

**IN THE INCOME TAX APPELLATE TRIBUNAL  
“I” BENCH, MUMBAI**

**BEFORE SHRI AMIT SHUKLA, JM &  
SHRI GAGAN GOYAL, AM**

आयकरअपीलसं./ I.T.A. No. 1857/Mum/2022  
(निर्धारणवर्ष / Assessment Year: 2019-20)

<b>Nan Lian Ship Management LLC</b> C/o- Chamber 2 & 3, Cosmos Trade Place, Ground floor, Khatu Building, Opp-BSE, Fort, Mumbai-400 001	<b>बनाम/ Vs.</b>	<b>ACIT (Int. Tax) – 3(3)(1),</b> 1630, 16 <sup>th</sup> floor, Air India Building Nariman Point, Mumbai-400 021
स्थायीलेखासं ./जीआइआरसं ./PAN No. AAGCN0478E		
(अपीलार्थी/ <b>Appellant</b> )	:	(प्रत्यर्थी / <b>Respondent</b> )

अपीलार्थीकीओरसे/ <b>Appellant by</b>	:	Shri Nishit Gandhi /Dhanlaxmi Iyer, Ld. ARs
प्रत्यर्थीकीओरसे/ <b>Respondent by</b>	:	Shri Soumendu Kumar Das, Ld. DR
सुनवाईकीतारीख/ <b>Date of Hearing</b>	:	03.11.2022
घोषणाकीतारीख / <b>Date of Pronouncement</b>	:	30.12.2022

आदेश / O R D E R

**Per Amit Shukla, Judicial Member:**

The aforesaid appeal has been filed by the assessee against the final assessment order dated 27.05.2022, passed by Ld. AO u/s

143(3) r.w.s. 144C(13) for the AY 2019-20 in pursuance of direction given by Ld. DRP vide order dated 18.05.2022 u/s 144C(5).

2. In the grounds of appeal, assessee has challenged the direction of Ld. DRP in treating the amount of Rs. 20,28,98,639/- received by the assessee on account of Time Charter of its ship as **'royalty'** and taxing the same u/s 9(1)(vi) of the Act.

3. The facts in brief are that, assessee is a company incorporated in and tax resident of UAE and is engaged in the business of shipping operation. It has entered into Time Charter contract with M/s Poompohar Shipping Corp. Ltd. (PSCL) dated 18.04.2018 for transporting coal from Paradeep port to Tutucorine in Tamil Nadu, through its ship 'MV Eastern View'. The said contract was a period of 13 months. The assessee in turn has chartered the vessel 'MV Eastern View' from M/s Power Overseas Investment LLC, again on Time Charter Basis. The assessee has disclosed the receipts of transporting coal from port to port from (PSCL) as shipping business and offered to tax u/s 44B of the Act, i.e. @ 7.5% of the gross receipt attributable to shipping operations carried out in India.

4. Ld. AO after analyzing the contract between the assessee and M/s PSCL, deduced that assessee is simply letting out the vessel and PSCL has hired the vessels for the period of 13 months for carrying out coal from Paradip port to Tuticorin, Tamil Nadu. He held that PSCL is paying the assessee for the use/right to use by way of leasing or letting out the vessel and therefore, the same is to be taxed under 'royalty' u/s 9(1)(vi). AO observed that assessee is being paid fixed amount irrespective of fact, whether the vessel is being used by the charter or not. He held that assessee is not being paid for transporting coal from one port to another within India territory albeit for leasing the vessel. Therefore, it cannot be taxed u/s 44B of the Act. Thus, on these facts he strongly relied upon the judgment of Hon'ble Madras High Court in the case of **M/s Poompuhar Shipping Corp. Ltd. vs. ITO (360 ITR 257)** and held that the amount received by the assessee is liable to tax under the head 'Royalty'.

5. Ld. DRP had confirmed the draft order of the AO after observing as under:-

5. We have perused the draft assessment order. We have also considered the written and oral submissions of the assessee. The fact of the matter is that the assessee is a non-resident entity. The assessee provided its ship for hire to an Indian company for a fixed period, for transportation of coal between two ports in India. The contract is a 'Time Charter' agreement in 'Government Form' 'approved by the New York Produce Exchange'. The assessee offered the hire charges for taxation u/s. 44B of the Act. The assessing officer did not agree, because he noted that the receipts in question were not for carriage of goods, but for use and hire of ship, which was an equipment, therefore, proposed it to be treated as royalty u/s. 9(1)(vi) of the Act. The assessing officer relied upon the decision of the Hon'ble Madras High Court in *Poompuhar Shipping Corporation Ltd. vs. ITO (International Taxation) - II Chennai*, [2013] 38 taxmann.com 50 (Madras).

