INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "D": NEW DELHI

BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER
AND
MS. ASTHA CHANDRA, JUDICIAL MEMBER

ITA No. 8960/Del/2019
Asstt. Year: 2015-16

FCC Co. Ltd. 7000-36, Nakagawa Hosoe-Cho, Kita-Ku,Hamamatsushi Shizuoka-Pref Shizuoka, Japan State : Not listed Pin 431139 PAN AABCF5381M	Vs.	ACIT, Int. Tax. Circle-1(3)(1) New Delhi.
(Appellant)		**(Respondent)**

ITA No. 54/Del/2019
Asstt. Year: 2014-15

FCC Co. Ltd. 7000-36, Nakagawa Hosoe-Cho, Kita-Ku,Hamamatsushi Shizuoka-Pref Shizuoka, Japan State : Not listed Pin 431139 PAN AABCF5381M	Vs.	DCIT, Int. Tax. Circle-1(3)(1) New Delhi.
(Appellant)		**(Respondent)**

Assessee by:	Shri K. M. Gupta, Advocate Shruti Khimta, Advocate
Department by :	Ms. Anupam Anand, CIT DR
Date of Hearing	31/01/2022
Date of pronouncement	09/03/2022

O R D E R

PER ASTHA CHANDRA, JM

These two appeals are filed by the assessee against the order of the Ld. Deputy/ Assistant Commissioner of Income-tax, International Taxation - 1(3)(1), New Delhi ("**AO**") under section 143(3) read with Section 144C(13) of the Income-tax Act, 1961 ("**Act**") dated 31.10.2018 and 16.10.2019 pertaining to assessment year ("**AY**") AY 2014-15 and AY 2015-16 respectively.

2. Since the issues are common in both the appeals they were heard together and are being disposed off by this common order.

3. The main issue common in both the appeals relates to the existence of the alleged Fixed Place Permanent Establishment ("**Fixed Place PE**") and Supervisory Permanent Establishment ("**Supervisory PE**") of the assessee in India under the provisions of Article 5 of the Double Taxation Avoidance Agreement entered into between India and Japan. ("**India-Japan DTAA**"). The other common issue relates to attribution of income from offshore supply of raw materials and components and supply of capital goods to the alleged PE of the assesee.

4. The assessee is a foreign company and a tax resident of Japan. It is governed by the provisions of the India-Japan DTAA being more beneficial. It is engaged in the business of manufacturing of clutch systems and facing for cars, motorcycles, utility vehicles, specialized tools and dies and molding and machining of plastics. The assessee entered into a joint venture agreement with Rico Auto Industries Limited ("**Rico Auto**") and formed a JV company in India, namely FCC Rico Limited ("**FRL**") in the year 1997. The assessee also incorporated a wholly owned subsidiary in India namely, FCC

Clutch India Private Limited ("**FCC Clutch**") on 7.11.2014. Both FRL and FCC Clutch are engaged in business of manufacturing and supply of automobile clutch assemblies. As a part of restructuring, Rico Auto exited FRL by transferring its stake to FCC Clutch and thereafter FRL was merged with FCC Clutch with effect from 1.1.2015. Consequently, as a part of merger, FRL ceased to exist and it stands dissolved from such date without being wound up.

5. In both the assessment years involved, the assessee received the following types of income from FRL:

(i) royalty income under the Licence Agreement, which was duly offered to tax @ 10% on gross basis under the provisions of India-Japan DTAA;

(ii) fees for technical services ("**FTS**") under the Agreement for Dispatch of Engineers, which was duly offered to tax @ 10% on gross basis under the provisions of India-Japan DTAA;

(iii) Income from supply of raw material, components and capital goods under the Master Sales Agreement ("**MSA**"). Receipts from transactions under MSA were not offered to tax as the assessee treated them to be in the nature of business profit not taxable in India in the absence of a PE under the provisions of India-Japan DTAA.

6. The Ld. AO after due verification of details and evidence submitted by the assessee concluded that the assessee has a business connection in India in terms of section 9(1)(i) of the Act and a Fixed Place PE as well as Supervisory PE in India under Article 5 of the India-Japan DTAA. The Ld. AO held that FRL's premises in addition to hosting the business activities of FRL, serve as a "branch" and an "office" of the assessee. Therefore, a Fixed Place PE is constituted. The Ld. AO after evaluating the key attributes of

