Services provided by the Bombay Stock Exchange to transact a business of sale and purchase of shares do not amount to fees for technical services – Supreme Court

Background

Recently, the Supreme Court in the case of Kotak Securities Ltd.¹, held that services provided by the Bombay Stock Exchange (BSE) to transact a business of sale and purchase of shares do not amount to Fees for Technical Services (FTS). The Supreme Court observed that the services provided failed the test of a specialised, exclusive and individual requirement of the user. In the absence of the same, the service, though rendered, would be merely in the nature of a facility offered. Therefore, such services are not FTS under Section 9(1)(vii) of the Income-tax Act, 1961 (the Act) and tax is not required to be deducted under Section 194J of the Act.

Facts of the case

- The Bombay High Court held that the transaction charges paid by a member of the BSE to transact a business of sale and purchase of shares amounts to a payment of FTS. On such payments, tax was deductible at source under Section 194J of the Act. Since tax was not deducted at source, transaction charges paid by the taxpayer were disallowed under Section 40(a)(ia) of the Act².

- Aggrieved by the Bombay High Court decision, the taxpayer appealed before the Supreme Court.

The Supreme Court’s ruling

Services are in the nature of a facility offered and not FTS

- The Supreme Court in the case of Bharti Cellular Ltd.³ dealt with the meaning of the word ‘technical services’ appearing in Explanation 2 to Section 9(1)(vii) of the Act. The Supreme Court held that the words ‘technical services’ have to be read in the narrower sense by applying the rule of ‘noscitur a sociis’⁴, particularly, because the words ‘technical services’ come in between the words ‘managerial and consultancy services’.

¹ CIT v. Kotak Securities Ltd. [2016] 67 taxmann.com 356 (SC)
² However, the Bombay High Court observed that in view of the apparent understanding between the taxpayer and the tax department with regards to the liability to deduct tax at source on the transaction charges paid to the BSE right from the year 1995 i.e. coming into effect of Section 194J of the Act till the assessment year in question, benefit should be granted to the taxpayer and the disallowance made by the tax officer under Section 40(a)(ia) of the Act was not correct. The Supreme Court has observed that it was not necessary to examine the correctness of the view taken by the Bombay High Court on the issue of the disallowance under Section 40(a)(ia) of the Act.
³ CIT v. Bharti Cellular Ltd. [2011] 330 ITR 239 (SC)
⁴ Meaning of an unclear word or phrase is to be determined (constructed) on the basis of its context, the words or phrases surrounding it
Service made available by the BSE online trading system

- The service made available by the BSE Online Trading System (BOLT) for which charges have been paid by the taxpayer, are common services that every member of the stock exchange is necessarily required to avail of to carry out trading in securities at the stock exchange.

- A member who wants to conduct his/her daily business in the stock exchange has no option but to avail of such services. Every transaction by a member involves the use of the services provided by the stock exchange for which a member is compulsorily required to pay an additional charge (based on the transaction value) over and above the charges for the membership of the stock exchange.

- These features of the services provided by the stock exchange are a kind of a facility provided for transacting business rather than a technical service. These features are provided to one or a section of the members of the stock exchange to deal with special situations faced by such a member(s) or the special needs of such member(s) during the conduct of business at the stock exchange.

- The view taken by the Bombay High Court that the transaction charges paid to the BSE by its members are for 'technical services' rendered is not an appropriate view. Such charges are in the nature of payments made for facilities provided by the stock exchange. Tax is not required to be deducted under Section 194J of the Act.

Our comments

The Supreme Court has held that the services made available by the BSE are common services and every member of the BSE is required to avail of them. There is no special, exclusive or customised service that is being rendered by the stock exchange. These features of the services provided...
are a kind of facility provided, rather than a technical service; and therefore, such services do not amount to ‘technical services’. Consequently, tax is not required to be deducted under Section 194J of the Act.

The Supreme Court in this decision has dealt with an important principle that to consider a service as technical in nature, there has to be exclusivity. Such services needs to be customised for the service recipient. Standard/common services provided by the service provider do not amount to technical services.
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