IN THE INCOME TAX APPELLATE TRIBUNAL
"L" Bench, Mumbai

Before Shri P.M. Jagtap, Accountant Member
and V. Durga Rao, Judicial Member

ITA No. 506/Mum/2008
(Assessment Year: 2004-05)

Yahoo India P. Ltd. Bldg. No. 12, 6th Floor, Solitare Corporate Park, Guru Hargovindji Marg, Andheri (E), Mumbai 400093 PAN - AAACY 1252 B	Vs.	DCIT, Range 7(3) Mumbai
Appellant		**Respondent**

Appellant by: Shri R. Muralidhar
Respondent by: Shri R.S. Srivastava

O R D E R

Per P.M. Jagtap, A.M.

This appeal filed by the assessee is directed against the order of the learned CIT(A) XXX, Mumbai dated 19.10.2007 whereby he confirmed the disallowance of ₹34,86,947/- made by the A.O. under section 40(a) on account of payment made by assessee to Yahoo Holdings (Hong Kong) Ltd. without deducting tax at source.

2. Assessee company in the present case is a fully owned subsidiary of Yahoo Inc, USA, which is engaged in the business of providing consumer services such as search engine, content and information on wide spectrum of topics, e-mail, chat, etc. It filed the return of income for the year under consideration on 30.10.2004 declaring total income of Nil after adjusting the brought forward losses to the extent of ₹3,91,47,123/-. During the course of assessment proceedings, it was noticed by the A.O. that the assessee has made a payment of ₹34,86,947/- to Yahoo Holdings (Hong Kong) Ltd. being cost of services/research material/advertisement media. Yahoo Holdings (Hong Kong) Ltd. is engaged in the business of providing internet services, technological tools and marketing solutions for business to customers in Hong Kong. It provides banner advertisement and microsite hosting services on the Yahoo Hong Kong Portal. The banner advertisement is also known as

web banner, which is a form of advertisement on the world wide web. This form of online advertising entails embedding an advertisement into a web page. During the year under consideration, the Department of Tourism of India through an advertisement agency Media Turf Worldwide intended to display a banner advertisement during the period from 18th February 2004 to 15th March 2004 on the portal owned by Yahoo Holdings (Hong Kong) Ltd. For this purpose, it hired the services of the assessee company to approach Yahoo Holdings (Hong Kong) Ltd. to provide uploading and display services for hosting the banner advertisement at Yahoo Hong Kong portal. Accordingly, the assessee company entered into a contract in the form of media insertion order for display of impressions with the Department of Tourism. The total consideration for the same was agreed at ₹65,11,500/- out of which assessee company agreed for granting agency discount to Media Turf of 25%. The Assessee company in turn hired the services of Yahoo Holdings (Hong Kong) Ltd. for uploading and display of banner advertisement on its Portal and the consideration for the said service was agreed at US $75,464 equivalent to Indian ₹34,86,947/-. The said payment to M/s. Yahoo Holdings (Hong Kong) Ltd. was made by the assessee during the year under consideration without deducting tax at source. The stand of the assessee as taken before the A.O. was that since the services/operations performed by Yahoo Holdings (Hong Kong) Ltd. were entirely outside India and since Yahoo Holdings (Hong Kong) Ltd. had no presence in India, the amount paid to them for the services rendered outside India was not taxable in India and no tax, therefore, was required to be deducted at source from the payment of the said amount. According to the A.O., the income attributable to the services claimed to be rendered outside India had accrued in India as per the provisions of section 9 and the same being taxable in India, the assessee was required to deduct tax at source before remitting the said amount to Yahoo Holdings (Hong Kong) Ltd. Since no such tax was deducted by assessee company from the payment remitted to Yahoo Holdings (Hong Kong) Ltd., the deduction claimed by assessee on account of the said payment was disallowed by the A.O. by invoking the provisions of section 40(a).

