



**EXPANDING CONTOURS OF PERMANENT ESTABLISHMENT THROUGH *HYATT INTERNATIONAL SOUTHWEST ASIA LTD. V. ADDITIONAL DIRECTOR OF INCOME TAX* BY HON'BLE SUPREME COURT**

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### ABSTRACT

The ever-so discussed issue of Permanent Establishment has reigned in a new development through the decision of the Hon'ble Supreme Court in the case of *Hyatt International Southwest Asia Ltd. v. Additional Director of Income Tax*. The judgement has erupted the discussion on changing dimensions of 'fixed place of business' of a foreign entity in India, inviting the scrutiny of tax audits and assessments. The significance of choosing of economic substance of an entity over its legal form for tax purposes ushers in a new era of scrutinizing the overall operations of a foreign entity and its business presence in India. This is essentially of critical importance when understanding tax implications that can be imposed on an entity. Tax treaties have a concept of Permanent Establishment where profits of a foreign entity can be taxed in a source country or a country from which its source of income arises (eg, India), only when it can be established that it has a Permanent Establishment in India. If such a situation of existence of PE is not establishment, the foreign entity cannot be made taxable in India from the profits that it earns in India (barring certain residual income and concepts such as royalty, interest dividend, FTS, etc.). This becomes crucial in determining which State will have the taxing power for the income that the foreign entity earns. Now, with this recent Hon'ble Supreme Court's decision, these contours of Permanent Establishment and its characterization as such has expanded with specific focus on what is to be considered as 'fixed place of business'. Thus, it becomes essential to delve into and examine the implications of the judgement with possible future dimensions for various entities.

**Keywords:** *Foreign Entity, Profit, Permanent Establishment, Future Dimensions, Economic Substance*

### I. Introduction

The ever-disputed concept of Permanent Establishment ('PE') in international taxation got a newer and wider interpretation with the landmark ruling by the Hon'ble Supreme Court in *Hyatt International Southwest Asia Ltd. v. Additional Director of Income Tax*<sup>1</sup> (hereinafter referred to as

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<sup>1</sup> 2025 INSC 891 (India).

“Hyatt International Ruling”). The Hyatt International ruling touched upon various facets of interpretation of the concept of PE in India along with adjudicating that substance overrides legal form. It becomes pertinent to evaluate how this ruling expands the horizons of permanent establishment in India and in connection to it the taxability of foreign entities from income earned in India.

## II. Factual Background of the Case

Hyatt International Southwest Asia Ltd. (*hereinafter* referred to as “Hyatt International” or “the company” or “the assessee”) is incorporated in and is a tax resident of United Arab Emirates (UAE). By entering into Strategic Oversight Services Agreement (SOSA) with Asian Hotels Limited in Delhi and Mumbai, the company provided strategic planning and know-how services. The company had declared its income as nil in its return of income (ROI) and claiming refund.

The Assessing Officer (AO) opened original assessment proceedings to which the company asserted that its income is not taxable in India owing to no provision for taxation of ‘Fee for Technical Services (FTS)’ under India-UAE Double Tax Avoidance Agreement (DTAA). Moreover, the company put forth that it does not have a ‘fixed place of business’ or Permanent Establishment (‘PE’)<sup>2</sup> in India to trigger Article 5 read with Article 7 of India-UAE DTAA and its employees have not crossed the threshold of nine-months stay in India as required under the DTAA<sup>3</sup>. Consequently, the company claimed that its business income cannot be made taxable in India.

However, subsequent to Dispute Resolution Panel’s (DRP) rejection of the company’s objections/claim, the AO passed the Assessment Order holding that the activities of Hyatt International constituted PE under Article 5 of the DTAA. The company appealed before the Income Tax Appellate Tribunal (ITAT) against the Ld. AO’s order contending that its activities did not constitute PE in India. Nonetheless, the Tribunal decided the appeal against Hyatt International by

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<sup>2</sup> India-UAE DTAA, art. 5(1).

<sup>3</sup> India-UAE DTAA, art. 5(2).

placing reliance on *Formula One World Championship Limited v. Commissioner of Income Tax, International Taxation-3, Delhi*<sup>4</sup> (hereinafter referred to as “Formula One ruling”).

