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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% **Judgment reserved on: October 24, 2024**
Judgment pronounced on: February 21, 2025

\+ ITA 785/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Mr. Ruchir Bhatia, SSC.

versus

NOKIA NETWORK OY .....Respondent
Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 786/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Mr. Ruchir Bhatia, SSC.

versus

NOKIA NETWORK OY .....Respondent
Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 882/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Mr. Ruchir Bhatia, SSC.

versus

NOKIA CORPORATION (FORMERELY KNOWN AS NOKIA NETWORK OY) .....Respondent
Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates

\+ ITA 883/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Mr. Ruchir Bhatia, SSC.

versus

NOKIA CORPORATION (FORMERELY KNOWN AS NOKIA NETWORK OY) .....Respondent
Through: Appearance not given.

\+ ITA 884/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Mr. Ruchir Bhatia, SSC.

versus

NOKIA CORPORATION (FORMERELY KNOWN AS NOKIA NETWORK OY) .....Respondent
Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates

\+ ITA 885/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Appearance not given.

versus

NOKIA CORPORATION (FORMERELY KNOWN AS NOKIA NETWORK OY) .....Respondent
Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates

\+ ITA 887/2019

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant
Through: Appearance not given.

versus

NOKIA CORPORATION (FORMERELY KNOWN AS

NOKIA NETWORK OY) .....Respondent

Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 166/2020

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant

Through: Mr. Aseem Chawla, SSC with Ms. Pratishtha Chaudhary, Advocate.

versus

NOKIA CORPORATION (FORMERLY KNOWN AS NOKIA NETWORK OY) .....Respondent

Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 170/2020

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant

Through: Mr. Aseem Chawla, SSC with Ms. Pratishtha Chaudhary, Advocate.

versus

NOKIA CORPORATION (FORMERLY KNOWN AS NOKIA NETWORK OY) .....Respondent

Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 171/2020

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant

Through: Mr. Aseem Chawla, SSC with Ms. Pratishtha Chaudhary, Advocate.

versus

NOKIA CORPORATION (FORMERLY KNOWN AS NOKIA NETWORK OY) .....Respondent

Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

\+ ITA 60/2023

THE COMMISSIONER OF INCOME TAX - INTERNATIONAL TAXATION -2 .....Appellant

Through: Mr. Aseem Chawla, SSC with Ms. Pratishtha Chaudhary, Advocate.

versus

NOKIA CORPORATION (FORMERLY KNOWN AS NOKIA NETWORK OY) .....Respondent

Through: Mr. Deepak Chopra, Mr. Ankit Goyal and Mr. Priyam Batnagar, Advocates.

CORAM:
HON'BLE MR. JUSTICE YASHWANT VARMA
HON'BLE MR. JUSTICE RAVINDER DUDEJA

J U D G M E N T

YASHWANT VARMA, J.

1. This set of appeals give rise to the following four principal questions: -

(A) Whether the assessee in the concerned **Assessment Years** [1] had a **Fixed Place Permanent Establishment**[2] in India?

(B) Whether **Nokia India Private Limited**[3], a wholly owned subsidiary of the assessee constituted a **Dependent Agent**

[1] AY
[2] PE
[3] NIPL

Permanent Establishment[4] of the assessee?

(C) Whether interest from delayed consideration of supply of equipment and licensing of software was taxable in the hands of the assessee as interest earned from vendor financing?

(D) Whether the revenue from supply of software could be classified as royalty or fee for technical services under the **Income Tax Act, 1961**[5] read along with the **India-Finland Double Taxation Treaty**[6]?

2. Mr. Bhatia and Mr. Mann, learned counsels who appeared for the appellants, had placed for our consideration the following chart which delineates the questions which arise in each of these appeals and also encapsulates details of the AYs to which they pertain. That chart is extracted hereinbelow: -

Commissioner of Income Tax, International Taxation-2 vs. Nokia Network OY
ITA Nos. 785, 786, 882, 883, 884, 885 and 887 of 2019, 170, 171 and 166 of 2020 & 60 of 2023

S.NO.	ITA NO.	AY	QUESTIONS ARISING FOR CONSIDERATION			
			Whether in the facts and circumstances of the case, the Assessee has a Fixed Place Permanent Establishment in India?	Whether in the facts and circumstances of the case, NIPL, which is a wholly owned subsidiary of the Assessee, constitutes DAPE of the Assessee in India?	Whether in the facts and circumstances of the case and in law, ITAT erred in holding that interest from delayed consideration of supply of equipment and licensing of software is not taxable in the hands of the Assessee as interest from vendor financing?	Whether on the facts and circumstances of the case, the ld. ITAT was correct in holding that Revenue from supply of software are not in the nature of royalty /fee for technical services under the provision of the Act and India- Finland tax treaty?
1	785/2019	1997-98	✓	✓	✓	×
2	786/2019	1998-99	✓	✓	✓	×
3	882/2019	1999-2000	✓	✓	✓	×
4	883/2019	2003-04	✓	✓	✓	×
5	884/2019	2000-01	✓	✓	✓	×
6	885/2019	2001-02	✓	✓	✓	×
7	887/2019	2002-03	✓	✓	✓	×
8	170/2020	2004-05	✓	✓	✓	✓
9	60/2023	2005-06	✓	✓	✓	✓
10	171/2020	2006-07	✓	✓	✓	✓
11	166/2020	2007-08	✓	✓	✓	✓

[4] DAPE
[5] Act
[6] DTAA

3. The litigation spawning these appeals has had a chequered history and saw not just a previous round of litigation landing at the doorstep of this Court but also witnessed two references to Special Benches of the **Income Tax Appellate Tribunal**[7] itself. It would thus be appropriate to take note of some of the salient facts leading up to the institution of these appeals. For the sake of brevity, we propose to take note of the facts as disclosed in ITA No. 786 of 2019 and which with the consent of learned counsels appearing for respective sides was designated as the lead appeal.

4. ITA No. 786 of 2019 was concerned with a common order passed by the Tribunal for AYs 1997-98 and 1998-99. From the disclosures made in that order, we gather that **Nokia Networks OY**[8]**,** the respondent assessee, was a company incorporated under the laws of Finland and engaged in the manufacture of advanced telecommunication systems and equipment. The GSM equipment manufactured was used in relation to fixed and mobile phone networks. Nokia OY was also engaged in the trading of telecommunication hardware and software.

5. In 1994, Nokia OY is stated to have established a Liaison Office and which was followed by the incorporation of a fully owned subsidiary, NIPL on 23 May 1995. According to the Respondent, in the period in question and while the Liaison Office was still operational, GSM equipment manufactured in Finland was sold to various Indian telecommunication operators from outside India on a principal-to-principal basis under independent buyer-seller arrangements.

6. Post incorporation of NIPL in May of 1995, the installation

[7] Tribunal
[8] Nokia OY

activities were undertaken by the said entity in terms of independent contracts which it entered into with Indian telecom operators. The details of the contracts which were entered into by the Respondent assessee stand duly captured in paragraph 2 of the judgment of the Tribunal. The assessee, Nokia OY, is stated to have consistently maintained the position that the said installation activities were undertaken by NIPL in terms of separate agreements which it had entered into with Indian telecom operators. The two exceptions to such contracts were those entered into with Modi Telstra (India) Limited and Skycell Communications Ltd. and which were signed prior to the incorporation of NIPL.

7. Undisputedly, Nokia OY did not file any Return of Income for the concerned period taking the position that offshore supplies were not exigible to tax. A return was ultimately filed consequent to notices which came to be issued under Section 142(1) of the Act on 03 November 1999. The **Assessing Officer**[9], while drawing up an order dated 02 March 2000 referable to Section 143(3), came to hold against Nokia OY on the question of taxability, the existence of a PE and attribution of income. The adverse findings so returned by the AO have been succinctly captured by the Tribunal in paragraph 3 of its order and which reads as under: -

> "3. The Assessing Officer completed the assessment u/s. 143(3) vide order dated 2.3.2000 in the following manner (as summarised by the Hon'ble High Court): -
>
> > *(a)* Nokia was carrying on business In India through a Permanent Establishment (PE). Both the Indian Liaison Office and Indian subsidiary were held to constitute a PE of Nokia in India. 'Installation PE' was also constituted on the basis that Nokia had supported Indian subsidiary in discharging its obligation under the installation contracts.

[9] AO

> *(b)* 70% of total equipment revenue (comprising of hardware and software) was attributed to sale of hardware and 40% of the same was estimated as income of Nokia from supply of hardware. Further 30% of the profits so determined were attributed to the PE of Nokia in India. The remaining 30% of the equipment revenues were attributed towards supply of software and the same was taxed as 'royalty' (on a gross basis) both u/s 9(1)(vi), of the Income-tax Act & under section 13 of the India-Finland DTAA, holding that software was not sold but licensed to the Indian telecom operators.
>
> *(c)* In addition, income from vendor financing and delayed payment was imputed at Rs.50,000,000/- for each assessment year on account of specific clause in this regard in the offshore supply contracts. The said income was classified as commercial income and added to the income from sale of equipment and licensing of software and taxed at the rate of 55%."

8. Basis the aforesaid conclusions, the AO proceeded to make additions under the head of profit on sale of hardware, profits on licensing of software as well as interest income. Nokia OY assailed the view so taken asserting that equipment supply contracts with at least two of the Indian telecom operators were signed even before NIPL had been incorporated and consequently it was only the installation activities undertaken pursuant to the original equipment supply contract having subsequently been assigned to NIPL that could have formed subject matter of taxation. It had further averred that all the equipment supplied by Nokia OY fell in the category of offshore supplies and profits earned from those transactions were thus not taxable in India. According to Nokia OY, it is this which led to the Revenue seeking to discover the existence of a PE.

9. Reverting then to the assessment made by the AO, Nokia OY aggrieved by the same petitioned the **Commissioner of Income Tax (Appeals)**[10] and which came to hold that the Liaison Office constituted

[10] CIT(A)

a Fixed Place PE of the respondent. Insofar as the connect between Nokia OY and NIPL was concerned, the CIT(A) took into consideration the fact that the latter was a wholly owned subsidiary and it thus being liable to be presumed that the latter was not acting independently. It consequently came to hold that the view of the AO that NIPL constituted a DAPE of the respondent was liable to be affirmed.

10. In the course of consideration of the appeal which came to be taken against the aforesaid decision, the matter came to be referred to a Special Bench of the Tribunal which rendered its judgment on 22 June 2005. The critical findings which the Special Bench came to return are duly noted by the Tribunal in Para 6.1 and which is extracted hereinbelow: -

> "6.1 These questions have been decided by the Special Bench vide judgment dated 22.06.2005; however, in so far as the appeal relating to the assessee is considered, the following findings have been given by the Special Bench which finding too has been summarized in the judgment of the Hon'ble High Court in the following manner: -
>
> *(1) Liaison Office neither constituted a business connection under the Act nor a PE of the Nokia under Article* 5 *of the India-Finland DTAA, as* it *merely carried on advertising activities in India.*
>
> *(2) Sale of hardware took place outside India and no income from sale of hardware accrued* to *Nokia in India.*
>
> *(3) Nokia was not responsible for installation of telecom equipment and Nokia's arrangement with the Indian Telecom Operators did not constitute a works contract. NIPL* is *a separate corporation entity and* is *also assessed separately for its installation income.*
>
> *(4) However, Nokia was held* to *have a PE in India in the form of NIPL on the basis that Nokia virtually projected itself in India through NIPL and guarantees given by Nokia that it will not 'dilute its shareholding in NIPL below 51% without written permission of Indian Telecom Operators was used as the main basis* to *hold that Nokia was in a position* to *control and monitor NIPL's activities.*

(5) While upholding NIPL as a PE of Nokia, the Special Bench observed that it *did not matter that there was no direct evidence for the control of NIPL by Nokia. For purposes of PE, what* is *relevant* is *only the perception that NIPL was a projection of Nokia, whether or not in fact and in truth its activities were being controlled/ monitored by Nokia. Following discussion ensued on this aspect: -*

> *'... We only meant* to *convey that because of the close connection between the assessee and NIPL,* it *was possible* to *look upon NIPL as a "virtual projection" of the assessee in India. We have in fact clarified in the same paragraph that what matters* is *that there was scope for previewing the assessee's soul in the body of NIPL and that* it *did not matter that there was no direct evidence for the control of NIPL by the assessee. For purposes of PE, what* is *relevant* is *only the perception that NIPL was a projection of the assessee, whether or not in fact and truth its activities were being controlled / monitored by the assessee. Our observations are therefore confined* to *the question of PE. Otherwise, both the assessee and NIPL remain separate corporate entities and NIPL has also been assessed separately for its installation income. Thus the observations in para 274(b) have no relevant* to what *has been discussed in this paragraph.'*

(6) Payment for supply of software was not in the nature of royalty because the same was for a copyrighted article and 'not for a copyright. Further, software was held to be integral part of GSM equipment. Payment for supply of software was held not taxable both under the provisions of the Act and under DTAA.

(7) Interest income from vendor financing was held to have been correctly added.

(8) Following 3 *activities were held to have been carried out by NIPL, the PE of Nokia in India:*

(a) Network Planning;

(b) Negotiations in connection with the sale of equipment; &

(c) Signing of supply and installation contracts.

(9) 20% of the net profit determined on the basis of the global net profit of Nokia (10% towards signing of the contract and 10% towards other two activities) was attributed to the PE in India. This margin was directed to be applied on the Indian sales of Nokia (clarified by the Special Bench of the ITAT to mean revenues arising from supply of hardware and software)."

11. It thus becomes apparent that the Special Bench of the Tribunal essentially held that the Liaison Office would neither qualify the test of a business connection nor was it liable to be viewed as a PE under Article 5 of the India Finland DTAA. It further pertinently held that the sale of equipment took place outside India and thus no income derived therefrom could be said to have accrued to Nokia OY in India. However, it held that NIPL would constitute a Fixed Place PE and answer to the test of virtual projection as enunciated by courts. It observed that notwithstanding the absence of direct evidence establishing control of NIPL by Nokia OY, perception of the former as a projection of the parent entity would suffice.

