

IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES "I-2" : DELHI

BEFORE SHRI BHAVNESH SAINI, J.M. AND SHRI L.P. SAHU, A.M.

ITA.No.229/Del./2016
Assessment Year 2010-2011

M/s. Cast Software Inc., 321 West 44 th Street, Suite 501, New York, NY 10036. PAN AA ECC1173D C/o. Manoj Patwari, M.C. Jain & Co. C.As. 470/21A, Ansari Road, Daryaganj, New Delhi-002.	vs.	The DDIT, Circle – 1 (1), International Taxation, New Delhi.
(Appellant)		(Respondent)

For Assessee :	Shri Tapas Ram Misra, Advocate.
For Revenue :	Shri H.K. Choudhary, CIT-D.R.

Date of Hearing :	16.01.2019
Date of Pronouncement :	17.01.2019

ORDER

PER BHAVNESH SAINI, J.M.

This appeal by Assessee has been directed against the assessment order dated 12.12.2013 passed by DDIT, Circle-1(1), International Taxation, New Delhi, under section 143(3) r.w.s. 144C (13) of the I.T. Act, 1961, for the A.Y. 2010-2011 on the following grounds :

1. *“That on the facts and in the circumstances of the case, the impugned assessment order passed u/s 143(3) read with section 144C(13) pursuant to direction of DRP under section 144C(5) of the Income Tax Act, 1961 ("the Act") is based on incorrect legal and factual premise, contrary to judgments of the jurisdictional High Court, and untenable in law.*
- 1.1. *That on the facts and in the circumstances of the case, the Assessing Officer erred on facts and in law in concluding, following the direction of DRP, that Rs.1,46,00,231/- on account of sale of software products to IBM India Private Limited to be taxable as “Royalty” under the provisions of the Income tax Act as well as provisions of DTAA entered by India with USA.*
- 1.2. *The Honorable DRP failed to appreciate that payment for a mere transfer of computer software de hors any copyright associated with it is not covered within the ambit of clause (v) of the definition of royalty under the Act, ignoring the well settled*

principles as laid down by the Jurisdiction Hon'ble High Court of New Delhi.

- 1.3. *The Learned AO as well as the Honorable DRP failed to appreciate that in order to qualify as a royalty payment within the Act, it is to be established that the acquirer, by making payment, obtains all or any of the copyrights of the literary work, being software. Further, distinction has to be made between the acquisition of a 'copyright right' and a 'copyrighted article'.*

2. *The learned AO and Honorable DRP have erred in determining the above said Income by placing excessive reliance on the retrospective amendment to section 9(1)(vi) by the Finance Act, 2012 read with explanation 4 to the said section by the Finance Act, 2012 holding the Income earned by the assessee as Royalty Income - not appreciating the fact that no retrospective amendment into a domestic law can be read into a Tax Treaty, as judicially decided."*

2. Briefly, the facts of the case are that in this case draft assessment order was passed. The assessee filed objections to the draft order dated 26.03.2013. The objections of the assessee had been that the A.O. has determined the taxable income to be Rs.1,46,00,231/-. The A.O. has erred in determining the above said income by placing excessive reliance on the retrospective amendment to Section 9(1)(vi) by the Finance Act, 2012 read with Explanation-4 to the said Section by the Finance Act, 2012, holding the income earned by the assessee as “Royalty Income” by not appreciating the fact that no retrospective amendment into a domestic law can be read into a Tax Treaty, as judicially decided.

3. The assessee filed its return of income for the assessment year under appeal 2010-2011 on 23.02.2012 declaring NIL income. The assessee-company has entered into an agreement dated 27.08.2009 with IBM India Pvt. Ltd., for supply of software products to IBM India Pvt. Ltd., During the year under consideration, the assessee has supplied software amounting to US Dollar 3,15,000

equivalent to INR Rs.1,46,00,231/- on limited use basis to IBM. The IBM withheld tax at source @ 10.56% of the gross amount of sale. The company has treated the sale value not taxable as in its view the amount of receipt is not royalty under Article 12 of the India-US DTAA (“the Treaty”).

4. The DRP noted that the primary issue for consideration is the taxability of the amount received by the assessee as royalty both under the domestic law as well as Treaty. In the detailed order, the A.O. has held that the payments received by the assessee are to be characterized as royalty under the Act as well as the Treaty”. The A.O. has amply demonstrated that the licensing of software is covered under the provisions of the Copyright Act as well.