We have considered all the material placed before us. We note that the Hon'ble Madras High Court has specifically dealt with the same kind of contract in standard time charter form, 'approved by the New York Produce Exchange' and held that time charter agreements are essentially for use and hire of ship and the amount received is not for carriage of goods. We note that the Hon'ble Madras High Court has relied upon the decision of the Hon'ble Supreme in the case of *Gosalia Shipping* [1978] 113 ITR 307 (SC) for the meaning of 'time charter agreement'. The Hon'ble Madras High Court has held that ship is an equipment within the meaning of section 9(1)(vi) r.w. explanation 2 of the Act and the amount

*received would fall under 'royalty' in the same section. We are of considered opinion that the decision of the assessing officer has merits and therefore, we do not find any reason to have different opinion from the opinion of the assessing officer. Therefore, the ground of objection no. 1 is dismissed.*

6. Before us, Ld. Counsel for the assessee submitted that, first of all, assessee has rightly offered the income u/s 44B of the Act for the reason that assessee is a non-resident company engaged in the business of operation of ships and therefore, income derived from business of operation of ships has to be taxed under the special provision. He submitted that from the perusal of the time charter agreement between the assessee and PSCL, it can be seen that the assessee is a vessel owner and was responsible for the crew as being the vessel master. The ship was under the control of the assessee company and the PSCL has only taken on a time charter basis for transporting the coal from one port to another. Even the vessels stowage plan was to be made under the Master's supervision and the master shall co-operate with the charters to load and stow the charter's intended cargo. Even the freight calculation was based on the quantity of the load which has to be assessed by the surveyor of charter and based on that the payment

was made to the assessee company. The assessee, i.e., owner of the vessel was obliged to keep the vessel and the crew up to date with complete certificate, approvals and equipment enabling the vessels to carry the cargo. Further, if on the delivery, the vessel was found more than the specified quantity of bunker resulting in short loading of cargo due to excess bunker on board, the pro-rata cost of short loaded cargo was to be charged to the owner's account. The owners had the liberty of flying their own house flag and this inter alia means that at all time, the possession and the ownership was with the assessee company and PSCL was only using the ship on a time charter basis. In support, he drew our attention to various clauses of the agreement. Thus, when the assessee had all the control over the vessel, the same cannot be said that PSCL had the full control of the ship, which cannot be treated as payment received was use or right to use the equipment i.e. ship. Further in support of his argument, he relied on the decision of ITAT Mumbai Bench in the case of **M/s Smit Singaport Pte Ltd. vs. DCIT (ITA No. 7055/Mum/2017 order dated 09.11.2020)** and the decision of ITAT in the case of **M/s Siscal Logistics Ltd. vs. ACIT in ITA No. 1074-1079/Mds/2015 order dated 14.12.2016.**

7. On the other hand, Ld. DR strongly relied on the orders passed by AO and Ld. DRP and submitted , in the case of Poompuhar Shipping Corporation Ltd, the Hon'ble Madras High Court has clearly held that the payment made to a non-resident company who has given the ship on time charter basis to Poompuhar Shipping Corp. Ltd. is a 'Royalty' within the meaning of section 9(1)(vi). Thus, this issue stands squarely covered against the assessee by the Hon'ble Madras High Court in the case of the payer itself therefore, no different view can be taken.

8. We have heard the rival submissions and also perused the relevant findings given in the impugned orders as well as material placed on record. The main issue involved here is, whether the income earned by the assessee is to be taxed u/s 44B of the Act on the presumption basis as claimed by the assessee in the return of income; or whether the receipt should be taxed as 'royalty' for use of an equipment in terms of clause (iva) to *Explanation 2* to section 9(1)(vi).

9. The case of the assessee is that, since it is a non resident company engaged in the business of operation of ships, i.e., the

ship of the assessee is used for transporting of coal and has operated a ship on time charter basis by PSCL, therefore it has been subjected to tax under the special provision of section 44B of the Act. Whereas, the case of the revenue is that the ship is equipment which has been let out by the assessee and hired by the charter. The receipts are in the nature of hire charges, therefore, it is the use of the equipment and accordingly, the judgment of Hon'ble Madras High Court is squarely applicable.

10. First of all, we have to see whether the income earned by the assessee was in the nature of 'royalty' within the meaning of section 9(1)(vi) r.w. *Explanation (iva)*. *Clause (iva)* to *Explanation 2* of section 9(1)(vi) reads as under:-

***(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44B.***

11. What is to be seen is, whether the assessee has given use or right to use the ship to PSCL and the payment received for time charter services falls within the ambit and definition of *Clause (iva)* (supra) or not. The relevant clauses of Time Charter agreement as noted and analysed by the AO reads as under:-



*Preamble - The agreement dated 18th April 2018 is between Nan Lian Ship Management LLC (Owner) and M/s Poompuhar Shipping Corpn Ltd., (charterer). That the said Owners agree to let, and the said charterers agree to hire the said vessel, from the time delivery, for a period of 9 months +3 months choption + 1 month at choption within below mentioned trading limits. Vessel to be placed at the disposal of the charterers, at thermal coal loading berth at Paradip any time day or night closed holiday in port excluded*

*b) Clause 1 - That the Owners shall provide and pay for a/I provision, wages and consular Shipping and discharging fees of the Crew; shall pay for the insurance of the vessel, also for all the cabin, deck, engine-room and other necessary stores,, including boiler water and maintain her class and keep the vessel in a thoroughly efficient state in hull, machinery and equipment for and during the service with classification and statutory certificates necessary to comply with current requirements at ports of call during the service.*