Fixed Place of business in the context of factual matrix in the present case concluded that the assessee deputed professionally qualified employees to the factory site of FRL in India and hence such factory site constituted a Fixed Place PE of the assessee in India. The Ld. AO also referred to certain clauses of the Licence Agreement viz-a-viz the facts of the present case and concluded that the employees visit in India were made to help FRL in setting up a new product line in India for which end-to-end supervision has been rendered by the assessee. Hence, the PE of the assessee in India under Article 5(4) of the India-Japan DTAA and a Fixed Place PE are clearly established. The Ld. AO arrived at his conclusion for the reason that certain employees of the assessee who visited India helped FRL in setting up a new product line in India for which end-to-end supervision has been rendered by the assessee. The period of stay of these employees in India exceeded 6 months and hence it constituted Supervisory PE of the assessee in India. Based on these reasoning, the Ld. AO proceeded to tax the receipts from sale of raw materials and capital goods by attributing 50% of the profits to the alleged PE.

7. Before the Hon'ble DRP, the objections raised by the assessee were rejected and the order of the Ld. AO was upheld by recording the following findings:

"3.3. The AO has elaborately discussed the issue in the draft assessment order holding that FCL constitutes a PE for the assessee under Article 5 of the India-Japan DTAA. The submissions made by the assessee before the Panel are the same which were submitted before the assessing officer and the Assessee has been unable to controvert the findings of the AO, holding that the assessee has an Fixed Place PE and Supervisory PE in India.

3.3.2 The Hon'ble ITAT in the case of HUAWEI TECHNOLOGIES CO LTD, China ,V. AD1T (ITA Nos. 5253/Del/2011, 5254/Del/2011, 5255/Del/2011

& 5256/Del/2011 dated 21/03/2014) - Del ITAT on the issue of existence of a PE held as under:

***Fixed place** PE On the basis of various information collected' during the survey it was clear that the taxpayer was carrying out the business in India. The business of the taxpayer in India is being conducted with active involvement of the employees of Huawei India. Such employees of Huawei India along with employees of the taxpayer have jointly prepared bidding documents for contracts, negotiated and concluded the contract on behalf of the taxpayer with its Indian customers. The taxpayer has given power of attorney in favour of its employees for signing the contracts, conducting negotiation and executing all necessary matters for the project in India. The taxpayer's business in India was carried out with the help of its employees, who regularly work from the premises of Huawei India. In view of the above, it was clear that the taxpayer, being tax residents of China, had fixed place PE in India in form of office premises of Huawei India. Agency PE The employees of Huawei India forms the sales teams of the taxpayer, such employees have habitually secured orders in India, wholly or almost wholly for the taxpayer. The documents in the form of agreements/purchase orders/copies of contracts also prove the active involvement of the employees of Indian company in the conclusion of contracts on behalf of the taxpayer. Huawei India was economically, technically and financially all dependent upon the taxpayer. Therefore, Huawei India also constitutes the agent other than an agent of independent status of Huawei China. This results into the creation of the dependent agent PE under the tax treaty and business connection under the Act Further, the process of joint bidding by the taxpayer and Huawei India constitutes Dependent Agent PE. Installation PE The taxpayer's employees also visited India to perform activities relating to installation projects lasting for more than 180 days, which constitutes Installation PE. Service PE The statements recorded during the survey also show that the employees render technical services continuing for more than 183 days, constituting Service PE. The facts recorded by the AO and upheld*

by the DRP in their order have not been controverted before the Tribunal, Accordingly, the Tribunal held that taxpayer had PE in India.

The above decision is squarely applicable to the case of the assessee as, on examination of the TP Study Report of FCL, the Panel finds that

- *In FCL substantial shares are held by FCC Japan, thus financially it is dependent on FCC Japan*
- *The supply chain framework seen from TP study report which clearly reflects the role of the AE in India and its dependence on capital goods and material for the production of goods to customers identified by the assessee.*
- *Participation of FCC Japan in the operations of the AF, which extends to identifying Indian suppliers/vendors, and also soliciting customers for the FCL products*
- *The Assessee controls and supervises FCL.*
- *FCL is both legally and economically dependent on the assessee.*
- *The sales claimed as direct are covered on account of Force Of Attraction on account of sales or other similar activities in the contracting state.*
- *The employees of the assessee are frequently visiting and engaging in non-technical monitoring and supervisory activities*
- *The products manufactured by FCL are sold to automobile manufacturers who have global collaboration with the assessee*

In view of the above discussion, it is apparent that FCL clears the Binding Test, Subjectivity test and Legal Dependence Test and Functional Test. The Panel upholds the stand of the assessing officer that FCL is a fixed place PE and supervision PE of the Assessee. Assessee's objection is rejected."

