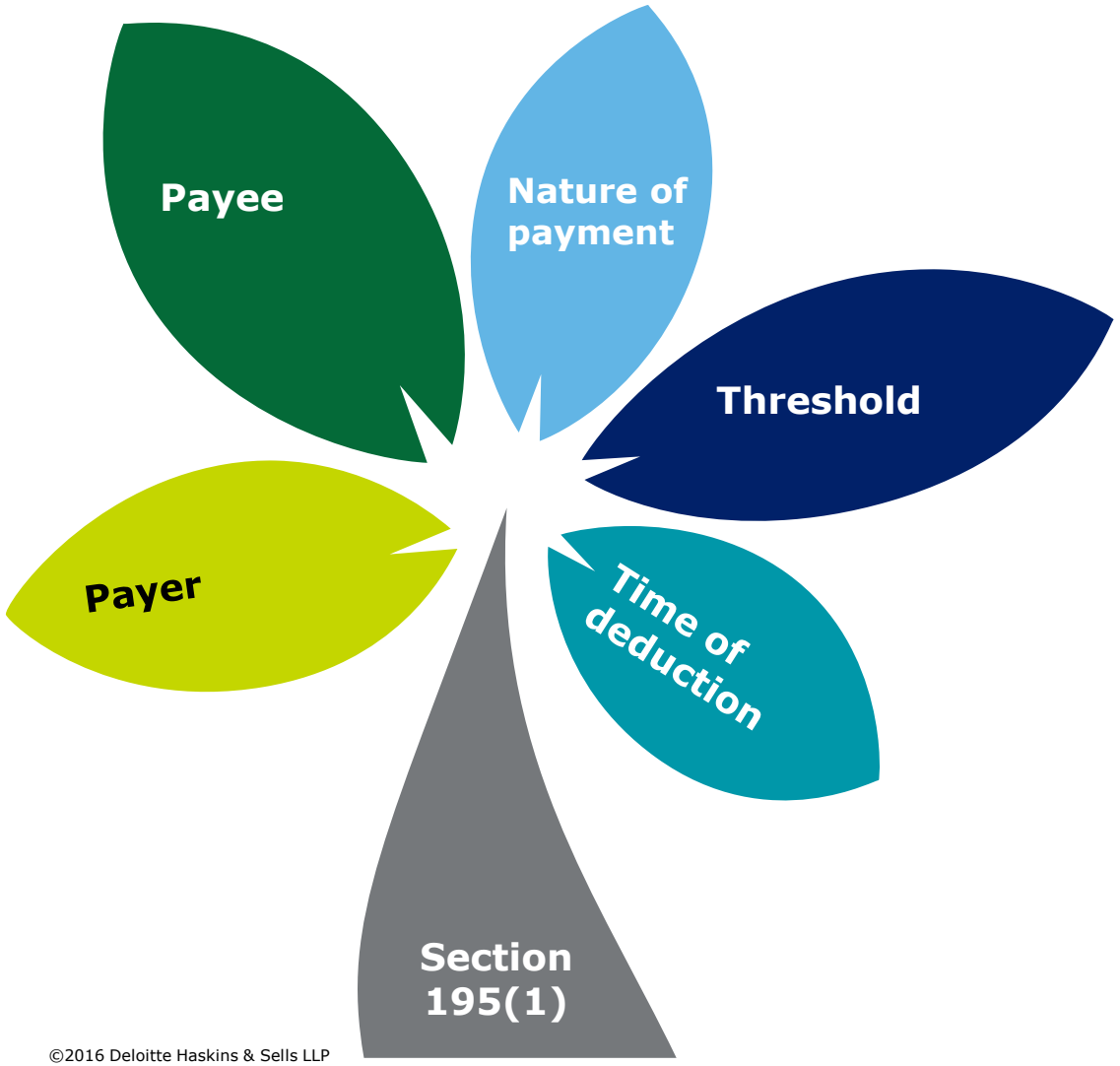
Non resident taxation

CA. N.C. Hegde

JB Nagar study circle
4th February 2024

TDS on payments to NR

Scope of section 195(1) of the IT Act



Payer
Any person responsible for paying – may be resident or NR (whether or not such NR has presence in India)

Payee
NR or a foreign company

Nature of payment
Any interest (other than interest referred to in section 194LB, section 194LC or section 194LD) or any other sum chargeable under the provisions of the IT Act (other than Salaries)

Threshold
No minimum threshold. Tax deduction applies on any amount paid to the NR if the same is chargeable to tax

Time of deduction
At the time of credit [including credit to Suspense account] or at the time of payment, whichever is earlier

TDS on payments to NR

Rate of TDS

Rate of TDS

- Section 195(1) provides for deduction of tax at the "rates in force"
- For the purpose of TDS u/s 195, "rates in force" mean the beneficial of:
  - the rates of income-tax specified in the Finance Act of the relevant year; or
  - the rates of income-tax specified in the DTAA entered u/s 90, or the agreement notified u/s 90A of the IT Act
- Levy of surcharge and cess over and above the tax rate provided under the DTAA, is not permissible as per the DTAA provisions - Sunil V Motiani [2013](59 SOT 37)(Mum ITAT), Capgemini SA [2016](72 taxmann.com 58)(Mum ITAT), Marubeni Corporation [2022] 139 taxmann.com 458 (Mum ITAT), FCC Co. Ltd. [2022] 145 taxmann.com 649 (Delhi ITAT)

Scope of Total Income

- Section 5 provides the scope of total income and lays foundation for what income is liable to tax in India.
- Charge on the basis of residential status of an assessee:
  i. Resident
  ii. Resident but not ordinarily resident
  iii. Non- resident.
- The scope of total income of an assessee depends upon the following three important considerations:

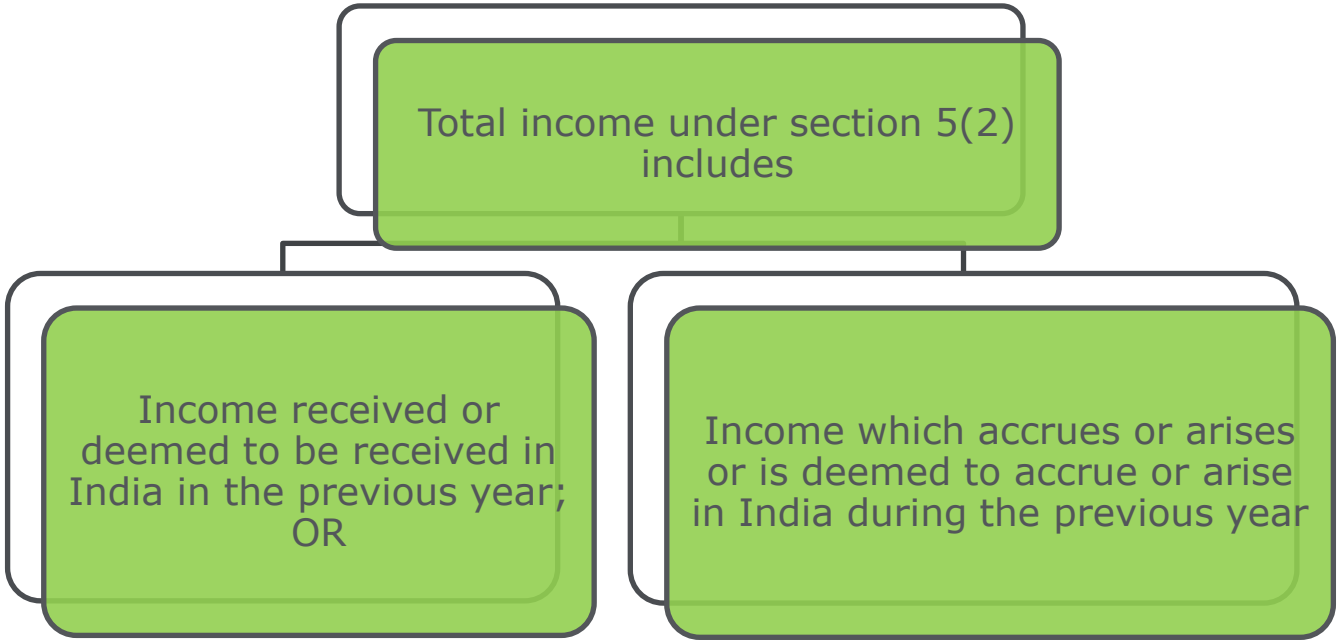
i. The residential status of the assessee.

ii. The place of accrual or receipt of income, whether accrual or deemed

iii. The point of time at which the income had accrued to or was received.

Scope of Total Income – Non-resident

Section 5(2) provides the scope of total income in case of a nonresident.



Income accruing or arising outside India is not liable for tax in India.

