KPMG

#KPMGjosh

TAX FLASH NEWS

7 January 2021

Payments for grant of distribution rights of channels are not taxable as royalty or FTS under the India-USA tax treaty

Recently, Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of NGC Network Asia LLC[1] (the taxpayer) dealt with the issue of taxability of distribution rights of channels granted by the foreign media company to the Indian entity. The Tribunal held that the distribution rights granted by the taxpayer to the Indian entity is only a commercial right/broadcast reproduction right and not a copyright and consequently consideration for the same cannot be treated as royalty or Fees for Included Services (FIS or FTS) under Article 12 of India-USA tax treaty (tax treaty). The Tribunal observed that the technical explanation provided in the tax treaty was issued by the tax authorities of USA and the same is not the official protocol or clarification which has been mutually agreed upon between the two countries. Hence, the said technical explanation would not bind the Tribunal.

Facts of the case

The taxpayer is a US based entity engaged in the media industry, and its business constitutes of broadcasting of its channels over various countries, including over Indian sub-continent. The taxpayer, vide agreement dated 21 February 2001, had granted rights to distribute the channels broadcasted by the taxpayer in India to its subsidiary company for a lump-sum consideration. The taxpayer does not have any control over the activities undertaken by Indian entity upon grant of distribution rights, nor does it undertake any activity in India as regards the distribution rights granted. Indian subsidiary in turn is allowed to independently enter into a contract with the media intermediaries/subscribers (i.e. cable operators) for distribution of channel in India

[1] NGC Network Asia LLC v. DDIT (ITA No.8671/Mum/2004) – Taxsutra.com

The Assessing Officer (AO) held that the distribution revenues earned by the taxpayer falls within the meaning of royalty under Article 12 of the tax treaty and accordingly, such distribution revenues are taxable in India. The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

Tribunal's decision

There were no copyrights in the channel or content that is transferred. It was clearly spelt out in the agreement which provides that the Indian subsidiary shall ensure that the intermediates do not modify or replace any copyrights trademarks, trade names, logos, names or likewise or any contents.

In fact, it is an obligation for Indian subsidiary to distribute the channel on an 'as is' basis, without making any amendment to channel. Further, Indian subsidiary or intermediaries cannot cut, edit, dub, voice-over, subtitle or otherwise change or alter any of the channel(s) or any of the content thereof, as required by any applicable law, without informing the taxpayer of all the details regarding the mandated changes or alterations. Indian subsidiary or intermediaries cannot copy any of the programmes included on the channel for the purpose of re-transmitting them later or for any other reason. Therefore, neither any copyrights are granted nor any rights to copy any programme have been granted to the Indian subsidiary or to any other intermediaries.

The taxpayer had granted Indian subsidiary the limited right to use the trade name, trademarks, service marks and logos (the Channel marks) solely to enable it to market and distribute the channel in accordance with the distribution agreement. The Indian subsidiary does not have the rights to exploit these service marks, in any manner. Hence, rights given by the taxpayer are not copyright as defined under the Copyright Act and therefore not covered by the definition of 'Royalty'.

The tax department relied on the technical explanation provided in the protocol to the tax treaty, to argue that the definition of 'Royalty' includes television broadcasting in India. However, the taxpayer contended that the reliance on technical explanation in the context of use or right to use of cinematographic films or films or tapes used for radio or television broadcasting, is erroneous. The provision was applicable only in the case of channel owner who acquires rights for any cinematographic films or tapes that used for the radio or broadcasting. However, in the present case, the taxpayer has granted distribution rights of 'Channel' to Indian subsidiary and not the rights of any 'cinematographic films' or 'tapes'. Indian subsidiary cannot copy any of the programmes included on the channel for the purpose of re-transmitting it later or it cannot modify or delete or cut or edit or otherwise, anything in the course of the distribution to the cable operators. In fact, it has to ensure that the channel is transmitted in its entirety.

Reliance placed by the tax department on the technical explanation is misplaced and was rejected. Moreover, it has been observed that the above technical explanation was issued by the tax authorities of USA and the same is not the official protocol or clarification which has been mutually agreed upon between the two countries. Hence, in any case, the said technical explanation would not bind this Tribunal.

The decisions[2] relied on by the tax department were distinguishable on facts of the present case. The Supreme Court in the case of Performing Rights Society Ltd. relied on by the tax department is actually in favour of the taxpayer as in the said case, the broadcast of the music was conducted by All India Radio from its stations in India, and hence, the source of income was held to be in India. However, in the present case the telecast of the channel happens from outside India. All the other core activities such as procurement/aggregation of the content, editing, uplinking, etc. are conducted by the taxpayer from outside India. Hence, the source of income for the taxpayer, even based on the principle laid down in Performing Arts Society cannot be considered to be in India.

Further, it is also a settled position that merely because the footprint of the satellite is in India and/or advertisers are in India, the source of income cannot be considered to be in India. The Tribunal relied on the decision of the Delhi High Court in the case of Asia Satellite Tele Communications Ltd.[3]. Further, the Tribunal relied on various decisions[4] to support its case.

