M/S Irunway India Private Limited , ... vs Deputy Commissioner Of Income Tax ... on 27 April, 2022

IN THE INCOME TAX APPELLATE TRIBUNAL
"B" BENCH : BANGALORE

BEFORE SHRI N. V. VASUDEVAN, VICE PRESIDENT AND
MS. PADMAVATHY S, ACCOUNTANT MEMBER

ITA No.229/Bang/2019
Assessment Year : 2015-16

M/s. IRunway India Private Limited, Regus Business Center, Office No.1015, 10th Floor, Tower-B, Unitech Cyber Park, Sector 39, Gurugram, Gurgaon, Haryana - 122 003. PAN : AABCI 5613 D	Vs. DCIT, Circle - 3(1)(1), Bengaluru.
APPELLANT	RESPONDENT

Assessee by : Shri. T. Suryanarayana, Senior Advocate
Revenue by : Mrs. Susan D. George, CIT(DR)(ITAT), Bengaluru.

Date of hearing : 20.04.2022
Date of Pronouncement : 27.04.2022

ORDER

Per N. V. Vasudevan, Vice President This is an appeal by the assessee against the order dated 03.12.2018 of CIT(A)-3, Bengaluru, relating to Assessment Year 2015-16.

2. The assesee is engaged in the business of providing technology, consulting and litigation support services with focus on intellectual property domain, especially patent, to companies, law firms and other technology investment and licensing firms. The assessee provides technology related analysis, comments and information in the following three key areas:

a. patent litigation;

b. patent portfolio management; and c. technology due diligence services.

In October 2008, the assessee set-up a 100% subsidiary, viz., iRunway Inc., in the United States of America.

3. The assessee filed its return of income for AY 2015-16 on 27 November 2015 declaring a total income of Rs. 52,289,620 under the normal provisions of the Income Tax Act, 1961 (Act). The AO

passed the assessment order dated 26 December 2017 u/s 143(3) of the Act making the following additions to the total income declared in the return of income by the assessee:

> (i) Outsourcing charges of Rs. 71,110,315 payable to iRunway Inc 'were treated as 'fees for technical services' r FTS1 and disallowed u/s 40(a)(i) of the Act by alleging that the Assessee had not deducted tax u/s 195 of the Act;

(ii) Sales commission of Rs. 4,505,685 payable to Neeraj Gupta was treated as FTS and disallowed u/s 40(aXi) of the Act by alleging that the Assessee had not deducted tax u/s 195 of the Act; and

(iii) Provision of Rs. 1,170,000 created towards professional charges was disallowed u/s 37 and u/s 40(a)(ia) of the Act.

On appeal by the Assessee, the CIT(A) confirmed the order of the AO. Hence, this appeal by the Assessee before the Tribunal.

4. The first issue that requires consideration in this appeal is as to whether the Revenue authorities were justified in disallowing a sum of Rs.7,11,10,315/- being outsourcing charges paid by the assessee to its 100% subsidiary M/s. IRunway Incorporation, USA, for non-deduction of tax at source and by invoking the provisions of section 40(a)(ia) of the Act. During FY 2014-15, the assessee entered into contracts with its customers located in the U.S.A. Portion of the services that it agreed to provide to its customers was outsourced to its 100% subsidiary, iRunway Inc., US. For this purpose, the assessee entered into a Services Agreement dated 1 April 2012 with iRunway Inc. for availing itself of certain services. The conceptualization and scope of work to be performed by iRunway Inc. was determined by the assessee. Further, the assessee took the overall responsibility for the deliverables, it being the primary contractor for rendering services to its client. In connection with the services availed by the assessee from iRunway Inc during the financial year relevant to AY 2015-16, the assessee incurred outsourcing charges of Rs. 71,110,315.

5. The assessee did not deduct taxes u/s 195 of the Act on such outsourcing charges on the basis that the same did not constitute 'sum chargeable to tax' in India. Under the provisions of Sec.40(a)(ia) of the Act, where tax is deductible at source on a payment under Chapter XVII B of the Act and where tax has not been so deducted at source, then the sum so paid by an assessee without deduction of tax at source, will not be allowed as an expenditure while computing income from business.

6. The AO called upon the assessee to show-cause as to why outsourcing charges should not be disallowed u/s 40(a)(i) of the Act for alleged non-deduction of tax at source. The assessee took a stand that the said charges did not qualify as 'Fees for Technical Services' (FTS) under the Act as well as 'Fees for Included Services' [FIS] under the India-US Tax Treaty, and therefore did not constitute 'sum chargeable to tax' in India for it to be subjected to TDS. The assessee provided the following documents:

> a) The service agreement executed by iRunway Inc. and the assessee along with the list of services which was included in section A of the said service agreement;

b) Copy of invoices raised by iRunway Inc. on the assessee towards sub-contracting fee;

c) Brief write-up on the relevant legal framework in the US for governing patent litigation; and

d) Sample contract entered into by the assessee with one of its US customers and documents/ e-mails exchanged between iRunway Inc and the assessee w.r.t. such contract.

7. The AO however held that the outsourcing charges as taxable as Fees for Technical Services (FTS) under the Act and as Fees for Included Services (FIS) under the India-US Tax Treaty and since the assessee had not deducted tax at source u/s 195 of the Act, the expenditure was disallowed u/s 40(a)(i) of the Act.

