

**IN THE INCOME TAX APPELLATE TRIBUNAL
"C" BENCH: BANGALORE**

**BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SHRI KESHAV DUBEY, JUDICIAL MEMBER**

IT(IT)A No.811/Bang/2024 & SP No.22/Bang/2024
Assessment Year: 2017-18

KDDI Corporation 2-3-2, NishiShinjuku Shinjuku-Ku Tokyo Japan 1638003 PAN NO : AAICK5961D	Vs.	DCIT (IT) Circle-2(1) Bangalore
APPELLANT		RESPONDENT

Appellant by	:	Sri Ajit Prasad, Sr. A.R.
Respondent by	:	Ms. Neera Malhotra, D.R.

Date of Hearing	:	05.06.2024
Date of Pronouncement	:	05.06.2024

O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER:

This appeal by assessee is directed against order of DCIT (International Taxation) Circle-2(1), Bengaluru for the assessment year 2017-18 passed u/s 143(3) r.w.s. 147 r.w.s. 144C(13) of the Income Tax Act, 1961 (in short "The Act"). The assessee has raised following concise grounds of appeal:

- "On the facts and circumstances of the case and in law, the final assessment order passed by the Learned Deputy Commissioner of Income-tax (International Taxation), Circle — 2(1), Bangalore ("Ld. AO"), under section 143(3) read with section 147 and section 144C(13) of the Income-tax Act, 1961 ("the Act") assessing the income of the Appellant at INR 2,34,34, instead of returned income of INR 2,34,34,767/- is bad in law.*
- On the facts and in the circumstances of the case and in law, the Hon'ble Dispute Resolution Panel -- 2, Bengaluru (" Ld. DRP") has erred in confirming the validity of initiation of the proceedings under section 147 of the Act in the case of the Appellant merely on the basis of proceedings initiated against Vodafone*

South Limited ("VSL") under section 201 of the Act without analyzing the facts of present case and jurisprudence in this regard.

3. *On the facts and in the circumstances of the case and in law, the Ld. DRP/ AO erred in holding that the interconnect usage charges amounting to INR 2,29,02,314/- received by the Appellant from various Indian Telecom Operators ("ITOs") accrues or arise in India and are in the nature of 'Royalty' under the provisions of the Act and India-Japan Double Taxation Avoidance Agreement ("DTAA").*
4. *On the facts and in the circumstances of the case and in law, the Ld. DRP/AO has erred in not following the ratio laid down by the Hon'ble Jurisdictional High Court in case of Vodafone Idea Limited v. DDIT (International Taxation) [(2023) 457 ITR 189 (Karnataka)] holding that payment for interconnect usage charge is not chargeable to tax as 'royalty'.*
5. *On the facts and in the circumstances of the case and in law, the Ld. DRP has erred in holding that the interconnect usage charges would fall under residuary Article 22 of India — Japan DTAA.*
6. *On the facts and in the circumstances of the case and in law, the ld. AO grossly erred in not granting the credit of tax deducted at source amounting to INR 1,09,683/- claimed by the appellant in the return of income."*

2. After hearing both the parties, we are of the opinion that similar issue came for consideration before this Tribunal in assessee's own case for the assessment years 2013-14 to 2015-16 vide order in IT(IT)A No.100 to 102/Bang/2024 dated 15.4.2024, wherein held as under:

7.1 *We note that the revenue characterised the payments received by assessee towards interconnectivity utility charges as 'Royalty', since the payment is made to "use the process" or "an equipment".*

7.2 *It is an admitted fact that various service providers in India entered into agreement with assessee for international carriage and connectivity services against which an interconnectivity charges are received by the assessee. We refer to the term "Process" occurs under clause (i), (ii) and (iii) to Explanation 2 to Section 9(vi). It reads as under:—*

'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;'

7.2.1 The term "process" used under Explanation 2 to section 9(1)(vi) in the definition of 'royalty' does not imply any 'process' which is publicly available. The term "process" occurring under clauses (i), (ii) and (iii) of Explanation 2 to section 9(1)(vi) means a "process" which is an item of intellectual property. Clause (iii) of the said Explanation reads as follows:

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

Clauses (i) & (ii) of the said explanation also use identical terms.

7.2.2 The words which surround the word 'process' in clauses (i) to (iii) of Explanation 2 to section 9(1)(vi), refer to various species of intellectual properties such as patent, invention, model, design, formula, trade mark etc. The expression 'similar property' used at the end of the list, further fortifies the stand that the terms 'patent, invention, model, design, secret formula or process or trade mark' are to be understood as belonging to the same class of properties viz. intellectual property.