3. The disallowance made by the A.O. under section 40(a) inter alia was challenged by the assessee in appeal filed before the learned CIT(A) and elaborate submissions were made on its behalf before the learned CIT(A) in support of its case that the amount paid to Yahoo Holdings (Hong Kong) Ltd. was not taxable in the hands of the said company in India and no tax therefore was deductible at source from the payment of the said amount made to Yahoo Holdings (Hong Kong) Ltd. It was submitted that there was no business connection between assessee company and Yahoo Holdings (Hong Kong) Ltd. and, therefore, no income from the impugned transaction was deemed to have accrued or arisen to the said company in India under the provisions of section 9(1)(i). It was also submitted that Yahoo Holdings (Hong Kong) Ltd. is engaged in the business of providing banner advertisement and microsite hosting services on its portal and the receipts from the impugned transaction of hosing banner advertisement of Department of Tourism of India on the said portal was in the nature of business income. It was submitted that since Yahoo Holdings (Hong Kong) Ltd. had no PE in India, the said amount constituting its business income was not chargeable to tax in India. It was further submitted that the banner Ad hosting services do not involve use or right to use any industrial, commercial or scientific equipment granted by Yahoo Holdings (Hong Kong) Ltd. to the assessee company since the uploading and display of banner advertisement on the Yahoo Holdings (Hong Kong) Ltd. were entirely the responsibility of Yahoo Holdings (Hong Kong) Ltd. It was submitted that assessee company was only required to provide banner Ad to Yahoo Holdings (Hong Kong) Ltd. for uploading the same on the Portal. It was contended that in order to treat any payment as in the nature of equipment royalty, the same must be made for the use of or right to use industrial, commercial or scientific equipments. It was contended that the customer/subscriber must have physical possession and control over the equipment alongwith significant economical or possessory interest in the equipment. It was contended that since the assessee company did not possess any degree of domain or control over the portal, the payment made to Yahoo Holdings (Hong Kong) Ltd. cannot be classified as equipment royalty under the provisions of section 9(1)(iva). It was reiterated that the

said payment constituted business income/profits in the hands of Yahoo Holdings (Hong Kong) Ltd. and since the same was not chargeable to tax in India, assessee company was not required to deduct tax at source from the payment thereof.

4. The learned CIT(A) did not find merit in the submissions made on behalf of the assessee. He held that irrespective of the definition of "business connection", once the source of income was established to be in India, the income was deemed to accrued or arose in India for the purpose of section 9 of the Income Tax Act, 1961. As regards the nature of the said income, the learned CIT(A) held that assessee company had booked the portal of Yahoo Holdings (Hong Kong) Ltd. for a specific period and therefore the payment as agreed to was made by the assessee company to Yahoo Holdings (Hong Kong) Ltd. obviously for use of commercial or scientific equipments. Relying on clause (iva) of Explanation 2 to Section 9(1)(vi), he held that the payment made for the use or right to use any industrial, commercial or scientific equipment was in the nature of royalty and the same being taxable in India in the hands of Yahoo Holdings (Hong Kong) Ltd, assessee was under obligation to deduct tax at source from the said payment. Relying on the decision of Authority for Advance Rulings in the case of Cargo Community Network Pte Ltd. 289 ITR 355, he held that assessee was liable to deduct tax at source from the payment made to Yahoo Holdings (Hong Kong) Ltd. and since no such tax was deducted by assessee, the disallowance made by the A.O. under section 40(a) was confirmed by the learned CIT(A). Aggrieved by the order of the learned CIT(A), assessee has preferred this appeal before the Tribunal.

5. We have heard the arguments of both the sides and also perused the relevant material on record. It is observed that the disallowance made by the A.O. on account of payment made by the assessee to Yahoo Holdings (Hong Kong) Ltd. for upholding and display of banner advertisement of the Department of Tourism of India on its portal without deduction of tax at source by invoking the provisions of section 40(a) has been confirmed by the learned CIT(A) treating the said payment as in the nature of royalty relying clause (iva) of Explanation 2 to section 9(1)(vi). The said clause inserted by the Finance Act, 2001 w.e.f. 01.04.2002 provides that "Royalty" includes

consideration paid for the use or right to use any industrial, commercial or scientific equipment. At the time of hearing before us, the learned D.R. has also mainly relied on the said clause in support of Revenue's case on this issue. He has contended that Legislative intention behind insertion of the said clause in the Statute is to widen the definition of "Royalty". A perusal of the relevant portion of the Board Circular shows that the Legislative intention behind insertion of the said clause is to overcome the situation where no tax at source was being deducted from the payment of lease rent of industrial, commercial and scientific equipment by taking shelter under the erstwhile definition of the term 'Royalty" as given in the Income Tax Act, 1961. The Legislative intention to insert clause (iva) of Explanation 2 to section 9(1)(vi) in the statute thus is to cover the lease rent of industrial, commercial and scientific equipments in the definition of "Royalty" and the said definition has been widened to that extent only.

6. In support of Revenue's case on this issue, the learned D.R. has also relied on the decision of the Hyderabad Bench of ITAT in the case of Frontline Soft Ltd. vs. DCIT 12 DTR 131 as well as the decision of the Authority for Advance Rulings in the case of Cargo Community Network Pte. Ltd. 289 ITR 355. We have carefully gone through these decisions cited by the learned D.R. It is observed that in the case of Frontline Soft Ltd. (supra), a mere right to use an equipment was held by the Tribunal to fall within the ambit of clause (iva) of Explanation 2 to section 9(1)(vi) of the Act. The Tribunal, in coming to the said conclusion, followed the ruling of the ITAT Delhi Special bench in the case of Asia Satellite Telecommunications Co. Ltd. 78 TTJ (Del) (SB) 489, which has been subsequently overruled by the Hon'ble Delhi High Court vide its judgement reported in 232 CTR (Del) 177. The proposition laid down by the Tribunal in the case for Frontline Soft Ltd. (supra) thus is contrary to the decision of the Hon'ble Delhi High Court in the case of Asia Satellite Communications Co. Ltd. (supra). In the case of Cargo Community Network Pte. Ltd. (supra) cited by the learned D.R., the facts involved were different in as much as the system connect fees paid for providing access and use of portal hosted from Singapore was inclusive of training charges, monthly subscription fee, fee for additional access and help desk charges. Having

