

**IN THE INCOME TAX APPELLATE TRIBUNAL
'C' BENCH, BENGALURU**

**BEFORE SHRI SUNIL KUMAR YADAV, JUDICIAL MEMBER
and
SHRI INTURI RAMA RAO, ACCOUNTANT MEMBER**

Sl. No	ITA No. & Asst. year	Appellant	Respondent
1	193/Bang/2010 (2008-09)	M/s.ANZ Operations & Technology Pvt. Ltd. Embassy Gold Links Business Park, Off Intermediate Ring Road, Bangalore-560071. <i>PAN:AABCA 9002G</i>	Deputy Commissioner of Income-tax, Circle 1(1), Bengaluru.
2	IT(IT)A No. 1508/Bang/2012 (2008-09)	-do-	Deputy Director of Income-tax, International Taxation, Circle 1(1), Bengaluru.
3	156/Bang/2010 (2007-08)	M/s.Jubilant Biosys Ltd. Plot 1A, Sector-16A, Noida-201301(UP) <i>PAN: AAACJ 9445 P</i>	Income-tax Officer (International Taxation), Ward 1(2), Bengaluru.
4	610/Bang/2010 (2007-08)	-do-	-do-
5	157/Bang/2010 (2008-09)	-do-	-do-
6	611/Bang/2010 (2008-09)	-do-	-do-

Assessee by : Shri Kaushik Mukherjee, CA.
Revenue by : Dr. P.V.Pradeep Kumar, Addl.CIT

Date of hearing : 08/01/2018
Date of pronouncement : 23/03/2018

O R D E R

Per BENCH :

These are appeals filed by M/s.ANZ Operations & Technology Pvt. Ltd. and M/s.Jubilant Biosys Ltd., directed against different orders of the learned Commissioner of Income-tax (Appeals)-IV, Bengaluru [CIT(A)], for the assessment years 2007-08 and 2008-09. Sine common issue is involved in all these appeals, we proceed to dispose of the same by way of this consolidated order. For the sake of clarity and convenience, facts

relevant in ITA No.193/Bang/2010 for assessment year 2008-09 are stated herein.

2. Briefly facts of the case are that the assessee is a company duly incorporated under the provisions of the Companies Act, 1956. It is engaged in the business of providing IT and IT enabled Services. During the financial year 2007-08, the assessee made the following remittances to its parent company ANZ Banking Group Ltd. Australia towards purchase of software.

<i>Sl.No.</i>	<i>Date of remittance</i>	<i>Amount (in AUD)</i>	<i>Amount (in INR)</i>
1	10/10/2007	504,316	1,78,07,425
2	10/10/2007	616,351	2,17,62,806

It was contended before the TDS Officer that remittance was in the nature of reimbursement of cost for providing software license. The parent company viz., M/s.ANZ Banking group, Melbourne had entered into agreement with Microsoft Pte. Ltd., Singapore for purchase of license. It was further stated that the assessee also utilized software license and cost pertaining to appellant had been charged by the parent company and the same was reimbursed by the appellant. It was further contended that payments were not subject to tax in India as the same were on cost to cost basis and no income element is embedded in it. Without prejudice to this, it was contended that the payment was towards purchase of off-shelf software which is not chargeable to tax in the hands of software vendor. It was further contended that payment cannot be characterized as royalty in terms of Article 12 of DTAA as the payment was in the nature of cost towards use of copy-righted article not towards use of copy-right.

3. The said contentions have been rejected by the TDS officer by holding that software is intellectual property which can be licensed to user and the consideration paid is only towards license for use. The TDS officer concluded that the payment was towards royalty which is taxable in India. As regards alternative contention of the appellant the TDS officer held that same is not in the nature of reimbursement of cost. The TDS officer rejected it by holding that appellant had failed to substantiate same by leading necessary evidence. Accordingly, the TDS officer held

the assessee as the 'assessee in default' for not deducting tax at source and remitting same to the account of the Government account and accordingly passed orders u/s 201(1) and 201(1A) of the Income-tax Act, 1961 [hereinafter referred to as 'the Act' for short] dated 29/08/2008 demanding tax at the rate of 10% of the remittance amount and the interest thereon.

4. Being aggrieved, an appeal was preferred before the Id.CIT(A) who, vide impugned order, dismissed the appeal by holding as under:

“...It is evident that the term "royalty" under the relevant DTAA refers to payments of any kind received as **consideration for the use of, or the right to use**, any copyright, patent, invention, model, design, secret formula or process etc. The appellant is not correct in trying to restrict the meaning of the term "royalty" to consideration for the use or right to use any copyright alone, especially when the provisions of the Act as well as the relevant DTAA clearly lay down that it is the consideration paid for grant of the right to the use of not merely a copyright, but also patent, invention, model, design, secret formula or process etc. In this connection, a reference may be made to the explanatory notes on the provisions of Explanation 2 to Section 9(1)(vi) when they were introduced. In Para 15.5 of CBDT Circular No.202 dated 05.07.1976 [source: 105 ITR 27 (St.)], it has been made clear that *"the definition (in Explanation 2) is wide enough to cover both industrial royalties and copyright royalties"*. Therefore, it can be seen that the legislative intent is not to restrict the scope of 'royalty' but *rather to make it wider*. Since the provisions of the Act and the relevant DTAA are very clear on this point, no reference is required to the provisions of the Copyright Act or to any other source. In view of this, it is not necessary even to refer to the OECD model and commentaries etc. as per law explained by the Hon'ble Apex Court in the case of *CIT v. P.V.A.L.Kulandagan 276 ITR 654 (SC)*. Accordingly, the reliance placed by the appellant on OECD commentaries and the US IRS Regulations is of no help to its case. It may be noted that the revised OECD commentary on software payment has not been accepted even by some of the OECD member countries and that the said commentary in any case cannot have precedence over the unambiguous and unequivocal statutory provisions of Section 9(1)(vi) of the Act.

4.3.6 It is now proposed to examine the applicability of various judicial decision cited by the appellant in support of its case. The decision in case of *Dunlop Rubber Co.* has already been distinguished by the AO in Para 6.5 on Page 18 of his order and needs no repetition. It is observed that the facts of the instant case have nothing in common with those in *Owen v. Pook* (supra) which was concerned

with the assessability to tax of the travelling allowance paid to a doctor on standby duty for attending emergency cases. This case has no relevance at all to the instant case. Likewise, ***Handicrafts and Handloom Export Corporation*** is also distinguishable on facts. The issue for determination in that case was whether the amount received by the assessee corporation from the State Trading Corporation of India towards reimbursement of the loss was assessable under the Act. No such question is obviously involved in the present case. In case of ***Industrial Engineering Projects***, not only are the facts different but the Hon'ble Tribunal has also recorded a finding that the amounts received were reimbursement of expenses. However, in the instant case, the appellant has not been able to establish that the impugned remittance to the ANZ Group is in the nature of reimbursement. As regards the judgment of Hon'ble Supreme Court of India in the case of ***Tata Consultancy Services***, it is observed that the decision in that case was rendered by the Hon'ble Apex Court in a sales tax matter. The issue under consideration was whether sale of disc/floppy containing software programme amounted to sale of goods under the Andhra Pradesh General Sales Tax, 1957. It may be mentioned that the legislative scheme of sales tax and income-tax law is very different. It would not be appropriate to apply ratio of that decision rendered in the context of Sales Tax law of Andhra Pradesh to the facts of the instance case in the context of the Act as well as the relevant DTAA. The ratio decidendi of a court decision which has binding authority must be read in the light of the facts of the case and the issue considered. In this regard, the following observation of the Hon'ble Supreme Court in ***CIT v. Sun Engineering Works Pvt. Ltd. (1992) 198 ITR297 (SC)*** deserves to be kept in mind:-

"It is neither desirable nor permissible to pick out a word or a sentence from the judgment of this Court, divorced from the context of question under consideration and treat it to be the complete 'law' declared by this Court"

4.3.8 In view of the aforesaid discussion, it is clear that payments made by the appellant to ANZ Group for software licenses would be termed as "royalty" u/s 9(1)(vi) of the Act as well as Article 12(3) of the relevant DTAA and would, therefore, constitute income chargeable under the Act in the hands of the recipient, namely, ANZ Group. Thus, the appellant was under a statutory obligation to deduct tax in terms of Section 195(1) on the impugned remittances. Since the appellant failed to do so, the action of the AO in treating the appellant as an assessee in default u/s 201(1) in respect of tax deductible at source 195(1) on the remittances made to ANZ Group and levying interest u/s 201(1A) of the Act for the period of default is upheld. Grounds bearing Nos.1 to 8 are found to be devoid of merit and are accordingly dismissed.ö

5. Being aggrieved by this order, the assessee is in appeal before us raising following grounds of appeal:

- I. The learned Commissioner of Income-tax (Appeals) ["CIT(A)"] has erred in affirming the order of the Deputy Director Of Income-tax, International Taxation, Circle 1(1), Bangalore ["DDIT"] and thereby treating the Appellant as an assessee in default under section 201(1) of the Income-tax Act, 1961 ("IT Act").
- II. The learned CIT(A) has erred in upholding the demand notice of Rs.4,352,725 (including Rs.395,702 towards Interest) issued by the DDIT as being payable by the Appellant.
- III. The order of the learned CIT(A) in so far as it is prejudicial to the interest of the Appellant is bad in law and in facts.
- IV. That on the facts and in the circumstances of the case, the learned CIT(A) has erred in determining the remittances made by the Appellant towards provision of standard software to ANZ Group to be in the nature of Royalty by treating it as a consideration received towards transfer of Copyright /Patent/ Invention/Design/Scientific Work/Secret formula or process.
- V. The learned CIT(A) has erred in treating the Appellant as an assessee in default and not appreciating that the remittances by the Appellant were made after duly obtaining a certificate from a Chartered Accountant to the effect, in accordance with the procedure laid down under section 195 of the IT Act.
- VI. The learned CIT(A) has erred in not considering the judicial precedents relied upon by the Appellant in support of its contention that remittances to ANZ Group ought not to be subject to withholding tax in India.
- VII. The Learned CIT(A) has erred in disregarding the submissions made by the Appellant distinguishing the applicability of the decision of Samsung Electronics Co. Ltd. and Ors.¹ to its case.
- VIII The Learned CIT(A) has erred in holding that the Assessing Officer ('AO') is right in holding the Appellant as an assessee in default only for the reason that the Appellant has not approached the AO for grant of an appropriate certificate under section 195(2) of the IT Act.