7.2.3 We also note that 'Intellectual property' as understood in common parlance means, Knowledge, creative ideas, or expressions of human mind that have commercial value and are protectable under copyright, patent, service mark, trademark, or trade secret laws from imitation, infringement, and dilution. Intellectual property includes brand names, discoveries, formulas, inventions, knowledge, registered designs, software, and works of artistic, literary, or musical nature.

7.2.4 We refer to the commentary in Prof.Klaus Vogel's Commentary on Double Taxation Convention, wherein, the term 'Royalty' is defined as under:

"Paragraph 2 contains definition of the term 'royalties'. These relate, in general, to rights or property constituting different forms of literary and artistic property, the elements of intellectual property specified in the text and information concerning industrial, commercial or scientific experience. The definition applies to payments for the use of, or the entitlement to use, rights of the kind mentioned, whether or not they have been, or are required, registered in a public register. The definition covers both payments made under a license and compensation which a person would be obliged to pay for fraudulently copying or infringing the right."

7.2.5 Thus the word "process" thus must also refer to specie of intellectual property, applying the rule of, ejusdem generis or noscitur a sociis, as held by Hon'ble Supreme Court in case of CIT vs. Bharti Cellular reported in (2011) 330 ITR 239.

7.2.6 We refer to the decision of Hon'ble Madras High Court in case of CIT vs. Neyveli Lignite Corpn. Ltd. reported in (2000) 243 ITR 459 wherein Hon'ble High Court observed as under:

"10.The term (royalty' normally connotes the payment made to a person who has exclusive right over a thing for allowing another to make use of that thing which may be either physical or intellectual property or thing. The exclusivity of the right in relation to the thing for which royalty is paid should be with the grantor of that right. Mere passing of information concerning the design of machine which is tailor-made to meet the requirement of a buyer does not by itself amount to transfer of any right of exclusive user, so as to render the payment made therefor being regarded as royalty".

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

7.2.8 Further we note that by Finance Act, 2012, Explanation 5 & 6 were added with retrospective effect from 1.6.1976 which reads as under:—

"Explanation 5: For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not - (a) The possession or control of such right, property or information is with the payer; (b) Such right, property or information is used directly by the payer; (c) The location of such right, property or information is in India.

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

7.2.9 By insertion of Explanation 5 & 6, meaning of word 'Process' has been widened. As per these explanations, the word 'Process' need not be 'secret', and situs of control & possession of right, property or information has been rendered to be irrelevant. However, in our opinion, all these changes in the Act, do not affect the definition of 'Royalty' as per DTAA. The word employed in DTAA is 'use or right to use', in contradistinction to, "transfer of all or any rights" or 'use of', in the domestic law. As per Explanation 5 & 6, the word 'process' includes and shall be deemed to included, transmission by satellite (including uplinking,

amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret. However, the Explanation does not do away with the requirement of successful exclusivity of such right in respect of such process being with the person claiming 'royalty' for granting its usage to a third party.

7.2.10 We may also refer to the following decisions of AAR wherein meaning of the phrase “use” or “right to use” has been explained.

The meaning attached to phrase “use” or “right to use” has been explained in following decisions:

- Decision of Authority For Advance Ruling(hereinafter referred to as AAR), in case of Cable & Wireless Networks India(P.)Ltd., In re, reported in (2009) 182 Taxman 76*
- Decision of AAR in case of ISRO Satellite Centre reported in [2008\) 307 ITR 59](#)*
- Decision of AAR in case of Dell International Services (India) P. Ltd.In.re. reported in (2008) 172 Taxman 418.*

7.2.11 The above decisions, lay down that, in order to satisfy 'use or right to use', the control and possession of right, property or information should be with payer.

7.2.12 In the decision of Authority For Advance Ruling, in case of Cable & Wireless Networks India(P.)Ltd., In re(supra), a similar issue was considered wherein Cable & Wireless Networks India(P.)Ltd was a company incorporated in India part of Cable & Wireless Group of companies. Cable & Wireless Networks India(P.)Ltd., was engaged in providing international long distance and domestic long distance telecommunication services in India. As per the agreement Cable & Wireless Networks India(P.)Ltd., would provide the Indian leg of service of using its own network and equipments and network of other domestic operators. Similarly, the international leg of services would be provided by the UK group company using its international infrastructure and equipments. The Cable & Wireless Networks India(P.)Ltd., sought for advance ruling in respect of nature of payments made by Cable & Wireless Networks India(P.)Ltd., to the UK Group company, whether the payment is taxable as ‘royalty’ or ‘FTS’ under section 9(1)(vi)/(vii). The AAR relied on following decisions:

