IN THE INCOME TAX APPELLATE TRIBUNAL "C" BENCH: KOLKATA
[Before Shri Mahavir Singh, JM& Shri B. P. Jain, AM]

I.T.A. No.431/Kol/2014
Assessment Year: 2010-11

Outotec GmbH, C/o Outotec India Pvt. Ltd. 12th Floor, South City Pinnacle, Plot No.-XI, Block EP, Sector V Salt Lake, Kolkata ï 700 091 (PAN: AAACO 8228K)	vs.	Deputy Director of Income Tax, (International Taxation)-2(1), Kolkata AayakarBhawanPoorva, 110 Shanti Pally Kolkata ï 700 107
(Appellant)		(Respondent)

I.T.A. No.432/Kol/2014
Assessment Year: 2010-11

Outotec (Canada) Ltd. (PAN :AABCO 2985L)	vs.	Deputy Director of Income Tax, (International Taxation)-2(1), Kolkata
(Appellant)		(Respondent)

I.T.A. No.283/Kol/2015
Assessment Year: 2011-12

Outotec GmbH (now converted into Outotec GmbH &Co.Kg) (Appellant)	vs.	Deputy Commissioner of Income Tax, International Taxation-2(1), Kolkata (Respondent)

Date of hearing: 06.05.2015
Date of pronouncement: 16.06.2015

For the Appellant: Shri J.P. Khaitan, Sr. Advocate
For the Respondent: Shri Vijay Kumar, Sr. CIT(DSD)

ORDER

Per Shri Mahavir Singh, JM:

These three appeals by assessee are arising out of orders of Deputy Director of Income Tax, International Taxation-2(1), Kolkata in all u/s.143(3) of the Income-tax Act, 1961 (hereinafter referred to as ñthe Actò) in appeal ITA No. 431/Kol/2014 for Assessment Year 2010-11& ITA No. 283/Kol/2015 for A.Y. 2010-12 in the case of Outotec GmbH dated 29.01.14 & 28.01.14 respectively and in ITA No. 432/Kol/2014 for AY 2010-11 in Outotec (Canada) Ltd. dated 23.02.2015. In all

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these cases, Deputy Director of Income Tax, International Taxation-2(1), Kolkata has followed the directions of Dispute Resolution Panel (DRP in short) Kolkata u/s 144C(5) r.w.s 144C(8) of the Act.

2. As the facts and circumstances are identical in all the three appeals, hence, we will consider the facts in the case of Outotech GmbH in ITA No. 431/Kol/14 and decided the issues first in this appeal.

ITA No.431/K/2014

3. The first issue in this appeal of assessee is against the taxability of supply of equipment in India. For this, assessee has raised following grounds:-

> *"Taxability of supply of equipment in India*
> *2(a) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that a part of the income earned by the appellant from sale of equipment to the Indian customers accrues or arises in India and thus taxable in India under the provisions of the Act read with the provisions of India-Germany Double Taxation Avoidance Agreement (DTAA).*
>
> *2(b) On the facts and in the circumstances of the case and in law Ld. AO/DRP has erred in holding that title of the equipment sold by appellant has passed on to the Indian customers in India and while reaching to this conclusion has further erred in misinterpreting various clauses of Sales of Goods Act, 1930.*
>
> *2© On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the sale of equipment by the appellant were not concluded until successful completion of various tests at the customers' sites in India without appreciating the fact that these tests are merely in the nature of warranty provision and this fact has been confirmed by the various courts/Tribunals//AAR in several judicial precedents.*
>
> *2(d) On the facts and in the circumstances of the case and in law, Ld. AO erred in rejecting the reliance placed by the appellant on the decisions of DIT Vs. Ericsson A.B [343 ITR 470], DIT Vs. LG Cable Ltd.[237 CTR 438] and Director of Income Tax vs. Ms. Nokia Networks Oy [253 CTR 417] merely on the contention that such decisions are sub-judice before the Hon'ble Apex Court.*
>
> *2(e) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that since the overall responsibility of the entire work is on the appellant the transfer of title to the customer on high seas of the equipment and entering into separate contracts would not make any difference without appreciating the fact that only in overall interest of the project and to facilitate co-ordination the appellant was given the overall responsibility and hence such responsibility would not have made any difference as far as sale of equipment outside India is concerned.*
>
> *2(f) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the contracts entered into by the appellant are composite contracts, for erection of plant purely based on surmise and conjecture without appreciating that the contracts are for supply of equipment.*

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2(g) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in not appreciating the fact that no Permanent Establishment (PE) of the appellant is created in India under Article 5 of the DTAA for offshore sale of equipment to the Indian customers and accordingly no income from such sale of equipment is taxable in India under the provision of the DTAA.

2(h) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that once thee is supervisory PE for one of the projects the said PE would become applicable for other projects as well without appreciating the fact that the wording of Article 5(2)(i0 of the DTAA clearly provides that PE has to be determined separately for each of the projects and hence for the projects for which there is no supervisory PE, the question of attribution on account of sale of equipment does not arise.

2(i) v, Ld. AO/DRP erred in holding that since the Acceptance Tests were carried out at customers' site in India the supervisory PE has a role to play in offshore sale of equipment without appreciating the fact that all the operation relating to design, fabrication and manufacture of the equipment were undertaken outside India and hence there is no role of supervisory PE in offshore sale of equipment.

2(j)On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the Protocol [Item 1(a)] to Article 7 of the DTAA is not applicable to the Supervisory PE and hence the benefit of the same cannot be given to the appellant.

2(k) On the facts and in the circumstances of the case and in law, Ld. AO failed in holding and Ld. DRP erred in not appreciating that there is no provision of sale PE under Article 5 of the DTAA.

2(l) On the facts and in the circumstances of the case and in law, Ld.AO/DRP erred in holding that the judgment of Ishikawajma-Harima Heavy Industries Ltd. Vs. DIT 288 ITR 408 and other judicial precedents relied upon by the appellant were based on their own facts without appreciating that such decisions are squarely applicable in the appellant's case."

4. Brief facts leading to the above issue, as noted in the order of DRP dated 23.12.13 and assessment order are that the assessee is a tax resident of Germany, engaged inter alia in the business of providing innovative and environmentally sound solutions for a variety of customers in metals and minerals processing industries. The assessee-company filed its return of income electronically for the relevant AY 2010-11 on 29-03.2012 declaring total income at Rs.1,85,60,360/-. The AO framed draft proposed assessment order u/s 143(3) r.w.s 144C of the Act proposing to assess the income from sale of equipment as taxable in India. According to AO, the assessee supplied equipment to seven Indian companies during the year under consideration relating to Steel Industry. The assessee raised invoices for sale of equipment amounting to Euro 79,776,994 equivalent Rs.475,71,02,152/- applying TT buying rate as on 31-03-2010. The assessee filed

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copies of contract for sale of equipment and AO after considering the submissions and documents proposed that a profit percentage @ 10% be chargeable to tax from sale of equipment. Aggrieved, assessee carried the matter to DRP. DRP issued direction u/s 144C(5) r.w.s. 144C(8) of the Act and directed the AO as under:-

> *"This panel has carefully considered the submissions of the assessee and also gone through the order of the Assessing Officer. The crux of the issue is whether sale of goods taken place in India or outside India? Whether testing activities connected with the supply of equipment is really linked to the very acceptance of the goods or it is merely in the nature of warranty? It is essential to look into the terms of the contract to arrive at a conclusion on this crucial question.*
>
> *During the year under consideration the assessee has earned from sale of equipment from TATA Steel Ltd., JSW Steel Ltd. Steel Authority of India Ltd., Bhushan Steel Ltd., Vedanta Aluminium Ltd.*
>
> *This panel has gone through the agreements and found that the supplies of the equipment on standalone basis are not the objective of the agreements. The agreements indicated that it is the supply, installation, testing and put the working equipment to the working condition. Some of the clauses which made this panel to arrive at this conclusion are discussed hereunder:*
>
> *<u>Agreement with TATA Steel, Kalingangar (No. TATA-KPO/CON/SP/FOB)</u>*
> *Scope of Work Clause 1.1.17. – Contractor's responsibility for completeness*
>
> *The contractor shall be fully liable and responsible for completeness of work that include all equipment, to fulfill the functional requirement of work as a whole and contractor's aforesaid responsibility shall be construed as included in the contract price.*
>
> *All items of equipment, whether specifically mentioned or not in the Technical Specification but which are usual and/or necessary for completion of work under the contract and are necessary for proper, efficient, sale and stable construction, operation and maintenance of the work and/or for the fulfillment of the performance guarantees, shall be supplied or provided or executed by the contractor without any additional price implication and without any dilution of this liabilities and responsibilities under contract.*
>
> > *Clause 16 : Cold tests, integrated cold test and start up*
> > *16.1 Cold tests shall be performed on all plant and equipment and items converted under the contract, individual sub-assemblies of the unit sand shall be designed to conduct the systematic check of the components and of functional operation thereof.*
> > *16.2 Cold tests shall include, inter alia, completion of erection, checking of alignment, rotation and vibration, checking of all electrical interlocks, checking of insulation, checking of cabling interconnection, input/output connection check, calibration of instruments, pressure testing of pipelines, idle and no-load tests.*
> > *16.3 A details program of cold tests including formats of check-sheets shall be prepared by the contractor and submitted at least three (3) months prior to commencement of cold tests to the Purchase/Engineers for comments and finalisation.*
> > *16.4 The completion of cold tests for all plant and equipment and items covered under the Contract collectively for the plant/unit as a whole and*

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thereby ascertaining proper erection/installation of all plant and equipment and functioning of the system as well as its readiness for start up and load tests shall mean the completion of Integrated Cold Test of the plant.

Clause 17.7
On the satisfactory completion of the performance test and on signing of the completion protocol between the purchaser and the contractor, the purchaser will promptly issue a Provisional Acceptance Certificate for the plant, provided that the contractor undertakes to promptly rectify defects, if any, which do not influence commercial operating but which are nevertheless present in the plant and which are indicated in writing by the Purchaser to the Contractor and the Contractor has fulfilled his obligations regarding his submission of designs and drawings including "As Built Drawings". Such certificate, however, shall in no way release the contractor from his liabilities and responsibilities in respect of the contract plant as a whole.

Clause 31 – Construction of Contract
31.1 The contract shall be governed by the laws in India.
31.2 This contract and the clauses thereof shall be interpreted and applied solely according to their wordings, to the objects in view. The contract shall in all respects be construed and operated as a contract as defined in the Indian Contract Act, 1872 and Sale of Goods Act, 1930, if applicable ad save as otherwise expressly provided herein shall be governed by the provisions of the said Act.
From the above the total contract value is Euro 24,130,550 for the entire contract which included cost of equipment and designs and drawings.
From the above it is clear that the scope of Contract is not confined merely to dispatch of equipment on FOB basis overseas but linked to free and trouble fee operation of the such equipment in the plant. Further acceptance of equipment is linked to the fulfillment of the performance guarantee obligations which includes Cold Test etc., As such when the acceptance of the equipment supplied is directly linked to the performance of test run, the assessee's argument fell flat.

The contract is to be interpreted in the main object of the parties who have entered into such contract. Though the price of the equipment, designs is separately shown, the real intent of the Indian customer is to erect the plant. It cannot be ignored that the plant cost is more than 100 crores. When the equipment becomes the integral part of the plant and till such state is the obligation of the assessee to ensure smooth commissioning of the plant, the contract cannot be viewed in isolation and in parts.
From the contacts it is noticed that the main purpose of the supply of equipment is to erect plant and such intention is not to be missed. The Hon'ble AAR in the case of Alstom Transport SA [2012] 208 Taxman 223 (AAR) held as under:

- *A contract for the installation and commissioning of a project cannot be split up into separate parts as consisting of independent supply of gods and for installation at the work site;*
- *The basic principle in interpretation of a contract is to read it as a whole and to construe all its terms in the context of the object sought to be achieved and the purpose sought to be attained by implementation of the contract [relying on the rulings in the case of Linde A.G. (AAR No. 962 of 2010) (AR) and in Roxar Maximum Resevoir Performance WLL (AAR No. 977 of 2010) (AR)]*
- *The AAR relied on the decision of the Supreme Court in the case of Vodafone International Holdings BV [2012] 341 ITR 1 (SC) wherein the Apex Court*

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*observed that it is the task of the Revenue/Court to ascertain the legal nature of the transaction and while doing so it has to '**look at**' the transaction as a whole and not to adopt a dissecting approach;*

- *Accordingly, the contract could not be split up to treat a part of it as confined to offshore supply of equipment not capable of being taxed in India.*

Regarding the assessee's contention that the AO did not consider the Delhi High Court judgment in DIT Vs. Ericsson A.B., New Delhi (343 ITR 470) (Del High Court) and, DIT vs. Nokia networks Oy (253 CTR 417) (Del High Court), the question before the Hon'ble High Court was when the title in the goods is passed outside India, there would not be any taxability in India, even in a composite contract. But the question here is whether the title is actually passed outside India. Since we have already held that acceptance of performance deliveries including testing and commissioning is linked to the supply of equipment, the title in the property has passed in India only. As such the reliance on these case laws is misplaced.

When the contract is for the erection and commissioning of the plant, in fact the equipment may not remain as a property and the whole contract becomes a project for Plant Erection. It is the assessee thus who agreed to erect the plant and for the sake of clarity and convenience the terms of supply designs and supervision have been specified. This will not alter the true character of the contract. It remains contract for erecting the plant.

If a question is put whether the equipment supplied by the contractor remains an equipment which is independently capable of functioning, the answer would be an obvious NO. If the enclosure 1 is closely examined, the entire equipment, designs becomes plant and this may be the reason, the liquidated damages are confined to 35% of the contract value. The absence of return of goods clause is apparently cannot be incorporated since the equipments part and parcel of the plant and cannot be goods in real sense.

