Film Financing and Television Programming

A Taxation Guide

For more than a decade, the KPMG Film Financing and Television Programming Taxation Guide has been recognized as a valued reference tool for industry professionals, filled with information drawn from the knowledge of the KPMG International global network of member firm media and entertainment Tax professionals. The 2022 edition is a fundamental resource for film and television producers, studio and streaming production executives, tax executives, finance executives, and attorneys involved with the commercial side of production.

Doing business across borders can pose major challenges and may lead to potentially significant tax implications, and a detailed understanding of the full range of potential tax implications can be as essential as the actual financing of a project. The Guide helps industry executives assess the many issues surrounding cross-border business conditions, financing structures, and issues associated with them, including development costs and rules around foreign investment. Recognizing the role that tax credits, subsidies, and other government incentives play in production financing, the Guide includes a robust discussion of relevant tax incentive programs in each country.

Each chapter focuses on a single country and provides a description of commonly used financing structures, as well as their potential commercial and tax implications for the parties involved. Key sections in each chapter include:

Introduction
A thumbnail description of the country's industry contacts, regulatory bodies, and financing developments and trends.

Key Tax Facts
At-a-glance tables of corporate, personal, and value-added (VAT) tax rates; normal nontreaty withholding tax rates; and tax year-end information for companies and individuals.

Financing Structures
Descriptions of commonly used financing structures in production and distribution, and the potential commercial tax implications for the parties involved. This section of each chapter covers rules surrounding co-productions, partnerships, equity tracking shares, sales and leaseback, subsidiaries, and other tax-efficient structures.

Tax and Financial Incentives
Details regarding the tax and financial incentives available from central and local governments as they apply to investors, producers, distributors, and actors, as well as other types of incentives offered.

India

Corporate Tax
Explanations of the corporate tax in the country, including definitions, rates, and how they are applied.

Personal Tax
Personal tax rules from the perspective of investors, producers, distributors, artists, and employees.

Streaming Tax Considerations
Provides a look at the unique tax issues that need to be addressed in this evolving segment of the industry. With considerations such as identifying tax collection and reporting obligations in a variety of jurisdictions, understanding international tax implications is essential for streaming providers.

KPMG and Member Firm Contacts
References to KPMG and other KPMG International member firms' contacts at the end of each chapter are provided as a resource for additional detailed information.

Please note: While every effort has been made to provide up-to-date information, tax laws around the world are constantly changing. Accordingly, the material contained in this publication should be viewed as a general guide only and should not be relied upon without consulting your KPMG or KPMG International member firm Tax advisor.

Production opportunities are not limited to the countries contained in this Guide. KPMG and the other KPMG International member firms are in the business of identifying early-stage emerging trends to assist clients in navigating new business opportunities. We encourage you to consult a KPMG or KPMG International member firm Tax professional to continue the conversation about potential approaches to critical tax and business issues facing the media and entertainment industry.

We look forward to helping you with your film and television production ambitions.

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India

India

Introduction

The Indian Film industry is known to be one of the world's largest film producers; being diverse in languages, including Hindi (the national language) and regional languages (Marathi, Gujrati, South Indian languages, and many more).The industry is always buzzing with new releases, increasing number of viewers and record-breaking box office collections.

Overall, the film industry was projected to grow at a fast pace. However, the COVID-19 pandemic has hit the pause button on the growth of Indian film industry. During most of FY21, there have been no theatrical releases due to closure of theatres. The emergence of a new distribution avenue for films on the digitals and the over the top (OTT) platforms provided some respite to a few films waiting for a release when the pandemic struck, and what followed was a spurt in digital/OTT releases.

While the film industry has suffered deep cuts in FY21, the revenues are projected to grow by 196% in FY22 over FY21, considering the low base.[1] The film industry will be reimagined, and the industry players will find newer ways to draw audiences to theatres.

Indian Cinema could see a momentous shift with optimal budgets and new models of production process with producers joining hands with the actors to co-produce films for decreasing talent cost and working capital requirements, increasing use of technology and OTTs emerging as a medium for movie releases. Box office collections are crucial for producers of big budget films to achieve profitability and hence, most big-budget films are unlikely to go for a digital-first release. In the long-term, small budget projects will resort to OTT releases.

The industry has restarted its activities, and big budget films are awaiting their release in cinema halls. Innovative approaches are already being adopted in shooting of films and television programs. We will have to see how effectively and quickly the industry comes out of the obstacles laid down by the pandemic.

Key Tax Facts

Corporate income tax rate: Domestic companies	22%/25%/30%[2]
Minimum Alternate Tax: Domestic companies	15%[3]
Corporate income tax rate: Foreign companies	40%
Maximum Marginal personal income tax rate	30%
Partnership including Limited Liability Partnership	30%
Alternate minimum tax (other than company)	18.5%

[1] KPMG in India's Media and Entertainment report 2020.
[2] Corporate tax at reduced rate of 25% is applicable to companies whose turnover or the gross receipts in the financial year 2018-19 does not exceed INR 4,000 million. Further, Finance Act, 2020 provides an option to domestic companies to avail benefit of lower corporate tax rate of 22%, subject to certain conditions.
[3] Finance Act, 2020 has reduced the rate of Minimum Alternate Tax from 18.5% to 15%. Further, the provisions of Minimum Alternate Tax regime shall not be applicable to companies opting for lower corporate tax of 22%.

Withholding tax rates[4] on non-residents/foreign companies:	
Dividends[5]	20%
Royalties	10%
Fees for technical services	10%
Capital gains (on sale of shares):	
Long-term capital gain on listed shares (where shares are held for more than 12 months)	Refer to note below[6]
Long-term capital gain on unlisted shares (where shares are held for more than 24 months)	10% (in the case of non-resident)
Short-term capital gain on listed shares (where shares are held for less than 12 months)	15%
Short-term capital gain on unlisted shares (where shares are held for less than 24 months)	40% (in the case of non-resident)
Indirect tax[7]	
Goods and Services Tax	Slab rate of 0%, 5%, 12%, 18%and 28%
Tax year-end: Companies and Individuals	March 31

The above rates share be increased by applicable surcharge and cess.

Film Financing

Financing Structures

Under the extant Indian tax laws, taxable entities that engage in film production and distribution, *inter alia*, include:

- Individuals[8]
- Associations of Persons
- Limited Companies
- Partnerships
- Limited Liability Partnerships.

[4] These rates are as per the Income-tax Act, 1961 (Indian tax law). In case of a non-resident, there is an option to choose between the rate as per the Double Taxation Avoidance Agreement and the Indian tax law, whichever is more beneficial.
[5] Dividend Distribution Tax ('DDT') is abolished vide Finance Act 2020. The dividends distributed by domestic companies are taxable in the hands of the recipient shareholder.
[6] Until financial year 2017–18, no capital gain was levied on a sale of equity shares listed on a recognized stock exchange in India and on which Securities Transaction Tax (STT) was paid. However, as per the Finance Act 0f 2018, long-term capital gains exceeding INR 0.1 million arising from the transfer of equity shares, unit of equity-oriented fund or unit of business trust wherein STT has been paid on acquisition and transfer of such capital asset, shall be taxed at the rate of 10% without indexation (plus applicable surcharge and cess, if any).
[7] The new GST law (subsuming a number of indirect taxes like VAT, Excise Duty, Customs, Service Tax, etc.) became effective on July 1, 2017. Hence, the prevailing rates in the former regime have been re-visited post the enactment of GST law.
[8] Taxability of individuals is discussed later in the chapter under the section titled "Personal Taxation."

Association of Persons (AOP)

AOP is an unincorporated body and the rights of its members are governed by the agreement. All AOP members are taxed as a single entity, i.e., as an AOP. An AOP can result in joint and several liabilities with an unintended exposure of each party to the tax liability of other members of the AOP. When a member has incurred losses from his part of the activity, he may still be liable for taxes, given that the combined profits and losses of all members are considered in one assessment of the AOP. Further, there may be the inability to offset losses or expenses incurred by the members independently against their share of the AOP profit. The income so assessed is liable to be taxed at the maximum marginal rate i.e., 30% (plus applicable surcharge and cess) or taxed at a higher rate, applicable to the member of the AOP. To avoid AOP status, members are required to carefully plan the production and exhibition/distribution rights arrangements. This is required particularly to ensure that the respective rights, obligations, scope of work, and income of each party are clearly defined and demarcated. Further, once the AOP is set up, there could be potential practical challenges in meeting day-to-day compliance requirements under the Indian tax laws, i.e., in payment and withholding of taxes, filing of an income-tax return, etc.

Limited Company

A limited company is considered an entity separate from its shareholders and is taxed as a separate entity. Pursuant to the amendment vide in the Finance Act 2020, Dividend Distribution Tax (DDT) has been abolished, and dividend distributions from a domestic Indian company are now taxed in the hands of recipient shareholders. The company's liability is limited to its paid-up share capital, and the shareholders are not personally liable for losses and debts of the company.

Partnership Firm (firm)

Under Indian tax law, a partnership firm is assessed as a separate entity. A firm cannot have limited liability; the liability of all partners is joint and several. The partner's share in the firm's income is not included while computing his total income. Salary, bonus, commission, and interest payments due to or received by each partner are allowed as a deduction to the firm, subject to certain restrictions. Such payments to partners are taxed as business profits in their hands.

