

LEGAL OPINION

Querist: Public Service Broadcasting Trust

Subject: *Whether service tax is payable by the querist on the amount received in terms of the Memorandum of Understanding dated 19.01.2010 with Films Division of Govt. of India for production of documentary films? Whether fellowships received by independent film directors for making documentary films from the querist in terms of "PSBT-Films Division Film Fellowships Agreement" are exigible to service tax?*

1. The querist has sought my opinion as to whether the grant received from Films Division of Govt. of India, under the Memorandum of Understanding signed on 19.01.2010 for production of documentary films by commissioning independent film directors, is exigible to service tax. The querist has also sought to know as to whether the film directors are liable to pay service tax on the fellowships received by them as per the PSBT-Films Division Fellowship Agreement. For the purpose of this opinion, the querist has provided copies of the Memorandum of Understanding with Films Division and PSBT-Films Division Fellowship Agreement along with the following narration on its arrangement.

The Government is implementing a Plan scheme under the 11th 5 year plan to promote the "Production of documentary films" aimed at encouraging the independent documentary film movement in the country. The Plan funds earmarked for the purpose are allocated to the Ministry of Information & Broadcasting (Films Division) in the form of a grant and released to the PSBT (a not for profit organization) by the Films Division as a grant under an MOU dated 19th January, 2010 for production of documentary films. The objective of the scheme is clear from para 2 of the agreement which states "The main objective of the scheme is to encourage the documentary film movement in the country and in line with this decision, provide funds to Non-Governmental Organizations (not for profit organizations) working in

the field of documentary film production, for the production of quality, independent documentary films in a public private partnership mode”.

Further, it is also laid down in para 3 of the agreement that the Government will provide the broad list of subjects on which documentary films are to be produced with this Grant. The films are produced on social issues ranging from the environment, gender, poverty elimination, interfaith harmony etc.

PSBT after a rigorous selection process led by its distinguished Board of Trustees – who include three winners of the Dada Sahib Phalke Awards Shyam Benegal, Adoor Gopalakrishnan, Mrinal Sen & people like Fali Nariman, Kiran Karnik & Sunita Narain – awards Film Fellowships to talented individuals. More than 50% of these are starting out film makers. The Fellowships also ensure geographical representation and diversity amongst the talent pool from all over the country. Given the limited budget the productions are on low end technology, which virtually eliminates any real possibility of commercial revenues. In a competitive media market dominated by commercially driven entertainment content there is no space for educational & socially driven documentary films of art & conscience. Financial returns from these documentary films of art & conscience. Financial returns from these documentary films are a token 1 to 2% of the cost. The entire production process is closely mentored to help film makers develop their skills and give off their best. PSBT’s documentary films have so far won 18 national awards from the President of India for excellence; approx. 100 other awards have been secured from around the world.

In the background explained above, it is evident that these documentary films produced under the plan scheme are not intended to serve any commercial purpose.

Arrangement with Film Division

2. From the perusal of the Memorandum of Understanding dated 19.01.2010 and the explanation given by the querist, I notice the following features of the arrangement which are relevant for the issue at hand.
 - (a) The arrangement has been entered into to provide funds to non-Governmental organisations with an objective to encourage the documentary film production.
 - (b) Films Division is to provide a broad list of subjects, on which documentary films of 46 to 52 minutes in any major Indian language including English are to be produced, to the querist from independent directors.

- (c) The querist is to receive grants of specified amounts in the Financial Years 2009-10, 2010-11 and 2011-12 for which it is to submit certificate of utilisation of grants. The querist is to maintain separate account for the grants received and furnish to the Government audited annual accounts within 9 months from the end of the Financial Year.
 - (d) Films Division is to have copyrights and ownership of the films to be produced under the arrangement but the querist is having exclusive marketing right of the documentary films produced for 7 years. Revenue earned from sale of the documentary films are shared among the directors of the film, PSBT and Films Division. The Director and PSBT can have maximum 25% of the revenue earned from marketing of a documentary film. The querist has specifically explained that financial returns from these documentary films cannot be more than 1 to 2% of the cost.
3. From the note forwarded by the querist, it can be appreciated that Films Division is interested in promotion of production of documentary films in India and have no interest in the production of these films for commercial exploitation. In the memorandum of understanding the amount being given to the querist has been termed as “grant”, which is required to be passed on by the querist to the independent directors engaged for production of the films. The expression “grant” is normally understood in the government parlance as voluntary payment to support a cause or socially purposive objective. In the present case, the Films Division is providing the money for promoting the production of documentary films. The querist has intimated that the hardly 1 or 2% of the cost is being recovered from the sale of these documentaries. Hence, the amount paid by the Film Division is not a consideration for any services by the querist.

