

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'B' NEW DELHI**

**BEFORE SHRI G.D. AGARWAL, VICE PRESIDENT
&
SHRI K.NARASIMHA CHARY, JUDICIAL MEMBER**

**ITA Nos.1328 to 1330/Del/2008
Assessment Years: 1997-98 to 1999- 2000**

M/s Microsoft Corporation, Vs Asstt. Director of Income-tax,
C/o SR Batliboi & Co. Circle 3(1), International Taxation
8th Floor, Golf View Corporate New Delhi.
Tower B, Sector -42, Gurgaon.

**Assessee by: S/Shri Nageshwar Rao
& Sandeep S. Karhail, Advocate
Revenue by: Shri G.K. Dhall, CIT-DR**

**Date of Hearing 01.05.2019
Date of Pronouncement 13.05.2019**

ORDER

PER K. NARASIMHA CHARY, JM

Aggrieved by the Common Order dated 30-01-2008 in Appeal Nos 06, 07 and 08/05-06 for the AY 1997-98, 1998-99 and 1999-2000 respectively, Assessee filed these three appeals. Since the assessee is same and the substantial questions for adjudication involved in these matters are also the same, we deem it just and convenient to dispose of these three appeals by way of this common order, with reference to the facts involved in the Assessment Year 1997-98.

2. Brief facts of the case are that the assessee is a company incorporated in 1981 and is based in USA. Assessee is a leading software developer and is the sole owner of intellectual property rights vested in Microsoft software. In response to the notice issued under section 148 of the Income-tax Act, 1961 (“the Act”), assessee submitted their returns of income and Learned Assessing Officer found that during the years under consideration the assessee earned income from two categories from India, namely, revenue arising from licensing of computer software to Original Equipment Manufacturer (OEM) and licensing of computer software to independent distributors in India. The assessee submitted that the income from licensing of computer software to OEMs was taxable in India and the same was offered to tax, but at the same time, it was contended by the assessee that the payment received from sale/licensing of software from the independent distributors was in the nature of business profits and is not taxable as it does not have Permanent Establishment (PE) in India.

3. Learned Assessing Officer observed that the facts involved in these Assessment Years are similar to the facts involved for the Assessment Year 1996-97 during which year the revenue arising from the sale/licensing of computer software to independent distributors in India was held as royalty income and accordingly assessed to tax. Learned Assessing Officer further observed that the Ld. CIT(A) vide order dated 14.1.2005 upheld the same. In this background, learned Assessing Officer proposed to bring this particular income from sale/licensing of computer software to independent distributors in India as royalty. He heard the assessee and while referring to the provisions relating to the taxability of the assessee under the Income-tax Act and

also on the DTAA between India and USA, learned Assessing Officer held that the payment received by the assessee from licensing of software was qualified to be royalty as per the Indian Income Tax Act, 1961 (for short “the Act”) as well as DTAA because,-

1. The software was licensed but not sold and the copyright of the software remained with the assessee but was allowed to be used by the persons making payments. According to Indian Copyrights Act, 1957, as amended in 1994, software is entitled to copyrights protection and the assessee possesses copyright in the software which it can enforce in India if any violation of such right is noticed by it. Further, the Indian Copyright Act recognises “copyright” as doing or authorising the doing of any of the act in respect of a work or any substantial part thereof, which includes in case of a computer program-to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer program and therefore on this ground it is clear that the assessee has authorised to use the copyright to the distributors in India;
2. The software owned by the assessee is a patented software and consideration for allowing the use of the patented article falls within the definition of royalty payment and even if it is considered that the software owned has not been patented still there is no denial of the fact that it is essentially an invention. The development of such software requires highly technical manpower, with highly sophisticated infrastructure and huge investments, and the software can also be considered as a

scientific work. On this score the software can also be said to be information developed out of scientific experience;

3. The payment was also qualified for the use of secret formula or process since the software of Microsoft when installed in a computer response to every instruction in a specific way and it recognises the command as per its programming yields the desired result and reflects the same on the output devices. Learned Assessing Officer drew strength from the fact that cost of the medium, namely, computer discs, floppy etc on which the program is written is negligible as compared to the overall price of the software and had it not been a secret programming, anybody could have written these types of programs and sold it at a very low price as compared to the price of the Microsoft software; and
4. In assessee's own case by order dated 14.1.2005 the Ld. CIT(A) had confirmed the addition made by the Assessing officer treating the sale proceeds as royalty income by observing that the end-user had acquired the limited rights to copy the software on its computer hard drive and a payment was towards the use of copyright of literary scientific work and therefore it is immaterial whether the same is sold as a shrinkwrap or otherwise, the consideration for the same will still be treated as royalty. Ld. CIT(A) further observed that is also immaterial whether the copy is "infringement" under copyright or not.
4. In view of all these reasons recorded by the learned Assessing Officer, he held the payment towards the software is royalty within the

meaning of Article 12 of DTAA between India and USA and added a sum of Rs.10,63,07,152/-towards 15% of tax as per Indo-US treaty.

