

# Emerging Tax Issues in the Broadcasting Industry

---

The Need to Remove Ambiguities,  
Retrospective Operation and  
Facilitate Doing Business in India

September 2013

## About NDA

Nishith Desai Associates (NDA) is a research based international law firm with offices in Mumbai, Bangalore, Silicon Valley, Singapore, New Delhi & Munich. We specialize in strategic legal, regulatory and tax advice coupled with industry expertise in an integrated manner. We focus on niche areas in which we provide significant value and are invariably involved in select highly complex, innovative transactions. Our key clients include marquee repeat Fortune 500 clientele.

Our practice areas include International Tax, International Tax Litigation, Litigation & Dispute Resolution, Fund Formation, Fund Investments, Corporate & Securities Law, Mergers & Acquisitions, Competition Law, JVs & Restructuring, Capital Markets, Employment and HR, Intellectual Property, International Commercial Law and Private Client. Our specialized industry niches include funds, financial services, IT and telecom, pharma and healthcare, media and entertainment, real estate and infrastructure & education.

Nishith Desai Associates has been ranked as the Most Innovative Indian Law Firm (2014 & 2015) at the Innovative Lawyers Asia-Pacific Awards by the Financial Times - RSG Consulting. Nishith Desai Associates has been awarded for “Best Dispute Management lawyer”, “Best Use of Innovation and Technology in a law firm”, “Best Dispute Management Firm”, and “M&A Deal of the year” by IDEX Legal 2015 in association with three legal charities; IDIA, iProbono and Thomson Reuters Foundation. Nishith Desai Associates has been recognized as a Recommended Tax Firm in India by World Tax 2015 (International Tax Review’s directory). IBLJ (India Business Law Journal) has awarded Nishith Desai Associates for Private equity & venture capital, structured finance & securitization, TMT and Taxation in (2014/2015). IFLR1000 has ranked Nishith Desai Associates in Tier 1 for Private Equity (2014). Chambers and Partners ranked us as # 1 for Tax and Technology-Media-Telecom (2014/2015). Legal 500 ranked us in # 1 for Investment Funds, Tax and Technology-Media-Telecom (TMT) practices (2011/2012/2013/2014). IDEX Legal has recognized Nishith Desai as the Managing Partner of the Year (2014).

Legal Era, a prestigious Legal Media Group has recognized Nishith Desai Associates as the Best Tax Law Firm of the Year (2013). Chambers & Partners has ranked us as # 1 for Tax, TMT and Private Equity (2013). For the third consecutive year.

International Financial Law Review (a Euromoney publication) has recognized us as the Indian “Firm of the Year” (2012) for our Technology - Media - Telecom (TMT) practice. We have been named an Asian-Mena Counsel ‘In-House Community Firm of the Year’ in India for Life Sciences practice (2012) and also for International Arbitration (2011). We have received honorable mentions in Asian Mena Counsel Magazine for Alternative Investment Funds, Antitrust/Competition, Corporate and M&A, TMT and being Most Responsive Domestic Firm (2012).

We have been ranked as the best performing Indian law firm of the year by the RSG India Consulting in its client satisfaction report (2011). Chambers & Partners has ranked us # 1 for Tax, TMT and Real Estate – FDI (2011). We’ve received honorable mentions in Asian Mena Counsel Magazine for Alternative Investment Funds, International Arbitration, Real Estate and Taxation for the year 2010.

We have been adjudged the winner of the Indian Law Firm of the Year 2010 for TMT by IFLR. We have won the prestigious “Asian-Counsel’s Socially Responsible Deals of the Year 2009” by Pacific Business Press.

In addition to being Asian-Counsel Firm of the Year 2009 for the practice areas of Private Equity and Taxation in India. Indian Business Law Journal listed our Tax, PE & VC and Technology-Media-Telecom (TMT) practices in the India Law Firm Awards 2009. Legal 500 (Asia-Pacific) has also ranked us #1 in these practices for 2009-2010. We have been ranked the highest for 'Quality' in the Financial Times – RSG Consulting ranking of Indian law firms in 2009. The Tax Directors Handbook, 2009 lauded us for our constant and innovative out-of-the-box ideas. Other past recognitions include being named the Indian Law Firm of the Year 2000 and Asian Law Firm of the Year (Pro Bono) 2001 by the International Financial Law Review, a Euromoney publication.

