Indian Taxation of a Foreign Satellite Owner's Income from Transmission of Television Programmes

Dr Amar Mehta[*]

Issue: Asia-Pacific Tax Bulletin, 2015 (Volume 21), No. 6
Published online: 1 December 2015

This article provides an analysis of the Indian case law on services of foreign satellite service providers. As satellites do not have a physical nexus with India, the fees for transponder services do not automatically land in a treaty provision. The issue is of particular interest for non-resident satellite providers and academics.

1. Introduction

There are several hundred television channels in India. Many of them avail services of foreign satellite service providers for transmitting/uplinking the signals for the television programmes. Although those satellites are not located in India, their footprints extend over India.

The Indian tax authorities have consistently viewed that the above-mentioned satellite service providers' incomes from television channels operating in India amount to royalties taxable in India.

In 2011, the Delhi High Court held[1] that these incomes did not amount to royalty under the Indian Income Tax Act 1961 (IITA1961) and, therefore, they were not taxable in India. But the royalty definition in the IITA1961 was retroactively amended in 2012, as a result of which transmission of signals through a satellite is now considered a "*process*". On that basis, under the IITA1961, the subject income is now regarded as royalty taxable in India. This article examines the relevant legislative and judicial aspects of the issue.

This article also examines as to whether the retroactive amendment in the IITA could adversely affect connotation of "royalty" in a tax treaty context.

2. Section 9(1)(vi) of the IITA1961

Section 9(1) of the IITA1961 provides that a non-resident's income is taxable in India if, inter alia, it is deemed to accrue or arise in India. As per section 9(1)(vi) of the IITA1961, a non-resident's royalty income is deemed to arise in India if it is payable by:

(1) the government of India;
(2) a person who is resident of India, except if the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or
(3) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India.

The term "royalty" is defined in Explanation 2 to section 9(1)(vi) of the IITA 1961. That definition was amended in 2012 with retroactive effect. Prior to that amendment, that term was defined to mean 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) …
(ii) …

---

* Dr Amar Mehta has advised numerous multinational companies on international business transactions with India. Formerly, he was tax partner at Ernst & Young in India, international tax senior manager at Ernst & Young in Toronto (Canada) and research associate with IBFD. He may be contacted at amarmehta@indi-genius.com.

1 *Asia Satellite Telecommunications Co. Ltd. v. DIT*, IT Appeal No. 131 and 134 of 2003, dated 31 January 2011.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

Exported / Printed on 1 Oct. 2019 by jitendra.sanghavi@relianceada.com.

(iii) the use of any patent, invention, model, design, secret formula or *process* or trademark or similar property; [Emphasis supplied.]
(iv) …
(v) …
(vi) …

The retroactive amendment to the above-mentioned definition was carried out in 2012 by means of insertion of an explanation, which provides as follows:

> Explanation 6. – for 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 as secret.

Thus, as per the amended definition in the IITA1961, a foreign satellite owner's income on account of transmission of signals of an television channel carrying on business in India is deemed as "royalty" arising in India and, hence, taxable in India.

Even prior to the retroactive amendment, the Indian tax authorities have attempted to tax the subject income as royalty deemed to arise in India. But, in 2011, the Delhi High Court rejected the Indian tax authorities' position. [That decision is discussed soon hereafter.] The amendment was carried out with the intention of overcoming the Delhi High Court's decision.

3. The Delhi High Court's Decision in *Asia Satellite Telecommunication Ltd.*

In *Asia Satellite Telecommunications Co. Ltd. v. DIT*,[2] the Delhi High Court examined as to whether a foreign satellite company's income on account of transmission of television signals from outside India could be regarded as royalty taxable in India. In that case, a Hong Kong company was engaged in the business of providing private satellite communication and broadcasting facilities. It had launched two satellites in geostationary orbit. Those satellites were not positioned over the Indian airspace, but their footprints extended over India.

The Hong Kong company had entered into agreements with certain foreign (non-Indian) television channels. Those television channels had their own relaying facilities situated outside India, from which they beamed signals in space. Those signals were received by the transponders located in the Hong Kong company's satellites.

