

IN THE INCOME TAX APPELLATE TRIBUNAL, MUMBAI BENCH "L",
MUMBAI

BEFORE SHRI N.V.VASUDEVAN(J.M) & SHRI B.RAMAKOTAIAH (A.M)

ITA NO.3824/MUM/2006
ITA NO.3825/MUM/2006
ITA NO.3826/MUM/2006
ITA NO.3827/MUM/2006
ITA NO.3828/MUM/2006
ITA NO.1932/MUM/2008
ITA NO.1933/MUM/2008
ITA NO.1934/MUM/2008
ITA NO.1935/MUM/2008
ITA NO.1936/MUM/2008
ITA NO.1937/MUM/2008
ITA NO.1938/MUM/2008

Standard Chartered Bank,
23-25, Mahatma Gandhi Road,
Fort, Mumbai 400 001.
PAN:AABCS 4681D
(Appellant)

Vs.

The Dy. Director of Income Tax,
(International Taxation)2(1),
Mumbai.
(Respondent)

ITA NO.1457/MUM/2008(A.Y.2004-2005)

Atos Origin IT Services Singapore
Pvt. Ltd., C/o. Atos Origin India Pvt.
Ltd., 126/127 SDF-IV, Seepz,
Andheri (East), Mumbai 400 096.
PAN: AAECA 9266F
(Appellant)

Vs.

The Dy. Commissioner of
Income Tax (International
Taxation) 1(1),
Mumbai
(Respondent)

Appellant by : S/Shri Kanchan Kushal,
Dhanesh Bafna &
Mrs. Sheetal Bandekar
Respondent by : Smt. Malathi Shridharan

ORDER

PER BENCH,

These are 12 appeals by Standard Chartered Bank (SCB) (hereinafter called as the appellant) against the following orders of CIT(A) XXXI, Mumbai.

ITA No.	Date of CIT order.
3824/M/06	27/03/2006
3825/M/06	27/03/2006
3826/M/06	27/03/2006
3827/M/06	27/03/2006
3828/M/06	27/03/2006
1932/M/08	09/01/2008
1933/M/08	09/01/2008
1934/M/08	09/01/2008
1935/M/08	09/01/2008
1936/M/08	09/01/2008
1937/M/08	09/01/2008
1938/M/08	09/01/2008

2. The grounds of appeal raised by the appellant is common in all the appeals. For the sake of reference the grounds raised in ITA No.3827/M/06 is reproduced as under:-

“1. That on the facts and in the circumstances of the case, the learned Commissioner of Income-tax (Appeals) XXXI, Mumbai (hereinafter referred to as ‘the CIT(A)’) erred in confirming the decision of the Assessing Officer that the amount of US \$ 14,08,292.74 payable by the appellant as data processing charges to M/s. Sema Group Outsourcing (Singapore) Pte Ltd. (now known as Schlumberger Sema Pte Ltd.) [‘SPL’], is liable to tax in India and subject to withholding tax at 15% under Article 12(3)(a) of the double Taxation Avoidance Agreement [hereinafter referred to as ‘Treaty’] between India and Singapore.

2. That on the facts and in the circumstances of the case, the sum of US \$ 14,08,292.74 payable by the appellant in favour of SPL, as referred to in ground no.1 above, neither being in the nature of ‘Royalties’ or ‘Fees for Technical Services’ within the meaning of Article 12 of the Treaty, but being in the nature of ‘Business Profits’ which were not attributable to any ‘Permanent Establishment’ of SPL in India, within the meaning of Article 5 of the Treaty, the same were

not taxable in India as per Article 7 of the Treaty and in the said premises, the appellant had no obligation to withhold tax thereon under section 195 of the Income-tax Act, 1961.

3. That the appellant craves leave to add/modify or alter, amend, rescind or modify the grounds hereinabove before or at the hearing of this appeal.”

3. The Appellant is a Non-resident Company engaged in the business of banking in India through branches established in the different states of India. The appellant entered into a Hubbing agreement dated 26th Sept. 1996 (hereinafter referred to as the Agreement), with M/s. Sema Group Outsourcing (Singapore) Pte Ltd. (now known as Atos Origin IT Services Singapore Pte Ltd.) (earlier also known as Schlumberger Sema Pte Ltd.) (hereinafter referred to as ‘SPL’), a company incorporated in Singapore. According to the Assessee, the agreement is for the provision of data processing support to the appellant for its business in India and that the data processing is done outside India. The main terms of the agreement in so far as it relates to a decision in the present appeals is as follows: (SPL is referred to as “Sema” and the appellant is referred to as “SCB”)

“1. Sema will make available SCB the following capacity in the Singapore Data Centre for SCB’s exclusive use:-

From November 6th 1996 to 5th December 2001 inclusive 32 MIPS and 100 Gigabytes.

From March 6th 1997 to 5th December, 2001 inclusive – an additional 20 MIPS and 100 Gigabytes making a total of 52 MIPS and 200 Gigabytes in this period.

Sema Group will install disc capacity and supporting tape subsystem in Singapore as soon as possible so as to assist SCB in the migration of data from Hong Kong to Singapore prior to November 6th. Any capacity made available prior to November 6th will be provided without additional charge to SCB.

2. In respect of the subsequent capacity of 20 MIPS and 100 Gigabytes, Sema will make available to SCB such branches as will be required on demand by SCB up to a total capacity of 52 MIPS and 200 Gigabytes. SCB will always give a minimum of one calendar month's notice of such additional requirements, and the first date upon which such notice can be served will be 6th February 1997, in order that the availability of the remaining resources can take place on or subsequent to 6th March 1997.

3. The service charges for the above requirements will be S \$ 9.798 million for the entire period of five years. The scope of the price for all four metros will include the following elements:

- Maintenance CPU
- Disc space
- 36 track tape subsystem
- Staff
- Site Preparation
- Upgrade to communications front end processor
- System software
- Disaster recovery (In line with Contractual levels.)

The Service charges also takes into account lower maintenance and running costs compared with those of the current configuration in Singapore at 1st September 1996.

.....

8. Should any of the capacity set out in 1 above not be required in connection with India 'Hubbing' requirements at any time during the five years to November 5th 2001, SCB will have the right to utilize any residual capacity at no extra cost and on the same terms in connection with any other similar requirements it may have for data processing to be performed in the Singapore.....

4. As can be seen from clause-1 of the agreement SPL has a Data Centre at Singapore and it has to make available for exclusive use by the appellant the from November 6th 1996 to 5th December 2001 32 MIPS and 100 Gigabytes to start with. It is not in dispute that the tenure of this agreement was further extended to cover the period in dispute in these appeals. The Agreement does not make any reference to any data processing to be carried out by SPL for the appellant at Singapore. However, clause-8 of the

Agreement mentions that the appellant will have the right to utilize any residual capacity at no extra cost on the same terms in connection with any other similar requirement it may have for data processing to be performed in Singapore. Further, the permission granted by Reserve Bank of India to the appellant vide letter dated 6/11/1996, shows that SPL was carrying out data processing for the appellant at Singapore. As per the agreement appellant was required to pay SPL fixed monthly installments with effect from January 1, 1998 over a period of 60 months. The Reserve Bank of India (RBI) had granted permission to renew the agreement between the appellant and SPL for data processing at SPL's Data Centre at Singapore vide letter of RBI dated December 19, 2001 subject to conditions stipulated in their letter dated November 6, 1996.

5. As per the agreement the appellant had to make payment to SPL for services rendered. The appellants filed applications u/s.195(2) of the Income Tax Act, 1961 (hereinafter referred to as "Act") before the AO for issue of the No Objection Certificate for making payments to SPL without deduction of tax at source at the time of making payment. According to the appellant, the nature of the fees paid by it to SPL does not fall within the ambit of the definition of royalty given in Section 9(1)(vi) of the Income Tax Act, 1961 (hereinafter referred to as the Act) as well as Article 12(3) of the Double Taxation Avoidance Agreement between India and Singapore (hereinafter referred to as the Treaty). It was the further claim of the Assessee that the receipts from the appellant in the hands of SPL would be in the nature of business profits and since SPL did not have a Permanent Establishment (PE) in India, the receipts are not income chargeable to tax in India in view of Article-7 of Treaty. It is an admitted position that in case the fee is not considered as royalty then the same would be business profits of SPL and since SPL did not have a PE in India, its business income in India would not be taxable under the Act.

