

Nangia Andersen LLP



HOSPITALITY NEWSFLASH

Delhi Tribunal holds Hotel Chain marketing services not taxable as Royalty

April 2022



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Issue- Taxability of hotel chain related Sales & Marketing, sales promotion, and reservation services

Outcome- In favour of the assessee

Background

The Delhi Bench of Income Tax Appellate Tribunal (ITAT) in the case of **ITO (Intl. Taxation) vs. Asian Hotels North Ltd. (ITA No. 210/DEL/2016)**, ruled in favour of the respondent on the issue of taxability of centralised chain marketing services including advertisement, sales promotion and computerized reservation under the provisions of the Income-tax Act, 1961 (“the Act”). The Tribunal held that remittance made by the assessee in relation to centralized services provided under the Strategic Oversight Agreement (“SOA”) by the Hongkong entity outside India for advertisement, sales promotion and computer reservation are not made for consideration for any of the items (i) to (vi) enumerated in Explanation 2 to section 9(1)(vi) of the Act.

Brief Facts and Contentions

- The assessee is running a hotel under the name and style of ‘Hyatt Regency’ as a franchisee of Hyatt International Asia Pacific Limited known as Hyatt.
- The assessee has entered into SOA with Hyatt International South West Asia Limited (“HISWAL”) in respect of carrying out hotel and management services. As per the SOA various other services are required to be provided by other affiliates of Hyatt.
- One such affiliate is Hyatt Chain Services Ltd. (“HCSL”) which provide centralized services outside India to the worldwide Hyatt Group of Hotels, which works under the supervision and control of Hyatt. HCSL conducts sales and marketing on behalf of all hotels affiliated to the Hyatt chain.

- The cost of expenses incurred by HCSL is allocated amongst the participating Hyatt Hotels worldwide on cost basis without having any profit element. Hyatt franchisees across the globe contribute to HCSL on agreed basis and HCSL defrays the advertising and administrative expenses. Shortfall if any, is made up by the franchisees on pro-rata basis.
- In the application made under section 195 the assessee stated that it proposed to remit HCSL its contribution @ USD 425 per annum per guestroom and @1% of room revenue excluding food beverage and other service bill.
- The assessee contended that no tax is required to be withheld as remittance is towards the prorated share of sales and marketing services performed by HCSL outside India and no income accrues or arises in India. It was further contended that there is no profit element earned by HCSL and payments are only in the nature of reimbursement of expenses incurred by HCSL outside India.
- The AO, while issuing the withholding tax order, rejected the claim of the assessee, relied on earlier DRP's findings in the assessment of HISWAL and concluded that the proposed payments is in the nature of royalty/ FTS under the Act.
- The assessee filed an appeal with CIT(A) who held in the favour of the assessee that payment made by the assessee is limited to the recovery of actual cost of providing marketing services and no part of such service can be held as FTS. Further, it was also held that the reliance by AO on the findings of DRP in the case of HISWAL has no precedence value in the impugned case.

Income Tax Appellate Tribunal's order

- That HCSL is a separate independent no profit entity and providing services outside India to various hotels operated by Hyatt across the globe. That HCSL does not have a PE / business connection in India.





Nangia Andersen LLP's Take

The decision of Hon'ble Delhi ITAT once again reiterates/ confirms position of global hospitality players rendering centralized sales & marketing, sales promotion, reservation and other centralized services that such services are not taxable in India, not only under provisions of tax treaties providing restrictive definition of 'FTS', but also under the wider definition under Indian domestic tax law.

Thus, even when payment is made to a non-resident company based out of a non-tax treaty jurisdiction of Hong Kong (no treaty between India & Hong Kong existed during relevant year of dispute), the payments have been held to be not taxable.

Further, the Hon'ble Delhi ITAT has held such services to be non-taxable also on additional/ alternative argument of taxpayer that the services were provided to all participating hotels/ entities on actual cost basis, without any profit element. Thus, there should be no withholding in absence of an income element.

- That the Ld. CIT(A) has rightly held that the case of HISWAL has no application in the case of the Assessee. HISWAL and the assessee are separate legal entities and the findings in one case cannot blatantly be applied to the other.
- That the issue of taxability of provision of similar centralised sales & marketing, sales promotion and reservation services rendered by a foreign entity in the field of hospitality industry outside India is covered by decision of Hon'ble Delhi High Court in the case of **DIT vs. Sheraton International Inc (2009) 313 ITR 267** wherein it was held that such services are neither royalty nor FTS as per provisions of section 9 of the At and accordingly not liable to tax in India.
- Accordingly, the Delhi ITAT in the present case held as under:

“Respectfully following the decision (supra) we hold that the payments made to HSCL by the assessee are not in the nature of royalty under the provisions of the Act and thus not chargeable to tax and not requiring the assessee to withhold any tax on such payments.”
- Additionally, relying on decision of Hon'ble Delhi High Court in case of **CIT vs. Expeditors International (India) (P.) Ltd. [2012] 209 Taxman 18 (Delhi)**, Delhi ITAT in the present case also upheld the assessee's argument that in case of reimbursement/ cost recovery on actual cost without any element of income at all, the payments made to HSCL could not be said to be in the nature of income deemed to accrue or arise to India in the form of royalty or FTS.

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