4 The CESTAT, in *APITCO Ltd. vs. CCE, 2010 (20) S.T.R. 475 (Tri.)*, has held that demand of service tax on grants-in-aid received from government for implementation of welfare schemes is not sustainable under the law as this is not a consideration for rendering any service to government. In *Indian Institute of Chem. Technology vs. CCE&ST, 2010 (17) S.T.R. 420 (Tri.)*, the Tribunal has noted the following Board's clarification wherein it has been clarified that grants or aids from the Government for conducting research/project work is not taxable.

6.***** In terms of the Board's Clarification dated 9-7-2001, the following clarifications has been issued.

Point raised for clarification	Clarification
Many public funded research institutions receive grants or aids from the Government for conducting research/project work. Whether such activities would be covered under the levy?	In the facts of this case, no service is rendered to anyone. Hence the question of payment of Service tax does not arise. However, if they render service to anyone on payment basis, service tax will be payable on such services.

In *Cultural Society of Angamally vs. CCE, 2007 (8) S.T.R. 25 (Tri.)*, the Tribunal has held that charitable donations and government/public grants excludible from taxable value for charging Service tax.

5. In the present case also, the querist is not receiving any consideration for rendering any service. It is merely receiving an amount to be utilised for production of documentary films on public interest issues through independent directors to promote the production of documentary film. For production of the documentary films, it is entering into "Film Fellowships Agreement" with an independent director, wherein it will pay an amount to the director as fellowship. Hence in this arrangement, the querist is receiving grant from the Government for promoting film culture on the given subject in India, and not as a consideration for rendering any service.

6. The Supreme Court in *TISCO General Office Recreation Club v. State of Bihar and Others, 2002 (126) STC 0547 (SC)* has considered the transaction wherein the difference between the income earned and the expenditure incurred by the dealer in running canteen for the employees of TISCO used to be made good every month by TISCO. The sales tax authorities had treated this subsidy given to the dealer as a part of the sale price and added it to the turnover and levied sales tax. The Supreme Court has held that this ex gratia payment is only as a measure of staff welfare and cannot be regarded as part of the sale price of the meals sold by the canteen to the employees and therefore not subject to sale tax. The Court observed as under:

For running the canteen different types of expenses are incurred and at the end of the month when the income and expenditure account is prepared the excess of expenditure over the income is made good by giving subsidy to the dealer. The subsidy so given cannot be said to be directly relatable to any item of food or goods sold. It is not possible to accept that the subsidies can possibly be regarded as valuable consideration in respect of sale or supply of goods.

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.....The expenses which are incurred which are relatable to the purchase of a taxable item may or may not be regarded as part of the purchase price but as far as the present case is concerned, lump sum payment which, in the very nature of things, is ex gratia cannot be regarded as being part of the sale price and consequently form part of the gross turnover of the dealer. There was no statutory obligation of TISCO to pay any amount to the dealer. It is only as a measure of staff welfare that ex gratia payment was made from time to time which, in our opinion, cannot be regarded as part of the sale price of the meals sold by the canteen to the employees.

The querist is not receiving any consideration from the government for rendering the service, but the grant for promoting production of documentary films in India by engaging independent directors. Therefore, there is no question of rendering taxable service for a consideration. Hence, no service tax is payable.

