

BEFORE THE AUTHORITY FOR ADVANCE RULINGS (INCOME TAX)

NEW DELHI

28th Day of September, 2011

A.A.R. No.835 of 2009

PRESENT

Mr. Justice P.K.Balasubramanyan (Chairman)

Mr. V.K. Shridhar (Member)

Name & address of the Applicant	Millennium IT Software Ltd.,
Commissioner concerned	The Director of Income-tax (International Taxation), Mumbai.
Present for the Applicant	Mr. Hitesh Joshi, PCS Mr. Rohit Aggarwal, Advocate
Present for the Department	Mr. Girish Dave, Advocate Mr. D.K. Mahajan, Addl.DIT (I.T.) Mr. Sanjay Agrawal, Addl.DIT.(I.T.) Range-4(1), Mumbai

RULING

(By Mr. V.K. Shridhar)

The applicant has entered into a Software License and Maintenance Agreement (SLMA) with Indian Commodity and Exchange Limited (ICEL) on 27.3.2009. Under the agreement the applicant has allowed ICEL to use the software product called 'Licensed Programme' owned by it. The Licensed Programme shall be developed and installed into the computer machines designated by ICEL as envisaged in the Implementation Plan. As use of the

Licensed Programme would require training, the applicant is to deploy its personnel to the designated site to train the employees of ICEL. After the installation is over and the software is given a line cutover, the applicant is required to provide at its own cost, maintenance and support services, via a help desk which will operate 24x7 through telephone, e-mail and facsimile number to fix or bypass programme errors. For installation and implementation of the Licensed Programme, applicant shall be paid Rs.4 crore. The software became live on 20.8.2009. The license to use the Licensed Programme is for 4 years and thereafter its renewal is left to the discretion of ICEL.

2. The applicant submits that after the installation and implementation of the Licensed Programme, the Agreement provides for payment of “License Maintenance Fee” from 1.1.2010 till 31.12.2014. The mode of the payment is such that a fixed amount of Rs.50 lacs per quarter is payable plus an additional fee based on the utilization of the Licensed Programme by ICEL, so much so that the total amount payable would not exceed Rs.150 lacs per quarter. There is further provision in SLMA for fee escalation upto 12% to accommodate inflation and operational cost.

3. Referring to the SLMA, the applicant submits that:

- i) The Licensed Programme is developed by it at its development centre in Sri Lanka.
 - ii) It is the author, inventor, copyright owner of the Licensed Programme.
 - iii) It has the authority to license the Licensed Programme as copyrighted article.
 - iv) It has granted ICEL a right to use the Licensed Programme for its business operations.
 - v) The rights granted under the SLMA are: non exclusive, non transferable, non assignable, indivisible.
 - vi) It has granted right to make copies of the Licensed Programme to be installed on equipments only at designated sites of ICEL. Each copy shall carry copyright, trademark and other notices relating to proprietary rights of the applicant.
 - vii) ICEL cannot sell, distribute or disclose the Licensed Programme or associated documents to any third party.
 - viii) No intellectual property right or license is granted to ICEL. Use of source code and reverse engineering of the Licensed Programme is strictly prohibited.
 - ix) The tenure of the license granted to ICEL is initially for 4 years. Thereafter, the renewal of the license is at the discretion of ICEL.
 - x) The payment prior to License Maintenance Fees on 1.1.2010 is towards goods. Thereafter, it is a business income taxable in India, if PE continues.
4. The applicant submits that the ‘Implementation fee’ and ‘Licence and Maintenance fee’ are not chargeable to tax as per Income-tax Act, 1961(Act) or under DTAA with Sri Lanka. The providing of maintenance service to ICEL

would not create a Permanent Establishment (PE) in India. As the payments are not liable to tax in India, ICEL is not required to withhold any tax under section 195 of the Act and would not be obliged to file a tax return in India. To support the above proposition, the applicant has placed reliance on the following judgements – Tata Consultancy Services [2004] 141 Taxman 132(SC), Dassault Systems K. K, AAR/821/2009, Infracsoft Ltd. [2009] 28 SOT 179, Sonata Information Technology 103 ITD 324.