8. Before CIT(A), it was submitted that section 195 of the Act casts an obligation on an Indian company that is liable to make payment of a sum chargeable to income-tax in India to a non-resident to withhold tax at source at the applicable rates in force. A foreign company is liable to income-tax in India, inter alia, on income that is deemed to accrue or arise in India. The assessee submitted that outsourcing charges paid to iRunway Inc. will not qualify as FTS u/s. 9(1)(vii) of the Act and as FIS under the India-US Tax Treaty, and hence not taxable in India, for it to warrant tax deduction u/s 195 of the Act by the assessee. The assessee explained that it enters into contract with its customers which are primarily located in the US. A portion of the services that it agrees to undertake to its customers is outsourced by it to its 100% subsidiary, iRunway Inc., US. The conceptualization and scope of work to be performed by iRunway Inc. is determined by the assessee. Further, the assessee takes the overall responsibility for the deliverables, it being the primary contractor for rendering services to its client.

9. For the above purpose, the assessee has entered into a Services Agreement dated 1 April 2012 with iRunway Inc. for availing itself of certain services as included in section A of the Agreement. In summary, the services availed by the assessee included the following:

a) Technology analysis for litigation [e.g., source code review, technical document review and analysis, accused system experimentation, and research; b) Patent Patent portfolio analysis;

c) Technology research & due diligence; d) Consulting services and assistance in anticipation and in support of litigation; and e) Developing evidentiary support for affirmative infringement contentions.

10. The assessee explained that in the US, the patent litigation matters are governed under the Export Administration Regulations issued by the Bureau of Industry and Security, US Department of Commerce. As per the applicable law.

a) A Party to any patent dispute is allowed to access confidential information including documents, testimony, or information containing or reflecting proprietary, trade secret, and/ or, commercially sensitive information of the other Party, under a process called 'Discovery'.

The confidential information that is accessed under the 'Discovery' process is referred to as `Discovery Material'.

b) The Parties are required to obtain an Order from the US Court that will lay down the conditions for treating, obtaining and using such Discovery Material. The access to Discovery Material is given only to those people who sign the Protective Order issued by the US Court.

c) Generally, the Protective Order will, inter alia, provide the manner in which the Discovery Material [also known as Protective Material] is to be stored/ maintained by the Parties and the location / place where such Material will be available to be accessed by the Parties.

The Protected Material is not allowed to leave the territorial boundaries of the US or be made available to any foreign national who is not:

> lawfully admitted for permanent residence in the US; or identified as a protected individual under the Immigration and Naturalization Act.
>
> d) Each party receiving the Protected Material is required to comply with all applicable export control statutes and regulations.
>
> e) The above prohibition extends to Protected Material (including copies) in physical and electronic form. The viewing of Protected Material through electronic means outside the territorial limits of the US is similarly prohibited

11. The assessee provided Sample contract between the assesee and its customers and the manner of rendering services.

a) The assesee entered into an Agreement for Services [AFS] with McKool Smith, a law firm, on 11 August 2014.. As per the AFS, the Assessee was required to provide consulting services to McKool Smith in relation to complaint for patent infringement to be filed by BMC Software [i.e., a client of McKool Smith] against Service Now, Inc. [i.e., the client of Cooley LLP, a law firm in California].

Pursuant to the AFS, the Assessee was required to provide various services w.r.t. patent litigation, inter alia, including patent review, patent infringement analysis, source code review, technical document review and analysis, accused system experimentation, etc.

b) In the BMC matter, since the accused products were software products, the Assessee was required to review the source code of the accused products to prove infringement under the `Discovery' process.

c) Accordingly, BMC Software and Service Now obtained a Protective Order dated 20 February 2015 from the US District Court. As can be seen from Page 25 [section 14] of the Protective Order issued by the US District Court:

> i) The source code produced in Discovery process by BMC Software was to be made available for inspection, in electronic form at the Dallas, Texas, or Houston, Texas office of its outside counsel McKool Smith PC, or any other location mutually agreed to by the Parties; and
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> ii) Any source code that is produced by Service Now Inc. was to be made available for inspection at the Palo Alto, California office of its outside counsel, Cooley LLP or any other location mutually agreed to by the Parties.

Given the legal restrictions in the US

a) the source code produced by the Parties were not allowed to be verified at any other location other than the US; and

b) were allowed to be verified by only those who were permanent resident of the US and identified as a protected individual under the Immigration and Naturalization Act.

Accordingly:

> a) the assesee requested iRunway Inc. for services whereby the employees of iRunway Inc. [who were legally qualified to access the Protective Material] would access the Protective Material in the US to perform relevant activities, and provide a report/ memo of its findings/ analysis to the Assessee; and
>
> b) The analysis performed by iRunway Inc.'s employees and provided to the Assessee was included in the deliverable that the Assessee provided to its customer i.e., Mckool Smith .

For reference, the Assessee also enclosed the following documents w.r.t. the contract with Mckool Smith:

> a) List of team members (both from the Assessee and iRunway Inc.) engaged on the_project with McKool Smith.
>
> b) Deliverable in the form of rebuttal memo sent by iRunway Inc. (by Kalyan Banerjee, an employee of iRunway Inc.,) to the Assessee (to Subhasri Das, an employee of the Assessee) ; and
>
> c) Final deliverable sent by Subhasri Das to Mr. Philip J. Lee from Mckool Smith.

12. The assessee submitted that the outsourcing charges does not qualify as FTS under the Act. In this regard the assessee submitted that as per section 9(1)(vii) of the Act, income by way of 'Fees for Technical Services [`FTS'] is deemed to accrue or arise in India if it is payable by a resident of India. Explanation 2 to section 9(1)(vii) of the Act defines the term `FTS' to mean any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head 'Salaries '" FTS has been defined in an exhaustive manner u/s 9(1)(vii) of the Act to mean consideration, inter alia, for rendering of any managerial, technical or consultancy service. Further, section 9(1)(vii) of the Act provides for certain exclusions wherein FTS earned by a nonresident taxpayer will not be taxable in India. As per sub-clause (b) of clause (vii) of sub-section (I) to section 9 of the Act, income of non-resident includes income by way of 'fees for technical services' payable by a person who is a resident, except where the fees are payable in respect of services utilized in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India.

