

Foreign remittance for warranty costs on exports sales not taxable as ‘Fees for Technical Services’ - Chennai Tribunal

Summary

The Chennai bench of Income-tax Appellate Tribunal (‘ITAT’ or ‘Tribunal’), in the case of **Nissan Motor India Pvt. Ltd**¹ (‘taxpayer’), has held that reimbursement of warranty costs incurred by non-resident dealer will not be taxable in India as fees for technical services (‘FTS’) under the Income-tax Act, 1961 (‘Act’) as it is incurred for the purpose of earning income from a source outside India. The Tribunal also held that payments made for obtaining license for use of standard software would not be in the nature of royalty.

Facts of the case

- The taxpayer is engaged in the business of manufacturing and selling motor cars in India as well as abroad. Motor cars are sold outside India through group companies who act as the taxpayer’s dealers.
- The taxpayer has made payments towards reimbursement of warranty expenses incurred by non-resident dealers and towards purchase of certain software from companies based in United Kingdom and Japan. No tax was deducted at source on these payments.
- The Assessing Officer (‘AO’) held that the contract of warranty is between the taxpayer and the end customers outside India. In order to comply with the warranty promised to the end customers, the taxpayer has engaged the services of its dealers, which are in nature of technical service as these services are provided by technical experts. Thus, the reimbursement of warranty expenditure was held to be taxable as FTS in India.
- Further, the AO held the payments made for the purchase of software as royalty.

¹ TS-153-ITAT-2018(CHNY)

- With regard to warranty reimbursements, the taxpayer took the following arguments:
 - The payment is for reimbursement of costs towards parts and labour incurred by the non-resident dealers. Hence, payment made is not in the nature of FTS;
 - The services are utilised for the purpose of earning income from a source outside India and hence are out of the purview of FTS under the provisions of the Act;
 - Further, where the payments are made to a country with which India has entered into a Double Taxation Avoidance Agreement ('DTAA' or 'Tax Treaty') and such DTAA does not have a FTS clause, such payments shall not be liable to withholding tax.
- On payments made for purchase of software from United Kingdom and Japan, the taxpayer placed reliance on the decision of the Chennai Tribunal in the case of Atmel R&D India (P) Ltd.²
- On appeal, the assessment order was upheld by the first appellate authority.

ITAT Ruling

- The ITAT observed that the dealers maintained the cars sold by them according to the terms of warranty promised by the taxpayer. The expenditure was incurred for a contractual obligation of the taxpayer, who reimbursed these expenses.
- The ITAT held that the taxpayer has incurred these expenses outside India for the purpose of earning income from source outside India. Such payment would fall within the exception provided in the Act and would not fall within the ambit of FTS.
- On the payments made for purchase of software, the ITAT relied on its own divisional bench ruling in the case of Atmel R&D India (P) Ltd (supra), wherein it was held that the payment is for purchase of a copyrighted article and not for granting of the copyright. It was also held that the license has been granted to permit the use of the programme and is only incidental to the facility extended to the licensee to make use of the copyrighted product for its internal business purpose.

² Atmel R&D India (P) Ltd. (2016) 74 taxmann.com 106 (Chennai Tribunal)

Our comments

The issue of when an income is said to arise from a source outside India has been a subject matter of considerable debate. There are conflicting High Court decisions on whether source of income in case of 'export sales' is located outside of India. Similarly, there are conflicting judgements on taxation of software payments. Thus, one needs to take a holistic view of the available jurisprudence and facts of a case while taking any position in this regard.



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