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Global Business Tax Alert
Sharp Insights

Income from offshore services of a foreign company exempt under tax treaty cannot be charged to tax in India

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In this issue:

The Mumbai Tribunal in the case of IHI Corporation ("assessee") has held that income from offshore services executed by a Japanese company having a project office in India, though chargeable to tax under the provisions of the Income-tax Act ('the Act') but exempt under the provisions of the tax treaty accordingly would not be subject to tax in India in view of the beneficial provisions of the tax treaty.

The assessee was a Japanese company which had been awarded engineering, procurement, construction and commissioning contracts in India. For the purpose of the execution of the contract, the assessee had set up a project office in India. The contract consideration receivable was segregated into offshore portion (comprising of offshore supply of equipment and services from outside India) and onshore portion (comprising of onshore supply of equipments and services in India and construction and erection). In the return of income filed, the assessee offered the income from onshore activities to tax in India whereas income from offshore supply and offshore services were not offered to tax on the ground that the income had neither accrued nor arisen in India. For this purpose, the assessee placed reliance on the decision of the Supreme Court in its own case (288 ITR 408).

The Assessing Officer [AO] after relying upon the retrospective amendment made in the Act by the Finance Act, 2010, held that the decision of the Supreme Court was no longer applicable and concluded that income from offshore services was chargeable to tax in India. The Dispute Resolution Panel [DRP] rejected the objections raised by the assessee.

On appeal before the Tribunal, the assessee submitted that the issue involved in the instant case was squarely covered by the decision of the Tribunal in the assessee's own case (58 SOT 225).

The Tribunal observed that the Supreme Court in assessee's own case had held that the income from offshore services are to be considered as 'Business Profits' as per India-Japan tax treaty. The Tribunal observed that it had further been held by the Supreme Court that since the entire services were rendered outside India having nothing to do with the permanent establishment, there can be no taxability of the income from offshore services in India. The Supreme Court had further held that offshore services were inextricably linked to supply of gods and hence, income from offshore services ought to be considered in the same manner.

The aforesaid decision of the Supreme Court had been relied upon by the Bombay High Court in assessee's own case and had held that as per the provisions of India-Japan tax treaty, income from offshore services in the hands of the assessee was not chargeable to tax.

The Tribunal further held that as the provisions of the Act, an assessee has the option to offer its income to tax as per the provisions of the Act or the applicable tax treaty, whichever is beneficial. Accordingly, even though the offshore services were chargeable to tax under the Act, the same were not taxable in the hands of the assessee in light of the beneficial provisions of the India-Japan tax treaty.

The Tribunal, considering the factual matrix of the case as well as the judicial pronouncements rendered by the jurisdictional High Court, Supreme Court and the Tribunal in favour of the assessee, concluded that the income from offshore services were not chargeable to tax in India.

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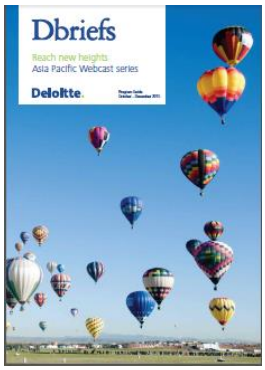

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