* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 17.03.2015
Pronounced on: 29.05.2015

\+ **ITA 325/2014**

COMMISSIONER OF INCOME TAX-IV ……Appellant
Through: Sh. Rohit Madan, Sr. Standing Counsel with Sh. Ruchir Bhatia and Sh. Akash Vajpai, Advocates.

Versus

M/S. GRUP ISM P. LTD. ……..Respondent
Through: Sh. Kaanan Kapur and Sh. Bhushan Kapur, Advocates.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE R.K. GAUBA

MR. JUSTICE S. RAVINDRA BHAT

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1. The following questions of law were framed by this Court at the time of admission of this appeal under Section 260A of the Income Tax Act, 1961 ("the Act"):

(1) Did the ITAT fall into error in holding that the payment incurred by the assessee to the extent of ₹ 94,31,826 to the UAE concerns was not technical service in terms of Second Explanation to Section 9 (1) (vii) read with Section 194J?

(2) Did the ITAT fall into error in holding that Article 14 of the Double Taxation Avoidance Treaty applied to the UAE concerns in the circumstances of the case?

2. During the course of assessment proceedings, for AY 2004-05, the Assessing Officer (AO) noticed that the assessee Company made payment of ₹ 56,54,963/- to M/s. CGS International, UAE ("CGS International") and ₹ 37,76,863/- to M/s. Marble Arts & Crafts LLC, UAE ("Marble Arts & Crafts") (aggregating to ₹ 94,31,826/-). The AO noted that no TDS had been deducted by the assessee while making the payment to the said two foreign concerns. Accordingly, AO required the assesse to show cause why the said expenditure should not be disallowed under Section 40(a)(i) of the Act. The assessee contended that the payments were made towards commission and that neither of these concerns had any business in India nor had they filed any Income Tax Return in India. The copies of accounts of these two concerns filed by the assessee revealed that the payment was made on account of consultancy charges and it had debited the said sum under the head "consultancy charges". Independent confirmation of CGS International also stated that it had received the payment towards consultancy services. The assessee further referred to Article 14 of Double Taxation Avoidance Agreement (DTAA) and contended that in view of such stipulation it was not required to deduct TDS. The AO rejected the assessee's contentions; he was also influenced by the fact that the assessee did not produce copies of the agreements with the two foreign concerns. Thus, the AO disallowed the amounts.

3. Before the CIT (A), the assessee contended that what was paid to the two foreign concerns was not consultancy fee. As regards Marble Arts & Crafts, the services included guiding the assessee about the procedural aspect of obtaining payment, checking the format and documentation of

invoice and other papers to be submitted for approval to the Works Department, Abu Dhabi; checking invoices submission of invoices to respective authorities and obtaining their approval, follow up with Works Department, Finance Department, Banks and other authorities for approval of invoices, and obtain staff approval and letters of credits. Marble Arts & Crafts was to be paid a fee of 5% of gross amount paid by Works Department to the appellant. In addition, the assessee agreed to pay one time fee of US$ 50000 to Marble Arts & Crafts for identification and selection of UAE national as a partner for the appellant in connection with supply of marble to the Works Department in UAE. As regards CGS International, the services included soliciting business for the assessee in various parts of the world except India, identifying, introducing and providing details of industries, companies, individuals and investors etc. CGS International was to be paid in terms of the agreement a fee equivalent to 15% of the gross value of the contract. Clause 7 of the agreement dated 05.04.03 with Marble Arts & Crafts provided for payment of US$ 50000 as fees towards identification and selection of UAE national as a partner for the appellant and subsequent assistance in framing legal documentation. The copies of agreements which formed the basis for payment to Marble Arts & Crafts and CGS International were furnished.