8. Aggrieved, the assessee is before us.

9. At the very outset, the Ld. AR submitted that in the present appeals, the solitary issue is in respect of the alleged existence of the PE of the assessee and the further attribution of profit on sale of raw material to FRL if FRL constitutes a Fixed Place PE and / or there is a Supervisory PE of the assessee in India. The Ld. DR conceded.

10. The Ld. DR strongly relied on the findings of the Ld. AO and Hon'ble DRP. He referred to the relevant clauses of the Licence Agreement, Agreement for Dispatch of Engineers and MSA with FRL and submitted that-

(i) All three agreements are integral to each other. It is evident from the fact that Article 5 of the Licence Agreement provides for entering into Agreement for Dispatch of Engineers. Article 17 of the Licence Agreement provides for procurement of parts and thus connects it to MSA.

(ii) From certain clauses under the MSA and License Agreement relating to acceptance, inspection of goods by the buyer, handling of rejected goods, product liability, claims in case of rejection of goods etc., it can be inferred that the title and risk associated with supply of goods passed in India and therefore, there is extension of business of the assessee in India in respect of the supply of parts to FRL/ FCC Clutch.

(iii) Fixed Place PE is created on account of presence of engineers at the work place in India. The Agreement for Dispatch of Engineers provides for engineers to be present at work place in India for technical guidance in manufacturing and assembly of products for which the Licensor is providing technical assistance to the Licensee. It also includes guidance of the Licensee's engineers and employees on operation procedures. Further, the Licence Agreement provides for after sales services and continues access to the improvement of manufacturing processes to Indian entity where its engineers visit frequently and work place is at its disposal for rendering

such services. The License Agreement also provides for permission to access work place in India for the purpose of inspection of parts procured, products manufactured, manufacturing processes etc. and the degree of control exercised by the assessee on Indian entity. The aforesaid facts signify that the business of the assesee is extended to India which is performed through engineers on visit to the work place in India. Thus, the work place at factory is the Fixed Place PE where the visiting engineers has control and access. In support, the Ld. DR relied on the judgment of the Hon'ble Delhi High Court in the case of GE Energy Parts Inc. (ITA No. 621/2017, dated 21.12.2018).

(iv) Supervisory PE is created due to the presence of the foreign expats in India throughout the year on various dates and their scope of work does include supervisory function in the form of technical guidance for the manufacturing and assembly work. It may be added that supervisory function includes the role of observing and directing/guiding the manufacturing and assembly activity. It also includes guidance on operational procedures for manufacturing facilities. Further, the stay period of engineers may be less than six months in the relevant assessment year but the project is in progress from the previous year(s) and hence, the threshold period of six months for supervision PE is satisfied at least in the AY 2015-16.

11. In its rebuttal to the arguments of the Ld. DR, the assessee made the following submissions:-

(i) Dispatch of Engineers Agreement and MSA are not integral to the Licence Agreement instead these are incidental/ consequential to it. It is stipulated under Article 5(3) that for providing technical guidance to FRL, the assesee would send the engineers the terms of which would be governed by a separate agreement i.e. Dispatch of Engineers Agreement. Similarily, MSA was entered later specifically for supply of goods and therefore, the

terms of MSA should supersede the clauses of License Agreement relating to the supply of goods and rights and responsibilities of both the parties i.e. the seller and the buyer in relation to such supplies.

(ii) Further, as far as the contention of Ld. DR of passing of title in goods in India is concerned, the assessee argued that the goods were manufactured outside India, sale of goods took place outside India and consideration was also received by the assesee outside India and thus, the assessee has not carried out any operation in India in relation to supply of the raw material and capital goods. Reliance placed by the Ld. DR on certain clauses from the MSA and License Agreement regarding acceptance inspection of goods by the buyer, handling of rejected goods, product liability, claims in case of rejection of goods etc. to emphasize that the title and risk associated with goods passed in India and upon certain judicial pronouncements [i.e. Ericsson AB (Delhi High Court) and Voith Paper GmbH (Delhi ITAT)] is completely misplaced since these cases are distinguishable on facts of the present case in hand. In these cases the supplies were made from outside India and were erected on particular site or locations in India, whereas the assessee's case is of simpliciter supply of raw material and capital goods used by the Indian AE (FRL) in manufacturing process. In support of its agreements, the assesee relied upon the judgment of the Hon'ble Supreme Court in the case of Mahabir Commercial Co. Ltd. Vs. CIT 1973 AIR 430 wherein the Hon'ble Supreme Court held that right to examine and repudiate the goods does not indicate that property in the goods has not passed to the buyer.