In an Asia survey by International Tax Review (September 2003), we were voted as a top-ranking law firm and recognized for our cross-border structuring work.

Our research oriented approach has also led to the team members being recognized and felicitated for thought leadership. NDAites have won the global competition for dissertations at the International Bar Association for 5 years. Nishith Desai, Founder of Nishith Desai Associates, has been voted 'External Counsel of the Year 2009' by Asian Counsel and Pacific Business Press and the 'Most in Demand Practitioners' by Chambers Asia 2009. He has also been ranked No. 28 in a global Top 50 "Gold List" by Tax Business, a UK-based journal for the international tax community. He is listed in the Lex Witness 'Hall of fame: Top 50' individuals who have helped shape the legal landscape of modern India. He is also the recipient of Prof. Yunus 'Social Business Pioneer of India' – 2010 award.

We believe strongly in constant knowledge expansion and have developed dynamic Knowledge Management ('KM') and Continuing Education ('CE') programs, conducted both in-house and for select invitees. KM and CE programs cover key events, global and national trends as they unfold and examine case studies, debate and analyze emerging legal, regulatory and tax issues, serving as an effective forum for cross pollination of ideas.

Our trust-based, non-hierarchical, democratically managed organization that leverages research and knowledge to deliver premium services, high value, and a unique employer proposition has now been developed into a global case study and published by John Wiley & Sons, USA in a feature titled 'Management by Trust in a Democratic Enterprise: A Law Firm Shapes Organizational Behavior to Create Competitive Advantage' in the September 2009 issue of Global Business and Organizational Excellence (GBOE).

Please see the last page of this paper for the most recent research papers by our experts.

## Disclaimer

This report is a copyright of Nishith Desai Associates. No reader should act on the basis of any statement contained herein without seeking professional advice. The authors and the firm expressly disclaim all and any liability to any person who has read this report, or otherwise, in respect of anything, and of consequences of anything done, or omitted to be done by any such person in reliance upon the contents of this report.

## Contact

For any help or assistance please email us on [concierge@nishithdesai.com](mailto:concierge@nishithdesai.com) or visit us at [www.nishithdesai.com](http://www.nishithdesai.com)

# Contents

<b>1.</b>	<b>EMERGING TAX ISSUES IN THE BROADCASTING INDUSTRY</b>	<b>01</b>
I.	Scheme of Taxability of Foreign Broadcasters	<b>01</b>
II.	Taxability Under the ITA	<b>01</b>
III.	Taxation of Distribution Income	<b>02</b>
IV.	Payment for use of 'Satellite Broadcasting Rights' as Constituting 'Royalty'	<b>03</b>
V.	Impact of Retroactivity of the Amendment	<b>03</b>
VI.	Position under the Direct Taxes Code, 2010 ("DTC")	<b>04</b>
VII.	Payments to Multi-System Operators as Constituting 'Royalty'	<b>04</b>
VIII.	Payments for Advertising to Broadcasting Channels	<b>04</b>
IX.	The Way Forward	<b>05</b>

# 1. Emerging Tax Issues in the Broadcasting Industry

## The Need to Remove Ambiguities, Retrospective Operation and Facilitate Doing Business in India

The issues around taxation of payments in the broadcasting sector are perhaps amongst the most litigious in the recent years. This industry has been at the forefront of tax controversies owing to the specific nature of cross-border business operations in the broadcasting sector, and the disputed nature of taxation of these transactions. Foremost amongst these are the issues of characterisation of such payments as ‘Royalty’ or otherwise, and their taxation as such.

### I. Scheme of Taxability of Foreign Broadcasters

Royalty payments are considered taxable under section 9(1)(vi) of the Income Tax Act, 1961 (“ITA”) if the payer is an Indian resident, unless such resident makes the royalty payment for a business carried on outside India. However, under section 90(2) of the ITA, if the non-resident is situated in a country with which India has a double taxation avoidance agreement (“Tax Treaty”), the taxpayer would, at his option, be taxable according to the provisions of the Tax Treaty or the ITA.

