

Practical insights into the taxability of FSC

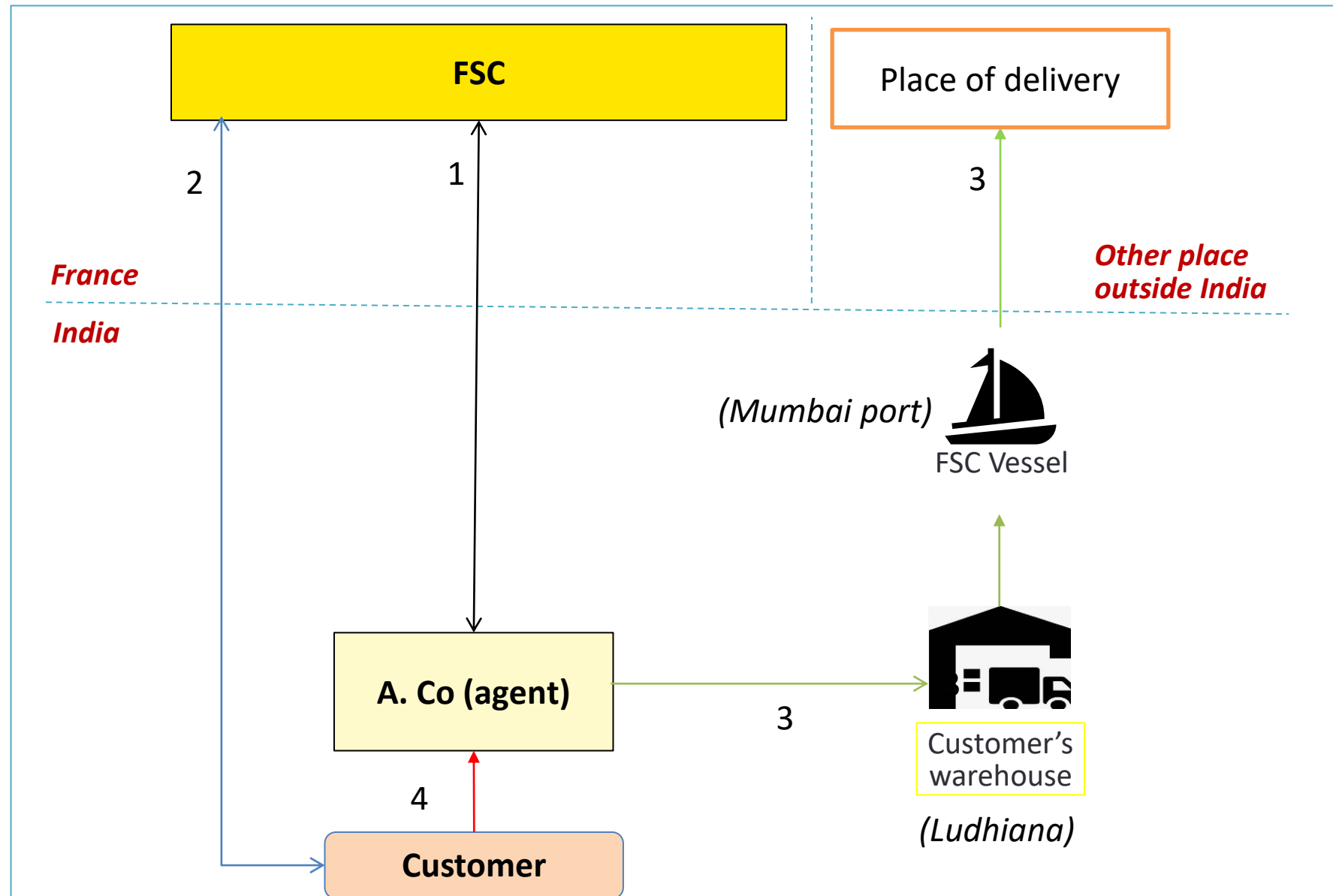
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WIRC, Mumbai
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Case study 1: Income from freight and inland haulage services

Structure



- ↔ Agency agreement for transportation of goods in international traffic
- ↔ Agreement for support services for transportation of goods and inland haulage
- Transportation of goods from exporter's warehouse to destination outside India
- Freight and IHC paid by customer to A.co

