2022 (9) TMI 436 - CESTAT NEW DELHI

COMMISSIONER OF SERVICE TAX, DELHI-II VERSUS M/S. FUTURE BRANDS

SERVICE TAX APPEAL NO. 53304 OF 2015

Order No. - FINAL ORDER NO. 50819/ 2022

Dated: - 8-9-2022

Levy of service tax - right to use component of the Trademark License Agreement - grant of license under the Trademark License Agreement would amount to deemed sale under article 366 (29A) of the Constitution, or not - period of dispute in the present appeal is from 2008-009 to 2013-14 - HELD THAT:- It can safely be said that under Sales Tax, there is transfer of possession and effective control in goods, while there is no such transfer of possession and effective control under Service Tax.

A perusal of the terms of the Trademark License Agreement dated August 27, 2008 and the Retail License Agreement executed on October 01, 2007 would show that there is a noticeable difference between the two. In the case of the Retail License Agreement only a non-exclusive and non-transferrable license to use the trademark was granted by the respondent to Pantaloon. Pantaloon also agreed that the respondent would have the right to control the standard and quality of the products. There is also no restriction in granting the license to others during the license period. This agreement is clearly, therefore, outside the purview of article 366 (29A) (d) of the Constitution that defines tax on the sale or purchase of the goods. Service tax would, therefore, be chargeable.

However, in the case of the Trademark License Agreement an exclusive license to use the trademark in any manner during the term of the agreement was granted. Such a license could not be granted to any other person during the period of the agreement. This would clearly fall within the meaning of the phrase “transfer of right to use the goods” and would be covered by article 366 (29A) (d) of the Constitution. Service Tax would, therefore, not be payable.

The Principal Commissioner, therefore, committed no illegality in holding that service tax could not be levied on the “right to use” component of the Trademark License Agreement - Appeal dismissed.

Judgment / Order

MR. DILIP GUPTA, PRESIDENT AND MR. P V SUBBA RAO, MEMBER (TECHNICAL)

Shri Ravi Kapoor, Authorized Representative for the Department

Shri Kumar Visalaksh, Shri Udit Jain and Ms. Surbhi Jain, Advocates for the Respondent

ORDER

The Commissioner of Service Tax, Delhi-II [**the Commissioner]** has filed this appeal to assail the order dated May 18, 2015 passed by the Principal Commissioner of Service Tax, New Delhi [**the Principal Commissioner**], by which the show cause notices dated April 24, 2014 and April 22, 2015 have been discharged. The show cause notices had been issued to M/s. Future Brands Ltd [**the respondent**] alleging therein that the respondent had not paid service tax on the “right to use” component of the

Trademark License Agreement executed on August 27, 2008 between the respondent and Pantaloon Retail (India) Ltd [**Pantaloon**] for brand 'Ajile'.

2. The Principal Commissioner, by the impugned order dated May 18, 2015, dropped the show cause notice for the reason that the grant of license under the Trademark License Agreement would amount to deemed sale under article 366 (29A) of the Constitution and, therefore, could not be subjected to levy of service tax. In support of his contention, the Principal Commissioner placed reliance upon the judgment of the Supreme Court in Bharat Sanchar Nigam Ltd. vs Union of India [**2006 (2) S.T.R. 161 (S.C.)**].

3. Shri Ravi Kapoor learned authorised representative appearing for the Department made the following submissions:

(i) The respondent had intentionally and deliberately bifurcated the gross value into two heads of royalty and right to use and had deliberately paid VAT on this portion of right to use in order to avoid paying service tax the rate of which was on the higher side as compared to VAT;

(ii) Bifurcation of income in two heads of royalty and right to use is arbitrary. Permission to use the brand is strictly according to the licensor's guidelines and any benefit of goodwill created by licensee's use is mandated to flow back to the licensor; and

(iii) Further, the fee payments towards license fee and additional license fee and terms and conditions do not indicate any consideration for sale. In this connection reliance has been placed on Eicher Good Earth.

4. Kumar Visalaksh learned counsel appearing for the respondent however supported the impugned order and made the following submissions:

(i) The transfer of right to use the Trademark on an exclusive basis, would qualify as 'deemed sale' under article 366 (29-A) of the constitution, thereby attracting the levy of VAT. Such transfer would be outside the purview of service tax;

(ii) An agreement is required to be read in a manner that it reflects the true intension of the parties thereto as regards the consideration agreed to be paid in return for the activities carried out under the agreement;

(iii) Service tax and VAT exclude each other and cannot be levied concomitantly on a transaction;

(iv) Incorporeal property such as 'trademarks' constitutes 'goods' for the purpose of the levy of VAT; and

(v) As for as the demand of Rs. 10,01,258/- for period April 2008 to September 2008 is concerned, thus it is beyond the limitation period of five years and hence, excludable.