5. Following questions were raised for a ruling by this Authority:

1. *Whether, on the facts and in the circumstances of the case, MILLENNIUM IT (Software) Limited (“The Applicant”) is/will be non-taxable in India under the Income-tax Act, 1961, with respect to Implementation and license & maintenance fees (“Fees”) paid by ICEL to Applicant company under the said agreement?*

2. *Whether, on the facts and in the circumstances of the case, the applicant is/will be non-taxable under the DTAA entered into between the Government of India and the Government of Sri Lanka?*

3. *Whether, on the facts and in the circumstances of the case, the applicant providing maintenance service to ICEL could not be treated as having a Permanent Establishment (“PE”) in India.*

4. *Without prejudice of above, whether on the facts and in the circumstances of the case, if the Applicant is not taxable in India for the fees paid by ICEL, would later be required to withhold tax u/s. 195 of the Income*

Tax Act, 1961 on the fees, and if ICEL has deducted withholding tax, will the applicant be entitled to get refund back?

5. *Assuming that the applicant has no other taxable income in India, whether on the facts and in the circumstances of the case, the applicant will be absolved from filing a tax return in India under the provisions of the IT Act with respect to the fees?*

6. The Learned DIT (Intl.Tax.) in her report submits that the payments to the applicant are taxable as 'Royalties' under the Act and under the DTAA with Sri Lanka. The applicant has granted a license to use the software developed by it. Software is not goods or tangible property but intangible intellectual property. It is a 'Process' and covered under clauses (i) and (iii) of Explanation 2 to Section 9, which defines Royalty under the Act. Alternately, the software is a property similar to patent, invention, design secret formula, process etc. The payment for acquisition of software under license is Royalty in view of CBDT's Circular No.621 of 19.12.1991. The intention of the legislation in bringing about the subsequent amendments to the second proviso to section 9(1)(vi), section 115A(1A) and 80HHE is clear in this regard. The meaning of the term Royalty in the DTAA with Sri Lanka is the same as in the domestic law. Referring to the Spl. Bench decision of ITAT in the case of Siemens Aktiengesellschafts [1987] 22 ITD87, learned DIT submits that for the purposes of interpretation of the term 'royalty' under DTAA, one has to go by its general meaning and not by the

definition given under Explanation 2 to section 9(1)(vi). According to the learned ITAT, a term of legal protection has no conclusive impact in determining whether payment is 'royalty' or not, nor the nature and mode of payment whether lump sum, single, or periodic. The payment for use of a property whether the property is protected under statute or not, is 'royalty'. The ownership of the property remains with the developer and only a limited right is given to the user. It is then submitted that the updating of software, removal of programme errors and maintaining performance standards under the maintenance services amount to supply of software. The onsite training to employees and maintenance service to ICEL could be treated as PE of the applicant in India, if the conditions under Article 5 of the DTAA are satisfied. In any case, the payments to the applicant are taxable in India and ICEL is required to withhold tax under section 195 of the Act. The applicant is liable to file a return of its income in India. For these propositions, reference has been made to the decisions in the cases of Tata Consultancy Services,[2004] 141 Taxman 132(SC) Airport Authority of India, AAR No.755-6, Davy Ashmore India Ltd., 190ITR 626; Citizen Watch Co. 148 ITR 774 and New Skies Satellites ITA NO.5384-87/2004 dated 19.10.2009.

