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Tax alert: Grant of distribution rights for broadcasting of channels, not royalty

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The Mumbai Bench of the Income-tax Appellate Tribunal (ITAT) has held that income earned by a non-resident taxpayer from grant of distribution rights for broadcasting of channels, is different from copyright as mentioned in the Copyright Act, 1957 and hence, is not taxable as royalty under section 9(1)(vi) of the Income-tax Act, 1961, as well as under provisions of the India-USA tax treaty.

In a nutshell

Section 37 of Copyright Act, 1957 (CA) separately defines broadcast reproduction right which provides that every broadcasting organisation shall have special rights to be known as 'broadcast reproduction right' in respect of its broadcasts. On a conjoint reading of section 14 and 37 of the CA, a holistic view can be taken that broadcast reproduction right is distinct and separate from Copyright Act.

Subscription charges paid by a large number of customers through different agencies, enabling customers to view channels operated by the taxpayer was not parting with any of the copyrights for which payment can be considered as royalty payment.

Broadcasting Reproduction Right is different from copyright, as mentioned in the CA.

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Background:

- The taxpayer[1] is a non-resident foreign company incorporated in the US, primarily engaged in the media industry. Its business constitutes broadcasting of channels over various countries including over the Indian sub-continent.
- The taxpayer, during the Financial Year (FY) 2014-15, corresponding to Assessment Year (AY) 2015-16:
  - Primarily had two streams of revenues from India, i.e., revenues from advertisement and revenues from distribution in India.
  - Was eligible for the benefits of the India-USA tax treaty and had obtained tax residency certificate (TRC).
  - Entered into a distribution representation agreement with an Indian company (I Co) appointing I Co as its exclusive agent for distribution of the channels to media intermediaries' subscribers in India, Nepal, and Bhutan.
- Further, I Co acted on behalf of the taxpayer, and entered into separate agreements with another Indian company, (A Co), for the distribution of the channels.
- The Assessing Officer (AO) during the course of audit proceedings for the year under consideration [i.e., FY 2014-15, corresponding to AY 2015-16], while holding that the payment received by taxpayer would qualify as royalty income, observed that:
  - A Co would procure each authorised purchase platform to telecast each of the channel, although with many restrictions. It showed that the taxpayer retained complete rights over the programmes.
  - The taxpayer, through I Co, had granted license to A Co to distribute the channels. A Co could not modify or delete anything from the transmission of the channels and had to ensure that channels were transmitted in their entirety. The taxpayer restricted A Co and the intermediaries -

    (i) from modifying, replacing, or copying any copyright, trademarks, trade names, logos and names

    (ii) from copying any programmes included on the channels
  - In the case under consideration, the ownership remained with the licensor, i.e., taxpayer, and A Co was allowed to distribute the channels with restrictions. A Co was not free to make use of the channels as per their discretion, but strictly in accordance with the terms laid down by the taxpayer.
  - The taxpayer enjoyed the rights of owners, whereas A Co was paying compensation for the exploitation of the channels. Hence, the transaction with A Co was license fees payment and covered within the definition of royalty under the Income-tax Act, 1961 (ITA), as well as under Article 12 of the India-USA tax treaty (related to Royalties), as being payments made for use of any copyright of a literary, artistic or scientific work, including cinematograph films or work on films, tape or other means of reproduction, for use in connection with radio or television broadcasting.
  - Accordingly, the distribution license fell within the ambit of royalty and was taxable at 15% with applicable surcharge and education cess under section 115A of the ITA (relating to taxation of certain incomes of non-resident taxpayers).
- Aggrieved, the taxpayer filed objections with the Dispute Resolution Panel (DRP), which sustained the additions made by the AO, except to exclude the distribution revenue received from Sri Lanka and Bangladesh, since the taxpayer received this distribution revenue outside India. Accordingly, the AO based on the DRP's directions, passed the final audit order.
- Aggrieved, the taxpayer filed an appeal before the Mumbai Bench of the Income-tax Appellate Tribunal (ITAT).

[1] Fox International Channels (US) Inc vs. DCIT (Int taxation), 4(1)(2) [2023] ITA No. 948/Mum/2023 (Mum-Trib.)

