

**BEFORE THE AUTHORITY FOR ADVANCE RULINGS (INCOME TAX)
NEW DELHI**

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PRESENT

Hon'ble Mr. Mr. Justice P.V. Reddi (Chairman)

Mr A. Sinha (Member)

Mr. Rao Ranvijay Singh (Member)

- (Member)

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A.A.R. NO. 786 OF 2008

Name and Address of Applicant

Cable & Wireless Networks India Private Limited
Unit 2(B) Creator Building, International Tech Park, Whitefield Road, Bangalore

Commissioner concerned

Director of Income Tax (International Taxation), Bangalore

Present for the Department

Mr.Narendra Kumar, Addl.DIT (Intl. Taxation), Bangalore

Present for the Applicant

Mr.N.Venkatraman, Sr.Advocate

RULING

(By Mr. A. Sinha)

This application has been filed under section 245Q(1) of the Income-tax Act, 1961 (the Act) by Cable & Wireless Networks India Private Limited. The applicant is a company incorporated in India and is a part of the Cable and Wireless Groups of Companies. It is engaged in the business of providing international long distance and domestic long distance telecommunication services in India. **The applicant proposes to enter into an agreement with another group company, namely M/s Cable and Wireless UK (C & W UK) with a view to providing end to end international long distance telecommunication services to its Indian customers.** C&W UK is stated to be a leading international telecom company which has a well established international network. The applicant submits that the Indian customers of the applicant would want to transmit their voice/data to places outside India. **Under the proposed agreement the applicant would provide the Indian leg of the service by using its own network and equipments and network of other domestic operators, and the international leg of the service would be provided by C&W, UK, using its international infrastructure and equipments. In other words, whereas the applicant will carry the calls and data within the country, C&W UK will further carry those calls and data to the recipients outside**

India. The network and equipments of C&W UK will not be used in India and the applicant's network and equipments will not be used outside India. Thus in telecom parlance, domestic half circuit will be provided by the applicant and international half circuit will be provided by C&W UK. In respect of the aforesaid services rendered by C&W UK, the applicant will pay fees to the former.

2. It is in this factual background that the applicant seeks ruling of this Authority on the following questions:

(1) Whether the amounts payable by the Applicant to Cable & Wireless UK ("C&W UK") under the terms of the proposed agreement/arrangement (the "Agreement") would be in the nature of "fees for technical services" ("FTS") within the meaning of the term in Explanation 2 to clause (vii) of section 9(1) of the Act, or not?

(2) Whether the amounts payable by the Applicant to C&W UK under the terms of the Agreement would be in the nature of "royalty" within the meaning of the term in Explanation 2 to clause (vi) of section 9(1) of the Act, or not?

(3) Whether the amounts payable by the Applicant under the Agreement between the Applicant and C&W UK would be in the nature of FTS within the meaning of the term in Article 13 of the Agreement for Avoidance of Double taxation entered into, between the Government of the United Kingdom and the Government of the Republic of India ("Treaty"), or not?

(4) Whether the amounts payable by the Applicant to C&W UK under the terms of the Agreement would be in the nature of "royalty" within the meaning of the term in Article 13 of the Treaty, or not?

(5) Based on the facts of this case, whether C&W UK has a Permanent Establishment ("PE") in India under Article 5 of the Treaty?

(6) Based on the answers to questions (1) to (5) above, and in view of the facts as stated in Annexure I, whether the income received by C&W UK will be chargeable to tax in India, or not? If the answer is in the negative, would such payments by the Applicant suffer withholding tax under section 195 of the Income Tax Act, 1961, or not, and if yes, at what rate?

