BEFORE THE AUTHORITY FOR ADVANCE RULINGS
NEW DELHI

6th Day of June, 2018

A.A.R. No 1573 of 2014

PRESENT

Mr. R.S. Shukla, In-charge Chairman
Mr. Ashutosh Chandra, Member (Revenue)

Name & address of the Applicant	:	MasterCard Asia Pacific Pte. Ltd. Singapore 152 Breach Road # 35-00 The Gateway East Singapore 189721
Present for the Applicant	:	Mr. S. Ganesh, Senior Advocate Mr. Rohinton Sindhwa, CA Mr. Harit Tandon, CA Mr. G. Chandrashekhar, CA Mr. Gaurav Saxena, CA Mr. Paras Sharma, CA
Present for the Department	:	Mr. Kamlesh Varshney, CIT (IT) Ms. Kavita Pandey, CIT (DR) Mr. Jivandeep Singh Kahlon, Addl. CIT Mr. Parikshit Singh, DCIT (International Taxation), Gurgaon

RULING
(By Ashutosh Chandra)

MasterCard Asia Pacific Pte Limited (MAPL or the Applicant), filed an application in Form no. 34C under section 245Q(1) of the Income tax Act, 1961 (the Act), on 23rd January 2014. In the said application, an advance ruling has been requested on the taxability of fees in respect of the services rendered with

regard to use of a global network and infrastructure to process card payment transactions for customers in India.

2. As per the details accompanying the application, the facts of the case are stated to be as under:

2.1 The Applicant belongs to the MasterCard Incorporated group of companies, one of the leading global payment solution providers facilitating financial institutions, businesses, merchants, cardholders and governments worldwide to use electronic forms of payment instead of cash and cheques. The Applicant is a wholly owned indirect subsidiary of MasterCard's wholly owned direct Delaware incorporated subsidiary, MasterCard International Incorporated ("MCI"). The Applicant is the regional headquarter for the Asia Pacific, Middle East and Africa ("APMEA") region and carries out the MasterCard group's principal business of transaction processing and payment related services under a family of products including "MasterCard". "Maestro" and "Cirrus" in the APMEA region.

2.2 The MasterCard Business is structured as an open bankcard association, in which the cardholder and merchant relationships are managed principally by the Applicant's customers which are primarily banks and financial institutions ("Customers") in APMEA region. The Applicant does not issue cards, extend credit to cardholders, set cardholder fees or determine interest rates or fees charged to cardholders using MasterCard products.

2.3 The services are provided by the Applicant to APMEA Customers pursuant to Master License Agreements ("MLA"), which the Applicant signs with each and every Customer in the APMEA region (including those based in India, pursuant to the proposed business operating mechanism to be adopted in India). Consequent to the terms of a MLA, the Applicant charges its Customers

transaction processing fees relating to authorization, clearing and settlement of transactions. The Applicant also receives assessment fees for building and maintaining a processing network that serves the needs of customers globally, for setting up and maintaining a set of rules that govern the authorization, clearing and settlement process for every payment transaction, so as to maintain the integrity and reputation of its network and also for guaranteeing settlement between the member banks/Customers for payment transactions processed by MasterCard. Additionally, it receives miscellaneous revenue for the provision of services which are ancillary to the transaction processing activities e.g. warning bulletin fees for listing invalid or fraudulent accounts either electronically or in paper form, cardholder service fees, program management services (e.g. foreign exchange margin, commissions, load fees), account and transaction enhancement services, holograms and publication.

2.4 The transaction processing activity consists of electronic processing of payments between banks of merchants ("Acquirer" or 'Acquirer bank") and banks of cardholders ("Issuer" or "Issuer bank") through the use of MasterCard Worldwide Network ("the Network"). The Network facilitates authorization, clearing and settlement of payment transactions between Customers on a proprietary, global payment system (which comprises both hardware and software). The Network links Issuers and Acquires around the globe for transaction processing services and through them permits MasterCard Cardholders to use their cards at millions of merchants worldwide.

2.5 Thus a typical transaction processed over the Network involves four entities, in addition to MasterCard: Cardholder, Merchant, Issuer (the cardholder's bank) and Acquirers (the merchant's bank), playing the following roles:

> *1. The Cardholder makes a purchase with the Merchant and presents a card for payment.*

2. The Merchant forwards the transaction to its bank (i.e. acquirer bank) for authorization. This, in turn, is forwarded to the Cardholder's bank (i.e. issuer bank) via the MasterCard Network. If the transaction is authorized by the Issuer, the Merchant is paid by the Acquirer (and typically the Merchant would be required to pay a "merchant service fee" to the Acquirer). MasterCard facilitates authorization, clearing and settlement of the transaction between the Cardholder and the Merchant via the Issuer and the Acquirer.

3. The settlement process between the issuer and the acquirer bank typically occurs through a settlement bank appointed by MCI. MCI is usually the entity which owns the settlement bank accounts as it is the entity within the MasterCard group which provides settlement services to other group companies. These bank accounts are used primarily for the purpose of ensuring that payment for transactions that have occurred between the merchant and cardholder are settled via the acquirer bank and issuer bank. If settlement occurs successfully across the issuers and acquirers, the settlement bank account would typically end up with a NIL bank balance. Settlement is usually in USD.

In some countries like India, alternative settlement options may be made available depending on the market demand and other factors.

4. The Issuer pays the Acquirer an amount equal to the value of the transaction, less interchange fees and posts the transaction to the Cardholder account.

5. The Issuer issues the Cardholder with a bill to collect the amount of the purchase.

2.6 The processing of electronic payment transactions involves significant steps such as initial level verification and validation of the transaction, authorization, and thereafter clearing and settlement. The two main processing centers of the MasterCard group are in the USA, owned by MasterCard Technologies LLC ("MCTLLC"), a wholly owned direct subsidiary of MCI. The other processing centers are in Belgium and Singapore. The Singapore processing centre is owned by the Applicant.

2.7 The Customer is provided with a MasterCard Interface Processor ("MIP") that connects to MasterCard's Network and processing centers. A MIP is about the size of a standard personal computer and is placed at the customers'

locations in India. It is through the network and processing centers outside India that MAPPL is able to facilitate the authorization, clearing and settlement of payment transactions.

2.8 The Applicant has a subsidiary in India, namely MasterCard India Services Private Limited ("Indian subsidiary"), in which it owns 99% of the shareholding. The remaining 1% is held by the Applicant's immediate holding company, MasterCard Singapore Holding Pte Ltd. The India subsidiary owns and maintains the MIPs placed at the Customers' locations in India.

3. On the above facts, as submitted by the Applicant, the following questions have been posed to us for an advance ruling:

> *(1). Whether on the facts and circumstances of the case, the Applicant has a permanent establishment (hereinafter referred to as "PE") in India under the provisions of Article 5 of the India-Singapore DTAA in respect of the services to be rendered with regard to use of a global network and infrastructure to process card payment transactions for Customers in India?*
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> *(2) Without prejudice to the above, where a PE of the Applicant (in the form of its Indian subsidiary) is found to exist in India, whether provision of arm's length remuneration to such PE for the activities to be performed in India, would absolve any further attribution of the global profits of the Applicant in India?*
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> *(3) Whether on the facts and circumstances of the case, the fees to be received by the Applicant from Indian Customers (comprising transaction processing fees, assessment fees and transaction related miscellaneous fees) would be chargeable to tax in India as royalty or fee for technical services within the meaning of the term in Article 12 of the India- Singapore DTAA?*

(4) Based on the answers to the above questions, and in view of the facts as stated in the subsequent part of the Applicant, whether any tax withholding at source would be required on the amounts to be received by the Applicant?

4. It is the Applicant's contention that the fees received from the customers are neither taxable as Royalty, nor as FTS. Further, since there is no PE it is also not taxable as business income. The Applicant's contentions in support of its claim, as contained in the application, are as under:

4.1 The Applicant is an entity incorporated in Singapore and does not have any presence in India. The Applicant does not own or maintain any Network or MIPs in India. The processing activities such as clearing and settlement of transactions shall be undertaken by the Applicant entirely from outside India and no portion of the same shall be undertaken in India. The information for carrying out the processing activities shall be transmitted outside India by MIPs, which shall be owned by the Indian subsidiary.

4.2 As with Customers in other countries in the APMEA region, the Applicant will enter into new MLAs or assume the rights and/or obligations under existing MLAs via assignment of such agreements with its Indian Customers. The MLAs enable the Customers to use the MasterCard Network to process payment transactions that occur between the cardholders and merchants and to allow its Customers to display the MasterCard logo on their cards and other electronic payment platforms, so as to identify the MasterCard network used to process the payment transactions. No fee is charged to the Customers for displaying the MasterCard logo, since such use is merely incidental to the principal purpose of the MLA, which is to provide processing services to the Customers. Any revenue derived from Customers is purely for the provision of transaction processing services and for building and maintaining the processing network infrastructure, including the setting up and maintenance of the set of rules that govern the

authorization, clearing and settlement process for every payment transaction and the provision of the guarantee settlement between the member banks/Customers for transactions processed by MasterCard. These are significant services that shall be provided by the Applicant.

4.3 It is submitted that the MasterCard network is important for Customers on account of its reliability and broad reach. The network allows the Customers to provide their cardholders and merchants access to a safe and secured transaction processing system. Accordingly, the Applicant will enable its Customers to enhance their businesses by providing a credible and efficient network. Additionally, it will receive miscellaneous Revenues for the provision of services which are ancillary to the transaction processing activities e.g. warning bulletin fees for listing invalid or fraudulent accounts either electronically or in paper form, cardholder services fees, program management services (e.g. foreign exchange margin, commissions, load fees), account and transaction enhancement services, holograms and publications.

4.4 The detailed processing of transactions shall be undertaken by the Applicant through the MasterCard processing centers situated outside India. The transaction data shall be transmitted outside India with the help of MIPs which shall be owned by the Indian subsidiary of the Applicant and shall be placed at the Customers' locations in India. MIPs are special purpose equipment with software embedded therein and consist of Central Processing Unit, Monitor, Router and Multi-protocol label switching unit. MIPs are used for undertaking preliminary examination / validation of information at the point of authorization. The preliminary validation generally involves activities such as PIN processing, validation of card codes, name and address verification etc.. In the case of errors, the MIP would alert the acquirer bank / financial institution on the need for a correction and the data is not authorized. If the initial validation is successful, the MIP located at the acquirer bank would transfer the data to the issuer bank's

MIP, which performs certain other functions, edits and processes. The MIP at the issuer bank will then direct the data to the issuer bank for further processing and verification. The issuer bank will then send a response (generally an approval message) through the MIP at the issuer bank to the MIP at the acquirer bank, which is then passed-on to the acquirer bank for transaction approval.

4.5 A given transaction is eventually authorized by the issuer bank and post authorization, the clearing and settlement takes place at the MasterCard Worldwide network outside India. In India, the settlement is intended to happen under either of the 3 following options:

- USD settlement, through settlement bank account outside India

In this case, the settlement between the acquirer and the issuer banks shall happen in US dollars through the settlement bank account of MCI outside of India.

- Domestic INR settlement through settlement bank account in India

In this case, the settlement between the acquirer and the issuer banks shall happen in Indian Rupees through the settlement bank account of MCI in India.

- Cross border settlement in INR through settlement bank account in India.

Under this option, the settlement of cross-border transactions can happen through a rupee-denominated bank account in India. For this purpose, MCI has been granted approval by the Reserve Bank of India ('RBI') to undertake this activity through its bank account in India. However, as per the Indian Regulations, MCI, being a non-resident, is not allowed overdraft facilities on such settlement account. As an alternative and on account of this inability, there is a possibility that the India subsidiary shall own the bank account on behalf of MCI. Apart from the ownership of the said bank account, the Indian subsidiary shall

not be involved in any settlement activities, which would continue to be managed by MCI from the USA.

4.6 Billing, reports, customer service and other functions shall take place from the processing centers based outside India. Accordingly, substantial processing of transactions shall be executed at the processing centers outside India. The Applicant shall enter into service agreements with the Indian subsidiary for rendering various services like provision of marketing and liaison services, provision of transaction processing support services via the MIPs owned and maintained by the Indian subsidiary, provision of advisory services to customers in India, Provision of advisory support services to MAPPL and other overseas MasterCard group entities; Provision of authentication services in relation to the Unique Identification number (UIDAI) initiative of the Government of India; Provision of marketing and liaison services to other MasterCard group entities such as Access Prepaid UK; and Provision of technology related liaison and coordination services to MasterCard group entities such as MasterCard Technologies LLC. In consideration thereof, the Indian subsidiary shall earn service fees from the Applicant and the respective parties.

4.7 The facts for which questions are asked in this ruling came into effect on 1st Dec 2014. Before that the transaction processing activity was carried out by MCI and it had a liaison office in India. From 1st Dec 2014, all the functions, risks and assets of this liaison office were transferred to Indian subsidiary MISPL and the transaction processing activity was now being carried out by the Applicant from Singapore.

5. The Revenue has submitted detailed reports, as under:

5.1 The Revenue submitted a detailed note from OECD Transfer Pricing Guidelines (accepted by India) with regard to contractual terms of the transaction

and analysis of risks in commercial or financial relations. Through these the Revenue has argued that we need to see actual conduct and for this we need to delineate the transactions. Once we do this we can find out if the payment is for transaction processing or for royalty or for both. This will also help in finding out if the work done in India is preparatory or auxiliary. This will further help us to identify who actually is the beneficiary of this service/use of intangibles and from whom this fee comes. Revenue also contended that the identification of risk is important to see who has the control over the risk and who has financial capacity to undertake the risk in connection with MIPs. This will help us decide who the actual owner of MIPs is and who has control over MIPs. Revenue also discussed that compensation should be based on economic activity carried out and value created in India. While the main economic activity is carried out in India and value is created in India, it is not adequately compensated for that.

5.2 The Revenue has objected to the Applicant's contention that no part of transaction processing activity happens in India. It relied on the factual details contained in the AAR application of the Applicant and also in the TP report of MISPL (for FY 2014-15) which states that MIPs are doing preliminary examination/validation of information at the point of authorization which involves PIN processing, validation of card codes, names and address verification etc.. The Revenue also objected to the Applicant's submission that no part of MasterCard Network is in India. It once again relied on the MISPL TP report (for FY2014-15) in its support.

5.3 With respect to risks, the Revenue relied on the TP report of MISPL (for FY 2014-15) to contend that all risks are undertaken by the Applicant as shown in the TP report. Though technology risk with respect to change in technology of MIP is shown to be taken by MISPL, it does not have control over this risk and

does not have financial capacity to take the risk. In support of this claim, the Revenue submitted that Applicant has given the details of six employees who are associated with transaction processing services (Amitabh Khanna, Harish Babu, Joy Sekhri, Rohan Rane, Sake Bhardwaj and Selwyn Kaitha) and none of them have technical qualification to address technology change associated with MIPs or take decision regarding MIPs. Before 1st Dec 2014, the maintenance was done by the overseas AEs and they continue to perform the maintenance work after 1st Dec 2014 under their name and not in the name of MISPL. The contract for maintenance continues to be entered by overseas AEs with the third party vendors, on their own account. The vendors carry out risk mitigation functions of maintenance of MIPs on behalf of overseas AEs and not on behalf of MISPL. It is only the cost of that maintenance that is allocated to MISPL. MISPL further allocates this cost to Applicant with mark-up, without any of its own value addition. This was demonstrated through actual figures. This clearly demonstrates that MISPL neither has financial capacity to undertake maintenance of MIPs nor technical qualification. It also does not undertake risk mitigation functions which involve taking decisions with regard to MIPs maintenance like taking decision to respond to technical changes, whom to contract for maintenance, when and how to upgrade the software inside MIPs. These decisions are taken by the Applicant and final cost is charged to the Applicant. The software inside MIP is also shown to be owned by the Applicant in the TP audit report of MISPL as all intangibles are shown to be owned by the Applicant and not by MISPL. Further, MISPL is shown to be performing only support services to transaction processing and not actual transaction processing. This also shows that actual control of MIPs is with the Applicant who owns the intangible inside MIPs, takes all decisions with respect to MIPs and controls all risks associated with MIPs. Thus MIPs are at its disposal.

5.4 With respect to clearing and settlement as well, the Revenue contended that these activities are happening in India and not overseas. The Revenue has relied on the reply from Yes Bank under section 133(6) of the Income-tax Act which has stated that flow of receivable/payable data is clearance. The Revenue has also relied on the Applicant's own reply that the clearing process establishes the settlement position. Revenue has contended that it has been accepted by the Applicant that in more than 90% of the transactions the customer is in India, the issuer banks and acquirer banks both are in India. In these over 90% transactions, both issuer banks and acquirer banks know all the transactions that have happened between them. Since there are multiple transactions in a day, these transactions have to be added up, fee deducted, to know the final net position between two banks. For this purpose, raw data is uploaded by the banks using the two application software (Master Connect and MasterCard File express). Then, an overseas AE compiles these to final shape, on behalf of the Applicant. The final information comes to Bank of India (or BOI) for passing the necessary entry in the banks account of both acquirer banks and issuer banks. The Revenue has contended that clearance happens in India since the flow of data relating to the position of each bank (who owes how much to whom) is generated in India and is known to each bank in India. Though the final net amount is calculated outside India, that net amount is already known to the respective banks in India.

5.4.1 The Revenue has quoted from Applicant's reply dated 4th October 2017, which has defined settlement as movement of fund between the issuer and acquirer bank and happens after the clearing process has established the settlement position. The Revenue has contended that this process of movement of fund between two banks happens when Bank of India passes the debit and credit entries and that happen in India. Revenue has relied upon the reply of Bank of India obtained under section 133(6) of the Income-tax Act to plead that

this work is carried out by dedicated team of staff of Bank of India and this settlement happens every day after getting instructions from the MCI. BOI carried out this work, on behalf of the Applicant. Revenue has also quoted from the settlement agreement between the Applicant and Bank of India to contend that it is the Applicant who is responsible for any error in settlement. Thus, the Revenue has contended that both clearance and settlement also happen in India.

5.5 The Revenue has also contended that though on paper MIPs are owned by MISPL but the de facto ownership lies with the Applicant. For this it has relied upon the fact that there is no agreement of MISPL with the banks with regard to use of MIPs and their use is governed by the agreement between the Applicant and the banks. Revenue also contended that MIPs were originally owned by the AEs of the Applicant and were subsequently transferred to MISPL. However, no VAT/GST has been paid on such sale till now even after three years. Thus there is no sale in the eyes of law. Thus the ownership of MIPs remains with the overseas AEs who have licensed it to the Applicant.

5.6 The Revenue further stated in its report that restructuring has been carried out in India with the main purpose of avoiding payment of tax in India. It has been submitted that till Dec 2014, the Applicant was working through Liaison Office in India which was shut down and all functions and employees were transferred to the Indian subsidiary. There was no change in business operations so far as customers are concerned, and for them the work continued like before. Thus, the tax liability in India should have been the same. It was submitted by the Revenue that by this restructuring the income offered in India has reduced from more than 50% of Revenue from India to about 2.5%. This has resulted in suppression of income in India of the tune of INR 300 to 400 crore every year. Before 1 Dec 2014, MasterCard admitted in its tax return (for 10 years) that there is a PE in India and 100% of income from India is to be attributed to this PE; that is, all the

Revenue from the transaction processing activity. On this Global Net Operating Profit Margin was applied to arrive at taxable income in India.

5.7 However, after 01.12.2014, with all operations remaining the same, MIPs continued to operate in the same manner (only ownership changed on paper from overseas entity to Indian subsidiary MISPL with no corresponding change in risk or functions associated with it), employees managing LO of MCI continued to perform the same functions with MISPL, however, MISPL was only shown to be doing support functions and not actual transaction processing functions which LO of MCI was doing earlier. Based on this, Revenue has contended that this is a colorable device to reduce the tax liability in India.

5.8 The Revenue has also relied upon the decision of the Hon'ble Hon'ble Delhi High Court in the case of CIT v. Abhinandan Investment Limited (IT appeal no 130 of 2001).This decision has considered various judgments like Hon'ble Supreme Court judgments in McDowell, Vodafone International Holdings BV, Azadi Bachao Andolan, Guj High Court decision in the case of Banyan and Beery, Sakarlal Balabhai and concluded that it is important to understand the business purpose behind a transaction. If it was to contrive a loss, the same is to be disallowed. Based on this it has been stated in the Revenue's report that there was no business purpose to restructure the transactions in India other than to reduce tax liability in India.

5.9 The Revenue has contended that the Applicant has various types of PEs in India. It has submitted that the Applicant has a fixed place PE under Articles 5(1) and 5(2) of India Singapore DTAA in the form of MIPs, MasterCard Networks, Bank of India premises as well as Indian subsidiary. It has also submitted that there is a service PE under Article 5(6) of India Singapore DTAA. It has also submitted that there is a dependent agent PE in terms of Articles 5(8) and 5(9) of India Singapore DTAA. Revenue has submitted that any one form of PE would

give taxation right to India, though there exist more than one form of PEs in this case.

5.10 The Revenue submits that the Applicant is carrying out its business of authorization (which is part of transaction processing) through MIPs in India which are at its disposal. It has been submitted that for creating fixed place PE it is not necessary that MIP should be fixed on the ground and for this reliance was placed on Note 5 of OECD commentary on Article 5 of Model Tax Convention. Further, it was submitted that there is no requirement that MIP should be owned by the Applicant and for this reliance was placed on Note 4.1 and note 4.2 of OECD commentary on Article 5 of Model Tax Convention as well as the Hon'ble Supreme Court decision in Formula One World Championship Limited vs CIT, 394 ITR 80 (Formula One or FPOWC). It was contended that automatic equipment like MIP or server could constitute a PE. Reliance was placed on the above mentioned judgment in FOWC, *Swiss Server Case* (quoted by Hon'ble Delhi High Court in the case of Formula one World Championship Limited [2016] 76 taxmann 6), ATO Server case, German Server case, French Online Video Game case and Sweden Data Center case. Last four foreign cases were cited from the book of Mr. Ashish Karundia on Taxmann's Law and Practice relating to Permanent Establishment. It was also contended that there is no requirement that employees of the Applicant should operate MIPs to create a PE in India.

5.11 The Revenue submitted that real test for creating PE is that MIP should have permanency attached to it (which is satisfied as it is placed in bank premises for the entire year) and the MIPs are at the disposal of the Applicant. The Revenue stated that various facts like (a) the Applicant controlling MIP through licensing agreement and MasterCard Rules, (b) no agreement between MISPL and customer banks regarding use of MIPs, (c) regular update, maintenance and risk mitigation functions of MIPs being carried out by overseas

AEs on behalf of the Applicant, (iv) the Applicant ultimately bearing all cost and (v) the fact that only the Applicant has the financial capacity to undertake risks associated with MIPs and having control over all the risks associated with MIP by decision making functions proves that MIPs are at the disposal of the Applicant. The Revenue also submitted that the functions performed by MIPs are not preparatory or auxiliary, and in support of this it quoted from the TP report of MISPL and the information contained in the application of the Applicant.

5.12 The Revenue has also contended that MasterCard network present in India in the form of MIP, Application software (Master connect and MasterCard file express), transmission towers, leased lines, fiber optic cables, nodes and internet, which all are part of Master Card network in India. MIPs are shown to be owned by MISPL but are at the disposal of the Applicant. Application software is owned by the Applicant and is at its disposal. Transmission towers, leased lines, fiber optic cable, nodes, internet etc. are provided by third party service provider but are at the disposal of the Applicant. Reliance was placed on judgments of the ITAT Delhi in the cases of Amadeus Global Travel Distribution SA vs DCIT [2008] 113 TTJ (ITAT Delhi) 767 and Galileo International Inc. [2008] 19 SOT 257 (Delhi) to support the case of MasterCard network creating a PE in India. The Revenue also relied upon a case from Austria (from the book of Mr. Ashish Karundia) where a mile long cable route used by the company for data transmission was held to constitute a PE.