4. The CIT (A) took into consideration the facts and noticed that the assessee was awarded project management consultancy by the Works Department of the Emirate of Abu Dhabi. It was to act as a consultant for project management of marble works for Shaekh Zayed Bin Sultan Al Nahyan mosque at Abu Dhabi. The contract required it to assist in quality

control measures for procurement of while marble from Makrana Rajasthan, to certify the quality, quantity and measurement by making selected block before transportation to Abu Dhabi, and undertake supervision of the cutting of the blocks at the site of Shaekh Zayad mosque. The assessee would supervise and evaluate the proposals of marble suppliers and shortlist and identify potential mines, and also supervise block quarrying and selection of blocks. Moreover it was required to supervise the loading of the blocks into containers, sealing of the containers and transporting the containers to the project site at Abu Dhabi. As regards the Abu Dhabi component of the agreement with the Works Department, the assessee was to act as consultant for procurement of marble, its processing, cutting etc. The CIT held that *"In short, the contract was for organizing procurement of Makrana marble from India and supervising its processing at Abu Dhabi. The first part of the contract was procurement of marble from India and the second was processing the marbles i.e. conversion thereof to the desired specification at Abu Dhabi."* It was further held that consultancy charges in terms of the assessee's accounts were paid in all to 54 parties for services such as landscape design, architectural design, conservation services, engineering services, soil engineering work, quality server, electrical plumbing and HVAC services, EDP services, acoustic services, research services, liaison services, stone services. All the payments barring two were made to concerns in India. However, in respect of CGS International, payments were made for 'agent in UAE work", and Marble Art & Crafts were paid for "liaison services in Abu Dhabi". Before the CIT (A), when the assessee produced copies of the agreements with the UAE companies, the AO objected. However, the CIT (A) was of the opinion that such documents had

to be examined, because they would be decisive in verifying whether the payments shown in the ledger of the assessee and other books were in accordance with the arrangement with the foreign concerns. It was further held that in respect of CGS International, @ 15% as per agreement, the assessee accounted for a total payment of ₹ 45,31,044/-. In respect of Marble Arts & Crafts, remuneration for the liaison services at 5% of the invoices realized, the appellant incurred an expense of ₹ 15,12,613/- and a further amount of ₹ 22,64,240/- by way of charges for identifying a UAE national as its partner. The agreement dated 5.4.2003 between the assessee and Marble Arts & Crafts contemplated 5% of the gross payments received from the Works Department in terms of an agreement dated 12-1-2003. The linkage between the payment and the amounts received from the foreign client therefore was established. The records also showed that an amount in excess of ₹3 crores were received from such contract with the Works Department. Marble Arts & Crafts was entitled to receive its consideration for assistance in documentation, guidance and liaison with various departments towards assisting the assessee in its work in the UAE. The contract with CGS International on the other hand, dated 25.11.2002, contemplated assistance by the latter, to the assessee to procure clients and market its services; for this, it was to receive 15% of the amounts received from the clients so introduced. The assessee paid ₹ 45,31 ,044/- on this score. In the background of these facts, the CIT(A) held that the payment made by the assessee to the two UAE entities would not come within the purview of 'technical services', as defined in Explanation 2 to Section 9(1)(vii) of the Act and consequently, the provisions of Section 9(1)(vii) were not attracted in the assessee's case. Further, the CIT(A) held that

Article 14 of the DTAA with UAE, dated 18.11.1993, is applicable in the facts of the case and that the AO could not have denied the applicability of the said on the sole premise that the two UAE entities are companies. Accordingly, since the remittances to such non-resident entities are liable to be taxed in the UAE, no TDS was required to be deducted.

5. The Income Tax Appellate Tribunal (hereafter referred to as "ITAT") dismissed the revenue's appeal and affirmed the CIT(A)'s order. Hence, the revenue has preferred the instant appeal.

Submissions of Parties

6. Mr. Rohit Madan, learned counsel for the revenue submits that the CIT(A) and the ITAT erred in their analysis of the payments made to the two UAE entities, and that the services provided by these entities clearly and unequivocally qualify as 'technical services' as defined in Explanation 2 to Section 9(1)(vii) of the Act. Learned counsel states that the agreements dated 25.11.2002 and 05.04.2003, entered into with CGS International and Marble Arts & Crafts respectively, cannot establish that services were in fact rendered by the two foreign concerns to the assessee whereas the CIT(A) and the ITAT have placed sole reliance on the said agreements for the same. Specifically, agreement dated 05.04.2003 could not have been relied upon for payments made prior to 31.03.2003. In fact, that the expenditure was incurred wholly or exclusively for the assessee's business also cannot be established.