*As per above clause, the owner (the assessee) to provide any to pay for all provisions, wages and shipping and discharging fees and all other expenses, of-the Master, Officers and Crew, to pay for ail insurance on the vessel including cover for P&I pollution risks, for all deck, cabin and engine room stores etc.). Even though the assessee has itself chartered the vessel from M/s Power Overseas Investment LLC, it does not absolve him from its contractual*

*liability with Poompuhar to fulfill all owner's obligation vis-à-vis Poompuhar.*

*c) Clause 2 - That the charterers whilst on hire shall provide and pay for all the fuel except as otherwise agreed. Port charges Pilotages charterer's agencies fees, commissions. Furnigatins ordered because of cargoes carried or ports visited while is employed under this charter to be for charterers account. Charterers are to provide necessary dunnage and shifting boards, also any extra fittings for a special trade or unusual cargo.*

*As per above clause, the Charterer (Poompuhar) to provide and pay for all fuel (except gallery fuel), towage and pilotage and shall pay agency fees, port charges, commissions, expenses of loading and unloading cargoes, canal dues etc.*

*d) Clause 3- That the charterers, at the port of delivery and the owners at the port of re-delivery, shall take over and pay for all fuel remaining on board the vessel.*

*e) Clause 4 - That the charterers shall pay for the 'use and hire of the said vessel at rate of USD 13100/- per running day 24 hrs per calendar month including overtime commencing on and from the day her delivery, as aforesaid^, and at and after-the same rate for any part of a month, hire to continue until the hour of the day of her re-delivery in like good order and condition wear tear expected, to the Owners (unless lost) at a safe berth..*

*As per above clause, the Charterer is making payment for the use and hire of the vessel at the rate of charter hire USD 13,100 PDPR (per day pro-rata).*

*f) Clause 6- That the cargo or cargos be laden arid/or discharged in any dock or at any wharf or place that charterers or their agents may direct,*

*g) Clause 7 - That the whole reach of the vessel's holds, decks and usual place of loading (not more than she can reasonably stow and carry), also accommodations for supercargo, if carried shall be at the charterer's disposal, reserving only proper, and sufficient space for Ship's officers, crew, tackle, apparel, furniture, provisions, store, and fuel.*

*As per above clause, it is clear that the charterer has the whole vessel at its disposal except for space required for officers and crew.*

*h) Clause 8 - The captain (although appointed by the Owner), shall be under the orders and direction of the charterers as regards employment and agency; and charterers are to load, stow, trim tally and discharge the cargo at their expense under the supervision of the captain, who is sign Mates receipt for cargo as presented in conformity with charterers appointed survey report without prejudice to this C/P. Charterers indemnifying owners ail consequences by Master signing the Bills of loading.*

*As per above clause, it is clear that the Charterer is to give the Master all requisite instructions and sailing directions and Master shall keep full. It is the charterer's responsibility to load, stow, trim, tally and discharge the cargo at their expense and the Captain is required to sign the Mates receipts as presented by the charterer. Furthermore, the Charterer has indemnified the Master from any consequences of signing on Bill of Lading by him which shows that the Master is to sign Bill of Lading at the instruction of the Charterer.*

*j) Clause 10- That the Charterers shall have permission to appoint a Supercargo, who shall accompany the vessel and see that voyages are prosecuted with the utmost despatch. He is to be furnished with free accommodation and same fare as provided for captain table charterers paying at the rate of Rs.30/- or USD.....per day.*

*As per above clause, it can be : seen that the Charterer is entitled to appoint its own officer/crew to ensure that the voyages are executed with utmost despatch which means that the Charterer has control over the officer and crew during the voyages taken by the vessel.*

*k) Clause 11- That the charterers shall furnish the captain from time with requisite instruction and sailing directions, in writing, and the caption shall keep a full and correct log the voyage, which are to be patent to the charterers or their agents, and furnish the charterers, their agents or supercargo, when required with a true*

*copy of daily logs, showing the course or the vessel and the consumption of fuel.*

*As per above clause, it is very much clear that the master, officers and crew are under the instruction and direction of the Charterer.*

12. The preamble which has been interpreted by the AO that it is for letting up the vessel and hiring by the charterer cannot be treated as giving up the vessel for hiring simplicitor or that the owner has agreed to be a captive service provider to the charter for transporting the coal between the ports. The vessel which has been stated to be at the disposal of the charterer means that the vessel during the period of time charter cannot be made available to any other party as the same is for the use of the charter for that period. In so far as *clause 1*, it stipulates that it is the owner who is responsible for everything right from the wages, salaries for crew and insurance and stows and for counselor shipping and discharging the fees of the crew and maintaining the vessel in a proper state. This inter alia state that the vessel is in possession and ownership and maintenance of the assessee and not that the charterer. In so far as *clause 2* is concerned, it only shows that expenses for usage which is valuable cost is that of the charterer