Whether the following incomes are to be included in Total income of a non-resident

S.No	Particulars	Taxability
1.	Income accrued or deemed to be accrued and received or deemed to be received in India	Yes
2.	Income accrued outside India but received or deemed to be received in India	Yes
3.	Income accrued or deemed to be accrued in India but received outside India	Yes
4.	Income accrued and received outside India from a business controlled in or profession set-up in India	No
5	Income accrued and received outside India a business controlled or profession set up outside India	No
6	Income accrued and received outside India in the previous year (it makes no difference if the same is later remitted to India)	No
7	Income accrued and received outside India in any year preceding the previous year and later on remitted to India in current financial	No

Business Connection

Section 9(1)(i) of the Act states that “all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India”.

Section 9(1)(i) - Business Connection

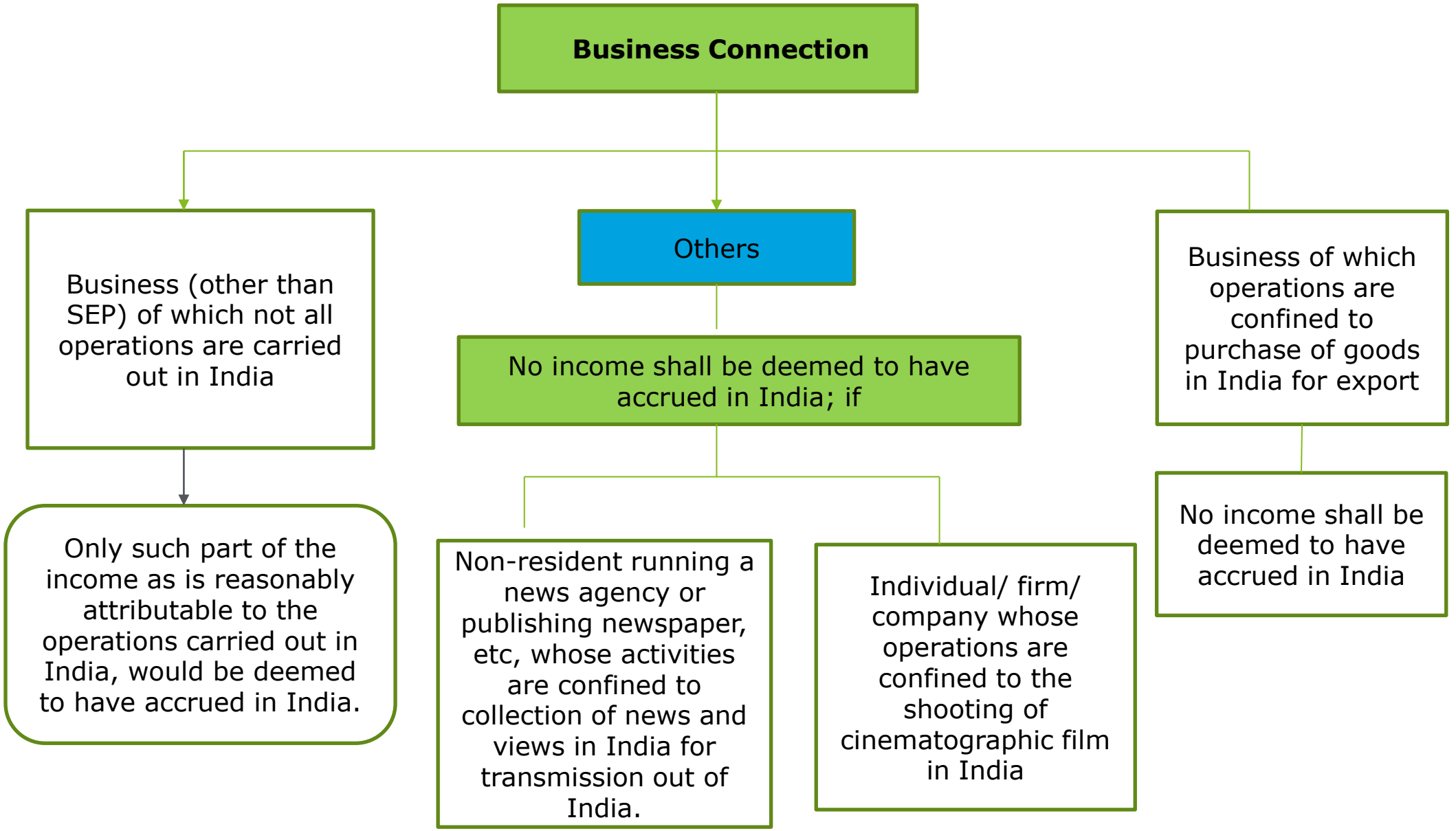
The following two conditions should be satisfied:

- The taxpayer has a ‘business connection’ in India.
- By virtue of ‘business connection’ in India, income actually arises outside India.

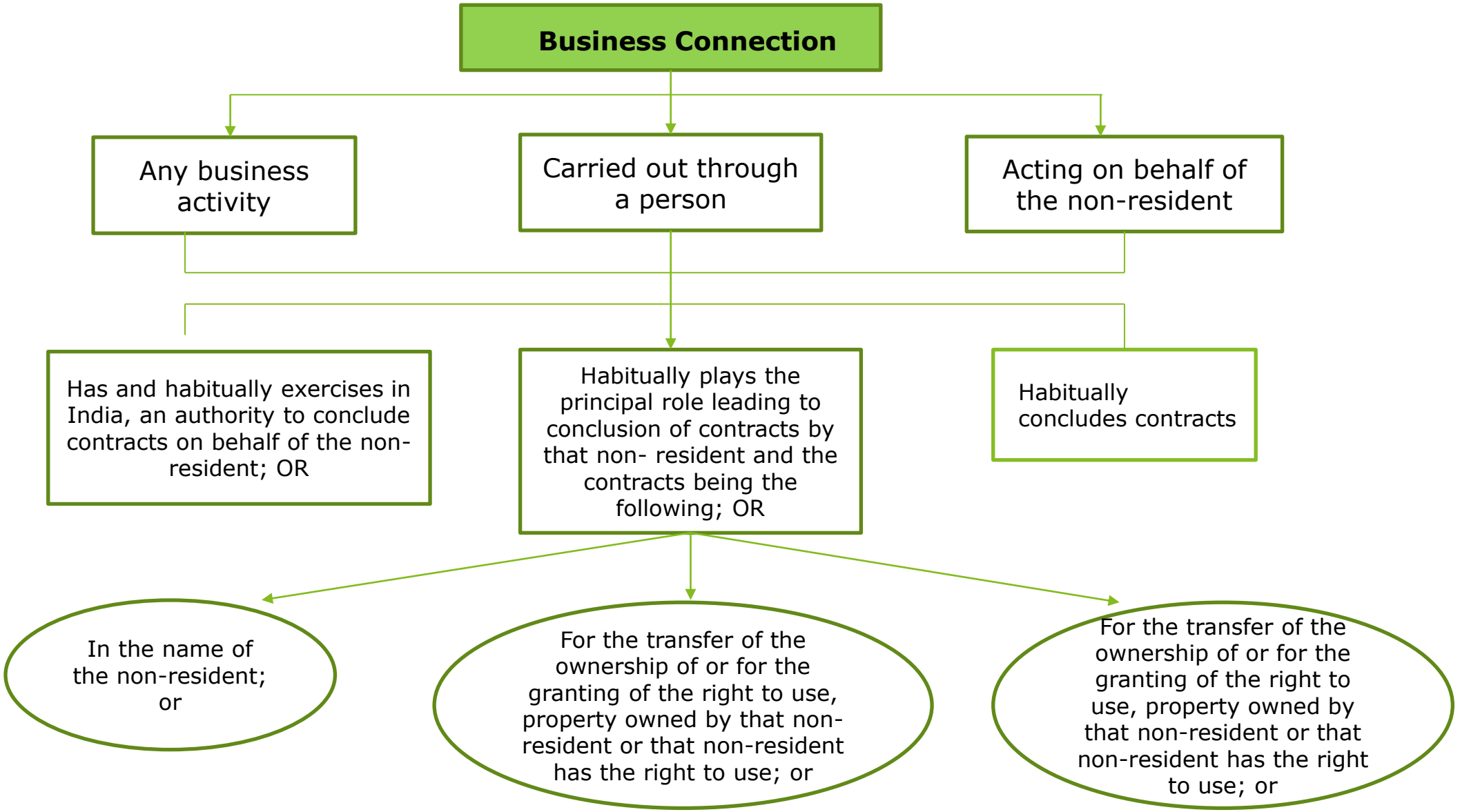
  If the above two conditions are satisfied, income which arises outside India because of business connection in India is deemed to accrue or arise in India. However, only such part of the income as is reasonably attributable to the operations carried out in India would be subject to tax in India.

- A business connection can arise between a non-resident and a resident if both of them carry on business and if the non-resident earns income through such a connection.
- The expression ‘business connection’ postulates a real and intimate relation between the trading activity carried on outside India and the trading activity within India.
- Further, relation between the two should contribute to the earning income by the non-resident in his trading activity.

