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Tax alert: Presumptive tax provisions override disallowance provisions

16 July 2024

The Chennai Bench of the Income-tax Appellate Tribunal (ITAT) has rendered its decision that provisions of section 44BB of the Income-tax Act 1961 (ITA) [relating to presumptive taxation of non-residents engaged in certain activities] would override other provisions of the ITA, including provisions of section 40(a)(i) of the ITA [relating to disallowance for non-deduction of tax].

In a nutshell

Provisions of section 44BB of the ITA have overriding effect on other provisions of the ITA, as the same provides complete code of computation of income from business of a non-resident to the exclusion of specified sections. Hence, the excluded provisions cannot be resorted to for the purpose of computing business of exploration of mineral oil under section 44BB of the ITA.

The payment to payee Singapore Company (S Co) was bareboat charter and was business receipt for S Co. S Co did not have permanent establishment (PE) and was not taxable in India as per Article 7 read with Article 5 of the India-Singapore tax treaty. The taxpayer was not liable to deduct any tax in India under section 195 of the ITA.

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Background:

- The taxpayer[1] is a Singapore based company, engaged in providing services and facilities relating to exploration and exploitation of mineral oil and natural gas.
- During the year under consideration i.e. Financial Year (FY) 2020-21 corresponding to Assessment Year (AY) 2021-22, the taxpayer filed its return of income as project office of the taxpayer in India. It offered income under section 44BB of the Income-tax Act, 1961 (ITA) [relating to special provision for presumptive taxation for taxpayers engaged in business of exploration, etc., of mineral oils] on presumptive basis @10% of gross receipts arising out of its project office situated in India.
- During the audit proceedings, the Assessing Officer (AO) observed / held that:
  - The taxpayer had taken three rigs on hire as bareboat from, amongst others, a Singapore based company (say S Co).
  - The taxpayer paid bareboat charges to S Co from which it had not deducted tax at source (TDS).
  - Since S Co remained in India for more than 183 days, it constituted permanent establishment (PE) in India.
  - The income of S Co on hire chargers was, therefore, taxable as business income in India and the taxpayer was required to deduct TDS on the same.

  Accordingly, the AO passed draft order by making disallowance for non-deduction of tax under section 40(a)(i) of the ITA [relating to disallowance of expenditure, *inter-alia,* on failure to deduct required taxes].
- The key contentions of the taxpayer were as follows:
  - The taxpayer reiterated that S Co was a non-resident company in India and agreement for bareboat charges was signed outside India.
  - The taxpayer as well as payee were non-resident entities, and the transaction was between two non-resident entities. Therefore, no income accrued or deemed to have accrued in India.
  - The taxpayer relied on non-obstante clause of section 44BB(1) of the ITA and contended that no disallowance under section 40(a)(i) of the ITA would be applicable as the income was offered on presumptive basis.
- The taxpayer filed objections against the draft order before the Dispute Resolution Panel (DRP), which directed the AO to uphold the disallowance. Accordingly, the AO passed the final order based on DRPs directions.
- Aggrieved, the taxpayer filed an appeal with the Chennai Bench of the Income-tax Appellate Tribunal (ITAT).

Relevant provisions in brief:

Extracts of section 44BB of the ITA:

"Special provision for computing profits and gains in connection with the business of exploration, etc., of mineral oils"

44BB. (1) ***Notwithstanding anything to the contrary contained in sections 28 to 41 and sections 43 and 43A****, in the case of an assessee, being a nonresident, engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils,* ***a sum equal to ten per cent of the aggregate of the amounts specified in subsection (2) shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession****"…*

[1] Aban Singapore Pte Ltd vs. DCIT [2024] 163 taxmann.com 140 (Chennai- Trib.)

…(3) Notwithstanding anything contained in sub-section (1), an assessee may claim lower profits and gains than the profits and gains specified in that subsection, if he keeps and maintains such books of account and other documents as required under sub-section (2) of section 44AA and gets his accounts audited and furnishes a report of such audit as required under section 44AB*, and thereupon the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee under sub-section (3) of section 143 and determine the sum payable by, or refundable to, the assessee…"*

Decision of the ITAT:

The ITAT noted / observed as follows:

- The provisions of section 44BB of the ITA start with a **non-obstante** clause and exclude the application of other provisions of sections 28 to 41 and sections 43 and 43A of ITA which would include the provisions of section 40a)(i) of the ITA also.