The significant distinction between taxation of payments made to foreign broadcasters under the ITA vis-à-vis the Tax Treaty, is that under the Tax Treaty, unlike under the ITA, the mere receipt of income in India will not make the taxable in India. Furthermore, the concept of permanent establishment (“PE”) under a Tax Treaty is more restricted in comparison with the concept of business connection under

the ITA. Consequently taxation of payments relating to foreign broadcasters under the provisions of the Tax Treaty are typically more favorable as compared to the ITA.

### II. Taxability Under the ITA

Section 9 is the deeming provision relating to the income of non-residents that are considered to have its source in India. Section 9(1)(vi)(b) of the ITA deals with royalty paid by an Indian resident and received by a non-resident, and Explanation 2 thereto defines ‘Royalty’ as:

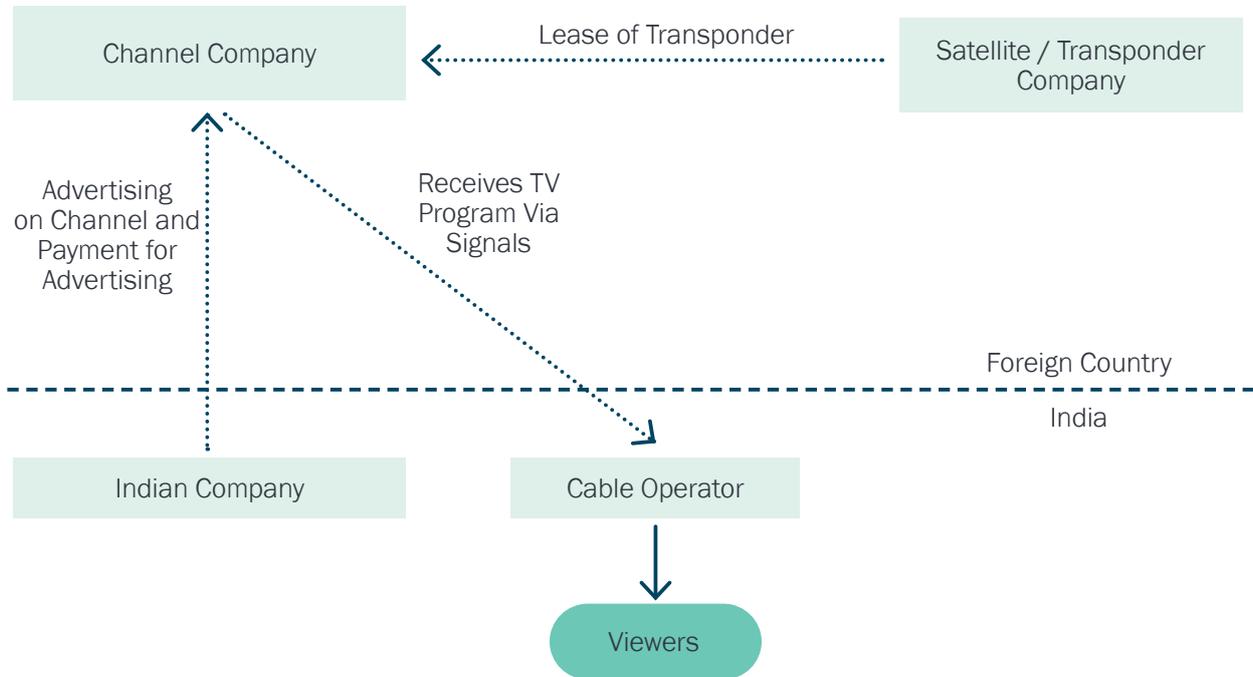
- 
- 
- “Explanation 2.—For the purposes of this clause, “royalty” means consideration ... for—*
- i. the transfer of all or any rights... In respect of... a process...;*
  - ii. the imparting of any information concerning the working of... a process...;*
  - iii. The use of any...process;*
- 
- 

It may be important to note in this regard that, through a *retrospective* amendment to the ITA by the Finance Act, 2012 the expression “*process*”, through Explanation 6 has been made to include transmission by satellite, including a blinking, amplification or conversion for down linking of any signal. This explanation is significant owing to the fact that the term ‘process’ now explicitly includes the use of transponders for satellite communication.

