

IN THE INCOME TAX APPELLATE TRIBUNAL "C" BENCH : KOLKATA

[Before Hon'ble Sri N.V.Vasudevan, JM & Dr.Arjun Lal Saini, AM]

I.T.A No. 673/Kol/2013

Assessment Year : 2010-11

I.T.C. Limited
Kolkata

-vs.-

A.D.I.T. (I.T.)-2(1)
Kolkata

[PAN : AAACI 5950 L]
(Appellant)

(Respondent)

For the Appellant : Shri J.P.Khaitan, Advocate
For the Respondent : Shri N.B.Som, JCIT. Sr.DR

Date of Hearing : 07.02.2017.

Date of Pronouncement : 01.03.2017.

ORDER

Per N.V.Vasudevan, JM

This is an appeal by the Assessee against the order dated 04.01.2013 of CIT(A)-VI, Kolkata relating to A.Y.2010-11. This appeal arises out of order passed by ADIT (International Taxation)-2 (1), Kolkata u/s 201 (1) and 201(1A) of the Income Tax Act, 1961 (Act).

2. The Appellant M/s I.T.C. Ltd made a payment of US\$ 2,80,8900/- and Rs.15,218/- on 21.05.2009 to a company by name M/s. New Page PTE Ltd (herein referred to as NPL). The subject matter of dispute in this appeal is as to whether the aforesaid payment is in the nature of royalty chargeable to tax in India and therefore the appellant herein was under an obligation to deduct tax at source at the time of making payment in terms of section 195 of the Act.

3. Under an agreement dated 15.12.2008 between the appellant and NPL it was agreed that NPL would grant licence to the appellant herein, a perpetual, non transferable non

exclusive non sub licensable right in respect of those components of the software set out in Schedule-I to the said agreement. The preamble to this agreement refers to the fact that NPL is a developer and owner of copyright in respect of various software packages and that the appellant herein is desirous of using the NPL software package identified in Part-B of Schedule-I to the agreement subject to certain terms and conditions. Clause-3 of the agreement regarding grant of licence is as follows :-

“3. **Grant of Licence**

3.1 Subject to the terms and conditions set forth in this Agreement, and in particular, the payment of the Licence Fees by ITC in accordance with this Agreement, NewsPage grants to ITC a perpetual, non-transferable (except as set forth in this Agreement), irrevocable, non-exclusive, non-sub licensable right:

3.1.1 in respect of those components of the Software (together with any Customisations thereof) licensed by reference to the number of users, for up to the Designated Number of Users to Use the specified Version of the Software; and

3.1.2 in respect of those components of the Software (together with any Customisations thereof) licensed by reference to the number of installations permitted, for ITC to install and Use up to the Designated Number of Installations of the specified Version of the Software;

3.2 all as more particularly described and set forth in Schedule 1 and provided pursuant to this Agreement, all at the Location, in object code form and in accordance with the Documentation ("the Software Licence"), and not otherwise. The Software Licence granted is solely for 'ITC's business purposes (which shall not in any event to extend to include renting, leasing, time sharing or providing any service bureau function to or on behalf of third parties). ITC may allow its customers and contractors to use the Software Licence for this purpose only. NewsPage retains all rights, title and interest in the Software. Source code is not provided with the Software.

3.3 Newspaper shall provide ITC all updates to the Software as maybe made available to its customers commercially from time to time. ITC may apply and use any update which NewsPage shall be obliged to provide in respect of the Software at any time, and unless NewsPage prescribes otherwise, the terms of this Agreement shall also apply in respect of the Use of such update.

3.4 ITC shall not permanently or temporarily move any part of the Software or operate the same at any other location other than the Location without the prior written consent of News Page.

3.5 Newspaper shall not be responsible for the installation of the Software. ITC will be entitled, at its option, to engage any other party for the purpose.”

Clause 3A of the agreement provides that the software will be delivered by electronic means and various other modes and these modes are set out in the said clause. Clause 4 of the agreement regarding other services to be provided by NPL reads as follows :-

“4. **Services**

4.1 Subject to the terms of this Agreement, NewsPage shall provide to ITC the Services more particularly described in Schedule 2 hereto upon the terms therein set forth, and provided always that ITC shall have paid to NewsPage the Charges in connection with the provision of such Services as specified in Schedule 3, and otherwise observed all of its obligations therein set forth.