7. The learned Representative appearing on behalf of the revenue submits that the term Permanent Establishment (PE) under Article 5 of the DTAA with Sri Lanka shall include especially:

“The furnishing of services, including consultancy services, by an enterprise through employees or other personnel, where activities of that nature continue within the country for a period or periods aggregating more than 183 days within any 12 month period”

It is argued that the applicant has undertaken a software development project to suit the requirement of ICEL. When the applicant's employees are in close association and coordination with the employees of the contractor in the development and customization of the software, the term, 'other personnel' will include such personnel. The entire period starting from the day the project started till the acceptance of the customized software with which ICEL would run the commodity exchange, would be includible for the purposes of counting the period to determine the PE. And then, considering the fact that the ICEL will continue to do business even after 4 years with the provision of new releases, the same software will continue with ICEL. Therefore it cannot be said that the stay of the employees of the applicant will not be for more than 6 months. As Schedule E to the Implementation Plan would make more than 183 days starting from 12.1.2009 to the date 20.8.2009 when the software was given a line cutover, the calculation of 159 days is incorrect. The applicant would have a PE in terms of Article 5 of the DTAA with Sri Lanka. The furnishing of services through other personnel cannot be ignored in counting the number of days.

8. Responding to the revenue's submissions, the applicant submits that the activities like customization of the software were carried out in Sri Lanka and it is not a project or a joint venture. The parties are not collaborators or the associates. The applicant is a software provider and such software are not developed only for ICEL but are supplied to other stock exchanges across the world with some changes according to their needs. The furnishing of services through other personnel is to be ignored in counting the number of days.

9. As regards the applicant's submission that as per DTAA it can have a PE only if the stay of the employees is for a period exceeding 183 days in any 12 months period, we may refer to the most favoured nation clause in the Treaty whereby the period gets relaxed to any period of longer duration in any of the DTAA's entered into by India. Since in the Treaty between India and Yugoslavia the period is 275 days, we read the period in Article 5 as 275 days in any 12 months. Even if the contention of the revenue is accepted that the number of days is more than 183 days if the days are counted from 12.1.2009 to 20.8.2009, it would still be less than 275 days. Accordingly, the existence of PE as per Article 5 of the DTAA with Sri Lanka is not satisfied.

10. The term 'royalty' as used under Article 12.3 of the DTAA is as follows –

“The term royalties used under this article means payment of any kind received as a consideration for the use of or the right to any copyright of literary, artistic or scientific work....”

Hence the issue that has arisen for our consideration is: *Whether the payment made by ICEL under SLMA is consideration for the use of or the right to any copyright of literary work?*

11. We must advert to the Copyright Act to understand the concept of copyright of literary works. The relevant provisions of the Copyright Act, 1957, which are pertinent to our matter, are 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;

(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 hire, or offer for sale or hire, any copy of the computer programme, regardless of whether such copy has been sold or given on hire on earlier occasions;"
2. (o) “literary work” includes computer programmes, tables and compilations including computer[databases];
- (ffb) 'computer' includes any electronic or similar device having information processing capabilities;
- (ffc) 'computer programme' means a set of instructions expressed in words, codes, schemes or in any other form, including a machine readable medium, capable of causing a computer to perform a particular task or achieve a particular result;”

Thus, under Indian copyright law, computer programs are considered to be literary works and accordingly entitled to copyright protection under Section 14 of the Copyright Act.

12. We must appreciate the wordings of the definition of computer programme which has been worded in liberal language. It defines computer programme as “a set of instructions expressed in words, codes, schemes or *in any other form*

(*emphasis supplied*)” The use of this language signifies the legislative intent to award copyright protection to both the source code and the object code of the computer programme.

13. As is well understood, the term ‘software’ is used to describe all of the different types of computer programmes. Computer programme are basically divided into ‘application programme’ and ‘operating system programme’. Application programme are designed to do specific tasks to be executed through the computer and the operating system programmes are used to manage the internal functions of the computer to facilitate use of application programme. These two types of programmes can be written in three levels of computer language—high level, low level and lowest level. High-level language consists of English words and symbols and are easy to learn. Lower-level language is assembly language which consists of alphanumeric labels. This language is also easily understandable by the programmer. Statements of these two languages are referred to as written in *source code*. The third, lowest-level language, is the machine language. This is a binary language using two symbols '0' and '1' called ‘bits’. This is the only language which can be followed by the machine but very difficult for the programmer to utilise. Statements in machine language are referred to as written in ‘object code’. [N.S. Gopalakrishnan: *Intellectual Property and Criminal Law*, pp. 159-60 (1994)].