Mechanics

1. FSC enters into agreement with an agent India (A.Co) to provide support services for transportation of goods in international traffic and inland haulage
2. Indian customer enter into agreement with FSC for transportation of their goods outside India along with inland haulage services
3. A.Co provides support services for transportation of goods from customer's warehouse place of delivery outside India
4. A.Co collects freight and IHC from Indian customer on behalf of FSC

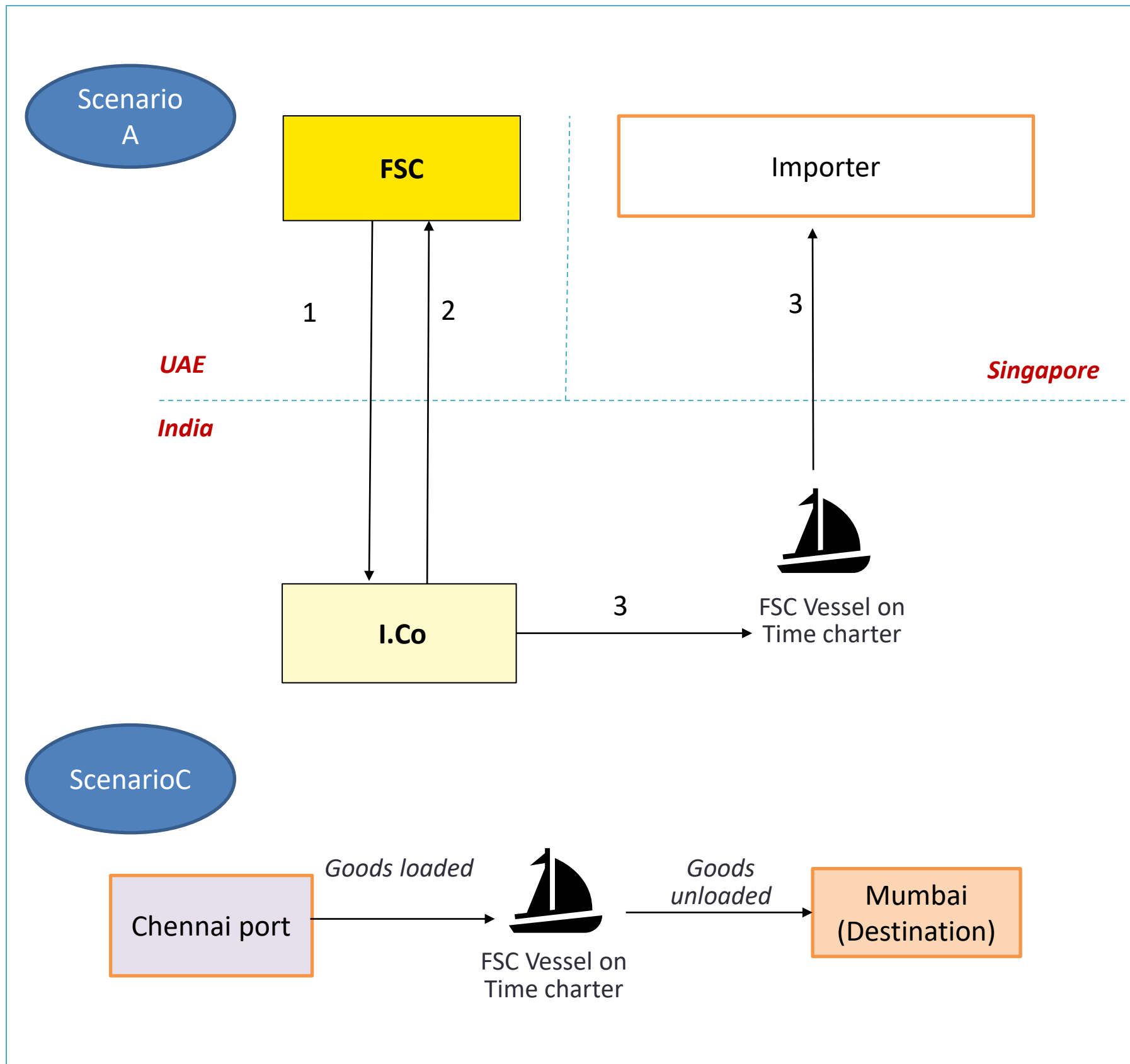
B/L issued by FSC to customer from place of customer's warehouse in India to place outside India

1. (a) Is freight received/receivable taxable for FSC in India?