Taxable category

7. In addition to the above conclusion, I would like to clarify that production of film is not classifiable under any of taxable category. The querist is receiving grant from the Films Division, Govt. of India, for promoting production of documentary films. Hence, it cannot be said that the querist is rendering any business auxiliary service for the simple reason that Films Division is not engaged in any sort of business. The taxable categories which may be considered are programme production, video tape production and copyright service.

8. Finance (No.2) Act, 2004, has inserted this taxable service in Finance Act, 1994, with effect from 10.09.2004. Section 65 of the Finance Act, 1994, defines the 'programme', 'programme producer' and 'taxable service' as follows:

(86a) "**programme**" means any audio or visual matter, live or recorded, which is intended to be disseminated by transmission of electro-magnetic waves through space or through cables intended to be received by the general public either directly or indirectly through the medium of relay stations;

(86b) "**programme producer**" means a commercial concern which produces a programme on behalf of another person;

(105) "**taxable service**" means any service provided -
(zzu) to any person, by a programme producer, in relation to a program;

9. C.B.E.C., in its letter F.No.B2/8/2004-TRU dated 10.09.2004, has explained the scope of this taxable service as under:

Services provided by a TV or radio programme producer have been brought under the purview of taxable service. Any programme produced (or any service rendered in connection of producing such programme) by a commercial programme producer, for telecasting/radio transmission by a broadcaster would fall under this category of taxable service including cases where a programme is sold to the broadcaster. However, a service rendered by an employee of the service receiver (i.e. the broadcaster) or by an amateur photographer who, say, shoots a footage for himself, would not be charged to service tax.

10. There is no stipulation in the agreement that the film to be produced by the filmmaker will be shown on television. Hence, such film is not made specifically to be disseminated by transmission of electro-magnetic waves. The circular itself clarifies that any programme produced (or any service rendered in connection with producing such programme) by a commercial programme producer, for telecasting/radio transmission by a broadcaster would fall under this category of taxable service. Hence, activities of the querist cannot be classified under this category, even if its activities are considered as service.

Video-tape Production Service

11. “Video-tape production agency”. “video-tape production” and taxable service in relation to video-tape production has been defined in Finance Act 1994 as under:

65(82) “video production agency” means any professional videographer or any commercial concern engaged in the business of rendering services relating to video-tape production;

65(83) “video-tape production” means the process of any recording of any programme, event or function on a magnetic tape and editing thereof, in any manner;

65(72) “taxable service” means any service provided or to be provided-

(zi) to a client, by a video production agency in relation to video-tape production, in any manner;

12. “Video-tape production” has been defined as the process of any recording of any programme, event or function on magnetic tape and editing thereof, in any manner. Programme and function are organized activities having a preplanned course. Though “event” means any happening its meaning appearing in Section 65 (83) would be restricted to the context in which it appears. In order to understand the scope of service provided by a video-tape production agency, it is appropriate to apply the rule of construction *Noscitur A Sociis* to the expressions, “programme”, “event” or “function”. Under this rule of construction, the

meaning of a word is to be judged by the company it keeps. This rule, according to MAXWELL (see Interpretation of Statutes, 11th edition, P. 321), means that when two or more words which are susceptible of analogous meaning are coupled together, they are understood to be used in their cognate sense. They take as it were their colour from each other, that is, the more general is restricted to a sense analogous to a less general. The philosophy of this rule is that the meaning of the doubtful word may be ascertained by reference to the meaning of words associated with it.

13. Applying this interpretation to “programme”, “function” and “event”, it would mean that the meaning of “event” would take colour from the words, “programme” and “function”, in whose company it appears. The Shorter Oxford English Dictionary defines ‘programme’ as under:

A descriptive notice, issued beforehand, of any formal series of proceedings, as a festive celebration, a course of study, etc. – a definite plan of any intended proceedings.

The same Dictionary defines ‘function’ as –

An action of performing – a religious ceremony – a public ceremony, a social or festive meeting conducted with each ceremony.

This Dictionary defines ‘event’ as –

An incident, an occurrence; esp. an occurrence of some importance. One of the items in a programme of sports.

Black’s Law Dictionary defines ‘event’ as –

the consequence of anything; the issue or outcome of an action as finally determined; that in which an action, operation or series of operations terminated; noteworthy happening or occurrence; something that happens.

