FTS under India-UK tax treaty – ‘make available’ condition required to be satisfied for development and transfer of technical plan or design also

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In brief

Recently¹, the Mumbai bench of the Income-tax Appellate Tribunal (Tribunal) held that the condition of ‘make available’ has to be read in conjunction with the second limb of Article 13(4)(c) of the India-UK Double Taxation Avoidance Agreement (tax treaty)², i.e., “or consists of the development and transfer of a technical plan or technical design” to treat the amount received as fees for technical services (FTS).

In detail

Facts

- The taxpayer is a tax resident of UK and primarily engaged in the business of providing engineering design and consultancy services.
- During the year under consideration, the taxpayer received an amount that inter-alia included towards providing of consulting engineering services³. It filed its return of income in India with nil income.
- The services rendered by the taxpayer included supply of design/ drawings and providing certain consultancy services.
- The tax officer (TO) treated the said receipt as FTS alleging that the words “make available” has to be read with technical knowledge, skill, knowhow, etc. but not with ‘the development and transfer of a technical plan or a technical design,’ while interpreting Article 13(4)(c) of the India-UK tax treaty.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the TO’s order and supplemented the same by observing that providing design and drawing required application of mind by various technicians with varied knowledge. Furthermore, the CIT(A) held that

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¹ ITA No. 1296/Mum./2017
² Article 13(4) of the India-UK tax treaty defines the term “fees for technical services” as follows:
   “For the purposes of paragraph 2 of this Article, and subject to paragraph 5, of this Article, the term ‘fees for technical services’ means payments of any kind of any person in consideration for the rendering of any technical or consultancy services (including the provision of services of a technical or other personnel) which:
   (a) …
   (b) …
   (c) make available technical knowledge, experience, skill know-how or processes, or consist of the development and transfer of a technical plan or technical design.”
³ The taxpayer also received against cost allocation for management charges, which was treated as taxable by the TO, alleging it to be ancillary to the consulting services. However, the primary ground adjudged by the Tribunal was with respect to the taxability of the consultancy services. Accordingly, the issue of taxability of cost allocation charges has not been discussed in this alert, for the sake of brevity.
overseeing its implementation and execution at site in India by the taxpayer’s technical personnel amounted to making available the technical services.

- Aggrieved, the taxpayer filed an appeal before the Tribunal.

**Issue before the Tribunal**

- Whether development and transfer of a technical design or a technical plan, without making available technical knowledge, experience, skill, knowhow, etc. was in the nature of FTS?

- If the condition of ‘make available’ was a prerequisite, whether the same had been satisfied in the present case?

**Taxpayer’s contentions**

- The taxpayer was rendering consultancy services; supply of design and drawings was only incidental to such services.

- The services rendered, including the supply of designs and drawings, were project-specific and could not be reused by the recipient.

- The taxpayer was hired to work on specialised services where the recipient of the services did not have the necessary skills. These were skills gained over years of working in this field, and the same were not transferred to the recipient merely because they worked jointly on a project.

- The second limb of Article 13(4)(c) of the India-UK tax treaty which refers to ‘consists of the development and transfer of technical plan or technical design’ cannot be read disjunctively but has to be read along with the first limb.

- Therefore, unless the development and transfer of a technical plan or technical design makes available technical knowledge, skills, experience, etc., such service cannot be treated as FTS.

**Revenue’s contention**

- The taxpayer did not execute the project itself. It provided consultancy services as well as technical designs to parties in India, enabling them to further apply and re-apply such technology in India.

- The taxpayer worked closely with the service recipient and supported them on various technical and engineering matters, thus making available technical knowledge and experience, etc.

- The technical designs provided by the taxpayer were capable of being used in the future, and there was no bar in the agreement for the service recipient for using such knowhow and knowledge in future.

**Tribunal’s ruling**

- As per the principles of *ejusdem* generis, the words “or consists of the development and transfer of a technical plan or technical design” appearing in Article 13(4)(c) of the India-UK tax treaty will take colour from the first limb i.e., ‘make available technical knowledge, experience, skill, knowhow or processes’.

- The technology is considered to have been made available when the recipient of such services is competent and authorised to apply the technology contained therein independently as an owner without depending upon the service provider.

- The technical designs/drawings/plans supplied by the taxpayer to Indian entity were project-specific and could not be used in any future projects. Therefore, it did not ‘make available’ the technical knowledge, skill, knowhow, etc. to the recipient.

- The onus of establishing that the services have met the ‘make available’ test is on the Revenue authorities.

**The takeaways**

The decision has read the condition of “make available” in the limb of “development and transfer of technical design” in the India-UK tax treaty. This interpretation could be adopted in India’s tax treaties (such as with the UK, US and Canada) where the limb on development and transfer of technical design forms part of the same sub-clause as ‘make available’. Accordingly, such interpretation could be useful for defending similar cases. However, it may be noted that the issue is far from settled, as there are contrary judgements on this aspect as well.

Accordingly, the principle of the instant ruling would have to be applied considering the specific facts of the case.

It is also pertinent to note that the said condition has been explicitly mentioned in certain treaties (such as with Singapore and Portugal), where the development and transfer of technical design should enable the service recipient to apply the technology therein to be treated as FTS.

**Let’s talk**

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor.