VERENDRA KALRA & CO LLP

CHARTERED ACCOUNTANTS

Communiqué

International Taxation

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HC: Clarificatory Amendment Cannot Create Retrospective Tax Liability

Facts

The The appellant entered into various contracts dated 20.09.1995 with Raytheon Ebasco Overseas Ltd. (REOL), Badger Energy Inc. (BEI), and Energy Overseas International Inc. (EOI) for offshore equipment supply, engineering, transportation, erection, construction materials, and related services. While making payments to REOL, the appellant deducted tax of Rs. 20,18,071/-. Subsequently, the Assessing Officer passed orders under section 201(1) of the Income-tax Act, 1961 for AYs 1996-97 and 1997-98, raising substantial demands for alleged failure to deduct tax at source on payments made to the non-resident entities. The demands were later revised through rectification orders passed under section 154 of the Act. Aggrieved by these orders, the appellant preferred appeals before the Commissioner of Income-tax (Appeals), who dismissed the appeals and held that the appellant was under a statutory obligation to deduct tax at source under section 195 of the Act. The CIT(A) further held that the services rendered by REOL constituted fees for technical services taxable in India under section 9(1)(vii) of the Act and Article 12 of the India-USA DTAA, since the services were utilized in India. The CIT(A) also observed that failure to deduct tax attracted consequential liabilities such as interest and penalty. The appellant thereafter filed appeals before the Income Tax Appellate Tribunal (ITAT), Bangalore. However, vide a common order dated 18.05.2005, the ITAT dismissed the appeals and upheld the view that the payments constituted fees for technical services chargeable to tax in India under section 9(1)(vii) of the Act and Article 12(4) of the India-USA DTAA. Challenging the findings of the ITAT, the appellant filed the present appeals before the higher judicial forum.

Ruling

In the present case, Karnataka High Court held that the Explanation inserted to Section 9(2) by the Finance Act, 2010 should be interpreted as applying prospectively and not retrospectively from 01.06.1976. The Court observed that although the amendment was introduced as a clarificatory provision and stated to be "for the removal of doubts", its effect was to widen the scope of Section 9(1)(vii) and impose a fresh tax burden on taxpayers for past years. Relying on the Supreme Court's decision in M.M. Aqua Technologies, the Court held that a provision described as clarificatory cannot be given retrospective effect where it substantively alters the law or expands the scope of a charging provision. The Court further noted that the amendment sought to negate the principles laid down by the Supreme Court in Ishikawajima-Harima Heavy Industries Ltd., which had emphasized the requirement of a nexus between the services rendered and India for taxation under Section 9(1)(vii). Accordingly, the Court ruled that a retrospective amendment cannot be used to create a new tax liability or bring within the tax net transactions that were not taxable under the law prevailing at the relevant time. The writ petition was therefore allowed, and the impugned amendment was read down to operate only prospectively.

Source : HC, Karnataka in the case of Jindal Thermal Power Company Limited, Vs DCIT vide [TS-1208-HC-2026(KAR)] on August 7, 2026

ITAT Holds SaaS Subscription Revenue Not Taxable as FIS

Facts

The assessee Branch Metrics Inc., a USA-based company and tax resident of the USA, provided SaaS-based products through a Software Development Kit (SDK) to Indian customers. For AY 2021-22, it received INR 24.16 crore from Indian customers, of which INR 7.42 crore was claimed exempt under Section 10(50) on account of Equalisation Levy and INR 16.74 crore was claimed as non-taxable business profits under Article 7 of the India-USA DTAA in the absence of a Permanent Establishment (PE) in India. During scrutiny proceedings, the AO issued notices to several Indian customers and, based on their responses, concluded that the assessee was providing customized marketing, analytics, and technical support services involving human intervention and technical account management. Accordingly, the AO treated the entire receipts of INR 24.16 crore as Fees for Included Services (FIS)/Fees for Technical Services (FTS) taxable under Article 12 of the India-USA DTAA read with Section 9(1)(vii) of the Act. The DRP upheld the AO's view, observing that the services were customized in nature and involved the exchange of technical know-how and skills. Consequently, the AO passed the final assessment order taxing the receipts at 10% under the DTAA. Aggrieved by the assessment order, the assessee preferred an appeal before the Tribunal.

