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

Decided on : 10.02.2015

+ **ITA NO.444/2014**

COMMISSIONER OF INCOME TAX-XIIIAppellant

Versus

M/S. ORIENTAL STRUCTURAL ENGINEERS PRIVATE
LIMITED AND KMC CONSTRUCTION PVT. LTD. –JV

.....Respondent

+ **ITA NO.445/2014**

COMMISSIONER OF INCOME TAX-XIIIAppellant

Versus

M/S. ORIENTAL STRUCTURAL ENGINEERS PRIVATE
LIMITED AND GAMMON INDIA LTD.–JV

.....Respondent

Through: Sh. Rohit Madan, Sr. Standing Counsel, for
Revenue in both appeals.

Sh. Rajat Navet, Advocate, for the assesseees in both the
appeals.

CORAM:

HON'BLE MR. JUSTICE S. RAVINDRA BHAT

HON'BLE MR. JUSTICE R.K. GAUBA

MR. JUSTICE S. RAVINDRA BHAT (OPEN COURT)

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1. The question of law which the revenue seeks to urge in these two appeals, being ITA Nos. 444-445/2014, which involve common questions of fact arising from a common order of the Income Tax Appellate Tribunal (ITAT) in ITA Nos. 2691-92/Del/2012 dated 07-02- 2014 is as follows:

“Whether a proportion of the project receipts, commensurate with the risks/performance obligations, should be attributed to the assessee JV to whom tender had been awarded for the project and undertook significant risks and responsibilities for the completion of the project and whether it is allowable for the assessee to divert the entire receipts to its JV partners by designing a sub-contract to that effect?”

2. The assessee in ITA No. 444/2014 is a joint venture (JV) between M/s Oriental Structural Engineers P. Ltd, New Delhi and M/s KMC Construction Ltd. Hyderabad, which was formed to undertake projects awarded by NHAI. The assessee reported NIL income for the relevant years and claimed refunds. The case was processed under Section 143(1) of the Income Tax Act, 1961 (hereafter “the Act”) and later on selected for scrutiny under compulsory scrutiny norms. Therefore, statutory notices were issued to the assessee and served. From the Profit and Loss Account, it was noticed that the assessee received gross receipt of ₹92,31,33,229/-. Against this receipt, the assessee debited an amount of ₹ 90,46,70,560/- towards payment to sub-contractors, i.e. the JV partners itself. Apart from this, the JV paid work contract tax of ₹ 1,84,62,669/- apart from other small expenses like bank charges, professional fees etc. The payment made to sub-contractors was

97.99% of the total receipts. The balance was utilized to make payment for work contract tax, professional fees, audit fees etc.

3. Similarly, the assessee in ITA No. 445/2014 is a joint venture (JV) between M/s Oriental Structural Engineers P. Ltd, New Delhi and M/s Gammon India Ltd., Mumbai, formed to undertake projects awarded by NHAI. The assessee in the said appeal reported NIL income for the relevant years and claimed refunds. The case was processed under Section 143(1) of the Act, and later on selected for scrutiny under compulsory scrutiny norms. Statutory notices were issued to the assessee and served. From the Profit and Loss Account, it was noticed that the assessee received gross receipt of ₹ 9,98,86,286/-. Against this receipt, the assessee debited an amount of ₹ 9,88,52,617/- towards payment to sub-contractors, i.e. the JV partners itself. Apart from this, the JV paid VAT/Sales Tax of ₹ 8,30,907/- apart from other small expenses like bank charges, professional fees etc. The payment made to sub-contractors was 98.96% of the total receipts. The balance was utilized to make payment for VAT/Sales Tax, audit fees etc.

4. The AO, on the basis of his evaluation of the risk and responsibilities undertaken by the assessee JV, the liabilities it undertook while accepting the contract awarded to it by NHAI, the sub-contracting of the said award to its partners and other such related factors, formed the view that the JV partners had,

"for their own purposes and benefits, not declared the income/profits in the hand of the assessee JV, which is a separate taxable entity as far as Income Tax Act, 1961, is concerned and have deliberately included such income/profits in their books in

order that the exact profits are not distinguishable easily in the complexities involved in their books, given the wide range of their respective business activities and operations."

