INTERNATIONAL TAXATION

Case Law Update

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Tribunal

1 *Magotteaux International SA v DCIT [[2022] TS-91-ITAT-Del] (Delhi - Trib.)*

Group Management Services rendered by a Belgian entity to an Indian company was held to be not taxable as Fees for Technical Services as it did not 'make available' technical know-how/skills (invoking MFN clause in India-Belgium DTAA along with the India-Portuguese DTAA) [AY 2011-12]

Facts

i) The assessee, a tax resident of Belgium, was engaged in the business of operational consultancy services to various group entities. Accordingly, in India, it had rendered such services to Magotteaux Industries Private Limited ('MIPL').

ii) The assessee had filed a NIL return of income. However, in the computation of income for the relevant Assessment Year ('AY'), the assessee had stated that it had entered into an agreement with MIPL for the provision of business support services, such as marketing, sales, finance, administration and other services. The services were provided by the assessee from outside India.

iii) The AO mentioned that the said services were in the nature of managerial and consultancy services and hence considered the same as taxable under the head 'Fees for Technical Services' ('FTS') both under Article 12 of the India-Belgium DTAA and also as per Section 9(1)(vii) of the Income-tax Act, 1961 ('The Act').

iv) The assessee when asked to prove why the said income shall not be taxed as FTS, the assessee contended that as per the protocol of the India-Belgium DTAA, the Belgium treaty provided taxation of FTS for a lower or restrictive rate as per the DTAA's entered by India with other OECD members on or after January 01, 1990. The assessee had accordingly relied on the India-Portuguese DTAA.

v) The AO however was of the firm belief that the services rendered by the assessee did make available knowledge, experience, know-how to the recipient and believed that the same was clearly visible on examining the nature of the services rendered and consequential benefits obtained by the recipient.

vi) The AO further rejected the contention of the assessee that the services were rendered outside India, relying on Explanation 9(1) of the Act. Objections were raised before the DRP but the same were of no avail.

vii) Aggrieved, the assessee filed an appeal before the Tribunal.

Decision

i) The Tribunal noted that as per the agreement entered into by the assessee, the parties subscribed exclusively to the following services:

- i) Legal services
- ii) Human Resources Services
- iii) Controlling, Accounting, Reporting and Cash
- iv) Management services
- v) Performance Management services
- vi) Quality Control, Safety and Environment services
- vii) Production Allocation services
- viii) Marketing services
- ix) Global Sales Coordination services
- x) Procurement services
- xi) New Projects and Industrialization services

ii) The Tribunal observed that perusal of the above-mentioned services were clearly routine in nature and definitely did not make available experience, know-how to the recipient MIPL.

iii) The Tribunal further mentioned that the DRP itself in Para 6.2 of its order had accepted that as per the service agreement, the services rendered were routine in nature and not at all complex.

iv) The Tribunal further mentioned that considering the protocol of the India-Belgium DTAA, the DTAA of India-Portuguese was considered for the most favourable nation clause. Further, the India-Portuguese DTAA stated that :

"*Fees for included services is defined as consideration for rendering of any technical or consultancy services..... under Article 12(b) is received or make available technical knowledge, experience, skill, know how or processes or consist of.....*"

v) The Tribunal observed that the services received by MIPL did not make available technology, skill know-how etc. and such services could not be considered to be in the nature of managerial, technical or consultancy in nature.

vi) The Tribunal, thus concluded that the business support services rendered by the assessee did not satisfy the make available test of the India-Belgium DTAA and hence the same was not taxable as FTS.

vii) Further, the Tribunal also mentioned that on the tax rate mentioned in the DTAA, the levy of education cess and surcharge was not applicable.

