

IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH, 'C' PUNE

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S. VISWANETHRA RAVI, JUDICIAL MEMBER

आयकर अपील सं. / ITA No.145/PUN/2021
निर्धारण वर्ष / Assessment Year : 2016-17

Husco International Inc., A4, Talegaon Dabhade Industrial Area, Taluka Maval – 410507 Maharashtra-India PAN : AABCH9478D	Vs.	ACIT (IT), Circle-1, Pune
Appellant		Respondent

Assessee by Shri Rahul Charkha
Revenue by Shri Anurag Srivastava

Date of hearing 24-09-2021
Date of pronouncement 27-09-2021

आदेश / ORDER

PER R.S.SYAL, VP :

This appeal by the assessee is directed against the final assessment order dated 05-03-2021 passed by the Assessing Officer (AO) u/s.143(3) r.w.s.144C(13) of the Income-tax Act, 1961 (hereinafter also called 'the Act') in relation to the assessment year 2016-17.

2. Briefly stated, the facts of the case are that the assessee is a company incorporated in the USA. It is engaged in the development and manufacture of hydraulic and electro hydraulic and electro-hydraulic controls for off-highway and automotive applications. The

assessee assists Original Equipment Manufacturers (OEMs) throughout the product development process. A return was filed declaring certain international transactions. The AO made a reference to the Transfer Pricing Officer (TPO) for determining the Arm's Length Price (ALP) of the international transactions. The TPO accepted all the transactions at ALP. During the course of draft assessment proceedings, the AO observed that total receipts of the assessee from Indian operations amounted to Rs.30,40,10,666/-, against which it had shown only receipts of Rs.6.29 crore as income. The assessee was show caused as to why the remaining revenue amounting to Rs.24,10,95,476/- be not charged to tax. In the absence of any detail or explanation forthcoming from the side of the assessee, the AO held the remaining amount of Rs.24.10 crore as receipts in the nature of Royalty/Fees for Technical Services (FTS) within the meaning of section 9(1)(vi)/9(1)(vii) and added it to the total income. The assessee approached the Dispute Resolution Panel (DRP) which allowed relief in respect of some of the items of revenue. For the remaining items of the revenue, the assessee has come up in appeal before the Tribunal.

3. We have heard the rival submissions and gone through the relevant material on record. The four items of revenue included by

the AO in the total income which have been assailed in the extant appeal are as under:

- i. Capital goods sales – Rs.96,58,128/-
- ii. Reimbursement of travelling, freight and other – Rs.12,68,764/-
- iii. Reimbursement of internet charges (received)– Rs.30,31,448/-
- iv. Allocation of insurance charges (received) – Rs.1,62,666/-

4. We espouse the above items *ad seriatim* for consideration and decision. The first item of sale of capital goods amounting to Rs.96,58,128/- has two components, namely, revenue from software licenses amounting to Rs.86,55,225/-; and revenue from sale of other capital goods amounting to Rs.10,02,903/-. Insofar as the revenue from software licenses is concerned, the assessee claimed before the DRP that it centrally negotiated and procured standardized software from third party vendors for its own use as well as other group entities globally. It was put forth that the allocation of such costs was done between the group entities on cost-to-cost basis without any mark up. Copies of invoices of third party vendors were produced as additional evidence. The DRP called for a remand report from the AO with reference to such additional evidence. The AO in his remand report submitted that the assessee's contention of the amount being in the nature of reimbursement of expenses was not tenable. He further opined that the issue of software licenses was disputed and pending before the Hon'ble Supreme Court and hence

the amount in question was held to be taxable as royalty. The assessee reiterated its contention that the amount paid by it to the third parties was cross charged as software cost to its group entities including the Indian entity for a sum of Rs.86.55 lakh. In the light of certain decisions including *CIT Vs. Samsung Electronics Company Ltd. (2010) 320 ITR 209 (Karnataka)*, the DRP held that the amount received by the assessee from its Indian counterpart was in the nature of Royalty and hence taxable. It also rejected the assessee's contention of reimbursement and held the amount chargeable to tax u/s.9(1)(vi) of the Act read with Explanations 4, 5 and 6 thereto along with the provisions of the Double Taxation Avoidance Agreement between India and the USA (DTAA).