3. The applicant has filed a copy of the agreement which it proposes to enter into with C&W UK. This agreement is called 'Service and Revenue Share Agreement'. It is stated in the recitals that the parties wish to provide to each other on reciprocal basis national and global telecommunications services. Article 1 of the agreement states that the parties shall provide services to each other through bandwidth connectivity and other similar facilities. The bandwidth service will comprise international leased circuit, managed private leased

services, managed private lines, etc. Article 3 requires the parties to interconnect their respective networks at Network Access Points. The expression 'Network Access Points' has been defined to mean physical points at which the networks of the parties are to be connected. As per article 5, the party availing the service shall pay fees to the party providing the service. The payment shall be on mutually agreed revenue share basis, which shall be calculated with reference to the revenue billed by the party to the customers at the originating point. The revenue share shall be settled on monthly basis. Each party shall bill the other in sterling pounds.

4. The applicant submits that the service to be provided by C&W UK is a standard facility and is not technical in nature. So the payment made for availing this service would not amount to fee for technical services as stipulated in section 9(1)(vii) of the Act. According to the applicant the payment in question would not either be regarded as 'fee for technical services' under article 13(4) of the Convention between the Government of India and the Government of the United Kingdom for the Avoidance of Double Taxation and Prevention of the Fiscal Evasion with respect to Taxes on Income and Capital Gains (the treaty), as C&W UK does not make any technical knowledge, skill or experience available to the applicant. The applicant further submits that the payment made to C&W UK is not for the use of any intellectual property or equipment. Under the proposed agreement, C&W UK will provide two way communication service to the applicant without allowing any right to use its network or equipment. As such, the payment in question would not come within the purview of royalty, either under section 9(1)(vi) or article 13(3) of the treaty. The applicant relies on the Report of the Technical Advisory Group (TAG) constituted by the Organization for Economic Cooperation and Development which lays down certain principles for drawing distinction between transactions for use of equipment and those for rendering of services. The applicant also cites the cases of Neyveli Lignite Corporation Ltd. 1, BSSL vs. UOI 2, WIPRO 3 and the decision of AAR in Dell International Services India Pvt. Ltd 4. The applicant states that C&W UK has no permanent establishment in India. It has no liaison office, branch office, project office or sales outlet in this country, nor does C&W UK render any services in India through its employees, personnel or agency.

5. The Director of Income-tax (International Taxation), Bangalore, who is the jurisdictional Commissioner in this case, first furnished his comments vide his letter dated 17.11.2008 and later vide letter dated 25.2.2009. He first of all points out that a group company, namely, M/s C&W India Ltd., a company registered in UK, has a branch office in Mumbai, which provides telecommunication networking services, designing and maintaining networks, etc. The Commissioner states that the address of its registered office given by the applicant is the same as that of the branch office of the said UK Company.

The Commissioner raises doubt that the applicant may take over the functions of this branch office. On the question of technical services, however, the Commissioner concedes that the services in question cannot be regarded as 'technical services' under article 13(4) of the treaty, since no transfer of technology is involved. He further states that the payments made by the applicant to C&W UK would be in the nature of royalty, both under section 9(1)(vi) of the Act as well as article 13 of the treaty. According to the jurisdictional Commissioner the services provided by C&W UK are not in the nature of standard facility as these use secret process. The applicant thus pays for using secret process. The jurisdictional Commissioner relies on Asia Satellite Communication⁵ case for this proposition. He also submits that as the actual service has not yet started, it cannot be said what equipment will be installed and where and this needs to be verified. The last point raised by the jurisdictional Commissioner relates to PE. He submits that the contract between the applicant and its Indian customers indirectly binds C&W UK. As such, the applicant acts as an agent of C&W UK and so C&W UK has agency PE in India. He also states that it is not clear at this point of time whether C&W UK will be deputing some of its employees for providing connectivity, technical or maintenance support in India. The Commissioner urges that the question of PE may be left open at this stage.

6.

6.1 The Authority, during the course of hearing, on 28.1.2009, directed the applicant to file affidavits clarifying certain technical details relating to the network/system by which connectivity is provided to the customers in India and any other factual information considered relevant by the applicant. The applicant filed two affidavits on 31.3.2009 – a technical affidavit and an affidavit explaining certain relevant factual details.