Ruling

The Hon'ble bench held that the the consideration received by the US-based assessee from Indian customers for providing SaaS-based products is not taxable as Fees for Included Services (FIS) under Article 12(4) of the India-USA DTAA or as Fees for Technical Services (FTS) under Section 9(1)(vii) of the Act. The Tribunal observed that the assessee was providing a standard, automated, off-the-shelf SaaS platform and not rendering customized technical, managerial, or consultancy services. It was further noted that the assessee did not make available any technical knowledge, skill, know-how, process, or technical plan to its customers. The customers were merely granted access to and use of the platform, while the underlying technology remained with the assessee. The ITAT emphasized that upon expiry of the subscription, customers were left with no technical knowledge or capability enabling them to independently perform the functions carried out by the platform. The recurring nature of the subscriptions itself demonstrated that no technology or know-how was made available to the customers. Accordingly, the Tribunal held that the receipts failed the "make available" test under Article 12(4) of the DTAA and, being consideration for a standard automated facility involving no human intervention, could not be characterized as FIS or FTS. Accordingly, the Tribunal allowed the assessee's appeal and held that the receipts from Indian customers were in the nature of business income. Since the assessee did not have a Permanent Establishment (PE) in India, such income was not taxable in India under Article 7 of the India-USA DTAA. The addition made by the Assessing Officer by treating the receipts as FIS/FTS was therefore deleted.

Source : ITAT, Delhi in the case of Branch Metrics Inc. vs DCIT/ACIT vide [TS-1239-ITAT-2026(DEL)] on August 14, 2026

Offshore Supplies Not Taxable in Absence of PE in India

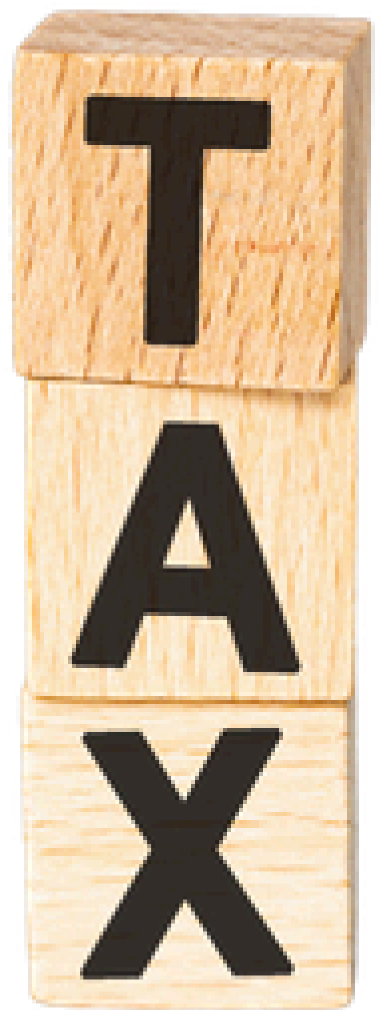
Facts

The assessee, a tax resident of the USA, was engaged in the offshore supply of spare parts, including replacement, refurbishment, and rotable parts, to customers in India. During the relevant assessment year, it received Rs. 108.57 crore from such offshore supplies and repair services carried out outside India, which it claimed as non-taxable income in India. During the assessment proceedings, the Assessing Officer (AO) held that the assessee had a Permanent Establishment (PE) in India and, therefore, the receipts from offshore supply of spare parts were taxable as business income attributable to such PE. Accordingly, the AO attributed 10% of the gross receipts, amounting to Rs. 10.86 crore, and added the same to the assessee's income. The assessee contended that the issue of PE was already settled in its favour by the Tribunal in its own cases for earlier assessment years, wherein it had been held that the assessee did not have a PE in India. The DRP also noted that the facts for the year under consideration were identical to those of earlier years and found no reason to deviate from the previous decisions. However, despite these findings, the AO concluded in the final assessment order that the assessee had a PE in India and proceeded to attribute profits thereto. On merits, the assessee argued that the project office of GE International Inc. could not be regarded as its fixed place PE under Article 5 of the India-USA DTAA. It further submitted that, since the Tribunal had consistently held that no PE existed in India, no profit attribution could be made. Alternatively, without prejudice, the assessee submitted that in earlier years the Tribunal had restricted profit attribution to 4%, and therefore the AO's attribution of 10% of gross receipts was excessive and unjustified.

