Consultancy services in the fields of exploration, mining and extraction are FTS and do not constitute a PE in India under India-Germany tax treaty

**Background**

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal), in the case Rheinbraun Engineering Und Wasser GmbH\(^1\) (the taxpayer) held that consultancy services in the fields of exploration, mining and extraction rendered by a German company do not constitute a Permanent Establishment (PE) in India under the India-Germany tax treaty (the tax treaty). Protocol to the tax treaty with respect to Article 7 states that income derived from a resident of a state from planning, project construction or research activities as well as income from technical services exercised in that state in connection with a PE situated in the other state, shall not be attributed to that PE. Accordingly, even if it is assumed that the taxpayer had a PE in India, it will not be governed by Article 7 of the tax treaty. Such services are taxable as Fees for Technical Services (FTS) under the Article 12 of the tax treaty.

**Facts of the case**

- The taxpayer filed its return of income declaring income of INR11.39 million. The taxpayer had offered the income received from Indian parties as FTS under Article 12 of the tax treaty. As per Article 12(5) read with Article 7(3) of the tax treaty, such receipts are taxed as per provisions of the domestic law of the respective country. Section 44D of the Income-tax Act, 1961 (the Act) deals with such receipts and as per Section 115A of the Act, fees received from Gujarat Industries Power Company Ltd. (GIPCL) are taxed at the rate of 30 per cent and the fees received from the remaining two parties are to be tax at the rate of 20 per cent.

- The Assessing Officer (AO) completed the assessment accepting the income returned by the taxpayer. However, the AO held that the taxpayer should have paid tax at a higher rate.

- The AO observed that the taxpayer entered into agreements with GIPCL, Nevyli Lignite Corporation Ltd. (NLC) and McNally Bharat Engg. Co. Ltd. (MNBEC) and received INR11.39 million from the Indian parties under the above agreements.

- The taxpayer had rendered various services to the Indian companies. The project undertaken by the Indian parties lasted more than six months.

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\(^1\) Rheinbraun Engineering Und Wasser GmbH v. DIT (ITA No. 2353/Mum/2006) – Taxsutra.com
• The AO held that the taxpayer had rendered various services including supervisory activities to GIPCL. The services were in the nature of installation or assembly project. The taxpayer rendered supervisory services to NLC also. The services rendered were connected with mining projects. As per the agreement entered into with MNBCECL, the taxpayer had to render services for the finalisation of the design problem at hand.

• The taxpayer had a PE in India as per Article 5(2)(i) of the tax treaty.

**Tribunal’s ruling**

• A scrutiny of the invoices prove that the taxpayer had rendered consultancy services and, therefore, same are governed by the provisions of Article 12 of the tax treaty.

• For computing continuous stay for PE purpose, actual stay of employees has to be considered and not the entire contract period.

• The Tribunal relied on the decision in the case of J Ray McDermott Eastern Hemisphere Ltd. wherein it was held that period of stay in India for a non-resident entity has to be counted from the actual date of commencement and completion of the contract, and date on which invoices were raised were not decisive factors to decide the existence of PE.

• If it had rendered services in India for more than six months continuously, it has to be held that it had a PE in India. The taxpayer had deputed one of its employees to India, and he had not stayed in India for more than 180 days. The taxpayer had informed the AO that its employee had visited India in pursuance of the agreements entered into with NLC and MNBCECL. It is also a fact that under these contracts no supervisory charges were booked by the taxpayer.

• The taxpayer had offered its income under the head FTS in its return. Article 12(4) of the tax treaty deals with FTS and talks of services of managerial, technical or consultancy nature.

• In view of above, payments received by the taxpayer should be assessed as per the provisions of Article 12 of the tax treaty and not as per Article 7 of the tax treaty.

• Protocol to the tax treaty with respect to Article 7 provides that income derived from a resident of a contracting state from planning, project construction or research activities as well as income from technical services exercised in that state in connection with a PE situated in the other state, shall not be attributed to that PE. Accordingly, even if it is assumed that the taxpayer had a PE in India for the year under consideration, it will not be governed by Article 7 of the tax treaty.

• The Tribunal held that the payments received by the taxpayer from GIPCL, NLC and MNBCECL have to be taxed at the rate of 10 per cent and that the provisions of Section 115A of the Act would not be applicable.

**Our comments**

The Mumbai Tribunal in the instant case observed that consultancy services in the fields of exploration, mining and extraction provided by the German company do not constitute a PE in India. Such services are taxable as FTS under Article 12 of the tax treaty.

It has also been observed that the protocol to the tax treaty with respect to Article 7 provides that income derived from a resident of a contracting state from planning, project construction or research activities as well as income from technical services exercised in that state in connection with a PE situated in the other state, shall not be attributed to that PE. Accordingly, even if it is assumed that the taxpayer had PE in India for the year under consideration, it will not be governed by Article 7 of the tax treaty.

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2 DCIT v J. Ray McDermott Eastern Hemisphere Ltd [2012] 54 SOT 363 (Mum)
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