It is well established that authorship of both the source code and the object code are protected by the Copyright Act as literary work. [*M/s. Gracemac Corporation vs. ADIT* and *Microsoft Corporation vs. ADIT* (ITAT Delhi)]. A number of judgments to this effect have been passed by the courts in USA. In *Williams Electronics, Inc. v. Artic International Inc.* 685 F.2d 870, 215 U.S.P.Q. 405 (3rd Circuit 1982). Third Circuit Court of Appeals rejected the argument that since the coding was in object code, it was a copy intelligible to humans and, therefore, outside the Copyright Act protection. In fact Courts in the USA have been awarding protection to not only the source code and the object code, but in some instances, the same has been extended to even “the overall structure” of a programme. *Whelan Associates Inc. v. Jaslow Dental Laboratory, Inc.* 230 USPQ 481 (3rd Circuit 1986). Reliance may also be placed on Article 10 of the Trade Related Intellectual Property Rights Agreement (TRIPs) which expressly provides that computer programs, whether in source code or object code, shall be protected as literary works under the Berne Convention, 1971, to which India is a party.

14. It has also come to our notice that during the process of registration of a copyright in a computer programme, the author also files the object code of the software with the Registrar of Copyrights. Hence, there is not an iota of doubt in our mind that both the source code and the object code of a computer programme are awarded copyright protection under the Copyright Act.

15. In the present case, the source code is expressly excluded from the purview of the SLMA. However, we may refer to clause 1.1.13 of the SLMA which reads as follows –

“1.1.13.Licensed Program means the object code software incorporating the software specification on an “as is” basis and consisting of a set of instructions or statements in machine- readable medium for executing the object code corresponding to the Source Code...”

Thus, under the SLMA, the program being licensed contains the object code which consists of ‘set of instructions’ in ‘machine- readable medium’. Thus what has been licensed, squarely falls within the definition of computer programme under section 2(ffc) and is a copyrightable subject matter.

16. We must now examine whether the license granted under the SLMA is use of or the right to use the copyright in the Computer Programme. A license is described in Stroud’s Judicial Dictionary, 5th Edition, as “an authority to do something which would otherwise be wrongful or illegal or inoperative” (per Latham C.J., in Federal Commissioner of Taxation v. United Aircraft Corporation 68 C.L.R. 525). It further describes License as “A dispensation or license, properly, passeth no interest, nor alters or transfers property in anything, but only makes an action lawful, which, without it, had been unlawful”. It describes Licensee as “a person who had permission to do an act which without such

permission would be unlawful”. In a similar manner, Ramanath Aiyar, in Law Lexicon, has described license as ‘an authority to do something which would otherwise be inoperative, wrongful or illegal.’ It is a permission or authority to do a particular thing.

Hence, it is clear that the license to use computer Program means right to use the intellectual property that is the copyright in the computer program in a particular way.

17. The term “Licensing” has been defined in the Black's Law Dictionary, (6th Edi.) as “The sale of a license permitting the use of patents, trademarks, or other technology to another firm.”

As per this definition, when intellectual property is licensed, essentially the use of the intellectual property (copyright in the present case) is passed on to another firm.

18. We may further substantiate this by reading the definitions of Royalty under the Act. The definition under the Act is as under –

“....”royalty” means the 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-

XX XX XX

(v) the transfer of all or any rights (including the granting of a license) in respect of any copyright, literary, artistic or scientific work....”

The phrase ‘including the granting of a license’ in the definition under section 9 of the Act is only explanatory in nature. It explains the term ‘all or any rights in respect of copyright’. It is deemed that all or any rights in respect of a copyright whether under DTAA or the Act should be held to include the grant of a license.

19. Since a license gives a right to do something which would otherwise be unlawful, let us examine whether the ICEL would be liable for copyright infringement if it uses the Computer Programme without entering into the SLMA.

