

IN THE INCOME TAX APPELLATE TRIBUNAL,
BANGALORE BENCH 'B'

BEFORE SHRI JASON P BOAZ, ACCOUNTANT MEMBER AND
SHRI N V VASUDEVAN, JUDICIAL MEMBER

ITA No.549/Bang/2011
(Asst. year 2005-06)

M/s Synopsys International Limited, RMZ Infinity, Tower A, 4 th & 5 th Floor, Municipal No.3, Old Madras Road, Benniganahalli, Bangalore-16. PA No. AAJCS 6844 A	vs	The Deputy Director of Income-tax (International Taxation) Circle-11(1), Bangalore.
(Appellant)		(Respondent)

Date of Hearing	:	7.11.2012
Date of Pronouncement	:	10.12.2012

Appellant by	:	Shri K P Kumar, Advocate
Respondent by	:	Shri Farhat Hussain Quereshi, CIT-II

ORDER

PER JASON P BOAZ :

This appeal by the assessee is directed against the order of the CIT (A)-IV, Bangalore, dated 25.02.2011 for the assessment year 2005-06.

2. The facts of the case, in brief, are as under:

2.1 The assessee is a foreign company incorporated under the laws of Ireland, engaged in the business of sales and marketing of software licenses in India and provision of ancillary services like consultancy, support, training, inspection and installation. The record indicates that the assessee

filed its return of income for the assessment year 2005-06 declaring NIL income pursuant to the issue of notice under section 148 of the I T Act, 1961 (hereinafter referred to as 'the Act') by the Assessing Officer on 5/4/2007. The assessment was completed by an order under section 143(3) rws 148 of the Act on 29/12/2008 in which the assessee's taxable income was determined at Rs.7,47,22,046/- on account of the Assessing Officer's finding hat the income from software supplied by the assessee would be chargeable to tax as Royalty.

2.2 Aggrieved by the order of assessment for the assessment year 2004-05 dated 29/12/2008, the assessee went in appeal before the CIT(A)-IV, Bangalore. The learned CIT(A) disposed off the appeal dismissing it except to the extent of adoption of rate of tax of 10% as against 15% adopted by the Assessing Officer.

3.0 Aggrieved by the order of the learned CIT(A)-IV, Bangalore dated 25/2/2011 for the assessment year 2005-06, the assessee is now before the Tribunal, In the ground raised, the assessee has submitted as under:-

1. Assessment bad in law and on facts

- The learned CIT(A) erred in not holding that the order of the Deputy Director of Income-tax (International Taxation), Circle-1(1), Bangalore ('DDIT' or 'Assessing Officer') is bad in law and on facts.

- The CIT(A) erred in concluding that the reassessment proceedings initiated upon the appellant were valid. The CIT(A) ought to have appreciated that the reassessment proceedings initiated under section 148 of the Act by the DDIT was invalid and without jurisdiction.

2. Erroneous demands

The DDIT erred in :

- a) Determining the total income of the appellant at Rs.74,722,046/-;
- b) Levying income-tax of Rs.74,72,205; and
- c) Levying interest under section 234B of the Act of Rs.16,83,045/-.

3. Erroneous treatment of the receipts from Indian customers as royalty

- 3.1 The DDIT/CIT(A) erred in holding that the payments received by the appellant are 'royalty' under the Income-tax Act, 1961 ('the Act').
- 3.2 The DDIT/CIT(A) erred in not holding that the payments received by the appellant do not qualify as 'royalty' under the Double Taxation Avoidance Agreement between India and Ireland ('the DTAA').
- 3.3 The DDIT/CIT(A) erred in not holding that whether the payments received by the appellant from Indian parties was in the nature of royalty had most appropriately to be judged under clause (v) of Explanation 2 to section 9(1)(vi) of the Act, which clause did not apply because there was no right in respect of any copyright granted by the appellant.