5.13 Revenue also contended that the Bank of India space where more than 90% settlement activity takes place through employees of BOI also creates a fixed place PE as the Applicant is carrying out its work of settlement through it. Settlement position transaction wise is captured in India and is already known to respective banks. MCI, on behalf of the Applicant, only compiles that information into a consolidated settlement position, which incidentally is also known to banks

in India beforehand. Based on this settlement position, the actual debit and credit is passed by dedicated team of BOI. If there is any error, it is the Applicant which is responsible. Thus, the space in BOI where settlement activity is happening is at the disposal of the Applicant and hence constitutes a PE. Reliance was placed on a Swedish case (from the book of Mr. Ashish Karundia) where home office of a Norwegian person was held to be a PE. Based on this the Revenue has submitted that the Applicant is carrying out its activities through dedicated employees of BOI who are specifically assigned a space within BOI to carry out the activity of the Applicant. The BOI is an agent of the Applicant and the space where settlement activity is carried out is at the disposal of the Applicant, and hence constitutes a PE. The Revenue also quoted from Note 4 of Article 5 of OECD commentary to point out that for creating a PE it is not required that the space should be at the exclusive disposal of the Applicant.

5.14 The Revenue has also contended that the Indian subsidiary MISPL is a PE of the Applicant. MCI had a liaison office in India which was admitted as PE by MCI itself in its tax returns for 10 years prior to restructuring. The functions performed by PE were taken over by MISPL, the employees of PE were taken over by MISPL, for Indian customers nothing changed (this has also been admitted by the Applicant), there was no new agreement, risk of MIP continues with overseas AE, ownership of MIP was not transferred through ST/VAT. Thus, the Indian subsidiary was found to be a projection of the erstwhile PE of MCI, and hence PE of the Applicant. Major part of transaction processing was admitted to be happening in India through PE of MCI for which full income was attributed in the return of income for ten years. Before 1.12.2014, about 50% of fees collected from India were offered as income in India, however, after 1.12.2014 only about 2.5% of fee collected from India is offered as income of the Indian subsidiary which took over the functions of PE of MCI and was shown to be performing only support service and not actual transaction processing service.

Thus, there are some functions and risk related to transaction processing which was earlier carried out by the PE of MCI and are still carried out by MISPL but not shown in the FAR of MISPL. Therefore, the subsidiary company MISPL creates PE of the Applicant in India. The Revenue has also relied on some foreign cases which are discussed later.

5.15 The Revenue has also contended that the Applicant has service PE in India as its own employees are visiting India. Further there is service PE through employees of Bank of India as through them service is being rendered. Details of visit of employees of the Applicant to India have been provided that which shows that in a year (FY 16-17), the threshold of 90 days of India Singapore treaty was crossed. The Revenue has relied upon Bangalore ITAT judgment in the case of ABB FZ LLC (ITA no 1103 of 2013) and Hon'ble Supreme Court judgment in E*Funds IT Solution Inc (86 Taxmann 240). The Revenue has also discussed the purpose of meetings, submitted by the Applicant, to support its case that the employees of the Applicant have visited India to render service to its clients. With respect to service PE through Bank of India's employees it has been submitted by the Revenue that for service PE the service could be provided through other personnel as well which in this case is Bank of India.

5.16 The Revenue has also claimed that MISPL is legally and economically dependent on the Applicant and is dependent Agent PE of the Applicant. It has also claimed that Indian subsidiary is habitually concluding contracts or securing orders for the Applicant. The Indian Singapore treaty has a clause for securing orders also.

5.17 The Revenue has submitted that it has not examined the aspect of employees of the Applicant on deputation to MISPL since the Applicant vide reply dated 20th Nov 2017 has submitted that no employee was ever deputed to

MISPL. Under these circumstances the Revenue did not press the point of PE being created due to deputation of employees to Indian subsidiary. Revenue has pleaded that if new facts emerge in these years or in later years, the department would like to examine afresh on this issue as to whether it creates a PE.

6. The Revenue has also contended that payment of transaction processing fee and Master Card network installation/management fee and other fees paid by Indian clients to the Applicant is both Royalty and Fees for Technical Services (FTS). It is royalty on account of use of brand name, trademarks and marks, patent etc., use of MIP equipment and Master Card Network and use of software.

6.1 The Revenue has contended that it is also FTS, as some part of fee may not be royalty but since it is technical/consultancy fee and is ancillary and subsidiary to the application or enjoyment of the right, property or information for which royalty is paid, it is FTS. For this part of FTS, the requirement of make available is not to be satisfied. Notwithstanding this, it has been submitted that the Applicant is also providing other services which make available technical knowledge, experience, skill, know how etc. to Indian clients which helps them in their business.

6.2 Further, the Revenue has contended that the Applicant is carrying on business in India through its PE, and the right, property or contract in respect of which royalties or FTS is paid is effectively connected with such PE, in terms of Article 12(6) of the India and Singapore DTAA. Hence, the royalty/FTS is to be taxed on net basis with the income of PE. The Revenue has specifically relied on Hon'ble Delhi High Court judgment in the case of Formula One World Championship Limited [2016] (supra), Bangalore ITAT judgment in the case of Google India Private Limited [ITA no 1511 to 1518/Bang/2013], Hon'ble Madras High Court judgment in the case of Verizon Communication Singapore Pte

Limited [361 ITR 525], AAR rulings in the case of Dishnet Wireless Limited (AAR no 863 of 2010), Hon'ble Madras High Court judgment in the case of Poompuhar Shipping Corporation (TS 528 HC 2013), Hon'ble Madras High Court judgment in the case of Skycell Communications Limited (251 ITR 53) and ITAT Delhi judgment in the case of Asia Satellite Telecommunications Co. Limited [2003] 78 TTJ 489. Various arguments put forward by the Revenue in support are discussed later.

7. In respect of question no 2, the Revenue has submitted that the Applicant has raised this question only on account of the Indian subsidiary creating a PE and not for other types of PEs. For other types of PEs, thus, there is no doubt that PE is to be remunerated and the remuneration given to MSIPL is not enough. With respect to the subsidiary PE as well, the Revenue has submitted that since the FAR profile of MISPL does not capture the full functions performed, assets employed and risks undertaken by erstwhile PE, the functions/assets/risks not captured are the one which belong to MISPL as PE of the Applicant. Thus for these functions/assets/risks there is need for separate compensation to MISPL as PE of the Applicant. Based on above, the Revenue, in response to question 4, has contended that there is requirement of withholding tax before payment is made to the Applicant.

8. The Applicant has filed its rebuttal to the Revenue's report. It has denied various facts cited by the Revenue and has also pleaded that it neither has PE in India nor there is any payment which can be characterized as royalty or FTS. The rebuttal of the Applicant is summarized below:

8.1 The Applicant has submitted that there are serious and substantial factual errors in the way the Revenue has interpreted its business. The Applicant charges its customer transaction processing fees for the services rendered

relating to the authorization, clearing and settlement of transactions. Additionally, it receives miscellaneous revenues for the provision of special services which are ancillary to the transaction processing service. The MasterCard network facilitates authorization, clearing and settlement of payment transactions between customers on a proprietary, global payment system. The network links issuers and acquirers around the globe for transaction processing services and, through them, permits MasterCard cardholders to use their card at millions of merchants worldwide. Through the Network, MasterCard enables the routing of a transaction to the issuer for its approval, facilitates the exchange of financial information between issuer and acquirers after a successfully conducted transaction, and helps to clear and settle the transaction by facilitating the determination and exchange of funds between parties via settlement banks chosen by MasterCard and its customers. The network is designed to ensure safety and security for the global payment system.

8.2 It further submitted that the detailed processing of the transaction (i.e facilitation of authorization, clearing and settlement) is undertaken by it through the processing centers situated outside India. Authorization happens directly between issuer and acquirer. Issuer bank effectively authorizes the transaction. All authorization messages virtually travel outside of India for the purposes of securing the transaction and for value added services. MIPs, which are owned by the Indian subsidiary of the Applicant and are provided to issuer and acquirer customers, encrypt the date for sending it outside India. It is a simple communication device and has software embedded therein which does the task of transmitting data in an encrypted form. The MIP enables the flow of transactions data and the routing of an authorization message between the acquirer and issuer banks. MIPs route all transactions to the data center(s) outside India for further processing. From there an authorization request is sent to the issuer bank that approves or declines the transaction and sends the

authorization message through the issuer MIP to the acquirer bank on the same route which the authorization message travelled.

8.3 According to the Applicant, the network consisting of computers located outside India carry out fraud checks on the transactions to prevent any kind of security breach. The Applicant, over the years, has developed detailed algorithms and also a computerized database that enable fraud detection and prevention. The Applicant, in certain situations, provides additional services like authorization of transaction using pre-established rules when there is technical glitch. It also provides certain value added services through data centers based outside India. Thus, the Applicant contended that significant authorization processes take place outside of India and MIPs on a standalone basis cannot undertake any significant processing activity other than preparatory and auxiliary edits/data validation and routing of transaction.

8.4 It has submitted that the Revenue has failed to appreciate that even though the transaction gets authorized by the issuer bank, the role of the Applicant's network is not limited to providing connectivity between the MIPs. The network validates the security of the transaction so that the risk of fraud is eliminated or minimized as much as possible. The network facilitates the authorization process to happen in an efficient, secured and expeditious manner. MasterCard has established operation command centers outside India, which monitors the working condition of MIPs all around the world on real time basis. This monitoring is critical to make sure that the transaction routing between the MIPs happens in an efficient manner.

8.5 Enquiries were made by the Revenue from different banks. The Applicant has responded to the findings of the Revenue. With regard to Yes bank reply regarding routing of transactions within India for authorization, it is submitted that

Yes Bank is not in a position to explain where exactly the network is located, what it consists of and what functions are performed outside India. It placed reliance on the reply of other banks like HDFC regarding transaction flows through MasterCard Global Clearing Management System (GCMS) which is located outside India. Similarly PNB has replied that details of the cardholder are routed to Applicant's server for verification. South Indian Bank has also replied that transaction flow happens through MasterCard worldwide network. Thus, the Applicant has contended that the functions of preliminary edits and validation, routing done in India by MIPs play a far less critical role as compared to the role played by the Applicant's processing infrastructure outside India.

8.6 The Applicant has contended that MIPs belong to Indian subsidiary and ordinary telephone lines, wire cables, internet etc. within India belong to third party service providers. The Applicant's network consists of processing centers along with the related machinery and equipment located outside India. MIPs are only routing and communication devices. The Applicant has spent significant sums of money in establishing and maintaining its computerized data processing centers outside India so that millions of transactions are undertaken on a daily basis in a secure manner. Cost of MIP is a fraction of the cost incurred by the Applicant in maintaining server and other equipment that are needed to facilitate and complete authorization, clearing and settlement. The Applicant's server, processing centers and other related machinery, which are located outside India, are valued at almost USD 248 million while value of MIPs located in India are only USD 300,000.

8.7 The Applicant has submitted that after authorization, the acquirer bank prepares a batch of the transactions undertaken for a certain period in a given day. Once the batch is closed, the acquirer bank uploads batch files (containing monetary transactions from their merchants) on the Applicant's network located

outside India. At this stage, the files are in raw form. After this, GCMS processes the raw data. For each transaction, GCMS performs data validation and data integrity to ensure that the transaction data can be processed. GCMS calculates various fees and sends out a file confirmation to the acquirer bank, containing the total count of transactions and any rejected transactions. GCMS generates the settlement positions of the banks. It processes millions of transactions on a daily basis.

8.8 From GCMS, the transaction data is transferred to the Settlement Account Management System (SAM) also located outside India. SAM performs the necessary calculations to determine the final settlement amount for the acquirers by incorporating adjustment data such as charge back, fee etc.. SAM facilitates the transfer of funds for the purpose of financial settlement of cleared transactions and the transfer of funds between MasterCard and its acquirers and issuers. On the basis of net settlement position sent out by SAM, Bank of India merely posts the entries in the accounts of the customer banks for the settlement to get completed. This is a very simple and clerical work which only takes a few minutes of work of one employee of BOI. Due to this low skilled nature of job, BOI is paid service charge of only USD 1500 per month, though the total value of settlement entries may come to as much as USD 114 million per day.

8.9 The Applicant has thus contended that main settlement activity is not passing of net debit and credit entries in the accounts of the acquirer and issuer bank. The task carried out by BOI is an insignificant part of the entire settlement function. The exercise carried outside India is quite complex as there are millions of transaction worldwide that get processed, analyzed and tabulated in the settlement process. The Applicant thus contended that settlement of all 100% of transaction (more than 90% that get settled in INR and remaining that get settled

in foreign currency) is completed outside India through the data centers located outside India.

8.10 The Applicant has also relied on the response received by the Revenue from Bank of India which stated that net settlement position is provided by the Applicant. It has specifically referred to the reply of the HDFC Bank which has referred to SAM. Similarly it has pleaded that various other banks have also confirmed that the Applicant is responsible for carrying out the settlement activities and they are responsible for any errors.

9. With regard to the ownership and functions of MIP, the Applicant has submitted that it was transferred by earlier owner (AE) to MISPL and the transferor has paid capital gains tax. MISPL has claimed depreciation on these MIPs which have also been allowed by the assessing officer in an order under section 143(3) of the Act. With regard to delay in VAT compliance it was submitted that MIPs are located in various states with different VAT laws and hence there is a delay in compliance. It has further submitted that customer banks have entered into an agreement with the Applicant for availing transaction processing services and the Applicant in turn has entered into an agreement with MISPL for provision of MIPs to the banks. Therefore, there is no need for MISPL to enter into any agreement with customer banks. The maintenance is done by third party specialized entity.

9.1 With respect to the Revenue's claim of MIPs and MasterCard network constituting fixed place PE of the Applicant in India, the Applicant has contended that its network is located outside India which consists of server and related machinery and equipment. The Applicant has said that it does not own MIP, routers, cables and wires. The Applicant has also submitted that it does not carry out its business through MIPs and related network that do not belong to it. It has further submitted that MIP and related network do not perform core functions.

The Applicant has also said that MIPs are not at its disposal. The Applicant has also stated that since MIP has no role to play in clearing and settlement it can't create PE since there is no use in authorizing a payment transaction if the money is never moved because there is no clearing or settlement.

9.2 It is submitted that the software inside MIP is preparatory and auxiliary in nature. The software upgrade happens through data centers outside India. These upgrades are routine and involve negligible cost. Cost of maintaining and upgrading the MIPs forms part of the cost base of MISPL on which it receives an arm's length mark up from the Applicant and hence it has financial capacity to maintain MIPs. The Applicant has further submitted that considering that the maintenance and upgradation of MIPs has been outsourced, it is logical that MISPL need not have employees who have the technical knowledge about MIPs. It is quite common for any business to outsource a portion of its business activity to a third party. It is not mandatory that the owner of an asset should have the capability to maintain such an asset. The owner of even very simple electronic equipment may not have the technical expertise to maintain or upgrade it. MIPs are communication device that are used for routing the transactions between the customer banks and the Applicant. MIPs do not make any decisions. Thus the functions performed by MIPs are of preparatory and auxiliary nature and do not involve complex activities. The cost of MIP is only USD 3000-4000 which is miniscule as compared to the value of processing centers located outside India.

10. With respect to Revenue's allegation of colorable device the Applicant has contended that this issue has already been examined by the AAR at the time of admission of the application. This issue of tax avoidance could have been considered only at the time of admission and cannot be considered now. Reliance was placed on Hon'ble AP High Court decision in the case of Sanofi Pasteur Holding SA (354 ITR 316) to plead that there is no power to review the

decision. It has further provided commercial reasoning as to why the APMEA operations were given to the Applicant. The Applicant relied on Hon'ble Supreme Court decision in the case of Vodafone International Holdings B.V. (341 ITR 1) to state that it is conventional to incorporate a separate company in each country for carrying on the business operations in that country. It also contended that it cannot be treaty shopping exercise as both India US and India Singapore DTAA are similar. With regard to difference in tax liability pre and post restructuring it was submitted that the Applicant admitted LO of MCI as PE only under MAP settlement under the DTAA. It is submitted that MAP based settlements were made only in order to obviate protracted litigation with the Indian tax authorities and also because the amounts involved in those years were relatively negligible and did not at all justify such litigation. Reliance was placed on the Hon'ble Supreme Court decision in the case of E*Funds IT Solution Inc (supra) wherein it has been held that, a MAP agreement or settlement is in the nature of a concession made by the Applicant which is not binding on the Applicant for assessment years other than those specifically covered by the MAP settlement.

11. The Applicant has relied upon the ruling of the Hon'ble Delhi High Court in the case of UAE Exchange Center Limited vs UOI (313 ITR 94) to support its point that it is only carrying out preparatory and auxiliary activities in India. The Applicant has stated that use of MasterCard Connect and MasterCard File express is incidental to the main activity of transaction processing service and they perform preparatory and auxiliary services. The Applicant has objected to Revenue's reliance on decision of ITAT Delhi in the cases of Amadeus and Galileo (supra) as the facts are different. It has been stated that Applicant's network and infrastructure is located outside India. The Applicant has distinguished Swiss server *case* on the basis that MIPs are not owned by the Applicant while the Swiss server was owned by the German company. In French online video game case, ATO case and Sweden Data center case the Applicant

has again raised the same objection that in its case, MIPs are performing only preparatory and auxiliary activities. The Applicant has also produced ruling by ATO in its own case where post restructuring, it was held by ATO that the Applicant does not have a PE in Australia. It has been pointed out that in the Australian case, MIP was continued to be owned by a group company outside Australia and were not transferred to Australian subsidiary. It has been pleaded that Revenue should accept this ruling about no PE of Applicant in Australia.

11.1 With regard to the Revenue's claim of BOI premises being a fixed place PE of the Applicant in India, it has pleaded that clearing and settlement activities happen outside India. It has also been contended that BOI cannot be taken as agent of the Applicant since it is an independent entity and can provide similar services to other companies as well. The Applicant has also contended that premise of BOI is not at the disposal of the Applicant as it does not have access to it. The employees of the Applicant cannot immediately walk into BOI and occupy some space. No equipment of BOI has been placed at its disposal. Employees of BOI are not subjected to instruction by the Applicant. BOI is providing services in the ordinary course of banking business for which it is remunerated at arm's length. Reliance has been placed on the Delhi ITAT SB order in case of Motorola Inc [95 ITD 269]. The Applicant has tried to distinguish Swedish home office case by stating that the person here was doing sales activity which was a significant activity. It has been contended that in settlement, significant activity of sorting and collating is done by the Applicant. It has been stated by the Applicant that the Revenue has mixed up the distinct concept of agency PE and service PE. The Applicant has again relied upon UAE Exchange Control case (supra) to argue that the settlement activity carried out by BOI is similar to downloading and dispatch activity performed in that case.

11.2 With respect to the Revenue's claim of Indian subsidiary MISPL constituting fixed place PE of the Applicant in India, the Applicant has submitted that LO of MCI was not a PE as it was doing only preparatory and auxiliary services and the fact of there being a PE has not been upheld by any court in India. It has quoted the Hon'ble decision in E*Funds (supra) to contend that MAP settlement does not lay down principle and tax paid prior to Dec 2014 was to buy peace and because the amount involved was not significant.

12. With respect to the Revenue's claim of MISPL constituting a Dependent Agent PE of the Applicant in India, the Applicant has contended that merely because MISPL is rendering Marketing support service does not mean that it is dependent agent PE. The Applicant has relied upon replies of Yes Bank, Central Bank, South Bank who has stated that they are not aware of role played by MISPL at the time of contract renewal. The Applicant has also relied on the statements of First Rand Bank, Canara Bank and Andhra Bank to contend that they have categorically said that MISPL is not involved. The Applicant has raised a contention that MISPL was not incorporated when agreement with Andhra Bank was signed in 2013. The Applicant has given details of the process in the rebuttal. The Applicant also submitted that MCI had already entered into contracts with most of the banks prior to the takeover of the Indian leg of the business by the Applicant in 2014. Accordingly, the process of negotiation, concluding and securing contracts had already been completed during the period when MCI was in operation. In last three years new agreements have been entered only with 7 new banks. Thus, it cannot be said that the activity is being done by the Applicant habitually. The Applicant also relied on Hon'ble Delhi High Court order in the case of Nortel Networks India International Inc (386 ITR 353).

13. With respect to the Revenue's claim of service PE on account of the Applicant's employees visiting India and BOI's employees, it has been submitted by the Applicant that Revenue has not submitted any evidence to support the

contention that visiting employees are rendering services to customer banks. It has been pleaded that the Applicant's system and processes are automated and do not require constant interaction with the customers. The Applicant also relied upon SC case in the case of Morgan Stanley (292 ITR 416) to plead that such activities should be categorized as stewardship in nature.

14. With respect to the Revenue's claim of use of brand name, trademarks and marks, patent etc. to constitute royalty, the Applicant has contended that all banks in their reply have submitted that the fees is for transaction processing service and not royalty. It is further contended by the Applicant that customer banks are not concerned with the machinery, equipment and the intangibles that are used for rendering transaction processing services. The banks only want their transactions to get authorized, cleared and settled in an efficient manner. They pay for the services and not for intangibles. The Applicant has also contended that no portion of settlement functions happen in India. The Applicant has relied on the Hon'ble Delhi High Court decision in the case of Formula One World Championship Limited(supra) to support its case that use of brand name, logo etc..is only incidental. The Applicant has further contended that service charges are based on the value and volume of transactions which are processed and hence it cannot be for use of brand name, logo etc.. The Applicant has also contended that it is not at all necessary that the Acquirer Bank should be a bank who has issued MasterCard cards bearing MasterCard logo. It could be a bank who has not issued any credit or debit cards or it would be a bank who has issued non Master Card cards. Even then he has to pay fees to MasterCard. This shows that the fee is for the services and not for royalty.

14.1 With respect to the Revenue's claim of use of equipment/ process to constitute royalty, the Applicant has submitted that customers pay service fee to the Applicant and use of MIP is preparatory and auxiliary. The Applicant has also stated that MIP is not owned by the Applicant. The Applicant has contended that

application software do not serve any purpose on standalone basis. The Applicant has submitted that the facts of Verizon Communication case (supra)are different from the facts of this case. The Applicant has submitted that in Verizon case(supra) the private links were under the customers' exclusive dominion and control. However, the control of equipments in this case is not with customer banks. The Applicant has relied upon the decisions of Hon'ble Delhi High Court in the case of Nokia Networks OY (358 ITR 259) and New Skies Satellite NV (382 ITR 114) to plead that amendment to the tax treaty cannot be read into the domestic laws. It has relied on Hon'ble Supreme Court decision in the case of Azadi Bachao Andolan (263 ITR 706) to claim that where provisions of tax treaty is more beneficial, then such provisions should be made applicable. The Applicant has relied on Hon'ble Delhi High Court decision in the case of Asia Satellite Communication Co Ltd (322 ITR 340) to support its case that charges received are for rendering service and not for use of secret process. The Applicant has relied upon AAR rulings in the cases of Dell International Services India Private Limited (172 Taxmann 418), Cable and Wireless Network India Private limited (315 ITR 72) and Factset Research systems Inc. (317 ITR 169) where the AAR has reiterated the proposition laid down by Hon'ble Delhi High Court. The Applicant has further contended that the payment made by customer banks is for availing of service and not for the use of a process. The Applicant has also contended that the process is not secret. It has relied upon Delhi ITAT decision in the case of Panamsat International Systems Inc. (9 SOT 100) to support its contention. The Applicant has also stated that the Revenue's reliance on decision of Bangalore ITAT in the case of Google India(supra) is erroneous. In Google case, Google India was using brand name, logo, and right in IPs. Further they were related parties.

14.2 With regard to the Revenue's claim of use of software constituting royalty, it has contended that there is no standalone provision of MIP and application

software (MasterCard Connect and MasterCard File express) and that the transaction is rendering of transaction processing service. The Applicant has relied upon the Hon'ble Delhi High Court Ruling in the case of Infrasoft Limited and M Tech India Private Limited in its support.