6. As we have already seen the Agreement is not very clear about the nature of services to be rendered by SPL. Based on Clause-8 of the Agreement and approval of the RBI referred to earlier, the appellant claimed that under the agreement SPL was processing data for the appellant in Singapore for appellant's exclusive use. The appellant submitted before the AO that the consideration payable to SPL for the data processing services has been computed having regard to the following -

1. Computer hardware and system software for operations of the appellant's computer applications.
2. Computer hardware to support data communications for using the services as stated above.
3. Manpower to handle daily and periodic computer based processing.
4. Suitable environment for housing the computer systems.
5. Disaster recovery capability for the services provided and testing of the same twice a year.

7. The nature of services rendered by SPL to the appellant was explained by the appellant in their letter dated 7.11.2003 in one of the application filed u/s.195(2) of the Act, dated 9/10/2003, for no objection to remit payments to SPL without deduction of tax at source, as follows:

1. The input data i.e., the raw data relating to branch transactions is fed by appellant via application software owned by it and then transmitted to SPL mainframe computer in Singapore for processing.
2. The application software owned and used by the appellant in this regard is not designed by SPL nor acquired from SPL.
3. After the raw data is transmitted into the hardware facility of SPL in Singapore, SPL staff based in Singapore process the raw data on an application software owned by appellant using the mainframe computer of SPL.
4. The raw data is processed by SPL staff as per the requirements of appellant using the application software owned by the appellant.
5. The processed data, i.e., the output data is transmitted electronically to the appellant in India using the software provided by the appellant, which is not designed by SPL.

8. SPL further confirmed by their letter dated 4/4/2005 filed before the AO (in the form of confirmation by Atos Origin), the nature of services performed

by it for the appellant. The same refers to the following as the nature of services performed by SPL pursuant to the Agreement.

- a) The appellant would send raw input bank transaction data through telecommunication lines to SPL at Singapore for processing.
- b) The processing is done by SPL at Singapore as per appellant's requirement using system hardware and software (through human intervention), whenever required.
- c) The operating software of SPL's mainframe computer was developed by the manufacturer of the computer and third party vendors and is not designed by SPL for the specific processing of appellant's data.
- d) The output of the processing generated in the form of reports as per appellant's specifications are transmitted to appellant in India through telecommunication lines.
- e) SPL also keeps the back-up of the processed data which are made available to appellant upon request.

Accordingly, the appellant filed an application for an NOC before the AO, who vide his order dated March 8, 2004 directed the appellant to deduct TDS @ 15% on the gross payment to be made or payable to the service provider (SPL).

9. It is based on the above material that we have to proceed to decide the dispute in these appeals, which is as to whether the payment by the appellant to SPL would constitute "Royalty" within the meaning of Article 12(3) of the Treaty read with Sec.9(1)(vi) of the Act?

10. The definition of Royalty under the DTAA between India and Singapore is contained in Article 12(3), which is as under:

"The term "Royalty" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use;

- a) Any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for 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, including gains derived from the alienation of any such right, property or information.

- b) Any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraph 4(b) of Article 8”

11. Explanation-2 to Sec. 9(1)(vi) of the Act defines “Royalty” as follows:

Sec.9 Income deemed to accrue or arise in India.--(1) The following incomes shall be deemed to accrue or arise in India –

- (vi) income by way of royalty.....

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;

(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films ; or

(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (v) ;

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

Explanation.—For the removal of doubts, it is hereby declared that income of the nature referred to in this clause payable for service rendered in India shall be regarded as income earned in India ;

Explanation.— For the removal of doubts, it is hereby declared that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India under clause (v) or clause (vi) or clause (vii) of sub-section (1) and shall be included in the total income of the non-resident, whether or not,—(i) the non-resident has a residence or place of business or business connection in India ; or(ii) the non-resident has rendered services in India.

12. The AO held that the payment by the appellant to SPL was in the nature of royalty and therefore taxable in India and on the gross payments and therefore appropriate rate of tax had to be deducted at source. In coming to the above conclusion, the AO held as follows:

1. The payment to SPL is for the purpose of availing CPU and disk capacity and supporting tape sub system capacity. Hence the payment made by the appellant for the above activities is royalty as per Article 12 of the DTAA between India and Singapore.
2. The service provider is not just providing the routine communications services but the service provider is providing the modern technical designs and models involving the customized communication and computation with the application of sophisticated information technology requiring constant upkeep and updating so as to meet the challenges of the advanced technology in this area.
3. The use of embedded secret software provided by the service provider for purpose of processing of raw data of the appellant clearly falls within the ambit of Article 12(3) of the DTAA and 9(1)(vi) of the Act.

4. The AO also held that the case of the appellant was similar to the ruling given by the Authority for Advance Ruling reported as P No.30 of 1999 (238 ITR 296) and has relied on the said ruling in coming to the above conclusion.

5. The AO also observed that processing is done in the service centre of SPL to generate information for the use of the appellant and that the information will have all the inputs made by the appellant.

13. Before the CIT(A) the appellant submitted that the Taxability of the fees in India will depend on the character of the fees payable to SPL. The Assessee contended :

a) As per the agreement SPL assured the appellant that it will ensure that it would provide the requisite capacity space in the mainframe computer of SPL at Singapore. This was to handle and process the specified volume of data and transactions of the appellant.

b) The input data i.e. the raw data relating to branch transactions is fed by the appellant via application software owned by it and then transmitted to SPL mainframe computer in Singapore for processing. The application software owned and used by the appellant in this regard has not been designed by SPL nor acquired from SPL.

c) After the raw data is transmitted into the hardware facility of SPL in Singapore SPL staff, based in Singapore apply their mind and brain to process the raw data on application software owned by the appellant using the mainframe computer of SPL. The processing work performed by SPL staff in Singapore on the main frame computer owned by SPL using their own intellect does not involve the transfer of any technical model or design to the appellant in India. The raw data is processed by the SPL staff as per the requirements of the appellant using the application software owned by the appellant. The processed data i.e. the output data is transmitted electronically to the appellant in India using the software provided by the appellant which incidentally has not been designed by SPL.

Thus, the appellant submitted that the payment being made to SPL is essentially for the purpose of data processing which does not involve the provision of technical models and designs as stated by the AO in his order. It was further submitted that except for the operating software of the mainframe computer of SPL in Singapore, all other software used in the

processing of the data belongs to and is owned by the appellant. It was pointed out that the agreement does not give the appellant either the permission to use or grant the right to use the mainframe computer or the software embedded in it which is necessary for its operation. It was also highlighted that under the Agreement, the appellant does not itself undertake the processing of the data. Hence the making available by SPL of software and secret process for use by the appellant does not arise.

14. On the question whether the nature of the fees indicated above falls within the ambit of the definition of royalty given in Section 9(1)(vi) of the Act or Article 12(3) of the Treaty, the appellant pointed out the definition of Royalty in Section 9(1)(vi) of the Act and Article 12(3)(a) of the Treaty has been defined as payment of any kind received as consideration for the use or the right to use inter-alia any copy right of a literary, artistic or scientific work including any patent, trade mark, design, plan, secret formula or process. The appellant pointed out that under the Agreement consideration payable to SPL is not a payment for the use of or the right to use any copyright owned by SPL. SPL has not allowed the appellant the use of or the right to use any literary, artistic or scientific work for which the consideration is payable under the Agreement. It was argued that under the Agreement, SPL has not made available to the appellant the use of or the right to use any software developed and owned by it. It was argued that the transmission of the raw data from the appellant in India to SPL in Singapore and the forwarding of the processed data by SPL from Singapore to the appellant in India were done through the software supplied by the appellant to SPL. The data was processed on the SPL mainframe computer in Singapore by SPL staff with the help of application software owned and supplied by the appellant. The said application software has neither been designed by SPL nor acquired by the appellant from SPL. It was submitted that though the data is processed on the main frame computer owned by SPL in Singapore, but the system software i.e. the operating software

necessary for the operation of the main frame computer was owned by the manufacturer of the main frame computer. Such operating software of the main frame computer is secret software belonging to the manufacturer of the hardware. SPL has the right to use the said operating software to the extent it is required to operate the main frame computer. SPL has neither acquired the operating software from the author nor has the rights of distribution and reproduction with regard to the said operating software. Consequently SPL cannot and has not granted to the appellant the use of or the right to use the said operating software of the main frame computer for a consideration.