12. The judgment of the Special Bench of the Tribunal was thereafter assailed before this Court by both the assessee as well as the Revenue in a batch of appeals in which the lead matter was **ITA No. 512 of 2007**. Those appeals came to be disposed of by a detailed judgment rendered by the Court on 07 September 2012. Para 7 of the order of the Tribunal identifies the substantial questions of law on which that appeal set came to be admitted and the manner in which they were ultimately answered by this Court. The table which appears in Para 7 is reproduced below: -

"7.

Revenue Appeals before the Hon'ble High Court (lead case ITA 512/2007)	
Substantial Question of Law admitted by Hon'ble High Court	*Conclusions*
Q1. Whether on a true and correct interpretation, of section 9(1)(i) of the Income Tax Act, the Respondent can be said to have a business connection in India in the form of a Liaison Office?	***Decided in favour of assessee*** *(Para 23 of HC Order)*

Q2. Without prejudice, whether the respondent has a 'permanent establishment' in India because of its Liaison Office within the meaning of the relevant provision of DTAA between India and Finland?	
Q3. Whether any part of the consideration for supply of software stated by the Respondent to be integral to the equipment is taxable as (royalty' either under section 9(l)(vi)or the relevant provision	***Decided in favour of assessee*** *(Para 30 of HC Order)*
Q4. Whether on facts and in law without prejudice, the Tribunal is correct in law in attributing only 20% of the Global Net Operating Profits to the PE in the form of NIPL (Nokia India Pvt. Ltd.) a subsidiary	***Issue remitted back to AO*** *(Para 31 of HC Order)*
Q5. Whether on facts and in law interest under section 234B is leviable?	***Decided in favour of assessee*** *(Para 30 of HC Order)*

Asseessee Appeals before Hon'ble High Court (ITA 1137 & 1138 / 2007)	
Q1. Whether on a true and correct interpretation of the relevant DTAAA the Tribunal's reasoning is right in law in holding that NIPL, (the subsidiary of the Appellant) is a permanent establishment?	***All these Issues have been remitted back to ITAT (Para 38 of High Court order)***
Q2. Whether the Tribunal was right in law in holding that a perception of virtual projection of the foreign enterprise in India results in a permanent establishment?	
Q3. Whether prejudice, if the answers to Q.1 & Q.2 are in affirmative, is there any attribution of profits on account of signing, network planning and negotiation of offshore supply contracts in India and if yes, the extent and basis thereof?	

Q4. Whether in law the notional interest on delayed consideration for supply of equipment and licensing of software is taxable in the hands of assessee as interest from vendor financing?	

13. It would also be apposite to reproduce the following salient passages which formed part of the judgment handed down by this Court: -

> "34. We may recapitulate that there are four contracts which have been referred to in the orders of the authorities below. The same are:
>
> i. Supply contracts between the assessee and various customers.
>
> ii. Installation Contract between he Indian subsidiary and the customers directly. Only two contracts with Modi Telstra and Skycell executed in February and March, 1995 were separate from the supply contracts and installation portion was assigned to the Indian subsidiary with the consent of all concerned.
>
> iii. Marketing support Agreements dated 19.4.1996 and 6.11.1997 between the assessee and its Indian subsidiary, and
>
> iv. Technical support agreement between Indian subsidiary and the customers.
>
> Whereas the marketing support ensures to the benefit of the assessee the technical support ensures to the benefit of the Indian customer, the technical support is in respect of the projects installed and has nothing to do with the supply contract. The consideration accruing or arising under the contracts already assessed in the hands of the Indian subsidiary and there is no adverse action in respect thereof The technical support agreement referred to supra has not even been referred to by the authorities below in support of any of the allegations. Only general or loose reference has been made by the Tribunal.
>
> The dispute hence only pertains to the consideration under the Supply Agreement entered between the assessee and the various customers.
>
> 35. It was the submission of Mr. Syali that although the Tribunal held that with the Indian subsidiary there was a business connection, they did not go into the issue of how much income can be attributed to the activities earned out in India because that analysis was only made in respect of the subsidiary constituting a PE. Even though a

business connection exists, if there is no income accruing or arising directly or indirectly through or from that business connection in India, nothing can be taxed in the hands of the assessee. It was the argument of Mr. Syali that Section 90(2) of the Act clearly stipulates that the treaty regime can be opted if it is more beneficial to the assessee and, therefore, it was necessary to ascertain as to whether any income was attributable to the PE. It was argued that no such income could be attributed to PE in India and these aspects were not correctly appreciated by the Tribunal Learned Senior Counsel submitted that the conclusion arrived at by the Tribunal was erroneous as it was based on various factual errors has crept in the orders of the lower authorities. According to him, the factual errors of the orders of the AO were specifically pointed out in the submissions to the CIT (A) and specific grounds were also taken before him which are as under :

(i) The Indian subsidiary was executing contracts on behalf of the appellant through its employees.

(ii) All the contracts with the operators were signed in India.

(iii) The employees of Indian Office (LO) were compensated by some other entity

(iv) From 1996 onwards all the expenses of the Indian office were shifted to Indian subsidiary

(v) The employees of the Indian Office were responsible for execution of the contracts with operators.

(vi) No compensation was paid to IC for marketing and support services prior to 1997.

(vii) PSC was set up in India to supervise the supply contact with TATA.

(viii) Certificate of acceptance was signed by Indian subsidiary on behalf of the appellant.

(ix) The appellant has accepted that the license of customized software is not sale, but royalty, and

(x) The appellant has equally earned interest from Vendor Financing an on account of delayed payments by the operators in the relevant previous year.

36. Mr. Parasaran, learned ASG appearing for the Revenue could not controvert the aforesaid pleas of Mr. Syali. We find that the aforesaid errors on facts have crept in. It is primarily for the reason that the Tribunal had taken the facts in the case of Ericsson case and on the presumption that those facts were common the case of Nokia as well and the legal questions in the appeals of Nokia were decided therefore the actual inaccuracy has crept in the fact findings of the

Tribunal. We find justification in the argument of Mr. Syali that the clear cut impact of such assumptions is evident from the fact that findings (i), (iv), (v) and (vi)are all suppositions in the absence of appreciating that there was a marketing support agreement in operation from 1.1.1996 to the 31-12.1996. Even as per the AO after the later agreement of 1997 there is no allegation made as regards shifting of expenses, no compensation paid to Indian subsidiary, etc. In other words, once there was an agreement the issue only revolved on the nature of the agreement. Once it is accepted that the position in 1997 and 1996 is pari-materia, there will not remain any such allegation.

37. We would like to record that the CIT (A)proceeded on the basis that Indian subsidiary incurred huge loss and the parent assessee was aware of its profitability. The CIT (A) also observed that since NPL was 100% subsidiary and the assessee had wide experience in this area of business, it is logical that a transaction between the assessee and the Indian subsidiary did not occur at arm's length. Mr. Syali argued that there was no basis for drawing such inference and at the time of arguments, the learned ASG conceded that there was no evidence to support that losses were absorbed by the Indian company. Again, pertinently, the Tribunal also observed that NIPL could be considered PE of assessee in India being subsidiary as it is the virtual projection of the company in India. Further, the accounts of the Indian subsidiary show that the company incurred huge losses as it was not compensated properly for the installation work carried on by it. In the opinion of the ITAT since it was a wholly owned subsidiary, the assessee would have direct and complete control over the activities of this subsidiary. The learned ASG also conceded that it was not correct.

38. As we find that the order of the Tribunal is based on many factual errors which are even accepted by the Revenue before us, it would be appropriate to refer the matter back to the Tribunal for fresh consideration on the issues as to whether the subsidiary of the assessee would provide business connection or is Permanent Establishment and even if it is so, is there any attributes of profits on account of signing, under working, planning and negotiation of off-shore supply contracts in India. If yes, to what extent and basis thereof Likewise, the question of notional interest on delayed consideration of supply of equipment and liaisioning of software taxable in the hands of assessee as interest from vendor financing would be considered afresh. The appeals of the assessee are thus disposed of with the aforesaid direction remitting the case rack to the Tribunal for fresh consideration on these issues."

14. As would be apparent from a reading of the 2012 decision, the aspect of offshore supplies came to be decided in favour of the

respondents. Our Court also held that the Liaison Office would not constitute a PE within the meaning of the relevant provisions of the DTAA. However, all issues relating to the interconnect between NIPL and Nokia OY and whether the former would constitute a PE were remitted back for the consideration of the Tribunal. Our Court also remanded back the issue pertaining to attribution of global net operating profits to NIPL. This led to the Special Bench of the Tribunal coming to be reconstituted. It is the judgment so rendered by the Special Bench pursuant to the remand by the Court which is impugned in these appeals.

15. As we read the judgment so rendered, the first issue which the Tribunal framed for consideration was whether NIPL would constitute a PE of Nokia OY. It has in this connection taken note of the conclusions as originally arrived at by the AO and who had held that while NIPL was liable to be treated as DAPE, the Liaison Office constituted a Fixed Place PE. Firstly taking up the issue of whether the Liaison Office could be treated as a PE, the Tribunal observed that since the said question had been answered in favour of Nokia OY by this Court, the same no longer survived for consideration.

16. Since elaborate arguments appear to have been addressed with respect to the engagement of Mr. Hannu Karavitra in the course of transactions which were entered into by Nokia OY, we deem it apposite to note that the said individual, the Tribunal has found, was employed as a Country Manager in the Liaison Office between 01 February 1994 and 31 December 1994. It has further been found on facts that Mr. Hannu Karavitra was subsequently employed in NIPL between 01 January 1996 and 31 July 1999 and whereafter he is stated to have

assumed the office of its Managing Director and functioned as such between the period 01 January 1996 to 31 July 1999. The Modi Telstra and Sky Cell contracts were signed on 23 March 1995 and 17 February 1995 and thus undisputedly at a time when he was not even employed with NIPL. The Tribunal further pertinently noted that the AO appears to have proceeded under the mistaken assumption of Mr. Hannu Karavitra being the Country Manager of NIPL between 01 February 1994 and 31 December 1999 ignoring the indisputable position of NIPL itself having come into existence only in May 1995.

17. The Tribunal further held that there was no material on the basis of which it could have been said that Mr. Hannu Karavitra had signed any supply contracts on behalf of Nokia OY after assuming the office of Managing Director of NIPL. It has in this connection encapsulated the principal contracts entered into between Nokia OY and NIPL in paragraph 13 of its judgment. It is pertinent to note that the aforenoted facts which emerge from the record were not questioned by the appellants before us.

18. Proceeding ahead, the Tribunal at the outset posed for its consideration the question whether NIPL was liable to be viewed as a PE of the respondent assessee by virtue of being a wholly owned subsidiary. It took note of the conclusions of the AO rendered in this respect and who had observed that the wholly owned subsidiary was liable to be viewed as a DAPE. For the purposes of appreciating the issues which arise in this regard, we deem this to be an appropriate juncture to extract Article 5 of the DTAA. It would also be relevant to bear in mind the subtle and yet significant amendments which came to be introduced in Article 5 and which becomes evident upon a review of

the following comparative table: -

"**ARTICLE 5**

PERMANENT ESTABLISHMENT

THE ORIGINAL ARTICLE	**POST AMENDMENT**
1. For the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carries on. 2. The term 'permanent establishment' includes especially - (a) a place of management; (b) a branch ; (c) an office ; (d) a factory ; (e) a workshop ; (f) a mine, a quarry or any other place of extraction of natural resources ; (g) a warehouse ; (h) premises used as a sales outlet or for receiving or soliciting orders. 3. The term 'permanent establishment', also includes - (a) a building site, a construction, assembly or installation project or supervisory activity in connection therewith, but only where such site, project or activities continue for a period of more than six months ; (b) a building site, a construction, assembly or installation project or supervisory activity being incidental to the sale of machinery or equipment, where such site project or activity continues for a period not exceeding six months and the charges payable for the project or supervisory activity	1.For the purposes of this Agreement, the term "permanent establishment "means a fixed place of business through which the business of an enterprise is wholly or partly carried on. 2.The term "permanent establishment" includes especially: — (a) a place of management; (b) a branch; (c) an office; (d) a factory; (e) a workshop; (f) a sales outlet; (g) a warehouse in relation to a person providing storage facilities for others; (h) a farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on; and (i) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources. 3. The term 'permanent establishment' likewise encompasses: — (a)A building site or construction, installation or assembly projector supervisory activities in connection therewith only if such site, project or activities last more than six months. (b) The furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only where

exceed 10 per cent of the sale price of the machinery or equipment. 4. Notwithstanding the preceding provisions of this Article, the term 'permanent establishment' shall be deemed not to include - (a) the use of facilities solely for the purpose of storage or display of goods or merchandise belongings to the enterprise; (b) the main tern of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display ; (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; (e) the maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information or for scientific research, <u>being activities, solely of a preparatory or auxiliary character in the business of the enterprise</u>. 5. Notwithstanding the provisions of paragraphs (1) and (2), where a person - other than an agent of an independent status to whom paragraph (7) applies - is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned Contracting State in respect of any activities which that person undertakes for the enterprise, if such a	<u>activities of that nature continue</u> (for the same or connected project) within the country for a period or periods aggregating more than 183 days within any 12 month period. 4. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include: — (a) the use of facilities solely for the purpose of storage or display of goods or merchandise belonging to the enterprise; (b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display; (c)the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; (e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character; (f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs (a) to (e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character. 5. Notwithstanding the provisions of paragraphs 1 and 2, where a person

person: (a) has and habitually exercises in that State an authority to conclude contracts in the name of the enterprise, unless the activities of such person are limited to those mentioned in paragraph (4) which, if exercised through a fixed place of business, would not make the fixed place of business a permanent establishment under the provisions of that paragraph ; or (b) has no such authority, but habitually maintains in the first-mention State a stock of goods or merchandise on behalf of enterprise . 6. Notwithstanding the preceding provisions of this Article, an insurance enterprise of a Contracting State shall, except in regard to reinsurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person other than agent of an independent status to whom paragraph (7) applies. 7. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, he shall not be considered an agent of an independent status within the meaning of this paragraph. 8. The fact that a company which is a	- other than an agent of an independent status to whom paragraph 7 applies-is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned Contracting State in respect of any activities which that person undertakes for the enterprise, if such a person:— (a) has and habitually exercises in that State an authority to conclude contracts in the name of the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph; or (b) has no such authority, but habitually maintains in the first-mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise; (c) habitually secures orders in the first-mentioned State, wholly or almost wholly for the enterprise itself. 6.Notwithstanding the preceding provisions of this Article, an insurance enterprise of a Contracting State shall, except in regard to re-insurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated there in through a person other than an agent of an independent status to whom paragraph 7 applies.

resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company or a permanent establishment of the other."	7. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it caries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph. 8.The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

19. The Tribunal before proceeding to rule on this aspect firstly identified the four principal contracts which merited examination and in the context of which the issue of PE and attribution of profits was liable to be answered. These were, in our opinion, correctly identified as being (a) supply contracts between the assessee and various customers (b) installation contracts entered into between NIPL and customers directly (c) marketing support agreements between Nokia OY and NIPL and (d) the technical support agreement between NIPL and customers.