The company reached the Hon’ble High Court of Delhi by way of appeal with four issues in question. Out of these four issues, two were answered against it (while one was in its favour and the fourth issue was referred to a larger bench of the Hon’ble High Court) holding that PE of the company existed in India with fixed place of business and its business profit would be taxable in India. Challenging the said decision of the Hon’ble High Court, Hyatt International approached the Hon’ble Supreme Court through a Special Leave Petition (‘SLP’).

### III. Circling around the Issues

The pertinent issue involved in the present case was that if Hyatt International had a permanent establishment in India in accordance to article 5 of the India-UAE DTAA. In case, it is concluded that it has a PE in India, the income that it has derived through SOSA would be taxable in India or not.

The case moves towards a crucial turn because in this case, Hyatt International did not have exclusive ownership over a fixed place of land in India. Therefore, in absence of such a place of operation, would an international entity or foreign enterprise still constitute a PE in India, which would require expanding the scope of interpretation of article 5 or ‘fixed place of business’ in India.

### IV. Pertinent Legal Principles in the Hon’ble Supreme Court’s Decisions

After eloquently analyzing the provisions of the SOSA, Formula One ruling and the ‘disposal test’, the Hon’ble Supreme Court sufficiently concluded that there do exist a permanent establishment in India of Hyatt International. The court touched upon the following concepts to eventually reason with the PE establishment in India:

#### The Extent of ‘Disposal Test’ under PE

The court reiterated the concept evolved through the judgement in Formula One ruling where it was explained that for establishment of PE, the disposal test is pivotal. This test signifies that where

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<sup>4</sup> (2017) 15 SCC 602 (India).

a place is used in a way enabling the assessee to carry out its operation, i.e. the place would be considered at the disposal of the assessee.

In such a scenario, the test is not to be levied only in case where a place or premise is actually owned by an entity but it should be carefully examined looking that the economic realities of the contractual arrangement.

Thus, even in a situation, where the premises are not officially owned by the assessee or the such a premise is not rented to the assessee but the place is at the disposal of the assessee for carrying out its operations and has control over such place. To assessee the disposal test, the essential component<sup>5</sup> would be:

- i. Right to use the premise; and
- ii. Control over the premise

In international transaction, where a foreign entity is earning income from the source derived from India, India would have a right to tax such an income only in case where there exist PE in India. If such a PE does not exist, the income can still be taxed if it forms part of residuary income like royalty, interest, dividend, Fee for Technical Services (FTS), etc. as enumerated in the relevant tax treaties.

To establish a PE, a fixed place of business must be there, i.e. a place from where the operations of the entity is carried out or the usage of 'disposal test'. It is however, to be noted that the Organisation for Economic Co-operation and Development ('OECD') does not define such a test and even though India is not a part of OECD, it frequently takes assistance from OECD guidelines for international transactions.

### **SOSA and its underlining contractual terms**

The Court examined the terms of SOSA agreement, wherein the assessee was not getting a fixed fee for the services that it was rendering, rather the revenue it receives is a percentage of room and other revenues<sup>6</sup>. The court reasoned that this revenue-sharing model from gross operating revenues evidenced that the assessee was at the helm of the operations.

Further, the assessee had power to formulate relevant policies related to HR, procurement, pricing, sale, etc., which indicated that it controlled operational facets of the hotel. The court essentially

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<sup>5</sup> *Id.*, at para 33.

<sup>6</sup> *Hyatt International Southwest Asia Ltd. v. Additional Director of Income Tax*, 2025 INSC 891 (India), para 12.3.

listed out that apart from the formulation of the policies, the assessee also undertook appointment and supervision of General Manager, managing operational banks, assigning personnel to hotels, controlling pricing, branding and marketing strategies, along with other such similar powers<sup>7</sup> vested over it.

This strengthened that the assessee did not only provide consultancy to AHL but also had exclusive control over the operations of the hotel business, actively participating in the strategic and financial dimensions.

### **Characteristics of PE**

In Formula One ruling, it was established that there are three characteristics of PE as follows:

- i. Stability;
- ii. Productivity; and
- iii. Dependence.

The court pointed out these three elements of the PE are completely satisfied in the present case wherein firstly, stability is established by the duration of SOSA which is for twenty years; secondly, it had continuous operational presence which was established by revenue-sharing model; and thirdly, it depended on the premises and staff to carry out the operations.

