



## Payment for the use of virtual voice network is neither fees for technical services nor royalty under the India-UK tax treaty

### Background

Recently, the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of *Interroute Communications Limited*<sup>1</sup> (the taxpayer) held that the payment for the use of Virtual Voice Network (VVN) is not taxable as Fees for Technical Services (FTS) under the India-UK tax treaty (tax treaty) since no services are made available to the recipient of such services. Further, the payment is not taxable as royalty since it is neither for a scientific work nor for any patent, trademark, design, plan or secret formula or process.

### Facts of the case

- The taxpayer is a UK tax resident company engaged in the business of providing international telecommunication network connectivity facility to various telecom operators around the world.
- During the year under consideration, the taxpayer had received the payment from Vodafone Essar South Limited, and Tata Telecommunications Ltd, towards the use of VVN. This VVN is a standard facility provided by the taxpayer to various customers for providing the interconnect service to third party carriers through taxpayer's port.

- The taxpayer claimed that since no part of the work is carried out in India and since all the infrastructure and equipment is situated outside India, the income is not taxable in India. However, the Assessing Officer (AO) held that the payment received by the taxpayer is in the nature of royalty or FTS and is to be taxed accordingly.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

### Tribunal's ruling

- The role played by the interroute facility is connecting the call to the end operator, and, it works like a clearing house. Similarly, in the case of incoming calls, calls originating from Europe and U.S., which are to end in India, are routed to the respective operators.
- The payment made by the Indian entities can be held to be royalty only when it is payment for scientific work, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience. However, such payment was not for a scientific work nor there any patent, trademark, design, plan or secret formula or process for which the payment was made.

<sup>1</sup> *Interroute Communications Limited v. DDIT* (I.T.A. No. 2284/Mum/2014) – Taxsutra.com

- There can hardly be any dispute that the payment was made for a service, which was rendered with the help of certain scientific equipment and technology. The facility is a standard facility which is used by other telecom companies. As for the dedicated ports, these things only provide a certain level of capacity in access but the payment is for the service nevertheless.
- Merely because the payment involves a fixed as also a variable payment does not alter the character of service. The Tribunal in the case Kotak Mahindra Primus Ltd<sup>2</sup> had held that the type of pricing of a service, by segregating the fixed and variable price, is not unusual. That does not alter the character of arrangement. The payment continues to be for service alone.
- The taxpayer may charge a fixed amount to cover its costs in employing enhanced capacity so as not to incur losses when this capacity is not used, but what the customer is paying for is a service and not the use of equipment involved in additional capacity, nor, for any scientific work, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience. Therefore, it cannot be taxed as royalty under Article 13 of the tax treaty.
- The payment for a service can be brought to tax under Article 13 of the tax treaty only when the technology is made available in the sense that recipient of service is enabled to perform the same service without recourse to the service provider. The Tribunal in the case of CESC Ltd<sup>3</sup> held that in order to be covered by the provisions of Article 13(4)(c) of the tax treaty, not only the services should be of technical in nature but it should result in making the technology available to the person receiving the technical services.
- In the present case, no services were made available in the sense that the recipient of service was not able to apply the technology, and do the same work without recourse to the service provider. There was no transfer of technology and in that sense, technical services were not made available. Accordingly, the service rendered by the taxpayer is not taxable as FTS under Article 13 of the tax treaty.

### Our comments

In the instant case, the Mumbai Tribunal has held that payment for the use of VVN is not taxable as FTS under the tax treaty since no services were made available. Further, such services are not taxable as royalty since payment is neither for a scientific work nor for any patent, trademark, design, plan or secret formula or process.

Recently, the Delhi Tribunal in the case of Bharti Airtel Ltd<sup>4</sup> held that payment of inter-connect usage charges in connection with its international long distance telecom service business, was not FTS under the Act since foreign telecom operator does not render any technical services to the taxpayer under the inter-connect agreement. Further, such services cannot be treated as royalty since there was no 'use' or 'right to use' of any process and there was no exclusive right over such process to characterise the same as royalty.

<sup>2</sup> Kotak Mahindra Primus Ltd v. DDIT [2007] 11 SOT 578 (Mum)

<sup>3</sup> CESC Ltd v. DCIT [2003] 87 ITD TM 653 (Kol)

<sup>4</sup> Bharti Airtel Limited v. ITO (TDS) [ITA Nos. 3593 to 3596/Del/2012]

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