5. The assessee has submitted that assessee has been selling software license without giving right of reproduction and commercial exploitation. It is a typical case of cross border sale which does not lead to taxability in India. As such in the absence of a P.E, the income emanating from the software licenses sale is not taxable in

India. The assessee has further submitted that A.O. has erred in placing excessive reliance on retrospective amendments to Section 9(1)(vi) of the Act read with Explanation-4 thereof without appreciating the fact that no retrospective amendment in domestic law can be read into a Treaty. The assessee relied upon decision in the case of DIT vs. Nokia Networks OY (2012) 25 taxmann.com 225 to justify its case. It was submitted that supply of software integral to the equipment was held not to be royalty. The assessee also stressed that sale of software without granting the copyright would not amount to sale of copyright in the light of Indian Copyrights Act, 1957. The assessee relied upon decision of the Hon'ble Supreme Court in the case of Tata Consultancy Services vs. State of Andhra Pradesh 271 ITR 401 (SC) and decision of Hon'ble Delhi High Court in the case of DIT vs. Ericsson AB (2012) 343 ITR 470 (Del.) to submit that in order to qualify the royalty payment within the Act, it is to be established that the acquirer by making payment obtains all or any of the copyrights of the literary

work being software. The assessee, therefore, requested that addition proposed may be deleted.

6. The DRP however noted that the issue for decision is whether the payment received by the assessee is covered within the definition of Royalty under section 9(1)(vi) of the Act and Article-12 of India-USA DTAA. The DRP found that all the objections raised in the submissions before it were also raised before the A.O. and that these have been elaborately discussed by the A.O. in the body of the draft order. The A.O. has held that the receipts in the hands of assessee are in the nature of royalty taxable under Clauses (i), (iii), (iva) and (v) Explanation-2 to Section 9(1)(iv) of the Act and the India-USA DTAA. Thus, the DRP following the same reasoning declined to interfere with the draft order. The DRP further observed regarding taxability of the Royalty and recent Jurisprudence and reproduced the provisions of the law and many case laws in the impugned order and also referred to judgment of Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronic Co. Ltd., 203 Taxman 477 (Kar.). The Articles under OECD model convention

along with other decisions are also discussed. Whatever case law were relied upon by assessee regarding the issue were found distinguishable and not a binding precedents. The DRP also prepared a chart with regard to matter in issue with reference to the Judgment of Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) and Judgment of Hon'ble Delhi High Court in the case of Ericsson A.B. 343 ITR 370 and ITAT, Special Bench in the case of Motorola and Others. However, following the decision of the Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) and others, rejected the objections of the assessee. It was also observed that since Treaty clearly covers both payments for the use simplicitor of or the right to use there is *prima facie*, no conflict between the Act and the DTAA. The A.O. was accordingly directed to pass the assessment order by rejecting objection of assessee.

7. The A.O. took-up the matter for final adjudication in the light of DRP directions. Notice was issued to assessee, but assessee remained ex-parte. The A.O. following the

directions of the DRP held that the receipts of the assessee from an Indian entity during assessment year under appeal are held to be in the nature of 'Royalty Income' taxable in India. The assessment order dated 12.12.2013 was accordingly passed.

8. The assessee is in appeal on the above grounds of appeal. Learned Counsel for the Assessee submitted that it is a sale of software product to IBM India Pvt. Ltd., for limited use. Therefore, sale cannot be treated as Royalty. It was a solitary transaction and that there are several decisions of the Hon'ble Delhi High Court in favour of the assessee which have not been properly appreciated by the DRP and the A.O. He has submitted that decision of the Hon'ble Karnataka High Court heavily relied upon by DRP in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) is not applicable as against the decision of the jurisdictional Delhi High Court. Learned Counsel for the Assessee submitted that recently the ITAT, Delhi Bench in the case of Black Duck Software Inc vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (2017) 86 taxmann.com 62 (Del.)

(Tribu.) considering the similar issue decided the issue in favour of the assessee in the light of various decisions of the Delhi High Court. In the said decision also, the decision of the Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) has been referred to by the Tribunal. In this case, the Tribunal has held that the receipt cannot be taxed under the Treaty as Royalty. He has, therefore, submitted that the Orders of the authorities below may be set aside and addition may be deleted.

9. On the other hand, the Ld. D.R. submitted that the decision of the Tribunal in the case of Black Duck Software Inc. vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (supra), decided on 11.09.2017 and it was not before the authorities below. The Ld. D.R. submitted that the matter may be remitted to the DRP for fresh consideration in the light of decision of the Tribunal relying upon several decisions of the Hon'ble Delhi High Court because the issue was not examined in the light of the above propositions decided in this. Therefore, the facts need further adjudication at the level of the DRP because at the

original stage the DRP has found that decision of Hon'ble Delhi High Court are not applicable in the present case. Therefore, decision of the Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) has been followed by the DRP.