20. Section 52 specifies the acts which do not constitute infringement of copyright. Insofar as it is relevant, the section is extracted below:

“ 52(a) xx xx xx xx xx xx xx xx

(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 utilize 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 utilize the computer programme for the purpose for which it was supplied;

.....

(ad) the making of copies or adaptation of the computer programme from a personally legally obtained copy for noncommercial personal use.”

In the ruling of this authority in Dassault Systems referred *supra*, in para 18, it is held that:

“customization or adaptation, irrespective of the degree, will not constitute ‘infringement’ as long as it is to ensure the utilization of the computer program for the purpose for which it was supplied. Once there is no infringement, it is not possible to hold that there is transfer or licensing of ‘copyright’ as defined in the Copyright Act and as understood in common law.”

21. We find it difficult to agree with this conclusion. A careful reading of Section 52 (aa) will reveal that the clause uses the term “lawful possessor”. It thus, carves out an exception for lawful possessors of a computer programme as far as copies or adaptation for personal use is concerned. However, the question before us is: if the customer had used the computer programme without paying for it, will not the assessee have the right to sue the customer for copyright infringement? It does not appear to be relevant to the discussion before us to determine what rights the customer will enjoy after having paid for the computer programme.

22. It was held in *Gracemac Corporation vs. ADIT* and *Microsoft Corporation vs. ADIT* (ITAT Delhi) that:

“ The expression "exclusive right" used in Section 14(a) or Section 14(b) of the Copyright Act refers to the rights of author/creator and not the "exclusive right" to be given by him *to some party to reproduce the copyrighted work or sell the computer programme etc. It also does not mean that non-exclusive right given by the owner of the copyright to some other party to do one or more acts will not have copyright in respect of the property.* Even grant of one right in respect of a copyright or work would amount to transfer or the use of copyright”

23. The ruling of this authority in *Dassault Systems*, referred to supra, has interpreted the phrase “use of or right to use any copyright” under Article 12.3 of the India-Japan Tax Treaty. It is in this context the ruling in *Dassault Systems* states that “Different considerations will arise if the grant is non-exclusive that too confined to the use purely for in-house or internal purpose”. The authority held that ‘non-exclusive’ and ‘in-house’ use of a software amounts to use of a copyrighted article and not use of copyright in the article. In doing so, the authority has conjointly read the phrase ‘use of or right to use any copyright’ instead of reading independently the phrases ‘use of’ and ‘right to use any copyright’. We find it difficult to agree that use purely for in-house or internal purpose is no ‘use of’

copyright or that 'use of' and 'right to use any copyright' have the same connotation.

24. The Applicant has pleaded that the Hon'ble Supreme Court in the case of Tata Consultancy Services referred *supra*, while dealing with the issue of off the shelf software (canned software), held that such canned software are 'goods' for the purposes of levy of sales tax and no distinction lies between branded and unbranded softwares. The reason for the Hon'ble Supreme Court to hold canned software as 'goods' was that even when intellectual property is put on to a media, whether in the form of books or canvas or computer discs or cassettes, and marketed it would become 'goods'. The copyright in a software programme may remain with the originator of the programme, but the moment copies are made and marketed, they become 'goods', which are susceptible to sales tax. It is so stated by the Court, because Copyright Act 1957 and Sales Tax Act are not Statutes in *Pari Materia*. In AAR 757-56 of 2007, this Authority, in the case of Airport Authority of India, has opined that Tata Consultancy decision is not applicable in such cases. The mere fact that customs law or sales tax law deems it to be goods for the purpose of those Act, does not change the inherent character of Software. The World Trade Organization has itself recognised goods (GATT), Services (GATS) and intellectual property rights (TRIPS) as distinct and different classes. The purchase of software from reseller is payment for use of intellectual property

and not for the purchase of goods, unless the payment falls under the exception provided by the second proviso to section 9(1)(vi) of the Act.