The Hong Kong company did not play any role in either uplinking activity or the signal-receiving activity. The Hong Kong company's only activities on earth were confined to telemetry, tracking and control of the satellites. Those tasks were performed from outside India. Therefore, as per the Hong Kong company, its income was not taxable in India.

But, the Indian tax authorities rejected the Hong Kong company's position. As per the Indian tax authorities, because the Hong Kong company had entered into agreements with television channels that downlinked programmes to India (and the Indian viewers watched those television programmes), the Hong Kong company had a *business connection* in India. Hence, as per the Indian tax authorities, a part of the Hong Kong company's income was taxable in India.

In first appeal, the Commissioner of Income Tax (Appeals) held that no portion of the Hong Kong company's income was taxable in India on account of business connection, but the Hong Kong company's income had to be characterized as royalty and, therefore, it was taxable in India.

In the next round of appeal, the Indian Income Tax Appellate Tribunal (ITAT) held that the Hong Kong company had a business connection in India but, since it did not carry on any activities in India, its income was not taxable in India. The ITAT, however, opined that this income was taxable in India as royalty.

Thereafter, the Delhi High Court reversed the ITAT's decision with respect to the royalty issue.

As per the High Court, inter alia, the Hong Kong company could not be regarded as carrying on business operations in India merely because the footprints of its satellites extended over India.

---

2 IT Appeal No. 131 and 134 of 2003, dated 31 January 2011.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

Exported / Printed on 1 Oct. 2019 by jitendra.sanghavi@relianceada.com.

The High Court also took into account the "royalty" definition in Explanation 2 to section 9(1)(vi) of the IITA1961 (as it existed prior to the retroactive amendment). The High Court noted that the term "royalty" included, inter alia, consideration for the transfer of all or any rights in respect of a process.

The High Court noted that the Hong Kong company retained control over, and operated, the satellites. It did not lease the equipment to customers – rather, it merely provided services to the customers without letting customers use any "process" (the signals beamed by the television channels were received/processed by the transponders in the satellites, but those satellites were operated by the Hong Kong company and not by the television channels). Further, any process carried out by the transponders could not be regarded as "performed in India", because the satellites in which the transponders were situated were located outside India.

Further, in the High Court's view, the television channels (i.e. the customers of the Hong Kong company) did not use any process in the transponders in the satellites.

In view of the above, the High Court concluded that the Hong Kong company's income did not amount to royalty taxable in India in terms of section 9(1)(vi) of the IITA1961.

Thereafter, as mentioned earlier, the "royalty" definition in section 9(1)(vi) of the IITA1961 was amended in 2012 with retroactive effect with the objective of overcoming the above-mentioned decision of the Delhi High Court.

4. The Delhi High Court's Decision Considered in Subsequent ITAT Decisions

The ITAT has taken into account the Delhi High Court's decision in a few subsequent decisions. At this juncture, it would be of interest to take a look at three decisions. All three decisions were pronounced by the ITAT's Mumbai bench: two involved similar facts but divergent conclusions, the third case involved facts of a different nature and was therefore distinguished.

The first decision is *Times Global Broadcasting Co. Ltd. v. DCIT*.[3] In that case, an Indian television broadcasting channel had used a US company's satellite/transponder services for uplinking television programmes. As per the Indian tax authorities, the US company's income amounted to "royalty", and it was taxable in India.

The ITAT rejected the Indian tax authorities' position. The ITAT followed the above-discussed decision of the Delhi High Court and noted that merely because a satellite's footprint area included India – and because the viewers of the television programmes were situated in India – it did not mean that the foreign company carried on business operations in India. The ITAT also noted the High Court's opinion that the uplinking facility provided by a satellite operator did not involve use of a "process" by an Indian television channel.

Accordingly, the ITAT concluded that the US company's income was not taxable in India.

In the second decision, i.e. *Zee Telefilms Ltd. v. ACIT*, [4] the ITAT reached a different and rather questionable conclusion. In that case, an Indian broadcasting company had paid transponder fees to a Mauritius subsidiary. The taxpayer company claimed, on the basis of the decision of the Delhi High Court, that the Mauritius subsidiary's income was not taxable in India. But, the ITAT opined that the relevant facts in *Zee Telefilms Ltd.* were distinguishable from those in the Delhi High Court's decision. Apparently, as per the ITAT, the parent-subsidiary relationship gave rise to the Mauritius subsidiary's permanent establishment (PE) in India. [With due respect to the ITAT, that conclusion is highly questionable because it violates article 5(6) of the 1982 Income Tax Treaty between India and Mauritius.]

