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Revenue earned from distribution of news and financial information products is not taxable in India, in the absence of a dependent agent PE and service PE under the India-UK tax treaty

Background

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Reuters Limited[1] (the taxpayer) held that the revenue earned from distribution of news and financial information products by the taxpayer is not taxable in India, in the absence of a dependant Agency Permanent Establishment (PE) and service PE under the India-U.K. tax treaty (tax treaty).

The Tribunal observed that the taxpayer's distributor in India i.e. an Indian subsidiary is not a dependent agent of the taxpayer. The qualified character of the agency is the authorisation to act on behalf of somebody else so much as to conclude the contracts. The Indian subsidiary is not acting on behalf of the taxpayer. It is an independent entity and the relationship between the taxpayer and the Indian subsidiary is on a principal-to-principal basis.

The Tribunal also observed that the employee deputed by the taxpayer in the form of a News Bureau Chief (NBC) cannot be constituted as a service PE in India, since such an employee has nothing to do with services provided by the taxpayer to the distributor. NBC was only acting as a chief reporter and text correspondent in India in the field of collection and dissemination of news.

Facts of the case

- The taxpayer is a resident of the U.K. It is engaged in the business of providing worldwide news and financial information products. The taxpayer produces, compiles and distributes news and financial information products through the 'Reuters Global Network' with a vast global communication network. Such network consists of data storage facilities situated in three locations i.e. London, New York and Singapore, which are linked by satellite links and terrestrial lines.
- The taxpayer uses the network to receive and transmit information and provide access to the compiled news and edited financial information to distributors in various countries. In India, the taxpayer provides Reuters products to its Indian subsidiary named as Reuters India Private Limited (RIPL) under certain specified agreements. In turn, the RIPL distributes Reuters products to the Indian subscribers independently in its own name.
- The taxpayer entered into three kinds of contractual agreements with RIPL i.e. license agreement, product distribution agreement and distributor agreement. Under the distributor agreement, RIPL has been appointed as the distributor to sell designated Reuter products to subscribers in India using the Reuters Global Network.
- Under the aforesaid agreement, the taxpayer provides RIPL, connection to the Reuters Global Network whereby products are made available to the RIPL, which are then distributed by RIPL to various subscribers in India independently.
- During the relevant year the taxpayer had deputed Mr. Simon Cameron Moore, as the NBC of Mumbai for gathering, writing and distributing the news and overall coverage of news.
- In terms of the distributor agreement, the taxpayer had received distribution fees which were claimed to be not taxable in India in the absence of a PE.

[1] Reuters Limited v. DCIT (ITA No. 7895/Mum/2011) (Mum) – Taxsutra.com

- The Assessing Officer (AO) held that the revenue earned by the taxpayer was taxable as Fees for Technical Services (FTS) under Article 13 of the tax treaty. It was further held that RIPL constituted to be a dependent agent PE in India under Article 5(5) of the tax treaty and therefore, income was taxable under Section 44D of the Income-tax Act, 1961 (the Act) on gross basis.
- The Dispute Resolution Panel (DRP) held that the taxpayer had a PE in India in the form of RIPL, as it was dedicated for the business of the taxpayer. Further, Mr. Simon Moore was deployed in India as NBC during the relevant period, for rendering service to RIPL on the taxpayer's behalf and such services will constitute a service PE in India.
- Accordingly, the AO passed the order in pursuance of the directions of the DRP. The AO taxed the entire distribution fee on a gross basis at 20 per cent under Section 44D read with Section 115A of the Act.

Tribunal's ruling

Agency PE

- On referring to Article 5(4) and 5(5) of the tax treaty, it indicates that an agent is deemed to be a PE, if he is not independent and habitually exercises an authority to conclude contracts on behalf of the enterprise or if he has no such authority, but habitually maintains a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise or he habitually secures orders solely or almost wholly for the enterprise. If any of these conditions mentioned in Article 5(4) of the tax treaty is not fulfilled, the agent cannot constitute a PE for the foreign enterprise.
- On referring to the relevant terms of the distribution agreement, it indicates that nowhere has it been specified or that there is any mandate that RIPL was habitually exercising its authority to negotiate and to conclude the contracts on behalf of the taxpayer in the territory of India, which is binding or can bind the taxpayer. It envisages simply delivering of taxpayer's services for a price which can be further distributed by RIPL for earning of its own revenue.
- There was no clause in the agreement that RIPL would act as an agent on behalf of the taxpayer *qua* the distribution to subscribers. In fact, RIPL has an independent contract with the subscribers, which was evident from the contract agreement between RIPL and third party subscribers in India.
- Similarly, when RIPL was supplying news and material to the taxpayer, the same is again on a principal-to-principal basis. The second condition as mentioned in Article 5(4) of the tax treaty, also was not fulfilled, because RIPL was not habitually maintaining stock of any goods and merchandise for which it can be held that it was regularly delivering goods on behalf of taxpayer. Lastly, it was not habitually securing the orders wholly and almost wholly for taxpayer.
- RIPL was earning substantial income from its own dealing with third party customers which was evident from the contract entered into by the third parties and also from the income shown from 'subscription fee' by RIPL from third party customers.
- Nothing was evident from the distribution agreement or financial accounts that RIPL was acting as an agent of the taxpayer. The character of an agent under Article 5(4) of the tax treaty which can be said to be dependent is that the commercial activities of the agent for the enterprise are subject to instructions or comprehensive control and it does not bear the entrepreneur risk.
- The main thrust of an agent being a PE under the tax treaty is whether the agent has an authority to conclude contracts in the name of the enterprise. Thus, the qualified character of the agency is the authorisation to act on behalf of somebody else so much so as to conclude the contracts.
- In the present case, there were no such terms which were borne out from the distribution agreement that RIPL was only acting on behalf of taxpayer or is any kind of a dependent agent. RIPL was a completely an independent entity and the relationship between the taxpayer and RIPL was on a principal-to-principal basis.
- Even under Article 5(5) of the tax treaty, the foremost condition is that the activities of such an agent are devoted wholly or almost wholly on behalf of the enterprise. In the present case, the activities of RIPL cannot be said to be devoted wholly or almost wholly on behalf of the taxpayer as it had entered into contracts with subscribers in India on an independent and a principal-to-principal basis for earning and generating its revenues.
- In fact revenue from third party subscribes was far excess than the transaction with the taxpayer. In the present case, it was not the case that RIPL was completely or wholly doing an activity for taxpayer and earning income wholly from taxpayer only. Thus, the conditions laid down in Article 5(5) of the tax treaty were also not fulfilled.

