

**IN THE INCOME TAX APPELLATE TRIBUNAL
“A” BENCH : BANGALORE**

**BEFORE SHRI GEORGE GEORGE K, VICE PRESIDENT AND
SHRI LAXMI PRASAD SAHU, ACCOUNTANT MEMBER**

IT(IT)A No.934/Bang/2023
Assessment Year : 2017-18

DCIT (International Taxation), Circle – 2(2), Bengaluru.	Vs.	M/s. Mathworks Inc., 3 Apple Hill Drive, Natick Massachusetts, Foreign United States. PAN : AAFCT 7230 H
APPELLANT		RESPONDENT

Assessee by	:	Shri. Manju L Prasad, AR
Revenue by	:	Shri. D. K. Mishra, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	04.01.2024
Date of Pronouncement	:	08.01.2024

ORDER

Per George George K, Vice President:

This appeal at the instance of the Revenue is directed against CIT(A)’s order dated 18.10.2023, passed under section 250 of the Income Tax Act, 1961 (hereinafter called ‘the Act’). The relevant Assessment Year is 2017-18.

2. Brief facts of the case are as follows:

Assessee is a foreign company incorporated in USA. It is engaged in the business of development of mathematical computing software for engineers and scientists. The assessee sells software licences to its distributor in India i.e., “MathWorks India Pvt. Ltd.,” who in turn sells the software licences to end-users.

For the Assessment Year 2017-18, return of income was filed on 30.03.2018 declaring income of Rs.89,58,63,752/-. Subsequently, assessee filed revised return on 20.06.2018 declaring Nil income and claimed refund of the entire amount deducted at source amounting to Rs.9,68,87,664/-.

3. The assessment was selected for scrutiny and notice under section 143(2) of the Act was issued on 22.09.2019. During the course of assessment proceeding, assessee was directed to produce breakup of receipts of Rs.89,58,63,752/-. In compliance, assessee had disclosed a sum of Rs.59,47,45,151/- as receipts on account of sale of software licence / annual licence fees. Further, a sum of Rs.30,11,18,601/- was classified under the head “service and maintenance” in relation to sale of software. The assessment was completed under section 143(3) r.w.s. 144C of the Act, vide order dated 05.02.2020. In the said Assessment Order, the sum of Rs.59,47,45,151/- received by the assessee during the subject Assessment Year was held by the AO to be “royalty” within the meaning of Article 12 of India-US Tax Treaty and also as per the provisions of section 9(1)(vi) of the Act. Further, receipt of a sum of Rs.30,11,18,601/- was held directly related to receipts towards sale of software licence, etc., which were already held to be “royalty”. Therefore, the said amount was taxed as “fees for included services” in terms of Article 12 of India-US Tax Treaty. Thus, the entire sum of Rs.89,58,63,752/- was brought to tax by the AO.

4. Aggrieved by the Order of the AO, assessee preferred appeal before the First Appellate Authority. As regards receipt of Rs.59,47,45,151/-, the CIT(A) followed the judgment of the Hon’ble Apex Court in the case of Engineering Analysis Centre of Excellence Private reported in 432 ITR 471 (SC). The CIT(A) held that same cannot be termed as “royalty” as per India-US DTAA. The CIT(A)

held that it is only a sale of copyrighted article and not rights in the nature of copyright under the agreement entered by the assessee with its distributor viz., ManWorks India Pvt. Ltd. As regards the receipt of Rs.30,11,18,601/- towards maintenance services, the CIT(A) held that since same is inextricably linked to the supply of software and since the receipts on account of sale of software licence itself is not taxable as “royalty”, the provisions of Article 12(4)(a) of India-US DTAA would not apply. Accordingly, the entire addition made by the AO was deleted by the CIT(A).

5. Aggrieved by the Order of the CIT(A), Revenue has filed the present appeal before the Tribunal. The learned DR strongly relied on the grounds raised and the Order of the AO. The learned AR submitted that the issue in question is squarely covered by the judgment of the Hon’ble Apex Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd., (supra).

6. We have heard the rival submissions and perused the material on record. The CIT(A), after examining the end-users license agreement and the distribution agreement, had categorically held that assessee has not parted with the rights in the nature of copyright under the said agreement. It was further held by the CIT(A) that assessee had only permitted the end-users to use a copy righted article and there is no sale of copy right *per se* in the said article. The Hon’ble Apex Court, after analyzing the provisions of Income Tax and the DTAA, the relevant end-users’ agreement, the distribution agreement, had categorically held that end-users are only purchasing copy righted article and payment for the same cannot tantamount to “royalty” under the DTAA. The relevant finding of the Hon’ble Supreme Court reads as follows:

“45. A reading of the aforesaid distribution agreement would show that what is granted to the distributor is only a non-exclusive, non-transferable license to resell computer software. it being expressly stipulated that no copyright in the computer programme is transferred either to the distributor or to the ultimate end-user. This is further amplified by stating that apart from a right to use the computer programme by the end-user himself. there is no further right to sub-license or transfer. nor is there any right to reverse-engineer. modify. reproduce in any manner otherwise than permitted by the license to the end-user. What is paid by way of consideration, therefore. by the distributor in India to the foreign. non-resident manufacturer or supplier, is the price of the computer programme as goods. either in a medium which stores the software or in a medium by which software is embedded in hardware, which may be then further resold by the distributor to the end-user in India. the distributor making a profit on such resale. Importantly. the distributor does not get the right to use the product at all.

