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TAX FLASH NEWS

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Marketing services rendered by a foreign company for Indian company's business outside India are not taxable as FTS

Recently, the Bangalore Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Orkla Asia Pacific Pte Ltd.[1] (the taxpayer) held that marketing services are not taxable as 'Fees for Technical Services' (FTS) under Section 9(1)(vii) of the Income-tax Act, 1961 (the Act) since services were rendered by the taxpayer outside India and such services were utilised in business carried on outside India by an Indian company. Therefore, the services rendered by the taxpayer cannot be deemed to have been accrued or arisen in the hands of the taxpayer in India.

The Tribunal also held that the services were not taxable as FTS under the India-Singapore tax treaty (tax treaty) since such services were not made available technical knowledge, skills, etc. to the Indian subsidiary.

Facts of the case

The taxpayer is a non-resident company incorporated in Singapore. The taxpayer is organised as a support and business development centre for all Orkla group companies in Southeast Asia region. The taxpayer rendered advice, support and assistance in the area of marketing and sales.

The taxpayer had entered into a service agreement with its Indian subsidiary in the year 2010 by which it renders marketing services for the benefit of the Indian company in Southeast Asian country i.e. outside India.

The Assessing Officer (AO) observed that the taxpayer was assisting the Indian subsidiary in market research, product launch, price negotiations, consultancy services by the experienced personnel and also on sales and marketing matters that helps in the business development and decision-making process of the Indian subsidiary. The AO held that the amounts received from the Indian subsidiary were taxable as FTS under the Act as well as under the tax treaty. The DRP upheld the order of the AO.

Tribunal's decision

Taxability under the Act

On perusal of the Service Agreement, it was observed that Indian subsidiary entered into an agreement with taxpayer as a company and not with the employee of taxpayers, who was to render the marketing research and sales support services. The services were rendered by the taxpayer outside India.

The Delhi Tribunal in the cases of Lufthansa Cargo India Pvt. Ltd.[2] and Titan industries Ltd.[3] held that as the source of earning income was outside India the amount paid will be covered in exception provided under Section 9(1)(vii)(b). Further, the Supreme Court in case of GVK Industries Ltd.[4] while dealing with the exception under Section 9(1)(vii)(b), observed that, such exception applies to a situation when fee is payable in respect of services utilised for business or profession carried out by an Indian payer outside India or for the purpose or making or earning of income from any source outside India.

In the instant case, services rendered by the taxpayer were utilised in a business carried on by Indian subsidiary outside India. Therefore, the services rendered by the taxpayer cannot be deemed to have been accrued or arisen in the hands of the taxpayer in India under the Act and not taxable in India.

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[1] Orkla Asia Pacific Pte Ltd. v. DCIT (ITA No. 193/Bang/2019) – Taxsutra.com

[2] Lufthansa Cargo India Pvt. Ltd. v. DCIT [2004] 91 ITD 133 (Del)
[3] Titan industries Ltd v. ITO [2007] 11 SLT 206 (Del)
[4] GVK Industries Ltd. v. ITO [2015] 371 ITR 453 (SC)

Taxability under the tax treaty

Under Article 12(4)(b) of the tax treaty, not only the payment should be in consideration for rendering of technical or consultancy services, but it should also 'make available' technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design.

The meaning of the expression 'make available' was considered by the Mumbai Tribunal in the case of Raymond Ltd.[5] where it was held that rendering of technical services could not be equated with making available the technical services. Similarly, the Karnataka High Court in the case of De Beers India Minerals (P.) Ltd.[6] dealt with similar issue. The High Court held that merely because business of service recipient is dependent on technical service which he receives from service provider, it does not follow that he is making use of technology which service provider utilises for rendering technical services.

The Tribunal observed that nothing is made available by non-resident taxpayer to the Indian subsidiary in India. Consequently, the services rendered by the non-resident taxpayer to the Indian subsidiary were not taxable as per the tax treaty.

Since the non-resident taxpayer does not have a permanent establishment (PE) in India, the income so arising cannot be taxed under Article 7 as 'business profits' either. Accordingly, the addition made by the AO is to be deleted in the hands of the non-resident taxpayer.

Our comments

The Supreme Court in GVK Industries Ltd.[7] while dealing with the exception under Section 9(1)(vii)(b)[8] observed that such exception applies to a situation when fee is payable in respect of services utilised for business or profession carried out by an Indian payer outside India or for the purpose of making or earning of income from any source outside India.

The Tribunal in various cases[9] applied this exception and held that since FTS was utilised in a business carried on by the taxpayer outside India or for earning any income from any source outside India, it will not be deemed to accrue or arise in India in the hands of a non-resident.

It is interesting to note that while dealing with the taxability of testing and certification services paid to a US company for the export of a product to the US, the Delhi Tribunal in the case of Havells India Ltd[10] held that the services have been rendered outside India and have been utilised for the purpose of making or earning any income from any source outside India. Accordingly, such payments would fall outside the purview of Section 9(1)(vii) and will not be deemed to accrue or arise in India. However, the Delhi High Court[11] overruled the Tribunal's decision and observed that the location of the manufacturing activity and conclusion of the export contract from India would determine the source of income. The High Court held that the taxpayer's case does not fall within the exception provided in Section 9(1)(vii)(b) and the FTS paid was taxable under the Act.

The Tribunal in the present case has held that marketing services were not taxable as FTS under Section 9(1)(vii) since such services were rendered by the taxpayer outside India and such services were utilised in business carried on outside India. Therefore, the services rendered by the taxpayer cannot be deemed to have been accrued or arisen in India.

The Tribunal also dealt with taxation of such services under the tax treaty. The Tribunal relying on various decisions dealing with the 'make available' clause held that the services provided by the taxpayer were not taxable as FTS under the tax treaty since such services were not made available technical knowledge, skills, etc. to the Indian subsidiary.

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[5] Raymond Ltd. v. DCIT [2003] 86 ITD 791 (Mum)
[6] CIT v. De Beers India Minerals (P.) Ltd. (2012) 21 taxmann.com 214 (Kar)
[7] GVK Industries Ltd. v. ITO [2015] 371 ITR 453 (SC)
[8] Non-taxability of services utilised in a business or profession, carried on by Indian resident, outside India or for the purposes of making or earning any income from any source outside India
[9] Aqua Omega Services (P.) Ltd. v. ACIT [2013] 31 taxmann.com 179 (Chennai), ADIT v. DQ Entertainment (International) P. Ltd. [2014] 164 TTJ 84 (Hyderabad), Nissan Motor India (P.) Ltd. v. DCIT [2018] 92 taxmann.com 127 (Chennai)

[10] Havells India Ltd v. ACIT [2011] 140 TTJ 283 (Del)
[11] CIT v. Havells India Ltd [2013] 352 ITR 376 (Del)

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