

**IN THE INCOME TAX APPELLATE TRIBUNAL
DEHRADUN BENCH, DEHRADUN**

Before Sh. Amit Shukla, Judicial Member

Dr. B. R. R. Kumar, Accountant Member

ITA No. 4561/Del/2013 : Asstt. Year : 2009-10

ITA No. 3824/Del/2014 : Asstt. Year : 2010-11

Smith International Inc., 806-807, Powai Plaza, Central Avenue, Hiranandani Garden, Powai, Mumbai-400076	Vs	ADIT, International Taxation, Dehradun
(APPELLANT)		(RESPONDENT)
PAN No. AAHCS3148R		

ITA No. 4651/Del/2013 : Asstt. Year : 2009-10

ITA No. 3909/Del/2014 : Asstt. Year : 2010-11

ADIT, International Taxation, Dehradun	Vs	Smith International Inc., 806-807, Powai Plaza, Central Avenue, Hiranandani Garden, Powai, Mumbai-400076
(APPELLANT)		(RESPONDENT)
PAN No. AAHCS3148R		

Assessee by : Sh. Salil Kapoor, Adv.

Revenue by : Sh. T. S. Mapwal, Sr. DR

Date of Hearing: 13.09.2021

Date of Pronouncement: 10.11.2021

ORDER

Per Dr. B. R. R. Kumar, Accountant Member:

The present appeals have been filed by the assessee and the Revenue against the orders of the Id. CIT(A)-II, Dehradun dated 21.05.2013 and 23.04.2014.

2. Since, the issues involved in all these appeals are identical, they were heard together and being adjudicated by a common order.

3. The assessee has been showing receipts out of the contracts executed to various drilling offshore contractees along with ONGC. The revenue's of Rs.27.62 crores has been offered to tax u/s 44BB as taxable receipts and applied DPR of 10% by the assessee. Further, during the year the assessee has entered into a new contract with ONGC Ltd. which along with revenues covered u/s 44BB also includes reimbursements, service tax reimbursement and supply component in respect of supply of drilling bits for execution of contract. These revenues were also offered to tax u/s 44BB.

4. Looking at the nature of the activities and scope of work of the contracts, the AO held that the contracts receipts are to be treated as Fee for Technical Services (FTS) in respect of equipment rental hire and claim of Section 44BB was denied and taxed the amount u/s 44DA of the I.T. Act.

5. We have gone through the provisions of Section 44BB and Section 44DA.

6. Section 44BB reads as under:

" 44BB. (1) Notwithstanding anything to the contrary contained in sections 28 to 41 and sections 43 and 43A, in the case of an assessee, being a non-resident, engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral

oils, a sum equal to ten per cent of the aggregate of the amounts specified in sub-section (2) shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession":

Provided that this sub-section shall not apply in a case where the provisions of section 42 or section 44D or section 44DA or section 115A or section 293A apply for the purposes of computing profits or gains or any other income referred to in those sections.

(2) The amounts referred to in sub-section (1) shall be the following, namely:—

(a) the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils in India; and

(b) the amount received or deemed to be received in India by or on behalf of the assessee on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils outside India.

(3) Notwithstanding anything contained in sub-section (1), an assessee may claim lower profits and gains than the profits and gains specified in that sub-section, if he keeps and maintains such books of account and other documents as required under sub-section (2) of section 44AA and gets his accounts audited and furnishes a report of such audit as required under section 44AB, and thereupon the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee under sub-section (3) of section 143 and determine the sum payable by, or refundable to, the assessee.

Explanation.—For the purposes of this section,—

(i) "plant" includes ships, aircraft, vehicles, drilling units, scientific apparatus and equipment, used for the purposes of the said business;

(ii) "mineral oil" includes petroleum and natural gas."

7. Section 44DA reads as under:

"Insertion of new section 44DA.