20. Proceeding ahead, the Tribunal firstly found that the supply of

telecom equipment by Nokia OY was on a principal-to-principal basis founded on independent buyer and seller contracts. This becomes evident from a reading of para 39 of the judgment of the Tribunal and which reads as under: -

> "39. Under this backdrop we would like to briefly recapitulate the relevant facts and the contentions raised by the party. The assessee company Nokia Networks Oy has been incorporated in Finland. At that point of time, it was a leading manufacturer of advance telecommunications systems and equipments (GSM Equipment) which were used in fixed and mobile phone networks. These GSM equipments manufactured by the assessee were sold to the Indian telecom operators from outside India on principal to principal basis under independent buyer-seller arrangements. These facts have been noted by the Hon'ble High Court also in paragraph 2 of its judgment and are also borne out from the order of the authorities below. Apart from supply of the equipments there were also installation contracts and for this purpose of installation activity and other connected activities, assessee had established a Liaison Office on 30th March, 1994. Two such agreements were signed between the assessee (through LO)and Indian Cellular Operators viz., Modi Telstra India Ltd. on 30.03.1995 and Skycell Communication Ltd. on 17.02.1995. These contracts were signed by the assessee during the period when there was a LO of the assessee in India. Later on a wholly own subsidiary in the name of Nokia India Pvt. Ltd. was incorporated on 23.05.1995. After the incorporation of NIPL, all the contracts for installation were either assigned or separately entered by the NIPL with the customers. Marketing Support Agreement was also entered in the year 1996 and 1997 between the assessee and NIPL for providing marketing services to assessee for whom NIPL was compensated with cost plus markup. Technical support agreement had also been entered by the NIPL with the Indian customers in respect of projects installed again on principle to principal basis. However, the off-shore supply contract of GSM equipments between the assessee and Indian customers continued to be done by the assessee. In the light of the facts and background discussed in detail in the foregoing paragraphs, we shall endeavor to examine whether the assessee company has any kind of business connection or permanent establishment in India either in terms of Section 9(1) of Income Tax Act; and/ or under Article 5 of then India- Finland DTAA."

21. This set the stage for it to consider the aspect of PE. The Tribunal notes that the aforesaid question was liable to be answered in the

context of signing of contracts, network planning and negotiation of offshore contracts in India. It firstly bore in consideration the assertion of the Revenue that it was the Liaison Office which was engaged in activities of network planning, negotiation and signing of contracts. However, it held that once and in the first round of litigation itself, the Liaison Office was found as not constituting a PE at all, those aspects would clearly pale into insignificance.

22. It thereafter reiterated its findings on facts pertaining to the engagement of Mr. Karavitra and held: -

> "45. First of all, in so far as the allegation that the Country Manager of the LO continued to be the Managing Director of the Indian Company, the same has with reference to one employee, namely, Mr. Hannu Karavitra who was the Country Manager in LO and in that capacity has signed two contracts in the month of February and March, 1995. These contracts were signed when NIPL was not even in existence. After the incorporation of NIPL on 23.05.1995, not an iota of evidence has been brought on record that Mr. Hannu Karavitra ,.had signed any contract on behalf of the assessee. He was a Managing Director of NIPL from 01.01.1996 to 31.07.1999 and after he was employed with NIPL, he has not signed any supply contracts with the Indian customers. All the installation contracts which have been signed by the NIPL have been executed by the NIPL independently with the Indian customers on principal to principal basis and any Income received or accrued thereof, was subject to tax In India. During the course of the hearing, it was brought to our notice that on one assignment letter dated 24.05.1995 was signed by Mr. Hannu Karavitra whereby on shore services were assigned to NIPL and while working in India ,he was receiving salary from assessee only. First of all, Mr. Hannu Karavitra was employed with the LO earlier, prior to the incorporation of NIPL and he was not employed with the Indian company. In any case assignment was from assessee to NIPL and no authority was being exercised on behalf of the assessee company vis-a.-vis the customers. Whether Mr. Hannu Karavitra was representative of the assessee and was working for NIPL or was receiving salary from assessee, same would have some relevance in the context of 'Service PE', but certainly not while examining the ' fixed place PE'. Even if the arguments sake it is accepted that he was a seconded employee to NIPL, then also if he had worked under the control of NIPL despite lien was maintained with assessee company, then also it does not lead to an inference that assessee company was having any kind

of a PE, leave alone under paragraph 1 of Article 5. Similarly the allegation has been made by the Assessing Officer as well as strongly contended by the learned CIT-DR that employees of the NIPL were mostly belonging to the assessee company as some of the expatriates / technical persons were working on installation contract of NIPL for which activities, salaries were paid and managed by assessee. This concept perhaps may assume some significance while deciding the concept 'Service PE' for which reliance was also placed by the learned CIT-DR on Morgan Stanley and Centrica off-shore Pvt. Ltd, however as per the then existing provision of Article 5 between India and Finland treaty, there was no such concept of 'Service PE' per se except for certain activities mentioned in clause (a) and (b) of Paragraph 3 of Article 5, which ostensibly are not applicable at all. Since none of the on-shore activities are carried out by the assessee in India albeit was done by its Indian subsidiary, provisions of paragraph 3 of Article 5 will also not attract. Once there is no concept of 'Service PE' (though there is no allegation by the Assessing Officer or CIT (A)that there is any kind of service PE), then such plea of the learned CIT-DR has no legs to stand. His core argument was on the point that installation activities done through employees of the assessee constitutes a 'Service PE' and assessee was unable to furnish the details of employees working in NIPL alongwith the details of their duration and therefore, in absence of such details adverse view should be drawn for treating these employees constituting PE in India. The entire thrust of his argument simply whittles down for the reason that firstly, there is absolutely no~.concept of 'Service PE' in the then existing provision of Article 5; and *secondly,* other than off-shore supply of equipment, no other activities has been carried out by the assessee after the incorporation of the Indian subsidiary NIPL and this fact has been accepted by the Hon'ble High Court also. Thus, any activities relating to NIPL under the independent contract cannot be reckoned to constitute a PE in the context of Article 5(1); and even if for argument sake it is accepted that the activities of NIPL were managed by assessee, then also, it does not constitute PE qua activities of supply contract or any activity from where it can be held that any income has been received or accrued to the assessee in India or through or from any asset in India. NIPLis an independent entity and all its income from India operation is liable for tax in India"

23. The Tribunal pertinently observed that Article 5 as it then existed in the DTAA had not incorporated or adopted the principles of a Service PE. This becomes evident when one views the pre and post amendment Article 5 and which we have sought to highlight by way of the comparative table extracted above. As is evident on a perusal of the

comparative table, the Article as it stood during the period in question contained no stipulation in respect of the posting of personnel for the purposes of rendering consultancy services.

24. However, and more importantly, it found that Nokia OY had only entered into offshore supply of equipment and with no other activity having been carried out by that assessee in India post the incorporation of NIPL. It was in the aforesaid backdrop that it held that the contracts executed and activities undertaken by NIPL under independent and separate contracts would be wholly irrelevant for the purposes of answering the question of whether it constituted a PE. It is these fundamental findings and conclusions which stand encapsulated in Para 45 which we have extracted above.

25. It also brushed aside the specious argument relating to NIPL providing access to telephones, faxes and conveyances and those being liable to be treated as germane or even sufficient for the deployment of the '*force of attraction rule'*. It thus held that that administrative support services would not meet or qualify the test of 'at the disposal of' and which is essential for the purposes of examining whether a Fixed Place PE had come into existence. The Tribunal in this context also rested its decision on the judgments of the Supreme Court in **Formula One World Championship Ltd. v. CIT**[11] and **ADIT v. E-Fund IT Solution**[12]**.** This becomes evident from a reading of paragraph 46 which reads thus: -

> "46. Another set of allegations which can said to have some significance is that; whenever the employees of the assessee were visiting India in the context of networking, assigning or negotiation of off-shore supply contract, the employees of the NIPL were either

[11] [(2017)15 SCC 602]
[12] [(2018) 13 SCC 294]

assisting by providing certain administrative support services made available in the form of telephone, fax, conveyance; or the NIPL was providing technical and marketing support services to assessee and hence it is assisting in sale of equipments of the assessee in India and therefore, NIPL *per se* by '*force of attraction rule'* will constitute a PE, because even if one sale of the assessee is through Indian company then by virtue of this rule as enshrined in Article 7 of India-Finland DTAA, PE will get constituted and there would be a deemed PE in the form of Indian company whose income has to be attributed accordingly. This second part of allegation does not hold ground at all, because; firstly as stated stat in the earlier part of the order, assessee and NIPL have entered into separate marketing and technical support agreements in respect of the projects installed and has no correlation with the supply contract. This has been specifically held so by the Hon'ble High Court also in paragraph 34 reproduced in the earlier part of the order; secondly, not only that, for rendering these services NIPL was compensated with cost plus mark up of 5% which though has been adversely commented by the Assessing Officer and Id. CIT (A) but there has been no determination of ALP under transfer pricing mechanism. This inter alia means that the remuneration paid by the assessee to NIPL for these services has to be reckoned at arm's length; and lastly, not one off-shore sale has happened in India through NIPL and this fact has again been accepted by the Hon'ble High Court in its order that no part of off-shore supply was concluded in India with any business connection in India as it was independent contract between Assessee and Telecom operators in India. In so far as allegation of administrative support services provided to employees of assessee in India for supply contract by NIPL and hence it leads to fixed place PE, strong reliance has been placed by Ld. CIT-DR on the statement of the then Managing Director, Mr. Simon Bresford. From the relevant statement he had pointed out that how the marketing support services chaver been provided by the Indian company to the astotsee see and also the administrative support services were provided by NIPL to assessee. Regarding marketing support services by NIPL to assessee we have already discussed above that it was done under separate contract and NIPL was remunerated at arm's length. In so far as administrative facilities being provided by the NIPL to the expatriates coming for signing of contract on behalf of the Nokia Finland, he had stated that, administrative support like office support, cars, telephones, etc. was being provided by NIPL; and earlier office of liaison office of NIPL are at the same premise in the year 1995. Relying on such statement, Id. CIT-DR has vehemently contended that this material facts itself goes to prove that there is a fixed place PE which was at the disposal of the assessee. In light of such contention, we have to see whether any place of business was provided by NIPL to the assessee which can be said to be at a disposal of the assessee for carrying out its business wholly or partly in India. The sequitur of the judgment of

Hon'ble Apex Court as incorporated above is that, in order to ascertain as to whether an establishment being a fixed place for PE or not is that physically located premises have to be 'at the disposal of the enterprises'. Nowhere the disposal test has been diluted by the Hon'ble Apex Court rather it has been reiterated at various places not only in the Formula One World Championship judgment but also in the subsequent judgment of E-Fund. As culled out from the certain observations of the Assessing Officer as well as the statement of the MD that the employees of the assessee whenever came to India for the purpose of supply contract for negotiation on network planning, then, they were provided administrative services like telephone, fax and conveyance. Now, whether such kind of facilities can at all be treated to be a fixed place of business of the assessee company. Telephone or fax or a car cannot be reckoned as physically located premise. The word used in Article 5(1) is fixed place of business through which business of enterprise is wholly or partly carried out'. A fixed place alludes to some kind of a particular location, physically located premise or some place in physical form. Nowhere is it borne out that any kind of physically located premise or a particular location was made available to the assessee which was at the disposal of the assessee for carrying out wholly or partly its business through that place. Not only there should be an existence of a fixed place of business but also through that fixed place business of the enterprise should be wholly or partly carried out. No such material has been brought on record that any kind of such fixed place was made available. Providing telephone or fax or conveyance services can ever be equated with fixed place. Even the co-location of earlier LO office and the Indian subsidiary company was only in the initial year of 1995 and later on LO office has moved out which is also evident from the statement of the Managing Director. Thus, providing such kind of administrative support services to the assessee's employees visiting India will not form fixed place PE, and therefore, the great emphasis by the leaned DR on this point is not much of credence as it lacks any further material support or evidence that any physical place was made available which can be said to be at the disposal of the assessee for carrying out its off-shore supply contract in India. In fact the entire allegation of fixed place was qua the LO and never in the context of NIPL by the Assessing Officer. The entire case of the Assessing Officer was that NIPL is a DAPE of the assessee, because all employees of the assessee were either working for the NIPL or NIPL was undertaking certain marketing and technical support services for the assessee. The concept of DAPE would be discussed in succeeding paragraphs. However, so far as the issue of fixed place PE is concerned the same does not get established at all by making to reference of providing of telephone, fax and car facility to the employees of assessee visiting India. As regards allegation that expatriates employees of assessee in India were assisting the NIPL and hence used the office of NIPL, is of no relevance qua assessee's business, because, the technical expatriates

> were in India to assist/help NIPL with performance of installation activities of NIPL and not to carry out the business of the assessee which was manufacturing and sale of network equipments. This activity per se cannot be reckoned that the Indian office was being used for the purpose of assessee's business or assessee was undertaking business in India through fixed place of business. The test laid down by the Hon'ble Supreme Court does not get satisfied in this case as nothing has been brought on record by the AO or Id. CIT-DR that any physical space was made available which can be said to be at the disposal of assessee for assessee's own business of supply and sale of equipments"

26. It then proceeded further to observe that the peripheral activities and administrative assistance which was extended by NIPL would fall within the meaning of preparatory and auxiliary services and which forms part of Article 5(4) of the DTAA. It thus came to conclude that NIPL would not constitute a Fixed Place PE.