6.2 In the technical affidavit, the applicant gives the description of a network by which it provides international connectivity between TCS premises located in Mumbai and Equifax located in Alpharetta, USA. The connectivity is provided through a dedicated private leased line. The applicant has installed a router at TCS premises. The voice/data is carried by the applicant in India on its own network and delivered to C&W UK at Marseilles in France from where the latter carries it to Alpharetta, USA. In the Indian leg of the service there is no involvement of the network or equipment of C&W UK. TCS pays one time charge for installation and recurring charges for connectivity services.

6.3 The second affidavit gives clarification about the nature of charges, revenue sharing with reference to the provisions of article 5 of the agreement. It is stated that the applicant charges its customers in India purely for rendition of service. No charges are taken for router which is completely under the control of the applicant. The applicant has by way of illustration stated that if it charges rupees 100 from its customer, it pay Rs. 44 to C&W UK for providing the international leg of the service. This affidavit also gives clarification about

the Indian branch of the UK group company

7. We shall first take up the issue whether the applicant pays fees to C&W UK for rendering 'technical services' under the Act or under the treaty. Explanation 2 to para (vii) of section 9(1) defines 'fees for technical services' to mean any consideration paid for rendering any managerial, technical or consultancy services, including provision of services of technical or other personnel. In the present case, in carrying telecom signals from Marseilles to other countries, C&W UK is not providing any managerial, technical or consultancy services, nor is it providing the services of its technical or other personnel to the applicant. C&W UK performs this part of service itself without the involvement of the applicant. **The applicant has thus rightly urged that the fees paid by it to C&W UK is not in the nature of fees for technical services under the Act.** So far as article 13(4) of DTAA is concerned, the first part of it defines 'technical services' in a manner similar to Explanation 2 to section 9(1)(vii), but it further qualifies this expression in clauses (a), (b) & (c). Clause (c) is relevant for the present consideration. This clause requires that the technical service in question should make available technical knowledge, experience, skill, know-how or process, or consist of the development and transfer of a technical plan or technical design (emphasis supplied). From the description of service presented before us, we do not find that the requirements of clause (c) are fulfilled here. **First, no technical service is rendered and secondly, there is no transfer of technology. The Revenue also concedes that this is not a case of payment of fees for technical services.**

8.

8.1 The question whether the fees paid by the applicant to C&W UK are in the nature of royalty has been much debated. The revenue vehemently contends that it is royalty income –both under the Act as well as the treaty. Before dealing with the issue, we may extract the provisions of the Act as well as the treaty. The relevant provisions of section 9 read as under:

"Income deemed to accrue or arise in India.

9. (1) The following incomes shall be deemed to accrue or arise in India :—

(i) to (v) xx xx xx xx xx xx xx xx

(vi) 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 :

xx xx xx xx xx xx xx xx xx

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 ;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill ;

(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;]”

xx xx xx xx xx xx xx xx xx

The relevant provisions of Article 13 of the treaty are as under:

“ARTICLE 13 -Royalties and fees for technical services –

1. xx xx xx xx xx xx xx xx xx

(2) However, such royalties and fees for technical services may also be taxed in the Contracting State in which they arise and according to the law of that State; but if the beneficial owner of the royalties or fees for technical services is a resident of the other Contracting State, the tax so charged shall not exceed :

xx xx xx xx xx xx xx xx xx xx xx xx xx

3. For the purposes of this Article, the term “royalties” means :

(a) payments of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic or scientific work, including cinematography films or work on films, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience; and

(b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial or scientific equipment, other than income derived by an enterprise of a Contracting State from the operation of ships or aircraft in international traffic.

xx xx xx xx xx xx xx xx xx xx”

