

INTERNATIONAL TAXATION

Case Law Update

CA Tarunkumar Singhal, Dr. Sunil Moti Lala, *Advocate* & CA Harsh Bafna

A. High Court

1 ***PCIT vs. Luwa India Pvt. Ltd. [TS-281-HC-2021 (KAR)-TP]***

While exercising jurisdiction u/s 92CA(3), the TPO can only determine the ALP of an international transaction and the said jurisdiction cannot be extended further to examine the allowability of the claim by applying the benefit test or the conditions as provided under Section 37(1) of the Act

Facts

i) The assessee, a domestic company was engaged in the business of manufacturing textiles machines for textile manufacturers in India. During the year under consideration i.e. AY 2007-08, the assessee, entered into several international transactions with its AE viz. for import of raw materials, spare parts and components, export of components of textile machinery, purchase of office equipment, payment of royalty and management fees and reimbursement of expenses. For the purpose of benchmarking its aforesaid international transaction, the assessee consolidated the transactions of purchases, royalty payment and sales and applied TNMM as the most appropriate method on an entity level basis and concluded that its aforesaid international transactions were at ALP.

ii) During the course of assessment, the TPO segregated the royalty transaction by treating it as an independent international transaction. By applying the Comparable Uncontrolled Price method, the TPO determined the ALP of said royalty payment at Nil on the ground that the assessee had failed to demonstrate receipt of technology, consequential economic benefit and proof as to whether its other group concerns or third parties were being charged for the identical royalty payment.

iii) On appeal, the CIT(A) deleted the aforesaid TP adjustment by observing that the assessee had produced relevant records including the agreement under which the technical know-how was granted to the assessee. The CIT(A) also accepted the methodology adopted by the assessee for benchmarking i.e. consolidation of all the transactions and applying TNMM on an entity level.

iv) On appeal by the Revenue against the order of the CIT(A), the Tribunal inter alia held that that the TPO was not justified in making the TP adjustment by determining the ALP of royalty payment as NIL when the assessee had produced the agreement between the assessee and its AE under which license was granted to the assessee to use technical know-how belonging to the AE for the purpose of manufacturing activity. Further, the Tribunal also observed that the jurisdiction of the TPO was limited i.e. to determine the ALP of its international transactions by comparing it with uncontrolled comparable price and could not be extended further to examine the allowability of the claim by applying the benefit test or the conditions as provided under Section 37(1) of the Act.

v) On Revenue's appeal before the Hon'ble Karnataka HC, the HC held as under:

Decision

i) The Karnataka High Court upheld the order of the Tribunal by observing that the issue whether the TPO while exercising jurisdiction u/s 92CA(3), can only determine the ALP of an international transaction was no longer a res integra as the same was already covered in favour of the assessee by the Hon'ble Delhi High Court in ***CIT vs. EKL Appliances Ltd. [2012] 24 taxmann.com 199 (Delhi)*** and Hon'ble Bombay High Court in ***CIT vs. Lever India Exports Ltd [2017] 78 taxmann.com 88 (Bombay)***.

ii) In view of the above findings, the Karnataka High Court dismissed the Revenue's appeal.

B. Tribunal

2 ***Prime Oceanic Pvt. Ltd vs. ITO [TS-450-ITAT-2021(JPR)] (ITA No. 652/JP/2019)***

Section 9(1)(vii) of the Act is not attracted when the assessee utilises the services of a non-resident service provider outside of India, for the purposes of earning commission income from its customers/ shipping companies outside of India

Facts

i) The assessee, a domestic commission agent was engaged in providing shipping services to its clients at various ports located all over the world. During the year under consideration i.e. AY 2013-14, the assessee availed sales and marketing services (i.e. introducing new clients as well as obtaining business) of M/s Trans Coral Shipping FZE, a company incorporated under the laws of UAE (hereinafter referred to as 'Trans Coral'). The assessee claimed that no taxes were required to be withheld u/s 195 of the Act on the said payments since the said payments were made for procuring the business from outside India for which no technical services were required or rendered and the income of the recipient i.e. Trans Coral was not chargeable to tax in India.

ii) During the course of assessment proceedings, the AO found that the assessee was engaged in a joint venture business with Trans Coral and the payment made to Trans Coral was merely a distribution of income and not an expense. The AO further observed that as per the Agency agreement, a fixed amount equivalent to 10% of the total commission receipt was to be shared in addition to one-third of the commission, in case the total commission received by the assessee exceeds INR 50 Lacs. In light of the above, the AO invoked provisions of section 9(1)(vii)(b) r.w section 195 and disallowed the said payment u/s 40(a)(i) of the Act.

