



## Supreme Court upholds the taxability of mobilisation fees for oil rigs under section 44BB

Section 44BB of the Income Tax Act, 1961 (Act) provides for an alternative mechanism for computing profits arising to non-resident taxpayers engaged in providing services, facilities or plant and machinery for the prospecting, extraction or production of mineral oils. Under this provision, a non-resident taxpayer is given a choice to apply a computation formula that deems 10% of certain specified amounts set out in section 44BB(2) as his taxable profits from such activities.

In the context of this provision, the Supreme Court ruled that mobilization charges for transportation of oil rigs should form part of the specified amounts determined under section 44BB(2). This decision was rendered while disposing a batch of appeals filed by **Sedco Forex International Inc.** and other taxpayers.

### The Background

The taxpayers in these appeals were foreign companies who had entered into agreements primarily with India's Oil and Natural Gas Corporation (ONGC) for giving their rigs on hire for exploration activities in India. As a part of their agreements, the taxpayers were paid mobilisation fees for mobilisation/movement of their rigs from their overseas locations to the desired site in India.

The taxpayers took the position that:

- a) Such mobilisation fees was in the nature of reimbursement of expenses without any profit element, and that they could not be considered as forming part of the 'amounts' specified under 44BB(2);
- b) In any event, these were in respect of services rendered outside India, and hence, they did not accrue or arise in India under section 5 read with section 9 of the Act.

The tax authorities rejected the above conditions and sought to include such mobilisation fees for computing the deemed profits under section 44BB of the Act.

Appeals by the taxpayers to the Income-tax Appellate Tribunal and the High Court were dismissed, and it was held that:



- a) Payments made towards mobilisation were not compensatory in nature as they were part of the obligation undertaken by the taxpayers under the agreement; and
- b) Section 44BB is a complete code in itself for calculation of profits and gains of the specified business. Therefore, provisions of Sections 5 and 9 of the Act must be excluded if the mechanism thereunder has been opted for.

### **Summary of the Supreme Court's decision:**

#### **On whether the mobilisation fees were in the nature of reimbursement**

The Court rejected the contention of the taxpayers that the mobilisation fees was in the nature of 'reimbursement'. In arriving at this conclusion, it noted that:

- a) The amount was described as a 'mobilisation fee' and not termed as a reimbursement of expenditure;
- b) Mobilisation fee was a fixed amount which could be more or less than the actual expenditure incurred, and that the incurring of expenditure was therefore immaterial;
- c) The contract was indivisible.

#### **On the applicability of sections 5 and 9 of the Act**

The Supreme Court rejected the High Court's view that sections 5 and 9 of the Act were not relevant while undertaking a computation under section 44BB of the Act. It held that section 4 (dealing with the charge of income-tax), and sections 5 and 9 (dealing with the scope of total income taxable in the hands of non-residents) continue to be relevant even if the assessment of the taxpayer's income was being done under section 44BB of the Act.

Having said this, the Court noted that the contention of the taxpayers that section 44BB was only a computational provision was also not entirely correct.

The Court noted that for the purposes of computation under section 44BB, it is necessary that the receipt in consideration must qualify as 'income' under section 5 and that it arises or is deemed to arise in India under section 9 of the Act. As regards the first requirement, the Court held that amounts paid as mobilisation fees are treated as profits and gains of a business. Hence, it would be 'income' under section 5. The Court also noted that section 44BB treats such income as being earned in India fictionally, and hence, the test of section 9 is also satisfied.

In other words, the Court ruled that once an amount is covered within the scope of section 44BB(2), by virtue of the fiction created under section 44BB, it becomes 'income' under sections 5 and 9 as well.

### **Our Comments**

This judgment addresses important issues that have long been controversial in the oil and gas services industry. Although its conclusions may provide some finality on the taxability of mobilisation fees under section 44BB, larger issues surrounding the interplay between the core charging provisions (sections 4, 5 and 9) and other presumptive taxation provisions in the Act may continue to remain contentious.



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