Enclosure-1 to the FOB contract is as under:

FOB (Contd.) *260*

Enclosure – 1

Break-up of price for design, manufacture and supply of imported plant, machinery and equipment with auxiliaries and initial fills, commissioning spares on F.O.B. basis for Sinter Plant at Kalinganagar, Orissa

Sl. No.	Item Descriptions	Qty. Nos.	Wt. MTs	Country of Origin	Currency	Fixed FOB price, packed (Euro)
1.O	Plant and Equipment/items, complete in all respects					
1.1						
1.1.1						
1.1.2						
1.1.3						
etc.						
1.2	Electrics					
1.2.1						
1.2.3						
etc.						
1.3	Instrumentation &					

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	Automation					
1.4	Utilities					
1.5	Water system					
2.0	Foundation bolts, special bolts and special embedments as required					
3.0	Special tools and tackles for operation and maintenance					
4.0	Commissioning spares up to provisional Acceptance					
5.0	Initial fill required for start-up and commissioning till Provisional Acceptance					
6.0	Any other item not specifically mentioned above but considered by the Contractor					
7.0	Designs and drawings for imported equipment/items					
	Total é é				Euro	24,130,550

Thus the equipment is part of whole plant which consists of various designs, electrical and automated systems. Though the contract is split into parts, the completeness of the contract is achieved only after the successful testing of the plant. The work done by the assessee may include supply of material, equipment, drawings documents, guaranteeing the work. The responsibility of the assessee did not stop with the supply of the equipment and when the contract is for the work the supply component need not be viewed separately.

In view of the above position, this panel is not in agreement with the contentions raised by the assessee and the objection on the non-taxability of sale of equipment is rejected."

The AO also followed the directions of DRP and assessed the estimated profit @ 10% of sale of equipment. Aggrieved, assessee-company filed appeal before Tribunal.

5. Before us, Ld. counsel for the assessee Shri J.P. Khaitan, Senior Advocate argued on behalf of the assessee-company and for Revenue Shri Vijay Kumar, CIT-DR argued. Ld. counsel for the assesses stated facts that the AO and DRP, noted in respective orders that assessee Company does have a PE in terms of Article 5(2)(i)

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of the India-Germany DTAA and there has been Sale of Equipment by the Company for various projects in the year under consideration. Revenue noted that as per the contracts for sale of equipment, the conclusion of sale is subject to various accepted tests and others, and also envisages that certain percentage of the payment will be payable upon the successful completion of those tests. Clauses exist in the contracts regarding the company liable for payment of liquidated damages in the event of performance guarantee parameters not being met. Therefore, the same has concluded in India and as the existence of a PE has already been admitted by assessee, then as to why attribution of profits from sale of Equipment should not be made. Ld. Counsel explained the factual and legal position with regard to sale of equipment before addressing the specific query with regard to acceptance tests and the attribution of profits from sale of equipment to the PE raised by revenue. According to Ld. Counsel the contracts relating to sale of equipment were broadly undertaken in the following manner:

> *(i) The designing, procurement of material, fabrication and manufacturing of equipment was undertaken outside India. The Company is not involved in the manufacturing of equipment and such equipment were sourced from third party vendors based outside India.*
>
> *(ii) The equipment was directly sold by the assessee on export sale basis and the title/ownership in the equipment was transferred outside India i..e before the equipment reached India.*
>
> *(iii) Consideration/payment for sale of equipment was received outside India in foreign currency.*
>
> *(iv) Majority of the payment (80% - 85% including 10% advance) for each and every part of shipment becomes payable upon delivery of equipment on FOB foreign port of shipment once shipping and other documents are send to the customer. Such payments are made through irrevocable letter of credit.*
>
> *(v) The buyers were the Indian customers who were independent and unrelated parties and purchased the equipment from the assessee on their own account and hence the price was at arm's length;*
>
> *(vi) The assessee was not legally or economically dependent upon the Indian customers;*
>
> *(vii) The contracts for the sale of equipment were concluded on a 'principal to principal' basis;*
>
> *(vii) Under the contracts, customer' inspection of the equipment was to be taken place outside India; and*

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(viii)The assessee did not have any office or place of business in India.

Ld. Counsel for the assessee Shri Khaitan clarified from the facts that operations relating to designing, fabrication and manufacturing of equipment, and sale of equipment took place outside the territory of India. He referred to relevant clauses of contract for sale of equipment for Tata Steel Kalinganagar Project (In short ñTSKP), which are reproduced as below:

Clauses relating to scope of work – Tata KPO project
"Schedule 1
Article 1.1. SCOPE Of WORK FOR DESIGN, MANUFACTURE AND SUPPLY OF IMPORTED EQUIPMENT
1.1.1 Designs, procurement of materials, manufacture/fabrication, inspection, testing and supply of all imported Equipment on F.O.B. port of shipment basis with the time stipulated in Schedule 3 (DELIVERY). The term ""Port of Shipment" shall mean the European sea ports and sea ports of South Korea.
The materials are to be suitably and securely packed for ocean shipment and for storage under tropical conditions as well as subsequent movement by road transport in India. The provisions of INCOTERMS 2000 for the term "FOB" shall be applied.
1.1.2 Supply of all equipment foundation bolts including bolts of special design and those made of alloy/special steels and imported special embedment's that may be required for the Equipment on F.O.B. Basis"

Clauses related to transfer of title/property in equipment outside India
"Schedule 3
1.1 Delivery of imported Equipment and Commissioning Spares
The FOB Delivery of all imported Equipment as listed in break—of Price given in Enclosure-I of this Agreement, will be completed by the Contractors within twenty three months (23) months from the Contract Effective Date….

SCHEDULE 4
TERMS OF PAYMENT
4.1.1 5% of Contract price for imported Equipment and items along with related designs and drawings for imported equipment will be payable by telegraphic transfer, within three (3) months from Contract Effectiveness Date….

4.1.3 75% of the Price of each and every part shipment for Equipment will be payable as per Billing cum Schedule approved by the Purchaser as per Schedule-5 of this Agreement and against presentation of following dispatch documents proving that the goods are delivered FOB port of shipment:

4.2 Mode of payment
4.2.2 Payments as per clause 4.1.3 and 4.14 are payable at sight against presentation of the stipulated documents out of an irrevocable letter of credit allowing partial payment to be opened by a first class bank in India in favour of the contractor within sixty (6) days from the date of signing the agreement.

15. REPLACEMENT OF UNSERVICABLE MATERAIALS
15.1 Up to FOB, if any Contract Work including supplies perishes or becomes unserviceable, including loss or damage in transit, Contractor shall repair or replace such parts without delay at Contractor's account and shall receive possible proceeds of the settlement from insurance.

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15.2 After FOB, if any Contract Work including supplies perishes or becomes unserviceable, including loss or damage in transit, due to reasons not attributable to the Contractor, Contractor shall on request by Purchaser repair or replace such parts and be entitled to payment from purchaser of the corresponding mutually agreed reasonable costs and time incurred by Contractor to do so.

Clauses relating to customer's inspection

"12.2 Inspection at Contractor's and / or at His Sub-Contractor's Premises

The purchaser and/or his authorised representative may have the right of inspecting and testing the Contract work or any part thereof including all Plant and Equipment, its components, sub[-assemblies and assemblies etc at all times or at any time during the manufacture at Contractor's and/or to at his Sub-contractor's premises and the Contactor, on demand from the Purchaser and/or his authorised representative and in his presence, shall carry out tests in accordance with the agreed inspection procedure together with details of tests to be conducted ... However, the Purchaser and/or his authorised representative shall bear Purchaser's travel, accommodation and related expenses. The Contractor shall also carry out other tests as may be required to be carried out by the Contractor under the Contract…

12.11 Despatch Clearance Certificate

Within 5 days of successful completion of inspection and/or tests at the Contractor's or sub-contractor's works, the purchaser/his authorised representative shall automatically issue a Despatch clearance certificate (DCC) approving thereby the concerned Plant and Equipment for shipment/dispatch.

18. Defective Plant, Materials and Workmanship

18.1 If the completed plant or any portion thereof after the performance test, be found defective due to the reasons solely attributable to the Contractor or fails to fulfill the performance guarantee parameters as per clause 3.4 of Schedule 3 of the Contract, the Purchaser shall be at liberty to inform the Contractor accordingly and give the Contractor notice as reasonably practical, setting forth particulars of such defect or failure. The Contractor shall, with all speed and at his own expense, make it comply with the requirement of the Contract. Should he fail to do so within a reasonable time, the Purchaser may repair and / or replace, at the cost of the Contractor, the whole or any portion of the plant, as the case may be, which is defective or fails to fulfill the requirements of the Contact. Such repair / and or replacement shall be carried out by the Purchaser, where reasonably possible to the same Technical specification. The Contractor's liability under this clause shall be to pay the purchaser all direct resulting cost for such repairs / or replacement, subject to a limit of 35% of the Contract price."

In view of the above, Shri Khaitan argued that the relevant extract of delivery/title transfer and other clauses under various contracts for which equipment has been supplied during the year under consideration to demonstrate that the sale has taken place outside India has already been explained before the AO and now filed in its paper book as Annexure-I. He contended that the sample bills of landing which clearly demonstrate that the title in equipment was transferred to the customers outside India, and this document is enclosed as Annexure-II.

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6. In view of these facts, Shri Khaitan referred to the provisions of Section 5(2) of the Act, which deals with the scope of total income of any previous year of a non-resident on which income-tax is chargeable under section 4 of the Act. According to him, section 5(2) of the Act provides that the total income of the non-resident would include all income from whatsoever source derived which (i) accrue or arise in India or (ii) deemed to accrue or arise in India or (iii) is received in India or (iv) deemed to be received in India. He explained that the consideration was also received outside India in foreign currency by the assessee, no part of revenue from sale of equipment can be considered as received or deemed to be received in India. Therefore, the only point that needs to be discussed is whether any income from the sale of equipment can be said to accrue or arise or deemed to accrue or arise in India. In order to explain the same, it would be important to take a note of relevant extracts of section 9(1)(i) that are reproduced below:

> *"9(1) The following incomes shall be deemed to accrue or arise in India:*
> *(i) All income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India or through the transfer of a capital asset situated in India.*
> *Explanation 1: For the purposes of this clause:*
> *(a) In the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India." (emphasis supplied)*

Sh. Khaitan explained the effect of section 5 read with section 9(1)(i) that income shall accrue or arise or deemed to accrue or arise in India if the same is earned through any business connection in India. However, Explanation 1(a) to section 9(1)(i) of the Act provides that where some operations are carried out in India then income only to that extent resulting from such operations can be taxed in India. In other words, if no operation is carried out in India, then no profit can be taxed in India. Thus, the point that merit consideration is whether the assessee has carried out any operation in India in relation to sale of equipment. According to Sh. Khaitanthe facts mentioned in above paragraphs including the clauses for TKPO project agreement clearly demonstrate that all the activities relating to designing, fabrication and manufacturing took placed outside India and 75% of the payment for each and every part of shipment becomes payable upon delivery of equipment on FOB

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foreign port of shipment once shipping and other documents are submitted to the customer and such payment has to be made through irrevocable letter of credit. It is needless to mention that no buyer would make the substantial payment for equipment of which the property has not been transferred to him. The irrevocable letter of credit further makes it clear that even if the ship does not sail or deliver the goods to the destination, the assessee receives payment out of L/C, guaranteed by the bank, upon FOB delivery. Therefore, it is clearly evident that the sale of equipment took place outside India on principal to principal basis and the consideration was also received outside India in foreign currency. Accordingly, it is submitted that the assessee cannot be considered to have carried out any operations in India with regard to equipment sold to the Indian customers. In view thereof, no portion of the receipts from sale of equipment can be taxed in India under the provisions of the Act. According to Ld. Counsel, since the income is not liable to tax in India under the provisions of the Act, therefore, the assessee is not required to examine the taxability under the provisions of the DTAA as mentioned by the Hon'ble Supreme Court in the judgment of Ishikawajma-Harima Heavy Industries Ltd. vs DIT (2007) 288 ITR 408 (SC) on page no. 444 of report wherein it has been held that ñ*The entire transaction having been completed on the high seas, the profits on sale did not arise in India, as has been contended by the appellant. Thus, having been excluded from the scope of taxation under the Act, the application of the double taxation treaty would not arise."*

7. Ld Counsel further argued that even under the provisions of the DTAA, no part of the profits can be taxed in India. This has been explained by Ld Counsel, briefly in the following paragraphs.

Legal position under the India-Germany DTAA.

*1. Income derived by the assessee from the sale of equipment to the Indian customers is governed by provisions of Article 7 of the DTAA which provides that '**Business Profits**' earned by a German resident is taxable in India only if that German resident carries on business in India through a permanent Establishment ("PE") in India in terms of Article 5 of the DTAA.*

1. The relevant provisions of Article 7(1) of the DTAA, is reproduced below: "ARTICLE 7 – Business profits -1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as

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aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment."

2. He stated that the assessee did not have any office or place of business in India for the year under consideration. Further, it has already been explained in the preceding paragraphs, that all the activities relating to manufacturing and sale of equipment took place outside India. Therefore, the assessee wishes to submit that no PE has been constituted in India with respect to sale of equipment and hence no profits from sale of equipment can be taxed in India. Further, for the projects for which supervisory PE has been constituted in India, it is submitted to designing, fabrication and manufacturing of equipment was done outside India and sale has also taken place outside India and hence profits arising from sale of equipment is not taxable under the provisions of DTAA.

