

IN THE HIGH COURT OF PUNJAB AND HARYANA AT
CHANDIGARH

ITAs-193-194-197-2015 (O&M)

Date of decision:- 07.08.2015

Pr. Commissioner of Income Tax-2, Chandigarh

...Appellant

Versus

M/s Mobisoft Tele Solutions P. Ltd.

...Respondent

CORAM: HON'BLE MR. JUSTICE S.J. VAZIFDAR, ACTING CHIEF JUSTICE
HON'BLE MR. JUSTICE G.S. SANDHAWALIA

Present: Ms. Urvashi Dhugga, Advocate,
for the appellant.

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S.J. VAZIFDAR, A.C.J. (ORAL)

These appeals are against the orders of the Income Tax Appellate Tribunal dated 28.10.2014 setting aside the order of the CIT (Appeals) for the assessment years 2006-2007, 2007-2008 and 2008-2009.

2. The CIT (Appeals) dismissed the respondent/assessee's appeal against the order of the Assessing Officer adding back the amounts paid by the assessee to one Tarun Mohan by way of royalty for the use of the brand name phoneytunes.com.

3. According to the appellant, the following substantial questions of law arise in these cases:-

(i) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT is justified in holding that royalty payment to a related person would be allowable for business expenditure u/s 37(1) of the Act whereas the same has not been exclusively and wholly incurred for business purposes?

(ii) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT is justified in holding that royalty payment would be allowable business

expenditure u/s 37(1) when the same has not been paid to the owner/holder of the patent, design, copyright and technical know how or to an inventor and where there is no transfer/acquisition of any assets?

(iii) Whether on the facts and in the circumstances of the case and in law, the Hon'ble ITAT is justified in holding that royalty payment would be allowable business expenditure u/s 37(1) inspite of the fact that expenditure on royalty payment is capital in nature?

(iv) Whether on facts and circumstances of the case and in law, the order of the Tribunal is not perverse in holding that the transaction was not a colourable device to reduce the tax liability of the company in which the Managing Director was none other than the beneficiary proprietor of royalty particularly when no evidence of any patented product in possession of the proprietor could be produced and all the stipulations in the agreement showed that it was for the exclusive benefit of the proprietor and also when no proof of brand value of phoneytunes.com was established?

4. The matter is in fact uncomplicated. The said Tarun Mohan is also a Director in the assessee-company. He and his family members are the only share-holders of the assessee-company. The said Tarun Mohan carried on business in the name and style of phoneytunes.com as the sole proprietor thereof. The business comprised of providing value added telecom services to various mobile companies for ring tones, images, wall papers etc. He had entered into agreements with various music companies under which he acquired their rights as also the right to make ring tones on the basis thereof. In turn, he provided individual mobile users the tones through cellular operating companies. He paid royalty to the music companies in consideration of these agreements. He in turn was remunerated by collecting fees from the customers for downloading the ring tones etc. The Tribunal

has come to a finding of fact that the said Tarun Mohan had invented technology through which ring tones can be created of the said songs. Whether it was an invention or not is not relevant. The fact is that he devised the manner of providing the said services. It appears that Tarun Mohan had also registered his copyright in respect of the word 'phoneytunes.com'.

5. On 18.02.2003, Tarun Mohan entered into an agreement with the respondent/assessee. Articles 2 and 3 of the agreement read as under:-

“Article 2 – Transfer

In consideration of the agreement and subject to the terms and conditions hereto, PT hereby agrees to sell, assign, transfer and convey the assets to ITIDA as provided herein and ITIDA would purchase and acquire the assets on and from the closing date subject to the terms and conditions of this agreement. The assets relating to the business which are to be sold, assigned, transferred and conveyed shall include without limitation the following:-

- 1. Fixed assets.*
- 2. All inventories to the extent listed in Schedule-1.*
- 3. The intellectual property rights in the business except the brand name of phoneytunes.com shall be transferred and for using the brand name ITIDA has to pay 2% of gross revenue receipts as royalty after two years of the closing date.*
- 4. All other current assets including cash & bank balances and loans & advances.*

The assets as mentioned above shall be sold, transferred, conveyed and assigned to ITIDA free and clear from any encumbrances, liens, charges, claims, restrictions of whatsoever nature.

Article 3 – Consideration

In consideration of PT agreeing to sell, assign, transfer and convey the assets to ITIDA on the terms and conditions stated in

this agreement, ITIDA shall pay to Mr. Tarun Mohan, sole proprietor of PT a purchase price or consideration of a sum of ₹ 5,81,231/- and in consideration of all intellectual property rights (other than brand name) and for the use of brand name of phoneytunes.com a consideration of 2% of the gross revenue receipts under the relevant business after 2 years of closing date.”

6. It is clear, therefore, that Tarun Mohan retained the brand name phoneytunes.com. He merely permitted the assessee to use the intellectual property right acquired by him, namely, the brand name/trade-mark phoneytunes.com. He had not assigned the same to the assessee, but only licensed the same to the assessee.

7. The Assessing Officer and the CIT (Appeals) wrongly came to the conclusion that Tarun Mohan being a Director of the respondent was not entitled to enter into an agreement for the transfer of his assets to the company. They held that the same person cannot enter into an agreement with himself. This ignores the fundamental concept that the assessee being a company incorporated under the Companies Act, 1956 is a separate legal juristic entity.

8. The Tribunal, therefore, rightly disagreed with this finding. The Tribunal also rightly observed that Tarun Mohan had in any event paid the entire taxes in respect of the royalty received by him. That, however, would not make a difference for if the deduction sought by the assessee is wrongful, the Assessing Officer is bound to disallow the same.

9. The CIT (Appeals) observed that there was no evidence to prove that Tarun Mohan had developed any product for which he had any copyright or trade mark. Firstly, as we noted earlier, he had obtained the copyright in respect of the artistic work comprised in the name phoneytunes.com. Registration of the copyright is, however, not