4.2 NewsPage shall not be obliged whether in relation to ITC or any third party or otherwise generally, to provide any Services:

4.2.1 unless specifically included as part of the Services in Schedule 2, and if so, only in accordance with the terms thereof.

NewsPage may sub contract all or any part of the services with the prior written consent of ITC. However, NewsPage acknowledges that it shall, at all times, remain responsible for the Services provided by such sub- contractors.

Clause-5 of the Agreement provides for consideration payable by the appellant to NPL for the rights conferred under the Agreement and the mode of payment of consideration and are not very material for rendering a decision on the issue that arises for consideration in this appeal. Clause 8 of the agreement deals with the intellectual property rights that are conferred under the agreement and it reads as follows :-

“8. **Intellectual Property Rights**

8.1 Save for the Software Licence granted to ITC in Clause 3, all rights, title and interest in and to the Software (except in any Agreed Customisation(s) or Customisation otherwise commissioned by ITC), including without limitation, any patent, copyright, registered design, trade mark, goodwill or other industrial or intellectual property rights in connection therewith ("NewsPage IP") shall vest solely and absolutely in NewsPage or its licensors and no additional right or license shall be granted to ITC by implication, estoppel or otherwise.

All rights, title and interest in and to the Agreed Customisation(s) and Customisation, otherwise commissioned by ITC, including without limitation, any patent, copyright, registered design, trade mark, goodwill or other industrial or intellectual property rights in connection therewith ("ITC IP") shall vest solely and absolutely in ITC and no additional right or license shall be granted to NewsPage by implication, estoppel or otherwise.

8.2 In particular, but without limitation, save as expressly provided hereunder, ITC shall not without NewsPage's prior consent, (i) translate any portion of the Software into any other format or language or otherwise, translate, or create derivative works from the Software; (ii) rent, lease, timeshare or otherwise grant access to the Software or its results or sublicense, distribute or otherwise transfer the Software to any third party; or (iii) merge the Software with other software; (iv) reverse engineer, decompile, disassemble, or otherwise attempt to derive the source code for the Software, except and only to the extent that such activity is expressly permitted by applicable law notwithstanding this limitation (but in such instance only upon prior notification to NewsPage); or (v) otherwise use or copy the Software except as expressly allowed under this Agreement. NewsPage may audit compliance with these terms during normal Business Hours and upon giving at least 7 Business Days prior notice.

8.3 The Software Licence confers no title or ownership and is not a sale of any rights in the Software, the Documentation, or the media on which they are recorded or printed.

8.4 ITC shall not remove, change, add to or alter any copyright, trade marks, logos, patent notices or other proprietary markings placed by NewsPage on or in connection with the Software. NewsPage shall not use any of ITC's logo, trademark or copyrights in its publicity or its communication material or any manner whatsoever. NewsPage may cite the performance of the Services to its clients and prospective clients as an indication of NewsPage's experience, without prior approval of ITC, unless ITC and NewsPage specifically agree otherwise in writing."

Clause 9 of the agreement regarding confidentiality of information provides that the appellant herein shall maintain confidentiality of information in the form of software it receives under this agreement and it provides that the appellant herein will not reverse engineer, decompile or disassemble any part of the software or source code of the software. Schedule I and II to the agreement regarding software licence details and services to be provided by NPL under the agreement are given as **Annexures 1 and 2** to this order.

4. In the light of the above terms of the agreement that the question whether the sums paid by the Appellant to NPL is in the nature of “Royalty” chargeable to tax in India has to be decided.

5. NPL is a foreign company and is a tax resident of Singapore. Under section 4 of the Act, the charge to tax is on the total income of every person. Section 5 of the Act explains the scope of total income of every person. Section 5(2) lays down the scope of total income of every person who is a non-resident. Any income received or deemed to be received in India and any income which accrues or arises in India or is deemed to have, accrued and arisen in India shall be included in his total income. Section 9 of the Act lays down as to when income shall be deemed to have accrued or arisen in India. If the payment in question is held to be “Royalty” then it is chargeable to tax in India in terms of Sec.9(1)(vi) of Act in the hands of NPL and therefore there would be an obligation on the part of the appellant to deduct tax at source in terms of Sec.195 of the Act. However such chargeability to tax in India, where there is a treaty between the country of which NPL is a Tax Resident, would depend on the terms of the treaty between India and the other country, in this case Singapore. Section 90 of the Act provides that Central Government may enter into an agreement with the Government of any country outside India for avoidance of Double Taxation of income under the Act and under the corresponding law in force in that country. Section 90(2) provides that