3. Ld Counsel stated that the above position has also been accepted by the Settlement Commission for Financial years 2007-08 and 2008-09, whereby after examining the facts of the case of the assessee it was held by the Commission that sale of equipment is not taxable in India both under the provisions of the Act and DTAA. Further, the significant portion of revenue from sale of equipment for the projects mentioned in the table below was covered under the settlement application and the major supplies had happened during the said period. During the year under consideration, the assessee has raised the invoices for remaining payments which mainly pertains to acceptance test etc., and do not relate to supply. The details of the same are mentioned below:

(Amount in Euros)

S.No.	*Name of project*	*Value of invoices raised for sale of equipment*
1	*Tata SP4*	*333,838*
2	*Vedanta Paste Plant*	*395,000*
3	*Vedanta Paste Plant (expansion)*	*633,472*

The assessee contended that to the best of the knowledge of the assessee even the revenue has accepted the settlement Commission order for FYs 2007-08 and 2008-09,the said order has not been challenged till date. Accordingly, there cannot be any question of the remaining payments for the above projects being taxable in India in light of the factual and legal position being confirmed by the settlement Commission Ld counsel Sh. Khaitan admitted that, except the projects covered under the application field before settlement commission, for the year under consideration, the supervisory PE exists only for SAIL IISCO project. Hence it was reiterated that, since all the work relating to designing, fabrication and manufacturing of equipment was done outside India and sale has also taken place outside India, there cannot be any question of role of supervisory PE in the off shore supplies for the said project and hence revenue from sale of equipment for IISCO project is not attributable to the said supervisory PE.

4. Apart from Article 7, Protocol [Item (a)] of the said DTAA also clarifies that the income arising on delivery of equipment from outside India cannot be taxed in India. The said protocol reads as under:

Protocol [Item 1(a)] of the Treaty

"With reference to Article-7
(a) In the determination of the profits of a building site or construction, assembly or installation project there shall be attributed to that permanent establishment in the

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contracting state in which the permanent establishment is situated only the profits resulting from the activities of the permanent establishment as such. If machinery or equipment is delivered from the head office or another permanent establishment of the enterprise (situated outside that contracting state) or a third person (situated outside that contracting state) in connection with those activities or independently there from there shall not be attributed to the profits of the building site or construction, assembly or installation project the value of such deliveries".

(Emphasis Supplied)

Thus the profits, if any, of the offshore supply of equipment will not be attributable to the PE even if the equipment is delivered in connection with the activities of the said PE."

8. On the other hand, Ld. CIT, DR Shri Vijay Kumar only relied on the orders of DRP and that of the AO. According to him, the assessee provided drawings, designs & engineering documents relating to steel industry to Indian customers for the operation and maintenance of the plant and claimed that supply of drawings, designs & engineering documents constituted ówithoutrightô sale, not connected with assesseeôs PE in India and hence not taxable in India. The assessee also placed reliance upon various judicial pronouncements, namely, *Scientific Engineering House (P) Ltd. v. CIT* 157 ITR 86 (SC) and *Modern Treads (India) LTD. v. DCIT* 69 ITD 115 (ITAT Jaipur). The AO gave a finding that the payment for supply of drawings, designs & engineering documents constituted ñ*royalty*ò under Explanation 2 to section 9(1)(vi) of the Income Tax Act as well as under Article 12(3) of the India-German DTAA. The AO, in his order, noted from the assesseeôs contract with TATA Steel, Jamshedpur in which clause 12.2 clearly stipulates that *"The Intellectual Property of all designs, processes, drawings and other documentation shall remain vested with the Contractor. The purchaser is granted a license to use such designs, process, drawings and other documentation for the operation and maintenance of the plant."* Such an identical clause is present in all the contracts with other Indian customers to whom, the assessee supplied the impugned drawings, designs and engineering documents. It makes it evident that in reality, it is not pertaining to any sale of goods but mere granting of a license to use the intellectual property embedded in such drawings, designs & engineering documents. Moreover, the judgment of the Hon'ble Supreme Court in the case of *Scientific Engineering House (P) Ltd.* cannot help the case of the assessee because it was rendered in the context of capitalization of assets for the purpose of claim of depreciation at the hand of the purchaser and the said judgment had nothing to do with the taxability of income in the hand of the supplier. The other judgments relied

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upon by the assessee are also based on their facts and not applicable to the case of the assessee. He argued that the DRP have found that on identical facts based upon the same contract, the Income Tax Settlement Commission (in short ITSC) in its order dated 30.12.2011 in assesseeôs own case gave elaborate findings that the payment for supply of drawings, designs & engineering documents constituted ñ*royalty*ò under Explanation 2 to section 9(1)(vi). The decision of ITSC on this issue still holds the field in the absence of any contrary decision by any higher judicial forum in the assesseeôs case. Since there have been no change on facts and circumstances even in the assessment year under consideration, there is no reason to make a departure from the ITSCôs decision on the same issue. He explained that under the contact, the assessee had actually granted a license to use i.e. right to use know-how and engineering information to enable the Indian customers not only to design, engineer, erect and set up the plant but also to commission, operate, test and maintain the plant and to manufacture the product in the plant. Certainly the payment in question covered consideration for information concerning industrial, commercial or scientific experience. The term ñ*industrial, commercial or scientific experience*ò alludes to the concept of ñ*knowhow*ò (vide paragraph 11 of the OECD Commentary on Article 12). As commonly understood, óknow-howô is the accumulated fund of knowledge acquired by years of observation, research, experimentation and experience. It grows in the shape of a formula, drawings, patterns, blue prints, specifications and so on. The material form it takes, not only facilitates preservation, collation and reference, but also makes it perceptible and visible and easily capable of being transmitted to others. Though physical records of know-how such drawings, designs, engineering and manufacturing data is imparted to another person, know-how is not lost to its owner who still continues to retain it for his own use. Therefore, income arising from an agreement under which such record is parted with cannot properly be termed as capital receipt. Technology is a science or body of knowledge applicable to the production of goods or services. Modern machinery is the product of technology. The concept of transfer of technology is complex phenomenon involving rights, obligations privileges and commitments of the parties concerned. The transaction permits access and control to advance means of production. In the present case what was transferred in the form of drawings designs, engineering information, documents, etc., covered the usage of industrial, commercial

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or scientific experience to ensure the successful set up, operation of the plant as well as maintenance of the process of manufacture, at the same time the transferee was required to maintain the confidentiality involved in the transferred records under a strict secrecy clause as contained in the relevant agreement. As mentioned earlier, in such a transfer the know-how is not lost to its owner who still continues to retain it for his own use. Law has evolved over the years and consideration paid for the transfer of know-how is defined both in the Income Tax Act and in the Tax Treaties as meaning ñ*royalty*ò. For the purpose, technical know-how means knowledge concerning industrial, commercial or scientific experience. It is the unrivaled technical information whether capable of being patented or not, that is necessary for the industrial production of a product or process, directly and under some condition, inasmuch as it is derived from experience [vide (1999) 105 Taxman 240 (AAR): Advance Ruling P. No. 30 of 1999]

9. Sh. Vijay Kumar further explained that in line with the above understanding, know-how transfers are generally viewed as involving transfer of pre-existing special knowledge or information to another, where such knowledge or experience remains confidential and the property of the supplier. The OECD MCC on Article 12 refers to the following key elements to identify transactions for the provision of know-how:

(i) According to the ANBPPI (Association des Bureaux pour la Protection de la Propriete Industrielle), know-how is "undivulged technical information that is necessary for the industrial reproduction of a product or process, directly and under some conditions, inasmuch as it is derived from experience, know-how represents what a manufacturer cannot know from mere examination of the product and mere knowledge of the process of technique."

(ii) In the know-how contract, one of the parties agrees to impart to the other, so that he can use them for his own account, his special knowledge and experience which remains unrevealed to the public.

(iii) In the know-how contract "the grantor is not required to play any part himself in the application of the formula and does not guarantee the results thereof".

(iv) The provision of know-how must be distinguished from the "provision of services, in which one of the parties undertakes to use customary skills of his calling to execute work himself for the other party".

Viewed from the above perspective and development of law on the subject, both the AO and DRP have correctly applied the law to the facts of the present case. The secrecy & confidentiality clause in the agreement under which the supply of drawings, designs,

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etc., was made cannot justify the assesseeôs claim of it being an óoutrightô sale of goods. By the transfer of drawings, designs, engineering information, etc. the recipient was enabled to ensure the operation and maintenance of the plant set up and the manufacturing process of the plant. The recipient was enabled to use or was imparted with the information concerning industrial, commercial or scientific experience through the said transfer. This would necessarily bring the payment within the ambit of ñ*royalty*ò in terms of clause (iv) of Explanation 2 to section 9(1)(vi) of the Act as well as Article 12(3) of the India-German DTAA. In the case of CIT vs. Klayman Procelains Ltd. [1998] 96 Taxman 221 (AP), the Hon'ble Andhra Pradesh High Court held that *"... if the amount in question had been paid by the Indian company to the non-resident company for imparting of any information concerning the working of or the use of patent, invention, model, design, secret formula or process or trademark or similar property or if it was paid for imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill, the amount would fall within the meaning of* 'royalty*',* as defined in Explanation 2 of section 9(12). This is a question of fact to be determined on the facts and circumstances of each case and the terms of agreement under which there has been a transferò [emphasis supplied]. In the present case, the supply of drawings, designs, engineering documents, etc., clearly fall within the ambit of the expression ñfor imparting of any information concerning industrial, commercial or scientific experienceò which is clearly stipulated in clause (iv) of Explanation 2 of section (1)(vi) of the Act as well as in Article 12(3) of the India-Germany DTAA.

10. We have heard rival submissions and gone through facts and circumstances of the case. We find from the facts of the case that the designing, procurement of material, fabrication and manufacturing of equipment was undertaken outside India. From the facts of the case it is clear that the Company is not involved in the manufacturing of equipment and such equipment were sourced from third party vendors based outside India. From the agreements and documents it is clear that the equipment was directly sold by the assessee on export sale basis and the title/ownership in the equipment was transferred outside India i.e. before the equipment reached India. Even the consideration/payment for sale of equipment was received outside India in foreign

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currency and majority of the payment (80% - 85% including 10% advance) for each and every part of shipment becomes payable upon delivery of equipment on FOB foreign port of shipment once shipping and other documents are send to the customer. Such payments are made through irrevocable letter of credit. From the documents and evidences it is very much clear that the buyers were the Indian customers who were independent and unrelated parties and purchased the equipment from the assessee on their own account. From the agreements it can be gathered that the contracts for the sale of equipment were concluded on a óprincipal to principalô basis. Under the contracts, customersô inspection of the equipment was to be taken place outside India and assessee did not have any office or place of business in India. We have gone through judgments relied upon by assessee, wherein it has been decided that the income from offshore sale of equipment is not taxable in India. The case law of Hon'ble Supreme Court in the case of Ishikawajma-Harima Heavy Industries Ltd.(supra), wherein dealing with the case of a Japanese Company, one of the similar issues that was whether the amounts received/receivable by the assessee a foreign company, for the off-shore supply of equipment and materials to an Indian Company was liable to be taxed in India under the provisions of the Act or the India-Japan Tax Treaty. That was a case wherein break-up of contract price for each of the segments i.e. for supply, services and construction and erection were separately given in the Agreement. In that connection, the Hon'ble Supreme Court held, on pages no 430 and 444 of the report, as under:

> *"... It is not in dispute the title in the equipment supplied was to stand transferred upon delivery thereof outside India on high-sea basis as provided for in Art. 22.1 Similarly, Art. 13.1 provides for a lump sum contract price, whereas Art. 13.3.2 specifically refers to the cost of offshore supplies." P. 430)*
>
> *...The entire transaction having been completed on the high-seas, the profits on sale did not arise in India as has been contended by the appellant. Thus, having been excluded from the scope of taxation under the Act, the application of the double taxation treaty would not arise..." (p. 444)*

In another case cited by assessee i.e. Hon'ble Supreme Court in the case of CIT and Anr V Hyundai Heavy Industries Co. Ltd. (2007) 291 ITR 482(SC)in which the assessee, a non-resident foreign company incorporated in South Korea had entered into an agreement with ONGC for designing, fabricating, hook-up and commissioning of South Bassein Field Central Complex Facilities in Bombay High. The contract was in two parts, one was for fabrication of the platform and the other was installation and

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commissioning of the said platform in South Bassein Field. Here the issue under consideration was, *whether the profits from Korean operations that arose outside India can be taxed in India.* The Hon'ble Supreme Court, on page no 492 of the report, held as under:

> *"On reading Article 7 of the CADIT, it is clear that the said Article is based on OECD Model Convention. Para (1) of the Article 7 states the general rule that business profits of an enterprise of one Contracting State may not be taxed by the other Contracting State unless the enterprise caries on its business in the Other Contracting State through its PE. The said para (1) further lays down hat only so much of the profits attributable to the PE s taxable. Para (1) of Article 7 further lays down that the attributable profit can be determined by the apportionment of the total profits of the assessee to its various part OR on the basis of an assumption that the PE is a distinct and separate enterprise having its own profits and distinct from GE. Applying the above test to the facts of the present case, we find that profits earned by the Korean GE on supplies of fabricated platforms cannot be made attributable to its Indian PE as the installation PE came into existence only after the transaction stood materialized. The installation PE came into existence only on conclusion of the transaction giving rise to the supplies of the fabricated platforms. The Installation PE emerged only after the contract with ONGC stood concluded. It emerged only after the fabricated platform was delivered in Korea to the Agents of ONGC. Therefore, the profits on such supplies of fabricated platforms cannot be said to be attributable to the PE. There is one more reason for coming to the aforestated conclusion.* ***In terms of para (1) of Article 7, the profits to be taxed in the source country were not the real profits but hypothetical profits which the PE would have earned if it was wholly independent of the GE. Therefore, even if we assume that the supplies were necessary for the purposes of installation (activity of the PE in India) and even if we assume that the supplies were an integral part, will no part of profits on such supplies can be attributed to the independent PE unless it is established by the Department that the supplies were not at arm's length price. No such taxability can arise in the present case as the sales were directly billed to the Indian Customer (ONGC). No such taxability can also arise in the present case assessee there was no allegation made by the Department that the price at which billing was done for the supplies included any element for services rendered by the PE. In the light of our above discussion, we are of the view that the profits that accrued to the Korean GE for the Korean operations were not taxable in India****."*

