



## Tax Insights

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### Revenue's appeal dismissed, affirming Tribunal's ruling that commission income received by taxpayer as per the commissionaire agreement from its Indian affiliate is not FTS, and subscription fees received by taxpayer are not 'royalty' – Delhi High Court

#### In brief

The Delhi High Court<sup>1</sup> holds that although the promotion, sale and distribution of publications or rendering of support services as per the commissionaire agreement involve human intervention, it is not covered in the category of technical or consultancy services. Moreover, the court observes that no special skills or knowledge are required to render such services, nor is any professional advice or specialised service rendered that could be categorised as a technical service. Therefore, the High Court holds that the commission income cannot be taxed as fees for technical services (FTS) in India.

On the issue of subscription fees for e-journals received by the taxpayer from other Indian entities, the High Court holds that such fees cannot be considered as 'royalty'. The reason being that there was nothing on record to demonstrate that the taxpayer has granted the copyright to the concerned subscribers. All that the taxpayer has done is, sell the copyrighted publication to the concerned entities, without conferring any copyright on the said material.

#### In detail

##### Facts

- The taxpayer, a resident of Germany, is a non-exclusive sales representative of the group's affiliated publisher entities, including the Indian entity.
- During the year under consideration, a commissionaire agreement was executed between the taxpayer and its Indian associated enterprise (AE). As per the commissionaire agreement, the taxpayer was required to promote, sell and distribute print books, electronic books and journals published by its Indian AE. The taxpayer was also required to provide services related to sales, marketing, customers, order handling, delivery invoicing, debtor and subscription management, and processing of return copies.
- The taxpayer had collected subscription fees and other revenue or fees from the sales of electronic books and journals to third-party customers. The taxpayer ultimately paid these fees to its Indian AE after retaining

<sup>1</sup> ITA No. 306 of 2023

its commission as agreed under the commissionaire agreement.

- Besides the above, the taxpayer had received subscription fees for e-journals from two other Indian entities.
- The taxpayer filed its return of income in India by declaring nil income. The taxpayer's case was selected for assessment proceedings. The tax officer (TO) made the following three additions while passing the assessment order:
  - a. commission received by the taxpayer from the Indian AE for activities performed under the commissionaire agreement (this was bifurcated into two buckets as per Form 3CEB: the commission fee and 'service charges');
  - b. subscription fees received by the taxpayer from its direct Indian customer's entity for e-journals; and
  - c. gross amount of the sale proceeds that were collected by the taxpayer from Indian customers for the sale of e-journals or books on behalf of the Indian AE.
- The TO treated all of the above three receipts as 'royalty' under the provisions of section 9(1)(vi) of the Income-tax Act, 1961 (the Act), and Article 12 of the India-Germany Double Taxation Avoidance Agreement.

## Revenue's contentions

### Taxability of commission fee received by the taxpayer under the commissionaire agreement

- Services that the taxpayer provided, such as the promotion, sale and distribution of products globally, should be categorised as consultancy services. Moreover, services such as order handling, inventory management, debtor management and subscription management should be categorised as managerial services.
- The Revenue contended that managerial, consultancy and technical services involve human intervention as per the commissionaire agreement. In this regard, the Revenue relied on the Supreme Court's decision in the case of Kotak Securities Limited<sup>2</sup>.
- Considering the above, the Revenue argued that services provided by the taxpayer would qualify for FTS as they are in nature of managerial, technical and consultancy services, as defined under Article 12 of the India-Germany DTAA and section 9 of the Act.

### Taxability of subscription fees received by the taxpayer

- The Revenue contended that the fees for services provided by the taxpayer to its affiliate Indian publisher would also be chargeable to tax as FTS. This is because the ambit and scope of the services provided are similar to those provided under the commissionaire agreement.
- Without prejudice to the above, as an alternative, the Revenue argued that subscription fees received by the taxpayer should qualify as 'royalty', as concluded by the TO and upheld by the Commissioner of Income-tax (Appeals).
- The Income-tax Appellate Tribunal (Tribunal) had relied on the Supreme Court's decision in the case of Engineering Analysis Centre of Excellence (P.) Limited<sup>3</sup> while adjudicating this issue. Accordingly, the Revenue contended that the final decision on this aspect would depend upon the review petition filed by the Revenue Department in the said case, which is presently pending before the Supreme Court.