5. In similar circumstances and on the similar question, learned Assessing Officer treated the income from sale/license of software from independent distributors as royalty for the Assessment Years 1998-99 and 1999-2000 also and made similar addition.

6. In the appeals preferred by the assessee for the Assessment years 1997-98, 1998-99 and 1999-2000 since a similar question was involved, Ld. CIT(A) considered the same and by way of a common order dated 30.1.2008 in Appeal No. 06, 07, &08/2005-06 gave a finding that the right to use the patent in lieu of payment itself characterised the nature of royalty paid under section 9(1)(vi) of the Act read with Article 12 of DTAA and on that premise he held that the income from software license is in the nature of royalty both under the domestic law and the DTAA and is taxable in India. He accordingly dismissed the appeals.

7. Hence the assessee is in appeal before us stating that the Ld. CIT(A) erred in characterising the income from sale of software as royalty under the Act without appreciating that Section 115A of the Act applies to royalty payments as defined under section 9(1)(vi) of the Act and in this case the revenue does not amount to royalty under the provisions of 9(1)(vi) of the Act, there is no basis to rely on the provisions of section 115 A.

8. At the outset, Ld. AR brought to our notice that the assessee licenses the software to the end user and they do not provide the source code to them, as such, it is not a case of sale/license of copyright but on

the other hand it is only a case of sale/license of the copyright article. He submits that the facts involved in this matter are squarely covered by the facts in the case of DDIT vs. Infra-soft Ltd (2013) 39 taxmann.com 88 (Delhi) and the addition thereon as is evident from the judgement. He further submitted that following the said decision of the Hon'ble jurisdictional High Court, a coordinate Bench of this Tribunal in MOL Corporation vs. ADIT in ITA No. 6089 to 6091/del/2012 by order dated 26.9.2016 held that inasmuch as the revenue from customising software was not considered as royalty, the issue in case of shrink wrapped or off the shelf software stands on a better footing, but however remanded the matter back to the file of the learned Assessing Officer to follow the ratio of the Hon'ble jurisdictional High Court in the case of Infra-soft Ltd (supra). He further submitted that this question was considered by another coordinate Bench of this Tribunal in the case of MOL Corporation for the Assessment year 2011-12 in ITA No. 1714/Del/2015 and by order dated 31/10/2018, the Bench followed the decision in ITA Nos.1689 to 1691/Del/2012, however, remanded the matter to the file of learned Assessing Officer to adjudicate the issue afresh in accordance with law. Ld. AR submitted that when once the Tribunal reached a definite conclusion that the decision of the Hon'ble jurisdictional High Court in the case of Infra-soft Ltd (supra) applies to the facts of the present case, no useful purpose would be served by remanding the matter to the file of the learned Assessing Officer.

9. We have gone through the record in the light of the submissions made on either side. We find that the facts of this case are identical to the facts involved in the case of infra-soft Ltd (supra), more particularly on a reading of the reasoning of the Ld. AO in this case to arrive at the

conclusion that the sales/licensing of the software was royalty in juxtaposition to Paragraph No. 11 of order of the Hon'ble jurisdictional High Court which are strikingly similar. Hon'ble Court after dealing with this issue extensively held that what is transferred in this matter is neither the copyright nor the use of the copyright in the software, but what is transferred is the right to use the copyrighted material or article which is clearly distinct from the rights in the copyright, and the right that is transferred is not a right to use the copyright but is only limited to the right to use the copyrighted material and the same does not give rise to any royalty income and would be business income only.

