

SATURDAY INTERNATIONAL TAX GYAN !!!

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Soktas Tekstil Sanayi Ve Ticaret AS

vs.

ACIT(International Taxation) Circle-3(1)(2)

SITG. NO.
134

HAPPY
NEW
YEAR

Consideration received on transfer of trademark and brand name can be treated as royalty under Article 12 of India - Turkey DTAA, instead of capital gains under Article 13 of the DTAA.

[2022] 145 taxmann.com 521 (Delhi - Trib.)[22-12-2022]

Date: 31.12.2022

Facts of the Case

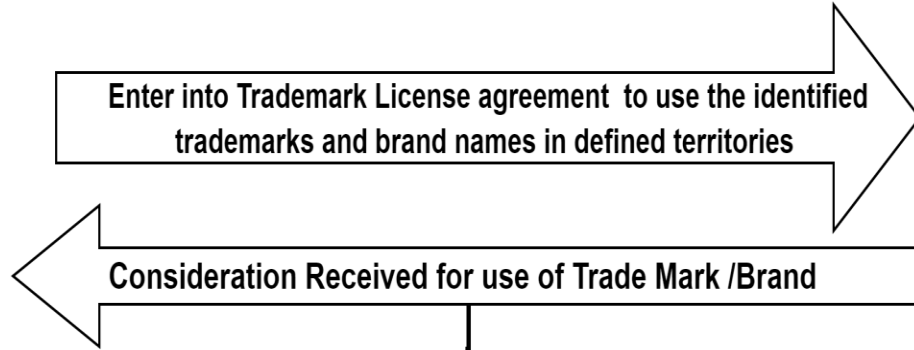
- ❖ The assessee is a non-resident corporate entity incorporated in Turkey and a tax resident of Turkey and has specialisation in designing and producing cotton and cotton fabric, which is exported around the world. The assessee had a wholly owned subsidiary Suktas India Pvt. Ltd.
- ❖ The assessee had entered into Trademark License Agreement (TLA) with the Indian subsidiary **transferring exclusive, irrevocable and perpetual rights to use the identified trademarks and brand names in defined territories**. The transfer of such right to use to the Indian subsidiary was for a lumpsum consideration.

Facts

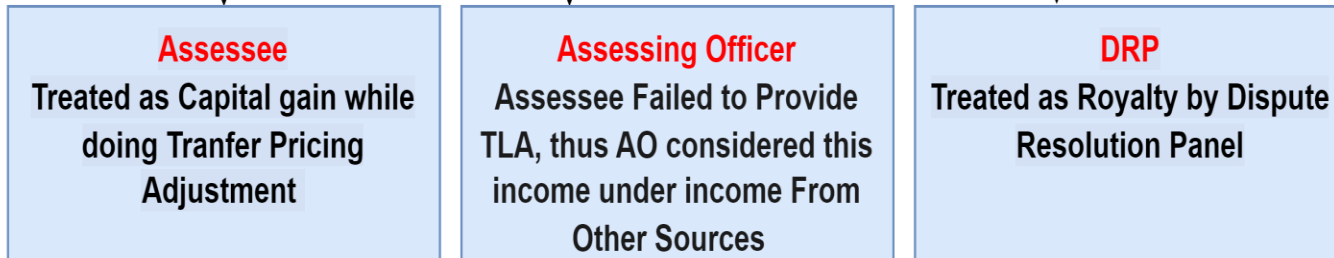


Turkish based Entity
(Assessee)

Taxinpic



Soktas Tekstil Sanayi
(Wholly Owned Subsidiary)



Assessee's Contention

- ❖ The assessee being of the view that the consideration received from transferring the right to use the trademarks and brand-names, whether is at arm's length or not, undertook a suo motu transfer pricing adjustment based on an independent valuation report and offered the adjusted **sale consideration as capital gain** in the return of income filed for the relevant assessment year.
- ❖ Further assessee contended that it has transferred an asset and thus taking **shelter under Article 13 of India - Turkey DTAA**, the assessee **claimed exemption** of the capital gain from taxation in India, as the Article 13 of the DTAA states that **Gains from the alienation of any property** other than that referred to in paragraphs 1 to 5 of Article 13 India Turkey DTAA shall be taxable in the Contracting State of which the alienator is a resident. Thereby the consideration received shall be taxed as capital gain in the Turkey .