According to the applicant, in the proposed business model, no intellectual

property rights are involved; C&W UK has not granted to it any right to use any intellectual property or any equipment. The Commissioner, on the other hand, states that the payment made by the applicant is clearly for using secret process. According to him the technology involved in the process of transmission of voice/data contains proprietary resources. It is not a case of mere rendition of service, but the quality of service and secrecy are also material. It is further stated that the services to be availed by the applicant would amount to the use of a secret process and thus is covered by royalty as stipulated in article 13(3) of the treaty. But, no material has been placed before us to show that C&W UK uses any secret process in the transmission of the international leg of the service, or that the applicant pays towards the use or right to use that secret process. **It is well settled that telecom services are standard services. The arrangement between the applicant and C&W UK is for rendition of service and the applicant pays for the same. It is for C&W UK to see how it will provide that service. The applicant is not concerned with the same. This Authority has dealt with this issue in the case of Dell International Services India Pvt. Ltd.(supra).**

In that case BT America provided two way transmission of voice and data to Dell India between India and USA. For providing this service, BT America had tied up with VSNL in India and other telecom service providers outside India. Dell India had an agreement with BT America for the entire service for which it made payment directly to BT America. One of the issues that arose for consideration was whether the payment made by the applicant to BT America was in the nature of royalty falling either under clause (iii) of Explanation-2 of section 9(1) or article 12(3) of the tax avoidance treaty between India and USA, which is materially similar to the provisions of article 13(3) of the treaty between India and UK. The Authority held –
“14. Whether the payment made by the applicant to BTA is in the nature of royalty falling under clause (iii) of Explanation 2 and/or Article 12(3) of the Treaty?

14.1. It is one of the contentions of the Revenue that the applicant makes use of or is conferred with the right to use a ‘process’ within the meaning of clause (iii) to Explanation (2) to Section 9(1) of the Act. That clause speaks of “the use of any patent, invention, model, design, secret formula or process or trade mark or similar property”. It is contended, relying on the decision of ITAT in the case of Asia Satellite Telecommunications Company Ltd. vs. Deputy Commissioner of IT (ITA No.166/DEL/2001* dated 1.11.2002) that the word ‘secret’ only qualifies the expression ‘formula’ and cannot be read before the word ‘process’. On such interpretation, it is submitted by the Revenue in its comments that the services provided to the applicant are clearly in the nature of a process and not in the nature of standard facility and the applicant has used and has been conferred with the right to use such process. However, this contention has not been urged before us by the learned Counsel for the Department for the obvious reason that the language used in the relevant clause of the Treaty does

not support any such interpretation. The expression in Article 12(3) (referred to at para 7.1 supra) is "for the use of or the right to use any copyright, patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience." It is thus clear that formula/process are part of the same group and the adjective 'secret' governs both. The reasoning of ITAT in the aforementioned case, based on the absence of comma after process and the impact of the immediately following word, 'trade mark', does not hold good in view of the clear language in Article 12(3) of the Treaty. It has been so pointed out very rightly by another Bench of ITAT in *Panamsat International Systems Inc. vs. Dy. Commissioner Income-tax (ITA. No.1796/DEL/2001 dated 11.8.2006)* at paragraph 6.18. Going by such interpretation, it cannot be held that there is, in the instant case, the use of or the right to use a secret process. In fact it is nobody's case that any secret process is involved here and the applicant makes use of it. The use of secret process is alien to the minds of contracting parties. Incidentally, we may mention that it was brought to our notice that similar bandwidth services through private circuits are being provided by many other telecom operators. Hence, the royalty definition under the Treaty relating to secret process is not attracted here. We may mention that the applicant contended that the decision of ITAT in *Asia Satellite case (supra)* is distinguishable on facts. It is unnecessary to deal with this aspect."

The Authority also considered in detail the question whether consideration was payable for using or for the right to use any equipment through which connectivity was provided. That question was answered in the negative. We are of the view that on the same reasoning the applicant does not pay for using any secret process in the present case also.