It was further submitted that even if it is assumed, though not accepted, that title of goods is transferred in India, no attribution of supplies could be made in absence of a PE in India. For attributing the income from supply of goods, the role of PE in such supplies would have to be established. In the instant case, neither the constitution of PE has been established nor has it been established that the alleged PE has played any role in supply of goods. Accordingly, no attribution could be made.

(iii) Due to non-satisfaction of disposal test and carrying on of business activity test by the assesee in India, allegation of Fixed Place PE is misconceived as held by the Hon'ble Supreme Court in Formula One World Championship [Civil Appeal No. 3849 of 2017]and E-Funds IT Solutions Inc. [Civil Appeal No. 6082 of 2015]

Further, reliance placed by the Ld. DR on the decision of Hon'ble Delhi High Court in the case of GE Energy Parts (supra) is not correct as the facts of the case were completely different. In the said case, the overseas company had a Liaison Office (LO) in India and the expatriates were having specific chambers/rooms allotted to them with their name plates affixed and they were occupying the same. Such expatriates along with employees of the Indian company were negotiating the contracts with Indian customers for sales/supplies to be made by the overseas company. Thus, the expatriates were undertaking the core business activities of the overseas company with the help of employees of the Indian company. However, in assessee's case no business of the assessee was undertaken by the expatriate employees in India. The expatriates only rendered technical services to assist FRL in its manufacturing process for which FTS was paid by FRL to the assessee. Moreover, it has never been established by the Revenue that any place was at disposal of the employees of the assessee in India. Merely providing access to the premises by FRL for the purpose of providing training/rendering technical services by the assessee does not amount to the place being at the disposal of the assessee. In the instant case, FRL is manufacturing and selling the goods in India using the technical information and know how provided to it by the assessee. Also, FRL is selling its goods under the brand name of FCC. Thus, to ensure the quality of goods and manufacturing facility is as per the global standards of the assessee, the latter has the right to inspect the products manufactured by FRL as well as manufacturing facilities of the FRL. Merely access for inspection does not establish that the place is at the disposal of the foreign

entity. Even otherwise, carrying on of inspection does not establish that core business activity of the assessee was being carried out in India.

(iv) Supervisory PE can be constituted only if supervision is in connection with a building site or construction, installation or assembly project. Also, the international tax commentaries suggest that installation and assembly project has to be mainly read in conjunction with building site or construction. The assessee further reiterates that its Indian AE is in the business of manufacture and assembly of clutches in India for which the assessee provides time to time technical assistance as required by its AE. The Ld. AO/DR confused the assembly of clutches with supervision of assembly project as envisaged in Article 5(4) of the India-Japan DTAA. In the facts of the instant case, the assessee is not doing supervision in connection with any building site or construction, installation or assembly project. Thus, question of establishment of supervisory PE does not arise. Services of the nature rendered by the assessee may give rise to Service PE (and not supervisory PE), however, in the absence of Service PE clause in the India-Japan DTAA, this issue becomes academic. The supervisory PE of the assesee was not established either in AY 2014-15 or AY 2015-16 as no building site or construction, installation or assembly project has been undertaken by FRL in India for which any supervision service was rendered by the assesee. Hence, the issue of computing the period of six months in the present case is academic. On the contrary, if the argument of the Ld. DR is accepted it would lead to a situation where the building site or construction, installation or assembly project is forever because on the year to year basis technical personnel are coming to India under the contract and it is unimaginable that such activity will continue till the Indian AE manufactured goods from the technical information provided by the assessee for manufacturing process of finished goods in India.

12. We have heard the Ld. Representatives of both the parties at length and perused the material on record. The primary issue before us is the determination whether FRL constitutes Fixed Place PE and / or if there is a

Supervisory PE of the assessee in India in the AYs under consideration. Lets first analyse the provisions relating to the Fixed Place PE as provided under the India-Japan DTAA.

12.1 Article 5(1) of the India-Japan DTAA provides that a PE of a foreign enterprise may exist in India when a foreign enterprise has a Fixed Place in India through which the business of the foreign enterprise is wholly or partly carried out.

12.2 In order to constitute a Fixed Place PE under Article 5(1), the following conditions needs to be satisfied:

(i) the existence of a 'place of business', i.e. a facility such as premises;

(ii) the place of business must be at the disposal of the enterprise;

(iii) this place of business must be 'fixed', i.e. it must be established at a distinct place with a certain degree of permanence; and

(iv) the 'carrying on of the business' of the enterprise through this fixed place of business.