5. Break-up of total software charges paid by the assessee to third party vendors and that recovered from its entities globally is available at page 24 of the written submissions, which reads as under:

Detailed working of software license cost of UDS 1,35,090 allocated by the Appellant to Husco India

Date	Name of Vendor	Doc No.	PO number	Amount of invoice (USD)	Paper book reference number
4-Nov-14	PTC Inc	55037910	384945	368,886	ITAT-1929 and ITAT 1939 to ITAT-1940
4-Nov-14	PTC Inc	55037910	384945	18,813	

12-Nov-14	Product Space Solutions Inc.	55037934	384987	11,750	ITAT-1931
13-Nov-14	CDW Computer Centers Inc.	55037936	384995	1,186	ITAT-1936
13-Nov-14	CDW Computer Centers Inc.	55037936	384995	784	
13-Nov-14	CDW Computer Centers Inc.	55037936	384995	795	
13-Nov-14	CDW Computer Centers Inc.	55037936	384995	144	
12-Sep-14	Product Space Solutions Inc.,	55038026	385037	11,750	ITAT-1932
2-March-15	Product Space Solutions Inc.,	55038354	385110	11,750	ITAT-1933
20-Mar-15	Product Space Solutions Inc.,	55038306	385143	11,750	ITAT-1934
30-Apr-14	Trainer expense	18003822	NA	313	ITAT-1945
15-Jan-15	Trainer expense	25018692	NA	5,177	ITAT-1945
	Total			443,098	
	Entity name	Allocation Key No. of employees	Allocation	Total (USD)	
	HUS	32	172,916.16	172,916.16	ITAT-1921
	Auto WK	10	54,036.30	54,036.30	
	HIL	12	64,843.56	64,843.56	
	HCP	3	16,210.89	16,210.89	
	HIP (INDIA) Invoice No. HIP2015023 dated May 30, 2015	25	135,090.75	135,090.75	ITAT-1919
		82			
	Total			443,098	

6. The figures in the above table are given in the US dollars. It can be seen that the assessee incurred total software expenses at 4,43,098 US dollars and recovered the equal amount from its group entities without any mark up with the share of the Indian entity standing at 1,35,090.75 US dollars, which is equivalent to Rs.86.55 lakh under consideration. The first major item of spending in the

above Table is purchase of software from PTC Inc. A copy of the invoice has been placed at page 1929 of the paper book. PTC Inc. raised this invoice on the assessee in the USA. Under the 'Invoice Description' column, the details have been given about the nature and quantity of each software product licensed to the assessee. For example, item at Sl.No.1 is PKG-3504G-F: Creo Engineer II with Advanced Assembly Global and number of licenses sold to the assessee are nine. Next item is MNT-3504GF-T2: Support For: Creo Engineer II with Advanced Assembly Global and number of licenses sold is again nine. There is another item with sale of sixty licenses given at Sl.No.8 as MNT-CPE5065F- T2: Support for:PTC PLM View and Print Only License. The last item in the invoice is one hundred twenty licenses of MNT-CPE5049F-T2: Support for: Windchill PDMLink-Heavy User License. Pages 25 to 29 contain terms of 'PTC Software Product Licensing Basis'. The term "Concurrent User" (CU) has been defined to mean "Each Concurrent User product license may be used by one individual person at any given time". The clause with the heading 'Global License' states: "A 'Global License' allows the Customer to install, operate and use such Licensed Product at any of the Customer's site(s) throughout the world, notwithstanding any restrictions in the License Agreement in

relation to limiting use of Licensed Products to the country of installation, but subject to compliance with all applicable export laws and regulations”. Similar is the position regarding other invoices raised by the third party vendors, namely, Product Space Solutions and CDW Computer Centers Inc. Pattern of invoices from the three companies indicates that a specific number of licenses of each software product were purchased by the assessee without acquiring any copyright therein and it was allowed user of such licenses by its group entities including India for which it got reimbursement of cost. Thus it is obvious that the licensors permitted the assessee only to install, operate and use their software products to the extent of copies purchased by it.

