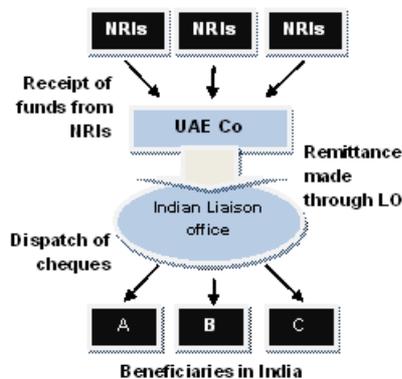


Tax Hotline

February 21, 2009

PE AUXILIARY ACTIVITY EXCLUSION: HIGH COURT ADOPTS A LIBERAL APPROACH

It is a settled principle of international tax jurisprudence that the maintenance of a fixed place of business solely for the purpose of carrying on any activity of a preparatory or auxiliary character would not give rise to a permanent establishment (“PE”). But, can an activity that is not merely auxiliary and actually forms a core part of the operations of the non-resident enterprise still fall within the scope of this exclusion? The recent decision of the High Court of Delhi seems to answer this question in the affirmative.¹



To briefly state the facts, a UAE-based company (“UAE Co”) offered remittance services to various non-resident Indians for transferring money from UAE to specific individuals in India. The remittance was made electronically by way of (i) telegraphic transfer through banking channels; or (ii) on the request of the remitter, dispatch of instruments / cheques through the Indian liaison office (“LO”) of UAE Co to the designated beneficiaries. UAE Co approached the Authority for Advance Rulings (“AAR”) for a ruling on whether its activities in India gave rise to a PE in India.

Since the role of the LO in the first mode of remittance was confined to addressing customer queries and complaints, the AAR held that such auxiliary involvement would not give rise to a PE in India as per the provisions of Article 5(3) (e) of the India-UAE Tax Treaty. However, in the second mode of remittance, the LO undertook the enhanced role of downloading online data regarding the amount to be remitted along with relevant names and addresses, and printing and dispatching the cheques / drafts to the designated beneficiaries by way of courier. The AAR observed that this effectively formed part of the core activity carried out by UAE Co and could not be viewed as auxiliary or incidental in nature. Considering that the LO was a fixed place of business through which UAE Co carried on business in India, the AAR held that UAE Co had a PE in India.

With a view to challenge the AAR’s decision, UAE Co then invoked the writ jurisdiction of the Delhi High Court under Article 226 of the Constitution of India. After reviewing the AAR’s construction of the domestic and treaty provisions, the Delhi High Court quashed the AAR’s decision on the basis that it suffered from ‘errors apparent on the face of record’. It may be noted that a contrasting approach was adopted by the Madras High Court in another recent case where the Court limited its judicial review to the legality of the procedure followed by the AAR and refused to venture into the correctness or legal validity of the AAR’s order.²

The Delhi High Court in the present case, undertook a liberal construction of the auxiliary activity exclusion in the Treaty so as to cover the role played by the LO, which in its view was merely supportive of the main activity of the LO. Accordingly, it was held that the LO could not be considered a PE of UAE Co in India.

If it is presumed that the LO and UAE Co essentially carried out the same activity (i.e. remittance of money), the decision of the Delhi High Court would clearly contradict the OECD view that “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.”

The High Court even went a step further to hold that under domestic tax law as well, UAE Co cannot be said to have a business connection in India so as to render its income taxable in India. Under the domestic provisions, business profits earned by a non-resident would be taxable in India only to the extent that it is attributable to a business connection in India.³ It seems that the Delhi High Court’s decision has the effect of narrowing down the scope of the business connection threshold.

The Delhi High Court’s liberal interpretation of the auxiliary activity exclusion and the concept of business connection, and its admonition of the AAR’s ‘errors apparent on the face of record’ is likely to give rise to similar

Research Papers

Medical Device Industry in India

April 28, 2025

Clinical Trials and Biomedical Research in India

April 22, 2025

Structuring Platform Investments in India For Foreign Investors

March 31, 2025

Research Articles

2025 Watchlist: Life Sciences Sector India

April 04, 2025

Re-Evaluating Press Note 3 Of 2020: Should India’s Land Borders Still Define Foreign Investment Boundaries?

February 04, 2025

INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

Audio

CCI’s Deal Value Test

February 22, 2025

Securities Market Regulator’s Continued Quest Against “Unfiltered” Financial Advice

December 18, 2024

Digital Lending - Part 1 - What’s New with NBFC P2Ps

November 19, 2024

NDA Connect

Connect with us at events, conferences and seminars.

NDA Hotline

Click here to view Hotline archives.

Video

Vyapak Desai speaking on the danger of deepfakes | Legally Speaking with Tarun Nangia | NewsX

litigation in the future.

- **Mahesh Kumar & Rajesh Simhan**

You can direct your queries or comments to the authors

¹ UAE Exchange Centre Ltd. v. UOI, 2009-TIOL-84-HC-DEL-IT

² *Anurag Jain v. AAR*, [2009] 308 ITR 302 (Mad) relying on the principle laid down by the Supreme Court in *Shreeram Durga Prasad v. Settlement Commission*, [1989] 176 ITR 169

³ The business connection threshold is wider than the PE threshold under the treaty and covers all situations where there is some sort of a real and intimate relationship between the offshore activities of the non-resident with its activities inside India.

DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

April 01, 2025

Vaibhav Parikh, Partner, Nishith Desai Associate on Tech, M&A, and Ease of Doing Business

March 19, 2025

SIAC 2025 Rules: Key changes & Implications

February 18, 2025