15. With respect to the Revenue's claim of payment made being in the nature of FTS, the Applicant has relied upon the Hon'ble Supreme Court decision in Bharti Cellular Limited (330 ITR 239) to contend that for service to be technical in nature there has to be an element of human intervention. It has been contended that in its case it is automated process and there is no human intervention. The Applicant has also relied on Hon'ble Supreme Court decision in Kotak Securities Limited (383 ITR 1) in support of its claim that what it provides is standard facility and not services. The Applicant has also relied upon Hon'ble Madras High Court Judgment in the case of Skycell Communications Limited (251 ITR 53) where it was held that the provision of facility for use of an electronic exchange, which had mobile communication network with a switching center did not constitute technical services. The Applicant has also contended that make available requirement is not fulfilled. The Applicant has given examples where use of technical equipment may not be use of technical service, like airline passenger paying for travelling in aircraft, consumer getting electricity, etc.. The Applicant has also contended that even if these are technical or consultancy services they are not in relation to the application/enjoyment of property for which royalty is received since there is no royalty in this case. The Applicant also submitted that since "make available" test is not satisfied, it cannot be taxed as FTS under India Singapore DTAA. The Applicant has relied upon various case laws in support.

16. We have considered the issues before us and the submissions of both the Revenue and the Applicant. During these proceedings, Mr. S Ganesh argued on behalf of the Applicant and the Revenue was represented by Mr. Kamlesh C. Varshney, CIT (IT), New Delhi. After conclusion of these proceedings both the

Applicant and the Revenue have also filed their written submissions, which have been duly considered by us. Let us take up each of the issues one by one.

16.1 The first issue is regarding creation or otherwise of a fixed place PE of the Applicant in India.

16.2 As per Article 5 of the India Singapore DTAA, the term "permanent establishment" means a fixed place of business through which the business of the enterprise is wholly or partly carried on.

16.2.1 Against the above, let us examine the Revenue's contention that a fixed place PE can be created under Article 5(1) of India Singapore DTAA on account of MIP if the Applicant carried out its business in India through MIP.As is seen from the above definition, to create a PE, one has to pass the three tests of: permanency, a fixed place and disposal. The Hon'ble Supreme Court in *Formula One World Championships Limited (2017) (supra)* explained the above in detail and added that the said fixed place should be at the disposal of the Applicant. We also have to examine whether the activities are the business proper or not and also whether the activities performed by MIPs are preparatory or auxiliary in character, ie. whether they fall within the exclusion of Article 5(7) of India Singapore DTAA.

16.2.2 On the facts mentioned above and the case cited, we agree with the Revenue's submissions that (i) an automatic equipment can also create PE[*Swiss Server* decision quoted by Hon'ble Delhi High Court in the case of Formula One World Championship Limited vs CIT (supra)] and (ii) to create a PE, fixed place does not mean that the equipment should be fixed to the ground. It is sufficient compliance that it remains on a particular site (Note 5 of OECD commentary on Article 5 of Model Tax Convention). This is also clear from the definition, as explained by the Hon'ble Apex Court in the Formula One case. Thus, even if MIPs are automatic equipment placed at the site of customer banks

in India, they can create a PE provided other tests are satisfied. In its written submission, submitted post hearing, the Applicant has indirectly raised an objection on the first issue when it has said that in the cases of *Amadeus and Galileo (supra)* the assessee was feeding the entry through manual operation, while MIPs are automatic equipment and hence the facts of two cases are different. We shall deal with this objection later.

16.2.3 There is also no dispute that MIPs also pass the test of permanency. They are placed on the site of customer banks throughout the year. Thus, this issue is not in dispute. In fact in the FOWC case, the Hon'ble Apex Court said that it would be sufficient if the fixed place is at the disposal of the foreign entity till the time required by the business. It does not mean forever. The main issues that are required to be discussed are whether there is a requirement that MIPs should be owned by the Applicant, and whether they are at the disposal of the Applicant, and also whether they are performing activities which are of preparatory or auxiliary in character.

16.2.4 The first objection of the Applicant is that MIPs are owned by the Indian subsidiary, MISPL, and not by it. The Revenue has contended that the fact of ownership is not important for creating PE and is relevant only when we come to the question of royalty. We agree with the view of the Revenue. It is clearly laid down in Note 4.1 of OECD commentary on Article 5 of Model Convention that the mere fact that an enterprise has a certain amount of space at its disposal which is used for business activities is sufficient to constitute a place of business. No formal legal right to own or use that place is therefore required. It is sufficient if it is placed at the disposal of the foreign entity. Thus, the fact that MIPs may not be owned by the Applicant is not relevant, if other tests are satisfied. Although Revenue has also pleaded that MIPs are defacto owned by the Applicant, but this issue is not relevant here and hence is not discussed at this point in time.

16.2.5 At this stage, let us look at whether the functions performed by MIPs are significant functions, as held in the case of E*Funds (supra) relating to processing of transactions or are only of preparatory or auxiliary character. There are three stages in transaction processing: authorization, clearance and settlement. Since MIP is involved only in facilitating authorization, we are dealing with authorization only at this stage. The Applicant has contended that MIP is a simple communication device and has software embedded therein which does the task of transmitting data in an encrypted form. It enables the flow of transaction data and the routing of an authorization message between the acquirer and issuer banks. It routes all transactions to the data center(s) outside India for further processing. From there an authorization request is sent to the issuer bank that approves or declines the transaction and sends the authorization message through the issuer MIP to the acquirer bank on the same route the authorization message travelled. It was also stated that MIP also performs some basic functions like simple edits/validation; and is only a communication device which is nothing but a glorified modem. The Revenue on the other hand submitted the extract from Applicant's own submission contained in the application made before us in Form no 34C, Annexure III (item 9) as well as in TP audit report of MISPL for FY 2014-15. It goes as under:

> *"MIPs are special purpose equipment with software embedded therein and consist of Central Processing Unit, Monitor, Router and Multi-protocol label switching unit.*
>
> *MIPs are used for undertaking preliminary examination/validation of information the point of authorization. The preliminary validation generally involves activities such as PIN processing, validation of card codes, names and address verification etc.. In the case of errors, the MIP would alert the acquirer bank/financial institution on the need for a correction and the data is not authorized.*

If the initial validation is successful, the MIP located at the acquirer bank would transfer the data to the issuer bank's MIP, which performs certain other functions, edits and processes. The MIP at the issuer bank will then direct the data to the issuer bank for further processing and verification. The issuing bank will then send a response (generally an approval message) through the MIP at the issuer bank to the MIP at the acquirer bank, which is then passed on to the acquirer bank for transaction approval." (emphasis added).

16.2.6 The above facts, submitted by the Applicant in its application as well as by MISPL in its TP audit report clearly reflect the actual and important functions performed by MIPs. The Applicant in its written submission, post hearing, submitted that the functions performed by MIP were briefly discussed in its application as it was not aware the PE issue would be discussed in such detail. Be that as it may, the quoted facts above are clear and unambiguous, and are not denied. It clearly says that the preliminary validation carried out by MIPs generally involves activities such as PIN processing, validation of card codes, names and address verification etc.. In the case of errors, the MIP would alert the acquirer bank/financial institution on the need for a correction and the data is then not authorized. This leaves no doubt about the important functions performed by MIPs.

16.2.7 The Applicant has again narrated the functions performed by MIPs in its written submission post hearing. As per this, when a MasterCard is swiped at a Merchant's Point of Sale("POS") machine, that machine sends a signal to the Acquirer Bank requesting the authorization of a payment transaction which gets transferred to the Acquirer Bank's MIP, and at this time, the MIP makes a basic scrutiny of the transaction by ensuring that the card used is a MasterCard which has been issued by one of the authorized banks, and the MIP notes the card number, the issuing bank's code number, value of the transaction and the name of the person to whom the card is issued. If a card is not a MasterCard, or it has not been issued by an authorized bank, or if the card number is not within the

recognized range, then the MIP will stop the transaction straightaway and prevent it from proceeding further. According to the Applicant, this is a limited and preliminary check only for the purpose of identifying non-qualifying transactions. The Applicant has further added that PIN code is known only to the Issuer Bank and not to the Acquirer Bank. Consequently, the MIP of the Acquirer Bank cannot possibly verify or validate the PIN code. All that the Acquirer Bank's MIP therefore does is, to transmit the PIN code number that is received in an encrypted form from the POS machine, in the same encrypted form to the Applicant's processing Center outside India. The verification and validation of the PIN code is subsequently done only by the Issuer Bank, which is then communicated through the Issuer Bank's MIP via the processing center outside India. The above facts also substantiate the point that MIPs are involved in preliminary validation/verification. There is no doubt that final validation (including PIN verification) is done by the issuer bank. However, it is also an admitted fact that preliminary verification/validation of PIN, card codes, names and address is done by MIPs (either at the premise of acquire bank or at the premise of issuer bank). The fact of MIPs raising an alert in case of error has also not be disputed by the Applicant.

16.2.8 Let us also have a look at as to how the authorization activity takes place. When a card holder sweeps his card, it is necessary to verify that he is the right person. For this, first there is a preliminary examination done by the merchant, which happens in India. Then the preliminary validation is done by MIPs located in acquirer bank premises, which involve preliminary verification of PIN, checking card codes, names and address verification. The actual part of authorization is played by the issuing bank that does the balance checking, PIN checking and final validation which authorizes the transaction. In between, the messages are encrypted for transmission by MIP. The transmission happens through transmission tower, leased lines, fiber optic cable, nodes, internet

(owned by third party service provider), and Master Connect and Master Card File express, Application software (owned by the Applicant). These are located in India as well as outside India. We say this as it was submitted before us that all transactions go to Singapore for processing, even when both the issuing bank and acquirer bank are the same entity. According to the Applicant, servers outside India perform functions of securing transaction flow, securing validation (to prevent hacking), fraud checks through algorithm and stand in services like back up facility.

16.2.8.1 The above mentioned authorization transaction(as per details given by the Applicant itself) shows the following:

- Preliminary examination/validation for authorization like PIN processing, validation of card codes, names and address verification happens through MIPs located at customer banks premises, in India;
- MIPs alert the acquirer bank if they notices an error and the data is not authorized;
- MIPs also encrypt the date for transmission;
- Transmission also happens through transmission tower, leased lines, fiber optic cable, nodes, internet (owned by third party service provider), and Master Connect and MasterCard File express, Application software(owned by the Applicant). These are located in India as well as outside India.
- The server at Singapore performs functions of securing transaction flow, securing validation (to prevent hacking), fraud checks through algorithm and stand in services like back up facility. These are also important activities for securing the transaction and for preventing frauds.
- The actual authorization is done by issuer bank in India

16.2.9 Hence, we see that the role played by MIPs is a significant one in facilitating authorization process, and without this initial verification/validation by MIPs, the authorization would not happen. Thus, this is a significant activity for authorization part of the transaction processing and cannot be said to be preparatory or auxiliary. We have no doubt that the server at Singapore is also doing important activities of securing the transaction and for preventing frauds, and sometimes stand in activities. However, when we have to see whether MIPs create a PE in India we need to look at the functions performed by them in India in detail and decide whether those functions are significant functions or preparatory or auxiliary in character. The functions performed by the facility at Singapore, such as securing of the transaction, prevention of fraud and add on functions performed by server outside India are also significant functions, but these would be important for attribution and apportionment purposes, which is not the issue under discussion.

16.2.9.1 It is an accepted fact that actual authorization is done by the issuer bank and the Applicant facilitates customer banks in doing that work. The work of facilitation involves preliminary validation/verification (performed by MIP in India), security/fraud detection/add on service (preformed by the Applicant in Singapore) and transmission of data which is crucial to authorization (this happens both in India and outside through MIP and MasterCard network). Thus, the initial verification/validation of PIN, card codes, names and address, and encryption and communication of data is important and crucial function in the context of overall functions performed by the Applicant to facilitate authorization. These functions cannot be called preparatory or auxiliary.

16.2.10 Coming to the question whether the MIPs are at the disposal of the Applicant, we find that these are shown to be owned by Indian subsidiary MISPL. However, the FAR profile of MISPL only shows that it is performing support activity and not actual transaction processing. This clearly means that

authorization part of the transaction processing activity, carried on by MIPs, is the activity of the Applicant and not of MISPL. Thus, this function performed by MIP, which is part of transaction processing, is the function of the Applicant and not the function of MISPL(which is only performing support functions).

16.2.10.1 It is also brought to our notice that the Applicant is controlling MIP through licensing agreement and MasterCard rules, which it enters into with customer banks in India. Though MIPs are shown to be owned by MISPL, there is no agreement between customer banks and MISPL. The situation has remained same even after restructuring when the MIPs ownership was transferred by the AEs of the Applicant to MISPL. It is admitted by the Applicant that regular update and maintenance is carried out by specialized third party entity. But it is important to see who enters into contract with this specialized entity and on whose behalf. It is admitted by the Applicant that AE of the Applicant outside India had entered into contract for maintenance and upgradation of MIPs before 1st Dec 2014 and the same situation continues after that also. Thus, the maintenance and upgradation of MIPs is not done on behalf of MISPL.

16.2.10.2 It is also seen that the cost of maintenance and upgradation of MIP is charged to MISPL but it is further seen that MISPL charges the same cost with mark up to the Applicant. In FY 2014-15, MISPL paid Rs 2,48,89,605 to overseas AEs for maintenance for MIP, added 12% mark-up and then charged Rs 2,78,76,396/- to the Applicant for provision of processing support. This clearly shows that all costs of MIP maintenance and upgradation ultimately get charged to the Applicant. Thus MISPL has neither financial nor the technical ability to do maintenance and upgradation. In the written submission post hearing it has been submitted by the Applicant that they have requisite skills to manage the operation of MIPs, though this is not substantiated. We are of the view that managing MIP is different from maintaining and upgrading, which require technical assistance.

16.2.10.3 The Applicant attempted to explain this position through the example of an owner of an electronic instrument, who need not have capability to undertake the maintenance work. This example doesn't help, since in the present case the owner, ie. MISPL does not exercise any of the rights of an owner, such as deciding whether and when to repair the instrument or buy a new one; agreeing to the terms and conditions of repair; whom to engage for repair and at what cost, and so on. In the present case, all these risk mitigation decisions are taken by the Applicant or its overseas AEs on its behalf. They enter into the agreement with third party service providers on their own behalf and not on behalf of the MISPL. The Applicant enters into agreement with banks. Thus all decisions with respect to MIPs are taken by the Applicant. All costs get charged to the Applicant. These facts, as brought out by the Revenue in its report, are not disputed by the Applicant. Further, the Applicant itself has admitted in the rebuttal that the software upgrade happens through data centers outside India, however, the upgrades are routine and involve negligible cost. Further, it is also admitted in the TP report of MISPL that all intangibles are owned by the Applicant and not by MISPL. Thus, the software inside MIP is also admitted to be owned by the Applicant and which is also upgraded by third parties on behalf of the Applicant.

16.2.10.4 In its written submission, the Applicant has also provided details of "MasterCard-one time license fee" referred to in the billing manual. This fee is charged to an affiliate member as a one-time on-boarding fee for availing transaction processing services. One time on-boarding fee is paid for the cost of MIP installation, for establishing connectivity and set-up of processors. This is an additional evidence to prove that MIPs are at disposal of the Applicant as the Applicant is charging fee for cost of its installation.

16.2.11 In view of the above analysis, we are of the view that these facts clearly establish that MIPs, though shown to be owned by MISPL, are not under

the control or disposal of MISPL. As mentioned earlier, in the case of Formula One (supra) it was clearly held that the being "at the disposal of" would mean right to use and having control over that place/equipment. Thus, it is clear that the Applicant has right to use MIP and has control over it. It is also admitted by both the Revenue and the Applicant that MIPs are not under the disposal of customer banks in whose premise these MIPs are located. This reinforces our view that the MIPs are under the disposal of the Applicant since all risk mitigation functions are performed by it and all decisions with respect to MIPs are taken by it.

16.2.12 As regards the clearing and settlement functions, as per the Applicant, this cannot create a PE since there is no use in authorizing a payment transaction if the money is never moved because there is no clearing or settlement. We do not agree. Transaction processing has three stages: authorization, clearing and settlement. It is not necessary that PE will be created only if the fixed place/equipment is involved in all three stages. Involvement in even one stage (without it being preparatory or auxiliary) can create PE, provided they are significant. The distinction of these three stages (authorization, clearance and settlement) would be important for profit attribution and not for creating a PE.

16.2.13 Thus, we hold that the Applicant is carrying out its business of facilitation of authorization of transaction through fixed place, ie. MIPs, since MIPs situated in India are at its disposal. The functions performed by MIPs in facilitation of authorization transaction are not preparatory or auxiliary in character and are significant functions. Hence, MIPs create a PE of the Applicant in India.

16.3 Let us see some of the arguments of the Applicant, other than the functioning and role of MIPs. Its reliance on the decision of the Hon'ble Delhi High Court in the case of UAE Exchange Center Limited (supra) appears to be misplaced, as the facts of this case are different. In that case the LO in India was like a post office company which used to download the remittance particulars through electronic media and then print the cheques/drafts for delivery. These were held to be subsidiary activities, as the main activity of fund transfer had already happened overseas and only supporting activity was happening in India, subsequently. In our case an important component ie. transaction processing and authorization is happening in India though MIPs. In the case of UAE Exchange, the work performed was of fund transfer which was happening outside and only supporting work was done in India which was found to be of no or very little significance. In this case the work of authorization, including validation of customer in the form of checking PIN, checking card codes, names and address verification, etc. are a significant activity, aligned to the other stages. The remaining process cannot go forward without this initial verification.

16.3.1 The Applicant's argument of the cost of MIPs being fractional to the cost of infrastructure that is outside India, is of no significance. We just need to look at the tests for creating PE which have been found to be satisfied in this case. Even otherwise, the infrastructure outside India is catering to many countries and is also used for activities other than transaction processing. The server outside India has important information about the people using credit card/debit card, their spending pattern, age profile etc.. This in itself is very useful and valuable information and the investment made for infrastructure outside India would be useful for storing and analyzing this valuable information which may not be relevant to transaction processing but can be sold later. Many companies like facebook, linkedin, whatsapp etc. are doing the same. But this has no relevance as far as the issue under discussion here is concerned.

16.3.2 As regards employees' strength going up in Singapore, again we see no relevance of this to the creation of PE in India. It may only indicate that the activities in Singapore are growing, but these do not cut through the importance and role of the MIPs in India.

16.3.3 Both the Applicant and the Revenue have admitted that responses received from various banks by the Revenue under section 133(6) of the Act would not present the correct picture as these banks would not be in a position to know how exactly transaction processing is happening. Hence, we are not relying on the responses Revenue has received from various banks.

16.3.4 We would ordinarily be inclined to accept the Ruling of the Australian Taxation Office (ATO), cited by the Applicant, where it was held by the ATO that the Applicant does not have a PE in Australia on account of MIP, provided the facts are similar. In the Australian case, MIPs were continued to be owned by a group company outside Australia and were not transferred to the Australian subsidiary. But in that case it appears that 'A' co. is tax resident of country A (the Applicant and tax resident of Singapore). 'B' co. is resident of Australia (subsidiary of MasterCard in Australia). 'C' co. is resident of country 'B' (some other MasterCard entity which owns MIPs and is resident in some third state, other than Singapore and Australia). These facts are confirmed by the applicant. Applying these to our case, we have 'A' as our Applicant, 'B' is the MasterCard subsidiary in Australia, and 'C' is MasterCard group entity outside Australia/Singapore, owning the MIPs. The ruling says that the computer processor (MIP) which performs the automated processing services is owned by 'C' co. and is located at each customer's premises. Through the computer processors (i.e MIPs) and through the processing centers that 'C' co. owns and operates in country 'B' (this is some third country where 'C' Company has a

processing centre), ‘C’ co. provides the processing services to ‘A’ co. and receives fees. Some processing services are performed at the processing center in Australia which is owned by ‘B’co. As between ‘A’ Co. and the customers, it is A co. that is responsible for the provision of the services. However, ‘A’ co. enters into separate agreements with ‘B’ Co. and ‘C’ co., so that it is ‘B’ co. and ‘C’ co. that perform the services. The picture that emerges is as under:

- Applicant does not own MIP and the company that owns MIP is providing transaction processing service and not the Applicant.
- MIP is shown to be doing transaction processing service and not any preparatory or auxiliary service. It is clearly stated that transaction processing service is rendered through MIP and processing center. The company owning MIPs (C) gets compensation for transaction processing service.
- Australian subsidiary is also providing transaction processing services.
- Transaction processing services are provided by Australian company (B) and another group company (C) to the Applicant (A).

The above facts are different from our case. In our case transaction processing is shown to be done by the Applicant and not by Indian subsidiary or any other MasterCard group entity. It is in this context this Australian ruling says that ‘A’ does not have PE in Australia. In Australia also, the MIP is not owned by the Applicant. However, still the issue of PE was examined. MIP was not held to be PE as it was not substantial equipment. In Australia Singapore DTAA there is special clause for substantial equipment and hence in the case of equipment constituting PE, the term “substantial” has to be satisfied. There is no such clause in India Singapore DTAA and hence whether MIP would constitute PE would be governed by general clause alone and there is no requirement of

proving “substantial”. The Australia Singapore treaty does not have service PE in their DTAA which we have in our DTAA with Singapore.

16.3.4.1 From the above it is clear that Australian ruling with limited facts support the case that MIP is doing transaction processing service and not any preparatory and auxiliary service and the company owning MIPs is getting compensation for transaction processing service. Further, it may not have created PE under Australia Singapore DTAA due to requirement of being “substantial equipment” but it can create PE in India since there is no such requirement under India Singapore DTAA.

17. We now come to the question as to whether the MasterCard Network creates a fixed place PE of the Applicant, in India. Although we have held that MIP constitutes PE but it is important to see whether MasterCard network also creates PE or not. This is for the reason that MIP is involved only in the authorization part of the transaction processing while the MasterCard Network is involved in all the three phases of transaction processing, i.e authorization, clearance and settlement. Thus, this would be relevant for the assessing officer for attribution purposes.

17.1 The Applicant has submitted that MasterCard Network lies outside India and no part of it is in India. However, the Revenue has quoted the following from the TP report of MISPL for FY 14-15:

> *“MCT LLC is responsible for management and maintenance of MasterCard Worldwide Network remotely from the USA. For the same, MCT LLC has entered into various agreements with third party service providers for the maintenance of the MasterCard Worldwide Network (this includes the MIPs owned by MISPL). The direct and indirect cost of maintaining the MIPs are allocated by MCT LLC to MISPL which forms part of the cost base of processing support services”.*

17.2 Thus, it is admitted that MIP is part of MasterCard Network and so are the transmission tower, leased lines, fiber optic cable, nodes and internet (owned by third party service provider), and Application software - Master Connect and Master Card File express (owned by the Applicant), which are in India as well as outside India. It is also admitted that MCT LLC is responsible for management and maintenance of MasterCard Worldwide Network remotely from the USA. The Revenue's contention is that this creates a PE of the Applicant.

17.3 MasterCard Network is helpful in authorization (through MIP and other part of network) which we have already discussed. MasterCard Network is also helpful in clearance and settlement. The Revenue has submitted that the Applicant has admitted in its reply dated 4th October 2017 that clearing process establishes a settlement position, and settlement is movement of the fund from issuer bank to acquirer bank. The Applicant has submitted that after authorization, the acquirer bank prepares a batch of transactions undertaken for a certain period in a given day. Once the batch is closed, the acquirer bank uploads batch files (containing monetary transactions from their merchants) on the Applicant's network located outside India through the application software Master Connect and Master Card File express. At this stage, the files are in raw form. After this, GCMS processes the raw data. For each transaction, GCMS performs data validation and data integrity to ensure that the transaction data can be processed. GCMS calculates various fees and sends out a file confirmation to the acquirer bank, containing the total count of transactions and any rejected transactions. GCMS generates the settlement positions of the banks. It processes millions of transactions on a daily basis.

17.3.1 From GCMS, the transaction data is transferred to the Settlement Account Management System (SAM) also located outside India. SAM performs

the necessary calculations to determine the final settlement amount for the acquirers by incorporating adjustment data such as charge back, fee etc.. SAM facilitates the transfer of funds for the purpose of financial settlement of cleared transactions and the transfer of funds between MasterCard and its acquirers and issuers. On the basis of net settlement position sent out by SAM, Bank of India merely posts the entries in the accounts of the customer banks for the settlement to get completed. This is a very simple and clerical work which only takes a few minutes of work of one employee of BOI. Due to this low skilled nature of job, BOI is paid service charge of only USD 1500 per month.