The AO considered it

"reasonable and appropriate to assessee (sic) the income in the hands of the assessee JV at 5% of the gross contractual receipts."

5. The AO's decisions were challenged before the Commissioner (Appeals) - i.e. CIT (A). The latter, by his order, reversed the findings of the AO and held *inter alia*, after analyzing the contents of the MOU of the assessee, as follows:

"The constituent of this JV are separate legal entities distinct from the JV. It is a fact that the JV constituents are already taxed at maximum marginal rate. Taxing the AOP would tantamount to double taxation. The assessing officer has applied ad hoc estimated rate of profit to the gross receipts without rejecting the books of accounts of the appellant."

6. The ITAT dismissed the appeals of the revenue for AY 2009-10 by relying upon its own order in the case of the assessee for AYs 2006-07 to 2008-09. In that order, ITAT had held that the issue raised in the appeals was decided by this Court in the assessee's favour for the AYs 2004-05 & 2005-06 and the Supreme Court had dismissed the Special Leave Petition filed by the revenue.

7. It is argued on behalf of the revenue that a careful analysis of the agreement constituting the JV showed that it was meant to operate as a separate entity and not merely to facilitate the JV partners to successfully bid for the contract. It, therefore, results in a situation where a proportion of

the project receipts, commensurate with the risks/performance obligations, should be attributed to the assessee to whom tender had been awarded for the project and undertook significant risks and responsibilities for the completion of the project and it is not allowable for the assessee JV to divert the entire receipts to its JV partners by designing a sub-contract to that effect.

8. Both the ITAT and the CIT (A) took note of the salient aspects of the JV agreement. The relevant discussions in the order of the CIT (A) are extracted below:

"d) Sub contract agreement with lead J.V. Partner M/s Oriental Structural Engineers Pvt. Ltd.

Based on the above role of Joint Venture Partners, a Sub-contract Agreement dated 07.02.2005 was entered between Joint Venture and its lead partner as a sub-contractor, wherein it is clearly stated: -

Para 2 Scope of Works to be performed by the sub-contractors

Para 2.1 "That Sub-Contractor shall execute all items of work contained in Bills of quantities as per Annexure 'A' to the extent of 50% (Approximately) value of the contract amount entered into the Joint Venture with the employer"

Para 4 PAYMENT/ DISBURSEMENT

Para 4.1: All payments for the executed items in sub-contractor bill of quantities and those received by the Joint Venture from the employer in connection with the main contract shall be passed on to the sub-contractor subject to deduction of income tax on sub contractor payment received within 1 day after receipt of the payment by the joint venture from the employer". Copy of Sub-contract Agreement Copy filed placed on record.

e) Sub contract agreement with J.V. Partner M/s KMC Constructions Ltd.

Based on the above role of Joint Venture Partners, a Sub-contract Agreement (MOU for Division of Contract Work) dated 15.03.2005 was entered between Joint Venture and its partner as a sub-contractor, wherein it is clearly stated:-

Para - 2 SCOPE OF WORKS TO BE PERFORMED BY THE PARTIES OF THE SECOND (M/s KMC Constructions Ltd.) AND THIRD PARTS (M/s Oriental Structural Engineers Pvt. Ltd.)

Para 2.1 “That party of the second part shall execute all items of work contained in bill of quantities as per Annexure ‘A’.

Para 2.2 “That party of the third part shall execute all items of work contained in Bill of Quantities as per Annexure ‘B’.

Para 2.3 “That work is divided among the parties of the second and third parts on the promise assumption or understanding that each of the parties are executing 50% of the project and shall receive 50% of the contract amount.”