All of the aforesaid grounds are independent and without prejudice to one another. Further, the Appellant craves leave to alter, amend, modify, amplify or withdraw any or all the above grounds of appeal, or add any further grounds, before or during the hearing of the appeal.

6. Learned AR of the assessee submitted that the remittances are towards purchase of shrink-wrap software which is not in the nature royalty. He relied on the following judicial precedents:

- Motorola Inc., Ericsson Radio Systems AB & Nokia Networks OY v. DCIT [(2005) 95 ITD 269 (Del ITAT) (SB)]
- Samsung Electronics Co. Ltd v. ITO [(2005) 94 ITD 91 (Bang ITAT)];
- Sonata Information Technology Ltd. v. Addl. CIT [(2006) 103 ITD 324 (Bang ITAT)];
- Sonata Software Ltd. v. ITO [(2006) 6 SOT 700 (Bang ITAT)] ;
- Hewlett-Packard (India) Pvt. Ltd. v. ITO [(2006) 5 SOT 660 (Bang ITAT)]

7. It was further submitted that it is only by the Finance Act, 2012, Explanation 2 to section 9(1)(vi) inserted with retrospective effect from June 1, 1976 whereby it was clarified that user or right to use computer software including granting of license is treated as royalty under the provisions of section 9(1)(vi) of the Act. Thus it was contended that when the remittance was made, the said Explanation was not in existence. The assessee could not have contemplated such amendment and the assessee cannot be expected to perform an act which is impossible to perform based on the maxim *lex non cogit ad impossibilia*. It was further contended that under the DTAA with Australia, the term 'royalty' has been defined in Article 12 of the Treaty to mean that use of right to mean payments of any kind received as a consideration for the use of, or right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof. In the present case, there is no transfer of copyright. It is only towards copy-righted article and not for use of copy-right. Therefore, even under DTAA, impugned payment cannot be characterized as royalty payment, therefore, no obligation to deduct tax at source. Finally, it is contended that when the assessee was under bona fide belief that there was no liability to deduct tax at source, assessee cannot be treated as an 'assessee in default'.

8. On the other hand, Id. Addl.CIT(DR) submitted that in light of the decision of the Hon'ble jurisdictional High Court in the case of *CIT vs. Samsung Electronics Co.Ltd.*(345 ITR 494)(Kar) and *CIT vs. Synopsis International Ltd.* (212 Taxman 454)(Kar) subject remittances are in the nature of royalty.

9. We heard rival submissions and perused the material on record. The only issue in the present appeal is whether remittances made for the

purpose of importing of software can be treated as a payment towards royalty thereby attracting liability to deduct tax at source u/s 195 of the Act. This issue is no longer *res integra* as the Hon'ble High Court in the case of *Samsung* (supra) held as under:

“14. It is clear from the scrutiny of the material on record, the fact that respondent-company has imported software from the non-resident is not in dispute. It is also not in dispute having regard to the contention of the assessee and the revenue and the counsel appearing for them that the assessee has acquired right to use the copyrighted article. It is also not in dispute that software which is in legal parlance called computer program is categorized as copyright in India and therefore software-computer program is copyrighted and copyright vests with the foreign supplier. However, substance of the argument of the revenue is that assessee was given right to use the software and the amount paid towards the same would constitute royalty within the meaning of Section 9(1)(vi) read with *Explanation* (2) of the Act and relevant clauses of DTAA agreement. However, according to the assessee respondent-company in all the appeals, the payment made does not come within the purview of royalty under Section 9(1)(vi) of the Act or within the provisions of the Act or clauses in DTAA, and what is purchased is an article which is taxable as business income and since exporter - non-resident is not having permanent establishment in India, such income which is accrued in India is not taxable, in any event, payment would not amount to royalty. Therefore, before considering the rival contentions of learned counsel appearing for the parties to find out as to whether the payment made by the respondent with foreign company would amount to 'royalty' or not, it is necessary to reproduce the definition 'royalty' and the circumstances under which the said payment is taxable in India so as to cast the obligation on the respondent-assessee to make deduction and also the provisions of DTAA in various countries regarding royalty.