13. There are two exclusions contained in sub-clause (b) of Section 9(1)(vii) of the Act from the taxability of FTS in India, viz., Exclusion 1 - FTS paid by a resident in respect of services utilised for the purposes of a a) business or profession carried on by such resident outside India; and

b) Exclusion 2 - FTS paid by a resident in respect of services utilised for the purposes of making or earning any income by such resident from any source outside India.

The assessee submitted that the outsourcing charges paid to iRunway Inc. ought to be regarded as being towards services utilised by the Assessee in its 'business carried on outside India', since, the services of iRunway Inc. are utilised in the project undertaken by the Assessee outside India; the customers of the Assessee are located outside India; and activities relating to the portion of the project with the customer, for which the sub- contracting charges are paid to iRunway Inc, are undertaken outside India. Without prejudice to the above, the outsourcing charges paid by the Assessee to iRunway Inc. ought to be regarded as being towards services utilised by the Assessee 'for making or earning of income front any source outside India', since:

i) the customers of the Assessee are located outside India;

ii) the payments to iRunway Inc. are towards services utilised by the assessee outside India and such services are rendered by iRunway Inc. outside India;

iii) the income earning activities are undertaken by the Assessee in the US; and

iv) there is a direct nexus between the payment made by the assessee to iRunway Inc. and agreement with customers outside India.

On the basis of the above the Assessee submitted that the outsourcing charges paid by it to iRunway Inc. cannot be held to 'deemed to accrue or arise' in the hands of iRunway Inc. in India u/s 9(1)(vii) of the Act. Thus, the outsourcing charges ought to fall under the exclusions provided in section 9(1)(vii)(b) of the Act. Accordingly, the underlying income would not be deemed to accrue or arise in India and as a result of which there would be no liability to deduct tax at source in respect of such payment and hence such expenditure ought not to be disallowed u/s 40(a)(i) of the Act.

14. Without prejudice to the assesee's contention above, even assuming while denying that outsourcing services are taxable u/s 9(1)(vii) of the Act, the assessee submitted that such charges ought not to be taxable as FIS in India under the India-US Tax Treaty. The assessee pointed out that Section 90(2) of the Act provides that the Act shall prevail over the provisions of the relevant Tax Treaty, wherever the provisions of the Act are more beneficial to the tax payer. As a corollary, the provisions of the relevant Tax Treaty shall prevail over the corresponding provisions of the domestic law to the extent they are more beneficial to the taxpayer. The assessee pointed out that as per Article 12 of the India-US Tax Treaty, technical services are construed as lee for included services' only if such services:

> are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received; or make available technical knowledge, experience, skill, know- how, or processes or consist of the development and transfer of a technical plan or technical design.

15. The assessee pointed out that in the Memorandum of Understanding [`MoU'] to the India-US Tax Treaty, technical services have been stated to mean services requiring expertise in a technology and consultancy services have been stated to mean advisory services. Also, the MoU states that the categories of technical and consultancy services are to some extent overlapping because a consultancy service could also be a technical service. Further, the term 'make available' has been explained in the Memorandum of Understanding 'MOU'] to the India-US Tax Treaty. As per the said MOU, technology will be considered' made available' when the recipient of the service is enabled to apply the technology. The assessee pointed out that (a) iRunway Inc. had provided services to the assessee from the US; (b) The activities involved were such that the employees of iRunway Inc. alone could access the confidential information and at the locations which are approved by the US District Court under a Protective Order; (c) Given the Protective Order, the source code could not be reviewed from any other location other than US; (d) iRunway Inc. is legally bound and restricted from accessing the Protective Material from any location/ in any manner other than what is approved by the District Court under the Protective Order. Therefore, iRunway Inc, would never have an occasion to transfer or make available the technology, skill, knowledge, process, etc involved in reviewing of source code [i.e., Discovery process] to the assessee; and (e) iRunway Inc, prepares its note/ report on the basis of its analysis and sends the same to the assessee which is in turn included in the deliverable to be sent by the assessee to the customer.

16. Further, the assessee also submitted that, owing to legal restrictions in the US for accessing protected material, iRunway Inc. did not have any occasion/ opportunity to 'make available' any technical knowledge to the assessee. Moreover, mere rendition of an output by iRunway Inc. based

on technical knowledge, by itself, cannot result in the 'make available' condition being satisfied. In the light of the above submissions, the assessee submitted that while rendering services, iRunway Inc. did not make available any technical knowledge, know-how, experience, skill or processes to the assessee which will enable the assessee to apply any such technical knowledge, etc. by itself in its business without recourse to iRunway lnc. For every new project/ new customer, the assessee has to invariably sub-contract the relevant portion of the Project to iRunway Inc. Hence, the outsourcing charges will not qualify as FIS under the India-US Tax Treaty hence, the payment of the same to iRunway Inc. did not warrant TDS u/s 195 of the Act.

