

Saturday  
International  
Tax  
Gyaan

SITG

# SATURDAY INTERNATIONAL TAX GYAN !!!

## #taxmadeeasy

SITG No.

191

### New series – International Business Transactions!!

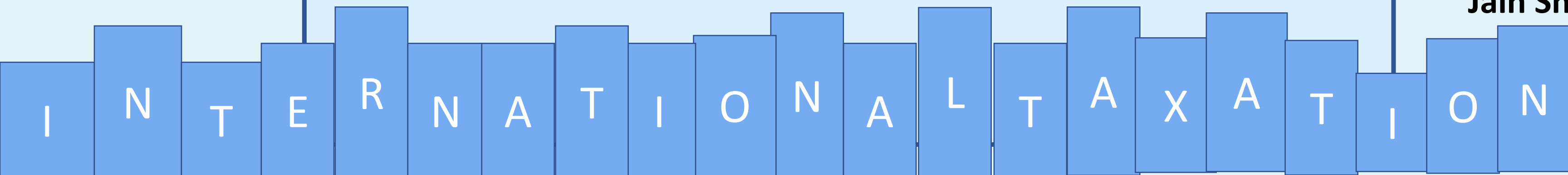
PART-V

### #Nature of transaction

### Repair, Maintenance & its related services

03.02.2024

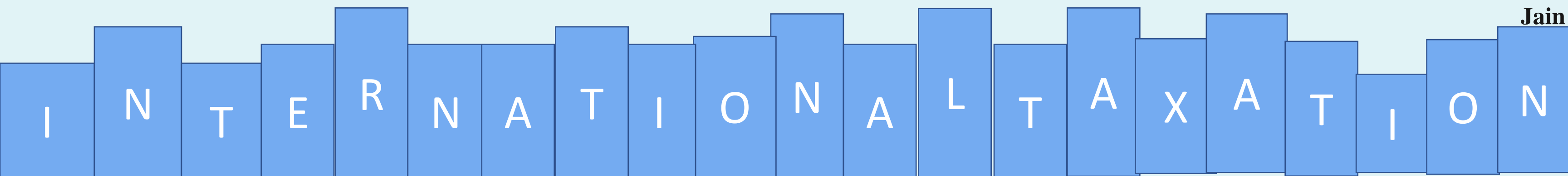
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# Concept and definition

## What shall constitute Repairs and maintenance services?

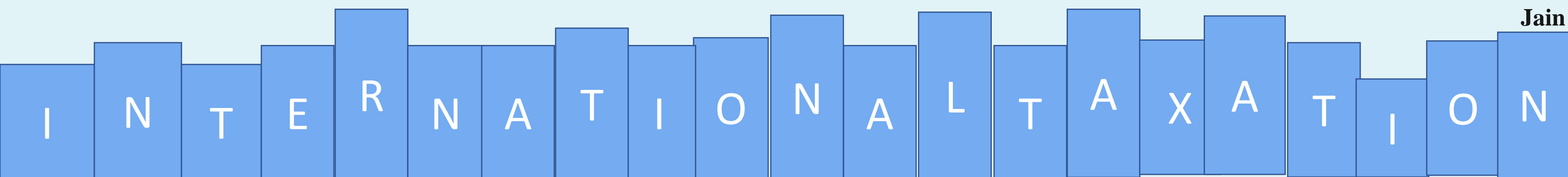
- The repairs of a physical asset may be routine repair services or may involve technical skill. It is normally done in case of asset break down, damage, regular maintenance or if the asset stops working.
- Similarly software maintenance is a continuous process of modifying or updating a software system after the product is delivered to the customer.
- Several key aspects of hardware as well as software maintenance are Bug Fixing, Enhancements, Performance Optimization, Porting and Migration, Re-engineering, and documentation.



# Repairs and maintenance treatment

## Workflow to treat repairs and maintenance of software for tax purpose?

- The question here is to consider that whether the receipts arising from the agreement for maintenance service would fall under the ambit of 'fees for included/ technical services', 'Royalty' or shall form part of 'Business Profits'.
- There are various questions which needs to be answered while determining the taxability of a service such as repair and maintenance.
  - Whether there is transfer of any right in relation to patent, trademark etc or copyright or any secret formula etc. (To Test royalty)
  - Whether there is any technical knowledge required while providing such service. (To Test FTS)
  - Is the knowledge made available where providing such service of repair and maintenance. (To Test FTS)
  - Does the service provider have any PE in India. (To test business income)