Hence, film production cannot be termed as the process of any recording of any programme, event or function. “Video Production Agency” has been defined to mean any professional videographer or any commercial concern engaged in services relating to video-tape production. A videographer is one who makes his earning by using his video camera. He is required to capture the happenings at a function or programme.

The video camera is only a tool for capturing the news. To a videographer the happening or event is assigned; he has to shoot the programme/function/event specifically chosen by the customer. This is not the querist's case. Hence, the service of a film production cannot be classified under this category.

Copyright Service

14. Finance Bill, 2010, has amended Finance Act, 1994, by inserting the sub-clause (zzzzt) in clause (105) of section 65 to levy service tax on temporary transfer or permitting the right to use or enjoyment of any copyright except the specified rights. The relevant provisions are reproduced below:

SECTION 65. Definitions – In this Chapter, unless the context otherwise requires,

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- (105) “taxable service” means any service provided or to be provided (zzzzt) to any person by any other person, for-
- (a) transferring temporarily or
 - (b) permitting the use or enjoyment of
- any copyright defined in the Copyright Act, 1957, except the rights covered under sub-clause (a) of clause (1) of section 13 of the said Act

15. Section 13 of this Act provides that copyright with respect to original literary, dramatic, musical and artistic works; cinematographic film and sound recording shall subsist throughout India subject to other provisions of the Act as follows:

13. Works in which copyright subsists:- (1) Subject to the provisions of this section and the other provisions of this Act, copyright shall subsist throughout India in the following classes of works, that is to say,-----

- (a) original literary, dramatic, musical and artistic works;
- (b) cinematograph films; and
- (c) sound recording.

Hence, transactions of temporary transfer or permitting the right to use or enjoyment of any copyright subsisting in cinematograph films and sound recording are being proposed to be taxed under this category.

CBEC in letter D.O.F. No.334/1/2010-TRU dated 26th February 2010 has explained the scope of this taxable category as follows:

7. Services related to two types of copyrights hitherto not covered under existing taxable service 'Intellectual Property Right (IPR)', namely, that on (a) cinematographic films and (b) sound recording.
- 7.1 The right to temporarily transfer or permit the use of Intellectual Property Rights (IPR), namely, trademarks, designs and patents was brought under tax net in 2004. However, one of the IPRs, i.e. copyright has been specifically kept out of the purview of the tax with an intent to encourage authors and artists, as it involves creative works, such as literary work, musical work and artistic work. In Budget 2008, Information Technology (IT) Software Service was also brought under tax net, which apart from involving development, up-gradation, assistance etc. also covered the IPR aspect i.e. right to use the information technology.
- 7.2 The provisions of copyright are incorporated in the Indian Copyright Act, 1957. As per section 13 of the said Act, the copyright subsists in the following classes of work:
 - (a) Original literary, dramatic, musical and artistic works;
 - (b) Recording of cinematographic films;
 - (c) Sound recordings.
- 7.3 The first category of copyright has been kept out of the tax net while the second and third categories of copyrights are being made taxable under this service. A cinematographic film means any work of visual recording on **any medium** (emphasis added) produced through a process from which a moving image may be produced. The same may be accompanied with sound reproduction also. Both the recording of the cinematographic film and the accompanying sound track are the property of the producer, who can temporarily transfer it or permit its use by another person for a consideration. It is this activity, which is being taxed under this service. It would have an impact on the royalty payments on both imported and indigenously produced films when the producer/right holder allows such use to another person, say the distributor.
- 7.4 Similarly, song, its music, lyrics and composition also enjoy the copyright protection to its owner who can commercially exploit it in the manner stated above. Normally, the copyright of music vests in the composer and the copyright of music recorded vests in the producer of the sound recording. It is possible that a lyricist or a singer may hold copyright for the words of a song or the song itself. Merely allowing that song to be recorded is a copyright, which would fall under category (a) of section 13 of the Copyright Act and thus would not be subject to service tax. However, after the performer has transferred his rights to a sound recording company, the sound recording company acquires the copyright mentioned in category (c) of section 13

supra. It is the transfer or allowing use of this right, which would be subjected to tax under the new service.

