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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ W.P.(C) 7753/2024

COMPONENTSOURCE COMPANY LTD. ..... Petitioner

Through: Mr. Salil Kapoor, Mr. Shivam Yadav, Ms. Ananya Kapoor, Mr. Sumit Lalchandani and Mr. Vibhu Jain, Advocates

versus

ASSISTANT COMMISSIONER OF INCOME TAX, CIRCLE INT TAX 1(2)(1), NEW DELHI ..... Respondent

Through: Mr. Aseem Chawla, Senior Standing Counsel for Revenue

CORAM:
HON'BLE MR. JUSTICE YASHWANT VARMA
HON'BLE MR. JUSTICE PURUSHAINDRA KUMAR KAURAV

O R D E R

% **27.05.2024**

CM APPL 32153/2024 (Exemption)

Allowed, subject to all just exceptions.

The application stands disposed of.

W.P.(C) 7753/2024 and CM APPL 32152/2024 (Stay)

1. The writ petitioner impugns the reassessment action initiated in terms of notice issued under Section 148 of the Income Tax Act, 1961 ["**Act**"] dated 28 March 2024. As would be evident from the record, a notice referable to Section 148A(b) of the Act came to be issued against the petitioner on 24 February 2024. The same was based on material gleaned from the Non-Filing Monitoring System of the Department and pertaining to Assessment Year ["**AY**"] 2020-21.

2. The respondents took the position that on the basis of the

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information appearing on the Insight Portal it appears that various payments were made to the writ petitioner and in respect of which tax had been deducted at source by various entities. It, accordingly, alleged that income amounting to INR 6,52,46,913/- remained unexplained and appears to have escaped assessment.

3. In response to the aforesaid notice the petitioner in terms of its reply dated 12 March 2024 explained that it was an overseas entity incorporated in Japan and is engaged in the supply of software. It was further averred that it procures software from its vendors on a principal-to-principal basis for purposes of sale/re-sale to its customers situate across the globe including India. The petitioners further asserted that in the course of that sale no right to reproduce, sub-licence, modify or translate any software is transferred.

4. Insofar as the question of taxability of income was concerned, the petitioner asserted that even if the income so generated were to be viewed as business income, the same would not be taxable in the absence of a Permanent Establishment ["**PE**"] of the petitioner existing in India. Benefit was thus claimed of the provisions contained in the India-Japan Double Taxation Avoidance Agreement ["**DTAA**"].

5. We take note of the specific stand taken in this regard in the reply dated 12 March 2024:

> "**4.1** The income earned by the Assessee from the sale/trade of the canned software is not liable to tax under Article 5, read with Article 7 of the DTAA as entered between India and Japan, because of the fact that the Assessee does not have any permanent establishment in India and in the absence of any PE the income as earned under the Article Business Income is not liable to tax in India. Reliance in this regard is placed upon the below mentioned judgements of the Hon'ble Apex Court:
>
> I. **Director of Income-tax (International Taxation) vs. Organ Stanley & Co.** reported as [2007] 162 Taxman 165 (SC)

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II. **Formula One World Championship Ltd. vs. Commissioner of Income-tax, (International Taxation)-3**, Delhi [2017] 80 taxmann.com 347 (SC)

III. **Ishikawajma-Harima Heavy Industries Ltd. vs. Director of Income-tax** reported as [2007] 158 Taxman 259 (SC)

IV. **Hyundai Heavy Industries Co. Ltd. vs. Director of Income-tax (International Taxation)** reported as [2007] 161 Taxman 191 (SC)

4.2 From the bare perusal of the captioned judgment, you will appreciate that the Hon'ble Apex Court has been consistent in its stand that the existence of a PE is a prerequisite for taxing the business profits in the source country. Hence, in the case at hand, as there is no PE in India (of any type), the Business Income earned from Indian customers is not chargeable to tax in India.

4.3 At the cost of duplicity, we would like to bring on record that the question of un-explained income only arise when the income is chargeable to tax and the Assessee intentionally or otherwise conceals the same, in the case at hand the income per se is non-taxable on account of the benefit available to the Assessee under the DTAA as entered between India and Japan which takes out the income as earned by the Assessee from Indian customers from the tax net of Income-tax Act as the income as earned by the Assessee is neither royalty nor business income as per the respective Articles of the DDTAA. Hence, the question of unexplained income dies not arise in the case at hand."

6. However, and while passing an order under Section 148A(d) of the Act the respondent has observed as under:

6. The assessee in its reply has claimed that no income is chargeable to tax in India and hence return not been filed but the assessee has not submit the copy of agreement, the end user license agreement or any other document to substantiate the nature of the software being sold. <u>Further the assessee has claimed that the royalty from the software is not taxable but the same needs verification of the nature of business and the product of the software.</u>

<u>Further, whether the assessee has a Permanent Establishment or not during the year under consideration is a question of fact and law and hence need to be verified.</u>

Further, the assessee has claimed that the income is exempt but since the assessee has not been filed ITR thus income neither be claimed on exempt nor justified to be so.

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> The assessee was required to file the ITR, declaring the income and justifying the claim that the income is exempt for India.
>
> Hence, prime facia it appears that assessee has not substantiated the non taxability of the receipts received by it."

7. We find ourselves unable to sustain the initiation of reassessment action bearing in mind the evident failure on the part of the respondent to deal with the fundamental challenge to reassessment as were raised by the petitioner. As would be evident from a perusal of the reply which was submitted to the Section 148A(b) notice, the petitioner had specifically alluded to the judgment rendered by the Supreme Court in **Engineering Analysis Centre of Excellence (P.) Ltd. vs. CIT** [(2021) 432 ITR 471(SC)] to contend that the monies received from the sale/re-sale of shrink-wrapped software would not amount to royalty so as to be taxable. It had additionally also questioned the initiation of action based on its assertion of no PE existing in India.

8. However, and as is evident from para 6 of the order under Section 148A(d) extracted above, those objections have been perfunctorily disposed of with the respondent observing that whether the revenue earned from the sale of software would amount to royalty would require further verification. Similarly, while dealing with the issue of PE it has chosen to observe that the same "*is a question of fact and law and hence need to be verified*".

9. In our considered opinion, the respondent has clearly failed to deal with objections which struck at the very root of assumption of jurisdiction. Findings on the aspect of royalty and PE could not have been deferred or made subject matter of further verification. This since at the stage of initiating action under Section 148, the respondent must

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be subjectively satisfied that income which was taxable has in fact escaped assessment. This aspect of criticality has clearly been ignored by the respondent while passing the impugned order.

10. Accordingly, and for all the aforesaid reasons, we allow the instant writ petition and quash the order passed under Section 148A(d) and notice under Section 148 of the Act, both dated 28 March 2024.

11. The matter shall consequently stand revived at the desk of the AO for being considered afresh and from the stage of the reply of the writ petitioner. All rights and contentions of respective parties are kept open.

YASHWANT VARMA, J.

PURUSHAINDRA KUMAR KAURAV, J.

MAY 27, 2024/kk

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