and the cost of any excess fuel on the expiry of contract will be back to the charter party. The AO has strongly referred *Clause 4* to interpret that charterer is making the payment for the usage and hire of the vessel at the rate of charter i.e. USD 13,100 per day pro-rata. This Clause very clearly shows that ***“Charterer shall pay for the use and hire of the said vessel of USD 13,100, per running day of 24 hours per calendar month including the overtime commencing on and from the day of delivery, as aforesaid, and at and after the same rate for any part of a month, hire to continue until the hour of the day of her re-delivery in like good order and condition.....”*** This Clause goes to show that the charterer had to pay for the use and hire of the vessel per running day of the calendar month. Once the hire charges is based on per running day, it cannot be inferred that it is a outright time charter agreement *per se*, wherein the ship has been given on lease rent simplicitor to the charterer to use and earn fixed rent which is typically in the case of time charter agreement. First of all, the usage of vessel by the charterer is for a specific purpose of transporting the coal and the charterer would need a dedicated service provider with the necessary competence. The method of

determination of remunerating the service provider has been arrived at on the basis of calculation of the load which has been provided in the said agreement. Similarly, *clauses 6 & 7* stipulate that, captive service provider has to provide service of transportation exclusively to the charterer and the vessel cannot be utilized for anyone else in the period of time charter. In so far as clause 8 is concerned, the captain (although appointed by the owner) shall be under the orders and direction of the charterer and for various other directions and it is the charterer responsibility for loading and stowing, etc. It merely signifies that charterer will decide the load and the voyage. Similarly, AO has referred clauses 10 & 11 which show the officers and crews were under the instruction and direction of the charterer. The AO has interpreted these clauses that the charterer alone had the control over the vessel. This control is only to the extent of exclusive use by the charterer to load and carry coal. In the case of a time charter, one has to appreciate that the vessel is maintained on the requirement of the charterer and all necessary documents is to be maintained by the owner to satisfy various requirement. However, the vessel continues to be owned, operated and maintained by the vessel as owner as per the requirements of the

charterer for which the compensation /remuneration has been agreed on certain basis which is fixed on cost + margin depending upon the load of the carriage. Though the payment may accrue whether the charterer requires it or not, but the compensation is paid to the owner for the transportation of the coal depending upon the load by the charterer. Even from the clause which has been referred by the AO that it is the lease or let out of a ship to the charter who is using the ship for the period of charter in the manner he desires on independent basis with no control of the owner is incorrect inference and does not envisage that the charterer has any control of the ship except for carrying the coal as per the requirement of the charterer and all time the ownership and control is with the owner which is evident from the terms of the agreement. The compensation is merely to decide the quantity of load on the ship by the charterer and not otherwise. To fall within the ambit of use or right to use equipment, it is *sine qua non* that the hirer or the charterer has complete control and ownership of the equipment for the period of lease and the owner is only earning passive income by simply letting out the equipment.



13. We have analysed further clauses of the time charter agreement between the assessee and the charterers which are enumerated here in after, clearly indicates that there is no absolute right to use of vessel has been given to charterer:

- Clause 24: As per this clause it has been provided that nothing in the agreement shall be construed as demise of the vessel to the time charterers. The owners are responsible for navigation, insurance, crew and all other matter in the same manner as if on their own account.
- Clause 25: As per this clause the vessel hire charges could be deducted based on the unavailability of the vessel.
- Clause 26: As per this clause the vessel stowage plans are to be made under the Master's supervision. This further provides that if the full cargo cannot be loaded the Owners (the Assessee) shall be liable to compensate for the dead freight computed on the basis of the loading quantity of the vessel which again proves that it is not a lease of equipment simplicitor as assumed by the AO or a mere right to use equipment as assumed by AO
- Clause 27: As per this clause the owners are responsible for delivering and keeping the vessel and its certificates, approvals, etc. upto date and any loss caused due to this failure shall be deducted from the hire dues.

- Clause(s) 29, 32 : As per these clauses the hire charges would be reduced pro-rata if the loaded bunker on the vessel leads to a lesser loading capacity for the charterer or the vessel is off hire for any reasons or the vessel is out of service. As such it is not a mere letting of equipment. Further it is also provided that if the vessel is off hired for a period of 24 hours to 8 days due to repairs all the charges including shifting charges, pilotage, berth hire, etc. will be to the owners account.

It is also provided that any loss due to underperformance of the vessel will also be on owners' account which clearly shows that it is not a bare letting of the vessel as assumed by the Ld. AO.

- Clause 37: As per this clause the Charterers are entitled to determine the damages and compensation for poor / low performance levels of the vessel. Even as per this clause specifically clause (d) load capacity is relevant to determine the compensation. It also provides for damages on account of delay in delivery or behind the lay days i.e., days on which the vessel is laid off. Interestingly, even for this the amounts are calculated based on the loading capacity of the Vessel and the loading capacity lost and based on this the damages are deducted from hire charges or to be recovered from the Owner.

- Clause 38: As per this clause, the Owners warrant the suitability of the vessel for loading and transporting coal meaning the fitness of the vessel for transporting coal is determinative for the purpose of the agreement.
- Clause(s) 44, 45: As per these clauses, the compensation for non-adherence to loading rate is provided for. Further, the compensation for incapacitation or breakdown of the vessel is also provided, as per which the said loss / compensation would be on owners account. The said loss / damage / compensation would be calculated on the basis of ocean freight charges. These clauses clearly indicate that the hire charge is not independent of the loading capacity / loading rate and therefore it is not a mere payment of hire for letting out of equipment as assumed by the Ld. AO.
- Clause 47: As per this clause, neither hire nor cost of bunker is payable by the Charterer in case the vessel is captured, seized, detained, etc. by any person. In case of simplicitor letting of the ship, this clause would not have been incorporated.
- Clause 58: This clause specifically excludes certain types of cargo to be loaded and transported. However, if it would have been a bare letting for use of the Ship, owners would not have a say in the matter. Further, the agreement specifically provides that the vessel cannot be used or engaged in scraps trading. It therefore follows that the

amount paid is only for an exclusive purpose of transportation of coal.