(b) Whether customer is obligated to deduct TDS on payment of IHC to A.Co?

Case study 2: Income from time charter

Structure



Mechanics

Scenario A:

1. FSC enters into agreement with I.Co to provide its vessel on time-charter for transportation of goods in international traffic
2. I.Co makes payment to FSC towards time charter charges
3. I.Co's export containers are loaded at port in India on the time-charter vessel and transported to Singapore

1. (a) Which DTAA shall be applicable to determine the taxability of time-charter income of FSC?:

- India-UAE
- India- Singapore
- UAE-Singapore

(b) Whether time charter payment by customer shall be taxable for FSC in India?

Scenario B:

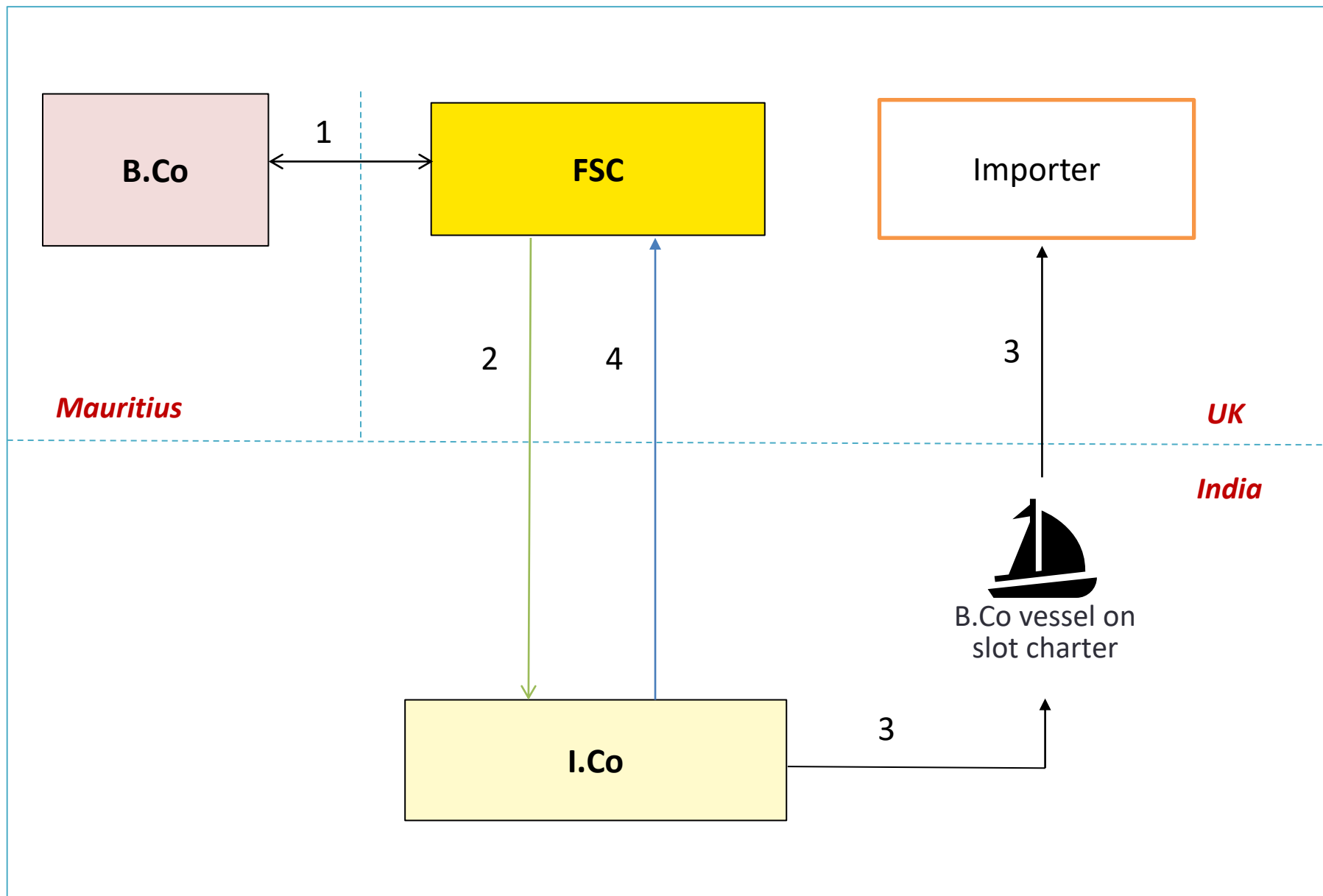
1. Assuming the vessel is on bareboat charter, what will be the taxability of the charter payment for FSC in India?