where such agreement exists with any country outside India, then in relation to an assessee to whom such agreement applies, the provisions of the Act, shall apply only to the extent they are more beneficial to that assessee. India and Singapore have entered into an Agreement for Avoidance of Double Taxation (DTAA) with effect from 27-5-1994 and therefore the taxability of any income that accrues or arises in India to the assessee who is non-resident in India and a tax resident of Singapore will have to be determined in accordance with the said DTAA. The said DTAA also defines as to what is "Royalty". Therefore if under the treaty the amount paid by the appellant to NPL is not in the nature of royalty then the same, even though it might be in the nature of royalty under the Act, yet would not be chargeable to tax in India by reason of the treaty provisions being more favourable. In such event the amount received by NPL would be in the nature of business income, if arises in the course of NPL's business. Business income would be chargeable to tax in India under Article 7(1) of the DTAA only if NPL has a Permanent Establishment (PE) in India. As to when a non-resident would be considered as having a PE in the other country is generally decided on the basis of the facts in each case, the criteria being the extent to which the Non-Resident has set a firm foot in the soil of the other country. Admittedly NPL did not have a PE in India and therefore the issue in this appeal will have to be confined to the question only as to whether the payment in question by the appellant to NPL is in the nature of royalty. We may also clarify here that there is a vague reference to the payment in question being in the nature of "Fees for Technical Services rendered" in para 21 of the CIT(A)'s order but the case of the AO as well as the CIT(A) is as to whether the payment in question is in the nature of "Royalty" and therefore that will be the only issue that arises for consideration in this appeal.

6. The definition of royalty as given in Article-12(3) of the DTAA is as follows:

“Article 12(3): The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use:

(a)	any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for 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, property or information;
(b)	any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraph 4(b) or 4(c) of Article 8.

7. The stand of the Assessing Officer (AO) was however that the key features of the software that were licenced to NPL showed that the same was for smooth functioning of the business of the appellant and effective management and monitoring of its field formation. According to the AO the software helps in the day to day administration by providing effective internal control mechanism and has been developed keeping in mind the business and commercial requirement and unique needs of the appellant. According to the AO the software was structured to suit the business model of the appellant and has been customized to cater to the specific business needs of the appellant. In coming to the above conclusion the AO made a reference to clause 8 and Appendix-II of the agreement for use of software dated 15.12.2008. The AO thereafter formulated the following issues for consideration :-

- a) What is the concept of royalty?
- b) Definition of Royalty under domestic law
- c) Whether sale of copyrighted article or transfer of copyright?
- d) Position under the treaty law.”

8. On the issue of what is the concept of royalty, the AO concluded that consideration paid to a person who has exclusive right over a thing or intellectual property for allowing others to use the thing or intellectual property had to be regarded as royalty.

9. On the question as to what is royalty in the domestic law, the AO after referring to the definition of 'Royalty' under Sec.9(1)(vi) of the Act and after listing out the list of intellectual property rights that are mentioned in the said section, concluded that there could be no doubt that software was intellectual property and therefore was not in the nature of goods and therefore license to use the software would be in the nature of royalty under the domestic law i.e., the Act. We may mention here that computer software is not specifically set out in section 9(1)(vi) of the Act and it was only by the Finance Act, 2012 w.r.e.f. 1-6-1976 that Explanation 4 was inserted which makes a reference to Computer Software. The discussion of the AO on this aspect is not very important because what is important is to see if the payment in question falls within the definition of "Royalty" as given in the DTAA as discussed in para-5 of this order and for other reasons that will be set out later.

10. On the question whether the payment in question is in the nature of royalty under the DTAA, the AO after extracting the definition of "Royalty" under Article 12(3) of the DTAA, expressed the view that the term royalty in the treaty is same as in the domestic law and it refers to:

- 1) patent, trademark, design or model, plan, secret formula or process.
- 2) Information concerning industrial, commercial or scientific experience.
- 3) Industrial, commercial or scientific equipment
- 4) Literary, artistic or scientific work including cinematograph films.