7. The revenue further submits that the assessee failed to establish the authenticity and genuineness of the agreements on which reliance has been

placed by the CIT(A) and ITAT. The learned counsel heavily relies on the fact that CGS International had independently confirmed that it received consultancy charges from the assessee during the year under consideration, as well as the assessee's treatment of these charges as such. Lastly, it is submitted that the CIT(A) and ITAT erred in applying Article 14 of the DTAA, and endorsed the AO's determination on this issue.

8. Mr. Kanan Kapoor, the assessee's counsel, submits that the findings of CIT(A), confirmed by the ITAT, cannot be faulted with, and are justified in the facts and circumstances of the case. The CIT(A), it is contended, thoroughly examined the issues at hand and on an analysis of the assessee's agreements with the two UAE entities as well as its contract with the Abu Dhabi Works Department, rightly rejected the AO's finding that the remittances made by the assessee were in respect of 'consultancy charges', attracting the provisions of Section 9(1)(vii) of the Act. Thus, TDS was not required to be deducted on the foreign remittances made by the assessee and the disallowance of amount by the AO on account of the non-deduction of TDS was incorrect.Further, the assessee submits that the CIT(A) correctly interpreted Article 14 of the DTAA in light of the definition of 'person' in Article 3 of the Treaty, and held it to be applicable. Thus, the assessee submits that the findings of CIT(A) and ITAT ought to be upheld.

Analysis and Conclusions

9. The assessee did not deduct TDS on the sum of₹ 94,31,826/- remitted by it to CGS International and Marble Arts & Crafts. Therefore, this amount would be allowed as deduction for computing the assessee's income only if it is held that the said remittances were not taxable under the Act, lest the

provisions of Section 40(a)(i) be attracted and the deduction would have to be disallowed. This sum would constitute income for the two UAE entities – CGS International and Marble Arts & Crafts –which, admittedly, do not have a permanent establishment in India. Thus, for these non-residents, the provisions of Section 5(2) would be applicable, which provides that the total income of a non-resident includes, *inter alia*, income that is deemed to accrue or arise in India. Section 9 enumerates several instances where income shall be deemed to accrue or arise in India.

10. The revenue had sought to bring this sum to tax under Section 9(1)(vii)(b) of the Act, and contended that the provisions of the India-UAE DTAA do not come to the assessee's rescue. To succeed in this appeal, the revenue must succeed on both these counts (framed as the two questions of law in this appeal). This Court proceeds to examine them both below.

Question No. 1:

11. At the outset, it would be apt to quote the relevant parts of Section 9(1)(vii), which read as follows:

> *"9. (1) The following incomes shall be deemed to accrue or arise in India:—*
>
> *...*
>
> *(vii) income by way of fees for technical services payable by—*
>
> *...*
>
> *(b) a person who is a resident, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or*
>
> *...*

Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head 'Salaries'."

12. The revenue contends that the remittances in question, made by the assessee (a resident) to the two UAE entities (non-residents), come within the scope of Section 9(1)(vii)(b).It is not in dispute that the two exceptions to the applicability of Section 9(1)(vii)(b), enumerated in the said sub-clause itself, do not apply in this case. The only dispute between the assessee and revenue concerns the interpretation of the phrase 'fees for technical services', as defined in Explanation 2 to Section 9(1)(vii).

13. Explanation 2 defines 'fees for technical services' to mean managerial, technical or consultancy services. Revenue contends that the services for which the assessee remitted the sums to CGS International and Marble Arts & Crafts classify as 'consultancy services'. This Court does not accept the revenue's submissions, and in light of the thorough determination carried out by the CIT(A), upheld by the ITAT, affirms their view.