17.4 Thus, it can be seen that the settlement position is nothing but the information as to which bank is to pay which bank and how much. It is accepted that in more than 90% of transactions both acquirer banks and issuer banks are in India. In a day, thousands of transactions happen amongst all these issuer banks and acquirer banks. Each transaction would make one bank liable to pay another bank. A sum total of all the transactions between two banks, on a given day, establish settlement position between those two banks. This is clearance. Now the question that arises, from our perspective, is as to whether this is happening in India or outside. There is no doubt that the data relating to transaction between two banks is transferred within India and outside India through transmission towers, leased lines, fiber optic cable, nodes and internet (owned by third party service provider) which is part of MasterCard Network.

17.4.1 The raw data is transferred outside by various banks using the two application software Master Connect and Master Card File express (owned by the Applicant), which is also part of MasterCard Network. Thus the activity of transmission of information between various banks in India and uploading of raw data and receipt of final data using application software are preformed in India. The Applicant has contended that actual calculation of final position happens

outside India. The Revenue has contended that this position is already known to banks in India and that is why the final data sent by Applicant to various banks is subject to confirmation by these banks in India. Thus, the Revenue has contended that clearing happens in India since the banks in India already know the final settlement position of each day. In the written submission post hearing, the Applicant has again stated that each Bank/NBFC issues millions of cards to customers all over India, and transactions on these cards also take place all over India. In all these millions of transactions, each Bank/NBFC may be involved as an acquiring (receiving) Bank or as an Issuing(Paying) Bank. Without the activities of the processing centers outside India, it is absolutely impossible for each Bank/NBFC to be aware of the total of the debit and credit transactions involving its cards, which have taken place each day. We do not agree to this. All transactions go through the customer bank in its capacity as acquirer bank or issuer bank. Both of them know the amount payable or receivable in that particular transaction. There may be thousands or millions of transactions every day, the position of all these transactions is already known to customer banks. These banks also sum up these transactions to know their net position in a particular day. That is why net position sent by the processing centre from outside India is further subjected to checks by these banks. This clearly establishes that even without the net position sent by the Applicant from overseas, Banks in India are already aware of their net position.

17.4.2 So far as the exact settlement is concerned, the Revenue has contended that this is done by Bank of India, since Applicant itself has admitted that settlement means movement of fund between two banks. This movement happens only when Bank of India passes debit and credit entries in the accounts of two banks here in India. Thus, the Revenue has contended that both clearance and settlement happens in India. In fact, Applicant has also admitted in Annexure III of its application that Domestic INR settlement happens in India

through the settlement bank account of MCI in India. As discussed earlier, domestic INR settlement accounts for more than 90% of transactions. The Applicant in written submission post hearing has stated that Settlement Function consists of the preparation of the settlement statement by SAM abroad. We do not agree to this, for the reason that the Applicant itself has agreed that the movement of funds between issuer banks and acquirer bank is settlement. The preparation of settlement position is incomplete unless the Bank of India actually moves the fund from one bank to another bank. Thus, settlement happens when Bank of India carries out this movement and this happens in India for more than 90% of the transactions. The Applicant in its application before us has also admitted that settlement happens in India for domestic settlement.

17.5 We are of the view that the Revenue is justified in taking a position that clearance and settlement happen in India. We do accept that there are functions performed by GCMS and SAM outside India which are also significant functions. However, it is true that even without those functions performed, Banks in India know their individual settlement position against each other. GCMS and SAM consolidate that position and prepare a final picture for all banks which helps in settlement. It is also true that actual settlement is movement of fund between two banks and that happens in India through Bank of India. Thus we hold that significant activities relating to clearance and settlement take place in India. Now we need to examine whether this creates a PE for Applicant in India or not.

17.5.1 MasterCard Network in India consists of MIP owned by MISPL, transmission tower, leased lines, fiber optic cable, nodes and internet- owned by third party service provider, and Application software - Master Connect and Master Card File express, owned by the Applicant. We have already discussed that ownership of equipment/space is not relevant to decide whether it creates a PE. What is important is that it should pass the test of permanence, fixed place

and disposal. There is no doubt that just like MIP, the network also passes the test of permanency and fixed place. It also passes the test of disposal since it is admitted in the TP report of MISPL that MCT LLC is responsible for management and maintenance of MasterCard Worldwide Network remotely from the USA. Infact, Application software- Master Connect and Master Card File express are owned by the Applicant and controlled by them, and are therefore at the disposal of the Applicant. About MIP we have already discussed that it is at the disposal of the Applicant. The part of network provided by third party service provider in India is also at the disposal of the Applicant. During hearing Senior Advocate Mr. S Ganesh appearing for the Applicant had submitted that the network in India is also secured by MasterCard to prevent fraud and to enhance security. Thus, MasterCard Network in India is at the disposal of the Applicant.

17.5.2 Reliance has been placed by the Revenue on the decision of Delhi ITAT in the cases of Amadeus Global Travel Distribution and Galileo International (supra) to support the case of MasterCard network creating PE in India. In these cases the non-resident enterprise was running a fully automatic computer reservation and distribution system with the ability to perform comprehensive information, communications, reservations, ticketing, distribution and related functions on a worldwide basis for the travel industry, particularly participating airlines, hotels, etc. (hereinafter referred to as 'CRS'). In India CRS was installed on the computer of travel agents. Customers approached the travel agent who used this CRS to transfer the requests to main server outside India which did the processing to throw up the best possible results for hotels and airlines, matching the customers' preferences. On these facts it was held that CRS constitutes PE of the nonresident enterprise in India. What was CRS in the Amadeus and Galileo cases is MIP and application software (Master Connect and Master Card file) in the present case. It is this important instrument and software which conducts the business of the Applicant in India and it is installed in India. In the

case of Amadeus and Galileo, it is installed inside the computers of travel agents (which could be computers of travel agent modified after including CRS or computer itself provided by assessee or its agent). In our case, the software and process technology (which is part of MIPs and is owned by the Applicant or licensed to it by the owner) is installed in the premises of the Customers (banks/FIs etc.) in India. The application software (Master Connect and Master Card file, owned by the Applicant) is installed at the computers of Banks/FIs. The connectivity to MIP and Banks computers is provided by various service providers through cables as well as internet. Similar was the position in the cases of Amadeus and Galileo as well.

17.5.3 However, before coming to any conclusion, let us examine whether the activities can be classified as preparatory or auxiliary in character. Revenue has relied upon the commentary by Klaus Vogel book on Double Taxation Conventions, Third Edition, page no 321 and 322 (copy placed on record during the course of hearing). According to it:

> *"As to whether or not a specific activity is of a preparatory or auxiliary character, each case will have to be examined on its merits; regard being had to the enterprise's overall activity. The question to be asked against this background is whether the activity concerned has a preparatory or auxiliary character in the sense of its being of no or of very little significance in view of the other work performed by the enterprise. Whether it is ordinary and necessary for the enterprise to undertake an activity itself is difficult to clearly determine, especially if the practice in an industry is such that more and more enterprises contribute to the production process so that the involvement of any one firm is smaller. It does not depend on the scope of the means employed. Thus a business representation with six employees but which lacked the authority to conclude contracts is also not a permanent establishment…………*
>
> *It is only where they are exercised for the enterprise itself that such preparatory or auxiliary activities do not constitute a permanent establishment. If they are services rendered for a consideration and for a third party, they will*

constitute the enterprise's main object, and corresponding facilities may well be permanent establishments. In an individual case, an activity of a specific kind exercised within the framework of an enterprise may be no more than of an auxiliary character, while being the sole business activity of some other enterprise, such as in the case of advertising or scientific research. Where a laboratory, generally performing nothing but preparatory services for the enterprise to which it belongs, or the advertising division of an enterprise, in certain cases also performs services directly for third parties, its activities will to that extent no longer be of an auxiliary character. The laboratory, or the advertising division, as a whole will then be subject to taxation as a permanent establishment………"

17.5.4 Thus, in order to decide whether a particular activity is preparatory or auxiliary we need to look at the work performed by the enterprise as a whole which is of transaction processing. In the context of transaction processing the work performed by MasterCard Network as outlined above cannot be termed as one of very little significance. Main authorization is done by issuer bank in India. The actual settlement by passing debit or credit entry is done by Bank of India in India. MIPs do preliminary validation/examination. Then the MasterCard Network helps in transmission of information amongst various entities. The Server in Singapore also does significant work of securing the transaction. Applicant also carries out maintenance of MIP and MasterCard Network. GCMS and SAM consolidate the data and give it final shape. In this background, the task performed by MIP (preliminary verification/validation part of authorization and encryption of data), network in India (transmission of data), application software (sending and receiving data) are significant activities when seen in the context of overall functions of transaction processing rendered to a third party. The above citation from Klaus Vogel talks about an important aspect that work of R&D and advertisement, if done for the enterprise may be preparatory or auxiliary but when done for third party it would not be preparatory or auxiliary. In this case the part of transaction processing performed by MasterCard Network is for third parties and therefore cannot be called preparatory or auxiliary. Thus, transmission of data when done for the third party (as is the case here) is not

preparatory or auxiliary, since the overall activity of MasterCard is of transmission of signal amongst merchant and banks, and after securing them the third party is paying for such services. If we include the functions performed by MIPs, the activity of MasterCard Network in India is more than just transmission of data. In fact, we find that the activities performed in India in this case are significantly more than what were performed in India in the cases of Amadeus Global Travel Distribution SA and Galileo International Inc(supra).

17.5.5 The Applicant has objected to Revenue's reliance on decision of ITAT Delhi in the cases of Amadeus and Galileo as the facts are different. It made a submission that CRS, in the cases of Amadeus and Galileo, installed in India had the ability to perform comprehensive information, communication, reservation ticketing, distribution and related functions, hence it cannot be compared to MIP. The Applicant in its written submission post hearing has contended that the definition of CRS in the agreement between the assessee and the Indian travel agent is of the utmost significance and the same is accordingly reproduced hereunder:

> *"'Computerised Reservation System' or 'CRS' means an automated system which processes Booking data and other data to provide any or all of the following functions:*
>
> *(a) the ability to display flight schedules and seat availability;*
> *(b) the ability to display and/or quote airline fares;*
> *(c) the ability to make airline seat reservations;*
> *(d) the ability to issue airline tickets; and*
> *(e) the ability to perform any or all of the functions similar to the above functions in respect of hotel, car and other travel related services other than air services;"*

17.5.5.1 According to the Applicant, the above-mentioned definition of CRS is critical because it clearly shows and establishes that in fact what was installed in the premises of the Indian travel agent was an integral part of the assessee's

worldwide CRS which was seamlessly integrated and inter-connected with the rest of the system operating elsewhere all over the world. As a result, the worldwide CRS database became instantly and continuously a part of the database which was continuously available to and at the disposal of the Indian travel agent at all times. This is what enabled the Indian Travel Agent to instantly give a confirmed reservation to a customer in India in respect of a hotel room or an airline seat anywhere in the world. Further, as per the Applicant, it was a fact that a part of the CRS was actually installed in the travel agent's office which enabled the travel agent to instantly issue a confirmed air ticket to a customer in respect of any particular flight of any particular airline. The Applicant believes that it is of utmost importance to understand that it is not as if the travel agent's computer was a mere communication device which merely sent a signal to a foreign operator or data processing center requesting for hotel reservation or an air travel confirmation. Further, the Applicant has submitted that, it is not as if that communication sent by the travel agent was then processed abroad, and the reservation or confirmation was then communicated or intimated from abroad by the foreign operator/processing center to the Indian travel agent. On the contrary, as per the Applicant, the processing of the request for hotel reservation/air travel confirmation took place and was finally completed in the travel agent's computer in India itself and an intimation of that final transaction was then fed into the worldwide database, only in order to avoid double booking. Thus, the Applicant has submitted that it was in these special and extra ordinary circumstances that the ITAT gave a specific finding (in Paras8.2and 17 of the judgment in the Galileo case) that the transaction which generated Revenue for the non-resident assessee, namely the confirmation of the hotel reservation or the issuance of airline ticket, itself took place in India and therefore, this was clearly a case of a fixed place of business PE of the non-resident in India, through which the core revenue generation activities were actually carried out.

17.5.5.2 The issue arising out of above contention of the Applicant needs to be clarified. It is important to know where exactly the processing activity takes place. That is when the request of the customer is fed into CRS, at which place that request is processed and best possible alternatives for the customer is generated. This is important to know before we compare the facts of this case with our case. Hence, it is necessary to see exactly what was ruled by Delhi ITAT in the case of Galileo (supra).The relevant portion of the judgment relied upon by the Applicant is as below:

> *" 8.2 In light of the above provisions in the Income-tax Act and the judicial pronouncements, we may appreciate the facts and deal with the issue. The appellant has developed a fully automatic reservation and distribution system known as Galileo system with ability to perform comprehensive information, communication, reservation, ticketing, distribution and related functions on a worldwide basis. Through this Galileo system, the appellant provides service to various participants, i.e., Airlines and hotels etc..whereby the subscribers who are enrolled through the efforts of NMC can perform the functions of reservations and ticketing etc.. Thus the Galileo system or the CRS is capable not only processing the information of various Airlines for display at one place but also enables the subscribers to book tickets in a way which is a seamless system originating from the desk of the subscriber's computer which may or may not be provided by the appellant but which in all cases are configured and connected to such an extent that such computers can initiate or generate a request for reservation and also receive the information in this regard so as to enable the subscriber to book the airlines seat or hotel room. The request which originated from the subscriber's computer ended at the subscriber's computer and on the basis of information made available to the subscriber, reservations were also possible. It is to be noted that all the subscribers in respect of which income is held taxable are situated in India. The equipment, i.e., computer in some cases and the connectivity as well as configuration of the computer in all the cases are provided by the appellant. The booking takes place in India on the basis of the presence of such seamless CRS system. On the basis of booking made by the travel agent in India, the income generates to the appellant. But for the booking no income accrues to the appellant. Time and again it is contended that the whole of the processing work is carried out at host computer situated at Denver in Colorado, USA and only the display of information is in India for the proposition that there is no business connection*

in India. We are unable to agree with such proposition. The CRS extends to Indian territory also in the form of connectivity in India. But for the request generated from the subscriber's computer's situate in India, the booking is not possible which is the source of Revenue to the appellant. The assessee is not to receive the payment only for display of information but the income will accrue only when the booking is completed at the desk of the subscriber's computer. In such a situation, there is a continuous seamless process involved, at least part of which is in India and hence, there is a business connection in India. The computers at the subscriber's desk are not dumb or are in the nature of kiosk incapable of performing any function. The computers along with the configuration has been supplied either by the appellant or through its agent Inter globe and the connectivity being provided by the appellant enables the subscribers to access the CRS and perform the ticketing and booking functions. The existence of business connection can be summarized thus :

(1) Assessee hires SITA nodes in most major cities in India together 800 land lines for maintaining telecommunication network in India as evident at page Nos. 278 to 281 of the assessee's paper book No. 1.

(2) Assessee secures the provision of the operation of the communication network from SITA node to travel agent as evident at page 281 of assessee's paper book No. 1.

(3)By Clause 15.3 of the Distribution Agreement, the assessee specifically authorises Interglobe (Galileo India) to conclude agreements with the Travel agents in India in accordance with the model Subscriber Agreement which forms an annexure to the said Agreement.

(4)Assessee lays down targets and closely supervise and reviews the performance of Galileo India on day-to-day basis in accordance with the Annual Plan and the service manual prescribed by it as per clause 14 of Distribution Agreement.

(5) Assessee allots access code to the travel agents for using the CRS.

(6) The assessee's business comprises of :

(a) Maintenance and running of CRS;

(b) Providing computer modem and software to the travel agents in India so that they can use the CRS for making the bookings which generate charge on the airlines;

(c) Assessee hires from SITA and maintains and operates telecommunication network in India so that travel agents could make the bookings.

All these activities are integral part of the core business carried on by the assessee and these are not auxiliary or preparatory in nature.

The contention of Shri Vyas regarding reliance on the decision in the case of Fisher (supra) in this case is misplaced. Whether the contract for sale of ticket is completed in India or outside is irrelevant for the purpose of present discussion as we are not to determine the taxability of income of various airlines accruing as a result of sale of tickets through the CRS in India. Thus, the availability of the tickets displayed through the CRS at the desk of travel agents in India is whether offer for sale or an invitation to an offer is not a deciding factor. What we find is that part of the Galileo system exists in India in the form of configuration and connectivity of such system through which booking activities can be performed in India. The decision of ITAT, Bangalore Bench in the case of Wipro Ltd. (supra) is also misplaced as in that case no part of the data processing facility was performed in India but wholly outside India. In the present case, the appellant operates the Galileo system which is the source of Revenue and part of such system exists in India. Thus there is a direct business connection established in India and hence in terms of section 9(1)(i) of the Act, the income in respect of the booking which takes place from the equipment in India can be deemed to accrue or arise in India and hence taxable in India."

Para 17 of the judgment is academic discussion and is not produced here

" 17.1 In the present case it is seen that the CRS, which is the source of Revenue is partially existent in the machines namely various computers installed at the premises of the subscribers. In some cases, the appellant itself has placed those computers and in all the cases the connectivity in the form of nodes leased from SITA are installed by the appellant through its agent. The computers so connected and configured which can perform the function of reservation and ticketing is a part and parcel of the entire CRS. The computers so installed require further approval from appellant/Interglobe who allows the use of such computers for reservation and ticketing. Without the authority of appellant such computers are not capable of performing the reservation and ticketing part of the CRS system. The computer so installed cannot be shifted from one place to another even within the premises of the subscriber, leave apart the shifting of such computer from one person to another. Thus the appellant exercises complete control over the computers installed at the premises of the subscribers. In view of our discussion in the immediately preceding paragraph, this amounts to a fixed place of business for carrying on the business of the enterprise in India. But for the supply of computers, the

configuration of computers and connectivity which are provided by the appellant either directly or through its agent Interglobe will amount to operating part of its CRS system through such subscribers in India and accordingly PE in the nature of a fixed place of business in India. Thus the appellant can be said to have established a PE within the meaning of paragraph 1 of Article 5 of Indo-Spain Treaty.

17.2 The next question to be considered is if there is a permanent establishment, whether the exception provided in paragraph 3 of Article 5 applies so as to hold that there is no permanent establishment in India. The case of the appellant is that the existence of such computers are merely for the purpose of advertising and the activities are preparatory or auxiliary in character and hence there is no fixed place PE in India in view of the Exception provided in paragraph 3 of Article 5. We are unable to accept such a contention. The function of the PE in India is not to advertise its products. The activity of the appellant is developing and maintaining a fully automatic reservation and distribution system with the ability to perform comprehensive information, communication, reservation, ticketing, distribution and related function on a worldwide basis. The computers installed at the premises of the subscribers are connected to the global CRS owned and operated by the appellant. Using part of the CRS System, the subscribers are capable of reserving and booking a ticket. Thus it cannot be considered as "solely for the purpose of advertising" of such CRS system. Similarly it is not in the nature of 'preparatory or auxiliary' character. It is difficult to distinguish between the activities which are 'preparatory or auxiliary' character and those which are not. The decisive criteria is whether or not the activity of the fixed place of business in itself forms an essential and significant part of the activity of the enterprise as a whole. Since part of the function is operated in India which directly contributes to the earning of Revenue, the activities as narrated above carried out in India are in no way of 'preparatory or auxiliary' character."

17.5.5.3 Facts of the above case in Galileo become clear from above part of judgment. Computers in the premise of travel agents in India are configured and connected to CRS of the non-resident assessee so that such computers can initiate or generate a request for reservation and also receive the information in this regard, so as to enable the subscriber to book the airlines seat or hotel room. The booking takes place in India on the basis of the presence of such seamless CRS system. On the basis of booking made by the travel agent in India, the

income generates and arises to the appellant. But for the request generated from the subscriber's computer situated in India, the booking is not possible which is the source of Revenue to the assessee. It was on this basis it was held that there is PE in India. In fact, it was clearly held that subscribers are capable of reserving and booking a ticket using only a part of the CRS system. It is clear from the above that the part of CRS system in India referred to here is the one which enables computers to initiate or generate a request for reservation and also receive the information in this regard so as to enable the subscriber to book the airlines seat or hotel room.

Thus, it is not a case that main processing of consumer request is done in India, as contended by the Applicant. This also becomes clear from paragraph 9 of the same Galileo judgment which is as under:

> *" 9. The next question therefore, arises is whether having held that there is business connection in India, how much income is chargeable to tax in India. As per section 9(1)(i) of the Act, income accruing or arising whether directly or indirectly through or from any business connection in India shall be deemed to accrue or arise in India. As per clause (a) of Explanation 1 to section 9(1)(i) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India. Thus in a given case if all the operations are not carried out in India, the income has to be apportioned between the income accruing in India and income accruing outside India. In the present case, we find that only part of CRS system operates or functions in India. The extent of work in India is only to the extent of generating request and receiving end-result of the process in India. The major functions like collecting the database of various airlines and hotels, which have entered into PCA with the appellant takes place outside India. The computer at Denver in USA processes various data like schedule of flights, timings, pricing, the availability, connection, meal preference, special facility, etc..and that too on the basis of neutral display real time on line takes place outside India. The computers at the desk of travel agent in India are merely connected or configured to the extent that it can perform a booking function but are not capable of processing the data of all the*

airlines together at one place. Such function requires huge investment and huge capacity, which is not available to the computers installed at the desk of subscriber in India. The major part of the work or to say a lion's share of such activity, are processed at the host computer in Denver in USA. The activities in India are only minuscule portion. The appellant's computer in Germany is also responsible for all other functions like keeping data of the booking made worldwide and also keeping track of all the airlines/hotels worldwide that have entered into PCA. Though no guidelines are available as to how much should be income reasonably attributable to the operations carried out in India, the same has to be determined on the factual situation prevailing in each case. However, broadly to determine such attribution one has to look into the factors like functions performed, assets used and risk undertaken. On the basis of such analysis of functions performed, assets used and risk shared in two different countries, the income can be attributed. In the present case, we have found that majority of the functions are performed outside India. Even the majority of the assets, i.e., host computer which is having very large capacity which processes information of all the participants is situated outside India. The CRS as a whole is developed and maintained outside India. The risk in this regard entirely rests with the appellant and that is in USA, outside India. However, it is equally important to note that but for the presence of the assessee in India and the configuration and connectivity being provided in India, the income would not have generated. Thus the initial cause of generation of income is in India also. On the basis of above facts we can reasonably attribute 15 per cent of the Revenue accruing to the assessee in respect of bookings made in India as income accruing or arising in India and chargeable under section 5(2) read with section 9(1)(i) of the Act.

17.5.5.4 Thus, CRS in India only performed the functions of generating requests and receiving end results. Main functions like collecting data base of airlines/hotels, processing of this data to find suitable flight/hotel with appropriate pricing was happening outside India. Thus, we do not accept the contention of the Applicant that in Galileo case (supra), the main processing of customer request was being done in India. Quite clearly this was done overseas and results were sent to the computer in India. Even then, this was found to be enough to create PE. What CRS is doing in Galileo case (supra) is the same what is being done by the application software (Master Connect and MasterCard

File) in our case, i.e. sending the request and receiving the result. Like Galileo, the final customer is also in India. The customer swipes a card in India, data flows between two banks in India, and the money too moves in India. Due to these activities income is generated for the Applicant. Thus like Galileo, Revenue generating activity is happening in India. Thus, till this point of time, the facts are quite the same, and relying on Delhi ITAT decisions of Galileo and Amadeus (supra) there is strong case for PE.