Limited Liability Partnership (LLP)

LLP combines the benefits of limited liability of a company and the flexibility of a general partnership firm, resulting in less onerous compliances and limited disclosure requirements. The corporate nature of LLP and the mode of functioning make it a unique structure.

In terms of Indian tax law, the provisions applicable to a partnership firm have also been extended to LLP.

Unlike LLPs in several other countries, Indian LLPs do not enjoy pass-through status. Accordingly, when a foreign partner receives his/her share of profits from an Indian LLP (which would be subject to tax in India in the hands of the LLP), claiming a tax credit in his home country may pose a problem in the absence of express provisions in the tax treaty(ies). Further, distribution of profits by LLP to its partners is not taxable in the hands of the partners.

LLP may be explored as a form of doing business when undertaking co-production activities in India, as discussed below.

Foreign Investment in Indian LLPs

While the government allowed foreign direct investment (FDI) in LLPs in 2011,[9] these changes were not simultaneously incorporated under the 1999 Foreign Exchange Management Act (FEMA)[10], leading to uncertainty among foreign investors in setting up LLPs in India. The Reserve Bank of India (RBI)[11] has incorporated the provisions related to FDI in LLP in FEMA.

FDI in LLP has been allowed in a calibrated manner in sectors where 100% FDI is allowed under the automatic route, i.e., where no prior approval is required and there are no FDI-linked performance conditions. Further, conversion of a company having FDI to an LLP is permissible under automatic route subject to the condition that the company having FDI is engaged in a sector where foreign investment up to 100% is permitted under automatic route and there are no FDI-linked performance conditions.[12]

Pricing of a partner's interest in an LLP should be as per internationally accepted pricing principles.

It is also pertinent to note that an Indian LLP, with foreign investment, is permitted to make downward investment in another company or LLP engaged in sectors in which 100%FDI is allowed under the automatic route and there are no FDI-linked performance conditions.[13]

The existing FDI policy permits 100% FDI under automatic route in the film sector. Therefore, as mentioned above, LLPs may be explored as another legal form of doing business in India, especially in the case of co-productions.

Other Financing Considerations

Modes of Film Financing

Producers engaged in film production in India rely essentially on the following modes of film financing:

- Self-funding
- Advances from distributors against distribution agreements
- Advances from financiers against financing agreements
- Sale of negative rights
- Sale of music rights
- Bank financing
- Venture capital investments
- Equity markets
- Corporate sponsorships and merchandising (including branded entertainment)
- Co-production.

For distribution agreements, which involve the grant of distribution rights by a producer to the distributor for a particular territory and/or period, the considerations are:

- A minimum guaranteed amount;
- A fixed percentage of commission/royalty on gross collections; and
- A combination of the above.

[9] Press Note No. 1 (2011 Series) dated May 20, 2011.
[10] The governing exchange control legislation.
[11] RBI is the apex body governing foreign exchange regulations in India.
[12] Notification no. FEMA 385/2017dated 3 March 2017 & Consolidated FDI Policy (effective from 15 October 2020).
[13] Notification no. FEMA 385/2017dated 3 March 2017 & Consolidated FDI Policy (effective from 15 October 2020).

Financing agreements involve receipt of funds by the producers in consideration of:

- Interest;
- Percentage of receipts/profits; and
- A combination of the above.

Such agreements sometimes also provide for share of losses by financiers. Additionally, film producers, distributors, and financiers can raise capital through equity and preference shares, debentures or bonds, deposits, etc.

Access to Finance etc., via Film Co-production Treaties

India has concluded 15 film co-production treaties[14] thus far. Film co-production treaties are entered into with an objective of developing the film industries of the contracting countries, promoting economic and cultural cooperation, and extending national film status to the co-produced film. National film status extends benefits to films in the respective contracting countries such as:

- Tax incentives
- Access to government funding at nominal interest rates
- Regional grants
- Publicity and marketing budgets from the government.

In India, various state governments are incentivizing filmmakers to shoot films in their respective states. The film industry acts as an important partner for state governments to promote tourism. The incentives offered by local governments include:

- **Fiscal benefits:** Tax concessions provided to all filmmakers or grants provided to subsidize production costs.
- **Film festivals and awards:** Festivals, exhibitions, etc., to honor filmmakers and events to promote film shooting in states.
- **Facilitation of shooting of films:** Single window clearances for filming at locations, assistance in travel and accommodation, etc.
- **Others:** Film cities/studios, animation films and studios, etc.

Several such co-production treaties also take within their ambit third countries, with which the respective contracting countries have entered into other similar agreements, thereby, enabling the participation of such third countries in the agreement entered into by the contracting countries. Such treaties with third countries can also be explored for benefits available in those jurisdictions.

[14] Italy, United Kingdom & Northern Ireland, Germany, Brazil, France, New Zealand, Poland, Spain, Canada, China, Bangladesh, Israel, Portugal, Republic of Korea, and Russia.

Foreign Exchange Regulations[15]

As discussed earlier, through the liberalization of the foreign exchange regulations, the Government of India has allowed 100% FDI in the Film Sector. For the purposes of FDI, film sector broadly covers film production, exhibition and distribution, including related services and products. FDI in the sector is permitted under automatic route, i.e., no prior approval is required and there are no entry-level conditions in the sector. However, investors must comply with certain post filing requirements, i.e., notifying the RBI within 30 days of the receipt of inward remittance in India, filing of certain documents within 30 days of allotment of shares, etc. Further, price of shares issued/transferred to foreign investors shall not be less than:

- **In the case of Listed companies –** Price worked out in accordance with the Securities and Exchange Board of India (SEBI) guidelines;
- **In the case of Unlisted companies –** Fair valuation of shares done by a SEBI registered merchant banker or chartered accountant as per internationally accepted pricing methodology on arm's length; and
- **Where shares are issued on a preferential allotment basis –** Price determined as per pricing guidelines in terms of SEBI guidelines or as per internationally accepted pricing methodology.

However, where foreign investors are making investments in an Indian company by way of subscription to its Memorandum of Association, such investments may be made at face value subject to their eligibility to invest under FDI scheme.

Foreign investors seeking to acquire shares of an existing Indian company (engaged in film production, exhibition, or distribution) from the resident shareholders are granted a general permission, subject to compliance with prescribed terms and conditions. This means that a prior approval of the RBI is not required.

Further, remittance of hiring charges of transponders by TV channels requires prior approval of the Ministry of Information and Broadcasting however, approval will not be required where withdrawal is made out of funds held in Resident Foreign Currency (RFC) Account or Exchange Earners' Foreign Currency (EEFC) account.

Loans and Borrowings

Borrowings in foreign currency are governed by the guidelines on External Commercial Borrowings (ECB guidelines) issued by the RBI. The revised ECB guidelines[16] stipulate that all entities eligible to receive FDI are permitted to raise ECB from eligible lenders. Considering that film/television sector is eligible to receive FDI, the entities in the sector shall be eligible to raise ECBs. However, the entities will have to comply with various ECB regulations relating to minimum tenure, eligible lender, end use, interests, and other costs, etc.

In this regard, it may be noted that for the purpose of the foreign exchange regulations, non-convertible/optionally convertible/partially convertible preference shares and debentures are considered ECB. Accordingly, these instruments would be subject to ECB regulations.

[15] The entire discussion is in respect of FDI in company; separate rules and regulations would apply vis-à-vis investment in LLP.
[16] RBI/FED/2018-19/67.

Corporate Taxation (as per Indian tax laws)

Taxability of Income in the Case of Non-residents

Non-resident Filmmakers/News Agency

The taxability of a person in India is determined based upon his/her residential status, i.e., whether such person is a resident or non-resident in India.

In the case of non-residents, the following income is taxable in India:

- Received or deemed to be received in India; and
- Accrues or arises or is deemed to accrue or arise in India.

Under existing Indian tax laws, income of non-residents arising from a business connection[17] in India is deemed to accrue or arise in India.

However, income from the following activities are not deemed to accrue or arise in India:

- Shooting of any cinematographic film in India
- Collection of news and views in India for transmission out of India for a non-resident who is engaged in the business of running a news agency or publishing newspapers, magazines, or journals.

Other Aspects

Taxability of income shall also be determined based on the manner in which the same is characterized, i.e., “royalty”, “fee for technical services (FTS),” etc.

It may be noted that earlier, the Indian tax laws specifically excluded consideration for the sale, distribution, or exhibition of cinematographic films in India from the definition of ‘”royalty.” However, the said exclusion has been deleted vide Finance Act 2020, and such considerations shall now be treated as “royalty” and taxable in the hands of the recipient. Further, such payments to residents now attracts WHT at the rate of 2%.

Transactions between Related Parties

Given the increased linkage between the Indian media players and their counterparts across the globe (coupled with the impressive growth achieved and targeted for the sector), the transactions between Indian players and their related parties overseas have increased manifold each year. Such related-party transactions come under the purview of transfer pricing (TP) regulations and require the same to be carried out at an arm’s length price. These regulations prescribe mandatory documentation which needs to be maintained annually to justify the arm’s length nature of such transactions.

The Indian tax authorities typically scrutinize TP aspects in a fairly large number of cases, and the media and entertainment industry is no exception. Key factors that need to be considered in the case of related-party transactions and analysis thereof include:

- Comprehensive function, asset and risk analysis to support methodology to determine the arm’s-length price;
- Transaction-by-transaction approach; and
- Choice of most appropriate method and selection of tested party in an economic benchmarking analysis.

[17] Business connection is akin to the concept of a permanent establishment discussed in tax treaty(ies) entered into by India with other countries.