25. The scope of SLMA extends beyond installation and implementation of the Licensed Program. The maintenance service in respect of the Licensed Program is an integral part of SLMA. As per Schedule-F of SLMA, trading transactions are to be processed using the Licensed Program. After paying the implementation and customization fee, the actual use of the Licensed Program is to begin from 1.1.2010 and will last till 31.12.2014. The payment for each quarter for this period is to be determined on the basis of average trades per day in a quarter. In bifurcating the payments before and after installation and implementation, the nature of the payments remain royalty for the use of the Licensed Program and would not change its character from royalty to business income. If it was to be in the nature of business income then the SLMA would have been sale and service of Licensed Program and the fee paid would have been taxable as business income under Article 7 of the DTAA, depending on whether the applicant has a PE in India or not under Article 5 of the DTAA.

26. Based on the above, we hold that since without the SLMA being in place, any usage of the computer programme by the customers would have amounted to copyright infringement, the payment made under the SLMA was for obtaining the

right to use the copyright in the software and taxable as royalty under the DTAA and the Act.

27. The questions are answered as under:

- Ans.1 Fees paid by ICEL to the applicant is taxable as royalty under clause (v) of Explanation 2 to Section 9(1)(vi) of the Act.
- Ans. 2 As the fees payable by ICEL to the applicant arise in India, it is taxable under Article 12.2 of the DTAA in India.
- Ans.3 The applicant does not have a PE in terms of Article 5 of the DTAA.
- Ans. 4 The applicant is taxable on the fees paid by ICEL. The provision of withholding tax under Section 195 would apply.
- Ans. 5 As the applicant is liable to tax in India, it is required to file a return of income under the provision of the Act.

(V.K.Shridhar)
Member(R)

The Chairman (adding)

I agree with the conclusion arrived at by the Member(R). Considering that the question is cropping up again and again, I think it proper to add a few words.

2. The applicant who is in the business of providing premium software solutions to customers across the globe, has entered into an agreement with the International Multi-commodity Exchange Limited which later came to be known

as the Indian Commodity Exchange Limited ('ICEL'). The agreement allows ICEL to use a specific software product developed and owned by the applicant on receipt of a consideration. According to the applicant, it is the author/inventor/copyright owner of the licensed programme with full corporate authority to license as copyrighted article for consideration, of the licensed programme developed by it. In terms of the agreement, according to the applicant, ICEL has been granted a non-exclusive, non-transferable, non-assignable, indivisible license to use the licensed programme without any sub-licensing rights for its business operations. ICEL has also been granted the right to take copies of the licensed programme restricted only to install the same at the designated premises as is reasonably required for the own use and back-up of ICEL. ICEL is not allowed to modify the licensed programme. The applicant seeks a ruling whether the income derived by it from this transaction with ICEL will be taxable in India under the Income-tax Act or whether it will be taxable under the Double Taxation Avoidance Agreement between India and Sri Lanka of which it is the tax resident. The applicant submits that it does not have any permanent establishment in India. According to the Revenue, what is payable by ICEL in terms of the agreement which enables it to use the computer programme over which the applicant has proprietorship and copyright, is royalty in terms of section 9(1)(vi) of the Income-tax Act and is taxable in India under the Income-tax Act and also under

Article 12 of the DTAA relied on by the applicant. It is the case of the applicant that what is involved is merely a sale of goods to ICEL and the payment is not royalty in terms of the Income-tax Act. Alternatively, it is contended that what is given is only the right to use the licensed programme and not the copyright in the licensed programme and hence it is not royalty. The distinction between 'use' or the 'right to use' a copyright and the use or the right to use a copyrighted article, is emphasized.

3. The applicant has reiterated that being the developer and owner of the licensed programme, it has, under the agreement, granted ICEL the right to use the licensed programme for the business operations of ICEL. Admittedly, this is done for a consideration. The question is, what is the character of the consideration received by the applicant under the transaction.