'44DA. Special provision for computing income by way of royal-ties, etc., in case of non-residents.—

(1) The income by way of royalty or fees for technical services received from Government or an Indian concern in pursuance of an agreement made by a non-resident (not being a company) or a foreign company with Govern-ment or the Indian concern after the 31st day of March, 2003,

where such non-resident (not being a company) or a foreign compa-ny carries on business in India through a permanent establishment situated therein, or performs professional services from a fixed place of profession situated therein, and the right, property or contract in respect of which the royalties or fees for technical services are paid is effec-tively connected with such permanent establishment or fixed place of profession, as the case may be, shall be computed under the head "Profits and gains of business or profession" in accordance with the provisions of this Act:

Provided that no deduction shall be allowed,—

(i) in respect of any expenditure or allowance which is not wholly and exclusively incurred for the business of such perma-nent establishment or fixed place of profession in India; or

(ii) in respect of amounts, if any, paid (otherwise than towards reimbursement of actual expenses) by the

permanent establishment to its head office or to any of its other offices.

Provided further that the provisions of Section 44BB shall not apply in respect of the income referred to in this Section.

This provisions has been inserted by the Finance Act, 2010 w.e.f. 01.04.2011 hence it is not applicable to the A.Y. 2009-10 and 2010-11

(2) Every non-resident (not being a company) or a foreign company shall keep and maintain books of account and other documents in accordance with the provisions contained in section 44AA and get his accounts audited by an accountant as defined in the Explanation below sub-section (2) of section 288 and furnish along with the return of income, the report of such audit in the prescribed form duly signed and verified by such accountant.

Explanation.—For the purposes of this section,—

(a) "fees for technical services" shall have the same meaning as in Explanation 2 to clause (vii) of sub-section (1) of section 9;

(b) "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9;

(c) "permanent establishment" shall have the same meaning as in clause (iia) of section 92F.'."

8. Aggrieved with the order of the Assessing Officer, the assessee is filed an appeal before the Id. CIT(A). The Id. CIT(A) after going through the contracts, agreements and the judicial pronouncements on this issue (page no. 5 to 10) deleted the addition made by the Assessing Officer.

9. Before us, the arguments taken up before the authorities below have been reiterated.

10. We have perused the record before us and the rationale of the Id. CIT(A). The Id. CIT(A) held that the distinction between PSC and non-PSC partners for deciding whether a receipt would be assessed u/s 44BB or as FTS or Royalty does not have the support of law or for that matters any judicial authority. Thus such a distinction has to be rejected as an artificial construct devoid of merit. Secondly, it also cannot be accepted that similar kinds of services can be taxed u/s 44BB of the Act if rendered to a PSC and thereafter, sought to be taxed as FTS or royalty if rendered to a non-PSC partner. The plethora of case laws cited by the Id. ARs and especially the case of CGG Veritas (50 SOT 335) makes it clear that once a PE is known or admitted to exist then the income as in this case, has to be assessed u/s 44BB of the Act more so because the equipment supplied and services rendered are for the purposes of extraction or production of mineral oils. Thirdly, treating of supply of skilled personnel to operate equipment supplied by the assessee cannot be viewed in isolation since the activity of supplying such manpower is part and parcel of the supply of equipment to be used for extraction or production of mineral oils. For this reason also, the income has to be assessed u/s 44BB of the Act only.

11. Further, we also find that preferring appeal by the Revenue against the decision of the Hon'ble High Court in the case of M/s BJ Services Co. (ME) Ltd. cannot be a ground for

confirming the appeal. Till the decision is reversed, the order of the Hon'ble High Court stands legally binding.

12. Since, the order of the Id. CIT(A) is on cogent reasoning, keeping in view the provisions of the Act which have been mentioned above, we decline to interfere with the order of the Id. CIT(A) on this issue.

Profits Attributable on revenues – 5.08% or 2%:

13. The Id. CIT(A) determined the profits attributable to India operations at 5.08% of the revenues received by the assessee from ONGC on account of supply of imported drill bits as opposed to 2% of revenues as attributed by the assessee to India operations. While arriving at 5.08%, the Id. CIT(A) has rejected KOA Tools Limited as a comparable company on account that it incurred losses.