17. The CIT(A) however did not agree with the aforesaid submissions made by the assessee. He held that the services rendered were in the nature of technical services within the meaning of Sec.9(1)(vii) of the Act and are taxable in India even though the services were not rendered in India. Thereafter the CIT(A) went into the question whether the services rendered by iRunway Inc., USA made available technical knowledge skill to the assessee so as to satisfy the requirements of Article 12(4)(b) of the Indo-US treaty. The CIT(A) analyzed the terms of the Agreement between the assessee and iRunway Inc., USA and found that Schedule A of the Agreement provided that iRunway Inc. was to provide services to the assessee which included Patent infringement analysis, invalidity searches, Patent litigation analysis and support Patent pre-litigation analysis and support, reverse engineering and analysis, product testing, source code review and analysis, product testing, source code review and analysis, evidence/target scouting for licensing/litigation, technical document review and analysis, claim chart preparation, Expert witness support, COMPASS tool/patent data base support, patent portfolio analysis and Patenting valuation/damage assessment. The agreement also provided that the intellectual protect rights (IPR) would remain with the assessee. The above aspects, according to the CIT(A), would be enough to hold that the US company made available to the assessee, which in turn was used by the assessee to further service it's clients. The CIT(A) also referred to the warranty clauses 8.1 and 8.2 of the Agreement between the assessee and iRunway inc., USA which provided that the assessee would indemnify iRunway Inc., USA against any liability, claims, law suits, losses, demands, cost and expenditure relating directly or indirectly to the IPR or the design, sale or use of any embodiment of the IPR. According to the CIT(A), all these aspects would show that the service provider made available to the assessee knowledge, skill to the assessee and therefore the 'make available' clause of the Indo-US treaty was satisfied.

18. On the argument of the assessee that the source of income of the assessee was from customers in USA (Outside India) and therefore the exclusion clause in Sec.9(1)(vii) (b) would operate to render the income not to have accrued or arisen in India, the CIT(A) held that the assessee carries on business in India notwithstanding that his clients are from USA. Merely because customers of the assessee are outside India that cannot be the basis to say that the source of income is in USA. The CIT(A) therefore rejected this argument of the assessee also.

19. Aggrieved by the order of the CIT(A), the assessee is in appeal before the Tribunal. Learned Counsel for the assessee reiterated submissions that was made before the Revenue authorities. He placed reliance on the decision of the Hon'ble Delhi High Court in the case of DIT Vs. Lufthansa Cargo India Ltd., (2015) 60 taxmann.com 187 (Delhi) in which the Hon'ble Delhi High Court took

the view that second part of exclusion contemplated vide section 9(1)(viii)(b) of the Act would be attracted. That was the case in which the assessee was an Indian resident who was engaged in wet leasing of aircrafts to foreign companies, on international routes. The assessee entered into an overhaul agreement with German Co., to carry out maintenance repairs was to be excluded since the source of income of the assessee was outside India and the maintenance charges were paid for the purpose of earning income from a source outside India. The Hon'ble Delhi High Court held that the Tribunal held that the overwhelming or predominant nature of the assessee's activity was to wet-lease the aircraft to, a foreign company. The operations were abroad, and the expenses towards maintenance and repairs payments were for the purpose of earning abroad. In these circumstances, the Tribunal's factual findings that the source of income of the assessee was outside India cannot be faulted. On the question whether the services in question made available in technical knowledge skill to the assessee, learned Counsel for the assessee placed reliance on the decision of the Hon'ble Karnataka High Court in the case of CIT Vs. De Beers India Minerals (P) Ltd., (2012) 21 taxmann.com 214 (Kar.) wherein the Hon'ble Karnataka High Court held that in terms of article 12 of India- Netherlands DTAA, in a case, if along with technical services rendered. service provider also makes available technology which they can use in rendering services, then it falls with definition of fee for technical services. Where however, if technology is not made available along with technical services whereas what is rendered is only technical services and technical knowledge is withheld, then, such a technical service would not fall within definition of technical services in DTAA and not liable to tax. In that case the assessee for the purpose of carrying out geophysical survey, for its mining company entered into an agreement with a Dutch company. Services included air borne survey for providing high quality, high resolution, geophysical data regal-dig diamond bearing mineral deposits. Assessing Officer treated consideration paid to Dutch company as fees for technical services. Since assessee had failed to deduct tax on payments made to Dutch company, Assessing Officer treated assessee as assessee-in-default. Dutch company performed servces using technical knowlege and expertise and it had given data, photographs and maps to assessee but they had not made available technical expertise, skill or knowledge in respect of collection or processing of data to assessee, which assessee could apply independently and without assistance and undertake such survey independently excluding Dutch company in future. In view of above, though Dutch company had rendered technical services as defined under section 9(1)(vii) Explanation 2, yet it did not satisfy requirements of technical services as contained in article 12 of Indo-Dutch DTAA and, therefore, assessee had no TDS liability qua said payment.

20. The learned DR firstly submitted that there is no dispute that the nature of services is in the nature of technical services. He submitted that under Article 12(4)(b) of the Double Taxation Avoidance Agreement (DTAA) between India and USA, payment of any kind made to a person in consideration for rendering technical services are taxable in India if such services consist of development and transfer of a technical plan or technical design. It was submitted by learned DR that without prejudice to the findings of the Revenue authorities that the technical services provided by the AE made available technical knowledge, experience, skill, the services involved development and transfer of a technical plan or a technical design by the assessee's foreign subsidiary in the form of reports of IPRs. In this regard, learned DR pointed out that the agreement between the assessee and Mckool Smit involved decoding of software and doing so was equivalent to making available technology to the assessee. On the applicability of the exclusion clause in section 9(1)(vii)(b) of the

Act, learned DR submitted that the assessee's source of income is in India and not USA. The fact that the assessee's clients are in USA will not mean that the assessee's source is from USA. In so far as the reliance placed by the learned Counsel for the assessee on the decision in the case of Lufthansa Cargo Pvt., (supra) is concerned, learned DR submitted that in the case of Lufthansa Cargo Pvt. Ltd., (supra), the activities were carried out outside India and therefore the aforesaid decision will not be applicable.

