IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'C' NEW DELHI

BEFORE SMT DIVA SINGH, JUDICIAL MEMBER
AND
SH.INTURI RAMA RAO, ACCOUNTANT MEMBER

I.T.A .No.-347/Del/2012
(ASSESSMENT YEAR-2003-04)

ADIT Intl. Taxation, 13A, Subhash Road, Aayakar Bhawan, Dehradun-248001. (**APPELLANT)**	vs	HRS Seismic Services Ltd., Earlier known as Hamptson Russel Software Services Ltd., C/o-Price Water House Coper Pvt.Ltd., Plot No.-18A, Nanak Road, Bandra (west), Mumbai-400050 (**RESPONDENT)**

Appellant by	**Sh.A.K.Siroha, CIT DR**
Respondent by	**Sh.Ravi Sharma, Adv.**

Date of Hearing	**20.08.2015**
Date of Pronouncement	**30.09.2015**

ORDER

This is an appeal filed by the Revenue assailing the correctness of the order dated 16.11.2011 of CIT(A)-II, Dehradun pertaining to 2003-04 assessment year on the following grounds:-

1. "Whether on facts and circumstances of the case, the CIT(A) has erred in not deciding the case on the merit.
2. Whether on facts and circumstances of the case, the CIT(A) has erred in quashing the proceedings u/s 147/148 by holding the AO was not justified to reopen the assessment proceedings on the basis of mere change of opinion which is contrary to the facts of the case since the issue of taxing the assessee's income from the grant of non-transferrable license to use software to its client as "Royalty" was not discussed in the original assessment.
3. Whether on facts and circumstances of the case, the CIT(A) had erred in holding that the proceedings initiated u/s 147/148 in the wake of the decision of the Hon'ble High Court in the case of the Forammar France (229ITR438) and explanatory notes to the Finance Bill 2010 were merely change of opinion and did not constitute material to initiate proceedings u/s 147/148, which is contrary to the decision given by the Hon'ble Allahabad High Court in the case of Kartikeya International V/s CIT (228CTR288) in which it was held that any subsequent decision of the Apex court or the jurisdictional High Court did constitute material to form a belief that there is an escaped income and the initiation of proceedings was legal and in accordance with the law.

4. Whether on facts and circumstances of the case, the CIT(A) had erred in quashing the proceedings u/s 147/148 contrary to the decision of the Hon'ble Bombay High Court in the case of the Indo European Breweries Ltd. where in it was held that reopening the assessment were valid despite lapse of 4 years time limit; Finding during subsequent year's assessment constituted 'tangible material 'for reassessment.
5. Whether on facts and circumstances of the case, the CIT(A) has erred in relying upon the decision given by a Single Judge of the Hon'ble Uttarakhand High Court in the case of B.G Services Co. Middle Ease Ltd. (201 Taxman 188)(UK) which has not been accepted by the Department and against which a special petition has been filed before the Division Bench of the same court.
6. The appellant prays for leave to add, amend, modify or alter any grounds of appeal at the time of before the hearing of the appeal."

2. Although the present has been filed by the Revenue however the Ld. AR at the outset submitted that the point at issue is fully covered in assessee's favour and this fact is brought in paras 3.2 & 3.3 of the impugned order itself. Copies of the following judgements and orders of the Tribunal were filed and relied upon in the 32 paged paper book:-

(i) B.J.Services Company Middle East Ltd. vs DDIT (Int. Taxation), Dehradun [201 Taxmann 188] (UK HC);
(ii) ADIT vs Hampson Russell Ltd. Partnership (ITA No.6072-6073 and 6074/Del/2012); and
(iii) CIT and Another vs ONGC {299 ITR 438} [UK HC].

3. On the date of hearing, Ld. Sr. DR sought time to study the decisions. Time was granted and the appeal was adjourned. On the next date, Ld. CIT DR placed reliance on the A.O. No distinguishing fact or circumstance was referred to in order to rebut the claim of the Ld.AR that the issue is conclusively concluded in favour of the assessee.

4. We have heard the rival submissions and perused the material available on record. In the facts of the present case, it is seen that for the following reasons the AO by the order passed u/s 144/147 held that the receipts of the assessee are in the nature of Royalty income covered under the provisions of Section 9(1)(vi) of the Act and hence taxable under section 115A of the Act:-

"The original assessment was completed by the ACTT, Circle 1, Dehradun u/s 143(3) of Income Tax Act, 1961. The assessment was reopened by notice u/s 148 of the IT Act, 1961 issued on 31/03/2010 requiring the assessee to file its return of income for A.Y 2003-04. Despite several notices, to the reasons best known to it the assessee failed to respond. Since the matter is getting barred by limitation, the undersigned is left with no alternative but to proceed with exparte assessment.

