

(2009) 10 SHI CK 0028
In the High Court Of Himachal Pradesh

Commissioner of Income Tax

APPELLANT

Vs

Maggronic Devices Pvt. Ltd.

RESPONDENT

Date of Decision : 07-10-2009

Acts Referred:

Income Tax Act, 1961 — Section 9

Citation : (2010) 228 CTR 241

Hon'ble Judges : V.K. Ahuja, J;Deepak Gupta, J

Bench : Division Bench

Judgement

Deepak Gupta, J.—This reference under the Income Tax Act, 1961 has been made to obtain the opinion of this Court on the questions of law:

i) Whether on the facts and in the circumstances of the case, the ITAT was right in law in holding that the payment of 15 million yen equivalent to Rs. 18,13,786/- cannot be treated as a royalty under the provisions of Section 9 of the Income Tax Act, 1961 and in allowing remittances without deduction of tax at source?.

2. The brief facts of the case are that the assessee-company is engaged in the manufacture of Audio Magnetic Sound Heads. This product is used for manufacturing of various types of audio system like tape- recorders, stereos, sound systems, telephone answering machines etc. The assessee company entered into an agreement with M/s. Sankyo Seiki (Singapore) Pvt. Ltd. at Singapore on 16.11.1989. This agreement was approved by the Government of India and the Reserve Bank of India. Under the agreement, the foreign company was to supply plant know-how and product know-how. In terms of the agreement entered into the assessee by the foreign company, if required, the foreign company would also make available the services of trained technicians for setting up the plant and machinery in accordance with the printed material and data. The foreign company was to be paid 15 million yen which is equivalent to Rs. 18,13,786/- for the supply of this data and information. This amount was to be paid in three instalments. 1/3rd was payable on the date of agreement, 1/3rd

upon the delivery of the documents of designs, machinery and plant which were necessary to start production. The final instalment was to be paid after the commercial production is started.

3. The assessee applied for a No Objection Certificate to pay the amount without deduction of tax at source on the ground that no liability to pay tax had accrued in India. The Assessing Officer refused to grant the certificate to the assessee-company as according to him the payment by the assessee to the foreign company was in the nature of fees for technical services. The assessee filed an appeal before the C.I.T (Appeals) who allowed the claim of the assessee and directed the Assessing Officer to issue No Objection Certificate so as to enable the assessee to make payment without deduction of tax at source. The revenue filed an appeal before the Income Tax Appellate Tribunal. The Tribunal held that the agreement envisaged two types of services - (1) Plant Know-How and (2) Product Know-How. It held that since the payment in dispute related to the acquisition of Plant Know-How in the form of technical and engineering data, design data, drawings, sketches, photographs etc. and these in fact had been purchased by the assessee from the foreign company at Singapore, no part of the income by the foreign company arose in India. It further held that this amount of 50 million yen cannot be treated as royalty even in terms of the extended definition of royalty. Thereafter, reference has been made as above.

4. We have heard Sh. Vinay Kuthiala, learned Counsel for the revenue and Sh. Vishal Mohan, Advocate appearing vice Sh. Pankaj Jain, learned Counsel for the assessee.

5. To understand the rival contentions of the party, it would be necessary to make reference to Section 5(2) of the Income Tax Act which provides that if any person who is a non-resident derives any income in the previous year from whatever source and such income is received or is deemed to be received in India or accrues or arises to it in India the same shall be deemed to be income for the purpose of Income Tax Act. Section 9(1)(vi) provides that income by way of royalty payable by a resident is taxable and Section 9(1)(vii) makes income even by way of fees for technical services payable by a resident is taxable.

6. The Contention of Sh. Vinay Kuthiala is that what the assessee purchased was the right to utilize the rights in respect of a patent, invention, model owned by the foreign firm for which the Assessee was liable to make payment and this is royalty within the meaning of Section 9(1)(vi) of the Act. In the alternative, it is contended that since the agreement provided that if necessary, the foreign company would send its some technicians, this can also be termed to be an agreement for providing technical services. In any eventuality, it was income by way of royalty/technical services payable by the assessee who is the resident in India and as such liable to tax.

7. Explanation 2 to Section 9(1)(vi) which has widened the scope of royalty and reads as follows:

- (i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;
- (ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;
- (iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property;
- (iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
- (v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films; or
- (vi) the rendering of any services in connection with the activities referred to in Sub-clauses (i) to (v).

8. On the basis of this definition, it is contended that the payment made is in fact royalty. On the other hand, Sh. Vishal Mohan, learned vice counsel for the assessee submits that what they have purchased is plant know how which is covered under the definition of "plant" and the purchase was made in Singapore and as such the payment is not income within the meaning of Income Tax Act and tax could be deducted at source.