Para 4 PAYMENT/DISTRIBUTION

Para 4.1 “All payment for the executed item in the bills of quantities parties of the second and third parts and those received by the JV from the Employer in connection with the Main contract shall be passed on to the parties of the second and third parts within one day after receipt of the payment by the JV from the Employer.

3. OPERATION OF THE CONTRACT WORK AWARDED TO JV

Based on these conditions of the JV agreements and sub contract agreements all the works were executed by JV partners at the rate at which the work was awarded to JV and paid to JV Partners as sub-contractors by J.V. On account of this JV will not have any income as the contracts were being executed by JV partners as sub-contractors on behalf of JV. The Joint Venture

does not have any staff, plant & machinery, financial resources or any other set up to execute the work; the partners have not invested any money in the Joint Venture. Joint Venture is basically an arrangement for participating in bidding process to take place for the work as one of the JV, partner OSE Pvt. Ltd. was having expertise in construction of Roads/ Highways and the other JV partner, KMC Constructions Ltd. was having expertise in construction of bridges, culverts and related works. The work was done by JV partners themselves & they billed to JV at the rates at which JV was awarded the contract by NHAI and JV acting as a conduit to raise the bill on NHAI for same amount and passes on to respective JV partners as soon as it was received from NHAI."

9. In the assessee's case for assessment year 2004-05, this court had the occasion to consider the issue in ITA No. 146/2010 decided on 11.02.2010. The relevant extracts from the said judgment are as reproduced below:

"The Tribunal returned a clear finding of fact indicating that the payments made by the joint venture / assessee to its partners was not excessive and, therefore, Section 40A(2) of the said Act would not come into play. The Tribunal held as a fact that the arrangement between the parties was clear that after receipt of the contract from the National Highways Authority of India, the work was to be executed by the joint venture members directly and no effort was to be made by the assessee/ joint venture itself in the execution of the contract. It was, therefore, found by the Tribunal that the assessee was created as a joint venture for obtaining works from the National Highways Authority of India without there being any requirement or necessity of the joint venture to carry out any activity itself. In fact, all the activities were to be carried out by the aforesaid two members of the joint venture and for which they were to be remunerated."

10. At the outset, this court notices that the issue sought to be argued on behalf of the revenue stands covered by a decision of a Division Bench,

which made references to several other judgments, including those of the Supreme Court when a "person" is said to exist as an association of persons. In that decision, i.e. *Linde AG, Linde Engineering Division and Anr. v. Deputy Director of Income Tax* W.P. (C) No. 3914/2012 & CM No. 8187/2012, reported in [2014] 365 ITR 1 (Delhi), first, the Court considered the definition of Association of Persons (Section 2 (31)) and then analyzed it in the following terms:

“(31) ‘person’ includes—
(i) an individual,
(ii) a Hindu undivided family,
(iii) a company,
(iv) a firm,
(v) an association of persons or a body of individuals, whether incorporated or not,
(vi) a local authority, and
(vii) every artificial juridical person, not falling within any of the preceding sub-clauses;
Explanation.— For the purposes of this clause, an association of persons or a body of individuals or a local authority or an artificial juridical person shall be deemed to be a person, whether or not such person or body or authority or juridical person was formed or established or incorporated with the object of deriving income, profits or gains;”
27. Section 3(42) of the General Clauses Act, 1897 defines a ‘person’ to include “any company or association or body of individuals, whether incorporated or not”.

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29. The Supreme Court in the case of *G. Murugesan and Brothers v. Commissioner of Income Tax, Madras*: (1973) 4 SCC 211 made the following observations:-

For forming an 'Association of Persons', the members of the association must join together for the purpose of producing an income. An 'Association of Persons' can be formed only when two or more individuals voluntarily combine together for a certain purpose. Hence volition on the part of the member of the association is an essential ingredient. It is true that even a minor can join an 'Association of Persons' if his lawful guardian gives his consent. In the case of receiving dividends from shares, where there is no question of any management, it is difficult to draw an inference that two more shareholders functioned as an 'Association of Persons' from the mere fact that they jointly own one or more shares, and jointly receive the dividends declared. Those circumstances do not by themselves go to show that they acted as an 'Association of Persons'." (emphasis supplied)

