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TAX FLASH NEWS

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Income from granting distribution rights of TV channels is not taxable as royalty under the India-USA tax treaty

The Delhi Bench of Income-tax Appellate Tribunal (the Tribunal) in the case of Turner Broadcasting System Asia Pacific Inc.[1] (the taxpayer) held that the income derived by a foreign channel company from granting distribution rights of TV channels to an Indian company is not taxable as royalty under the India-USA tax treaty. The taxpayer had merely granted rights to the Indian company. The copyright of the content in the product remained with the taxpayer and it was not transferred to the Indian company. Further, the taxpayer had already offered the said income as business income in terms of the Mutual Agreement Procedure (MAP) of earlier years. Therefore, the income declared by the taxpayer in accordance with MAP and upheld by the tax department in the earlier years must be accepted.

Facts of the case

The taxpayer is a U.S. based company. During the relevant Assessment Years (AYs)[2], the taxpayer derived advertisement and distribution income from grant of exclusive rights to an Indian company, to sell advertising on the products[3] and to distribute the products. Indian company acts as an exclusive distributor of those products to the cable operators and other permitted systems on ‘principal to principal basis’. The distribution agreement allowed Indian company to distribute the products to various cable operators and ultimately to the consumers in India. The distribution income collected by an Indian company was to be shared between the taxpayer and Indian company. The copyrights and other propriety rights in the products (channels) have always remained with the taxpayer.

The taxpayer does not have any office, branch or place of management in India. Indian company is an independent agent and remuneration paid to it is at arm’s length. Accordingly, an Indian company cannot be considered as a Permanent Establishment (PE) of the taxpayer in India. The taxpayer in order to avoid prolonged litigation and to buy peace and bring finality to Income-tax proceedings declared the income as per the MAP order. In the earlier assessment years 2001-02 to 2004-05, the agreement between competent authorities of India and U.S. under MAP held that 10 per cent of the advertising and subscription income received from Indian sources will be deemed to be the net profit chargeable to tax in India. The taxpayer in AYs 2007-08 and 2008-09 filed its return of income on the same basis. The facts for all the AYs remains the same and the same has been accepted by the Assessing Officer (AO) in the assessment orders for AY 2007-08 and AY 2008-09.

However, during the subsequent AYs[4], the AO treated the distribution revenue as royalty under Section 9(1)(vi) of the Income-tax Act, 1961 (the Act) and Article 12 of the India-U.S. tax treaty (tax treaty). The AO observed that the taxpayer had granted various rights relating to its products including the right to sub-license. The rights granted by the taxpayer under the agreement was purely a commercial right for distribution of products to the ultimate viewers which clearly falls under the ‘Broadcast reproduction right’ given under Section 37 of the Copyright Act, 1957.

The Dispute Resolution Panel (DRP) confirmed the order of the AO. Aggrieved, the taxpayer filed an appeal before the Tribunal.

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[1] Turner Broadcasting System Asia Pacific Inc. v. DDIT (ITA No. 1343/Del/2014) – Taxsutra.com

[2] AYs 2009-10, 2010-11, 2011-12, 2012-13, 2013-14

[3] a) Satellite delivered television services called Cartoon Network, TCM Turner Classic Movies, POGO and Boomerang; b) From interactive entertainment services known as 'CartoonNetworkIndia.com' and `POGO.tv; and c) From entertainment mobile telecommunications services 'Cartoon network Mobile and Boomerang Mobile'

[4] AYs 2009-10, 10-11, 11-12, 12-13, 13-14

Tribunal's decision

On perusal of the agreement, it indicates that the taxpayer had the sole right to determine the content of the products and change such content from time to time. All the copyrights and other priority rights in the products and in any promotional material vested in the taxpayer alone. It is a copyright of the content in the product which always remained with the taxpayer and was never transferred. The clause merely provides right to distribute the product.