2 *Vanderlande Industries (P.) Ltd vs. ACIT [(2022) 135 taxmann.com 144 (Pune)]*

Payment made to Netherlands entity for the use of its ICT (i.e Information Communication Technologies) infrastructure was held to be taxable as 'Royalty' and consequently disallowance under Section 40(a)(i) for non-deduction of TDS was held to be justified. [AY 2012-13]

Facts

i) The assessee (wholly owned by Vanderlande Industries Holding, B.V, Netherlands ('VIBV'), an Indian based Private Limited Company, was engaged in the business of baggage handling at Airports, Distribution Centre, Express Parcel Sortation facilities and related services.

ii) The assessee, for the year under consideration i.e. AY 2012-13, paid an amount of ₹ 53,53,204 to VIBV (the payment made was reimbursement for Desktop services, like storage of data or backup and restore, Communication services like Instant Messaging, remote VPN Access and Application services like Solidworks, SugarCRM, Primavera, JD Edwards Enterprise, E-mail & Calendaring etc.) and claimed the same to be reimbursement on account of IT Support Services. Hence, no deduction for tax at source was made.

iii) The assessee stated that VIBV had entered into arrangements in Netherlands for various facilities and services which were to be used by Vanderlande and its group companies located in different countries, including India.

iv) The assessee contended that as such the payment made to VIBV was in the nature of Fees for Technical Services ('FTS') and as it did not 'make available' any services as per the India-Netherlands DTAA, it could not be taxed as even FTS.

v) The AO rejected the contention of the assessee and considered the said payment under the purview of 'Royalty' as per Section 9(1)(vi) of the Income-tax Act, 1961 ('The Act') and even as per Article 12 of the India-Netherlands DTAA. The CIT(A) upheld the order of the AO.

vi) Aggrieved, the assessee filed an appeal before the Tribunal.

Decision

i) The Tribunal noted that an agreement was entered into between the assessee and VIBV known as 'The Service Agreement' on September 01, 2009, wherein Clause III of the Agreement defined many services under the head 'Information Communication Technologies ('ICT') and Quality Management Services.

ii) The Tribunal further noted that Article 2 of the Agreement mentioned that the payment was made on the basis of 'Cost plus arm's length mark-up' and the cost was defined to include direct (allocable reasonable expenses) and indirect costs (allocable overhead expenses of services).

iii) The Tribunal further noted that 'JD Edward Software' was purchased by VIBV (i.e 744 licenses were purchased) which were used by VIBV in its overall ICT Infrastructure. Further, it noted that the assessee had for the months of November 2011 to February 2012 - access to 18, 19, 18 and 20 units (described as No. of work stations) respectively of the overall ICT Infrastructure.

iv) The Tribunal further noted that VIBV had purchased many software's and all the group entities were allowed access to the ICT infrastructure.

v) The Tribunal observed that the assessee claimed that a composite payment was made to the VIBV towards the purchase of software and FTS and both were not chargeable to tax in the hands of the VIBV in light of i)the decision of the Apex Court in the case of Engineering Excellence Analysis Centre Ltd. Ii) the

fact that nothing was made available to the assessee. However, Tribunal held that the assessee was charged only for the usage of IT Infrastructure and not for the cost of any identified software.

vi) The Tribunal observed that the Apex Court's decision would apply in the hands of the VIBV, at the time of purchase of the software from third-party vendors before installing them in its overall ICT Infrastructure and not at the time of earning revenue from the group entities including the assessee for allowing access to its overall ICT Infrastructure.

vii) The Tribunal further observed that the assessee, in fact, paid a monthly sum to VIBV depending upon the extent of the user of the overall ICT infrastructure set up by the latter.

viii) The Tribunal concluded that the payment made by the assessee to VIBV was taxable as Royalty as per Explanation 2 read with Explanations 4 & 5 to Section 9(1)(vi) of the Act on the rationale that the payment was for the use of ICT Infrastructure maintained by VIBV, and that therefore the said payment was a consideration for "the use or right to use any industrial, commercial…equipment", covered under clause (iva) of Explanation 2 to section 9(1)(vi) of the Act. Further, it held that Explanation 5 provides that the Royalty includes consideration, inter alia, in respect of `any property whether or not the possession or control of it was with the payer or was used directly by the payer or the location of such property was in India.

ix) Further, the Tribunal held that even as per India-Netherlands DTAA, the payment being a case of industrial royalty was covered in the amended Article 12 of the DTAA w.e.f April 01, 1999, and that as the year under consideration was AY 2012-13, only the amended treaty law would apply. The Tribunal further observed that since para 4(b) of Article 12 of the DTAA specifically covers consideration for use of any industrial or commercial equipment, the payment made by the assessee for use of the overall ICT Infrastructure set up by its Netherlands entity would fall within the term `Royalties' under the DTAA and also as per the Act and hence the same was taxable as Royalty.

x) Thus, the Tribunal upheld the disallowance of royalty payment under Section 40(i)(a) of the Act for non-deduction of TDS.