According to him, mere use in the case of first three categories was royalty and in case of fourth category alone it was necessary that there should be use of copyright right. According to him, the minor differences were-

- 1) in case of first category, instead of transfer of any right, the treaty uses the word 'right to use'

- 2) the treaty uses specific words 'copyright of literary, artistic or scientific work' whereas domestic law says 'copyright, literary, artistic or scientific work'.
- 3) The treaty does not use the word 'a similar property'
- 4) There is a comma after the phrase 'secret formula or process' which is not there in the domestic law using the same phrase as 'secret formula or process or.' It means the word secret should also be applied to the word process. So, to qualify as royalty it should be a secret process.

The AO held that the above differences do not change the position in respect of software once they are classified as process. They are also secret because the source code is not given to the user. The use of secret process implies use of a process which is secret, i.e, not available in public domain. It is not necessary that the secret should be divulged to the user. In the present world of technology, it is possible to allow others to use a process without disclosing the secrecy of the process. For instance software to determine whether a number is prime number or not is a secret process. The user of such software uses the process without knowing how the software works. The AO therefore concluded that the payment for use of software is for use of secret process and therefore the payment in question would be in the nature of royalty.

11. On the question whether the software in question was sale of “Copyrighted Item” or transfer of “Copyright right”, the Assessee’s argument was that the software acquired is a copyrighted item and not copyright right. It was argued that in the case of a book, when the books are sold, it is the sale of copyrighted item but when a right to copy is given to a distributor who in turn makes copies and sales books, it is said that distributor has acquired a copyright right. The payment for copyright right is royalty and not for copyrighted item. According to the AO, the above statement would be correct when dealing with tangible properties like books, paintings, model etc because these are the end products in themselves but would not hold good in the case of intangible properties like software, designs etc. The AO thereafter observed that Royalties were of two types-

copyright royalties and know-how royalties. In case of later, the payment for mere use would qualify as royalty. For instance standardized design for construction of a particular type of bridge. The developer only gives a right to use to the payer. The design is given in the form of a booklet with detailed drawings etc. It is in the physical form but it does not qualify as a tangible property or a copyrighted item. It comes under the know-how royalty. Similar is the case of software. Even the standardized software will fall under the category of know how royalty. The AO further observed that even if it is presumed that software on carrier media disks or tapes is an copyrighted article and not an intangible property, then sale of software on a CD will not be royalty but if the same software is downloaded on internet with the permission of developer, it would not be an article. Consequently, it would be in the nature of royalty. According to him taxability of a payment for acquisition of the same property cannot be determined on the basis of method of deliver. According to him the fact that the payment is made for the use of contents in a CD is alone relevant. Therefore software cannot be classified as copyrighted article.

12. For the above reasons, the AO came to the conclusion that the payment in question was in the nature of “Royalty” and that the appellant ought to have deducted tax at source at the time of making payment to NPL. Consequently the appellant was held as an Assessee in default in respect of the tax that ought to have been deducted at source and consequent liability for tax and interest thereon was imposed u/s.201(1) & 201(1A) of the Act.

13. On appeal by the Appellant, the CIT(A) concurred with the view of the AO. The CIT(A)’s conclusions, were similar to the conclusions reached by the AO and hence not discussed. These observations are contained in paragraph 28 to 34 of his order.

14. Aggrieved by the order of the CIT(A), the Appellant has preferred the present appeal before the Tribunal. We have heard the very elaborate submissions made on behalf of the Assessee and the learned DR. The learned counsel for the Assessee made his submissions on identical lines as was made by the Assessee in the case of DDIT(International Taxation) & others Vs. Reliance Industries Ltd. & others 159 ITD 208 (Mumbai) wherein on identical facts, the Hon'ble Mumbai Bench of the ITAT held that the payment was not in the nature of "Royalty". The learned DR's arguments were on the lines set out by the AO in the order passed u/s.201(1) of the Act. He placed reliance on the decision of the ITAT Bangalore Bench in the case of Vodafone South Ltd. Vs. DDIT(International Taxation), Circule-1(1), Bangalore (2015) 53 taxmann.com 441(Bangalore) for the proposition that as tax deductor, the person making payment cannot seek to rely on DTAA as a defence for non deduction of tax at the time of making payment. Further reliance was placed on a decision of the Chennai Bench of the ITAT in the case of Organisation Development Pte.Ltd Vs. DDIT(IT) (2012) 19 taxmann.com 156(Chennai) in which the issue was as to whether the payment in that case was in the nature of "Fees for Technical Services"(FTS). We have already observed in the earlier part of this order that the issue in the present appeal is as to whether the payment in question is in the nature of "Royalty" and therefore this decision in our view will not be of any assistance to the case of the revenue. We will deal with specific arguments in the following paragraphs

