viz., one for the off-shore supplies and other relating to on-shore service were minutely gone into and threadbare discussed. Reliance was placed on the question of law laid down by the Authority for Advance Ruling in the matter of **Inshikawajma-Harima Heavy Industries Co. Ltd.** [271 ITR 193]. Principle of law laid down by the AAR was applied on those facts. Relevant portions of the said judgment are extracted below:

"25. Since it was not in dispute that the title in the equipments supplied was to stand transferred upon delivery thereof outside India on high-seas basis as provided for in Article 22(1), the Authority for Advance Rulings proceeded on the basis that supplies had taken place offshore. It, however, rendered its opinion on the premise that offshore supplies or offshore services

(9)

were intimately connected with the turnkey project and proceeding on that basis the Authority, as already stated, opined that the assessee company was liable to pay tax in India though the property in the goods which were subject matter of the offshore supply passed outside India, in view of the fact that it had a business connection in India. It further opined that if a contract envisaged a composite compensation for the various obligations to be performed and if certain operations are to be performed by or through a business connection then, profits would be deemed to have accrued in India. The petitioner had a permanent establishment in India within the meaning of the said term in paragraph 3 in Article 5 of the Double Taxation Avoidance Agreement entered into between the Governments of India and Japan.

26. Reversing the aforesaid finding of the Authority for Advance Rulings, the Supreme Court in respect of the offshore supply and equipments held as under: -

"Re: Offshore Supply:

(1) That only such part of the income, as is attributable to the operations carried out in India can be taxed in India.

(2) Since all parts of the transaction in question, i.e. the transfer of property in goods as well as the payment, were carried on outside the Indian soil, the transaction could not have been taxed in India.

(3) The principle of apportionment, wherein the territorial jurisdiction of a particular state determines its capacity to tax an event, has to be followed.

(4) The fact that the contract was signed in India is of no material consequence, since all activities in connection with the offshore supply were outside India, and therefore cannot be deemed to accrue or arise in the country.

(5) There exists a distinction between a business connection and a permanent establishment. As the permanent establishment cannot be said to be involved in the transaction, the aforementioned provision will have no application. The permanent establishment

cannot be equated to a business connection, since the former is for the purpose of assessment of income of a non-resident under a Double Taxation Avoidance Agreement, and the latter is for the application of Section 9 of the Income Tax Act.

(6) Clause (a) of Explanation 1 to S. 9(1)(i) states that only such part of the income as is attributable to the operations carried out in India, are taxable in India.

(7) The existence of a permanent establishment would not constitute sufficient „business connection“ and the permanent establishment would be the taxable entity. The fiscal jurisdiction of a country would not extend to the taxing entire income attributable to the permanent establishment.

(8) There exists a difference between the existence of a business connection and the income accruing or arising out of such business connection.

(9) Paragraph 6 of the Protocol to the DTAA is not applicable, because, for the profits to be „attributable directly or indirectly“ the permanent establishment must be involved in the activity giving rise to the profits.”

27. Applying the aforesaid law enunciated by the Supreme Court in the case of **Ishikawajma (supra)**, there can be no manner of doubt that the offshore supplies in the instant case are not chargeable to tax in India. The instant case, in fact, in our view stands on a better footing as two separate contracts have been entered into between the parties, albeit on the same day, one for the offshore supply and the other for the onshore services, but even assuming that both these contracts need to be read together as a composite contract, the issue in controversy is nevertheless squarely covered by the decision of the Supreme Court in **Ishikawajma (supra)**. It is beyond dispute that PGCIL had issued irrevocable letter of credit in favour of the respondent-assessee and in paragraph 31.2 agreed that the property in the goods will pass to the buyer (PGCIL) as and when the respondent-assessee loads the equipment onto the mode of transport for transportation from the country of origin. The stipulation in the second agreement (Erection Contract)

(11)

relating to certain performances by the respondent-assessee including port handling, custom clearance, transportation, insurance, handling on site, unloading at transportation site, testing and commissioning to the satisfaction of the buyer are in a separate agreement for a separate consideration which is clearly enunciated in the second agreement as follows: - "Whereas the employer desires to engage the contractor for performance of all activities within India..... subject to the terms and conditions hereinafter appearing."