11. Dealing with the case of taxability of equipment in the case of non- resident company, in the above judgment the Hon'ble Delhi High Court in the case of DIT Vs. Ericsson A.B. New Delhi (2012) 343 ITR 470 (Del) held that since the transaction relates to the sale of goods, the relevant factor and determinative factor would be as to where the property in goods passes. Since the goods were manufactured outside India and even the sale has taken place outside India, it was held by the Hon'ble High Court that the sale of equipment is not taxable in India despite the fact that the clauses relating to acceptance tests were mentioned in the contract. Similar observation were also made by the Delhi High Court in the recent case of DIT Vs. M/s Nokia Network OY (2012) 253 CTR 417 (Del.) and DIT Vs. LG Cable Ltd. (2011) 237 CTR 438 (Del.). In the case of LG Cable Ltd. (Supra), a Korean company entered into two contracts with Power

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Grid Corporation of India Limited (ñPGCILò) in connection with the supply and installation of ñFibre Optic Cablesò in India. One contract was for onshore execution, installation and erection of the cables (ñOnshore Supplyò) and the second contract was for offshore supply of equipment and related services (ñOffshore Supplyò). In order to facilitate the Onshore Supply, the tax payer set up a project office in India. Dealing with the issue as to whether the two contracts (Offshore Supply and Onshore Supply) could have been regarded as a single composite contract and the consideration for offshore supply of equipment was attributable to India, the Hon'ble Delhi Court a page no. 462 and 463 of the report, held as under:-

> *"In the final analysis we have no hesitation in holding that viewed from any angle, the fact situation in the instant case is almost identical to that in the case of Ishikawajma (supra) and the law as enunciated by the Supreme Court in the said case will squarely apply to the facts of the present case. If at all there is a difference, the facts in the present case stand on a better footing than in Ishikawajma (supra). In Ishikawajma (supra) there was a turnkey contract with four separate component activities turnkey contract with four separate component activities, viz., offshore supply, offshore services, onshore supply and onshore services awarded by Petronet LNG to a consortium of companies led by the Japanese company Ishikawajma-Harsima. In the instant case there are two separate contracts i.e., offshore supply and the onshore services contract awarded by the PGCIL to the respondent-assessee. As in the said case the considerations for offshore contract and onshore contract are separate and distinct from each other, inasmuch as the consideration in the case of offshore supply contract was received outside India through the mechanism of a letter of credit in foreign exchange while the consideration for onshore contract was receive, for the most in Indian rupees with a nominal amount in foreign currency, the latter being for training charges. The title to the equipment supplied from outside India was transferred in favour of PGCI outside India. In the assessee of Ishikawajma (supra), it was transferred on the high seas but in the instant case, it was transferred in the country of origin itself as soon as the goods were loaded upon the mode of transfer to be used to convey the plant and machinery, i.e., the shipping vessel, even prior to the goods reaching the high seas. Once the title was the transferred in the aforesaid manner, there was no provision either in the agreement or in law providing recourse to the respondents to take back the title.*
>
> *36. With regard to the setting up of PE also, the PE of the respondent in the instant case, as in the case of Ishikawajma (supra), had no role to play in the execution of the offshore supply contract and as a matter of act was set up for the sole purpose of enabling the performance of the onshore services contract.*
>
> *The contract, however, in the instant case as in the case of Ishikawajma (supra) would be said to have been successfully performed only after the satisfactory commissioning and erection of the plant and equipments. Since the PE was not at all involved in the transaction of the offshore supply of equipment, the existence of the PE [which has held in Ishikawajma (supra) is for the purpose of assessment of income of a nonresident under the DTAAI], would be irrelevant in the instant case. Clause (a) of Expln. 1 to s. 9(1)(i) would not be attracted at all which provides that in the case of a business where all operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India. In the instant case there was no operation* qua *the*

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agreement for supply of equipment, which was carried but in India, and therefore, no income could be deemed to have accrued or arisen in India whether directly or indirectly or through any business connection in India."

12. The Authority for Advance Ruling (AAR in short)in the case of Joint Stock Company Foreign Economic Association ñTechnopromexportò, In re. (2010) 322 ITR 409(AAR) discussed the issue that the assessee, a Russian Company, entered into three contracts, namely, (i) offshore supply contract; (ii) onshore supply contract; and (iii) onshore services contract, with NTPC. An issue similar to assesseeôs case arose for consideration before Authority for Advance Ruling (ñAARò) that whether the consideration from offshore supply of all plant and machinery can be taxed in India under the provisions of the Act and India-Russia Tax Treaty. The AAR while deciding the case in favour of the assessee, at page **no. 420** of the report held as under:

"In view of our above analysis, perusal of documents and case laws, we find that no portion of consideration is received by the applicant in India. Further, no income accrues or arises in India to the applicant as all the transactions took place outside India. The materials were shipped outside India, the title and property passed outside India (on high seas) and the payment was received outside India and therefore the applicant is not liable to pay income-tax in India.

In view of our discussion, it is ruled that the applicant is not liable to pay tax under the provisions of the IT Act read with India-Russia DTAA in respect of the amount received from the NTPC for execution of offshore supply contract and we therefore answer the question in the negative."

Further the AAR in the case of Hyosung Corpn. In re (AAR) (2009) 314 ITR 343 dealing with the issue similar to the one which is involved in the case of assessee i.e. as to whether the offshore supply of equipment, materials etc., were liable to tax under the provisions of the Act and India-Korea Tax Treaty, the AAR, on page no. 359 of the report, held as under:*"Thus, viewed from any angle, the title to ad property in the goods shipped by the applicant at the foreign port stood transferred at the port of shipment or while the goods were on high-seas. The event of sale took place clearly outside the territory of India. The income arising out of such sale cannot be said to have accrued or arisen in India. The accrual of income derived from the sale price of the off-shore supplies cannot be attributed to any operation in India. It is not possible to accept the contention of the Revenue that the transfer of title/property in the goods must be deemed to have taken place in India or testing and successful commissioning of the project cannot be upheld…*

In a recent case, the ITAT Delhi Bench-I had an occasion to consider the same issue in relation to the contract between Power Grid and another Korean Company. The learned Members of the Tribunal, after a thorough discussion held that in view of the decision of the Supreme Court in Ishikawajima, the receipts from offshore supply contract cannot be

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taxed under the Income-tax Act and that a percentage of income cannot be subjected to tax by reason of the fact that certain operations – post-supply of goods, took place in India…

As the onshore erection contract was separate in that case and the income attributable to those operations in India was offered to tax, that decision does not apply in all fours to the present case. But, to the extent 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."

13. Further, the coordinate bench of this Tribunal in the case of DCIT Vs. Roxon Oy (2007) 291 ITR (AT) 275 (Mum.) discussed that this case relates to a Finland entity, having a PE in India. The Finnish entity was awarded a turnkey contract by Nava Seva Port Trust (NSPT) to design, manufacture, deliver, erect, test and commission, certain bulk-handing facility. As per the terms of the contact, the taxpayer entity supplied the required equipment from outside India and sent its employees for erection, commissioning and training purposes. In this case, while dealing with the taxability of equipment supplied from outside India, it was held that the direct sale of equipment by the Finnish entity from outside India to the Indian customers is not taxable in India. The Mumbai Bench of this Tribunal, at **page no 291** of the report, held as under:

*"…As per art 7(2) profits attributable to a PE are the profits "*which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a PE*". Thus, the profits of the PE are to be calculated as if the PE is hypothetically independent of the enterprise of which it is a PE. The profits to be taxed in the source country are thus not the real profits made by the enterprise but hypothetical profits which the PE would have earned if it was wholly independent of the enterprise of which it is PE. Therefore, even if it is assumed that the supplies were necessary for the purpose of the activities of the PE and were integral part of the activities thereof, unless I is established at the supplies were not at an arm's length price to the PE no part of profits on such supplies can be treated as attributable to the PE. The arm's length price is best indicated by the price at which enterprise is selling the same to the customer. The hypothetical sale to and the hypothetical sale by the PE being at the same price, there cannot be any profits on account of the transaction. No such taxability can, therefore, arise in the case before us because the sales are directly billed to the Indian customer and also because there is no suggestion that the prices at which billing is done includes any element for services rendered by the PE…"*

In view of the above facts and circumstances of the case, it is clear that no portion of receipts from sale of equipment can be taxed in India both under the provisions of the Act and DTAA since all the activities relating to designing, fabrication and manufacturing took place outside India, the sale of equipment also took place outside India on principal to principal basis, Indian customers were independent parties who made purchases on their own account and hence, the transaction was at

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armôs length and the consideration was also received outside India in foreign currency. As mentioned above, even the ITSC has accepted these facts for Financial Years 2007-08 and 2008-09 and has held that income from sale of equipment in the case of assessee is not liable to tax in India. One pertinent facts is required to be discussed here that as to why attribution of profits from sale of equipment should not be made, since the assessee has admitted a supervisory PE in India under Article 5(2)(i) of the DTAA and the conclusion of sale is subject to various acceptance tests and the contracts also envisages that certain payment would be payable upon successful completion of those tests and there are clauses for liquidated damages if performance guarantee parameters are not being met. Now, we have to examine the acceptance tests referred by assessee to contend that the sale has taken place in India are the integrated cold tests, performance tests etc conducted at the customer site in India. Before advancing the argument as to how such tests by any stretch of imagination cannot be construed to mean that the sale has taken place in India, the assessee placed the clauses relating to such acceptance tests for TKPO project, which reads as under:-

"Clauses relating to acceptance tests

Schedule 6 … …

"16.0 COLD TESTS, INTEGRATED COLD TEST AND START UP

… … …

16.5 The Purchaser shall promptly issue the Integrated Cold Test Certificate upon successful completion of Integrated Cold Tests.

17. PROVISIONAL ACCEPTANCE

… … … … … …

17.7 On the satisfactory completion of the performance test and on signing of the Completion protocol between the purchaser and the Contractor, the Purchaser will promptly issue a Provisional Acceptance Certificate for the plant … … … ..

Schedule 4
Terms of Payment

… … … …

4.1.5 5% of Contract Price for the imported Equipment along with related designs and drawings will be payable on satisfactory completion of Integrated Cold Test… …

4.1.6 5% of Contract Price for the imported Equipment along with related designs and drawings will be payable after the issue of Provisional Acceptance Certificate…

4.1.6 The last 5% of the Contract Price for the imported Equipment along with related designs and drawings will be payable after the issue of Final Acceptance certificate."

3.4 Limited Damages for Non-fulfillment of the Performance Guarantee parameters. The total liquidated damages (LD) for non-fulfillment of the Performance Guarantee

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parameters/values as defined below for the reasons not attributable to the Purchaser, is limited to 35% of Contract Price…."

14. From the above the above clauses (clauses 16 and 17) relating to acceptance tests are part of normal commercial arrangements generally agreed in common trade parlance and partake the character of trade warranties. Besides, on delivery of equipment on a foreign port, generally 85% (including advance payment) of the total contract price for each and every part of shipment becomes due to the assessee from the customer and merely 15% of contract price is receivable by the assessee upon completion of the above mentioned tests as evident from clauses of Schedule 4. Further, in case these tests were not successful Tata Steel becomes entitled to claim liquidated damages from their assessee upto 35% of contract price. Accordingly, this 15% payment is merely a deferred payment and the acceptance tests clauses mentioned under the contract are merely in the nature of warranty provisions and cannot be construed to mean that the acceptance of goods by the customer has taken place in India and any portion from sale of equipment can be taxed in India. Further, the act that deferred payment does not have any impact on the sale of goods is also supported by the relevant portion of definition of ñ***sale***ò mentioned under Section 2(g) of the Central Sales Tax Act, 1956, which provides as under:

"Sale" with its grammatical variations and cognate expressions, means any transfer of property in goods by one person to the another for cash or deferred payment or for any other valuable consideration and includes …. ….."

Similarly, the above clauses relating to liquidated damages (clause 3.4 of Schedule 3) clearly indicates that when the performance tests do not provide the desired output, the assessee is liable to pay liquidated damages. This is also a normal commercial arrangement agreed in common parlance in the industrial world. This cannot be construed to mean all the contracts should be clubbed together or that the title in equipment did not pass outside India. Reliance in this regard is placed on LG Cable Ltd. (supra). Under identical circumstances, Hon'ble Delhi High Court in LG Cable Ltd. (supra) held that income from offshore supply of equipment cannot be taxed in India despite the fact that such clauses existed in the agreement entered for such sale of equipment. In the connection of tests, Hon'ble Delhi High Court, at page no. 460 of the report, has held as under:-

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"29. Thus, the mere fact that 15% of the payment was to be retained by the PHCIL to be period 30 days after operational acceptance on erection and completion of the system cannot be construed to mean that the title in goods did not pass to the buyer in the contrary of origin.

30. Then again, in our considered opinion, undue importance cannot be attached to the fact that the agreement imposed in the assessee company the obligation to handover the equipment functionally completed. The obligation has rightly been construed by the Tribunal to be in the nature of a trade warranty….

"31. We may note also that the buyer's right to examine and repudiate the goods in law does not itself indicate that the property ion goods had not passed, as it is evident from the provisions of section 59 of the Sale of Goods Act, which read as under:-

> õ59. Remedy for breach of Warranty ï (1) Where there is a breach of warranty by the seller, or where the buyer elects or is compelled to treat any breach of a condition on the part of the seller as a breach of warranty, the buyer is not by reason only of such breach of warranty entitled to reject the goods, but he may ï
>
> (a) Set up against the seller the breach of warranty in diminution of extinction of the price; or
> (b) Sue the seller for damages for breach of warranty.