5. In order to appreciate the submissions advanced by the learned authorized representative appearing for the Department and the learned counsel appearing for the respondent, it would be appropriate to refer to the relevant clauses of the aforesaid Trademark License Agreement dated August 27, 2008 between the respondent (referred to as the licensor in the Agreement) and Pantaloon Retail (India) Ltd. (referred to as the licensee in the Agreement). The relevant clauses are reproduced below:

"RECITALS:

A. WHEREAS, the Licensor is the proprietor of the Trademarks set out in Schedule 1 hereto ("Trademarks") and applied for in respect of the classes of goods detailed therein; and

B. WHEREAS, the Licensee wishes to use the "Trademarks on an exclusive basis, in connection with the Products (defined below) manufactured by the Third Party Manufacturer and sold by the Licensee.

NOW THEREFORE, in consideration of, and subject to, the mutual covenants, agreements, terms and conditions herein contained, the Parties agree as follows:

xxxxx xxxxx

3. GRANT OF LICENSE

3.1 Grant of License

3.1.1 The Licensor grants to the Licensee, an exclusive license to use the Trademarks in any manner during the Term of this Agreement, on the terms set out in this Agreement.

3.1.2 The Licensee hereby acknowledges and agrees that any goodwill created by the Licensee's exclusive use of the Trademarks shall inure to the sole and exclusive benefit of the Licensor.

3.1.3 The Licensee hereby agrees that the Trademarks shall not be used by the License in any manner prejudicial to the interest of the Licensor.

3.1.4 For the avoidance of doubt, the Trademarks licensed hereunder are exclusively licensed for use.

3.1.5 During the Term of this Agreement, the Licensor shall not grant to any third party, including any Future Group Companies, the license to use or enjoy the Trademarks in any manner.

3.1.6 During the Term of this Agreement, the Licensor shall not use or enjoy the Trademarks in any manner.

xxxxx xxxxx

5. LICENSEE'S RIGHTS AND OBLIGATIONS

5.1 The use of Trademarks by the Licensee shall be in conformity with the recommended brand usage guidelines. The brand usage guidelines as on the Effective Date are set out in Schedule 3 to this Agreement.

5.2 In the event that the Products are not in conformity with the brand usage guidelines, the Licensee shall take necessary steps to align the use of the licensed Trademarks with such guidelines. In the event the use of the Trademarks remain in non-compliance with the brand usage guidelines, even after the License has taken all necessary steps, the License shall cause the Trademarks to be permanently removed from such Products and/or any Packaging and Labels in relation thereto, prior to the distribution or sale or shall cause such Products and/or any Packaging and Labels in relation thereto be destroyed at the sole cost of the Licensee.

5.3 The Licensee agrees to retain test, process and final inspection records on Products bearing the Trademarks for the duration of the time stipulated by the Applicable Law but at least for a period of five five(5) years.

5.4 The Licensee shall during the Term of the Agreement maintain records of all Products manufactured, promoted, distributed or sold under the Trademarks.

5.5 The Licensee shall be entitled to use the Trademarks on an exclusive basis, in accordance with the terms of this Agreement and shall not allege and/or claim any rights, title, interest in or to the said Trademarks by virtue of the use of the Trademarks by the Licensee."

6. A similar Trademark License Agreement was executed between the respondent and Future Value Retail Limited for brand 'Srishti'.

7. It would also be appropriate to note that a Retail License Agreement was also executed on October 01, 2007 between the respondent and Pantaloon for brand "Dreamline". Under this Agreement, a non-

exclusive, non-transferable license to use the Trademark was granted by the respondent to Pantaloon. Clause-V of this Agreement relates to Quality and Control. It stipulates that Pantaloon agrees that the respondent has the right to control the standards and quality of the products in connection with which the Trademarks are used by Pantaloon and that Pantaloon also agrees that it will manufacture the products in accordance with such minimum quality standards and manufacturing specifications as the respondent may furnish or fix from time to time.

8. The period of dispute in the present appeal is from 2008-009 to 2013-14 and in connection with the Trademark License Agreement, the respondent has produced details of the royalty component on which service tax was paid and the 'right to use' component on which service tax was not paid and only VAT was paid. The Chart is reproduced below:

Period	**Total Value (in Rs.)**	**Royalty (35%)**		**Right to use (65%)**	
		Value (in Rs.)	**Value (in Rs.)**	**Value (in Rs.)**	**VAT Paid (in Rs.)**
2008-09	162,255,994	56,789,598	6,223,926	105,466,396	4,218,656
2009-10	253,761,360	84,322,280	8,685,195	169,439,079	7,404,488
2010-11	331,249,642	115,939,193	11,941,737	215,310,449	10,765,522
2011-12	359,011,103	125,653,886	12,942,350	233,357,217	11,667,861
2012-13	317,865,761	111,253,016	13,750,873	206,612,745	10,330,637
2013-14	254,629,232	154,141,761	19,051,922	100,487,471	5,024,374
	1,678,773,091	**648,099,734**	**72,596,002**	**1,030,673,357**	**49,411,538**

