

# Tribunal rules payment made by Google India to Google Ireland under Adword distribution agreement is taxable as ‘royalty’

## Summary

In a recent ruling, the Bangalore Tribunal (‘Tribunal’) in the case of **Google India Private Limited (reported in TS-468-ITAT-2017(Bang))** has held that payment made by Google India Private Limited (‘Google India’) to Google Ireland Limited (‘GIL’) under the Google Adword Program Distribution agreement (‘Adword agreement’) qualifies as ‘Royalty’ under the Income Tax Act, 1961 (‘the Act’) and the India-Ireland Double Taxation Avoidance Agreement (‘DTAA’ or ‘Treaty’) and consequently subject to withholding tax in India. The Tribunal rejected Google India’s contention that it is merely a reseller of advertisement space under the Adword agreement and no rights in the intellectual property of Google was granted to Google India.

## Facts of the case

- Google India is a wholly owned subsidiary of Google International LLC, US. It has been appointed by GIL as a non-exclusive authorised distributor of the Adword Program in India under the Adword Program Distribution Agreement. Under the Adword agreement, Google India was granted marketing and distribution rights of Adword program to the advertisers in India.
- Google India is also engaged in providing Information Technology (‘IT’) and IT enabled Services (‘ITES’) to its overseas group companies towards ensuring that the advertisements conform with Google’s guidelines and local regulations for which Google India is separately compensated on an arms-length basis.
- The activities carried on by Google India as per the Adword agreement are as under:

- Google India is authorised for resale of advertisement space to the Indian customers;
  - Google India carries on marketing related activities to promote the sales of advertising space to Indian advertisers;
  - Google India enters into contracts with India advertisers for sale of advertisement space under the Adword program;
  - It provides assistance / training to Indian advertisers, if needed in order to familiarise them with the features / tools available as part of the Adword product;
  - Google India raises resale invoice on the advertisers and collects payments.
  - Google India remits the amount payable to GIL under the Adword agreement towards purchase of advertising space.
- Based on the above facts, Google India contended that it merely resells the products and services (under the Adword agreement) which are developed by Google Incorporation USA and its subsidiaries outside India. Google India further contended that no rights in the intellectual property of Google were transferred to it by GIL under the Adword agreement.
  - Accordingly, the payments do not qualify as royalty and Google India was not liable to withhold any tax on payments made to GIL.
  - The Assessing Officer (“AO”) initiated proceedings under section 201(1) of the Act and treated Google India as assessee in default for not withholding tax on these payments. The AO held that the payments qualified as royalty and was subject to withholding tax in India. On appeal, the CIT(Appeals) upheld the order of the AO.
  - Aggrieved by the order passed by the CIT(Appeals), Google India filed an appeal before the Bangalore Tribunal.

We have summarised the arguments of Google India and the revenue authorities before the Tribunal and the ruling of the Tribunal in the table below:

Key issues for consideration	Google India Contentions	Revenue Contentions	Tribunal Ruling
<p><b>Whether purchase of advertisement space under the Adword agreement is equivalent to transfer of right or right to use any copyright, patent, invention, know how or use of industrial, commercial and scientific equipment</b></p>	<ul style="list-style-type: none"> <li>• The amount payable by Google India to GIL is towards purchase of advertisement space under the Adword program and not in relation to transfer of any 'right' or 'right to use' any copyright, patent, know how etc.</li> <li>• The Adword agreement does not envisage use of patents, invention, model, design, secret formula or process or trademark or similar property by Google India. Further, all rights, title and interest in all information and data are owned by GIL.</li> <li>• The training material/ information are publicly available and therefore, the same cannot be</li> </ul>	<ul style="list-style-type: none"> <li>• Intellectual Property Rights ("IPR") of Google resides in search engine technology, associated software and other features. Hence, the right to use IPR for performing various activities like accepting advertisements and providing after sale services would clearly fall within the ambit of "Royalty".</li> <li>• By acquiring the distribution and marketing rights, Google India gets license to use the above IPR.</li> <li>• The knowledge of tools and training on the usage of IPR, knowledge on trademark</li> </ul>	<ul style="list-style-type: none"> <li>• The gamut of activities performed by Google India indicates that the Adword agreement was not for providing advertisement space but for utilising the search engine technology, associated software and other features required for performing various activities including accepting advertisements and providing before and after sales services.</li> <li>• This facilitates display and publishing of an advertisement to the target customer. The IPR of the Google search engine technology, therefore</li> </ul>