21. We have given a very careful consideration to the rival submissions. We shall first take up for consideration argument of the assessee that the sum paid by the assessee to iRunway Inc., USA cannot be brought to tax in India even assuming that the nature of the payment was FTS within the meaning of the Act because under the Indo US Treaty, FTS is taxable in India only when the recipient of the payment 'makes available' technical knowledge, experience, skill, know-how or processes, or consist of the development and transfer of a technical plan or technical design. We have already set out the details of the services which iRunway Inc., USA was to provide to the assessee. These are contained in paragraph 9 to 11 and 14 to 16 of this order. The services so provided were (a) Technology analysis for litigation [e.g., source code review, technical document review and analysis, accused system experimentation, and research; (b) Patent portfolio analysis;

(c) Technology research & due diligence; (d) Consulting services and assistance in anticipation and in support of litigation; and (e) Developing evidentiary support for affirmative infringement contentions. In short it was in the nature of services in connection with patent registration, patent litigation and procuring evidence for patent litigation and similar services. The customers of the Assessee are based in USA. iRunway Inc., USA is a tax resident of USA and therefore the taxability of the payment received from the Assessee has to be tested on the basis of the relevant clauses of the Indo US Treaty. The relevant articles in the treaty are is Article 12 which deals with taxability of Royalties and fees for included services. In terms of Article 12(1) Royalties and fees for included services arising in a Contracting State (USA in this case) and paid to a resident of the other contracting State (India/Assessee in this case) may be taxed in that other state (i.e., USA). The relevant clause on which reliance was placed by the assessee for non taxability of the sum in question in India in the hands of iRunway Inc. USA was Article 12(4) which provides as follows:

> (4) For the purposes of this article 'fees for included services' means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provisions of services of technical or other personnel) if such services :
>
> a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in para 3 is received; or
>
> b) make available technical knowledge, experience, skill, know-how or processes, or consist of the development and transfer of a technical plan or technical design.

22. The case of the assessee is that in terms of Article 12(4)(b) of the Indo US treaty, only rendering of technical or consultancy services as 'make available' technical knowledge, experience, skill or

know-how etc can be taxed in India in the hands of iRunway Inc. In other words, in order to attract the taxability of an income under Article 12(4)(b), not only the payment should be in consideration for rendering of technical or consultancy services, but in addition to the payment being consideration for rendering of technical services., the services so rendered should also be such that 'make available' technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design. These worlds are 'which make available'. The meaning of the expression make available were considered by the Tribunal in the case of Raymond Ltd. Vs. DCIT (2003) 80 TTJ (Mum) 120. The Tribunal after elaborate analysis of all the related aspects observed that :-

> "The words 'making available' in Article 13.4 refers to the stage subsequent to the 'making use of' stage. The qualifying words is 'which' the use of this relative pronoun as a conjunction is to denote some additional function the 'rendering the services' must fulfil. And that is that it should also 'make available' technical knowledge, experience, skill etc. The word which occurring in the article after the word 'services' and before the words 'make available' not only described or defines more clearly the antecedent noun '(services') but also gives additional information about the same in the sense that it requires that the services should result in making available to the user technical knowledge, experience, skill, etc. Thus, the normal, plain and grammatical meaning of the language employed is that a mere rendering of services is not roped in unless the person utilizing the services is able to make use of the technical knowledge, etc. by himself in his business or for his own benefit and without recourse to the performer of the services in future. The technical knowledge, experience, skill etc. must remain with the person utilizing the services even after the rendering of the services has come to an end. A transmission of the technical knowledge, experience, skill, etc. from the person rendering services to the person utilizing the same is contemplated by the article. Some sort of durability or permanency of the result of the 'rendering services' is envisaged which will remain at the disposal of the person utilizing the services. The fruits of the services should remain available to the person utilizing the services in some concrete shape such as technical knowledge, experience skill etc.

23. In the Raymond's case (supra), the Tribunal also held that rendering of technical services cannot be equated with making available the technical services. In the case of CESC Ltd. Vs. DCIT (2003) 80 TTJ (Cal) (TM) 806:

> (2003) 87 ITD 653 (Cal)(TM) also the question regarding the scope of expression making available came up for the consideration of the Tribunal.

In that case, the Tribunal was dealing with the scope of Article 13(4)(c) of the Indo-UK tax treaty which is admittedly in pari materia with Article 12(4) of the India-USA tax treaty with which we are presently concerned. The majority view was that in order to attract the provisions of the said article of the tax treaty, not only the services should be technical in nature but should be such as to result in making the technology available to person receiving the technical services in question. The Tribunal

also referred to with approval the extracts from protocol to the Indo-US tax treaty to the effect that 'generally speaking, technology will be considered made available, when the person acquiring the service is enabled to apply the technology.

