

TAX FLASH NEWS

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Offshore distribution commission income is not ‘reasonably attributable’ to India

Background

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Credit Suisse (Singapore) Ltd.¹ (the taxpayer) dealt with the taxability of income from distributing mutual funds abroad. The Tribunal observed that for the purpose of treating the business income as deemed to accrue or arise in India, it is relevant that the said income should be ‘reasonably attributable’ to the operations carried out in India. In the present case, all the operations of the taxpayer were carried outside India. Therefore, offshore distribution commission income earned by the foreign entity cannot be taxed in India.

Facts of the case

- The taxpayer is a Singapore based entity and it is a registered as Foreign Institutional Investor (FII) with Securities and Exchange Board of India (SEBI). During the Assessment Year (AY) 2014–15, the taxpayer carried out transactions in equity shares, Global Depository Receipts (GDRs), Foreign Currency Convertible Bonds (FCCBs), Indian Depository Receipts (IDRs), Exchange Traded Derivatives, Debt Securities, Mutual Fund, etc in its capacity as SEBI registered FII/FPI.
- Further, the taxpayer entered into an Offshore Distribution Agreement with HDFC Asset Management Co Ltd (Indian Co./HDFC). The taxpayer agreed to distribute Mutual Fund schemes launched by HDFC, with a view to procure subscriptions for such schemes from investors outside India.
- As per the Agreement, the taxpayer creates awareness about the schemes of funds, and identifies investors from amongst its clients and procures subscriptions to units in the schemes of the funds. Under the Agreement, the taxpayer also ensure that the subscriptions are made in accordance with and on the terms and conditions set out in the offer document and without making any representations of giving warranties not contained in the offer document.
- During the Assessment Year 2014–15, the taxpayer inter-alia, earned offshore distribution commission income from HDFC, which was claimed as exempt under Article 12 of the tax treaty. The taxpayer claimed that the commission income received by it could not be treated as Fees for Technical Services (FTS) under Article 12(4) of the tax treaty as it had neither provided any technology to HDFC nor made available any technical knowledge, experience, skill, know-how or process. Thus, ‘make available’ test is also not satisfied in the present case. Thus, offshore distribution commission income was not taxable in India under Article 12 of the tax treaty.
- The Assessing Officer (AO) held that commission received by the taxpayer was not FTS. The taxpayer was carrying out distribution activity of products of HDFC, which were regulated by SEBI in India. The location, control and management of the fund was situated in India, which constituted a business connection in India and it creates a sufficient nexus of the offshore distribution income with India. Accordingly, the AO taxed the commission income received by the taxpayer under Article 23 of the tax treaty read with Section 5(2) of the Act.

¹ DCIT v. Credit Suisse (Singapore) Ltd. (ITA no.6098/Mum./2019) – Taxsutra.com

- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the conclusion of the AO that the offshore distribution income was not taxable as FTS. The CIT(A) further held that offshore distribution income earned by the taxpayer was in the nature of business income and in the absence of PE was not taxable in accordance with Article 7 of the tax treaty. The CIT(A) on reference to the decision of the Tribunal in the case of Credit Suisse AG² held that offshore distribution income was not taxable and thus, deleted the additions made by the AO.
- Aggrieved, the tax department filed an appeal before the Tribunal

Tribunal's decision

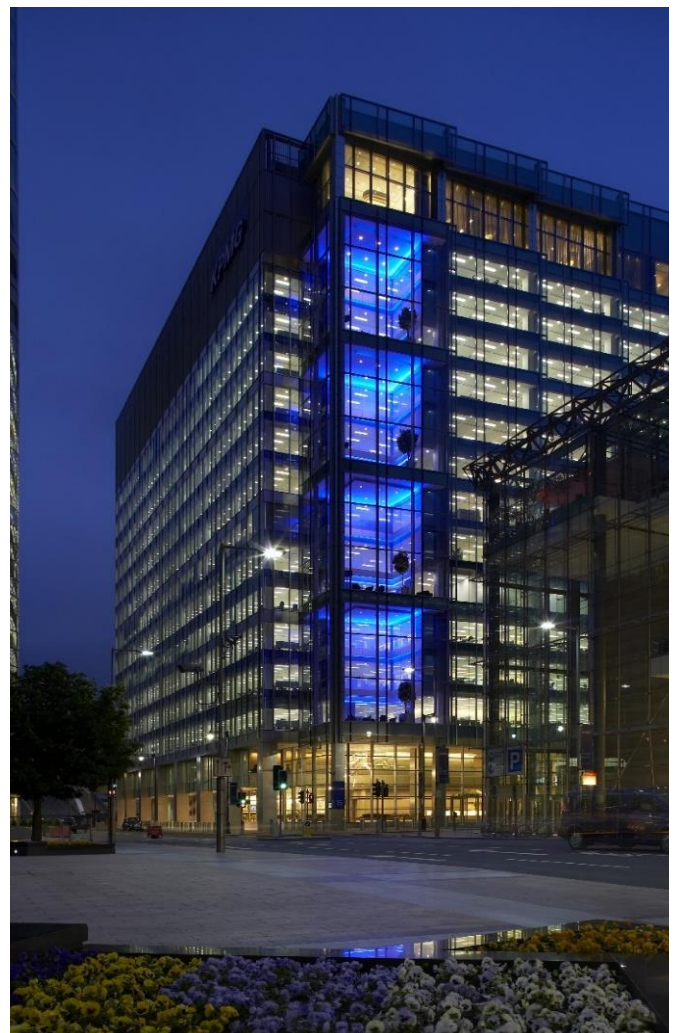
- The Tribunal held that in the present case, the taxpayer also conducts portfolio investments in Indian securities in its capacity as SEBI registered FII/FPI and hence the conclusion of the CIT(A) that the offshore distribution commission income was in the nature of 'business income' of the taxpayer does not require any interference.
- Further, the Tribunal also referred to the decision of the Supreme Court in the case of Toshoku Ltd³ where it was held that the offshore distribution income earned by the taxpayer was not chargeable to tax in India since the non-resident taxpayer did not carry out any business operation in India and the income was earned for services rendered outside India.
- In light of above, the Tribunal observed that as per the provisions of Explanation 1(a) to Section 9(1)(i), it is only that portion of the income which is 'reasonably attributable' to the operations carried out in India shall be deemed to accrue or arise in India for the purpose of taxation under the Act. In the present case, all the operations of the taxpayer were carried out outside India, therefore, in such circumstances offshore distribution commission income earned by the taxpayer could not be treated as being 'reasonably attributable' to any operation carried out in India.

² DCIT v. Credit Suisse AG [2018] 198 TTJ 67 (Mum)

³ CIT v. Toshoku Ltd. [1980] 125 ITR 525 (SC)

Our comments

Taxability of commission income earned by non-residents for distribution activities undertaken outside India has seen fair bit of litigation where tax department has argued the commission income to be in the nature of 'fees for technical services' and hence taxable in India. In this case, the tax department sought to establish business connection in India by virtue of the fact that the Mutual Funds distributed by the non-resident were controlled and regulated by SEBI and RBI in India. The Tribunal has thus limited its observations to the business connection by re-emphasising the requirement of the non-resident to have operations in India for income to be attributed to the business connection.



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