- Decision of Hon’ble Supreme Court in case of BSNL vs. UOI reported in (2006) 3 STT 245*
- Decision of AAR in case of Dell International Services India Ltd. In.re reported in (supra)*
- Decision of Hon’ble Madras High Court in case of CIT vs. Neyveli Lignite Corpn. Ltd. reported in (2000) 243 ITR 459*
- Decision of coordinate bench of this Tribunal in case of WIPRO Ltd. Vs. ITO reported in (2003) 86 ITD 407.*

7.2.13 *The AAR relying on its view in case of Dell International Services India Ltd. In., held as under:*

12.5 *It seems to us that the two expressions 'use' and 'right to use' are employed to bring within the net of taxation the consideration paid not merely for the usage of equipment in praesenti but also for the right given to make use of the equipment at future point of time. There may not be actual use of equipment in praesenti but under a contract the right is derived to use the equipment in future. In both the situations, the royalty clause is invokable. The learned senior counsel for the applicant sought to contend, relying on the decision of Andhra Pradesh High Court in the case of Rashtriya Ispat Nigam Ltd. v. CTO [1990] 77 STC 182 which was affirmed by the Supreme Court, that mere custody or possession of equipment without effective control can only result in use of the equipment whereas a right to use the equipment implies control over the equipment. We do not think that such distinction has any legal basis. In the case of Rashtriya Ispat Nigam Ltd. (supra), what fell for consideration was the expression "transfer of right to use any goods" occurring in a sales-tax enactment. Obviously, where there is a transfer, all the possessory rights including control over the goods delivered will pass on to the transferee. It was in that context, emphasis was laid on 'control'. The Supreme Court affirmed the conclusion of the High Court that the effective control of machinery even while the machinery was in use of the contractor remained with RIN Ltd. which lent the machinery. The distinction between physical use of machinery (which was with the contractor) and control of the machinery was highlighted. The ratio of that decision cannot be pressed into service to conclude that the right of usage of equipment does not carry with it the right of control and direction whereas the phrase 'right to use' implies the existence of such control. Even in a case where the customer is authorized to use the equipment of which he is put in possession, it cannot be said that such right is bereft of the element of control. We may clarify here that notwithstanding the above submission, it is the case of applicant that, it has neither possession nor control of any equipment of BTA.*

12.6 *The other case cited by the learned counsel for applicant to explain the meaning of expressions 'use' and 'right to use' is that of BSNL v. UOI (2006) 3 STT 245 (SC). Even that case turned on the interpretation of the words "transfer of right to use the goods" in the context of sales-tax Acts and the expanded definition of sale contained in clause (29A) of section 366 of the Constitution. The question arose whether a transaction of providing mobile phone service or telephone connection amounted to sale of goods in the special sense of transfer of right to use the goods. It was answered in the negative. The underlying basis of the decision is that there was no delivery of goods and the subscriber to a telephone service could not have intended to purchase or obtain any right to use electro-magnetic waves. At the most, the concept of sale in any subscriber's mind would be limited to the handset that might have been purchased at the time of getting the telephone connection. It was clarified that a telephone service is nothing but a service and there was no sale element apart from the obvious one relating to the handset, if any. This judgment, in our view,*

does not have much of bearing on the issue that arises in the present application. However, it is worthy of note that the conclusion was reached on the application of the well-known test of dominant intention of the parties and the essence of the transaction.

The word 'use' - what it means:

12.7 *Let us now explore the meaning of the key word 'use'. The expression 'use' has a variety of meanings and is often employed in a very wide sense, but the particular meaning appropriate to the context should be chosen. In S.M. Ram Lal &*

Co. v. Secretary to Government of Punjab [1998] 5 SCC 574, the Supreme Court noted that 'in its ordinary meaning', "the word 'use' as a noun, is the act of employing a thing; putting into action or service, employing for or applying to a given purpose". In the New Shorter Oxford Dictionary, more or less the same meaning is given. The very first meaning noted there is: "the action of using something; the fact or state of being used; application or conversion to some purpose". Another meaning given is "Make use of (a thing), especially for a particular end or purpose; utilize, turn to account... cause (an implement, instrument etc.) to work especially for a particular purpose; manipulate, operate". The various shades of meanings given in the decided cases in America are referred to in Words and Phrases, Permanent Edition Vol. 43A. Some of them are quoted below :

"The word 'use' means to make use of; convert to one's service; to avail oneself of; to employ". (Miller v. Franklin County)

"The word 'use' means the purpose served, a purpose, object or end for useful or advantageous nature". (Brown v. Kennedy)

"Use' means to employ for any purpose, to employ for attainment of some purpose or end, to convert to one's service or to put to one's use or benefit. (Beach v. Linington)

"Use', as a noun, is synonymous with benefit and employment and as a verb has meaning to employ for any purpose, to employ for attainment of some purpose or end, to avail one's self, to convert to one's service or to put to one's use or benefit". (Esfeld

Trucking Inc. v. Metropolitan Insurance Co.)