7. The primary contention of the assessee has been that the receipt is in the nature of reimbursement and hence not taxable. In principle, chargeability is attracted on the income element embedded in a revenue receipt. A receipt *de hors* profit element, which is only Reimbursement, is not taxable. However, we need to examine from the facts if it is really a case of Reimbursement. The assessee made factual submission before the DRP, as has been reproduced on page 23 of its Direction, to the effect that: `Husco USA centrally negotiates and procures standardized software from third party

vendors, without any customization or modification, for the use of self and for use by Husco group entities globally and *distributes the same to the group/affiliate companies as per their requirement*’. When the DRP sent the relevant material to the AO for his comments, which have tabulated on page 28 of the Direction, the AO, did not approve the contention of Reimbursement. The assessee in response to the AO’s comments, as extracted on the same page in tabular form, stated: ‘The appellant had paid such amount to third parties for expenses incurred on behalf of the Indian group entity which was later on cross charged at actual cost basis to the Indian group entity.’ From the stand of the assessee taken before the AO/DRP, it is evident that it set up a case that it purchased certain number of licenses of different software and charged, *inter alia*, the Indian entity for the licenses issued to the latter. However, page 24 of the written submissions before the Tribunal as extracted *supra* narrates a different story. It demonstrates that the costs incurred by the assessee on all the software products purchased from PTC Inc. and two other vendors were aggregated and such total invoice value was allocated between five entities including the assessee itself on the basis of number of employees of each entity. A fortiori, it is a case of ‘allocation’ of the aggregated costs on the basis of number of

employees and not `reimbursement`. The patent reason is the missing of one-to-one link between the cost of purchase of the software for the Indian entity and its, as such, recovery, which is a condition precedent for `reimbursement`. Had it been a case of the assessee purchasing a particular number of software licenses from the vendors and then transferring them at the identical price to the Indian entity, it would have amounted to reimbursement. The manner of charging done by the assessee runs contrary to the concept of reimbursement. The contention of the assessee that it cross-charged all the entities without any mark-up does not advance the case any further. Insofar as the Indian taxability of a non-resident is concerned, it is only the amount of revenue from India which matters and not what the non-resident earns from its group entities situated in other countries. Even if allocation of combined cost is without any mark-up, it need not necessarily be reimbursement *qua* each participant individually.

8. From the above Table, it can be seen that the assessee incurred total costs at 4,43,098 USDs for which vendors invoices have been placed on record. Such amount has been cross charged to five entities including self and the Indian entity. The charge to the Indian entity is 1,35,090.56 USDs (about 30% of total cost) on the basis of proportion of number of its employees to the total employees of five

entities taken together. It is not a case of identical recovery of the exact cost of the designated number of software purchased and transferred to the Indian entity. The very fact that the Indian entity has been charged on the basis of number of employees, divorced from the actual number of software products transferred to it, amply proves that there is no one-to-one correlation between the out-go and in-come of the assessee on this score, thereby jeopardising the concept of Reimbursement. If the Indian entity is charged higher or lower than what is actually due from it with the corresponding downward or upward adjustment in the share of allocation to the entities situated in other foreign destinations, the dented share of revenue from the Indian entity will affect the Indian income tax due from the non-resident assessee notwithstanding the fact that its overall cost recharge remains without any mark-up. For the foregoing reasons, we are not inclined to countenance the contention of 'Reimbursement', which is hereby repelled.