Ruling

In the present case, The Delhi ITAT held that GE Energy Parts Inc., a US tax resident, did not have either a Fixed Place Permanent Establishment (PE) or a Dependent Agent PE (DAPE) in India under Article 5 of the India-US DTAA. The case involved receipts from offshore supply of equipment, spare parts, repairs, and refurbishment services rendered to Indian customers, which the assessee claimed were not taxable in India. The Assessing Officer, however, treated the project office of GE International Inc. (GEII) as the assessee's PE in India and attributed profits thereto. The Tribunal observed that the title in the equipment passed outside India and that the repair and refurbishment activities were also carried out entirely outside India. Relying on the Supreme Court's decision in Ishikawajima-Harima Heavy Industries Ltd., the ITAT held that offshore supplies and services performed outside India do not give rise to taxable income in India. It further noted that the Revenue had failed to bring any evidence on record to demonstrate that the conditions prescribed under Article 5 of the India-US DTAA for constituting a Fixed Place PE or DAPE were satisfied. The Tribunal also rejected the Revenue's contention that the offshore supply and onshore service contracts were artificially split to avoid taxation, observing that they were separate arrangements from the bidding stage itself. Following its earlier decisions in the assessee's own case, the ITAT concluded that the assessee had no PE in India and, therefore, the receipts from offshore supply of equipment, repairs, and refurbishment services were not taxable in India. Consequently, no question of profit attribution arose, and the assessee's appeal was allowed.

Source : ITAT, Delhi in the case of GE Energy Parts Inc vs ACIT, vide [TS-1214-ITAT-2026(DEL)] on August 10, 2026



Delhi ITAT Rejects DAPE (Dependent Agent PE) Based Solely on Operational Linkages

Facts

The brief facts are that the assessee, a Japanese tax resident, filed its return declaring income from royalty and fees for technical services received from its Indian associated enterprise, MKCI, and paid tax at the DTAA rate of 10%. During assessment, the AO held that the assessee had a Fixed Place PE in India through its seconded employees working from MKCI's premises and that MKCI also constituted a Dependent Agent PE (DAPE) under the India-Japan DTAA. Accordingly, the AO held that the profits from offshore sales made to MKCI were attributable to the alleged PE in India and taxed a portion of such profits as business income. The DRP upheld the AO's findings following its directions for the preceding assessment year. Consequently, the AO passed the final assessment order attributing profits to the alleged PE in India. Aggrieved by the order, the assessee filed an appeal before the Tribunal.

Source : ITAT, Delhi in the case of Mitsui Kinzoku Company Ltd vs ACIT, vide [[TS-1305-ITAT-2026(DEL)] on August 24, 2026

Ruling

The Hon'ble bench held that the Mitsui Kinzoku Components India Pvt. Ltd. (MKCI) could not be regarded as a Dependent Agent Permanent Establishment (DAPE) of the Japanese assessee under Article 5(7) of the India-Japan DTAA. The Tribunal observed that MKCI was an independent entity carrying on its business on a principal-to-principal basis, assuming its own risks and responsibilities, and was neither economically, functionally, nor legally dependent on the assessee. The AO/DRP had treated MKCI as a DAPE based on the technical know-how, documentation, and operational control exercised by the assessee over MKCI. However, the Tribunal noted that mere operational linkages, technical support, or business coordination between a foreign parent and its Indian subsidiary do not automatically result in a DAPE. The Revenue failed to establish that MKCI habitually concluded contracts on behalf of the assessee, maintained stock for delivery, or habitually secured orders for the assessee, which are essential conditions under Article 5(7) of the DTAA. Relying on the Supreme Court's decision in E-Funds IT Solution, the Tribunal held that interactions and cross-transactions between a foreign company and its Indian subsidiary, by themselves, are insufficient to constitute a DAPE. Accordingly, the Tribunal concluded that MKCI could not be treated as the assessee's DAPE merely on account of operational linkages, technical support, or oversight of its operations. The Tribunal, therefore, deleted the addition made on account of the alleged DAPE and held that, in the absence of satisfaction of the conditions prescribed under Article 5(7) of the India-Japan DTAA, no profits could be attributed to MKCI as a DAPE of the assessee in India.

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