In addition, the court pointed out these functions that were performed by Hyatt International were not mere ‘auxillary’<sup>8</sup> (like consultancy) functions to be covered under the exception to article 5 of the India-UAE DTAA and as per the ruling in the case of *Union of India v. U.A.E. Exchange Centre*.<sup>9</sup> The functions as performed by the assessee were integrated in the core operational functions satisfying the criteria of fixed place of business.

### **Daily operations by Separate Entity – A Valid Defense?**

One of the arguments undertaken by the assessee was that there was a separate entity established in India by the assessee, Hyatt India Pvt. Ltd., which carried out daily operations of the hotel. This argument was negated by the Hon’ble Supreme Court holding that the ‘economic substance’ has overriding value in determination of PE status. What this essentially puts forth is that even if there is a separate Indian entity established, the foreign entity would be judged on its own operations as

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<sup>7</sup> *Id.*, at para 16.

<sup>8</sup> India-UAE DTAA, art. 5(3)(e).

<sup>9</sup> (2020) 9 SCC 329.

to the formation of a PE in India. Although, Hyatt International had its legal form in UAE, its economic substance with major operational dimensions in India, construed and justified its presence in India through PE.

### **Relevancy of Stay of Employees in India**

Another significant argument put forth by the assessee was that none of its employees stayed beyond 9-months duration as is the specific threshold and thus, PE cannot be considered in such a scenario. The Hon'ble Supreme Court observed that the essential criteria for establishing a PE or fixed place of business is the continued business presence in India. Since it was clearly established that there was continued business presence in India, the duration of stay and presence in India becomes unimportant. Thus, it can be concluded that the presence of employees does not play a factor in considering whether a PE is established in India or not for a foreign entity.

The Hon'ble Supreme Court concluded that Hyatt International has a PE in India through the hotel premises and its income would be taxable in India. It is also to be noted that though, it didn't adjudicate on the issue but it noted the decision of the Hon'ble Delhi High Court's larger bench's decision in *Hyatt International Southwest Asia Ltd v. Additional Director of Income Tax*<sup>10</sup> wherein it was concluded that in a situation where the foreign entity incurs losses, the profit can still be attributed to the PE as the tax is attributed to the business presence and not on the global margins (and in this case, global losses).

## **V. Implications and Conclusions**

The legal ramification of Hyatt International ruling is wider in scope. With no longer the surety of contractual specification that a particular entity does not have a PE in India or usage of 'No PE Certificate' as a safeguard, the foreign entity might need to re-evaluate the legal terms and conditions surrounding its operations in India. The ruling emphasized that not the physical presence or legal form of an entity but ultimately how the ultimate operations are conducted in India and the consequent economic implications of it will determine if a permanent establishment is formed in India or not, for its operations to be considered taxable under Article 5 of the relevant DTAA.

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<sup>10</sup> ITA 216/2020.

The Revenue would now move towards looking beyond the contractual terms and towards the reasoning as to which entity has the ultimate control or decision-making power in the transactions. It might mean that foreign entities that have higher control over its Indian counterparts might invite scrutiny from the Department and even re-opening of assessments or audits, in certain cases.

Another important element that needs to be considered and is pivotal is that the presence of employees of foreign entity for a short duration was negated as an argument by the Hon'ble Supreme Court for establishment of fixed place of business in India. Nonetheless, what can be substantially concluded is that it might not be a relevant factor or short duration of employees in India would not have an effect of fixed place operations in India.

What the Hon'ble Supreme Court's decision intensified was the significance of 'disposal test' in determining the PE of an entity in India. Even in cases where there is no allocated office or specified employees, the PE can still be established in India and the revenue from such operations can be made taxable in India, if the ultimate economic substance of the entity lies in India, even if its legal form exists outside India.

It is also interesting to note that to determine a PE from understanding the circumstances of the agreement essentially involves a question of fact. It is apt to say that in taxation, the ITAT is considered as the final fact-finding authority while Hon'ble High Courts and Hon'ble Supreme Court look into question of law (or 'substantial question of law' involved). Very rarely does apex court enter into factual dilemma, unless there is perversity of facts involved.

This widening of contours of permanent establishment in India has extensively widened the scope of interpretation of treaty provision. Further, it has led to foreign entities wanting to enter into contractual transactions in India to clearly and adequately define their FAR (functions performed, assets utilized and risks undertaken) and re-assess their already existing obligations and contractual framework in India in creation of permanent establishment in India.