9. We have noted above the assessee's contention that it purchased a certain number of different software products and transferred some of them to the Indian entity at the same cost and hence no taxable event occurred. The AO, apart from not accepting the contention of reimbursement, observed that: 'Further, one of the

transaction pertaining to software of Rs.86,55,225 is a disputed matter and pending before the Hon'ble Supreme Court. Given the stand of the department, the said amount should be considered as royalty income taxable in the hands of the assessee'. The DRP held the receipt to be in the nature of 'Royalty' by relying on the *Samsung Electronics (Karn)*. Thus it is established that the authorities below have treated the amount charged from the Indian entity as royalty in the hands of the assessee on account of transfer of software licenses to the former. For doing this, they relied on the judgments, *inter alia*, *Samsung (Karn)(supra)*. The question whether the transfer of computer software partakes of the character of Royalties recently came up for consideration before the Hon'ble Supreme Court in *Engineering Analysis Centre of Excellence Pvt. Ltd. Vs. CIT (2021) 432 ITR 472 (SC)*. After analyzing the identical issue in the backdrop of similar expression as used in Article 12(3) of the DTAA, it has been held that ownership of copyright in a work is different from the ownership of the physical material in which the copyrighted work may happen to be embodied. Parting with copyright entails parting with the right to do any of the acts mentioned in section 14 of the Copyright Act. Where the core of a transaction is to authorize the end-user to have access to and make use of the "licensed" computer

software product over which the licensee has no exclusive rights, no copyright is parted with.

10. Adverting to the facts as obtaining in the instant case, it is seen that the assessee acquired only a limited right of user in respect of specific software products from PTC Inc. and two other vendors, which are in the nature of copyrighted articles. As such, there cannot possibly be a situation of it passing on the copyright in them to its group entities. It hardly needs to be accentuated that no one can transfer a better right in a product than he himself has. Since the assessee itself obtained only a limited access to the software products *de hors* the right to copy the same, the *sequitur* is that it could not have transferred anything more than that to its entities globally including India. Ergo, there can be no question of treating the amount received from the Indian entity on transfer of copyrighted articles as Royalty in the hands of the assessee within the meaning of Article 12(3) of the DTAA. Respectfully following the *ratio decidendi* in the case of *Engineering Analysis Centre of Excellence Pvt. Ltd. (supra)*, we hold that the authorities below were not justified in including the amount in question in the total income of the assessee as Royalty by relying on the judgment in the case of *Samsung (Karn)(supra)*, which is no more a good law after the

advent of the *Engineering Analysis (SC)(supra)*. Resultantly, the receipt is held to be not taxable notwithstanding the rejection of the contention of Reimbursement.

11. The next moot question is that if the receipt from the Indian entity is not Royalty, can it be charged to tax as regular business income? Article 7 of the DTAA deals with 'Business profits'. In order to bring any business profit within the fold of total income, it is *sine qua non* that the assessee must have a permanent establishment in India. Absent any permanent establishment of an assessee in India, the receipt cannot be included in the total income on that score.

12. It is worthwhile to mention that the assessee made sale of finished goods in India including the first transaction of Rs.7.21 crore and odd as taken note by the AO on page 7 of the draft order. The DRP excluded it from the total income after receiving remand report from the AO accepting that the assessee did not have any permanent establishment in India. The same *raison d'être* applies here also and hence the amount of Rs.86,55,225 cannot be charged as Business profits as well under the DTAA. In the final analysis, the receipt of Rs.86,55,225 is not chargeable to tax.

13. The second component of this receipt is revenue from other capital goods amounting to Rs.10,02,903/-. The AO included this

amount in the total income of the assessee. The DRP allowed relief to the extent of Rs.4,31,870/- . The assessee is in appeal against the confirmation of disallowance of Rs.5,71,033/- towards procurement and supply of capital goods. Ground no. 8 raised in this regard was not pressed by the ld. AR. The same is, therefore, dismissed as not pressed.

14. The next issue raised in this appeal is against the taxability of Reimbursement of Travelling, Freight and other charges amounting to Rs.12,68,764/-. The assessee contended before the DRP that it was a mere case of reimbursement of Travelling and related expenses incurred on behalf of its Indian entity without any mark up and hence the same did not constitute its income. The DRP did not accept the assessee's version on the ground that there was no evidence of reimbursement.