14. It was argued that ignoring the functional comparability of KOA Tools Limited which is against comparability study. The company operates in 3 segments i.e., segment tools, Trading of tools and parking. Since the profile of this company, in respect of its trading business is comparable to SIO in terms of functions performed, risks assumed and assets employed, the trading segment of this company has been considered as comparable to SIO for AY 2009-10. However, for AY 2008-09 and AY 2007-08, the trading segment was not available, hence the company has not been considered comparable for these years. As regards the losses for AY 2009-10, the assessee submitted that losses are a regular business phenomenon. If a company is otherwise comparable in terms of functions

performed, risks assumed and the assets employed, it cannot be rejected as a comparable merely because it has incurred losses in a particular year.

15. It was argued that Koa Tools India Limited meets all comparability criteria examined by the Appellant in view of income-tax regulations and OECD guidelines and hence, should be considered as comparable as per the law.

16. The assessee relied on the ruling of the Special Bench of Chandigarh ITAT in the case of DCIT vs. M/s Quark Systems Private Limited [2010-TIOL-31-ITAT-CHD-SB], wherein it was held as under:

"25..... While we agree that merely because a comparable is making loss, it cannot be excluded from the list of comparables, Imercuis is a case in which not only functional area is different....."

17. The above principle has also been upheld by other benches of ITAT in the case of UCB India (P) Limited vs. ACIT (2009) (121 ITD 131) (Mumbai ITAT), ACIT vs. Wockhardt Limited (6 Taxmann.com 98) (Mumbai ITAT), Brigade Global Services Private Limited vs. ITO (ITA No 988/Hyd./2011) (Hyderabad ITAT).

18. In view of the orders of the Co-ordinate bench of ITAT, we hold that Koa Tools India Limited which clears the FAR test should not be rejected as a comparable for the AY 2009-10.

Reimbursement of expenses amounting to Rs 2,85,38,643:

19. Not Pressed

Service Tax Reimbursement:

20. The AO treated service tax collected by the assessee as a part of its gross receipts. The assessee submitted that the service tax should not be treated as part of gross receipt as there is/there wouldn't be any element of profit in it.

21. The order of the Id. CIT(A) is as under:

"6.5 According to the Appellant the quantum of Service Tax collected by it should not be treated as part of its gross receipts because there is no element of profit in it. This argument is hard to subscribe to since under section 44BB of the Act profit is determined not transaction-wise but with reference to the gross value of transactions done by the assessee during a particular period. The Service Tax has to be treated as part of the turnover following the logic of the decision in the case of Chowringhee Sales Bureau (P) Ltd. (87 ITR 542). Also the scheme of presumptive determination u/s 44BB of the Act was considered by Hon'ble Uttarakhand High Court in the case of CIT vs. Halliburton Offshore Services Inc. (300 ITR 265) it was held that this section is a complete code in itself and provides for taxation of all receipts whether arising in India or outside. Based on that decision the ITAT Delhi Bench in the case of DDIT (Inti Tax) vs. Technip Offshore Contracting BV 29 SOT 33 (Del) also held that Service Tax received by the assessee has to be considered as part of his gross receipt for the purposes of

presumptive determination of his profit. This reasoning was also followed in another case of ACIT vs. Halliburton Offshore Services in para 4 of this order [IT Appeal No. 1659(Delhi) of 2006, order dated 13-05-2009].

(I) The Appellant has also relied upon certain case laws to canvass the point that Service Tax is "pari passu" with Customs Duty. In DIT vs. Schlumberger Asia Services Ltd. (317 ITR 156) - the Hon'ble High Court of Uttarakhand held that the Customs Duty, being statutory in nature, could not form part of the deemed profits unlike other amounts received towards reimbursements. The line of reasoning being that for the import of the machinery or equipment, liability to pay the customs duty was on the Oil and Natural Gas Corporation (ONGC) in this case as per the contract documents. However, this is not the case with Service Tax which the assessee receives during the course of its business. Hence, the ratio of the case relied upon by the Appellant is not applicable in this case.