# Determining the taxability as per the act

- **Income Tax Act:** Although the service of repair of software could be an auxiliary service to software which is covered under Royalty. However, repair of such software could not itself fall under royalty as it is not a transfer of a copyright or trademark etc.
- Hence, we need to check **Explanation 2 to section 9(1)(vii)** of the act defines the scope of FTS, which includes the **consideration received for rendering of any managerial, technical, or consultancy services** but does not include consideration received for construction, assembly or mining or like projects undertaken by the recipient or income received chargeable to tax under the head “salaries”.
- Therefore, referring to the meaning and nature in the earlier slide and above, for services which are considered technical in nature while repairing machinery, we can safely assume that **it shall come under the ambit of ‘FTS’ since such services might be either a part of technical service or consultancy service**. However, if it is proved that repair service does not require any technical knowledge then it would not fall under FTS.
- Although the terms ‘managerial’, ‘technical’, and ‘consultancy’ is not defined in the income tax law. The Hon’ble courts in various case laws have defined such terms in various cases like-
  - i. **[2012] 26 taxmann.com 267 (Bom) Zuari Agro Chemicals Ltd. v. CIT**
  - ii. **[2013] 378 ITR 205 (Delhi) CIT v. Grup Ism (P) Ltd.**

Since the services involving an element of ‘managerial’ (as discussed in the earlier slide) are taxable as per the provisions of income tax act. Now, therefore we shall test the taxability as per the provisions of DTAA.

# Case Laws where repair services-

## Qualify as FTS

- Lufthansa Cargo India Pvt. Ltd. (2004) 91 ITD 133 (Delhi ITAT)

## Do not qualify as FTS

- CIT(TDS) v. Mumbai Metropolitan Regional Development Authority [2018] 97 taxmann.com 461 (Bom HC)
- DCIT- (TDS) v. M/s SBI Life Insurance Company Ltd. No.- ITA No. 2398/ Mum/ 2017
- HCL Comnet Ltd. [TS-456-ITAT-2016(DEL)]
- Ad. DIT v. BHEL-GE-Gas Turbine Servicing P Ltd [2012] 24 taxmann.com 25 (Hyderabad)
- Kandla Port Trust v. DCIT (2011) 16 taxmann.com 273 (Rajkot- Trib.)
- Hero MotoCorp Ltd. v. Ad CIT (2013) 7 TaxCorp (A.T.) 33215 (Delhi)

# Determining the taxability as per DTAA

## ■ As per DTAA:

- As per DTAA, generally 'FTS' means payment of any kind to any person in consideration for the rendering of any managerial, technical or consultancy services (including through the provision of services of technical or other personnel).
- However, one should need to read the respective DTAA before applying the provisions of it because every DTAA has different nuances in FTS article, which vary agreement to agreement and therefore creates a huge impact on the transaction between countries.
- Generally in repair service the knowledge is not made available and many repair service or updation service does not require technical knowledge hence we need to check whether the nature of service received by the service recipient is in nature of technical or is knowledge made available?
- If the service does not fall under FTS and if company is engaged in the same business then we need to check whether the service provider has Permanent establishment in India or whether the employees of such company visited India to provide such repair service which led to creation of PE in India.

Further with regards to understand the taxability as per DTAA for such transactions, we shall try to understand the flow of taxability with the help of a flowchart which is shared in the next slide.



# Comments

- There is no fixed template that helps you decide that whether the repair or maintenance service shall fall under the scope of FTS or shall be treated as 'Business Profits' or under any other head. Therefore a lot more depends upon the nature of such repair or maintenance service rendered.
- For example, if there are minor repairs, cleaning of aircrafts, routine repairs, updating software or even if there is an Annual Maintenance Contract (AMC), it shall not be treated as FTS if it is proven that this does not require technical skill, whereas services relating to component overhauling, machine maintenance involves technical expertise, and hence it shall be treated as FTS. However, there might be few situations where such services can even lead to non-technical services and hence outside the purview of FTS.
- Further, in various DTAA's it is mentioned that services ancillary to the royalty service will fall under FTS and repair and maintenance being ancillary could fall under FTS irrespective of whether it is technical or not however, for that we need to be first sure that software would fall under Royalty. If not then it's ancillary service would also not fall under FTS.
- The place where such services are rendered also plays an important part in deciding whether it shall come under the FTS or Business Income. If in case the services of maintenance of software is provided virtually, or if the machine has been sent to abroad for repairs or maintenance, then in such case there shall be no PE, hence it might escape the provisions of Business Income as well. However, this hypothesis shall work only when the assessee is sure that no such service of repairs or maintenance shall be covered under the ambit of 'FTS'

# Reference of previous SITGs of International Business Transactions

<b>S. No.</b>	<b>Services offered</b>	<b>Link</b>
Part- I	Project Review, Feasibility Study, and its Report	<a href="#"><u>Click Here</u></a>
Part- II	Survey and related services	<a href="#"><u>Click Here</u></a>
Part- III	Reimbursement of International transactions	<a href="#"><u>Click Here</u></a>
Part- IV	Managerial service	<a href="#"><u>Click Here</u></a>





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