15. It was further submitted that the Agreement does not make available to the appellant the use of or the right to use any secret process. It will be appreciated that the appellant is merely transmitting the raw data and getting back the processed data which is the end product. The appellant does not itself use or operate the main frame computer (far less the system software necessary for the operation of the main frame computer) or undertake any processing whatsoever of the raw data. Therefore the question of use or the right to use the mainframe computer or any secret process provided by SPL in processing of the said data does not arise. It was submitted that the substance of the Agreement was the processing by SPL of the raw data as per the requirements of the appellant and supply of the processed data to the appellant for which SPL guaranteed and assured the appellant that it has the hardware infrastructure to handle the large volume of data required by the appellant to be processed.

16. The CIT(A) did not agree with the submissions of the appellant and he held as follows:

“3.1 The appellant had entered into an agreement with SPL for processing of the appellant’s data at Singapore. This agreement is for a period of 5 years starting from 26.09.1996 and it appears, later on this agreement was renewed further. The services being provided by SPL have been examined and have been quoted in the order in brief.

The appellant collects the data about its customers in India and thereafter transmits its electronically in Singapore. SPL has set up a vast computer system by utilizing various computer hardware and software. It has got massive capacity for processing of data provided by the appellant. After the data is processed and reports as required by the appellant are prepared, the data is transferred back to the appellant in India. SPL also maintains back up of the processed data in case of any loss. From these facts it can be very well understood that the SPL is providing service of 'processing of data' which can be termed as a process. Sec.9(1) Explanation (2) of the I.T. Act.....

3.2 Article 12(3) of the DTAA provides definition of "royalties",

Since by virtue of section 90(2) of the IT Act, if the provisions of DTAA are beneficial to a non-resident, they shall prevail over the provisions of I.T. Act. It is therefore, necessary to examine whether the services provided by SPL are covered by definition of 'royalty' both under explanation (2) of Sec. 9(1)(vi) as well as Article 12(3) of the DTAA.

3.3 Clause (iii) of the Explanation (2) provides that the royalty means consideration for the use of any patent, invention, model, design, secret formula or process or trade mark or similar property. The appellant has not obtained any software of its own and therefore there is no question of any copy right or right to use any copy right. However, the SPL has provided a process by providing its computer facility to process the data provided by the appellant. The AR has argued that the software and hardware of the computer system of the SPL is not been designed or manufactured by SPL. It is not necessary that SPL should itself design, assemble and set up the computer system. It can do so by obtain various components from the market including copyrighted software or using software and hardware available from the market. It can also design or can get the software and hardware designed for use of its computer system for the efficient processing of data. In clause (iii) of explanation (2) there is no requirement that the process should be a copy right process of which the provider should be the owner. It is sufficient if the provider of a process provides such a process for which payment is made to him.

17. The CIT(A) thereafter relied on the decision of the Hon'ble Delhi ITAT in the case of Asia Satellite Telecommunication Co. Ltd. (2003) 85 ITD 478 (Del) and held that the appellant had made payment for right use of process.

Further the CIT(A) agreed with the view of the AO regarding the applicability of the decision of the AAR in the case of P No.30 of 1999 (supra).

“3.8. The appellant has referred to the decision of the Hon’ble ITAT in the case of Motorola Inc. vs. DCIT (95 ITD (Del) (SB) (supra). The facts obtaining in that case were entirely different. In that case, software was being supplied for setting up the cellular hone net work. Thus the facts in the case of Motorola Inc are entirely different. Similarly the decision in the case of Samsung Electronics Company Ltd. vs. ITO [(94 ITD 91 (Bang)] was also rendered on different facts. Both these decisions relates to acquisition of software and whether payment made for such purchase amounts to royalty. The appellant company has not acquired any software and therefore facts in the case are totally different from these two cases.”

18. While dealing with another appeal arising out of application under section 195 of the Act (which is subject matter of ITA No.1936/M/08) the CIT(A) added another reason as to why the payment in question should be held to be royalty.

“2.17 On perusal of the above quoted portion of the agreement, it is clear that the payment being made by SCB India, pursuant to the aforesaid agreement is for the purpose of availing CPU and disc capacity and supporting tape subsystem capacity i.e. the capacity which has been created for the exclusive use of SCB India. This fact was not present in the Kotak case, as discussed above, and its agreement (the relevant portion of which has been quoted from the order of the Hon’ble Tribunal) also did not speak about a captive exclusive disc capacity being granted to the appellant in the Kotak case. This fact is also contrary to what the appellant has stated in its own written submissions above, that the payment envisaged under the ‘Hubbing’ Agreement is a consideration payable to SPL only for rendering a service i.e. the processing of the raw data as per SCB’s requirement using SPL’s infrastructure in Singapore and not for any disc capacity.

2.18 It is thus clear from the wording of the agreement between the appellant and SCB that though SCB India does not have any physical possession of the property, it is exercising constructive control over the infrastructure facilities because these facilities can be utilized only by the SCB India as per the terms of agreements.

2.19 It is also seen that SCB India is also having significant economic interest in these facilities because as per para 9.1 of the agreement, any reduction in SPL's overall net profitability during the period of agreement will be funded on a 50/50 basis by SPL and SCB India. Also as per the para 8 of the agreement, the capacity/scientific equipment is at the disposal of SCB India.

2.20. All these facts satisfy most of the "tests" suggested by the Technical Advisory Committee of OECD, and referred to by the appellant itself in its written submissions quoted above, mainly that in order to constitute user of equipment, the customer should actually have domain or control over the equipment, or in other words, the equipment should be at its disposal. In the present case the disc space is very well part of the equipment which is at the disposal of the appellant.

2.21. On these facts, the arrangement appears to one of renting out disc space in the hardware system of assessee company in favour of the SCB India. The payments made by SCB India to the assessee company can be terms as having been made for the rights to use the scientific equipments as well as for a process being made available by the appellant to SCB as discussed in Paras 3.5 to 3.6 above. All these facts are very different from the facts obtained in the case of Kotak Mahindra Primus Ltd. relied upon by the assessee. This being the case, the case of Kotak Mahindra relied upon by the appellant cannot be considered as applicable to the appellant's case and is distinguishable on basic facts itself."

19. Aggrieved by the orders of the CIT(A) the appellant has preferred the present appeals before the Tribunal. The learned counsel for the Appellant submitted before us that the conclusion of the revenue authorities that the payment by the Appellant to SPL is taxable in India is not correct. He reiterated the stand of the Assessee on the nature of service that SPL was to provide to the appellant. These have already been narrated in the earlier part of this order and are not being repeated here. He brought to our notice the definition of Royalty under the DTAA between India and Singapore. The learned counsel for the appellant after referring to the agreement and the manner in which data is sent by the Appellant to SPL and how the same is processed and received back from SPL, submitted that the payments in question were charges paid for data processing. In this regard the learned

counsel for the Appellant submitted that the definition of royalty provides for use of, or the right to use any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for 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. It was submitted by him that the appellant did not have the right to use the mainframe computer or the software embedded in it which is necessary for its operation. The appellant provided all the software used in the processing of the data by SPL in Singapore except the operating software of the mainframe computer of SPL in Singapore. Thus the Assessee did not use or have the right to use any right to use any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process. SPL owned the mainframe computer which processed the data sent by the appellant from India. The operating system for operating the mainframe was owned by the manufacturer of the mainframe and SPL by virtue of purchase of the mainframe had only a licence to use the operating system to operate the mainframe computer. Since SPL did not have a Permanent Establishment (PE) in India, the receipt in the hands of SPL cannot be taxed as income in India.