15. It may also be noted at this stage itself that if is well settled that while considering the decision of the Hon'ble Supreme Court, the same cannot be considered *de hors* the context in which it was rendered and it is necessary to ascertain the *ratio decidendi* laid down in the said case. In *Sun Engineering Works (P.) Ltd.*'s case (supra), the Hon'ble Supreme Court has held as under:-

"It is neither desirable nor permissible to pick out a word or a sentence from the judgment of this court, divorced from the context of the question under consideration and treat it to be the complete "law" declared by this court. The judgment must be read as a whole and the observations from the judgment have to be considered in the light of the questions which were before this court. A decision of this court takes its colour from the questions involved in the case in which it is rendered and, while applying the decision to a later case, the courts must carefully try to ascertain the true principle laid down by the decision of this court and not to pick out words or sentences from the judgment, divorced from the context of the questions under consideration by this court, to support their

reasonings. In *Madhav Rao Jivaji Rao Scindia Bahadur v. Union of India* [1971] 3 SCR 9; AIR 1971 SC 530, this court cautioned (at page 578 of AIR 1971 SC):

"It is not proper to regard a word, a clause or a sentence occurring in a judgment of the Supreme Court, divorced from its context, as containing a full exposition of the law on a question when the question did not even fall to be answered in that judgment."

Section 90 of the Income Tax Act, which deals with agreement with foreign countries or specified territories reads as under:

90. (1) The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India, -

- (a) for the granting of relief in respect of-
 - (i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or
 - (ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or
- (b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory, as the case may be, or
- (c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or
- (d) for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be,

and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

(2) Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

Explanation 1.- For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate

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at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

Explanation 2.- For the purposes of this section, "specified territory" means any area outside India which may be notified as such by the Central Government."

Section 245S of the Act which deals with Applicability of Advance ruling reads as under: -

"245S.(1) The advance ruling pronounced by the Authority under section 245R shall be binding only-

- (a) on the applicant who had sought it;
- (b) in respect of the transaction in relation to which the ruling had been sought; and
- (c) on the Commissioner, and the income-tax authorities subordinate to him, in respect of the applicant and the said transaction.

(2) The advance ruling referred to in sub-section (1) shall be binding as aforesaid unless there is a change in law or facts on the basis of which the advance ruling has been pronounced."

15.1 Section 9 of the Act deals with income deemed to accrue or arise in India, which reads as under:

9. (1) The following incomes shall be deemed to accrue or arise in India:-

- (i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

Section 9(1)(vi) of the Act reads as under:

(vi) income by way of royalty payable by-

- (a) the Government; or
- (b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of 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; or
- (c) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India:

Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April 1997, and the agreement is approved by the Central Government:

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Provided further that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any right (including the granting of a license) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development and Training, 1986 of the Government of India.

Explanation (2) reads as under:

Explanation 2. - For the purposes of this clause, "royalty" means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for -

- (i) the transfer of all or any rights (including the granting of a license) 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;
- [(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB,]
- (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 [(iv), (iva) and] (v).

The definition of the term 'royalty' is similar in all the DTAA agreements entered into with foreign countries and the same reads as under:

"Payment of any kind received as consideration for the use of, or the right to use, any copyright of a literary, artistic or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use or disposition hereof."

16. The Hon'ble Supreme Court in *Azadi Bachao Andolan's* case (*supra*) has laid down that provisions of DTAA prevails over the provisions of the Act if

the provisions of DTAA is more beneficial to the assessee. It is clear on perusal of the definition of 'royalty' under the Act and the DTAA as culled out above, the definition of 'royalty' is restrictive in DTAA whereas, the definition of 'royalty' under the Act is broader in its content. Therefore, the definition of 'royalty' in DTAA is more beneficial to the assessee as according to the assessee, payment is not royalty and therefore, the royalty in the restricted meaning under DTAA is more beneficial to the assessee and hence, we have to find out as to whether the payment made by the respondent, would amount to royalty under the clause in DTAA. Even otherwise, it is clear that if the payment is held to be royalty within the restricted meaning given to the term in the DTAA, naturally, it would also to be covered within the term 'royalty' in the broader meaning to the term 'royalty' under the Act.

17. It is clear from the scrutiny of the material on record and the contentions of the parties *viz.*, revenue and the respective respondent in these cases that the fact that payments have been made by the respondent herein to non-resident for having imported shrink wrapped software/off-the-shelf software is not disputed. There is also no dispute that no tax was deducted at source by the respondent under Section 195(1) of the Act in respect of such payments on the ground that the same were made for the purpose of purchase of shrink wrapped software/off-the-shelf software. It is contended by the respondent that since there is no permanent establishment of the non-resident in India, the said payments have to be treated as income from business and is not taxable under the Income Tax Act in India and consequently, there is no obligation on the part of the respondent to deduct the advance tax under Section 195 of the Act and also consequential proceedings would not be attracted. Therefore, the dispute between the revenue and the respondent in these cases is whether payments made by the respondent to the non-resident would constitute 'royalty' or 'Income from Business' and if it is to be treated as 'Income from Business', whether the non-resident is required to have a permanent establishment in India. Further, in the absence of any permanent establishment of the non-resident in India, is there no obligation on the part of the payee, the respondent herein to deduct tax at source under Section 195 of the Act. Therefore, the fact that the payments made by the payee, the respondent herein to the non-resident would constitute income of the non-resident is indisputable. However, the dispute is as to whether such income in the hands of the non-resident is to be treated as sale and income from business covered under Article 7 of the DTAA with respective countries or whether the payments would amount to royalty in the hands of the non-resident, for which no permanent establishment is required for making payment in India. There is also no dispute that if the payments made by the respondent are held to be royalty and not 'Income from Business', there is an obligation on the part of the payee, the respondent herein to deduct the tax at source and in default, the respondent herein would be considered as a default assessee. Once there is an obligation to deduct tax at source under Section 195 of the Act, which imposes a statutory right on any person responsible for paying to a non-resident, any interest (not being interest on securities) or any other sum (not being dividend) chargeable under the provisions of the Act, to deduct income-tax at the rates in force unless he is liable to pay income-tax thereon as an agent. Payment to non-residents by way of royalty and payment for technical services rendered in India are common