3 *Autoliv ASP Inc v. DCIT [[2022] 135 taxmann.com 263] (Delhi - Trib.)*

Engineering fees received by U.S Company was held to be not taxable as 'Fees for Included Service' ('FIS), as the same did not make available any technology to the Indian service recipient [AY 2015-16]

Facts

i) The assessee, a non-resident company, incorporated under the laws of the United States of America, was engaged in the business of providing design and development services and engineering services of the vehicle safety system.

ii) M/s Autoliv India Private Limited ('Autoliv') undertook a project to develop a vehicle safety system for Ford brand of cars in India. As the technical centre of Ford group was based in the US, therefore, Autoliv was required to co-ordinate/interact with the engineers/ technical personnel of the Ford technical centre in the US.

iii) For administrative convenience, Autoliv had entered into a subcontractor agreement with the assessee for availing itself of the related engineering services whereby the employees of the assessee company would co-ordinate/interact with the engineers/technical personnel of Ford technical centre in the US for gathering requisite inputs on the designing and development of the product.

iv) The assessee rendered engineering services to Autoliv from the US and none of the employees of the assessee visited India in connection with the rendering of such engineering services to Autoliv. The activities performed by the assessee primarily involved coordinating/interacting with the engineers/technical personnel of the Ford technical centre. The assessee performed analysis and provided the same to Autoliv, which, in turn, was used by Autoliv in preparing a prototype of the product for Ford brand of cars in India.

v) The assessee, during the year under consideration, had thus received from Autoliv, Revenue from different streams like engineering fees (₹ 70,01,452), reimbursement on software costs (₹ 3,53,693) and reimbursement of salary and related costs (₹ 4,79,63,123) which is claimed to be non-taxable.

vi) However, the AO was of the opinion that the services provided by the assessee were technical services. The Assessing Officer was of the firm belief that these services made available technical knowledge, skill etc and, accordingly, treated the revenue from engineering services as FIS in terms of Article 12 of the India- US DTAA.

vii) Further, as far as the reimbursement of software cost was concerned, the assessee contended the same to be not taxable as it did not constitute any income. However, the AO, considered the same as income from Royalty, considering the amendments in the statute.

viii) The assessee raised objections before the DRP, which were dismissed.

ix) Aggrieved, the assessee filed an appeal before the Tribunal.

Decision

i) The Tribunal observed that as per Section 90(2) of the Act, the beneficial provisions of the DTAA would prevail and as per Article 12 of the India-USA DTAA, FIS is defined as:

"Fees for included services "means payments of any kind to any person inconsideration for the rendering of any technical or consultancy services, if such services.....(b)make available technical knowledge experience, skill, know-how, or processes or consist of the development and transfer of a technical plan or technical design".

ii) The Tribunal held that the assessee had no occasion to transfer or make available any technology, skill, knowledge, process, etc. involved in carrying out the engineering services to Autoliv. On the contrary, for every new project/requirement for the Ford brand of cars in India, Autoliv had to invariably sub-contract the relevant portion of the Project to the assessee. The engineering fees earned by the assessee under the 'sub-contractor' agreement included costs that it had incurred on labour, depreciation, rent, materials, supplies and other resources and costs incurred by Autoliv US on transportation, food

and lodging and was marked up by 7% on the internal costs.

iii) The Tribunal observed that for every project from Ford US, Autoliv India had to approach the assessee for engineering design etc., which meant that even after receiving the services from the assessee, Autoliv was not enabled to apply technology for other projects. It relied on the judgement of the Hon'ble Karnataka High Court in ***De Beers India Minerals [Pvt] Ltd [12 Taxmann.com 214]*** and held that technology only will be considered as made available when the person acquiring such knowledge is possessed of the same enabling him to apply in future at his own. If the services were consumed without leaving anything tangible with the payer for use in future, then it would not be characterized as 'making available' of the technical services notwithstanding the fact that its benefit flowed directly and solely to the payer of the service. What was necessary was that the service provider should transmit the technical knowledge to the payer so that the payer can make use of such technology in future without the involvement of the service provider.