However, regardless of changes to the ITA, the

definition of royalty under the DTAA remains unchanged and the provision beneficial to the assessee will apply. This position has been upheld by the Income Tax Appellate Tribunal

in the case of *B4U International Holdings Ltd. v. DCIT*.<sup>1</sup>



As may be gathered from the figure above, issues surrounding the characterization of payments, as royalty or otherwise, emerge of two main streams of income, being (i) Use of the satellite or transponder company for the transmission of signals, or (ii) payments made to the broadcasting company in the nature of subscription or advertising revenue. The following illustrate some of the key concerns surrounding the same.

### III. Taxation of Distribution Income

In a contract where foreign broadcasters grant rights to distribute data content in Indian territory to Multi-System Operators

(“MSO”) / cable operators / DTH operators, a percentage of the revenues derived from the distribution of such content is paid to the foreign broadcasters as ‘license fees’ for such distribution rights. There are conflicting opinions on whether such distribution income would be taxable in India, as contingent on the question of whether such income ‘accrued or arises’ in India. For instance in two rulings, *Performing Rights Society Ltd. v. CIT*<sup>2</sup> and *Metro-Goldwyn-Mayer v. CIT*<sup>3</sup>, it was held that such distribution in fact would be taxable in India, on the grounds that the fees payable are predicated on the exploitation of television content in India. On the contrary, the Supreme Court in the case of *CIT v. Carborandum*<sup>4</sup> held that merely on account of the fact that the quantum of income accruing to the non-

1. TS-358-ITAT-2012.  
 2. 106 ITR 11.  
 3. 7 ITR 176.  
 4. 108 ITR 335.

resident is contingent on exercise of such rights in India, the inference that operations were carried on by the non-resident in India, does not logically follow; in the absence of any operations carried out by the non-resident in India the income accruing to him from distribution of such rights cannot be said to accrue or arise in India.

#### IV. Payment for use of ‘Satellite Broadcasting Rights’ as Constituting ‘Royalty’

Taxability of income for the use of the satellite or transponder is an issue that has found conflicting opinions from various adjudicatory fora. As regards characterisation of subscription revenues, the question arises as to whether it is in the nature of business income or royalty, and this has been a matter of much controversy. While foreign broadcasters claim such revenues are business income, and therefore not subject to tax in India, tax authorities term such income as royalty and subject to 25% tax on a gross basis. The question here is whether payments for the use of a satellite by broadcasting companies, constitutes ‘royalty’ under section 9(1)(iv) of the ITA. There have been differing viewpoints on this issue; for instance in *Asia Satellite Telecommunication Co. Ltd.*<sup>5</sup> the Delhi High Court held that no income accrued in India from the use of satellite outside India to beam signals for viewing in India even if the bulk of revenue arises from India. Similarly, in *ADIT v. Neo Sports Broadcast Pvt. Ltd.*<sup>6</sup> the ITAT held that payment for licences for live broadcast of cricket matches was not ‘royalty’ under the ITA. The position has expectedly changed pursuant to the amendment to the ITA vide

Explanation 6; accordingly, the Chennai ITAT in *Balaji Communications*<sup>7</sup> held that payment for satellite broadcasting rights constituted royalty under section 9(1)(iv) of the ITA and should be taxed.