12.8 *The word 'use' in relation to equipment occurring in clause (iva) is 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 words*

"equipment" suggests that there must be some positive act of utilization, application or employment of equip-ment for the desired purpose. If an advantage is taken from sophisticated equipment installed and provided by another, it is difficult to say that the recipient/customer uses the equipment as such. The customer merely makes use of the facility, though he does not himself use the equipment.

13. *It is the contention of the revenue that dedicated private circuits have been provided by BTA through its network for the use of the applicant. The utilization of bandwidth upto the requisite capacity is assured on account of this. The electronic circuits being 'equipment' are made available for constant use by the applicant for transmission of data.*

The access line is installed for the benefit of the applicant. Therefore, the consideration paid is towards rent for circuits and the physical components that go into the system. It is further contended that rendition of service by way of maintenance and fault repairs is only incidental to the dominant object of renting the automated telecommunication network.

13.1 *There is no doubt that the entire network consisting of under-sea cables, domestic access lines and the BT equipment - whichever is kept at the connecting point, is for providing a service to facilitate the transmission of voice and data across the globe. One of the many circuits forming part of the network is devoted and earmarked to the applicant. Part of the bandwidth capacity is utilised by the applicant. From that, it does not follow that the entire equipment and components constituting the network is rented out to the applicant or that the consideration in the form of monthly charges is intended for the use of equipment owned and installed by BTA. The questions to be asked and answered are: Does the avilment of service involve user of equipment belonging to BT or its agent by the applicant ? Is the applicant required to do some positive act in relation to the equipment such as operation and control of the same in order to utilize the service or facility ? Does the applicant deal with any BT equipment for adapting it to its use ? Unless the answer is 'yes', the payment made by the applicant to BTA cannot be brought within the royalty clause (iva). In our view, the answer cannot be in the affirmative. Assuming that circuit is equipment, it cannot be said that the applicant uses that equipment in any real sense. By availing of the facility provided by BTA through its network/circuits, there is no usage of equipment by the applicant except in a very loose sense such as using a road bridge or a telephone connection. The user of BT's equipment as such would not have figured in the minds of parties.*

As stated earlier, the expression 'use' occurring in the relevant provision does not simply mean taking advantage of something or utilizing a facility provided by another through its own network. What is contemplated by the word 'use' in clause (iva) is that the customer comes face to face with the equipment, operates it or controls its functioning in some manner, but, if it does nothing to or with the equipment (in this case, it is circuit, according to the revenue) and does not exercise any possessory rights in relation thereto, it only makes use of the facility created by the service provider who is the owner of entire network and related equipment. There is no scope to invoke clause (iva) in such a case because the element of service predominates.

13.2 *Usage of equipment connotes that the grantee of right has possession and control over the equipment and the equipment is virtually at his disposal. But, there is nothing in any part of the agreement which could lead to a reasonable inference that the possession or control or both has been given to the applicant under the terms of the agreement in the course of offering the facility. The applicant is not concerned with the infrastructure or the access line installed by BTA or its agent or the components embedded in it. The operation, control and maintenance of the so-called equipment, solely rests with BTA or its agent being the*

domestic service provider. The applicant does not in any sense possess nor does it have access to the equipment belonging to BTA. No right to modify or deal with the equipment vests with the applicant. In sum and substance, it is a case of BTA utilizing its own network and providing a service that enables the applicant to transmit voice and data through the media of telecom bandwidth. The predominant features and underlying object of the entire agreement unerringly emphasize the concept of service. The consideration paid is relatable to the upkeep and maintenance of specific facility offered to the applicant through the BTA's network and infrastructure so that the required bandwidth is always available to the applicant. The fact that the international circuit as well as the access line is not meant to offer the facility to the applicant alone but it enures to the benefit of various other customers is another pointer that the applicant cannot be said to be the user of equipment or the grantee of any right to use it. May be, a fraction of the equipment in visible form may find its place at the applicant's premises for the purpose of establishing connectivity or otherwise. But, it cannot be inferred from this fact alone that the bulk of consideration paid is for the use of that item of equipment.