Explanation 1 to Section 9(1)(i)



Explanation 2 to Section 9(1)(i)



Explanation 2 to Section 9(1)(i)

- Has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or
- Habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident.
- Agents having independent status are not included in Business connection.

Volkswagen Finance Pvt. Ltd.
[2020] 115 Taxmann.com 386 (Mumbai Trib.)

Facts of the case:

- Volkswagen Finance (P.) Ltd. (the taxpayer)1 is an Indian company.
- The taxpayer and Audi India (a division of Volkswagen Group Sales India Ltd) jointly planned an event in Dubai for launch of Audi A-8L facelift model. While the event was held in Dubai, the purpose of the event was the launch of a new model of Audi car, Audi A-8L facelift model for the Indian market.
- The taxpayer had flown in about 150 people mostly prospective buyers and some journalists to the launch ceremony.
- Kim Productions Inc., a company incorporated in the USA, agreed to facilitate the appearance of Nicholas Cage (celebrity) for three consecutive hours. In exchange, the taxpayer paid consideration of US$ 440,000 and other incidental costs.
- The taxpayer and Audi India, as a part of the arrangement, received full rights of the launch event capturing the celebrity's presence across all platforms for a period of 6 months from the date of launch event, and for an unlimited period of time only for internal usage within the Volkswagen Group.

Volkswagen Finance Pvt. Ltd.
[2020] 115 Taxmann.com 386 (Mumbai Trib.)

Facts of the case:

- Aggrieved by the order passed by the CIT(A), the taxpayer filed an appeal with the Mumbai Bench of the Income-tax Appellate Tribunal (ITAT).
- Conclusion:

  ITAT held that, income embedded in payment to international celebrity, for participation in the event in Dubai was taxable in India as it was an India centric event and the target audience was in India and therefore, there was a business connection . Consequently, VFPL had the liability to withhold taxes on such payment.

Significant Economic Presence

Section 9(1)(i)

- Finance Act, 2020 added Explanation 3A to section 9(1)(i) to provide that income attributable to the operations carried out in India will include income from:
  - Such advertisement that targets a customer who resides in India or a customer who accesses the advertisement through IP address located in India;
  - Sale of data collected from a person who resides in India or from a person who uses IP address located in India;
  - Sale of goods or services using data collected from a person residing in India or uses IP address located in India

SEP applies from AY 2022-23 & onwards

Prescribed threshold:
Revenue – Rs.2 crore
Users – 3 lakh users

Interplay between EL & SEP to be examined, particularly for transactions with non-treaty countries

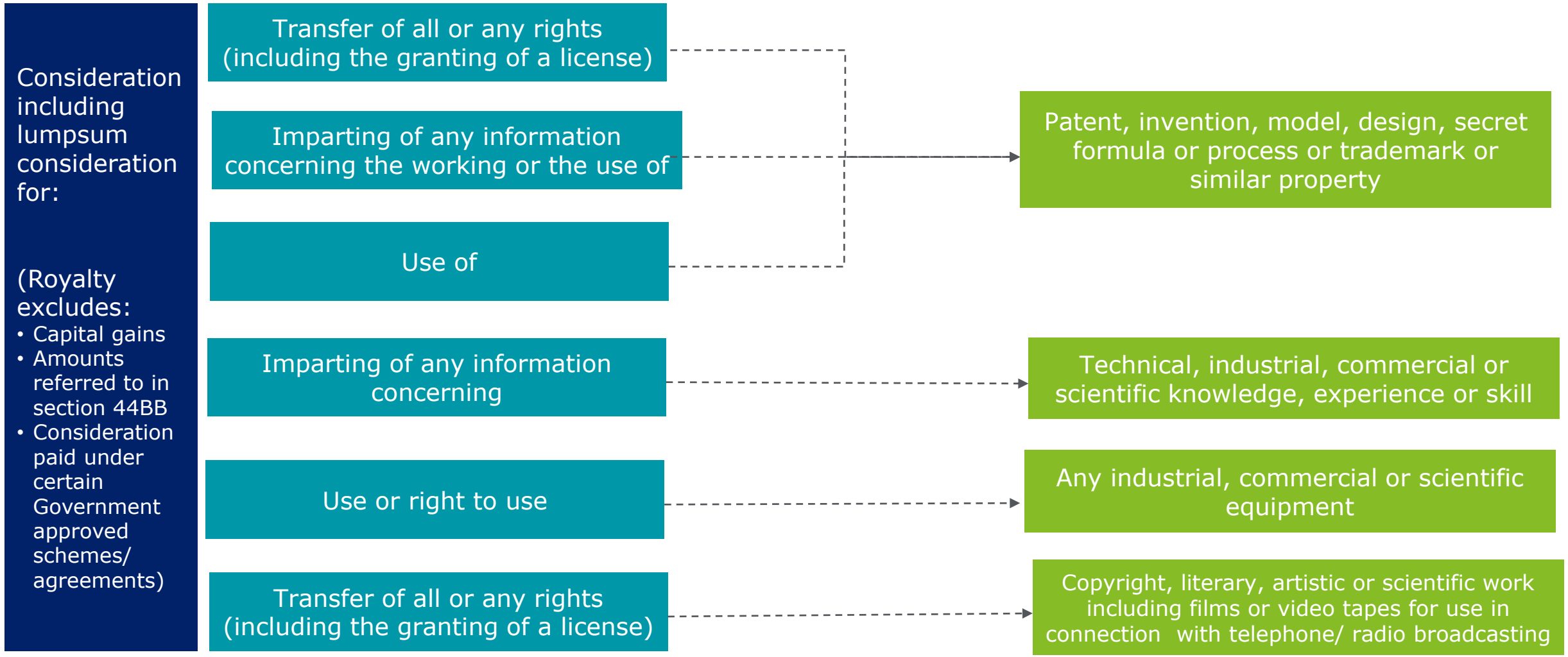
Explanation 2A to Section 9(1)(i)

- SEP is one of the options discussed by 2015 BEPS Action Plan 1 - - Addressing the Tax Challenges of the Digital Economy for taxing digital transactions having no physical nexus with the source country.
- It may also be noted that India has expressed a reservation to the 2017 OECD commentary by reserving the right to tax business not having physical presence, based on the concept of SEP discussed in BEPS Action Plan 1.
- India is possibly one of the first countries proposing to codify multiple options of the BEPS Action Plan 1 in the form of SEP and Equalisation Levy.
- The Government has clarified that the motive of codifying the concept of SEP which enables it to amend / re-negotiate its tax treaties based on similar principles.

Royalty

Royalty

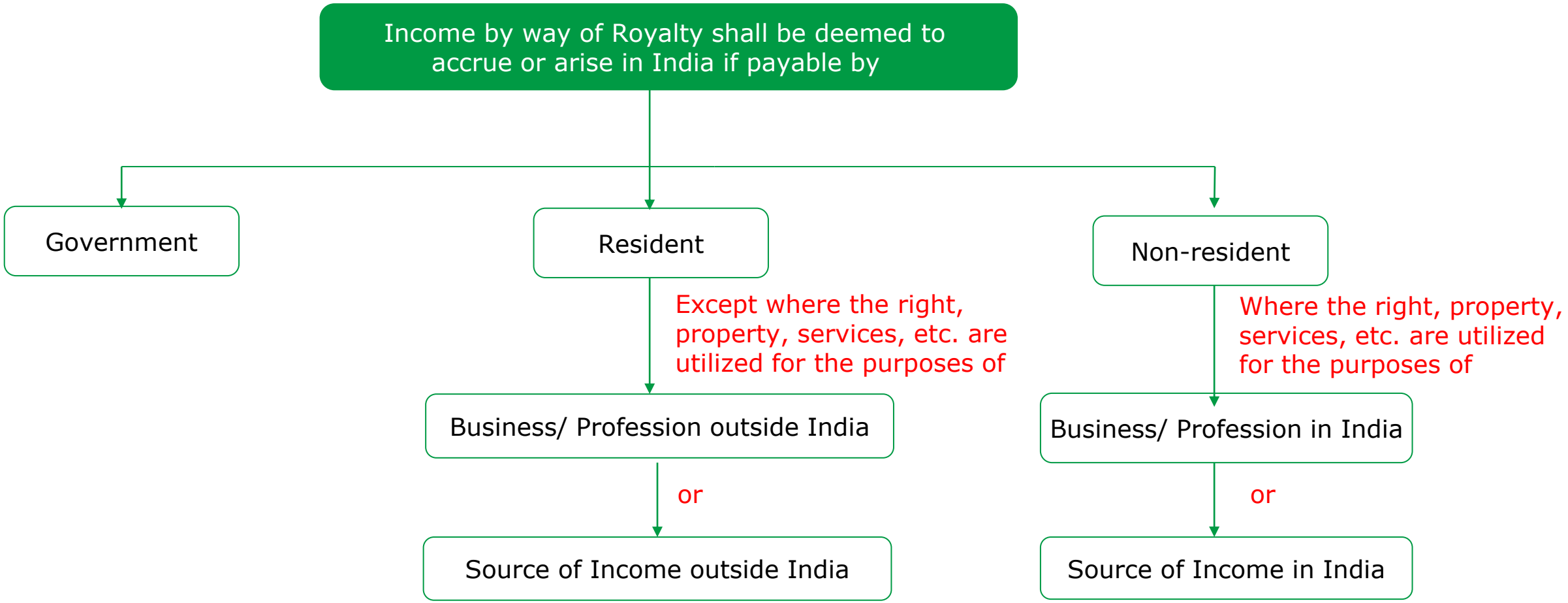
Definition – Explanation 2 to section 9(1)(vi)



