IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH : C : NEW DELHI

BEFORE SHRI G.E. VEERABHADRAPPA, HON'BLE VICE PRESIDENT
AND
SHRI I.P. BANSAL, JUDICIAL MEMBER

ITA No.5237/Del/2010
Assessment Year : 2007-08

Samsung Heavy Industries Co. Ltd., C/o Vaish Associates, Flat No.5,10, Hailey Road, New Delhi.	Vs.	ADIT (International Taxation) Dehradun.

PAN : AAJCS7859K

(Appellant)		(Respondent)
Assessee by	:	Shri Ajay Vohra, Shri Rupesh Jain & Shri Sachit Jolly, Advocates
Revenue by	:	Shri Ashwani Kumar Mahajan, CIT/DR

ORDER

PER I.P. BANSAL, JUDICIAL MEMBER

This is an appeal filed by the assessee. It is directed against the order passed by the Assessing Officer dated 25th October, 2010 u/s 143(3)/144C(13) of the Income Tax Act (the Act). The impugned assessment order has been passed by the Assessing Officer as per order passed by Dispute Resolution Panel-II, Delhi, dated 30th September, 2010 for assessment year 2007-08. Grounds of appeal read as under:-

> *1. That on the facts and circumstances of the case and in law, the order passed by the Assessing Officer ("the ld. AO") under section 143(3) read with section 144C of the Income-tax Act, 1961 ("the Act") without affording adequate opportunity of being heard to the appellant, is in violation of principles of natural justice and is, therefore, bad in law and void ab-initio.*

1.1 That the AO/DRP erred on facts and in law in not providing an opportunity to the appellant to cross examine the officer of Oil and Natural Gas Corporation Limited ("ONGC") on the basis of whose opinion adverse inferences against the appellant have been drawn and without confronting the data relied upon for arriving at the estimated profit from offshore operations.

2. That on the facts and circumstances of the case and in law, the ld. AO erred in completing the assessment at an income Rs. 28,12,60,801/- as against loss of Rs. 23,50,939/- returned by the appellant holding that the appellant was liable to tax in India, in respect of the activity performed in India and outside India during the relevant previous year.

3. That on the facts and circumstances of the case and in law, the ld. AO erred in holding that the appellant had a fixed place 'Permanent Establishment' ("PE") in India under Article 5 of the Double Tax Avoidance Agreement between India and Korea ('the Treaty'), in the form of project office in India.

3.1 That on the facts and circumstances of the case and in law, the ld. AO erred in alleging that the profit office was involved in marketing and negotiating tender bids, not appreciating that the profit office name into existence post completion of preliminary activities like bidding for the contract, notification of award of contact, signing of the contract.

3.2 Without prejudice that the AO erred on the facts and in law in not appreciating that the activities carried out by the project office in India were merely preparatory and auxiliary as referred to in Article 5(4) of the Treaty and did not lead to establishment of fixed placed PE in India.

3.3 That the ld. AO erred on facts and in law in not appreciating that there could only be, if at all, installation/assembly PE as mentioned in Article 5(3) of the Treaty as opposed to fixed place PE.

3.4 That the ld. AO erred on facts and in law in further not appreciating that no such PE was established in the relevant previous year as no activity leading to establishment of installation/assembly PE took place in India during the relevant previous year.

3.5 That the ld. AO erred in ignoring the fact that activities like bidding for the contract, notification of award of contact, signing of the contract and pre-bidding surveys, being events earlier to the execution of the contract in India, could not lead to establishment of installation PE in India.

3.6 That on the facts and circumstances of the case and in law, the ld. AO erred in holding that the pre-engineering and pre-construction survey lead to establishment of PE even though these activities wee carried out by independent subcontractors.

4. That on the facts and circumstances of the case and in law, the ld. AO erred in holding that the contract with ONGC was not divisible in terms of activities to be performed in and outside India, and, therefore, the profit arising to the appellant from the activities performed outside India (designing, engineering and material procurement) was chargeable to tax in India.

4.1 That on the facts and circumstances of the case and in law, the ld. AO erred in holding that the consideration under the contract for the work carried out in India and outside India was neither identifiable nor divisible not appreciating that the contracting parties had themselves identified and allocated the consideration in the contract itself having regard to the location of work.

4.2 That the ld. AO erred on facts and in law in ignoring the principles of taxation laid down by the Hon'ble Apex Court in the case of Ishikawajma Harima's : 288 ITR 408 (SC) in respect of taxability of turnkey contract where different parts of the contract are to be carried out in different tax jurisdictions.

5. Without prejudice even if it is assumed that the contract was not divisble and the appellant had a PE in India, no income on account of offshore activities, i.e., the operations carried out outside India (viz., designing, engineering and material procurement activities) was attributable to the alleged PE, as the offshore activity was carried out outside India and the alleged PE had no role to play in such activity.

5.1 That the ld. AO erred in holding that revenue from operation of design, engineering and material procurement outside India was taxable, even though there was no allegation that the price at which billing was done was not at arm's length.

6. On the facts and circumstances of the case the ld. AO erred in not appreciating that even if the appellant is assumed to have PE in India, since the appellant incurred overall loss on the aforesaid project, both in respect of operations in India and outside India, there was, in any case, no income liable to tax in India in relation to the said project.

7. Without prejudice to the submission that no income is liable to tax in India, the ld. AO/DRP erred in

- *Disregarding the profit and loss statement filed by the appellant in respect of the offshore activities and in estimating,*

on ad hoc basis, profits from such activities @ 25% of revenues during the relevant previous year.

- *In not allowing deduction for direct and indirect expenses and selling and administrative expenses incurred by the appellant outside India in relation to the offshore activities, alleging that the same had not been substantiated by the appellant and the profitability statement was not authenticated by the appellant.*

- *In not allowing expenses relating to sub-contractors' cost on the ground that no tax had been deducted therefrom.*

- *In making reference to the mean net profit rate of companies namely, 'Artefact Projects Limited', Engineers India Limited', Ezyone Holdings Limited' and 'Dolphin Offshores Enterprises India Limited', without confronting the same to the appellant, and on that basis approving the rate of 25% applied by the AO to the contract receipts to arrive at the income from the offshore activities.*

- *In ignoring the global profit and loss account filed by the appellant which demonstrates the worldwide profit margin earned by the appellant and in not appreciating that in terms of Rule 10 of the Income-tax Rules the said margin could at most be applied to sales made to ONGC to the extent attributable to the PE, to determine the income of the appellant liable to tax in India.*

8. That the ld. AO erred in giving lower credit of the tax deducted at source as claimed by the appellant in its return of income.

9. That the ld. AO erred in charging interest u/s 234B of the Act, not appreciating that since the entire income of the appellant was subject to tax withholding, if such income were to be held chargeable to tax in India, the appellant was not liable to pay advance tax.

10. That the ld. AO erred on facts and in law in charging interest u/s 234D of the Act.

The above grounds of appeals are without prejudice to each other.

That the appellant craves leave to add, alter, amend or withdraw all or any objections herein or add any further grounds as may be considered necessary either before or during the hearing of these objections."

2. Though, in the present appeal various issues are raised, but, during the course of hearing of this appeal the issue relating to

existence of Permanent Establishment (PE) was argued by both the parties on the basis of which the claim of the assessee is depending. According to the assessee, for its activity relating to outside India operation PE does not exist. Therefore, it is the case of the assessee that no part of the revenue received by it with regard to the activities carried on outside India is taxable. As against that, it is the case of the revenue that on its outside India operations, the assessee is liable for taxation as there is an existence of PE of the assessee in India. To understand the controversy, it will be relevant to mention the following facts.

3. Vide agreement dated 28th February, 2006, the assessee company along with M/s Larsen & Toubro Ltd. (L&T) had entered into an agreement with Oil and Natural Gas Corporation (ONGC) to carry the work of "Surveys (pre-engineering, pre-construction/pre-installation and post construction), design, engineering, procurement, fabrication, anti corrosion and weight coating, load out, tie down/sea fastening, tow out/sail out, transportation, installation, modifications at existing facilities, hook up testing, pre-commissioning, start up and commissioning of entire facilities covered under Vasai East Development Project. The recital clause vide which such work is stated in the agreement read as under:-

> "WHEREAS the Company is desirous of carrying work of Surveys (Pre-Engineering, pre-construction/pre-installation and post construction), Design, Engineering, Procurement, Fabrication, Anti Corrosion and Weight Coating, Load out, Tie down/Sea fastening, Tow out/Sail out, Transportation, Installation, Modifications at existing facilities, Hook up Testing, Pre-Commissioning, start up and commissioning of entire facilities covered under Vasai East Development Project (hereinafter referred to as the 'Work' or 'Works' and more particularly defined in Clause 1.1.37 of General conditions of the contract) on turnkey basis at its Western Offshore site."

4. The above mentioned contract was on turnkey basis at ONGC's western offshore site. ONGC invited tenders for this work vide notice dated 30th June, 2005 in pursuance of which the aforementioned contract was awarded to the assessee company along with L&T.

5. The assessee company and L&T for carrying out this work had entered into a Memorandum of Understanding which is dated 15th October, 2005 copy of which is filed at page 272 of the paper book. The allocation of work between them as specified in the said Memorandum of Understanding was as under:-

> "SAMSUNG: BCPA-2 Deck, Jacket, Building module including TG. Installation of all the structures (except modification) and insurance.
>
> L & T : Booster Compressor Modules, HP Compressor Module, Bridges and Modification to existing facilities."

6. The above allocation was further revised by amendment to Memorandum of Understanding dated 16th November, 2005 a copy of which is placed at page 274 of the paper book and the revised allocation was as under:-

> "SAMSUNG: BCPA-2 Deck, Jacket, Building module including TG, Bridges and modification to existing facilities. Installation of all the structures and insurance.
>
> L & T : Booster Compressor Modules, HP Compressor Module."

7. The recital clause of the aforementioned agreement dated 28th February, 2006 states the contract price as USD 38,14,59,881/- + ₹ 346,08,97,000/-. For the sake of convenience the said clause is reproduced as under:-

> "AND WHEREAS Pursuant to the above and the discussions conducted with the Contractor, the company has awarded to the

> **Contractor the Contract for the said Work at a total lumpsum Contract price of USD 381,459,881/- + INR 346,08,97,000/- (United States Dollars Three Hundred Eighty One Million Four Hundred Fifty Nine Thousand Eight Hundred Eighty One plus Indian Rupees Three Hundred Forty Six Crores Eight Lakhs Ninety Seven Thousand only) by its NOA MR/OW/MM/VED/03/2005 dated 24.01.2006 which is the effective date of commencement of this contract) and on the terms and conditions as agreed to by the two parties as of the said date of NOA and as outlined in this Agreement (hereinafter also referred to as "the Contract")**

8. Annexure A to the aforementioned agreement dated 28th February, 2006 describe the general conditions of the contract and Annexure B comprise of bidding documents, etc. There are other annexures also, Annexures C, D, E, F and G. Annexure C prescribe the contract price schedule and rental rate schedule and Annexure D prescribe the construction schedule/project key dates. Annexure E prescribe milestone payment formula. Annexure F is integrity pact duly signed by consortium members (assessee and L&T) and ONGC. Annexure G is Memorandum of Understanding concluded between the assessee and L&T. The Clause (d) of the said agreement describe as under:-

> "(d) The Contractor hereby covenants with Company to perform the Work in conformity in all respect with provisions of the Contract and in consideration of the carrying out and completion of the Works by the Contractor, the Company hereby covenants to pay the amounts at the times and in the manner described hereinafter."