13.3 *In cases where the customers make use of standard facility like telephone connection offered by the service provider, it does not admit of any doubt that the customer does not use the network or equipment of the service provider. But, where the service provider, for the purpose of affording the facility, has provided special infrastructure/network such as a dedicated circuit (as in the instant case), controversies may arise as to the nature of payment received by the service provider because it may not stand on the same footing as standard facility. However, even where an earmarked circuit is provided for offering the facility, unless there is material to establish that the circuit/equipment could be accessed and put to use by the customer by means of positive acts, it does not fall under the category of 'royalty' in clause (iva) of Explanation 2.*

We also refer to the commentary relied by the Ld.Counsel from Prof. Klaus Vogel's Commentary on Double Taxation Convention, wherein 'Secrete formulae or process' is defined as under:

Secret formulae or processes: *This covers Know-how in the narrower sense of the term viz., all business, secrets of a commercial or industrial nature. In most of the countries, they enjoy at least relative protection or are capable of being protected. That is why Article 12(2) very properly use, in connection with such formulae, etc., the criterion 'right to use', which is pertinent to them (letting) as it is in the case of absolute proprietary rights. As a rule, the 'right to use' already come into existence in these instance by authorized information(legitimate disclosure of secrets) . It may be restricted in the point of time in respect of the period following the expiry of the license. On the difference between a product with relatively simple technology, and a business secret.*

We note that, in case of DCIT v. PanAmSat International Systems Inc., reported in (2006) 9 SOT 100, Hon'ble Delhi High Court distinguished the decision of Asia Satellite Telecommunication Co.

Ltd. v. Dy. CIT reported in (2003) 85 ITD 478 and held as under:—

19. The question that first comes up for consideration is whether section 9(1)(vi) of the Income-tax Act, read with the Explanation 2 below thereto, is applicable. This also involves the subsidiary question whether the issue is covered by the order of the Delhi Bench of the Tribunal in the case of Asia Satellite Telecommunication Co. Ltd. (supra) which is also a case of a nonresident company based in Hongkong which owned a transponder and allowed it to be used by broadcasters. Both issues are interlinked in the sense that in the above order the Tribunal has held in the context of the provisions of clause (iii) of Explanation 2 below section 9(1)(vi), that a "process" is involved when the signals that are uplinked through the earth stations to the transponder get converted into different frequencies and fit for being down-linked via earth stations over the footprint area. It was therefore held that the payment was for the use of a "process" and hence royalty within the meaning of the aforesaid clause. The clause reads as follows :

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

It was not disputed before us on behalf of the assessee that the nature of the activity carried on by it is the same as in the case of Asia Satellite Telecommunication Co. Ltd. (supra). If that is so, we have to hold, respectfully following the order of the co-ordinate Bench, that there is a "process" involved in the activity carried on by the assessee before us. In Asia Satellite Telecommunication Co. Ltd.'s case (supra) it was further held that the word "secret" appearing in clause (iii) above qualifies only the word "formula" but not the word "process" and therefore even if the process involved in the operation of the transponder is in the public domain and no longer a secret known only to a few, the payment for the process would still be taxable as royalty. The reason or logic given in paragraph 6.18 of the order by the Tribunal to hold that the word "secret" does not qualify the word "process" is that "there is no comma after the use of the word 'secret' till the end of clause (iii) and if the intention has been to apply the word 'secret' before the word 'process' also, then a comma would have been used after the word 'formula'" and further that the word "secret" cannot also be applied to the word "trademark" because once registered there is nothing secret about the trademark and the impossibility of reading the word "secret" before the word "trademark" further strengthens the view that the word "secret" cannot be read before the word "process" also. This naturally takes us to the question whether there is anything in article 12.3(a) of the DTAA between India and USA which militates against such a view. It must be remembered that India had no DTAA with Hongkong and hence the view taken by the Tribunal (supra) with regard to the clause (iii) of Explanation 2 below section 9(1)(vi) would apply if we were to also interpret the same provision. But article 12.3(a) is worded as below :

"The term 'royalties' as used in this article means :

(a) payments of any kind received as consideration for the use of, or the right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trademark, 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 or property which are contingent on the productivity, use or disposition thereof; and"

In Asia Satellite Telecommunication Co. Ltd.'s case (supra) the Tribunal pointed out, while repelling the argument that the word "secret" also qualifies the word "process" appearing in clause (iii) of Explanation 2, that there is no comma after the word "secret" till the end of the clause and had the intention been to qualify the word "process" also with the word "secret" there would have been a comma after the word "process" (by mistake mentioned in the order as "formula"). The Tribunal was thus prepared, with respect, to accept the argument that both the words "formula" and "process" can be said to be qualified by the word "secret" had the clause been drafted as under :

"the use of any patent, invention, model, design, secret formula or process, or trademark or similar property"