17.5.5.5 Further to the above, we are of the view that facts of this case are stronger for the creation of a PE. Once we look at MIPs, we can see that MIPs are performing more than what CRS was doing in India. MIPs, apart from generating signal for transaction processing and receiving end results of transaction processing, are also doing activity relating to facilitation of authorization. It has been discussed earlier that the Applicant itself has admitted in the AAR application as well as in TP report of MISPL that MIPs are used for undertaking preliminary examination/validation of information at the point of authorization. The preliminary validation generally involves activities such as PIN processing, validation of card codes, name and address verification etc.. In the case of errors, the MIPs alert the acquirer bank/financial institution on the need for a correction and the data is not authorized. With these additional activities besides sending and receiving signal (which CRS in India was doing in Galileo case) the case of MasterCard network creating a PE is actually stronger.

17.5.5.6 The Applicant in its written submission post hearing, has also sought to distinguish facts of Galileo and Amadeus (supra) on the basis that in these two cases there was a person feeding entries in India while in our case there is no human intervention. We are of the view that this difference is not material to determination of existence of PE. It has been held that automatic equipment can also create PE and no human intervention is necessary. In this regard we will like

to quote from the Hon’ble Hon’ble Delhi High Court decision in the case of Formula One World Championship Limited (supra) which is reproduced below:

> *“48. In the Swiss Server decision [Case No. II 1224/97 dated 6 September 2001, Finanzgericht of Schleswig-Holstein (Tax Court of First Instance)], D Co –tax resident company of Germany – owned an Internet server installed at a rented place in Switzerland. The company stored programs and dealt with its Swiss client’s files, in the server. The server functioned without involvement of D Co’s employees in Switzerland. A second company, S Co, which was D CO‟s affiliate and a Swiss tax resident, managed the server (i.e. computer programs and information about D Co’s clients in Switzerland). D Co argued before the German tax authorities that its Swiss server amounted to permanent establishment and its income attributable to it was exempt from German tax. The German tax authorities rejected this argument. In D Co’s appeal, the German Tax Court of First Instance held that the server constituted Deco’s fixed place of business and a fixed place permanent establishment in Switzerland. The Court’s view was that, for a fixed place permanent establishment to exist, it was unnecessary that the server had to be operated by human beings (i.e. employees of D Co, a contractor or any other enterprise). The Court pointed out that any equipment could amount to a fixed place permanent establishment even if it functioned fully automatically without human intervention. In so holding the Court also took into account Art. 5(3)(a) of the Germany-Switzerland tax treaty (which was similar to Art. 5(4)(a) of the OECD MC 2010). As per that provision, the term “permanent establishment” did not include facilities used solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise. In that respect, the Court expressed that only the assets that could be „itemized‟ on the enterprise's balance sheet could be regarded as goods and merchandise. Therefore, in the Court's view, Art. 5(3)(a) of the tax treaty did not apply to the server used for storing the information that was supplied by D Co to its customers in Switzerland.”*

Thus, it is clear that even automatic equipment like server can also create PE and there is no requirement of human intervention.

17.5.6 The Applicant has stated that use of MasterCard Connect and MasterCard File express is incidental to the main activity of transaction

processing service and they perform preparatory and auxiliary services. We have already discussed how the role of these two application software is similar to what CRS was doing in Amadeus and Galileo cases in India. Thus, the objection of the Applicant is not valid. In addition, when we talk about MasterCard network, we have to see as a whole whether all the constituents of MasterCard network, i.e. MIP, transmission tower, leased lines, fiber optic cable, nodes, internet, Master Connect and Master Card File express, together, perform activities which can be considered as preparatory or auxiliary. We have already demonstrated that MIP alone does activities which are not preparatory or auxiliary. When combined with transmission tower, leased lines, fiber optic cable, nodes, internet, application software, the scope of activity gets even bigger and cannot be called preparatory or auxiliary.

17.5.7 The Applicant has also claimed that net debit/credit balance calculation of millions of transactions by GCMS and SAM involve high power computers and analysis. We have already discussed that settlement position of two banks for various transactions are already known to them. What Applicant is doing outside India is simple calculation to add all these transactions and deduct the fee charged to arrive at net position. Even otherwise, there is no case that once significant activities are happening outside India; there cannot be a PE in India, even though significant activities are also happening in India. For deciding whether there is PE in India, we need to see what are the functions performed in India in the context of overall functions performed by the Applicant and whether the tests of PE are passed or not.

17.6 In view of above discussion, we hold that MasterCard Network also creates fixed place PE of the Applicant in India.

18. Now let us examine the role of the Bank of India premises, and whether any fixed place PE is formed on its account.

18.1 The Revenue has contended that the Bank of India space where settlement activity takes place through employees of Bank of India creates a fixed place PE. This is for the reason that there is dedicated team in Bank of India to carry out the settlement activity under the direction and on behalf of the Applicant and these employees of Bank of India have space available to them. The Applicant has objected to this claim of Revenue.

18.2 We have already discussed that more than 90% of transaction involve domestic INR settlement for which Bank of India passes necessary entries. The Applicant himself has stated that settlement process is essentially the movement of funds between the issuer bank and the acquirer bank. This task (for more than 90% of settlement) is done by BOI in India on behalf of the Applicant through a dedicated team. As discussed earlier, settlement position transaction wise is captured in India and is already known to respective banks. MCI, on behalf of the Applicant, only compiles that information into a consolidated settlement position, which incidentally is also known to banks in India already. Based on this settlement position the actual debit and credit is done by a dedicated team in BOI. If there is any error it is the Applicant who is responsible. For constituting space at Bank of India as fixed place PE of the Applicant it is necessary that the functions of the Applicant are carried out through that space. There is no doubt that settlement activity is happening in the premises of Bank of India. This settlement activity is the function of the Applicant, carried out by BOI on its behalf and with all responsibility of error on the Applicant. The process of movement of fund between two banks (which is actual settlement) happens only when Bank of India passes the debit and credit entries. The Applicant has also admitted in Annexure III of its application that Domestic INR settlement happens in India

through the settlement bank account of MCI in India. Since, settlement is an important constituent of transaction processing, there is no doubt that this function of the Applicant is being carried out by Bank of India, in India.

18.3 The Bank of India carries out this function on behalf of the Applicant. The Applicant sends the instruction every day regarding which account to debit and which to credit. The dedicated team at Bank of India only has to carry out that instruction on behalf of the Applicant. If there is any error the liability is on the Applicant. These facts are admitted by both the Applicant and Revenue. These facts establish that Bank of India carries out the settlement activity as an agent of the Applicant and under its instruction and responsibility. It is not a principal –to-principal transaction as the liability is always of the Applicant and employees of Bank of India to carry out their work according to the instruction given by the Applicant. Thus the employees of Bank of India carrying out this work are under control and supervision of the Applicant and the space occupied by them in Bank of India is at the disposal of the Applicant. It is true that Bank of India is also carrying out other activities as it is an established bank in India. However, it is well understood that for constituting PE the space may not be exclusively used by the non-resident enterprise. OECD has also agreed to this principle in Note 4 of OECD commentary on Article 5 of Model Tax Convention. Thus we hold that Bank of India premise constitutes fixed place PE of the Applicant.

18.4 The Applicant has contended that job of BOI is clerical and they pay only USD 1500 per month for this job. It is not material whether passing debit and credit entry is clerical or what fees is paid. What matters is that this is a settlement and this activity only triggers the movement of fund between banks which is admitted by the Applicant itself as settlement.

18.4.1 Further, the remuneration cannot determine whether the work carried out by Bank of India is significant or not. This is more so for the reason that Bank of India gets other benefit in the form of floating money from all the banks at its disposal without any interest expense. All banks that use MasterCard have to maintain floating money with Bank of India. This interest free floating money which is at the disposal of Bank of India is sufficient remuneration for Bank of India to carry out the work at low remuneration from MasterCard. Similar example is the case of advance tax payment in India. Banks compete with each other to collect advance tax from taxpayers in India, though they do not get any collection fee from Government of India. This is for the reason that they get to use the floating money in the form of tax collected for some time before remitting it to the Consolidated Fund of India. Thus, the low remuneration from MasterCard to Bank of India would not determine whether the work of settlement carried out by Bank of India is significant or not. The Applicant itself has admitted in its AAR application at Annexure III that settlement is happening in India.

18.5 The Applicant has contended that BOI cannot be taken as agent of the Applicant since it is an independent entity and can provide similar services to other companies as well. It is clarified that BOI is not being treated as dependent agent. It is independent, but is still agent. It has been admitted by the Applicant that BOI works as per the instruction of the Applicant and all the responsibility for the act performed by BOI is on the Applicant. These admitted facts clearly make BOI the agent of the Applicant.

18.6 The Applicant has also contended that premises of BOI are not at the disposal of the Applicant as it does not have access. The employees of the Applicant cannot immediately walk into BOI and occupy some space. Reliance has been placed on Delhi ITAT SB order in case of Motorola (supra). In this case of Motorola, PE was sought to be created through employees of non-resident

enterprise who did not have free access to the premise of the subsidiary in India. In our case, the Revenue is claiming creation of a PE by stating that employees of BOI are doing activities for Applicant and are dedicated to carry out that function and have space available to them in the office for which they have free access. The fact that BOI is acting as an agent of the Applicant and under its instruction and supervision, and has a space at its disposal, it means that the space is at the disposal of the Applicant.

18.6.1 Revenue has cited the Swedish Home case (Page 32 of Taxmann's Law and Practice relating to Permanent Establishment written by Ashish Karundia) in which a Norwegian company hired a Swedish sale person who used to work from his home office and used to receive remuneration for that activity. It was held that home office constitutes a PE of the Norwegian company. The Applicant has tried to distinguish the Swedish home office case by stating that the person here was doing sales activity which was a significant activity. It has been contended that in settlement, significant activity of sorting and collating is done by the Applicant. We have already discussed that significant activity in settlement is movement of fund by passing debit and credit entry which is done by BOI in India and hence the objection of the Applicant is not tenable.

18.6.2 The Applicant has again relied upon UAE Exchange Control case (supra) to argue that the settlement activity carried out by BOI is similar to downloading and dispatch activity performed in that case. We have already dealt with this issue earlier when we discussed preparatory and auxiliary activity. This is to be seen in the context of the overall functions performed by the enterprise. Downloading and dispatching may be auxiliary activity on the facts of one case but not when moving funds between two banks. We have already discussed as to how movement of fund between two banks by passing debit and credit entry is

a major settlement activity and that is performed by BOI. Thus UAE Exchange Control case does not appear to be applicable on the facts of our case.

19. Next is the role played by the Applicant's subsidiary MISPL in India and whether that can constitute a fixed place PE of the Applicant.

19.1 The Revenue has submitted that till Dec 2014, MCI had a liaison office in India, and it (through its overseas AE) owned MIPs which were placed in the premises of the Indian Customers. MCI had entered into licensing agreement with various Indian customers. Employees of Liaison office were found to be performing more than preparatory and auxiliary services. In fact, for ten years prior to Dec 2014, the Applicant disclosed income from transaction processing service rendered in India at full 100% attribution at global net profit rate. From Dec 2014, the Applicant had shut down the Liaison office and had transferred that work to the Indian Subsidiary MISPL. The employees of Liaison office were taken over by the Indian subsidiary and they continued to perform the same functions. Similarly the work of MCI was transferred to the Applicant's Singapore entity. So far as Indian customers (banks/FIs) are concerned there was no effect on their activities. MIPs continued to remain in their premises. There was no new agreement regarding MIPs. The risk regarding MIP continued to be with overseas AE. The authorization, clearance and settlement continue to happen in the same way it used to happen before. There was no new licensing agreement either. Same licensing agreement got unilaterally assigned to the Indian subsidiary. Similarly there was no change in the activities that cardholders were required to do. Thus, everything remained the same on the ground.

19.2 However, the Revenue submits that the income shown in India has undergone a drastic change. Before 1stDec 2014, for 10 Years (A. Yr 2005-06 to 2014-15) MCI in its return of income in India admitted to be carrying on

transaction processing activities and 100% income was attributed to this activity and global net profit rate was applied which was about 50%. But, after restructuring no income is shown in the hands of MCI or the Applicant and only support services are shown to be carried on by MISPL. Thus, the income offered in India has reduced from more than 50% of revenue from India to about 2.5% of revenue from India. This has resulted in suppression of income in India of the tune of 300 to 400 crore every year. Based on this Revenue has contended that this is a colorable device to reduce the tax liability in India. Revenue has also relied upon the decision of Hon'ble Delhi High Court in the case of CIT v. Abhinandan Investment Limited (supra).This decision has considered various judgments like Hon'ble Supreme Court judgments in McDowell, Vodafone International Holdings BV, Azadi Bachao Andolan, Hon'ble Gujarat High Court decision in the case Banyan and Beery, Sakarlal Balabhai, and concluded that it is important to understand the business purpose behind a transaction. If the main purpose is to contrive a loss, then that is to be disallowed. Based on this it has been stated in the Revenue's report that there was no business purpose to restructure the transaction in India other than to reduce tax liability in India.

19.3 To illustrate the above contention, the following details are given for the period prior to 1stDec 2014:

Assessment Year	Income shown in the tax return by the assessee (MCI)	GNOP rate declared by the assessee (MCI)	GNOP rate agreed under MAP
2005-06	5.17 crore	14.64%	18.14%
2006-07	9.17 crore	16.55%	No MAP in this case
2007-08	22.85 crore	22.85%	23.85%
2008-09	34.91 crore	30.76%	30.76%
2009-10	58.62 crore	40.16%	MAP pending
2010-11	83.62 crore	45.82%	MAP Pending

2011-12	105.05 crore	50.47%	No MAP request
2012-13	128.99 crore	52.32%	No MAP request
2013-14	171.16 crore		No MAP request
2014-15	224.24 crore	55.43%	No MAP request

19.4 For the first ten months of AY 15-16 (Till 30 Nov 2014), MCI has filed return of income declaring income of Rs 157.51 crore. However, for the next four months (post 1 Dec 2014) MISPL has filed return of income declaring income of only Rs98.12 lakh. After 1st Dec 2014, MISPL has shown the following income in their return (MCI and the Applicant have shown nil return)

Assessment Year	Total Revenue from India	Income disclosed by MISPL	Income as percentage of Revenue from India
16-17	663.58 crore	12.54 crore	1.89%
17-18	833.25 crore	21.63 crore	2.59%

19.5 Before 1stDec 2014, MasterCard admitted in its tax return (for 10 years) that it is carrying on transaction processing activity in India and 100% of income from India is to be attributed to this activity; all Revenue being from transaction processing activity. On this Global Net Operating Profit Margin of around 50% was applied to arrive at taxable income in India. However, post 1 Dec 2014, with all operations remaining same, MISPL was only shown to be doing support functions and not actual transaction processing functions which LO of MCI was doing earlier. Same activities which were creating a PE for MCI in India and for which full attribution out of transaction processing was done is now shown as only support activities and not actual transaction processing activities. Thus, there are some functions and risk related to transaction processing which were earlier carried out by MCI in India and are still carried out by MISPL(as MISPL

had taken over everything) but not shown in the FAR of the MISPL. Therefore, the subsidiary company MISPL creates a PE of Applicant in India.

19.6 With respect to the Revenue's allegation of colorable device, the Applicant has contended that this issue has already been examined by the AAR at the time of admission of the application. This issue of tax avoidance could have been considered only at the time of admission and cannot be considered now. Reliance was placed on Hon'ble AP High Court decision in the case of Sanofi Pasteur Holding SA (supra) to plead that there is no power to review the decision. It has further provided commercial reasoning as to why the APMEA operations were given to the Applicant. The proposed restructuring plan had approval of the Board and evidences were produced in support. It also submitted that this was also accepted by US IRS. Thus the business restructuring was not done with an intention to avoid tax. It further submitted that pursuant to this decision to effect business reorganization, the workforce of the Applicant was substantially increased by more than three times from about 115 (prior to reorganization) to about 400 approx (after the reorganization). Indian operations just formed 4.54% of total APMEA operation and were carried out after business reorganization of many other countries in that region. Thus it claimed that business reorganization was carried out purely on grounds of business efficiency and commercial expediency. The Applicant relied on SC decision in the case of Vodafone International Holdings B.V. (supra) to support that it is conventional to incorporate a separate company in each country for carrying on the business operations in that country. It also contended that it cannot be treaty shopping exercise as both India-US and India-Singapore DTAA are similar.

19.6.1 With regard to difference in tax liability, pre and post restructuring, it was submitted that the Applicant admitted LO of MCI as PE only under MAP settlement under the DTAA. It submitted that MAP based settlements were made

only in order to obviate protracted litigation with the Indian tax authorities and also because the amounts involved in those years were relatively negligible. Reliance was placed on Hon'ble Supreme Court decision in the case of E*Funds IT Solution Inc (supra)wherein it has been held that, a MAP agreement or settlement is in the nature of a concession made by the Applicant which is not binding on the Applicant for assessment years other than those specifically covered by the MAP settlement. The Applicant in its written submission, filed after hearing, has submitted that in its returns of income, MCI has expressly declared that it has no PE in India. Thus while the Applicant disclosed the income in the return for AYs 2005-06 to 2015-16, it also stated that there is no PE in India and it admitted income on without prejudice basis to buy peace of mind. With respect to non furnishing of information regarding import of MIPs, it has been submitted that the Applicant has never imported any MIPs in India and the group company of MasterCard importing MIPs in India has not maintained any records regarding the custom duty paid while importing MIPs in India, therefore, the Applicant has not been able to produce the requisite custom duty related information on MIPs. Additionally, the Revenue has failed to establish the significance of the information in respect of the questions raised by the Applicant in the application filed before the AAR. For not producing Customer Business Application (CBA) before the Revenue, the Applicant has submitted that this information does not have any relevance to the core issue arising in the application filed before AAR. It was also submitted that Revenue has already obtained it from Syndicate Bank under section 133(6) of the Act.

19.6.2 With respect to the Revenue's claim of Indian subsidiary MISPL constituting fixed place PE of the Applicant in India, the Applicant has submitted that LO of MCI was not a PE as it was doing only preparatory and auxiliary services and the fact of there being PE has not been upheld by any court in India. It has quoted the E*Funds case (supra) to contend that MAP settlement

does not lay down any principle and tax paid prior to Dec 2014 was to buy peace and because the amount involved were not significant. The Applicant has again submitted the commercial reasoning behind restructuring to support that restructuring was not for avoidance of tax. The Applicant has quoted from the reply of various banks that there has been no change in the operation because of restructuring. This does not lead to conclusion that the restructuring was done for avoidance of tax. The Application submitted that the ownership of MIPs is with MISPL. The Applicant has contended that core activities are happening outside India, and that no facilities, personnel, premise of MISPL are at the disposal of the Applicant. The Applicant has submitted that under Article 5(10) of DTAA, subsidiary cannot be regarded as the PE, as held in the case of Morgan Stanley (supra).

19.7 We have gone through both the submissions of the Applicant and the Revenue. With regard to the reasons for restructuring/reorganization, we agree with the Applicant that there were reasons of business efficiency and commercial expediency for the operations to move from USA to Singapore. Board meeting minutes, conversation with US IRS, increase in employee strength, catering to entire APMEA region etc. necessitated such a move. Even otherwise, it is not for the Revenue to decide for the Applicant as to what structure is most suitable to it and where the facilities should be set up. Such business decisions can only be taken by the business itself keeping its business interests in mind, in terms of profitability, efficiency and expediency. Unless a reorganization serves no other purpose except bypassing tax laws, no adverse inference can be drawn by the Revenue. In the instant case we cannot say that the restructuring was a case of tax avoidance or a colourable device to that end.

19.7.1 However, it appears that the main objection of the Revenue is that while LO of MCI was accepted as doing transaction processing activity with

100% income from transaction processing attributed to it, MISPL is shown as doing only support activities, resulting in drastic reduction of income returned in India. The Applicant has responded by saying that MCI never accepted having PE in India and it accepted PE only under MAP. We are not in agreement with this contention. MCI had accepted PE under MAP only for years before AY 2005-06. The Applicant himself has taken support from the case of E*Fund (supra)to say that a MAP agreement is not binding on the AYs other than those covered by the MAP settlement. Hence the Applicant's argument cannot be accepted for the period after AY 2005-06, till 2014. The fact that PE was accepted to buy peace of mind, in our view, will not take away the admitted position in the tax return. The income accepted by MCI in its tax return has legal consequences. If MCI is of the view that there is no PE there should be nil income returned in India. In that case, the assessing authority will look into the PE issue. However, once MCI admits income in its tax return, on account of 100% attribution of profit to India, it means that legally it has accepted carrying out those operations in India through PE. In that situation the assessing authority would not look into this aspect. Thus, MCI having accepted income in India in its tax return cannot at the same time say that it was actually not carrying out these activities.

19.7.2 It is submitted by the Revenue that the assessing officer also has passed an assessment order assessing the income with a finding that there is PE and attributed 100% income from transaction processing activity to that PE, and the same has been accepted by MCI. We would take it that it is carrying on transaction processing activities in India through a PE. The argument that the PE was accepted as the amount was small has also been opposed by the Revenue, as in last four years income disclosed is more than Rs100 crore, whereas there was a reduction of Rs 300 crore due to the change.

19.7.2.1 While we do not hold that there is a colourable device we do notice that the transaction processing activity was earlier shown to be carried out by the office of MCI in India. However, MISPL has only shown these as support services in its FAR. Thus, there are some functions and risks related to transaction processing which were earlier carried out by MCI in India and are still carried out by MISPL(as MISPL had taken over everything) but not shown in the FAR of the MISPL. Therefore, the subsidiary company MISPL creates PE of Applicant in India. The fact that MISPL is carrying on work of the Applicant, to that extent facility, service, personnel and premise of MISPL are at the disposal of the Applicant. This is for the reason that it is through these facility, service, personnel and premise, the Applicant is carrying on transaction processing activity and undertaking risks which are not reflected in the FAR of MISPL.

19.7.3 We will also like to consider that even if we go by Applicant's argument that past returns of MCI should not be relied upon to decide what work was being carried out in India, we will find that there is transaction processing work that is being carried out through MIPs and MasterCard network in India but not reflected in the FAR profile of MISPL. The Indian subsidiary MISPL is only shown to be carrying out support activity in its FAR and it is not carrying out actual transaction processing service which is happening in India through MIPs claimed to be owned by it. Thus, for this transaction processing activity, that is happening in India, and which is not reflected in the FAR of MISPL, subsidiary company MISPL created PE of the Applicant. Thus, the other work of the Applicant is being carried out by the facilities, services, personnel, premises etc. of MISPL which are available to the Applicant Company and constitute its PE.

19.7.4 The Applicant has submitted that under Article 5(10) of DTAA a subsidiary cannot be regarded as the PE. We are of the view that the Article only states that the subsidiary will not automatically become a PE of the foreign

enterprise, and not that it cannot be PE in any situation. In the case of Morgan Stanley (supra)relied upon by the Applicant in this regard, the Indian subsidiary (MSAS) was actually held to be a PE of the non-resident enterprise (MSCo). It was only on profit attribution that it said that if TPO and AO had held the transaction between MSCO and MSAS at arm's length, nothing more is to be attributed. The relevant portion of the ruling reads as under:

> *"32…………………...Under the impugned ruling delivered by the AAR, remuneration to MSAS was justified by a transfer pricing analysis and, therefore, no further income could be attributed to the PE (MSAS). In other words, the said ruling equates an arm's length analysis (ALA) with attribution of profits. It holds that once a transfer pricing analysis is undertaken; there is no further need to attribute profits to a PE. The impugned ruling is correct in principle insofar as an associated enterprise, that also constitutes a PE, has been remunerated on an arm's length basis taking into account all the risk-taking functions of the enterprise. In such cases nothing further would be left to be attributed to the PE. The situation would be different if transfer pricing analysis does not adequately reflect the functions performed and the risks assumed by the enterprise. In such a situation, there would be a need to attribute profits to the PE for those functions/risks that have not been considered. Therefore, in each case the data placed by the taxpayer has to be examined as to whether the transfer pricing analysis placed by the taxpayer is exhaustive of attribution of profits and that would depend on the functional and factual analysis to be undertaken in each case. Lastly, it may be added that taxing corporates on the basis of the concept of Economic Nexus is an important feature of Attributable Profits (profits attributable to the PE)."*

This ruling actually supports the case of MISPL being PE of the Applicant. Since in our case we find that there are functions being carried out by MISPL on behalf of the Applicant, which are not reflected in the FAR profile of MISPL, hence an attribution on this score could be considered by the assessing officer. However, since the valuation or TP issues are not dealt with by the AAR and are beyond its scope, we shall not deal with this issue any further.