- 7.5 As such, depending upon the nature and conditions of the contract, companies distributing music, owners of copyright of cinematographic films etc. would be prospective taxpayers. It may be noted that this taxable service will not cover individual artists, composers, performers etc. as their copyrights fall under clause (a) of Sec. 13 of the Copyright Act.

16. From the above, it is clear that temporary transfer or permitting the right to use or enjoyment of any copyright of cinematographic will be taxable under this category. However, it is relevant to examine whether any transaction relating to copyright is envisaged in this transaction of the querist. The memorandum of understanding provides that copyright in the film to be produced will vest in Films division. Clause (b) of Section 17 of the Copyright Act, 1957, clearly provides that in case of cinematograph film made for valuable consideration at the instance of any person, such person shall, in the absence of any agreement to the contrary be the first owner of the copyright therein. The relevant provision is reproduced below:

17. **First owner of copyright:-** Subject to the provisions of this Act, the author of a work shall be the first owner of the copyright therein:

Provided that--

(a) in the case of a literary, dramatic or artistic work made by the author in the course of his employment by the proprietor of a newspaper, magazine or similar periodical under a contract of service or apprenticeship, for the purpose of publication in a newspaper, magazine or similar periodical, the said proprietor shall, in the absence of any agreement to the contrary, be the first owner of the copyright in the work in so far as the copyright relates to the publication of the work in any newspaper, magazine or similar periodical, or to the reproduction of the work for the purpose of its being so published, but in all other respects the author shall be the first owner of the copyright in the work;

(b) Subject to the provisions of clause (a), in case of a photograph taken, or a painting or portrait drawn, or an engraving or a cinematograph film made, for valuable consideration at the instance of any person, such person shall, in the absence of any agreement to the contrary, be the first owner of the copyright therein;

17. Hence, under the law, the producers are the first owners of the copyright in the films to be produced by fellowship director. The agreement provides that the Government will hold copyright in the films. Hence, there is no transaction relating to copyright in the proposed arrangement. Further, the Government will enjoy the copyright permanently which cannot be considered as temporary transfer or transfer of right to use copyright. Therefore, service tax is not payable by the querist under this category.

Fellowship to the Film Directors

18. In this arrangement, the querist is awarding Film Fellowships grant to the independent directors for making the documentary films. The agreement makes it clear that the persons who are directly engaged in making of the film are only entitled for the fellowship. The directors are to produce the films in consultation with the querist. The agreement further provides that all of the titles, interests and copyrights in all work developed or produced by the film director under this agreement shall be property of PSBT for seven years from the date of completion and thereafter, it shall be property of the Films Division. I understand that querist is granting the fellowship from the grant received from the Films Division. I have already noted that the querist has explained that these films are not having any substantial commercial value. Hence, for the same reason, it can be appreciated that the fellowship given by the querist is not the consideration for making film but ex-gratia payment to the film maker. Besides that I have already explained that the making of documentary film is classifiable under any of the taxable category. Hence, the film directors are liable for payment of service tax.

Conclusion

19. Films Division, Government of India, has entered into MoU with the querist, which is a non-profit making organisation with an objective to

encourage documentary film movement in the country as per the scheme “Production of Documentary Films”. Under this MoU, PSBT will receive grant for production of the documentary film on the subjects broadly specified by the Government. I find that the querist undertakes these activities and on the amounts invested in the venture, the films do not return more than 2% of the cost of production. Thus, it is actually an ex-gratia payment to the film maker. The Government does not intend to get anything of value, except for promoting cultural activities in the society. Hence, the amount received by the querist is only grant and not any consideration for rendering of service. Therefore, no service tax is payable by the querist. Besides this, the querist’s activity envisaged in the memorandum of understanding is not classifiable under any of the taxable categories. No service tax is payable by the querist on the grant received by it. For the same reasons, the film directors are also not liable for payment of service tax on the fellowship grants received by them from the querist.

Advised accordingly.

P. K. Sahu, Advocate
11th June, 2011

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