What the Tribunal has pointed out stands fulfilled in article 12.3(a) of the treaty with USA. From the article quoted above, it may be seen that there is a comma after the words "secret formula or process" which indicates that both the words "formula" and "process" are qualified by the word "secret". The requirement thus under the treaty is that both the formula and the process, for which the payment is made, should be a secret formula or a secret process in order that the consideration may be characterised as royalty. We do agree with the argument of the Special Counsel for the Department, on the strength of the several authorities cited by him, that normally punctuation by itself cannot control the interpretation of a statutory provision and in fact the learned counsel for the assessee did not seriously dispute the proposition. However, the punctuation the use of the comma coupled with the setting and words surrounding the words under consideration, do persuade us to hold that under the treaty even the process should be a secret process so that the payment therefore, if any, may be assessed in India as royalty. The Tribunal in Asia Satellite Telecommunication Co. Ltd.'s case (supra) have recognized that all the items referred to in clause (iii) of Explanation 2 such as patent, invention, model, formula and process etc. are intellectual properties. Similarly, the words which surround the words "secret formula or process," in article 12.3(a) of the treaty refer to various species of intellectual properties such as patent, trademark, design or model, plan, etc. Thus the words "secret formula or process" must also refer to a specie of intellectual property applying the rule of ejusdem generis or noscitur a socii.

20. That takes us to a consideration of the question whether the process carried on by the assessee is a secret process. On this question, we have weighed the elaborate arguments advanced by both the sides carefully and hold that so far as the transponder technology is concerned there appears to be no "secret technology", known only to a few. There is evidence adduced before us to show that the technology is even available in the form of published literature/book from which a person interested in it can obtain knowledge relating thereto. There is no evidence led from the side of the Department to show that the transponder technology is secret, known only to a few, and is either protected by law or is capable of being protected by law. This aspect of the matter was not required to be considered by the Tribunal in the case of Asia Satellite Telecommunication Co. Ltd. (supra) because the view taken by the Tribunal was that there was no requirement in clause (iii) of Explanation 2 below section 9(1)(vi) of the Act that the process involved, for which the payment is being made, should be a secret process. But in the view we have taken on the language employed by article 12.3(a) of the treaty coupled with the punctuation and the setting and surrounding words, the payment would be considered as royalty only if it is made for the use of a secret process. Since there is nothing secret about the process involved in the operation of a transponder, the payment for the use of the process assuming it to be so does not amount to royalty.

7.2.14 Similar issue came up before Hon'ble Delhi Tribunal in case of Bharti Airtel vs. ITO (TDS) reported in (2016) 67 taxmann.com 223. The issue considered therein was in respect of payment towards call interconnectivity charged for call transmission on foreign network. The Tribunal therein, on applying ratios pronounced in the above referred decisions, held it not as 'Royalty'.

Therefore in our opinion, the Payments made by the assessee in lieu of services provides by the assessee cannot fall within the ambit of 'Royalty' under section 9(1)(vi) Explanation 5 & 6.

7.2.15 We also note that the Explanations 5 and 6 to section 9(1)(vi) are not found in the definition of "Royalty" under IndiaJapan DTAA. The definition of "Royalty" under the DTAA is much more narrower in its scope and coverage, than the definition of "Royalty" contained in section 9(1)(vi) r.w. Explanations 2,5 and 6 of the act.

7.2.16 On perusal of the agreement between the assessee and the end users placed at pages 46 to 64 of paper book for A.Y. 2010-11, it is noted that the installation and operation of sophisticated equipments are with the view to earn income by allowing the users to avail the benefits of such equipments or facility and does not tantamount to granting the use or the right to use the equipment or process so as to be considered as royalty within the definition of "royalty" as contained in clause 3 of Article 12 of India-Japan DTAA.

7.2.17 We also note that in the present facts of the case, at no point of time, any possession or physical custody, control or management over any equipment is received by the end users / customers. It is also noted that the process involved in providing the services to the end users / customers is not “secret” but a standard commercial process followed by the industry players. Therefore the said process also cannot be classified as a “secret process”, as is required by the definition of “royalty” mentioned in clause 3 of Article 12 of India-Japan DTAA. We are therefore of the opinion that the receipt of IUC charges cannot be taxed as Royalty under Article 12 in India of IndiaJapan DTAA.

7.2.18 The above observations are supported by the view expressed by Hon’ble Karnataka High Court in case of Vodafone Idea Ltd. (supra). Hon’ble High Court in the group of cases had considered following questions of law which are as under:

“1. Whether the Income-Tax Appellate Tribunal (ITAT) was correct in holding that the application of the Double Taxation Avoidance Agreement (DTAA) cannot be considered in proceedings under Section 201 of the Act and that it is not open to the payer to take benefit of the DTAA when he is making payment to a non- resident?

