Sum paid as 'affiliation fee' not connected with transfer of technology couldn't be treated as royalty

Summary – The Hyderabad ITAT in a recent case of Customer Lab Solutions (P.) Ltd., (the Assessee) held that Affiliation fee, a one time payment by assessee to US. company, which did not provide for transfer of technology, was not royalty

Facts

- The assessee entered into an agreement with US company for the purpose of its consultancy business and, accordingly, paid a sum as fee.
- The Assessing Officer held the fee paid as royalty within the meaning of clause (*vi*)(*b*) of sub-section (1) of section 9 and disallowed the amount under section 40(*a*)(*i*) on the ground that no TDS had been deducted.
- Before the Commissioner (Appeals), it was contended by assessee that the amount paid by the assessee to US company was affiliate fee and amount was not in connection with use of any right to use any material or service provided by the non-resident. As there was no income accruing in India.
- The Commissioner (Appeals), however, after detailed discussion held that the payment was in nature of royalty under the Income-tax Act and DTAA as well.

Held

- The agreement dated 31-03-2005 between the assessee and US company, specifies various terms and conditions and the relationship, vision philosophy which Commissioner (Appeals) has painstakingly considered and extracted in the order to indicate that there is arrangement for use of technical knowledge. However, as seen from the agreement itself, there are two types of payments. The affiliation fee is one-time payment which does not provide for transfer of any technology. On signing the agreement, the affiliate shall play an affiliate fee of US $ 35,000. This fee being annual fee is subject to increase or decrease on changing economic conditions. The annual fee does not provide for any transfer of technology. However, there is further fee to be paid "Fees on consulting and reports" in the agreement. This fee will be paid based on the performance, targets achieved by assessee in consulting technology, tools etc. What assessee has paid and claimed was only an affiliation fee and not the fee on consulting and reports. The payment of affiliation fee does not involve any transfer of technical knowledge or use of technical knowledge.
- As seen from the paper book placed on record, what assessee got is in the form of two magazines which are published by the Harvard Business School with a title 'Balanced Scorecard Report'. This magazine, short of management jargon, is nothing but a periodical magazine with various write- ups, which cannot be considered as a right to use a copy right. Assessee being management consultant, the agreement with M/s. Balanced Scorecard Collaborative inc. of USA, had this high sounding

© 2018, Tenet Tax & Legal Private Limited

management terminology, but put it simply, assessee has paid only the affiliation fee and not a fee for consultation or for technical knowledge. Since there is no transfer of technical know-how or technical knowledge or use of technical knowledge, the definition 'royalty' either under IT Act or under the DTAA does not apply to the present payment of affiliation fee. Since U.S. company does not have any PE in India, the payment itself *per se* does not attract any TDS provisions.

- Since the payment of affiliation fee alone does not result in either providing any technical service or use of technical knowledge, both the Assessing Officer and CIT (A) have erred in considering the fee as in the nature of royalty. Since there is no transfer of technology or use of any technology and payment is only simply for affiliation, the above amount cannot be considered as 'royalty' either under the provisions of Income Tax Act or under the provisions of DTAA.

© 2018, Tenet Tax & Legal Private Limited