24. It is the allegation of the revenue that iRunway Inc. had made available to the assessee, the knowledge generated in the course of rendering technical and consultancy services on the basis that the employee of iRunway Inc. prepared a rebuttal memo which was reviewed by the employee of the assessee company to 'make use' of the same in the final deliverable given to the client. We are of the view that the AO has made incorrect interpretation of 'make use' to be equivalent to 'make available' of technical knowledge. The analysis provided in the memo prepared by the employee of iRunway Inc. was only made a part of the final deliverable. The same did not result in the employee of the assessee being enabled to be in a position to arrive at the analysis done by the employee of iRunway Inc. independently in the future, due to absence of the requisite knowledge. Therefore the revenue has incorrectly interpreted rendition of an output, i.e., analysis performed by iRunway Inc. based on technical knowledge as, it having made available technical knowledge itself, to the assessee. It is also the case of the revenue that as per the US court order, the confidential codes could be given to the counsel's support personnel which would be assessee's personnel in the instant case and doing so was making available technology, skill etc. We are of the view that the AO has incorrectly interpreted that the US Court's Protective order provided access to confidential source code to counsel's support personnel which includes assessee's employees, although no reference to the access being granted to the assessee or its employees has been made in the Protective order. In this regard, one cannot forget the fact that 'Undertaking of Experts or Consultants regarding Protective order' signed by the relevant employees of iRunway Inc. who were given access to the protective information under the protective order specifically provides that the authorized person will not divulge information to anyone. These individuals are employees of iRunway Inc. and fulfill the criteria of the relevant US statutory requirements to be able to access the protective information. None of these individuals are employees of the assessee as incorrectly alleged by the revenue. Further, the AO failed to appreciate that owing to the legal restrictions in the US, iRunway Inc. or its employees did not have an opportunity or any occasion to 'make available' any technical knowledge to the assessee or its employees while rendering services. As far as agreement for services with McKool Smith entered by the assessee for providing services in relation to patent litigation matters, do not mention about outsourcing of any kind of services including protective order clearance. The conclusion of the revenue authorities that iRunaway Inc., made available technical knowledge to the assessee or its employees is neither correct nor sustainable. The other services rendered were purely litigation oriented or services with regard to patent registration or patent search process and these services by no stretch of imagination can be considered as making available any technical knowledge to the assessee. In view of the fact that the services provided by iRunaway Inc., did not make available any technical knowledge to the assessee, the same cannot be regarded as taxable in India. Consequently, there was no obligation on the part of the assessee to deduct tax at source at the time of making payment.

Hence, the disallowance made u/s 40(a)(ai) of the Act cannot be sustained and is directed to be deleted.

25. The next issue that arises for consideration is as to whether the Revenue authorities were justified in disallowing a sum of Rs.45,05,685/- being sales commission paid by the assessee to one Mr. Neeraj Gupta, a non-resident and tax-resident of USA, by invoking the provisions of section 40(a)(ia) of the Act and for non deduction of tax at source and the payments made to Mr. Neeraj Gupta. The facts as far as this addition is concerned are that the assessee had entered into an iRunway Sales Contractors Agreement' with Mr. Neeraj Gupta, wherein the assessee availed itself of certain sales consulting services. In consideration thereof, sales commission of 8% to 10% aggregating to Rs. 4,505,685 was payable by the assessee to Neeraj Gupta for FY 2014-15. This commission was arrived at on the basis of fixed percentage of sales. The AO called upon the assessee to show cause as to why sales commission paid to Mr. Neeraj Gupta should not be disallowed u/s 40(a)(i) of the Act for alleged non-deduction of tax at source. The assessee submitted its response vide letter dated 21 November 2017 as to why the said charges did not qualify as 'income' or `FTS' under the Act, and therefore did not constitute 'sum chargeable to tax' in India for it to be subjected to TDS. Along with the letter dated 21 November 2017, the assessee had also appended the following documents:

> a) A copy of the iRum;vay Sales Contractors Agreement' executed between Mr. Neeraj Gupta and the assessee ; and
>
> b) Details of sales commission recorded as payable by the assessee during FY 2014-15.

26. However, in the impugned order, disregarding the assessee's submission as above, the AO held that the services provided by Mr. Neeraj Gupta qualified as FTS under the Act and as FIS under the India-US Tax Treaty. By alleging that the assessee had not deducted tax at source u/s 195 of the Act, the AO the same u/s 40(a)(i) of the Act.

27. Before CIT(A) the assessee explained as to why sales commission paid to Mr. Neeraj Gupta is not taxable in India. The assessee pointed out that it entered into an agreement called iRunway Sales Contractor Agreement' with Mr. Neeraj Gupta wherein it availed itself of certain sales consulting services. As per the said agreement, Mr. Neeraj Gupta would:

> a) assist the assessee in acquiring new customers or acquire new business from existing customers of the assessee;
>
> b) work closely with Assessee's legal department to ensure that all terms and conditions for proposed sale is being approached in a manner consistent with the Assessee's policies and objectives; and
>
> c) ensure timely collection of payment and manage communications with and retention from the customers introduced by him.

The pointed out that Mr. Neeraj Gupta was a tax resident of the US for FY 2014-15. The services under the aforesaid agreement were rendered by Mr. Neeraj Gupta from the US. Mr. Neeraj Gupta

did not visit India during FY 2014-15 for the purposes of rendering services to the assessee under the said agreement; and Sales commission at a fixed % on the amount of revenue earned from the relevant client which was solicited by Mr. Neeraj Gupta was payable by the assessee. In consideration of the above services availed, sales commission of Rs. 4,505,685 was payable by the assessee to Mr. Neeraj Gupta for FY 2014-15.