- 3.4 The DDIT/CIT(A) erred in holding that the payments received by the appellant from Indian parties was towards the use of 'process' within the meaning of clause (iii) of Explanation 2 to section 9(1)(vi) of the Act, and accordingly, are 'royalty' as defined in section 9(1)(vi) of the Act.
- 3.5 The DDIT/CIT(A) erred in not holding that, as the appellant did not give the right to Indian customers to reproduce and distribute to the public the copyrighted programme, the payments received by the appellant could not be construed as 'royalty'.
- 3.6 The DDIT/CIT(A) erred in not holding that, as the payment received by the appellant from Indian customers was not to be measured by reference to the productivity or use of the software, it could not be construed as 'royalty'.
- 3.7 The DDIT/CIT(A) erred in holding that software is not 'goods'.
- 3.8 The DDIT/CIT(A) erred in not appreciating the reliance placed by the appellant on the decisions in the following cases:-

- *Motorola Inc. v Deputy Commissioner of Income Tax (2005) 95 ITD 269 (Delhi) (SB);*
- *Samsung Electronics Co. Ltd. v ITO (2005) 94 ITD 91 (Bang.);*
- *Sonata Information Technology Limited v ACIT (2006) 103 ITD 324 (Bang.);*
- *Infrasoft Limited v ADIT (2009) 28 SOT 179 (ITAT-Delhi);*
- *Velankani Mauritius Ltd. v DDIT (2010) 132 TTJ 124 (ITAT Bang.);*
- *Dassault Systems K K (2010) 188 Taxman 223 (AAR);*
- *DDIT v M/s TII Team Telecom International Ltd. (ITA No.309/Mum/2007) (Mum ITAT);*
- *DDIT v Alcatel USA International Marketing Inc (Mum) (2010-TII-123-ITAT-MUM-INTL);*

- *DDIT (International Taxation) v M/s Reliance Industries Ltd. (ITA No.116/Mum/2008) (ITAT Mum);*
- *Hewlett-Packard (India) (P) Ltd. v ITO (2006) 5 SOT 660 (ITAT-Bangalore);*
- *M/s Kansai Nerolac Paints Ltd. v Addl. DIT (2010) ITA No.568/Mum//2009 (ITAT Mum.); and*
- *Addl. Director of Income-tax (Int. Taxation) v M/s Tata Communications Ltd. (2010) ITA No.1473/Mum/2009 (ITAT Mumbai).*

3.9 The CIT(A) erred in relying upon the decision of the Karnataka High Court in the case of Commissioner of Income Tax and others v Samsung Electronics Co. Ltd. And Others (2009) 227 CTR 335.

3.10 The CIT(A) ought to have followed the principles laid down by the Supreme Court in Union of India v Kamalakshmi Finance Corporation Limited (1991) ELT 433 (SC) and ought to have set aside the order of the DDIT.

4. Interest levied under section 234B of the Act

The DDIT/CIT(A) erred in levying interest under section 234B of the Act.

5. Interest under section 234A of the Act

The appellant prays that it be granted the consequential relief in respect of levy of interest under section 234A of the Act.

6. Initiation of penalty proceedings

The CIT(A) erred in not reaching a conclusion that the initiation of penalty proceedings by the DDIT under section 271(1)(c) was not justified in the case of the appellant.

7. Relief

The appellant prays that the DDIT be directed to grant all such relief arising from the preceding grounds as also all relief consequential thereto.

4.0 In the ground at sl.no.1, the assessee has contended that the order of assessment is bad in law as the re-assessment proceedings initiated under section 147 and pursuant to issue of notice under section 148 of the Act were carried out in violation of the procedure laid down by law and the judicial decisions on the subject and therefore, the order of assessment required to be struck down as invalid, null and void ab-initio. The learned AR, at the outset, submitted that, the assessee had been required to file the return of income for the assessment year 2005-06 pursuant to the issue of notice under section 148 of the Act on 2/4/2007, which admittedly, it did on 30/4/2007. The return of income was enclosed with a covering letter dated 16/4/2007 (filed on 30/4/2007) addressed to the Assessing Officer wherein the assessee had requested him to provide the reasons for initiating the proceedings under section 148/147 of the Act (at page 10 of the paper book filed by the learned AR on 07/11/2012). It was submitted by the learned AR that the reasons for initiating proceedings under section 147/148 of the Act sought for by the assessee were never made available to it by the Assessing Officer in the course of assessment proceedings which, it is argued, was against the settled position of law on the subject. The learned AR pointed out that the reasons recorded by the Assessing Officer for initiation of proceedings under section 147/148 of the Act were finally made available to the assessee only on 28/1/2010 by the learned CIT(A) in the course of appellate proceedings, as can be seen from the narration in