Royalty also includes consideration for the rendering of any services in connection with the above

Royalty

Deemed to accrue or arise in India



Residential status of recipient of royalty income is not relevant in determining taxability of royalty in India

Royalty

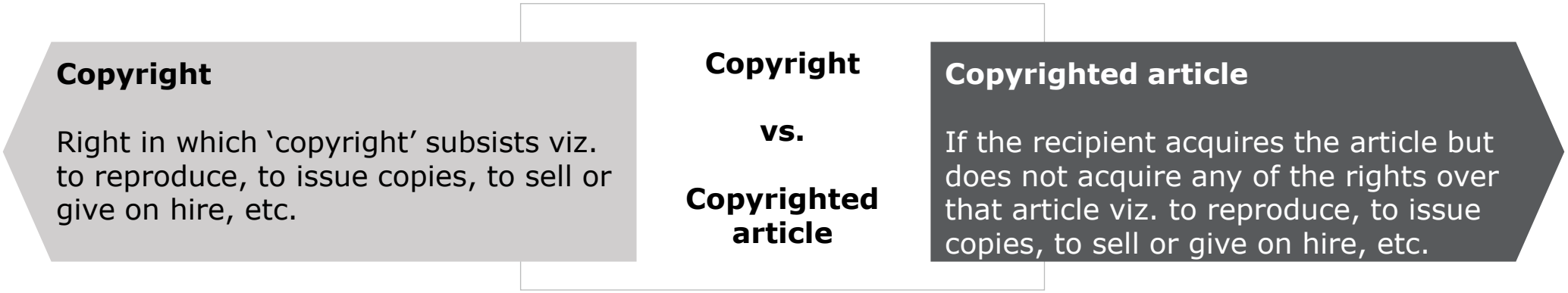
Explanations to section 9(1)(vi) inserted with retrospective effect from 1 June 1976

Explanation 4	Explanation 5	Explanation 6
For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred”	For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not— (a) the possession or control of such right, property or information is with the payer; (b) such right, property or information is used directly by the payer; (c) the location of such right, property or information is in India.	For the removal of doubts, it is hereby clarified that the expression “process” includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fiber or by any other similar technology, whether or not such process is secret

"computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data

Royalty

Software



Meaning of 'copyright' – Section 14 of the Copyright Act, 1957

Exclusive right in respect of a work to reproduce, issue copies, perform in public, make translation, etc.

OECD Commentary

What constitutes Royalty?

- Payment for exploitation of rights that would otherwise be the sole prerogative of the copyright holder

What does not constitute Royalty?

- Payment for transfer of full ownership of the rights in the copyright

OECD recognizes a distinction between the copyright in the program and software which incorporates a copy of the copyrighted program

Royalty

Software

Engineering Analysis Centre of Excellence (P.) Ltd. [2021] 432 ITR 471 (SC)

- A reading of the Distribution Agreement would show that what is granted to the distributor is only a non-exclusive, non-transferable license to resell computer software, it being expressly stipulated that no copyright in the computer programme is transferred either to the distributor or to the ultimate end-user
- Apart from a right to use the computer programme by the end-user himself, there is no further right to sub-license or transfer, nor is there any right to reverse-engineer, modify, reproduce in any manner otherwise than permitted by the license to the end-user
- What is "licensed" by the NR supplier to the distributor & resold to the resident end-user, or directly supplied to the resident end-user, is in fact the sale of a physical object which contains an embedded computer programme and is therefore a sale of goods
- There is a clear distinction between consideration for transfer of copyright rights and consideration for transfer of copyrighted articles
- Copyright is an exclusive right which is negative in nature, being a right to restrict others from doing certain acts
- Copyright is an intangible, incorporeal right, in the nature of a privilege, which is quite independent of any material substance. Ownership of copyright in a work is different from the ownership of the physical material in which the copyrighted work may happen to be embodied, e.g., the purchaser of a book or a CD/DVD becomes the owner of the physical article, but does not become the owner of the copyright inherent in the work, such copyright remaining exclusively with the owner

Royalty

Software

Engineering Analysis Centre of Excellence (P.) Ltd. [2021] 432 ITR 471 (SC)

- Even where such transfer is in respect of' copyright, the transfer of all or any rights in relation to copyright is a sine qua non under Explanation 2 to section 9(1)(vi) of the Act i.e., there must be transfer by way of license or otherwise, of all or any of the rights mentioned in section 14(b) with section 14(a) of the Copyright Act
- The OECD Commentary will continue to have persuasive value for interpretation of the term "royalties"
- Consideration paid for the resale/use of the computer software through End User License Agreements/ Distribution Agreements is not payment of royalty for the use of copyright in the computer software

Points for consideration:

- In view of the retrospective amendments made to section 9(1)(vi) by the Finance Act 2012 with regard to widening the scope of royalty, the narrower definition provided under the DTAA would prove more beneficial
- Payments for computer software are specifically covered as royalty in some Indian DTAAs viz. Kazakhstan, Kyrgyz Republic, Morocco, Namibia, Romania, Russia, Trinidad and Tobago, Turkmenistan
- In view of the SC ruling, the said payments would have to be examined for applicability of EL
- If tax has been deducted in the past & the NR has been able to claim full FTC, one may have to evaluate if continuing to apply TDS & claiming FTC is more beneficial or EL - Can a claim by the taxpayer that the software receipts are royalty be sufficient compliance to claim exemption from EL?
- Overlap of EL with SEP provisions which apply from AY 2022-23

Royalty

Subscription fee for access to online database and journals

Issue: Whether imparting of information concerning industrial and commercial knowledge, experience, skill?

American Chemical Society [2023] 146 taxmann.com 133 (Mumbai ITAT)	Uptodate Inc. [2023] 150 taxmann.com 231 (Delhi ITAT)	Elsevier BV [2021] 432 ITR 251 (AAR)	Dun & Bradstreet Information Service India P Ltd [2011] 338 ITR 95 (Bombay)
Consideration received was not royalty as the assessee merely identified, aggregated and organized publicly disclosed chemistry related scientific information or published research work submitted by scientists worldwide. This information was available in public domain and was the experience of various scientists, researchers, etc. and not that of the assessee. By granting access to the database, the assessee neither shared its own experience, technique or methodology employed in evolving databases with the users, nor imparted any information relating to them	Subscription received for providing access to online database was not taxable as royalty as the assessee was neither the creator of the content put in the database, nor had it transferred any copyright or license to use the content of the database. The assessee's activities merely included collating data relating to healthcare as available in public domain and putting them in one place by creating a database. The only improvement the assessee made in the database was analysis, indexing, description, appending notes for facilitating easy access to the customers. Customers were only granted access to the contents of the database, but they were not permitted to copy, print, reproduce, modify, translate, adapt or create derivative works. Customers could not share usernames, passwords or other security information for access to the licensed products and all the rights, titles and interests in the licensed products, including all copyrights and IPRs, remained with the assessee. The assessee hence could not be said to have transferred right to use any copyright of literary, artistic or scientific work or any other secret formula or process or information concerning industrial, commercial, scientific experience	Receipts from Indian subscribers for access to database containing books/journals/articles with a limited right of printing, making e-copies, and storing information was not royalty as there was no transfer of know-how or previous or new experience to subscribers	Business Information Report ("BIR") was a standardized product of the assessee that provided factual information on the operation, financial condition, management, line of business, rating of the company, etc. BIR was accessible to any subscriber on payment of requisite price with regular internet access for which no particular software or hardware was required. The copyright in the BIR was neither licensed nor assigned to the group co or to the Indian customer. Therefore, payments made for purchase of BIRs was not

Contra view in Thought Buzz (P.) Ltd [2012] 346 ITR 345 (AAR), ONGC Videsh Ltd. [2013] 141 ITD 556 (Delhi ITAT), Wipro Ltd [2013] 355 ITR 284 (Kar)

Royalty

Web hosting charges/ Consideration for cloud-based services

Issue: Whether user acquires use/ right to use underlying infrastructure, software, service?