Agreements Relied Upon by the Assessee:

14. The agreements dated 25.11.2002 (between CGS International and the assessee) and 05.04.2003 (between Marble Arts & Crafts and the assessee) were first produced before the CIT(A) and were duly taken on record under Rule 46A. The AO made its submissions on these agreements and sought to highlight various infirmities in these agreements. In furtherance of that

contention, the revenue submits that the agreements are not authentic in nature and that it cannot be concluded that the remittances made were in pursuance of those agreements. The CIT(A) took note of the fact that the assessee entered into the two agreements with CGS International and Marble Arts & Crafts to fulfill its obligations under its contract with the Works Department, Abu Dhabi. The CIT(A)'s observations on these two aspects are as follows:

> "*From a reading of the appellant's agreement with the Works Department, Abu Dhabi – and further agreements with CGS International and Marble Arts & Crafts, it cannot be said that payments have not been made to the latter two concerns in connection with the contract entered into by the appellant with the Works Department, Abu Dhabi. Whereas Marble Art & Craft was paid $50000 for identifying the suitable partner for the project at Abu Dhabi, and a consideration at 5% of the gross remittances receivable from the Works Department, Abu Dhabi for assisting the appellant in the day to day work towards checking the documentation and formats for invoices etc., CGS International was paid 15% of the sum received by the appellant from the Works Department, Abu Dhabi towards soliciting business for the appellant. <u>There is nothing in the agreements or the related documents thereof to indicate that the payments to the concerned two parties have not been incurred wholly or exclusively for the appellant's business at Abu Dhabi, or that the payments to the non-residents are in excess of the agreements entered into with them or that the payments are not in conformity with the regulations governing remittances abroad</u>.*
>
> *The AO has pointed out various infirmities in the agreements by way of absence of place of execution, no payment of stamp duty, non certification by the Notary Public and concludes that there is no legal validity of such agreements. Facts on record show that the agreement with CGS International dated 25.11.02 was prior to the agreement dated 12.01.03 entered into by the appellant with the Works Department, Abu Dhabi. The agreement with Marble Arts & Crafts*

dated 05.04.03 were subsequent to the agreement with the Works Department, Abu Dhabi. Both the agreements with CGS International and Marble Arts & Crafts concerned the appellant's contract with the Works Department, Abu Dhabi. For making the remittances outward to CGS International or Marble Arts & Crafts, the appellant has indicated to the bankers remitting the amount, the respective agreements governing the payments to those parties. In effect, both the agreements, entirely commercial in character, have been acted upon by the parties to the agreements i.e. by delivering services and receiving payment thereof. Rights and liabilities have accrued and acknowledged by the parties to the agreements. The question of legal enforceability of the agreements will not have as much implication for deciding the revenue implications of the payments made as much as a finding that the parties to the agreements did not render the service mentioned in the agreements or that the payments made are in excess of the agreements. In so far as both the agreements with CGS International and Marble Arts & Crafts relate to the main contract entered into - by the appellant with the Works Department, Abu Dhabi, and payments to the above two parties have been made for the purposes of appellant's project work, and so intimated to the bankers remitting the proceeds abroad, I hold that the fact of the expenditure itself has been established from the relevant records, notwithstanding the infirmities in the said agreements."

(emphasis supplied)

15. These findings of fact were upheld by the ITAT, noting that the revenue had been unable to show any material factual error. This Court, in this appeal under Section 260A of the Act, cannot interfere with these findings, to the extent that they conclude that the remittances were made pursuant to the two agreements entered into with CGS International and Marble Arts & Crafts. Further, this Court does not find any merit in the revenue's contention that the ITAT's and CIT(A)'s sole reliance on the two agreements to establish the authenticity of the transaction was erroneous.

The CIT(A), while relying on the two agreements, looked at the entire conspectus of facts and the materials placed on record by the assessee, all of which supported the assessee's case.