15. The first and foremost question for adjudication before us is as to whether the definition of 'Royalty' as provided under the Income Tax Act is to be taken or that which has been provided in the DTAA between India and Singapore. So far as the definition of royalty as provided under Expln.2 & 4 to section 9(1)(vi) of The Income Tax Act is concerned, the relevant part of the said provision is reproduced 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 licence) 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).”

“Explanation 4.—For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.”

(inserted by Finance Act, 2012 w.r.e.f. 1-6-1976)

16. The definition of “royalty” as provided under DTAA with Singapore: **Article 12(3)**

“The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use:

a. any copyright of literary, artistic or scientific work, including cinematograph film, or films or tapes used for 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, property or information;

b. any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraph 4(b) or 4(c) of Article 8.”

17. A comparison of the definition of ‘royalty’ as provided under the DTAA, as reproduced above, with the definition of ‘royalty’ as provided under the Act shows that the definition provided under the DTAA is not as exhaustive as the definition as contained in the Act. The definition of “Royalty” in the DTAA covers only payment which is received as consideration for the ‘use of’ or the ‘right to use’ **‘any copyright** of literary, artistic, scientific work including” (emphasis supplied by us). The right to use a computer software/programme has not been specifically mentioned in the DTAA. Article 3 of the DTAA for the purpose of ready reference is reproduced as under:

Art 3. “(2.) As regards the application of the Agreement by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have, the meaning which it has under the law of that State concerning the taxes to which the Agreement applies.”

The expression computer software was not specifically defined in the Act or the DTAA prior to insertion of Explanation-4 to Sec.9(1)(vi) of the Act. Therefore prior to such insertion, one has to look at the provisions of the Copyright Act, 1957 which defined various forms of intellectual property in India. We have to clarify that Explanation-4 to Sec.9(1)(vi) of the Act was inserted by the Finance Act, 2012 w.r.e.f 1-6-1976 which enlarges the definition of “Royalty” and therefore not beneficial to NPL in so far as it treats mere “right for use” or “right to use” a computer software as distinct from the definition in Article 12(3) of the DTAA which refers to ‘use of’ or the ‘right to use’ **‘any copyright** of literary, artistic, scientific work including. In view of Sec.90(2) of

the Act NPL can opt to be governed by the DTAA which is more favourable rather than Explanation-4 to Sec.9(1)(vi) of the Act which imposes a tax burden on NPL. The question whether Explanation-4 to Sec.9(1)(vi) which was enacted after the DTAA can override the provisions of the DTAA is another question which will be discussed later. Therefore the definition of “Royalty” as given in the DTAA has to be adopted.

18. The next question before us, at this stage, is as to whether the term ‘literary work’ as mentioned in the definition of royalty in the treaty would include ‘software’ or not? As per the provisions of section 2(o) of the Indian Copyright Act, 1957, the term ‘literary work’ includes computer programs, tables and compilations including computer data base. Therefore, the computer software has been recognized as a literary work in India, if they are original intellectual creations.

19. What is the right that was given to the Appellate by NPL under the agreement dated 15.12.2008 and whether the said right can be said to right to use copyright in computer software. Section 14 of the Copyright Act, 1957 explains the meaning of “Copyright” as under:

“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 authorize 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-cl. (i) to (vi);

(b) in the case of a computer programme,-

(i) to do any of the acts specified in cl. (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.”

20. A perusal of the above provisions of the copyright Act reveals that the computer software is included in the definition of literary work and is covered under the purview and scope of copyright. The **exclusive rights** to do or authorize the doing of certain acts as mentioned in clause (a) and clause (b) of section 14 vests in the owner of the work such as to reproduce the work, to issue copies, to make translation or adaptation, to sell or give on commercial rental in respect of a work. The internal use of the work for the purpose it has been purchased does not constitute right to use the copy right in work. A combined reading of clause-3 and clause-8 of the Agreement dated 15.12.2008 between the appellant and NPL, clearly shows that the Appellant had only a right to use the computer software and did not have **right to use copyright in the computer software**. In other words none of the rights as is envisaged under Sec.14(a) or (b) of the Copyright Act, 1957 was conveyed by the agreement dated 15.12.2008. Therefore the payment in question made by the Assessee to NPL cannot be regarded as “Royalty”. As we have already observed the Act does not specifically include “computer software” in the term “literary work” and under such circumstances, if we apply the provisions of Act to