27. It then turned its attention to the question of whether a DAPE could be said to have come into existence. As would be evident from a reading of Article 5(5), the prerequisite for a DAPE to be acknowledged to exist is that of a person, other than an agent of independent status, who acts on behalf of an entity in a Contracting State and has or habitually exercises in that territory an authority to conclude contracts. It in this regard observed: -

> "50. Admittedly, paragraph 6 of Article 5 is not applicable. Paragraph 7 of Article 5 deals with 'agent of independent status.' Independence of an agent has to be both legal as well as economic independence. Legal independence has to be seen from the context, whether the agent's commercial activities for his principal are subject to detailed instructions or comprehensive control by the principal or not; or to what extent the agent exercises freedom in the conduct of his business on behalf of principal; or the agent's scope of authority is affected by limitations on the scale of business which may be conducted by the agent. Economic independence has to be seen from the context as to what extent the agent bears the "entrepreneurial risk" or "business risk" and agent's activities are not integrated with those of the principal; and whether the agent acts exclusively for the principal. The tests for determining the

independent status has to be seen from what kind of activities is being carried out by the agent for his principal. Here in this case, first of all we have to borne in mind that installation activity carried out by NIPL is not generating any revenue or income for the assessee in India albeit any income from such activity is already subject to tax in India. The off-shore supply contract is carried out by assessee on FOB basis from Finland and as discussed in foregoing paragraphs NIPL is carrying out various onshore activities, like installation activity, marketing and technical support services, which fact has been clearly highlighted by the Hon'ble High Court in para 34, that these activities have nothing to do with supply contract. The consideration accruing or arising under the contracts undertaken by NIPL is already assessed in the hands of NIPL in India and there is no adverse inference in this respect. The dispute as highlighted by the Hon'ble High Court only pertains to the consideration under the Supply Agreement entered between the assessee and the various customers. Qua the supply contract nothing is being performed by the NIPL in India as agent of the assessee. None of the onshore activities of NIPL can be said to be devoted wholly and almost wholly on behalf of the assessee, because, the contracts undertaken and signed by NIPL in India independent and on principal to principal basis with the Indian customers and assessee has not signed any kind of installation contract with the Indian customers for which it could be said that the installation activity of NIPL was wholly and almost wholly on behalf of the assessee. The two contracts which were signed earlier prior to the incorporation of NIPL were separate and assigned to it and income from such installation has been shown in the hands of NIPL in India. There is no income whatsoever from installation activities has been earned by the assessee in India or can be attributed either directly or indirectly through NIPL. Insofar as other activities like marketing and technical support services are concerned, same has been transacted at arm's length as discussed in detail in foregoing paras, hence no profit can be attributed from these activities as held by the Hon'ble High Court. Even if NIPL is held to be; subject to significant control with respect to the manner in which work is to be carried out; is subject to detail instructions from the assessee as to the conduct of work; is exercising less freedom in the conduct of business on behalf of assessee; seeking approval from the assessee for the manner in which the 'business is to be conducted; etc., then all such control if at all could be only in relation to the contracts carried out by the NIPL in India to ensure technical quality of the contact work done. When there is absolutely no income generated to the assessee from installation contract work done in India by the NIPL, then all such comprehensive control does not have much relevance. Article 5(7) will apply only when some of the activities of the foreign enterprise are done by an agent wholly or almost wholly on behalf of that enterprise. Here the crucial test is that activities of the assessee must be carried out through the agent wholly and almost

> wholly for the assessee. When installation activity is not carried out by the assessee in India and is done by NIPL on principal to principal basis with the customers then there is no question of examining the installation activity for purpose of PE. The activity carried out by the assessee through an agent in India would be key factor for examining PE. Thus, provision of paragraph 7 of Article 5 will also not apply."

28. As is evident from the above, what appears to have weighed upon the Tribunal in holding against the appellants in this respect was that the revenue being earned by NIPL from installation activities undertaken did not constitute revenue or income of Nokia OY. Insofar as the offshore supply contracts was concerned, the Tribunal found that the same were on FOB basis from Finland as opposed to the onshore activities which NIPL undertook. The income so generated from onshore activities undertaken by NIPL, the Tribunal records, had already been subjected to tax and assessed in its hands. It thus came to conclude that since no income had accrued to the respondent assessee from the installation and contract work undertaken in India, it would be wholly incorrect to assume that a DAPE had come into existence. It has also and in unequivocal terms found that NIPL in any case had not been shown to have been accorded the authority to conclude contracts in the name of Nokia OY. It is these principal findings which stand reflected in the judgment handed down by the Tribunal.

29. Having broadly noticed the conclusions which were rendered by the Tribunal with respect to Fixed Place PE and DAPE, it would be pertinent to briefly advert to its conclusions on the aspect of vendor financing and which the Tribunal has answered in the following terms:-

> "60. Now coming to the last issue of taxability of interest from Vendor Financing ,we find that the Assessing Officer in his order has made the addition on the ground that assessee provided credit facilities to its customers for which it should have charged the

interest on the same. For coming to this conclusion, he has referred to one clause given in paragraph 6.9 of the contract between the assessee and Modi Telstra to conclude that purchaser were liable to pay interest @180/0 for each day elapsed from the due date of actual payment. Thus, the only reason for making such an addition was existence of a particular clause in the agreement signed between the assessee and some of the Indian Cellular Operators. The ld. CIT (A) too has confirmed the said addition on the ground that, since the assessee is following a mercantile system of accounting and as per the contract assessee was entitled to receive such interest, and therefore, same should have been accounted for and in support he has relied upon the judgment of Hon'ble Supreme Court in the case of State Bank of Travancore (supra). Ld. counsel for the assessee had submitted that the said judgment has already been distinguished in the subsequent judgment of Hon'ble Supreme Court in the case of DCa Bank vs. CIT (supra) and secondly, only the real income can be brought to tax and not something on hypothetical basis, because there has to be corresponding liability to the other party to whom the income becomes due and here such a clause was never enforced by the parties. Already the arguments of both the parties have been incorporated in earlier part of the order; therefore, same is not being discussed again.

61. After considering the relevant finding and rival contentions, we find that, it has been brought on record that in any of the contract the assessee had charged any interest on delayed payment or providing any credit facilities to its customers or any customer has paid any such amount for each day elapsed from the due date to the actual payment. Once none of the parties have either acknowledged the debt or any corresponding liability of the other party to pay, then it cannot be held that any income should be taxed on national basis which has neither accrued nor received by the assessee. Whence the benefit of credit period given to the customers has neither accrued to the assessee nor acknowledged by the other person, then it cannot be said that interest on notional basis should be calculated for the purpose of taxation. Otherwise, it is a well settled proposition that income cannot be generated, actual or accrued if no income has actually been accrued or received to the assessee. There has to be some income which has resulted to the assessee and even though in books, entries have been made about hypothetical income which does not materialized at all cannot be brought to tax. The income tax is levy on real income, i.e., the profits arrived on commercial principles. Assessee must have received or acquired a right to receive the income before it can be taxed. In other words, there must be a debt owed to it by somebody if it is to be taxed on accrual basis unless a debt has been created in favour of the assessee by somebody it cannot be said that income has accrued to it or it has a right to receive the income. This proposition has been well settled by Hon'ble Supreme Court in the case of **E. D. Sassoon Co. Ltd. Vs.**

CIT, (1954) 26 ITR 27 (SC), CIT vs. Ashokbhai Chaamanbhai, (1965) 56 ITR 42, CIT vs. Shoorji Vallabhdas and Co, (1962) 46 ITR 144 (SC) and Godhara Electricity Company Ltd. Vs. CIT, 225 ITR 746. Further, the judgment of Hon'ble Supreme Court in the case of State Bank of Travancore, reported in (1986) 158 ITR 102 (SC) which has been relied upon by the ld. CIT (A), has not been treated to be correct enunciation of law by the Hon'ble Supreme Court in the case of Godhara Electricity Company Ltd. v/s. CIT (supra) and UCO Bank v/s. CIT (supra). Here in the present case, the assessee itself has not treated the amount of interest to be due from any of the telecomm operators either recognised as a debt or as a legal claim. Even the conduct of the parties show that such a clause even though may have been agreed upon has never been enforced or acted upon. In such a situation, In our opinion, the amount of interest cannot construe a debt due to the assessee. Further, assessee has not debited the account of any customer with interest which can be treated as income of the assessee. Nowhere has it been held by the Assessing Officer/ CIT (A)that such an interest is legally claimable right against the Indian customers in respect of interest on delayed credit period on Vendor Financing. Thus, we hold that when assessee has neither treated the amount to be legally claimed nor has acknowledged any debt due too on its customer as delayed payment then it cannot be held that any interest accrued to the assessee, and therefore, such a notional charging of interest for each day elapsed from the due date to the actual payment cannot be held to be taxable to the assessee. This proposition has also been now well upheld by Hon'ble Supreme Court in the case of **CIT vs. Excel Industries Ltd., (2013) 358 ITR 259 (SC).** Hence, no income can be said to accrue to the assessee on account of delayed payments as neither there was any corresponding liability on such an interest. Accordingly, this issue is also decided in favour of the assessee."

30. The Tribunal while ruling on this aspect has noted that no real income had in fact been generated. According to it, the entire addition was based on a notional accretion, and thus clearly unsustainable. It pertinently observed that the Department had failed to place any evidence on the record which may have established that Nokia OY had in any instance arising out of any of the contracts charged interest on delayed payment or extended credit facilities to its customers. It also held that there was not an iota of evidence which may have even tended to indicate that any of the customers of Nokia OY had in fact paid such

sums. It was in the aforesaid backdrop that it observed that since the Act is clearly not concerned with taxation of a notional income, the entire premise on which the said addition was based was rendered untenable. This becomes apparent from a reading of Paras 60 and 61 of the order of the Tribunal and which have been extracted in the preceding parts of this judgment. We are of the firm opinion that the view expressed by the Tribunal is clearly unexceptionable and merits no interference.

31. As was noticed in the introductory parts of this decision, the essential facts were really not disputed by the appellants. The conclusions of the Tribunal and which represent its understanding of issues which stood settled in the first round of litigation and questions which no longer survived as well as those which were liable to be tried afresh was also not contested. We do so observe in light of the Tribunal having, in our considered opinion, correctly appreciated the findings which had come to be returned by the Special Bench in the first instance as well as the judgment of this Court rendered in 2012. It has thus correctly found that the aspect pertaining to the Liaison Office constituting a PE was one which stood duly laid to rest. It also held, and in our view correctly, that the solitary issue insofar as PE was concerned would be whether NIPL could be viewed as either constituting a Fixed Place PE or a DAPE.

32. For the purposes of evaluating the challenge which stands raised in these batch of appeals, it becomes pertinent to firstly notice the provisions made in Article 5 of the DTAA. As that Article presently stands and forms part of the Convention, a PE is defined to mean a fixed place of business through which the business of an enterprise may

be wholly or partly carried out. Paragraph 2 of Article 5 thereafter spells out categories of establishments which would constitute a PE.

33. It would also be relevant to compare Para 3 of Article 5 as it stood in the relevant AYs as contrasted with how it exists today. A Service PE in terms of Article 5(3) as it then existed would be deemed to have come into existence either where a building site, construction assembly or installation project were established and continued for a period of more than six months or where such a site incidental to the sale of machinery or equipment came to be set up and such a site continued for a period not exceeding six months. None of these stood attracted to the facts which obtained in the years in question since it was not even the case of the appellants that a building or construction site had in fact come into existence. It was only later that Article 5 came to include the furnishing of services by an enterprise through employees and which is now recognised as a distinctive feature of a Service PE. We, however, are concerned with the pre-amendment Article 5 and this issue, thus, merits no further elaboration.

34. As was noticed in the preceding parts of this judgment, it was the activities of the Liaison Office which were borne in consideration by the respondents in support of their assertion that a Fixed Place PE had come into existence. Their case with respect to NIPL had principally proceeded on the basis that it constituted a DAPE. However, and as the Tribunal has correctly noted, NIPL had never been established on facts to be a dependent agent. Even before us, the appellants had failed to draw our attention to any evidence which may have even remotely qualified the test of an authority to conclude contracts in the name of Nokia OY having been conferred. It is these

facts which have ultimately weighed upon the Tribunal to hold against the appellants insofar as the issue of DAPE is concerned. It had also identified the independent source of income of NIPL and the same having been duly offered and subjected to tax.

35. The Tribunal, as noted above had also found that Nokia OY was not undertaking any installation activity in India and those activities were being performed by NIPL on a principal-to-principal basis for the benefit of its own customers under independent contracts. We thus and at the outset proceed to evaluate whether NIPL could be said to have constituted a Fixed Place PE.

36. The question of when a fixed place PE can be said to have come into being, is no longer res integra and is one which has come to be settled by a series of decisions including the *locus classicus* on the subject being the decision of the Andhra Pradesh High Court in **Commissioner of Income Tax vs. Visakhapatnam Port Trust**[13] and where for the first time the expression 'virtual projection' appears.

37. We had an occasion to review the entire body of precedent which has come to evolve over the years on the subject of Fixed Place PE in our decision in **Progress Rail Locomotive Inc. v. Deputy Commissioner of Income-tax (International Taxation) and Others**[14] and relevant parts whereof are extracted hereinbelow: -

> "**67.** Mr. Datar had with his characteristic erudition and clarity not only sketched out the well-recognised principles governing the question of a permanent establishment, he had also placed for our consideration various academic texts and treatises to enable us to obtain a broader perspective on the concept of a permanent establishment. We, however, deem it apposite to additionally notice some of the principles which stand enunciated in Klaus Vogel's

[13] [1983 SCC OnLine AP 287]
[14] [2024 SCC OnLine Del 4065]

seminal work on Double Taxation Conventions [Klaus Vogel on Double Taxation Conventions, Edited by Ekkehart Reimer and Alexander Rust, Wolters Kluwer, 5th edition, 2022.]. While explaining the "control" test which would be determinative for the purposes of acknowledging the existence of a place of business under the sufficient command of an entity situate in one of the contracting States, the learned author observes as under:

> "110. For all types of business activities, control can be based on legal titles or factual circumstances. Legal control might be derived from ownership or any other right, including equitable rights under common law if the respective right conveys factual mastery of a place of business to the taxpayer enterprise. Such rights are perfect where the taxpayer enterprise is the legal proprietor of the place of business. Likewise, the position of the taxpayer as a tenant, a lessee (leaseholder, even in cases of short-term lease) or even a co-tenant will usually qualify as a controlling interest under article 5(1) of Organization for Economic Co-operation and Development and UN MC (No. 44 OECD MC Comm. on article 5).
>
> 111. But even in the absence of a legal right to use that place, the control test can be met if the taxpayer enterprise has sufficient command of the place of business as a matter of fact (No. 11 et seq. OECD MC Comm. on article 5). Thus, for instance, a permanent establishment could exist where an enterprise illegally occupied a certain location where it carried on its business (as mentioned explicitly in No. 11 et seq. OECD MC Comm. on article 5). Likewise, a company may create a permanent establishment on the premises of an associated company if this associated company grants accommodation to, or tolerates the lasting presence of employees of the first-mentioned company (see infra m. No. 430 et seq.)."