- Clause 60: As per this clause all taxes, levies, duties, etc. on the vessel are to be on the owners account except for the taxes on cargo transported by charters.

14. All these clauses clearly indicates that, *firstly*, the compensation is based on freight as per the loading per voyage; *secondly*, the vessel owner is responsible for the entire maintenance and keep of the vessel; *thirdly*, the hire charges are liable to be reduced pro-rata if the load on the vessel leads to lesser loading capacity for the charterer or if the vessel is out of service, then the charges are accordingly reduced and if there is any action, the vessel is not hired for a period of 24 hours to 6 days, then all those charges will be on owners account; and *lastly*, any compensation for non-adherence to loading or breakdown of the vessel loss/damage, the compensation is calculated on the basis of ocean freight charges. Thus, the hire charges are not independent of the loading capacity and therefore, it cannot be inferred that payment of hire is for letting out of equipment as assumed by the AO. Thus, it is not a case of leasing out of an equipment and use or right to

use of equipment is for the carriage in the vessel owned and operated by the owner and it is not a case of simply by letting out the ship for certain time period.

15. Further, one very important fact which is emerging is from Clause 26, where the owner and the charterer have decided the method of calculation for arriving at the dead freight and the cost.

The relevant portion of which reads as under:-

Dead-freight calculations;

1. Charter period from RFA previous discharge port to RFA next discharge port

..... Days ..... Hours ..... Minutes x charter hire per day

2. Bunker consumption for the above voyages

FO                      MT x              Rs.....      (at current price)

HFHSD              MTx      Rs.....      (at current price)

3. Actual port charges levied by the port(s)

Load port = Rs,

Discharge port = Rs,

4. Miscellaneous expenses -Rs. ....

Total cost (X)                      = Rs.

Total cargo loaded (Y) -                      mt

5. Cost per tonne (Z) =  $\frac{(X) \text{ Total expenses incurred for one round voyage}}{(Y) \text{ Total cargo loaded}}$  =Rs.

6. Cost to be recovered towards of dead freight = Z x dead freight quantity

*The short loaded quantity as assessed by charterer surveyor at load port shall be taken for dead freight calculation. Due allowances shall be given for dock water density, excess bunkers on board, limitation at the berth due to draught restrictions, charterer's / agents instruction on specific voyages to sail short loaded in order to catch the tide or high water. Charterers shall also rely upon the cargo declarations made by Owners at the time of offer as the base figures for dead freight assessment.*

16. This clearly shows that the payment was subject to load of the cargo and it was not simply for leasing or renting out the ship for the time charter period. Thus, from the reading of various clauses of the agreement, it cannot be inferred that it was purely fixed rental receipt by the assessee for lease of equipment. In fact all throughout the control of the equipment remained with the assessee and at no point of time owner has transferred the vessel to the charterer for carriage of goods. Albeit, the agreement envisages more of voyage charter by the vessel owner and therefore, in our opinion, the same cannot be fall strictly within the realm of definition provided of 'royalty' in terms sub clause (iva) to *Explanation 2*. The concept of dominance or control over ship by the charterer on the equipment is paramount in determining the character of payment as payment of 'royalty' and in absence of the same cannot be treated as royalty. This is also coupled of the fact

that payment received by the owner from the charter is firstly, based on use of per running day; and secondly, calculation of dead freight was dependent upon the load per voyage. In such a situation, the payment received by the owner from the charterer has to be reckoned as payment from operations of carriage of goods from one port in India to another port in India, which falls under the ambit of carrying out shipping business or shipping operators.

17. We find that this Tribunal in the case of Smit Singapore Pte Ltd. similar charter agreement was under consideration by a foreign resident owning a ship who has given it on a time charter to an Indian company. The relevant observation and finding of the Tribunal reads as under:-

*15. In our considered view, the genesis of the controversy involved in the present appeal primarily hinges around the aspect that as to whether or not the lower authorities were right in concluding that the consideration received by the assessee from the time charter of the vessel viz. 'Smit Borneo' alongwith the crew was to be treated as 'royalty', both as per the clause (iva) of the 'Explanation 2' to Sec. 9(1)(vi) of the Act, AND Article 12(3)(b) of the India-Singapore Tax Treaty. Before proceeding any further, it may be relevant to point out that the fact that the assessee during the year under*

*consideration had not constituted any PE in India is not in dispute before us. For a fair appreciation of the issue under consideration, it would be relevant to cull out the definition of the term 'royalty' as contemplated in 'Explanation 2' to Sec. 9(1)(vi) of the Act, AND Article 12(3)(b) of the India-Singapore tax treaty. The term 'royalty' as defined in the 'Explanation 2' of Sec. 9(1)(vi) of the Act, reads as under:*

*"Explanation 2.—For the purposes of this clause, "royalty means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head 'Capital gains") for-*