4. There is no dispute that the right to copyright is a valuable right. Copyright as such is not defined in the Income-tax Act or DTAA. But, it is a well-known right. The Copyright Act, 1957 protects that right in India. Under section 2(y) 'work' is defined, inter alia, as meaning a literary, dramatic, musical or artistic work. Under section 2(o), a literary work is defined to include computer programmes, tables and compilations including computer data-bases. Under section 2(ffb) a computer is defined as to include any electronic or similar device having information processing capabilities. Section 2(ffc) defines computer

programme as meaning a set of instructions expressed in words, codes, schemes or in any other form including a machine readable medium, capable of causing a computer to perform a particular task or to achieve a particular result. Section 14 provides that for the purposes of the Act, Copyright means the exclusive right subject to the provisions of the Act, to do or authorize the doing of any of the acts described therein in respect of a work or any substantial part thereof. In the case of a computer programme copyright means an act, to reproduce the work in any material form including the storing of it in any medium by electronic means and so on, as described in clause (a) of that section or to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer programme. Section 17 deals with right of ownership of a Copyright and Section 18 entitles the owner to assign the Copyright. Section 19 prescribes the mode of assignment. Section 30 contemplates the granting of licenses by owners of Copyright. The owner of a Copyright in any existing work may grant any interest in the right by license in writing signed by him. Section 51 deals with infringement of Copyright and provides, inter alia, that when any person without a license granted by the owner of the Copyright, does any thing the exclusive right to do which is by the Act conferred upon the owner of the Copyright, it is an infringement.

5. The applicant has no case that it is not the owner of the Copyright. There is no dispute that a use of the programme over which the applicant has a Copyright,

by ICEL without permission, would amount to an infringement of the Copyright. What the applicant has granted to ICEL, is a license to use the computer programme developed by it and owned by it and over which it has a Copyright. This is done for a consideration. But for the license granted, the user by ICEL of the programme would be an infringement of the Copyright of the applicant. When a software developed over which a Copyright is acquired, is permitted to be used by another for a consideration or another is given a right to use it including the taking of copies for the purpose of its business, for a consideration, it appears to me to be a case of receiving royalty for enabling that person to exercise the right to use the programme or the literary work. In terms of the Income-tax Act, royalty means consideration for the transfer of all or any right, including the granting of a license, in respect of any Copyright or literary work. Is not the payment received for transferring the right to use the programme developed by the applicant and over which it has a Copyright, royalty as defined in the Act?

6. What is sought to be argued is that when a software is permitted to be used and in this case copied also for the purpose of ICEL and its business, what is involved is a sale of a copyrighted article or grant of a right to use a copyrighted article, as distinct from the copyright itself and the licensing of the copyright itself alone attracts royalty as defined in the Act. It may be noted that neither the Income-tax Act nor the Copyright Act uses the expression, copyrighted article. It

is an expression borrowed from the United States and from the OECD commentary. Under the Copyright Act, 1957 the owner of a copyright can deal with it in two modes. He can either assign his right wholly or partially, generally or with limitations, or he can grant any interest therein by license. What the applicant has done here is to grant a license to ICEL to use the software, the copyright over which it owns, for a consideration. This is a license recognized by the Copyright Act and it is a known mode of exploitation of a copyright. The applicant has not parted with its title over the copyright in the software. It has conveyed to another a right to use the software over which it has a copyright. The right of user of software, thus, given involves the right to use the copyright. The user of a software created, over which a copyright is acquired cannot be divorced from the use of the copyright itself. When that right of user is given, the right to use the copyright is also given. On the terms of the Income-tax Act read in the light of the Copyright Act, the right granted for use of a copyrighted article for a consideration, would also be royalty since going by the relevant definition, the grant of a right to use the copyrighted article would also be a license by the owner of the Copyright, though limited in nature, limited to the use of the other contracting party alone, without entitling the grantee to further exploit the Copyright. The exclusion in the further proviso of payment made by a resident for the transfer of all or any rights (including the granting of a license) in respect of

computer software supplied by a non-resident manufacturer in two identified situations also indicates that the granting of a license by a non-resident in respect of a computer software for consideration would generate income by way of royalty in other instances or cases. It is, therefore, not possible to accept the argument that what is involved is the mere permitting of the right to use a copyrighted article and the payment involved is not royalty. Indian law does not distinguish between copyrighted article and the copyright. What is needed to attract liability is the farming out of the right to use or of the right itself for consideration.