Scenario C: The vessel in Scenario A plies only between Chennai and Mumbai port only

1. Whether time-charter charges received by FSC under such scenario shall be taxable in India for FSC?

Case study 3: Income from slot charter

Structure



- ←→ Agreement for slot charter in B.Co's vessel by FSC
- Agreement for transportation of goods in international traffic
- I.Co's goods loaded on vessel obtained on slot-charter and are transported outside India
- Payment by I.Co to FSC towards slot charter

Mechanics

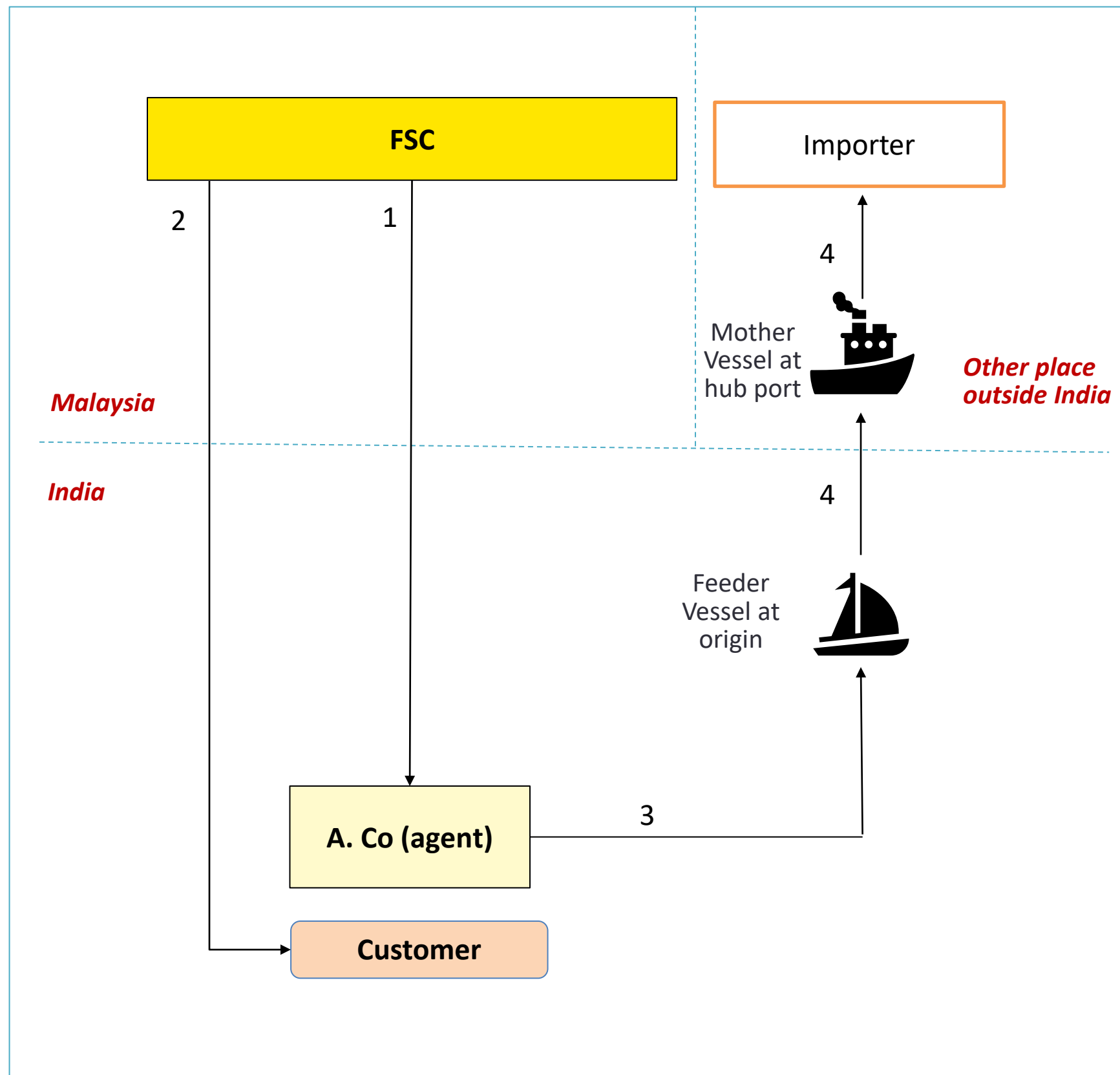
1. FSC, who charters its ships in international traffic, enters into agreement with a Mauritius based company viz. B.Co to avail slot hire facilities obtained on B.Co's vessel
2. I.Co enters into agreement with FSC to transport its goods outside India through FSC's vessel operated on slot charter
3. I.Co goods are loaded on vessel obtained on slot-charter, for transportation outside India
4. I.Co makes payment to FSC towards slot charter