(II) The Appellant during the course of hearing also submitted a judgment in the case of M/s Sedco Forex International Drilling Inc. vs. Addl. DIT (Intl. Tax.) (ITA no. 5284/Del/2011) wherein it was held that reimbursement of Service Tax is not to be included in the revenue chargeable to tax u/s 44BB of the Act. On a close reading of the judgment, it is observed that the Hon'ble ITAT has relied on the case of Islamic Republic of Iran Shipping Lines Vs. DCTT [I.T. Appeal no. 8845(Mum) of 2010]. This may be discussed.

(a) It is seen that in the case of Islamic Republic the Hon'ble ITAT decided the issue in favour of the assessee by relying on the decision of Hon'ble Bombay High Court in the case of Sudershan Chemical Industries Ltd (245 ITR769) . In that case the issue was whether Sales Tax and Excise Duty were to be included in the total turnover for the purpose of computing deduction under section 80HHC. It was observed by the Hon'ble Court that no Excise Duty and Sales Tax were leviable in respect of exports. The detailed reasoning given by the Hon'ble court may be extracted as under:

"...under section 80HHC, the Legislature intended that the profits from exports should not be taxed. For this purpose, a formula has been introduced whereby if the business is of composite nature then the proportionate profit relatable to the export business is to be found out by multiplying the profits of a business by export turnover and dividing the product by total turnover. This formula finds place in section 80HHC(3) as it stood at the relevant time. Under clause (b) to the Explanation of section 80HHC, export turnover is defined to mean sale proceeds received in India by the assessee in foreign exchange. Under the said definition, export turnover is defined to mean the sale proceeds of any goods which are exported out of India but which will not include freight or insurance. Clause (ba) defines total turnover to exclude freight or insurance. This clause (ba) explains the turnover in a negative manner so as to exclude freight or insurance. Therefore, a combined reading of the above two clauses shows that they include anything which has nexus with the sale proceeds. Correspondingly, they show that they exclude

everything which has no nexus with the sale proceeds. Further, the meaning of export turnover in clause (b) of the Explanation to section 80HHC, therefore, clearly show that export turnover did not include Excise Duty and Sales Tax. Export turnover is the numerator in the above formula whereas- total turnover is the denominator. The above formula has been prescribed to arrive at profits from exports. In the circumstances, the above two items, namely, Sales Tax and Excise Duty cannot form part of total turnover. In fact, if the denominator was to include the above two items and if the numeration excluded the above two items then the formula would become unworkable. In the circumstances, we are of the view that in order of ascertain the export profits, the above two items cannot introduced to inflate total turnover artificially in order to reduce the benefit which an assessee is entitled.....”

(b) Thus the Hon’ble High Court had held that the Sales Tax and Excise Duty were not to be included in the total turnover for the purposes of deduction u/s 80HHC as the same were not leviable in respect of exports. For if the denominator was to include the above two items and if the numerator excluded the above two items then the formula would become unworkable. On the other hand Service Tax is leviable on the assessee in course of its business. Hence, the ratio of this judgment does not apply to the present case.

(c) Thus most respectfully it is averred that the reliance placed by the Hon’ble ITAT in the case of Islamic Republic of Iran Shipping Lines Vs. DCIT on the case of Sudarshan Chemicals

(Bombay High court) and consequently the reliance placed by ITAT in the case of M/s Sedco Forex International Drilling Inc (supra) on the decision of Islamic Republic of Iran Shipping Lines vs. DCIT appears worthy of a differing view in the present appeal since this judgment has distinguished the decision of the co-ordinate bench in the case of DDIT(Intl Tax) vs. Technip Offshore Contracting BV 29 SOT 33 (Del) which is directly on the issue and this case has also been relied upon in another case pertaining to the present jurisdiction, ACIT vs. Halliburton Offshore Services (supra), to hold that Service Tax would form part of the receipts for the purposes of section 44BB of the Act.