Nature of services rendered by the UAE Entities

16. This Court, in its recent ruling in *Director of Income Tax v. Panalfa Autoelektrik Ltd.*, (2014) 272 CTR 117 discussed the meaning of the phrase 'consultancy services' as employed in Explanation 2 to Section 9(1)(vii). The Court noted as follows:

> *"20. The moot question and issue is whether the non-resident was providing consultancy services. In other words, what do you mean by the term "consultancy services"? This Court in Bharti Cellular Limited and Others (supra) had referred to the term "consultancy services" in the following words:-*
>
> > *"14. Similarly, the word "consultancy" has been defined in the said Dictionary as "the work or position of a consultant; a department of consultants." "Consultant" itself has been defined, inter alia, as "a person who gives professional advice or services in a specialized field." It is obvious that the word "consultant" is a derivative of the word "consult" which entails deliberations, consideration, conferring with someone, conferring about or upon a matter. Consult has also been defined in the said Dictionary as "ask advice for, seek counsel or a professional opinion from; refer to (a source of information); seek permission or approval from for a proposed action". It is obvious that the service of consultancy also necessarily entails human intervention. The consultant, who provides the consultancy service, has to be a human being. A machine cannot be regarded as a consultant."*
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> *The AAR in the case of In Re: P.No. 28 of 1999, reported as [1999] 242 ITR 208 had observed:-*

> *"By technical services, we mean in this context services requiring expertise in technology. By consultancy services, we mean in this context advisory services. The category of technical and consultancy services are to some extent overlapping because a consultancy service could also be technical service. However, the category of consultancy services also includes an advisory service, whether or not expertise in technology is required to perform it."*
>
> *21. The word 'consultant' refers to a person, who is consulted and who advises or from whom information is sought. In Black's Law Dictionary, Eighth Edition, the word 'consultation' has been defined as an act of asking the advice or opinion of someone (such as a lawyer). It may mean a meeting in which parties consult or confer. For consultation service under Explanation 2, there should be a provision of service by the non-resident, who undertakes to perform it, which the acquirer may use. The service must be rendered in the form of an advice or consultation given by the non-resident to the resident Indian payer."*
>
> *(emphasis supplied)*

Subsequent to the decision in *Panalfa Autoelektrik (supra)*, the aforesaid definitions were also adverted to by the Supreme Court in *GVK Industries Ltd. v. ITO*, (2015) 371 ITR 453.

17. Gauged from the above excerpts, it is evident that 'consultancy services' would mean something akin to advisory services provided by the non-resident, pursuant to deliberation between parties. Ordinarily, it would not involve instances where the non-resident is acting as a link between the resident and another party, facilitating the transaction between them, or where the non-resident is directly soliciting business for the resident and generating income out of such solicitation. Indeed, as held by this Court in *Panalfa Autoelektrik (supra)*, since Section 9 is a deeming provision, the interpretation cannot be overly broad in nature.

18. In the case at hand, at the outset, this Court clarifies that the mere fact that CGS International confirmed that it received consultancy charges from the assessee would not be determinative of the issue. The actual nature of services rendered by CGS International and Marble Arts & Crafts needs to be examined for this purpose. It would be appropriate to note the details of services provided by the two entities, which were highlighted by the CIT(A):

> *"The agreement dated 5.4.2003 between the appellant and Marble Arts & Crafts provides that the latter will render guidance to the appellant about the procedural aspect of obtaining the payment and check the format and documents of the invoices that are to be submitted for approval to the Works Departments, Abu Dhabi, to receive and periodically check the invoices of the appellant, to submit the invoices to the respective authorities and obtaining their approval, to follow up with various authorities in the Works Department, finance department, banks and other authorities for obtaining the approval of the invoices raised by the appellant...*
>
> *In so far as CGS International is concerned, the agreement dated 25.11.2002 between the appellant and CGS International provided for a consideration payable by the appellant for liaison or solicitation charges. On its part, CGS International will identify, introduce and provide details of industries, companies and individuals, where the appellant can utilize its expertise in the field of architecture, material procurement project management etc. In short, CGS International as per agreement would market the appellant and solicit project management and architectural work in UAE and also, in various parts of the world except India. The consideration is a fee equivalent to 15% of the gross value of the contract to be received from each client, who CGS International has solicited and has rendered services to procure the contract. The appellant has made the payment of Rs.45,31,044/- to CGS International being 15% of a total receipt of $665195 from the Works Department Abu Dhabi. Payments to CGS International are in terms of an earlier agreement entered into with the appellant.*"