*(i) the transfer of all or any rights (including the granting of a license) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;*

*(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;*

*(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;*

*(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;*



*(v) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;*

*(vi) the transfer of all or any rights (including the granting of a license) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films; or (*

*vii) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v)"*

*Further, the term 'royalty' has been defined as per Article 12 of the India Singapore tax treaty, as under: —*

*3. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use :*

*(a) any copyright of a literary, artistic or scientific work, including cinematograph films or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right, property or information;*

*(b) any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraphs 4(b) or 4(c) of Article 8.*

*As observed by us hereinabove, the assessee in order to impress upon us that its case does not fall within the meaning of the term 'royalty' as defined in 'Explanation 2' to Sec.9(1)(vi) of the Act, had come forth with two fold contentions viz. (i) that, as the assessee had time chartered its vessel 'Smit Borneo' along with the crew to Leighton India Contractor Pvt. Ltd., and had not given or parted with the 'use' or 'right to use' of the said vessel to the charterer viz. Leighton India Contractor Pvt. Ltd, therefore, the consideration received in lieu thereof could not be held as royalty; and (ii) that, as the services provided by the assessee by time charter of its vessel viz. 'Smit Borneo' were inextricably connected with prospecting, extraction and production of mineral oils, the consideration therein received from the charterer being in the nature of amounts referred to in Sec. 44BB of the Act, would thus fall within the exclusion carved out in the definition of the term 'royalty' as contemplated in clause (iva) of the 'Explanation 2' to Sec.9(1)(vi) of the Act. We shall first deal with the second limb of the aforesaid contention advanced by the ld. A.R before us. As observed by us hereinabove, it is the claim of the assessee that as the time charter receipts were covered by Sec. 44BB of the Act, the same would thus fall within the exclusion carved out in the definition of the term 'royalty' as contemplated in clause (iva) of the 'Explanation 2' to Sec. 9(1)(vi) of the Act. We are unable to persuade ourselves to accept the*

*aforesaid claim of the assessee. As had been observed by us hereinabove, in the absence of the assessee's PE in India, the aforesaid time charter receipts could not have been brought to tax under Sec.44BB of the Act. In fact, the assessee had itself not offered the aforesaid amount for tax under Sec.44BB of the Act. Accordingly, in the backdrop of the aforesaid facts, now when the time charter receipts during the year under consideration had not been brought to tax, or in fact, could not have been subjected to tax under Sec. 44BB of the Act, therefore, the claim of the assessee that the same would fall within the scope and gamut of the exclusion carved out in the definition of term 'royalty' as contemplated in clause (iva) of the 'Explanation 2' to Sec. 9(1)(vi) cannot be accepted, and is thus rejected.*

18. Thus, in our view, the payment received by the assessee cannot be treated as 'royalty' u/s 9(1)(vi).

19. Now coming to the judgment of Hon'ble Madras High Court in the case of **Poompuhar Shipping Corporation Ltd. (supra)**. In the bunch of appeals, in one of the bunch, the issue involved was, whether the payment made for taking ship on time charter basis would constitute 'royalty' as defined in section 9(1)(vi) of the Act and tax has to be deducted at source; and whether charterer merely acquires a right for performance of services by the ship owner for

carry of goods and is not for the use of ships pure and simple. The another controversy was whether the ship is an equipment or not. The Hon'ble High Court after detail discussion, held that firstly, the ship falls within the ambit and scope of equipment as contemplated in section 9(1)(vi) *clause (iva) of Explanation 2*. Thereafter, the Hon'ble High Court after considering the various gamut of arguments and the judgments had made the following relevant observations:-

*78. As far as the present case is concerned, 'royalty' means the consideration paid for "the use or right to use". Irrespective of whether there is any transfer or not, the consideration paid for use or right to use simpliciter is sufficient for the consideration being called as 'royalty'. **The presence or absence of possession effective/ general control and custody with the assessee, even though may be matters of agreement, are not of any relevance to decide the character of payment. The assessee, as per the agreement, had the right to use the ship, selecting the time and the decided route as per its requirement, for which it paid the foreign enterprise, the consideration and we have no hesitation in holding that the character of payment is nothing but royalty.***

**92. Thus, when the use or right to use the ship for an economic benefit is given to the assessee, the consideration for the use of the industrial, commercial and scientific equipment is 'royalty', assessable under Explanation 2(iva) to [Section 9\(1\)\(vi\)](#) of the Income Tax Act. Thus, for the purposes of [Income Tax Act](#), under the time charter, the payment made being for the use of the ship, the same comes within the meaning of the word "royalty".**