One would notice that even though the ITA has been retrospectively amended to specifically include satellite transmissions within the purview of section 9 and consequently held to be taxable, the position under the Tax Treaty remains unaffected by such amendment. Resultantly, since the taxpayer has the right to be governed by either the ITA or the Tax Treaty, whichever is more beneficial, the position would have no bearing in the context of foreign broadcasters claiming under a Tax Treaty. This position was reiterated by the Mumbai Tribunal in *B4U International Holdings Ltd.*<sup>8</sup>

#### V. Impact of Retroactivity of the Amendment

Given that Explanation 6 to section 9(1)(vi) has been introduced with retrospective effect from 1976, certain questions arise with respect to the of disallowance in respect of payments made in lieu of broadcasting rights previous years; In such cases, taxes may not have been deducted relying on the position of law prior to 2012. Resort, in such situations may lie generally with principles of interpretation of statutes, interpretations to the Constitution against retroactivity of statutes and lastly, judicial precedent.

In this respect, the Mumbai tribunal in a recent case of *Channel Guide Limited*<sup>9</sup> relied on the legal maximum ‘*lex non cogit ad impossibilia*’ and thereby ruled out disallowance (in the context of Explanation 4 on account of non-deduction of taxes in

5. 85 ITD 478.

6. TS-649-ITAT-2011.

7. 140 ITD 687.

8. 18 ITR 62.

9. 139 ITD 49.

respect of satellite payments made for earlier years. Based on the principle underlying the Tribunal's decision in this ruling and in the case of *Sonata Information Technology*,<sup>10</sup> it could be argued that Explanation 6 to section 9(1)(vi) of the ITA is not relevant for determining the disallowance under section 40(a)(i) and accordingly payments made prior to 2012 are not to be disallowed.

## VI. Position under the Direct Taxes Code, 2010 ("DTC")

Along the same lines, the definition of 'royalty' under the Direct Taxes Code, 2010, is expanded to include the use or right to use of transmission by satellite, cable, optic fibers of the technology of the transfer of all or any rights in respect of live coverage of any event. Accordingly, lease payments made for the use of transponders would be taxable as royalties under the DTC.

## VII. Payments to Multi-System Operators as Constituting 'Royalty'

Another significant issue on which the broadcasting industry is at loggerheads with the tax authorities relates to withholding tax on payment for production of TV programs, carriage fees/ placement charges paid to MSOs and cable operators, and so on. Broadcasting companies claim that such payments attract tax deductible at source ("TDS") of 2 per cent as payment for 'work' carried out by the recipients. Their rationale is that since the term 'work' has been defined in section 194C(iv)(c) of the ITA-as including broadcasting and telecasting including production of programs for such broadcasting and telecasting- it must consequently be taxed as such. The tax authorities contend that

such payments are in the nature of royalty/ fees for technical services and consequently liable to be taxed at 25% and liable to be withheld under section 194J of the ITA. This aspect has come up particularly often over the last two years with a large number of initial assessments by the Assessing Officer characterizing such payments in the nature of Royalty. One must note here that while 194J is the provision for withholding of taxes on 'royalty', section 194C is the provision that specifically applies to withholding in case of broadcasting and telecasting; based on established norms of interpretation, that the specific provision would over-rule the general provision, it should follow that tax on such payments must be withheld pursuant to section 194C.

In case where the distribution rights granted by foreign broadcasters are in fact termed as 'royalty', the same would be taxed in case of foreign companies under section 115A (1)(b) at the rate of 30%, 20% or 10% based on date on which such agreement was entered into.

## VIII. Payments for Advertising to Broadcasting Channels

The primary controversy relating to taxation of advertising income in India that relates to determination of the place of accrual of advertising income so derived. In this respect, the case of *Star Ltd. vs. DDIT*<sup>11</sup> held that advertisement contracts will not contract for sale of goods; consequently the nature of advertising agreements could essentially be considered in the nature of contract for rendering of services. Based on this ruling, advertisement income would be said to accrue or arise at the place where the primary obligations under the contract for advertisement up formed. Under the down

10. 343 ITR 397.

11. 99 ITD 91.

linking model, given that the primary activity of displaying advertisements, broadcasting of the television channels carry on outside India, income accruing of such contracts would be said to accrue or arise outside India, and consequently not taxable under the ITA.

