

## TAX FLASH NEWS

### Management and procurement services do not make available any technical knowledge, skills, etc. and, therefore, are not taxable as fees for technical services under the India-UK tax treaty

#### Background

Recently, the Authority for Advance Rulings (the AAR) in the case of Measurement Technology Ltd.<sup>1</sup> (the applicant) held that services rendered by a group director to its group company in India are 'managerial services'<sup>2</sup>. Such management services and procurement services rendered by the UK procurement team do not make available any technical knowledge, skills, etc. Therefore, such services are not taxable as Fees for Technical Services (FTS) under the India-UK tax treaty (the tax treaty). Further, these services are general and routine in nature and do not create any intellectual property and therefore, it will not qualify as royalty under the tax treaty.

#### Facts of the case

- The applicant is a company incorporated in the UK and is engaged in the development and supply of intrinsic safety explosion protection devices, field bus and industrial networks, etc. It is a wholly owned subsidiary of MTL Instruments Group Ltd., UK (MTL UK).
- MTL Instruments Private Limited (MTL India) is an Indian company, and a subsidiary of MTL UK. MTL India is engaged in the business of manufacturing industrial control equipment used for process control in hazardous environments.
- The applicant entered into two service agreements with MTL India for providing certain services. The first agreement is MTL Instruments Intra Group agreement for products and services according to which the nature of services (hereinafter referred to as 'Management Services') provided by the applicant are as follows:
  - Strategy and direction of business development of MTL India.
  - Attendance in person or by phone at regular operational meetings to discuss the progress of financial and operational activities.
  - Management of personnel including conducting staff interviews, setting individual targets and carrying out performance appraisals.
  - Any other services related to the above.
- The above mentioned services were provided through one of the employees of the applicant based in the UK designated as Group Operations Director (GD) by means of telephone calls, e-mails and occasional visits to India.
- While sitting in the UK, the GD monitors the financial and operational progress of activities of MTL India. The GD also renders services as regards human resource matters of MTL India such as hiring new personnel, setting up individual performance targets, assisting in performance appraisal, etc. The GD was also involved in quality and design reviews.
- As per the first agreement, MTL India shall compensate the applicant for providing the 'management services' at cost plus 5 per cent and for this purpose only 50 per cent of the cost (total remuneration of the GD) is allocated by MTL UK.

<sup>1</sup> Measurement Technology Ltd. (A.A.R. No 966 of 2010) - Taxsutra.com

<sup>2</sup> Under the old India-UK tax treaty, 'managerial services' were covered in the FTS Article. The tax treaty has been amended with effect from 11 February 1994. The words 'managerial services' have been omitted in the definition of FTS under the tax treaty.

- The second agreement was entered i.e. 'Intercompany Services Agreement' to provide procurement services with a view to reduce cost and to avoid duplication of procurement efforts within the MTL Group. As per the agreement, the applicant had constituted a procurement team in the UK to look into the global sourcing requirements of raw materials within the MTL Group including MTL India.
- The procurement team travels to different countries to visit suppliers and distributors to determine the best price that would be available to MTL group. Their services include setting up the material supply chain, logistic support and providing support to resolve technical issues with supplies from global sources.
- MTL UK was compensated for the procurement services on a cost to cost basis (without any mark-up) and for this purpose only 30 per cent of the cost of the procurement term was allocated to MTL India.

## AAR's ruling

### Management Services

- Under Article 13(4) of the tax treaty dated 11 November 1981 (earlier tax treaty), the FTS, *inter alia*, meant payments in consideration for services of a managerial, technical or consultancy in nature. The earlier tax treaty was amended with effect from 11 February 1994.
- After such amendment, managerial services are not covered in the definition of FTS and even technical or consultancy services, if they do not meet the criteria of 'make available', cannot be treated as FTS.
- The services under the first agreement relate to review by the GD and general guidance given by him on financial, operational, human resource, targets and performance appraisal related matters.
- The GD provides these services mainly from the UK and his visits during a year are generally for a short duration having an aggregate number of days of visit in a year never exceeding 30 days. The AAR held that these are routine managerial activities and cannot be classified as technical or consultancy services.
- In the case of *Invensys Systems*<sup>3</sup>, the AAR held that even though some of the services may have the trappings of technical or consultancy services, looking at the nature and the predominant nature of the services, they primarily fall under the category of 'managerial services'.

<sup>3</sup> *Invensys Systems Inc.* [2009] 183 Taxman 81 (AAR)

- In the present case, the AAR held that by providing such services, the GD was not making available any technical knowledge of enduring benefit in nature which would enable employees of MTL India to apply them on their own in future.

### Procurement Services

- In relation to the procurement services provided under the second agreement, the procurement team travels to different countries to visit suppliers and distributors to determine the best price that would be available to the entire MTL Group including MTL India. These types of services can never be classified as technical or consultancy in nature and were not making available any technical knowledge, experience, know-how, etc.
- The AAR rejected the reliance of the revenue on the rulings in the case of *Intertek Testing Services*<sup>4</sup> and *GVK Industries*<sup>5</sup>.

### Service PE

- The tax department may ascertain the facts in the course of the assessment proceedings, whether visits by employees other than the GD, were for more than 30 days in a year and constituted a 'service PE' under Article 5(3)(k) of the India-UK Tax Treaty.

### Services do not constitute royalty

- The services provided under both the agreements are general and routine in nature and do not create any intellectual property and therefore, rendering of such services would not qualify as royalty as per the provisions of Article 13 of the tax treaty.
- Accordingly, the amount received by the applicant for services rendered as per both the agreements is not chargeable to tax in India as per the provisions of the tax treaty.