Reasoning Global E-Application Ltd. [2022] 145 taxmann.com 464 (Hyd ITAT)

Web hosting charges paid to US company was merely a consideration for online access of cloud computing services for process and storage of data or run applications and could not be considered as royalty as the service recipient did not get any rights of reproduction

Microsoft Regional Sales Pte. Ltd. [2022] 140 taxmann.com 70 (Delhi ITAT), MOL Corporation [2022] 195 ITD 1 (Delhi ITAT)

Since cloud-based services did not involve any transfer of rights to customers in any process and grant of right to install and use software included with subscription did not include providing any copy of said software to customer, payments made for same were not royalty but merely a consideration for online access of cloud computing services

PDR Solutions FZC [2023] 146 taxmann.com 84 (Mum ITAT), Rackspace, US Inc [2020] 113 taxmann.com 382 (Mum ITAT), EPRSS Prepaid Recharge Services India (P.) Ltd. [2018] 100

Where assessee, a US company, earned income from providing cloud services including cloud hosting and other supporting and ancillary services to Indian customers, since there was no leasing of any equipment by assessee and customers were not having physical control or possession over servers and right to operate and manage the infrastructure/servers vested solely with assessee, said income was not royalty

Royalty

Supply of technical drawings, designs, plans

Issue: Whether transfer of design/ copyright/ IPR?

Ruling	Held
Davy Ashmore India Ltd. [1990] (190 ITR 626) (Calcutta HC)	Consideration for outright sale of drawings and designs (where the NR seller did not retain any property in them) cannot be characterized as "royalty" as defined in Article 13 of the India-UK DTAA
Outotec (Finland) Oy [2019] 109 taxmann.com 69 (Kolkata ITAT)	Where assessee a foreign company, had primarily earned revenue from sale of designs and drawings to Indian customers, since designs and drawings were used by Indian customers for internal business purposes for setting up of their plants and not for any commercial exploitation, designs and drawings sold by assessee tantamounted to use of copyrighted article rather than use of a copyright and was, therefore, business income
Neyveli Lignite Corporation Ltd [1999] (243 ITR 459) (Madras HC), Mitsui Engineering and Ship Building Co Ltd [2001] (259 ITR 248) (Delhi HC)	The total contract price paid to a foreign company towards designing, manufacture, supply, erection and commissioning of an equipment (not involving transfer of any license in a patent, invention, model or design) was not in the nature of "royalty" as defined in section 9(1)(vi) of the Act. The same was on the basis that the design supplied was not to enable the assessee to commence the manufacture of the machinery itself with the aid of such design. The limited purpose of the design and drawings was only to secure the consent of the assessee to the manner in which the machine was to be designed and manufactured, as it was meant to meet special design requirements of the buyer.

Royalty

Supply of technical drawings, designs, plans

Ruling	Held
Finoram Sheets Ltd. V. ITO [2014](52 taxmann.com 206) (Pune ITAT)	• Payment for obtaining plant know-how, i.e., designing, characterization of plant and machinery, etc., cannot be considered as payment falling within purview of 'royalty' • The payments made for technical Product knowhow or Process know-how though would fall under ambit of royalty
Klayman Porcelains Ltd [1997] (229 ITR 735) (Andhra Pradesh HC)	Amount paid by an Indian company to NR company for technical drawings pertaining to engineering of a kiln was not towards imparting any information concerning the working of, or the use of any patent, invention, model, design, secret formula or process. Since it inter alia involved an outright transfer of technical drawings (pursuant to which the kiln was constructed), it did not constitute "royalty" u/s 9(1)(vi) of the Act
Andritz Hydro (P.) Ltd. [2017] 83 taxmann.com 166 (Indore ITAT)	Where assessee purchased technical drawings and designs from its associated enterprise to manufacture generators as per needs of customers, since technical know-how relating to design and drawings was not transferred to assessee, amount paid in respect of same was not taxable as royalty

Royalty

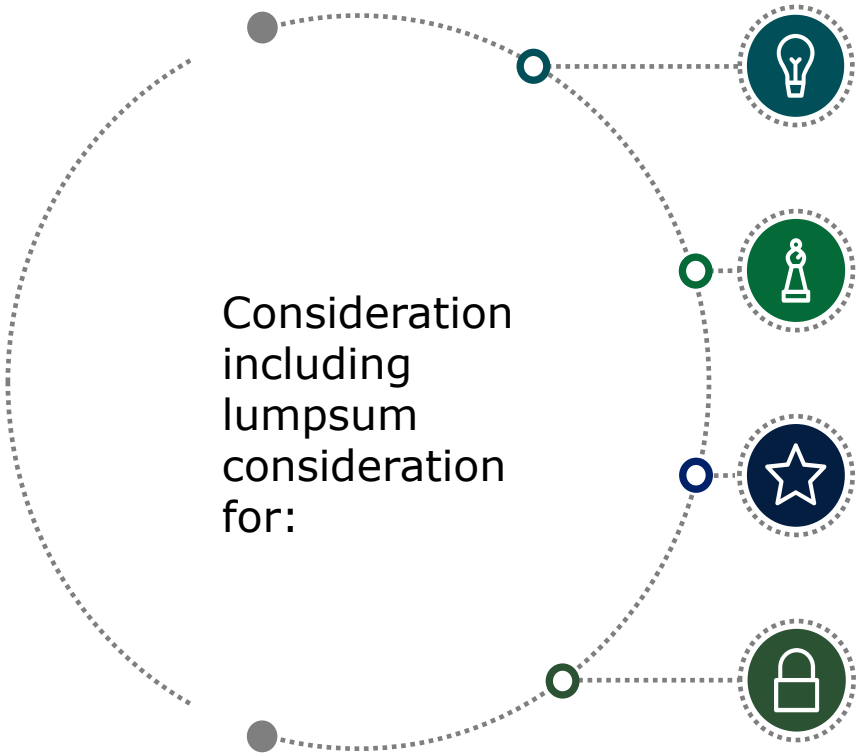
Miscellaneous

Ruling	Consideration for	Held
PDR Solutions FZC [2023] 146 taxmann.com 84 (Mum ITAT)	Domain name registration – Whether use/ right to use trademark?	• Consideration not royalty as the taxpayer functioning as a domain name Registrar did not have rights to the domain name registered in the name of the customer/registrant, least in the IPR/intangible asset in the nature of 'trademark' • Activity of the Registrar did not result in transferring of any right to the domain name since it only facilitated the registration of the domain name after checking its availability in the database maintained by the Registry • Delhi ITAT's ruling in GoDaddy.Com distinguished as the assessee therein did not claim DTAA benefit
Vanderlande Industries (P.) Ltd. [2022] 194 ITD 229 (Pune ITAT)	Use of Information Communication Technology ("ICT") infrastructure – Whether use/ right to use equipment?	• Payment to Dutch holding co for use of ICT infrastructure set-up was royalty • Similar view in Rieter Machine Works Limited [(2021) ITA No. 19/PUN/2021] • Contra view in EY Global Services Ltd [2022] 285 Taxman 10 (Delhi HC) that payment received by a UK entity for providing access to computer software (procured from third-party vendors) to its member firms within its network located in India, did not amount to 'royalty'
Fox Network Group Singapore Pte [2020] 121 taxmann.com 330 (Delhi ITAT)	Broadcasting rights in relation to live feeds, live telecast – Whether integrated bundle of rights?	• Not royalty since a live feed cannot constitute a 'work' in which copyright can subsist and broadcast or live coverage does not have a copyright, hence payment for live telecast is neither payment for transfer of any copyright nor any scientific work
Global Cricket Corp [2022] 145 taxmann.com 570 (Mum ITAT)	Non-live exhibitions & non-live/ recorded content in live feed	• Amounted to payment for use of copyright and hence was taxable as royalty under the India – Singapore DTAA

Fees for Technical Services

FTS

Definition – Explanation 2 to section 9(1)(vii)



Managerial services

Technical services
"

Consultancy services
"

Provision of services of technical or other personnel

Excludes:
Consideration for construction
Consideration for assembly
Consideration for mining or like project
Consideration chargeable under the head “Salaries” in the recipient’s hands