9. The learned authorized representative appearing for the appellant submitted that the "right to use" under the Trademark License Agreement had not been transferred in absolute and unrestricted terms and the legal right of possession and effective control remained with the respondent. Therefore, there was no 'deemed sale' and in support of his contention learned authorized representative placed reliance upon the decision of the Tribunal in Eicher Good Earth Ltd. vs Commissioner of Service Tax, New Delhi [**2012 (28) S.T.R. 279 (Tri.-Del.)**].

10. Learned counsel appearing for the respondent, however, supported the impugned order and submitted that on a careful analysis of the terms of the Trademark License Agreement and the decision of the Supreme Court in BSNL, it is clear that the Agreement seeks to transfer the 'right to use' in terms of paragraph 91(d) of the said judgment. Learned counsel submitted that the transfer of 'right to use' of Trademark on an exclusive basis would qualify it as 'deemed sale' under article 366(29A) of the Constitution thereby, attracting levy of VAT and would consequently be outside the purview of service tax.

11. To appreciate, whether service tax can be levied on the transaction, it would be necessary to analyse the relevant statutory provisions as they existed prior to 01.07.2012 and after 01.07.2012.

12. Section 65(55a) of the Finance Act 1994 [**the Finance Act**] defines 'intellectual property right' as follows:

"means any right to intangible property, namely, trade marks, designs, patents or any other similar intangible property, under any law for the time being in force, but does not include copyright;"

13. Section 65(55b) defines 'intellectual property service' as follows:

"intellectual property service' means:-

(a) transferring temporarily; or

(b) permitting the use or enjoyment of,

any intellectual property right;"

14. Taxable service 'under section 65(105)(zzr) of the Finance Act means any service provided or to be provided:

"……

(zzr) to any person, by the holder of intellectual property right, in relation to intellectual property service;"

15. For the period post 01.07.2012, section 65B (44) defines service as follow:

"**65B (44)** "service" means any activity carried out by a person for another for consideration, and includes a declared service, but shall not include-

(a) an activity which constitutes merely,-

(i) a transfer of title in goods or immovable property, by way of sale, gift or in any other manner; or

(ii) such transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of clause (294) of article 366 of the Constitution; or

(iii) a transaction in money or actionable claim"

16. Section 66E of the Finance Act deals with 'declared services' and the relevant portion is reproduced below:

"66E. The following shall constitute declared services, namely:-

……

(c) temporary transfer or permitting the use or enjoyment of any intellectual property right;"

17. The relevant clauses of the Trademark License Agreement have been reproduced above. Clause-3 deals with grant of license. Under it, the licensor has granted to the licensee an exclusive license to use the Trademark in any manner and during the term of the Agreement the licensee shall not grant to any third party, including any Future Group Companies, the license to use or enjoy the Trademarks in any manner nor will the licensor use or enjoy the Trademark in any manner.

18. The dispute in the present appeal relates to Trademarks License Agreement and is particularly on the 'right to use' component of the Agreement, which is to the extent of 65 per cent and not on the Royalty component, which to the extent of 35 per cent. The respondent contends that on the 'right to use' component value, it has regularly paid VAT, as it would amount to a deemed sale under article 366 (29A) of the Constitution and, therefore, no service tax is leviable.

19. In this connection, it would be pertinent to refer to Entry 54 of List II of the Seventh Schedule to the Constitution. It empowers State to levy tax on sales and purchase of goods. The relevant Entry is reproduced below:

"**54**. Taxes on the sale or purchase of goods other than newspaper, subject to the provisions of Entry 92 A of List I"

20. The forty-sixth amendment to the Constitution extended the meaning of "sale or purchase of goods" by giving an inclusive definition to the phrase "tax on the sale or purchase of goods" under article 366(29A) of the Constitution. The same is reproduced below:

"**366(29A)** "tax on the sale or purchase of goods" includes-

(a) a tax on transfer, otherwise that in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;

(b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of works contract;

(c) a tax on the delivery of goods on hire purchase or any system of payment of installments;

(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

(e) ……

(f) ……"

(emphasis supplied)

21. It would be seen from the aforesaid that the Constitution empowers the State to levy Sales Tax/VAT on transactions in the nature of transfer of right to use goods, which were earlier not exigible to sales tax as such transactions were not covered by the definition of "sale" as given in the Sales of Goods Act, 1930.