Robust Backup Documents and Agreements

Robust analysis, comprehensive documentation, and clarity in TP policies are of paramount importance. The TP policies should be based on thorough functional and economic analysis that identifies the various functions including the value drivers, risks, and location of the company's assets. The existence of TP documentation, alongside policy and procedural documentation, typically helps in streamlining the discussions with Indian tax authorities. In addition, establishing a robust set of TP policies and guidelines could help proactively identify and effectively manage new TP exposures that are created as a result of business expansions, acquisitions, restructurings, etc. As much as it acts as a tool for risk mitigation, it also enables easy fact-finding during scrutiny by authorities, thereby highlighting the transparency maintained by the taxpayer.

Since the introduction of TP laws in India in 2001, there have been significant developments in practice, as the tax authorities in India consider TP one of the key focus areas. Given the volume of tax litigation and uncertainty arising therefrom, the multinational companies operating in India have generally considered TP as one of the most important tax exposure areas.

Considering the amount of tax litigation in this area, an Advance Pricing Agreements (APA) program was introduced in India in 2012. The APA program has provided the taxpayers with a way of attaining certainty with respect to taxation on their international transactions for a maximum of the next five years. It also provides taxpayers with an option for renewal of the APA for another term of five years, subject to prescribed conditions. The APA program has seen good success thus far with a large number of applications filed, reflecting heightened optimism from taxpayers.

Going forward, taxpayers in India should use the applicable guidelines, capture need, cost, and benefit analysis of transactions, undertake robust TP analysis backed up by contemporaneous TP documentation, and make use of programs like APA to achieve up-front certainty on complex TP issues.

Deduction of Expenditure

Film Production and Distribution Cost

There are specific rules[18] provided for under the Indian tax laws that govern the deduction of production expenses for feature films and for the acquisition of distribution rights.

As per the prescribed rules, a deduction is permitted for expenditures incurred on production of films or acquisition of distribution rights therein, either in the first year of release or over a period of two years, either based on when the copyrights/distribution rights in films are used or on the date of release of the film.

A film producer who sells the entire exhibition rights of the film is entitled to a deduction of the entire cost of production incurred in the same year in which the Censor Board certifies the film for release in India. A similar deduction is available to a film distributor for outright sale of the film distribution rights acquired. In the case of a partial sale and/or partial exhibition of film rights by the film producers/distributors, the film must be released at least 90 days before the end of the tax year to claim a full deduction of specified production costs or specified costs of acquiring distribution rights.

Where the film is not released at least 90 days before the end of the tax year, then the costs of production/acquisition costs of the film distributor, limited to the amount earned from the film, shall be allowed as a deduction in the current tax year and the remaining cost shall be allowed in the following year.

[18] Rules 9A and 9B of Income-tax Rules, 1962 (the Rules).

Where the producer does not exhibit the feature film himself or does not sell, lease, or transfer the film on a minimum guarantee basis or the distributor does not exhibit the film commercially or does not sell/lease the rights of exhibition, no deduction of the cost shall be allowed in the current tax year. The entire cost shall be allowed in the succeeding tax year(s).

The sale of rights of exhibition also includes the lease of such rights or their transfer on a minimum guarantee basis.

There are a few ambiguities surrounding the applicability of Rule 9A/9B, including whether it extends to satellite, music, home videos, and other rights in addition to theatrical rights, whether it is directory or mandatory, whether it overrides all other provisions of the Indian tax laws, e.g., whether the deduction of expenditure under Rule 9A/9B is allowable irrespective of whether it is capital or revenue in nature, whether tax has been deducted at source or not, etc., deductibility of expenses that are not covered by Rule 9A/9B, etc.

Other Expenditures

As a general rule, all expenses incurred 'wholly and exclusively' for business purposes are deductible. However, there are limits/disallowances on certain types of expenses, such as (illustrative list only):

- Expenses in the nature of interest, royalties, fees for technical service, or any other sum chargeable to tax paid to residents and non-residents on which tax has not been withheld or after withholding has not been deposited with the Government of India within the prescribed time. As per the Indian tax laws, the disallowance is limited to the extent of 30%of expenditures in relation to payments to residents. Deductions, however, will be allowed in the year in which such tax has been deposited with the government treasury subject to fulfillment of prescribed conditions;
- Corporate tax, securities transaction tax, etc.;
- Provisions in accounts for specified statutory liabilities pertaining to employees, duties, taxes, and interest on borrowings from financial institutions, not actually paid before the specified dates;
- Indirect general and administrative costs of a foreign head office in excess of 5% of taxable income (before unabsorbed depreciation, etc.); and
- Expenditures on social welfare activities[19] (Corporate Social Responsibility).

Depreciation

Depreciation is calculated with a reducing balance method on the 'block of assets.' The 'block of assets' concept requires aggregation of all assets of the same class with the same depreciation rate applied to a common block. Depreciation is allowed at varying rates on different classes of assets, subject to a maximum rate of 40%.

If in the year of purchase, an asset is used for less than 180 days, then the depreciation is allowed at half of the normal rate. In other cases, depreciation is allowed at full normal rates. In the year of sale of an asset, the sale proceeds must be deducted from the value of the 'block of assets.'

Depreciation is also allowed on intangible assets like technical know-how, patents, copyrights, goodwill, etc.

[19] The Companies Act of 2013 has made it mandatory for companies, both domestic and foreign (having presence in India), to spend 2% of their average net profits for three years on prescribed social welfare activities.

WHT on acquisition of copyright

Under the Indian tax laws, payments to an Indian resident for sale, distribution, or exhibition of cinematographic films attracts 2% WHT. Acquisition of other copyright in content (for example, music rights, etc.) attracts 10% WHT.

WHT on professional payments made in kind

In the case of Red Chillies Entertainment,[20] the assessed had gifted certain items to its business associates who had worked for a film. The Mumbai Tribunal held that the provisions of section 194J could not apply where the professional or technical fees are paid in kind. While deciding the issue, relying on certain judicial precedents of the Supreme Court and High Courts,[21] the Tribunal categorically concluded that the term "any sum" under the relevant provisions would only mean cash amount of money, and since payments are made in kind, there was no requirement to withhold tax.

Certain Specific Tax Issues

Broadcasting Industry

Taxation of transponder charges

Broadcasting companies pay transponder charges to satellite companies for transmission of their TV signals. The tax authorities contend that payments made towards transponder charges are in the nature of royalties. However, in the case of Asia Satellite Telecommunications Co. Ltd.,[22] the Delhi High Court has held that such payments do not constitute royalties and are not liable to tax in India.

Subsequently, the definition of "royalty" under the Indian tax laws was amended via the Finance Act 2012, with retrospective effect, to bring within its ambit payments made for transmission of signals by satellite.

Furthermore, the Delhi High Court[23] has held that the amended definition of royalty under Indian tax law does not extend to the definition of "royalty"' under the tax treaties and even post the amendment payments received by foreign satellite companies for lease of transponders should not be subject to tax in India under the tax treaty. Following this decision, the Calcutta High Court[24] and the Mumbai Tribunal[25] have held that transponder payments are not taxable as 'royalty' under the tax treaty.

Thus, non-resident taxpayers can contribute to avail benefit under tax treaties entered into with India to contend that such payments are not in the nature of royalty/fees for technical services under the tax treaty and hence, not liable to tax in India. Further, tribunal decisions,[26] wherein connectivity charges paid to a non-resident are held as not for royalty under the Indian tax laws, could also apply to transponder payments.

Tax Issues for Foreign Television Channels/Telecasting Companies (FTC)

The two primary sources of revenues for FTCs are income from the sale of advertising airtime on the TV channel and subscription revenues:

[20] Red Chillies Entertainment Pvt Ltd vs. ACIT-ITA No. 1577/MUM/2013 (Mumbai Tribunal).
[21] H.H. Sri Rama Verma vs. CIT (1990)187 ITR 308 (SC); CIT vs Hindustan Unilever Limited (2014) 361 ITR 1 (Karnataka HC); CIT vs. Chief Accountants Officer, Bruhat Bangalore Mahagar Palike – ITA no.94 of 2015.
[22] Asia Satellite Telecommunications Co. Ltd. [2011] 197 Taxman 263 (Delhi HC).
[23] DIT vs. New Skies Satellite BV and Shin Satellite Public Company Limited: [2016] 382 ITR 114 (Delhi HC).
[24] DITvs M/S ATN International Limited (2016):TII 41-HC-KOL-Intl (Delhi HC).
[25] M/s Taj TV Ltd. (ITA No.467A-MUM/2007,412/MUM/2008, 4176/MUM/2009, 5537/MUM/2008, 5537/MUM/2008 and 4706/MUM/2009) (Mumbai Tribunal) and United Home Entertainment P. Ltd. (ITA No. 5171 to 5181/MUM/2013) (Mumbai Tribunal).
[26] Geo Connect Ltd (ITA Nos. 1927/Del/2008 & 127/Del/2011) (Delhi Tribunal); Atos Information Technology HK Ltd. 2017(ITA Nos. 237 to 240/MUM/2016) [Mumbai Tribunal]; Bharti Airtel Limited vs Income-tax officer (TDS) [2016] (67 taxmann.com 223) [Delhi Tribunal].