68. Klaus Vogel, while seeking to amplify the importance of the expression "through" when used in the context of the business of the holding company being carried on by the subsidiary, makes the following pertinent observations:

> "134. Article 5(1) OECD MC (since 1977; see supra m. No. 45) requires that the business of an enterprise (for these terms, see supra m. No. 27 et seq.) is carried on through the fixed place of business. The preposition 'through' specifies the functional relation between the place of business and the activities of the taxpayer. This relation can be described best by the notion of a functional integration of the place of business in the enterprise of the taxpayer. Such functional integration contains several aspects which need to be carefully distinguished from one another. Their common denominator,

however, is the type and degree of proximity of the place of business to, or even identification with, the taxpayer's paramount economic activity.

135. The first function of the term ‘through’ is to make it clear that the taxpayer has to control the permanent establishment (see supra m. No. 106 et seq. for details).

136. Secondly, functional integration presupposes that the taxpayer ‘wholly or partly carrie(s) on’ his business (article 5(1) OECD MC; the OECD MC Comm. uses the verb ‘carried out’ synonymously (No. 35 OECD MC Comm. on article 5)). However, like ‘business' and ‘enterprise’ (cf. supra m. No. 27 et seq.), these words do not function as a substantive filter either. While early draft Model Conventions contained the condition that the fixed POR should have a productive character, this requirement was never adopted by the OECD Model (see No. 35 OECD MC Comm. on article 5). None of the current MCs provide a specific productivity test. It follows that place of business may constitute a permanent establishment even if they perform activities which mainly or exclusively expenditures to show for.

137. Likewise, the ‘carrying-on’ requirement does not imply an activity in the sense of an active and visible work. It includes even stand-by services and omissions. This gains significant relevance where the omission is profitable (e.g., in the case of a place of business earning money in the source State simply by fulfilling, for whichever period of time, a non-competition agreement relating to the territory of that State).

138. However, a diffuse passivity which equals a (temporal or lasting) suspension of the activities which the place of business has been designed for may indicate that the place of business is not ‘permanent’. For details, see supra m. No. 87 et seq.

139. Thirdly, the phrase ‘through which’ indicates that the taxpayer makes use of the place of business in that he employs it an instrument (equalling or resembling an operating asset) for his entrepreneurial activities. This third aspect of the functional integration is by far the most disputed one.

140. Historically, the instrumental character of the place of business for the carrying-on of the enterprise could not be taken for granted. Between 1963 and 1977, the OEEC/Organization for Economic Co-operation and Development did not employ this term. Rather, it was sufficient that the taxpayer carried on his business ‘in’ the place of business (see supra m. No. 45). Based on the old Model, some older DTCs use the words ‘in which’ still today. While some authors have denied any divergence in substance,

the 1977 amendment is a strong reason to assume a semantic shift indeed.

141. In a different context (viz., in article 5(4.1) of the Organization for Economic Co-operation and Development and UN MC, (as amended in 2017), the Organization for Economic Co-operation and Development and UN have returned, in one specific regard, to this old line by stating that an enterprise should carry on business 'at the same place'. However, the simultaneous use of this language on the one hand and the terms 'used or maintained by an enterprise' on the other, in one and the same sentence in the initial phrase of article 5(4.1) of Organization for Economic Co-operation and Development and UN MC, proves how careful and attentive the 2017 Models have been drafted. This dualism is another good reason to stipulate a different meaning of 'through', as opposed to 'in' or 'at'. For all of these reasons, we do see a substantial difference between both terms.

142. It follows that on the one hand, the activities mentioned in article 5(1) of the Organization for Economic Co-operation and Development and UN MC need no longer be carried on 'in' or 'at' the place of business. In this respect, the 1977 change of article 5(1) of OECD MC has enlarged the scope of the permanent establishment definition. Especially if one thinks of an activity as a human behaviour, one can now (unlike before 1977) easily subsume unmanned facilities under the permanent establishment definition (see supra m. No. 45 and see, e.g., No. 127 OECD MC Comm. on article 5).

143. On the other hand, the requirement of an instrumental character of the place of business has become irrefutable. Even stronger than the English amendment ('through which' instead of 'in which'), the corresponding modification of the French text ('par l'intermediaire de laquelle' instead of 'ou') has stressed the functional integration of the place of business in the business.

144. The OECD MC Comm. has weakened the meaning of 'through' since 2003. The Commentary holds the view that the requirement of a functional integration is met as soon as the taxpayer exercises the business in a fixed place of business which is at his disposal (No. 20 OECD MC Comm. on article 5 (added on January 28, 2003)). This is the reason for the characterisation of the famous painter example (i.e., the fictitious case of a painter who, for two years, spends three days a week in the large office building of its main client) as a service permanent establishment. In substance, the view of the OECD MC Comm. limits the meaning of 'through' to the first two instead of all three semantic aspects required by article 5(1) OECD MC (supra m. No. 135 et seq. and 139 et seq.)."

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86. The principles pertaining to fixed place permanent establishment were more lucidly explained by the Supreme Court in *Formula One World Championship Ltd.* [*Formula One World Championship Ltd.* v. *CIT (International Taxation)*, (2017) 394 ITR 80 (SC); (2017) 15 SCC 602; (2017) 295 CTR 12 (SC); (2017) 248 Taxman 192 (SC).] in the following terms (page 100 of 394 ITR):

> "Emphasising that as a creature of international tax law, the concept of permanent establishment has a particularly strong claim to a uniform international meaning, Philip Baker discerns two types of permanent establishments contemplated under article 5 of Organization for Economic Co-operation and Development Model. First, an establishment which is part of the same enterprise under common ownership and control—an office, branch, etc., to which he gives his own description as an 'associated permanent establishment'. The second type is an agent, though legally separate from the enterprise, nevertheless who is dependent on the enterprise to the point of forming a permanent establishment. Such permanent establishment is given the nomenclature of 'unassociated permanent establishment' by Baker. He, however, pointed out that there is a possibility of a third type of permanent establishment, i.e., a construction or installation site may be regarded as permanent establishment under certain circumstances. In the first type of permanent establishment, i.e., associated permanent establishments, primary requirement is that there must be a fixed place of business through which the business of an enterprise is wholly or partly carried on. It entails two requirements which need to be fulfilled : (a) there must be a business of an enterprise of a contracting State (FOWC in the instant case); and (b) permanent establishment must be a fixed place of business, i.e., a place which is at the disposal of the enterprise. It is universally accepted that for ascertaining whether there is a fixed place or not, permanent establishment must have three characteristics : stability, productivity and dependence. Further, fixed place of business connotes existence of a physical location which is at the disposal of the enterprise through which the business is carried on…
>
> The principal test, in order to ascertain as to whether an establishment has a fixed place of business or not, is that such physically located premises have to be 'at the disposal' of the enterprise. For this purpose, it is not necessary that the premises are owned or even rented by the enterprise. It will be sufficient if the premises are put at the disposal of the enterprise. However, merely giving access to such a place 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.…

Taking cue from the word ‘through’ in the article, Vogel has also emphasised that the place of business qualifies only if the place is ‘at the disposal’ of the enterprise. According to him, the enterprise will not be able to use the place of business as an instrument for carrying on its business unless it controls the place of business to a considerable extent. He hastens to add that there are no absolute standards for the modalities and intensity of control. Rather, the standards depend on the type of business activity at issue. According to him, ‘disposal’ is the power (or a certain fraction thereof) to use the place of business directly.…

Organization for Economic Co-operation and Development commentary on Model Tax Convention mentions that a general definition of the term ‘permanent establishment’ brings out its essential characteristics, i.e., a distinct 'situs', a ‘fixed place of business'. This definition, therefore, contains the following conditions : (i) the existence of a ‘place of business', i.e., a facility such as premises or, in certain instances, machinery or equipment; (ii) this place of business must be ‘fixed’, i.e., it must be established at a distinct place with a certain degree of permanence; (iii) the carrying on of the business of the enterprise through this fixed place of business. This means usually that persons who, in one way or another, are dependent on the enterprise (personnel) conduct the business of the enterprise in the State in which the fixed place is situated.

The term ‘place of business' is explained as covering any premises, facilities or installations used for carrying on the business of the enterprise whether or not they are used exclusively for that purpose. It is clarified that a place of business may also exist where no premises are available or required for carrying on the business of the enterprise and it simply has a certain amount of space at its disposal. Further, it is immaterial whether the premises, facilities or installations are owned or rented by or are otherwise at the disposal of the enterprise. A certain amount of space at the disposal of the enterprise which is used for business activities is sufficient to constitute a place of business. No formal legal right to use that place is required. Thus, where an enterprise illegally occupies a certain location where it carries on its business, that would also constitute a permanent establishment. Some of the examples where premises are treated at the disposal of the enterprise and, therefore, constitute permanent establishment are : a place of business may thus be constituted by a pitch in a

market place, or by a certain permanently used area in a customs depot (e.g. for the storage of dutiable goods). Again the place of business may be situated in the business facilities of another enterprise. This may be the case for instance where the foreign enterprise has at its constant disposal certain premises or a part thereof owned by the other enterprise. At the same time, it is also clarified that the mere presence of an enterprise at a particular location does not necessarily mean that the location is at the disposal of that enterprise.…

As per article 5 of the Double Taxation Avoidance Agreement, the permanent establishment has to be a fixed place of business 'through' which business of an enterprise is wholly or partly carried on. Some examples of fixed place are given in article 5(2), by way of an inclusion. Article 5(3), on the other hand, excludes certain places which would not be treated as permanent establishment, i.e., what is mentioned in clauses (a) to (f) as the 'negative list'. A combined reading of sub-articles (1), (2) and (3) of article 5 would clearly show that only certain forms of establishment are excluded as mentioned in article 5(3), which would not be permanent establishments. Otherwise, sub-article (2) uses the word 'include' which means that not only the places specified therein are to be treated as permanent establishments, the list of such permanent establishments is not exhaustive. In order to bring any other establishment which is not specifically mentioned, the requirements laid down in sub-article (1) are to be satisfied. Twin conditions which need to be satisfied are : (a) existence of a fixed place of business; and (b) through that place business of an enterprise is wholly or partly carried out.…

We are of the opinion that the test laid down by the Andhra Pradesh High Court in *CIT* v. *Visakhapatnam Port Trust* [(1983) 144 ITR 146 (AP); 1983 SCC OnLine AP 287; (1984) 38 CTR 1 (AP); (1983) 15 Taxman 72 (AP).] fully stands satisfied. Not only the Buddh International Circuit is a fixed place where the commercial/economic activity of conducting F-1 Championship was carried out, one could clearly discern that it was a virtual projection of the foreign enterprise, namely, Formula-1 (i.e., FOWC) on the soil of this country. It is already noted above that as per Philip Baker (A Manual on the Organization for Economic Co-operation and Development Model Tax Convention on Income and on Capital), a permanent establishment must have three characteristics: stability, productivity and dependence. All characteristics are present in this case. Fixed place of business in the form of physical location, i.e., Buddh International Circuit, was at the disposal of FOWC through which it conducted business. Aesthetics of law and taxation jurisprudence leave no doubt in our mind that taxable event

has taken place in India and the non-resident FOWC is liable to pay tax in India on the income it has earned on this soil."

87. As per the Manual on the Organization for Economic Co-operation and Development Model Tax Convention, and the precedents rendered on the subject, there are two basic conditions which are spelt out and which must be fulfilled for acknowledging a permanent establishment being existent and constituting a fixed place of business. They are:

(a) a place which stands placed at the "disposal" of an enterprise; and

(b) The establishment answering the characteristics of stability, productivity and dependence.

88. The expression "disposal" was explained to mean a right to use a place and exercise "control" thereupon. "Control" was explained further to mean the place of business being at the "disposal" of an enterprise and which may have use of the same to a considerable extent. It was further observed that the test of place of business being under the "control" of a foreign enterprise would be met even though the said premises may not be directly owned or taken by way of lease or on rental basis. In Formula One World Championship Ltd., the Supreme Court observed that even a certain amount of space which may be placed at the "disposal" of an enterprise for the purposes of the use of its business activities would be sufficient. The Supreme Court significantly observed that for the purposes of recognizing the existence of a fixed place permanent establishment, no formal legal right to use need be discerned or proven. It was thus held that as long as it is a space in an establishment or premises placed at the constant "disposal" of the enterprise, it would satisfy the test of a fixed place permanent establishment as contemplated under articles 5(1) and 5 (2)(a)-(k) of the Double Taxation Avoidance Agreement.