	<p>considered as imparting of information concerning working of or use of any patent.</p> <ul style="list-style-type: none"> <li>Moreover, Google India is not concerned with the infrastructure/server installed by GIL or the components embedded in it. The operation, control and maintenance of the server, solely rests with GIL.</li> </ul>	<p>policy, advertisement content policy has been imparted through extensive training by GIL to Google India which would amount to transfer of know-how and would classify as royalty.</p> <ul style="list-style-type: none"> <li>Adword program is in one way commercial and scientific equipment and without having access to the servers running on the Adword platform, Google India cannot perform its functions/ exploit its rights as per the Adword agreement.</li> </ul>	<p>vests in Google India and the payments made to GIL falls with the ambit of 'Royalty'.</p>
<p><b>Whether transaction involved grant of right to use of Trademarks and Brand features</b></p>	<ul style="list-style-type: none"> <li>Google India merely resales / distributes advertisement space under Adword program and use of Google brand is only incidental to this main purpose. Such an</li> </ul>	<ul style="list-style-type: none"> <li>Under Adword agreement, Google India has been granted right to use trademarks and brand</li> </ul>	<ul style="list-style-type: none"> <li>Under the Adword agreement, Google India was permitted to use trademark, service mark, domain etc. which is essential and pivotal for doing the</li> </ul>

	<p>incidental use cannot be considered as royalty.</p> <ul style="list-style-type: none"> <li>• Reliance was placed on Delhi High Court decision in case of Sheraton International Inc.<sup>1</sup> and Formula One Worldwide Championship Ltd.<sup>2</sup></li> </ul>	<p>features for the purpose of selling advertisement space.</p> <ul style="list-style-type: none"> <li>• The right to use Google trademarks and other brand features would amount to use of intellectual property and the consideration therefore, constitutes Royalty under the Act.</li> </ul>	<p>business of selling of advertisement space.</p> <ul style="list-style-type: none"> <li>• In the absence of the Google trademark, it is difficult to comprehend that Google India would attract lot of advertisers. Therefore, payment made under the Adword agreement was not only for marketing and promoting the Adword programs but also for use of Google brand features.</li> <li>• The Tribunal held that the rulings in case of Sheraton International and Formula One relied upon by Google India are not applicable in the present case as use of trademark for advertising, marketing and booking in</li> </ul>
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<sup>1</sup> (2009) 313 ITR 267 (Del)

<sup>2</sup> (2016) 76 Taxmann.com 6 (Del.)

			<p>these rulings were incidental activities of the assessee and not the main activities. Whereas in the present case the main activity of the assessee is to do marketing of advertisement space for Google Adword Program.</p>
<p><b>Whether grant of distribution rights involves transfer of rights in process</b></p>	<ul style="list-style-type: none"> <li>• Adword program cannot be considered as a "process" within the meaning under Explanation 2(i) to section 9(1)(vi) of the Act.</li> <li>• Further, Adword Program cannot be equated to a secret process since information relating to the program is freely available in the public domain.</li> </ul>	<ul style="list-style-type: none"> <li>• Under the Adword agreement, Google India has been granted distribution rights involving transfer of rights in process.</li> <li>• The entire search engine technology on which license has been granted to Google India for selling advertisement space to the advertisers is a "process". Hence the payment towards license to</li> </ul>	<ul style="list-style-type: none"> <li>• Although details of Adword Program are available in public domain, but the manner in which the Adword program functions for targeted marketing campaign and promoting advertisements are only possible with the use of secret formula or process.</li> <li>• Therefore conclusion of the AO that Google India was using the secret process for</li> </ul>

		use the "process" would qualify as "royalty".	marketing and promoting of the advertisement is correct.
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Some of the other key observations of the Tribunal are as follows:

- The findings of the Technical Advisory Group and High Powered Committee on taxability of payment for online advertisement was held to be not applicable to the present case as Google India's case is peculiar and facts specific which was neither considered or deliberated by the committee.
- The Tribunal distinguished the Kolkata Tribunal ruling in the case of Right Florist Private Limited<sup>3</sup> and Mumbai Tribunal ruling in the case of Pinstorm Technologies P. Ltd<sup>4</sup> and Yahoo India P. Ltd<sup>5</sup>. It stressed on the detailed working of the Adword program and noted that Google India is having the right to access to the patented technology, customer data, information (like telephone number, user behaviours, region, gender, language, colour, photographs, place of visit, mobile device used, time spent etc.) which was not the case in the aforesaid decisions.
- The Tribunal also states that there is inter-se bidding amongst the advertisers for displaying the advertisements on a real time basis, which envisages the fact that the advertisement space is not sold by Google India, rather the placement of the advertisement to a particular targeted customer at a particular time is bided among the advertisers. Google India provided these services to advertisers with the help of patented Adword program.

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<sup>3</sup> (2013) 154 TTJ 142 (Kolkata Tribunal)

<sup>4</sup> (2013) 154 TTJ 173 (Mum Tribunal)

<sup>5</sup> (2011) 46 SOT 105 (Mum Tribunal)

## Our View

The decision of the Bangalore Tribunal in Google's case is fact specific as the Tribunal has analysed several aspects of the Adword program and gone beyond the scope of the distribution arrangement. The judgment may have implications on taxability of payments under reseller/ distribution arrangements for several kinds of digital transactions.

While the ruling is likely to be challenged before higher judicial forum, with introduction of equalization levy on payments to non-resident for online advertising effective 1 June 2016, this ruling should not affect taxability of payments by advertisers for online advertisements going forward.



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