iii) On Appeal, the CIT(A) confirmed the assessment order by observing that Explanation to section 9(2) inserted by Finance Act, 2010 w.e.f. Apr 1, 1976, provided that income of a non-resident shall be deemed to accrue or arise in India as per clause (v), (vi) or (vii) of Section 9(1), irrespective of any business connection in India or rendering of services in India and therefore the payment made by the assessee to Trans Coral was taxable in India.

iv) The assessee filed an appeal before the Tribunal:

Decision

i) The Tribunal observed that the obligation to deduct tax at source u/s 195 of the Act applies to all persons but it does not and cannot take away the fundamental requirement that the sum has to be chargeable under the provisions of the Act and therefore tax is deductible from the sum paid only if the said sum is chargeable to tax in India.

ii) The Tribunal after perusing the Agency agreement observed that Trans Coral was appointed as a sole service provider to promote the activities and services provided by the assessee company in return for 1/3rd commission share on the commission received by the assessee and an additional incentive @ 10% of commission where total commission earned by the assessee exceeded INR 50 lacs. Thus, the relationship between the two companies was that of a principal and agent and could not be termed as that of joint venture partners. The Tribunal further held that the structure of payment of commission as provided in the agreement could not be a sole determinative factor of a joint venture and was merely a mode of determination of fees as agreed between the two companies.

iii) The Tribunal observed that such sales promotion expenditure paid and credited to the account of the non-resident i.e. Trans Coral for services rendered outside India would not fall within the purview of income received or deemed to be received in India as well as accrue or deemed to accrue in India.

iv) Further, the Tribunal also held that the provisions of section 9(1)(vii) were not attracted in the instant case as the assessee company had utilized the services of the non-resident service provider outside of India for the purposes of earning commission income from its customers/shipping companies outside of India and therefore when the source of assessee's income for which the services were utilised, were outside India, and the services were also rendered outside India, the payment made for rendering the said services would not taxable in India as per the provisions of the Act. The Tribunal relied on the decision of the Hon'ble Supreme Court in ***GVK Industries Ltd. vs. ITO 371 ITR 453 (SC).***

v) Further, the Tribunal also observed that even under the India-UAE DTAA, in the absence of PE of Trans Coral in India during the year under consideration, the said business income was not chargeable to tax in India.

vi) In light of the above, the disallowance of commission was deleted by the Tribunal.

3 *Ansys Inc. vs. ACIT [2021] 127 taxmann.com 731 (Pune - Trib.)*

Sale of software/license cannot be brought within the ambit of 'Royalties' under Article 12 of India-USA DTAA, when the transaction is to authorize end-user to have access and make use of 'licensed' computer software product over which licensee has no exclusive rights since no copyright is parted with

Facts

i) The assessee, a tax resident of the USA, was engaged in the business of sale of software/license relating to the development of software. During the year under consideration i.e. AY 2009-10 & AY 2014-15, the assessee had not filed return of income. The AO initiated re-assessment proceedings by recording that a receipt of INR 2.42 crore as consideration for the sale of software/license relating to the development of software from M/s. Honeywell Technology Solutions Lab Pvt. Ltd. escaped assessment as it was in the nature of Royalty chargeable to tax in India. The claim of the AO was upheld by the DRP and the AO concluded the re-assessment proceedings by holding that the aforesaid receipt was chargeable to tax in India under the Act as well as under the India-USA DTAA.

ii) The assessee filed an appeal before the Tribunal:

Decision

i) The Tribunal referring to Article 12 of the India-USA DTAA and by placing reliance on the decision of the Hon'ble Supreme Court in ***Engineering Analysis Centre of Excellence Pvt. Ltd. vs. CIT [2021] 432 ITR 472 (SC)***, observed that 'royalty' means consideration for the use or right to use any copyright of a literary, artistic or scientific work etc. and that the ownership of the copyright in a work is different from the ownership of the physical material in which the copyrighted work may happen to be embodied. Therefore, where the core of a transaction is to authorize the end-user to have access to and make use of the "licensed" computer software product over which the licensee has no exclusive rights, no copyright is parted with.

ii) In light of the above, the Tribunal held that since in the facts of the present case, the receipt by the assessee was for sale or software and not for parting with the copyright of the software, the amount could not be brought within the ambit of 'Royalties' under Article 12 of the India-USA DTAA.

iii) Further, in the absence of PE of the assessee in India during the year under consideration, the said receipt would also not be chargeable to tax under Article 7 of the India-USA DTAA.

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