Similarly, taxability of advertising revenues remains disputed despite the broadcasters paying an arm's length remuneration to their Indian Associated Enterprises ("AE"), which act as agents for advertising sales. The position on attributability of profits in the event of arms' length compensation, has been settled by several rulings, most significantly in *Set Satellite (Singapore) Pte. Ltd.*<sup>12</sup>, *BBC Worldwide v. DCIT*<sup>13</sup>, and the Mumbai Tribunal in *B4U International Holdings v. Department of Income Tax*.<sup>14</sup> However, at the levels of lower authorities, there seems to be a persistent attempt to attribute profits of the non-resident to a permanent establishment ("PE") even on arms' length compensation.

The disallowance of advertising sales and promotion expenditure incurred by the Indian Associated Enterprises of foreign broadcasting companies has raised several concerns. While it is contended that such expenditure is purely business expenditure and consequently should be allowed as a deduction, the tax authorities deny the deductibility of such expenses on the ground that such expenditure is primarily incurred for the benefit of the foreign broadcasting company, and therefore such companies ought to bear it. On this position, the Bombay High Court recently ruled in favour of allowing expenditure; However the matter has been appealed by the authorities in the Supreme Court and is therefore *sub judice*.

The controversy also arises on the question of whether tax should be withheld on the payments made to the entities as agency

commission by broadcasters on advertising agencies, or as royalty payments, with broadcasting companies and tax authorities differing on this point. Resultantly, the non-withholding or short-withholding of taxes has led to huge tax burdens on the broadcasting companies.

## IX. The Way Forward

Industry-wide issues such as those faced by the broadcasting sector are typically resolved by binding judicial precedent. However, since most of the issues in this sector have emerged only recently in the past few years, the law has not yet been settled by higher courts and tribunals. In the absence of judicial precedent, the parliament, by way of a law and the Central Board of Direct Taxes, by way of notification under section 295 of the ITA, have the power to clarify the legal position in this regard. Pending the resolution of such issues, there is bound to be significant litigation around disputes with the tax authorities.

It is also noticed that the tax environment governing the broadcasting sector in India is contrary to international practices. This increasing attempt by the authorities to tax payments made to foreign broadcasters de hors application of the principle of territoriality of tax laws has led to creating an environment that dis-incentivizes foreign companies from doing business in India. In this regard, it is of utmost importance for policy makers and the government to take quick and adequate steps to clear the ambiguities in the emerging tax framework and ensure that laws are tailored to facilitate growth and not stifle it.

12. 307 ITR 205.

13. 203 Taxman 554.

14. 18 ITR 62.

The following research papers and much more are available on our Knowledge Site: [www.nishithdesai.com](http://www.nishithdesai.com)

	<b>Fund Structuring and Operations</b>		<b>E-Commerce in India</b>		<b>The Curious Case of the Indian Gaming Laws</b>
	July 2016		July 2015		September 2015
	<b>Corporate Social Responsibility &amp; Social Business Models in India</b>		<b>Joint-Ventures in India</b>		<b>Outbound Acquisitions by India-Inc</b>
	March 2016		November 2014		September 2014
	<b>Internet of Things</b>		<b>Doing Business in India</b>		<b>Private Equity and Private Debt Investments in India</b>
	April 2016		June 2016		June 2015

## NDA Insights

TITLE	TYPE	DATE
ING Vysya - Kotak Bank : Rising M&As in Banking Sector	M&A Lab	January 2016
Cairn – Vedanta : ‘Fair’ or Socializing Vedanta’s Debt?	M&A Lab	January 2016
Reliance – Pipavav : Anil Ambani scoops Pipavav Defence	M&A Lab	January 2016
Sun Pharma – Ranbaxy: A Panacea for Ranbaxy’s ills?	M&A Lab	January 2015
Reliance – Network18: Reliance tunes into Network18!	M&A Lab	January 2015
Thomas Cook – Sterling Holiday: Let’s Holiday Together!	M&A Lab	January 2015
Jet Etihad Jet Gets a Co-Pilot	M&A Lab	May 2014
Apollo’s Bumpy Ride in Pursuit of Cooper	M&A Lab	May 2014
Diageo-USL- ‘King of Good Times; Hands over Crown Jewel to Diageo	M&A Lab	May 2014
Copyright Amendment Bill 2012 receives Indian Parliament’s assent	IP Lab	September 2013
Public M&A’s in India: Takeover Code Dissected	M&A Lab	August 2013
File Foreign Application Prosecution History With Indian Patent Office	IP Lab	April 2013
Warburg - Future Capital - Deal Dissected	M&A Lab	January 2013
Real Financing - Onshore and Offshore Debt Funding Realty in India	Realty Check	May 2012
Pharma Patent Case Study	IP Lab	March 2012
Patni plays to iGate’s tunes	M&A Lab	January 2012
Vedanta Acquires Control Over Cairn India	M&A Lab	January 2012

