Indian court releases Nokia assets frozen in royalty tax dispute

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The Delhi High Court on 12 December 2013 ordered India's Department of Revenue to release the immovable assets of Finnish mobile phone company Nokia, including its Chennai factory, which tax authorities froze in September as a result of an INR 20.8 billion (about $335 million) royalty tax dispute.

The court ruled in *Nokia India Private Ltd v. Commissioner of Income Tax; CM No. 15485/2013; 6150/20132013* in favour of Nokia's appeal to lift the freeze and allow the transfer of some of its assets to Microsoft as part of a $7.3 billion deal. Under the deal, which was announced on 3 September, Nokia will sell its handset business and license patents to Microsoft; the transaction is scheduled to close in the first quarter of 2014.

However, in exchange for the asset release, Nokia is required to fulfil several conditions, including depositing INR 22.5 billion (about $364 million) in an escrow account and promising to pay any taxes, including penalties and interest, due under India's Income Tax Act, 1961. The court also held that Microsoft will not be liable for Nokia India's tax obligations.

According to a Nokia spokesman, the conditions are expected to be in line with international treaties and practices, and the company must now provide Indian tax authorities with additional documentation.

"The company will now start to prepare for the planned transfer of the assets, but notes that there are still a number of statutory clearances that remain before the assets can transfer," the spokesman said. "Nokia repeats its call for the Indian government to work with urgency to facilitate the other approvals needed for the transfer and secure employment for the tens of thousands of employees involved." The Nokia-Microsoft deal is expected to close on schedule, he said.

The spokesman said the court's decision does not resolve the tax dispute but could have a significant effect on the Chennai plant and its employees.

The ruling is the latest development in the ongoing dispute between Nokia and the Indian tax authorities, which came to a head in March when the Income Tax Department made a collective tax assessment of more than INR 20 billion (about $323 million) for five fiscal years, starting with 2006-2007. The demand stemmed from Nokia India's payments to its parent company in Finland for software used in the production of devices at the Chennai plant, one of the company's largest phone manufacturing units. Tax authorities argued that the payments were actually royalties, which are subject to a 10% tax deducted at source.

Nokia and the tax department went back and forth at the judicial level, with the phone company eventually approaching the Finnish competent authority for dispute resolution assistance through the mutual agreement procedure (MAP) under the Finland-India income tax treaty. The MAP was launched at the end of May.

In September Nokia won an appeal before the Delhi High Court, which released the company's bank accounts, but its immovable assets remained frozen. (For prior coverage, see Nokia wins appeal after Indian authorities freeze assets in tax dispute.)

Nokia then filed another appeal, asking the court to lift the freeze on the immovable assets by 12 December, and even approached the tax authorities directly with an offer to pay INR 22.5 billion to an escrow account to free the assets. However, the tax department rejected the offer.

However, Justices Sanjiv Khanna and Sanjeev Sachdeva wrote in their judgment that keeping the assets frozen would be detrimental to the Indian economy. They said the future of the employees at Nokia's Chennai factory is at stake and cannot be ignored. Nokia employs 8,000 workers directly and 25,000 workers indirectly.

The judges also said closing Nokia's Indian operations when the parent company is trying to sell its business to Microsoft may not be a sound decision and could lead to a sharp decline in the market value of Nokia's Indian assets.

The next step in the case is not immediately clear, but the judges speculated in their ruling that the dispute could be taken to the Supreme Court for final adjudication.