19.7.5 The Revenue has also quoted Spanish Roche Vitamins case and Borax case from the book of Ashish Karundia, to support the claim that MISPL constitutes a PE of the Applicant. While the Revenue gave some details on the case, the Applicant in its submission, post hearing, stated that the full text of these cases were not provided and hence it could not respond. We agree that unless the full text is available and the entire context of the case is not examined, we cannot rely upon or respond to, much less give a finding on casual references.

20. We now take up the possibility of creation of a PE through the Applicant's visiting employees and employees of Bank of India.

20.1 The Revenue has contended that the Applicant has a service PE in India as its own employees are visiting India. Further there is service PE through employees of Bank of India as through them service is being rendered. Details of visit of employees of the Applicant to India have been provided which shows that in a year (FY 16-17), the threshold of 90 days of India Singapore treaty is crossed. Revenue has relied upon Bangalore ITAT judgment in the case of ABB FZ LLC (ITA no 1103/2013) and Hon'ble Supreme Court judgment in E*Funds (supra) to plead that a combined reading of these two orders require that service may be provided without physical presence in India and even then service PE could be created. However, Revenue states that even otherwise, a service PE is created since the presence of employees of Applicant in India exceeds 90 days in a year (FY 16-17). The purpose of the visits of employees in India was stated by the Applicant (in its reply dated 17th October 2017) as business meeting with clients. Hence, it creates service PE.

20.1.1 With respect to service PE through Bank of India's employees it has been submitted by the Revenue that for service PE, the service could be

provided through other personnel as well which in this case are the employees of the Bank of India, which is carrying out settlement functions in India on the direction of the Applicant and the responsibility of the work lies with the Applicant. Thus, a part of transaction processing function of the Applicant is being carried out through other personnel (Bank of India) in India and it creates a service PE.

20.2 The Applicant has not accepted the Revenue's above referred contention regarding service PE. It is submitted that the Revenue has not submitted any evidence to support the contention that visiting employees are rendering services to customer banks. It has been pleaded that the Applicant's system and processes are automated and do not require constant interaction with the customers. Hence, it does not have employees in India and do not provide service through them. It has been further submitted that the infrastructure and network is present outside India. Hence, there cannot be a service PE in India. Relying on the case of Morgan Stanley (supra) it is submitted that such activities should be categorized as stewardship in nature. The settlement activity is happening outside India. BOI is an independent entity which is carrying on minimal and clerical work for which it is getting compensation at arm's length.

20.2.1 We have considered the submission of both Revenue and the Applicant.

The India Singapore DTAA under Article 5(6) states that:

> *" 6. An enterprise shall be deemed to have a permanent establishment in a Contracting State if it furnishes services, other than services referred to in paragraphs 4 and 5 of this Article and technical services as defined in Article 12, within a Contracting State through employees or other personnel, but only if :*
>
> *(i) activities of that nature continue within that Contracting State for a period or periods aggregating more than 90 days in any fiscal year; or*

(ii) activities are performed for a related enterprise (within the meaning of Article 9 of this Agreement) for a period or periods aggregating more than 30 days in any fiscal year."

20.2.2 The Revenue states that it is not in dispute that the threshold of 90 days in a fiscal year is met. We only need to see whether the employees of Applicant visiting India are rendering any service. The Applicant, in its rebuttal, has stated that its employees visit India for understanding the future requirement, informing new products and to monitor the efficiency of the operation and not in connection with the signing of the contracts.

20.2.3 First of all, it is important to understand that clients of the Applicant are in India. Thus, relying on the case of E*Funds IT Solutions Inc (supra), the first test for creating service PE is satisfied since service is provided to Indian customers. As discussed earlier, the threshold of 90 days of the DTAA is also satisfied. Thus, we only have to see if the work of understanding the future requirement, informing new products and to monitor the efficiency of the operation, is a part of the transaction processing service. The Revenue states that the actual act of settlement can be facilitated only if employees of Bank of India pass debit and credit entries. Even otherwise, other employees are required to facilitate transaction processing. It is admitted by the Applicant, in its rebuttal, that employees' strength in Singapore increased from 115 (prior to reorganization) to about 400 (after the reorganization). This indicates that there is requirement of human beings to undertake the transaction processing service.

20.2.4 During these proceedings, the Revenue cited the example of Automated Teller Machine (ATM), provided by banks. Customers can get money in cash using a card through an automated machine without going to a bank branch. But that does not mean that there are no humans associated with this

rendering service. Even if the main task of disbursing cash is done by an automatic machine, there are human beings who are needed to facilitate that service, such as the guard, the person who checks the functioning of ATM, the person who puts cash in the box and tallies the withdrawal etc. Same is the situation in this case. Even if a part of the process is automated, employees are needed to check if the process is working alright; to interact with clients, to meet clients and take feedback etc..These are part of the service rendered to clients and are not steward activities. In our view these are part of service that Applicant renders to clients in India. Taking feedback is also part of service provider activity as it improves services to the customer. When employees visit India to inform clients about new products, this is also part of service that would be provided by the Applicant to these clients. In the context of transaction processing service that the Applicant is providing, this is an integral part of the Applicant's profession to provide new avenues of service to clients. Thus, we are of the view that the employees of the Applicant visiting India are providing services to Indian clients and hence, once they cross the threshold of 90 days in a year, a service PE is created.

20.2.5 The Applicant has relied upon the judgment in the case of Morgan Stanley (supra) to plead that stewardship activities cannot create service PE. The facts of the case are different here. In the Morgan Stanley case, the Indian subsidiary was providing service to foreign parent and the employees of foreign parent were visiting India to check if services are meeting the requirements that it had set. It is in this context, the activities were called stewardship activities. Here it is not a case where visiting employees are checking the service provided by MISPL to see if it meets their requirement. They are meeting clients in India to whom they are rendering service. They are talking about the possibility of improving and adding services. This is not stewardship activity as held by

Hon'ble Supreme Court in Morgan Stanley. This is part of the main functions that are to be performed by any organization for rendering service to its clients.

20.3 The Revenue has also argued that the employees of Bank of India are rendering service of domestic INR settlement in India on behalf of the Applicant, and hence they also constitute a service PE. They come under the category of "other personnel" and work for 365 days in a year. Hence, the Applicant is carrying out its activities through the employees of Bank of India who are assigned to carry out the activity of MasterCard. We are not in agreement with this view, as this stretches the argument much beyond what is contemplated in the DTAA. The employees of the bank are neither employees of the Applicant nor are they other personnel engaged by the Applicant to render its services. As employees of the bank they render services to the bank in lieu of the salaries they receive from the bank. As bank employees they are rendering services on behalf of the bank to the Applicant. Thus the Revenue has incorrectly understood the role of the bank employees in coming to the conclusion that these bank employees working in the bank premises for the settlement function also constitute a service PE of the Applicant in India. Disagreeing with the Revenue, we hold that the employees of the Bank of India, in India, do not constitute a service PE of the Applicant in India.

21. The Revenue has also claimed that MISPL is legally and economically dependent on the Applicant, being 100% subsidiary, and is a dependent agent PE of the Applicant. It gets instructions from and caters only to the Applicant, and has no business other than related party business, and it is compensated through cost plus remuneration model with no risk being undertaken. The Revenue has quoted from the replies received from various banks (obtained under section 133(6) of the Income-tax Act) about their dealing with employees of the Indian company. The Revenue has also claimed that Indian subsidiary is

securing orders for the Applicant. The India Singapore treaty has a clause for securing orders also. It has been claimed that the Indian subsidiary is securing orders from Indian clients and that creates a dependent agent PE even though the terms of the contracts are finalized by the Applicant.

21.1 The Applicant has opposed the above view of the Revenue. It is contended that merely because MISPL is rendering Marketing support service does not mean that it is dependent agent PE. The Applicant has relied upon the replies received from Yes Bank, Central Bank and South Bank who have stated that they are not aware of the role played by MISPL at the time of contract renewal. The Applicant has also relied on the statements of First Rand Bank, Canara Bank and Andhra Bank to contend that they have categorically said that MISPL is not involved. It is submitted that MISPL was not even incorporated when agreement with Andhra Bank was signed in 2013. The Applicant states that MISPL provides the proposals to the Indian banks that are prepared, validated and approved by the Applicant. The proposals contain the rates at which the Applicant proposes to provide services to the customer banks. In case the customer does not agree with the proposed terms and makes a counter proposal, the same is uploaded on the portal of the Applicant outside India by the employees of MISPL. Thereafter, it is completely up to the Applicant operating from outside India to accept the counter proposal of the customer or reject the same. For the new customers there is constant interaction between the Applicant and MISPL. Employees of MISPL act for an on behalf of MISPL and are in no way control or managed by the Applicant. The Applicant also submitted that MCI had already entered into contracts with most of the banks prior to the takeover of the Indian leg of the business by the Applicant in 2014. Accordingly, the process of negotiation, concluding and securing contracts had already been completed during the period when MCI was in operation. In the last three years new agreements have been entered into only with 7 new banks (Tamilnadu

Mercantile Bank, Bandhan Bank, Lakshmi Vilas Bank, Airtel Payment Bank, Kerala Gramin Bank, Oriental Bank of Commerce and IDFC Bank) from whom no reply has been obtained by the Revenue under section 133(6) of the Act. Thus, it cannot be said that the activity is being habitually done by the Applicant. The case of Nortel Networks India International Inc (386 ITR 353) has been cited where it has been explained by the Hon'ble High Court that concluding contracts is not the only criteria for constituting the dependent agent PE and such contracts should be concluded habitually. The Applicant has also relied on Note 33.1 of OECD commentary on Article 5 of the Model Tax Convention in support.

21.2 Let us first see what Article 5(8) of India Singapore DTAA says:

> *"8, Notwithstanding the provisions of paragraphs 1 and 2, where a person - other than an agent of an independent status to whom paragraph 9 applies - is acting in a Contracting State on behalf of an enterprise of the other Contracting State that enterprise shall be deemed to have a permanent establishment in the first-mentioned State, if—*
>
> *(a) he has and habitually exercises in that State an authority to conclude contracts on behalf of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise;*
>
> *(b) he has no such authority, but habitually maintains in the first-mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise; or*
>
> *(c) he habitually secures orders in the first-mentioned State, wholly or almost wholly for the enterprise itself or for the enterprise and other enterprises controlling, controlled by, or subject to the same common control, as that enterprise.*

21.2.1 Clauses (a) and (c) may of relevance to us. Clause (a) talks about an agent habitually concluding contracts, on behalf of the non-resident enterprise. We agree with the Applicant that Revenue has produced no evidence to invoke this clause. The replies received from the banks in response to the information called for by the Revenue under section 133(6) of the Act, and

discussed by the Applicant, clearly suggest that MISPL is not habitually concluding contracts. Almost all the banks have denied MISPL's role in this regard or have expressed lack of any information on the same. We do not have before us any evidence placed on record by the Revenue that even indicates that MISPL habitually concludes contracts on behalf of the Applicant.

21.2.2 With respect to clause (c), the requirement is that MISPL should habitually secure orders in India wholly or almost wholly for the Applicant. It is not in dispute that MISPL works only for the Applicant. Although it was envisaged that MISPL would also be rendering services to third parties but it has been accepted that as of now there is no service to third parties. We also agree with Revenue that MISPL is legally and economically dependent on the Applicant, being a 100% subsidiary of the Applicant. It gets its instructions and remuneration from the Applicant.

21.2.2.1 Regarding habitually securing orders, the Applicant has given the process of how agreements are concluded with the banks. MISPL provides the proposals to the Indian banks that are prepared, validated and approved by the Applicant. The proposals contain the rates at which the Applicant proposes to provide services to the customer banks. In case the customer does not agree with the proposed terms and makes a counter proposal, the same is uploaded on the portal of the Applicant outside India by the employees of MISPL. Thereafter, it is completely up to the Applicant operating from outside India to accept the counter proposal of the customer or reject the same. For the new customers there is constant interaction between the Applicant and MISPL. This process clearly establishes that orders or agreements are routed through MISPL though the finalization of the contract is by the Applicant in Singapore. To illustrate, if MISPL takes the proposal, vetted by the Applicant, to the customer bank and the bank accepts that proposal, immediately an order is placed to the Applicant

through MISPL. In some cases, this may happen after a few rounds of proposals and counter proposals. Though the proposals and counter proposals would be vetted by the Applicant in Singapore, it would ultimately get accepted by the customer banks in India when MISPL brings that proposal or counter proposal to it.

21.2.2.2 In our view, the above position may not satisfy the requirement of "concluding contract" but it certainly satisfies the requirement of "securing order". We have taken support from Delhi ITAT and Hon'ble Delhi High Court judgment in the case of Rolls Royce Plc v DIT [(2008) 19 SOT 42 (ITAT Delhi) affirmed by Hon'ble Delhi High Court(2011) 339 ITR 147 (Del)] to arrive at this conclusion. This case is useful since the provisions of agency PE on account of "securing order" in India Singapore DTAA are the same as in India UK DTAA. In this case of India UK DTAA, Rolls Royce Plc supplied aero engines and spare parts to Indian customers though the support services were provided through a UK incorporated subsidiary having an office in India. The UK incorporated subsidiary provided services such as procuring orders, organization of events and conferences in India, media relations and administrative support. The UK incorporated subsidiary being a dependent agent was not disputed by the taxpayer. The ITAT, Delhi observed that the UK incorporated subsidiary habitually secures orders in India for the taxpayer, and as a practice no customer in India sends its order directly to the taxpayer. They are required to be routed only through the subsidiary. Accordingly, it was held that an Agency PE is created. In our case, there are very few orders.

21.2.2.3 The case before us is not a case where there are several orders. There would be only a few agreements with new banks during the year and some renewals. The Applicant itself has accepted that since 1 Dec 2014, there have been only seven new agreements with Tamilnadu Mercantile Bank, Bandhan

Bank, Lakshmi Vilas Bank, Airtel Payment Bank, Kerala Gramin Bank, Oriental Bank of Commerce and IDFC Bank. From the narration given by the Applicant, it is clear that the proposal for these agreements, though finalized by the Applicant, are taken to the banks by MISPL before it gets accepted by the banks. Thus, all agreements are routed through MISPL. Hence, MISPL secures orders on behalf of the Applicant.

21.2.3 The other issue is whether the requirement of "habitual" is satisfied. The Applicant has quoted from Note 33.1 of OECD commentary on Article 5 of model tax convention which reads as under:

> *" The requirement that an agent must " habitually" exercise an authority to conclude contracts reflects the underlying principle in Article 5 that the presence which an enterprise maintains in a Contracting State should be more than merely transitory if the enterprise is to be regarded as maintaining a permanent establishment, and thus a taxable presence, in that state. The extent and frequency of activity necessary to conclude that the agent is "habitually exercising" contracting authority will depend on the nature of the contracts and the business of the principal. It is not possible to law down a precise frequency test."*

21.2.3.1 It may be clarified that above comments in OECD commentary are with respect to "authority to conclude contract", since OECD Model Article does not have provision of "securing of order" in the Article concerning dependent agent PE. However, since both "authority to conclude contract" and "securing order" use the term "habitually", the commentary is equally applicable to "securing order" as well. Thus, it is acknowledged that the term "habitually" is to be interpreted in the context of business of the Applicant. When the business is trading and there are hundreds of orders, the term will have a different meaning from that as in our case, where there are only 7 new agreements in three years, as we mentioned in the para above. In our case, if the above process is followed

in all the new agreements, even though only 2 or three new contracts are entered into in a year, the requirement of "habitually" would be satisfied. Thus, we have no hesitation in holding that MISPL constitutes a dependent agent PE under Article 5(8) of India Singapore DTAA on account of habitually securing orders wholly for the Applicant.

22. The other possible PE could be on account of the employees taken on deputation. However, the Revenue has submitted that it has not examined the aspect of employees of the Applicant on deputation to MISPL since the Applicant vide reply dated 20th Nov 2017 has submitted that no employee was ever deputed to MISPL. Under these circumstances the Revenue did not press the point of a PE being created due to deputation of employees to Indian subsidiary. Revenue has pleaded that if new facts emerge later, the department would like to examine afresh on this issue as to whether it creates PE. Since the Applicant has categorically stated that none of its employee has ever been deputed to MISPL, we would like to consider that there is no PE on this account at present, unless subsequent facts are suggestive of a different picture. In that case, of course, this Ruling on this issue would become inapplicable.

23. We now come to question number 3, ie. whether, the fees to be received by the Applicant from Indian Customers, such as transaction processing fees, assessment fees and transaction related miscellaneous fees, would be chargeable to tax in India as royalty or fee for technical services ("FTS") within the meaning of the term in Article 12 of the India- Singapore DTAA.

23.1 The Revenue has relied on Hon'ble Delhi High Court judgment in the case of Formula One World Championship Limited (FOWC), (supra), though in that case it was held that use of brand/trademark was incidental. However, Revenue

has shown how the facts of this case are different from FOWC and how on the facts of this case it is a case of royalty. The Revenue has also quoted from license agreement between MCI and banks in India (which was later assigned to the Applicant) in which MCI has granted the banks, licensee right to use various trademarks and marks (IP) owned by it solely in connection with License's payment card programs. The Revenue has also produced the extract from billing manual issued by Applicant to show that part of the fee in the billing manual is on account of use of license. The Revenue has made a submission as to how brand/logo/trademark is not needed for transaction processing and that transaction processing activity is done by the Applicant and for that it does not have to license the IP to the banks (service recipient). The IP is licensed to banks to attract the users to buy MasterCard as it provides reliable, safe and secured system and credible and efficient network. Thus, licensing of IP is not incidental to transaction processing service. The Revenue has also given details as to how huge expenditure is incurred on advertising MasterCard brands in India. The Revenue has also produced an agreement between the Applicant and MCI to show that the Applicant is paying royalty to MCI in the US (the actual owner of brand, logo, trade name, trademark, patent etc.) for use of intangibles in Asia Pacific. The Indian part of the royalty pertains to use of intangibles in India. The Revenue has pointed out the reply of the Applicant that this payment of royalty is for right to carry on business in India, but no agreement has been produced to support that contention. The agreement produced clearly states that the royalty paid by the Applicant to MCI is for use of IP in India. Hence, a part of the fee collected by the Applicant from Indian clients is also for use of IP in India.

23.1.1 The Revenue has also produced a list of patents for transaction processing technology which are registered in India in the name of MCI, and MCI has granted a license to the Applicant for using such patents. The Revenue has also relied on the decision of Bangalore ITAT in the case of Google India Private

Limited (supra) to support its contention that licensing of trademark was the main activity and was not incidental.

23.2 With respect to the Revenue's claim of use of brand name, trademarks and marks, logo, patent etc. to constitute royalty, the Applicant has contended that all banks in their reply have submitted that the fees are for transaction processing service and not royalty. It is further contended by the Applicant that customer banks are not concerned with the machinery, equipment and the intangibles that are used for rendering transaction processing services. The banks only want their transactions to get authorized, cleared and settled in an efficient manner. They pay for the services and not for the intangibles. The Applicant has of course been contending that no portion of settlement functions happen in India. The Applicant has relied on Hon'ble Delhi High Court judgment in the case of Formula One World Championship Limited (supra) to support its case that use of brand name, logo etc. is only incidental. The Applicant has further contended that service charges are based with reference to the value and volume of transactions which are processed and hence it cannot be for use of brand name, logo etc.. The Applicant has also contended that it is not at all necessary that the Acquirer Bank should be a bank which has issued MasterCard cards bearing MasterCard logo. It could be a bank which has not issued any credit or debit cards or it would be a bank which has issued non MasterCard cards. Even then he has to pay fees to MasterCard. This shows that the fee is for the services and not for royalty.

23.3 We have considered the arguments of both the Applicant as well as the Revenue. We have also noted that all banks in their reply to Revenue under section 133(6) of the Act have admitted that the payment made by them to the Applicant is for services and not for royalty. However, we need to go by the actual nature of the transaction and not by how it is classified by the Applicant or by the customer banks. Since the Applicant has classified its activities as a

service and has entered into agreement with the customer banks accordingly, it is obvious that customer banks would also understand it as a service. There are many decisions where the courts have gone by the real nature of the transaction and not by how it has been classified. In Google India Private Limited (supra),the ITAT has held the payments referred to in that case, as royalty, though the same were classified as service. Similarly in Godaddy.com LLC (ITA no 1878/Del/2017) the ITAT Delhi classified the payment as royalty even though the assessee had classified it as service.

23.4 To decide whether a payment is royalty or service, there are certain tests which have been laid down by Hon'ble Delhi High Court in the case of Formula One World championship Limited (FOWC)(supra). Incidentally, both the Applicant and the Revenue have relied upon this judgment. Although the Hon'ble Delhi High Court decided that on facts the payment is not royalty, the Revenue has relied on this judgment since it is of the view that if we examine the five reasons for which Hon'ble Delhi High Court decided in favour of the assessee, and apply these five reasons to the facts of our case, the payment would be classified as royalty in our case.

23.4.1 In brief, FOWC entered into a Race Promotion Contract (RPC) with Jaypee Sports through which it granted Jaypee sports the right to host, stage and promote the Formula One Grand Prix of India event for a consideration of USD 40 million. An Artworks License Agreement (ALA) was also entered into the same day through which Jaypee was permitted the use of certain marks and intellectual property belonging to FOWC, for a consideration of USD 1. One of the questions before AAR was if the payment of USD 40 million is also for the use of marks and IP and hence royalty. AAR concluded that it was royalty. However, in appeal Hon'ble Delhi High Court held that the payment is not royalty as the use of logo, trademark etc. is only incidental. With this background, let us

examine the reasoning of Hon'ble Delhi High Court in FOWC and examine whether it applies to the facts of our case.

23.4.1.1 The Hon'ble Delhi High Court had relied upon the Note 10.1 of OECD commentary on Article 12 of the Model Convention. According to this Note, payments solely made in consideration for obtaining the exclusive distribution rights of a product or service in a given territory are not royalty, since the resident distributor does not pay for the right to use the trade name or trade mark under which the products are sold but merely obtains the exclusive right to sell in his state of residence, the product that he is agreeing to buy from the manufacturer; such payments will be characterized as business income. This Note is not applicable on the facts of our case. In our case there is no distribution right for any product or service involved. What the banks/FIs want to do is to issue their own cards and on that they want to use the logo/trade mark and other marks owned by Master Card. They do not obtain distribution right for the cards as the cards are not owned by the Applicant. They are owned by the Banks/FIs. Banks/FIs do not make payment for obtaining such distribution rights of cards and hence it cannot be said that payment is for getting distribution rights, and the use of intangibles is incidental.

23.4.1.2 Hon'ble Delhi High Court held that the ALA did not confer any additional rights, neither a license nor any form of right to use the trademark given to Jaypee by FOWC which resulted in royalty payment within the meaning of Article 13 of the DTAA. The ALA stated that FOWC wished to grant a license to Jaypee permitting only the incidental use of certain IP rights and artwork "solely for the limited purpose of facilitating the hosting, staging and promotion of the event". FOWC under the RPC, made available to Jaypee all of the elements which constitute the event. In particular, this includes nominating (to FIA) the promoter's event for inclusion in the official F1 racing calendar; after such

inclusion the F1 racing teams with their F1 cars and drivers were bound to participate in Jaypee's event held at the Promoter's racing circuit, strictly in conformity with the requirements of the F1 Sporting and Technical Regulations and the FIA Sporting Code. Therefore, it was held that the grant of F1 rights by the FOWC to Jaypee is merely incidental to the hosting and staging of the event by Jaypee. Unlike RPC and ALA in FOWC, there is no indication in our case that license is granted as incidental to some other rights.