6.6 The foregoing discussion leads to the conclusion that for the purposes of presumptive determination of the Appellant's profit, the quantum of amount received by it from its customers against its Service Tax obligation has to be considered as part of the receipt. If the Appellant felt that the profit determined in this manner was excessive and that its profit was actually lower it had the option to produce its books of account and tax audit report so that its income could be determined under the regular provisions of the Income Tax Act. In view of the foregoing discussion, the amount is treated as part of its receipts.

6.7 This Appellate Authority is also conscious of the fact that a different view is being taken than the case of Sedco Forex (supra). This may give rise to a feeling that the principles of Judicial Discipline are being violated. However, it needs to be reiterated that for the present Appeal reliance has been placed on 2 decisions of the ITAT as also the fact that judicial

precedents are not supposed to be mechanically followed. This point may also be discussed.

6.8 The judicial precedents should not be followed mechanically as held in Deena alias Deen Dayal vs. Union of India:

".....Any case, even a locus classicus is an authority for what it decides. It is permissible to extend the ratio of a decision to cases involving identical situations, factual and legal, but care must be taken to see that this is not done mechanically, that is, without a close examination of the rationale of the decision which is cited a precedent. Human mind, trained even in the strict discipline of law, is not averse to taking the easy course of relying on decisions which have become famous and applying their ratio to supposedly identical situations....." (p. 1166)

It is also settled law that a decision is not an authority on point, which was not argued as held in Mittal Engineering Works (P.) Ltd. v. Collector of Central Excise, [1997] 1 SCC 203). Also in A-One Granites v. State of UP reported in AIR 2001 SCW 848 it was observed as under:

"The first question which falls' for consideration of this court is as to whether the question regarding applicability of rule 72 of the Rules in relation to the present lease is concluded by the earlier decision of this court rendered in Prem Nath Sharma v. State of UP [1997] 4 SCC 552; 1997 AIR SCW 2121; AIR 1997 2252; (1997) A U1201. From a bare perusal of the said judgment of this court it would be clear that the question as to whether rule 72 was applicable or not was

never canvassed before this court and the only question which was considered was whether there was violation of the said rule.

This question was considered by the Court of Appeal in Lancaster Motor Co. (London) Ltd. v. Bremith Ltd. [1941] 1 KB 675, and it was laid down that when no consideration was given to the question, the decision cannot be said to be binding and precedent sub silentio and without arguments are of no moment."

In the present situation it is seen that the judicial precedent of the Chowringhee Sales Bureau case was never cited before the Hon'ble members while deciding the Sedco Forex (supra) case and thus two decisions of other benches of coordinate strength have greater persuasive value than the case of Sedco Forex (supra) being relied upon by the Appellant Keeping in view the above discussion it is held that Service Tax would form part of the receipts for the purposes of computation u/s 44BB of the Act."

22. We have gone through the moot issue as to whether service tax be included the total turnover for the purpose of Section 44BB or not?

23. Provisions contained in sub-sections (1) and (2) of Section 44BB of the Act seek to tax only those amounts, which are received or deemed to be received by the Assessee on account of provision of services and facilities in connection with, or supply of plant and machinery on hire, or to be used, in the prospecting for, or extraction or production of, mineral oils

outside India. Service tax collected/ received by SII from its customers is not on account of provision of services and facilities; but is a tax levied on value of taxable services, collected by SII from its customer and deposited with the Government of India.

24. The issue under consideration has been recently adjudicated by the Uttarakhand High Court (Full Bench) in assessee's own case and Others (414 ITR 1) wherein the Uttarakhand High Court on similar facts has held that amount reimbursed to the assessee by ONGC representing service tax paid earlier by assessee to the Government of India and not "on account of provision of services in connection with exploration and production of mineral oil", would not form part of aggregate taxable amount as referred under section 44BB.