Taxation of Advertisement Revenues

Under Indian tax law, advertisement revenue of FTCs is taxable in India, when FTCs have a 'business connection' to India. When an FTC operates from a country with which India has a tax treaty, the advertisement revenues would be taxable in India only if the FTC has a PE in India. The taxability in such cases is only on the income that is attributable to the PE/operations carried out in India. The circumstances in which the FTCs constitute a PE/business connection in India and the determination of income attributable to such PE/operations carried out in India continue to be a contentious issue between the FTCs and the tax authorities.

FTCs generally appoint agents in India for marketing advertisement airtime slots. Agents also facilitate collection of advertisement revenues from advertisers and its remittance abroad. The tax authorities contend that the agent of the FTC in India constitutes its PE for various reasons.

The Bombay High Court[27] has held that where an FTC has an agency PE in India, i.e., PE on account of its agent, a payment of arm's length remuneration by the FTC to its Indian agent extinguishes its tax liability in India. A similar view has been taken by the Delhi High Court,[28] Bombay High Court [29] and Mumbai Tribunal.[30]

However, in one case, the Mumbai Tribunal[31] has held that an Indian company procuring advertisement in India for a foreign company constituted a dependent agent in India. Further, it also rejected the argument that payment of arm's length remuneration to an agent extinguishes any further tax liability in India by distinguishing the decision of the Supreme Court in the case of Morgan Stanley and that of the Bombay High Court in the case of SET Satellite Singapore[32] (presently pending adjudication at the Supreme Court).

Taxation of Subscription Revenues

Subscription revenues are usually collected by the Indian distributors from MSOs/cable operators and subsequently paid to the FTCs. FTCs are of the view that the payment for grant of distribution rights in the TV channels is not for any copyright and hence is not in the nature of royalty (which is taxable on gross basis at a specified rate). FTCs are of the view that the payment is in the nature of business income and is not taxable in India in the absence of any PE in India. However, the tax authorities hold a contrary view and contend that the subscription revenue are liable to tax as royalties.

The Bombay High Court[33] has held that distribution charges received on account of telecasting of TV channels in India are not taxable as royalty since the taxpayer was not parting with any copyrights.

WHT on Various Payments by TV Channel Companies

Television broadcasting companies pay placement/carriage fees to Direct-To-Home (DTH) operators, multisystem operators and various cable operators towards placement/carriage of the channels. The channel companies are of the view that such payments attract WHT at the rate of 2%[34] However, the tax authorities contend that such payments are liable for WHT at 10% on the ground that the payments are towards technical services/royalty. This has resulted in protracted litigation.

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[27] Set Satellite (Singapore) Pte Ltd. vs. Deputy Director of Income Tax (International Tax) – [2008] 173 taxman 475 (Bombay HC).
[28] DIT vs BBC Worldwide Ltd. (2011) 203 taxman 554 (Delhi HC).
[29]DIT vs B4U International Holdings Ltd [2015] 57 taxman.com 146 (Bombay HC).
[30] Taj TV Limited vs ADIT-ITA no. 9079/MUM/2010; 2065/MUM/2012; 456/MUM/2013 and ADIT vs Taj TV Ltd: ITA no.2073/MUM/2012 and 391/MUM/2013 and International Global Networks BV vs. ADIT, ITA no. 5689 to 5695 MUM/2014
[31] NGC Network Asia LLC vs. CIT (2015) 64 taxman.com 289 (Mumbai Tribunal).
[32] SET Satellite (Singapore) Pte. Ltd. vs DDIT (2008) 307 ITR 453 (Bombay HC).
[33] CIT vs MSM Satellite (Singapore) Pte Ltd [(2019) 265 Taxman 376 (Bombay HC)].
[34] Section 194C of the Indian tax law.

The Supreme Court[35] has dismissed the tax department's special leave petition challenging the Bombay High Court order holding that placement fees/carriage fees paid to cable operators/multisystem operators/DTH Operators are payments for work contract covered u/s 194C and not "fee for technical services" u/s 194J. This order of the Apex Court is a welcome order on the issue, which has been a subject matter of litigation for many years and hopefully should put the pending litigations to rest.

Television broadcasting companies also make significant payments to software production houses towards production of TV programs. With reference to the applicability of provisions dealing with WHT on payments made by broadcasters or television channels to production houses for production of content or programs, the issue has been clarified via a circular no. 4/2016, dated February 29, 2016 issued by the Central Board of Direct Taxes (CBDT). It has been stated in the circular that where the content is produced as per the specifications provided by the broadcaster/telecaster and the copyright of the content program is transferred to the broadcaster/telecaster, such contract is covered within the definition of 'work' which is liable for WHT as per the Indian tax laws. However, where the broadcaster/telecaster acquires only the broadcasting/telecasting rights of the content which is already produced by the production house, and there is no contract for carrying out any work, then such payments are not liable for WHT as per Indian tax laws (but may be liable for other applicable WHT provisions).

DTH industry

WHT on discount on sale of Set Top Boxes (STBs)/Recharge Coupon Vouchers (RCVs)

From an income tax perspective, an issue arises vis-à-vis applicability of WHT on the discount given to distributors on the sale of STBs/RCVs. Tax authorities are of the view that discount on the sale of STBs/RCVs is in the nature of commission, subject to WHT at the rate of 10% under section 194H of the Indian tax laws. However, the industry is of the view that the discount is not in the nature of commission and hence, section 194H is not applicable.

The Mumbai Tribunal[36] has held that trade discounts provided to distributors/dealers on sale of STBs and RCVs shall not be considered as "commission" subject to WHT under section 194H of the IT Act, since the relationship between the taxpayer and the distributors/dealers is on a principal to principal basis. This decision has been followed by the Mumbai Tribunal in the case of another taxpayer.[37]

The Karnataka High Court in the case of Bharti Airtel Ltd,[38] held that the discount given to distributors on sale of SIM cards/RCVs does not generate income in the hands of the distributor since the distributors derive income only on subsequent sale of prepaid cards. However, the High Court held that if, in the books of account of the taxpayer, the discount is reflected separately, then the liability of deducting taxes under section 194J of the Indian tax laws arises on the taxpayer. Though the said decision is in the context of the telecom industry, the decision may also apply to the DTH industry.

Losses

The Indian tax law permits an offset of losses from one business against the gains of another. However, the net unabsorbed business losses can be carried forward and offset against the business profits of the subsequent years, for a maximum period of eight years. In the absence of adequate profits, unabsorbed depreciation can also be carried forward and offset against the profits of future years without any time limit.

[35] CIT TDS vs Times Global Broadcasting Co. Ltd [2019] 105 taxmann.com 314 (SC).
[36] JCIT vs Bharat Business Channels Limited [2019] 92 taxmann.com 216 (Mumbai Tribunal).
[37] Tata Sky Ltd vs ACIT [2018] 99 taxmann.com 272.
[38] Bharti Airtel Ltd.vs DCIT [2014]228 Taxman 219 (Karnataka HC).

Other developments/issues impacting the Media and Entertainment (M&E) industry

Equalization levy

The provisions relating to equalization levy were included in the Finance Act of 2016, in line with the recommendation of the OECD BEPS project. Effective June 1, 2016, payments to non-residents by Indian residents/Indian PEs of non-residents in relation to online advertising and other notified services shall attract equalization levy at the rate of 6% if the aggregate payment to a party during the year exceeds INR 100,000.The Government has, in its continued efforts to transform the way digital businesses are taxed, enacted a law to expand the scope of equalization levy vide in the Finance Act 2020. While the erstwhile provisions were applicable to payment for online advertisement and certain other services, its scope has now been significantly expanded to include online sale of goods and/or provision of services (including facilitating the same) through a digital platform. Equalization levy on payment for online advertisement services continues at six %; however, the expanded scope would be subject to EL at the rate of 2%.

The expanded scope is wide enough to cover B-to-B and B-to-C transactions, online transactions involving supply of goods, provision of services, and also transactions between non-residents in certain specified circumstances. What this means is that if an overseas entity owns/operates or manages a digital platform for selling products or services to Indian buyers/users across sectors such as digital media/online streaming, travel, retail, hospitality, education, and marketplace/aggregators, among others, then this expanded equalization levy might impact them. Though the levy cuts across sectors, it is expected to have a significant impact on the M&E sector.

General Anti-Avoidance Rule (GAAR)

The GAAR provisions, which were introduced into Indian tax law by the Finance Act of 2012 have now become effective from April 1, 2017. GAAR is applicable to arrangements regarded as 'impermissible avoidance arrangements,' which could result in, among other things, re-characterization of such arrangements, denial of tax benefits or treaty benefits, etc.

Place of Effective Management (POEM)

The 2016 Finance Act made a significant amendment to the definition of 'resident in India' in the context of companies. A company having turnover or gross receipts exceeding INR 500 million shall now be considered as 'resident' if its POEM (i.e., place where key management and commercial decisions necessary for conduct of business are in substance made) is in India. The government has issued guiding principles for determining POEM.[39]

Amendments in tax treaties

The Indian government has renegotiated treaties with the governments of Mauritius, Cyprus and Singapore amending, *inter alia*, the capital gain tax provisions. Taxation of capital gains arising from transfer of shares changed from residence-based taxation to sourced-based taxation. Limitation of Benefit clauses have been introduced/modified in the Mauritius/Singapore tax treaties specifying the conditions necessary for the taxpayer to satisfy to avail the treaty benefit. With this, the government has sought to plug the tax loopholes exploited by companies to avail tax benefits under these treaties vis-à-vis capital gains.