The third decision is *Reuters Transaction Services Ltd. v. DDIT*, [5] wherein the taxpayer sought to invoke the Delhi High Court's decision. In this case, a UK company provided an "electronic platform" to foreign exchange dealers across the world on subscription basis. As per the UK company, its income from Indian subscribers had to be characterized as "business profits", which were not taxable in India because they were not attributable to a PE in India. On the other hand, the Indian tax authorities viewed that the said income amounted to royalty taxable in India.

As per the ITAT, the decision of the Delhi High Court was not relevant in the present case. The ITAT found that the Indian subscribers were allowed to use the UK company's electronic exchange and manipulate information to suit their individual needs. The subscribers were also allowed to store that information and distribute or sublicense the information to others to a certain extent. Therefore, in the ITAT's view, the consideration receivable by the UK company from the

---

3 ITA No. 5868/Mum/2010 dated 13 January 2012.
4 ITA No. 2308/Mum/2010 dated 15 March 2013.
5 ITA Nos. 6947 and 7211/Mum/2012 dated 18 July 2014.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

Exported / Printed on 1 Oct. 2019 by jitendra.sanghavi@relianceada.com.

Indian subscribers was on account of “use or right to use” an equipment (i.e. the computer server, in which the relevant information was stored).

In the ITAT’s view, the UK company’s platform was in the nature of commercial equipment allowed to be used by the clients/subscribers. Therefore, the payments made by the Indian clients/subscribers were for use or the right to use such equipment and information for processing their requests related to purchase and sale of foreign exchange. Therefore, the ITAT opined, the UK company’s income amounted to royalty taxable in India.

5. Could Retroactive Amendment in the IITA1961 Affect a Tax Treaty Situation?

As discussed above, the Delhi High Court has held (prior to the 2012 retroactive amendment to the royalty definition) that a foreign satellite owner’s income from transmission of television signals did not amount to royalty. Since the taxpayer in that case was tax resident of Hong Kong, it did not involve a tax treaty. However, it should not have made a difference even if the taxpayer would have been resident of a tax treaty jurisdiction. In other words, even under a tax treaty, that income was unlikely to be characterized as royalty.

Subsequent to the above-mentioned retroactive amendment to the royalty definition in the IITA1961, the ITAT has reached divergent conclusions on the issue whether the amendment in the IITA1961 could affect the connotation of “royalty” under a tax treaty.

B4U International Holdings v. DCIT [6]

In this decision, a Mauritius company had made payments to a US company on account of transponder hire charges in respect of broadcasting of programmes for television channels that had Indian audience. The taxpayer company contended before the ITAT, inter alia, that the 2012 retroactive amendment to the royalty definition did not influence income characterization under the Income Tax Treaty between India and the United States, because the royalty definition in that tax treaty was not amended. The ITAT accepted that argument.

Subsequently, in *DIT v. B4U International Holdings Ltd.*,[7] the Bombay High Court declined to disturb the ITAT’s decision.

Vodafone South Ltd. v. DDIT [8]

Surprisingly, the ITAT reached a different (and questionable) conclusion in *Vodafone South Ltd. v. DDIT*. In that case, an Indian telecommunication company had paid “interconnect usage charges” to certain non-resident telecommunication operators. One such recipient was tax resident of Belgium. The Indian tax authorities rejected the Indian telecommunication company’s claim that the said payments did not attract Indian withholding tax because the foreign telecommunication operators had merely provided “services”. The ITAT rejected the Indian telecommunication company’s claim that the Belgian operators’ income for provision of interconnect services could not be characterized as royalty for the purposes of the Income Tax Treaty between India and Belgium.

The ITAT rejected the Indian telecommunication company’s argument that the retroactive amendment to the royalty definition in the IITA1961 could not affect the tax treaty definition of royalty.

The ITAT found, inter alia, that the interconnect arrangement between the Indian company and the Belgian telecommunication operator permitted the Indian company to connect with a process running on the telecommunication network of the Belgian operator. Hence, in the ITAT’s view, that arrangement allowed the Indian telecommunication company to use a process.

