

(i)

- The Inland Revenue Act No. 24 of 2017 (“IRA”) in section 4 provides that a non-resident person is liable to pay income tax in Sri Lanka on the profits and income arising in or derived from a source in Sri Lanka.
- Section 75 (2) of the IRA specifies that where Sri Lanka has entered into a double tax agreement with another country, the provisions of such DTA will supersede the domestic law.
- Sri Lanka has entered into a double tax agreement with India and the articles of such DTA will apply to transactions between Seiki India and customers in Sri Lanka.
- Section 75 (3) specifies that any concessions/exemptions available under the DTA will only be available to an entity where more than 50% of the ownership of that entity is held by individuals in that State. However, this restriction will not apply as per section 75(4) if the entity is listed on a stock exchange in the other contracting state.
- According to the facts provided, Seiki India is a listed company based in India. Therefore, we do not have to check on the ultimate ownership of Seiki India when applying the provisions of the DTA.
- Article 7 of the DTA specifies that an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein.
- Article 5 explains that a permanent establishment (“PE”) will be created where Seiki India has a fixed place of business through which business of the enterprise is wholly or partly carried on in Sri Lanka.

Model 1 : Lease model

On profits arising from the lease of construction machinery to customers in Sri Lanka

- In this model, it is necessary to ascertain whether Seiki India will have a fixed place of business in Sri Lanka.
- Seiki India does not create any of the fixed places of business listed in Article 5(2).
- Seiki India will lease the construction equipment to the customers in Sri Lanka, and during the lease the responsibility and control of the machinery will be with the customer. However, the ownership of the machinery will be with Seiki India.
- Seiki India will have equipment it owns in Sri Lanka. However, this equipment will be moved from place to place for construction purposes. Therefore, Seiki India cannot be considered to have a fixed place of business in Sri Lanka.
- Therefore, Seiki India will not create a PE in Sri Lanka and therefore, it will not be liable to pay income tax in Sri Lanka.

On any profit on the supply of support services to customers in Sri Lanka

- Seiki India will not provide support services, but it will appoint a few independent dealers in Sri Lanka, to provide the support services.
- Such independent dealers will directly charge their fee from the customers for such services and Seiki India will not be contractually providing such services.
- Therefore, no PE will be created due to the presence of the independent dealers for Seiki India. Therefore, no tax liability would arise.

Model 2 : Sale model

On profits arising from the sale of construction machinery to customers in Sri Lanka

- The contract negotiations with the customers in Sri Lanka will take place remotely. Once the orders are placed, Seiki India will directly sell the machinery to the customers in Sri Lanka and invoice for it.
- In this model the goods are directly being transferred from Seiki India to the customers in Sri Lanka which will be considered as a direct sale or trading transaction.
- Seiki India will not create a PE under the DTA Article 5.
- Therefore, Seiki India will not be liable to pay income tax in Sri Lanka.

On any profit on the supply of support services to customers in Sri Lanka

- Article 5(5) specifies that a PE is deemed to be created in certain situations given in that section.
- It includes a person carrying on certain activities on behalf of the non-resident person where that person habitually secures orders in the first mentioned State, wholly or almost wholly for the enterprise.
- Based on the facts given, the distributor provides support services to customers of Seiki India and such services are exclusively provided to customers of Seiki India. Further, Seiki India provides the detailed instructions and manuals to provide such support services.
- Therefore, it can be considered that since the distributor is acting in this manner on behalf of Seiki India, that Seiki India will be deemed to create a PE in Sri Lanka.
- Therefore, Seiki India will be liable to pay income tax in Sri Lanka on the profits that are attributable to such PE in Sri Lanka.

(iii)

- Section 85 (1A) provides that a person making a payment with a source in Sri Lanka to a non resident person must withhold tax at the rate specified in the First schedule.
- This includes a payment of technical service fee.
- Section 73 defines a “technical service fee” as “a service fee for managerial, technical, or consultancy services, including a fee for the provision of services of technical or other personnel.”
- The first schedule specifies that the rate of withholding tax applicable for such payment should be 14%.
- The DTA however, in Article 12(2) provides that technical services may also be taxed in the contracting State in which they arise, but the tax so charge should not exceed 10% of the gross amount of the fees for technical services.
- Therefore, since the DTA provides a rate lower than the domestic law, the DTA will prevail. Therefore, any technical service fee paid from Sri Lanka to Seiki India will be subject to withholding tax at 10%.