10. In the batch of cases in ITA Nos.6089 to 6091/Del/2012, a coordinate Bench of this Tribunal considered the question as to the effect of the retrospective amendment by the Finance Act, 2012 in the light of the decision of the Hon'ble jurisdictional High Court in the case of DDIT vs New Skies Satellite BV 382 ITR 114 wherein it was held that unless Double Taxation Avoidance Agreement is jointly amended by both the countries to incorporate particular income partaking the nature of "royalty" or amend the definition in a manner so that such income automatically becomes royalty, the Finance Act, 2012 which inserted several explanation to Section 9(1)(vi) of the Act by itself would not affect the meaning of the term "royalty" as mentioned in Article 12 of the Double Taxation Avoidance Agreement, and reached a conclusion that the retrospective amendment made to the Income tax Act will not apply in deciding the issue of taxability of income of the assessee in the present batch of cases. The coordinate Bench in this batch of appeals returned a finding that after the decision of the Hon'ble jurisdictional

High Court in the case of Infra-soft (supra), the decision in the case of Gracemac Corporation is no longer remains a good law.

11. It is argued by the Ld. DR that the facts of this case have to be verified with the facts of the case in Infra-soft (supra) and also MOL Corporation (supra), and, therefore, the proper course would be to remand the matter to the file of the Assessing Officer for verification of facts and to decide the issue according to law.

12. On a careful reading of the facts of Infra-soft Ltd (supra), as could be culled out from paragraphs 3 to 12 we find that the facts in both the cases are identical and the issue that was dealt with is also identical. We, therefore, do not have any hesitation in our mind to hold that in view of the decision of the Hon'ble jurisdictional High Court in the case of Infra-soft (supra), the issue involved in this matter is no longer res integra and has to be answered by stating that there is no transfer of any right in respect of copyright by the assessee and it is the case of mere transfer of copyrighted article and the payment was for a copyrighted article and represents the purchase price of an article and cannot be considered as royalty even under the Income Tax Act, 1961 or under the DTAA. When once we reach such a conclusion, we do not find any need for further verification of any fact at the end of the Assessing Officer. Insofar as the law laid down by the Hon'ble High Court is concerned, whether or not this particular judgement was available before the Assessing Officer at the time of framing of the assessment, it makes little difference because the decision of the Hon'ble High Court binds the learned Assessing Officer in the same way as it binds this Tribunal also. We, therefore, do

not find any need to remand the matter back to the file of the learned Assessing Officer.

13. For the reasons recorded in the preceding paragraphs, we answer the issue holding that inasmuch as the assessee does not provide the source code to the end-users and also in view of the decision of the Hon'ble jurisdictional High Court, what is transferred is neither the copyright in the software nor the use of copyright in the software, but what is transferred is the right to use the copyrighted material or article which is clearly distinct from the rights in copyright and the right that is transferred is not a right to use the copyright but is only limited to the right to use the copyrighted material and the same does not give rise to any royalty income and it would only be the business income. It is not the case of Revenue that the assessee has any Permanent Establishment (PE) in India, in the absence of which under article 7 of the DTAA between India and USA, the business income is not taxable. We, therefore, allow the grounds of appeal of the assessee.

14. On the aspect of interest under Section 234B, Ld. AR placed reliance on the decision of the Hon'ble Delhi High Court in the case of DIT Vs GE Packaged Power Inc. (2015) 373 ITR 0065 (Delhi). In this case, the Hon'ble High Court of Delhi referred and followed its decision in the case of Director of Income Tax vs. Jacobs Civil Incorporated (2011) 330 ITR 0578 wherein it was held that Sec. 195 put an obligation on the payer i.e., any person responsible for paying any amount to a non-resident, to deduct tax at source at the rates in force from such payments, thus, entire tax is to be deducted at source which is payable on such payments made by the payer to the non-resident; that if

the said payer has defaulted in deducting tax at source, the Department can take action against the payer under the provisions of Section 201 of the Act and compute the amount accordingly; that in such a case, the non-resident is liable to pay tax but there is no question of payment of advance tax; and that, therefore, assessee is not liable to pay interest under Section 234B on account of default of the payer in deducting tax at source from the payments made to the assessee. It is pertinent to note that the decision in *Jacobs Civil incorporated(supra)* relates to the AY2001-02.

15. Be that as it may, inasmuch as we held in the preceding paragraphs that there is no royalty income involved in this matter, and for want of Permanent Establishment, the business income of the assessee is not taxable in India, we, therefore, in these circumstances and also while respectfully following the decision of the Hon'ble Jurisdictional High Court, hold this issue in favour of the assessee in all the assessment years.

16. In the result, appeals of the assessee are allowed.

Order pronounced in the Open Court on 13th May, 2019.

Sd/-

**(G.D. AGARWAL)
VICE PRESIDENT**

Sd/-

**(K. NARASIMHA CHARY)
JUDICIAL MEMBER**

Dated: 13th May, 2019

VJ

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR
ITAT NEW DELHI

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