23.4.1.3 At this point we may refer to the MasterCard Electronic License Agreement between MCI (AE of the Applicant) and the Indian customer banks (who pay fees to the Applicant), which were later assigned to the Applicant, and here we find an important clause:

> *"2. Grant of License. MCI grants to Licensee, and Licensee accepts (as granted), a non-exclusive license to use the Marks now identified in Schedule A of this License Agreement solely in connection with Licensee's payment card programs in the geographic area(s) and to the extent indicated in Schedule A; presided that such uses and such programs comply with the quality assurance and other standards set forth in the rules, procedures, policies, bulletins, memoranda, actions of the board of directors, and other directives adopted, modified, supplemented, changed or rescinded, from time to time in connection with such Marks (each, a "Rule"). Upon application by Licensee, and approval by MCI, MCI may, from time to time, amend Schedule A by adding new trademarks/service marks or by modification of existing Marks, in which event, such added or modified trademark/service marks shall be included in the defined term Marks for purposes of this License Agreement. Licensee may use a particular Mark only in the manner authorized in Schedule A and only after the date indicated on Schedule A for such Mark."*

From this it can be seen that MCI has granted Licensee right to use various trademarks and marks owned by it, solely in connection with License's payment card programs. Thus, it is clear that the dominant purpose of the agreement is to allow use of intangibles for the payment card programs of licensees, ie. of the banks and FIs. There is no mention of any transaction

processing service in this agreement or any other agreement. From nowhere in the License agreement can it be inferred that the licensing of the trademark was not the main purpose and was only incidental to allow use of trade mark for transaction processing. In fact for transaction processing rendered by the Applicant, it does not need to license its brand/trademark of Master Card to Banks who are service seekers and not service provider. One could understand owners of goods or services licensing their brands to distributors since the distributors would be distributing their goods and services. There seems no justification for the Applicant to license its trademarks/logo etc. to customer banks in India who are receiving services and not providing services. The brand/trade mark is needed by the Banks/FIs for attracting people to buy their cards and not for transaction processing. Thus, brand/trademark of Master Card is needed for selling activity of the Banks and not for transaction processing activities. There is a certain reliability and trust associated with MasterCard brand name and network which attracts people to buy these cards. This is also evident from the agreement when it says that MCI has granted Licensee right to use various trademarks and marks owned by it, solely in connection with License's payment card programs. This fact is also admitted by the Applicant in its application before us, where it has submitted that:

> *"the MasterCard network is important for Customers on account of its reliability and broad reach. The network allows the Customers to provide their cardholders and merchants access to a safe and secured transaction processing system. Accordingly, the Applicant will enable its Customers to enhance their businesses by providing a credible and efficient network."*

Thus, we are of the view that unlike in the case of FOWC, in MasterCard License Agreement, granting of license of trademarks/marks is the main purpose. MCI has granted Licensee right to use various trademarks and marks owned by it solely in connection with License's payment card programs. The payment card

programs are programs of Licensee (i.e. of Banks and FIs) and not of MasterCard.

23.4.1.4 It was also noted by the Hon'ble Delhi High Court in the FOWC case that there are strong indications that the parties did not intend, through the RPC and the ALA, to license the trademark. They most certainly are not for the use of trademarks or IP rights, but rather for the grant of the privilege of staging, hosting and promoting the Event at the promoter's racing circuit in Noida(NCR). This is a finding of facts. It was also observed that Jaypee's permitted use, as it were, was for a limited duration and of an extremely restricted manner; as event promoter and the host Jaypee had to publicize the F1 Grand Prix Championship. Therefore, it was bound to use the F1 marks, logos and devices.

23.4.1.5 Unlike RPC and ALA in FOWC, there is clear indication in our case that the parties intend to license the trademark. In fact the agreement between the Applicant and customer banks is quite clear that the dominant purpose is to license the trademark/mark. The Agreement has no reference to transaction processing. Further, unlike FOWC, the use of trademark/mark is not for a limited period and also not for use in a restricted manner.

23.4.2 We have also perused the licensing agreement between the Applicant and MCI US, who is the real owner of the Intellectual Property (IP). Under this agreement, the Applicant is paying royalty to MCI for use of IP in various countries, including India. This is discussed in detail in the subsequent part of this ruling. This licensing agreement and payment of royalty for use of IPs in India further establishes that a part of payment made by the customer banks in India to the Applicant is for use of these IPs.

23.4.2.1 The Hon'ble Delhi High Court relied on the Ericsson case (343 ITR 470) and did not hold the payment as royalty since it was a lump sum payment and was not a payment, which is based on either the number of tickets sold or the total amount of Revenue earned by Jaypee in each of the said years or indeed on any other measure. It was held that the definition in the Income-tax Act specifically covers and includes lump-sum payments, whereas Article 13(3) of the DTAA only refers to payments.

However, in our case the facts are different. There is no lumpsum payment in our case. The payment is mainly based on the amount transacted through cards of the participating banks/FIs, in addition to some one-time fee. Thus the finding in Ericson case based on lumpsum payment is not applicable in this case.

23.4.2.2 The Hon'ble Delhi High Court also relied on the judgment in the case of Sheraton International Inc (313 ITR 276)in which it pointedly observed that there was no evidence brought on record by the Revenue to enable them to hold that the agreement was a colourable device, in particular, that the payments received were for use of trade mark, brand name and stylized mark "S". In our case, the Revenue has made out a case that the payment of transaction processing is actually for the use of trademark/mark/logo disguised as part of payment for transaction processing fee, and hence our case is different. We also find that the main activity in Sheraton case was provision of hotel rooms and use of trademark was incidental to that. Hence the facts are different in the two cases.

23.4.3 Thus, we do find that the facts of FOWC case are different from the facts of our case and the judgment of Hon'ble Delhi High Court is not applicable on the facts of our case. In fact, in our case the licensing of trademark/mark/logo etc. (IP) is the dominant purpose as can be seen from the license agreement

between MCI US (the actual owner of these IPs) and the Applicant, which is actually for licensing of intangibles referred to as intellectual property (IP) in the agreement. This agreement was submitted by the Applicant to the Revenue and was also produced before us. Some of the relevant clauses of this agreement are:

> *"WHEREAS, LICENSOR owns the entire right, title and interest in and to certain Intellectual Property (as defined in Section 1.3 below) relating to the design, development, marketing, distribution and license of global payment solutions;*
>
> *WHEREAS, LICENSEE is a wholly owned indirect subsidiary of LICENSOR; and*
>
> *WHEREAS, LICENSEE desires to acquire, and LICENSOR desires to grant to LICENSEE, certain rights to use and sublicense the Intellectual Property in conjunction with the promotion, performance and sublicensing of the Services.*
>
> *1.3 "Intellectual mean and include any and all inventions, Patents (as defined in Section 1.11), works of authorship, copyrights, Mark (as defined in Section 1.4), trade secrets, computer programs (in source code and object code form), flow charts, formulae, enhancements, updates, modifications, translation adaptations, information, specifications, designs, process technology, manufacturing requirements, quality control standards, information and supply chain information systems, Confidential Information, know-how and any other intellectual and industrial property rights intangible property rights, and proprietary acquired by LICENSOR prior to or after the Effective Date, and any and all additions, modifications, improvements, enhancements, updates, renewals, extensions, derivative works, formulations or further developments thereto, which pertain to the development, testing, installation, implementation, customization, optimization, configuration, operation, support, promotion, marketing, advertising, sale or other use of the Services.*
>
> *1.4 "Marks" shall mean and include those trademarks, service marks, trade names, trade dress, domain names, logos and trading styles, whether registered or unregistered, that are owned or licensed by LICENSOR on or after the Effective Date, and used in connection with any or all other Services, including, but not limited to the marks set forth on Schedule A, which may be amended from time to time.*

1.10 "Net Revenues" shall mean and include total gross Revenues, as determined under U.S. Generally Accepted Accounting Principles, derived from licenses (including assessments, fees and other Revenue) and sales of Processing Services in the Territory, less any rebates and incentives, credits, discounts, allowances, returns and refunds with respect to such Revenues and excluding any value-added tax ("VAT"), goods and services tax ("GST"), consumption tax or similar taxes applied to such Revenues.

1.11 "Patents" shall mean and include all patents, patent applications, and patent disclosures (including all related divisions, continuations, continuing prosecution applications, continuations in part, reissues, renewals, reexaminations, and extensions thereof), as set forth on Schedule C, which may be amended from time to time.

1.13 "Processing Services" shall mean and include the transaction processing services that facilitate payments between Cardholders and Merchants.

1.14 "Territory" shall mean and include all of the geographic areas that constitute the Asia Pacific and Middle East and Africa regions under the MasterCard Bylaws and Rules, as may be modified from time-to-time. A list of the countries in the Territory are attached hereto as Schedule E, which may be amended from time to time.

2 Grant of License; Assignment of MLAs; Ownership Rights Reserved.

2.1 Grant of License. Subject to the terms and conditions set forth in this Agreement, LICENSOR hereby grants to LICENSEE a non-exclusive license, with the right to grant sublicenses, to use the Intellectual Property in the Territory solely in connection with the promotion and sale of the Services (the "License").

2.2 Sublicensing Rights. LICENSOR hereby grants to LICENSEE the right to grant sublicenses of the rights granted in the License solely to Member Banks and MCI Affiliates. LICENSEE shall be responsible for enforcing the terms and conditions in the MLAs and shall provide regular reports to LICENSOR on the Member Banks' compliance with the MLAs and the MCI Affiliates' compliance the MCI Affiliate License Agreements.

2.3 Assignment of MLAs. LICENSOR hereby assigns to LICENSEE all of its rights and obligations under the MLAs, and LICENSEE hereby accepts such assignment and assumes such obligations. LICENSOR shall give notice of

this assignment to the other parties to the MLAs and direct those parties to remit payments under the MLAs to LICENSEE.

4.1 Quality of Services. LICENSEE agrees that in its conduct of business Services and the Intellectual Property, LICENSEE shall observe and art s: standards LICENSOR issues from time to time. LICENSEE further agrees that it shall use the Intellectual Property only in conjunction with Services that are of high quality and that it will preserve the goodwill and outstanding reputation associated with the Intellectual Property. LICENSEE agrees that if LICENSOR determines that aspects of the quality services offered by LICENSEE under a Mark are not of an acceptable level of quality, or that any promotion of the Services published by LICENSEE reflects use of a Mark, image or other material likely to injure the goodwill or good reputation associated with the Marks or Services, LICENSEE will comply with reasonable requests and guidelines set by LICENSOR to rehabilitate and/or improve the quality of Services and/or modify the promotion of the Services.

4.5 LICENSOR's Right of Inspection. LICENSEE agrees that LICENSOR or LICENSOR's representative shall have the right, upon reasonable notice and during normal business hours, to inspect the operations of LICENSEE in connection with the Intellectual Property to confirm that the Services offered by LICENSEE under the Intellectual Property are of a quality adequate to preserve the goodwill and good reputation associated with the Marks, Services and LICENSOR. LICENSOR—shall be responsibilities for all costs associated with such inspections unless otherwise agreed to by the parties.

5.1 Royalties- In consideration for the rights and licenses granted to LICENSEE by LICENSOR under this Agreement, LICENSEE shall pay to LICENSOR royalties equal to a percentage of LICENSEE's Net Revenues, as specified in Schedule D attached hereto.

23.4.3.1 Hence, through this License agreement, MCI US has granted to the Applicant a non exclusive license, with the right to grant sublicenses, to use the Intellectual Property in the Territory (India in our case) solely in connection with the promotion and sale of services. And for these rights and licenses granted by MCI US to the Applicant, the Applicant is paying royalty to MCI US.

23.4.4 Intellectual property is defined in para1.3 of the above agreement and what constitute marks and patents are defined in paras 1.4 and 1.11 above. Intellectual property includes trade mark, service mark, trade name, logo, patents, inventions, computer programs, copyright, trade secrets, process technology etc. Quite clearly the royalty paid by Applicant to MCI US (in INR) is for the use of intellectual property in India for and in connection with the promotion and sale of services. Intellectual property in the form of brand, logo, patents, marks etc. are almost always used for promotion and sale of goods or services, and in this case the agreement clearly establishes that royalty paid is for use of these intangibles in India. The Applicant has further licensed these IPs to banks so that banks can use them for selling their cards which in turn would increase the transaction processing activity of the Applicant. By using these IPs, banks/FIs were issuing cards to its customers. These customers of banks/FIs see the MasterCard logo, marks etc. and buy these cads for the trust, brand name and reliability associated with such logo, marks etc.. This in turn helps Master Card to increase the transactions on its network and hence more Revenue from Banks/FIs. Thus, the agreement is clearly for use of IP in Asia Pacific region including in India.

23.4.4.1 The Applicant submitted that the royalty payment made by it to MCI US is for the right to carry on business, and licensing of IP is only incidental. We do not agree with this contention. There is nothing in the licensing agreement which says that the royalty paid by Applicant to MCI US is for the right to carry on the business. The agreement clearly says that royalty paid by the Applicant to MCI is for use of intellectual property, which has been licensed by MCI US to Applicant, and also for the right given to the Applicant allowing it to further sub-license these intellectual properties to member banks in various countries, including in India. The Applicant has not produced before us any agreement

which says that the royalty paid by the Applicant to MCI US is for the right to carry on business.

23.4.4.2 In view of the above, a question arises as to whether if the Applicant is paying royalty to MCI US for use of intangibles and these intangibles are used in India by the banks, then the fees that the Applicant is charging from the customers (member banks/FIs) in India would be nothing but consideration for use of these intangibles in India. We see a direct nexus. There cannot be a situation where the Applicant is based in Singapore and paying royalty to its US parent company for use of intangibles in India but it does not receive that royalty back from Indian banks to whom these intangibles have been further licensed for use. The clauses of the above referred Agreement were brought out by the Revenue in its report, but have not been rebutted by the Applicant in its submissions or during the course of the hearing in this case.

23.4.4.3 In its written submission, post hearing, the Applicant has only submitted that this agreement is of no relevance or consequence whatsoever to the present case, for the simple reason that MCI is not rendering any transaction processing services or any other services to the Applicant. The objection of the Applicant does not address the real issue. The Applicant has not disputed that it is paying royalty to MCI for use of IPs in India. Whether MCI is rendering transaction processing service or not does not matter. What matters is that these IPs for which the Applicant is paying royalty to MCI, is further sublicensed by the Applicant to various Banks and are used by these banks in India for selling their cards. Thus, the payment received by the Applicant represents consideration for use of the IPs in India and hence is to be classified as royalty.

23.4.4.4 The Applicant has further submitted in its written submission filed post hearing that, in the MLA entered into between the Applicant and its

customers in India, a license or permission to use the said trademark/logos has been given not separately/independently, but only as an inseparable part of the package of services rendered by the Applicant to its Indian customers. In other words, there is no grant of any license to use the trademark/logos independently from the card transaction processing services availed of by the said customers from the Applicant. We have already discussed this issue earlier when we discussed that the license agreement between the Applicant and customer banks (earlier between MCI and customer banks which got assigned to the Applicant post restructuring) clearly states that banks are allowed to use these trademarks/logos solely in connection with bank's payment card programs. Thus it is clear that the dominant purpose of the agreement is to allow use of intangibles for the payment card programs of banks and FIs. There is no mention of any transaction processing service in this agreement or any other agreement. From nowhere in this License agreement can it be inferred that the licensing of the trademark was not the main purpose and was only incidental to allow use of trade mark for transaction processing. We have also discussed how transaction processing service is rendered by the Applicant to banks that are recipients of service and not provider of service. The use of these trademarks/logo etc. is by the banks and not by service provider (the Applicant) and it is for selling of cards by these banks in India. Thus, the inference drawn by the Applicant does not appear to be correct.

23.4.4.5 It is also seen that the Applicant is incurring huge amounts for advertisement and promotion in India. Rs 31.85 crore was incurred in FY 2014-15 (4 month period, beginning 1st Dec 2014) and Rs126.59 crore in FY 2015-16. This advertisement and promotion is for attracting customers to buy MasterCard cards. Quite clearly that would be done only when the Applicant wants to promote MasterCard brand and trade name in India. If the use of brand of MasterCard was only incidental to transaction processing, there was no need to

incur such expenditure for advertisement / promotion in India. Thus, this high spend on advertisement / promotion also supports the Revenue's contention that licensing of brand/trademark is not incidental but the main activity, so that people buy credit cards with MasterCard logo.

23.4.5 Based on above reasoning we are of the view that licensing of various IPs in the form of brand/trade name/mark etc. are not incidental to the activity of transaction processing and the payment made by various customer banks in India to the Applicant is also for the use of these IPs and hence is royalty. We also hold that this is effectively connected with various types of PEs that we have discussed. Thus it would get taxed with the PE under Article 7 and not under Article 12. How much of the transaction processing fees would constitute royalty and how much would be in the nature of business income are issues that are not in the domain of the AAR. However, once we have held that it would be taxable under Article 7, the bifurcation may not be material, as the entire amount will get taxed under Article 7 of India Singapore DTAA, after appropriate attribution by the assessing officer.

23.4.6 The Applicant has also contended that the customer banks are not concerned with the machinery, equipment and the intangibles that are used for rendering transaction processing services. The banks only want their transactions to get authorized, cleared and settlement in an efficient manner. They pay for the services and not for intangibles. It is true that customer banks pay for the service. But they also pay for licensing of IPs which they have taken on license from the Applicant for selling their cards. This licensing of IPs is not incidental to the transaction processing service because that service is provided by the Applicant, and IPs are used by the banks for selling their cards (and not Applicant's cards). In fact, the use of IPs is actually by the final consumers who buy MasterCard debit/credit card based on its brand, logo, reputation, reliability,

trust, etc.. It is these final consumers (the holder of credit/debit card) who are ultimately making the payment for the services. It may appear that it is banks that are making payment to the Applicant, but in reality the incidence of this payment falls on final consumers as merchants price their products keeping in mind the fee that they have to pay to MasterCard. Thus, the person who swipes his MasterCard to make plastic payment is the one who bears the actual fees paid by banks to the Applicant. This person uses MasterCard for its brand, logo, reputation, reliability, trust, etc.. The Applicant contended that the fee is paid by acquirer bank even in cases where the Applicant has not licensed the IPs to this bank. The Applicant thus contended that this fact proves that the fee is for service and not for use of IPs. We have said above that the fee may be paid by acquirer bank but the actual incidence of fee is on the consumer who has used the merchants, and whose account is with acquirer bank. The fee paid by acquirer bank is recovered from the merchant and the merchant recovers that amount from the price of product/service paid by the consumer. Thus the incidence of fee finally falls on the consumer who is using the MasterCard. It is he who is using the IPs associated with MasterCard and hence, the payment made by it to merchant has a part which represents payment for use of MasterCard IPs. That part is then paid by merchant to acquirer bank and then by acquirer bank to the Applicant. Issuer bank/Acquirer bank is only a medium for the fee to be ultimately paid to the Applicant by the final consumer. And this consumer uses the intangibles of MasterCard in the form of brand, reputation, trust, reliability, logo etc. and hence constitutes royalty. This classification gets further strength from the fact that after getting this royalty from India, the Applicant pays it to MCI and the Applicant has admitted that this payment to MCI is royalty.

23.4.7 The Applicant has also contended that service charges are with reference to the value and volume of transactions which are processed and

hence they cannot be royalty. We have noted from the billing manual, produced by the Applicant and reproduced in the Revenue's report, that payment of fee is also for license fee which are not based on value and volume of transactions and are one time. To illustrate, the licensing agreement clearly talks about MasterCard one time licensing fee and Maestro/Cirrus one time licensing fee. In addition, there are other fees like minimum Revenue fee, warning bulletin fees etc. which are not based on value and volume of transaction. Even otherwise royalty payment could also be based on volume and value of transactions, for example, the advertisement and use of intangibles to increase the use of MasterCard in India reflect a relationship with the value and volume of transactions in India. In CGI Information Systems and Management Consultants Pvt. Ltd. [ITA No. 209/2008] (Karnataka), w.r.t Cost Sharing Arrangement as a basis, it was held that the methodology of payment does not alter the nature of the arrangement, and receipt under such an arrangement could be in the nature of Royalty, irrespective of the mode of payment. In fact, in the FOWC case (supra) the fact of lump sum payment went against its characterization as royalty.

23.5 Another issue raised by the Revenue is with regard to the use of equipment, and whether allowing the use of the same would constitute royalty. It is contended that the use of MIP along with MasterCard network and processing technology constitute equipment/process royalty. The Revenue has contended that the Applicant is the real owner or licensee of MIP though on paper it is shown to be owned by MISPL. MIPs continue to be owned by overseas AEs even after 1st Dec 2014 and are licensed to the Applicant. The Process technology is part of IP licensed by MCI to the Applicant who in turn has a right to sub-license it to Indian customers. Thus process technology which is part of the MIP and MasterCard Network is owned by the Applicant or is licensed to it. The application software (Master Connect and MasterCard File express) are admitted to be owned by the Applicant or licensed to it. Thus the fees represent money

paid by Indian customers to the Applicant for use of equipment and process which amounts to royalty.

23.5.1 The Revenue has relied upon the decision of the Hon'ble Madras High Court in the case of Verizon Communication Singapore Pte Limited (supra). It was held therein that after the amendment introduced in the year 2012, with effect from 01.06.1976, irrespective of possession, control with the payer or use by the payer or the location in India, the consideration would nevertheless be treated as 'royalty. The Hon'ble Madras High Court relied on the AAR ruling in the case of Cargo Community Network Pte Ltd (289 ITR 355) as well as Dishnet Wireless Limited (353 ITR 646) where AAR had remarked that Expl. 5 and 6 to Sec. 9(1)(vi) of the Income-tax Act, 1961 made it clear that payment was against a right to use the process and/or right to use a commercial or scientific equipment. It also relied on the coordinate bench ruling in Poompuhar Shipping Corporation (supra) where it was remarked that the 'retrospective amendment' has thus removed all doubts in so far as the expression 'use or right to use' to be understood in the context of possession, control or location. The Hon'ble Madras High Court held that the Hon'ble Delhi High Court ruling in Asia Satellite Telecommunications Co. Ltd (supra) is not effective after insertion of Explanation 4 and 5. It held that process includes transmission by satellite, cable, optic fibre or any other similar technology and it need not be secret. It also held that there is use of equipment and cable in the transmission of the data/voice from one end to the other and it is difficult to accept the case of the assessee that the nature of transaction is only that of service.

23.5.2 Revenue has pleaded that the facts of the Verizon case (supra) are similar to the present case. In the Verizon case it was DCE/CPE which was installed at the premises of customers, and in this case MIP is installed at the premises of the customers. Master Connect and MasterCard File express applications owned by Applicant (or under license to it) are used by Banks/FIs in

India. In both cases, the payment is actually for use of this equipment and the network associated with the equipment (cable, optical fibre, internet etc.) is used to transfer the data. By placing the equipment in the premises of the customers, the customer acquired significant, economic or possessory interest in the equipment of the Applicant to the extent of the dedicated network hired by the customer, which enable it to carry out its functions. Revenue has also pleaded that Note 9.1 of OECD commentary on Article 12 only requires physical possession with the customer to constitute equipment royalty for cases where in the equipment royalty provision is there, and there is no condition of control being with the customer. Thus, requirement of control is not a Treaty requirement and it can always be clarified through clarificatory amendment in domestic law. The insertion of Explanation 5, so far as it gives clarification on 'control', does not amount to overriding the DTAA as there is no requirement of control in the DTAA. Revenue has also pleaded that the Hon'ble Madras High Court judgment in Verizon involves India Singapore DTAA and hence is of greater significance. In any case, in our case even the requirement of possession with the customer is satisfied.