paras 3.2 and 3.3 of the learned CIT(A)'s order. The learned AR argued vehemently that on being asked for the reasons recorded for initiation of proceedings under section 147/148 of the Act, it was obligatory on the part of the Assessing Officer to communicate the same to the assessee; but which was not done. This, it was submitted, was in violation of the decisions of the Hon'ble Apex Court in the case of *GKN Driveshafts (India) Ltd. v ITO* (259 ITR 19) (SC) and of the Hon'ble Bombay High Court in the case of *Allana Cold Storage Ltd. v ITO* (287 ITR 1) (Bom.) which mandated that the Assessing Officer was bound to furnish the reasons sought within a reasonable time, which he did not do. In support of the proposition that failure on the part of the Assessing Officer to furnish the reasons for initiation of proceedings under section 147/148 of the Act during the pendency of assessment proceedings would render the resultant order of assessment bad in law, void ab-initio and liable to be quashed, the assessee also relied on the following decisions:-

- (i) *ACIT v K V Venkataswamy Reddy* of the ITAT, Bangalore in ITA Nos.797, 807, 798 & 808/Bang/2009 dated 21/5/2010 - wherein the Tribunal, following the decision of the Hon'ble Apex Court in the case of *GKN Driveshafts (India) Ltd. v ITO* (supra) and of the Hon'ble Bombay High Court in the case of *Allana Cold Storage Ltd. v ITO* (287 ITR 1) (Bom.), held that the orders of assessment have no legal sanctity as they are not passed in conformity with the ruling of the Courts (supra) and quashed them.
- (ii) *Tata International Limited v DCIT* (ITA Nos.3359 to 3361/Mum/2009 dated 29/6/2012 of ITAT, Mumbai).
- (iii) *CIT v Videsh Sanchar Nigam Ltd.* (ITA No.4235 of 2010 dt.20/7/2011).

4.1 Per contra, the learned DR supported the order of the authorities below. He submitted that the request for copy of reasons recorded for initiation of 147 proceedings vide letter dt.16/4/2007 addressed to the Assessing Officer was for filing of the return of income for the assessment year 2005-06. No separate application was made by the assessee to the Assessing Officer, for obtaining the reasons. It was further submitted that as the reasons were provided to the assessee by the learned CIT(A) that would suffice as compliance with the requirements of law and procedure as laid down by the Courts and therefore, proceedings initiated under section 147/148 of the Act and the resultant order of assessment under section 143(3) rws 148 of the Act dated 29/12/2008 were valid in law. In support of this proposition, the learned DR placed reliance on the decision of the Hon'ble Delhi High Court in the case of Nestle India Ltd. v DCIT reported in (2004) 189 CTR (Del.) 70.

4.1.1 We have heard the rival contention, perused and carefully considered the relevant material on record and the judicial decisions cited. Though the arguments on merits were also made, however, at this stage, we will confine ourselves to the issue of the validity of the initiation of proceedings under section 147/148 of the Act and the resultant order of the assessment for the assessment year 2005-06.

4.1.2 As per the records, we find that the then Assessing Officer had recorded in writing the reasons for initiation of proceedings under section 147/148 of the Act. It is also a matter of record that the assessee's letter dated 16/4/2007, for filing the return of income for the

assessment year 2005-06 in response to notice under section 148 dt.2/4/2007, contained a specific request to the Assessing Officer to be provided with the reasons for initiating the proceedings under section 147/148 of the Act (copy on page 10 of assessee's paper book filed on 07/11/2012). The assessee's letter dated 16/4/2007 forms a part of the record of assessment with the Assessing Officer. It is clear from a perusal of paras 3.2 and 3.3 of the learned CIT(A)'s order that reasons recorded by the Assessing Officer for initiation of proceedings under section 147/148 of the Act were never provided to the assessee by the Assessing Officer during the pendency of assessment proceedings which culminated in the order of assessment on 29/12/2008, almost one year and eight months after the request for the same was made by the assessee on 16/4/2007. In para 3.2 of his order, the learned CIT(A) states that the reasons recorded for initiation were given to the assessee on 28/1/2010 only. This establishes the fact that the assessee was never given the reasons for initiation of proceedings under section 147/148 of the Act by the Assessing Officer during the pendency of assessment proceedings but only during appellate proceedings almost 33 months after the assessee made the request for the same by letter dated 16/4/2007.

