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SC confirms Fixed Place PE of Hyatt UAE observing degree of control & supervision and other factors; emphasises on 'no one formula' for Fixed Place PE applying 'Formula One'

Snapshot

Whether the foreign entities activities constitute a Permanent Establishment ('PE') has, as a concept always been as clear as mud. This ruling provides clarity on how the foreign entities' activities constitute a fixed place PE, but at the same time it might also open a "Pandora's box".

By applying the 'substance over form' doctrine while dissecting the terms of the service agreement between the foreign and the Indian entity, the Supreme Court concluded that the taxpayer had a fixed place PE in India. This decision emphasizes the importance of examining whether the foreign enterprise's conduct indicates that it is operating its business in India through the Indian entity's premises.

This ruling shall have far-reaching implications on foreign taxpayers operating in India, particularly enterprises operating through brand control agreements, prompting them to reassess their PE exposure in India. The Supreme Court's decision reflects an evolving understanding of PE establishment in response to changing business models. Notably, this judgment sets a stringent benchmark for evaluating PE constitution, even surpassing the standards set in earlier similar cases.

Background & Context

The Hon'ble Supreme Court delivers another landmark ruling on the constitution of Permanent Establishment ('PE') by Foreign entities in India. The case reinforces the Indian judiciary's emphasis on the 'substance over form' approach and a holistic evaluation in PE analysis, focusing not merely on formal presence of a PE, but also whether the entity is acting in a manner akin to having one. This Supreme Court's judgment has shifted the focus from 'dedicated physical place' to 'activities of the foreign entities in India' for evaluating Fixed Place PE in the evolving global tax landscape. The present article attempts to explain the case and share a few thoughts on the subject.

In the present case[1], the taxpayer, Hyatt International Southwest Asia Limited, tax resident of UAE, entered into Strategic Oversight Services Agreements ('SOSA') to provide strategic planning services and "know-how" to two Indian entities to ensure the hotels of the entities were developed and operated as an efficient & high-quality international full-service establishments. These agreements were notably long-term, stipulating a twenty-year term from the effective date, with a provision for extension by an additional ten years through mutual agreement.

For the AY 2009-10, the taxpayer filed its return declaring 'Nil' income and claiming a refund. Following scrutiny, the AO held that the taxpayer's activities constituted a business connection under Section 9(1)(i) of the Income-tax Act, 1961 (the 'Act'), and a PE under Article 5 of the India-UAE DTAA. On same grounds, appeals were also filed by the taxpayer for

[1] *Hyatt International Southwest Asia Ltd vs. ADIT (Civil Application No. 9767 to 9773 of 2025) (SC)*

different years wherein the AO's view was upheld by the ITAT and also the Hon'ble High Court of Delhi. The Tribunal and HC heavily relied on the judgement of SC in case of *Formula One*[2] World Championship Limited v. CIT (Civil Appeal Nos. 3849 to 3851 of 2017). Hence aggrieved by the order of High Court, taxpayer preferred an appeal before the Hon'ble Supreme Court (the 'SC').

The core question before the SC was whether taxpayer had a PE in India under Article 5(1) of the Indo-UAE DTAA, and consequently, whether its income derived from SOSA was taxable in India.

Arguments of the Taxpayer

Against the contentions raised by the Revenue that the taxpayer had a PE in India, the taxpayer refuted the claim citing multiple counter arguments. It vehemently contented that it entered into SOSA with each hotel owner individually wherein it is explicitly stipulated that it shall render services from Dubai and not obligated to send or station any employee in India. However, only on occasional and temporary basis, it may send its employees to India.

The taxpayer further contended that it did not form any Fixed Place PE in India as there was no designated space or office at the hotel premises at its disposal. Further, the ownership and operational control of the hotel remained entirely with the Indian entity, as per the SOSA, and it was not involved in the daily management of hotels. To sum it up, the taxpayer's argument hinged on the following facts:

- It did not have any Fixed place of business, office or branch in India,
- There was no specific or reserved place in the Hotel for the employees of the taxpayer,
- Absence of ownership or exclusive use of hotel space,
- There was no control of the taxpayer over the hotel premises,
- Taxpayer's employees visited India occasionally and on temporary basis,
- No employees stayed in India exceeding 9 months threshold as required under Article 5(2)(i) of India-UAE DTAA,
- Taxpayer was only involved in policy decisions and there was no involvement in day-to-day business operations which was carried out by Indian entities,
- Visits by the taxpayer's employees in India were intended to ensure brand uniformity and quality compliance.

Accordingly, the taxpayer contended that the facts of Formula One are distinguishable from those of the present case, thus the precedents set therein were not applicable in the taxpayer's case. Basis above, taxpayer pleaded before the Hon'ble SC that PE was not established in India and accordingly, income derived from SOSA was not taxable in India.

Findings of the Hon'ble Supreme Court

Dissecting the facts of the agreement

The Hon'ble Supreme Court meticulously reviewed SOSA and heftily relied on the facts mentioned therein. Basis the said analysis, the SC observed as under:

- SOSA is to remain in force for a term of 20 years with possibility extension of 10 years,
- The taxpayer is vested with complete control and discretion in formulating and establishing plans for all aspects including daily operations,
- The taxpayer assigned its personnel to the hotel without requiring the owner's consent,
- The taxpayer has the authority to appoint and supervise non-local General Manager and other key personnel,
- The taxpayer controls pricing, branding, and marketing strategies of the Indian entities,

[2] *Formula One World Championship Limited v. CIT (Civil Appeal Nos. 3849 to 3851 of 2017) (SC)*

- The taxpayer has the authority to frame policies for managing operational bank accounts of the hotel
- The taxpayer is eligible for a guaranteed fees linked with commercial profits of the Indian entity,

Basis the above facts, the SC was of the view that this degree of control and supervision clearly surpasses a mere advisory capacity and indicates that the taxpayer was an active participant in the core operational activities of the hotel. Accordingly, the Court concluded that the taxpayer's role "was not confined to mere policy formulation" but conferred upon it a "continuing and enforceable right to implement its policies and ensure compliance in all operational aspects of the hotel". Accordingly, the SC noted that the activities being carried out by the taxpayer clearly transcends a mere advisory role and aligns with Fixed Place PE principles.

Analyzing the 'Disposal Test'

In line of the above observation, the SC evaluated the concept of Fixed Place PE and stated that the two most important factor to constitute a Fixed Place PE are – 1) the place to be at the disposal of the taxpayer, and 2) the business of the taxpayer to be carried on through such place. The SC stressed on the 'Disposal Test' concept defining it as the enterprise's right to use the premises in such a way that enables it to carry on its business activities.

Relying on its ruling in Formula One (*Supra*) for the discussion of Disposal Test and thereby Fixed Place PE, the SC held that there is no straight-jacket formula which may be applied to all cases for determining it and it needs to be seen on case-to-case basis.

Considering the powers vested with the taxpayer, the SC concluded that the taxpayer exercised pervasive and enforceable control over the hotel's strategic, operational, and financial dimensions and thus these rights go well beyond mere consultancy and indicates that the taxpayer was an active participant in the core operational activities of the hotel.

Further, the SC also noted that the facts involved in the case of the taxpayer satisfied the three core attributes of PE as discussed in the case of Formula One (Supra), namely – Stability, Productivity and Dependence.

SC on non-exclusive possession of premises

Further, the Court explicitly rejected the taxpayer's argument that the absence of an exclusive or designated physical space within the hotel precluded a PE, reiterating Formula One's principle that "exclusive possession is not essential; temporary or shared use of space is sufficient, provided business is carried on through that space". This reiterates the position that the courts interpret "fixed" element of a PE as the enduring nature of the business activity and the right to use a location for that activity, rather than strict physical permanence or exclusivity of the foreign entity's own dedicated space.

Conclusion of Fixed Place PE

After analysing the above facts in the context of Fixed Place PE, the SC was of the view that the taxpayer was responsible for activities directly contributing to the local entity's primary revenue-generating operations, particularly when linked to profit-sharing or pervasive control. This clearly indicates that the taxpayer's involvement went beyond mere "auxiliary" services, instead reflecting a significant role in the entity's core business activities. Given the taxpayer's conduct in India, involving continuous participation in the local entity's business activities, a fixed place PE would be constituted following the "substance over form" doctrine.

It is interesting to note that while negating the taxpayer's argument that none of its personnel were in India for a period exceeding 9 months, the SC held that for evaluating Service PE, the intermittent presence or return of employees becomes insignificant once it is found that there is "continuity in the business presence in aggregate".

KCM Comments

Evolving Judicial Interpretation of Permanent Establishment in India

Indian judicial authorities have increasingly adopted a substance-over-form approach in determining the existence of a Permanent Establishment or Business Connection of foreign entities in India. In the landmark Formula One(*Supra*) case, the SC held that even a one-day use of the race circuit constituted a Fixed Place PE stressing on control over the premises and operations during the event and given a new perspective to the *'Permanency Test'* in Fixed Place PE. In another case of *Volkswagen*[3], the Mumbai Tribunal acknowledged the existence of a Business Connection in India even though the event took place outside the country, considering the event was India-centric targeting primarily Indian audiences. And now the SC's interpretation in the present case wherein one can see shift from strict, literal reading to a more nuanced, fact-driven exercise again considering the economic substance and functional role of the foreign enterprise's activities in India at large. This evolving judicial approach reflects a more assertive stance by Indian authorities in attributing a fair share of multinational profits to India, based on actual economic contribution and presence.

Whether the taxpayer carries 'its business' in India?

It can be seen that the SC has heavily relied on its decision in case of Formula One (*Supra*) while evaluating whether a fixed place of business or PE has been constituted in India in the case of the taxpayer. Considering the operational and managerial activities carried out by the taxpayer in India, the SC held that it meets the criteria of Fixed Place PE – particularly the factor that the taxpayer controls the hotel premises & carries its business through such hotel premises.