2. The assessee has given various services to entities involved in business of Oil Exploration. Such services include supply, upgradation & maintenance of software. The Assessing Officer in its previous assessment order had accepted that such receipts are not taxable without even considering that they may fall in category of Royalties.

3. The assessee entered into an agreements with the Indian customers for the grant of non exclusive, nontransferable license to use the assessee software programs and provisions of related support/ installation. On payment the customers are granted a limited right to use the system.

The software supplied by the assessee is not just another off-the-shelf software available to the customers but is a specially customized software program developed by the assessee which is used in oil & gas industry. In the agreement with the Indian customers the customers are not sold the copies of the programme but granted licences which are not exclusive and nontransferable. The license is granted for usage of software on specific terminals for which license fees is paid by the customer. The amount of license fee changes as per the number of workstations only to the software has been installed. The assessee undertakes the responsibility to configure, maintain and ensure compatibility of the software. The assessee also provides installation & commissioning at an additional charge. The copies and documents, in form of user manuals, made available to the customer remains the property of the assessee.

A Process is a series of actions or steps towards achieving a particular end, whereas a Computer program means a set of instructions expressed in words, codes, schemes or in any other form, including a machine readable medium, capable of causing a computer to perform a particular function to achieve a particular result i.e a Computer Software is a set of computer programs that define a series of actions or steps that must be taken by the Computer Hardware to achieve the desired result. The Computer Software Program therefore defines a process to achieve the result through a set of instructions used to control the elements of hardware. The program is written in a language which can be comprehended by human beings, this is called source code. But when this set of instructions is converted into executable files i.e machine language, they become non-understandable by humans. It is these machine language executables which are provided to the user in form of Computer Software and not the set of instructions expressed in words which could be understood by humans. A software program in machine language or in form of executable files forms a sort of black box which accepts inputs and accordingly generates output by controlling the machine hardware. How the input commands are processed is not known unless one has access to the source code. Thus a software program basically acts as a secret process which processes the input commands of the user. The payment made for right to use of such secret process would definitely take form of 'royalty' as the definition of Royalty in DTAA as well as the Income Tax Act encompasses the right to use of a secret process.

Even otherwise the Computer Program is a process protected as Intellectual Property and the payment made for right to use this process would certainly take the form of royalty.

Without prejudice to anything discussed above, in Income Tax Act, the definition of Royalty is very wide and includes within its sweep, the transfer of rights or license in respect of a patent, invention,

model, design, secret formula or process, or in respect of a copyright, literary, artistic or scientific work, or the imparting of any information concerning technical, industrial, commercial or scientific knowledge or skill. With effect from 01.04.2002 use of any industrial, commercial or scientific equipment is also covered. The computer program forming part of the software falls within the description of literary or scientific work, and license to use of it would fall in definition of 'Royalty'.

A copyright in or over the computer software produced by the applicant is in the nature of an intangible, incorporeal right belonging to the category of intellectual property rights. All intellectual property rights in the licensed programs exclusively belong to the person who develops it. The enjoyment of some or all the rights which the copyright owner has, is necessary to trigger the 'royalty' definition. The present payment falls in territory of Royalties due to these considerations :

a) The use of any right in Intellectual Property even for internal use is nonetheless a business/commercial use and would therefore tantamount to use of copyright.

b) It is clear from the agreement that the product is licensed and not sold. The consideration received is license fee."

4.1. Accordingly considering section 14 of the Copyright Act which defines copy right, the AO rejected the claim of the assessee on the following reasoning:-

"Mere perusal of section 14 of the Copyright Act, 1957 giving definition of Copyright with regard to the software clearly indicates that in case of computer programmes, selling or giving on hire of software for sale or hire any copying of computer programme regardless of whether such copy has been sold or given on hire on earlier occasions constitutes a grant of or right to use copyright. The definition also makes it clear that copy of legally obtained software on an electronic medium which may either be a computer or a network constitutes grants or exercise of a copyright. Neither the Indian Copyright Act, 1957 nor any circular issued by the CBDT makes any distinction between copyright right and copyrighted article and such distinction made in foreign regulations or OECD guidelines are not binding on India and as such cannot be extended to the Indian territory because India being a sovereign state, the laws promulgated by the Indian sovereign should only apply.