examples of sums chargeable under the provisions of the Act to which the aforesaid requirement of TDS applies. The tax so collected and deducted is required to be paid to the credit of Central Government in terms of Section 200 of the Act read with rule 30 of the Income Tax Rules, 1962. Failure to deduct tax or failure to pay tax would also render a person liable to penalty under Section 201 read with Section 221 of the Act. In addition, he would also be liable under Section 201(1A) to pay simple interest at 12 per cent per annum on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid. Therefore, if the amount is held to be royalty, the other consequences as referred to above would follow.

18. In view of the substantial question of law framed by the Hon'ble Supreme Court to be adjudicated in these appeals and the above said contentions of the learned counsel appearing for the parties, the only contention which is required to be considered is as to whether the payments made by the respondent - payee to a non-resident includes the amount chargeable to tax under the Act and if so, is there an obligation on the part of the respondent to make a deduction under Section 195(1) of the Act or as to whether the said payments would only amount to sale of the shrink wrapped software or off-the-shelf software and would constitute income from business in the office of the non-resident and in the absence of any permanent establishment of the non-resident in India, the same would not impose any obligation on the part of the payee, the respondent herein to deduct tax at source under Section 195 of the Act and consequently, they cannot be treated as default assesseees as referred to above.

19. In view of the above said observations and the contents of the DTAA with different Countries, wherein definition of 'royalty' is common in all the agreements, it is necessary to reproduce the said definition of 'royalty' in clause 12 of the DTAA, which reads as under:-

"Article 12 of DTAA WITH USA:

Article 12: Royalties and fees for included services

1. Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

[** ** **

3. The term "**royalties**" as used in this article means:

(a) payments of any kind received as consideration for the use of or the right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trade mark, design or model plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use or disposition thereof and

(b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial or scientific equipment, other than payments derived by an

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enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(c) or 3 of article 8."

In view of the above said definition of 'royalty', it is clear that the necessary ingredient to be satisfied to find out: as to whether the payment would amount to "royalty" is as follows:-

- payment of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work.

It has been universally accepted that a literary work is entitled to copyright and wherefore, a literary work is entitled to be registered as copyright. In India, the provisions of Section 2(o) of the Copyright Act, 1957 defines 'literary work' as under:-

"literary work" includes computer programmes, tables and compilations including computer [databases];

Therefore, "computer software" has been recognized as copy right work in India also.

20. Having regard to the above said definition of 'royalty', we have to consider the contents of software licence agreement entered into by non-resident with Samsung Electronics and also respondents in the case represented by Sri Ganesh, learned senior counsel and Sri Aravind Dattar, wherein it is a case of purchase, sale or distribution or otherwise of the off-the-shelf software. It is described as a 'software licence agreement', wherein it is averred that customer accepts an individual, non-transferable and non-exclusive licence to use the licensed software program(s) program(s) on the terms and conditions enumerated in the agreement. It is further averred that the customer - Samsung Electronics shall protect confidential information and shall not remove any copyright, confidentiality or other proprietary rights provided by the non-resident. However, what is granted under the said licence is only a licence to use the software for internal business without having any right for making any alteration or reverse engineering or creating sub-licences. What is transferred under the said licence is the licence to use the software and copyright continue to be with the non-resident as per the agreement. Even as per the agreement entered into with the other distributors as also the end-user licence agreement, it is clear that the distributor would get exclusive non-transferable licence within the territory for which he is appointed and he has got right to distribute *via* resellers the Software, upon payment of the licenses set forth in Exhibit A to the agreement only to End Users pursuant to a valid Actuate shrinkwrap or other Actuate license agreement and except as expressly set forth in the said agreement, distributor may not rent, lease, loan, sell or otherwise distribute the Software the Documentation or any derivative works based upon the Software or Documentation in whole or in part. Distributor shall not reverse engineer, decompile, or otherwise attempt to derive or modify the source code for the Software. Distributor shall have no rights to the Software other than the rights expressly set forth in the agreement. Distributor shall not modify or copy any part of the Software or Documentation. Distributor may not use sub-distributors for further distribution of the Software and Documentation without the prior consent of Actuate. What is charged is the licence fee to be paid by the Distributor of the Software as enumerated in