[39] CBDT Circular No.8/2017 dated 24 January, 2017.

Indirect Taxation

Goods and Services Tax ('GST') is one of the biggest Indirect tax reforms in India. GST was implemented in India effective July 1, 2017. It is a comprehensive tax levied on manufacture, sale and consumption of goods and services with a mechanism for allowance of input tax credit ("ITC" paid at each stage of supply. GST, which is generally described as "one nation one tax," has subsumed all previous indirect taxes such as Excise Duty, Service Tax, CVD, Value Added Tax ("VAT"), Central Sales Tax ("CST"), Entertainment Tax at State level, Entry Tax etc. and only one tax i.e., GST is levied and collected on value additions at each stage of the supply of goods and services at National level. In India, there is a dual levy of GST, i.e., on all Intra-State supplies, Central Goods and Service Tax ("CGST"), and State Goods and Service Tax ("SGST") are levied and on all Inter-State supplies, Integrated Goods, and Service Tax ("IGST") is levied.

GST is the destination-based tax wherein the tax revenue would be earned by the state where goods and services are consumed rather than the place where they are produced or the services are being provided. Currently the GST rates broadly prescribed for goods and services are 0%, 5%, 12%, 18%, and 28%.

The impact of GST on different trade and business varies. In the ensuing paragraphs of this section, we have broadly touched upon certain impact areas for the various segments functional in the film industry.

Film industry

1. Multiple registrations and increased compliances

Under the GST regime, every Company needs to obtain separate registration for each state in which it has presence basis the threshold limit of the "aggregate turnover." Multiple registrations have resulted into multiple return filings which has increased the compliance burden. Also, the concept of distinct person has resulted into increased inter branch billing on account of "deemed supply" between the various branches of the companies located across states and the head office located in different state. All of this together has led to huge unwarranted compliance costs as well as time and effort for media companies.

2. Rate on copyright transfer

When GST law was introduced permanent transfer of intellectual property right was part of service schedule under the GST regime attracting GST at the rate of 12%. Further, by virtue of a notification, permanent transfer of intellectual property right (which includes copyright) has been incorporated in the goods schedule, attracting GST at the rate of 12%.However, entry under service schedule has not yet been amended/deleted thus creating unwarranted ambiguity. Also, determination of place of supply (i.e., location of termination of delivery), in case of permanent transfer of copyright (if the same is treated as goods) is still a challenge, since, copyright is intangible in nature.

Further, the Karnataka GST department has issued a circular wherein they have mentioned that, currently the distribution of film services rendered by the distributors are being classified by the distributors under HSN 9973 and are discharging GST at the rate of 12%on the same, however, the said services appear to be more appropriately classifiable under HSN 9996 attracting GST at the rate of 18%. Accordingly, the Karnataka GST department is of the view that the distribution of film services shall be subject to GST at the rate of 18%and not 12%. This has led to a stir in the film industry as most of the players have been paying GST at the rate of 12%on such distribution services as they are engaged in supply of distribution rights (i.e., copyright) in a cinematographic film.

3. Specific restriction to avail ITC on certain inward supplies

Expenses incurred towards beauty treatment, serving food and beverages, and hiring conveyance including vanity vans for actors and technicians and rent-a-cab services directly relate to core business activity of any production house. However, the production houses cannot avail ITC of GST paid on such expenses, since, the same are specifically restricted under the GST law.

Also, there is no clarity as to whether the services of a make-up artist will fall under beauty treatment services. The restriction for availing ITC of GST paid on these services has added on to the tax burden of production houses and has adversely impacted their working capital cycle and profitability.

4. Input tax credit blockage due to place of supply of services

The place of supply of services by way of hotel accommodation (in case of outdoor shoots) is the place at which such immovable property i.e., hotel is located. The input tax credit of state levies charged by the service provider cannot be availed in another state. Whenever the production houses carry out shooting outside the state of their registration, the hotels in such outside states levy state levies of that specific state. To avail such ITC of such state levies, the production houses need to obtain registration under GST in the state in which such hotel is located.

It is practically impossible for production houses to obtain registrations in all the states where the shooting is carried out. This builds up a significant tax cost on account of non-availment of input tax credit on such services received in states where the production houses are unregistered. Such tax cost adversely impacts the working capital cycle and profitability of the production houses.

5. States not entitled to grant tax exemption status

If any state declares a film as tax free, it has the authority to only waive off the state GST component (i.e., SGST), which is half of the total GST charged i.e., 6% or 9%, as the case may be (based on ticket prices). Therefore, the Central GST component still needs to be discharged even where the film is declared tax free in a state. This leads to increased outflow on account of higher CGST component as compared to SGST component (as the same is exempt) for which the SGST ITC cannot be used and the tax payment may have to be made in cash.

The government should consider granting overall tax exemption to films spreading social messages to the society i.e., both central and state taxes (CGST and SGST) must be waived off. Also, tax exemption should be provided for the corresponding input and input services in such cases so that there is no ITC blockage.

6. Input tax credit on advances paid for production

In the media industry it is a common practice where companies pay huge advances to the copyright owners against the copyright to be obtained for the movie that is under production. Such advances are paid against which the copyright owners issue receipt vouchers. However, the companies paying the advances are unable to avail input tax credit on the amount paid as GST law requires possession of invoices and receipt of services for availing the input tax credit. Since the movie awaiting receipt of copyright would be still under production, receipt of services is difficult to justify. Also, a receipt voucher is not a valid document with which ITC can be availed under GST Law. Accordingly, the input tax credit for the GST paid on advance cannot be availed immediately, and availment is deferred, causing huge impact on the cash flow.

In such cases where the Government collects GST on advances, there needs to be a mechanism in place to allow availment of ITC of GST paid on advances.

7. Challenges in determining value of supply in case of barter transactions

Various promotional activities such as providing free movie tickets, tie-in promotions, distributing free merchandise, making appearances for events, etc. are being undertaken by the production houses and artists without any flow of monetary consideration for each other. Such promotional activities which benefit both the parties, are barter transactions which fall under the definition of supply as per the GST law, even though there is practically no flow of monetary consideration. Such transactions will now have to be valued, and GST will have to be paid by both the parties.

In such kind of transactions determining the value of supply of services is a challenging task. There is no readily available market value of such supply nor are there any comparable supplies to arrive at value of services of like kind and quality, since the value is dependent on success of the film or event. Further, the parameters of success may vary for each movie or event.

8. Municipality empowered to levy tax on entertainment and amusement

In certain states, municipal authorities have started levying and collecting taxes on entertainment and amusement. Consequently, the likely benefit being received by the industry on account of subsumed entertainment tax may fade away. On account of such levy the industry may suffer multiple tax levies and cascading tax effect similar to what was prevalent in the pre-GST regime, thereby defeating the very objective of GST. Such multiple tax levies may also affect the working capital cycle and profitability of the industry.

Broadcasting industry

1. Clarification with respect to broadcasting services

The ambiguity with regards to the place of supply for broadcasting services was resolved by the government by issuing a clarification to the effect that, the place of supply for the channel distribution/broadcasting services would be the location of recipient of services as per the records of the supplier. This has provided a great relief to the broadcasters as tracking of head-ends/IRD boxes provided to the multiple system operator/cable operators might have been a herculean task.

2. Advertisement services provided to the government

In case of supply of advertisement services on television channels to the Central Government, a State Government, a statutory body or a local authority, the place of supply of such service shall be amount attributable to services provided in each respective state. In the absence of any contract with the recipient of services, there was no mechanism to arrive at such amount. It has now been prescribed vide IGST Rules that, such amount attributable to each state shall be determined based on the viewership in each state.

3. GST Rate applicable on leasing of satellite transponder charges

Broadcasters lease transponder services of communication satellites in order to provide broadcasting services. An ambiguity exists on applicability of GST rate on leasing of satellite transponder charges that whether the same shall be classified under chapter heading 8803 i.e., Parts of goods of Heading 8802 (i.e., Satellites) and be subject to GST at the rate of 5% or the same shall be classified under chapter heading 8525 i.e., Other satellite equipment and be subject to GST at the rate of 18%. The advance ruling issued by the Karnataka Authority for Advance Ruling in the case of New Space India Limited[40] states that the transponder is an integral part of the communication satellite, and, accordingly, leasing of transponder charges services shall be classified under chapter heading 8803 and shall attract GST at the rate of 5% being the rate of GST applicable on supply of like goods i.e., part of Spacecraft (including satellites). A similar ratio was also followed in the advance ruling issued by the Karnataka Authority for Advance Ruling in the case of Antrix Corporation Limited.[41]

However, despite the above advance rulings, many broadcasters are paying GST at the rate of 18% to avoid litigation/queries from the GST authorities and also since the entire GST paid is eligible as ITC. The aforementioned advance rulings may be adopted to clear the ambiguity around applicability of GST rate on leasing of transponder charges.

[40] Advance Ruling No. KAR ADRG 19/2020, dated 31 March 2020, Karnataka Authority for Advance Ruling in the case of New Space India Ltd.
[41] Advance Ruling No. KAR ADRG 19/2019 dated 26 August 2019, Karnataka Authority for Advance Ruling in the case of Antrix Corporation Ltd.