22. It needs to be remembered that the term "transfer of right to use goods" has neither been defined in the Constitution nor in any of the State VAT Acts or Central Sales Tax Act. The said phrase was interpreted by the Supreme Court in Bharat Sanchar Nigam Ltd., wherein the Supreme Court laid down five attributes for a transaction to constitute a "transfer of right to use goods". Paragraph 91 of the judgment, which deal with this aspect, is reproduced below:

"91. To constitute a transaction for the transfer of the right to use the good, the transaction must have the following attributes:

a. There must be goods available for delivery;

b. There must be consensus ad idem as to the identity of the goods;

c. The transferee should have a legal right to use the goods-consequently all legal consequences of such use including any permission or licenses required therefore should be available to the transferee;

d. For the period during which the transferee has such legal right, it has to be the exclusion of the transferor this is the necessary concomitant of the plain language of the statute- - viz. a 'transfer of the right to use' and not merely a license to use the goods;

e. Having transferred the right to use the goods during the period for which it is to be transferred, the owner cannot again transfer the same rights to others."

(emphasis supplied)

23. It can safely be said that under Sales Tax, there is transfer of possession and effective control in goods, while there is no such transfer of possession and effective control under Service Tax.

24. The Principal Commissioner, after analyzing the provisions of the Agreement, and the decision of the Supreme Court in BSNL observed as follows:

> "62. On going through the submissions and the observations of the Hon'ble Supreme Court, **it is clear that in the case of Retail License Agreements what is granted by the noticee is merely a license to use the goods. In such a case the noticee is not debarred from permitting the same license to others during the license period.** Therefore, such agreements are outside the purview of under Clause (d) of Article 366 (29-A) and are chargeable to service tax under List I of the said Seventh Schedule. **However, in the case of Trademark License Agreements, the language of the agreements provides the license in an exclusive manner to a customer and thus it bars the noticee from transferring the same right to some other person during the period of agreement. As has been clarified by the Hon'ble Supreme Court the latter type of agreement would clearly fall within the phrase of "transfer of right to use the goods". Thus, such a transfer agreement will definitely covered the said Clause (d) of Article 366 (29-A) of the List 2. xxxx xxxx xxxx. Therefore, in my view the noticee is correct in such cases of agreements service tax would not be chargeable**. Royalty is the payment for use of copyright owned by somebody else and this is not a transfer of right to another person. Therefore, the service tax very much leviable on that part, which the noticee has been doing. Therefore, issuance of two invoices (i.e. ST invoice for royalty and VAT invoice for right to use) is the proper way of observing the State as well as the Union law.
>
> 63. There is no doubt that as pointed out in para 19 of the show cause notice the noticee is the sole owner as proprietor of trademark, is solely responsible for brand promotion and maintenance of brand image, can terminate the agreement by giving notice and that there is no apparent sale in the instant case. However, as pointed out by the noticee and explained by the Hon'ble Supreme Court the said Clause (d) of Article 366 (29-A) created a legal fiction where activities that would normally not consider as sale and purchase of goods would be treated so on account of this special definition, therefore, the transfer of right to use may be revocable and temporary and does not divests the noticee from their ownership over the rights, nonetheless it is sale or purchase of goods because of the said constitutional provision. **Therefore, the ground on which the show cause notice has proceeded to demand is not supported by the law and needs to be rejected."**

(emphasis supplied)

25. A perusal of the terms of the Trademark License Agreement dated August 27, 2008 and the Retail License Agreement executed on October 01, 2007 would show that there is a noticeable difference between the two. In the case of the Retail License Agreement only a non-exclusive and non-transferrable license to use the trademark was granted by the respondent to Pantaloon. Pantaloon also agreed that the respondent would have the right to control the standard and quality of the products. There is also no restriction in granting the license to others during the license period. This agreement is clearly, therefore, outside the purview of article 366 (29A) (d) of the Constitution that defines tax on the sale or purchase of the goods. Service tax would, therefore, be chargeable.

26. However, in the case of the Trademark License Agreement an exclusive license to use the trademark in any manner during the term of the agreement was granted. Such a license could not be granted to any other person during the period of the agreement. This would clearly fall within the meaning of the phrase "transfer of right to use the goods" and would be covered by article 366 (29A) (d) of the Constitution. Service Tax would, therefore, not be payable.

27. The Principal Commissioner, therefore, committed no illegality in holding that service tax could not be levied on the "right to use" component of the Trademark License Agreement.

28. The appeal, therefore, deserves to be dismissed and is dismissed.

(Order Pronounced on 08/09/2022.)

Citations: in 2022 (9) TMI 436 - CESTAT NEW DELHI

1. 2006 (3) TMI 1 - Supreme Court
2. 2012 (4) TMI 104 - Cestat, New Delhi