9. Contractor in the agreement means the consortium of the assessee and L& T.

10. It will also be relevant here to mention the **scope of work** described under the head 'subject matter of contract' containing in clause 2.0 of Annexure A to the contract:-

2.0 SUBJECT MATTER OF CONTRACT

2.1 Scope of Work

The scope of work for the Contract shall include in general but not limited to Surveys (pre-engineering, pre-construction/pre-installation and post-installation), Design, Engineering, Procurement, Fabrication, Anticorrosion & Weight coating of risers and submarine pipe line spools, Load out, Tie down/sea fastening, Tow-out/Sail-out, Transportation, Installation, Hook-up, Modifications on existing facilities, Testing, Pre-commissioning, Commissioning of entire facilities as described in the bidding documents. Included among these functions, but not limited to these are :

a) Carry out all engineering and design requirements to completely design and engineer these facilities including all safety studies.

b) Provide purchasing, expediting, inspection, handling and transportation of all materials and equipment.

c) Prepare and issue purchase specifications after obtaining approval from the Company where required, for all equipment as well as obtaining vendor certified prints, instructions, parts lists, etc.

d) Prepare and issue all engineering, purchasing and construction schedules for approval of Company.

e) Supervision & monitoring and progress reporting during design & engineering fabrication/installation, hook-up, testing, pre-commissioning, start up & commissioning, etc.

f) Prepare and issue all drawings required for carrying out this project.

g) Provide all manpower, materials, load-out, tie-down, transportation, handling and erection of equipment, machines, tools and instruments; storage and fabrication facility; personnel housing, mess and transportation; and all services necessary to perform the work for the complete installation as described in Part IV of bidding document.

h) Comply with all Central, State and Local Government Regulations applicable to the work.

i) Observe all applicable Company's and accepted industry safety practices and, in addition, all Governmental regulations as appropriate for this Work.

j) Comply with applicable codes and standards as per Contract, of engineering, fabrication, construction and safety.

k) Provide necessary documents and drawings for the scrutiny of the appointed Third Party Inspection and Certifying Agency.

l) Provide all as-built drawings, documents and manuals.

m) Provide Third Party Inspection and Certificate of approval for all the facilities under the scope of work.

n) Provide all statutory approvals, insurance, guarantee.

Further details on Scope of Work have been provided in Part-IV of bidding document."

11. The existing facilities have been described as under:-

"2.1.2 Existing Facilities

Following are the existing facilities with reference to the scope of work of this Contract:

"BPA complex" comprising of the following facilities

i) BPA – Process platform bridge connected to BLQ-1, BA and Flare structure BF-1.

ii) BLQ-1 – Living Quarters platforms bridge connected to BPA.

iii) BCP-A – Gas Compression platform bridge connected to BPA & BLQ-1."

12. The effective date of the commencement of the contract has been written as 24th January, 2006 and date of completion as described in clause 6.3.1 is 2nd April, 2008. Under the head 'general obligation of the contractors' stated in clause 2.3 the obligation of the contractor as described in clause 2.3.1.3 is as under:-

> *"Contractor shall be deemed to have satisfied himself as to the correctness and sufficiency of the Contract Price for the Works. The consideration provided in the Contract for the Contractor undertaking the Works shall cover all the Contractor's obligations and all matters and things necessary for proper execution and maintenance of the Works in accordance with the Contract and for Complying with any instructions which the Company's Representative may issue in accordance with in connection therewith and of any proper and reasonable measures which the Contractor takes in the absence of specific instructions from the Company's Representative."*

13. Clause 2.3.5.1 states an obligation cast upon the contractor to supply to ONGC within 21 days of the effective date of commencement of work or prior to kick off meeting, whichever is earlier, an organization chart showing the proposed organization to be established by the contractor for execution and the work including the identities and curriculum vitae of the key personnel to be deployed and any revision or alteration to such organization chart was to be promptly informed to the assessee company.

14. The Clause 3 describe the payments. Under clause 3.1 contract price has been described as under:-

> *"The Company shall pay to the Contractor in consideration of satisfactory completion of all the works covered by the Scope of Work under the Contract the Contract Price of Contract price of USD 381, 459, 881 + INR 346, 08, 97, 000.00 (United States Dollars Three Hundred Eighty One Million Four Hundred Fifty Nine Thousand Eight Hundred Eighty One plus Indian Rupees Three Hundred Forty Six Crores Eight Lakhs Ninety Seven Thousand only) as per the details and break-up of prices given in schedule of prices. The contract price is a firm price and the Contractor shall be bound to keep the same firm and without escalation on any ground whatsoever until completion of entire works against this contract. Unless otherwise specified in the Contract, cost of execution of Works on turnkey basis and tests etc. as specified in Contract and all expenses, duties, taxes, fees charges in relation to or in connection therewith including insurance risk of weather, Constructional Plant and Equipment breakdown and Site conditions etc. as per provisions of the Contract, shall be deemed to be included in the Contract Price. Payment shall be made in the currency or currencies given in the schedule of prices for the work executed as per the*

procedure set forth in Clause 3.2. Adjustment to Contract Price, if any, shall be made in accordance with provisions of Contract."

15. Under the head 'payment procedure' in clause 3.2, provisional progressive payments for part of the work executed by the contractor are stated to be made on the basis of completion of work as per the milestone payment formula and the said clause read as under:-

"Pending completion of the whole Works, provisional progressive payments for the part of the Works executed by the Contractor shall be made by Company on the basis of said work completed and certified by the Company's Representative as per the milestone payment formula provided in the bidding document at Annexure-E of Agreement. Such certification of the Work completed shall be made by the Company's Representative within 15 days of receipt of Contractor's Application for Certification with all required supporting documents. No payments shall become due and payable to the Contractor until Contract is signed by the two parties and Contractor furnishes to the Company Performance Guarantee (as per Clause 3.3) and Certificate of Insurance for Policy/Policies specific for the project (as per requirement of Cl. 7.3) and a copy of permission from Reserve Bank of India for opening Project Office in India (in the case of foreign Contractor)."

16. In Clause 3.3 under the head 'performance guarantee' the contractor is under an obligation to furnish to ONGC a bank guarantee within two weeks from the date of signing of the contract of equivalent amount of 10% of the contract price. Clause 3.5 describe the adjustment to the contract price which, for the year under consideration, is not relevant as no such exigency has been shown to be happened.

17. During the year under consideration, as per letter dated 24th May, 2006 of the RBI, Mumbai, the project office is opened on 24th May, 2006. The assessee furnished the return of income in accordance with Article 7 of Double Taxation Avoidance Agreement (DTAA) between Indian and Korea. The assessee offered the revenue of Rs.23,73,45,563/- on account of aforementioned contract. However,

the return of income was filed at nil showing loss of Rs. 23,50,939/-. The Assessing Officer required the assessee to show cause as to why the return of income was filed at nil. In response to such show cause notice, it was stated by the assessee that the business of the assessee company is governed by the accounting standard VII (Revised) and the accounts have been prepared on the basis of completion method. The percentage of completion is determined as a proportion of cost incurred upto the date of each accounting period to the total estimated cost. The provision is made for foreseeable losses when current estimate of total contract cost and revenues indicate a loss. The assessee is governed by the provisions of Article 7 of the DTAA and as per the said article all expenses incurred in earning income are fully deductible based on the commercial accounting principle in computing the said business profits chargeable to Indian income-tax. The Assessing Officer observed that Profit & Loss Account of the Mumbai Project office as showing the gross income of Rs.23,73,93,083/- against which the assessee had claimed the expenses of Rs.24,34,70,741/-. The contract revenue of Rs.23,73,45,563/- was 14.56% of the total revenue of the contract for inside India work which was Rs.162.97 crore. The invoices raised by the assessee for inside India activity were to the tune of Rs.3,25,82,569/- which have been listed at para 5 of the assessment order. It was further noticed that out of total expenses incurred at Rs. 24,34,70,741/-, which was debited to Profit & Loss Account, the assessee had incurred expenses on account of cost of revenues, selling, general and administrative expenses and depreciation on total amount of Rs.24,34,70,741/-. It was further observed that cost of revenues were shown under the following three sub-heads for an aggregate sum of Rs. 23,91,08,293/-:

(i) Hook up and commissioning - Rs. 89,04,947/-;
(ii) Insurance - Rs. 22,66,85,140/-; and

(iii) Pre-engineering and survey - Rs. 35,18,206/-;

18. It was further noticed that the insurance was paid by the assessee to IFFCO-TOKIO General Insurance Company Ltd. and the policy taken was in the name of Samsung Heavy Industries Ltd. So far as it relates to the amount of Rs. 89,04,947/- claimed on account of hook up and commissioning, the same was paid to 'Offshore Hook up and Construction Services India Pvt. Ltd.' for which the TDS was deducted, hence, the Assessing Officer allowed the said amount to the assessee. He found that TDS on pre-engineering and survey was belatedly made, therefore, he excluded the expenses of Rs. 35,18,206/- on the ground of application of Section 40(a)(ia) of the Act. It was also noticed that the Assessing Officer had disallowed the said amount and the Assessing Officer has calculated the income of the assessee from inside India activity at a loss of Rs. 23,33,939/- in the following manner:-

Income from business or profession		
Income as per P/L A/c		- 6129944
Add:		
Provision for taxation		
Provision for FBT	35319	
Provision for Deferred Tax Liability	16967	
Depreciation computed under sch. XIV of the Companies Act	236561	
Disallowance u/s 40(a)(i)	3759997	
Disallowance u/s 40A (3)	4100	
Disallowance as discussed above	17000	4069944
		-2060000
Less : Depreciation allowed u/s 32		273939
Taxable income		-2333939

19. It was further noticed by the Assessing Officer that the assessee did not declare income out of revenue earned by it on the activities allegedly carried outside India and the assessee was required to show cause as to why the said revenue should not be brought to tax in India as those activities are carried from inside India operations. In

response, it was submitted that the consideration for supply of goods is received in USD in respect of 'offshore supply' and 'offshore services' by the assessee outside India, the sale is completed outside India and the same is not attributable to the permanent establishment. No part of the income for the 'offshore supply' or 'offshore services' is received in India. The property in goods, which were the subject matter of offshore supply, passed on to ONGC outside the territory of India. According to Section 5 (2) of the Income-tax Act, the assessee being non-resident, will be chargeable to tax in India only in the event when income accrue or arise to it in India or is deemed to accrue or arise in India or income is received or deemed to be received in India and not otherwise. All the operations in connections with offshore supply are carried out outside India, therefore, the question of any portion of the consideration to be regarded as deemed to accrue or arise in India would not arise. The requirement of the assessee to perform certain services in India such as unloading, port clearance, transportation of the equipments supplied would not render the assessee eligible to tax as the consideration thereof is embedded in the consideration for offshore supply. Although the assessee was required to carry out certain activities in India, the consideration for offshore services had separately been provided for. It was submitted that the fact that the contract has been fashioned as a turnkey contract by itself may not be of much significance. The project is a turnkey project, the contract may also be a turnkey contract, but the same by itself would not mean that even for the purpose of taxability the entire contract must be considered to be an integrated one so as to make the assessee to pay tax in India. The taxable events in execution of a contract may arise at several stages in several years. The supply obligations is distinct and separate from service obligation. The price for each of component of contract is separate. Similarly, offshore supply and offshore services have separately been dealt with. The prices in each of the segment

are different. The very fact that in the contract the supply segment and service segment have been specified in different parts of the contract is a pointer to show the liability of the assessee thereunder is also different. The contract undisputedly was executed in India. By entering into a contract in India although parts thereof will be carried out outside India will not make the entire income derived by the assessee to be taxable in India. It was submitted that only such part of income as was attributable to the operations carried out in India would be taxable in India. The interpretation of the treaty should be made in accordance with the OECD model and reference was made to the commentary written by Klaus Vogel vide which the second sentence of Article 7.1 was stated to have allowed the state of the permanent establishment to tax the business profit, 'but only so much of them as is attributable to the permanent establishment.'