20. He brought to our notice that the AO in coming to the conclusion that the payment by the appellant to SPL is "Royalty" within the meaning of Article 12(3) of the DTAA between India and Singapore has primarily relied on the decision of the AAR in the case of P.No.30 of 1999(supra). It was his submission that the facts in the said decision were different from the facts as it prevails in the case of the appellant. It was submitted by him that in the aforesaid case, the applicant before the AAR, Y, a company formed and incorporated in the U.S.A. and belonging to a group of companies which

operate in the worldwide credit card and travel business. It was engaged in providing international credit cards, travellers' cheques and other travel related services. These instruments are used, discounted and encashed all over the world by travellers on tour or business. To keep track of the expenses incurred on a travellers' credit card or purchase and encashment of travellers' cheques, etc., Y maintains a centralised computer in the USA. The centralised computer or the central processing unit (CPU) is a huge high technology computer complex having 15 to 20 mainframe IBM computers and other related hardware and software facilities involving substantial investment and capable of very high volume storage and high speed processing of data. This central processing unit was accessed and used by various group entities located worldwide through a consolidated data network maintained in Hong Kong. The transactions done by a traveller in a particular country were reported to a centralised computer in that country. In India, this is done by XT, located at Delhi. The said Indian company XT received information on computer through telephonic and microwave links about the use of credit cards and travellers' cheques by travellers all over the country. XT also serviced thirteen group companies in Asia and the Pacific, in a similar manner. The information was then passed on to the Hong Kong computer centre of the applicant. For carrying out this operation, XT obtained leased lines from VSNL. The applicant-company, Y charged XT, the Indian company, for the use of its computer set up in Hong Kong and that in the USA. XT, the Indian company, is a sub-subsidiary of the applicant. On these facts, the applicant sought an advance ruling on the questions whether payment due to the applicant under the transactions with XT was liable to tax in India and, if so, whether the payment due to the applicant under the transactions was covered under article 12(3)(a) or article 12(3)(b) of the Double Taxation Avoidance Agreement between India and the USA. The Authority ruled:

(i) That the definition of the expression "royalty" under section 9(1)(vi) of the Income-tax Act, 1961, read with its Explanation 2(vi), included rendering of any services in connection with any activities for the use of any patent, invention, secret formula or process, etc. Hence the transmission of information is through encryption as the data related to clients and strict confidentiality is observed. It is for the downloading of the software that the royalty is paid. In this context, the source rule becomes relevant which requires that the royalty is sourced in the State of payer. The royalty is, therefore, taxable in India.

(ii) That according to the agreement between the applicant and the Indian company, the facilities are to be accessed only by XT. The consideration payable is for the specific programme through which XT is able to cater to the needs of the group companies located in Japan, Asia Pacific, Australia and New Zealand. The transaction would relate to a "scientific work" and would partake of the character of intellectual property. The payments received in such transactions are for the use of intellectual property and partake of the character of royalty. The software is customised and secret. From the facilities provided by the applicant to the Indian company, which are in the nature of online, analytical data processing, it would be clear that the payment is received as "consideration for use of, or the right to use... design or model, plan, secret formula or process..." within the meaning of the term "royalties" in article 12(3)(a). The use by XT of the central processing unit and the consolidated data network of the applicant is not merely "use of or the right to use any industrial, commercial or scientific equipment", as envisaged in article 12(3)(b) of the DTAA but more than that. From the transactions of the applicant with the Indian company it is quite clear that the central processing unit/consolidated data network of the applicant are modern technological designs or models involving customised communication and computation with application of sophisticated information-technology requiring constant upkeep and updating so as to meet the challenge of the advance of technology in this area. It is the use of embedded secret software (an encryption product) developed by the applicant for the purpose of processing raw data transmitted by XT which would clearly fall within the ambit of article 12(3)(a) of the Double Taxation Avoidance Agreement between India and the U.S.A.

21. It was submitted by the learned counsel for the Appellant that in the present case, the appellant did not have any right to access the mainframe of the computer at Singapore. The Appellant can only send data to the mainframe and receive back processed data in a particular form. The right

to access is thus a very crucial distinction and in the light of the definition of royalty both under the Act as well as DTAA, the payment in question is a business receipt in the hand of SPL and not royalty. It was submitted by him that the decision of the AAR relied upon by the Revenue authorities have been rendered based on a set of facts which are totally different from the facts of the Appellant's case.

22. The learned counsel for the appellant submitted that the learned CIT(A) had placed reliance on the decision of the Delhi ITAT in the case of Asia Satellite Telecommunication Co. Ltd. 85 ITD 478 (Del) and that decision has since been reversed by the Hon'ble Delhi High Court (reported in 332 ITR 340(Delhi)). He pointed out that the ruling of the Hon'ble Delhi High Court supports the case of the Appellant. In the case of Asia Satellite Telecommunication Co. Ltd. (Supra), the facts were, Asia Sat, registered in Hong Kong, derived income from leasing transponder capacity on the satellites, owned and operated by it, to various customers to enable them to relay (ie uplink and downlink) their signals in Indian and non-Indian territories. To provide these transmission services, Asia Sat used its own assets and infrastructure comprising the satellite and control centre, which are located outside India. The assets and the processes embedded in them are controlled, operated and maintained by Asia Sat. Asia Sat did not exercise any control over the signals uplinked/downlinked by its customers. Asia Sat claimed it was not subject to tax in India. The Revenue held that the fee received by Asia Sat from persons using transponder was Royalty under section 9(1)(vi) of the Act and was taxable as royalties under the Act. On appeal, the ITAT upheld the claim of the Revenue in this regard. On further appeal by the Assessee, the Hon'ble Delhi High Court held that the meaning of the term 'process' being a series of actions or steps taken in order to achieve a particular end, in the present case it is evident that the particular end ie viewership was achieved only through a series of steps taken by receiving the uplinked signals, amplifying them and relaying them

after changing the frequency in the footprint area including India. The applicability of the provisions of section 9(1)(vi) of the Act, would depend on nature of services provided by Asia Sat to its customers as per the agreement executed between them. The substance of the agreement between Asia Sat and its customers is the provision of broadband capacity available on the transponder by Asia Sat and not the right to use any process embedded therein. The data sent by the customers does not undergo any change for improvement through the media of the transponder. Thus the revenues earned by Asia Sat cannot be on account of providing its customers a right to use a process or equipment as the ultimate control on the process and equipment resides with Asia Sat. The High Court has categorically stated that in its view, Asia Sat's customers do not make a payment for the use of a process. The transponder is an inseverable part of the satellite and cannot function without the continuous support of various systems and components of the satellite. Consequently it is incorrect to assume that a transponder is a self-contained unit, the control and constructive possession of which can be handed over by the satellite operator to the customer. Asia Sat was the operator of the satellites and continued to be in control of the satellites and had not leased the satellite to its customers.

23. The learned counsel for the Appellant pointing out to the above decision of the Hon'ble Delhi High Court submitted that in the case of appellant, the appellant had no right to use the mainframe. He highlighted the fact that the ultimate control of the mainframe computer lies with SPL at Singapore and the fact that the substance of the agreement was the use of capacity of mainframe computer of SPL. Thus there was no right to use a process.

