LANDMARK **ADVANCE RULING** DATED 17/6/2009 IN RELATION TO INTERNATIONAL TAXATION DEALING WITH A) AOP CONCEPT B) OFF SHORE SUPPLY C) SUPERVISORY PE UNDER DTAA

Facts:

Applicant a company incorporated in Korea, engaged in business of power stations, was awarded a contract by Power Grid Corporation of India, wherein on applicant behest, L&T was involved as an independent contractor for carrying out onshore supply and services contract. The offshore supply part remained with applicant. This ruling can be better studied along with earlier Madras High Court ruling in Ansaldo case (analyses enclosed).

Ruling of AAR (short analysis):

a) There was no AOP (Association of Persons) between applicant and L&T as "Each party performs the obligations under the respective contracts awarded to them separately and receives the monies payable under the contracts independent of each other. L&T, which was not a party to the bid, is recognized as an independent contractor in various documents. L&T is entitled to raise the bills for the work carried out by it separately and such bills shall be payable by Power Grid directly to L&T without recourse to the applicant (vide para 3 of Assignment Deed). Thus, the individual identity of each party in doing the part of work entrusted to it is preserved, notwithstanding the coordination between the two and the overall responsibility of the applicant. It cannot therefore be said that the two contractors have promoted a joint enterprise with a view to earn income (vide the dicta in CIT vs. Karunakaran*"

b) On offshore supply part executed by applicant: "....it held that under the offshore supply contract, the sale was completed outside India and there was no accrual or deemed accrual of income in India, the decision of the Tribunal is directly in point. We share the same view as the Tribunal has taken on this aspect..." (In turn relied upon SC ruling in Ishilawajima Harima case)

c) As regards existence of applicant's Permanent Establishment (PE) under Article 5 of India Korea DTAA under clause (3) which states: "3. The term permanent establishment likewise encompasses a building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only where such site, project or activities continue for a period of more than nine months" AAR concluded that:

i) "12. It must be noted that there are two limbs to para 3 of Art.5. The first limb is – "building site, construction, and assembly or installation project" and the second limb is supervisory activities in connection therewith. Both should extend over 9 months in order to constitute a PE. The applicant's case cannot be brought within the first limb because the construction and installation work is being undertaken by L&T. The question then is whether the duration test of 9 months vis-à-vis supervisory activities is satisfied. .....It is the contention of the Revenue that the applicant's supervisory role starts from the date of clearance of the equipment from the port as it is necessary to supervise the transportation and storage of equipment in order to ensure that no damage takes place. We do not think that this contention can be accepted. The applicant, in carrying out the equipment to the work site

and in safeguarding the same from any damage, is only carrying out the contractual obligations incidental to the offshore supplies of goods. It cannot be considered to be a supervisory activity contemplated by Art.5.3 of the Treaty."

ii) "The Revenue contends that all the projects of the nature described in Art 5.3 which are being carried out by the applicant should be seen together for the purpose of determination of PE in India. If so, the duration of supervisory activities in connection with both the projects shall be aggregated for the purpose of arriving at the period of 9 months. ..... If the establishment that is being maintained for the purpose of executing a different contract with a different party is separate, distinct and independent of the other contract work being executed by the applicant, it is not in our view permissible to combine the establishments of two different projects of fairly long duration for the purpose of arriving at the threshold period of 9 months."

iii) "14.1. No doubt, the contract does not specify the consideration payable for the supervisory activities to be carried out by the applicant especially at the stage of testing and commissioning. But, that does not mean that attribution of profits is not possible or permissible. A reasonable quantum of income attributable to such operations intimately connected with the PE (if any) has to be arrived at on an estimated basis. 15. The counsel for the applicant contended rather faintly that the activities by way of supervision of testing and commissioning of the plant are auxiliary in character and, therefore, the maintenance of fixed place of business for that purpose cannot be regarded as PE in view of clause (e) of Article 5.4. of the Treaty. We find no substance in this contention. The term 'auxiliary' means something which aids or is subsidiary to the main thing or act. The supervisory activities which the applicant had undertaken in terms of the contract are quite independent of offshore supply/sale of equipment."

d) As regards agency PE, AAR observed that "Then, in regard to agency PE, it has been clarified by the applicant that the Indian agent Alpasso Industries Pvt. Ltd., is an independent entity working for various clients and is not a dependent agent. In the affidavit filed on behalf of Alpasso Industries Pvt. Ltd., it is stated that the company is engaged in the business of rendering consultancy / marketing services and the relationship between the applicant and the said company is purely on principal to principal basis and that of a service provider and client. On the facts stated, it is not possible to infer an agency PE. "

e) As regards revenue's contention that "The other contention that L&T is a sub-contractor of the applicant is an extreme contention and we have no hesitation in rejecting the same. This contention has been raised by the Revenue to put forward a case that in computing the 9 month period, whatever work is done by L&T should also be taken into account., AAR observed that: There is no legal or factual basis for branding an independent contractor described as such in the contract document as a sub-contractor of the applicant.