7. The consideration received is for permitting another to do something which, but for the permission is actionable. If that be so, the grant of the right to use the Copyright for a consideration can only be royalty as understood and cannot be understood as sale price because there is no parting of the right or title by the owner of the Copyright in favour of the grantee.

8. The DTAA involved herein is the one between India and Sri Lanka. The definition of royalty contained in this Treaty in Article 12.3 shows that it is a payment of any kind received as consideration for the 'use of or the right to any copyright'. This is seen to differ from some of the later treaties like the one with USA wherein royalty is payment of any kind received as consideration for the 'use of, or the right to use, any copyright'. The definition in the India-Sri Lanka DTAA is wider than the one found in the Income-tax Act. For, it takes in even the

consideration received for permitting another to use a copyright. Even a right to use need not be conferred.

9. The definition embraces two situations. In the first, it need only be consideration received for permitting another to use a copyright. In the second, it is consideration for conveying a right in the copyright. The DTAA is seen to be wider in this context to rope in even a payment as consideration for mere use of a copyright as royalty. It is not necessary even to grant the right to use the copyright if one were to look at it literally, though the grant of a right to use could be said to be included in the grant of a right in the copyright.

10. In the present case, not merely the use is licensed but the licensee is given the right to copy it and use it wherever it is needed by it for its business. The right given for a consideration to copy the copyrighted software and use it for its own purposes by ICEL whenever and wherever needed by it, clearly attracts the definition of royalty to the consideration paid by ICEL to the applicant, though the right granted may be limited and does not take in a right to further transfer the right or its use.

11. In the Ruling in Dassault Systems (AAR 821 of 2009), this Authority dealt with a different fact situation. In that case the applicant was marketing licensed software products through a distribution channel. It was found therein that “no rights in relation to copyright have been transferred nor any right of using the

copyright as such has been conferred on the licensee.” It has also to be noted that the definition in DTAA including use of a copyright was also not dealt with specifically. Use of a process found in the Income-tax Act was alone specifically dealt with. The enjoyment of some or all the rights which a copyright owner has is necessary to trigger the royalty definition, it was observed. Is it necessary in the context of the DTAA speaking of receipt of consideration for use of any copyright of a literary, artistic or scientific work and the entitlement of an owner of a copyright to license any interest in the copyright? Surely, will not the right to use the software exclusively, a right or interest of the owner of the copyright which is granted or shared with another by the grant of a license for consideration? That consideration, it appears to me, can only be royalty in terms of the DTAA and the Income-tax Act.

12. In the case on hand we find that a right is conferred on ICEL to use the copyright over the software for its purpose and even to copy it for use for its business purposes. On the terms of the transaction, we find that the right given to ICEL to copy the software for its purposes, is a right to use the copyright. In any event, the use of a copyright has been given to ICEL for consideration and that would be royalty in terms of the DTAA.

13. I agree with the Rulings given by Member(R) on the questions posed for our Ruling.

(Justice P.K.Balasubramanyan)
Chairman

Accordingly ruling is given and pronounced on 28th Day of September,
2011.

Sd/-
(P.K.Balasubramanyan)
Chairman

Sd/-
(V.K.Shridhar)
Member

F.No. A.A.R. No.835 of 2009

Dated 28.9.2011

- (A) This copy is certified to be a true copy of the advance ruling and is sent to:
1. The applicant.
 2. The Director of Income-tax (International Taxation) Mumbai.
 3. The Joint Secretary (FT&TR-I), M/Finance, CBDT, Bhikaji Cama Place, New Delhi.
 4. The Joint Secretary (FT&TR-II), M/Finance, CBDT, Bhikaji Cama Place, New Delhi
 5. Guard file.
- (B) In view of the provisions contained in Section 245S of the Act, this ruling should not be given for publication without obtaining prior permission of the Authority.

(Nidhi Srivastava)
Addl. Commissioner of Income-tax(AAR- IT)