12.3 In the present case, FRL is alleged to be the place of business from which the business of the assesee is being carried out. It is well settled position that in order to constitute a Fixed Place PE it is a prerequisite that the alleged premise must be at the disposal of the enterprise. The Hon'ble Supreme Court in the case of Formula One world Championship Vs. CIT [Civil Appeal No. 3849 of 2017] has held that merely giving access to the premise to the enterprise for the purposes of the project would not suffice. The place would be treated as at the disposal of the enterprise when the enterprise has right to use the said place and has control thereupon.

12.4 In light of the facts of the case and various judicial precedents wherein the constitution of Fixed Place PE has been considered and adjudicated upon, in our opinion the conditions laid down for creation of a Fixed Place PE is not satisfied in the assessee's case. Merely providing access to the premises by FRL for the purpose of providing agreed services by the assessee would not amount to the place being at the disposal of the assessee. No doubt the assesee has access to the factory premises of FRL but it is for the limited purposes of rendering agreed services to FRL without any control over the said premises. Moreover, FRL is an independent legal entity carrying on its business with its own clients for which the assessee provides time to time technical assistance as required by it. The business of the assesee is not being carried out from the alleged Fixed Place PE. The Ld. DR in support of his contention that FRL constitutes Fixed Place PE of the assessee has placed reliance on certain clauses of the Licence Agreement and argued that title of goods supplied by the assessee to FRL passed in India and hence the assessee is carrying on business in India. In our opinion, reference to these clauses is irrelevant to conclude that the title of goods passed in India and thus Fixed Place PE of the assessee is created in India in view of the judgment of the Hon'ble Supreme Court in Mahabir Commercial Co. Ltd (supra). Since the goods were manufactured outside India, sale of goods took place outside India and consideration was also received by the assessee outside India, title passed outside India and hence the assessee has not carried out any operation in India in relation to supply of the raw material and capital goods. We therefore hold that the assessee does not have a Fixed Place PE in India.

13. Now coming to the Supervisory PE, Article 5(4) of the India-Japan DTAA provides as under-

"An enterprise shall be deemed to have a permanent establishment in a Contracting State and to carry on business through that permanent establishment if it carries on supervisory activities in that Contracting State for more than six months in connection with a building site or construction, installation or assembly project which is being undertaken in that Contracting State."

13.1 In the previous hearing held on 1.11.2021 this Bench had directed the assessee to file the description of services rendered by the employees of the assessee on their visit to India and the corresponding clause under the Agreement for Dispatch of Engineers under which such services would fall. In response, the assessee furnished Annexure 1 for AY 2014-15 and Annexure 2 for AY 2015-16 vide its written submission filed on 17.11.2021 providing the names of the employees who visited India along with the work performed by them giving reference of the relevant clause of the Agreement for Dispatch of Engineers along with Request for Technical Services (RFT) of the respective employee. The said Annexure 1 and Annexure 2 are on record.

13.2 Perusal of the above documents show that the employees of the assessee visited India to assist FRL in relation to supplies made by FRL/FCC Clutch to its customers; resolving problems relating to production, fixing of machines, maintenance of machines; checking safety status at the premises and suggesting ways for enhancing safety; support in quality control; IT related services; support for launch of new segment line; etc. In our considered opinion, none of these activities performed by the employees are in the nature of supervisory functions, supervision being the act of overseeing or watching over someone or something which is not reflected in the work done by the engineers in India for FRL.

13.3 Moreover, no installation or assembly project was on going at FRL's premises. FRL is in the existing business since many years and no new line of business has been launched by FRL. The employees were not rendering any services in connection with building site or a construction project or an installation project or an assembly project. From the nature of the services rendered by the employees, it is amply clear that these activities were not in connection with a building site or construction installation or assembly project. Hence the issue of computation of period of six months also becomes academic. The employees are visiting India on year to year basis under the contract. In AY 2014-15 and AY 2015-16, the employees visited India to render certain technical services under the Licence Agreement read with Dispatch of Engineers Agreement which have been duly offered to tax by the assessee as FTS as per the provisions of India-Japan DTAA. We therefore hold that the there is no Supervisory PE of the assessee for the AYs under consideration.

13.4 Since we have held that the assessee does not have a PE, the issue of attribution of profits to such PE does not arise for consideration.

14. The grounds relating to charge of interest under section 234B and levy of penalty under section 271(1)(c) of the Act are consequential.

15. In the result, the appeals of the assessee are allowed.

Order pronounced in the open court on 9th March, 2022.

sd/-	**sd/-**
(N.K. BILLAIYA)	**(ASTHA CHANDRA)**
ACCOUNTANT MEMBER	**JUDICIAL MEMEBR**

Dated: /03/2022

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