

## Tax Hotline

April 26, 2007

### MUMBAI TRIBUNAL HOLDS ARM'S LENGTH PAYMENT TO DEPENDENT AGENT DOES NOT EXTINGUISH LIABILITY OF A PERMANENT ESTABLISHMENT

The Mumbai tax tribunal ("Tribunal") has recently held in case of SET Satellite (Singapore) Pte. Ltd. ("SET") that payment of arm's length price to the dependent agent does not extinguish the tax liability of the foreign company in India. The Tribunal has endorsed the 'dual entity approach' and held that dependent agent Permanent Establishment ("PE") is distinct from the dependent agent and both can be taxed separately in India. This means even though arm's length price is paid to a related entity in India by a foreign company, additional tax can be imposed on the foreign company's revenues earned from India. This ruling is likely to increase tax uncertainties in India, thus increasing business risks for foreign companies doing business in India through a dependent agent.

The ruling comes in the middle of a raging controversy on attribution of income to a PE. Recently, the Authority for Advance Rulings had held in the case of Morgan Stanley that if the Indian company is paid an arm's length price, no further attribution can be made to the PE in India. The tax office had appealed to the Supreme Court of India on this issue, and a ruling is expected shortly.

In this case, SET was a telecasting company tax resident in Singapore. SET had appointed an agent in India for marketing airtime slots and the agent constituted a dependent agent PE. SET argued that as it remunerated the Indian agent at an arm's length price, nothing further would be attributable to it in India. In arriving at this position SET relied on Circular no. 23 of 1969 and Circular no. 5 of 2004 (which was a clarification on the taxation in case of outsourcing industry) issued by the Central Board of Direct Taxes.

The Tribunal decided the case against SET holding that the 'dependent agent' and the 'dependent agent PE' were two different tax payers. The income earned from India by the dependent agent PE would be taxable in India and a deduction would be allowed for the payment made to the dependent agent.

In coming to this conclusion the Tribunal relied on the OECD Report on 'Attribution of Profits to PE', and the Australian Tax Office paper on the attribution of profits in case of dependent agent PE. In countering the argument that, as stated in the OECD Report a change in the language of the tax treaty currently in place between India and Singapore would be required in order for the report to be applied, the Tribunal held that the language of the treaty as it currently stands merits this interpretation.

The Tribunal thus seems to have departed from the single tax payer approach thus far followed in India, and adopted the dual tax payer approach advocated by the OECD. It remains to be seen which approach the Supreme Court of India will take with regard to the issue. This decision is likely to impact many foreign companies which are doing business in India through dependent agents.

- Annapoorna Jayaseelan & Shefali Goradia

Source: ITA No. 205 and 535 / Mum / 04

### DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

## Research Papers

### Telemedicine in India

August 31, 2024

### Clinical Trials and Biomedical Research in India

August 31, 2024

### Compendium of Research Papers

August 27, 2024

## Research Articles

### Acquirers Beware: Indian Merger Control Regime Revamped!

September 15, 2024

### Navigating the Boom: Rise of M&A in Healthcare

August 23, 2024

### Navigating The Change in Shareholding and Management Rule for Non-Banking Financial Companies in India: A Practical Perspective

August 22, 2024

## Audio

### Renewable Roadmap: Budget 2024 and Beyond - Part I

August 26, 2024

### Renewable Roadmap: Budget 2024 and Beyond - Part II

August 26, 2024

### Renewable Roadmap: Budget 2024 and Beyond - Part III

August 26, 2024

## NDA Connect

Connect with us at events, conferences and seminars.

## NDA Hotline

Click here to view Hotline archives.

## Video

### Union Budget: Key takeaways for Private Equity Investors and Foreign Companies

July 24, 2024

**Self Declaration Certificate For Ads:  
Decoding The Complexities Of Ad  
Regulations**

July 08, 2024

**Future of India-Mauritius tax treaty –  
Impact of new Protocol on M&A  
deals and Private Equity structures**

April 23, 2024