B/L issued by FSC to customer from place of origin in India to destination outside India

Whether slot charter charges paid by I.Co to FSC are taxable for FSC in India?

Case study 4: Income from transshipment

Structure



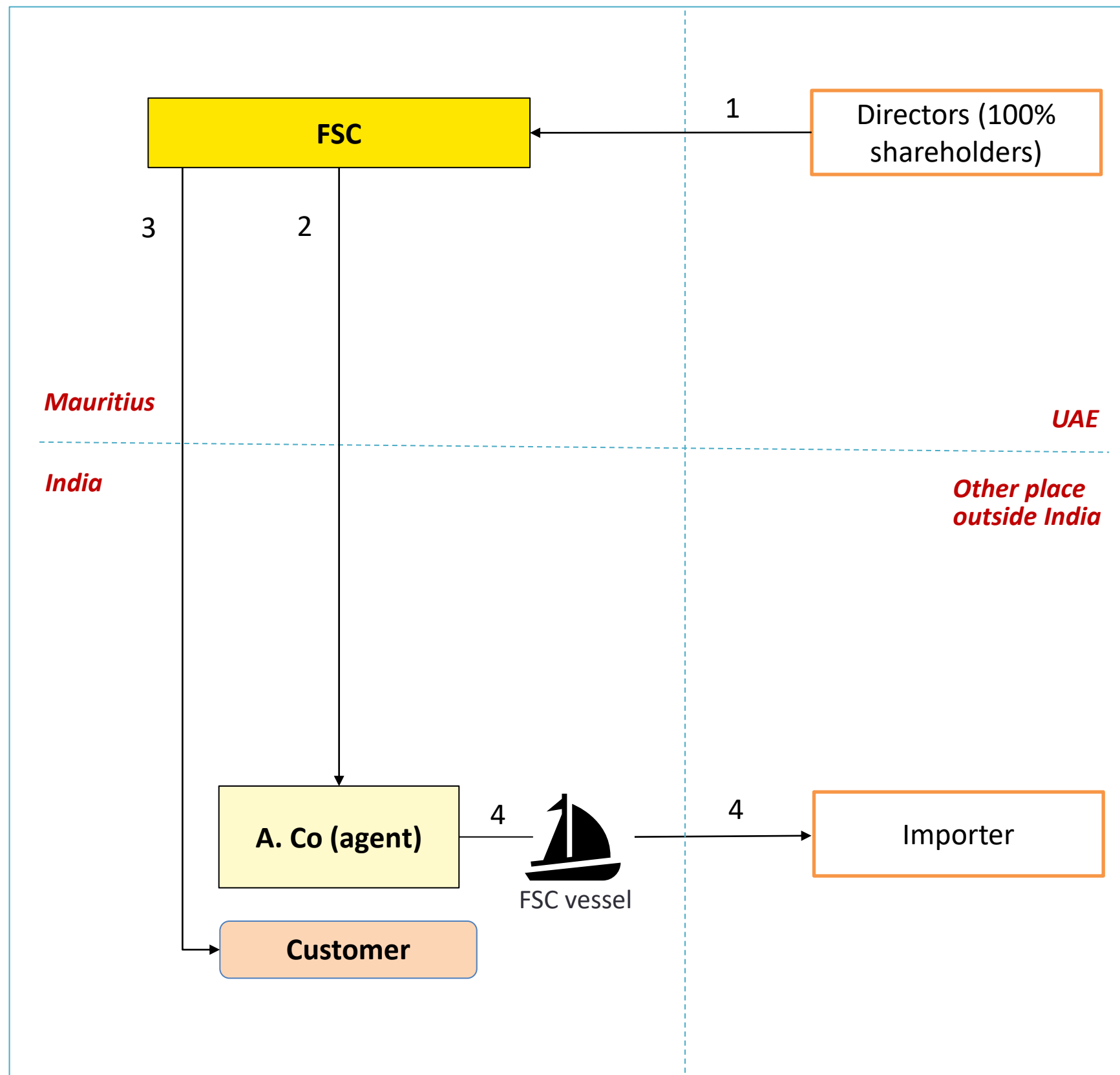
Mechanics

1. Agency agreement between FSC and A.Co for support services for transportation of goods in international traffic
2. Contract between FSC and Indian customers for transportation of goods to destination outside India;
3. Agent in India provides support services for loading of goods in feeder vessel (not owned/pooled/chartered by FSC) at origin by way of slot charter
4. Goods are then loaded from feeder vessel to mother vessel (owned/chartered/pooled by FSC) for transportation to destination outside India

Whether income earned through transportation of goods through feeder vessel owned by third party, is taxable for FSC in India?

Case study 5: POEM located in third country

Structure



Mechanics

1. Directors of FSC based in UAE, hold entire shareholding in FSC
Major policy decisions undertaken in UAE
2. Agency agreement between FSC and A.Co for support services for transportation of goods in international traffic.
3. Contract between FSC and Indian customers for transportation of goods to destination outside India;
4. FSC earns freight income from goods are then transported outside India in FSC vessel

Is freight taxable for FSC in India?



Annexures

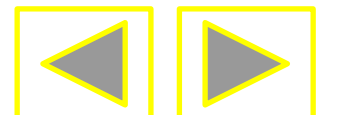
Annexure 1: Shipping Article under India-France DTAA

Relevant provisions of Article 9 under India-France DTAA

1. ***Profits derived by an enterprise of a Contracting State from the operation of ships in international traffic shall be taxable only in that Contracting State.***
2. ***Notwithstanding the provisions of paragraph 1, such profits may be taxed in the other Contracting State from which they are derived, provided the tax so charged shall not exceed:***
 - (a) ***during the first five fiscal years after the entry into force¹ of this Convention, 50 per cent, and***