9. It would be pertinent to refer to the undisputed facts. Two of the Directors of the assessee-company traveled to Singapore for the purchase of plant know how pursuant to the resolution of Board of Directors of the assessee-company passed on 24.7.1990. They collected the technical documents including designs, photographs etc. from the Singapore Company on 7th August, 1990. What was obtained was data including drawings, designs, sketches, photographs etc. which were handed over by the Singapore company to the Directors of the assessee. On the same day, payment of 5 million yen was made to the Singapore Company. An agreement was entered into between the companies. This agreement consisted of two parts. One part consisted of the transfer of the Plant Know How and the other part consisted of Product Know How. The Plant Know How was defined in Clause 1(a) of the agreement and included all inventions, processes, patents, engineering and manufacturing skills about plant and machinery and other technical information for manufacture of the product. This plant was transferred for a consideration of 15 million yen to be paid in three instalments as mentioned above. Clause 10(a) of the agreement reads as follows:

10(a) This agreement shall remain effective for a period ending five years from the date of signing the agreement. Upon the expiry of this agreement, the know

how THEREFORE delivered to "A" shall remain its property for its full and free use thereof.

10. The question which arises is whether the agreement to transfer all such know how falls within the meaning of royalty as contained in explanation to Section 9(1)(vi) or was outright sale of the plant. There can be no dispute that even drawings, designs, processing data etc. constitute plant within the meaning of the Income Tax Act. Reference in this behalf may be made to the judgment of the Apex Court in Scientific Engineering House (P) Ltd. Vs. Commissioner of Income Tax, Andhra Pradesh,

11. This Court in ITR No. 6 of 1996 titled Commissioner of Income Tax v. Shivalik Hatcheries Pvt. Ltd. following the aforesaid judgment had come to the conclusion that the scope of plant is quite wide. In the aforesaid judgment decided on 24th June, 2008, we held as follows:

The line of demarcation between what is a "plant" or not is a very thin one. Each case will have to be decided with reference to the particular facts of the case. It, however, needs to be noted that the definition of "plant" in Section 43(3) is not an exhaustive definition. It is only inclusive in nature. Therefore, there is a wide scope for including in the definition many items. It is clear that the legislature by including, ships, vehicles and books in the definition of plant, had widened the scope of the word "plant". As noted above, now the legislature has stepped in and specifically excluded buildings from the definition of the word "plant". This itself indicates that prior to the exclusion with effect from 1.4.2004, buildings if specifically constructed and felling within the guidelines of the various authorities referred to here-in-above could be treated as "plant". The various authorities referred to above also indicate that very wide amplitude has been given to term "plant". The definition of "plant" engulfs within its ambit many diverse subjects, such as, ships sailing on the high seas, books used by lawyers or engineers and scalpels used by doctors.

12. Thus there can be no manner of doubt that a plant was purchased. In Income Tax Officer and Others Vs. Shriram Bearings Ltd., a Division Bench of the Calcutta High Court considered the question which is virtually similar to one which arises in the present appeal. In that case, the Indian assessee had entered into an agreement with a Japanese Company. By the first part of the agreement, the foreign company agreed to sell to the Indian company its trade secrets relating to the products and relating to the manufacturing technique including the right to use patent rights etc. The second part of the agreement related to the rendering of technical assistance and training of personnel. After considering the entire law on the subject, the Calcutta High Court held that as far as the agreement related to the sale of trade secrets, no part of the activity or operation was carried out or took place in India and could not be considered being income u/s 5(2) of the Act. This decision of the Calcutta High Court has been upheld by the Apex Court in Income Tax Officer and Others Vs. Shriram Bearings Ltd. and Others,

13. The Calcutta High Court held that the agreement could be divided in two parts. The consideration for the sale of trade secrets and the consideration of technical assistance were separately provided for and mentioned under separate sections. Any part of the income relating to sale of trade secrets could not have been said to be earned in India.

14. On behalf of the revenue, reliance has been placed on *Leonhardt Andra Und Partner, GmbH Vs. Commissioner of Income Tax*, in which the Calcutta High Court held that the sums received by the assessee for design and technical services for the construction work are in the nature of royalty which is taxable under the Income Tax Act and do not constitute industrial and commercial profit. It would be relevant to mention here that in this case the agreement provided that the Indian company would not be entitled either directly or indirectly to make use of the documents supplied to it by the foreign company beyond the works to which the contract relates. In the present case, Clause 10(a) which we have quoted above clearly shows that the title in the documents stood transferred to the Indian Assessee and it became the owner and could use the same for any purpose albeit after a period of five years. Therefore, in our considered opinion, the learned Tribunal was right in holding that the Indian assessee had purchased Plant Know How at Singapore and the amount being paid was on account of purchase of the plant and not as royalty.

15. While taking this view, we find support from the judgment of the Andhra Pradesh High court passed in *Commissioner of Income Tax Vs. Klayman Porcelains Ltd.*, . In the present case, the documents and the agreement clearly show that the Indian assessee purchased the entire drawings, sketches, designs etc. It may be true that the foreign company was required to provide technical assistance, if required, but the fact is that no such technical assistance was ever required nor was provided. The payment of 15 million yen was the price of the documents purchased and in our considered opinion would not fall within the meaning of royalty quoted here-in-above.

16. The foreign company has no business in India. It has no plant in India. The transaction took place in Singapore. The agreement was entered into between the parties at Singapore and the documents were handed over to the representative of the Indian company at Singapore. This is a case of outright purchase of plant know how and not a case of transfer of interest.

17. We, therefore, find that the income Tax Appellate Tribunal was right in holding that the Assessee had purchased the designs, sketches, photographs etc. and, therefore, uphold the order of the Tribunal. The question is accordingly answered in favour of the assessee and against the revenue.

18. The appeal is disposed of in the aforesaid terms. No order as to costs.