89. The principles governing fixed place permanent establishment were again spelt out and enunciated by the Supreme Court in *Morgan Stanley and Co. Inc.* [*DIT (International Taxation)* v. *Morgan Stanley and Co. Inc.*, (2007) 292 ITR 416 (SC); (2007) 7 SCC 1.] and *Samsung Heavy Industries Co. Ltd.* [*DIT (International Taxation)* v. *Samsung Heavy Industries Co. Ltd.*, (2020) 426 ITR 1 (SC); (2020) 7 SCC 347.] In *Morgan Stanley and Co. Inc.* [*DIT (International Taxation)* v. *Morgan Stanley and Co. Inc.*, (2007) 292 ITR 416 (SC); (2007) 7 SCC 1.] , and where the following pertinent observations came to be rendered (page 421 of 292 ITR):

"With globalisation, many economic activities spread over to several tax jurisdictions. This is where the concept of permanent establishment becomes important under article 5(1). There exists a permanent establishment if there is a fixed place through which the business of an enterprise, which is

multinational enterprise (MNE), is wholly or partly carried on. In the present case MSCo is a multinational entity. As stated above it has out sourced some of its activities to MSAS in India. A general definition of permanent establishment in the first part of article 5(1) postulates the existence of a fixed place of business whereas the second part of article 5(1) postulates that the business of MNE is carried out in India through such fixed place. One of the questions which we are called upon to decide is whether the activities to be undertaken by MSAS consist of back office operations of MSCo and if so whether such operations would fall within the ambit of the expression 'the place through which the business of an enterprise is wholly or partly carried out' in article 5(1).…

In our view, the second requirement of article 5(1) of the Double Taxation Avoidance Agreement is not satisfied as regards back office functions. We have examined the terms of the Agreement along with the advance ruling application made by MSCo inviting the AAR to give its ruling. It is clear from a reading of the above Agreement/ application that MSAS in India would be engaged in supporting the front office functions of MSCo in fixed income and equity research and in providing Information Technology enabled services such as data processing support centre and technical services as also reconciliation of accounts. In order to decide whether a permanent establishment stood constituted one has to undertake what is called as a functional and factual analysis of each of the activities to be undertaken by an establishment. It is from that point of view, we are in agreement with the ruling of AAR that in the present case article 5(1) is not applicable as the said MSAS would be performing in India only back office operations. Therefore to the extent of the above back office functions the second part of article 5(1) is not attracted."

90. *Morgan Stanley and Co. Inc.* was followed by the Supreme Court in *Samsung Heavy Industries Co. Ltd.* and where and in the context of a fixed place permanent establishment, the Supreme Court held (page 18 of 426 ITR):

"A recent judgment of this court, namely, *Asst. DIT v. E-Funds IT Solution Inc.*, concerned itself with the India-US Double Taxation Avoidance Agreement with similar provisions. Dealing with what was referred to as a 'fixed place', permanent establishment, this court held (SCC p. 310, para 16 and page 51 of 399 ITR):

"The Income-tax Act, in particular section 90 thereof, does not speak of the concept of a permanent establishment. This is a creation only of Double Taxation Avoidance Agreement. By virtue of article 7(1) of the Double Taxation Avoidance Agreement, the business income of companies which are

incorporated in the US will be taxable only in the US, unless it is found that they were permanent establishments in India, in which event their business income, to the extent to which it is attributable to such permanent establishments, would be taxable in India. Article 5 of the Double Taxation Avoidance Agreement set out hereinabove provides for three distinct types of permanent establishments with which we are concerned in the present case : fixed place of business permanent establishment under articles 5(1) and 5(2)(a) to 5(2)(k); service permanent establishment under article 5(2)(1) and agency permanent establishment under article 5(4). Specific and detailed criteria are set out in the aforesaid provisions in order to fulfil the conditions of these permanent establishments existing in India. The burden of proving the fact that a foreign assessee has a permanent establishment in India and must, therefore, suffer tax from the business generated from such permanent establishment is initially on the Revenue. With these prefatory remarks, let us analyse whether the respondents can be brought within any of the subclauses of article 5.' ”

Dealing with 'support services' rendered by an Indian company to American companies, it was held that the outsourcing of such services to India would not amount to a fixed place permanent establishment under article 5 of the aforesaid treaty, as follows (SCC p. 320, para 22 and page 63 of 399 ITR):

“This report would show that no part of the main business and revenue earning activity of the two American companies is carried on through a fixed business place in India which has been put at their disposal. It is clear from the above that the Indian company only renders support services which enable the assessees in turn to render services to their clients abroad. This outsourcing of work to India would not give rise to a fixed place permanent establishment and the High Court judgment (*DIT v. E-Funds IT Solution*); is, therefore, correct on this score ”

A reading of the aforesaid judgments makes it clear that when it comes to 'fixed place' permanent establishments under double taxation avoidance treaties, the condition precedent for applicability of article 5 (1) of the double taxation treaty and the ascertainment of a 'permanent establishment' is that it should be an establishment 'through which the business of an enterprise' is wholly or partly carried on. Further, the profits of the foreign enterprise are taxable only where the said enterprise carries on its core business through a permanent establishment. What is equally clear is that the maintenance of a fixed place of business which is of a preparatory or auxiliary character in the trade or business of the enterprise would not

be considered to be a permanent establishment under article 5. Also, it is only so much of the profits of the enterprise that may be taxed in the other State as is attributable to that permanent establishment ....

Though it was pointed out to Income-tax Appellate Tribunal that there were only two persons working in the Mumbai office, neither of whom was qualified to perform any core activity of the assessee, the Income-tax Appellate Tribunal chose to ignore the same. This being the case, it is clear, therefore, that no permanent establishment has been set up within the meaning of article 5(1) of the Double Taxation Avoidance Agreement, as the Mumbai project office cannot be said to be a fixed place of business through which the core business of the assessee was wholly or partly carried on. Also, as correctly argued by Shri Ganesh, the Mumbai project office, on the facts of the present case, would fall within article 5(4)(e) of the Double Taxation Avoidance Agreement, inasmuch as the office is solely an auxiliary office, meant to act as a liaison office between the assessee and ONGC. This being the case, it is not necessary to go into any of the other questions that have been argued before us."

91. When we test the stand taken by the respondents, bearing in mind the aforesaid precepts as culled out from the various judgments noticed hereinabove, we find ourselves unable to sustain even the prima facie formation of opinion by the first respondent in this respect. It is pertinent to note that the impugned notices and the reasons set out for initiating action under section 147/148 nowhere allude to a particular space or a part of the premises situated in Noida or Varanasi having been placed under the exclusive or significant "control" or "disposal" of the petitioner. The first respondent fails to rest its prima facie opinion with respect to fixed place permanent establishment on any part of the Noida or Varanasi premises which may have been set apart or exclusively placed in and under the "control" of the petitioner for use of its business activities and which may have tended to indicate that the space was made available for the use of the petitioner and from where it was conducting its business activities. It would have had to be shown that the "control" of that space answered the test of considerable extent. We recall Vogel describing this particular genre of a permanent establishment as being akin to an "instrument (equalling or resembling an operating asset) for his entrepreneurial activity". The concept of "virtual projection" is concerned with a functional integration between the two units and which would mean an establishment which has been virtually used for all purposes to carry out the paramount business activity of the petitioner. None of these factors are either alluded to or appear to have been borne in consideration before arriving at the conclusion that the Indian establishment constituted a fixed place permanent establishment.

xxxx **xxxx** **xxxx**

94. We also take note of the judgment in *Formula One World Championship Ltd.* [*Formula One World Championship Ltd.* v. *CIT (International Taxation)*, (2017) 394 ITR 80 (SC); (2017) 15 SCC 602; (2017) 295 CTR 12 (SC); (2017) 248 Taxman 192 (SC).] and where it was significantly observed that a permanent establishment must qualify and meet the tests of stability, productivity and dependence. Of equal significance were the observations which explained the phrases "at the disposal of" and "through". Tested on the aforesaid precepts also, the impugned notices and the reasons set out for initiating action under section 147/148 woefully fail to rest on any evidence which could have possibly compelled us in acknowledging that a fixed place permanent establishment had come into being."

38. On a more jurisprudential level, a Full Bench of our Court in **Hyatt International Southwest Asia Ltd. Vs. Additional Director**[15] had while expounding upon the basic concepts underlying a PE had enunciated the legal position in the following terms: -

> "**40.** The Commentary on the United Nations Model Double Taxation Convention between Developed and Developing Countries 202114 while explaining the concept of a PE makes the following pertinent observations: —
>
> > 7. It could perhaps be argued that in the general definition some mention should also be made of the other characteristic of a permanent establishment to which some importance has sometimes been attached in the past, namely that the establishment must have a productive character, i.e. contribute to the profits of the enterprise. In the present definition this course has not been taken. Within the framework of a well-run business organisation it is surely axiomatic to assume that each part contributes to the productivity of the whole. It does not, of course, follow in every case that because in the wider context of the whole organisation a particular establishment has a "productive character" it is consequently a permanent establishment to which profits can properly be attributed for the purpose of tax in a particular territory (see Commentary on paragraph 4).
>
> **41.** The concept of a PE is more lucidly explained in the commentary as follows: —

[15] 2024 SCC OnLine Del 6546

"41. Also, a permanent establishment may exist if the business of the enterprise is carried on mainly through automatic equipment, the activities of the personnel being restricted to setting up, operating, controlling and maintaining such equipment. Whether or not gaming and vending machines and the like set up by an enterprise of a State in the other State constitute a permanent establishment thus depends on whether or not the enterprise carries on a business activity besides the initial setting up of the machines. A permanent establishment does not exist if the enterprise merely sets up the machines and then leases the machines to other enterprises. A permanent establishment may exist, however, if the enterprise which sets up the machines also operates and maintains them for its own account. This also applies if the machines are operated and maintained by an agent dependent on the enterprise.

42. It follows from the definition of "enterprise of a Contracting State" in Article 3 that this term, as used in Article 7, and the term "enterprise" used in Article 5, refer to any form of enterprise carried on by a resident of a Contracting State, whether this enterprise is legally set up as a company, partnership, sole proprietorship or other legal form. Different enterprises may collaborate on the same project and the question of whether their collaboration constitutes a separate enterprise (e.g. in the form of a partnership) is a question that depends on the facts and the domestic law of each State. Clearly, if two persons each carrying on a separate enterprise decide to form a company in which these persons are shareholders, the company constitutes a legal person that will carry on what becomes another separate enterprise. It will often be the case, however, that different enterprises will simply agree to each carry on a separate part of the same project and that these enterprises will not jointly carry on business activities, will not share the profits thereof and will not be liable for each other's activities related to that project even though they may share the overall output from the project or the remuneration for the activities that will be carried on in the context of that project. In such a case, it would be difficult to consider that a separate enterprise has been set up. Although such an arrangement would be referred to as a "joint venture" in many countries, the meaning of "joint venture" depends on domestic law and it is therefore possible that, in some countries, the term "joint venture" would refer to a distinct enterprise.

43. In the case of an enterprise that takes the form of a fiscally transparent partnership, the enterprise is carried on by each partner and, as regards the partners' respective shares of the profits, is therefore an enterprise of each Contracting State of which a partner is a resident. If such a partnership has a permanent establishment in a Contracting State, each partner's share of the profits attributable to the permanent establishment will therefore constitute, for the purposes of Article 7, profits derived by an enterprise of the Contracting State of which that partner is a resident (see also paragraph 56 [of the Commentary on Article 5 of the 2017 OECD Model Tax Convention] below).

44.A permanent establishment begins to exist as soon as the enterprise commences to carry on its business through a fixed place of business. This is the case once the enterprise prepares, at the place of business, the activity for which the place of business is to serve permanently. The period of time during which the fixed place of business itself is being set up by the enterprise should not be counted, provided that this activity differs substantially from the activity for which the place of business is to serve permanently. The permanent establishment ceases to exist with the disposal of the fixed place of business or with the cessation of any activity through it, that is when all acts and measures connected with the former activities of the permanent establishment are terminated (winding up current business transactions, maintenance and repair of facilities). A temporary interruption of operations, however, cannot be regarded as a closure. If the fixed place of business is leased to another enterprise, it will normally only serve the activities of that enterprise instead of the lessor's; in general, the lessor's permanent establishment ceases to exist, except where he continues carrying on a business activity of his own through the fixed place of business".

42. The concept of a PE is based upon the undertaking of economic activity in a particular State irrespective of the residence of an enterprise and the same being understood to be in the nature of a conglomerate or an entity which may have many arms or independent functional units situate in various fiscal jurisdictions. Any entrepreneurial activity which gives rise to income or profit thus becomes liable to be taxed at source irrespective of the ultimate recipient or owner of that income. Source here would mean the location which gives rise to the accrual of profits or income or which is the location where the same arises. The PE

principle thus enables the assignment of tax to the State which constitutes the source. The PE concept thus creates a functional relationship and connect between the principal entity and the place of business whose activities give rise to the income or profit. It is this fictional creation of an independent economic center in a Contracting State which informs the allocation of taxing rights. Once the DTAA confers an independent identity upon the PE, it would be wholly erroneous to answer the question of taxability basis either the activities or profitability of the parent or the entity which seeds and sustains the PE.

43. The Contracting State in which this imagined entity is domiciled and undertakes business thus becomes identified as an independent profit or revenue earning center which is liable to be taxed. Once such an entity is found to exist in one of the Contracting State, it is viewed as a unit which contributes to the economic life of that State and thus be liable to tax. It is these basic precepts which convince us to debunk the theory of taxation in the source State being dependent upon a global profit or taxation being subject to income or profit having been earned at an entity level.

44. The identity which attaches to a PE for the purposes of ascertainment of a taxing liability cannot possibly be doubted bearing in mind the succinct observations of the Supreme Court in Morgan Stanley and where their Lordships without a degree of equivocation acknowledged the distinction that is liable to be drawn between a PE with respect to income earned in the Contracting State where it is domiciled or deemed to exist and the global enterprise of which it may be a part. Vogel explains the PE concept as constituting the threshold and the "essential demarcation line" in the source State which sanctions the imposition of a tax in a fiscal jurisdiction other than the State of residence. This would clearly appeal to logical since the right of taxation which inheres in the source State is connected to the "economic life" of that transnational enterprise which is moored and berthed by virtue of the existence of a PE which may be found to exist. Regard must also be had to the fact that right of the source State to tax does not extend to profits which are not allocable to the PE. All of the above, thus clearly leads us to hold that the existence and identity of the PE is separate and distinct and subject to tax to the extent of activities that it may undertake in a State distinct from that of its principal.

45. It would also be pertinent to note that a cross-border entity may structure its operations in a manner where it operates in more than one taxing jurisdiction. If it be open for such an entity to assert that its global profits and income are not liable to be taxed on the basis of the source principle, it would be wholly impermissible for it to contend that the income which accrues or arises in the Contracting State is also exempt from tax. In any case, the usage of the phrase

> "…so much of them as is attributable to the permanent establishment." is a clear indicator of the DTAA warranting the PE being liable to be viewed as an independent center of revenue.
>
> **46**. The identifiable parts of Article 7 not only restrict the right of one of the Contracting States to tax, it also provisions for the extent to which a tax may be imposed by that State. This becomes evident from it freeing a trans-border entity from the specter of a tax liability if it does not have a PE in the introductory part of that covenant. It then proceeds to restrict the impost by adopting the principle of attribution. It thus constructs an objective criterion for identification of a PE and when a foreign enterprise with sufficient economic presence would become subject to tax. All of the above, convinces us to hold against the argument of a PE not being taxable on an independent evaluation being misconceived."

39. In *Progress Rail (supra)*, we also had on occasion to examine what would constitute 'preparatory' and 'auxiliary' activities, expressions found in Para 4(f) of Article 5, and which stipulates that as long as the activities undertaken could be said to be preparatory or auxiliary, the establishment would not be liable to be construed as constituting a PE. Clause (f) of Para 4 thus provides that a maintenance of a fixed place of business, even if it be for the undertaking of any of the activities stipulated in the preceding clauses, would still not qualify as a PE if the overall character of such activities were found to be of a preparatory or auxiliary character. In *Progress Rail*, we had while dealing with the meaning liable to be ascribed to these twin expressions held: -

> "**69.** Proceeding further to deal with the concepts of "preparatory" and "auxiliary" services and which are intended to remove a place of business which may otherwise fall within the meaning of a permanent establishment and which phraseology is mirrored in article 5(3)(e) of the India-USA Double Taxation Avoidance Agreement, Klaus Vogel's work has the following instructive passages:
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> > "59. (Determination of the activity's character) It is often difficult to distinguish between activities which have a preparatory or auxiliary character and those which have not. The decisive criterion is whether or not the activity of the

fixed place of business in itself forms an essential and significant part of the activity of the enterprise as a whole. Each individual case will have to be examined on its own merits. In any case, a fixed place of business whose general purpose is one which is identical to the general purpose of the whole enterprise, does not exercise a preparatory or auxiliary activity.

60. (Preparatory character) As a general rule, an activity that has a preparatory character is one that is carried on in contemplation of the carrying on of what constitutes the essential and significant part of the activity of the enterprise as a whole. Since a preparatory activity precedes another activity, it will often be carried on during a relatively short period, the duration of that period being determined by the nature of the core activities of the enterprise. This, however, will not always be the case as it is possible to carry on an activity at a given place for a substantial period of time in preparation for activities that take place somewhere else. Where, for example, a construction enterprise trains its employees at one place before these employees are sent to work at remote work sites located in other countries, the training that takes place at the first location constitutes a preparatory activity for that enterprise. An activity that has an auxiliary character, on the other hand, generally corresponds to an activity that is carried on to support, without being part of, the essential and significant part of the activity of the enterprise as a whole. It is unlikely that an activity that requires a significant proportion of the assets or employees of the enterprise could be considered as having an auxiliary character.…

69. (Collect information) The second part of sub-paragraph (d) relates to a fixed place of business that is used solely to collect information for the enterprise. An enterprise will frequently need to collect information before deciding whether and how to carry on its core business activities in a State. If the enterprise does so without maintaining a fixed place of business in that State, sub-paragraph (d) will obviously be irrelevant. If, however, a fixed place of business is maintained solely for that purpose, sub-paragraph (d) will be relevant and it will be necessary to determine whether the collection of information goes beyond the preparatory or auxiliary threshold. Where, for example, an investment fund sets up an office in a State solely to collect information on possible investment opportunities in that State, the collecting of information through that office will be a preparatory activity. The same conclusion would be reached in the case of an insurance enterprise that sets up an office solely for the collection of information, such as statistics, on risks in a particular market and in the case of a newspaper bureau set up

in a State solely to collect information on possible news stories without engaging in any advertising activities : in both cases, the collecting of information will be a preparatory activity."

70. Speaking in greater detail on the aspect of "preparatory" and "auxiliary" functions, the author observes:

"303. Already before the 2017 Update to the OECD MC, all of the activities listed in article 5(4)(a) to (f) of OECD and UN MC had to be preparatory or auxiliary (infra m. No. 304 et seq.). This followed from the use of the word 'other' in article 5(4)(e) of UN MC. This word relates not only to the subsequent word 'activity' (otherwise, one should have expected an if-clause or a 'provided that'- clause after 'activity', like in article 5(4)(f) of UN MC) but to the entire phrase 'activity of a preparatory or auxiliary character'. The 2017 update to the OECD MC has made this entirely clear by adding the words 'provided that such activity or, in the case of sub-paragraph (f), the overall activity of the fixed place of business, is of a preparatory or auxiliary character' as a joint supplement to sub-paragraphs (a)-(f). By contrast, other requirements in article 5(4)(e) of UN MC have no paramount relevance but apply within the ambit of this sub-paragraph only (infra m. No. 315 et seq.).

304. The preparatory or auxiliary character of the activities listed in article 5(4) of OECD MC can be based on an absolute standard or based on a relative standard. For example, consider a comparison of two enterprises : (1) an integrated enterprise which covers many steps in the creation of value (e.g., all steps from agricultural production through the processing of raw materials, further refinement up to marketing, sale and delivery of the goods to final consumers) and (2) a specialised enterprise which focuses on one of these steps only (e.g., on the delivery of goods). Suppose that each enterprise maintains a place of business in a foreign State just for the sake of the delivery of goods. The same activity (the delivery of goods) is ancillary and subordinate for enterprise (1) while it constitutes the core business of enterprise (2).

305. The amount of value added by either enterprise is the same, and so is the potential tax revenue in the source State. An absolute standard suggests equal treatment of cases (1) and (2).

306. However, the ordinary meaning of both 'preparatory' and 'auxiliary' requires the identification of a point of reference. One may say that the absolute standards are based on an analysis of the function of the core activity in relation to the entire chain of economic value added. It is more convincing, however, to apply relative standards in the sense that the value

added is considered on a micro rather than a macro level, that is, that the core activity should be compared to the entirety of all activities exercised by the enterprise. This relative view would deny a permanent establishment in case (1), and assume a permanent establishment in case (2). This view is shared by No. 60 of OECD MC Comm. on article 5 as well as by most authors.

307. It seems to your author, however, that the strict and exclusive application of relative standards would not do justice to cases where an enterprise of type (1) above (supra m. No. 283) is so large that place of businesses which, from an absolute perspective, are respectable entities with valuable assets, a considerable number of employees and full-fledged bureaucratic and administrative facilities of their own, just seem to be small, preparatory or auxiliary from the perspective of the company's headquarters. If they are still the biggest employer in a given municipality, it is hardly justified from the viewpoint of fiscal equivalence to exempt such place of businesses under article 5(4) of OECD and UN MC.

308. It follows that a combined approach is most appropriate. While relative standards apply at the outset (supra m. No. 304), absolute standards require a second filter:

The activities of a place of business qualify as being 'of a preparatory or auxiliary character', as compared to the overall activities of the enterprise if they have not more than a marginal relevance within the enterprise's overall business plan. It should be noted that it is not the share in actual profits or losses on which the comparison should be based. Rather, the characterisation of an activity as preparatory and/or auxiliary depends on the type, sector and intensity of the activity, as compared to the core business of the enterprise as a whole.

If the activities of a place of business qualify as preparatory and/or auxiliary under these relative standards, they still do not fall under article 5(4) of OECD MC if the place of business (and the activities exercised through it) alone, when looked at separately from the rest of the enterprise, exceeds a certain size and degree of professional entrepreneurship.…

313. A further group of examples covers rooms and facilities which an employer makes available in order to accommodate his employees or help them to recreate or spend their idle time. This includes hotels, bedrooms, lounges or restrooms maintained outside the ordinary premises which the employer uses for the purpose of his core business. Similarly, locker rooms and coaches' rooms occupied by a baseball team while playing in venues outside the headquarters of the team do not

constitute permanent establishments of the baseball clubs. In contrast, sales activities of a manufacturing company are not of an auxiliary character. If they occur in a fixed place of business, they create a permanent establishment even if the sales contracts are subject to approval by the head office or another permanent establishment."

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98. That takes us then to further test the stand as struck by the respondents and to examine the correctness of their conclusion that the activities undertaken by the Indian subsidiary could not be said to be of a "preparatory" or "auxiliary" character. The decision of the Supreme Court in *Morgan Stanley and Co. Inc.* [*DIT (International Taxation)* v. *Morgan Stanley and Co. Inc.*, (2007) 292 ITR 416 (SC); (2007) 7 SCC 1.], while explaining the meaning to be ascribed to support services and activities of a "preparatory" or an "auxiliary" nature enunciates the legal position in the following terms (page 425 of 292 ITR):

"In our view, the second requirement of article 5(1) of the Double Taxation Avoidance Agreement is not satisfied as regards back office functions. We have examined the terms of the Agreement along with the advance ruling application made by MSCo inviting AAR to give its ruling. It is clear from a reading of the above Agreement/application that MSAS in India would be engaged in supporting the front office functions of MSCo in fixed income and equity research and in providing Information Technology enabled services such as data processing support centre and technical services as also reconciliation of accounts. In order to decide whether a permanent establishment stood constituted one has to undertake what is called as a functional and factual analysis of each of the activities to be undertaken by an establishment. It is from that point of view, we are in agreement with the ruling of AAR that in the present case article 5(1) is not applicable as the said MSAS would be performing in India only back office operations. Therefore to the extent of the above back office functions the second part of article 5(1) is not attracted.…

There is one more aspect which needs to be discussed, namely, exclusion of permanent establishment under article 5(3). Under article 5(3)(e) activities which are preparatory or auxiliary in character which are carried out at a fixed place of business will not constitute a permanent establishment. Article 5(3) commences with a non obstante clause. It states that notwithstanding what is stated in article 5(1) or under article 5(2) the term permanent establishment shall not include maintenance of a fixed place of business solely for advertisement, scientific research or for activities which are

preparatory or auxiliary in character. In the present case we are of the view that the abovementioned back office functions proposed to be performed by MSAS in India falls under article 5(3)(e) of the Double Taxation Avoidance Agreement. Therefore, in our view in the present case MSAS would not constitute a fixed place permanent establishment under article 5(1) of the Double Taxation Avoidance Agreement as regards its back office operations."

xxxx xxxx xxxx

101. The aspect of whether an Indian establishment was performing functions of a "preparatory" or an "auxiliary" character was considered by this court in *National Petroleum Construction Co.* v. *DIT (International Taxation)* [(2016) 383 ITR 648 (Delhi); 2016 SCC OnLine Del 571.], and where it was pertinently observed (page 672 of 383 ITR):

"The language of sub-paragraph (e) of paragraph (3) of article 5 of the Double Taxation Avoidance Agreement is similar to the language of sub-paragraph (e) of paragraph (4) of article 5 of the Model Conventions framed by Organization for Economic Co-operation and Development, United Nations as well as the United States of America. The rationale for excluding a fixed place of business maintained solely for the purposes of carrying on activity of a preparatory or auxiliary character has been explained by Professor Dr. Klaus Vogel. In his commentary on 'Double Taxation Conventions, Third Edition', he states that 'It is recognised that such a place of business may well contribute to the productivity of the enterprise, but the services it performs are so remote from the actual realisation of profits that it is difficult to allocate any profit to the fixed place of business in question. Examples are fixed places of business solely for the purpose of advertising or for the supply of information or for scientific research or for the servicing of a patent or a know-how contract, if such activities have a preparatory or auxiliary character'….

The *Black's Law Dictionary* defines the word 'auxiliary' to mean as 'aiding or supporting, subsidiary'. The word 'auxiliary' owes its origin to the Latin word 'auxiliarius' (from auxilium meaning 'help'). The *Oxford Dictionary* defines the word 'auxiliary' to mean 'providing supplementary or additional help and support'. In the context of article 5(3)(e) of the Double Taxation Avoidance Agreement, the expression would necessarily mean carrying on activities, other than the main business functions, that aid and support the assessee. In the context of the contracts in question, where the main business is fabrication and installation of platforms, acting as a communication channel would clearly qualify as an activity of

auxiliary character - an activity which aids and supports the assessee in carrying on its main business.

In view of the above, the activity of the assessee's project office in Mumbai would clearly fall within the exclusionary clause of article 5(3)(e) of the Double Taxation Avoidance Agreement and, therefore, cannot be construed as the assessee's permanent establishment in India."

102. When tested on the aforesaid principles, it becomes apparent that the activities undertaken by the Indian subsidiary clearly do not appear to travel beyond being "preparatory" or "auxiliary". It is pertinent to note that both entities do not appear to have been established with a commonality of general purpose. The expression "preparatory" has been understood to mean work which is undertaken in contemplation of the essential and significant part of the principal activity of an entity. The principal or for that matter the essential activity of the petitioner is the manufacture and production of goods needed by railroad companies. The principal activity is concerned with the core business activity of the petitioner. That has clearly not been shown to have been undertaken at the Noida premises. Of equal significance are the observations appearing in National Petroleum, and where the court had held that while activities undertaken by an entity which is asserted to be a "permanent establishment" may contribute to the productivity of the foreign enterprise, but if those functions be remote from the actual realisation of profits, the tests of a permanent establishment would not be satisfied."

40. Proceeding ahead and while speaking on DAPE, we had in *Progress Rail* observed: -

"111. It is pertinent to recall that in order to fall within the scope of article 5(4), it was imperative for the respondents to have found that the Indian subsidiary not only stood conferred with the "authority to conclude contracts" but also that it was in fact "habitually" engaged in acting in discharge of that authority. The issue of a habitual or recurrent exercise of authority does not arise at all since we have already found that an "authority to conclude contracts" never stood conferred. Suffice it to observe that there is not an iota of evidence which may have even remotely justified article 5(4)(a) being invoked.

112. Similar is the position which emerges when the case as set up against the petitioner is examined on the anvil of article 5(4)(c) of the India-USA Double Taxation Avoidance Agreement ((1991) 187 ITR (Stat) 102). This would have required the respondents to have established or found, as a matter of fact, that the Indian subsidiary was engaged or created solely for the purpose of securing orders for

> the petitioner. Clause (c) of article 5(4) would have been attracted if the respondents had, even on a prima facie examination, found that the Indian subsidiary was concerned primarily with securing orders for the petitioner. This, in the light of the said clause using the expression "wholly or almost wholly for the enterprise". Clause (c) not only alludes to aspects of an enterprise being exclusively concerned with working for the fulfilment of the business interests of another, it would also have to be additionally proven that it does so "habitually".

