Sum received by Warner Bros. for distribution of films in India isn't 'royalty'; ITAT follows previous decision

Summary – The Mumbai ITAT in a recent case of Warner Bros. Distributing Inc., (the Assessee) held that where assessee, a US based company, engaged in distribution of cinematographic films, received certain amount from its divisional office on account of distribution of films in India, following order passed by Tribunal in assessee's own case relating to earlier assessment years, amount in question could not be taxed as royalty within meaning of Act or DTAA and, at same time, it could not be taxed as 'business income' because assessee did not have Permanent Establishment in India.

ORDER

This is an appeal filed by the assessee. It is directed against assessment order dated 18/10/2012 passed under section 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 (the Act). The grounds of appeal read as under:

1. On the facts and in the circumstances of the case and in law the order dated 18 Oct 2012, made under section 143(3) read with section 144C(13) for assessment year 2009-10 is wrong and bad in law.

2. On the facts and in the circumstances of the case and in law the learned Assessing Officer erred in assessing the royalty received by the appellant from Warner Bros. Pictures (India) Pvt. Ltd as business income u/s 5(2)19(1) (i) of the Income-tax Act, 1961 pursuant to the directions given by the Hon'ble Dispute

   Resolution Panel —II, Mumbai vide their order dated 03/09/2012 when in the case of Warner Bros. Pictures Inc. (the predecessor company), for AY. 2006-07 the claim of the assessee that the royalty received by it is not taxable either under the Income-tax Act, 1961 or India - USA DTAA is accepted by the Hon'ble ITAT, "L" Bench, Mumbai dismissing the appeal of the Department vide their order dated 30th December, 2011.

   (Now for A.Y. 2007-08 the claim of the appellant that the royalty received by it is not taxable either under the Income-tax Act, 1961 or India - USA DTAA is also accepted by the Hon'ble (ITAT, "I" Bench, Mumbai vide their order dated 10th October 2012)

3. On the facts and in the circumstances of the case and in law the learned Assessing Officer erred in holding that Warner Bros. Pictures (India) Pvt. Ltd is the Dependent Agency Permanent Establishment of the appellant pursuant to the directions given by Dispute

Resolution Panel -II, Mumbai vide their order dated 03/09/2012 ignoring the findings given by the Hon'ble ITAT, "I" Bench, Mumbai in the case of Warner Bros. Pictures Inc. (the predecessor company), for assessment year 2006-07 vide their order dated 30th December, 2011 that Warner Bros. Pictures (India) Pvt. Ltd is not the DAPE of the appellant.

(Now for AY. 2007-08 the claim of the appellant that Warner Bros Pictures (India) Pvt. Ltd is not the DAPE of the appellant is also accepted by the Hon'ble ITAT, "L" Bench, Mumbai vide their order dated 10th October 2012)

4. On the facts and in the circumstances of the case and in law the learned Assessing Officer erred in holding that the royalty received by the appellant from Warner Bros. Pictures (India) Pvt. Ltd is taxable in India pursuant to the directions given by Dispute Resolution Panel II, Mumbai vide their order dated 03/09/2012, even though the TPO has accepted that the royalty paid by Warner Bros. Pictures (India) Pvt. Ltd to the appellant is at arm's length.

5. On the facts and in the circumstances of the case and in law the learned Assessing Officer erred in holding that 65% would be the profits attributable to the alleged DAPE in India which amounts to Rs 2,16,25,721 pursuant to the directions given by Dispute Resolution Panel -II Mumbai vide their order dated 03/09/2012 when cogent evidence was produced before the AO/DRP-II that during the year under consideration the assessee company's world vide operating loss from distribution of films is 18.58%.

The assessee is a tax resident of USA and is engaged in the distribution of cinematographic films. The assessee entered into an agreement with Warner Bros. Pictures International, a division of the assessee through a letter dated 1/05/2006 and that unit is receiving royalty income from Indian company on account of distribution of film. The same was treated to be royalty and taxed accordingly. The assessee is aggrieved and hence, has raised aforementioned grounds of appeal.

During the course of hearing it was brought to our notice that the same issue initially arose in assessment year 2006-07 and has been decided by the Tribunal vide its order dated 30/12/2011 in ITA No.3160/Mum/2010 and C.O No. 17/Mum/2011, whereby the appeal filed by the revenue was dismissed with the following observations. Copy of the order is filed at pages 149 to 161 of the paper book.