 - (b) ***during the subsequent five fiscal years, 25 per cent, of the tax otherwise imposed by the internal law of that Contracting State. Subsequently, only the provisions of paragraph 1 shall be applicable.***

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¹ Entry into force of the Convention on 1 August 1994

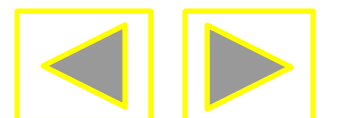


Annexure 2: Shipping Article under India-UAE DTAA

Relevant provisions of Article 8 under India-UAE DTAA

1. *Profits derived by an enterprise of a Contracting State from the operation by that enterprise of ships in international traffic shall be taxable only in that State.*
2. *For the purposes of this Article, profits from the operation of ships in international traffic shall mean profits derived by an enterprise described in paragraph (1) from the transportation by sea of passengers, mail, livestock or goods and shall include :*
 - (a) *the charter or rental of ships incidental to such transportation ;*
 - (b) *the rental of containers and related equipments used in connection with the operation of ships in international traffic;*
 - (c) *the gains derived from the alienation of ships, containers and related equipments owned and operated by the enterprise in international traffic.*

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Annexure 2A: Relevant OECD commentary on 'Operation of ship'

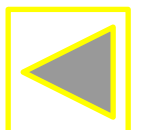
Paras 5 of OECD Commentary¹

*5. Profits obtained by leasing a ship or aircraft on charter fully equipped, crewed and supplied must be treated like the profits from the carriage of passengers or cargo. Otherwise, a great deal of business of shipping or air transport would not come within the scope of the provision. However, **Article 7, and not Article 8, applies to profits from leasing a ship or aircraft on a bare boat charter basis except when it is an ancillary activity of an enterprise engaged in the international operation of ships or aircraft.***

Relevant extract of India position on Article 8 as per OECD Model¹

5.1 India reserves the right to apply Article 12 and not Article 8 to profits from leasing ships or aircraft on a bare charter basis.