Relevant provisions in brief:

- **Extracts of section 9(1)(vi) of the ITA:**

  "9(1)(vi). Income by way of royalty by—

  (a) the Government; or…

  (c) a person who is non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India…

  Explanation 2. For the purposes of this clause, "royalty" means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for-

  (i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property

  (ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;

  (iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;

  (iv) the imparting of any information concerning technical, industrial, commercial, or scientific knowledge, experience, or skill

  (iva) the use or right to use any industrial, commercial, or scientific equipment8 but not including the amounts referred to in section 44BB;]

  (v) the transfer of all or any rights (including the granting of a licence8) in respect of any copyright, literary, artistic, or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting; or

  (vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to 10[(iv), (iva) and] (v)."

Decision of the ITAT:

The ITAT had observed/noted as below:

Earlier rulings:

- The Bombay High Court, in an earlier ruling[2], having similar facts, had held as follows: -
  - The taxpayer received a part of subscription charges paid by a large number of customers through different agencies. The said subscription charges enabled the customers to view channels operated by such taxpayer. The taxpayer was thus not parting with any of the copyrights for which payment could be considered as royalty payment.
  - The term 'copyright' has been defined in section 14 of the Copyright Act, 1957 (CA), which has been defined to mean exclusive right, subject to the provisions of this Act, to do or authorise the doing of any of the acts specified in the said provision in respect of a work or any substantial part thereof.
  - The term 'work' is defined under section 2(y) of the CA, to mean any of the works namely a literary, dramatic, musical, or artistic work or a cinematograph film and a sound recording.

[2] CIT v. MSM Satellite (Singapore) Pte. Lte. [2019] 106 taxmann.com 353 (Bom-HC)

- Section 14(1) of the CA lists several Acts in respect of a work in relation to which exclusive right would be termed as copyright.
- The taxpayer had not created any literary, dramatic, musical, or artistic work or cinematograph film and/or a sound recording.
- In fact, section 37 of the CA separately defines broadcast reproduction right which provides that every broadcasting organisation shall have special rights to be known as 'broadcast reproduction right' in respect of its broadcasts. Section 37(2) of the CA provides that the broadcast reproduction right shall subsist until 25 years from the beginning of the calendar year next following the year in which the broadcast is made.
- The payment in the case under consideration could not be covered expression of royalty as explained in Explanation (2) of section 9(1)(vi) of the ITA. It was not a case where payment of any copyright in literary, artistic, or scientific work was being made.
- Even going by definition of royalty under Article 12 of the India-Singapore tax treaty, the payment in question could not be categorized as royalty.

- The coordinate Bench of the Delhi ITAT in another earlier ruling[3] held as follows:
  - The issue was whether the subscription/distribution revenue received by the taxpayer (being Mauritius entity and a tax resident of Mauritius) from India entity towards grant of sub-distribution right amounted to royalty as defined under Article 12 of the Indian–Mauritius tax treaty.
  - An entity, being tax resident of Singapore (Singapore entity), was the owner of certain sports channels. The Singapore entity had entered into an agreement with the taxpayer to appoint the taxpayer as a distributor to distribute and make available for sub-distribution its network programming services in India, Pakistan, Bangladesh, Sri-Lanka and Nepal via cable television system, satellite master antenna television systems and direct to home via satellite.
  - The agreement between Singapore entity and the taxpayer made it clear that the taxpayer had not been conferred with any rights whatsoever with regard to copyright, title or any other proprietary or ownership interest in or any elements thereof. The agreement made it explicit that all rights in the contents were expressly reserved by the Singapore entity and the distributor would not use, authorize or permit the use of channel service or any element thereof for any purpose other than the purpose expressly specified in the agreement.
  - The agreement also specified that the taxpayer had to distribute the channel services in its entirety, without any alteration, editing, dubbing, scrolling or ticker tape, substitution or any other modification, addition, deletion, or any other variation whatsoever.
  - The taxpayer would have the right to approve any of the distributors mentioning or using of such names or marks and publicity about the channel service. However, the distributors would not publish or disseminate any material in violation of any restrictions imposed by ESS or ESPN Inc.
  - Thus, the terms of the agreement between the taxpayer and Singapore entity made it clear that copyright over the programs of channels were held by Singapore entity and not parted with the taxpayer. Similarly, based on the agreement between the taxpayer and Indian entity, it was observed that the taxpayer had only granted right to distribute channels in India to the Indian entity.
  - A reading of the agreement as a whole, as well as certain specific clauses of the agreement made it clear that the taxpayer did not transfer any right to use of any copyright to the Indian entity, insofar as it related to certain sports channels owned by the Singapore entity.
  - The taxpayer merely granted distribution rights of channel service through sub-distributors/cable operators.