Service PE

- On reference to provisions of Article 5(2)(k) of the tax treaty, it is clear that an enterprise shall be deemed to have a PE in India if it furnishes managerial or other services except services which are taxable as 'royalty' or 'fees for technical

services', through employees or other personnel, provided the duration of activities within the contracting state exceeds the prescribed period. The main thrust of Article 5(2)(k) of the tax treaty is furnishing of services through employees or other personnel in another contracting state.

- The NBC was a very senior and experienced reporter or correspondent who was responsible for collecting and analysing the news and holds a management position in the news centre or news room. He was mainly responsible for coordinating the efforts of the reporting staff to investigate and cover stories for dissemination of news to print and media outlets. He has been assigned to India by the taxpayer as a 'Text Correspondent' to perform functions of a Bureau Chief. In this case, his functions and duties had nothing to do with, in so far as the distribution agreement is concerned.
- There was no furnishing of services by the NBC to the RIPL which had lead to earning of a distribution fee to the taxpayer. The NBC has nothing to do for providing of taxpayer's services to the distributor. Thus, it cannot be held that the NBC constitutes a service PE in India for the taxpayer under Article 5(2)(k) of the tax treaty as he had not furnished any services in India on which the taxpayer had earned the distribution fee.

Accordingly, it was held that neither under Article 5(2)(k) nor under Article 5(4) read with 5(5) of the tax treaty, the taxpayer had a PE in India and, therefore, the distribution fee received by the taxpayer cannot be held to be taxable in India.

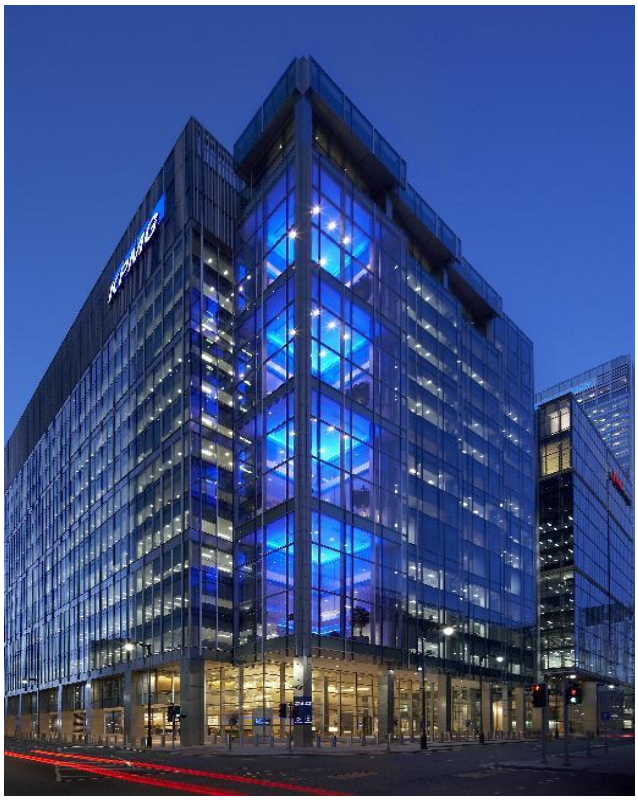
Our comments

Post liberalisation many more global companies are focusing on India as a market for their products and services. These companies often use the services of Indian enterprises to sell their products and services in the country. In many cases, such arrangements may cause a dependent agency PE of a foreign enterprise in India.

In the case of E-Funds Corporation[2], the Delhi High Court held that the subsidiary by itself cannot be considered to be a dependent agent PE of the principal. However, a subsidiary may become a dependent or an independent PE agent provided the tests specified under Article 5(4) and 5(5) of the relevant tax treaty are satisfied. The transactions between the taxpayers and E-Fund India were at an arm's length and were also taxed on the arm's length principle and therefore, requirements of Article 5(5) were not satisfied. Therefore, there was no agency PE of the taxpayer in India.

The Mumbai Tribunal in the case of Varian India Pvt. Ltd.[3] held that an Indian branch does not constitute a dependent agent PE of the USA parent and overseas group companies under the India-USA tax treaty, since the taxpayer does not have the authority to negotiate or conclude contracts on behalf of foreign companies. Further, neither does it maintain a stock of goods sold by such foreign companies nor does it secure orders on behalf of foreign companies in India.

The Mumbai Tribunal in the present case has held that the revenue earned from distribution of news and financial information products is not taxable in India in the absence of a dependent agent PE or service PE under the India-U.K. tax treaty.



[2] DIT v. E-Funds Corporation [2014] 364 ITR 256 (Delhi)

[3] Varian India Pvt Ltd. v. ADIT [2013] 33 taxmann.com 249 (Mum)

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