15. Reliance is also placed on the decision of special bench in the case of *Motorola Income. vs DCIT* (Del ITAT Special Bench) [(95 ITD 269)] wherein it was held by the Hon'ble Tribunal Special Bench, that income from offshore supply of equipment cannot be taxed in India despite the fact that such clauses existed in the agreement entered for such sale of equipment. The finding of the Hon'ble Tribunal was also confirmed by the Hon'ble Delhi High Court (343 ITR 470). This finding was again confirmed by the Hon'ble Delhi High Court in the case of *Director of Income Tax vs M/s Nokia Networks Oy* (253 CTR 417). Further, even in the case of *Addl. CIT vs. Skoda Export Praha* (172 ITR 358) (Andhra Pradesh High Court), the High Court that a mere provision in the agreement that assessee was to satisfy himself about the quality and standard of the machinery supplied in India would not mean that the sale has not taken place outside India. The relevant observation of the High Court on page 362 of the report is reproduced below:-

> *"There was a good amount of controversy as to whether the sale of machinery is an isolated and independent transaction or is a part of the business venture between the assessee and the non-resident. We do not think there is any room for such controversy. The sale of machinery, though completed outside India, was not an independent or isolated transaction. It was a part and parcel of the business venture, or business connection, between the assessee and the non-resident. The sale of machinery was in pursuance of and one of the things to be performed under and in pursuance of the agreement entered into between them. This is also the view expressed by a Bench of this Court in Bharat Heavy Plate and Vessels Ltd. vs*

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Additional, Commissioner of Income-tax (1979) 119 ITR 986. The same view is expressed in the subsequent decision in Skoda Export vs. Additional, Commissioner of Income-tax (1983) 143 ITR 452 (AP) as well.

*We may also mention that learned standing counsel for the Department challenged the finding of the Tribunal that the sale of machinery was completed outside India. According to him, the sale was completed only in India, inasmuch as the assessee was entitled to inspect and satisfy itself about the quality and standard of the machinery supplied. We do not see any substance in this contention. The various clauses in the agreement referred to above make it clear that the sale of machinery was F.O.B. European port, and the time of fulfillment of delivery was prescribed as the date of the bills of lading. The payment was also to be made outside India. The agreement further makes it clear that the insurance risk during the course of the journey was that of the assessee and it paid for the same : even the freight charges from the European port to the place of destination were paid by the assessee. Thus, judged from any angle, the sale of machinery, which are "***goods***" within the meaning of the Sale of Goods Act, was completely outside India. A mere provision in the agreement that the assessee is entitled to satisfy itself about the quality and standard of the machinery in India cannot, in the circumstances of this case, detract from the fundamental position that the sale took place outside India. In such a situation, one has to apply the test of predominance and decide where the sale took place? On a combined reading of the clauses of the agreement, we have no doubt that the sale of machinery did take place outside India."*

16. Dealing with the similar issue of performance guarantee tests in the case of a Korean company wherein 10% of the contract price of the offshore equipment was payable on successful completion of erection, testing and commissioning, it was held that the off-shore sale of equipment is not taxable in India. In this regard, the AAR in the case of Hyosung Corpn., In re (supra), on page no 359 of the report, has held as under:

"Thus, viewed from any angle, the title to and property in the goods shipped by the applicant at the foreign port stood transferred at the port of shipment or while the goods were on high-seas. The event of sale took place clearly outside the territory of India. The income arising out of such sale cannot be said to have accrued or arisen in India. The accrual of income derived from the sale price of the off-shore supplies cannot be attributed to any operation in India. It is not possible to accept the contention of the Revenue that the transfer of title/property in the goods must be deemed to have taken place in India on testing and successful commissioning of the project cannot be upheld…."

From the above observations of Delhi High Court, Tribunal and AAR, it is clear that the acceptance tests are merely in the nature of warranty provisions. Further, the observation of Delhi High Court also clarify that breach of warranty could result in payment of damages and does not by itself mean the property/title in the goods did not pass to buyer outside India. Accordingly, the clause of acceptance tests and liquidated damages are nothing but merely in the nature of warranty provision and

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its remedial measures. Hence, undue importance cannot be given to such clauses and the same cannot be construed to mean that any portion from the sale of equipment can be taxed in India. The fact that the acceptance test would not have any impact on the transfer of title has also been agreed and accepted by the ITSC in the order passed for Financial Years 2007-08 and 2008-09.

17. Further, the alternative plea of the assessee that the acceptance tests would not have any impact on conclusion of sale in India and hence no attribution can be made to the supervisory PE on this account, the assessee argued that in case of supervisory PE only the income arising on account of supervisory activities can be taxed in India since the PE has been constituted merely on account of rendition of supervisory services under Article 5(2)(i) of the DTAA which provides that *"The term "permanent establishment: includes especially, - (i) a building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities continue for a period exceeding six months."*. The entire value of the invoices raised by the assessee on the rendition of supervisory services during the year under consideration (for which a supervisory PE has been constituted) has already been offered to tax at the net profit rate of 17.93% and therefore, no further attribution is warranted. As far as sale of equipment is concerned, no PE of the assessee is constituted in India for any of the projects and hence there cannot be any question of attribution of profits to PE for sale of equipment. This position has also been accepted by the ITSC in the order passed for Financial Years 2007-08 and 2008-09. The relevant observation of the ITSC is reproduced below:

> *"…With regard to the attribution of profits from sale of equipment to the supervisory PE, we find force in the contention of the applicant and are of the view that since the said PE has been constituted merely on account of rendition of supervisory services, there is no question of any attribution of profits arising from sale of equipment being made to the said PE. This observation has also been made by the Supreme Court in the case of Hyundai Industries (supra). In this regard, the Supreme Court on page number 493 of the report held as under:*
>
> > *'…In terms of para (1) of Article 7, the profits to be taxed in the source country were not the real profits but hypothetical profits which the PE would have earned if it was wholly independent of the GE. Therefore, even if we assume that the supplies were necessary for the purposes of installation (activity of the PE in India) and even if we assume that the supplies were an integral part, still no part of profits on such supplies can be attributed to the*

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independent PE unless it is established by the Department that the supplies were not at arm's length price. No such taxability can arise in the present case as the sales were directly billed to the Indian Cu9stoemer (ONGC)…'

18. Further, majority of the projects the assessee does not have a supervisory PE in India under Article 5(2)(i) of the DTAA since the said work has been awarded by the customer to Outotec (India) Private Limited and in some projects the supervisory services have not commenced till the end of Financial Year. Since there is no supervisory PE in India for the said projects, the question of any attribution being made for supply of equipment to the supervisory PE does not all. The fact that the PE under the DTAA has to be determined separately for each of the project is clearly evident from the wording of Article 5(2)(i) of the DTAA which reads as under:-

'The term "permanent establishment" includes especially, - (i) a building site ors construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities continue for a period exceeding six months.'

The word ñsuch project, project or activitiesò mentioned under Article 5(2)(i) of India-Germany DTAA clearly indicates that the supervisory PE has to be examined separately for each of the project. The above legal position has also been confirmed by the Mumbai. This position has also been affirmed by the Mumbai Tribunal in the case of *M/s Krupp Udhe GmbH vs Addl. CIT* (28 SOT 254), which is also based on India-Germany DTAA. In this regard, the Mumbai Tribunal has held as under:-

"24. We have gone through the various treaties referred to by the learned counsel for the assessee. The perusal of such treaties shows that whenever the contracting parties intended that different sites should be taken together, they had expressly provided so. For example, in the Indo-Denmark Treaty, Article 5(2)(k) provides as under:

óArticle 5: Permanent Establishment:-

1. *…. … ..*
2. *The term 'permanent establishment' includes especially:*
   a) to j)… …
   k) a building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities (together with other such sites, projects or activities, if any) continue for a period of 183 days or more.
   (Since Sub-clauses a to j *are not relevant, the same are not reproduced above)'*
   Similar provisions have been made in Article 5 of the various treaties entered into by India width China, USA, Canada Italy etc., It is pertinent to note that Indo-German treaty came into existence vide notification dated 29.11.96 while the other treaties mentioned above

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(except Canada) were in existence period to 29.11.96. Hence it is clear beyond doubt that India was aware of such provisions while drafting Indo-German treaty. Therefore, it appears to us that contracting parties deliberately deviated from such provisions by not including the words 'together with other such sited, projects or activities.' Accordingly, it cannot be said that other sites can also be taken together for determining the scope of PE in India.

25. We have also gone through the commentary (Third Edition) be Klause Vogel. At each Page 308, it is said 'the rule is that a minimum period should be determined for each building, site or construction or installation project concerned (Cour d' Appeal Anvers 25 ET 224, 225 (1985): DTR Belgium/Netherlands). The question whether there is PE n a specific contracting state or not should be considered separately for each business activity performed in that state i.e. for each individual place of business existing there as well (Hoge Road, Rol no. 16305, BNB 197/71 : DTC German/Netherlands)'.

26. In this connection, it would also be useful to refer to para 31.4 at page 115 of the book 'Principles of International Taxation' which is reproduced as under:

> õ31.4 The time set applies to each individual site or project. No account should be taken of the time spent by the contractor concerned on other sites that are totally unconnected with the tested site. On the other hand, a site should be regarded as a singe unit, even if it is based on several contracts, provided that it forms a coherent whole, commercially and geographically.ô

27. We may also refer to the decision of the co-ordinate Bench in the case of Sumitumo Corporation (supra) wherein it has been held that could be different PE's with reference to different unconnected contracts even though each contracts may be entered into by the same parties. In that case, MarutiUdyog Limited awarded various supervisory contracts on Sumitumo Corporation which were to be executed independently at different sites in the factory of MarutiUdyog Ltd., Since there was no effective connection between such contracts, it was held that minimum period of 130 days was to be separately for each contract and could not be aggregated."

28. In view of the above discussion, it is held that in computing the minimum period of 6 months, various sites cannot be considered together particularly when different contracts had no effective interconnection with each other. In the present case, the assessee had entered into various contracts with various parties in respect of various independent projects located at different places. Hence, the lower authorities were not justified in considering the various sites together while computing the minimum period of six months prescribed in Article 5(2)(i) of the DTAA."

19. In view of the above facts and legal position, we are of the view that the sale of equipment is concluded outside India because all work relating to manufacturing, designing, fabrication etc. of equipment is done outside India and sold to the assessee directly on export sale basis. The contract provides for delivery of equipment on FOB Foreign Port of Shipment majority of payments i.e. 80-85% for

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each and every part of shipment becomes payable upon delivery of equipment on FOB foreign Port of Shipment the above payments are through irrevocable letter of credit which makes it clear that even if the ship does not sail or deliver the goods to the destination, the assessee receives payment out of Letter of Credit guaranteed by bank upon FOB delivery. Even the customerôs inspection for equipment is outside India. The buyers were Indian customers and unrelated parties and purchased equipment from assessee on their own account. Moreover, sale was on principal to principal basis and at armôs length. The assessee entered into either separate contracts each with its own scope of supply or service with separate consideration or single contract with separate scope of supply and services as well as separate consideration. The findings of DRP and that of the AO that the contracts are single contract split into separate parts is not correct. Even if the contract is considered to be integrated one, then also the taxability of each of the component has to be determined separately based on the decision of Hon'ble Supreme Court in the case of Ishikawajma-Harima Heavy Industries Ltd., supra. Further, the reliance placed by DRP on the case of AAR of Alstom Transport SA, supra to hold that the contract for installation and commissioning of a project cannot be split up into separate parts as consisting of independent supply of goods and for installation at the work site. For reaching to the above conclusion AAR relied on the decision of Linde AG of AAR but the decision of AAR in the case of Linde AG was overruled by Hon'ble Delhi High Court, which is cited supra. The acceptance tests are merely in the nature of warranty provisions for the reason that only 15% of the payment is receivable by the assessee on completion of various tests. In case these tests are unsuccessful Tata Steel or the party concerned can claim liquidated damages not exceeding 35% of the contract price. Accordingly, the clause of acceptance tests is merely in the nature of warranty provisions. Even the reliance placed by AO on various clauses of Sales of Goods Act is misplaced. Since the Hon'ble Delhi High Court in the case of LG Cables Ltd., supra after considering the provisions of Sales of Goods Act held that such acceptance tests are merely in the nature of warranty provisions. Even there is no PE for sale of equipment in view of the decision of Hon'ble Supreme Court in the case of Hyundai Heavy Industries, supra and in addition to this, there is no concept called sale PE under DTAA. In light of the facts

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and legal position, we hold that the profit arising to the assessee from sale of equipment is not taxable in India. This issue of assesseeôs appeal is allowed.

20. The next issue in this appeal of the assessee is against the order of DRP and that of the AO in assessing the income from supervisory services. For this, assessee has raised following grounds:

> *"Income from Supervisory Services*
> *3(a) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in ignoring the net profit rate of 17.93% on gross revenue based on the average margin of comparable companies as considered by the appellant for computing the taxable income from supervisory services in India without showing any cogent reason.*
> *3(b) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in considering the net profit rate of 27.5% for computing the taxable income from supervisory services in India which is excessive."*

21. Briefly stated facts are that the assessee had provided supervisory services in India during the relevant year and earlier years also. The assessee was merely engaged by its customers for supervising the detailed engineering, installation and commissioning activity undertaken independently by the customer/third party vendors appointed by the customers. The assessee before ITSC during FY 2007-08 and 2008-09 admitted that it has supervisory PE in India for supervisory services rendered on standalone basis. The assessee for the purpose of computation of profit for the assessment year under consideration computed the average profit margin earned by the comparable Indian Companies, which worked out to 17.93% of sales. The assessee, therefore, attributed profits of INR 1,85,60,360/- to the supervisory PE which was computed by applying a net profit rate of 17.93% on gross revenue of INR 10,35,15,673/- earned from supervisory services. The assessee before AO and DRP submitted that during the proceedings before the ITSC for the earlier assessment years the assessee disclosed a profit percentage of 25% on its revenue from the supervisory services. The ITSC enhanced the same to 27.5% for the relevant years. However, for those previous assessment years the assessee did not have the details relating to the net profit earned by comparable India companies. During the current year, based on the profitability of the comparable Indian companies a net profit percentage of 17.93% was arrived at and considered by the assessee. However, the AO has completely disregarded such comparable companies and has merely applied the net profit percentage of 27.5% as adjudicated

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by the ITSC for Financial Years 2007-08 and 2008-09. Thus, rejection of the net profit percentage of 17.93% by the AO is not correct and is bad in law. In addition to the above, it is argued that the net profit rate of 27.5% as considered by the AO is excessive for the relevant year and thus not acceptable to the assessee. Aggrieve, assessee preferred appeal before Tribunal.