  Provisions of section 44BB of the ITA have overriding effect on other provisions of the ITA. Further, section 44BB of the ITA provides complete code of computation of income from business of a non-resident of the nature specified in section 44BB, to the exclusion of specified sections.

  Therefore, the excluded provisions could not be resorted to for the purpose of computing business of exploration of mineral oil understand 44BB of the ITA.

- In taxpayer's own case[2] for earlier year i.e. AY 2019-20, the ITAT had held as under:

  Provisions of section 44BB of the ITA

  — As per the provisions of section 44BB(1) of the ITA, a sum equal to 10% of the aggregate of the amount specified in section 44BB(2) of the ITA is deemed to be the profits and gains of such business chargeable to tax under the head 'Profits and gains of business or profession'. It was because the provisions of section 44BB of the ITA had quantified the deemed income of the non-resident taxpayer at 10%, it had opened with the clause 'Notwithstanding anything to the contrary' contained in sections 28 to 41 and sections 43 and 43A of the ITA.

  — As per the section 44BB(3) of the ITA, the non-resident could claim a lower profit and for this, the non-resident must file a return and prove the same with support of his regular books of accounts and other documents and by complying with other conditions specified therein i.e., 44AA, 44AB and 143(3) of the ITA.

  Provisions of section 195 of the ITA

  — The taxpayer had exercised the option available under section 44BB of the ITA by maintaining regular books of accounts and got the book audited. Since, the payment done to S Co was bareboat charter, and was business receipt for S Co, S Co did not have PE and was not taxable in India as per Article 7 read with Article 5 of the India-Singapore tax treaty; the taxpayer was not liable to deduct any tax in India under section 195 of the ITA. Reliance was placed on earlier rulings[3] in this regard.

  — Therefore, no disallowance for the expenditure under section 40(a)(i) of the ITA was warranted.

Considering that similar facts existed before the ITAT in the year under consideration, no change in facts had been demonstrated and the said ruling was not reversed by any higher judicial authorities, the AO's order was set-aside and the taxpayer's appeal was allowed.

[2] Aban Singapore Pte.Ltd.v. Dy.CIT [IT(TP) No.38(Chny) of 2022, dated 20 July 2023]

[3] Transmission Corporation of AP Ltd. v. CIT vide citation [1999] 105 Taxmann 742 (SC), GE India Technology Cen. (P) Ltd. v. CIT, (2010) 193 Taxman 34 (SC) and ACIT v. Interocean Shipping (I) (P) Ltd. [1994] 51 ITD 582 (Delhi-Trib.)

Comments:

The ITA provisions provide for taxation of taxpayers on presumptive basis in certain cases such as provisions of section 44B of the ITA which provide for taxation @ 10% of gross income. Further, such provisions may also provide the taxpayer an option to offer lower income to tax subject to fulfilment of certain conditions (such as maintaining the books of account and other documents, having them audited and furnishing the tax audit report).

In such cases a controversy may arise with respect to applicability of certain provisions such as disallowance for non-withholding of taxes under section 40(a)(i)/(ia) of the ITA.

The ITAT in this ruling in the context of section 44BB of the ITA, has upheld the principle that:

- Provisions of section 44BB of the ITA have overriding effect on other provisions of the ITA, as the same provides complete code of computation of income from business of a non-resident to the exclusion of specified sections. Hence, the excluded provisions cannot be resorted to for the purpose of computing business of exploration of mineral oil under section 44BB of the ITA.

Further, it has held that since the payment done to S Co was bareboat charter, and was business receipt for S Co, S Co did not have PE and was not taxable in India as per Article 7 read with Article 5 of the India-Singapore tax treaty; the taxpayer was not liable to deduct any tax in India under section 195 of the ITA.

The ITAT has also considered the issue of whether the taxpayer had disclosed lower rate of profit by netting of income by Goods and Services Tax (GST) for the purposes of presumptive taxation. In this regard the ITAT observed that the Supreme Court in an earlier ruling[4] had confirmed the stand of the High Court that reimbursement of service tax ought not to be included in aggregate of amounts specified in section 44BB(2) (a) and (b) of the ITA since it was not an amount received by the taxpayer on account of services provided by them in prospecting, extraction, or production of mineral oils. Services tax as well as GST bear same character of receipts and therefore, the disallowance by the AO was to be deleted.

Taxpayers with similar facts may want to evaluate the impact of this ruling to the specific facts of their cases.

[4] CIT v. Vantage International Management Co. [2023] 156 taxmann.com 23/[2024] 296 Taxman 160 (SC)

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