15. We have gone through the details of Travelling and Freight expenses incurred by the assessee and recovered from various group entities including the one in India. Such copious details have been placed at page 43 of the written submissions. The first major amount is payment to M/s Crystal Migration Services Corporation totaling to 8,880 USD. A copy of the invoice raised by M/s Crystal Migration Services Corporation is available at page 1952 of the paper book.

Immediately next page of the paper book contains break-up of such charges. Seven employees of the Indian entity availed this benefit whose names along with the amount charged by M/s Crystal Migration Services Corporation have been given on the next page totaling 1920 USDs. It is this amount that has been charged to the Indian entity. The next invoice is of GO Riteway Transportation group with total 5,655.85 USDs. A copy of such invoice has been placed at page 1960 of the paper book. Details on the invoice indicate three employees of the Indian entity and the charge is towards their transportation. The amount pertaining to only these three employees has been recovered as such from the Indian entity. Again, there is another invoice of GO Riteway Transportation at page 1963 of the paper book with value of 8,898.04 USDs. Employees of the Indian entity have been named at two places in such an invoice. The exact amount as charged by GO Riteway Transportation group from the assessee has been recovered from the Indian entity. This invoice is also for transportation. Similar is the position regarding other invoices which are in relation to Lodging and Boarding of Indian employees recovered from the Indian entity without any profit element. In view of the above discussion, it is clear that one-to-one link is overtly established between the amount

paid by the assessee to third party vendors and that recovered from the Indian entity, which is evidently without any mark up. As it is only reimbursement of cost not containing any profit element, there can be no question of including such receipts in the total income of the assessee. This issue is determined in favour of the assessee.

16. The next issue is against the inclusion of Reimbursement of Internet charges from the Indian entity to the tune of Rs.30,31,448/-. The AO included such amount in the total income as per the draft order. The assessee assailed the same before the DRP, which rejected the assessee's contention by observing that no evidence was furnished.

17. We have gone through the material on record. The assessee has placed a tabulation of sample invoices of Internet charges allocated by it to the Indian entity on page 44 of the written submissions. A vendor called Verizon raised invoices on the assessee, sample of which have been placed at page 2008 to 2022 of the paper book. These invoices distinctly point out 'Location/Service Index', namely, the user. Indian address with the exact amount of charge has been mentioned, which has been recovered. Thus it is evident that it is not a case of cost sharing of total costs between all the entities on some allocation key but charging the exact amount

paid for the Indian entity. This indicates that the assessee paid the amount in question to Verizon for internet access and then recovered it from the Indian entity as such without any mark up. As it is also a case of reimbursement, there cannot be any question of including it in the total income of the assessee. We, therefore, order to exclude Rs.30,31,448/- from the total income of the assessee on this score. The assessee succeeds.

18. Another issue raised in this appeal is against the rate of tax at which the income declared by the assessee has been charged. The facts apropos this issue are that the assessee filed its return declaring total income of Rs.6,29,15,190/-. A copy of such return has been placed at page 10 onwards of the paper book. Detail of the income has been given therein under the head 'Revenue earned by the Company', which consists of Royalty; Allocation of management charges; Installation of capital goods; Insurance charges; Engineering charges; Software charges; and Interest income of Rs.27,64,952/-. The interest income was separately offered for taxation. We are concerned only about the rate at which the remaining income of Rs.6,01,50,239/- should be charged to tax. The assessee offered such income under Article 12 of the DTAA @15%. Schedule OS of the Income-tax return with the caption 'Income from other sources',

fairly indicates that the assessee offered such income of Rs.6.01 crore as “Income from Royalty and Technical services”. The AO taxed such income at the offered tax rate of 15% in the draft order. The assessee contended before the DRP that the income of Rs.6.01 crore was wrongly offered for taxation at 15% as per the provisions of the DTAA and the same should be charged to tax at lower rate of 10% plus surcharge and cess as per section 115A of the Act. The DRP, relying on the judgment of Hon’ble Supreme Court in *Goetz (India) Ltd. Vs. CIT (2006) 284 ITR 323 (SC)*, held that the claim of the assessee was not maintainable because it had not filed a revised return with the correct rate of tax. That is how, the assessee is aggrieved by the taxation of Rs.6.01 crore @15%.