2. Whether the ITAT was correct in holding that amendment to provisions of royalty under Section 9(1)(vi) by inserting Explanation 5 and 6 under the Income-tax Act (hereinafter referred to as the 'Act') will also result in amendment of the DTAAS?

3. Whether ITAT was correct in holding that payments made to non-resident telecom operators for providing interconnect services and transfer of capacity in foreign countries is chargeable to tax as royalty in view of the inclusion of the terms "right" & "process" in the clarificatory Explanation 2, 5 and 6 of Section 9(1)(vi) of the Act, and consequently, appellant was bound to deduct tax at source thereon under Section 195 of the Act?

4. Whether the income tax authorities in India have jurisdiction to bring to tax income arising from extraterritorial source, that is outside India, in respect of business carried on by foreign companies outside India just because Indian residents use and pay for the facilities provided by these foreign companies contrary to the Constitution of India, International Law and Treaties and law declared by the Apex Court?

5. Whether the first respondent was correct in holding that for the current assessment year the withholding tax

liability should be levied at a higher rate at 20% in accordance with section 206AA of the Act?

6. Whether the Hon'ble Tribunal was right in repelling the contention of the Appellant to the effect that, as a deductor, it cannot be held liable for non-reduction of tax at source for payments made for the Assessment Year 2008-09 to Assessment Year 2012-13 on the basis of a subsequent amendment to Section 9(1)(vi) whereby Explanation 5 and 6 were introduced?"

Hon'ble High Court for considering the above questions had looked into the agreement between Vodafone Idea Ltd. and the various service providers from whom Vodafone Idea Ltd. had received the IUC services. Hon'ble High Court also considered the various decisions by other High Courts referred to hereinabove vis-a-vis the arguments advanced by the Ld.Counsel.

7.2.19 In case of Vodafone Idea Ltd. (supra), Hon'ble Court also observed that the equipments and submarine cables are situated overseas and that Vodafone Idea Ltd. had availed certain services from the non-resident telecom operators and that such agreements would not create a permanent establishment of such non-resident telecom operators in India. Thereafter Hon'ble High Court after verifying the facts of the case having regards to the decision of Hon'ble Supreme Court in case of Engineering Analysis Centre of Excellence Pvt. Ltd. vs. CIT reported in (2021) 432 ITR 471 observed and held as under:

"12. We have carefully considered the rival contentions and perused the records.

13. Undisputed fact of the case are, Assessee is an ILD license holder and responsible for providing connectivity to calls originating/terminating outside India. Assessee has entered into an agreement with NTOs for international carriage and connectivity services. According to the assessee, payment made to NTOs is towards interconnectivity charges.

14. Assessee has also entered into a CTA with a Belgium entity Belgacom. Belgacom had certain arrangement with the Omantel for utilisation of bandwidth. Omantel transferred certain portion of its capacity to Belgacom and Belgacom had in turn transferred a portion of its capacity to the assessee.

15. Admittedly the equipments and the submarine cables are situated overseas. To provide ILD calls, assessee had availed certain services from NTOs. It is also not in dispute that Belgacom, a Belgium entity with whom assessee has entered into an agreement does not have any 'permanent establishment' in India.

16. *Shri. Pardiwala contended that the payments made by assessee cannot be treated as either Royalty or FTS34 or business profits as no part of the activity was carried out in India. Revenue's reply to his contention is that, the income belongs to the payee. If, in the opinion of assessee, tax was not deductible, he ought to have approached the AO for the nil deduction certificate. It is also the further case of the Revenue that the agreement between assessee and the payee did not specify that income was not taxable.*

17. *The first question is whether the ITAT was correct in holding that DTAA cannot be considered under Section 201 of the Act. It was argued by Shri. Percy Pardiwala that this issue is covered by the decision in GE Technology. We may record that a DTAA is a sovereign document between two countries. In GE Technology, the Apex Court has held as follows:*

"7. ...While deciding the scope of Section 195(2) it is important to note that the tax which is required to be deducted at source is deductible only out of the chargeable sum. This is the underlying principle of Section 195. Hence, apart from Section 9(1), Sections 4, 5, 9, 90, 91 as well as the provisions of DTAA are also relevant, while applying tax deduction at source provisions."