20. Heavy reliance was placed by the assessee on the decision of Hon'ble Supreme Court in the case of Hyundai Heavy Industries Ltd. (2007) 291 ITR 482 (SC) wherein while explaining the attraction rule, it was held by Hon'ble Apex Court that it implies that when an enterprise (GE) set up a PE in another country, it brings itself within the physical jurisdiction only of that another country to such a degree that such another country can tax all profits from the GE derived from the source country – whether through that PE or not. It is the act of setting out a PE which triggers the taxability of transactions in the source state and it was submitted that unless the PE is set up, the question of taxability does not arise irrespective of the fact that whether the transactions are direct or they are through the PE. In the case of turnkey projects, the PE is set up at the installation stage while the entire turnkey project including the sale of equipment is finalized before the installation stage. The setting up of the PE in such a case, is a stage subsequent to the conclusion of the contract. It is a result of sale of equipment that

the installation PE came into existence. It was submitted that the contract in the present case was concluded on 28th February, 2006 as against that assessee's installation PE came into existence on 24th May, 2006 and if the law laid down in aforementioned decision of Apex Court is taken into consideration, then, revenue for sale of equipment finalized before the setting up of installation PE cannot be attributed to PE which was not even in existence at the time of the said sale. Hence, no part of outside India revenue could be attributed to the revenue.

21. Reference was also made to the decision in the case of Ishikawajima – Harima Heavy Industries Co. Ltd. (2007) 288 ITR 408 (SC) wherein it was held that for offshore work rendered outside India; the permanent establishment would have no role to play in respect thereto in earning the said income. Secondly, the entire services having been rendered outside India and income arising therefrom cannot be attributable to the permanent establishment so as to bring within the charge of tax. For attracting the taxing statute, there has to be some activity through permanent establishment. If income arises, without any activity of the permanent establishment, even under the DTAA the taxation liability in respect of overseas services would not arise in India. Section 9 spells out the extent to which the income of the non-resident would be liable to tax in India. Section 9 has a direct territorial nexus.

22. Thereafter, the Assessing Officer made various inquiries from the assessee regarding the activities carried on by the assessee which are listed at page 13 of the assessment order. The Assessing Officer also called for information from ONGC and from the information so received, he found that the assessee had actively participated in the bidding process, pre-bid meetings, negotiations and submissions of the tender documents/process of award of contract. He observed that the

project office of the assessee at Mumbai was always in existence, actively involved right from the kick off meeting which was held on 15th February, 2006. In the minutes of the kick off meeting, it was mentioned that the ONGC has informed the assessee that the need to open project office in India is necessary to comply with the contractual requirements and Reserve Bank of India guidelines for obtaining of RBI approval for release of payments in foreign currency. He further observed that the charges of insurance policy was also to be borne by the assessee which was included in the contract price and the insurance for the entire project was taken by the assessee in India. The title was to pass on to ONGC only after the completion of the project and successful acceptance by the ONGC in India. The transportation to the site of all goods/material was the responsibility of the assessee. Thus, the Assessing Officer observed that all these things show that the whole project was carried out by the assessee in India. The consideration mentioned in the contract is for the full contract to be executed in India and, therefore, income earned by the assessee in respect of outside India activity is liable to be taxed in India as per the provisions of Section 5 of the Act and also Article 7 of DTAA read with Article 5 as the assessee was having PE in India.

23. As against the above view of the Assessing Officer, the assessee denied to have its liability to be assessed on the revenue relating to activity carried on outside India based on the aforementioned decisions of Hon'ble Supreme Court in the case of Ishikawajima – Harima Heavy Industries Co. Ltd. (supra) and Hyundai Heavy Industries Ltd. (supra). It was submitted that the payments were to be received by the assessee as per milestone payment formula which was duly supported by the achievement certificates. So as it relates to insurance premium, it was submitted that insurance expenses were incurred by the assessee purely for and on behalf of ONGC and the same have been reimbursed

to the assessee in full. It was submitted that the assessee did not have any project office in India prior to 24th May, 2006 as the project office of the assessee had come into existence on 24th May, 2006 after getting the approval and the RBI vide letter dated 24th May, 2006. The installation PE of the assessee came into existence only after 17th November, 2007 when the jackets were brought to the offshore site for installation. It was reiterated that revenue relating to outside India activity was not taxable as per provisions of DTAA.

24. Considering these submissions, the Assessing Officer has observed that the assessee has placed heavy reliance on the decision of Hyunday Heavy Industries Ltd. (supra) and he noted that the assessee in that case had opened its office in India some times in 1983 and since then the assessee was regularly taking the execution of various projects in India most of which were related to projects of ONGC on high-sea. The said office of that assessee was approved only as a liaison office and was not permitted to undertake any business activity on behalf of the assessee. However, there was dispute with the income-tax department in this regard. According to the department, the said liaison office had crossed the bound of liaison office and undertook the business activities for and on behalf of the assessee. He also referred to the observations of the Apex Court from the said decision in which they have observed that the contract in that case was in two parts; one was for fabrication of the plat-form and the other was for installation and commissioning of the said plat-form in South Bassein Field. It was further noted by the Apex Court that the Indian operations consisting of installation and commissioning commenced on 11th November, 1986 and were completed on 12th April, 1987. It was noted that the contract was divisible and the Profit & Loss Account was prepared in two parts. One for the Korean operation and the other for Indian operation. It was also noted that fabricated

platform was handed over to ONGC in Korea in September, 1987 and, therefore, before coming into existence of the PE of the assessee, the work of fabrication was completed in Korea. According to the Assessing Officer, the Apex Court has held that the taxable unit is the foreign company and not its branch or PE in India. Ascertainment of a foreign enterprise's taxable business profits in India involves an artificial division between profits earned in India and profits earned outside India. Referring to the observations of apex court in para 9 of the judgement 'the assessee places reliance on article 7 of CADT and submitted that on completion of the work of fabrication of platforms, the same were handed over to the agents of ONGC in Korea and, therefore, the assessee was not liable to be taxed……." and further observations in para 11 "we find that the profits earned by Korean GE of supplies of fabricated platform cannot be made attributable to its Indian PE as the installation PE came into existence only after the transaction stage materialize. The installation PE came into existence only on completion of transaction giving rise to the supply of fabricated platform. The installation PE emerged only after the contract with the ONGC stood concluded. It emerged only after the fabricated platform was delivered in Korea to the agents of ONGC. Therefore, the profit on such supplies cannot be said to be attributable to PE". Further he referred to the observations of their lordships in para 12 "in the case of turnkey projects, the PE is said to be at the installation stages while the entire turnkey project, including the sale of equipment is finalized before the installation stage. The setting up of PE, in such a case, is a stage subsequent to the conclusion of the contract. It is as a result of the sale of equipment that the installation PE comes into existence. However, this is not an absolute rule, in the present case there was no allegation made by the department that the PE came into existence even before the sale took place outside India".

25. From the above observations of their lordships, the Assessing Officer has culled out the facts as found in that case as under:-

> "(i) The contract was in two parts, one for fabrication of platform and the other for installation.
>
> (ii) The installation PE in India came into existence only after the conclusion of the contract for supply of fabricated platforms.
>
> (iii) The installation PE in India came into existence only after the conclusion of the contract for supply of fabricated platforms.
>
> (iv) There was no allegation by the department that the PE came into existence before the sale took place.
>
> (v) The sale of fabricated platform took place outside India."

26. Comparing the aforementioned facts with the case of the assessee, ld. Assessing Officer has held that the facts of the case of the assessee are materially different from the facts of aforementioned case. The Assessing Officer referred to the various terms of the agreement entered into by the assessee with the ONGC. He first referred to the scope of the work which did not include any sale or supply of material to ONGC and has observed that the contract in the present case does not begin with the installation, but begin with pre-engineering and pre-construction service. The effective date of commencement of work is 24th January, 2006. He referred to the clause 2.3.7 and from there he found that it was the responsibility of the contractor from the commencement of the work till the certificate of completion and acceptance by the ONGC and that too in a condition

where the work done by the contractor is found to be in good order and condition and conformed in every respect the requirements of the contract. He referred to clause 3.2 which describe the milestone payment formula and it is stated therein that pending completion of the whole work, provisional progressive payment for part of the works executed by contractor will be made on the basis of work completed and so certified by the representative of the company and the said clause also stipulates that the provisional payments would be made as per the agreed milestone formula. The invoices would be raised every month on the basis of work completed for such provisional payments. Thus, referring to this clause, the Assessing Officer found that the milestone payments are only provisional payments and it clearly shows that contract is not divisible. He also referred to clause relating to obligation of the contractor for payment of customs duty. He also referred to the clause 5.4.2 which provides that contractor may have to dismantle or modify any existing facility or equipment and if it is so done that will be at contractor's own cost and responsibility. Under clause 5.5.1 contractor was under an obligation to provide office space and secretarial service, etc. during the time of engineering and design review and, in this manner, he has mentioned various clauses of the agreement and after analyzing all these clauses, the AO concluded that the main thrust of the arguments of the assessee was that it was not having any PE in India before the work of fabrication got completed and the fabricated material was imported in India. The installation PE was having limited task of installation and commissioning of the project and the title to the material passed in Korea. Examining such contention of the assessee, the AO has framed following issues:-

(i) Whether the fabricated material was sold to ONGC in Korea before the PE in India came into existence.

(ii) Whether the contract was divisible into two portions, one for supply of material and other for installation and commissioning.

27. Adverting to the first issue, the AO observed that terms of contract with ONGC did not stipulate any sale of material to them. The preamble and the scope of work stipulates various works at the Vasai East Development Project. There may be various stages in executing the work like survey, designing, fabrication, procurement and installation and commissioning but these are mere stages of the total project. The ONGC does not purchase any material from the assessee. ONGC takes over the completed work when all parts of the work are executed. The ownership of the fabricated material remained with the contractor till the complete project was handed over to the ONGC. It is observed by the AO that main reliance of the assessee is on schedule of milestone payments which stipulates value of each item, the currency in which such payment is to be made and also the stage of payment. He observed that as clarified by ONGC, these milestone payments are in the nature of "Provisional Progressive Payments" pending completion of whole work as per clause 3.2 of the agreement. The letter of clarification obtained from ONGC states that such arrangement is done with a view to provide adequate liquidity of the funds to the contractor and it has been further clarified that the payment is made in the choice of the currency of the contractor. The reliance by the assessee on clause 7.1.1 to contend that ownership gets transferred on completion of fabrication of material and ownership of material was transferred to the company upon issuance of certificate towards part completion or completion and acceptance of the work is clearly contrary to the clarification given by ONGC. He rejected the contention of the assessee for giving the opportunity of cross examination of the official of the ONGC who had given the

clarification as according to the AO, the reply given by the official of ONGC was on the basis of material available on record. The AO also observed that the clarification given by him was put to the assessee to comply with the requirements of principles of natural justice and assessee has not given any cogent reason to find any infirmity in the said clarification. The completion of work was in India, the handing over of completed work was also in India. The deployment of men and material was in India. The insurance cover was taken by the assessee in India. The import was made by the assessee on its own account and custom duty was also paid by them. The entire transportation was done on the contractor's risk. Therefore, it is not comprehensible that how the assessee can take the plea that the title of the goods passed outside India. The fact that ONGC kept a close watch on the quality of material and did approve design and quality from time to time by making periodical inspection and approving vendors etc., does not mean that the title in goods, under any circumstances, had passed outside India. The work of fabrication and procurement of material was very much a part of the contract for execution of work assigned by ONGC. The work was wholly executed by the PE in India and it will be absurd to suggest that PE in India was not associated with the designing or fabrication of materials.