DTH industry

1. Clarification in connection to Customers Premise Equipment (CPE) supplied by DTH operators

In the pre-GST regime, the state government had raised huge VAT demands contending that grant of CPE constitutes a deemed sale as per VAT laws. Under the GST regime, the ambiguity around the same has been resolved by the government. The Government has clarified that CPEs are not sold by the DTH service providers/cable operators to the end customers, and they are merely placed at the customers' location for supply of digital cable services. Such clarification has put to rest the long-standing dispute under the erstwhile tax regime where it was contended that grant of CPE constitutes a deemed sale as per VAT laws.

General

1. E-invoicing under GST

The Government with the aim to standardize invoicing system in the country and to ensure complete interoperability of invoices across the entire GST ecosystem has implemented e-invoicing in the GST system. The Government has specified that the registered persons having an aggregate turnover of more than INR 100 crores shall generate invoice electronically from the GSTN network. The Government has also specified the schema/template for generating e-invoice from the GSTN network.

2. Restriction in availment of ITC

The availment of ITC in respect of invoices/debit notes, the details of which have not been uploaded by the supplier in its outward supply return, has been restricted to the extent of 5% of the invoices/debit notes the details of which have been uploaded by the vendor in its outward supply return. The amended rule has imposed additional compliance on the taxpayer of monthly reconciliation of input tax credit before availment.

3. Restriction in utilisation of ITC

Recently the Government has brought in restriction on utilization of ITC in excess of 99 % of the output tax liability, in case where the value of taxable supplies in a month exceeds INR 50 lakh. Accordingly, now the Companies will have to mandatorily pay 1% of the output tax liability in cash. However, there are certain exceptions provided where the said restriction shall not be applicable. Further, the aforementioned restriction is applicable GST registration wise, accordingly, the Companies will have to evaluate the aforementioned restriction GST registration wise.

4. Stringent provisions for cancellation/suspension of GST registration

The provisions in connection to cancellation or suspension of GST registration by the department have become more stringent. As per the recent amendments, the Government may cancel or suspend the GST registration in multiple cases, for example:

- Where there is difference in the amounts disclosed in GSTR 1 (i.e., outward return) vis-à-vis the amounts disclosed in GSTR 3B (i.e., payment return) for one or more tax periods;
- ITC is availed in violation of provision of GST Law;
- Difference in ITC availed in GSTR 3B (i.e., payment return) vis-à-vis GSTR 2A (i.e., GSTR 1 filed by the vendor), etc.

Transfer Pricing

The Indian TP regulations require a taxpayer to undertake international transactions and Specified Domestic Transactions ('SDTs') with Associated Enterprises on an arm's length basis. Further, the regulations mandate the use of one of the six prescribed methods as the Most Appropriate Method for the determination of the arm's length price ('ALP'). From a compliance perspective, the regulations prescribe maintenance of mandatory documentation by taxpayers on an annual basis in relation to their international and SDTs and also cast a compliance obligation on the taxpayers, which involves filing of an annual TP certificate (known as Accountant's Report) with the tax authorities disclosing details of such transactions in a prescribed format.

Recent developments

TP landscape in India has constantly evolved over the years from the 2001 Finance Act which introduced the TP regulations in India for the first time to the implementation of a three-tiered documentation requirements contained in the Action Plan 13 of Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) project by the Union Budget 2016 to introduction of e-proceedings to conduct Tax Scrutiny. While Faceless Assessment Scheme has been rolled out and is being implemented in Direct Tax (Corporate Tax) scrutiny and Appeal cases, it is yet to apply to Transfer Pricing scrutiny cases.

BEPS refers to tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations resulting in little or no overall corporate tax being paid. In the post BEPS era, multi-national enterprises (MNEs) would be called upon to review and realign their structures to ensure consistency between allocation of income and value creating activity. Consequently, the implementation of Action Plan 13 of OECD BEPS project regarding Country-by-Country (CbyC) reporting from financial year 2016–17 was seen as a game changer, and not only increased the documentation burden, but also invited additional attention by tax authorities.

The TP environment has further undergone a significant change over the past 12 months, especially due to COVID-19. Various compliance due dates were extended giving relaxations to taxpayers for undertaking relevant compliances.

Earlier this year, the Central government passed The Direct Tax Vivad se Vishwas Act, 2020 ("the VsV Act"). This Act has provided an alternative to taxpayers for settlement of long outstanding litigation with significant leverage on waiver of penalty and interest. Further, since the settlement under the VsV Act does not amount to setting a precedence, taxpayers are free to pursue litigation for other years on merits, where they have not opted for settlement under VsV Act.

The APA provisions have proved to be a step in the right direction and the Indian government has consciously put the APAs on a fast track which has helped in boosting taxpayers' confidence in the government's APA program.

Additionally, the tax authorities have taken various measures to improve the TP landscape in India during the previous years. With a view to reduce litigation, the government had introduced certain measures to move away from a quantitative basis for selection of cases for transfer pricing audit to a risk-based system and CBDT had issued revised instructions prescribing certain additional mandatory criteria for reference of matters to TPOs. This has helped in reducing the number of cases under audit and thus, has reduced litigation.

Key transfer pricing issues for the M&E industry

The increased cross-border activity coupled with the peculiarities of the nature of transactions undertaken in the M&E industry poses several practical challenges in establishing the fact that the transactions undertaken between related parties are at arm's length. The sections below provide an overview of TP-related issues faced by the M&E industry.

India

Comparability for distinct transactions

The Indian TP regulations provide that the comparability of an international transaction with an uncontrolled transaction should be judged with reference to:

- The specific characteristics of the property transferred or services provided in the transaction;
- Functions performed, taking into account assets employed or to be employed and risks assumed, by the respective parties to the transactions;
- The contractual terms (whether or not such terms are formal or in writing) of the transactions which describe, explicitly or implicitly, how responsibilities, risks and benefits are to be divided between the respective parties to the transactions; and
- Conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, laws and government orders in force, costs of labor, overall economic development, level of competition, and whether the markets are wholesale or retail.

In consideration of the above mentioned parameters, if the nature of international transactions entered into between parties in the M&E industry are analyzed, it would be seen as distinct, peculiar and not comparable to those undertaken in any other industry, mainly due to the nature of assets or intangibles being traded between the parties. The following examples will help provide a better understanding of the concept.

- An Indian TV broadcasting company purchases film rights from a related party situated abroad. However, the price paid may vary significantly for various films and would depend on factors such as whether a film is being telecast on television for the first time, the timing of telecast, etc.
- Similarly, in the case of an Indian company which owns a channel being telecast in a foreign country and grants advertisement rights on a revenue split basis to related parties abroad, the proportion of split may vary significantly depending upon economic and commercial factors.

Given the nature of transactions undertaken, it poses peculiar challenges from a benchmarking perspective. Firstly, it is usually difficult to gather information from the public domain on similar independent transactions undertaken in this industry. Secondly, even if some data is available on certain similar transactions undertaken between unrelated parties, they can seldom be used for benchmarking the related party transactions because of material differences between the two transactions being compared.

Difficulty in application of prescribed methods

The Indian TP regulations have prescribed six methods under the law (as prescribed by the CBDT) for the purpose of determination of the arm's length price, viz., (1) Comparable Uncontrolled Price ('CUP') Method; (2) Resale Price Method ('RPM'); (3) Cost Plus Method (CPM); (4) Profit Split Method (PSM); (5) Transactional Net Margin Method (TNMM); and (6) Other Method [notified by the CBDT on 23 May, 2012 vide a Notification and Rule 10AB inserted in the Income-tax Rules, 1962 (the Rules) thereafter].

Rule 10AB describes the other method as "any method which takes into account the price which has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts." This rule is effective from financial year 2011–12.

Given the distinctiveness of international transactions entered into between related parties in the M&E space, it is often felt that the benchmarking analysis may not always be possible within the purview of the five methods prescribed under the law.

With the introduction of the 'other method,' taxpayers may have a little more flexibility to use tender documents, third-party bids, proposals, valuation reports, standard rate cards, price quotations, and commercial and economic business models, etc. to demonstrate arm's length intent. The application of the 'other method' could be particularly helpful in cases where application of the other five specific methods is not possible due to difficulties in obtaining comparable data as a result of distinctiveness of transactions such as intangible transfers, etc.

Increased compliance burden on the foreign M&E entities undertaking TP compliances in India

In a landmark decision of a foreign taxpayer,[42] the Delhi Tribunal dealt with the issue of Transfer Pricing compliance to be undertaken by overseas entities. The Delhi Tribunal held that it is mandatory to obtain an independent Accountant's Report in respect of all international transactions between associated enterprises for non-resident entities. Further, the foreign entities are mandatorily required to maintain documents of its own and confirmed the penalty under section 271AA for non-maintenance of TP documentation under section 92D.

The Tribunal opined that "the Assessee mandatorily has to maintain documents of its own," and further stated that "Non-maintaining documents on account that there is no international transaction and merely relying on the supporting documents of Associated enterprise, cannot be termed as reasonable cause for not maintaining the documents on its own...;" Taking into account the mandate to obtain an independent accountant's report/documents with AE cannot be diluted by the so called reasonable cause given u/s.273B, Tribunal held that "Assessing Officer was right in imposing the penalty under Section 271AA of the Income Tax Act and the CIT(A) was not right in deleting the penalty."

Given the above, it is observed that it is critical to maintain documentation for the non-resident entities as well, with respect to their international transactions with their AEs and not simply rely on the documentation maintained by its Indian counterpart.

In another landmark decision of a foreign taxpayer,[43] the Special Bench of Kolkata Tribunal dealt with the issue of 'base erosion'.