24. Further reliance was placed by the learned counsel for the Assessee on the decision of the AAR in the case of Dell International Services (India)

P.Ltd., In Re 305 ITR 37 (AAR). The applicant before the AAR in the said case was a Non-resident, which was a Parent company of an Indian company, which entered into an agreement with non-resident company for providing Indian company with two-way transmission of voice and data through telecom bandwidth. The Indian company did not have any right over equipment of foreign company. The Fixed monthly charges paid by Indian company was held to be not in the nature of rent as there was no “use” of equipment in the legal sense. It was also held that it was not in the nature of “royalty”. The AAR ruled that the monthly recurring charges could not be brought within the sweep of clause (iva) of Explanation 2 to section 9(1)(vi) of the Income-tax Act, 1961, or article 12(3) of the Agreement for Avoidance of Double Taxation and Fiscal Evasion between India and the U. S. A. The word “use” in relation to equipment occurring in clause (iva) was not to be understood in the broad sense of availing of the benefit of an equipment. The context and collocation of the two expressions “use” and “right to use” followed by the word “equipment” indicated that there must be some positive act of utilization, application or employment of equipment for the desired purpose. If an advantage was taken from sophisticated equipment installed and provided by another, it could not be said that the recipient/customer “used” the equipment as such. The customer merely made use of the facility, though he did not himself use the equipment. That the entire network consisting of under-sea cables, domestic access lines and the BT equipment, whichever was kept in the connecting point was providing a service to facilitate transmission of voice and data across the globe. One of the many circuits forming part of the network was devoted and earmarked to the applicant. Part of the bandwidth capacity was utilized by the applicant. From this it did not follow that the entire equipment and components constituting the network were rented out to the applicant or that the consideration in the form of monthly charges was intended for the use of the equipment owned and installed by BT. Assuming that the circuit was

equipment it could not be said that the applicant used the equipment in any real sense. By availing of the facility provided by BT through its network/circuits, there was no usage of the equipment by the applicant except in a very loose sense, such as using a road, bridge or a telephone connection. What was contemplated by the word “use” in clause (iva) of Explanation 2 to section 9(1)(vi) was that the customer came face to face with the equipment, operated it or controlled its functions in some manner. But if it did nothing to or with the equipment and did not exercise any possessory rights in relation thereto, it only made use of the facility created by the service provider who was the owner of the entire network and related equipment. There was no scope to invoke clause (iva) in such a case because the element of service predominated. The predominant features and underlying object of the agreement unerringly emphasized the concept of service. That even where an earmarked circuit was provided for offering the facility, unless there was material to establish that the circuit/equipment could be accessed and put to use by the customer by means of positive acts, it did not fall within the category of “royalty” in clause (iva) of Explanation 2 to section 9(1)(vi) of the Act. That the payment by the applicant to BT was also not in the nature of “royalty” within the meaning of clause (iii) of Explanation 2 to section 9(1)(vi) as well of article 12(3) of the Agreement for Avoidance of Double Taxation and Fiscal Evasion between India and the U. S. A.

25. Reliance was placed on the decision of the AAR in the case of ISRO Satellite Centre (ISAC), In Re 307 ITR 59 (AAR). The applicant before the AAR entered into a contract with Inmarsat Global of the U. K. for leasing of the Inmarsat navigation transponder capacity, under which it had taken on lease the space segment capacity of L1 and L5 transponder centered on an Inmarsat 4th generation satellite, making an orbit at 36,000 km altitude

above the earth's atmosphere. The capacity was utilized through data commands sent from a ground station set up by the applicant to that transponder out of many which was for navigation purposes which dispatched signals in space on two specified frequencies. The corrected or augmented data sent from the satellite and transmitted by the transponder were used for better navigational accuracies. The applicant paid a fixed annual charge regardless of the actual use of transponder capacity. On these facts the applicant sought the ruling of the Authority on the questions (i) whether the payment to Inmarsat Global of the U. K. for leasing of transponder was not royalty within the meaning of article 13 of the Agreement for Avoidance of Double Taxation between India and the U. K. ; and (ii) whether the applicant had to deduct tax at source under section 195 of the Income-tax Act, 1961, in respect of the lease amount. The Authority ruled that the applicant could not operate the transponder in space. It would only be transmitting/uplinking the augmented data to the navigation transponder. In the course of carrying out its objectives and operations the applicant would not be using any equipment of Inmarsat Global of the U. K. satellite or transponder. The applicant only needed to adjust or tune its system to access the navigation transponder space segment capacity. By earmarking a space segment capacity of the transponder for use by the applicant, the applicant did not get possession (actual or constructive) of the equipment of Inmarsat Global of the U. K. ; nor did the applicant use any equipment of Inmarsat Global of the U. K. Lease of space segment capacity only meant that a segment of the navigational transponder through which the data passed was allocated to the applicant so that it could utilize for the specific purpose of making available the augmented data sent by the applicant through its ground station to the users extensively. The expression "use of space segment capacity" of the transponder had no reference to any operations performed by means of the transponder. The operation and regulation of the transponder remained always with Inmarsat Global of the

U. K. The payment made by the applicant could not, therefore, be regarded as payment made for the use of the equipment of Inmarsat Global of the U.K.

26. Further reliance was placed on the decision of the ITAT Mumbai in the case of Kotak Mahindra Primus Ltd. Vs. DCIT 105 TTJ (Mumbai) 578. The question before the Tribunal was as to whether the appellant before the Tribunal which was in the business of providing finance for purchase of cars, was required to deduct tax at source on payments made to M/s. Ford Credit Australia Ltd., Australia, a non-resident, the payment being an annual Maintenance fee charge for right to have system updates released by Ford Credit and access to Ford Motor Company and/or its affiliates overseas based mainframe computer system and its software applications for the running and operating business operations. The Tribunal held the Indian company did not have any control over, or physical access to, the mainframe computer in Australia and therefore the payment was not for use of equipment. In this regard the Tribunal ruled that Indian company does not have any control over the mainframe computer or physical access to the mainframe computer and that the payment is for act of specialized data processing by the Australian company.

27. The learned D.R. relied on the orders of the revenue authorities. It was submitted by her that one has to look at the agreement to find out the nature of payment rather than the case laws. In this regard, she took us through the agreement and submitted that the agreement merely provides for the right to use the mainframe of SLP at Singapore to the Assessee. In this regard, she submitted that there is nothing in the agreement to show that there was processing of data by SLP. In this regard it was also submitted by her that a mere confirmation from Atos Origin would not be

sufficient to prove the case of the appellant that SLP rendered service of data processing to the appellant. She relied on the decision of the AAR in the case of P.No.30 of 1999 (Supra) which the AO has also referred to in his order. Further reliance was placed on the decision of the ITAT Hyderabad Bench in the case of Frontline Soft Ltd. Vs. DCIT 12 DTR (Hyd)(Trib.) 131 wherein it was held that payment made by an Assessee to a Non-resident US company for availing connectivity facility to enable the Assessee to generate and to cater to outbound PSTN calls within USA through co-located equipment comprising of multimodal switches (MUX) belong to the US Company and located in USA with a certain bandwidth alongwith maintenance services is use of MUX and ancillary equipments belonging to US Company which is commercial and scientific equipment, hence royalty within the meaning of clause (iva) of Expln.2 to Sec.9(1)(vi) inserted wef 1/4/02 r.w. Article 12(3)(b) of Indo-US DTAA. It was further held that payment for use of software belonging to non-resident and payment made for such use would be royalty. Reliance was placed on the decision of the AAR in the case of Cargo Community Network Pte Ltd. In Re 289 ITR 355(AAR) wherein the question that was considered was as to whether Providing access to internet based air cargo portal outside India which an Indian subscriber paying fees for access and use of portal for booking cargo with airlines, training subscribers and help connected therewith and Fees paid for such use, is income that can be said to arise in India and whether they are in the nature of royalties and fees for technical services. The AAR held that the fee so paid is Royalty and Fees for technical services and therefore Taxable in India. Reference was made to the decision of the Delhi Bench of ITAT in the case of Millennium Infocom Technologies Ltd. Vs. ACIT 117 ITD 114 (Delhi) relating to AY 01-02, wherein the question was whether payment for hosting websites on servers in USA i.e., whereby space is provided on the servers by the non-resident for the purpose of hosting website was royalty. The Tribunal ruled that clause (iva) to Expln.2 to Sec.9(1)(iv) was inserted by

the finance Act, 2001 w.e.f. 1-4-2002 whereby the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in Sec.44BB was to be treated as royalty. Since the case related to AY 01-02 the tribunal held that the payment was not royalty. According to the learned D.R. the case of the Assessee being one relating to period after 1-4-2002, the payments should be treated as covered by clause(iva) to Expln.2 to Sec.9(1)(iv) of the Act. Reference was also made to the India's objections to the OECD commentaries regarding use and right to use scientific equipments in the context of royalty as opined therein.