Exhibit A to the agreement. Further, Clause 6.01 of the agreement dealing with title states that the Distributor acknowledges that Actuate and its suppliers retain all right, title and interest in and to the original, and any copies (by whomever produced), of the Software or Documentation and ownership of all patent copyright, trademark, trade secret and other intellectual property rights pertaining thereto, shall be and remain the sole property of Actuate. Distributor shall not be an owner of any copies of, or any interest in, the Software, but rather is licenced pursuant to the Agreement to use and distribute such copies. Actuate represents that it has the right to enter into the Agreement and grant the licences provided therein and confidentiality is protected. Therefore, on reading the contents of the respective agreement entered into by the respondents with the non-resident, it is clear that under the agreement, what is transferred is only a licence to use the copyright belonging to the non-resident subject to the terms and conditions of the agreement as referred to above and the non-resident supplier continues to be the owner of the copyright and all other intellectual property rights. It is well settled that copyright is a negative right. It is an umbrella of many rights and licence is granted for making use of the copyright in respect of shrink wrapped software/off-the-shelf software under the respective agreement, which authorizes the end user *i.e.*, the customer to make use of the copyright software contained in the said software, which is purchased off the shelf or imported as shrink wrapped software and the same would amount to transfer of part of the copyright and transfer of right to use the copyright for internal business as per the terms and conditions of the agreement. Therefore, the contention of the learned senior counsel appearing for the respondents that there is no transfer of copyright or any part thereof under the agreements entered into by the respondent with the non-resident supplier of software cannot be accepted.

21. It is further contended by the learned senior counsel appearing for the respondents that in view of the fact that what is supplied by the non-resident to the respondent in India is only a shrink wrapped software/off-the-shelf software, which is not customised to suit the needs of the respondent, the said software is to be treated as goods and there is sale of the software and copy of the software. Therefore, the question of paying any royalty would not arise. In support of the said contention, the learned senior counsel appearing for the respondents has strongly relied upon the decision of the Hon'ble Supreme Court in *Tata Consultancy Services'* case (*supra*) (hereinafter referred to as the TCS's case), wherein the Hon'ble Supreme Court was considering the question as to whether the canned software sold by the appellants can be termed to be "goods" and as such assessable to sales tax under the Andhra Pradesh General Sales Tax Act, 1957. Having regard to the broad definition of 'goods' under Section 2(h) of the said Act and also the provisions of Article 366(12) of the Constitution of India, the Hon'ble Supreme Court was pleased to answer the said question for determination by holding that once the 'information' or 'knowledge' is transformed into physical existence and recorded in physical form, it is corporeal property. The physical recording of the software is not an incorporeal right to be comprehended and accordingly, held that the software marketed by the appellants therein indisputably was canned software and thus, sale of the same would attract the provisions of the Andhra Pradesh General Sales Tax Act, 1957.

22. The question as to whether the payment made for import of software or supply of software by the non-resident Companies was royalty or not was not at all in issue in TCS's case and the question was whether canned software sold by the appellants therein amounted to sale of goods under the Andhra Pradesh General Sales Tax Act. Further, the issue of transfer of right to use the goods as per the expanded definition of 'sale' did not come up for consideration in that case. On the other hand the issue in the present case is as to whether the payment would amount to 'royalty' within the meaning of Income Tax Act and DTAA. In the said TCS's case, it has been held that copyright in computer program may remain with the originator of the program, but, the moment copies are made and marketed, it becomes goods, which are susceptible to tax. The contention of the assessee that the consideration received by the non-resident supplier towards the software products would amount to 'royalty' within the meaning of DTAA with respective country was not at all considered in the said case. Therefore, the said decision in TCS's case is not helpful to the respondents in the present cases. It is well settled that the intent of the legislature in imposing Sales Tax and Income Tax are entirely different as Income Tax is a direct tax and Sales Tax is an Indirect Tax and wherefore, mere finding that the computer software would be included within the term 'Sales Tax' would not preclude this Court from holding that the said payments made by the respondents to the non-resident Company in the present cases would amount to 'royalty' unless the respondents are able to prove that the said payment is for the sale of computer software, wherein the income would be from the business and in the absence of any permanent establishment of the non-resident supplier, there is no obligation on the part of the payee to make deduction under Section 195(1) of the Act.