In this case, the taxpayer (foreign entity) had offered interest-free loans to its Indian subsidiary for commercially justified reasons. The TPO did not accept the lack of interest charge and made a TP adjustment in the hands of the taxpayer. The taxpayer argued that such adjustment ought not be made following the principles of 'base erosion' since any increase in the income of the foreign company (e.g., additional WHT at 10%) will imply a corresponding higher claim of expenses by the Indian company (e.g., additional corporate tax deduction of 30%) and hence, the overall effect of the adjustment will lead to a reduction of tax base for the country (of 30% *Less* 10% = 20%). The Kolkata Tribunal constituted a Special Bench to adjudicate on the taxpayer's appeal.

The Special Bench refused to accept the taxpayer's plea and held that establishing whether there is an erosion of the overall Indian tax base is not a relevant factor in determining whether TP provisions apply to a transaction. Therefore, the principle of 'base erosion' was not upheld.

The Special Bench has rejected the base erosion theory in principle which would not be restricted only to interest free loans but to wider classes of transactions. If implemented by the tax authorities, this ruling could have wide spread ramifications for foreign M&E entities complying with TP rules in India. In the immediate short-term, the ruling may increase the compliance and litigation burden for taxpayers and the overall impact could be adverse.

[42] DCIT Circle-1(2)(1), International Taxation vs Convergys Customer Management Group Inc. [ITA Nos. 3529 & 3530/Del/2015] (Delhi Tribunal).
[43] Instrumentarium Corporation Limited [TS-467-ITAT-2016-TP] (Kolkata Tribunal SB).

In fact, the lower authorities have taken a cue from the above decision and have started framing aggressive TP assessments of foreign M&E entities. Consequently, foreign M&E entities undertaking TP compliances in India by taking support of the base erosion argument need to reassess arm's length justification reasons in light of this decision.

Update on Advance Pricing Agreements

The APA Scheme was introduced to Indian tax law in 2012 and the 'Rollback' provisions were introduced in 2014. The scheme aims to provide certainty to taxpayers by specifying the method and determining the prices of international transactions in advance thus avoiding future TP disputes.

Since its inception, the APA scheme has received a lot of interest from taxpayers which has resulted in more than 1100 applications (unilateral and bilateral) filed in approximately last 8 years. CBDT has already signed 271 APAs (240 unilateral APAs and 31 bilateral APAs), by March 31, 2019, which has been highly appreciated nationally as well as internationally.

Until recently, signed APAs pertained to mainstream industry transactions. However, a growing number of APAs have been signed for complex and litigious transactions. The APAs signed for management cross charges and royalties have particularly helped in boosting taxpayers' confidence in India's APA program. Further, the Indian government has consciously put the APAs on a fast track which has helped in boosting taxpayer confidence in the government's APA program.

Further, CBDT has also concluded an APA under the new remote signing mechanism, which was introduced given the COVID-19 pandemic. This reinforces the focus and flexibility of the APA program and establishes it as a perfect platform for taxpayers to constructively resolve potential transfer pricing disputes.

M&E players in India have significant intercompany transactions in the nature of royalty given their tie-ups with international M&E entities and nature of their operations. While the recent APA and MAP for brand royalty was not signed for an entity in the M&E industry, payment of brand royalty being a contentious TP issue in Indian TP audits, conclusion of an APA/MAP on the same is a welcome move, and M&E players could benefit from the precedent set by the said APA.

Other key developments

Scope of APA and Safe Harbor Rules expanded

The scope of APA and Safe Harbor provisions have been expanded to cover determination of income deemed to accrue or arise in India as referred to in Section 9(1)(i) or Permanent Establishment (PE). This shall provide significant relief to taxpayers with issues concerning attribution of profits to PEs.

The manner of determining the arm's length price include methods provided under the Income-Tax Rules, 1962, i.e., Transfer Pricing (TP) methods, with adjustments or variations as appropriate. The manner of determining income attributable to operations carried out in India would be as per rules to be prescribed, with adjustments or variations as appropriate

Secondary Adjustment

Secondary adjustment postulates a situation of adjustment to income of a taxpayer which has been accepted by the taxpayer under certain defined circumstances. It is provided that such an adjustment to the income (referred to as primary adjustment) of the taxpayer results in underlying excess cash with the foreign associated enterprise and the same should be repatriated into India (i.e., money should be brought into India) and accounted for as income of the Indian taxpayer. Failure to do so beyond a specified period of time would render re-characterization of such adjustment as an advance given by Indian taxpayer to its AE and interest shall be imputed thereon.

Notable amendments made to this provision include permitting receipt of money from any of the non-resident AEs of the taxpayer and not necessarily the one with whom international transaction was entered into. This provided significant relief to taxpayers facing such adjustments.

The provisions were further amended to provide an option to the taxpayer to pay additional tax in case repatriation of funds is not possible. Thus, where money is not repatriated on time, the taxpayer can pay tax at the rate of 18% plus surcharge and relieve itself of bringing the excess money into India.

This provision has also helped many taxpayers to avoid incurring interest cost year on year where repatriation of money from AEs is not feasible.

Amendment in Section 94B

Deduction of interest expenditure incurred by an Indian company or a permanent establishment of a foreign company, in respect of debt issued by an NR, Associated Enterprise ("AE"), shall be restricted to 30% of the EBIDTA provided such interest exceeds INR 10m and is deductible under the head "business income." This restriction on deduction also extends to loans provided by an unrelated lender (e.g., foreign bank branch in India) but guaranteed by an AE. These provisions do not apply to an Indian company or a PE of foreign company that is engaged in the business of banking or insurance. The term AE, inter alia, includes an entity that has advanced a loan to another entity, and such loan constitutes at least 51% of the book value of total assets of the borrower enterprise. In such a situation, the provisions with regard to limitation on the deduction of interest expenditure are attracted. Said provisions discourage companies from raising debt from the PE of a foreign bank. Further, the branches of foreign banks are taxable in India on their income.

In view of this, the Interest limitation rule has been amended to exclude interest paid/payable on loan extended by a PE of a non-resident bank for determining tax deductibility. This amendment provides much needed exemption to the Indian branches of foreign banks operating in India.

Dispute Resolution Panel ("DRP") route for non-resident

Objections before the DRP can be filed by the eligible assessee for any variation in the income or loss returned which is prejudicial to the interest of the eligible assessee.

"Eligible assessee" means any person in whose case the variation arises as a consequence of the TP order or a foreign company.

The definition of eligible assessee will be expanded to include an NR, not being a company, in addition to a foreign company.

Personal Taxation

Residential Status and Taxability of Income in India

Residential Status

An individual is taxable in India based on his "residential status" in the relevant financial year[44]. Residential status is determined on the basis of physical stay/presence in India. The residential status of an individual could be that of a "resident" or a "non-resident."

Resident

A person is said to be a "resident" of India if:

(a) He stays in India for 182 days or more in the relevant financial year

(b) He stays in India for a period of 60 days or more in the relevant financial year coupled with a stay of 365 days or more in the four financial years immediately preceding the relevant financial year.

[44] Indian financial year runs from April 1 to March 31 of the following year.

Non-resident ("NR")

A person is said to be a "non-resident" if he does not satisfy any of the above two conditions, i.e., neither condition (a) is satisfied nor condition (b) is satisfied.

When an Indian citizen leaves India during the relevant financial year for the purpose of employment or an Indian citizen/Person of Indian Origin (PIO) while being outside India** comes to India on a visit during the financial year, his residential status would be that of a "resident" only if he stays in India for 182 days or more.

**Additional exception in b) above- 60 days to be replaced by 120 days in case of Citizen of India/PIO having total income (other than income from foreign sources) exceeding INR 1.5 million.

Note: 1) Income from foreign source means income which accrues or arises outside India (except income derived from a business controlled in or profession setup in India).

2) Interpretation of "visits to India" should continue to be analyzed as per specific facts of each case.

"Resident" is further subdivided into:

Resident but Not Ordinarily Resident (NOR): An individual is said to be an NOR if he is:

a) A *nonresident* in India in 9 out of 10 financial years preceding the relevant financial year

b) Present in India for 729 days or less during the 7 financial years preceding the relevant financial year.

Resident and ordinarily resident (ROR): A person becomes an ROR if he does not satisfy any of the above said conditions, i.e., neither condition (a) nor condition (b) is met.

Normally, a foreign citizen who is visiting India for the first time would become an ROR in the third/fourth financial year, from the year of the start of his assignment.

The Act has also added a sub-section (1A) to Section 6 to state that an individual, being a citizen of India, shall be deemed to be resident in India in the relevant tax year if:

- An individual has a total income (other than income from foreign sources) exceeding INR 1.5 million during relevant tax year; and
- An individual is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.

Note: Interpretation of "liable to tax" especially for citizens residing in countries with no personal tax regime, continues to remain litigious.

Please note that the individuals qualifying as deemed resident under above provision and citizen of India/PIO having total income (other than income from foreign sources) exceeding INR 1.5 million present in India for 120 days or more but less than 182 days during the relevant tax year shall always qualify as NOR in India.

Taxability of Income Based on Residential Status

Based on the residential status, an individual is taxable as below:

ROR: Liable to tax on worldwide income, i.e., salary income and income other than salary earned/received in India or abroad

NOR: Liable to tax on the income sourced, i.e., accruing or arising/deemed to accrue or arise, from India or received/deemed to receive in India or on the income derived from a business controlled or profession set up in India

India

NR: Liable to tax only on the income sourced, i.e., accruing or arising/deemed to accrue or arise from India or received/deemed to be received in India

The salary income earned by an NOR/NR for "services rendered in India" is liable to tax in India, irrespective of the place of receipt of such income, i.e., whether the salary income is received in India or overseas.

