

Tax Hotline

April 15, 2019

TAXING CROSS-BORDER PRODUCTION ACTIVITIES – CONTRACT LANGUAGE RE-EMPHASIZED

- Line producer not an intermediary - held to be providing services on a principal to principal basis
- Costs paid to pure agent for procurement of goods and services to be part of service fees of pure agent if the invoices for such goods and services are in the name of the pure agent
- Services provided by Indian line producers to offshore clients may qualify as GST free export of services

A recent tax ruling¹ by the West Bengal Authority for Advance Rulings (AAR) has interesting takeaways for Indian film producers that wish to appoint offshore line producers / producers.

Following the introduction of the Goods and Services Tax (GST) in India, tax authorities and courts have increasingly relied on the wording of key contract terms to tax cross-border supplies of goods and services. The ruling has re-emphasized the need to have robust contractual terms in place to mitigate tax risks arising from a potential re-characterization of transactions by tax authorities and courts.

FACTS OF THE CASE

The ruling arose out of an application for advance ruling filed by Udayan Cinema (Applicant), an Indian entity involved in feature film production.²

In this case, the Applicant proposed to shoot feature film at locations outside India. For this purpose, the Applicant sought to appoint CDI Virtual Films Inc (CDIVF), a foreign entity, as a line producer in Brazil, and sought an advance ruling on two points:

- whether the Applicant would be liable to pay Integrated Goods and Services Tax (IGST) on reverse charge on payments to be made to CDIVF; and
- whether any reimbursements made to CDIVF on an actual cost basis would also be subject to IGST.

As per the terms of the proposed contract between the Applicant and CDIVF, CDIVF was to “facilitate the provisioning” of production services in Brazil and the Applicant was to reimburse CDIVF the cost of procuring these services based on bills raised by the service providers, bearing the name of the feature film. CDIVF was to hire local actors in Brazil, procure insurance cover for the crew originating and residing in Brazil, and also hold insurance to cover all accidents and injuries during the production of the film in Brazil. CDIVF was entitled to retain all production rights and talent buyouts for production in Brazil as security, till final payment of all amounts due to it under the proposed contract.

APPLICANT’S ARGUMENTS ON TAXABILITY

The Applicant chiefly argued that CDIVF was supplying “intermediary services” by facilitating the supply of goods and services (such as crew accommodation, supply of food, props, and ancillary services like renting of shooting locations etc.) by third party foreign suppliers to the Applicant. Under GST law, an “intermediary” is any person who arranges or facilitates the supply of goods or services or both between two or more persons, but not including a person who supplies such goods or services or both on his own account. The Applicant submitted that CDIVF satisfied this definition as it could not alter the nature of services supplied by foreign suppliers, and since the Applicant knew in advance the amounts that were to be charged to it by each foreign supplier, in as much as the budgeted amount was shared with the Applicant in advance by CDIVF. Under GST law, the place of supply of intermediary services being the location the supplier (i.e., the location of the intermediary), the Applicant argued that GST would not be applicable on the services supplied by CDIVF to the Applicant as the service should be deemed under law to have been provided outside India.

In the alternative, the Applicant argued that CDIVF would be acting as “pure agent” for GST purposes, since the contract expressly provided for the Applicant to reimburse CDIVF at cost based on bills raised by third party service providers in the name of the feature film. For GST purposes, a “pure agent” is one who while making a main supply to the recipient, also receives and incurs expenditure on some other supply on behalf of the recipient and claims reimbursement at cost for such other supply from the recipient. Thus, while the relationship between the supplier and the recipient in respect of the main supply is on a principal to principal basis, the relationship between them in respect of the other supply is that of a pure agent. A classic example of pure agency is the relationship between an importer and a customs broker – the expenses incurred by the customs broker in clearing the importer’s goods (such as transport charges, customs duties, warehousing charges etc.) are typically reimbursed at cost by the importer. Expenditure incurred by a supplier in its capacity as a pure agent of the recipient becomes relevant for determining the value of supply for levy of GST. The valuation rules under GST provide for such expenditure to be excluded from the value of supply, provided all conditions for classification as a pure agent are satisfied by the supplier.

RULING OF THE AAR

Research Papers

The Tour d’Horizon of Data Law Implications of Digital Twins

May 29, 2025

Global Capability Centers

May 27, 2025

Fintech

May 05, 2025

Research Articles

2025 Watchlist: Life Sciences Sector India

April 04, 2025

Re-Evaluating Press Note 3 Of 2020: Should India’s Land Borders Still Define Foreign Investment Boundaries?

February 04, 2025

INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

Audio

CCI’s Deal Value Test

February 22, 2025

Securities Market Regulator’s Continued Quest Against “Unfiltered” Financial Advice

December 18, 2024

Digital Lending - Part 1 - What’s New with NBFC P2Ps

November 19, 2024

NDA Connect

Connect with us at events, conferences and seminars.