41. The aforesaid precepts which we had recognized as being pertinent to and determinative of whether a Fixed Place PE or DAPE could be said to have come into existence also find resonance in our judgment in **Director of Income Tax, International v. Western Union Financial Services Inc**[16] and where we had held as follows: -

> "**49.** For the purposes of being acknowledged as a PE, the said office would have had to qualify the provisions of sub-paras 1 and 2 of Article 5. It would thus have to be held to be a 'fixed place 'through which the business of the enterprise was being wholly or partly carried out. In order to constitute a Fixed Place PE, it would have to satisfy the tests of virtual projection, a takeover of the premises as well as the precepts of control and disposal and the undertaking of core business activity of the enterprise.
>
> **50.** Of equal importance are the provisions comprised in Article 5(3) and which excludes places of business related to an enterprise in the other contracting state and which undertakes "*other activities*" which are liable to be countenanced as being preparatory or auxiliary. It is thus Article 5(3)(e) which clearly appears to be applicable when viewed in juxtaposition with the activities which the LO performed and the functions that it discharged. This becomes evident from the discussion which follows.
>
> **51.** We note that the position commended for our acceptance by the appellants would have been sustainable, provided the activities and functions performed by that LO met the aforenoted tests. However, we find ourselves unable to sustain those submissions bearing in mind the peripheral character of the actual activities which were undertaken by that office."

42. Proceeding to explain the concept of DAPE, we had in *Western Union* observed: -

[16] [2024 SCC Online Del 8913]

"**56.** That then takes us to the argument based on the criterion of DAPE being met under the DTAA. The said contention would have to be evaluated on the basis of Article 5(4) and which speaks of entities who may be connected with the enterprise in the other Contracting State and not being an agent of independent status. It is only once such entities are found to be acting in the Contracting State on behalf of that enterprise that Article 5(4) would be attracted. For the purposes of being viewed as DAPE, it would have been incumbent upon the appellants to have established that the LO was acting on behalf of Western Union Financial Services and that its functions fell within the four corners of clauses (a), (b) and (c) of Article 5(4). For the purposes of being held to be a dependent agent, it was incumbent for the appellants to establish that such an entity habitually exercised an authority to conclude contracts. It could have also been proved by the appellants that the LO habitually secured orders for Western Union Financial Services. However, none of these conditions are met in the facts of the present case. In the absence of these conditions being found to exist, it would be wholly incorrect in law for the LO to be classified as a DAPE.

57. Regard must be had to the fact that Article 5(4) introduces a legal fiction in cases where it be found that the enterprise has an agent which is acting on its behalf in the other Contracting State. The first limb of Article 5(4), when met, gets coupled to the legal fiction embodied in para 4 and which is "*shall be deemed to have a permanent establishment*". However, of crucial significance is the use of the word '*if*', which precedes clauses (a), (b) and (c) and thus being indicative of the clear intent of the contracting parties of recognizing the existence of a DAPE only if one of those were also met. The appellants have not relied on any evidence or material which may have even remotely established the criterion of either clauses (a), (b) or (c) being satisfied by the LO"

43. When tested on the aforenoted foundational principles, we have no hesitation in holding that the Tribunal has committed no error in answering the questions posited in favour of Nokia OY. Undisputedly, the issue of the Liaison Office constituting a PE had come to be settled in the first round of the litigation which ensued before the Tribunal and came to be ultimately affirmed by the 2012 judgment of this Court. The broad questions on which this Court remanded the matter to the Tribunal stood confined to NIPL and its interrelationship with Nokia OY.

44. In the first round of litigation, the question of whether NIPL constituted a PE appears to have been principally answered in light of it being the wholly owned subsidiary of Nokia OY. The Revenue had essentially approached the issue from this angle failing to bear in mind the incontrovertible negative covenant which stands enshrined in Article 5(8) of the DTAA. The Convention in unequivocal terms injuncts the Revenue from either readily presuming or harbouring a presumption that a subsidiary would ipso facto constitute a PE. This is evident from the language of Para 8 and which employs the expression *"shall not of itself"*. It is thus apparent that Article 5(8) bids us to bear in mind that the mere control of an entity by a parent or a holding company would not be determinative of whether a PE exists. A subsidiary or an entity which is substantially controlled by another would still have to meet the test prescribed by Paras (1), (2), (3), (5) and (6) of Article 5 before it can be said to constitute a PE.

45. We are also of the firm opinion that the question of PE is not liable to be answered on the basis of a "perception" of virtual projection. The DTAA does not leave this seminal issue to be decided on the basis of individual estimations or impressions. It lays in place certain empirical standards which must be borne in mind when answering the question whether a PE exists. Issues of *"virtual projection"* and *"functional integration"* are liable to be answered on an appreciation of facts as may be found to exist. It is here that the precepts propounded by learned scholars such as the use and maintenance of a place of business, the place being at the disposal of an enterprise or being liable to be viewed as an operating asset of the enterprise itself assume significance. What, however, needs to be emphasized is that these are aspects which cannot possibly be left to

depend upon the tenuous thread of fluctuating perceptions, impressions and mutable beliefs. Article 5 thus bids us to answer the question of PE based on measurable evidence and the objective benchmarks incorporated therein. The exercise to ascertain whether a PE exists is thus founded on evidence-based standards rather than a theory or mere surmise. We consequently find ourselves unable to countenance the perception test which was propounded by the Tribunal in the earlier round of litigation.

46. When tested on the standards consistently recognized by courts, it becomes apparent that the appellants had woefully failed to establish that NIPL or its premises could be recognised to be a PE when tested on the mandated criterion of either a Fixed Place or a Dependent Agent PE. Having gone through the copious material which was examined and evaluated by the Tribunal, we have no hesitation in affirming its view insofar as Fixed Place PE is concerned.

47. We also find ourselves unconvinced of the arguments advanced by the appellants before us in their attempt to question the correctness of its conclusions insofar as DAPE is concerned. The reasons underlying our conclusion are set out hereinafter.

48. It becomes pertinent to note that the Tribunal has in unequivocal terms found that NIPL was pursuing an independent line of business with Indian telecom operators. The appellants have abjectly failed to prove that NIPL stood conferred with the authority to bind or conclude contracts on behalf of Nokia OY. Insofar as installation activity was concerned, it was found that NIPL was not generating any revenue or income for the respondent assessee. In any event, absent the conferral of authority upon NIPL to conclude contracts binding Nokia OY or

securing contracts on its behalf would lead one to the irresistible conclusion that no DAPE existed in the relevant AYs'. Our Court had in its 2012 judgment found that onshore activities of NIPL were totally disconnected with the supply contracts of Nokia OY. The assessee had clearly established that the offshore contracts were on FOB basis from Finland. There was thus a clear and discernible distinction between the activities undertaken by NIPL and the supply contracts executed by Nokia OY. Even with respect to the two pre-incorporation contracts which were assigned to NIPL, the income derived therefrom had been taxed in its hands and had been found to satisfy the test of arm's length. Regard must also be had to the fact that no transfer pricing reference was ever made in this respect. There was thus no occasion to delve into any further exercise of attribution.

49. That takes us then to the task of examining the minority opinion which came to be penned and which the appellants commended for our acceptance. It becomes pertinent to note that the learned Member has, in our opinion, correctly noted that there is no general presumption in law that a subsidiary can never be acknowledged to be a PE. This since Article 5(8) itself merely states that the said factor alone shall not be determinative of the PE question. The covenant thus clearly obliges us to evaluate the facts based on the other provisions comprised in Article 5 of the DTAA.

50. We also concur with the minority opinion when it held that the appellants had failed to establish the existence of a DAPE. It has, however, in this respect observed that while the view expressed in the previous round, *stricto sensu*, may not have been wholly accurate or tenable, the question of PE would still be liable to be answered basis

the essence of the arrangement between Nokia OY and NIPL as was discerned by the AO and the CIT(A). The first issue which was thus identified by the Member was that of business connection. According to the Member, the *"unmistakable thrust"* of the findings of the AO and the CIT(A) would inevitably lead one to answering the business connection question in favour of the Revenue. According to the minority, the slew of services and expertise which was provided by Nokia OY to its Indian subsidiary would lead one to the definitive conclusion that NIPL was created to *"artificially block creation of PE if the realities of actual operations was not to be vitiated by these projections and devices."*

51. The second aspect which appears to have weighed upon the minority was the commitment towards technical support as held out by Nokia OY as well as its assurance against dilution of its interest in NIPL. All this, according to the minority, amounted to a virtual performance guarantee and ultimately concerned with *"furtherance of the business interests of the assessee company in India, as much, if not more, for its own economic and business interests."* It is this underlying theme and line of reasoning which then breathes through the entire opinion.

52. The minority then proceeds to notice and apply the principle of alter ego companies as being pertinent to the issue of PE. However, the alter ego test was subjected to the caveat of it being found that the resident company had no significant independent activity of its own. The minority then also culled out a distinction between an associated PE (and which it chose to describe as a direct PE) and an unassociated PE ("indirect PE" as per the minority).

53. In our opinion, the reasoning so adopted clearly seeks to blur the distinction which the law seeks to draw between associated enterprises and which may legitimately enter into transactions inter se and which would satisfy the arm's length test. Quite apart from this constituting the first fault line in the reasoning assigned and adopted by the minority, it has also chosen to advert to the unassociated PE doctrine as propounded by Baker in his famous treatise and which was also noticed by the Supreme Court in *Formula One World Championship* losing sight of the crucial aspect of the concept of unassociated PE having been alluded to in the context of an agent contemplated by Article 5(5) and which is coupled to an authority to conclude contracts or habitually securing orders in the first mentioned State.

54. The agency PE which is contemplated in Article 5(5) is concerned with a person who acts on behalf of an enterprise and undertakes activities specified in clauses (a), (b) and (c) thereof. Such an agent must and in light of the textual construct of Article 5(5) be one who acts "on behalf of", "in the name of" and "for the enterprise itself". The minority thus in its attempt to conflate a Fixed Place PE with DAPE has merely confounded two distinct issues. It has thus chosen to ignore the primordial conditions of "virtual projection" and premises at the disposal of an enterprise being found to exist so as to constitute a PE.

55. More fundamentally, it has failed to bear in mind that Article 5(5) speaks of an agent who acts not for itself but principally in furtherance of the business interest of the enterprise. We fail to comprehend how NIPL could have been possibly recognised as carrying on the business of Nokia OY when the revenue generated by

the former was admittedly being taxed in its hands and recognised as income accruing to it. The fact that both Nokia OY and NIPL were acting in discharge of independent contractual obligations does not appear to have been a point of contestation at all. We also bear in mind the consistent stand of the assessee who had gone in great detail to explain the nature of the onshore activities undertaken by NIPL as distinct and separate from the offshore supplies affected by Nokia OY. The minority has thus chosen to yet again proceed on the basis of a "perception of virtual projection" as opposed to what the DTAA expects, namely, a conclusion on facts.

56. The minority opinion then attempts to overcome the judgments in *Formula One World Championship* and *E Funds* by significantly observing that the virtual projection test need not be met if the "basic rules" concerning a PE are satisfied. This is ex facie contrary and flies in the face of an entire body of precedent which has evolved on the subject. We find ourselves unable to appreciate how "virtual projection" and the host of attendant tests propounded by courts do not themselves constitute the grundnorm. This Court, in its humble understanding, is unable to conceive of a more cardinal or foundational prerequisite and which would overshadow or eclipse the tests as propounded by courts and noticed above.

57. Not stopping here, the minority further observes that the earlier ruling of the Special Bench on core issues had remained untouched and thus seeks to read our 2012 judgment as being confined to mere factual mistakes. This, in our respectful consideration, was a wholly convoluted reading of the judgment handed down by this Court and this alone being sufficient to outrightly reject the view expressed by the

minority.

58. The minority then also doubts the aspect of whether consideration paid was at arm's length. We fail to appreciate how this was an aspect which could have been even questioned or doubted since admittedly no transfer pricing reference had been made nor does this aspect appear to have been argued. While undertaking this long and twisted journey, the minority also clearly overlooked the factum of admitted offshore sales and the issue of taxability in that respect having been conclusively settled by **Ishikawajama–Harima Heavy Industries Ltd. v. Director of Income Tax, Mumbai**[17]. It has also, and in our opinion, unjustifiably sought to distinguish **Nortel Networks India International Inc. v. Director of Income Tax**[18] on reasoning which is clearly untenable.

59. While closing, we may only observe that a parent or a holding company would invariably be expected to have an interest and concern in the working of an overseas subsidiary. This essentially represents its right of oversight, supervision and protection of shareholder interest. However, the exercise of those powers does not denude the subsidiary of its independent economic existence. As Article 5(8) explains, the mere fact that the enterprise is a subsidiary of another would not in itself be sufficient to recognise it as a PE. The decisions rendered in this context have on more than one occasion instructed courts to bear in mind the distinction between the income of an enterprise earned in a Contracting State and the global enterprise of which it may be a constituent.

60. Ultimately, it would have been imperative for the appellants to

[17] [(2007) 3 SCC 481]
[18] [2016 SCC OnLine Del 2607]

have established that NIPL was an enterprise through which Nokia OY was operating and carrying on its own business and that the former was no more than an adjunct of Nokia OY itself. The mere fact that Nokia OY held out an assurance in respect of a fledgling venture in its formative years fails to convince us to hold that the former constituted its PE. The assurances were clearly not liable to be viewed as being evidence of Nokia OY using NIPL as a vehicle for its own enterprise.

61. Insofar as the issue of software is concerned, it was fairly conceded that the same would be liable to be answered against the appellants in light of the judgment of the Supreme Court in **Engineering Analysis Centre of Intelligence Private Limited v. Commissioner of Income Tax and Anr.**[19]

62. We would thus answer the questions as posited in the negative and against the appellants. The appeals, in consequence, fail and shall stand dismissed.

YASHWANT VARMA, J.

RAVINDER DUDEJA, J.

FEBRUARY 21, 2025/neha/DR

[19] (2022) 3 SCC 321