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34. ...It is, thus, essential that an Association of Persons has the trappings of a partnership for conducting the joint enterprise which makes it amenable to be treated as a separate taxable entity. A person carrying on business may in the usual course cooperate with others for a common purpose. In many instances, the test of common purpose and common action, if literally applied, may also hold true. However, treating every instance of such cooperation between two or more persons as resulting in an Association of Persons would militate against the purpose of considering an association as a separate tax entity. Whether an arrangement or collaborative exercise between two or more persons results in constituting an Association of Persons as a separate taxable entity would depend on the facts of each case including the nature and the extent of collaboration between them. The Supreme Court in Indira Balkrishna (supra) had also clarified that:- "there is no formula of universal application as to what facts, how many of them and of what nature are necessary to come to a conclusion that there is an association of persons within the meaning of Section 3.

35. It is obvious that unless the facts lead to a conclusion that there is sufficient joint participation for a common enterprise, it would not be appropriate to treat two or more persons as an Association of Persons for the purposes of assessing them as a separate taxable entity. A mere cooperation of one person with another in serving one's business objective would not be sufficient to constitute an Association of Persons merely because the business interests are common. A common enterprise, which is managed through some degree of joint participation, is an essential condition for constituting an Association of Persons.

36. It follows from the above discussions that before an association can be considered as a separate taxable entity (i.e. an Association of Persons), the same must exhibit the following essential features:

- (i) must be constituted by two or more persons.
- (ii) the constituent members must have come together for a common purpose.
- (iii) the association must move by common action and there must be some scheme of common management.
- (iv) the cooperation and association amongst the constituent members must not be perfunctory and/or merely in form. The association amongst members must be real and substantial which is sufficient to treat the association as a separate homogenous taxable entity.”

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47. It is material to note that even, as per the terms of the Contract, the scope of work to be executed by Linde and Samsung was separate and was accordingly specified in the annexures to the Contract. The payments to be made for separate items of work were also specified. The currency in which the payments were to be made was also separately indicated. Thus, insofar as execution of the work was concerned, even OPAL recognised that different items constituting the Contract would be performed independently by Linde and Samsung. The consideration for the work performed was to be made directly to

the concerned member of the Consortium in accordance with the work performed by him. Annexure C of the Contract specified the payment schedule i.e. the amount to be paid for the supply of goods and services rendered by both the members of consortium. Linde and Samsung were to be paid on the basis of the separate invoices raised by them respectively. There was no arrangement for sharing of profits and losses between Linde and Samsung. And, each of them would make profits or incur losses based on the price as agreed by them and the costs incurred by them for performance of the contract falling within their independent scope of work.

48. *It follows from the above, that Linde and Samsung had joined together to (a) bid for the contract; (b) present a façade of a consortium to OPAL for execution of the contract and accept joint and several liability towards OPAL for due performance of the contract and completion of the project; and (c) put in place a management structure for inter se coordination and execution of the project. However, in all other respects, both Linde and Samsung were independent of each other and were responsible for their own deliverables under the Contract, without reference to each other.”*

11. In the present case too, the Court is of opinion that the consistent and concurring opinions of CIT (A) and ITAT were that the JV was formed only to secure the contract, in terms of which the scope of each JV partner's task was distinctly outlined. Further, the entire work was split between the two JV partners; they completed the task, through sub-contracts and were responsible for the satisfaction of the NHAI. Therefore, applying the principles of the law declared in *Linde AG, Linde Engineering division and Anr*, it is held that the ITAT did not fall into error of law, in holding that the JV was not an association of persons and liable to be taxed on that basis.

The question of law framed is accordingly answered in favour of the assessee and against revenue.

12. For the foregoing reasons, the appeal has to fail; it is dismissed.

S. RAVINDRA BHAT
(JUDGE)

R.K. GAUBA
(JUDGE)

FEBRUARY 10, 2015