23.5.3 In response to the Revenue's contentions mentioned above, the Applicant has submitted that the customers pay service fee to the Applicant and use of MIP is preparatory and auxiliary. The Applicant has also stated that MIP is not owned by the Applicant. The Applicant has contended that application software do not serve any purpose on standalone basis. The Applicant has submitted that the facts of Verizon Communication case(supra) are different from the facts of this case. In the Verizon case the private links were under the customers' exclusive dominion and control. However, the control of equipments in this case is not with customer banks. The Applicant has relied upon the decisions of Hon'ble Delhi High Court in the case of Nokia Networks OY (supra) and New Skies Satellite NV (supra) to plead that amendment to the domestic law cannot be read into the tax

treaty. It has relied on the Hon'ble Supreme Court decision in the case of Azadi Bachao Andolan (supra) to claim that where provisions of tax treaty is more beneficial then such provisions should be made applicable. The Applicant has relied on Hon'ble Delhi High Court decision in the case of Asia Satellite Communication Co Ltd (supra) to support its argument that charges received are for rendering service and not for use of secret process. The Applicant has also relied upon AAR rulings in the cases of Dell International Services India Private Limited (supra), Cable and Wireless Network India Private limited (supra) and Factset Research systems Inc. (supra) who have reiterated the proposition laid down by Hon'ble Delhi High Court. The Applicant has further contended that the payment made by customer banks is for availing of service and not for the use of a process. The Applicant has also contended that the process is not secret. It has relied upon Delhi ITAT decision in the case of Panamsat International Systems Inc. (supra) to support its contention. The Applicant has also contended that the Revenue's reliance on decision of Bangalore ITAT in the case of Google India (supra) is erroneous, as in that case Google India was using brand name, logo, and right in IPs. Further they were related party.

23.6 We have considered the arguments of both the Applicant and the Revenue. In order to classify a payment of fees as royalty for use of equipment (MIP), it is necessary that MIP is to be owned by the Applicant or is under license to it. The Revenue has cited Verizon case (supra) but in that case the CPE installed at the premises of the customers were owned by the assessee. In our case the MIPs are shown to be owned by MISPL. The Revenue has made a claim that effectively MIP is owned by the Applicant. This is based on the submission that MIPs are under the control of the Applicant, a stand that we have accepted earlier, and that ownership of MIPs were not transferred under ST/VAT as no invoices were issued and these taxes were not paid. The Applicant has claimed that the seller of MIPs has paid capital gains tax and has been allowed

depreciation by the assessing officer under section 143(3) of the Act. There is no dispute on these facts. But we are of the view that the main purpose of Income-tax Act is only to determine taxable income. For a transfer of ownership, a sale must be effected and sales tax/VAT paid. Only then it is complete. Hence, the latter is a better determinant of a transfer taking place. Since, there is no compliance of sales tax at the time of transfer of ownership in Dec 2014, in fact even till today, there is no transfer of ownership under the eyes of law, and hence, the MIPs continue to be owned by the overseas AEs of the Applicant (as before reorganization) and that AEs have given the MIPs to the Applicant under a license.

23.6.1 In this connection it may also be highlighted that in the written submission, filed post hearing, the Applicant has provided details of “MasterCard-one time license fee” as referred to in the billing manual. As per the Applicant, this fee is charged to an affiliate member as a one-time on-boarding fee for availing transaction processing services. This is paid for the cost of MIP installation, for establishing connectivity and set-up of processors. It is clear from the above description that the MIPs are defacto owned by the Applicant as they are charging fee for cost of MIP installation. Thus, the first test for equipment royalty is held to be satisfied.

23.7 Another important test is whether it is necessary that the control of MIPs should be with the banks in whose premises they are installed. There is no dispute that control is not with the Banks. The Applicant has relied on the Hon’ble Delhi High Court decision in Asia Satellite (supra) as well as on New Skies Satellite (supra) to claim that since control is not with the user, there cannot be a royalty. With regard to explanation 5 to section 9(1)(vi) of the Act it has been submitted that the Hon’ble Delhi High Court has held in New Skies Satellite NV (supra) that amendment to the domestic law cannot be read into the tax treaty. The Revenue has relied upon the decision of Madras High Court in the case of

Verizon Communication Singapore Pte Limited (supra). The Hon'ble Madras High Court in this case, has held that after the amendment introduced in the year 2012, with effect from 01.06.1976, irrespective of possession, control with the payer or use by the payer or the location in India, the consideration would nevertheless be treated as 'royalty'. The Hon'ble Madras High Court relied on the AAR ruling in the case of Cargo Community Network Pte Ltd (supra) as well as Dishnet Wireless Limited (supra) where AAR had remarked that Expln. 5 and 6 to Sec. 9(1)(vi) of the Act made it clear that the payment was against a right to use the process and/or right to use a commercial or scientific equipment. The Hon'ble Madras High Court also relied on the coordinate bench ruling in Poompuhar Shipping Corporation (supra) where it was remarked that the 'retrospective amendment' has thus removed all doubts in so far as the expression 'use or right to use' is to be understood in the context of possession, control or location. The Revenue has also pleaded that the Hon'ble Madras High Court decision should be relied upon as it is on the India Singapore DTAA. Revenue has also pleaded that Note 9.1 of OECD commentary on Article 12 only requires physical possession with the customer to constitute equipment royalty for cases where, in Treaty, equipment royalty provision is there, and there is no condition of control being with the customer. Thus, requirement of control is not a treaty requirement and it can always be clarified through a clarificatory amendment in domestic law.

23.7.1 We are of the view that the Hon'ble Madras High Court decision in Verizon Communication (supra) has more persuasive value than Hon'ble Delhi High Court decision since Verizon case is on India Singapore DTAA, which is relevant to our case. Further, the AAR has also relied on explanation 5 in its rulings in the cases of Cargo Community Network Pte Ltd (supra) as well as Dishnet wireless Limited (supra). Thus we hold that in view of Explanation 5, there is no requirement of control with the user. We are also of the view that, as submitted by the Revenue, there is no Treaty requirement of control with the

user, and hence domestic law can always be amended to clarify this. There is no doubt that possession of MIPs is with customer banks in India. Thus, we hold that MIPs are equipment whose use constitutes royalty and they are effectively connected with PE created on account of MIPs as well as other PEs.

23.8 We now come to the question of process royalty. The Applicant has contended that the payment made by customer banks are for availing of service and not for the use of a process. The Applicant has relied upon the decision in the case of Asia Satellite(supra) and New Skies Satellite(supra). The Revenue has relied upon the decision of Madras High Court in Verizon Communication (supra). We are of the view that Verizon decision is applicable here as it is a case of India Singapore DTAA and just as in our case, the process in that case was also happening in India. On the other hand, in Asia Satellite and New Skies, the facts were such that use of process and equipment was outside India and only footprint of that use was in India. These were important material facts in these cases for which it was held that there is no royalty. These facts are not present in our case since both the equipment and the process are in India.

23.8.1 The next question is whether it is a secret process. Although Explanation 6 to section 9(i)(vi) of the Act makes it clear that process may not be secret, the Revenue has submitted that the payment is royalty for use of or right to use of secret process in the operation of MIP, which is not in public domain. The Revenue has relied on the agreement between MCI and the Applicant to plead that process technology is intellectual property licensed to the Applicant who in turn has sublicensed it to Indian customers (Banks/FIs). On the other hand the Applicant has contended that the process is not secret. It has relied upon Delhi ITAT decision in the case of Panamsat International Systems Inc. (supra). We find that this decision too was not on India Singapore treaty. Verizon Communication which was on the India Singapore treaty has clearly held that the process need not be secret. Without prejudice to this, in Panamsat there was a

factual finding that transponder technology is available off the shelf in the form of published literature and hence it is not a secret process. However, the facts in our case are different. There is no published technology of transaction processing. If we see the list of patents filed by the Applicant in India (which were produced as an annexure to license agreement between the Applicant and MCI US) we can see that there are a number of patents related to process used for transaction processing. Some examples are: a system and method for secure telephone and computer transaction, customer authentication in e-commerce transaction, a system for authenticating card holder transaction with a merchant on an electronic network, method and system for authorizing a transaction using a dynamic authorization code, system and method for generating collision free identifiers for financial transaction cards, method and system for using contactless payment cards, method and system for conducting contact less payment cards, reference equipment for testing contactless payment devices, payment card signal characterization methods and circuits, contact less payment card reader, collision detection and avoidance scheme, method and system using a bitmap, techniques for authorization of usage of a payment device, apparatus and method for bill payment card enrolment, methods and systems for paying a bill using a transaction card account. The Applicant, in its written submission filed post hearing, has stated that only three patents out of these have been granted so far. Further, it has said that these patents are not licensed to customer banks.

23.8.2 The fact that only three patents are granted so far in India, would not have an impact on the inference that technology is patented and hence secret. Quite clearly, they are patented and hence cannot be known to and be used by the public. Thus these are secret process. There is also a press release of Master Card dated 4th Feb 2015 (which was produced by the Revenue during these proceedings) in which they have stated that Pune and Vadodra technology

hub in India are key part of the company's strategy to derive the development of cutting edge payment technologies. The team in India will be developing solutions that enhance online transactions and payments value chain, as well as innovation around mobile and contact less payment services. It further adds that the 2014 acquisitions of Vadodra based C-SAM and Pune based ECS brought MasterCard development and processing expertise to India. Several innovations developed in India are already being integrated into MasterCard solutions. Thus it is evident that patented and secret technology is used in transaction processing, some of which are developed in India. The list of patents granted includes such technologies. Thus, there is use of a secret process and hence, we hold a part of the fee paid to the Applicant is also for use of secret process and hence royalty. It is not necessary that this secret technology is licensed to customer banks. It is sufficient if secret process is used, as the definition of royalty in India Singapore DTAA classifies use of secret process as royalty. This royalty is also effectively connected to the PE created on account of MasterCard Network as well as other PEs.

23.8.3 We do not agree with the Applicant's contention that reliance should not be placed on the ITAT Bangalore decision in the case of Google India since it was the case of a related party and the facts are not the same. We are of the view that there is no need for two parties to be related to each other to constitute a payment as royalty. The Applicant in its rebuttal and written submission post hearing, has submitted that the facts of our case are different from facts of Karnataka ITAT judgment in Google India case (supra). It is true that exact facts are different but material facts for which the ITAT held the payment as royalty in the Google case are similar to facts in our case. Like in the Google case, in our case as well, right in intellectual property of master card is allowed to be used by Indian customers. Indian customers are allowed to use trademark of MasterCard to sell the cards owned by them. Further, intellectual property in the MIP and in

the Master Card network (in the form of software and process technology) is used for authorization, clearance and settlement. This process works only with the help of patented tools, software and process technology owned by MCI and licensed to the Applicant. Without the use of these intangibles, the entire process of authorization, clearance and settlement would not happen. The intellectual property in MIPs and Master Card Network vest with the MCI which has licensed it to the Applicant. These activities also use a secret process which is not in public domain. Thus use of brand name, intellectual property and secret process of Master Card by the Indian customers clearly falls under the definition of royalty, both under the Act as well as under the DTAA. Hence, the facts being the same, reliance can also be placed on Bangalore ITAT decision to hold the payments to be in the nature of royalty.

23.8.4 Another question we are faced with is as to whether there is use of software so as to constitute royalty. The Revenue has contended that payment is also made for the use of software inside the MIPs and on the cards and also the application software (Master Connect and Master Card File express). Use of this software amounts to royalty. It has relied upon the Hon'ble Karnataka High Court judgments of Synopsys India (P) Limited (2016-LL-0405-63) and Samsung Electronics Company Limited (245 CTR-481 HC-2011) in this regard, and also the latest AAR ruling on this issue in the case of SkillSoft Ireland Limited (AAR no 985 of 2010). It has also relied upon explanation 4 to section 9(1)(vi) of the Act to contend that use of software amounts to transfer of right in copyright and hence it is royalty.

23.8.5 The Applicant has contended that there is no standalone provision of MIP and application software (MasterCard Connect and MasterCard File express) and that the transaction is rendering of transaction processing service.

The Applicant has relied upon the Hon'ble Delhi High Court ruling in the case of Infrasoft Limited and M Tech India Private Limited in its support.

23.9 We have considered both the arguments. We have already discussed that classification as done by the Applicant is not important. The fact is that there is use of software, and the legal position is that use of software would amount to royalty. Hence, it needs to be held as royalty. There is nothing like standalone provision of MIP and application software. The use of software inside MIP, and cards in the application software are essential part of the transaction without which no transaction can be completed. The Applicant has relied upon the Hon'ble Delhi High Court ruling in the case of Infrasoft Limited in its support. However, the AAR decision in the case of SkillSoft Ireland Limited (supra) considered the decision of Hon'ble Delhi High Court in the case of Infrasoft and still ruled that use of software is royalty. Hence, we also hold that the use of software is royalty and is effectively connected to the PE.

24. In its written submission, post hearing, the Applicant has submitted that facts of the Skillsoft case(supra) and Synopsis case (supra) are different. These judgments deal with sales of packaged software, which carry a license granted by the owner to make copies of the said software for use on the purchaser's hardware. On the basis of said grant of license, it was successfully contended by the Revenue that payments were in the nature of royalty. There is no such provision of software, either in a sale or license basis, by the Applicant to any of its customers. We do not agree with this submission of the Applicant. In these two cases there was no license to copy and sell the software. What was allowed under license was only to copy the software on the computer enabling the user to use the software. We find similar facts in the case before us. Customer banks have to copy the application software on their computer and then only they can use it. Thus, the objection of the Applicant is not acceptable.

25. We shall now consider as to whether the fee payable to the Applicant is taxable as FTS under India Singapore DTAA.

25.1 The Revenue has also contended that a part of the payment may represent service fee which is taxable as FTS. It is technical service (as it involves use of MIP, process technology and network) and is in connection with application/enjoyment of property for which royalty is paid. In this regard paragraph 4 of Article 12 of India Singapore DTAA has been relied upon. The Revenue has relied upon decision of the ITAT Delhi in the case of Asia Satellite Telecommunications (supra) in support of its claim that it is not a facility and hence it is service. In support of its claim that it is in connection with application/enjoyment of property for which royalty is paid, the Revenue has also relied upon the billing manual where fee paid relates to both licensing as well as for service. Revenue has also pleaded, on without prejudice basis, that some part of the fee is also for advisory services to Indian customers. This is a technical or consultancy service provided by MasterCard to its customers in India which make available technical knowledge, experience, skill, know-how in the form of spending habits of the person who uses MasterCard. The fee charged from the banks also include a component for making available technical knowledge, experience in the form of spending habit of persons using MasterCard. Thus, with respect to these advisory services even make available test is satisfied.

25.2 The Applicant has replied by relying upon Hon’ble Supreme Court decision in the case of Bharti Cellular Limited (supra) to contend that for service to be technical in nature there has to be an element of human intervention. It has been contended that in his case it is automated process and there is no human intervention. The Applicant has also relied on the decision in Kotak Securities

Limited (SC) (supra) in support of its claim that what he provides is standard facility and not services. The Applicant has also relied upon the judgment in the case of Skycell Communications Limited (Madras) (supra) where it was held that the provision of facility for use of an electronic exchange, which had mobile communication network with a switching center, did not constitute technical services. The Applicant has also contended that in its case, the make available requirement is not fulfilled. The Applicant has given examples where use of technical equipment may not be use of technical service, like airline passenger paying for travelling in aircraft, and a consumer getting electricity. The Applicant has also contended that even if these are technical or consultancy services they are not in relation to the application/enjoyment of property for which royalty is received since there is no royalty in this case. The Applicant also submitted that since "make available" test is not satisfied, it cannot be taxed as FTS under the India Singapore DTAA. Various case laws have been relied upon.

25.3 Before we examine the question of applicability of FTS provision in the India Singapore DTAA, we need to see whether the service is a facility as laid down by various courts. Hon'ble Supreme Court in Kotak Securities Limited (supra) has stated that fees paid in connection with standard facility cannot be classified as FTS. Although the Applicant has relied upon Bharti Cellular Limited (SC) (supra) as well, however, in Kotak Securities subsequently it was held that modern day scientific and technological developments may tend to blur the specific human element in an otherwise fully automated process by which such services may be provided. The Hon'ble Supreme Court thus held that human intervention is not the right test and the right test is whether the service provided is standard facility. Thus, relying on the Kotak Securities case, we need to first ascertain whether there is standard facility or not.

25.3.1 The Applicant has relied upon the case of Skycell Communications Limited (Madras) (supra) where it was held that the provision of facility for use of an electronic exchange, which had mobile communication network with a switching center, did not constitute technical services as it was a standard facility. The Revenue has relied upon the Delhi ITAT decision in the case of Asia Satellite Telecommunications Co. Ltd (supra) where the Hon'ble Madras High Court judgment of Skycell was also discussed. In Skycell it was held that the service provided by mobile service providers to customers is standard facility. Delhi ITAT in Asia Satellite discussed this and observed that the facts in their case are different. The operation starts by up linking the signals from the earth stations by the TV channels to the satellite and then after undergoing various processes in the satellite the signals are down linked so as to be made available to the cable operators, who in turn provide these to the public. In this chain of processes it was observed by Delhi ITAT that first is the relation between the TV channels and the assessee, second is the relation between assessee and the cable operators and the third between cable operator and public. In the light of the difference between the use of 'facility' and 'process', the ITAT held that the relation between the cable operators and the public is that of use of 'facility', whereas the first relation between the TV channels and the assessee is for the use of the 'process', as a result of which the programmes uplinked by TV channels become fit for being relayed.

25.3.1.1 Delhi ITAT further observed that the decision of the Hon'ble Madras High Court was in the context of the third relation in the context of their facts, namely, the cable operators and the public. It was explained at p. 58 of the Madras judgment that satellite television has become ubiquitous and when a person receives such transmission of television signals through the cable provided by the cable operators, it can't be said that the home owner, who has such a cable connection, is receiving a technical service. No doubt the 'public'

(analogous to the subscribers to the cellular phone in that case) use the facility provided by the cable operators (analogous to the petitioners in that case) but the payment made by the TV channels for receiving, processing and relaying the programmes is for the use of the process provided to them. Thus, the Revenue has pleaded that the relation between the banks and the Applicant is for the use of process, though the relation between final user of cards and the Applicant may be of use of a facility.

25.3.2 We are unable to agree with the stand taken by the Revenue on the above issue. We have already held that ultimately the beneficiary is the final consumer who is using the card. Whether a particular payment is royalty or service or facility needs to be seen from his perspective. Banks are only a medium for payment of fee to the Applicant. Hence, we hold that the relation between final consumer and the Applicant is of use of a standard facility and hence, transaction processing service rendered by the Applicant cannot be taxed under the Article concerning Fees for Technical Services in India Singapore DTAA.

25.4 We have also noted that there are services other than transaction processing services. They are in the nature of warning bulletin fees for listing invalid or fraudulent accounts either electronically or in paper form, cardholder service fees, program management services (e.g. Foreign exchange margin, commissions, load fees), account and transaction enhancement services, holograms and publication fees and advisory services etc. We are of the view that these services are not standard facility and for that specific service is required to be rendered to specific customer who has requested such services. Hence, they are technical services. However, they do not make available technical knowledge, experience, skill, know-how to the service recipient. Hence, they cannot be classified as Fee for Technical Services under Article 12 of India Singapore DTAA.

25.5 Thus, the part of fee paid to the Applicant, which is not royalty, is business income which is taxable under Article 7 and not under Article 12 of India Singapore DTAA. Since we have already held that there is PE in India, the fee paid will get taxed as business income arising through the PE.

26. In Question no 2 the Applicant has asked whether where a PE of the Applicant (in the form of its Indian subsidiary) is found to exist in India, whether provision of arms' length remuneration to such PE for the activities to be performed in India, would absolve any further attribution of the global profits of the Applicant in India.

26.1 This question is with respect to our ruling where we have held that the Indian Subsidiary MISPL is the PE of the Applicant as fixed place as well as dependent agent. The Applicant has relied on the decision of the Hon'ble Supreme Court in the case of Morgan Stanley (supra), to contend that no further attribution can be made to the PE even if there is a PE.

26.2 The judgment cited by the Applicant is with respect to agency PE and not with respect to fixed place PE. Thus, where a subsidiary is a fixed place PE, the above cited rulings would not apply. More so because, the functions performed and risks undertaken by a nonresident enterprise through the subsidiary is not fully captured in the FAR profile of the subsidiary. To illustrate, in this case there was a PE in India. All the functions performed by this PE, all assets/liabilities of this PE were taken over by MISPL. However, the FAR profile of MISPL does not capture the full functions performed, assets employed and risk undertaken by erstwhile PE. Thus there are functions that are being performed, risks that are being undertaken by MISPL on behalf of Applicant which are not reflected in its FAR. As MISPL constitutes a PE of the Applicant, the Assessing Officer may consider a further attribution to this PE on this score.

26.3 Coming to agency PE, we have already discussed the decision in Morgan Stanley (supra) earlier. Even in the case of dependent agent PE, the FAR profile of the Applicant AE is different from FAR of the dependent agent (Indian subsidiary). It is only when the two FAR are the same that one can say that there cannot be any further attribution. We have already held earlier that in this case the PE of the Applicant created through Indian subsidiary (agency PE) is entering into contract with Indian Customers by securing orders. This function performed and risks undertaken are not reflected in the FAR profile of the Indian subsidiary and hence the remuneration to subsidiary would not extinguish attribution to the PE for those extra functions and risks. We had earlier discussed that in Morgan Stanley it was held that no further attribution to PE would hold good only when the AE has been remunerated on an arm's length basis taking into account all risk taking functions of the nonresident enterprise. If TP analysis does not adequately reflect the functions performed and the risks assumed by the nonresident enterprise, there would be a need to attribute further profits. Thus, even in case of a dependent agent PE in this case, there is need for further attribution since all the functions/risks are not reflected in the FAR of MISPL.

27. The last question raised by the Applicant is with regard to tax withholding at source, as to whether the same would be required on the amounts to be received by the Applicant, and what would be the applicable rate.

27.1 We have held that the Applicant has a PE in India (on various accounts) and that payment to the Applicant constitutes royalty. Further, since the Applicant is carrying on business in India through a PE, and the right, property or contract in respect of which royalties is paid is effectively connected with such PE, in terms of Article 12(6) of the DTAA between India and Singapore, the royalty is to be taxed on net basis with the income of the PE. Hence, tax is required to be withheld at source at the full applicable rate at which the non-resident is

subjected to tax in India. We however agree that all the revenues received by the Applicant from customers in India would not be attributed to the Indian PE since significant activities are also carried out by the Applicant outside India. Thus, there is a need for attribution which is required to be done by the assessing officer. On such attribution of income to the PE, the tax is required to be withheld at full applicable rate at which the nonresident is subjected to tax in India.

28. During course of these proceedings, the Revenue had raised certain issues regarding possibility of change of facts and laws and had requested that ruling should not apply to the new facts and the changed position of law. Examples were cited, such as that (i) the Applicant has not produced details of import of MIPs even though these were mostly imported in 2013 and 2014; (ii) the Applicant has not produced Customer Business Agreement; (iii) the server of the Applicant may have to be relocated to India due to the latest RBI instructions in this regard; and (iv) the tax treaty between India and Singapore may get amended due to Multi Lateral Instrument. We may clarify that the ruling is given on facts brought before us and as per the law/treaty existing today.

29. On the basis of the above detailed discussion, the questions posed to us seeking a Ruling, are answered as under:

(1) The Applicant has a PE in India under the provisions of Article 5 of the India Singapore DTAA in respect of the services rendered/to be rendered with regard to use of a global network and infrastructure to process card payment transactions for Customers in India. There is fixed place PE, service PE and dependent agent PE.

(2) Arm's length remuneration to PE on account of Indian Subsidiary for the activities performed / to be performed in India, would not absolve the Applicant from any further attribution of its global profits in India since the FAR

of the Indian Subsidiary does not reflect the functions/risks of the Applicant performed/undertaken by it.

(3) A part of the fees received/to be received by the Applicant from Indian Customers (comprising transaction processing fees, assessment fees and transaction related miscellaneous fees) would be classified as royalty within the meaning of the term in Article 12 of the India- Singapore DTAA. However, since it is effectively connected to PE, it would be taxed under Article 7 and not under Article 12. The fee cannot be classified as FTS under Article 12 of India-Singapore DTAA.

(4) The Applicant is required to withhold tax at source on amount attributed to the PE in India at the full applicable rate at which the non-resident is subjected to tax in India.

This ruling is accordingly given and pronounced on this 06 day of June, 2018.

Sd/-	**Sd/-**
(Ashutosh Chandra)	**(R.S.Shukla)**
Member (Revenue)	**In-charge Chairman**