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SITG No. 194

Deputy Commissioner of Income-tax
Vs
Orange (formerly known as France Telecom)

Income received for inter-connectivity services being provided by a foreign company (NTO) to an Indian company for seamless communication outside India cannot be taxed in India as Royalty.

24.02.2024

Jain Shrimal & co

[2024] 158 taxmann.com 186 (Bangalore - Trib.)

Facts of the Case

- **The assessee, M/s. Orange (formerly known as France Telecom), is a foreign company, engaged in the business of provision of telecom services. During assessment year 2011-12, assessee company had received payment of Rs. 5,16,82,746/- from M/s. Vodafone South Limited (VSL) toward provision of telecom interconnect facility.**

- Proceedings u/s.201 were initiated in the case of VSL for the financial years 2009-10 to 2011-12 in respect of non-deduction of tax at source on payments made to its Non-Resident Telecom Operators (NTOs) for the provision of bandwidth capacity and for provision of interconnect services because AO considered it as Royalty/FTS u/s 9.

- Based on the proceeding u/s 201 of VSL, Ld. AO started proceeding against orange and therefore, added this receipt from VSL to the assessee's income in India as Royalty.

- **Aggrieved by the order of the Ld. AO**, assessee preferred appeal before the Ld. CIT (A).

- The **contention of assessee was accepted by Ld. CIT(A**) and aggrieved by the same revenue went in appeal before the honourable ITAT.

Revenue's Contention

Opposing the order passed by Ld. CIT(A) and the arguments presented by the Ld. Counsel of the assessee, the counsel for the Revenue, submitted the following:

- The processes were triggered from India, thereby making the source of such income accrue/arise out of India, for the NTOS to earn the income and the payments were made by the deductor by collecting it from the ultimate payer i.e., the end consumer in India for services rendered.

- The income accrued and arose in India at the time of the call being made and no receipt would be available for the Indian entity also in the event the call did not go through.

- On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has erred in relying on the decision of Hon'ble High Court of Karnataka, wherein the Hon'ble High court relied on the case of Engineering analysis as the reasoning of the case would not apply to the case on hand because retrospective amendments to section 9 of the act by insertion of Explanation 6 does not affect the definition of royalty. Moreover, the Engineering analysis case was rendered in the context of section 14 of the Copyright Act, 1957 whereas the Submarine cable system and the telecom network falls under the Patents Act, 1970.

Assessee’s Contention

- The **payment received** by the assessee **cannot be characterized as royalty or FTS, or business profits in India** since such **activities were not carried out in India** and the **payments to the NTOs are not made in the nature of use of process or equipment as mentioned in section 9(1)(vi)**.

- The **NTOs have no presence in India** whatsoever, and the A.O. has not deviated from the stated view. Hence, without any PE of NTOs in the country, such **income is not taxable within the Indian territory**.

- The Ld. Counsel of assessee has relied on the judgement of Hon’ble High court of Karnataka in case of Vodafone South and various other judgement of coordinate bench of this Tribunal and argued that such income earned by them in India is not taxable in India. Further, the word "process" thus must also refer to specie of intellectual property, applying the rule of, ejusdem generis or noscitur a sociis, as held by Hon'ble Supreme Court in case of CIT v. Bharti Cellular Ltd. [2010] 193 Taxman 97/[2011] 330 ITR 239.

Legal Provisions

According to **Section 9(1)(vi)** of Income Tax Act, 1961,

income by way of royalty payable by—

(a) the Government; or

(b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the royalty is payable in respect of any right, property, or information used or services utilized for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

***Provided** that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April 1976, and the agreement is approved by the Central Government :*

Legal Provisions

Provided further *that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a license) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development, and Training, 1986 of the Government of India*

Explanation 2, 4, 5 and 6 to Section 9(1)(vi) of Income Tax Act, 1961 suggests that

Explanation 2*— For the purposes of this clause, "royalty" means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for—*

(i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;

Legal Provisions

Explanation 4—*For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.*

Explanation 5—*For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not—*

(a) the possession or control of such right, property or information is with the payer;

(b) such right, property or information is used directly by the payer;

(c) the location of such right, property or information is in India.

