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TAX FLASH NEWS

25 October 2021

Export commission is not taxable as FTS by invoking MFN clause under the India-France tax treaty

Recently, the Delhi Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Rajinder Kumar Aggarwal (HUF)[1] (the taxpayer) dealt with the issue of taxability of export commission paid to non-resident agent in France. The Tribunal held that export commission paid to agent in France is not taxable as Fee for Technical Services (FTS) under the India-France tax treaty (tax treaty) by invoking the 'Most Favoured Nation' (MFN)[2] clause.

Facts of the case

The taxpayer, a Hindu Undivided Family (HUF), was engaged in the business of manufacturing and export of leather footwear in the name of proprietary concern 'Regency Impex'. The taxpayer appointed a non-resident entity as its agent (France based entity) for procuring export orders in France.

During the Assessment Year 2012-13, the taxpayer paid commission on export sales and no tax was deducted at source on said payment. The taxpayer claimed that the commission was business income and in the absence of foreign entity's Permanent Establishment (PE), no income was chargeable to tax in India. Accordingly, the taxpayer was not required to deduct tax at source under Section 195.

The Assessing Officer (AO) rejected the contention of the taxpayer and held the export commission was liable to be taxed as FTS. Therefore, the taxpayer was liable to deduct tax on the said payment under Section 195. Consequently, the taxpayer was liable for disallowance of such export commission under Section 40(a)(i). The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the finding of the AO.

Tribunal's decision

The tax department could not bring any evidence as regard to change of scope of services rendered by the foreign agent in the year under consideration as compared to earlier year. According to the agreements, the rate of the commission was 9 per cent for the period from 1 April 2011 to 30 September 2011 and 10 per cent for the period from 1 October 2011 to 31 March 2012. In the AY 2010-11, the said rate of the commission was 8 per cent as observed by the Tribunal[3]. In the said AY, the Tribunal has dismissed the appeal of the tax department observing that the commission was paid to a non-resident agent (payee) who is a tax resident of France. The payee was simply assisting procuring export orders for the taxpayer in his ordinary course of business in France. The commission was paid for activities of the payee outside India and the amount is received by the payee outside India through normal banking channels. The commission income paid to the foreign agent neither accrued in India nor deemed to be accrued in India as per deeming provisions of Section 9 and nor the same was received nor deemed to be received in India.

The Delhi High Court in the case of Steria India Ltd[4] held that MFN clause of the protocol will form an integral part of India-France tax treaty and it will be automatically applicable without any further notification. Therefore, in view of MFN clause, the beneficial provision of the tax treaty between India and other OECD country, i.e., U.K. automatically extends to India-France tax treaty. Under the India-U.K. tax treaty, FTS exclude the term 'managerial services' and provides for 'make available clause'. While analyzing the FTS definition as per the India-France tax treaty, in view of the MFN clause, the entire definition of the FTS can be imported from India-U.K. tax treaty.

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[1] Rajinder Kumar Aggarwal (HUF) v. DCIT (ITA No.2996/Del/2016) – Taxsutra.com

[2] due to non-fulfilment of 'make available' clause read into India-France tax treaty from India-U.K. tax treaty

[3] ACIT v. Rajinder Kumar Aggarwal (HUF) (ITA No. 4142/Del/2015)

[4] Steria India Ltd v. DCIT [2018] 255 Taxman 110 (Del)

Applying the ratio of the decision of the Delhi High Court in the case of Steria (India) Ltd to the facts of the present case, it was observed that for bringing the services under the net of FTS under the India-France tax treaty, the 'make available' clause has to be satisfied. However, in the services rendered by the non-resident of procuring export order for the taxpayer, no knowledge has been provided to the taxpayer which could be exploited further by the taxpayer. In such circumstances, the services rendered by the non-resident cannot be held as 'FTS' under the India-France tax treaty. Accordingly, such services will not be chargeable in India in the hands of non-resident under the tax treaty and, therefore, TDS provisions under Section 195 were not applicable. Consequently, the payment to the said non-resident was not liable to disallowance under Section 40(a)(i).

Our comments

Various tax treaties entered into by India have beneficial MFN clause for e.g. tax treaties with Netherlands, Sweden, France, Spain, Hungary, etc.

In some of the cases[5], Courts/Tribunal have held that the restricted scope with respect to FTS under various OECD tax treaties[6], was applicable to the India-France tax treaty and hence services were held to be not taxable as FTS by virtue of beneficial 'make available' clause under the relevant tax treaties.

However, Courts in some of the cases[7], based on specific facts of those cases, have held that managerial services rendered by a foreign company were taxable as FTS under Article 13(4) of India-France tax treaty in spite of MFN clause provided under the tax treaty.

The Tribunal in the present has relied on the India-U.K. tax treaty to import the term 'make available' by involving MFN clause in the India-France tax treaty and held that services provided by non-resident entity were not taxable as FTS in India.

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[5] DDIT v. IATA BSP India (ITA No. 1149/Mum/2010), Steria India Ltd v. DCIT [2018] 255 Taxman 110 (Del)
[6] India-US, India-UK, India-Portuguese tax treaty
[7] Mersen India Private Limited [2013] 353 ITR 628 (AAR), Steria (India) Ltd [2014] 45 taxmann.com (AAR)

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