23. It is well settled that in the absence of any definition of 'copyright' in the Income Tax Act or DTAA with the respective Countries, in view of clause 3 of the DTAA, reference is to be made to the respective law regarding definition of 'Copyright', namely, Copyright Act, 1957, in India, wherein it is clearly stated that "literary work" includes computer programmes, tables and compilations including computer [databases]. Section 16 of the Copyright Act, 1957 states that no person shall be entitled to copyright or any similar right in any work, whether published or unpublished, otherwise than under and in accordance with the provisions of the said Act or of any other law for the time being in force, but nothing in this section shall be construed as abrogating any right or jurisdiction to restrain a breach of trust or confidence. Section 14 of the said Act dealing with meaning of 'Copyright' reads as follows:-

"14. **Meaning of Copyright.** - For the purposes of this Act, "copyright" means the exclusive right subject to the provisions of this Act, to do or authorise the doing of any of the following acts in respect of a work or any substantial part thereof, namely: -

(a) in the case of a literary, dramatic or musical work, not being a computer programme,-

(i) to reproduce the work in any material form including the storing of it in any medium by electronic means;

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- (ii) to issue copies of the work to the public not being copies already in circulation;
 - (iii) to perform the work in public, or communicate it to the public;
 - (iv) to make any cinematograph film or sound recording in respect of the work;
 - (v) to make any translation of the work;
 - (vi) to make any adaptation of the work,
 - (vii) to do, in relation to a translation or an adaptation of the work, any of the acts specified in relation to the work in sub-clauses (i) to (vi);
- (b) in the case of a computer programme,-
- (i) to do any of the acts specified in clause (a);
 - (ii) to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer programme:
Provided that such commercial rental does not apply in respect of computer programmes where the programme itself is not the essential object of the rental.
- (c) in the case of an artistic work,-
- (i) to reproduce the work in any material form including depiction in three dimensions of a two-dimensional work or in two dimensions of a three-dimensional work;
 - (ii) to communicate the work to the public;
 - (iii) to issue copies of the work to the public not being copies already in circulation;
 - (iv) to include the work in any cinematograph film;
 - (v) to make any adaptation of the work;
 - (vi) to do in relation to an adaptation of the work any of the acts specified in relation to the work in sub-clauses (i) to (iv);
- (d) in the case of a cinematograph film,-
- (i) to make a copy of the film, including a photograph of any image forming part thereof;
 - (ii) to sell or give on hire, or offer for sale or hire, any copy of the film, regardless of whether such copy has been sold or given on hire on earlier occasions;
 - (iii) to communicate the film to the public;
- (e) in the case of a sound recording,-
- (i) to make any other sound recording embodying it;
 - (ii) to sell or give on hire, on offer for sale or hire, any copy of the sound recording regardless of whether such copy has been sold or given on hire on earlier occasions;
 - (iii) to communicate the sound recording to the public.

Explanation.- For the purposes of this section, a copy which has been sold once shall be deemed to be a copy already in circulation.

It may also be noted that under Section 51 of the Act dealing with "When Copyright infringed" states that Copyright in a work shall be deemed to be infringed - when any person, without a licence granted by the owner of the Copyright or the Registrar of Copyrights under the Act or in contravention of the conditions of a licence so granted or of any condition imposed by a competent authority under the Act: does anything, the exclusive right to do which is by the Act conferred upon the owner of the Copyright. Section 52 of the Act dealing with Certain acts not to be infringement of copyright states that the following acts shall not constitute an infringement of copyright, namely-

*** ** **

(aa) the making of copies or adaptation of a computer programme by the lawful possessor of a copy of such computer programme, from such copy.

- (i) in order to utilise the computer programme for the purpose for which it was supplied; or
- (ii) to make back-up copies purely as a temporary protection against loss, destruction or damage in order only to utilise the computer programme for the purpose for which it was supplied."

24. It is clear from the above said provisions of the Copyright Act that the right to copyright work would also constitute exclusive right of the copyright holder and any violation of the said right would amount to infringement under Section 51 of the Act. However, if such copying of computer program is done by a lawful possessor of a copy of such computer programme, the same would not constitute infringement of copyright and wherefore, but for the licence granted in these cases to the respondent to make copy of the software contained in shrink-wrapped/off-the-shelf software into the hard disk of the designated computer and to take, a copy for backup purposes, the end user has no other right and the said taking backup would have constituted an infringement, but for the licence. Therefore, licence is granted for taking copy of the software and to store it in the hard disk and to take a back up copy and right to make a copy itself is a part of the copyright. Therefore, when licence to make use of the software by making copy of the same and to store it in the hard disk of the designated computer and to take back up copy of the software, it is clear that what is transferred is right to use the software, an exclusive right, which the owner of the copyright *i.e.*, the respondent-supplier owns and what is transferred is only right to use copy of the software for the Internal business as per the terms and conditions of the agreement. The decision of the Delhi High Court in *Dynamic Veritcal Software India (P.) Ltd.'s case (supra)* relied upon by Sri Aravind Dattar, learned senior counsel appearing for the respondents in some of the cases in support of his contention that by no stretch of imagination, payment made by the respondents to the non-resident suppliers can be treated as 'royalty' is not helpful to the respondents in the present cases as in the said case, Delhi High Court was

considering the provisions of Section 40(a)(i) of the Act and the order of the High Court reads as follows :-

"What is found, as a matter of fact, is that the assessee has been purchasing the software from Microsoft and sold it further in Indian market by no stretch of imagination, it would be termed as royalty."