The Indian tax authorities contended that the government of India had not agreed with a tax treaty partner that, for consideration for a process to be characterized as royalty, the process had to be *secret*. Therefore, as per the Indian tax authorities, the Belgian operator’s income amounted to royalty for the tax treaty purposes. The ITAT accepted that line of argument.

---

6 ITA No. 3326/Mum/2006 dated 28 May 2012.
7 Income tax Appeal No. 1274 of 2013 dated 29 April 2015.
8 IT(IT)A Nos. 449 to 453/Bang/2013 dated 30 December 2014.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

Exported / Printed on 1 Oct. 2019 by jitendra.sanghavi@relianceada.com.

ITAT's decision in *Vodafone South Ltd. v. DDIT* leads to "treaty override"

The ITAT's approach in the above-mentioned decision seems questionable because it results in treaty override, which violates the *Vienna Convention of the Law of Treaties 1969* (VCLT). Such an approach is also disapproved by Indian courts.

In absence of the above-mentioned retroactive amendment to the royalty definition in the IITA1961, a payment by an Indian telecommunication operator to a foreign operator for interconnect facility could not be regarded as a payment for a process. Similarly, as the Delhi High Court has held in *Asia Satellite Telecommunications Co. Ltd. v. DIT*, a foreign satellite owner's income for transmission of television signals could not be inferred as payment for a process. Hence, it could not amount to royalty. Thus, the retroactive amendment is merely a *legal fiction* for construing the term "royalty" under the IITA1961. Unless bilaterally agreed, that legal fiction should not be permitted to travel beyond the confines of the IITA1961. In other words, that legal fiction should not have any role in interpretation of the term "royalty" under an Indian tax treaty.

The above-mentioned view finds due support from the Bombay High Court's observation – in *Siemens Aktiongesellschaft* [9] – that in case of an item of income not taxable (in the source state) under a tax treaty, the source state cannot tax that income by means of a unilateral amendment to the domestic law. Also, the ITAT has acknowledged that position in *Delmas France v. Asst. DIT*.[10]

Similarly, in *Infotech Enterprises Ltd. v. Addl. CIT*, [11] the ITAT has acknowledged that a retroactive amendment in a domestic legislation cannot have any impact on tax treaty interpretation. That decision involved the Income and Capital Tax Treaty between India and the Netherlands. The ITAT opined that for construing the term "royalty" in the context of the tax treaty, one could not look beyond the definition of that term as provided in the tax treaty.

Even in *Reuters Transaction Services Ltd. v. DDIT*,[12] the ITAT has acknowledged that if a particular item of income was not taxable under a tax treaty, then a unilateral amendment in the source state's statute could not render such income taxable in the source state.

Accordingly, it is submitted that the 2012 retroactive amendment to the royalty definition in the IITA1961 should not have any influence over the connotation of royalty under an Indian tax treaty.

6. Conclusion

The tax treatment of a foreign satellite owner's income from transmission of signals for a television channel operator carrying on business in India differs under the IITA1961 and an applicable tax treaty. In the January 2011 decision discussed in this article, the Delhi High Court has held that such income should not amount to royalty and, hence, should not be taxable in India. However, that decision has been overridden by means of a retroactive amendment in the royalty definition in the IITA1961 in 2012. Hence, the said income is now rendered taxable under the IITA1961. But, as such, that amendment in the IITA1961 should not influence tax treaty interpretation. Therefore, taxpayers from treaty jurisdictions are likely to enjoy considerable advantage as compared to taxpayers from jurisdictions with which India has not entered into a tax treaty.

Unfortunately, the ITAT has pronounced divergent decisions. It is doubtful whether the ITAT's decision – that the aforesaid income could be treated as royalty for tax treaty purposes – could withstand test of time, because that approach leads to treaty override.

---

9 310 ITR 320.
10 ITA No. 1955/Mum/2011 dated 19 November 2014.
11 ITA No. 115/Hyd/2011 dated 16 January 2014.
12 ITA Nos. 6947 and 7211/Mum/2012 dated 18 July 2014.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

Exported / Printed on 1 Oct. 2019 by jitendra.sanghavi@relianceada.com.