12. Mr. Abhishek Maratha, learned counsel appearing for the Revenue, could not dispute that the identical issue was decided by the Tribunal earlier, which view was upheld by this Court in the case of **Director of Income Tax, New Delhi Vs. LG Cable Ltd.** (in ITA No.703/2009 decided on 24.12.2010). Faced with this, his only submission was that even in respect of off-shore supply in the instant case, the AO had found that the contract between the assessee and PGCIL even for off-shore supply provided that the assessee had appointed an Indian agent, viz., M/s. Alpasso Industries Pvt. Ltd. who was working for the assessee in India. Therefore, this contract demonstrated that the assessee was to be represented by the Indian agent in India, from which it should be discerned that the operation in respect of off-shore had been carried out through India by an agent. This contention of the learned counsel does not cut much ice. Construing this very

(12)

agreement, it has also been held that two contract, one for off-shore supply and other for on-shore service are independent of each other. Again, a finding of fact was arrived at viz M/s. Alpasso Industries Pvt. Ltd. was concerned only with on-shore contract and had no any other role to play in respect of off-shore/overseas supplies. In the agreement relating to off-shore supply between the assessee and the PGCI, no doubt, PGCI had agreed to pay 1.01%% of the CIF price of the goods as the Indian agent's commission to M/s. Alpasso Industries Ltd. as a part of contract process for overseas supply. In fact, M/s. Alpasso Industries Ltd. was engaged by other foreign companies also as their Indian agents while entering into similar contacts for overseas supply with PGCI. M/s. Alpasso had filed an affidavit that it was an independent entity working for several clients. As per the off-shore contract for overseas supply, the goods were manufactured by the assessee overseas in its establishment and dispatched from abroad. The property in the goods passed into purchaser on delivery at the foreign port. The on-shore erection contract was in respect of the service of customs clearance, inland transportation and erection of commissioning of transmission cables. The

(13)

above work was attended to by the project office, which constituted permanent establishment of the assessee company in India. In view of the above, the only work which could be entrusted by the assessee to its Indian agent, M/s. Alpasso was general administrative coordination and liaison with PGCI and nothing else.

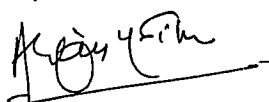
13. Therefore, we are of the view that all the aspects are duly considered by the Tribunal in the light of provision of Section 9 (1) of the Act. The Tribunal had pointed out that clause (i) of sub-section (1) of Section 9 is very wide whereas Explanation 1(a) is restrictive and provides that in case of a business where all operations are not carried out in India shall be only such part of income as is reasonably attributable to operations carried out in India would accrue in India. The ITAT had categorically held that the delivery of goods, documents and receipt of substantial part of sale consideration did take place outside India and hence income relating to sale outside India had not accrued in India. Such income could only be taxed outside India and not under Indian law. Further, there cannot be a business connection between a seller and purchaser (Hindustan Shipyard Ltd. – 109 ITR 158). The income from onshore

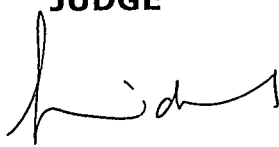
services was taxable in India, simply because such income accrued in India from services rendered in India. One need not look for business connection to tax such income. The assessee company had shipped the goods from abroad with the bill of lading in the name of Power Grid Corporation against an irrecoverable letter of credit. The assessee had assumed, under the onshore contract, the responsibility of customs clearance on behalf of Power Grid Corporation as an agent only and it would be wrong to assume that the ownership of the goods did not. The Tribunal has rightly held that the property in the equipment had passed to the buyer as stipulated in para 31.2 of General Conditions of the Contract. Stipulation in the on-shore contract relating to certain performances by the assessee including port handling, customs clearance, transportation, insurance, handling on site, unloading at transportation site, testing and commission to the satisfaction of the buyer are under a separate agreement for a separate consideration.

14. Thus, the aforesaid arguments of the learned counsel for the Revenue is not acceptable and there is no reason to change the decision arrived at in the case of **LG Cable Ltd. (supra)** in ITA No.703 of 2009.

15

15. No question of law arises. These appeals are, accordingly,
dismissed.


(A.K. SIKRI)
JUDGE


(SIDDHARTH MRIDUL)
JUDGE

SEPTEMBER 30, 2011
pmc