define the scope of “Literary Work”, then perhaps the “computer software” will be out of the scope of the term royalty as defined under the DTAA. However, if we apply the Copyright Act, then the “computer software” will have to be included in the term “literary work” but to constitute “royalty” under the DTAA, the consideration should have been paid for the use of or the right to use the copyright in the “literary work” and not the right to use “literary work” itself.

21. What is the effect of insertion of Explanation-4 in the definition of “Royalty” in Sec.9(1)(vi) of the Act by the Finance Act, 2012, w.r.e.f. 1-6-1976. The Hon’ble Delhi High Court in the case of “DIT vs Nokia Networks OY” [2012] Taxmann.com 225 (Delhi) has held that though ‘Explanation 4’ was added to section 9(1)(vi) by the Finance Act 2012 with retrospective effect from 1.6.1976 to provide that all consideration for user of software shall be assessable as “royalty”, the definition in the DTAA has been left unchanged. That in “Siemens AG” 310 ITR 320 (Bom), it was held that amendments cannot be read into the treaty. As the assessee has opted to be assessed by the DTAA, the consideration cannot be assessed as “royalty” despite the retrospective amendments to the Act. The relevant findings of the Hon’ble Delhi High Court as given in para 23 of the said decision, for the sake of convenience are reproduced as under:

“However, the above argument misses the vital point namely the assessee has opted to be governed by the treaty and the language of the said treaty differs from the amended Section 9 of the Act. It is categorically held in CIT Vs. Siemens Aktiengesellschaft, 310 ITR 320 (Bom) that the amendments cannot be read into the treaty. On the wording of the treaty, we have already held in Ericsson (supra) that a copyrighted article does not fall within the purview of Royalty.”

22. Further, in a recent judgment in the case of “DIT Vs New Skies Satellite BV,” (ITA 473/2012 vide order dated 08.02.2016), the Hon’ble Delhi High Court has observed that no amendment to the Act, whether retrospective or prospective can be read in a manner so as to extend its operation to the terms of an international treaty. In other words, a

clarificatory or declaratory amendment, much less one which may seek to overcome an unwelcome judicial interpretation of law, cannot be allowed to have the same retroactive effect on an international instrument affected between two sovereign states prior to such amendment. That an amendment to a treaty must be brought about by an agreement between the parties. Unilateral amendments to treaties are therefore categorically prohibited. Even the Parliament is not competent to effect amendments to international instruments. As held by the Hon'ble Supreme Court in "Azadi Bachao Andolan" (2003) 263 ITR 607, these treaties are creations of a different process subject to negotiations by sovereign nations. Therefore insertion of Explanation-4 in the definition of "Royalty" in Sec.9(1)(vi) of the Act by the Finance Act, 2012, w.r.e.f. 1-6-1976, has no effect whatsoever and the issue has to be decided in the light of the definition of "Royalty" as contained in the DTAA read with the relevant provisions of the Copyright Act, 1957.

23. The learned counsel for the Assessee also addressed arguments to the effect that the right to use the software in the present case is akin to sale of copyrighted article rather than sale of copyright. Reference was made to the decision of the Hon'ble Delhi High Court in the case of Director of Income Tax Vs. Ericsson A.B., New Delhi ITA No.504/2007 dated 23.12.2007 wherein it was held that the license granted to the licensee permitting him to download the computer programme and storing it in computer for its own use is only incidental to the facility extended to the licensee to make use of the copyrighted product for his internal business purposes. The said process is necessary to make the program functional and to have access to it. Apart from such incidental facility, the licensee has no right to deal with the product just as the owner would be in a position to do. The Hon'ble Delhi High Court has observed that in such a case there is no transfer of any right in respect of copyright to the assessee and it is a case of transfer of a copyrighted article. The payment is for a copyrighted article and represents the purchase price of an article and cannot be considered as royalty. The Hon'ble Delhi High Court has further held that what is transferred is neither can be right

