RE-DISCUSSING THE ROYALTY PAYMENT ISSUE

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The DIPP is likely to bring a discussion paper for review of the proposal on 50% rise in royalty payments by Indian companies to their foreign partners or parents. So, essentially, the paper will invite comments on whether or not the royalty ceiling applicable till 2009 should be re-imposed. Know that until December 16, 2009, lump sum royalty payments were capped at $2 million. For the cases where there were no flat rates, royalty payment for technological collaboration was capped at 5% of the domestic sales and 8% of exports. Further, for the usage of a brand name, royalty could be paid up to 1% of sales and 2% of exports. Beyond these levels, approval of the Foreign Investment Promotion Board was required.

PSA view – Seeing the great increase in payments to foreign companies in royalty payments, DIPP is mooting the present step. The outflow of royalties has increased as most of the sectors have been opened for foreign investment or cap increased. In the budget of FY 2013-2014, the withholding tax on royalties paid by Indian companies to their foreign parents was increased from 10% to 25% but an exception was carved out for those companies with which India has double taxation avoidance treaty. As India has this treaty with more than 80 countries the increase in tax rate had no implication. Further, the new Companies Act, 2013 has tried to tighten the rules on royalty payments, wherein section 188 has made it mandatory that all related-party transactions be passed through a special resolution, requiring consent of 75% of minority shareholders.

Increase in license fee on ISP

TRAI has suggested increasing the license fee applicable on ISP from the existing 6% to 8%. According to TRAI, it will help the government plug loss of revenues accruing to it from ISPs who have not yet rolled out services, despite obtaining the spectrum in 2010. TRAI has also suggested a new definition of revenue for ISPs on which the government should levy 8% annual fee. ISP licenses must cover all kinds of revenue from internet services, allowing for only deductions available for pass through charges and taxes/levies like in the case of access services, without any set-off for expenses.

PSA view – TRAI had earlier recommended that the government should levy 8% license fee from April 1, 2013 but there were some questions raised on revenue items that should be considered for calculating final charges. The flip side of raising the license fee can be adverse on ISP which are already losing revenues to mobile operators, such step could further hurt their profitability in near future as well.

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