28. The learned counsel for the appellant in rejoinder submitted that it is too late in the day for the learned D.R. to contend that the nature of services rendered by SPL is not data processing. In this regard, he again drew our attention to the findings of the AO as well as CIT(A) in their orders. It was also submitted by him that the appellant filed confirmation from SPL regarding the nature of services rendered by SPL and the AO and the CIT(A) did not express any adverse opinion about the confirmation of SPL. In this regard it was submitted by him that the revenue authorities proceeded under the assumption that the nature of services rendered by SPL was data processing. The learned counsel for the appellant also distinguished the cases cited on behalf of the revenue.

29. We have very carefully considered the rival submissions. At the outset we have to reject the argument of the learned D.R. regarding the absence of evidence to show that SPL carried out the work of data processing for the appellant at Singapore. In this regard, we have already noticed that the Agreement is not clear in as much as there is no reference to any data processing to be carried out by SPL at Singapore. We have also referred to

the fact that the RBI permissions refer to the payment by the appellant to SPL as towards data processing to be carried out by SPL at Singapore. Before the AO the Appellant has explained the nature of the transaction between the appellant and SPL. SPL also filed a confirmation before the AO regarding the nature of services rendered by it to the appellant. The AO did not at any stage dispute or call for any additional evidence regarding the claim made by the appellant before him. It is not open to the learned D.R. at this stage to raise dispute regarding the nature of services claimed to have been rendered by SPL. We therefore have to proceed on the basis of the agreement and the claim made by the appellant before the AO.

30. The nature of services rendered is very important to come to a conclusion as to whether the payment by the appellant to SPL is in the nature of Royalty. The facts are therefore recapitulated. SPL had a Data Centre at Singapore and it agreed to make available for exclusive use by the appellant the From November 6th 1996 to 5th December 2001 inclusive 32 MIPS and 100 Gigabytes and thereafter increased capacity. It is not in dispute that the tenure of this agreement was further extended to cover the period in dispute in these appeals. The Agreement does not make any reference to any data processing to be carried out by SPL for the appellant at Singapore. However, clause-8 of the Agreement mentions that the appellant will have the right to utilize any residual capacity at no extra cost on the same terms in connection with any other similar requirement it may have for data processing to be performed in Singapore. Further, the permission granted by Reserve Bank of India to the appellant vide letter dated 6/11/1996, shows that SPL was carrying out data processing for the appellant at Singapore. As per the agreement appellant was required to pay SPL fixed monthly installments with effect from January 1, 1998 over a period of 60 months. The Reserve Bank of India (RBI) had granted permission to renew the agreement between the appellant and SPL for data

processing at SPL's Data Centre at Singapore vide letter of RBI dated December 19, 2001 subject to conditions stipulated in their letter dated November 6, 1996. The appellant submitted before the AO that the consideration payable to SPL for the data processing services has been computed having regard to the following -

1. Computer hardware and system software for operations of the appellant's computer applications.
2. Computer hardware to support data communications for using the services as stated above.
3. Manpower to handle daily and periodic computer based processing.
4. Suitable environment for housing the computer systems.
5. Disaster recovery capability for the services provided and testing of the same twice a year.

31. The nature of services rendered by SPL to the appellant was explained by the appellant in their letter dated 7.11.2003 in one of the application filed u/s.195(2) of the Act, dated 9/10/2003, for no objection to remit payments to SPL without deduction of tax at source, as follows: (the same was also confirmed by SPL in their confirmation filed before the AO)

1. The input data i.e., the raw data relating to branch transactions is fed by appellant via application software owned by it and then transmitted to SPL mainframe computer in Singapore for processing.
2. The application software owned and used by the appellant in this regard is not designed by SPL nor acquired from SPL.
3. After the raw data is transmitted into the hardware facility of SPL in Singapore, SPL staff based in Singapore process the raw data on an application software owned by appellant using the mainframe computer of SPL.
4. The raw data is processed by SPL staff as per the requirements of appellant using the application software owned by the appellant.
5. The processed data, i.e., the output data is transmitted electronically to the appellant in India using the software provided by the appellant, which is not designed by SPL.

32. The case of the Revenue is on two counts. Firstly according to the revenue the payment by the appellant to SPL is in the nature of royalty

because it is a payment falling within Clause (iii) of the Explanation (2) to Sec.9(1)(iv) of the Act and Article 12(3)(a) of DTAA since the payment in question was a consideration for the use of process. According to the revenue SPL has provided a process by providing its computer facility to process the data provided by the appellant. The fact that the software and hardware of the computer system of the SPL has not been designed or manufactured by SPL or the fact that SPL itself did not design, assemble and set up the computer system is no ground to hold that the payment is not for use of any process. SPL without being the owner of the process can obtain various components from the market including copyrighted software or using software and hardware available from the market. It can also design or can get the software and hardware designed for use of its computer system for the efficient processing of data. In clause (iii) of explanation (2) there is no requirement that the process should be a copy right process of which the provider should be the owner. It is sufficient if the provider of a process provides such a process for which payment is made to him.

33. The second reason assigned by the revenue is that the payment falls within the ambit of Expln-2 clause (iva) to sec. 9(1)(vi) of the Act viz., the use or right to use, any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB and Article 12(3)(b) of the Treaty which provides that payment of any kind received as a consideration for the use of, or the right to use any industrial, commercial or scientific equipment.

34. We shall take up for consideration the first reason assigned by the Revenue authorities viz., that the payment in question is a payment for use or right to use process. In this regard, we notice that the AO has made vague observations while concluding that the payment in question is

Royalty. The CIT(A) has held that SPL provided a process by providing its computer facility to process the data provided by the appellant. The CIT(A) has further gone on to hold that the fact that SPL was not manufacturer of the hardware or the software of the computer system will not make any difference. According to CIT(A) there is no requirement in clause (iii) of expln.2 to Sec.9(1)(vi) of the Act that the process should be owned by the person who allows a right to use the process. This line of reasoning of the CIT(A) in our view is fallacious. We have already seen the manner in which the appellants use the mainframe computer owned by SPL. The appellant transmits raw data through operating software owned by it to the hardware facility of SPL in Singapore. SPL merely receives the data so transmitted. Thus at this stage there is no use or right to use any process of SPL by the appellant. The next stage is that the raw data transmitted is processed by SPL staff as per the requirements of appellant using the application software owned by the appellant. At this stage the appellant does not use or have any right to use any process. Consideration paid for carrying out processing is not a payment for use or right to use a process. The third stage is that the processed data, i.e., the output data is transmitted electronically to the appellant in India using the software provided by the appellant, which is not designed by SPL. Even at this stage there is no use or right to use any process. The application software by which data is transmitted to hardware at Singapore and processed by SPL at Singapore is owned by the appellant. Thus what is used by the Appellant is the Computer hardware owned by SPL. The payment in question can therefore be said to be a payment for a facility which is available to any person willing to use the facility as laid down by the Hon'ble Madras High Court in the case of Skycell communications Ltd. Vs. DCIT 251 ITR 53 (Mad). The system software which is embedded in the computer hardware by which the computer hardware functions is not owned by SPL and SPL only has a licence to use the system software. SPL employs manpower to process the data and also

provides disaster recovery. The consideration received by SPL from the appellant is therefore for using the computer hardware which does not involve use or right to use a process. The data is received by application software which is owned by the appellant. The consideration paid by the appellant to SPL is for processing its data. This part of the consideration cannot be said to be a consideration paid for use or right to use process as the processing of the data is done by SPL using the system software owned by the appellant. Therefore it cannot be said that the payment by the appellant to SPL is Royalty within the meaning of Article 12(3)(a) of the treaty.