Revenue Contention

- ❖ The Assessing Officer while drafting Assessment order was of the view that the **income derived from transfer of right to use of trademark/brand name** is to be treated as **income from other sources under Article 21 of the Tax Treaty** alleging that the assessee did not furnish the requisite documents to support its claim of exemption on capital gain

Dispute Resolution Panel (DRP) Observation

- ❖ DRP accepted that the assessee has furnished the requisite documentary evidences, including, TLA before the Assessing Officer. Thus, **learned DRP did not agree with the decision of the Assessing Officer that the consideration received under the TLA is to be treated as income from other sources.**
- ❖ Further Learned DRP was of the view that the assessee had not parted its ownership rights over the trademark and brand-names while entering into the TLA with the Indian subsidiary as through the TLA, the assessee granted an exclusive, perpetual and irrevocable license to the Indian subsidiary for creation of brand-name/trademark so **where ownership right has not been alienated, the consideration is for the use of or the right to use the trademark, hence, represents royalty.**
- ❖ Furthermore Learned DRP observed, that the terms and conditions of TLA clearly make out that the payment is not in consideration for the transfer of **full** ownership rights on trademark/brand name but is the consideration for rights to use of brand-name/trademark, thus, partakes the character of royalty and not capital gain as **relinquishment or extinguishment of any rights in capital asset amounts to transfer attracts capital gain..**

Legal Provision - Income Tax Provisions

- ❖ **As per Sec.9(1)(vi) of the Income Tax Act 1961:** Royalty means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for—
 - ❖ (i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property ;
 - ❖ (ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;
 - ❖ (iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;
 - ❖ (iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill ;
 - ❖ (iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;
 - ❖ (v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting ; or
 - ❖ (vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v).

India-DTAA Provisions

❖ Article 12 of India - Turkey DTAA :

- ❖ Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
- ❖ However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the recipient is the beneficial owner of the royalties the tax so charged shall not exceed 15 per cent of the gross amount of the royalties or fees for technical services
- ❖ The term "**royalties**" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films or films or tapes used for radio or television broadcasting, **any patent, trade mark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial, or scientific experiment.**

Ruling

- ❖ It was held that the assessee **has not sold, exchanged or relinquished or extinguished its rights** either wholly or partially with reference to the trademarks/brand names. Therefore it will not amount to capital gain as **Article 13 of the Tax Treaty, which provides for taxation of capital gains, speaks of alienation of any property** and in the present appeal **the assessee has not alienated its ownership rights over the brand names** and trademarks, either fully or partially but has **simply permitted the licensee the right to use of brand name and trademark** in a particular geographical territory.
- ❖ Further, it was held that with respect of Terms of TLA, the assessee has received the consideration for the use of or the right to use of trademark/brand names. **The consideration received by the assessee for permitting the right to use of brand name/trademark under TLA is nothing else but in the nature of royalties as defined under section 9(1)(vi) read with Article 12(3) of India - Turkey tax treaty.**

Our Comments

- ❖ There should be clear demarcation between license and assignment in order to assess taxability as royalty and Capital gain.
- ❖ Few important factor to examine whether it is license or assignment are-
 - i. whether the user acknowledges the licensor's right and title over the trademark.**
 - ii. whether it is a mere right to use the trademark or it was a transfer/assignment of a permanent nature.**
 - iii. Further, whether the mode and manner of use is specified and restricted and the effect thereof on the rights of the user.**
 - iv. And last whether an exclusive license which excludes the owner from using the trademark and vests perpetual rights without any termination clause could constitute an assignment.**
- ❖ Thus in present case it was a clear indication of license conferring right to use the trademark/brand name and not assignment/transfer of brand name/trademark in favor of the licensee. Therefore the consideration arising on transferring such use of license would constitute royalty.
- ❖ Note : While entering into any agreement it is very important to bifurcate that the transaction is related to usage of any right or relinquishment of rights because on the basis of this the taxability will arise either under royalty or capital gain or any other head.

Court	ITAT Delhi
Date of decision	22.12.2022
Section/Article	Section 9(1)(vi) of the Act read with Article 12 of the tax treaty
DTAA/Country	India, Turkey

Note: Case law name in **Red**- in favour of the revenue, **Green**-In favour of the Assessee, **Orange** = Partial



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Wishing you all a very happy
and prosperous new year