FTS

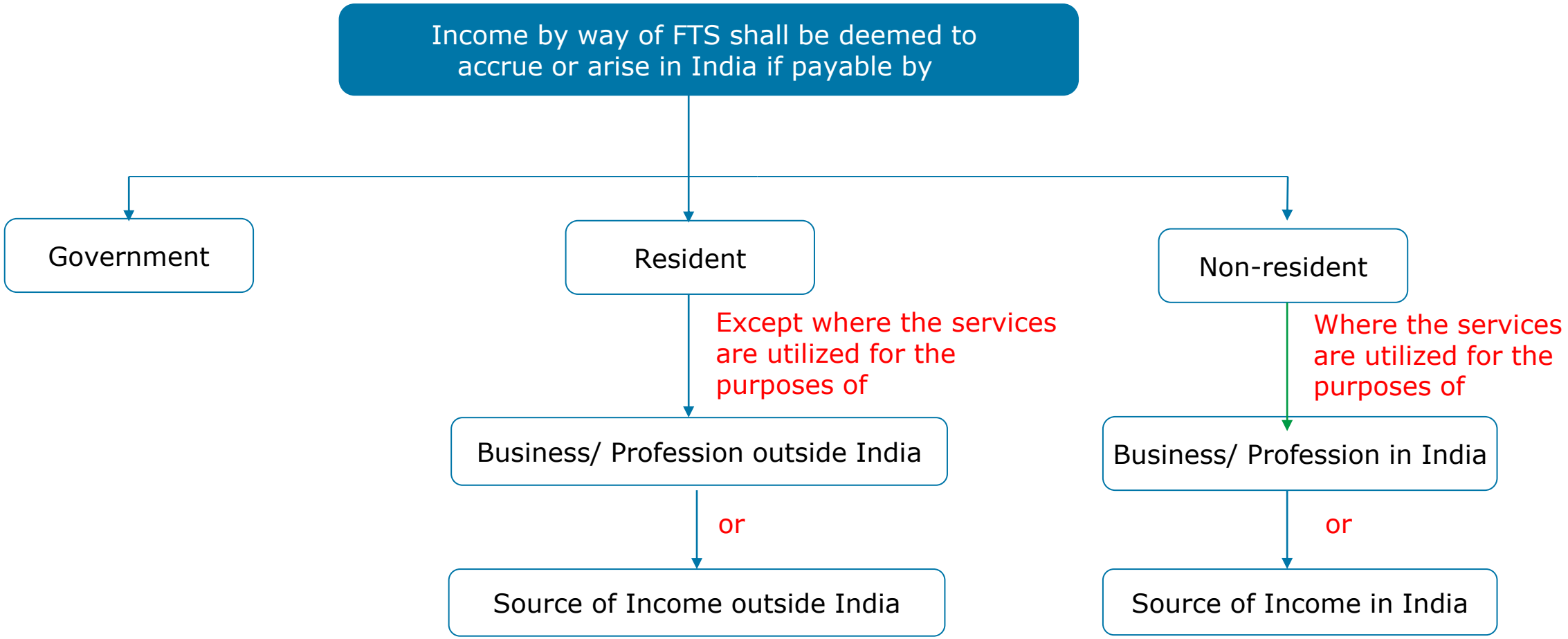
Definition – Explanation 2 to section 9(1)(vii)

Managerial services	Technical services	Consultancy services
R. Dalmia [1977] 106 ITR 895 (SC) - "management" includes the act of managing by direction, or regulation or superintendence. Accordingly, managerial service essentially involves controlling, directing or administering the business	Kotak Securities Ltd.[2016] 383 ITR 1 (SC) - 'Technical services' like 'Managerial and Consultancy service' would denote seeking of services to cater to the special needs of the consumer and the making of the same available by the service provider. It is the above feature that would distinguish/ identify a service provided from a facility offered	Bharti Cellular Ltd. & others [2008] 319 ITR 139 (Delhi HC) - The word "consultant" is a derivative of the word "consult" which entails deliberations, consideration, conferring with someone, conferring about or upon a matter. The consultant, who provides the consultancy service, has to be a human being. A machine cannot be regarded as a consultant
Intertek Testing Services India Pvt. Ltd., [2008] 175 Taxman 375 (AAR) - "managerial" relates to "manager" or "management". A "manager" is a person who manages an industry or business or who deals with administration or a person who organizes other people's activity	Bharti Cellular Ltd. [2011] 319 ITR 139 (Delhi HC) - Should be construed in a narrow sense by applying the rule of Noscitur Sociis as it comes in between the words "managerial" and "consultancy services". Since both "managerial" and "consultancy" services involve some element of human intervention, "technical services" would also have to be interpreted accordingly	Advance Ruling P. No. 28 of 1999 [2000] 242 ITR 208 (AAR) - The category of technical and consultancy services are to some extent overlapping because a consultancy service could also be technical service. However, the category of consultancy services also includes an advisory service, whether or not expertise in technology is required to perform it

GVK Industries Ltd [2015] 371 ITR 453 (SC) - The said expressions have not been defined in the Act and therefore it is obligatory to examine how the same are used and understood by persons engaged in business. The general and common usage of the said words has to be understood at common parlance

FTS

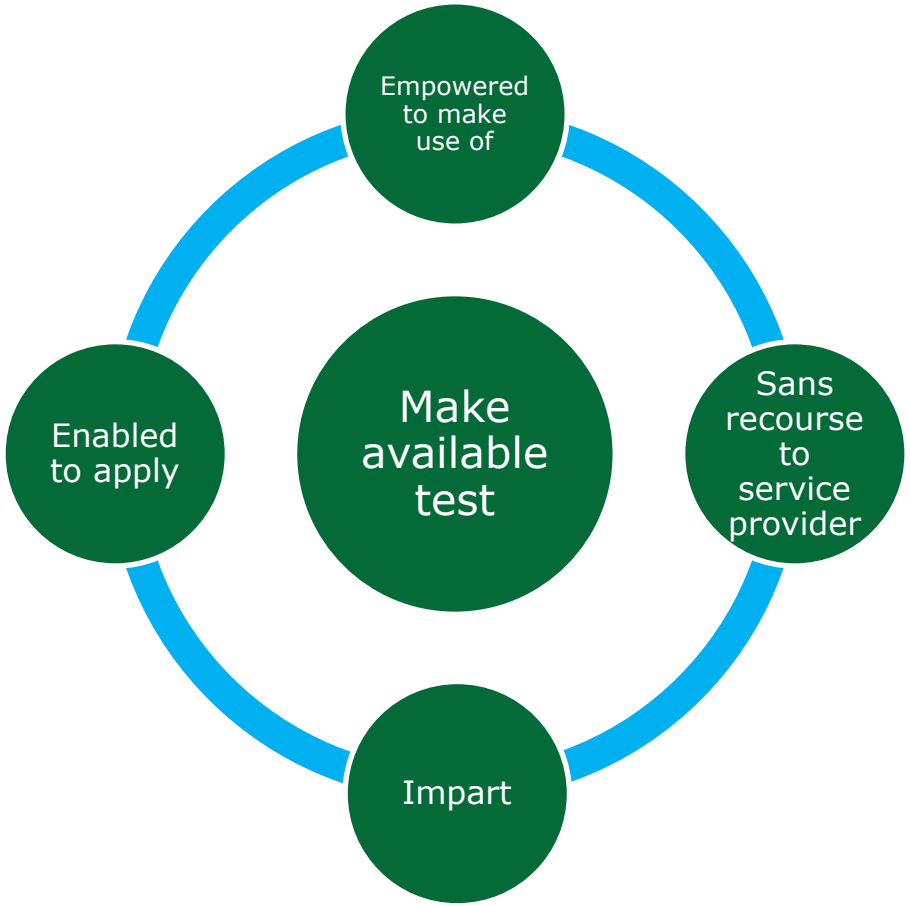
Deemed to accrue or arise in India



Residential status of recipient of FTS income is not relevant in determining taxability of FTS in India

FTS

“make available” under the India-USA DTAA



“Included Services” defined narrowly to mean technical or consultancy services which “make available” technical knowledge, experience, skill, know-how, or processes, or which consist of the development and transfer of a technical plan or technical design