The concept of fixed place PE resides primarily on two essential conditions: (a) the place must be "at the disposal" of the foreign enterprise and (b) the business of the foreign enterprise must be carried on through that place. While the Supreme Court provided a detailed analysis of the 'Disposal Test' — emphasizing that the taxpayer had control over the premises and authority over the hotel's operational functions, it did not delve deeper into how Taxpayer's business was conducted from India. Additional clarity on this aspect would have provided valuable insight into the basis for the Court's conclusion that the taxpayer's activities in India were "core business activities" rather than merely "auxiliary or preparatory".

This raises an important question: if service fees are linked to profits of the Indian entities coupled with the fact that the taxpayer is involved in day-to-day business operation of the Indian entities, can it be concluded that taxpayer is indeed carrying out its business in India? While the issue of what constitutes business of taxpayer in context of Fixed Place PE remains debatable even in the global context, the SC appears to have regarded this issue as settled. Interestingly, similar linkage of fees to revenue / profits of the Indian entities is generally seen under several arrangements such as franchise model arrangements, thus in light of SC ruling should such franchise model arrangements now be examined from PE perspective provided other conditions of Fixed Place PE also gets triggered?

Fixed Place PE vs. Service PE

While evaluating the principles of PE in the global context, it is generally understood that when a MNC provides services in the source country through its employees, who remain on the payroll of, or under lien to, the MNC— a service PE may arise. This principle was also affirmed by the SC in the case of Morgan Stanley[4] (Civil Appeal Nos. 2914 and 2915 of 2007).

[3] *Volkswagen Finance Pvt Ltd v. ITO [ITA No. 2195/Mum/2017]*

[4] *DIT (Int. Tax) v. Morgan Stanley & Co. (Civil Appeal Nos. 2914 and 2915 of 2007) (SC)*

However, in the present case it is interesting to note that the Hon'ble SC didn't evaluate the Service PE aspect in depth and considered the facts only from Fixed Place PE context. Notable, the court itself acknowledged in the ruling that "typically, trading operations require a continuously used fixed place, whereas service-oriented businesses may not". Given the taxpayer's involvement in rendering services, the Court's decision to conclude that the taxpayer's activities constituted a Fixed Place PE in India without evaluating Service PE comes as a surprise to many.

Interpretation of Service PE threshold

It is noteworthy that towards the end of its ruling, the SC addressed the taxpayer's key argument—that none of its employees remained in India for a period exceeding nine months, and therefore, no PE should arise under the Service PE clause of the India-UAE DTAA. In this regard, the Court took an interesting position, holding that for the purposes of Service PE, the relevant factor is the "continuity of the business presence in aggregate" in the source country and that the duration of stay of individual employees is not determinative of PE existence. Notably, the term "continuity of business presence in aggregate" lacks a specific definition in both the India-UAE DTAA and the Act. This ambiguity may lead to increased litigation in the future due to differing interpretations.

While it is a well-established principle that continuity of business presence is critical when assessing an Installation/Construction PE, the SC's extension of this reasoning to Service PE comes as a surprise for tax Practitioners and experts in this domain. Traditionally, the determination of a Service PE is based on the number of days for which employees are physically present in India, rather than an aggregated assessment of business continuity. Given the SC's interpretation, it is worthwhile to examine how different Indian DTAAs define and frame the concept of Service PE.

Whether intra-group arrangements now to be examined from PE Lens?

In the present case, the taxpayer provides services to Hyatt group hotels to ensure brand uniformity and adherence to quality standards across the chain. To facilitate these services, the taxpayer enters into intra-group service agreements with group entities for which it receives service fees. This model is commonly followed by MNCs globally, where a designated group company is entrusted with maintaining the brand's consistency and operational standards. However, in light of the principles laid down by the Supreme Court in the aforementioned ruling, such intra-group arrangements may now come under radar of PE wherein the Revenue authorities are likely to challenge these arrangements.

Conclusion

The ruling serves a critical reminder that the existence of a PE is a fact specific determination and legal form does not override economic substance in such determination. The extent of control, strategic decision making and influence exercised were viewed as critical determining factors, not just the physical access to, or formal right to use, a dedicated place of business in India.

This ruling serves as a siren call for companies in the service sector, particularly those operating through brand control agreements with foreign enterprises, to reassess their position regarding the constitution of a fixed place PE in India. The judgment reinforces the Supreme Court's consistent approach, as seen in cases like Formula One, where substance prevails over form, and each case's facts are evaluated holistically. Interpretation of law / DTAA has to be done taking into consideration changing times and evolving business situation/model.

Also, the ruling may be seen as a welcome development for the Revenue authorities, as it effectively empowers them to scrutinize every arrangement from PE perspective. Conversely, for taxpayers, the ruling raises critical concerns regarding the manner in which business operations are to be conducted in India, as each step or activity could become pivotal in the Revenue's assessment of a PE.

For further analysis and discussion, you may please reach out to us.

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