## Our comments

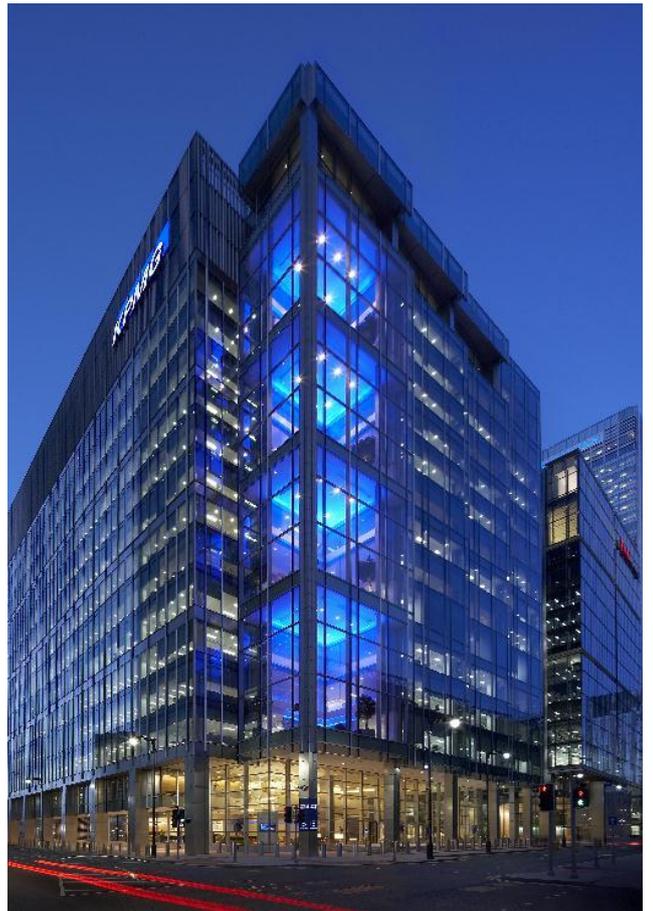
This is welcome ruling of the AAR where it has been held that the consideration received by the applicant for management and procurement services is not taxable in India as per the provisions of the India-UK tax treaty since such services do not make available any technical knowledge, skills, etc. The AAR observed that managerial services are not covered in

<sup>4</sup> *Intertek Testing Services India Pvt. Ltd.* [2008] 307 ITR 418 (AAR)

<sup>5</sup> *GVK Industries Ltd. v. ITO* [1997] 228 ITR 564 (AP)

the definition of FTS in the tax treaty and the same are routine managerial activities and cannot be classified as technical or consultancy services. Further, the AAR also observed that procurement services can never be classified as technical or consultancy in nature and therefore, such services are not FTS under the tax treaty.

The Delhi Tribunal in the case of Adidas Sourcing Limited<sup>6</sup> held that buying agency services were purely in the nature of procurement services and hence, cannot be characterised as managerial, technical or consultancy services. Accordingly, the consideration received by the taxpayer was classified as 'commission' and not FTS under the Income-tax Act, 1961.



---

<sup>6</sup> Adidas Sourcing Limited v. ADIT [2013] 55 SOT 245 (Del)

[www.kpmg.com/in](http://www.kpmg.com/in)

**Ahmedabad**

Commerce House V, 9th Floor,  
902 & 903, Near Vodafone House,  
Corporate Road,  
Prahlad Nagar,  
Ahmedabad – 380 051  
Tel: +91 79 4040 2200  
Fax: +91 79 4040 2244

**Bengaluru**

Maruthi Info-Tech Centre  
11-12/1, Inner Ring Road  
Koramangala, Bangalore 560 071  
Tel: +91 80 3980 6000  
Fax: +91 80 3980 6999

**Chandigarh**

SCO 22-23 (1st Floor)  
Sector 8C, Madhya Marg  
Chandigarh 160 009  
Tel: +91 172 393 5777/781  
Fax: +91 172 393 5780

**Chennai**

No.10, Mahatma Gandhi Road  
Nungambakkam  
Chennai 600 034  
Tel: +91 44 3914 5000  
Fax: +91 44 3914 5999

**Delhi**

Building No.10, 8th Floor  
DLF Cyber City, Phase II  
Gurgaon, Haryana 122 002  
Tel: +91 124 307 4000  
Fax: +91 124 254 9101

**Hyderabad**

8-2-618/2  
Reliance Humsafar, 4th Floor  
Road No.11, Banjara Hills  
Hyderabad 500 034  
Tel: +91 40 3046 5000  
Fax: +91 40 3046 5299

**Kochi**

Syama Business Center  
3rd Floor, NH By Pass Road,  
Vytilla, Kochi – 682019  
Tel: +91 484 302 7000  
Fax: +91 484 302 7001

**Kolkata**

Unit No. 603 – 604,  
6th Floor, Tower – 1,  
Godrej Waterside,  
Sector – V, Salt Lake,  
Kolkata 700 091  
Tel: +91 33 44034000  
Fax: +91 33 44034199

**Mumbai**

Lodha Excelus, Apollo Mills  
N. M. Joshi Marg  
Mahalaxmi, Mumbai 400 011  
Tel: +91 22 3989 6000  
Fax: +91 22 3983 6000

**Noida**

6th Floor, Tower A  
Advant Navis Business Park  
Plot No. 07, Sector 142  
Noida Express Way  
Noida 201 305  
Tel: +91 0120 386 8000  
Fax: +91 0120 386 8999

**Pune**

703, Godrej Castlemaine  
Bund Garden  
Pune 411 001  
Tel: +91 20 3050 4000  
Fax: +91 20 3050 4010

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2015 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.

The KPMG name, logo and "cutting through complexity" are registered trademarks or trademarks of KPMG International Cooperative ("KPMG International").

This document is meant for e-communications only.

© 2015 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.