Taxability of Self-Employed in India

Non-resident Artists (self-employed)

Income from Profession

Artists are taxed in India with respect to income earned from performances in India. The Indian taxpayer is obliged to withhold at the appropriate rate of income tax applicable to nonresident individuals. However, this is, subject to any benefits that may have been available to the artist under the relevant double tax avoidance treaty (article on "artistes and sportsmen") and Indian tax law, respectively.

Some specific cases, where the consideration paid to an artist may be taxed in India,[45] have been illustrated hereunder:

- For acquiring copyrights of performance in India for subsequent sale in India (of CDs, etc.); and
- Portion of endorsement fees relating to artist's performance in India.

Resident Artists (self-employed)

Taxability of Income

Indian residents are taxed on their worldwide income from all sources.

Relief for Foreign Taxes in India

A resident in India is entitled to a credit for foreign taxes paid on foreign-sourced income in the following manners:

- Where agreement for avoidance of double taxation exists between the two countries, in accordance with the terms of that agreement; and
- Where there is no double taxation avoidance agreement, as per the provisions of the Indian tax laws.

Maintenance of Books of Account

Every person carrying on a profession notified by the CBDT (like film artist, company secretary, etc.) is required to maintain books of account in the prescribed format as per Indian tax law for the income earned in India and expenses incurred in the course of profession.

Compulsory Tax Audit

Every person carrying on a profession, whose gross receipts exceed INR 5 million in the current tax year, shall have his accounts audited by an accountant and furnish the report in the prescribed format before the specified date.

Social Security Regime in India

General Principles of the Social Security Scheme

Persons Covered

Social security regime in India is primarily governed by Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (the EPF Act) and comprises the following schemes:

a) Employees' Pension Scheme, 1995 (EPS);

b) Employees' Provident Funds Scheme, 1952 (EPFS); and

c) Employees' Deposit Linked Insurance Scheme, 1976 (EDLI).

[45] Circular No. 787 dated February 10, 2000.

The above schemes provide for the social security of employees working in an establishment employing 20 or more persons.

The Ministry of Labour and Employment, Government of India issued a notification, dated 1 October 2008, wherein special provisions were introduced in the EPF Act to define a new category of workers called International Workers (IWs).

IWs have been defined[46] to mean:

(i) An Indian employee who have contributed to the social security programme of a country that has a Social Security Agreement (SSA) with India and who have gained or are going to gain eligibility for benefits under this SSA; and

(ii) An employee other than an Indian employee, holding other than an Indian passport, and working for an establishment in India to which the EPF Act applies.

Provided that the worker who is a Nepalese national on account of Treaty of Peace and Friendship of 1950 and the worker who is a Bhutanese national on account of India-Bhutan Friendship Treaty of 2007, shall be deemed to be an Indian worker.

The IWs i.e., non-Indian passport holders have to be enrolled from the first day of his employment in India or from November 1, 2008, whichever is later.

All employees who fall within the definition of IWs are required to become members of the Schemes under the EPF Act unless they qualify as "excluded employees."

An "excluded employee" has been defined to mean:

i. An International Worker, who is contributing to a social security programme of his country of origin, either as a citizen or resident, with whom India has entered into a social security agreement on reciprocity basis and enjoying the status of detached worker for the period and terms, as specified in such an agreement; or

ii. An International Worker, who is contributing to a social security programme of his country of origin, either as a citizen or resident, with whom India has entered into a bilateral comprehensive economic agreement containing a clause on social security prior to 1st October 2008, which specifically exempts natural persons of either country to contribute to the social security fund of the host country."

In view of the above, IWs are exempt from contributing to Indian social security/PF if:

- They are contributing to social security in their country of origin and obtained a Certificate of Coverage (CoC) under the relevant SSA; or
- Deputed from a country with which India has entered into a bilateral comprehensive economic agreement before October 1, 2008. (Currently with Singapore only); or
- They are Nepalese national on account of Treaty of Peace and Friendship of 1950 and the worker who are Bhutanese national on account of India-Bhutan Friendship Treaty of 2007, shall be deemed to be Indian workers. (Date of effect: November 2, 2016)

[46] 2(ja) of paragraph 83 of the EPF Scheme.

Scheme for salaried persons

The above-mentioned schemes are applicable only to employees working with covered establishments. Every employee, as mentioned above, working with a covered establishment, is required to become a member of the schemes. Both employee and employer are required to contribute towards the schemes. The schemes provide for retirement savings, retirement pension, and life insurance benefits to the employees.

Scheme for self-employed persons

The above schemes do not cover the self-employed persons and are applicable only to employees.

Incomes Subject to Social Security Contribution

Scheme for salaried persons

Calculation of the contributions to be paid by salaried persons is based on the salary earned by the employee.

"Salary" for the purpose of the PF contribution would include basic wages, dearness allowance (including cash value of any food concession) and retaining allowance.[47]

Dearness allowance is likely to include any allowance granted to an employee to compensate for the rise in the cost of living.

Scheme for self-employed persons

As mentioned above, the above schemes are not applicable to the self-employed persons.

However, for self-employed persons, Public Provident Fund, National Pension System and private pension plans are some of the schemes available in India.

Social Security Rates

The above schemes are financed by collecting contributions paid by the employees and employers.

- **Employee's social security rate** – Every employee is required to contribute to the EPFS at the rate of 12% of his eligible salary; and
- **Employer's social security rate** – An employer is also required to make a matching contribution of 12%. Employees who joined the Indian establishment on, or after, September 1, 2014 and have not been covered under the PF Act earlier, shall apply the complete 12% of employer contribution under the EPFS. In the case of an employee who has been a member of EPFS prior to September 1, 2014, the employer would require the employee to contribute towards pension fund i.e., EPS. Therefore, from the 12% of employer's contribution, 8.33% will be contributed towards the pension fund (EPS) and 3.67% will be diverted towards EPFS. Apart from the above, the employer is also required to contribute towards the administrative costs levied by the PF authorities.

How Social Security Contributions are levied?

Scheme for salaried persons

Generally, the employer is required to withhold the employee's contribution from the salary of the employee and contribute the same along with its own contribution to the fund. The employer is also required to comply with certain filing requirements at the time the employee joins and on a monthly basis.

Scheme for self-employed persons

As mentioned above, the social security schemes are not applicable to the self-employed persons.

[47] Section 6 of the EPF Act.

Benefits Covered (for Salaried Persons)

Provident Fund

The amounts contributed by the employee and employer are accumulated in a separate account maintained by the social security authority in India, which also allows interest on the said amount on a monthly basis.

IW(s) can withdraw the amount standing to their credit under the PF scheme in the following situations:

- On retirement from service in the establishment at any time after the attainment of 58 years of age;
- On retirement on account of permanent and total incapacity from work due to bodily or mental infirmity duly certified by the medical officer/registered medical practitioner designated by the organization;
- On suffering from tuberculosis, leprosy, or cancer, even if contracted after leaving the service on the grounds of illness but before the payment has been authorized; or
- In respect to the member covered under an SSA, on ceasing to be an employee in an establishment covered under the EPF Act.

Monthly Pension

The employee is entitled to *monthly pension* in the following manners:

- Superannuation pension: In the case of employees (both from SSA as well as Non-SSA countries) with 10 years or more of contributory service, they would be qualified to receive a monthly pension.
- Early pension: A member, if he so desires, may draw an early pension from a date earlier than 58 years of age but not earlier than 50 years of age. In such a case, the amount of pension shall be reduced at the rate of 4% for every year the age falls short of 58 years.

Pension Accumulation

In relation to pension withdrawal, the lump sum refund will be available only to those employees who are covered under an active SSA and who have not completed the eligible service of 10 years even after including the totalization of service under the respective SSAs.

An employee who is covered under an SSA and who has not completed eligible service of 10 years may withdraw the full amount standing to his credit in the pension account:

- On retirement from service after attaining the age of 58 years; or
- On exit from employment.

In the case of employees from non-SSA country, they will not receive the lump sum refund.

Life Insurance

The employee is required to nominate a person at the time of joining a scheme. The nominated person is entitled to the amount of life insurance in case of a death of the individual.

Tax Implications in Respect of PF Scheme

- *At the time of making of contribution*

  Employees can claim deduction up to the maximum amount prescribed. Presently, the maximum amount of deduction prescribed under the Indian tax laws is INR 150,000 per financial year. Further, employer's contribution up to 12% of the salary is exempt from tax under the Act.

- *At the time of withdrawal of accumulated balance*

  When the employee has rendered less than five years of continuous service

In this case, the refund of employer's contribution and the interest thereon would be fully taxable as salary income. The employee's contribution would be taxable to the extent of deduction claimed, if any, under the Act. The interest earned on employee's total contributions would be taxable as income from other sources in the hands of the employee.

When the employee has rendered more than five years of continuous service

In this case, the entire accumulated balance received by an employee would be exempt from tax under the Act.

Recently, Government of India has passed following four new labor codes which will replace existing 29 central labor laws. They will come into force from the date notified by Central Government:

- The Code on Wages, 2019
- The Code on Social Security, 2020
- The Occupational Safety, Health and Working Conditions Code, 2020

Industrial Relations Code 2020

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