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TAX FLASH NEWS

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Reimbursements for mobilisation/ demobilisation of vessels are taxable under Section 44BB of the Income-tax Act. Further, the service tax collected is not to be included in gross receipts

Background

Recently, the Delhi Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Western Geco International Ltd.[1] (the taxpayer) held that the reimbursement for mobilisation/ demobilisation of vessels attributable to the distance travelled outside India are taxable under Section 44BB of the Income-tax Act, 1961 (the Act).

The service tax collected from its clients cannot be included in the gross receipts while computing its income under Section 44BB of the Act.

For the period prior to amendment in Section 44BB of the Act by the Finance Act, 2010, the services in the nature of 'seismic surveys' were in connection with the prospecting for, or extraction or production of mineral oils, and therefore, the consideration is taxable on a presumptive basis under Section 44BB of the Act, and not under Section 44DA of the Act.

Facts of the case

- The taxpayer is a non-resident company, incorporated under the laws of British Virgin Islands, and is engaged in the business of acquisition and processing of two-dimensional (2-D) and three-dimensional (3-D) seismic data for companies engaged in exploration and production of mineral oils in India. The taxpayer had set up a project office in India for execution of the contract with the upstream companies and tires.
- It was submitted that the taxpayer has a permanent establishment (PE) in India. Also, such data is widely used by oil exploration companies to help them ascertain the existence of potential hydrocarbons and to determine the size and structure of known reservoirs in the area designated for seismic survey.
- This seismic survey and processing of data acquired in the survey are one of the most critical activities in the exploration of mineral oils. Since the services provided are in connection with prospecting for, or extraction or production of mineral oil, the taxable income has been computed as per the provisions of Section 44BB of the Act at a deemed profit of 10 per cent of gross revenues.
- During the year under consideration, the taxpayer received certain consideration from the above contracts with Indian companies, which was offered for taxation as per Section 44BB of the Act.
- The Assessing Officer (AO) observed that the taxpayer was rendering technical services; therefore, Section 44BB was not applicable.
- The taxpayer submitted that its income was taxable under Section 44BB of the Act as the services rendered by it were not technical services within the meaning of Explanation 2 to Section 9(1)(vii) of the Act. Further, for services in the nature of 'seismic surveys', the applicable Section was 44BB and said services could not be taxed under Sections 44D, 44DA or 115A of

[1] Western Geco International Ltd. v. ACIT [2016] 71 taxmann.com 166 (Del)

of the Act. Also, the amendment to Section 44BB by way of insertion of Section 44DA in the proviso to Section 44BB was prospective in nature and, accordingly, the applicability of Sections 44D and 44DA got excluded.

- However, the AO concluded that taxpayer's receipts were effectively connected with the project office in India and therefore, taxable under Section 44DA of the Act, as these are fees for technical services. Further, the AO made the addition in respect of reimbursement of mobilisation/ demobilisation receipts in the hands of the taxpayer. Also, certain reimbursement of service tax received by the taxpayer was disallowed.

The Tribunal's ruling

Mobilisation/demobilisation receipts attributable to distance travelled outside India

- The issue with respect to whether the revenue received from mobilisation/demobilisation is taxable in India is covered by the taxpayer's case[2] for the Assessment Year (AY) 2009-10, wherein it was held as follows:
  - The issue is covered by the judgment of the High Court in the case of Sedco Forex International Inc.[3].
  - Mobilisation is a stage payment, as part of the total consideration for the execution of the contract. The taxpayer would be moving its machinery from one place of work to another place of the berth.
  - Mobilisation is paid as advance for such movement and is generally adjusted against running bills. It is not a case where a separate payment is made for a transportation contract.
  - The submission that the taxpayer would try to work out, based on some basis, the revenue attributable to the activity of mobilisation carried out outside India, cannot be accepted, as such an exercise would amount to estimating income for activities outside India, when the scope of the contract is for execution of the contract in India.
  - Mobilisation is an incidental activity to the main activity of carrying out the contract in India.
  - The decision of the Supreme Court in the case of Ishikawajima and Hyundai Heavy Industries Ltd.[4] has been discussed by the High Court in the case of Sedco Forex International Inc. The ratio laid down by Supreme Court in that case is not applicable here as it is not a case where separate parts of a contract are executed at different places. The argument that the payment was in the nature of reimbursement of expenses incurred by the taxpayer company and hence not income was also rejected by the High Court.
- Following the above decision of this Tribunal, it was held that the receipts from mobilisation/ demobilisation of vessels attributable to the distance travelled outside India are taxable under Section 44BB of the Act.

Taxability of service tax

- The Tribunal relied on the decision of the Delhi High Court in the case of Mitchell Drilling International (P.) Ltd.[5] where it was held that:
  - For the purpose of computing the presumptive income of the taxpayer for the purpose of Section 44BB of the Act, the service tax collected by the taxpayer for rendering services is not to be included in the gross receipts in terms of Section 44BB(2) read with Section 44BB(1) of the Act.
  - The service tax is not an amount paid or payable, or received or deemed to be received by the taxpayer for the services rendered by it. The taxpayer is only collecting the service tax for passing it onto the government.

[2] Western Geco International Ltd v. ADIT (International Taxation) [2014] 44 taxmann.com 478, 150 ITD 283 (Del)
[3] Sedco Forex International Inc. v. CIT [2008] 299 ITR 238 (Utt)
[4] Ishikawajma-Harima Heavy Industries Ltd. v. DIT [2007] 158 Taxman 259 (SC)
[5] DIT v. Mitchell Drilling International (P.) Ltd. [2015] 62 taxmann.com 24 (Del)

- The High Court while deciding this issue has dealt with the Supreme Court's decisions in the case of Chowringhee Sales Bureau (P.) Ltd.[6] and George Oaks (P) Ltd.[7]. The High Court has distinguished these decisions to the facts therein, which are identical to that of the present case.