35. The CIT(A) in coming to the conclusion to the contrary has placed reliance on the decision in the case of Asia Satellite Telecommunication Co. Ltd. 85 ITD 478 (Del)(SB) for the proposition that process need not be secret process and that the definition in Sec.9(1)(vi) Expln.2 and the treaty are one and the same. The aforesaid decision of the Special Bench has since been reversed by the Hon'ble Delhi High Court in the case of Asia Satellite Telecommunications Co. Vs. CIT 332 ITR 340 (Del) wherein it was held that where transponder is allowed to be used for transmitting signals, it would not amount to allowing right to use process. The decision of the AAR in the case of P.No.30 of 1999 (supra) is materially different from the facts as it prevails in appellant's case. In the case before AAR, an entity (Non-Resident) maintained a centralised computer in the USA. The centralised computer or the central processing unit (CPU) which was accessed and used by various group entities located worldwide through a consolidated data network maintained in Hong Kong. The transactions done by a traveller in a particular country were reported to a centralised computer in that country. In India, this was done by an Indian company, located at Delhi. The said Indian company received information on computer through telephonic and

microwave links about the use of credit cards and travellers' cheques by travellers all over the country. The Indian company also serviced thirteen group companies in Asia and the Pacific, in a similar manner. The Non-resident charged the Indian company, for the use of its computer set up in Hong Kong and that in the USA. As can be seen from the facts of the aforesaid case, the Indian company had a right to access the data by having access to the computer maintained at USA. In the present case before the Tribunal, the appellant did not have any right to access the mainframe of the computer at Singapore. The Appellant can only send data to the mainframe and receive back processed data in a particular form. In the case before the AAR, the right to access the software (by encryption) of the non-resident was a right to use secret process and this is a very crucial distinction. Thus the facts that prevailed in the case before AAR are totally different from the facts of the Appellant's case.

36. The decision relied upon by the learned counsel for the Appellant in the case of Kotak Mahindra Primus Limited (supra), that payment made for specialized data processing of raw data using mainframe computers located abroad is not liable to tax as royalty and the company is not liable to withhold tax from such payments in our view is squarely applicable to the facts of the present case. Kotak Mahindra Primus Ltd., the taxpayer, an Indian Company, was engaged in the business of providing finance for purchase of cars. The company was jointly formed by Kotak Mahindra Finance Limited, India and Ford Credit International Inc., USA (FCII). The company which is engaged in the business of providing finance for purchase of cars, had entered into a data processing agreement with Ford Credit Australia Limited (FCAL) to enable it to upload the raw data in the mainframe computer in Australia and the output data, after due processing would be transmitted back to the company. The fee payable had a fixed

component for annual maintenance and licensing charges and a variable component based on the amount of data processed. On the above facts, the question that was to be considered by the Tribunal was as to whether the payment by the taxpayer was Royalty and therefore taxable in India and therefore there was an obligation to withhold tax at source at the time of making payment to the non-resident. The Tribunal held that though the payment had a fixed and a variable component they had to be taken together and not in isolation. The fixed fee did not give any independent rights to the Indian company as it was only paid as the company could not avail the unit cost of processing unless the fixed fee was paid. The Tribunal held that both these payments taken together were only payments for processing of data. The Tribunal further observed that no part of the payment could be said to be for use of specialized software on which data is processed as no right or privilege were granted to the company to independently use the computer. The company had no control over the actual processing of data which was exclusively controlled by FLCA. It was further observed that the company did not have any physical access or control over the mainframe computer therefore it could not be said that the payment was for the use or right to use of mainframe computer. The Tribunal held that the payment was being made for data processing and not for the use of the computer though the use of the computer was an important aspect of the activity of data processing. The Tribunal did not accept the Ruling of the Authority for Advance Rulings (AAR) in the case of P.No.30 of 1999 In re (supra) where it was held that such payments are in the nature of royalty and therefore subject to tax. The Tribunal held that it was not in agreement with the views of the AAR . The Tribunal also observed that the decisions of the AAR could at best only have a persuasive value and the ruling was only binding on the applicant and therefore they were not obliged to follow it. For the reasons given above, we hold that the payment by the appellant to SPL is not “Royalty” within the meaning of Article 12(3)(a) of the treaty.

37. We shall now examine the second reason assigned by the revenue authorities for treating the payment in question as royalty viz., consideration paid for use or right to use any industrial, commercial or scientific equipment within the meaning of Article 12(3)(b) of the Treaty.

38. The conclusion of the CIT(A) in this regard was that the payment being made by appellants to SPL was for the purpose of availing CPU and disc capacity and supporting tape subsystem capacity i.e. the capacity which has been created for the exclusive use of appellants. The further reasoning is that though the appellants do not have any physical possession of the property, it is exercising constructive control over the infrastructure facilities because these facilities can be utilized only by the appellants as per the terms of agreements. According to CIT(A), the arrangement was one of renting out disc space in the hardware system of SPL in favour of the appellants and the payments made by appellants to SPL is for right to use the scientific equipments.

39. The meaning of the expression “use or right to use” as used in Article 12(3)(b) has to be first understood. In the case of ISRO Satellite Centre (ISAC), In Re (Supra), the AAR had to decide whether the consideration paid by ISRO to Inmarsat Global of the U. K. for leasing of the Inmarsat navigation transponder capacity, would be Royalty under the DTAA between India and U.K. The Authority after looking into the nature of the agreement, ruled that by earmarking a space segment capacity of the transponder for use by the applicant, the applicant did not get possession (actual or constructive) of the equipment of Inmarsat Global of the U. K. ; nor

did the applicant use any equipment of Inmarsat Global of the U. K. The payment made by the applicant could not, therefore, be regarded as payment made for the use of the equipment of Inmarsat Global of the U. K. This decision was followed by the Hon'ble Delhi High Court in the case of Asia Satellite Telecommunications Ltd. (supra). In the case of Dell International Services (India) P.Ltd. In Re (supra) it was held the word "use" in relation to equipment occurring in clause (iva) was not to be understood in the broad sense of availing of the benefit of an equipment. The context and collocation of the two expressions "use" and "right to use" followed by the word "equipment" indicated that there must be some positive act of utilization, application or employment of equipment for the desired purpose. If an advantage was taken from sophisticated equipment installed and provided by another, it could not be said that the recipient/customer "used" the equipment as such. The customer merely made use of the facility, though he did not himself use the equipment. What was contemplated by the word "use" in clause (iva) of Explanation 2 to section 9(1)(vi) was that the customer came face to face with the equipment, operated it or controlled its functions in some manner. But if it did nothing to or with the equipment and did not exercise any possessory rights in relation thereto, it only made use of the facility created by the service provider who was the owner of the entire network and related equipment. There was no scope to invoke clause (iva) in such a case because the element of service predominated. The predominant features and underlying object of the agreement unerringly emphasized the concept of service. That even where an earmarked circuit was provided for offering the facility, unless there was material to establish that the circuit/equipment could be accessed and put to use by the customer by means of positive acts, it did not fall within the category of "royalty" in clause (iva) of Explanation 2 to section 9(1)(vi) of the Act. The ITAT Mumbai in the case of Kotak Mahindra Primus Ltd. (supra) has also taken a similar view.

40. Though the payment made for the user of equipment, is included in the scope of “royalties” under the UN model tax treaties, the same is currently not included in the scope of “royalties” under the OECD model tax treaties. Earlier, the OECD model tax treaties contained such a provision, however, by virtue of the amendments made to such model in the year 1977, payment made for the user of equipment, was deleted from the scope of “royalties”. However, in a Report to Working Party No.1 of the OECD Committee on Fiscal Affairs, submitted by the Technical Advisory Group of OECD on Treaty Characterization of Electronic Commerce Payments, dated February 1, 2001, the Technical Advisory Group of OECD specifically considered the scope of payments made for the user of equipment in the context of electronic commerce related issues. Since a number of tax treaties across the world still covered such payments within the scope of “royalties”. Commenting upon under what circumstances a computer hardware, namely an equipment, could be said to have been made available for user to a customer, the Technical Advisory group of OECD brought out the following “tests”, the fulfillment of all or some of which would render the transaction to be user of equipment-

- a) The customer is in physical possession of the property.
- b) The customer control the property.
- c) The customer has a significant economic or possessory interest in the property.
- d) The provider does not bear any risk of substantially diminished receipts or substantially increased expenditure if there is non-performance under the contract.
- e) The provider does not use the property concurrently to provide significant services to entities unrelated to the service recipient.
- f) The total payment does not substantially exceed the rental value of the equipments for the contract period.