Therefore, the contention of the learned senior counsel appearing for the respondents that there is no Transfer of any part of copyright or copyright under the impugned agreements or licenses cannot be accepted. Accordingly, we hold that right to make a copy of the software and use it for internal business by making copy of the same and storing the same in the hard disk of the designated computer and taking back up copy would itself amount to copyright work under Section 14(1) of the Act and licence is granted to use the software by making copies, which work, but for the licence granted would have constituted infringement of copyright and licensee is in possession of the legal copy of the software under the licence. Therefore, the contention of the learned senior counsel appearing for the respondents that there is no transfer of any part of copyright or copyright and transaction only involves sale of copy of the copyright software cannot be accepted. It is also to be noted that what is supplied is the copy of the software of which the respondent-supplier continues to be the owner of the copyright and what is granted under the licence is only right to copy the software as per the terms of the agreement, which, but for the licence would amount to infringement of copyright and in view of the licence granted, the same would not amount to infringement under Section 52 of the Copyright Act as referred to above. Therefore, the amount paid to the non-resident supplier towards supply of shrink-wrapped software, or off-the-shelf software is not the price of the C.D. alone nor software alone nor the price of licence granted. This is a combination of all and in substance, unless licence is granted permitting the end user to copy and download the software, the dumb C.D. containing the software would not in any way be helpful to the end user as software would become operative only if it is downloaded to the hardware of the designated computer as per the terms and conditions of the agreement and that makes the difference between the computer software and copyright in respect of books or prerecorded music software as book and prerecorded music C.D. can be used once they are purchased, but so far as software stored in dumb C.D. is concerned, the transfer of dumb C.D. by itself would not confer any right upon the end user and the purpose of the C.D. is only to enable the end user to take a copy of the software and to store it in the hard disk of the designated computer if licence is granted in that behalf and in the absence of licence, the same would amount to infringement of copyright, which is exclusively owned by non-resident suppliers, who would continue to be the proprietor of copyright. Therefore, there is no similarity between the transaction of purchase of the book or prerecorded music C.D. or the C.D. containing software and in view of the same, the Legislature in its wisdom, has treated the literary work like books and other articles

separately from 'computer' software within the meaning of the 'Copyright' as referred to above under Section 14 of the Copyright Act.

25. It is also clear from the above said analysis of the DTAA Income Tax Act, Copyright Act that the payment would constitute 'royalty' within the meaning of Article 12(3) of the DTAA and even as per the provisions of 9(1)(vi) of the Act as the definition of 'royalty' under clause 9(1)(vi) of the Act is broader than the definition of 'royalty' under the DTAA as the right that is transferred in the present case is the transfer of copyright including the right to make copy of software for internal business, and payment made in that regard would constitute 'royalty' for imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill as per clause (iv) of *Explanation 2* to Section 9(1)(vi) of the Act. In any view of the matter, in view of the provisions of Section 90 of the Act, agreements with foreign countries DTAA would override the provisions of the Act. Once it is held that payment made by the respondents to the non-resident Companies would amount to 'royalty' within the meaning of Article 12 of the DTAA with the respective country, it is clear that the payment made by the respondents to the non-resident supplier would amount to royalty. In view of the said finding, it is clear that there is obligation on the part of the respondents to deduct tax at source under Section 195 of the Act and consequences would follow as held by the Hon'ble Supreme Court while remanding these appeals to this Court. Accordingly, we answer the substantial question of law in favour of the revenue and against the assessee by holding that on facts and circumstances of the case, the ITAT was not justified in holding that the amount(s) paid by the respondent(s) to the foreign software Suppliers was not 'royalty' and that the same did not give rise to any 'income' taxable in India and wherefore, the respondent(s) were not liable to deduct any tax at source and pass the following Order:-

All the appeals are allowed. The order passed by the Income Tax Appellate Tribunal, Bangalore Bench 'A' impugned in these appeals is set aside and the order passed by the Commissioner of Income Tax (Appeals) confirming the order passed by the Assessing Officer (TDS)-I is restored.”

The same ratio was followed in subsequent decision in the case of *CIT vs. Ansys Software (P.) Ltd.* (23 taxmann.com 344). Thus in the light of the decision of the Hon'ble jurisdictional High Court in the cases cited supra, we hold that payment made for use of software is royalty and the assessee is liable to deduct tax at source on the said payments. Accordingly, we uphold the orders of the lower authorities.

10. In the result, the appeal filed by the assessee is dismissed.

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11. Since identical facts are involved in other appeals viz., IT(IT)A No.1508/Bang/2012, ITA Nos.156, 157, 610 & 611/Bang/2010, for parity of reasons in ITA No.193/Bang/2010, all the appeals filed by the assessee are dismissed.

Order pronounced in the open court on 23rd March, 2018.

Sd/-
(SUNIL KUMAR YADAV)
JUDICIAL MEMBER
srinivasulu, sps

sd/-
(INTURI RAMA RAO)
ACCOUNTANT MEMBER

Copy to :

- 1 Appellant
- 2 Respondent
- 3 CIT(A)
- 4 CIT
- 5 DR, ITAT, Bangalore.
- 6 Guard file

By order

Senior Private Secretary
Income-tax Appellate Tribunal
Bangalore