- Following the decision of High Court, it is held that the service tax collected cannot be included in the gross receipts in terms of Section 44BB(1) of the Act.

Taxability of fees for technical services

- The AY under consideration is 2010-11, which is prior to the AY 2011-12. The insertion of Section 44DA in the proviso to Section 44BB with effect from 1 April 2011 has been held to be prospective in nature.

- This has been considered in detail by decisions of this Tribunal and that of the jurisdictional High Court in the case of Baker Hughes Asia Pacific Ltd.[8] wherein it was held as follows:

  - The department's contention is that Section 44DA inserted by the Finance Act, 2010 with effect from 1 April 2011 in Section 44BB is retrospective and, therefore, royalty and fees for technical service should be taxed under Section 44DA and not under Section 44BB of the Act.

  - The High Court held that the amendment cannot be held to be retrospective particularly because it brings substantial change in the taxability of taxpayer. It is well-settled law that an amendment to the taxing statute if results in the higher tax burden on taxpayer then it is prospective in nature and not retrospective.

  - This issue has been dealt elaborately by the Uttarakhand High Court in the case of B.J. Services Company Middle East Ltd.[9].

  - The contentions advanced on behalf of the tax department are not accepted since the issue is squarely covered by the decision of the Delhi High Court in the case of OHM Ltd.[10] and by the decision of the Tribunal in the case of CGG Veritas Services SA [11].

- In the taxpayer's case[12] the Delhi High Court held the finding of this Tribunal that in respect of fees received by a non-resident taxpayer for providing service in connection with prospecting for, or extraction or production of mineral oil, such taxpayer would be covered by Section 44BB till AY 2011-12.

- The Tribunal in the case of Baker Hughes Asia Pacific Ltd. has relied on the decision of the Uttarakhand High Court in the case of B.J. Services for rejecting the tax department's contention that Section 44DA inserted by the Finance Act 2010 with effect from 1 April 2011 in Section 44BB is retrospective.

- The Supreme Court in the case of Oil & Natural Gas Corpn. Ltd.[13] has set at rest the entire controversy by holding that provisions of various services in connection with the prospecting for, or extraction or production of mineral oils is taxable on the presumptive basis under Section 44BB of the Act.

- Accordingly, the gross receipts of the taxpayer are taxable under Section 44BB, and not under Section 44DA of the Act.

Our comments

Taxability of the profits and gains in connection with the business of exploration, etc., of mineral oils has been a matter of debate before the Courts/Tribunal.

In the oil and gas sector as a normal practice, customers generally compensate a contractor for mobilisastion/demobilisation activities. In relation to the mobilization/demobilization charges attributable to the distance travelled outside India, generally, the taxpayers contend that such

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[6] Chowringhee Sales Bureau (P.) Ltd. v. CIT [1973] 87 ITR 542(SC)
[7] George Oaks (P) Ltd. v. State of Madras [1962] 2 SCR 570
[8] Baker Hughes Asia Pacific Ltd. v. Addl. DIT (International Taxation) [2014] 47 taxmann.com 1, 151 ITD 79 (Del)
[9] DDIT v. B.J. Services Company Middle East Ltd. [2013] 35 taxmann.com 245 (Utt)
[10] DIT v. OHM Ltd. [2012] 28 taxmann.com 120 (Del)
[11] CGG Veritas Services SA v. Addl. DIT, International Taxation [2012] 50 SOT 335/18 taxmann.com 13 (Del)
[12] DIT(International Taxation) v. Western Geco International Ltd., [2013] 35 taxmann.com 345/216 Taxman 216 (Del)
[13] Oil and Natural Gas Corpn. Ltd. v. CIT [2015] 59 taxmann.com 1/233 Taxman 495 (SC)

activities are carried outside India and therefore, not subject to the tax of India. Accordingly, the income taxable in India should be restricted only to the income attributable to the distance travelled in the Indian territorial waters as compared to the total distance travelled. The Tribunal in some of the decisions[14] held that the mobilisation/demobilisation revenues attributable to the distance travelled outside India is not taxable in India.

On the other hand, the tax department generally contends that in Section 44BB(2)(a) of the Act, the phrase 'whether in or out of India' is used, and therefore, the consideration received for provision of services referred to in that clause for prospecting, etc., would be taxable whether the same are received in India or outside of India. Subsequently, the Uttarakhand High Court in the case of Sedco Forex International Inc.[15] held that in view of the fictional taxing provision contained under Section 44BB of the Act, the amounts received by the taxpayer towards mobilization charges are taxable. Also, the Uttarakhand High Court in the case of Halliburton Offshore Services Inc.[16] held that in the case of a non-resident company, the amount received on account of reimbursement of freight and transportation charges was to be added to its total income. In line with these decisions, the Tribunal in the present case has held that reimbursement for payment for mobilisation/demobilization is liable to be included in total income computed as per Section 44BB of the Act.

The Tribunal has also held that the service tax collected cannot be included in the gross receipts in terms of Section 44BB(1) of the Act. The decision of the Tribunal in the present case in relation to non-inclusion of the service tax in the gross receipts will help the taxpayers who are engaged in providing services/facilities in connection with the business of exploration, etc., of mineral oils and who opt for presumptive provisions of Section 44BB of the Act.

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[14] R and B Falcon Drilling Co v. ACIT [2007] 14 SOT 281 (Del), McDermott ETPM v. DCIT [2005] 92 ITD 385 (Mum)
[15] Sedco Forex International Inc. v. CIT [2008] 299 ITR 238 (Utt)
[16] CIT v. Halliburton Offshore Services Inc. [2008] 169 Taxman 138 (Utt)

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