19. Section 115A(1)(b)(A) & (B), as amended by the Finance Act, 2015 w.e.f. 01-04-2016, prescribes the rate of tax at 10% on income of a non-resident by way of royalty and fees for technical services. Prior to that, the rate of tax under these provisions was 20% and 25% respectively. On the other hand, the DTAA prescribes the rate of tax of Royalty and FTS at 15%. The assessee did not notice the change in the rate of tax coming into force from the A.Y. 2016-17 under consideration for the first time. Since the rate of tax as per the DTAA was beneficial than the old rate as per section 115A, the assessee

filed its return with the rate as per the DTAA. Later on, the mistake was realized and the claim was lodged, which came to be repelled. Nature of income under consideration as Royalty/Fees for technical services is not disputed. The rate of tax under the Act on such income for the year got slashed to 10%. Section 90(2) of the Act clearly enunciates that where the Central Government has entered into a DTAA then “*the provisions of this Act shall apply to this extent they are more beneficial*” to the assessee. It means that if the provisions of the Act favour the assessee over those of the DTAA, it can opt for the former. No exception can be taken to the assessee exercising the option of being governed by the rate of tax under the Act. The authorities below have rejected the assessee’s claim on the ground that it was not made in the income tax return. In our opinion, there can be no estoppel against the provisions of the Act. The purpose of an assessment is to determine the correct amount of income and tax payable thereon. If the Act provides for soft-peddling, then that cannot be whisked away by the Officers. As it is a matter of exercising the option and the assessee did it in a particular way which was more beneficial to it albeit during the course of the assessment proceedings itself, the claim ought not to have been denied. Be that as it may, even though the judgment in *Goetze*

(*supra*) provides that the AO has no power to entertain claim made otherwise than by way of a revised return, it unequivocally provides: 'that the issue in this case is limited to the power of the assessing authority and does not impinge on the power of the Tribunal under s. 254 of the IT Act, 1961'. Thus it is evident, that there is no such constraint on the power of the Tribunal and it can grant rightful relief on a point for which no claim was made in the return of income. We, therefore, hold that no fault can be found with the assessee exercising the option as per section 90(2) of the Act to be governed by the reduced rate of tax of 10% plus surcharge etc. in terms of section 115A of the Act. It is, therefore, directed that tax be charged on the declared income of the assessee from Royalty and FTS at 10% under the Act.

20. Ground No.7 about insurance charges was not pressed, which is hereby dismissed. Other grounds are either consequential or premature.

21. In the result, the appeal is partly allowed.

Order pronounced in the Open Court on 27th September, 2021.

Sd/-
(S.S. VISWANETHRA RAVI)
JUDICIAL MEMBER

Sd/-
(R.S.SYAL)
VICE PRESIDENT

पुणे Pune; दिनांक Dated : 27th September, 2021
सतीश

आदेश की प्रतिलिपि □ ग्रेषित/Copy of the Order is forwarded to:

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The DRP-3, Mumbai-1/ DRP-3, Mumbai-2/
DRP-3, Mumbai-3/
3. The CIT(IT & TP), Pune
4. DR, ITAT, 'C' Bench, Pune
5. गार्ड फाईल / Guard file.

आदेशानुसार/ BY ORDER,

// True Copy //

Senior Private Secretary
आयकर अपीलीय अधिकरण ,पुणे / ITAT, Pune

		Date	
1.	Draft dictated on	24-09-2021	Sr.PS
2.	Draft placed before author	27-09-2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

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