28. The assessee pointed out that under Section 195 of the Act an obligation exists on the assessee making payment of a sum chargeable to income-tax in India to a non-resident to withhold tax at source at the applicable rates in force. A non-resident Company is chargeable to income-tax in India, inter alia, on income that is deemed to accrue or arise in India. The assessee submitted that sales commission paid to Mr. Neeraj Gupta did not qualify as 'sum chargeable to tax' in India and therefore assessee did not have an obligation to deduct tax at source u/s 195 of the Act, for the following reasons:

> i) Mr. Neeraj Gupta had not rendered any managerial, technical or consultancy services;
>
> ii) As per the exclusion provided for u/s 9(1)(vii) of the Act, sales commission payable by the Assessee to Mr. Neeraj Gupta for services utilised in its business carried on outside India, and for earning income from its customers outside India, is not taxable in India;
>
> iii) Sales commission payable by the Assessee was not taxable as FIS under Article 12 of the India -- US Tax Treaty as the services did not make available any technical knowledge to the Assessee;
>
> iv) Sales commission is also not taxable under Article 15 of the India-US Tax Treaty as it was in the nature of Independent personal service.

29. The submission with regard to point (i) to (iii) above are identical to the submissions as was made on the first issue of disallowance u/s.40(a)(ia) of the Act of payments made to iRunway Inc., USA which we have already dealt with in the earlier paragraph. As far as point (iv) above is concerned, the submission was that Article 15 of the India-US Tax Treaty provides that income derived by a person from the performance of professional services. shall be taxed in the country of which he is resident except where the professional has a fixed base regularly available to him in India for the purpose of performing his activities or has stayed in India for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year. It was submitted that Mr. Neeraj Gupta did not satisfy the criteria as provided in Article 15 of the India-US Tax Treaty since neither he had a fixed base regularly available to him in India, neither he stayed even for a single day in India. Accordingly, sales commission paid to Mr. Neeraj Gupta is not taxable under Article 15 also of the India-US Tax Treaty as it does not satisfy either of the criteria specified therein.

30. The CIT(A) however upheld the order of the AO. He held that u/s.5(2)(b) of the Act, income that is deemed to accrue or arise to a person who is non-resident, in India is taxable in India. He held

that the non- resident did not merely procure orders for the assessee but negotiated price and terms of the contact, opening of LC, shipment and payment and attend to queries in regard to shipment. Therefore the non-resident provided technical and consultancy services and hence the sum in question is taxable in India as it is deemed to have accrued and arisen to the non-resident in India. On the application of make available clause in Article 12(4)(b) of the Indo us treaty, the CIT(A) held that Mr.Neeraj Gupta had experience in patent litigation management and his services rendered to the assessee made available technical skill knowledge etc., to the assessee. The CIT(A) did not render any finding with regard to non taxability of the sum in India in the hands of Mr.Neeraj Gupta by virtue of Article 15 of the Indo US treaty.

31. Aggrieved by the order of the CIT(A), the assessee is in appeal before the Tribunal. Learned Counsel for the assessee reiterated the submissions made before the lower authorities. Learned Counsel for the assessee drew our attention to the invoices raised by Mr. Neeraj Gupta and pointed out that none of the services were rendered in India. Copy of the invoices is at page 327 of the assessee's Paper Book. Learned DR pointed out that Mr. Neeraj Gupta is a highly respected professional in IP world and IP litigation. Hence, the sales commission cannot be merely said to be sales commission and is in the nature of FTS. Learned DR drew our attention to clause 13 of the agreement of rendering services between the assessee and Mr. Neeraj Gupta dated 01.04.2015 wherein it was specifically provided that the assessee will be the owner of the IPR in all inventions conceived in whole or in part by the services of Mr. Neeraj Gupta. According to the Learned DR, this clause is clear evidence that technical services were not only rendered by Mr. Neeraj Gupta but those services made available technical skill, etc., to the assessee. She therefore submitted that the sum in question cannot be regarded as sales commission and was rightly treated as fees for technical services by the Revenue authorities.

32. We have given a careful consideration to the rival submissions. We shall take up the argument on the issue with reference to Indo US treaty, first. The findings on applicability of Article 12(4)(b) of the Indo US treaty while deciding the disallowance of sums paid to iRunway Inc., USA, will equally apply to this disallowance also, ie., the disallowance of payments made to Mr.Neeraj Gupta u/s.40(a)(ia) of the Act. Mr.Neeraj Gupta was paid commission on the basis of sales orders procured. Merely because he was technically qualified, sales commission paid for enabling sale cannot become payment for rendering technical services. Even in terms of Article 15 of the Indo US Treaty, the sum in question qualifies as that income derived by a person from the performance of professional services and therefore shall be taxed in the country of which he is resident except where the professional has a fixed base regularly available to him in India for the purpose of performing his activities or has stayed in India for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year. Admittedly, Mr. Neeraj Gupta did not satisfy the criteria as provided in Article 15 of the India-US Tax Treaty since neither he had a fixed base regularly available to him in India, neither he stayed even for a single day in India. Accordingly, sales commission paid to Mr. Neeraj Gupta is not taxable under Article 15 also of the India-US Tax Treaty as it does not satisfy either of the criteria specified therein. We therefore hold that the disallowance of the sum paid to him u/s.40(a)(ia) of the Act cannot be sustained and the addition is directed to be deleted.

33. The next issue that arises for consideration is as to whether the Revenue authorities were justified in disallowing a sum of Rs.1,19,305/- under section 40(a)(ia) of the Act on the ground that the assessee did not deduct tax at source on the provisions created towards professional charges. The facts as far as the aforesaid grounds is concerned are that during the financial year relevant to AY 2015-16, the assessee incurred certain expenses in the nature of professional charges. As per the mercantile system of accounting followed by it, the assessee had to accrue these expenses in its books of account as at 31 March 2015.In the absence of invoices from the relevant vendors, instead of crediting the 'liability account', the assessee recorded a provision for expenses of Rs. 1,170,000 as at 31 March 2015.On 1 April 2015, the assessee reversed the above provision for expenses of Rs. 1,170,000 and recorded the actual expenditure upon receipt of the relevant vendor invoice at a subsequent date. In the absence of invoices from the relevant vendors and the exact amount of expense, instead of recording these expenses by crediting a 'liability', the assessee had made a provision for expense by crediting 'expenses payable'. Further, since the vendor's right to receive such professional fees arose only after 31 March 2015 when an invoice was raised by it, the assessee did not deduct any taxes at source at the time of recording a provision as at 31 March 2015.