Explanation 6—*For the removal of doubts, it is hereby clarified that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret;*

Ruling

- At no point of time, any possession or physical custody, control or management over any equipment is received by the end users/customers. It is also noted that the process involved in providing the services to the end users/customers is not "secret" but a standard commercial process followed by the industry players. Therefore the said process also cannot be classified as a "secret process", as is required by the definition of "royalty" mentioned in clause 3 of Article 13 of India-France DTAA.

- Shri. Pardiwala while presenting the case before Hon’ble High court in case of Vodafone South contended that the payments made by VSL cannot be treated as either Royalty or FTS or business profits as per section 9(1)(vi) of Income Tax Act as no part of the activity was carried out in India.

- Further, CIT(A) in case of assessee had held that since the payment made by VSL has been held by the Hon'ble High Court of Karnataka to not be royalty u/s 9(1)(vi) and on which tax was not supposed to be deducted, there is no ground for treating the same payment as the income of the appellant, given that there is no finding by the AO that the appellant had a Permanent Establishment in India and that this payment would be the appellant's business income. Therefore, the addition made by the AO of the amounts paid by VSL to the appellant towards interconnect charges is deleted.

Ruling

- Similar issue came up before Hon'ble Delhi Tribunal in case of Bharti Airtel Ltd. The issue considered therein was in respect of payment towards call interconnectivity charged for call transmission on foreign network. The Tribunal therein, on applying ratios pronounced in the above referred decisions, held it not as 'Royalty'. **Therefore in our opinion, the Payments made by the assessee in lieu of services provides by the assessee cannot fall within the ambit of 'Royalty' under section 9(1)(vi) Explanation 5 &6.**

- Further, It is an admitted fact that there is no transfer of any intellectual property rights or any exclusive rights that has been granted by the assessee to the service recipients for using such intellectual property. **Therefore Explanation 2 to section 9(1)(vi) cannot be invoked.**

- We are therefore of the opinion that the receipt of IUC charges cannot be taxed as Royalty under Article 13 in India of India-France DTAA. The payment received by the non-resident assessee amounts to be the business profits of the assessee which is taxable in the resident country and is not taxable in India under Article 5 of the DTAA as there is no case of permanent establishment of the assessee that has been made out by the revenue in India. Even Hon'ble High Court has in para 25, held that the non-resident service providers do not have any presence in India.

Various judgement also passed in favour of assessee in relation to IUC charges

- Based on the below mentioned judgement's we have ample amount of precedents to state that services in relation to inter connectivity cannot be considered as Royalty if the service is provided outside India:

  - **Telefonica Depreciation Espana SA v. ACIT (IT)/Deputy Commissioner of Income-tax (IT) -** [2023] 154 taxmann.com 436 (Bangalore - Trib.)[10-08-2023]

  - **Telefonica UK Ltd. v. Deputy Commissioner of Income-tax (International Taxation)** – [2023] 154 taxmann.com 475 (Mumbai - Trib.)/[2023] 203 ITD 171 (Mumbai - Trib.)[22-09-2023]

  - **Telecom Italia Sparkle Singapore Pte. Ltd. v. Deputy Commissioner of Income-tax (International Taxation) -** [2023] 155 taxmann.com 404 (Bangalore - Trib.)[31-08-2023]

  - **Al Telekom Austria Aktiengesellschaft v. Deputy Commissioner of Income-tax, (International Taxation)-** [2023] 156 taxmann.com 155 (Bangalore - Trib.)[25-08-2023]

Section/Article	Section 9(1)(vi)- Explanation 2,4,5 & 6 of Income Tax act read with Article 13 of DTAA.
DTAA/Country	India-France.
Court	Hon'ble Bangalore ITAT
Date of decision	22.12.2023

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