8.2 We may now consider the next submission of the Revenue that, since the services are yet to commence, it is premature to say whether C&W UK will install any equipment at the premises of the applicant in India. We notice from the pleadings and averments of the applicant that C&W UK will be providing telecom services to the applicant outside India. The network of the applicant will inter-connect with the network of C&W UK at Marseilles in France. Thus the telecom signal will move on the network of the applicant from India to Marseilles. It is beyond Marseilles that the network and equipment of C&W UK will be used for transmission of the signal. We also notice from the draft agreement that there is neither any stipulation for provision of any equipment nor payment of any fee for the same. On the basis of the records placed before us, we are of the view that no case is made out to presume that any equipment will be installed by C&W UK at the premises of the applicant in India and the applicant will pay for the same. The averment of the Commissioner is based merely on the doubt entertained by him for which he has not shown any basis. The affidavits filed by the applicant after first hearing clarify the factual position in this regard. In the light of the view taken by us, it is not necessary to examine the TAG report.

8.3 The Revenue has thus failed to show how the payments made by the applicant will be royalty income in the hands of C&W UK.

9.

9.1 We may now take up the last issue which relates to permanent establishment. As already pointed out, the Revenue has mentioned about the existence of another group company in India whose address is alleged to have been used by the applicant as its registered office. The applicant has submitted that the Cable and Wireless India Limited which is a company incorporated in UK, has set up a branch office in India under Reserve Bank of India (RBI) permission, a copy of which has been filed. This branch office performs ancillary telecom services, such as network designing, project implementation services and providing network management and maintenance services. This branch has not been granted any licence by the Department of Telecommunication to carry out NLD/ILD services. The applicant also states that its registered office does not share the premises with the above branch office. We find that the applicant and the branch office of Cable and Wireless India Ltd. are separate legal entities which perform different types of telecom services. The said branch office is not in the business of providing voice / data transmission service.

9.2 The Revenue also states that it cannot be said at this point of time whether C&W UK would be deputing its personnel to provide technical and maintenance support to the applicant. The applicant states that there is no such stipulation in its agreement with C&W UK. From the case presented before us, there is no reasonable basis to entertain the doubt that C&W UK will depute its technical personnel for providing maintenance and support to the applicant.

9.3 The next contention of the Revenue is that the applicant will be entering into an agreement with the Indian customers for providing end-to-end international long distance telecom transmission, the Indian leg of which will be provided by the applicant and the foreign leg will be provided by the C&W UK. Thus the contract between the applicant and the Indian customers would indirectly bind C&W UK, so far as the international leg of the transmission is concerned. As such the applicant would be acting as an agency PE for C&W UK. **The applicant states that it does not act on behalf of the C&W UK in India, nor does it conclude any contract on behalf of that company. The applicant in its independent capacity negotiates and concludes contracts with its customers on principal-to-principal basis, to which C&W UK is not a party. Similarly, the agreement with C&W UK is also on principal-to-principal basis, the Indian customer not being a party to the same. The breach of one type of contract does not affect the rights and obligation arising under the other type of contract.**

10. In the light of the above discussion, we have come to the conclusion that the payments made by the applicant to C&W UK are in the nature of business profits. In the absence of there being any permanent establishment of C&W UK In India, this income is not at all taxable here. Since this income is not chargeable to tax under the Act, there is no question of making any deduction at source under section 195. In the result, we answer all the questions in negative.
Pronounced in the open Court of the Authority on this 30th day of June, 2009.

Sd/-
(A. SINHA)
MEMBER

Sd/-
(P.V. REDDI)
CHAIRMAN

Sd/-
(RAO RANVIJAY SINGH)
MEMBER

F.No. AAR/786/2008/ Dated: 30.6.2009

This copy is certified to be a true copy of the advance ruling and is sent to:

1. The Applicant.
2. The DIT (International Taxation), Bangalore.
3. The Joint Secretary (FT &TR-I), M/o Finance, CBDT, Bhikaji Cama Place, New Delhi
4. The Joint Secretary (FT &TR-II), M/o Finance, CBDT, Bhikaji Cama Place, New Delhi
5. Guard File.

(Batsala Jha Yadav)
Addl. Commissioner of Income-tax (AAR)