34. During the assessment proceedings, the AO directed the assessee to show-cause as to why provision for expenses of Rs. 1,170,000 should not be disallowed u/s 37 of the Act by holding it to be contingent in nature and u/s 40(a)(ia) of the Act since the assessee had not deducted tax at source on the provision made. The assessee submitted vide letter dated 21 November 2017 the basis on which such provision for expenses did not warrant a tax deduction at source as that the expense was recorded on estimate basis and that the actual invoices were not received. However, the AO disallowed provision for expenses u/s 40(a)(ia) of the Act since the assessee had not deducted tax at source on the provision made.

35. Before CIT(A), the assessee submitted that the assessee follows mercantile system of accounting as per which it would record for any expenses/ income on accrual basis in its books of account. Accordingly, the assessee has recorded a 'provision' towards certain expenses as at 31 March 2015. These amounts represented expenses for which services were availed of by the assessee during FY 2014-15 and thus, under the mercantile system of accounting the expenses were to be accrued during FY 2014-15 itself. In the absence of invoices from the relevant vendors and the exact amount of expense, instead of recording these expenses by crediting a 'liability', the assessee had made a provision for expense by crediting 'expenses payable'. The above provision towards expenses payable was reversed upon receipt of actual invoice and an accounting entry recording exact liability for such expenses were recorded as and when invoices were received from the relevant Vendors. Based on the above , the Assessee submits that there was no requirement to deduct tax on provision for professional fee and that it did qualify for deduction u/s 37 of the Act. The Assessee also placed reliance on the following decision in this regard:

> a) Decision of the jurisdictional Karnataka High Court in the case of ACTT v. Motor Industries Company (249 ITR 141). In the context of section 195 of the Act, the Hon'ble High Court, inter alia, held that:

> "It is only, thereafter, at the time of credit of any income to the account of the payee or at the time of payment thereof that the liability to deduct income-tax at source would arise on the part of the assessee."

(Our emphasis supplied)

b) Decision of the jurisdictional Bangalore bench of the ITAT in the case of Telco Construction Equipment Co. Ltd. [DCIT v. Telco Construction Equipment Co. Ltd. ITA No. 478/ Bang/ 2012]. In this case:

> The assessee company had recorded provision towards sales commission based on the sales made during the relevant year and the company did not deduct any tax on such provision since the same was not credited to the account of the agent. The ITAT held that, at the time of recording such expenditure, the company had credited the amount to provision account and not to the credit of respective agent's account. It further affirmed that the agents would get vested right to receive the commission only when they fulfill the obligations under the agreement for commission and accordingly held that provisions of section 194H of the Act could be applied only when the amount is credited to the agent account.
>
> (Our emphasis supplied) Based on the above discussions, the Assessee submitted that there was no requirement to deduct tax on provision for professional fee as at 31 March 2015 and therefore such provision ought not to be disallowed u/s 40(a)(ia) / 37 of the Act.
>
> 36. Without prejudice to the above, it was submitted that provision towards professional charges ought to be disallowed u/s 40(a)(ia) of the Act, the AO erred in disallowing 100% of the provision made, instead of 30%, as required u/s 40(a)(ia) of the Act vide amendment made by Finance Act, 2014 w.e.f. 1 April 2015. Without prejudice to the above grounds, and even assuming while denying, that provision towards professional charges ought to be disallowed u/s 37/ 40(a)(ia) of the Act for AY 15-16, a deduction for the corresponding reversal of provision in the subsequent year, viz., AY 2016-17 ought to be allowed to the Assessee.
>
> 37. The CIT(A) however upheld the order of the AO by following the decision of ITAT Bangalore in the case of IBM India (P) Ltd. (2015) 59 taxmann.com 107 wherein it was held that even in respect of provision for expenses made in the books of accounts, the assessee had to deduct tax at source at the time of entry to the suspense account. Hence the present appeal by the assessee before the Tribunal. Learned Counsel for the assessee reiterated submissions made before the Revenue authorities.

Learned DR relied on the order of the CIT(A).

38. We are of the view that the statutory provisions require deduction of tax at source even when the nomenclature used by the assessee for describing as an expenditure as in the nature of suspense account or a profession. The learned Counsel for the assessee however made a prayer that if the disallowance is upheld, the same amount should not be disallowed when the provision is reversed on the first day of April of the subsequent Assessment Year as doing so would result in double disallowance. The prayer so made by the learned Counsel for the assessee is accepted and the AO is directed to ensure that there is no double disallowance of the same amount. With these observations, we dismiss this issue also.

39. The other grounds with regard to levy of interest under section 234B and 234C are purely consequential. The AO is directed to give consequential relief.

40. In the result, appeal of the assessee is partly allowed.

Pronounced in the open court on the date mentioned on the caption page.

Sd/-	Sd/-
(S. PADMAVATHY)	(N.V. VASUDEVAN)
Accountant Member	Vice President

Bangalore,
Dated: 27.04.2022.
/NS/*

Copy to:

1.	Assessees	2.	Respondent
3.	CIT	4.	CIT(A)
5.	DR	6.	Guard file

By order

Assistant Registrar,
ITAT, Bangalore.