iv) The Tribunal thus concluded that the aforesaid fees were not taxable in India as per the India-USA DTAA.

v) W.r.t reimbursement of cost, the Tribunal noted that the assessee had centrally purchased software primarily consisting software AMC's from third-party vendors outside India for, and on behalf of, all of its group companies, including Autoliv. Out of the software charges paid by the assessee to the vendor it had allocated ₹ 3,53,693/- towards charges recoverable from Autoliv and claimed the same as reimbursement on an 'at-cost' basis and without any profit element. Since neither the AO nor CIT(A) had stated that there was any profit element embedded in the aforesaid payments; by relying upon the judgement of the Hon'ble Apex Court in ***A P Moller Maersk AS [(2017) 392 ITR 186],*** the Tribunal held that the amounts received by the assessee company were in the nature of 'at-cost' reimbursements and no technical services were rendered by the assessee company to the Indian agents, and hence such reimbursements were not taxable as FTS.

vi) The Tribunal, after relying on various judicial precedents concluded that since the term 'Royalty' has been defined in the DTAA, the definition of the term 'Royalty' under the Act could not be applied, and that in light the decision of the Hon'ble Supreme Court, in the case of Engineering Analysis Centre of Excellence Pvt Ltd reimbursement towards software charges were not taxable as royalty as well.

4 *Kellogg India Private Limited vs. ACIT – TS-80-ITAT-2022 (Mum)-TP*

Singapore AE accepted as tested party & RPM accepted as MAM for import of finished goods

Facts

i) The assessee was engaged in manufacturing and sales of breakfast cereals and convenience foods and it operated as a licensed manufacturer of ready to eat cereals.

ii) During the year under consideration, the assessee had commenced the business of distributing Pringles products in the Indian markets and the said products were purchased by the assessee from

its AE in Singapore viz Pringles International Operations SARL.

iii) The Singapore AE did not manufacture pringles, but in turn, it got the same manufactured from a third-party contract manufacturer. Thereafter, the goods were supplied to the assessee at cost plus a markup of 5% on third party manufacturer's cost.

iv) In the TPSR, the assessee classified itself as a distributor of Pringles products and was responsible for the strategic and overall management of principle business in India. On the other hand, Singapore AE was classified as the least complex entity and was selected as the tested party for benchmarking the international transaction of import of finished goods. Further, the assessee conducted a search in the Asia Pacific region to identify manufacturers and based on benchmarking analysis of 14 comparables and considering the PLI as GP/direct and indirect cost, the transaction of import of finished goods was claimed to be at ALP.

v) The TPO rejected the benchmarking approach and selected the assessee as the tested party. Further, the TPO considered TNMM as the most appropriate method for the import of finished goods transactions and after considering Indian comparables, he made an adjustment on the ground that the assessee's net margin was not at ALP

vi) The DRP upheld the actions of TPO. Aggrieved, the assessee filed appeal before the Tribunal.

Decision

i) The Tribunal opined that the assessee was bearing significant entrepreneurial risk in India. Further, the Tribunal held that the Singapore AE was remunerated on a mere cost plus markup basis and had undertaken only limited functions. Accordingly, the Tribunal accepted the Singapore AE as the tested party.

ii) The Tribunal further held that RPM was the most appropriate method as the assessee was only engaged in the purchase of and resale of goods without any substantial value addition thereon. Comparing the gross margin of the Singapore AE with the comparables chosen by the assessee, it held that the transaction of import of finished goods was at ALP. Further, the Tribunal noted that alternatively, gross margins of the assessee were more than the gross margins of comparables chosen by the TPO and therefore even considering TPO's comparables, no adjustment to ALP was required to be made with respect to the transaction of import of finished goods.

***Note**:*

The Tribunal also relied on its decision in assessee's own case for AY 2013-14, wherein it was held that in absence of an express arrangement/agreement between the assessee and the AE for incurring AMP expenditure to promote the brand of the AE, AMP expenditure incurred by making payment to third parties for marketing and promoting the product manufactured by the assessee, did not come within the purview of an international transaction and that the bright-line test method was not a valid method to benchmark the transactions. It thus directed the TPO to delete the adjustments as the facts were identical for the year under consideration.

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