The taxpayer had merely granted rights to the Indian company to 'receive, promote, market, license, distribute and sub-distribute the products to cable, satellite, broadcast, hotel, interactive and telecommunication entities and other users, 'sell advertising' and performing ancillary activities. The term copyright has been used in the 'Royalty' Article under the tax treaty but has not been defined in the tax treaty. However, the same has been defined in the Copyright Act which lists several acts in respect of a work in relation to which exclusive right would be termed as copyright.

The Indian company is carrying out the distribution and selling of the advertisement and it does not have any kind of right to edit, interpret, add the products distributed by it. The taxpayer only granted commercial rights in the nature of 'broadcast reproduction right' to the Indian company, which has been separately defined under Section 37 of the Copyright Act and therefore, the income derived by the taxpayer for distribution of products cannot be taxed as 'royalty' although it is a business income of the taxpayer.

The ability to initiate legal action against the infringer of the copyright by Indian company was merely a commercial term incorporated in the agreement to safeguard the interest of the taxpayer which is situated in the US. The Indian company can enter into an agreement with respect to the content of the programmes but this right does not allow them to take ownership of the content. The copyright within the product has always been vested with the taxpayer.

What is streamed is uplinked and downlinked without any change in the content. The Indian distributor cannot separate content from the channel stream. The product in the present case is a channel and what is streamed is the content, all of which gets distributed without any separation or dissection. Accordingly, the amount received from Indian company cannot be brought to tax as 'royalty' in the hands of the taxpayer.

The Assessing Officer has tried to justify the distribution revenue as royalty by applying the retrospective amendment made in Explanation 6 of Section 9(1)(vi). Such an approach cannot be upheld because there is no similar amendment in the definition of royalty under the tax treaty. The Tribunal relied on the Delhi High Court decision in the case of New Skies Satellite BV[5] where it was held that amendment in the domestic law cannot be imported or read into the tax treaty.

The Tribunal relied on the decision of the Bombay High Court in the case of MSM Satellite[6]. Further, following the jurisprudential principle the Tribunal observed that the law has itself recognised two different right and exploitation of one cannot be confused with the use of other. The Tribunal distinguished the decision of the Supreme Court in the case of Star India Private Limited[7] relied on by the tax department. In that decision, the Supreme Court observed that the broadcasting was a separate right from the copyright. The Tribunal held that the observations of the Supreme Court supports the case of taxpayer and its reliance on the decision of the Bombay High Court to contend that the broadcasting right is a separate right which cannot fall within the purview of copyright gets fortified.

Accordingly, the Tribunal held that the distribution income earned by the taxpayer cannot be taxed as royalty. Since, taxpayer has already offered income as business income in terms of the MAP, therefore, the income as declared by the taxpayer in accordance with the MAP and accepted by the tax department in the earlier years must be accepted for the current years also.

Our comments

The issue with respect to the taxability of distribution charges received by a foreign channel company on account of distribution of TV channels in India has been a subject matter of debate before the Courts/Tribunal.

The Mumbai Tribunal in the case of Taj TV Ltd.[8] held that the distribution income on account of distribution of the pay channel to the various cable operators and ultimately to the consumers in India was not in the nature of royalty under the India-Mauritius tax treaty. Further, the Bombay High Court in the case of MSM Satellite Pte. Ltd. has held that distribution charges received on account of telecasting of TV channels in India were not taxable as royalty since the taxpayer was not parting with any copyrights.

The Tribunal in the present case has held that the income derived from granting distribution rights of TV channels is not taxable as royalty. The taxpayer had merely granted rights to the Indian company. The copyright of the content in the product remained with the taxpayer and it was not transferred to the Indian company.

[5] New Skies Satellite BV [2016] 382 ITR 114 (Del)

[6] MSM Satellite (Singapore) Pte Limited v. DDIT [ITA No. 2523/Mum/2010]
[7] Star India Private Limited v. Department of Industrial Policy and Promotions & Others [C.A. Nos. 7326-7327 of 2018]
[8] DDIT v. Taj TV Ltd [2016] 72 taxmann.com 143 (Mum)

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