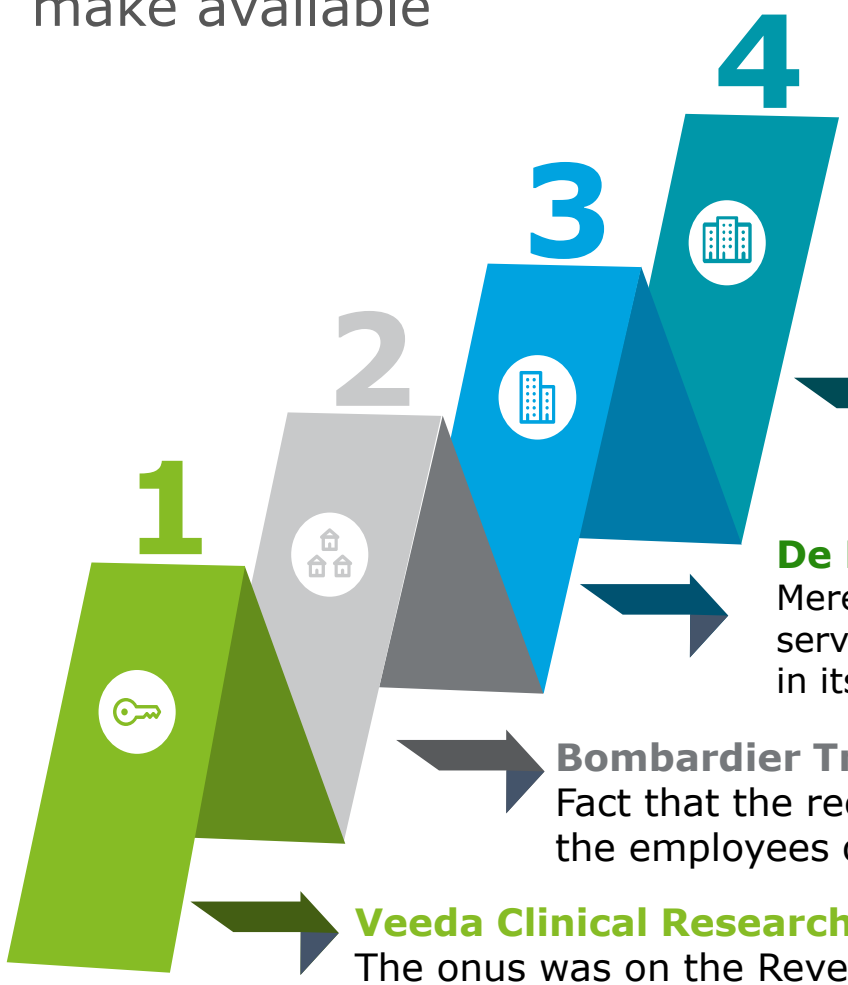
MoU to the India-USA DTAA**:**

- Generally speaking, technology will be considered "made available" when the person acquiring the service is enabled to apply the technology
- The fact that the provision of the service may require technical input by the person providing the service does not per se mean that technical knowledge, skills, etc., are made available to the person purchasing the service
- Use of a product which embodies technology shall not per se be considered to make the technology available

If the service does not “make available” technical knowledge, etc., it is not taxable as FTS/ FIS

FTS

"make available"



Intertek Testing Services India Pvt. Ltd. [2008] 307 ITR 418 (AAR)
The interpretation given in the MOU to the India-USA DTAA can be usefully adopted while dealing with a provision similarly worded.

De Beers India Minerals P. Ltd. [2012] 346 ITR 467 (Kar HC)
Mere rendition of services does not fall within the gamut of "make available" unless the service recipient is enabled and empowered to make use of the technical knowledge by itself in its business or for its own benefit without aid of the original service provider in future

Bombardier Transportation India P. Ltd. [2017] 162 ITD 586 (Ahd ITAT)
Fact that the recipient immensely benefitted from the services, even resulting in value addition to the employees of the recipient, was irrelevant

Veeda Clinical Research P. Ltd. [2013] 144 ITD 297 (Ahd ITAT)
The onus was on the Revenue to demonstrate that the training services made available transfer of technology.

Some other DTAA with "make available" test – Netherlands, Singapore, UK
DTAA in which "make available" imported through MFN – Belgium, France, Spain

FTS

MFN

The dispute

- Meaning - More favorable DTAA terms granted to other countries extended to existing DTAA countries by source country
  - Lower tax rate or narrowing the scope of income liable to tax
- The Delhi HC in Concentrix Services Netherlands B.V. [2021] 434 ITR 516 (Delhi HC),
  - Granted the benefit of the lower rate of dividend by invoking MFN clause through India-Slovenia DTAA w.e.f. the date Slovenia became a member of the OECD, i.e., from 21 July 2010
  - Held that the requirement of the state to be a member of OECD should exist not necessarily at the time when the subject DTAA was executed but when the benefit of MFN needs to be invoked
  - Relying on its earlier judgment in Steria (India) Ltd. [2016] 386 ITR 390 (Delhi HC) (rendered in the context of the India-France DTAA), also held that there is no requirement of notification in order to trigger the MFN clause in the India-Netherlands DTAA
- The ruling in Concentrix Services was followed by the Delhi HC in Cotecna Inspection SA [2022] 286 Taxman 342 (Delhi HC) and Deccan Holdings B V [2022] 284 Taxman 300 (Delhi HC)
- Unilateral positions were taken by Netherlands, France and Swiss Confederation on availability of MFN clause in their DTAA with India

FTS

MFN

The dispute

- CBDT Circular 3/2022 dated 3 February 2022 provides that the MFN clause can be invoked only when all the following conditions are met:
  - India subsequently entered into a DTAA with a third state;
  - The subsequent DTAA is entered into between India and a state which is a member of the OECD at the time of signing the DTAA;
  - The subsequent DTAA provided for a lower rate or restricted scope of taxation; and
  - India has issued a notification permitting invocation of MFN clause on account of beneficial treatment accorded in the subsequent DTAA.
- GRI Renewable Industries S.L [2022] 100 ITR(T) 470 (Pune ITAT)
  - Once the DTAA is notified, the Protocol, which is an integral part of the DTAA, also gets automatically notified along with the DTAA. Therefore, separate notification is not required for granting benefit under MFN clause
  - CBDT Circular dated 3 February 2022 specifying the need for a separate notification for importing the beneficial treatment from another DTAA, overlooks the plain language of section 90(1) of the Act which treats the MFN clause as an integral part of the DTAA
  - The CBDT Circular is binding on the tax authorities and not on the taxpayer or the appellate authorities

FTS

DTAA does not have Article on FTS

Whether taxable as:

- Business income under Article 7 of DTAA? or
- Other income under the residuary Article of DTAA? or
- Income from Independent Personal Services under Article 14 of DTAA? or
- Per the provisions of the Act?

Differing views

Held	Ruling	DTAA involved
Article 7 on Business Profits shall apply, and income shall be taxable only if the assessee has a PE in India	Kalpataru Power Transmission Ltd. [2023] 200 ITD 420 (Ahd ITAT), Booz & Co (ME) FZ-LLC [2018] 192 TTJ 33 (Mum ITAT), Bangkok Glass Industry Co. Ltd. [2013] 215 Taxman 116 (Madras HC), Paramina Earth Technologies Inc [2020] 182 ITD 45 (Visakhapatnam ITAT)	UAE, Thailand, Philippines
Article 22 on Other Income shall apply	Lanka Hydraulic Institute Ltd. [2011] 337 ITR 47 (AAR)	Sri Lanka
Provisions of the Act shall apply	TVS Electronics Ltd [2012] 52 SOT 287 (Chennai ITAT)	Mauritius
The scope of Business profit and Independent personal service covers FTS as well	Welspun Corporation Ltd. [2027] 183 TTJ 697 (Ahd ITAT)	UAE, Thailand
Not taxable under the DTAA as well as under the Act	Tetra Pak India (P.) Ltd [2019] 111 taxmann.com 205 (Pune ITAT)	Malaysia, Thailand, Indonesia, UAE, Saudi Arabia

FTS

Supply of technical drawings, designs, plans

Issue

- Whether development and transfer of a technical plan or technical design simplicitor without making available technical knowledge, experience, skill, knowhow or processes, etc., would be in the nature of FTS?

- In the event that development and transfer of a technical plan or a technical design also requires making available of technical knowledge, experience, skill, knowhow or processes, etc., whether the said condition was satisfied?

Buro Happold [2022] 145 taxmann.com 450 (Mum ITAT), Forum Homes (P.) Ltd. [2022] 192 ITD 184 (Mum ITAT)

- The words "or consists of the development and transfer of a technical plan or technical design", appearing in the second limb of Article 13(4)(c) had to be read in conjunction with "make available technical knowledge, experience, skill, knowhow or processes"
- As per the rule of ejusdem generis, the words "or consists of the development and transfer of a technical plan or technical design" would take color from "make available technical knowledge, experience, skill, knowhow or processes"
- Technology is considered to have been made available if technical knowledge, experience, skill remains with the service recipient even after the rendering of services has come to an end. The service recipient must be at liberty to use the same in his own right
- The technical design, drawings, etc. supplied by the taxpayer were project-specific and could not be used by the service-recipient in any other project in future
- The "make available" test was hence not met, and the receipt could not be taxed as FTS

FTS

Standard automated services sans human intervention

Issue

- Whether consideration for standard connectivity and networking services such as intranet, internet and broadband services, partakes the character of FTS?

Hitachi Metglas (India) (P.) Ltd. [2022] 192 ITD 357 (Delhi ITAT), Kotak Securities Ltd. [2016] 383 ITR 1 (SC), Estel Communication (P.) Ltd. [2008] 318 ITR 185 (Del HC)

- The word "technical" as appearing in section 9(1)(vii) of the Act was preceded by the word "managerial" and succeeded by the word "consultancy", and the same took color from the word "managerial and consultancy"
- The words "managerial" and "consultancy" were a definite indicative of the involvement of a human element. Managerial services and consultancy services were to be given by humans only, and not by any means or equipment. Therefore, the word "technical" was to be construed in the same sense involving direct human involvement, and without that, the services provided could not be held to be technical services u/s 9(1)(vii) of the Act
- By their very nature and inherent characteristics, networking services over internet and intranet, including e-mail services could not be provided by human intervention
- Where the entire process, resulting in provisioning of service was fully automated with no human intervention, charges paid for provision of such services could not be classified as FTS

FTS

Sales commission paid to overseas agents

Issue

- Whether services rendered by foreign agents amount to “technical services” or “managerial services”?