c) The software is licensed not sold. The copyright of the software remains with the assessee. However, it allows the use of copyright to the person making payment to it. As per the Indian Copyright Act 1957 as amended in 1994 software are entitled to copyright protection. The developer possesses Copyright in the software, which it can enforce in India if any violation of such right is notices by it. Further the Indian Copyright Act recognizes 'copyright' as doing or authorizing the doing of any of the following acts in respect of a work or any substantial part thereof namely, - in case of a computer programme to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer program. It is therefore clear that the assessee has authorized to use of the copyright to the customer in India.

d) The software owned by the developer is patented software. Consideration for allowing the use of the patented article falls within the definition or royalty payment. Even if it is considered that the

software owned has not been patented, there is no denial of the fact that it is essentially an invention. The development of such software requires highly technical manpower, with highly sophisticated infrastructure and huge investments. Similarly the software can also be considered as a scientific work. Therefore, the software can also be said to be information developed out of scientific experience. The payment made for right to use of such item would certainly constitute royalty.

e) As per provisions of section 9(l)(vi) the royalty income should satisfy twin conditions that there has to be consideration, and this consideration should be for transfer of all or any right (including the granting of the licence) in respect of the copyright, patent, invention, design, secret formula or process, scientific work. In this case the payment under software license agreement has fulfilled both the conditions and the income from software license was taxable in India as royalty.

f) As per provision of section 9 the payment made for import of software are royalty payment and the only exception provided is in the form of second proviso to section 9(l)(vi) of the Act which excludes such royalty income from purview of section 9(l)(vi) only when the computer software is supplied by a non-resident manufacturer along with computer or computer based equipment under any scheme approved under the policy of computer software export, software development and training 1986 of the Government of India. However, this exception is not applicable to the facts of this case where appellant had granted software licence to various Indian customers.

g) The characterization taxability of income from import of software has been made amply clear in the Income-tax Act through section 1I5A of the Act which specifically refers to cases where royalties are paid to non-resident for the transfer of all or any right (including the granting of the license) in respect of any computer software to a person resident in India.

h) A copy of software supplied by the appellant did not amount to a sale but it is a licence to use the software. This is because software is an intellectual property right (IPR) which can be licensed to one user and can be given further to any number of user. In other words the IPR in software still remain intact with the supplier. The "sales treatment" of computer software under sales tax law, does not, per se, influence income-tax treatment of software transactions, as income-tax law defines this transaction differently. Therefore the license of mere usage is a sort of lease of software and thus the software has been merely given on rental and the payment received against it would constitute royalty.

i) OECD recommendations remain mere recommendations unless they are incorporated into domestic law and/or DTAAs. The distinction between "copyright right" and "program copy" recommended by the OECD has been dissented from even by several member States not to speak of India which is not even a member of the OECD. Indian laws and India's DTAA recognize only two types of transactions in respect of computer software: sale and licence (letting). No further dissection of

licensing (on the lines of the OECD commentary) is permitted under the Indian Copyright Act, Income-tax Act and Indian DTAAs. Therefore, notwithstanding attractive phraseology and nomenclature, any computer software licence fees, where the vendor retains ownership and grants user rights only to the licensee are, without an iota of doubt, taxable as 'royalties, having an Indian source.

The next is whether the receipts from installation, maintenance and commissioning under the head royalties. Even if such installation and commissioning is a part of the contract, it is included in the cost of licensing of the software. Thus such receipt would invariably be the part of supply of software and would come under the purview of royalty. Such gross receipts would be taxable @20%u/s 115A."

4.1.1. Accordingly the taxable income of the assessee was computed in the following manner as under:-

4. "With the above comments the tax of the assessee is being calculated as under:
Gross receipts taxable as FTS @20% $ 68,746.66 = Rs 30,93,600 (@45)"

4.2. In appeal before the CIT(A apart from various other arguments on jurisdiction it was also pleaded that the appeal of the assessee deserved tobe allowed on the basis of the decision of the Hon'ble Uttarakhand High Court in the case of B.J. Services Company Middle East Ltd. vs DDIT (Int. Taxation), Dehradun [201 Taxmann 188] (UK HC) which on similar facts has held that it amounted to a change of opinion.