We have considered the rival contentions and examined the facts on record. There is no dispute with reference to the fact that the assessee has entered into agreement with Warner Brothers Pictures India (P) Ltd. outside India and the amounts were also received outside India. There is also no dispute with reference to the fact that the definition of royalty under section 9(I)(vi) Explanation 2 to (v) excludes the payment received with reference to sale, distribution and exhibition of cinematographic films. There is

also no dispute with reference to the provisions of DTAA entered into by India with USA, notified on 20th December, 1990, that the term royalty used in the Article 12 does not include payment of any gain received as consideration for the use of any copyright or literary, artistic or scientific work including cinematographic films or work on films, tape or other means of production for use in connection with Radio or TV. broadcasting. In view of this specific provisions, the amount received by the assessee cannot be considered as royalty as was done by the Assessing Officer while invoking the Article 12(2) of the DT for taxing the amounts. To that extent the findings of the CIT (A) are correct and there is no need to deviate from such findings. In view of this the amount received by the assessee cannot be considered as royalty within the meaning of Indian Income Tax Act or under the DTAA.

The issue can be examined in another dimension whether the amount is taxable under the Indian Income Tax Act in India if not as royalty, but as business income. The CIT (A) finding is that assessee has a business connection in India. However, he considered that there is no PE to the assessee, the fact of which was also accepted by the Assessing Officer as he has invoked only Article 12(2) and not considered the amounts business income as per PE proviso. It was the contention of the learned Departmental Representative that the assessee having business connection, the findings of which was given by the CIT (A), the amount cannot be excluded without examining 'PE proviso' provisions of the DTAA. In this regard the learned Counsel's submission that under the Income Tax Act as well as under the provisions of DTAA the transaction between the assessee and Indian Company to whom license was granted by virtue of the agreement cannot be considered as Agency PE as the Indian assessee is not exclusively dealing with the assessee and referred to the receipts from another company 20th Century Fox to submit that the assessee is also dealing with the other Non Resident Companies, so assessee cannot be considered as Agency PE within the definition of Permanent Establishment.

We have examined this aspect also. As rightly held by the CIT (A) even if income arises to the Non-Resident due to the business connection in India, the income accruing or arising out of such business connection can only be taxed to the extent of the activities attributed to permanent establishment. In this case, the assessee does not have any permanent establishment in India. Since the Indian company who obtained the rights is acting independently, Agency PE provisions are not applicable to the assessee company. The assessee relied on the decision of Ishikawajma-Harima Heavy Industries Ltd vs. Director of Income Tax 2007-(158)-TAXMAN 0259-SC that incomes arising to a Non-Resident cannot be taxed as business income in India, without a PE. As the assessee does not have any permanent establishment in India, the incomes arising outside Indian Territories cannot be brought to tax. Therefore, there is no need to differ from the findings of the CIT (A) and accordingly the Revenue Appeal is dismissed..

The aforementioned order was also followed by the Tribunal vide its order dated 10/10/2012 in respect of assessment year 2007-08. The reference in this regard can be made to the order of the Tribunal, in ITA No.8734/Mum/2010, copy of which is placed at pages 162 to 167 of the paper book. Thus it was pleaded by Ld. AR that the appeal filed by the assessee should be allowed.

Ld. DR did not dispute that the facts relating to aforementioned assessment years and the year under consideration were similar. However, he relied upon the assessment order.

In view of the above situation, after hearing both the parties, respectfully following the aforementioned decision of the Tribunal in assessee's own case we hold that income arising to the assessee cannot be taxed as royalty within the meaning of Income Tax Act or DTAA and it also cannot be taxed in the hands of the assessee as 'business income' as assessee does not have any Permanent Establishment in India.

Before parting, we may mention here that aforementioned order of Tribunal in respect of assessment year 2006-07 was referred by the assessee before DRP. However, DRP has not accepted such claim of the assessee on the ground that the issue before the Tribunal was only in respect of section 9(1)(vi) of the Act and the issue regarding its taxability as 'business income' was not decided elaborately and it was only in respect of additional ground preferred by the revenue. It is also mentioned in the order that Department has filed an appeal before the Hon'ble High Court against the order of the Tribunal. However, from the observations of the Tribunal, which are reproduced above, it is clear that Tribunal has extensively considered this issue and the issue has been decided in detail by the Tribunal that the receipts of the assessee cannot also be taxed as business income in India as assessee does not have any Permanent Establishment in India. Therefore, the observations of DRP to that extent are contrary to the order of the Tribunal.

In the result, the appeal filed by the assessee is allowed in the manner aforesaid.