28. On the aspect of question that whether the contract was divisible into two parts, the AO observed that contract is on turnkey basis which has been executed in India. The title in goods as well as constructed pipe lines were transferred once the Indian company accepts the project as complete. The case of the assessee has no comparison to a case of an isolated supply contract. It is a clear case of a works contract executed in India where the assessee has also the obligation of fabrication and procurement of certain material to be used in the work. If assessee's version is accepted, it will amount to accepting the

fact that if a builder is given a contract to construct flats as per agreed terms and the builder imports certain design and material, he claims that a portion of his income is exempt from tax on the ground that supply is under a separate and divisible contract. He has given an example of a contract for construction of a house where contractor carries on survey of the site, makes drawing and designs, procures material and brings it to the site and does the construction work and hand over the house to the owner and in that case he cannot be said to have sold bricks, iron rods, cement, wooden door, tiles etc. but he is constructing the house and handing over the same to the owner. The procurement of material has no relevance to location from where it has been brought. The contractor may import it or procure it locally. Procurement itself means buying it from third party and thus, there was no basis on which it could be said that contract could be divided into two parts. The assessee has executed the projects with ONGC on turnkey basis. The scope of the project included works relating to pre-engineering surveys, designing, fabrication, procurement, installation and commissioning of the project of laying of the pipelines. All these obligations were part of “works”, the scope of which is well defined in the contract. The contract was not divisible. The obligations and the risk of the assessee continued till the completion of the work and grant of completion certificate by ONGC. The PE in India existed for the entire duration of the project which commenced with the kick off meeting and ended with the completion of the work. The so called project office acted as PE for the initial part and later the operational part was executed by the project office at a different location. The title in the goods passed in India and PE in India utilized the material on its own account and on its own behalf. Thus, the entire profits from the work under the contract arise in India and are liable to tax as such. He rejected the alternative contention of the assessee that even if the receipts on account of outside India revenues are held liable to be

taxed, the income cannot be computed at more than 10% of such revenues under Section 44BB of the Act and the AO observed that such contention of the assessee is totally misconceived. The assessee has maintained accounts for its India operations. The provisions of Section 44BB are applicable in a case where services are rendered in connection with prospecting for or extraction and exploration of mineral oil. The project is neither for prospecting of mineral oil nor is the assessee rendering any service in the exploration of mineral oil. The work of the assessee is installing a pipeline which may be used by the contractee for exploration of oil but as far as the assessee is concerned, they are not rendering service in connection with the exploration of mineral oil. At best, the assessee is building an infrastructure which may be used in the exploration. While coming to the computation of income, the learned AO has observed that assessee has not been able to substantiate the following expenses:-

(i) Rs.28,00,38,791/- on account of direct expenses.
(ii) Rs.5,75,18,011/- on account of selling and administrative expenses.
(iii) Rs.21,68,31,926/- on account of indirect cost.

29. These sums were disallowed by the AO. The AO further observed that the assessee has debited a sum of Rs.52,13,79,129/- on account of contractor's cost in respect of which TDS has not been deducted. He has further found that out of material cost, the value of steel material has not been given and keeping in view all these facts, he has estimated the income of the assessee at the rate of 25% of the revenue allegedly earned by the assessee outside India at Rs.113,43,78,960/- and has computed the income from such revenue at Rs.28,35,94,740/-. In this manner, the assessment of the assessee

has been framed. The assessee is aggrieved, hence has filed the aforementioned appeal.

30. After narrating the facts, it was submitted by learned AR that as per Article 7(1) of the DTAA between India and Korea, business profits of Korean enterprise can be taxed in India only if Korean enterprise carries on a business in India through a PE situated in India. Thus, he submitted that existence of PE in India is a sine qua non to bring into tax Korea entity in India. He further submitted that Article 5(1) and (2) define permanent establishment and as per provisions of Article 5(1) unless core business activities are carried on through a fixed place in India, no PE can be said to have come into existence. He also referred to the OECD commentary, according to which, the requirements of Article 7 are as under:-

> "7. **For a place of business to constitute a permanent establishment the enterprise using it must carry on its business wholly or partly through it**. As stated in paragraph 3 above, the activity need not be of a productive character. Furthermore, the activity need not be permanent in the sense that there is no interruption of operation, **but operations must be carried out on a regular basis.**"

31. It was further submitted that examples also have been set out in para (2) of Article 5 which, if read in juxtaposition with the general definition under para 1 of Article 7, then, here existence of 'place of management' or 'a branch' or 'an office' is not sufficient to conclude that there exists permanent establishment of the non-resident in India and it has to be demonstrated with the evidence that the business of the non-resident is wholly or partly carried on through such place of management, office or branch. Reference in this regard was made to the following commentary given with regard to para 2:-

> "Paragraph 2
> 12. This paragraph contains a list, by no means, exhaustive, of examples, each of which can be regarded, prima facie, as

constituting a permanent establishment. As these examples are to be seen against the background of the general definition given in paragraph 1, it is assumed that the Contracting States interpret the terms listed, "a place of management", "a branch", "an office", etc. in such a way that such places constitute permanent establishments only if they meet the requirements of paragraph 1.

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11. A permanent establishment begins to exist when the enterprise commences to carry on its business through a fixed place of business. This is the case once the enterprise prepares the activity for which the facility is permanently to be used. The period of time during which the fixed place of business itself is being set up by the enterprise should not be counted, provided that this activity differs substantially from the activity for which the place of business is to serve permanently. The permanent establishment ceases to exist with the disposal of the fixed place of business or with the cessation of any activity through it, that is when all acts and measures connected with the former activities of the permanent establishment are terminated (winding up current business transactions, maintenance and repair of facilities).

32. He also referred to the decision of Delhi Tribunal in the case of R&B Falcon Offshore Ltd. vs. ACIT in ITA Nos.389/Del/2005 and 4752-4753/Del/2005 to contend that mere existence of an office is not sufficient to hold that such office constituted PE of the non-resident in India and it must be demonstrated that evidence that 'business of the non-resident' is wholly or partly carried on through such 'place of management' 'office' or 'branch'. Reference in this regard was made to para 9 of the said order.

33. He further referred to Article 5 (4) of DTAA and contended that fixed place of business in India carrying on the work which is of preparatory or auxiliary in nature vis-a-vis business of non-resident would not be construed as resulting in PE in India. He submitted that according to the facts of the case, the assessee along with the L&T was awarded VED project by ONGC on 28th February, 2006. At the instance

of ONGC the assessee opened a project office in India. Application was made to RBI and approval was granted by RBI on 24th May, 2006. The assessee employed only two persons, namely, Mr. S.S. Park (MBA) and Mr. Ravinder D Joshi (Accountant) at the project office. Both of them are non-technical people and were entrusted to act as interface/communication channel between the assessee and ONGC. Pre-contract meeting was held in January and February, 2006 which could not have been carried out by the project office which came into existence only in May, 2006. The personnel deputed at the project office did not have the technical competence to carry out the work under the contract with ONGC.

34. He further submitted that the activities like pre-engineering survey, etc. were carried out through contractors, viz. Fugro Geonics (P) Ltd., and Offshore Hook-up and Construction Services India (P) Ltd., who were awarded contracts by the Korean head office. The said activities were carried out for a period of 1-3 days and that too to facilitate the design, engineering and fabrication activities being carried out outside India. There is no evidence on record to prove that the said activities were carried on through project office of the assessee and no such finding have been recorded either in the assessment order or in the order passed by the DRP that such activities are either conducted through the project office or the project office had any role in facilitating such activity. These activities were for un-substantial period of time during the relevant previous year and no other activity was carried out. If insurance cost of 22.66 crore is excluded from the total expenditure of 23.9 crore incurred during the relevant previous year, the expenditure incurred in India in relation to the project was only Rs.1.3 crore which is less than 1% of the revenue relatable to the activity to be performed in India and on that ground also it cannot be alleged that any substantial activity was carried out in

India, leave aside the same having been conducted through the project office.

35. The nature of expenses incurred by the project office the copy of which is placed at page 521 of the paper book-I would show that the same were in the nature of general administrative expenses like rent, telephone, printing, salary, etc. and no technical work was carried out by the project office.

36. It was further submitted that the project office was to act only as a communication channel between the ONGC and the assessee for the purpose inter alia, recovering invoices received by the head office on ONGC and passing them on to ONGC, recurring milestone completion certificates from ONGC and transmitting the same to head office, arranging security clearance as and when required for personnel and equipment. He submitted that there is no evidence on record to suggest that the project office had undertaken anything apart from acting as an interface between the assessee and ONGC. He submitted that even if it is admitted that some activity was undertaken from the project office, the said activity being preparatory and auxiliary in nature vis-a-vis the scope of the overall project which included inter alia all design, engineering, fabrication and installation, the project office cannot be treated as PE of the assessee in India in view of the clear mandate of Article 5 (4) of DTAA.

37. Then, Ld. AR referred to the provisions of Article 5 (3) and his contention is that the same being special provision has overriding effect over other provisions. He submitted that the work to be performed by the assessee in India related to installation of platforms which were designed and fabricated outside India and also hook up and commissioning of the said platform with the existing ones after modification. Thus, the assessee had undertaken to execute an

installation project in India and, therefore, what was relevant to determine was whether the assessee had an 'installation PE' in India in terms of Article 5(3) of the DTAA and not fixed place PE.

38. He also referred to the revised OECD commentary which state that enterprises in India engaged in construction/installation activities are more appropriately covered under Article 5(3). In such a case it is essential that installation activities should have commenced and that such activity carries for more than the threshold period prescribed in the applicable DTAA in order to constitute a PE in the source of jurisdiction. The relevant extract from the said commentary was referred to as below:-

> "16. This paragraph provides expressly that a building site or construction or installation project constitutes a permanent establishment only if it lasts more than twelve months. **Any of those items which does not meet this condition does not itself constitute a permanent establishment, even if there is within it an installation, for instance an office or a workshop within the meaning of paragraph 2, associates with the construction activity. Where, however, such an office or workshop is used for a number of construction projects and the activities performed therein go beyond those mentioned in paragraph 4, it will be considered a permanent establishment if the conditions of the Article are otherwise met even if none of the projects involve building site or construction or installation project that lasts more than 12 months."**

39. Ld. AR further referred to the decision of the Delhi Tribunal in the case of Hyundai Heavy Industries (2009) 31 SOT 482 wherein it was held that mere existence of a project office could not be held to be constituting PE, given the nature of the contract which was pre-dominantly in the nature of installation project. Reference was made to the observations of the Tribunal in para 10 and 11 of the said order. It was submitted that in the present case the work to be undertaken by the assessee was undisputedly in the nature of an installation project, therefore, mere existence of project office is not sufficient to constitute PE. Installation PE can be said to have come into existence only if

installation activity had commenced during the relevant previous year. He submitted that on the facts, in the present case, the fabrication, design and engineering of the platform and jacket was sub-contracted to Aker Malaysia and the said activity was carried on outside and reference in this regard was made to page 323 to 325 of the paper book and also 568 onwards of the paper book II where invoices and completion certificate issued by ONGC have been placed. He submitted that jackets after fabrication outside India started arriving in India only in November, 2007 and, therefore, the installation activity could not be said to have commenced prior thereto. As installation PE having not come into existence during the relevant previous year, no part of income is liable to be taxed in India. Therefore, the Assessing Officer is wrong in applying the provisions of Section 5 (1) of DTAA to hold that the assessee had fixed place PE in India during the relevant previous year in the form of a Project office. In this manner, Ld. AR of the assessee has concluded his argument with respect to the point to contend that the assessee's PE did not exist in India during the year under consideration, hence, no part of assessee's activity relating to outside India operation could be brought to tax by the Assessing Officer.

40. On the other hand, it was submitted by Ld. DR that the grounds of appeal raised by the assessee in the present case is in respect of two main issues: (i) about existence of PE; and (ii) about attribution of profits to such PE. It was submitted that Hon'ble Bench has proposed to decide first the existence or otherwise of PE and his arguments for this issue are as under.