22. We have heard rival contentions and gone through facts and circumstances of the case. We find that DRP has decided this issue of taxability of income earned from supervisory services in India by the assessee and adopted the profit margins at 27.5% of profit attribution by relying on the decision of the ITSC for FY 2007-08 and 2008-09 by observing as under:

> *"The AO has relied on the order of the ITSC for the FY 2007-08 and 2008-09 wherein a profit percentage of 27.5% of gross revenue was determined supervisory services. The AO has concluded that the facts for the current year were similar to the aforesaid two years and thus considered it reasonable to apply a profit percentage of 27.5% on the income earned by the assessee from providing supervisory services.*
>
> *The assessee contended that the profit percentage of 17.93% is based on the margins earned by the similar Indian comparable companies. The AO cannot simply reject the same without showing any basis. The attribution before the ITSC cannot be considered as binding for the subsequent years and this fact has also been stated by the Ld. AO while dealing with the taxability for sale of equipment. Thus reference by the AO of proceedings before ITSC is not relevant and is contradictory to his own stand. Such decision of ITSC was accepted merely to buy peace and to avoid protracted litigation with the Income Tax Department for those years and a letter to this effect was also filed with the AO.*
>
> *The assessee's main contention is to examine the profit rate independently on the basis of comparable margins of Indian companies which it had furnished rather than relying on settlement commission order.*
>
> *There is no dispute that the assessee has a supervisory PE in India. Above all, after admitting income on its own, in the return of income (outside the purview of ITSC), the assessee cannot take any new ground on the issue of PE.*
>
> *The only issue is what profit percentage can be attributed to such activity in the absence of any books of account maintained by the assessee. In the absence of books of account the Assessing Officer has rightly resorted to invoke the Rule 10 of the IT Rules. However, whether this power of the AO is absolute? Merely because no books of account are maintained, whether the opinion of the AO's reliance on ITSC is order is final? From the order, this panel has found that the AO maintained that there is no change in the facts in the present year as that of from the FY 2007-08 and 2008-09, and hence the assessee's own submission before the ITSC is considered to arrive at the profit rate of 27.5%*
>
> *We find no infirmity in the order of the AO it is not correct to say that assessee admitted 27.5% profit before the Settlement Commission. The assessee admitted*

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25% profit before the ITSC. After considering overall circumstances and the facts, the ITSC held that 27.5% profit attribution can be made. The mere mentioning of profit margins of some Indian Companies par se will not justify the profit margin admitted by the assessee. The assessee is in the business of rendering of supervisory services which are highly technical in nature. These services are specific to the high end metal industry where plant works with crores of rupees have been executed. Thus comparing these highly skilled specific services with normal supervisory services is not correct. Before us also the assessee could not demonstrate the functional similarity of services of the comparable companies so as to consider the comparability and accept the profit margin.

In view of the above we upheld the profit margin adopted by the AO and reject the objection of the assessee on the issue of profit margin on supervisory services."

23. Before us the assessee contended that it has computed the profit percentage at 17.93% based on margins earned by similar Indian comparable companies. The DRP as well as AO in its orders has mentioned that profit margins of some Indian companies, per se, will not justify the profit margins admitted by assessee as the assessee failed to demonstrate the functional similarity of the services of the comparable companies. The assessee contended that the comparable companies relied on by the assessee are involved in the business of engineering and technical services and such comparable companies have been rightly relied upon by assessee in order to arrive at the net profit margin of 17.93% on gross revenue earned from supervisory services. It was contended that the final order of the ITSC for FY 2007-08 and 2008-09, the margins of comparable companies was not a basis before the ITSC and hence, the ITSC did not had an occasion to analyse the same. It was contended that the decision of ITSC was accepted to buy peace and to avoid protracted litigation with the revenue. We find that even now before us the assessee could not file any reason to deviate from the decision of the ITSC wherein the profit margins were rightly applied at 27.5%. Hence, this issue of assesseeôs appeal is dismissed.

24. Sh. Vijay Kumar Ld. CIT-Dr stated facts and made argument that the assessee reported to have earned gross revenue from supervisory services amounting to Rs.10,35,15,673/- out of which Rs.1,85,60,360/-, being 17.93% of the gross revenue, was allocated to the Indian PE. In assessment, AO had enhanced this allocation to 27.50% which works out to Rs.2,84,66,810/-. The DRP also confirmed the action of the AO for the reason that on identical facts and circumstances, the

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ITSC attributed profits @ 27.50% in the assesseeôs own case for AYs 2008-09 and 2009-10 respectively. For the AYs 2008-09 & 2009-10 before the ITSC and now for AY 2010-11 before the AO, the assessee admitted to have PE in India to which the impugned supervisory services were effectively connected, but no books of accounts were maintained for the same. This was in clear violation of provisions of section 40AD of the Act. In such circumstances, the factual finding of the ITSC towards attribution of profits to the extent of 27.50% on the revenue earned from supervisory activities in India cannot be faulted with and for the very same reason, the action of the AO in attributing profits @ 27.50% was rightly confirmed by DRP. We also hold so. This issue of assesseeôs appeal is dismissed.

25. The next issue in this appeal of assessee is against the order of DRP and that of the AO in taxing income earned from supply of designs and drawings in India. For this, assessee has raised following grounds:

> *"4(a) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the income earned by the appellant from sale of designs and drawings is taxable as Royalty under Article 12(3) of the DTAA read with the provisions of Section 9(1)(vi) of the Act and is not in the nature of sale of product.*
>
> *4(b) On the facts and in the circumstances of the case and in law, Ld. DRP erred in holding that the income earned by the appellant from sale of designs and drawings is taxable as Royalty merely based on the conclusion of the Hon'ble Income Tax Settlement Commissioner (ITSC) in the past years ignoring that the conclusion of ITSC is not as per the provision of the law and the appellant has accepted the decision of Hon'ble ITSC merely to buy peace.*
>
> *4(c) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the sale of designs and drawings by the appellant as granting of license allowing the Indian customer to use it without appreciating the fact that the customers use these designs and drawings for internal purpose of setting up their plants and not for commercial exploitation.*
>
> *4(d) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that merely because the intellectual property in designs and drawings has not been transferred to the customer the nature of transaction will change from sale of goods to use of license."*

26. Brief facts relating to this issue are that the assessee provided drawings, designs & engineering documents relating to steel industry in India to the customers for the operation and maintenance of the plant. During the year under consideration, the assessee raised invoices to the tune of Rs.79,42,01,177/-. The DRP and the AO holds the income earned from supply of drawings and designs as taxable in India.

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The DRP for taxing the income earned from supply of drawing and designing observed as under:

"The AO in his draft assessment order after giving due consideration to the arguments of the assessee opined that the consideration received by the assessee is not a sale but Royalty under Article 12(3) of the DTAA as well as Explanation 2 to Section 9(1)((vi) of the IT Ac. The AO based his conclusion on the following reasons.

1. *The supply of design and drawing s does not pertain to any sale of goods but takes the characteristics of granting of a license allowing the Indian client to use it.*

2. *The AO has made reference to Design Act, 2000 and the decision in the case of The Wimco Limited vs Meena Match Industries (AIR 1983 Delhi 537) for reaching to the conclusion that the income constitute royalty.*

3. *The judgment of Hon'ble Supreme Court on Scientific Engineering [157 ITR 86] relied upon by the assessee deals with the capitalization of assets in the books of purchaser and has no applicability in the case of the assessee. Other judgments relied upon by the assessee are based on their own facts and are not applicable in assessee's case.*

The assessee contended before this panel that consideration received for sale of designs and drawings is not taxable for the following reasons.

1. *The basic engineering packages sold by the assessee to the Indian customers have been largely designed on the basis of standard technologies available with it. The consideration was therefore for the sale of a product which is embedded in the plant set up by the Indian customers and does not constitute royalty and is in the nature of business income. Since the work was done outside India and sale has taken place outside India, such income is not taxable under the provisions of the Act and DTAA. Sample copies of airway bills were also submitted to the AO to demonstrate that sale has taken place outside India.*

2. *Reliance is placed on the judicial precedents of Supreme Court in the case of Scientific Engineering House P. Ltd. vs. CIT (157 ITR 86) and Jaipur Tribunal in the case of Modern Threads (India) Ltd. vs CIT (69 ITD 115). Relevant part of the decision of Hon'ble Jaipur ITAT is reproduced herein below:*

'Having regard to the facts, material on records and ratio of various decisions(s) cited I come to the irresistible conclusion that the amount payable to Italian company for supply of technical know-how and basic process engineering documentation for setting of the plant in India for manufacturing of PTA is the business profit in the hands of Italian company and the Italian company having no permanent in India the same is taxable in Italy and not in India. The Revenue authorities are, therefore, not justified in taxing the said payments in India treating the same as royalty…'

3. *Retaining intellectual property in designs and drawings is similar in nature to the retaining of patented rights in any goods / machinery. Restriction on the intellectual property in designs and drawings sold by the assessee for the purpose of setting up a plant in India does not change the character of the transaction from the sale of the product to the use of license/know-how.*

4. *The mere fact that the word license has been used in the agreement would not make any difference in the taxability of the income.*

5. *Although Hon'ble ITSC has held the payment received by Design and Drawings as royalty in its order, the assessee does not agree with such decision of the ITSC. Such*

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decision of ITSC was accepted merely to buy peace and to avoid protracted litigation with the income tax department for those years and a letter to this effect was also filed with the AO. AO's reliance on Design Act, 2000 and the decision of The Wimco Limited vs. Meena Match Industries (AIR 1983 Delhi 537) are not relevant in the instant case since this is the case where designs and drawings have been sold to the Indian customers for the internal purpose of setting up plants and not for commercial exploitation.

We have carefully considered the arguments put forth by the assessee before us. Similar contentions have been made before the Hon'ble ITSC. The Hon'ble ITSC after an elaborate discussion held as under in its order dated 30-12-2011.

76. We have duly considered the reports, written submissions, paper books, documents etc. As well as arguments advance by both the sides and the entire facts of the case. We are of the view that the designs and drawings developed by the applicants are the result of specialized knowledge and information on wide range of technologies acquired after extensive R&D effort, and they are exclusively in the possession of the applicants. The copyright in such designs and drawings is vested and is retained by the applicants. The designs and drawings provided by the applicants to the Indian clients constitute an item in which the intellectual property is embedded. No proprietary rights in the designs and drawings have been transferred. In our considered opinion, the clients have only been given the 'right to use' the underlying technical knowledge, process and information which are exclusively in the position of the applicants and so the receipt by the applicant companies for such allowance of 'right to use' is the lump sum consideration received by the applicants. Thus providing these designs and drawings to the customers does not amount to sale of goods or copyrighted article. This was a license or specific authority to have the right to use on payment of a lump sum amount, and so the payment made for thee designs and drawings is in reality nothing but ***Royalty****. The concept of sale here, therefore, does not come at all. The compensation for such rights given to the customers has to be treated as royalty in terms of Section 9(1)(vi) Explanation 2 because under the agreement the applicant companies had granted license to the Indian companies to use the technical know-how for setting up the plants. It is also important to realize that the know-how was to remain exclusive property of the applicant companies and the Indian companies had to maintain secrecy of the know-how which could not be disclosed to other parties, and it could be re-used by them only after further payment to the applicant companies as per future separate agreements. The case laws relied upon by the Ld. AR do not specifically deal with such set of facts which are peculiar to the applicant's case, and are hence not applicable in the case of the applicants. The applicants' case is thus primarily covered by Explanation (2) of Section 9(1)(vi) of the IT Act, which define royalty.*
77. We have closely examined the TDS certificate filed before us by the Ld. AR and observe that some of the payments on which TDS has been deducted are on account of technical services. We further observe that the technical know-how provided by the applicants is so highly specialized that the clients have to heavily depend on the applicant's skill and expertise for setting up the plant and make it fully operational. Thus we have reason to believe that technical services in fact have also been provided to the Indian companies by the applicants, and the fees paid for the same are included in the consideration received by the applicants for making over the designs and drawings to the Indian customers. Keeping in view the facts of the case and taking an overall view, we estimate that 40% of the consideration is towards fees for technical services which is taxable under Section 9(1)(vi) of the IT Act.
78. Therefore we hold, that 60% of the payments received by both the applicants for making over the designs and drawings to the Indian customers are in the nature of royalty payments and balance 40% payments are fees for technical services. Further, as per the IT Act, as well as he respective DTAA; both kind of receipts are taxable @ 10%.

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The issue upheld by the ITSC is clear and this panel has no reason to differ on the issue of sale of design and drawings. Accordingly, this Panel is of the opinion that the drawing and designs are clearly 'right to use' but not in the nature of sale of goods as contended by the assessee.

Though the assessee submits that the decision of the ITSC is accepted to buy peace that itself cannot be a valid ground to defer with the ITSC view in the absence of any valid argument made before us. We also make it clear that the order of the AO is clear and the reasoning given by the ITSC on this issue is clear from any ambiguity. In view this we uphold the order of the AO and reject the assessee's objection."

Aggrieved, assessee preferred appeal before Tribunal against the orders of DRP and that of the AO.

