



Tax Insights

8 April 2024

Amount received by taxpayer from sale of online advertisement space through its AdWords program cannot be characterised as royalty or FTS under the India-Ireland DTAA – Bangalore bench of the Tribunal

In brief

The Bangalore bench of the Income-tax Appellate Tribunal (Tribunal) in a recent ruling¹ concluded that the amount received by a non-resident taxpayer from the sale of online advertisement space cannot be characterised as royalty or fees for technical services (FTS). Moreover, the Tribunal re-affirmed its earlier view that, in the absence of a taxpayer's permanent establishment (PE) in India, such receipts cannot be taxed as business income in India.

In detail

Facts

- The taxpayer is a foreign company with its registered office in Ireland. The taxpayer was involved in the business of sale of online advertisement space to A Limited under a distribution agreement (AdWords program).
- The taxpayer did not file its return of income (ROI) for the assessment years (AYs) in consideration, in the belief that revenue from sale of advertisement space under its AdWords program is not taxable in India. No taxes were also deducted on the payments by the payer, i.e. A Limited.
- The tax authorities were of the view that A Limited was a taxpayer-in-default for not deducting taxes on the payments made to the non-resident for purchase of online advertisement space. The proceedings under section 201 of the Income-tax Act, 1961 (the Act) in the hands of A Limited formed the basis for opening reassessment proceedings in the taxpayer's case for a block of AYs under section 148 of the Act.
- As a response and pursuant to the notice received under section 148 of the Act, the taxpayer filed nil ROIs for the AYs under scrutiny.
- The tax officer (TO) passed a draft assessment order for the block of AYs wherein, receipts from A Limited for the sale of online advertisement space were characterised as royalty. Moreover, the dispute resolution panel confirmed the said addition and a final assessment order was passed.

¹ IT(IT)A Nos. 191 to 194/Bang/2024

Taxpayer's contentions

- Regarding the characterisation of receipts from sale of advertisement space as royalty, the taxpayer relied on the Tribunal's ruling passed in favour of the taxpayer for AY 2007–08. The taxpayer had relied on the Supreme Court's decision in the case of Engineering Analysis Centre of Excellence (P) Limited². The taxpayer contended that the definition of the term 'royalty' in Article 12(3) of the India-Ireland Double Taxation Avoidance Agreement (DTAA) overrides the definition of royalty provided in Explanation 2 to section 9(l)(vi) of the Act by virtue of section 90(2) of the Act. Therefore, it was contended that the definition of 'royalty' under the India-Ireland DTAA, being beneficial to the taxpayer, must be considered.
- In addition, the taxpayer relied on the aforementioned judgement and contended the following: Mere use of or right to use a computer program without any transfer of the underlying copyright in it as per sections 14(a), 14(b) or 30 of the Copyright Act, 1957, does not satisfy the definition of royalty under the Act or the DTAA. Therefore, receipts from sale of online advertisement space under the AdWords program cannot be characterised as royalty.
- The taxpayer further contended that the receipts in question are in the nature of business profits chargeable to tax in Ireland but not in India. Moreover, the Revenue never alleged in its proceedings that the taxpayer had a PE in India in terms of Article 5 of the India-Ireland DTAA. Accordingly, by virtue of Article 7(1) of the India-Ireland DTAA, the right to tax these profits is solely with Ireland.
- In addition, the taxpayer also relied on a co-ordinate bench ruling³ for the same block of AYs. This ruling had concluded that the payments made by A Limited to the non-resident for the purchase of online advertisement space under the AdWords program cannot be characterised as royalty or FTS. Therefore, the payments were not subject to tax in India.

Tribunal's ruling

- As regards the allegation that payments received by the taxpayer were in the nature of royalty, the Tribunal observed the following: In its earlier judgements in the cases of the taxpayer and A Limited, the Tribunal was of the view that such payments are not in the nature of royalty but business profits; in the absence of a PE in India, these payments are not chargeable to tax in India and hence, there is no requirement to deduct taxes on the said payments.
- The Tribunal relied on its own order in the taxpayer's case for AY 2007–08, wherein it had relied on the Supreme Court's decision in the case of Engineering Analysis² and concluded that the advertising program being used by A Limited is essentially a computer program or software, and the issue regarding the use of computer software tantamounting to royalty now stands resolved. Moreover, the Tribunal stated that the provisions of equalisation levy are applicable specifically for the provision of specified services (including provision of advertisement space); hence, payments received for online advertisement space are covered under the equalisation levy and not royalty.

The takeaways

This ruling re-affirmed the view that an online transaction or sale of online advertisement space under the AdWords program does not entail the provision of any rights or intellectual property rights to customers. Therefore, the payments made are not taxable as royalty. Moreover, the ruling concluded that the said transaction does not tantamount to FTS, noting that it is a standard facility and not customised as per each customer's needs or requirements.

² Engineering Analysis Centre of Excellence Private Limited v. CIT & Anr. [2021] 432 ITR 471 (SC)

³ [IT(TP)A No(s). 1513 to 1516/Bang/2013]; You may click [here](#) to refer to our Tax Insights.

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