41. It was submitted by Ld. DR that the very fact that the assessee had filed its return of income is sufficient to establish that the assessee was conscious of the fact that its PE is in existence in India. He submitted that as per Article 7 of the DTAA a non-resident enterprise is

taxable in India only if there exist a PE in India. He submitted that learned counsel of the assessee made a statement that in its return of income only income from inside India activity has been declared and, therefore, it cannot be said that the assessee was conscious of existence of PE. He submitted that the said statement of ld. Counsel is legally incorrect as it is against the very first principle contained in Article 7 of DTAA which states that non-resident enterprise can be taxed in India only if PE exist in India. He submitted that this is true for any kind of business income whether from inside India activity or outside India activity. According to Article 7 even income from inside India activity is not taxable if there is no PE in India. The very fact that the assessee has furnished income tax return declaring income from inside India activity indicates that the assessee has no doubt in its mind about the existence of PE in India particularly when it has not given any note in its return of income in this regard. He referred to page 321 of the paper book which is minutes of Board of Directors meeting signed by the President & CEO of the assessee and copy of such minutes is placed at page 321 of the paper book. He submitted that the contents of the said minutes are as under:-

> " The co. hereby open one project office in Mumbai, India for co-ordination and execution of Vasai East Development Project for ONGC.
>
> That the co. hereby does make, constitute and MR. SangSoon Park Yard General manager of the co., as the company's true and lawful representative with full power and authority of the purpose of establishing a project office and co-ordinating and executing delivery documents in connection with construction of offshore platform and modification of existing facilities for ONGC above."

42. Ld. DR further referred to page 323 of the paper book which is a letter dated 25th May, 2006 and which is an approval from RBI regarding such project office. He submitted that this approval

indicates that there is a project office opened in Mumbai for carrying on and execution of contract with ONGC. Therefore, she submitted that project office is PE under Article 5(1) of DTAA and he referred to the Article 5 (1) of DTAA which read as under:-

> "For the purposes of this convention, the term permanent establishment means a fixed place of business through which business of enterprise is wholly or partly carried on."

43. Therefore, ld. DR submitted that there are two requirements for existence of PE under Article 5 (1); one is that there should be a fixed place of business and the second is that business of the enterprise should be wholly or partly carried on through that fixed place. He submitted that as project office is a fixed place having an address in Mumbai, therefore, the first condition is satisfied. The resolution of Board of Directors that this project office is opened for carrying on and execution of contract with ONGC is an admission on behalf of the contractor that the contract with ONGC is executed through its project office and such a situation satisfies the second condition also. Therefore, he submitted that the project office of the assessee in Mumbai fulfills the condition laid down for existence of PE in India as per Article 5(1) of the DTAA.

44. He submitted that Ld. AR of the assessee has contended that no activity was done through project office in relation to contract and in fact project office was opened at the insistence of ONGC; the letter from board of director of the company is just a formality and the project office was never intended to be used for co-ordination and execution of the contract; the project office was manned by only skeletal staff and it was used for exchange of communication between ONGC and assessee company in Korea. He further submitted that Id. AR has explained that documents like approval for mile stone payments were routed through the project office and he has further

contended that whatever activities were done through project office are in nature of auxiliary or preparatory in nature and hence project office does not constitute PE; the project office was used for arranging security pass for visiting officials of the company which does not amount to carrying on of business of contract; that the Assessing Officer has not put up any positive evidence to prove that some commercial activities were done in the project office. Ld. DR submitted that in this manner, Ld. AR has tried to compare liaison office with project office and contended that courts have held that unless it is proved that some commercial activity is done in LO, it does not constitute PE. He submitted that such arguments of ld. AR cannot be accepted because resolution of the board of directors is a positive evidence to show that project office was opened for co-ordination and execution of contract with ONGC and vide the said resolution, the assessee has appointed a lawful representative for co-ordination with ONGC. He submitted that in view of such positive evidence which amounts to self admission on the part of the assessee, what else will be required to be proved the existence of PE by the AO. He submitted that ld. AR has also not led any evidence to establish that the positive assertion by board of directors was incorrect or was not meant to be so. The terms of contract clearly indicate that there will be continuous co-ordination between ONGC and the assessee which is required at all the stages of execution of contract.

45. He referred to para 2.3.4.1 of the contract which says that the company and the contractor shall discuss and agree upon the work procedures to be followed for effective execution of the work. Referring to Para 2.3.5.1 of contract, he submitted that the contractor shall authorise the supervisor or his representative to receive directions and instructions from the company's representatives or engineer's representatives. He submitted that as mentioned earlier, the resolution of the board of directors has appointed a representative for

the purposes of co-ordination with ONGC. Ld. DR further referred to Para 5.1.7.2 which is regarding review and approval of design and engineering which says that design and engineering shall be reviewed and approved by ONGC continuously. Para 5.1.9 is regarding drawing and specification records which stipulates that all drawings, specifications and data sheets shall be approved by the ONGC. Para 5.1.10 says that even purchases to be made by assessee company were to be approved by ONGC. He submitted that these terms of contract clearly indicate that ONGC has to be continuously in co-ordination with assessee company and for this purpose assessee company has appointed a representative in its project office. Therefore, he contended that the project office is meant for continuous co-ordination with ONGC which is important part of the contract, therefore, obviously, these activities are not auxiliary or preparatory in nature as these are vital part of contract itself and without these, contract can not be executed. He submitted that ld. Counsel for assessee has accepted that certain documentation like approval of mile stone payments etc. were exchanged through project office and, according to him, some degree of co-ordination was affected through project office. He submitted that as per the requirement of Article 5(1) of DT AA the business should be wholly or partly carried on through fixed place so as to make it a PE. He submitted that in view of acceptance by the ld. AR that some co-ordinating activities were carried out through project office, it amounts to carrying on of assessee' business through project office though those may or may not be significant enough from the point of view of attribution of income. He submitted that project office cannot be compared with liaison office and such argument of ld. AR is misplaced because under rules, LO is invariably permitted to be opened for only for liaison purpose and no commercial activity is permitted through it, whereas the project office is permitted to be opened for execution of a

project. Thus, he submitted that these are two species of offices which are absolutely unlike and if it is a project office and project has been carried on through that office, then, the onus is not on the Assessing Officer to prove that the project is executed through it.

46. Coming to another argument of ld. AR regarding installation PE under Article 5 (3) and his reliance upon the decision of Hon'ble Supreme Court in the case of Hyundai Heavy Industries Ltd. (supra), Ld. DR submitted that such contention of assessee's counsel is against the principles contained in Article 5 of DTAA which is regarding permanent establishment. He submitted that according to scheme of Article 5, fixed place PE under Article 5(1) is the primary form of permanent establishment which comes into existence if two conditions are fulfilled. Such fixed place PE is based on 'permanence test' and it is irrespective of kind of business of the assessee. He submitted that there can be certain kind of business which do not require a fixed place for its execution and, thus, the assessee may claim that as there is no fixed place PE, its income cannot be taxed. To take care of such situations, Article 5(3) relaxes permanence test for building, construction or installation projects and has laid down 'duration test' for PE to exist. He submitted that Article 5(3) does not preclude Article 5(1) and hence it cannot be said that there cannot be a fixed place PE in case of kinds of businesses mentioned in Art 5(3). He submitted that it will be pertinent that only income attributable to activities done through such fixed place PE can be brought to tax and such view has been clearly expressed in OECD commentary in paragraph 3 of Article 5 and there is no question of Art 5(3) being over ridden by Article 5(1).

47. He submitted that application of the decision in the case of Hyundai Heavy Industries Ltd. (supra), to the facts of the present case is misplaced because in that decision nowhere it has been laid down by hon'ble Supreme Court that in a contract involving designing,

fabrication and installation, there can only be installation PE and no fixed place PE. He submitted that the facts in the case as noticed by Hon'ble Supreme Court were that the said concern had entered into a contract with ONGC for designing, fabrication, hook-up and commissioning of a platform. The agreement was in two parts, one for fabrication of structure in Korea and other for its installation and commissioning. After fabrication, platform was handed over to ONGC in Korea. In these circumstances, it was held by Hon'ble Supreme Court that the activities upto fabrication of platform have occurred outside India and hence these cannot be attributed to Installation PE which came into existence after fabrication was completed. He submitted that in that case, the department did not allege that there was a PE before handing over of platform in Korea and in such a situation, Hon'ble Supreme Court has held that since installation PE came into existence after fabricated platform was handed over to ONGC in Korea, activities prior to handing over of platform cannot be attributed to such installation PE. After installation PE came into existence, income has been held to be attributable to it. He submitted that Hon'ble Supreme Court has nowhere held that there cannot exist any PE before start of installation stage. The crucial fact in that case was that the department did not allege that there was any PE before start of installation stage. He drew our attention to the following para from the said decision:-

> "There is one more aspect to be discussed. The attraction rule implies that when an enterprise sets up a permanent establishment in another country, it brings itself within fiscal jurisdiction of that other country to such a degree that such other country can tax all profits that GE derives from source country whether through permanent establishment or not. It is act of setting up of permanent establishment which triggers the taxability of transactions in source state. Therefore, unless permanent establishment is set up, the question of taxability does not arise - whether transactions are direct or through permanent establishment. In case of turnkey project, permanent establishment is set up at installation stage while entire turnkey project including sale of equipment is finalized before installation stage. The setting up of permanent establishment in such a case is a stage subsequent to conclusion of contract. It is

> as result of sale of equipment that the installation permanent establishment comes into existence. However, this is not an absolute rule. In present case, there was no allegation made by department that permanent establishment came into existence even before sale took place outside India "
>
> (emphasis upplied)"

48. He submitted that the fact as found by the Hon'ble Supreme court was that the contract of the assessee in that case with ONGC is divisible into two parts, one is fabrication and sale of platform and the other is its installation. The sale of fabricated platform occurred in Korea. In view of these facts, Hon'ble Supreme Court has held that the contract of sale of equipment is finalized before installation stage and upto installation stage there was no PE in existence and that existence of PE was not even alleged by the department. Therefore, the activities upto the sale of platform in Korea could not be attributed to installation PE which came into existence later on after the installation actually started.

49. He submitted that according to the facts of the present case, during the period under consideration, fabrication stage has started and installation started only during next year as is evident from chart given by the Assessing Officer at page 28 of his order. He submitted that thus, there is no question of installation PE coming into existence during the period under consideration. He submitted that admittedly, there were no installation activities during the year under consideration, therefore the contention of the assessee that only installation PE can exist in such cases and no other kind of PE can exist should not be accepted. He submitted that the project office is a fixed place of business and unlike in the case of Hyundai Heavy Industries Ltd. (supra), in the case of the assessee, there is no sale of fabricated platform outside India, and, rather in the present case, the sale occurred in India only after successful installation of platform as is evident from clause 7.1.1 of contract which stipulates that the

ownership of material shall be transferred to ONGC upon the date of issuance of certificate and it is at the completion or completion and acceptance of works. Therefore, he contended that unlike the case of Hyundai Heavy Industries Ltd. (supra) the contract is not divisible in assessee's case and it has been demonstrated in earlier arguments that the fixed place PE of project office is in existence since start of the contract and it has been used by the assessee for co-ordination and execution of contract with ONGC. Thus, he submitted that there is vital difference in the facts of the case of the Hyundai Heavy Industries Ltd. (supra), when they are compared to the facts of the case of the assessee.