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106. [Section 9\(1\)\(vi\)\(b\)](#) states that income by way of royalty payable by a person who is a resident arising or accruing whether directly or indirectly through or from business connection in India shall be deemed to accrue or arise in India. Sub-clause (b) states that the income by way of royalty is payable by a person who is a resident. The only exception herein is that the royalty is payable in respect of any right, property or information used or services utilised for the purpose of business or profession carried on by such person outside India, or for the purpose of making or earning any income from any source outside India alone is excluded in 9(1)(vi) of the [Income Tax Act](#). In other words, royalty payable by a resident in India to a non-resident in respect of any right, property or information used or services utilised for the purposes of business or profession carried on by him in India would satisfy the definition of 'royalty'. Explanation (2) defines what royalty is. Clause (iva) of Explanation 2 states that consideration paid for use or right to use

any industrial, commercial, scientific equipment but not including the amounts referred to in [Section 44BB](#) would be royalty. Thus, one has to note that the royalty payment is among other things relates to use or right to use any industrial, commercial or scientific equipment for the purposes of business or profession carried on by the resident herein and the said royalty is payable to a non-resident foreign enterprise. It is no doubt true that Clause (iva) refers use or right to use of any industrial, commercial and scientific equipment and not plant and machinery, nevertheless we may point out that the key word in the Clause herein is the use or right to use any industrial, commercial or scientific equipment. Thus, read in the context of [Section 9\(1\)\(vi\)\(b\)](#) and the purport of deeming an income to accrue or arise in India, the presence of the word 'any' preceding an equipment, clearly points out the need for construing 'equipment' widely, so as to embrace every article employed by the employer for the purposes of his business. 'Equipment', in whatever name called either as an apparatus or as plant or machinery, so long as they are employed for the purposes of one's income, the same shall stand covered by Clause (iva). Thus a ship is equipment of the business of a ship owner on a natural and ordinary meaning of the word, we do not find any justification to go by the definition under the [Merchant Shipping Act](#).

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117. Thus the Explanation clarifies that irrespective of control or possession or use or location in India such right, property or

*information with the payer; the payment made on the transfer of all or any rights, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property; the use of any patent, invention, model, design, secret formula or process or trade mark or similar property; the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill; the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in [section 44BB](#) and the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films, the payment would be considered as 'royalty'. As rightly pointed out by the Revenue, as far as the use or right to use is concerned, even going by the OECD commentary, even with the possession of the ship with the owner, the right to use being part of bundle of rights that the owner has and this parted with for a consideration, the Revenue need not take the assistance of Explanation 5 to substantiate its case. With the Explanation, the case of the Revenue becomes more firm on the issue of 'royalty'.*

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118. Referring to BC Mitra in his Law of Carriage by Sea in the decision reported in (1978) 113 ITR 307 ([Union of India V. Gosalia](#)

Shipping Pvt. Ltd.), the Apex Court pointed out that a time charter party is one in which the ownership and also possession of the ship remain with the original owner whose remuneration or hire is generally calculated at a monthly rate on the tonnage of the ship. It further pointed out that sometimes the ship itself, and the control over her working and navigation are transferred for the time being to the persons who use her. In such cases, the contract is really one of letting the ship. The reading of the various time charter in the case on hand shows that hire is payable for the use of the ship for a specific period of time, irrespective of whether the charterer chooses to use it for carrying cargo or lays it up out of use. The ownership and possession of the vessel which remain with the owner are separated from the use of the ship, which is granted to the charterer. The agreement states that the charterer may send the vessel to safe berths, safe ports and safe anchorages, the owners are responsible for the navigation of the vessel and the Master has the obligation to prosecute the voyage with utmost care. The payment is calculated according to the time stated in the agreement rather than the same is performed. The right to remuneration is unaffected by the lay off by the charterer. Thus with the possibility in law and permissible too under law that various rights and interest in a property may be vested in various persons, the Explanation merely recognises what is evident in law and thus clears whatever



***doubt one may have on the aspect of use or right to use, be it with regard to tangible or intangible property, rights and information. Consequently, we do not find any need for giving Explanation 5 a restrictive application to Clauses (i) to (iv) and (v) alone. In the circumstances, apart from the fact that the case of the Revenue could stand even without Explanation 5, the case of the Revenue stands reinforced with the Explanation, which according to us merely clarifies what is already there in the provision.***

119. In the background of the above decision, we hold that ship is an 'equipment'. The consideration paid is for the use of the ship for which the assessee need not have possession and control of the ship. The specific exclusion of the income under [Section 44BB](#) clearly shows that what is otherwise includible under equipment, used for industrial, commercial and scientific equipments alone stands excluded. The Explanation has brought in clarity and made it more explicit to the law already in existence. The payment towards the employment of the vessel is clearly in the nature of 'royalty'. The use or right to use the ship for a consideration means and relates to the economic aspect of the equipment as a business asset, and the exploitation of the earning potential of the Vessel. Hence, we have no hesitation in holding that the consideration paid under the time charter fits in with the definition of 'royalty' under Clause (iva) of Explanation 2 to [Section 9\(1\)\(vi\)](#) of the Income Tax Act.