¹ OECD Model convention as updated in 2017

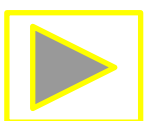


Annexure 3: Shipping Article under India-UK DTAA

Relevant provisions of Article 9 under India-UK DTAA

1. *Income of an enterprise of a Contracting State from the operation of ships in international traffic shall be taxable only in that State.*
2. *The provisions of paragraph 1 of this Article shall **not apply to income from journeys between places which are situated in a Contracting State.***
3. *For the purposes of this Article, income from the operation of ships **includes income derived from the rental on a bareboat basis of ships if such rental income is incidental to the income described in paragraph 1 of this Article.***
4. *Notwithstanding the provisions of Article 7 (business profits) of this Convention, the provisions **of paragraphs 1 and 2** of this Article shall **likewise apply to income of an enterprise of a Contracting State from the use, maintenance or rental of containers** (including trailers and related equipment for the transport of containers) used for the transport of goods or merchandise.*

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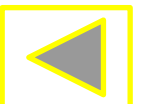


Annexure 4: Shipping Article under India-Malaysia DTAA

Relevant extracts of Article 8 of India- Malaysia DTAA

1. *Profits derived by an enterprise of a Contracting State from the **operation of ships or aircraft in international traffic shall be taxable only in that State***
2. *For the purposes of this Article, profits from the operation of ships or aircraft in international traffic **shall mean** profits derived by an enterprise described in paragraph 1 from the **transportation by sea or air** respectively of passengers, mail, livestock or **goods carried on by the owners or lessees or charterers** of ships or aircraft including:
 - (a) *the sale of tickets for such transportation on behalf of other enterprises; and*
 - (b) *the rental of ships or aircraft incidental to any activity directly connected with such transportation.**

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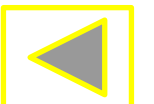


Annexure 5: Shipping Article under India-Mauritius DTAA

Relevant provisions of Article 8 – India Mauritius DTAA

- 1. Profits from the operation of ships or aircraft in international traffic shall be taxable only in **the Contracting State** in which the **place of effective management** of the enterprise is situated.*
- 2. If the place of effective management of a shipping enterprise is aboard a ship, then it shall be deemed to be situated in the Contracting State in which the home harbour of the ship is situated or, if there is no such home harbour, in the Contracting State of which the operator of the ship is resident.*

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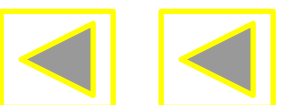


Annexure 6: Relevant OECD commentary on 'Operation of ship'

Paras 6-7 of OECD Commentary¹

6. Profits derived by an enterprise from the transportation of passengers or cargo **otherwise than by ships or aircraft that it operates in international traffic** are covered by the paragraph to the extent that such transportation is **directly connected** with the operation, by that enterprise, of ships or aircraft in international traffic **or is an ancillary activity**. One **example would be that of an enterprise engaged in international transport that would have some of its passengers or cargo transported internationally by ships or aircraft operated by other enterprises**, e.g. under code-sharing or slot-chartering arrangements or to take advantage of an earlier sailing...
7. **A further example** would be that of an enterprise that transports passengers or cargo by ships or aircraft operated in international traffic which undertakes to have those passengers or that cargo picked up in the country where the transport originates or transported or delivered in the country of destination by any mode of **inland transportation operated by other enterprises**. In such a case, any profits derived by the first enterprise from arranging such transportation by other enterprises are covered by the paragraph even though the profits derived by the other enterprises that provide such inland transportation would not be.

¹ OECD Model convention as updated in 2017



Glossary

Abbreviations	Particulars
Act	Income Tax Act,1961
AO	Assessing Officer
DTAA	Double Tax Avoidance Agreement
FSC	Foreign Shipping Companies
IHC	Inland Haulage Charges
OECD	Organization for Economic Co-operation and Development
PE	Permanent Establishment
POEM	Place of Effective management



Thank you

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