10. After considering the rival submissions, we are of the view that the matter requires reconsideration at the level of the DRP. The assessee claimed that it has entered into an agreement with IBM India Pvt. Limited for supply of software products to IBM India Pvt. Ltd. During the assessment year under appeal, assessee has supplied software amounting to Rs.1,46,00,231/- on limited use basis to IBM. The assessee claimed that sale value is not taxable as the receipt of the same amount is not Royalty in nature under Article 12 of India-USA DTAA. The DRP however relied upon the decision of Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra). The assessee further claimed before the DRP that assessee has sold software license without giving right of reproduction and commercial exploitation. It is a case of

sale. Therefore, in the absence of a P.E, the income emanating from the software license sale is not taxable in India. The assessee also submitted that the A.O. has erred in placing reliance upon the retrospective Amendment to Section 9(1)(vi) of the Act read with Explanation-4 thereof without appreciating the fact that no retrospective Amendment in domestic Law can be read into Treaty. The assessee, therefore, prayed that sale consideration should not be treated as Royalty and as such, its income is not taxable in India. Learned Counsel for the Assessee relied upon the Order of the ITAT, Delhi Bench in the case of Black Duck Software Inc vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (supra) which is passed on 11.09.2017. In this case, during the year under consideration, assessee has sold software under a master license and subsequent agreement to Indian entities. The A.O. took a view that receipts of the assessee pertaining to licensing of software were taxable as Royalty and under section 9(1)(vi) as well as under Article 12(3) of India-USA DTAA. It was noted from the records that assessee had

provided to its customers a non-exclusive, non-transferable license within applicable subscription period. It was also found that the customers were not permitted any access or use of programmes for any users other than the user's license paid for by them. It was, in these circumstances held by the Tribunal that the amount received by the assessee was not liable to tax as Royalty in India. The assessment year involved in the case of Black Duck Software Inc. vs. DCIT, International Taxation, Circle 1(1)(2), New Delhi was A.Y. 2012-2013. However, the appeal under consideration is of A.Y. 2010-2011. The Tribunal decided the issue of the taxability of the receipts on supply of software which has been treated as Royalty. The Tribunal also referred to decision of Hon'ble Karnataka High Court in the case of CIT vs. Samsung Electronics Co. Ltd., (supra) relied upon by DRP and other decisions of the Delhi High Court. The Tribunal after considering the rival submissions found that the sole issue involved in this appeal is, whether the payment received by assessee from supply of software is taxable in India "as royalty in India or not", either under

section 9(1)(vi) or under Article 12(3) of India-USA DTAA or both. The Tribunal on perusal of the scope of license and other material and decisions of the Delhi High Court held in para-22 as under :

“22. Thus, in view of the discussion made above and respectfully following the judgment of Hon'ble Delhi High Court, in the cases of Nokia Networks (supra); Ericsson A.B. (supra); Infrasoftware Ltd. (supra); and Alcatel Lucent Canada (supra)., we hold that the payment received by the assessee does not fall within the ambit of 'royalty' under Article 12(3) of India-USA DTAA and hence, the same cannot be taxed under the terms of India USA Treaty. If the receipts cannot be taxed under the treaty as royalty, then it cannot be taxed under the domestic law under section 9(1)(vi) Income Tax Act and the amended provision cannot be read into treaty as held by the Hon'ble Delhi High Court in aforesaid cases. Accordingly, the appeal of the assessee is allowed.”

11. In the above case, the Tribunal examined the issue on facts in the light of scope of license and decisions of Hon'ble Delhi High Court and others which clearly suggests that the DRP should re-examine the issue afresh in the light of material on record and decision of the Tribunal in the case of Black Duck Software Inc. vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (supra). The Ld. D.R, therefore, rightly suggested that the matter may be remanded to the file of DRP with a direction to re-decide the issue in the light of latest decision of the Tribunal on the subject because the facts shall have to be re-examined in the light of ratio of the decision in the case of Black Duck Software Inc vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (supra). We may also note that assessee did not raise any objection before A.O. because it was an ex-parte order. Considering the above discussion, we set aside the Orders of the authorities below and restore the matter in issue to the file of DRP with a direction to re-decide the above issue by re-examining the Agreement in question and material facts of the case in the light of Order of ITAT, Delhi

Bench in the case of in the case of Black Duck Software Inc vs. DCIT, International Taxation, Circle-1(1)2, New Delhi (supra). The DRP shall give reasonable, sufficient opportunity of being heard to the assessee before passing the Order as per Law.

12. In the result, appeal of Assessee is allowed for statistical purposes.

Order pronounced in the open Court.

Sd/-
(L.P. SAHU)
ACCOUNTANT MEMBER

Sd/-
(BHAVNESH SAINI)
JUDICIAL MEMBER

Delhi, Dated 17th January, 2019

VBP/-

Copy to

1.	The appellant
2.	The respondent
3.	CIT(A) concerned
4.	CIT concerned
5.	D.R. ITAT 'I-2' Bench, Delhi
6.	Guard File.

// BY Order //

Assistant Registrar : ITAT Delhi Benches :
Delhi