Marketing services for expansion of business overseas are not in the nature of fees for technical services

Background
The Kolkata Tribunal in the case of Batlivala & Karani Securities (India) (P.) Ltd¹ (the taxpayer) held that payment towards marketing support services and expansion of business abroad do not constitute Fees for Technical services (FTS) in accordance with India-UK and India – Singapore tax treaties.

Since there is no Permanent Establishment (PE) in India, the said payments cannot be taxed as business profits in India. Therefore, no disallowance under Section 40(a)(ia) of the Income-tax Act, 1961 (the Act) is attracted.

Facts of the case
- The taxpayer is a stock broker company and carries on the business of brokerage on behalf of its institutional clients.
- During the year under consideration, the taxpayer company made payments to its subsidiaries in the U.K. and Singapore for providing marketing support services and towards the expansion of its business in the U.K. and Singapore along with the European region and the South East Asian countries respectively.
- As consideration for their services, the taxpayer company remunerated the subsidiaries by reimbursing their costs along with a service fee of 29 per cent on the costs. No tax was deducted at source on such reimbursement of costs made to the subsidiaries.
- The Assessing Officer (AO) considered that the taxpayer company was bound to deduct tax at source on the entire remittance (including reimbursement) since the entire payment made to the non-resident subsidiaries constituted FTS and were taxable in their hands. Pursuant to, the AO disallowed the payment made as reimbursement to the subsidiary under Section 40(a)(ia) of the Act for non-deduction of Tax at Source (TDS)
- The Commissioner of Income Tax (Appeals) upheld the disallowance by observing that TDS was required to be deducted on gross payments by the taxpayer.

Tribunal ruling
- The services provided by the subsidiaries were in the nature of marketing services of introducing foreign institutional investors to invest in the capital markets in India.
- Article 12(4) of the India- Singapore tax treaty and Article 13(4) of the India-UK tax treaty is the same as Article 12(4)(b) of the India-US tax treaty and thus the Memorandum of Understanding to the India-US treaty could be used as aid to understand if services constituted FTS.
- Given the language used in the tax treaties, unless services also make available technical knowledge, skill, experiences, etc. to the recipient of the services, the same do not qualify as FTS under the tax treaties. Since no technical service was being made available to the taxpayer by its subsidiaries, payments did not fall within the definition of FTS as per the provisions of the tax treaties.

¹ Batlivala & Karani Securities (India) (P.) Ltd [2016] 71 taxmann.com 142 (Kol)
This decision also covers other issues. However, this Flash news only deals with the issue pertaining to whether marketing services constitute Fees for technical services.

© 2016 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.
• As the subsidiaries had no PE in India, the said payments could not be taxed in India even as business profits.

• The provisions of the tax treaties being more beneficial to the taxpayer, the Tribunal did not analyse the taxability in terms of the Act by considering it as academic in nature.

• In considering the retrospective amendment in Explanation 2 to Section 195(1) of the Act with effect from 1962, the Tribunal held that it is not possible to fasten a liability to deduct tax at source basis a retrospective amendment. Reliance for the same was placed on the decision in the case of Subhotosh Majumder².

• As no income was chargeable to tax in India, relying on the Supreme Court’s decision in case of GE India Technology Centre P Ltd.³ directed the AO to delete the disallowance.

Our comments

The issue of whether particular services constitutes FTS has been a subject matter of debate before the courts. The type of service, arrangements/agreements between the parties, and related facts of the case plays a pivotal role in deciding whether the nature of services can be said to fall under the category of FTS.

In the instant case, the Kolkata Tribunal observed that marketing services provided by the subsidiaries do not fall under FTS as the services do not make available technical knowledge, experience, etc. to the taxpayer. Also, since the subsidiaries had no PE in India, the payments were not taxable in India in view of the provisions of India-UK and India-Singapore tax treaties.

The ruling, however, did not examine the nature of payment under the Act. Courts have in certain cases⁴ observed that payment made to agents for promoting business in a foreign country do not fall within the meaning of FTS under Section 9(i)(vii) of the Act. This decision is yet another example where the courts have emphasised the test of ‘make available’ for constituting FTS under the beneficial tax treaties.

---

² DCIT v. Subhotosh Majumder [2016] 65 taxmann.com 42 (Kol)
³ GE India Technology Centre P Ltd v. CIT [2010] 327 ITR 456 (SC)
⁴ Le Passage to India Tours & Travel (P.) Ltd. v. DCIT [2015] 54 taxmann.com 138 (Del)
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.