

Global Tax Update

India

Deloitte Tohmatsu Tax Co.

September 2016

1. Situs¹ of intangible assets are to be determined on the basis of situs of the owner

The Court has held that in the absence of any specific provision in Indian domestic tax law² for location of an IP³ such as trademarks, brands, logos etc., situs of IP is to be determined on basis of situs of the owner of such IP. Further, Court held that offshore IP transfer is not taxable in India in the absence of any specific provision.

Australian company, Foster's Australia Limited had transferred trademarks that it had owned and assigned to an Indian subsidiary company to a foreign company outside India. The AAR⁴ had earlier held that income arising from transfer of these trademarks would be deemed income accruing in India on the basis of its finding that the trademarks were being used in India.

The Court, reversing the AAR ruling, held that situs of owner of IP would be closest approximation of situs of IP. This is an internationally accepted rule, unless it is altered by local legislation. Since there is no specific provision in Indian domestic tax law to deal with the situs of IP, the situs of trademarks and other IPs, which were owned and assigned/transferred by Foster's Australia Limited would not be situated in India, this is so because the owner thereof was not located in India at the time of the transaction.

2. In⁵ absence of evidence, royalty income could not be said to be effectively connected with PE

Tribunal refused assuming facts and overlooking taxpayer's submissions and held that in absence of inquiry and substantive material produced with regard to the nature of services performed, it is not possible to presume that income from such services is effectively connected to taxpayer's PE (Permanent Establishment). Hence, income earned by taxpayer under TCL⁶ was held to be taxable at 10% on gross basis as royalty under the tax treaty and not as business income taxable at 40%⁷ on net basis.

Taxpayer received royalty income on account of TCL from Indian company and also accrued business income in respect of activities carried out by its branch office (engaged in sourcing engines and exporting the same outside India, providing after-sale support services for products sold and licenses granted to customers in India, and provision of technical support services to customers in India). In the course of tax audit, tax authorities contended that royalty income earned under the TCL is also attributable to the activities carried out by the branch office, and thus, taxed as business income at 40%⁸ without making adequate enquiry.

Fees for technical services/ royalty income would be treated as business income only if it can be established that the services were effectively connected with the PE in India. To 'effectively

1 Delhi High Court rules in the case of CUB Pty Ltd v. UOI (71 taxmann.com 315)

2 Indian domestic tax law – Income-tax Act, 1961

3 Intellectual property

4 Authority of Advanced Rulings

5 The Delhi Income Tax Appellate Tribunal - in the case of Iveco S.p.A. (72 taxmann.com 195)

6 Technical Collaboration and License Agreement

7 Plus applicable surcharge and education cess

8 Plus applicable surcharge and education cess

connect' royalty income with the PE revenue, the following should be established:

- PE should be engaged in performance of technical services or should be involved in actual rendering of such services;
- It should arise as a result of the activities of the PE; and
- PE should, at least, facilitate, assist or aid in performance of such services irrespective of the other activities PE performs.

The Tribunal held that in absence of any material to prove that services were rendered by taxpayer through its branch office in India, royalty income earned by taxpayer under TCL could not be said to be effectively connected with PE in India. The royalty income was held to be taxable as per Article 13 of the tax treaty, and not as business income.

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