4.3. Considering the said plea, the Ld. CIT(A) allowed the appeal of the assessee holding as under:-

3.2 "The facts on this issue are that the original assessment was completed by the ACIT, Circle-1, Dehradun u/s 143(3) of the Act. Thereafter a notice u/s 148 of the Act was issued on 31.03.2010. The reasons recorded by the Id. AO (copy has been placed on record) show that the reopening has taken place due to the contention that the appellant's income is taxable as Fees for Technical Services considering the judgement in the case of CIT vs. ONGC (as agent for Foramer France) reported in 299 ITR 438 (UK) and the insertion of proviso to section 44DA(1) of the Act through the Finance Act, 2010. While the case laws cited by the Id. AR may have some bearing on the issue at hand, it is seen that the recent judgement in the case of B.J.Services (supra) is squarely applicable on the facts of this case. The head notes of this case law are reproduced as under:-

> *"Section 147, read with section 9, 44BB and 44DA, of the Income-tax Act, 1961 -Income escaping assessment - Non-disclosure of primary facts - Assessment year 2003-04 - Whether reassessment can be initiated on a mere change of opinion to merely re-examine an issue on basis of information or material which was already available to Assessing Officer at time of completion of original assessment - Held, no - Whether*

subsequent pronouncement by a Court or a Superior Court entitle Assessing Officer to reopen assessment proceedings on ground that Assessing Officer has reasons to believe that income has escaped assessment or that assessee has not fully and truly disclosed all material facts -Held, no - Assessee, a British company, was engaged in business of providing services and facilities in connection with exploration and extraction as well as production of mineral oil - For relevant assessment year, it offered its gross revenue to be taxed under section 44BB - Assessing Officer, after examining return of income and other documents and replies filed by assessee and after applying its mind, issued an assessment order under section 143 (3) - After a lapse of more than four years. Assessing Officer issued notice under section 148 proposing to reassess assessee 's income on grounds that assessee's income was liable to be taxed as a fee for technical services in view of decision of Uttaranchal High Cowl in case of CIT v. O.N.G.C. [2008] 299 ITR 438 ; and that in view of Explanatory Note to Finance Bill, 2010, combined effect of provisions of sections 44BB, 44DA and 115A is that if income of a non-resident is in nature of fee for technical services, it is taxable under provision of section 44DA or section 115A irrespective of business to which it relates - Whether when under existing provisions contained in sections 44BB. 44D, 115A and Explanation II of section 9(1)(vii). it was open to Assessing Officer to tax assessee either under section 44BB or 44D or under section 9(1)(vii) on basis of material produced before him and Assessing Officer, after due enquiry and verification and after applying mind to facts of case, came to conclusion that assessee was liable to be taxed under section 44BB, reopening of assessment on basis of subsequent decision of High Court was unjustified - Held, yes.
Section 44BB of the Income-tax Act. 1961 - Mineral oil, special provisions for computation in case of business exploration - Whether amendments to sections 44BB and 44DA by Finance Act, 2010 would take effect from 1-4-2011 and would apply in relation to assessment year 2011-12 and subsequent years - Held, yes [in favour of assessee]"

3.3. Since the above mentioned case of the jurisdictional High Court is squarely applicable on the facts of this case, the proceedings emanating through issue of notice u/s 148 of the Act are hereby quashed. Since the first ground has been accepted there is no adjudication on the merits of this case and the rest of the grounds are not decided."

5. Aggrieved by this, the Revenue is in appeal before the Tribunal. Before us, the Ld. AR apart from relying upon the judgement of the Single judge of the Hon'ble Uttarakhand High Court dated 20.08.2011 in the case of B.J. Services Company Middle East Ltd. & Others has placed on record a later judgement of the Hon'ble Uttarakhand High Court dated 07.07.2014 in Al Mansoori Specialized Engineer and other batch of appeals where the Hon'ble Court in the

absence of any contrary decision was pleased to follow the decision in the case of B.J.Services Company Middle East Ltd.(cited supra). Apart from that order of the Co-ordinate Bench dated 11.09.2013 in the case of ADIT vs Hampson Russel Ltd. Partnership (cited supra) has been relied taking a similar. In the absence of any contrary fact, circumstance or argument, we find no infirmity in the finding of the Ld.CIT(A). Accordingly for the reasons given herein above the departmental appeal is dismissed.

6. In the result, the appeal of the Revenue is dismissed.

The order is pronounced in the open court on 30th of September, 2015.

Sd/- **Sd/-**

(INTURI RAMA RAO) **(DIVA SINGH)**
ACCOUNTANT MEMBER **JUDICIAL MEMBER**

Dated:30/09/2015
Amit Kumar

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR
ITAT NEW DELHI