27. Before us, the assessee explained this issue that the scope of the assessee was limited to designs and drawings being in the nature of basic engineering for which work was done primarily outside the territory of India. Basic engineering includes sale of designs and drawings to the customers that pertain to the location of plant, layout drawings, placement of various equipment, types of equipment to be installed, process description, manufacturing of indigenous equipment in India etc. that are needed as per specifications by the customers to erect the plant. The assessee has access to a wide range of technologies such as sinter plant technology, pellet plant technology etc that are required for the purpose of setting up/erection of plants. Such technologies are developed after undertaking various research and development activities. The designs and drawing are largely the products of the aforesaid technologies that are sold to its Indian customers after being modified, to meet their requirements. The modification activities have been performed by the assessee in its own country i.e. the entire work has been undertaken / performed outside India. The designs and drawings sold by the assessee were used by the Indian customers for internal business purpose of setting up of their plants and not for any commercial exploitation. Sale of designs and drawings has also effected outside India. Copies of the sample airway bills evidencing that the delivery of designs and drawings for various projects has taken place outside India is enclosed in assesseeôs paper book. Consideration/payments for the basic engineering work were received by the assessee outside the territory of India in foreign currency. All

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the contracts were net of tax contracts and the liability to pay taxes was on the Indian customers.

28. The relevant clauses of contracts for supply of imported designs and drawings for civil and structural work, utilities etc for Tata Steel Pellet project (ŏTata Pellet projectõ) are reproduced below:

Clauses relating to scope of work – Tata Pellet Project

"Schedule I
Article 1.1 SCOPE OF WORK FOR SUPPLY OF IMPORTED DESIGDNS AND DRAWINGS

In consideration of the payments to be made by the purchaser, the Contractor shall be responsible for supply on FOB basis of following imported designs and drawings as detailed in the Technical Specification. In the event of air transportation at the sole direction of the purchaser, "FOB port of shipment' shall be considered as FCA airport of dispatch.'
1.1.1 Supply of imported designs and drawing for civil and structural work, utility and other services, erection, start-up, commissioning and demonstration of performance tests for Pelletising Plant on FOOB port of shipment to be submitted by the Contractor..,

Article 1.1 SCOPE OF WORK FOR SUPPLY OF IMPRTED DESIGNS AND DRAWINGDS

Schedule 3
3.1 Delivery of imported designs and drawings
The delivery schedule of imported designs and drawings to be supplied by the Contractor as per Drawings and Document submission schedule is
given in the Technical Specifications
Engineering work shall be completed by the Contractor within Thirteen (13) months from the Contract Effectiveness Date in accordance with the agreed schedule"

In light of the above facts, it was explained by Ld. Counsel for the assessee that the basic engineering packages sold by the assessee company to the Indian customers have been designed largely on the basis of standard technologies available with it. The consideration received by the assessee was therefore for the sale of a product which is embedded in the plant set up by the Indian customers. Accordingly, the income earned from the sale of designs and drawings is in the nature of business income, being the consideration received from the sale of a product and no further income can be assessed.

29. Ld. CIT-DR Sh. Vijay Kumar argued that the taxability of the Contract for Supply of Equipment had been elaborately analysed both by the AO and DRP and

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the facts involved in the case and came to the concurrent finding that 10% of the sales revenue attributable to the Indian PE would be income assessable to tax in India. When the contract is for the erection and commissioning of the plant, the equipment may not remain as a property and the whole contract becomes a project for plant erection. It is the assessee whoop agreed to erect the plant and for the sake of convenience the terms of supply of equipment, designs, supervision, etc., were specified. Given the fact that the assessee had a PE in existence to undertake the project, it should have undertaken a robust transfer pricing methodology while allocating prices to different work segments and the supply for equipment should have been proved by the assessee to be at armôs length, which was evidently not done by the assessee. The DRP in its order at page 18 notes that ó*Thus the equipment is part of whole plant which consists of various designs, electrical and automated systems. Though the contract is split into parts, the completeness of the contract is achieved only after the successful testing of the plant. The works done by the assessee may include supply of material, equipment, drawings documents, guaranteeing the work. The responsibility of the assessee did not stop with the supply of the equipment and when the contract is for the work, the supply component need not be viewed separately*.ô As can be seen from the above, it was not a case of sale of equipment simplicitor, but it involves a host of services employed at the site level to complete the whole plant. Unless these services and other obligations at the site level are not separately compensated at armôs length, it cannot be said that the price paid for supply of equipment was at armôs length. A bare perusal of the contract documents would suggest that no separate remuneration or compensation for services like Cold Test, Integrated Cold Test, Start-up, local level training, performance test, etc., have been provided. This could be possible only if compensation for such services was actually embedded in the price set for the supply of equipment itself. In other words, a portion of profit having its *situs* in India at the plant site level always stood loaded in the supply of equipment which is now sought to be labeled as offshore supply not amenable to taxation in India. Therefore, the payment for the offshore supply needed to be segregated amongst the sale simplicitor and a host of other services performed at the plant site level till completion of the whole work. Clearly the onus was on the assessee which it had

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failed to discharge, no robust transfer pricing methodology or documentation was undertaken by the assessee in this regard. Therefore, the AO had taken the best recourse to rule 10 of the Income Tax Rules in order to attribute profits to the Indian PE at Rs.5,19,12,709/-, which was also confirmed by the DRP after giving cogent and justifiable reasons.

30. We have heard rival submissions and gone through facts and circumstances if the case. The facts mentioned above, clauses of contract and the sample copies of airway bill clearly indicate that the entire work relating to designs and drawings was done outside the territory of India; sale was affected outside India and the consideration was also received outside India in foreign currency. In view thereof and the detailed legal submission mentioned above with regard to income from sale of equipment, it is submitted that the business income earned by the assessee from the sale of designs and drawings is not liable to tax in India both under the provisions of the Act and DTAA. Now we have to consider the Judgments dealing with the non-taxability of sale of designs and drawings outside India as cited by Ld. Counsel for the assessee. Hon'ble Supreme Court in the case of Scientific Engineering House P. Ltd. Vs. CIT (SC) 157 ITR 86 dealing with the issue of whether the drawings, designs, charts, plants etc. constitute a plant and are entitled to depreciation, Hon'ble Supreme Court held in the affirmative case on **page no 97** of the report as under:

> *"Obviously, the purpose of rendering such documentation service by supplying these documents to the assessee was to enable it to undertake its trading activity of manufacturing the odolites and microscopes and there can be no doubt that these documents had a vital function to perform in the manufacture of these instruments; in fact it is with the aid of these complete and up-to-date sets of documents that the assessee was able to commence its manufacturing activity and these documents really formed the basis of the business of manufacturing the instruments in question. True, by themselves, these documents did not perform any mechanical operations or processes but that cannot militate against their being a plant since they were in a sense the basis tools of the assessee's trade having a fairly enduring utility, though owing to technological advances, they might or would in course of time become obsolete. We are, therefore, clearly of the view that the capital asset acquired by the assessee, namely, the technical know-how in the shape of drawings, designs, charts, plans, processing date and other literate falls within the definition of "plant" and is, therefore, a depreciable asset". (Emphasis supplied)*

Since the assessee supplied the designs and drawings for setting up plants in India, in light of the above judgment, such designs and drawings partake the character of a

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product and accordingly, it is clear that the income arising to the assessee is in the nature of business income.

31. A similar issue arose before Jaipur Bench of the ITAT in the case of Modern Threads (India) Limited V DCIT 69 ITD 115(Jp), wherein brief facts were that Modern Threads, an Indian company was interested in building in India a plant for the production of PTA. It, therefor, entered into an agreement with Tecnomint SPA., a tax resident of Italy entered for grant of rights and sub-license to use the ópprocess and technical know-howô for designing, construction and operation of the plant. The agreement, inter alia, provided for lump sum technical know-how fee of USD 250 lakhs and USD 50 laks for supply of basic process engineering documentation. The issue was whether the payment for the supply of technical know-how and basic process engineering documentation for designing, construction and operation of the plant could be taxed as óRoyaltyô or not? ITAT on **page no. 157** of the report held as under:

> *"Having regard to the facts, material on records and ratio of various decision(s) cited I come to the irresistible conclusion that the amount payable to Italian company for supply of technical know-how and basic process engineering documentation for setting of the plant in India for manufacturing of PTA is the business profit in the hands of Italian company and the Italian company having no permanent in India the same is taxable in Italy and not in India. The Revenue authorities are, therefore, not justified in taxing the said payments in India treating the same as royalty …." (Emphasis supplied)*

32. The revenue authorities has asked assessee to explain as to why the revenue sale of design and drawing made by the Company in the FY 2009-10 should be considered as non-taxable, where, as per the various contracts in respect of the above mentioned services, the ultimate ownership of the designs and drawings are never passed to the buyer, and only license to use the same is granted. In this way, the true nature of the receipts are Royalties under section 9(1)(vi) of the Income Tax Act, 1961 and Article 12 of India-Germany DTAA rather than Sale of designs and Drawings as a product. It was explained that the nature of retaining intellectual property in designs and drawings, due to which the ownership has never passed on to the buyer, is similar in nature to the retaining of patented rights in any goods / machinery. For example, if any customer purchases a car, in that case, the company

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does not transfer its patent or intellectual property to the buyer of the car but that does not change the nature of the transaction from sale of a product to use of a patent/intellectual property. Similarly, restriction on the intellectual property in designs and drawings sold by the assessee for the purpose of setting up a plant in India does not change the character of the transaction from the sale of the product to the use of license/know-how and the mere fact that the word license has been use in the agreement would not make any difference. The assessee explained that the design and drawings sold by it were used by the Indian customers for internal business purpose of setting up of their plants and not for any commercial exploitation. Accordingly, the designs and drawings sold by the assessee tantamount to the use of a ó*copyrighted article*ô rather than use of a ó***copyright***ô and is therefore in the nature of business income. Reliance in this regard is also placed on Commentary on Double Tax Conventions by Klaus Vogel. The relevant extract is reproduced below:

> *"....In a partial transfer of rights the consideration is likely to represent a royalty only in very limited circumstances. One such case is where the transferor is the author of the software (or has acquired from the author his rights of distribution and reproduction) and he has placed pat of his rights at the disposal of a third party to enable the latter to develop or exploit the software itself commercially for example by development and distribution of it ...."*
>
> *"the acquisition of the software will generally be for the personal or business use of the purchaser. The payment will then fall to be dealt with as commercial income in accordance with Article 7 or 14. It is of no relevance that the software is protected by copyright or that there may be restrictions on the use to which the purchaser can put it."(Emphasis supplied)*

33. Reliance in this regard is also placed on the various observations made in the Model convention of OECD 2010 on the Article 12 i.e. Royalties and Fee for Technical Services. The relevant paras are outlined below:

> *"131. Payments made for the acquisition of partial rights in the copyright (without the transfer or fully alienating the copyright rights) will represent a royalty where the consideration is for granting of rights to use the program in a manner that would without licence, constitute an infringement of copyright. Examples of such arrangements include licences to reproduce and distribute to the public software incorporating the copyrighted program, or to modify and publicly display the program. In these circumstances, the payments are for the right to use the copyright in the program (i.e. to exploit the rights that would otherwise be the sole prerogative of the copyright holder)....*
>
> *13. In other types of transactions, the rights acquired in relation to the copyright are limited to enable the user to operate the program, for example, where the transferee is granted limited rights to reproduce the program. This would be the common*

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situation in transactions for the acquisition of a program copy. The rights transferred in these cases are specific to the nature of computer programs. They allow the user to copy the program, for example on to the user's computer hard drive or for archival purposes. In this context, it is important to note that the protection afforded in relation to computer programs under copyright law may differ from country to country. In some countries the act of copying the program onto the hard drive or random access memory of a computer would, without a license, constitute a breach of copyright. However, the copyright laws of many countries automatically grant this right to the owner of the software which incorporates computer program. Regardless of whether this right is granted under the law or under a license agreement with the copyright holder, copying the program onto the computer's hard drive or random access memory or making an archival copy is an essential step in utilizing the program. Therefore, rights in relation to these acts of copying where they do n more than enable the effective operation of the program by the user, should be disregarded in analysing the character of the transaction for tax purposes. Payments in these types of transactions would be dealt with as commercial income in accordance with Article 7.

14.2 The method of transferring the computer program to the transferee is not relevant. For example it does not matter whether the transferee acquires a computer disk containing a copy of the program or directly receives a copy on the hard disk of her computer via a modem connection. It is also of relevance that there may be restriction on the use to which transferee can put the software."

34. Further, the Authority For Advance Ruling in the case of GeoQueste Systems B.V. In re., 327 ITR 1(AAR) dealing with the non-taxability of payment for software, held that payments would not constitute ôroyaltyô since the licensed product could not be commercially exploited by the licensee/customer. This was despite the fact there were clauses regarding the restriction on Intellectual Property. In this regard, the AAR in the captioned case, at **page no 113** of the report, held as under:

"There is also a specific provision in both the agreements that intellectual property rights would always remain with the owner of the product or the licensor. Such restrictions placed on the user of software and the fact that the license/customer had no right to interfere with source code and that the licensed produce cannot be commercially exploited by the license/customer are inconsistent with the inference that the rights in respect of copyright or the right to use the copyright of the computer programmer have been conveyed to the customer. Further, there is nothing in the agreement to suggest that the underlying technical knowledge in developing the software has been transferred. Notwithstanding the grant of authority to use the license (on non-exclusive and non-transferable basis), the copyright imbedded in the software remains with the owner intact."

