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What's New

Tax Insights

13 June 2024

In absence of FTS clause in the India-Thailand DTAA, technical service rendered to Indian AE, being in the nature of business income, are not-taxable in India in absence of PE in India – Delhi bench of the Tribunal

In brief

The Delhi bench of the Income-tax Appellate Tribunal[1] (Tribunal) observed that the technical services provided by the taxpayer are in the nature of business income of the taxpayer. Accordingly, the provisions of Article 7 of the India–Thailand Double Taxation Avoidance Agreement (DTAA) is relevant in the instant case. The technical service rendered to Indian associated enterprises (AEs) by the taxpayer are not taxable in the absence of permanent establishment (PE) in India.

The Tribunal added that the residuary provisions of Article 22, other income of the India–Thailand DTAA will not apply to items of income, which can be classified under other provisions of the DTAA. However, their taxability is subject to fulfilment of conditions mentioned therein.

In detail

Facts

- For assessment year (AY) 2020–2021, the taxpayer, a resident of Thailand, provided business administration, material engineering services, design and development services, testing and technical services of automotive components to its AEs in India being in the nature of fees for technical services (FTS).
- The taxpayer treated the same as business income in the absence of FTS clause in the India–Thailand DTAA. In the absence of PE in India, the taxpayer treated such income as non-taxable.
- Subsequently, assessment proceedings were concluded wherein the tax officer (TO) accepted the nature of income as FTS. However, the TO was of the view that the said FTS income is not in the nature of business income of the taxpayer and accordingly invoked Article 22 of the India–Thailand DTAA and, consequently, taxed the same at 10% as per section 9(1)(vii) of the Income-tax Act, 1961 (the Act).
- Aggrieved with the assessment order, the taxpayer filed an appeal before the Tribunal contending that the FTS income earned by the taxpayer is in nature of business income and should be dealt as per Article 7 of the India–Thailand DTAA in case of absence of FTS clause.

[1] ITA No. 1986/Del/2023

Revenue's contentions

- The chargeability of any income is always defined under the Act, and the respective DTAA only provides relief from the said chargeability as specified under section 90 of the Act (if it is dealt under said DTAA). In the absence of FTS clause in the DTAA, the FTS income to be taxed within the ambit of Article 22 of the India–Thailand DTAA.
- On the basis of the web portal of the taxpayer, the TO concluded that services provided to the AEs are not in the nature of primary business activities of the taxpayer. The mere mentioning of activities in the Memorandum of Association (MoA) does not entail the taxpayer to claim such activity as part of its primary business activities. Accordingly, recourse of Article 7 of the DTAA will not be applicable in the facts of the case.

Taxpayer's contentions

- Section 90 of the Act provides an option to the taxpayer to be governed by the provision of the Act or DTAA to the extent it is more beneficial to the taxpayer[2]. In the absence of an FTS clause in the India–Thailand DTAA, the taxability of FTS income, being in nature of business activities, should be first tested under Article 7 of the India–Thailand DTAA before directly approaching Article 22 of the India–Thailand DTAA.
- The services rendered by taxpayer to its AEs are in direct nexus with the business activities of the taxpayer. In support of this, the taxpayer submitted comprehensive evidence that includes the MoA, the agreement between the taxpayer and its AEs, a certificate issued by the Department of Business Development outlining the nature of business activities and copies of invoices.
- The taxpayer placed reliance on certain judicial precedents[3], wherein it was held that, in the absence of an FTS clause in the DTAA, income is to be covered under Article 7 of the DTAA, and in absence of a PE in India, receipts from technical services should not be taxed in India.

Tribunal's ruling

- The Tribunal noted that the MoA is the relevant document to determine the nature and scope of taxpayer's business activity. Moreover, the web portal is not a conclusive evidence to determine the business activities of the taxpayer.
- The Tribunal noted that the FTS is a species of income with a specific definition and components, as mentioned under the provisions of the Act[4]. In case the DTAA does not make any separate reference on the taxability of the FTS income, then Article 22 of the said DTAA (which deals with residuary powers) can be invoked only when the FTS income is not subject to any other Articles of the DTAA.
- The intention of residuary powers of taxing income under Article 22 of the DTAA is to deal with incomes that, owing to lack of regularity, continuity and frequency, do not form part of regular business activities of the entity.
- The Tribunal, on perusal of the documentary evidence filed and taking into consideration the nature of services rendered by the taxpayer, concluded that the same are in the nature of FTS and can very well be part of the business income of the taxpayer.
- The Tribunal was of the view that, in the absence of a PE in India of the taxpayer, the FTS income will not be taxable under Article 22 of the India–Thailand DTAA.

The takeaways

This Tribunal order is a welcome ruling and adds to the list of the favourable judicial precedents that have concluded that, in the absence of the FTS Article in the DTAA, the technical services rendered by the taxpayers cannot be directly taxed under Article 22 other income of the DTAA without testing other Articles of the DTAA. Thus, the technical service rendered by the taxpayers can be claimed as non-taxable in India as long as they do not have a PE in India and the services rendered are in the normal course of their business activities.

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2 Motorola Inc. *v.* DCIT [2005] 95 ITD (Delhi)(SB)

3 Bangkok Glass Industry Co. Limited *v.* ACIT [2013] 34 taxmann.com 77 (Madras); Solvay Asia Pacific (P.) Limited *v.* DCIT [2024] 159 taxmann.com 90 (Delhi Tribunal); DCIT *v.* Michelin ROH Co. Limited [2022] 138 taxmann.com 497 (Delhi – Tribunal); ACIT *v.* IQOR India Services Private Limited [ITA No.7592/Del/2019]; DCIT *v.* Campus Eai India Private Limited [ITA No. 355/Del/2021]; etc.

4 Section 9(1)(vii) of the Act

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