[2] Pilcom v. CIT [2020] 425 ITR 312 (SC), Performing Rights Society ltd. v. CIT [1977] 106 ITR 11 (SC), MSM Satellite (Singapore) Pte Ltd.
[3] Asia Satellite Tele Communications Ltd. v. DIT 332 ITR 340 (Del)
[4] DDIT (IT) v. SET India Pvt. Ltd. (ITA No.4372/Mum/2004), Sony Pictures Network India Pvt. Ltd. v. DCIT (ITA No. 971/M/2016)

Even if it is contended that the channel has a copyright, what Indian subsidiary is paying for is a right to use the copyrighted article (i.e. if the channel could be considered to be so) by virtue of being permitted to distribute the channel. Accordingly, since Indian subsidiary does not acquire any right in the underlying copyright (i.e. right to modify / reproduce channel / content), the distribution rights granted by the taxpayer to the Indian subsidiary is only a commercial right/broadcast reproduction right. Consequently, consideration received by the taxpayer for the same cannot be treated as royalty or FTS under Article 12 of the tax treaty.

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 Bombay High Court in the case of MSM Satellite Pte. Ltd.[5] 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 Mumbai Tribunal in the case of Taj TV Ltd.[6] held that the distribution income on account of distribution of the pay channel to various cable operators and ultimately to the consumers in India was not in the nature of royalty under the India-Mauritius tax treaty.

Recently, The Delhi Tribunal in the case of Turner Broadcasting System Asia Pacific Inc.[7] 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.

The Mumbai Tribunal in the present case has held that the distribution rights granted by the taxpayer to the Indian entity is only a commercial right/broadcast reproduction right and not a copyright and consequently consideration for the same cannot be treated as royalty or FTS under Article 12 of India-USA tax treaty. The Tribunal observed that the technical explanation provided in the tax treaty was issued by the tax authorities of USA and the same is not the official protocol or clarification which has been mutually agreed upon between the two countries. Hence, the said technical explanation would not bind the Tribunal.

[5] CIT v. MSM Satellite (Singapore) Pte Ltd [2019] 265 Taxman 376 (Bom)
[6] DDIT v. Taj TV Ltd [2016] 72 taxmann.com 143 (Mum)
[7] Turner Broadcasting System Asia Pacific Inc. v. DDIT (ITA No. 1343/Del/2014)

KPMG in India addresses:

Ahmedabad
Commerce House V, 9th Floor,
902, Near Vodafone House, Corporate Road,
Prahlad Nagar,
Ahmedabad – 380 051.
Tel: +91 79 4040 2200

Bengaluru
Embassy Golf Links Business Park,
Pebble Beach, 'B' Block,
1st & 2nd Floor,
Off Intermediate Ring Road, Bengaluru – 560071
Tel: +91 80 6833 5000

Chandigarh
SCO 22-23 (1st Floor),
Sector 8C, Madhya Marg,
Chandigarh – 160 009.
Tel: +91 172 664 4000

Chennai
KRM Towers, Ground Floor,
1, 2 & 3 Floor, Harrington Road,
Chetpet, Chennai – 600 031.
Tel: +91 44 3914 5000

Gurugram
Building No.10, 8th Floor,
DLF Cyber City, Phase II,
Gurugram, Haryana – 122 002.
Tel: +91 124 307 4000

Hyderabad
Salarpuria Knowledge City,
6th Floor, Unit 3, Phase III,
Sy No. 83/1, Plot No 2, Serilingampally Mandal,
Ranga Reddy District,
Hyderabad – 500 081.
Tel: +91 40 6111 6000

Jaipur
Regus Radiant Centre Pvt Ltd.,
Level 6, Jaipur Centre Mall,
B2 By pass Tonk Road,
Jaipur – 302 018.
Tel: +91 141 - 7103224

Kochi
Syama Business Centre,
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682 019.
Tel: +91 484 302 5600

Kolkata
Unit No. 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata – 700 091.
Tel: +91 33 4403 4000

Mumbai
1st Floor, Lodha Excelus,
Apollo Mills,
N. M. Joshi Marg,
Mahalaxmi,
Mumbai – 400 011.
Tel: +91 22 3989 6000

Noida
Unit No. 501, 5th Floor,
Advant Navis Business Park,
Tower-A, Plot# 7, Sector 142,
Expressway Noida,
Gautam Budh Nagar,
Noida – 201 305.
Tel: +91 0120 386 8000

Pune
9th floor, Business Plaza,
Westin Hotel Campus, 36/3-B,
Koregaon Park Annex,
Mundhwa Road, Ghorpadi,
Pune – 411 001.
Tel: +91 20 6747 7000

Vadodara
Ocean Building, 303, 3rd Floor,
Beside Center Square Mall,
Opp. Vadodara Central Mall,
Dr. Vikram Sarabhai Marg,
Vadodara – 390 023.
Tel: +91 265 619 4200

Vijayawada
Door No. 54-15-18E,
Sai Odyssey,
Gurunanak Nagar Road, NH 5,
Opp. Executive Club, Vijayawada,
Krishna District,
Andhra Pradesh – 520 008.
Tel: +91 0866 669 1000

home.kpmg/in

#KPMG josh

home.kpmg/in/socialmedia

KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011
Phone: +91 22 3989 6000, Fax: +91 22 3983 6000