35. The principle of license and copyright was also discussed by the AAR in the case of *Dassault Systems K.K. In re. 322 ITR 125(AAR),on* **page no 144** of the report, held that

"Passing on a right to use and facilitating the use of a product for which the owner has a copyright is not the same thing as transferring or assigning rights in relation to

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the copyright. The enjoyment of some or all the rights which the copyright owner has, in necessary to trigger the royalty definition. Viewed from this angle, a non-exclusive and non-transferable licence enabling the use of a copyrighted product cannot be construed as an authority to enjoy any or all the of the enumerated rights ingrained in a copyright. Where the purpose of the licenceors the transaction is only to establish access to the copyrighted product for internal business purpose, it would not be legally correct to state that the copyright itself has been transferred to any extent. It does not make any difference even if the computer programme passed on to the user is a highly specialized one. The parting of intellectual property rights inherent in and attached to the software product in favour of the licencee/customer is what is contemplated by the definition clause in the Act as well as the Treaty. As observed earlier, those rights are incorporated in Section 14. Merely authorizing or enabling a customer to have the benefit of data or instructions contained therein without any further right to deal with them independently does not, in our view, amount to transfer of rights in relation to copyright or conferment of the right of using the copyright. However, where, for example, the owner of copyright over a literary work grants an exclusive license to make out copies and distribute them within a specified territory, the grantee will practically step into the shoes of the owner/grantor and he enjoys the copyright to the extent of its grant to the exclusion of others. We may in this context usefully refer to the well-reasoned opinion expressed by OECD in its Commentary on Article 12.

"Transfers of rights in relation to software occur in many different ways ranging from the alienation of the entire rights in the copyright in a programme to the sale of a product which is subject to restrictions on the use to which it is put……Therefore, rights in relation to these acts of copying, where they do no more than enable the effective operation of the programme by the user, should be disregarded in analyzing the character of the transaction for tax purposes. Payments in these types of transactions would be dealt with as commercial income in accordance with Article 7 ….

The method of transferring the computer programme to the transferee is not relevant. For example, it does not matter whether the transferee acquires a computer disk containing a copy of the programme or directly receives a copy on the hard disc of her computer via a modem connection. It is also of no relevance that there may be restrictions on the use to which the transferee can put the software."

36. From the above submissions read with judicial precedents, it is clear that the restriction on intellectual property would not make any difference since the designs and drawings sold by the assessee were used by the Indian customers for internal purpose of setting up plants and not for commercial exploitation. In view thereof, the income earned by the assessee is not taxable both under the Act and the DTAA. Further, the assessee argued that though the ITSC in the final order passed for FYs 2007-08 and 2008-09 has held that the payment for designs and drawings would be taxable as Royalty and Fee for Technical Services @ 10% on gross basis, however the assessee does not agree with the said observation. In this regard, the assessee has also filed a letter dated March 07, 2012 with the AO and DRP that the assessee

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has accepted the order of the ITSC on this issue merely to buy peace of mind and to avoid protracted litigation with the revenue.

37. From the above facts and legal position, it is clear that the basic engineering packages sold by the assessee to the Indian customers have been largely designed on the basis of standard technologies available with it. The consideration was, therefore, for the sale of the product, which is embedded in the plant set up by the Indian customers and does not constitute royalty and is in the nature of business income. Since the work was done outside India and sale was taken place outside India, such income is not taxable under the provisions of the Act and DTAA. Retaining intellectual property in designs and drawings is similar in the nature to the retaining of patented rights in any goods/machinery. Restriction on the intellectual property in designs and drawings sold by the assessee for the purpose of setting up a plant in India does not change the character of the transaction from the sale of the product to the use of licence/know-how. Normally, designs and drawings sold by foreign customers were used by Indian customers for internal business purposes for setting up of their plants and not for any commercial exploitation. Accordingly, the designs and drawings sold by the assessee tantamounts to the use of copyrighted article rather than use of a copyright and is, therefore, in the nature of business income. This issue of assesseeôs appeal is allowed.

38. The next ground in this appeal of assessee is against the order of AO not allowing credit for TDS. For this, assessee has raised following ground:

> *"5. On the facts and in the circumstances of the case and in law Ld. AO has erred in denying TDS credit to the extent of Rs.3,38,43,393/-."*

39. We have gone through the facts and arguments of both the sides. The claim of the assessee is that the original TDS certificates were submitted before the AO during the course of assessment proceedings in support of its claim of TDS. But the AO has not allowed the claim in full. We direct the AO to verify the TDS certificates and allow the claim actually.

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40. The next issue in this appeal of assessee is as regards to levy of interest u/s. 234A and 234B of the Act. This charging of interest u/s. 234A and 234B of the Act is consequential in nature and AO will recompute the same accordingly.

41. Coming to ITA No. 432/K/2014 for AY 2010-11. The issue as regards to taxability of supply of equipments in India, the assessee has raised following grounds:

> *"Taxability of supply of equipment in India*
>
> *2(a)On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that a part of the income earned by the appellant from sale of equipment to the Indian customers accrues or arises in India and thus taxable in India under the provisions of the Act read with the provisions of India-Germany Double Taxation Avoidance Agreement (DTAA).*
>
> *2(b) On the facts and in the circumstances of the case and in law Ld. AO/DRP has erred in holding that title of the equipment sold by appellant has passed on to the Indian customers in India and while reaching to this conclusion has further erred in misinterpreting various clauses of Sales of Goods Act, 1930.*
>
> *2© On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the sale of equipment by the appellant were not concluded until successful completion of various tests at the customers' sites in India without appreciating the fact that these tests are merely in the nature of warranty provision and this fact has been confirmed by the various courts/Tribunals//AAR in several judicial precedents.*
>
> *2(d) On the facts and in the circumstances of the case and in law, Ld. AO erred in rejecting the reliance placed by the appellant on the decisions of DIT Vs. Ericsson A.B [343 ITR 470], DIT Vs. LG Cable Ltd.[237 CTR 438] and Director of Income Tax vs. Ms. Nokia Networks Oy [253 CTR 417] merely on the contention that such decisions are sub-judice before the Hon'ble Apex Court.*
>
> *2(e) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the contracts entered into by the appellant are composite contracts, for erection of plant purely based on surmise and conjecture and without appreciating that the contracts are for supply of equipment.*
>
> *2(f) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in not appreciating the fact that no Permanent Establishment (PE) of the appellant is created in India u9nder Article 5 of the DTAA for offshore sale of equipment to the Indian customers and accordingly no income, from such sale of equipment is taxable in India under the provision of the DTAA.*
>
> *2(g) That on the facts and in the circumstances of the case Ld. AO/DRP erred in holding that for the purpose of supervisory PE under Article 5(2)(k) of the DTAA all site or project need to be clubbed together and hence once there is a supervisory PE the role of such PE in other contracts for offshore sale of equipment cannot be ruled out without appreciating the fact that the appellant has not rendered su9pervisory*

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services for the contracts relating to offshore sale of equipment and hence such clause would not apply in the case of the appellant.

2(h) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that since the performance tests were carried out at customers' site in India the supervisory PE has a role to play in offshore sale of equipment without appreciating the fact that all the operation relating to design, fabrication and manufacture of the equipment were undertaken outside India and hence there is no role of supervisory PE in offshore sale of equipment.

2(i) On the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the judgment of Ishikawajma-Harima Heavy Industries Ld. Vs. DIT 288 ITR 408 and other judicial precedents relied upon by the appellant were based on their own facts without appreciating that such decisions are squarely applicable in the appellant's case.

42. As the facts and circumstances are exactly identical to the facts and circumstances of the case of Outotec GambH for the same assessment year 2010-11, hence, taking a consistent view and applying the same decision, we allow this issue of assesseeôs appeal in this case also.

43. The issue as regards to taxability of supervisory services income in India, the assessee has raised following grounds:

"Income from Supervisory Services
3(a) On the facts and circumstances of the case and in law, Ld. AO/DRP erred in ignoring the net profit rate of 17.93% on gross revenue based on the average margin of comparable companies as considered by the appellant for computing the taxable income from supervisory services in India without showing any cogent reason.
3(b) On the acts and in the circumstances of the case and in law, Ld. AO/DRP erred in considering the net profit rate of 227.5% for computing the taxable income from supervisory services in India which is excessive."

44. As the facts and circumstances are exactly identical to the facts and circumstances of the case of Outotec GambH for the same assessment year 2010-11, hence, taking a consistent view and applying the same decision, we dismiss this issue of assesseeôs appeal in this case also.

45. The next issue in this appeal of assessee is as regards to levy of interest u/s. 234A and 234B of the Act. This charging of interest u/s. 234A and 234B of the Act is consequential in nature and AO will recompute the same accordingly.

46. Coming to ITA No. 283/K/2015 for AY 2011-12. The issue as regards to taxability of supply of equipments in India, the assessee has raised following grounds:

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"Taxability of supply of equipment in India

2(a) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that a part of the income earned by the appellant from sale of equipment to the Indian customers accrues or arises in India and thus taxable in India under the provisions of the Act read with the provisions of India-Germany Double Taxation Avoidance Agreement (DTAA).

2(b) That on the facts and in the circumstances of the case and in law Ld. AO/DRP erred in holding that title of the equipment sold by appellant has passed on to the Indian customers in India and while reaching to this conclusion has further erred in misinterpreting various clauses of Sales of Goods Act, 1930.

2© That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the sale of equipment by the appellant were not concluded until successful completion of various tests at the customers' sites in India without appreciating the fact that these tests are merely in the nature of warranty provision and this fact has been confirmed by the various courts/Tribunals//AAR in several judicial precedents.

2(d) That on the facts and in the circumstances of the case and in law, Ld. AO erred in rejecting the reliance placed by the appellant on the decisions of Hon'ble Delhi High Court in the case of DIT Vs. LG Cable Ltd.[237 CTR 438] and other related judicial precedents merely on the contention that such decisions are sub-judice before the Hon'ble Apex Court.

2(e) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that since the overall responsibility of the entire work is on the appellant a part of income earned from sale of equipment is taxable in India.

2(f) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the contracts entered into by the appellant are composite contracts, for erection of plant purely based on surmise and conjecture without appreciating that the contracts are for supply of equipment.

2(g) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in not appreciating the fact that no Permanent Establishment (PE) of the appellant is created in India under Article 5 of the DTAA for offshore sale of equipment to the Indian customers and accordingly no income from such sale of equipment is taxable in India under the provision of the DTAA.

2(h) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that the appellant has a supervisory PE in erms of Article 5(2)(i) of the DTAA.

2(i) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that since the Acceptance Tests were carried out at customers' site in India the supervisory PE has a role to play in offshore sale of equipment without appreciating the fact that all the operation relating to design, fabrication and manufacture of the equipment were undertaken outside India and hence there is no role of supervisory PE in offshore sale of equipment.

2(j) That on the facts and in the circumstances of the case and in law, Ld. AO/DRP erred in holding that once there is supervisory PE for one of the projects the said PE would become applicable for other projects as well without appreciating the fact that the wording of Article 5(2)(i) of the DTAA clearly provides that PE has to be determined separately for each of the projects.

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2(k) That on the facts and in the circumstances of the case and in law, Ld. AO /DRP erred in holding that the judgment of Ishikawajma-Harima Heavy Industries Ltd. Vs. DIT 288 ITR 408 and other judicial precedents relied upon by the appellant were based on their own facts without appreciating that such decisions are squarely applicable in the appellant's case."

47. As the facts and circumstances are exactly identical to the facts and circumstances of the case of Outotec GambH for the same assessment year 2010-11, hence, taking a consistent view and applying the same decision, we allow this issue of assesseeôs appeal in this case also.

48. The issue as regards to taxability of supervisory services income in India, the assessee has raised following grounds:

"Income from Supervisory Services

4. That on the facts and circumstances of the case and in law, Ld. AO/DRP erred in increasing the net profit rate to 27.5% on the gross revenue from supervisory services against the net profit rate of 16.49% applied by the appellant."

49. As the facts and circumstances are exactly identical to the facts and circumstances of the case of Outotec GambH for the same assessment year 2010-11, hence, taking a consistent view and applying the same decision, we dismiss this issue of assesseeôs appeal in this case also.

50. The next issue in this appeal of assessee is against the order of DRP and that of the AO in taxing income earned from supply of designs and drawings in India. For this, assessee has raised following grounds:

"Taxability of income from supply of design and drawings:

4(a). That on the facts and in the circumstances of the case and in law, Ld. AO/DRP grossly erred in holding that the income earned by the appellant from sale of designs and drawings is for use of copyright and taxable as Royalty under Article 12(3) of the DTAA read with the provisions of section 9(1)(vi) of the act.

4(b) That on the facts and in the circumstances of the case Ld. DRP erred in rejecting the reliance placed by the appellant on the decision of Hon'ble Delhi High Court in the case of DIT Vs. Infrasoft Ltd. (39 Taxmann.com 88)."

51. As the facts and circumstances are exactly identical to the facts and circumstances of the case of Outotec GambH for the same assessment year 2010-11, hence, taking a consistent view and applying the same decision, we allow this issue of assesseeôs appeal in this case also.

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52. The next issue in this appeal of assessee is as regards to levy of interest u/s. 234B of the Act. This charging of interest u/s. 234B of the Act is consequential in nature and AO will recompute the same accordingly.

53. In the result, appeals of assessee in ITA No. 431 & 432/K/2013 & ITA No. 283/K/2015 are partly allowed.

54. Order is pronounced in the open court on 16.06.2015.

Sd/-	Sd/-
(B. P. Jain)	(Mahavir Singh)
Accountant Member	Judicial Member

Dated: 16th June, 2015

*JD. Sr.P.S

Copy of the order forwarded to:

1. APPELLANT ï Outotec GmbH, C/o Outotec India Pvt. Ltd, & Outotec (Canada) Ltd. 12th Floor, South City Pinnacle, Plot No-XI, Block EP, Sector V, Salt Lake,Kolkata-700 091
2. Respondent ï The D.D.I.T. (International Taxation)-2(1), Kolkata, AayakarBhawanPoorva, 110 Shanti Pally, Kolkata-700 107
3. The CIT(A), Kolkata
4. CIT Kolkata
5. DR, Kolkata Benches, Kolkata

/True Copy, By order,

Asstt. Registrar.

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