## High Court's decision and observations

### Taxability of the commission fee received by the taxpayer under the commissionaire agreement

- The High Court has observed that, to construe that the consideration received by the taxpayer for the services rendered under the commissionaire agreement is FTS, the services must be covered under one or more of the following three categories: managerial, technical or consultancy services.

<sup>2</sup> CIT v. Kotak Securities Limited [2016] 383 ITR 1 (SC)

<sup>3</sup> Engineering Analysis Centre of Excellence (P.) Limited v. CIT [2021] 432 ITR 471 (SC)

- Accordingly, the High Court has analysed the three categories of FTS as follows and ruled in favour of the taxpayer.
- **Managerial service:**
  - The High Court observes that as per the commissionaire agreement, the taxpayer was required to promote, sell and distribute books and journals published by the Indian AE. The title of the publication remained with the Indian AE, and the taxpayer had assigned only 'property licences' to third parties on behalf of its Indian AE. Moreover, the taxpayer provided support services such as related to global sales, marketing, customers, order handling, stock keeping, inventory management and invoicing.
  - Based on the above findings, the High Court notes that the commissionaire agreement includes nothing that demonstrates that the taxpayer was required to –
    - discover, develop, define or evaluate goals that the taxpayer's Indian AE had to reach;
    - frame policies leading to these goals; or
    - supervise, execute or change policies that were already adopted.
  - Thus, High Court concludes that the taxpayer had rendered support services that were executive and supervisory in nature, and they cannot be considered as managerial services.
- **Technical service:**
  - Regarding technical services, the High Court observes that generally such services are connected to applied and industrial sciences or artisanship, involves special skills or knowledge, and excludes fields such as arts and human sciences.
  - Since the taxpayer's personnel were required to possess no special skills or knowledge to render the services contemplated under the commissionaire agreement, the services cannot be called technical services.
- **Consultancy service:**
  - Regarding consultancy services, the High Court observes that consultancy services involve rendering professional advice or services in a specialised field. As the taxpayer had not rendered such services, their income cannot be said to have been received on account of consulting services.
- Considering the above, the High Court observes that the services rendered by the taxpayer to its Indian AE would not be covered in any of the following categories: managerial, technical or consultancy services. Accordingly, the fees received could not be treated as FTS in nature.
- Thus, the High Court has disregarded Revenue's contention that the services the taxpayer rendered should be considered technical services on account of human intervention. Moreover, the court holds that mere 'human intervention' in the performance of a service would not make the fees received for the services as FTS.

### Taxability of subscription fees received by the taxpayer

- The High Court observes that Revenue's argument that subscription fees should be considered as FTS, as an alternative to 'royalty', has been presented for the first time before the High Court. Accordingly, High Court has not accepted this argument, as this was not the Revenue's stand before the Tribunal. In this regard, the High Court holds that this constitutes a flip-flop, which the taxpayer would do well to abjure.
- There is nothing on record demonstrating that the taxpayer has granted copyright to the concerned subscribers of the e-journals. The taxpayer had just sold the copyrighted publication to the concerned entities, without conferring any copyright on the said material.
- Considering the above, the High Court has upheld the Tribunal's ruling by holding that the Tribunal had rightly deleted the TO's addition under this head, following the Supreme Court's decision in the case of Engineering Analysis<sup>3</sup>.

## The takeaways

While adjudicating the issue of FTS, the High Court has analysed in detail the categories of FTS—managerial, consultancy and technical services. The High Court has further established that mere intervention of human element while providing the services does not make the fees received to be covered under FTS unless a specialised skill or knowledge is required to provide such service. While dealing with the issue of 'royalty', the High Court has affirmed the Income-tax Appellate Tribunal's (Tribunal) ruling. The Tribunal had followed the Supreme Court's decision in the case of Engineering Analysis<sup>3</sup>, although the Revenue Department has filed a review petition against the said decision, which is still pending for adjudication before the Supreme Court.

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