50. It is further contended by Ld. DR that so as it relates to reliance by the Ld. AR on the decision of the Tribunal in the case of DCIT v. Hyundai Heavy Industries Co. Ltd. [2009] 31 SOT 482 (Delhi) a copy of which is placed at pages 72 to 78 of paper book wherein in para 11 ITAT has held that provisions of Article 5(3) are specific and therefore they will over-ride the provisions of Article 5(1) and 5(2). He referred to the observations of the Tribunal in para 11 on page 492 where it was observed by the Tribunal that the assessing officer was not able to show that PE of the assessee existed in India before fabrication and, in this manner, the ITAT, following the decision of Hon’ble Supreme Court has held that profits before fabrication stage could not be taxed because there exist no PE before installation stage. He contended that Hon'ble Supreme Court in the case of Hyundai Heavy Industries Ltd. (supra) has no where held that Article 5(3) takes precedence over Article 5(1) and 5(2) and such observations of ITAT is not even supported by OECD commentary in paragraph 3 of Article 5. He also contended that in the last line of para 11 on page 493 it has been observed by the ITAT that project office in that case did not carry out any commercial activity as these were prohibited by the RBI. So, ld.

DR contended that the facts of the case of the assessee are vitally different from the case of Hyundai Heavy Industries Ltd. (supra). In the present case, there is a fixed place PE during fabrication stage as has been argued earlier and RBI had placed no restriction on the project office from doing any commercial activity. He submitted that in view of his arguments it should be held that PE of the assessee exists under Article 5(1) in the form of project office in Mumbai and so as it relates to attribution of income to such PE, the matter may be decided accordingly after hearing both the parties.

51. In the rejoinder, it was submitted by ld. AR that mere filing of the return does not lead to the conclusion that the appellant had a PE India. The return of income was filed on the presumption that the contract was divisible contract. While loss in respect of inside India revenues was disclosed, outside India revenues were not offered for taxation on the ground that PE in India did not come into existence during the relevant year. He submitted that without prejudice to the above, there is no estoppel in law in resiling from a position incorrectly taken in the return of income and considered in that light, even if the assessee had filed a tax return on the presumption that there was PE in India, such position mistakenly taken could be resiled in the proceedings before the assessing authority or the appellate authorities and, in this regard, he placed reliance on the decision in the case of CIT v. Bharat General Reinsurance Co. Ltd.: 81 ITR 303 (Del) and also the decision of the Special Bench of the Tribunal in the case of Indo Java & Co. v. lAC, 30 ITD 161 (SB)(Del). He submitted that the question whether the assessee has a PE in India or not has to be determined with reference to the fact of the case and the position in law and not on the basis of filing of return of income by the assessee, more so where the assessee has resiled from the position taken in the return.

52. He further submitted that the Board Resolution, in fact, only authorized the project office to coordinate and execute delivery documents. The said project office was, therefore, not empowered to do anything beyond acting as an interface or a channel of communication between the assessee and the ONGC. He submitted that the word 'execute' in the first part of the resolution have to be read not de hors but in conjunction with the later part of the said resolution, which explains that the term ‘execution’ has been used only with reference to delivery of documents. He submitted that in any case, the personnel deputed at the project office were not technical persons and were not capable of carrying out any work for which the assessee was engaged by ONGC under the contract. He submitted that no evidence has been placed by the Assessing Officer or by the ld. CIT (DR) to demonstrate that the project office was involved in executing the VED project. The nature and quantum of expenses incurred by the project office, on the other hand, amply demonstrate that no work in relation to the project was executed by the project office and it was only acting as a communication channel between the assessee and the ONGC.

53. With reference to the contention of Ld. DR that the business of the assessee was carried on through Project Office for which the reliance was placed by Ld. DR on various clauses of the contract agreement, it was submitted by Ld. AR that such argument of Ld. DR is erroneous inasmuch as those clauses only authorized the assessee through its representatives to co-ordinate with ONGC regarding the work to be performed by the assessee under the agreement. The representative of the assessee means employees/agents of the assessee duly authorized to deal with ONGC in relation to the contract and this, does not, however, mean that the project office was involved in the execution of the installation project. There was nothing in the

agreement to suggest or any other positive evidence to prove that the work had, indeed, been carried out through the project office of the assessee in India.

54. He submitted that according to the facts of the case the assessee has carried out limited activities in India during the relevant previous year and that, in any case, the project only carried out preparatory and auxiliary activities, as it is evident from the audited statement of accounts and the milestone payment certificates certified by ONGC. He submitted that the burden to prove otherwise was on the Revenue to bring some evidence on record to establish that some activity had, indeed, been carried on through the project office before concluding that the project office of the assessee constituted PE in India. He referred to the decision of the Tribunal in the case of R&B Falcon Offshore Ltd. dated 28.02.2011 in which the Tribunal did not entertain the argument submitted by the Revenue to similar effect on the ground that there was absence of any evidence being brought on record by the Revenue. He submitted that the assessee could not be asked to prove that the project office did not carry out any profit generating activity as that would amount to asking the assessee to prove the negative. He submitted that perusal of audited accounts filed by the assessee along with the milestone certificates issued by ONGC would lead to an inescapable conclusion that during the relevant previous year no substantial activity was carried out In India. The expenditure mainly are incurred in respect of insurance premium. Assuming for the sake of argument that the project office was involved in the execution of the contract, since the duration threshold of nine months in Article 5(3) of the Treaty in relation to the installation project was not crossed during the relevant previous year, as the installation activity began only in the subsequent financial year, the existence of the project office would not result in a PE of the assessee in India in

terms of Article 5(1) of the DTAA, as explained in the OECD Commentary and as held by the Delhi Tribunal in the case of Hyundai Heavy Industries Ltd. (supra). He submitted that the interpretation sought to be conveyed by ld. DR that Article 5 (1) is not overridden by Article 5(3) even in the case of an Installation project would render the duration test under Article 5(3) otiose and, therefore, such an argument of learned DR should not be accepted.

55. Referring to the decision of Hon'ble Supreme Court in the case of Hyundai Heavy Industries Ltd. (supra) ld. AR submitted that normally it is a result of sale of equipment that the installation PE comes into existence but this is not an absolute rule. He submitted it has not been appreciated by Ld. DR that the aforesaid observations of the Hon'ble Supreme Court were not in the context of the issue of fixed place PE vis-a-vis installation PE. It was observed by the court that in a turnkey project, the PE is set up at the installation stage while the entire turnkey project, including the sale of equipment is finalized before the installation stage. However, the aforesaid may not be the case if the Department demonstrates that PE comes into existence even before the sale took place outside India, e.g., in a contract for only supervision of installation/construction activity, the installation PE of a non-resident may come into existence as soon as the supervisory activities are undertaken by the non-resident assessee and the existence of such a PE would be independent of the supply of material. He submitted that in the present case the project office was set up after the contract had been awarded to the assessee by ONGC and had no role to play either in procurement of the contract or the installation activity to be carried on by the appellant, which started only in November, 2007. He submitted that the aforesaid decision of the Supreme Court supports the case of the assessee notwithstanding the existence of a project office in India, which was held to be constituting

PE of Hyundai by the lower authorities, it was held by the apex Court that the PE of Hyundai came into existence only after the fabricated platforms were delivered to the agents of ONGC in Korea and he drew our attention towards the following observations of the Hon'ble Supreme Court in the said decision:-

> "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, still 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 as 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." [Emphasis supplied]

56. Thus, it was submitted by the Ld. AR that the project office of the assessee did not constitute PE of assessee in India and, therefore, the assessing officer has erred in bringing to tax revenues relating to outside India activity carried out by the assessee.

57. In this manner, both the parties concluded their arguments.

58. We have carefully considered the rival submissions in the light of the material placed before us. We have carefully gone through the

contract entered into between the assessee and L & T on the one part and ONGC on the other part in pursuance of which the revenue has been received by the assessee. We have also carefully gone through the papers/documents referred to by both the parties during the course of hearing and referred by them in the synopsis filed for their arguments. It is the main case of learned AR that though the existence of PE in India is sine qua non to tax the assessee in India, but the assessee does not have a PE in India for the year under consideration as no core business activity has been carried out through fixed place (Mumbai Project Office); the assessee is governed by the provisions of Article 5 (3) which regulates installation PE, therefore, the provisions of Article 5 (3) being specific provision will have overriding effect over the general provisions contained in Article 5 (1) and 5 (2); the activity, if any, carried on by Mumbai Project Office is in the nature of preparatory or auxiliary in nature which falls under the exception laid down in Article 5 (4) of the DTAA; according to the accounts maintained by the assessee, Mumbai Project Office has not incurred any expenditure relating to execution of contract and details of expenditure therein will show that it had no role in carrying on the core business activities on the basis of which the assessee can be taxed in India on the activities carried on by it outside India; the contract of the assessee is divisible in two parts and before fabricated platform was deported from Malaysia, where it has been fabricated, installation PE cannot be said to have come into existence, therefore, prior to that point of time no part of outside India activity can be taxed in India in the absence of the installation PE; the revenue received by the assessee mainly constituted insurance cost and if the same is ignored, then, negligible work has been carried out by the assessee which is less than 1% of the revenue relatable to the activities to be performed in India.

59. On the other hand, it is the case of the department that the PE of the assessee came into existence upon the event of opening of Mumbai Project Office; the submission of the return of income by the assessee itself will show that the PE of the assessee had existed in India as in the absence of PE no part of income of the assessee can be taxed in India; the documents in the shape of minutes of Board of Directors Meeting, the letter issued by the RBI allowing the assessee to open Project Office in Mumbai and the contents of these documents prove beyond doubt that Mumbai Project Office was opened to carry out the work allotted by the ONGC and all these documents are sufficient to come to the conclusion that the PE of the assessee was existing in India at all points of time; the onus does not lie on Assessing Officer but on the assessee as it is only the assessee, who is claiming that no part of its income is taxable in India despite the fact that assessee has PE in India in the shape of Mumbai Project Office; no further proof was required to be submitted by the Assessing Officer as the onus will be on the assessee to prove to the contrary; various clauses of the contract will show that the contract is indivisible and the revenue received by the assessee in pursuance of such contract was taxable in India right from the beginning to the extent profit attributable to such PE; the decision in the case of Hyundai Heavy Industries Ltd. (supra) cannot be applied to the case of the assessee as there is material difference in the facts of that case and the facts of the case of the assessee; in the case of the assessee, Mumbai Project Office having come into existence, the PE was established under Article 5(1), therefore, one does not need to go to the provisions of Article 5 (3) as the case of the assessee falls under Article 5 (1) which has equal force. Therefore, it is the case of the revenue that the assessee is liable to pay tax on the revenue received/receivable by it in respect of the contract with ONGC to the extent the profit is attributable to PE in

India, irrespective of the fact that those activities are carried on by the assessee either in India or outside India.

60. To examine the contention of both the parties, it is necessary to dwell upon the terms of the contract to find out whether the contract was divisible one so as to say that one part of it was related to fabrication of platform and the other part of it was related to installation or commissioning of the said platform. Some of the terms of the contract have already been referred to and reproduced in the above part of this order. The nature of work given in the recital of the agreement has been described in para 3 of this order and the work of the assessee start from the survey to be done with regard to the activity of pre-engineering, pre-construction/pre-installation and post construction and it include design, engineering, procurement, fabrication, anti corrosion and weight coating, load out, tie down/sea fastening, tow out/sail out, transportation, installation, modifications at existing facilities, hook up testing, etc. Though earlier the work of modification to existing facility was agreed to be carried out by L & T in the MoU arrived at between the assessee and the L & T, but, later on, by amendment in MoU, modification to existing facility was assigned to the assessee.

61. The price which was to be received by the assessee in respect of work to be carried on by it in pursuance of the contract has been stated in para 7 of this order. The scope of the work has been described in para 10 of this order and the existing facilities have been described in para 11 of this order. The effective date of commencement of the contact is 24th January, 2006 and the completion date is 2nd April, 2008. The assessee was under an obligation to supply to ONGC within 21 days of the effective date of commencement of work and prior to kick off meeting, whichever is

earlier, an organization chart showing the proposed organization to be established by the contractor for execution and work including the identities and curriculum vitae of the key personnel to be deployed and any revision or alteration to such organization chart was also to be promptly informed by the assessee company. These terms have been described in para 13 of this order.

62. In para 14 of this order, it has been stated under clause 3.1 of the contract that the contract price is a firm price and the contractor shall be bound to keep the same firm and without escalation on any ground whatsoever until completion of the entire work against the contract.

63. In para 15 the payment procedure has been described under clause 3.2 and it has clearly been mentioned that the payments pending the completion of whole work are **provisional progressive payments** for the part of the work executed by the contractor on the basis of completion and certificate issued by the ONGC representative in accordance with the milestone payment formula provided in the bidding document. The payment as per mile stone formula does not in any manner indicative of the consideration of the work completed by that point of time so as to make the said payment relatable to the respective part of the work contract to say that the payment made is only for that part of work. Therefore, on the basis of payment schedule mentioned in mile stone formula cannot be interpreted to be payment made by ONGC to the assessee relating to the work on completion of which payment is released as it has been clearly mentioned in this clause that it is only in the shape of provisional progressive payment. What is material for ONGC is not that part of the contract but completion of whole of the contract itself. Thus, it can be clearly seen that the amount to be paid to the assessee in accordance with the

milestone payment formula are not the payment with regard to the work completed by that time, but it is only a provisional progressive payment which was to be made to the contractor.

64. Further according to the terms of clause 3.2, no payment shall be due and payable to the contractor until the contract is signed by the two parties and the contractor furnishes to the company a performance guarantee as per clause 3.3 and certificate of insurance for policy/policies specific for the project as per requirement of clause 7.3 and a copy of permission from Reserve Bank of India for opening project office in India. Such stipulation is in clause 3.2, the relevant portion of which is described in para 15 of this order and these terms will clearly reveal that the nature of the contract is indivisible. Any payment made in pursuance of contract will become due only on the fulfillment of the condition of submission of performance guarantee, certificate of insurance policy/policies for the project and a copy of permission from Reserve Bank of India for opening project office in India. Thus, for the contract it was a condition precedent to obtain permission from the Reserve Bank of India for opening Project Office in India. There is no dispute to the effect that the assessee had opened its project office in India on 24th May, 2006 and the said fact has been described in para 17 of this order. The revenue which has been recognised by the assessee is also described in para 17 of this order which is relating to hook up and commissioning, insurance and pre-engineering and surveys.

65. Thus, it can be seen from the above discussion that the contract obtained by the assessee from ONGC is a composite contract starting right from surveys of pre-engineering, pre-construction/pre-installation, design engineering procurement etc. till the startup and commissioning of the entire facilities. The duration of the contract as

per agreement is from 24.1.2006 till 2.4.2008. The assessee was under obligation to supply to ONGC within 21 days of effective date of commencement of work and prior to kick of meeting, whichever is earlier, an organization chart showing the proposed organization to be established by the contractor for execution and work including the identities and curriculum vitae of the key personal to be deployed and any revision or alteration to such organization chart was also to be promptly informed by the assessee company. As a condition precedent, the assessee company was required to open a project office in India before the commencement of the activity of the contractor. It will be relevant here to describe the contents of the application submitted by the assessee to RBI for opening the project office which is dated 24.4.2006, a copy of which is also placed at page 316 of the paper book which read as under: -

General Manager
Reserve Bank of India
Regional Office *April 24, 2006*
Mumbai

Dear Sir,

Re: M/s Samsung Heavy Industries Co. Ltd. (SHI)
Application for registration of Project Office

Our aforesaid client (SHI) has entered into contract with M/s Oil and Natural Gas Corporation Ltd. (ONGC) vide contract number MR/OW/MM/VED/03/2005. Under the instructions of our above-referred client, we have to enclose following documents in connection with Registration of Project office in India:

1) *Letter dated (.....) on the letter head of the company for the details of the project as Notification FEMA 95/2003-RB dtd. 2nd July, 2003 Foreign Exchange Management (Establishment in India of Branch or Office or other place of business) (Amendment) Regulations 2003 along with the copy of letter from ChoHung Bank for opening Bank account.*

2) Copy of the POA in our favour and in favour of M/s Hemand Arora and Co., CA.
3) Certified copy of the POA in the name of the Mr. S.S. Park, who has signed the application.
4) Certified copy of the certificate of registration of the company in South Korea.
5) Certified copy of the notarized Board Resolution for opening a Project office in India.
6) Certified copy of Extract of contract entered into by our client.

Kindly take the above documents on record. Please take on record our clients Project office and register the same. If you require any clarification, please let us know.

Thanking you,

66. It will also be relevant to reproduce copy of power attorney given by the assessee company to Mr. S.S. Park through Jing Wan Kim, President and CEO of the assessee company, a copy of which is placed at page 318 of the paper book.

To Whom It May Concern:

I, the undersigned hereby duly certify that Mr. SangSoon Park, General Manager of Samsung Heavy Industries Co., Ltd., has been appointed as our representative to sign the documents for opening of a project office and bank account in India and look after the operations of project office in respect of our contract with ONGC for Vasai East Development Project at Mumbai, India.

This power of Attorney shall remain in full force until our further notice.

I confer onto Mr. SangSoon Park of Samsung Heavy Industries Co. Ltd., whose signature is described as

Sd/-
the power to represent our company, Samsung Heavy Industries Co. Ltd., in overall decisions of activities to be required in the India relating to

opening of a Project Office and bank account for performance of Vasai East Development Project.

Jing Wan Kim
President & CEO

For Samsung Heavy Industries Co.Ltd.

67. Copy of resolution of Board of Directors dated 3.04.2006 for opening of Mumbai Project Office is placed at page 320 of the paper book which read as under: -

To Whom It May Concerned

RESOLUTION OF THE BOARD OF DIRECTORS

We hereby certify that the following Resolution of the Board of Directors of Samsung Heavy Industries Co., Ltd. ("SHI") was passes at a time of the Board meeting held on April 3, 2006 and has been duly recorded in the Minute Book of the said Company:

"Resolved: SHI a Corporation duly organized and existing under laws of the Republic of ;Korea, and with its principal business office at 11th Floor, KIPS Bld., 647-9, YoksamDong, Kangnam-Ku, Seoul, Korea, 135-080, that the opening Mumbai project office and Bank account in India for Vasai East Development Project with Oil and Natural Gas Corporation Limited, India ("ONGC").

"Resolved further, that Mr. SangSoon Park is fully authorized to the opening of Project Office and Bank Account in India for ONGC Project."

In Witness Whereof, I have hereunder set my hand on this 3rd April in 2006.

Samsung Heavy Industries Co. Ltd.
SAMSUNG HEAVY INDUSTRIES CO. LTD.

647-9, Yoksam-Dong, KangnamKu, Seoul, Korea, 135-080

68. Minutes of the Board of Directors meeting of the assessee company held for opening of Mumbai Project Office in India is placed at page 321 which read as under: -

MINUTES OF BOARD OF DIRECTORS' MEETING
OF
SAMSUNG HEAVY INDUSTRIES CO. LTD.

A meeting of the Board of Directors of Samsung Heavy Industries Co. Ltd. (the "Company") was duly called and held on the 3rd day of April 2006 at the office of the Company in Seoul the Republic of Korea, at which 3 of 3 Directors were present and acting throughout.

Jing Wan Kim, President and CEO of Samsung Heavy Industries Co. Ltd. announced that the notice of meeting was duly given to all Directors and a quorum was present and the meeting was duly called to order and held.

RESOLVED:

1. ***That the Company hereby open one project office in Mumbai, India for coordination and execution of Vasai East Development Project for Oil and Natural Gas Corporation Limited ("ONGC"), India.***

   That the Company hereby does make, constitute and Mr. SangSoon Park Yard General Manager of the Company, as the Company's true and lawful representative with full power and authority for the purpose of establishing a project office and coordinating and executing delivery documents in connection with construction of offshore platform modification of existing facilities for ONGC above.

IN WITNESS WHEREOF, the President and Directors present at the meeting have hereunto affixed their names and seals on this 3rd day of April 2006.

Sd/-
Samsung Heavy Industries Co., Ltd.
President and CEO
Jing Wan Kim

(emphasis ours)

69. Copy of approval given by RBI is placed at page 322 which read as under:

FEO, Mumbai CAD/080/04.02.2001/05-06 24th May, 2006

M/s Davesh K. Shah & Co.,
Chartered Accountants,
106, Banaji House,
361, Dr. D.N. Road,
Flora Fountain,
Mumbai 400 001.

Dear Sirs,

Registration of Project Office – M/s Samsung Heavy Industries Co. Ltd. – (SHI)

Please refer to your letter dated 24th April, 2006 on the captioned subject. In this connection, we advise having noted a Project Office in India in terms of prevision contained in AP (DIR Series) Circular No. 37 dated 15th November, 2003.

Yours faithfully,

Sd/-
(A.D. Kala)
P. General Manager

70. It can be seen from all the above documents that the scope of Mumbai Project Office has neither been restricted by the assessee company itself or it has also not been restricted by RBI in any terms.

This is relevant for the reason that in Hyundai Heavy Industries case, it is a matter of record that project office opened by the said assessee, according to permission given by RBI, was to work only as a liason office and was not authorized to carry on any business activity. This is the vital difference between the two cases namely the case of the assessee and Hyundai Heavy Industries case.

71. There is a force in the contention of ld. DR that the words "*That the Company hereby open one project office in Mumbai, India for coordination and execution of Vasai East Development Project for Oil and Natural Gas Corporation Limited ("ONGC"), India"* used by the assessee company in its resolution of Board of Directors meeting dated 3rd April, 2006 makes it amply clear that project office was opened for coordination and execution of impugned project. In absence of any restriction put by the assessee in the application moved by it to RBI, in the resolutions passed by the assessee company for the opening of the project office at Mumbai and the permission given by RBI, it cannot be said that Mumbai project office was not a fixed place of business of the assessee in India to carry out wholly or partly the impugned contract in India within the meaning of Article 5.1 of DTAA. These documents make it clear that all the activities to be carried out in respect of impugned contract will be routed through the project office only. Pre-surveys were to be first conducted which will determine the nature of the designing on the basis of which pre-engineering and pre-designing was to be done with respect to entire project. The next main condition of the contract was that, as a condition precedent, the assessee had to obtain insurance with respect to the entire project which has been in fact obtained by the assessee in India for which the assessee has received major payment during the year under consideration itself. The said policy has not been shown to be restricted only with regard to activities of the assessee outside India.

72. On the basis of decision of Hon'ble Supreme Court in the case of Hyundai Heavy Industries (supra), it has been the case of assessee that the assessee having installation contract was engaged in a fabrication of platform and unless fabricated platform is delivered from the country, where it has been fabricated, the installation PE cannot said to have come into existence. This argument of the assessee is not acceptable for the reason that the facts in that case, as observed by Hon'ble SC, were that the contract was divisible into two parts, one was for fabrication of the platform and the other was installation and commissioning of the said platform. On these facts, it was the case of the assessee that before the fabrication work was completed no PE can be said to have come into existence as its Mumbai office cannot be termed to be PE as it was only a liason office as per permission given by RBI. In that case Mumbai office was not considered as PE as it was not permitted by RBI to carry on any business activity in India. The assessee in that case was having no other place of business in India prior to fabrication work was completed outside India. Therefore, it was held that installation PE came into existence at the point of time when fabrication work was completed and fabricated material was deported to India. Prior to that point of time no part of income of assessee could be taxed in India as assessee in that case did not have any PE. As against that, according to the facts of the present case, Mumbai project office, as per resolution of the Board of Directors dated 3rd April, 2006, was opened for coordination and execution of project and no restriction has been imposed by RBI on the working of project office. Thus, in the case of present assessee, the fixed place PE has come into existence in the shape of Mumbai project office on the day when assessee was permitted by RBI to open its such office. Such project office is PE within the meaning of Article 5.1 of DTAA as the assessee has wholly or partly carried out its business activity through it.

73. Here, it has been the case of the assessee that article 5.3 has to be read in isolation. This argument of the assessee cannot be accepted in view of above discussion. This proposition is also not supported by the provisions contained in DTAA. To explain and properly understand it will be relevant to reproduce the provisions of article 5 which defines "permanent establishment":-

> *"ARTICLE 5 – Permanent establishment –1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.*
>
> *2. The term "permanent establishment" shall include especially-*
> *(a) a place of management;*
> *(b) a branch;*
> *(c) an office;*
> *(d) a factory;*
> *(e) a workshop; and*
> *(f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.*
> *3. The term "permanent establishment" likewise encompasses a building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only where such site, project or activities continue for a period of more than nine months."*
> *4. Notwithstanding the preceding of this article, the term "permanent establishment" shall be deemed not to include-*
> *(a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;*
>
> *(b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;*
>
> *(c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;*

(d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or for collecting information, for the enterprise;

(e) the maintenance of a fixed place of business solely for the purpose of advertising, the supply of information, scientific research or any other activity, if it has a preparatory or auxiliary character in the trade or business of the enterprise;

(f) the maintenance of a fixed place if business solely for any combination of activities mentioned in sub-paragraphs (a) to (e) of this paragraph, provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

5. Notwithstanding the provisions of paragraphs (1) and (2) if a person – other than an agent of independent status to whom paragraph (6) applies – is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts in the name of the enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise unless the activities of such person are limited to those mentioned in paragraph (4) which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment by virtue of that paragraph.

6. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, where such persons are acting in the ordinary course of their business.

7. The fact that a company which is a resident of a Contracting controls or is controlled by a company which is a resident of the other Contracting State, or which caries on business in that other State (whether through a permanent establishment or otherwise)

shall not of itself constitute either company a permanent establishment of the other."

74. Article 5.1 describes that for the purpose of DTAA, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on. Article 5.2 states that the term "permanent establishment" shall include especially (a) a place of management; (b) a branch; (c) an office; (d) a factory; (e) a workshop and (f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources. Article 5.2 has enlarged the meaning of "permanent establishment" in addition to what has been stated in article 5.1. Article 5.3 used the words "likewise encompasses" and these items are, a building site; a construction; assembly or installation project or supervisor activity in connection therewith but only in a case where such site/project or activity continue for a period of more than nine months. So, it has further enhanced the term "permanent establishment" to these entities. Therefore, it will be wrong to say that Article 5.3 is an exclusionary clause, restricting the scope of Article 5.1 or Article 5.2.

75. Reliance on the commentary of OECD of Article 5.3 is misplaced as for the purpose of relying on Article 5.3, it has been presumed that no PE of the assessee exists within the meaning of Article 5.1 & 5.2. It has already been pointed out that Article 5.3 only extends the scope of PE and it cannot be read in isolation. Otherwise also, if the PE of a non-resident entity exists under Article 5.1 & 5.2 than it is not necessary that it should also fall within the scope of Article 5.3 to make it liable to be taxed in the source country. In the present case, it has already been held that the PE of the assessee came into existence on the opening of project office in Mumbai. Similarly reliance on the decision of Tribunal in the case of DCIT Vs. Hyndai Heavy Idnsutries Co. Ltd. 31 SOT 482 (Del) is misplaced as in that case assessee's Mumbai

Office was not considered as PE for the reason that it was not allowed to carry out any business activity by the RBI and it was to work only as liaison office.

76. Article 5.4 is an exclusionary clause which describes that in specified circumstances "permanent establishment" will not be considered to be "permanent establishment". Article 5.4 starts with the words "notwithstanding preceding of this article" and exclusions are (a) use of the facilities solely for the purposes of storage, display or delivery of goods, mercantile belonging to the enterprises; (b) the maintenance of stock of goods or mercantile belonging to the enterprise solely for the purpose of storage, display or delivery; (c) the maintenance of stock of goods or mercantile belonging to enterprise solely for the purpose of processing by another enterprise; (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or for collecting information for the enterprise; (e) the maintenance of a fixed place of business solely for the purpose of advertising, the supply of information, scientific research or any other activity, if it has a preparatory or auxiliary character in the trade or business of the enterprise; and (f) the maintenance of fixed place if business solely for any combination of activities mentioned in sub-paragraphs (a) to (e) provided that overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character. The other clauses are not relevant for the purpose of the present case as it is not even the case of assessee that its Mumbai project office cannot be considered to be "permanent establishment" in the light of Article 5.5, 5.6 and 5.7.

77. Here, to contest the taxability of outside India revenue, it is the main case of the assessee that its Mumbai project office cannot held to be "permanent establishment" within the meaning of Article 5.1 and

5.2 as its Mumbai project office does not have any role to play in the business activity of the assessee company either wholly or partly. In absence of existence of PE within the meaning of Article 5.1 and Article 5.2 the PE of the assessee can be said to have come into existence only when fabricated platform was deported from Malaysia to the offshore site of ONGC and from that date the installation PE of the assessee can be said to have come into existence within the meaning of Article 5.3. To contend that Mumbai project office cannot be termed to be "permanent establishment" either within the meaning of Article 5.1 or Article 5.2, it is the case of ld. AR that its Mumbai project office is not involved in any core activity of business. The activity, if any, carried on by the Mumbai project office was in the character of preparatory or auxiliary which is excluded within the meaning of Article 5.4. It is also the case of ld. AR that the accounts maintained by the assessee in India have demonstrated that Mumbai project office did not incur any expenditure relating to project and the employees deployed there have no technical qualification or skill to enable them to carry out the activity of the project. We have carefully considered these arguments of ld. AR. It has already been discussed that in absence of any restriction put by RBI on the activities of Mumbai project office, the said office is in the character of "permanent establishment" in view of Article 5.1 and 5.2. If it is so, then material is available on record according to which it can be said that "permanent establishment" of the assessee has come into existence on the opening of Mumbai project office. There is no force in the arguments of ld. AR that, in any case, its Mumbai project office falls under exclusions described under Article 5.4, as the activities carried on by the Mumbai project office are in the nature of preparatory of auxiliary in nature. The way the terms of the contract are described and the way the work on contract has to proceed clearly describe that in all the activities of contract there will be the role of Mumbai project office as

the same has to work as a channel between assessee company and ONGC. If PE of the assessee exists within the meaning of Article 5.1 and 5.2 and assessee claims that despite there being PE in terms of clause 5.1 and 5.2, it falls under exclusionary Article 5.4 then onus is on assessee to prove that activities of its PE are in the nature of preparatory or auxiliary in nature. No material has been brought on record by the assessee to prove the said fact. The arguments put forward in this respect are only by inference such as the accounts maintained by the assessee in India through which it is the argument of ld. Counsel of the assessee that it does not contain any expenditure relating to execution of the contract. But such argument is not acceptable as the maintenance of account is in the hands of assessee and mere the mode of maintaining the accounts alone cannot determine the character of PE as the role of PE only will be relevant to determine that what kind of activities it has carried on. As pointed out earlier the way the contract has to proceed, Mumbai project office of the assessee has to play a vital role in the execution of entire contract and if assessee wants to contend otherwise, the onus is on assessee and not on the revenue. No material has been brought on record by the assessee to show that its Mumbai office does not have any role to play in the execution of contract, therefore, the argument of the assessee cannot be accepted that the Mumbai project office has carried out only preparatory or auxiliary activities so as to bring the PE of the assessee under exclusionary Article 5.4. Therefore, such argument of the assessee has to be rejected and this issue is decided in favour of revenue.

78. Having come to the conclusion that the PE of the assessee existed in India in accordance with Article 5.1 and 5.2 and it does not fall under exclusionary clause, now the question which will required to be determined is that whether AO is justified in attributing 25% of the

outside India revenue to the PE of the assessee in India. There is lack of material made available on record to ascertain as to what extent the activities of business were carried on by the assessee through its Mumbai project office and such fact has to be determined before deciding the percentage of attribution of the outside India activity of the assessee to its PE in India. The AO in the present case has attributed 25% of its outside India activity as income related to PE of the assessee to India. But we find no material on record to support such attribution particularly in absence of any reasoning or basis given for that. Necessary material in this respect has to be brought on record to arrive at a proper conclusion that what percentage will be appropriate to be attributed to the PE of the assessee in India during the year under consideration. Therefore, we consider it just and proper to restore this issue to the file of AO for proper determination thereof after ascertaining the necessary facts and after bringing the proper material or record to support that conclusion. We direct accordingly. Needless to mention that AO will give proper opportunity of hearing to the assessee.

79. So far as it relates to levy of interest u/s 234B, it is the case of the assessee that it being non-resident, sec. 195 of the Act puts an obligation on the payer i.e. any person responsible for paying to the non-resident, to deduct income tax source at the rates in force from such payments excluding those incomes which are chargeable under the head “salaries”. Therefore, the entire tax which is payable on such payments made by the payee to the non-resident is to be deducted at source. Sec. 201 of the Act lays down the consequences of the failure to deduct or pay. These consequences include not only the liability to pay the amount which such a person was required to deduct at source from the payments made to a non-resident but also penalties, etc. Once it is found that the liability was that of the payer and the payer

has defaulted in deducting the tax at source, the department can take action against the payer under the provisions of sec. 201 of the Act and compute the amount accordingly. If the person (payer) who had to make payments to the non-resident had defaulted in deducting the tax at source from such payments, the non-resident is not absolved from payment of taxes thereupon. In such a case, the non-resident is liable to pay tax but the question to payment of advance tax would not arise. Therefore, it would be impermissible for the revenue to charge any interest u/s 234B of the Act. For raising such contention reliance has been placed on the following decisions: (1) Director of Income Tax Vs. Jacabs Civil Incorporated etc. 330 ITR 578 (Del.), (2) CIT Vs. Sedco Forex International Drilling Co. Ltd. 264 ITR 320. The copies of these decisions are enclosed by the assessee in the paper book at pages 207 to 212 and 202 to 206 respectively.

80. In this view of the situation, we find that interest u/s 234B shall not be chargeable in the case of assessee. It is seen that though this issue was raised by the assessee before AO who has followed the directions of DRP. The DRP has dealt with this issue collectively in para 5.3 of its order along with interest levied u/s 234A and 234C, wherein mainly relying upon the decision of Hon'ble Supreme Court in the case of Anjum M.H. Ghaswala 252 ITR 1 it is held that interest levied under the sections are compensatory in nature and gets automatically attracted from default of the assessee. Ld. DRP has also relied upon the decision in the case of Insilco Ltd. reported in 321 ITR 105. In this regard it may be mentioned that it was not a case of non-resident where tax was deductible u/s 195 and the case of assessee was that levy of interest u/s 234B was not specifically directed to be charged in the assessment order. The facts of the present case are entirely different. According to the facts of the present case the case relates to non-resident, where tax was deductible upon the amounts paid to it u/s

195 and the aforementioned decision of Delhi High Court in the case of DIT Vs. Jacabs Civil Incorporate (supra) will be applicable. As these decisions have not been considered by the DRP and the AO, we restore this issue to the file of AO to consider them and thereafter decide this issue as per law keeping in view the aforementioned decisions. We direct accordingly.

81. As it relates to levy of interest u/s 234D the same was stated to be consequential. The AO will compute the interest accordingly after determining the income of the assessee in accordance with our aforementioned directions.

82. In the result, appeal is partly allowed for statistical purposes in the manner aforesaid.

The order pronounced in the open court on 30.08.2011.

Sd/-	Sd/-
[G.E. VEERABHADRAPPA]	[I.P. BANSAL]
VICE PRESIDENT	JUDICIAL MEMBER

Dated, 30.08.2011.
*dk
*Kavita
Copy forwarded to: -
1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT
TRUE COPY

By Order,

Deputy Registrar,
ITAT, Delhi Benches