46. When it comes to an end-user who is directly sold the computer programme. such end-user can only use it by installing it in the computer hardware owned by the end-user and cannot in any manner reproduce the same for sale or transfer. contrary to the terms imposed by the EULA.

47. In all these cases. the "license" that is granted vide the EULA. is not a license in terms of section 30 of the Copyright Act. which transfers an interest in all or any of the rights contained in sections 14(a) and 14(b) of the Copyright Act. but is a "license" which imposes restrictions or conditions for the use of computer software. Thus. it cannot be said that any of the EULAs that we are concerned with are referable to section 30 of the Copyright Act. inasmuch as section 30 of the Copyright Act speaks of granting an interest in any of the rights mentioned in sections 14(a) and 14(b) of the Copyright Act. The EULAs in all the appeals before us do not grant any such right or interest least of all. a right or interest to reproduce the computer software. In point of fact, such reproduction is expressly interdicted. and it is also expressly stated that no vestige of copyright is at all transferred. either to the distributor or to the end-user. A simple illustration to explain the aforesaid position will suffice. If an English publisher sells 2000 copies of a particular book to an Indian distributor, who then resells the same at a profit, no copyright in the aforesaid book is transferred to the Indian distributor, either by way of license or otherwise, inasmuch as the Indian distributor only makes a profit on the sale of each book. Importantly there is no right in the Indian distributor to reproduce the aforesaid book and then sell copies of the same. On the other hand, if an

English publisher were to sell the same book to an Indian publisher. this time with the right to reproduce and make copies of the aforesaid book with the permission of the author. it can be said that copyright in the book has been transferred by way of license or otherwise. and what the Indian publisher will pay for, is the right to reproduce the book. which can then be characterised as royalty for the exclusive right to reproduce the book in the territory mentioned by the license.”

7. In light of categoric finding by the CIT(A) that end-users in the instant case have been only granted a non-exclusive / non-transferrable and a non-sub licensable licence, payment received by the assessee from MathWork India Pvt. Ltd., on sale of software to the end-users cannot be termed as “royalty” under the relevant DTAA.

8. As regards taxability of amount of Rs.30,11,18,601/- received by the assessee towards maintenance services, the CIT(A) had held the same is inextricably linked to the supply of software licence and when the software licence itself is not taxable as “royalty”, the provisions of Article 12(4)(a) of the India-US DTAA would not apply. The relevant finding of the CIT(A) in this regard reads as follows:

“The next issue for consideration is that taxability of the amount of Rs.30,11 18.601/-received by the appellant towards maintenance services. As per para 7 of the Software Licence Agreement. reproduced below. the maintenance services relate to the fixing of bugs and technical glitches.

“Technical support means assistance by telephone, web and e-mail with the installation and/or use of the then- current release of the licensed Programs. including all available bug fixes and patches and their interaction with supported hardware and operating systems ("Platforms"). Software Maintenance Service may include additional administrative support services for the licensed programs and access to certain online features and services made available by MathWorks

from time to time. Levels of support and services available may vary by License Offering."

The AO had held that these services, being ancillary and subsidiary to the sale of software, the payment for which had been characterized as royalty by the AO would be taxable under the provisions of Article 12(4)(a) of the Treaty. reproduced below:

4. For 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 provision 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 paragraph 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.

However, as the receipts of the appellant from the sale of software have been held to not be royalty, the receipts from maintenance services being related to the use of the software, cannot be taxed under the aforesaid provisions of the treaty. The decision of the Mumbai Tribunal in the case of Reliance General insurance Co Ltd. [2018] 97 taxmann.com, 350, which in turn relied on the decision of the Delhi Tribunal in Infrasoftware Ltd. vs Asst. DIT (International Taxation) 12009] 28 SOT 179 and the Delhi ITAT decision in the case of Aspect Software Inc. vs ADIT Circle 1(1) International Taxation, New Delhi, have held that the provision of maintenance services was inextricably linked to the supply of software. Therefore, when the supply of software is itself not taxable as 'royalty', the provisions of Article 12(4)(a) of the India-U.S.A. DTAA would not apply. Further, it was also held that the payment for these services was not in the nature of fees for technical services as the 'make available' clause of Article 12(4)(b) of the Treaty was not satisfied. The facts of the present case are similar to those of the decisions cited above. Hence the appellant also gets relief with respect to the receipts from maintenance services, which would be the business receipts of the appellant, but would not be taxable in India in the absence of a PE. The grounds of appeal are therefore allowed."

9. The CIT(A) had relied on various ITAT Orders to hold that when receipts are on account of maintenance which is inextricably linked to the supply of software licence and when the supply of the software itself is not taxable as

“royalty”, the receipts cannot be termed as “fees for included services”. In view of aforesaid reasoning and the judgment of Hon’ble Apex Court cited supra, we see no reason to interfere with the order of the CIT(A) and we uphold the same. It is ordered accordingly.

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

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

Sd/-

(LAXMI PRASAD SAHU)
Accountant Member

Sd/-

(GEORGE GEORGE K)
Vice President

Bangalore.

Dated: 08.01.2024.

/NS/*

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| 1. Appellants | 2. Respondent |
| 3. DRP | 4. CIT |
| 5. CIT(A) | 6. DR, ITAT, Bangalore. |
| 7. Guard file | |

By order

Assistant Registrar,
ITAT, Bangalore.