in the software nor the use of the copyright in the software, but is the right to use copyrighted material or article which is clearly distinct from the rights in a copyright and the same does not give rise to any royalty income and would be the 'business income' of the non-resident. The learned DR however placed reliance on the decision of the Hon'ble Karnataka High Court in "CIT vs. Samsung Electronics Company Ltd. & Others" (2012) 345 ITR 494 wherein it has been observed that under the agreement, what had been transferred was only a license to use the copyright belonging to the non-resident subject to the terms and conditions of the agreement and that the non-resident supplier continued to be the owner of the copyright and all other intellectual property rights; license is granted for making use of the copyright in respect of software under the respective agreement and that the same would amount to transfer of part of the copyright. The learned counsel for the Assessee submitted that there is no decision of the Hon'ble Calcutta High Court rendered on the issue and therefore where two views are possible on an issue, the view favourable to the Assessee should be followed. It was his contention that following the view expressed by the Hon'ble Delhi High Court in the case of DIT Vs. Ericsson AB, New Delhi (Supra), which is favourable to the Assessee, it should be held that the consideration received by the NPL was not royalty. The receipts would constitute income from business in the hands of NPL and since NPL did not admittedly have a permanent establishment in India its' income from business cannot be taxed in India in the absence of a permanent establishment.

24. We are of the view that the view expressed by the Hon'ble Delhi High Court in the case of DIT Vs. Ericsson AB, New Delhi (Supra), which is favourable to the Assessee, should be followed and therefore we hold that the consideration received by the Assessee for software was not royalty. The receipts would constitute business receipts in the hands of the NPL. Admittedly NPL does not have a permanent establishment and therefore business income of the NPL cannot be taxed in India in the absence of a permanent establishment.

25. The learned DR submitted that the Appellant, whose obligation is to deduct tax at source u/s.195 of the Act, cannot place reliance on the DTAA as NPL could do in defence of non taxability in India of income deemed to accrue and arise in India and in this regard relied on the decision of the decision rendered by the ITAT Bangalore Bench in the case of Vodafone South (supra). We have perused the said decision and we find that the observations of the Tribunal were made in the context of dispute raised by the revenue that the payee was not tax resident of a country, the benefits of DTAA between India and the said country were sought to be pressed into service by the payer. This is clear from a complete reading of paragraph 37 of the said decision. In the present case there is no dispute raised by the revenue that NPL was not a tax resident of Singapore and that the benefits of DTAA between India and Singapore cannot therefore be available to the appellant. We are of the view that the decision in the case of Vodafone South (supra) is therefore of no help to the plea of the revenue before us. The decision rendered by the Chennai bench of ITAT in the case of Organisation Development Pte.Ltd., (supra) is again in the context of FTS and the findings in that case is on the facts of that case. The learned DR was neither able to establish nor do we see any parity of facts between the aforesaid decision and the facts of the present case before the Tribunal.

26. For the reasons given above, we hold that the amount paid by the appellant to NPL is not in the nature of royalty within the meaning of the DTAA between India and Singapore and therefore the amount received by NPL would be in the nature of business income which would be chargeable to tax in India under Article 7(1) of the DTAA only if NPL has a Permanent Establishment (PE) in India. Admittedly NPL did not have a PE in India and therefore the payment in question is not chargeable to tax in India and therefore there was no obligation on the part of the appellant to deduct tax at source u/s.195 of the Act. Consequently, the Assessee could not be treated as an Assessee in default u/s.201(1) of the Act nor could interest be levied on tax not deducted at source on tax not deducted at source till date of payment to the account of the Central

Government u/s.201(1A) of the Act. The orders u/s.201(1) and 201(1A) of the Act are accordingly cancelled.

27. In the result appeal by the Assessee is allowed.

Order pronounced in the Court on 01.03.2017.

Sd/-
[Dr.Arjun Lal Saini]
Accountant Member

Sd/-
[N.V.Vasudevan]
Judicial Member

Dated : 01.03.2017.

[RG PS]

Copy of the order forwarded to:

1. I.T.C. Limited, Taxation Department, 37 J.L.Nehru Road, Kolkata-700071.
2. A.D.I.T. (International Taxation)-2(1) Kolkata.
3. C.I.T.(A)-VI, Kolkata. 4. CIT Kolkata
- 5.CIT(DR), Kolkata Benches, Kolkata.

True copy

By Order

Asstt.Registrar, ITAT, Kolkata Benches