regard to the nature of this composite fees, the contention of the assessee that the cargo booking agency never uses the server of the assessee for processing or obtaining any data was found to be untenable by the Authority for Advance Rulings. It was held that use of portal was not possible without use of server and the server platform being a scientific equipment, the payment made for concurrent access to utilise the sophisticated services offered by the portal would be covered by the expression "Royalty" as used in Article 12 of the DTAA as well as section 9(1)(vi) of the Income Tax Act, 1961. In the present case, the amount was paid by assessee to Yahoo Holdings (Hong Kong) Ltd. for the services rendered for uploading and display of the banner advertisement of the Department of Tourism of India on its portal and there was no direct use by the assessee either of the portal or of the server as was there in the case of Cargo Community network Pte. Ltd. The decision of the Authority for Advance Rulings in the said case thus is not applicable to the facts of the case of assessee.

7. On the other hand, the decision of the Authority for Advance Rulings in the case of Isro Satellite Centre 307 ITR 59 and in the case of Dell International Services (India) P. Ltd. 305 ITR 37 cited by the learned counsel for the assessee are found to be directly applicable to the issue involved in the present case. In the case of Isro Stellite Centre (supra), the question involved was whether the consideration paid by ISRO to Immarsat Global of U.K. for using the Immarsat navigation transponder capacity would be Royalty under the DTAA between India and U.K. The AAR 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 Immarsat Global of U.K. nor did the applicant use any equipment of Immarsat Global of U.K. It was held that 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 has been followed by the Hon'ble Delhi High Court in the case of Asia Satellite Telelcommunications Ltd. (supra). In the case of Dell International Services (India) P. Ltd. (supra), it was held by the AAR in the similar context that the word "use" in relation to equipment occurring in

clause (iva) of Explanation to section 9(1)(vi) 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 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.

8. As already noted by us, the payment made by assessee in the present case to Yahoo Holdings (Hong Kong) Ltd. was for services rendered for uploading and display of the banner advertisement of the Department of Tourism of India on its portal. The banner advertisement hosting services did not involve use or right to use by the assessee any industrial, commercial or scientific equipment and no such use was actually granted by Yahoo Holdings (Hong Kong) Ltd. to assessee company. Uploading and display of banner advertisement on its portal was entirely the responsibility of Yahoo Holdings (Hong Kong) Ltd. and assessee company was only required to provide the banner Ad to Yahoo Holdings (Hong Kong) Ltd. for uploading the same on its portal. Assessee thus had no right to access the

portal of Yahoo Holdings (Hong Kong) Ltd. and there is nothing to show any positive act of utilization or employment of the portal of Yahoo Holdings (Hong Kong) Ltd. by the assessee company. Having regard to all these facts of the case and keeping in view the decision of the Authority of Advance Rulings in the case of Isro Satellite Centre (supra) and Dell International Services (India) P. Ltd. (supra), we are of the view that the payment made by assessee to Yahoo Holdings (Hong Kong) Ltd. for the services rendered for uploading and display of the banner advertisement of the Department of Tourism of India on its portal was not in the nature of royalty but the same was in the nature of business profit and in the absence of any PE of Yahoo Holdings (Hong Kong) Ltd. in India, it was not chargeable to tax in India. Assessee thus was not liable to deduct tax at source from the payment made to Yahoo Holdings (Hong Kong) Ltd. for such services and in our opinion, the payment so made cannot be disallowed by invoking the provisions of section 40(a) for non-deduction of tax. In that view of the matter we delete the disallowance made by the A.O. and confirmed by the learned CIT(A) u/s 40(a) and allow the appeal of the assessee.

9. In the result, appeal of the assessee is allowed.

Order pronounced in the open court on 24th June 2011.

Sd/-	Sd/-
(V. Durga Rao)	**(P.M. Jagtap)**
Judicial Member	**Accountant Member**

Mumbai, Dated: 24th June 2011

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The CIT(A) – XXX, Mumbai*
4. *The CIT– VII, Mumbai City*
5. *The DR, "L" Bench, ITAT, Mumbai*

By Order

//True Copy//

Assistant Registrar
ITAT, Mumbai Benches, Mumbai

n.p.