(Emphasis supplied)

18. *The above passage has been noted and extracted in Engineering Analysis. Thus it is clear that an assessee is entitled to take the benefit under a DTAA between two countries. Hence, the ITAT's view that DTAA cannot be considered in proceedings under Section 201 of the Act is tenable.*

19. *The second question for consideration is whether the ITAT was correct in holding that the amendment to provisions of Section 9(1)(vi) inserting the Explanations will result in amendment of DTAA. The answer to this question must be in the negative because in Engineering Analysis, the Apex Court has held that Explanation 4 to Section 9(1)(vi) of the Act is not clarificatory of the position as on 01.06.1976 and in fact expands that position to include what is stated therein vide Finance Act, 2012.*

20. *The Explanation 5 and 6 to Section 9(1)(vi) of the Act has been inserted with effect from 01.06.1976. This*

aspect has also been considered in Engineering Analysis holding that the question has been answered by two Latin Maxims, lex no cogit ad impossibilia i.e. the law does not demand the impossible, and impotentia excusat legem i.e. when there is disability that makes it impossible to obey the law, the alleged disobedience of law is excused and it is held in Engineering Analysis as follows:

“85. It is thus clear that the “person” mentioned in section 195 of the income Tax Act cannot be expected to do the impossible, namely, to apply the expanded definition of “royalty” inserted by explanation 4 to section 9(1)(vi) of the Income Tax Act, for the assessment years in question, at a time when such explanation was not actually and factually in the statute.”

“100. Also, any ruling on the more expansive language contained in the explanations to section 9(1)(vi) of the Income Tax Act would have to be ignored if it is wider and less beneficial to the assessee than the definition contained in the DTAA, as per section 90(2) of the Income Tax Act read with explanation 4 thereof, and Article 3(2) of the DTAA.....”

21. *The third question is, whether the payments made to NTOS for providing interconnect services and transfer of capacity in foreign countries is chargeable to tax as royalty. It was argued by Shri. Pardiwala, that for subsequent years in assessee’s own case, the ITAT has held that tax is not deductible when payment is made to non-resident telecom operator. This factual aspect is not refuted. Thus the Revenue has reviewed its earlier stand for the subsequent assessment years placing reliance on Viacom etc³⁵, rendered by the ITAT. In that view of the matter this question also needs to be answered against the Revenue.*

22. *The fourth question is whether the Income Tax Authorities have jurisdiction to bring to tax income arising from extra-territorial source. Admittedly, the NTOs have no presence in India. Assessee’s contract is with Belgacom, a Belgium entity which had made certain arrangement with Omantel for utilisation of bandwidth. In substance, Belgacom has permitted utilisation of a portion of the bandwidth which it has acquired from Omantel. It is also not in dispute that the facilities are situated outside India and the agreement is with a Belgium entity which does not have any presence in India. Therefore, the Tax*

authorities in India shall have no jurisdiction to bring to tax the income arising from extra-territorial source.

23. *The fifth question is whether the Revenue is right in holding that withholding tax liability should be levied at a higher rate. It was contended by Shri. Pardiwala that this issue is covered in assessee's favour in CIT Vs. M/s. Wipro³⁶ and the same is not disputed. Hence, this question also needs to be answered against the Revenue.*

24. *The sixth question is whether assessee can be held liable for non-reduction of tax at source for payments made for the A.Ys. on the basis of amendment to Section 9(1)(vi) of the Act. This aspect has been considered by us while answering question No.2. It is held in Engineering Analysis that an assessee is not obliged to do the impossible. Admittedly, the A.Y.s under consideration are 2008-09 to 2012-13 and the Explanation has been inserted by Finance Act, 2012. In addition, we have also held that assessee is entitled for the benefits under DTAA."*

7.2.20 *Respectfully following the above view, in case of Vodafone Idea Ltd. (supra), and the discussions hereinabove, we hold that payments received by assessee towards interconnectivity utility charges from Indian customers / end users cannot be considered as Royalty to be brought to tax in India under section 9(1)(vi) of the Act and also as per DTAA.*

7.2.21 *The payment received by the non-resident assessee amounts to be the business profits of the assessee which is taxable in the resident country and is not taxable in India under Article 5 of the DTAA as there is no case of permanent establishment of the assessee that has been made out by the revenue in India.*

Accordingly, the grounds on merit referred to in para 5 stands allowed in favour of assessee.

In the result, all the three appeals filed by assessee stands partly allowed.

2.1 Accordingly, the appeal of the assessee is allowed.

2.2 Since we have allowed the appeal of the assessee, the stay petition has become infructuous and dismissed accordingly.

3. In the result, appeal of the assessee is allowed and stay petition is dismissed.

Order pronounced in the open court on 5th June, 2024

**Sd/-
(Keshav Dubey)
Judicial Member**

**Sd/-
(Chandra Poojari)
Accountant Member**

Bangalore,
Dated 5th June, 2024.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The DR, ITAT, Bangalore.
5. Guard file

By order

**Asst. Registrar,
ITAT, Bangalore.**