

Tax Hotline

January 03, 2004

INDIAN BOARD OF DIRECT TAXES CLARIFIES TAXATION OF BPO COMPANIES IN INDIA

The Ministry of Finance ("**Ministry**") vide Circular No. 1/2004 dated January 2, 2004 ("**Circular**") has clarified the extent to which global profits of a non-resident enterprise is to be attributed to the activities of the BPO unit in India in various circumstances. In order to take the benefit of cost arbitrage and skilled labor available in India, many global companies have outsourced their business processes such as answering sales related queries, procurement of orders for sale of goods/provision of services, software maintenance service, debt collection service, software development service, credit card/mobile telephone related service, etc. to India. The Circular clarifies that the manner and extent of attribution of profits to the Indian BPO unit will depend on the facts of each case and the nature of services rendered by the BPO unit. Further, the same has to be determined in accordance with the provisions of the applicable tax treaty and the domestic law. In a case where a non-resident carrying on manufacture and sale of goods or provision of services outside India, outsources some of its activities such as conclusion of contracts and procurement of orders to a BPO unit in India, which constitutes a permanent establishment of the non-resident principal, no income shall separately accrue or arise to the non-resident principal in India provided BPO unit is compensated on arm's length/fair market price for the same. Examples of such services could be the services provided by:

- a) an Indian call centre unit engaged or set up by a foreign company manufacturing and selling computers to customers abroad to procure orders from customers abroad and to answer sales related queries on telephone;
- b) an Indian call centre unit appointed or set up by a foreign insurance company insuring risks in countries other than India to attend to calls from customers outside India regarding acquisition of new insurance policy or revision of existing policy, to disseminate relevant information and accept insurance proposals from the customers, while actual policy issuance as well as collection of premium is done outside India by the foreign insurance company; or
- c) an Indian call centre unit appointed or set up by a foreign credit card company issuing credit cards to customers living in countries other than India to attend to calls from customers outside India seeking to acquire a new credit card, disseminate relevant information and accept the request for issue of a credit card from the customer, while the actual card issuance, the delivery of the card and collection of charges are being done outside India by the foreign credit card company.

On the other hand, where a foreign company outsources the whole or part of its core revenue generating business activities such as the services of a travel agent, software developer, software maintenance, investment consultant, debt collection service, etc. to a BPO unit in India and the BPO unit renders the services either directly to the customers abroad or through the non-resident principal, then profits attributable to the BPO unit in India would be taxable in India if Indian BPO unit constitutes a permanent establishment of the foreign company in India. It appears that the Circular instead of clarifying a simple proposition that there should not be any additional attribution of profits to India in the event that the Indian BPO unit constitutes a permanent establishment of the foreign company provided the relation between the parties is at arm's length, has complicated the issue by classifying the services into core and non-core which would create more uncertainty as regards tax implication of such activities in India.

Source: Circular no. 1/2004 dated the January 2, 2004

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