19. It is evident that in the transaction between the assessee and Marble Arts & Crafts, the former (non-resident) acted as an agent of the assessee for the purposes of the latter's dealings with the Works Department, Abu Dhabi, which included coordinating with the authorities in the said department and handling invoices for the assessee. As far as CGS International is concerned, it acts as a liaisoning agent for the assessee, and receives its remuneration from each client that it successfully solicits for the assessee. Facially, such services cannot be said to be included within the meaning of 'consultancy services', as that would amount to unduly expanding the scope of the term 'consultancy'. Therefore, this Court does not accept the revenue's contention that the services provided were in the nature of 'consultancy services'. Consequently, the remittances made by the assessee would not come within the scope of the phrase 'fees for technical services' as employed in Section 9(1)(vii) of the Act. This question is answered against the revenue and in favour of the assessee.

Question No. 2

20. This question involves a determination of whether the services provided by the UAE entities are in the nature of 'independent personal services' defined in Article 14 of the DTAA. Article 14, to the extent relevant here, reads as follows:

> *"1. Income derived by a resident of a Contracting State in respect of professional services or other independent activities of a similar character shall be taxable only in that State...*
>
> *2. The term "professional services" includes independent*

scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, surgeons, lawyers, engineers, architects, dentists and accountants."

21. The two requirements for the applicability of Article 14, as applied in this case, are: a) income must be of a resident of the Contracting State (herein, UAE); and b) income must be in respect of professional services or other independent activities of a similar character. Article 4(1)(b) of the DTAA defines 'resident of a contracting state' in the context of UAE to mean any *person* who under the laws of that State is liable to tax therein. Article 3(e) defines 'person' to include a company. Therefore, the CIT(A) rightly rejected the revenue's contention that Article 14 is inapplicable for the reason that the services in question were provided by companies, as opposed to individuals. As to whether Article 14 applies to the nature of services provided by CGS International and Marble Arts & Crafts, the CIT(A) observed as follows:

"In the DTAA with UAE, there are Article (sic) to consider assessability of income from immovable property (Article 6), business profit (Article 7), shipping (Article 8), associated enterprise (Article 9), dividends (Article 10), interest (Article 11), royalties (Article 12), capital gains (Article 13), Independent personal services (Article 14), dependent personal services (Article 15) etc. There is no clause or Article governing payment for the so called technical services as in other DTAAs i.e. Article 13 of DTAA with UK or Article 12 of DTAA with Singapore. In view of the fact that the non residents do not have any permanent establishment within the meaning of Article 5 of DTAA in India, the remittances to them could only have been considered under Article 14 or Article 22 of DTAA. Under Article 14 of DTAA, the consideration paid to the non-resident is liable to be taxed in the contracting state i.e. UAE. In case remittances are considered as other income under Article 22 of the DTAA, it would also be taxable in the contracting state i.e. UAE."

22. This Court agrees with the CIT(A)'s approach, quoted above. Since the income of CGS International and Marble Arts & Crafts can only be classified under Article 14 or Article 22 of the DTAA – both of which provide that the income shall be taxable in the State of residence (UAE)–the issue as to whether the services provided by the two UAE entities fall within the scope of 'professional services' under Article 14 is irrelevant to the outcome of this case. Their incomes would necessarily be taxable in UAE, whether by virtue of Article 14 or Article 22. For this reason as well, the assessee was not obligated to deduct tax on the remittances made to CGS International and Marble Arts & Crafts. The second question is answered accordingly.

23. Thus, both questions of law are answered against the revenue and in favour of the assessee. Consequently, the appeal is dismissed. No costs.

S. RAVINDRA BHAT
(JUDGE)

R.K. GAUBA
(JUDGE)

MAY 29, 2015