## Research @ NDA

**Research is the DNA of NDA.** In early 1980s, our firm emerged from an extensive, and then pioneering, research by Nishith M. Desai on the taxation of cross-border transactions. The research book written by him provided the foundation for our international tax practice. Since then, we have relied upon research to be the cornerstone of our practice development. Today, research is fully ingrained in the firm's culture.

Research has offered us the way to create thought leadership in various areas of law and public policy. Through research, we discover new thinking, approaches, skills, reflections on jurisprudence, and ultimately deliver superior value to our clients.

Over the years, we have produced some outstanding research papers, reports and articles. Almost on a daily basis, we analyze and offer our perspective on latest legal developments through our "*Hotlines*". These *Hotlines* provide immediate awareness and quick reference, and have been eagerly received. We also provide expanded commentary on issues through detailed articles for publication in newspapers and periodicals for dissemination to wider audience. Our *NDA Insights* dissect and analyze a published, distinctive legal transaction using multiple lenses and offer various perspectives, including some even overlooked by the executors of the transaction. We regularly write extensive research papers and disseminate them through our website. Although we invest heavily in terms of associates' time and expenses in our research activities, we are happy to provide unlimited access to our research to our clients and the community for greater good.

Our research has also contributed to public policy discourse, helped state and central governments in drafting statutes, and provided regulators with a much needed comparative base for rule making. Our *ThinkTank* discourses on Taxation of eCommerce, Arbitration, and Direct Tax Code have been widely acknowledged.

As we continue to grow through our research-based approach, we are now in the second phase of establishing a four-acre, state-of-the-art research center, just a 45-minute ferry ride from Mumbai but in the middle of verdant hills of reclusive Alibaug-Raigadh district. The center will become the hub for research activities involving our own associates as well as legal and tax researchers from world over. It will also provide the platform to internationally renowned professionals to share their expertise and experience with our associates and select clients.

We would love to hear from you about any suggestions you may have on our research reports. Please feel free to contact us at [research@nishithdesai.com](mailto:research@nishithdesai.com)

# Nishith Desai Associates

LEGAL AND TAX COUNSELING WORLDWIDE

## MUMBAI

93 B, Mittal Court, Nariman Point,  
Mumbai 400 021 India

Tel: +91 - 22 - 6669 5000

Fax: +91 - 22 - 6669 5001

## SILICON VALLEY

220 S California Ave., Suite 201,  
Palo Alto, CA 94306, USA

Tel: +1 - 650 - 325 7100

Fax: +1 - 650 - 325 7300

## BANGALORE

Prestige Loka, G01, 7/1 Brunton Rd,  
Bangalore 560 025, India

Tel: +91 - 80 - 6693 5000

Fax: +91 - 80 - 6693 5001

## SINGAPORE

Level 30, Six Battery Road,  
Singapore 049909

Tel: +65 - 6550 9855

Fax: +65 - 6550 9856

## MUMBAI BKC

3, North Avenue, Maker Maxity  
Bandra - Kurla Complex,  
Mumbai 400 051, India

Tel: +91 - 22 - 6159 5000

Fax: +91 - 22 - 6159 5001

## NEW DELHI

C-5, Defence Colony  
New Delhi - 110024, India

Tel: +91 - 11 - 4906 5000

Fax: +91 - 11 - 4906 5001

## MUNICH

Maximilianstraße 13  
80539 Munich, Germany

Tel: +49 - 89 - 203006 - 268

Fax: +49 - 89 - 203006 - 450