4.1.3 As held by the Hon'ble Apex Court in the case of GKN Driveshafts (India) Ltd. v ITO (259 ITR 19) (2003) that on being requested by the assessee, the Assessing Officer is bound to furnish the reasons recorded for initiation of proceedings under section 147 of the Act within a reasonable period of time so that the assessee could file its objections thereto and the Assessing Officer was to dispose off the same by passing a

speaking order thereon. Even as per the rules of natural justice, the assessee is entitled to know the reasons on the basis of which the Assessing Officer has formed an opinion that income assessable to tax has escaped assessment. The furnishing of reasons to the assessee is to enable/facilitate it to present its defence and objections to the initiation of proceedings under section 147/148 of the Act. We are of the considered opinion that there was no justifiable reason for the Assessing Officer to deprive the assessee of the recorded reasons by him for initiating proceedings under section 147/148 of the Act.

4.1.4 In the decision cited by the learned AR in CIT v Videsh Sanchar Nigam Ltd. (ITA No.4235 of 2010 dt.20/7/2011), the Bombay High Court has held that re-assessment proceedings were invalid for the reason that the reasons recorded for reopening of the assessment were not furnished despite requests by the assessee till the completion of the assessment and were furnished only after completion of the assessment. From this decision it is clear that the reasons recorded for initiation of proceedings under section 147/148 of the Act are required to be furnished by the Assessing Officer to the assessee within a reasonable period in order for the assessee to raise its objections at the preliminary stage of proceedings. If the reasons are not furnished to the assessee during the assessment proceedings, then the subsequent furnishing of the reasons after completion of assessment proceedings would serve no purpose and would amount to the assessee being denied its right to raise objections to the validity of proceedings initiated under section 147/148 of the Act. In the light of the findings of their Lordships in this case, it is clear that the

completion of assessment/re-assessment without furnishing the reasons recorded by the Assessing Officer for initiation of proceedings under section 147/148 of the Act is not sustainable in law as it is incumbent on the Assessing Officer to supply them within reasonable time as held by the Hon'ble Apex Court in the case of GKN Driveshafts (India) Ltd. v ITO (supra). The subsequent furnishing of reasons i.e. after completion of assessment would not make good the defect/invalidity with which the initiation of proceedings under section 147/148 of the act is tainted. Similar view has been held by coordinate benches of the ITAT in the case of (i) ACIT v K V Venkataswamy Reddy of the ITAT, Bangalore in ITA Nos.797, 807, 798 & 808/Bang/2009 dated 21/5/2010 and (ii) Tata International Limited v DCIT by the ITAT, Mumbai in ITA Nos.3359 to 3361/Mum/2009 dated 29/6/2012.

4.1.5 From the discussion in paras 4.1.1 to 4.1.4 of this order (supra), it is clear that the settled proposition of law, as laid down by the Hon'ble Apex Court, Hon'ble High Court of Mumbai and as followed by the two decisions of the coordinate benches of the Tribunal (all cited supra), is that the reasons as recorded by the Assessing Officer are required to be furnished to the assessee within reasonable time of their being recorded and certainly prior to the completion of assessment. In the instant case, the undisputable facts on record establish beyond doubt that the reasons recorded for initiation of proceedings under section 147/148 of the Act were never furnished to the assessee by the Assessing Officer before completion of the assessment proceedings on 29/12/2008, 33 months after the request was made by the assessee by letter dated 16/4/2007. The

subsequent furnishing of the reasons recorded to the assessee by the learned CIT(A) by letter dated 28/1/2010 does not achieve any purpose or mitigate the illegality of the action of depriving the assessee its right to raise objections against the initiation of proceedings under section 147/148 of the Act. In this view of the matter, we hold that the order of assessment passed under section 143(3) rws 148 of the Act dated 29/12/2008 for the assessment year 2005-06 without the Assessing Officer furnishing the recorded reasons for initiation of proceedings under section 147/148 of the Act to the assessee within reasonable time and prior to the completion of the assessment proceedings, renders this order of assessment invalid and unsustainable in law.

5. Since we have quashed the order of assessment dated 29/12/2008 for the assessment year 2005-06 as being invalid and unsustainable in law, we therefore do not propose to go into the merits of the issues raised in this appeal.

6. In the result, the appeal filed by the assessee for the assessment year 2005-06 is allowed.

Order pronounced in the open court on 10th day of December, 2012

Sd/-
(N V VASUDEVAN)
JUDICIAL MEMBER

Sd/-
(JASON P BOAZ)
ACCOUNTANT MEMBER

Copy to :

1. The Revenue
2. The Assessee
3. The CIT concerned.
4. The CIT(A) concerned.
5. DR
6. GF

MSP/

By order

Senior Private Secretary, ITAT, Bangalore.