25. Key observations by the Division Bench in the said ruling are as under:

- Section 44BB specifically states that "any amount paid or payable (in or outside India) or any amounts received or deemed to be received in India on account of the provision of services and facilities". Accordingly, chargeability under Section 44BB is restricted only to the amounts received/ receivable on account of provision of services and facilities in connection with exploration and production of mineral oil.
- Service tax is a tax levied on "services" and cannot be treated as "service" itself. Hence, service tax does not form a part of consideration received/ receivable for

services rendered in connection with exploration and production of mineral oil.

- Even otherwise, it is not every amount paid on account of provision of services and facilities which must be deemed to be the income of the assessee under section 44BB of the Act. It is only such amounts, which are paid to the assessee on account of services and facilities provided by them, in the prospecting for or extraction or production of mineral oils, which alone must be deemed to be the income of the assessee. On a plain and literal reading of clauses (a) and (b) of section 44BB of the Act, it shall be noted that reimbursement of service tax ought not to be included in the aggregate of the amounts specified in clauses (a) and (b) of section 44BB(2), as the same is not an amount received by the assessee on account of services provided by them in the prospecting, extraction or production of mineral oils.
- Section 43B of the Act provides for certain deductions (such as tax, duty, cess or fee) to be made only on actual payment. Accordingly, no deduction shall be allowed where the liability to pay tax has accrued and the said taxes are not paid. However, assessee can claim a deduction of such payment of taxes while computing its income under section 28. Given that section 44BB overrides section 28 to section 43a, the provisions of section 44BB would prevail notwithstanding anything contained in, inter-alia, section 28 also. Thus, section 43B(a) has no application in

computing the presumptive income under section 44BB of the Act.

- Service tax is an indirect tax levied on certain services provided by certain categories of persons including, a company. As per the service tax law, the service provider can collect service tax from the users of the service and such tax recovered, is on behalf of or as an agent of the Government. Therefore, any service tax collected is payable to the Government and where excess service tax has been collected, such excess is also bound to be payable to the Government. Accordingly, there is no benefit obtained by the assessee by collecting the service tax from the customer.
- Since service tax, an indirect tax, can be passed on by a service provider to the service recipient, reimbursement thereof, by the service recipient to the service provider, cannot be treated as the presumptive income of the service provider under section 44BB of the Act.
- Further, the CBDT itself in two of its circulars viz., Circular No 4/2008 dated 28 April 2008 and Circular No 1/2014 dated 13 January 2014 in context of deduction of tax at source under section 194-I and section 194J respectively has supported that service tax does not form a part of the income and thus, taxes on service tax collected should not be withheld. In Circular No.4/2008 dated 28 April 2008, it was clarified that "Service tax paid by the tenant doesn't partake the nature of "income" of the landlord. The

landlord only acts as a collecting agency for Government for collection of service tax. Therefore, it has been decided that tax deduction at source under section 194-I of the Act would be required to be made on the amount of rent paid/payable without including the service tax. In Circular No. 1/2014 dated 13 January 2014, it has been clarified that service tax is not to be included in the fees for professional services or technical services and no TDS is required to be made on the service tax component under section 194J of the Act. This can only be on the footing that it is not a part of the "fee for professional services" and contemplated by section 194J(1)(a). If service tax cannot be treated as a part of the fee for professional services, then it cannot be treated as a payment on account of services as contemplated by Section 44BB(2).

26. Given the above reasons, the Division Bench held that reimbursement of service tax collected by the assessee should not be included while computing taxable gross receipts under section 44BB of the Act.

27. Similar view has also been taken by the Hon'ble Delhi High Court in the case of Mitchell Drilling International Pvt. Ltd. (380 ITR 130).

28. Hence, keeping in view, the pronouncements of the Hon'ble Court, we hold that the service tax cannot be made a part of the Gross turnover.

29. In the result, both the appeals of the assessee are allowed and both the appeals of the Revenue are dismissed.

Order Pronounced in the Open Court on 10/11/2021.

Sd/-

(Amit Shukla)
Judicial Member

Dated: 10/11/2021

Subodh Kumar, Sr. PS

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

Sd/-

(Dr. B. R. R. Kumar)
Accountant Member

ASSISTANT REGISTRAR