Deccan Creations (P.) Ltd. [2022] 193 ITD 5 (Bang ITAT), Evolv Clothing Company Pvt Ltd. (2018) 407 ITR 72 (Mad HC), Faizan Shoes Pvt. Ltd. (2014) 367 ITR 155 (Mad HC)

- The leather garments industry was prone to changes in fashion and the quality and selling price, inter alia, also constituted an important element for securing foreign orders
- It was quite natural for the taxpayer to seek those details from the agents, which the agents could furnish in view of their local presence. Thus, the foreign agents had provided the details of market trends and requirements of foreign buyers, which were usually provided by any agent. Hence the same could not constitute managerial services
- In effect, the agents had acted as the link between the taxpayer and its customers and had received commission on sales effected through them
- The services rendered by the foreign agent can at best be called as a service for completion of the export commitment and would not fall within the definition of FTS
- The service rendered was essentially brokerage service 'to procure orders'. The market research abroad or co-ordination with the supplier or to ensure timely payment or making available its office space for visit by the suppliers, were ordinary things which any agent or broker undertook incidental to brokerage service
- The consideration constituted business income in the hands of the agents which was not taxable in the absence of a PE in India

FTS

Leadership training fee

Issue

- Whether consideration paid for leadership training constitutes FTS?

Sandvik AB [2021] 190 ITD 110 (Pune ITAT)

- The taxpayer was entitled to the beneficial provisions of the India-Portugal DTAA based on the MFN clause in the India-Sweden DTAA
- The word 'managerial' was absent in the FTS definition of India-Portugal DTAA
- In order to decide whether the training fees was a consideration for managerial services, it was necessary to first comprehend the real nature of services rendered by the taxpayer. The philosophy of equating the nature of training with the rendition of the same nature of service, was unfounded
- Ordinarily, training was conceived as passing on of some proficiency by the trainer to the trainee. It simply led to honing up the skills of the other in the subject, which patently could not be termed as an equivalent of rendering service in that field, e.g., acquainting someone in a formal manner with techniques to boost sales did not stand at par with rendering marketing services
- Doing the activity was synonymous with rendering of service of that nature; Simply equipping or enabling the others for doing an activity was a step anterior to rendition of such services
- Rendering leadership training was hence not a managerial service
- The training also did not constitute a technical or consultancy service as the "make available" condition as per the India-Portugal DTAA was not satisfied

FTS

Reimbursement of expenses

Issue

- Whether services provided by Seconded employees/ General and Administrative services viz. Accounting services, Human Resource services, Production services, Information Technology services, are in the nature of technical, managerial or consultancy services?

Flipkart Internet P. Ltd. [2022] 288 Taxman 699 (Kar HC), ITP Publishing India [2023] 148 taxmann.com 250 (Mum ITAT)

- Where assessee entered into an inter-company master services agreement with its overseas group co. for secondment of employees, since the said secondment did not satisfy the "make available" test prescribed under the DTAA, the payments made merely for technical, or consultancy services rendered by the seconded employees would be insufficient to treat the same as FTS under the DTAA
- Further, the payment made towards general and administrative services was not a consideration for managerial or technical or consultancy services
- In any case, the payment represented reimbursement of actual/ allocated cost and no element of income was involved

Taxability of Royalty and FTS

Taxability of Royalty and FTS

Increase in tax rate u/s 115A on Royalty/ FTS income of NR

Earlier, NRs' income from royalty/FTS which is not effectively connected to a PE in India, was taxed at the rate of 10% (plus surcharge and cess) u/s 115A of the IT Act

Finance Act, 2023 doubled the said tax rate from 10% to 20% (plus surcharge and cess) for amounts payable on or after 1 April 2023

The proposal was not part of the Finance Bill 2023 that was presented on 1 February 2023

It was introduced as part of the amendment to the Finance Bill 2023 on 24 March 2023 and was approved by the Lok Sabha without any debate

Major amendment introduced without prior information, debate or stakeholders' consultation

Taxability of Royalty and FTS

Increase in tax rate u/s 115A of the Act

Impact of the amendment

- The lower tax rates prescribed under most DTAAs shall now prove more beneficial
- DTAA benefit is subject to satisfaction of beneficial ownership test, LOB, PPT, furnishing of TRC and Form 10F
- Section 115A(5) provides that NR need not file ROI if its income consists of Royalty/FTS on which tax has been deducted at a rate not less than that specified in section 115A(1)(b). Earlier, NR preferred to avail this exemption even in cases where the DTAA rate was marginally beneficial (10.92% under the IT Act as against 10% in DTAAs such as Belgium, France, Hungary, Israel, Netherlands, etc.) as it saved compliances such as obtaining PAN, filing ROI, filing TP report, etc.
- Post amendment, the exemption from filing ROI shall not be available to NR claiming DTAA benefit
- Increase in compliance-cost for NR claiming DTAA benefit
- As FTC may not be available in respect of EL paid, earlier, some NR offered to tax, income from sale of software licenses as Royalty/ FTS and hence claimed that the same was exempt from EL. This stand may require reconsideration in light of the increased tax rate u/s 115A

Taxability of Royalty and FTS

MLI

MLI modifies the operation of existing DTAA between parties;

MLI and DTAA to be read together

Each party to the MLI specifies to which existing DTAAs & to what extent the MLI applies (Covered Tax Agreements - CTAs);

MLI to apply only if both parties notify the DTAA as CTA

93 jurisdictions notified by India as CTAs

Key modifications in India's DTAAs:

Preventing tax treaty abuse

Widened scope of PE

Improving dispute resolution

Tie breaker test on dual residency

Taxation of capital gains

India deposited instrument of ratification along with its final MLI positions on 25 June 2019

Notable Indian DTAA for which MLI entered into effect from 1 April 2020 for WHT and other taxes:

Australia, Belgium, France, Japan, Netherlands, Russia, Singapore, Sweden, UK, UAE

USA has yet to sign the MLI

Equalisation levy vs. TDS u/s 195

EL vs. TDS u/s 195

EL Provisions

	EL 1.0	EL 2.0
Applicable from	1 June 2016	1 April 2020
Applicable on	Consideration (other than Royalty/ FTS) for any 'specified service' being online advertisement, digital advertising space, any other facility/ service for online advertisement & other notified service	Consideration (other than Royalty/ FTS) received or receivable from specified payers by an NR e-commerce operator from e-commerce supply or services made or provided or facilitated by it
Payer	A resident carrying on business/ profession or a PE of an NR	• A person resident in India; or • An NR in 'specified circumstances' • A person who buys such goods or services or both using IP address located in India
Payee	NR not having a PE in India	NR e-commerce operator i.e., NR who owns, operates or manages digital or electronic facility or platform for online sale of goods/ online provision of services or both
Exclusion	• NR service provider having an Indian PE • Aggregate consideration in a year not exceeding Rs. 1 lakh • Payment for specified service by the resident payer or the Indian PE, is not for the purposes of carrying out business/ profession	• NR e-commerce operator having PE in India with which the e-commerce supply/ service is effectively connected • Cases where EL 1.0 is leviable • Cases where sales, turnover or gross receipts of the NR e-commerce operator from e-commerce supply or services is less than Rs. 2 crore during the FY
Rate	6%	2%
Person responsible for depositing EL	Payer i.e., Resident carrying on business/ profession or Indian PE of NR shall deduct EL from the amount payable for specified service	Payee i.e., NR e-commerce operator

EL vs. TDS u/s 195

Section 10(50) of the Act

EL shall not be charged on Royalty or FTS income which is taxable under the Act read with DTAA

Section 10(50) of the IT Act and Proviso to section 163 of the Finance Act, 2016

Coursera Inc [2022] 285 Taxman 6 (Delhi)

- Taxpayer was a US e-platform operator, acting as an aggregator of educational institutions and providing access to various courses
- It paid EL 1.0 on receipts from Indian customers
- AO rejected taxpayer's NIL rate application u/s 197 and directed TDS @10%
- The Delhi HC set aside the impugned order and directed that a fresh order be passed on taking into account section 10(50) of the IT Act as the assessee, a US e-platform operator, had paid EL on receipts from Indian customers

Google Asia Pacific Pte Ltd. [TS-57-HC-2022(DEL)] (Delhi)

- Assessee, a Singapore-based entity engaged in providing cloud services in India, filed a writ petition challenging the certificate issued u/s 195(2) directing Google Cloud India to deduct tax @ 10% on payments made to Assessee
- Assessee submitted that since it had already paid EL of 2% on the said sums, the TDS created double jeopardy
- The Delhi HC took cognizance of the EL paid and granted interim relief by allowing the Assessee to receive remittances from Google Cloud India after TDS of 8% i.e., [10% as per the certificate u/s 195(2) – EL paid @ 2%]

Thank You!!