[3] ESS Distribution (Mauritius) SNC et Compagnie v. DDIT (International Taxation) [2022] 145 taxmann.com 267 (Delhi – Trib.)

- The agreement also made it clear that the distributor had to distribute the channel service provided by the taxpayer in its entirety, without any alteration, editing, dubbing, scrolling or ticker tape, substitution or any other modification, addition, deletion, or any other variation whatsoever.
- Article 12 of the India-Mauritius tax treaty made it clear that the expression royalty meant consideration received for the use of or right to use of any copyright of literary, artistic, or scientific work (including cinematograph films and films or tapes for radio or television broadcasting, any patent trade-mark design, model plan, secret formula plan etc.
- The expression copyright has not been defined either under the ITA or under the India-Mauritius tax treaty. The consequences for infringement of copyright and broadcast reproduction right have been dealt with differently under the CA. On a conjoint reading of section 14 and 37 of the CA, a holistic view could be taken that broadcast reproduction right is distinct and separate from the Copyright Act.
- In the taxpayer's case there was no transfer of any right to use of any copyright and there was specific restriction imposed upon Indian entity that it had to provide the channel services through sub-distributors without any editing, interruption, deletions, additions etc.
- In an earlier ruling[4], the Bombay High Court while dealing with the issue, whether identical nature of distribution rights granted to an entity in India was in the nature of royalty, held that consideration received was in respect of a commercial transaction, hence, distinct, and different from copyright as defined under the CA.
- In another earlier ruling[5], on the issue whether revenue received by the non-resident company from Indian company from distribution right granted in respect of telecast/broadcast of certain channels in India through cable operators would be in the nature of royalty, after taking note of the difference between the meaning of copyright and broadcast reproduction right under the CA, it was held that the right granted to the Indian entity was a commercial right and not copyright.
- What the taxpayer granted to Indian entity through the distribution agreement was broadcast reproduction right, as defined under section 37 of the CA and not any copyright. When the taxpayer itself did not have ownership over the copyright, it could not have transferred such right to any other party.

Conclusion

- In view of the above rulings, the ITAT held that the Broadcasting Reproduction Right was different from the copyright as mentioned in the CA. Accordingly, the distribution revenue earned by taxpayer was not 'royalty' within section 9(1)(vi) of the ITA and Article 12 of the India-USA tax treaty and hence, not taxable in India.

Comments:

Taxability of broadcast distribution rights of media content has been subject of litigation considering the definition of 'royalty' under the provisions of the ITA and various relevant tax treaties. The ITAT in this ruling, while holding that distribution revenue earned by the taxpayer is not 'royalty' within section 9(1)(vi) of the ITA and Article 12 of the India-USA tax treaty has held as follows:

- Section 37 of the CA separately defines broadcast reproduction right which provides that every broadcasting organisation shall have special rights to be known as 'broadcast reproduction right' in respect of its broadcasts. On a conjoint reading of section 14 and 37 of the CA, a holistic view can be taken that broadcast reproduction right is distinct and separate from Copyright Act.
- Broadcasting Reproduction Right is different from the copyright as mentioned in the CA.

[4] Set Satellite (Singapore) Pte Ltd. Vs. DDIT [2008] 307 ITR 205 (Bom HC)

[5] NGC Network Asia LLC Vs. DCIT [IT Appeal No. 1178 of 2015 and 6677 and 6678 (Mum.) of 2018] (Mum-Trib.)

- Subscription charges paid by a large number of customers through different agencies, enabling customers to view channels operated by the taxpayer was not parting with any of the copyrights for which payment can be considered as royalty payment.

Taxpayers may evaluate the impact of this ruling to the facts of their cases.

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