NDA Hotline

Click here to view Hotline archives.

Video

Vyapak Desai speaking on the danger of deepfakes | Legally Speaking with Tarun Nangia | NewsX

April 01, 2025

The AAR ruled against the Applicant on both counts. On the first count, the AAR, after undertaking a detailed analysis of the responsibilities and functions of a line producer, ruled that a line producer's job was not limited to arranging or facilitating the provisioning of services to the main producer, but involved assisting and collaborating with the film crew in the physical production of the motion picture. Referring to the terms of the proposed contract, the AAR noted that CDIVF could not retain production rights and talent buy-outs as security *unless* it was engaged in the production and realization of a motion picture. This meant that the line producer was supplying motion picture production services on his own account and not as an "intermediary".

On the second count, the AAR noted that the proposed contract did not specify CDIVF to be a pure agent of the Applicant. Instead, it merely recorded that bills for services procured by CDIVF were to bear the name of the feature film and would be paid on an actual cost basis. In the AAR's opinion, the crucial test of pure agency was whether these services would be a charge on CDIVF or the Applicant. Given that CDIVF was to hold the production rights as security, the AAR ruled that all procurements of goods and services would be a charge on CDIVF, *unless specifically excluded*, and the fact that the bills raised for such goods and services were to bear the name of the feature film and not the Applicant corroborated this conclusion. The AAR also noted that the proposed contract did not specify what separate services, if any, CDIVF was supplying to the Applicant *in addition to the ones* for which it was purportedly acting as a pure agent. The AAR stated that if CDIVF was acting only as an intermediary between the Applicant and third-party service providers, the value of its service, being a fee or commission for arranging such services, should be clearly identifiable in the contract between the Applicant and CDIVF. Accordingly, the AAR ruled that CDIVF was not acting as a pure agent of the Applicant and hence reimbursements given to CDIVF would not be deductible from the value of supply for levy of GST.

KEY TAKEAWAYS AND PLANNING POINTS

While several recent rulings on export of goods and services have highlighted the tax risks arising from mischaracterization of outbound supplies (largely resulting in re-characterization of export supplies as domestic supplies), there has been comparatively little jurisprudence on taxation of supplies characterised as imports.

The present ruling has changed that trend and once again re-emphasized the need for careful consideration of key contract terms to prevent tax authorities or courts from applying an interpretation resulting in adverse tax consequences, particularly in a cross-border scenario. While the risk of re-characterization may seem greater in the context of digital transactions and evolving business models, the present ruling aptly illustrates how even established business arrangements could continue to face tax exposure in India, in the absence of clear documentation. To prevent such tax exposure, parties should ensure that contract clearly and adequately demarcates the functions performed and risks assumed, and identifies the nature, purpose, and quantum of consideration payable thereunder. If the same entity is discharging multiple functions, then separate consideration ought to be allocated.

Thus, in an "intermediary" context, the contract between the intermediary and the recipient should clearly identify that the purported intermediary would not be supplying any goods or services on its own account (i.e., on a principal to principal basis), but only be arranging or facilitating supplies between the recipient and third-party suppliers of goods and services. The payment arrangement between the purported intermediary and the recipient should clearly reflect this relationship with the payment terms in the case of a pure agent or intermediary arrangement demarcating the sums payable towards fees and costs separately.

Similarly, to establish pure agent status, the contract between a purported pure agent and the recipient should clearly identify the services for which the former would be acting as a pure agent of the latter, in addition to clearly delineating the services being provided on a principal to principal basis. The payment made by the pure agent on behalf of the recipient should be separately identified in the invoice issued by the pure agent to the recipient, and all bills from third-party service providers should be raised in the name of the recipient, and not the pure agent. The pure agent should not hold or intend to hold any title to the goods or services so procured or use such goods or services for its own interest and should only receive the actual expense incurred for procuring such goods or services as reimbursement.

Separately, with respect to the findings of the AAR on the service provided by a line-producer constituting a service on its own account (as in the facts of present case), the consequence could be a benefit to line-producers having similar arrangements with offshore producers as it should now arguably qualify as an export of services and therefore not be subject to GST.

— Anandu Unnikrishnan, Meyyappan Nagappan & Gowree Gokhale
You can direct your queries or comments to the authors

¹ Udayan Cinema (P.) Ltd., In re, [2019] 103 taxmann.com 219 (AAR-West Bengal).
² An advance ruling is a pre-assessment mechanism to determine an applicant's tax liability in relation to any supply of goods or services or both being undertaken or proposed to be undertaken by it. Advance rulings are binding on the applicant as well as the tax authorities and are intended to avoid long drawn and expensive litigation at a later date

DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.