On a close reading of the said ‘tests’ suggested by the Technical Advisory Committee of OECD, it appears that in order to constitute user of equipment, the customer should actually have domain or control over the equipment, or in other words, the equipment should be at its disposal. The customer should be in a position to use the equipment in its business activities. However, if a customer is given the mere access to some infrastructural facilities of the service provider, in a situation where the service provider has all the control, disposition and possession of such infrastructure and also the service provider operates such infrastructure on its own, then the customer cannot be said to have been assigned a right to use the equipment in the form of the infrastructure. In that case, the transaction partakes of the character of provision of services or facilities by the owner of the infrastructure in favour of the customers, as against giving the infrastructure to the customer itself for being used in the manner desired by the customer. Incidentally, the Technical Advisory Committee of OECD has expressly clarified that data warehousing services would not give rise to user of equipment, since the customer does not have possession or control over the equipment and shall utilize the equipment concurrently with other customers.

41. The facts of the present case are that SPL has a Data Centre at Singapore and as per the agreement between the appellants and SPL it has to make available for exclusive use by the appellant 32 MIPS and 100 Gigabytes in its computer hardware at its Data Centre in Singapore. From November 6th 1996 to 5th December 2001. From March 6th 1997 to 5th December, 2001 an additional 20 MIPS and 100 Gigabytes has to be made available making a total of 52 MIPS and 200 Gigabytes in this period. SPL has to provide to the appellants, the following elements:

- Maintenance CPU
- Disc space

- 36 track tape subsystem
- Staff
- Site Preparation
- Upgrade to communications front end processor
- System software
- Disaster recovery (In line with Contractual levels.)

We have already seen the nature of services rendered by SPL to the appellants. The appellants as already seen have no right to access the computer hardware except for transmitting raw data for further processing. The appellants have no control over the computer hardware or physical access to it. There is nothing to show positive act of utilization, application or employment of equipment for the desired purpose. The appellants cannot come face to face with the equipment, operate it or control its functions in some manner. The appellants had no possessory rights in relation to the computer mainframe. The appellants took advantage of a facility of use of sophisticated equipment installed and provided by another, it could not be said that the recipient/customer "used" the equipment as such. The appellant merely made use of the facility, though they did not themselves use the equipment. There is nothing on record to establish that the hardware could be accessed and put to use by the appellants by means of positive acts. Therefore it cannot be said that the payment is royalty within the meaning of Article 12(3)(b) of the treaty.

42. The learned D.R. has placed reliance on the decision of the AAR in the case of Cargo Community Network Pte.Ltd. In Re (Supra). The question that was considered by the AAR was as to whether Providing access to internet based air cargo portal outside India which an Indian subscriber paying fees for access and use of portal for booking cargo with airlines, training subscribers and help connected therewith and Fees paid for such use, is income that can be said to arise in India and whether they are in the nature

of royalties and fees for technical services. The AAR held that the fee so paid is Royalty and Fees for technical services and therefore Taxable in India. As rightly contended on behalf of the Appellant, the right to access various airlines for booking cargo is a vital distinction. In such cases, there is a positive right to use the equipment. The decision in the case of Frontline soft Ltd. (Supra) is a case where mere right to use an equipment was held to fall within the ambit of clause(iva) of Expln.-2 of Sec.9(1)(vi) of the Act. The tribunal in coming to the above conclusion followed the ruling of the ITAT Delhi Special Bench in the case of Asia Satellite Telecommunications Co. Ltd. Vs. DCIT 78 TTJ (Del) 489, which has been overruled by the Hon'ble Delhi High Court in the case of Asia Satellite Telecommunications Co. Ltd. (Supra). We are of the view that the proposition laid down in this decision is contrary to the decision of the Hon'ble Delhi High Court in the case of Asia Satellite (supra). The decision in the case of Millennium Infocom Technologies Ltd. Vs. ACIT(Supra) was a case where the question was whether payment for hosting websites on servers in USA i.e., whereby space is provided on the servers by the non-resident for the purpose of hosting website was royalty. The Tribunal ruled that clause (iva) to Expln.2 to Sec.9(1)(iv) was inserted by the finance Act, 2001 w.e.f. 1-4-2002 whereby the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in Sec.44BB was to be treated as royalty. Since the case related to AY 01-02 the tribunal held that the payment was not royalty. According to the learned D.R. the case of the Assessee being one relating to period after 1-4-2002, the payments should be treated as covered by clause(iva) to Expln.2 to Sec.9(1)(iv) of the Act. In our view the decision rendered as above cannot be said to be strictly a precedent as the issue was neither discussed or argued by the parties. Besides the above, the said decision is contrary to decision of the Hon'ble Delhi High Court in the case of Asia Satellite (supra). The decisions relied upon by the learned D.R. do not therefore support the case of the revenue.

We therefore hold that the payment by the appellants to SPL is not royalty within the meaning of Article 12(3)(b) of the treaty.

43. For the reasons stated above, we allow all the appeals by the Assessee.

44. ITA No. ITA NO.1457/MUM/2008 for AY 04-05: This appeal is by SPL against the order of CIT(A) XXXI, Mumbai dated 27/12/2007 for AY 2004-05. The grounds of appeal raised in this appeal by the Assessee reads as follows:

“On the facts and circumstances of the case and in law, the learned Commissioner of Income-tax (Appeals) XXXI [CIT(A)] erred in confirming the following grounds:

- 1.1 That on the facts and in the circumstances of the case, the learned Commissioner of Income Tax (Appeals) XXXI, Mumbai (hereinafter referred to as ‘CIT(A)’) erred in confirming the decision of the Assessing Officer (‘AO’) that the amount of INR 31,96,97,753/- payable to Atos Origin IT Services Singapore Pte Ltd. (“ATOS”) is liable to tax in India as royalty income under Section 9(1)(vi) of the Income Tax Act, 1961 (“the Act”) as well as Article 12(3)(a) of the Double Taxation Avoidance Agreement (“DTAA”).
- 1.2 The learned CIT(A) has erred on facts and in law in directing the AO to grant relief to Atos only to the extent of levying taxes twice on the income appearing in the erroneous Tax Deducted at Source (“TDS”) certificate. In doing so, the learned CIT(A) has failed to appreciate that the TDS certificate bearing no.SCB-02-03-1 is erroneous in nature and the same has been withdrawn by the entity issuing the same. In light of such withdrawal, the total income mentioned in the erroneous TDS certificate should not be charged to tax at all.”

45. The assessment has been made by the AO on the basis that the payment received by SPL from the appellants, viz., Standard Chartered Bank was “Royalty” and therefore taxable in India. The payments received by the Assessee were brought to tax accordingly. The order of the AO was confirmed by the CIT(A) giving rise to the present appeal by the Assessee before the Tribunal.

46. It is not in dispute before us that the facts and circumstances giving rise to this appeal is identical to the case of Standard Chartered Bank. The reasons given while deciding the appeals of standard Chartered Bank would equally apply to this appeal. For the reasons stated therein, we hold that the receipts by the Assessee from Standard Chartered Bank are in the nature of business income and since the Assessee does not have PE in India, the same is not taxable in India in accordance with Article 7 of the DTAA. The appeal by the Assessee is accordingly allowed.

47. In the result, all the appeals are allowed.

Order pronounced in the open court on the 11th day of May, 2011.

Sd/-

(B.RAMAKOTAIAH)
ACCOUNTANT MEMBER

Sd/-

(N.V.VASUDEVAN)
JUDICIAL MEMBER

Mumbai, Dated. 11th May, 2011

Copy to: 1. The Appellant 2. The Respondent 3. The CIT City –concerned
4. The CIT(A)- concerned 5. The D.R”L” Bench.

(True copy)

By Order

Asst. Registrar, ITAT, Mumbai Benches
MUMBAI.

Vm.

	Details	Date	Initials	Designation
1	Draft dictated on	2/5/11		Sr.PS/PS
2	Draft Placed before author	5/5/11		Sr.PS/PS
3	Draft proposed & placed before the Second Member			JM/AM
4	Draft discussed/approved by Second Member			JM/AM
5.	Approved Draft comes to the Sr.PS/PS			Sr.PS/PS
6.	Kept for pronouncement on			Sr.PS/PS
7.	File sent to the Bench Clerk			Sr.PS/PS
8	Date on which the file goes to the Head clerk			
9	Date of Dispatch of order			