21. Thus, the Hon'ble High Court has categorically held that under the time charter agreement, the ownership and compensation of the vessel remain with the owner but are separated from the use of the ship which is granted to the charterer and thus any payment towards employment of the vessel is clearly in the nature of royalty. The use or right to use the ship for consideration means relates to the economic aspect of the equipment as a business asset and the exception of the earning potential of the vessel. One important observation of Hon'ble Apex Court in the case [Union of India V. Gosalia Shipping Pvt. Ltd.](#) (supra), as relied upon Hon'ble High Court is that, time charter party is one in which the ownership and also possession of the ship remain with the original owner whose remuneration or hire is generally calculated at a monthly rate on the tonnage of the ship. It further pointed out that sometimes the ship itself, and the control over her working and navigation are transferred for the time being to the persons who use her. Thus, there is transfer of ship and the control over navigation to charterer. Hon'ble High Court after going the various time charter in those cases revealed that hire was payable for the use of the ship for a specific period of time,

irrespective of whether the charterer chooses to use it for carrying cargo or lays it up out of use. This is not the case here. Their Lordships held that to fall in the realm of 'royalty', ownership and possession of the vessel which remain with the owner is separated from the use of the ship, which is granted to the charterer.. Further, it was observed in those cases that the payment was calculated according to the time stated in the agreement rather than the same was performed. The right to remuneration is unaffected by the lay off by the charterer.

22. Now we have to see, whether these parameters is applicable in the present case and whether, it can be held that the consideration paid under time charter fits in the definition of the royalty under clause (a) of section 9(1)(iv). In our opinion and analysis of the agreement before us, the aforesaid principle and ratio laid down by the Hon'ble High Court is not applicable in the present case for the reasons enumerated hereunder:

- i. The assessee is a UAE based company which has hired ship on Time Charter from M/s Power Overseas Investment LLC owner, a different entity. Thereafter it has entered into time charter

agreement with M/s Poompuhar Shipping Corp. Ltd. Though for all purposes the assessee can be said to be owner of the ship till it is in its possession and control for the time period it has taken on time charter. As per the terms of the agreement which we have discussed hereinabove, firstly it can be seen that the payment which assessee was receiving was not purely on account of giving use or right to use the ship to M/s Poompuhar Shipping Corp. Ltd., that is, the charterer and the payment was calculated on the basis of daily freight and load capacity.

- ii. The assessee though the owner of the ship but was never separated from the use of the ship nor granted the ship to the charterer, which is generally is in the case of typical time charter.
- iii. If the agreement provides that the charterer will pay for the use and hire of the said vessel per running day of 24 hours per calendar month, it means that the payment was to be calculated on per day basis which is a kind of voyage freight. This is also further evident from the method and manner of

freight calculation and dead freight calculation. If freight is calculated on pro-rata basis, then under no circumstances, it can be inferred that use or right to use of the ship is given to the charterer.

- iv. It was never the condition that the ship itself, and the control over the working and navigation was transferred for the time period to the charterer who used the vessel and there was never a transfer of ship and the control over navigation to charterer, which was one of the condition laid down in the aforesaid judgement. Even though, pressing of compensation or functional control and custody of vessel with the assessee is not relevant factor for deciding the equipment royalty, but then there has to be leasing and letting of the equipment with complete use or right to use of vessel giving to the hirer or charterer. There has to be some kind of economic benefit while giving use or right to use the ship to the charterer which here in this case is not fully satisfied. Had it been so, then the assessee would have only received fixed amount for the time period of the time charter agreement and nothing would have depending on loading capacity and freight calculation based on loading of

carriage. The freight is not calculated when there is no carriage of goods due to certain circumstances and the charterer was not required to make any payment.

- v. Another important observation made by the Hon'ble High Court while deciding this issue and on the reading of various charter agreements involved in those cases that hire was payable for the use of the ship for specific period of time irrespective of whether the charterer choose to use it for carrying carriage or lays it out of the use and the owner and possession of the vessel which even though remain with the owner who was separated for the use of ship which was granted to the charterer. Here this condition is absent in the present time charter agreement, because the payment is decided purely on the basis of the loading of the good and the determination of the freight is based on the loading capacity and not to the some kind of fixed amount. This material difference itself distinguishes the facts involved in the case before the Hon'ble High Court.

23. Thus, we hold that the aforesaid judgment of Hon'ble High Court is not applicable on the facts of the present case. Accordingly, we hold that;

- Firstly, the payment received by the assessee from M/s Poompuhar Shipping Corp. Ltd. is not in the nature of 'royalty' and hence, the same is not taxable under section 9(1)(vi) of the Income Tax Act.
- Secondly, the agreement and the payment received by the assessee is for carriage of goods and for operating the ships, therefore the income of the assessee has rightly been offered to tax u/s 44B of the Act.

24. In the result, the appeal filed by the assessee stands **allowed**.

*Orders pronounced in the open court on 30<sup>th</sup> December, 2022.*

*Sd/-*  
(Gagan Goyal)  
Accountant Member

*Sd/-*  
(Amit Shukla)  
Judicial Member

मुंबई Mumbai;दिनांक Dated : 30.12.2022

*Sr. PS. Dhananjay*

**आदेशकीप्रतिलिपिअग्रेषित/Copy of the Order forwarded to :**

1. अपीलार्थी/ The Appellant
2. प्रत्यर्थी/ The Respondent
3. आयकरआयुक्त(अपील) / The CIT(A)
4. आयकरआयुक्त/ CIT- concerned
5. विभागीयप्रतिनिधि, आयकरअपीलीयअधिकरण, मुंबई/ DR, ITAT, Mumbai
6. गार्डफाईल / Guard File

आदेशानुसार/ BY ORDER,

उप/सहायकपंजीकार (Dy./Asstt.Registrar)

आयकरअपीलीयअधिकरण, मुंबई/ **ITAT, Mumbai**