

**IN THE INCOME TAX APPELLATE TRIBUNAL
“C” BENCH: BANGALORE****BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER**

IT(IT)A Nos.177 & 178/Bang/2023
Assessment Years: 2015-16 & 2016-17

Deputy Commissioner of Income-tax Intl. Taxn., Circle-1(2) Bengaluru	Vs.	M/s. IBM Singapore Pvt. Ltd. No.12, Subramanya Arcade Bannerghatta Main Road Bangalore 560 029 PAN NO : AACCI2917B
APPELLANT		RESPONDENT

Appellant by	:	Ms. Neera Malhotra, D.R.
Respondent by	:	Shri Sharath Rao, A.R.

Date of Hearing	:	03.05.2023
Date of Pronouncement	:	03.05.2023

O R D E R**PER BEENA PILLAI, JUDICIAL MEMBER:**

These appeals by revenue are directed against different orders of CIT(A) for the assessment years 2015-16 & 2016-17 both are dated 11.1.2023. The issues in both the appeals are common in nature. Hence, these are clubbed together, heard together and disposed of in a common order for the sake of convenience.

2. The common grounds raised in both the appeals are as follows:-

“1. *The Learned CIT(A) erred in upholding that the payments received by the assessee towards sale of software amounting to Rs*

531,95,30,146/- in the AY 2015-16 & Rs.413,70,91,151/- in the AY 2016-17 is not 'Royalty.

2. *The Learned CIT(A) erred in not considering the fact that the Supreme Court's decision in the case of Engineering Analysis had taken into consideration only one sample agreement with a related party, which may not represent the complete picture on the nature of softwares sold by the assessee and the rights granted to the purchaser of software.*

3. *The learned CIT (A) erred in failing to take cognizance of the fact that a review petition has been filed by revenue in the case of Engineering Analysis before the Hon'ble Supreme Court."*

3. Facts of the case are as narrated in assessment year 2015-16 are as follows:-

3.1 The assessee filed its return of income for A.Y. 2015-16, declaring income of Rs.27,25,41,490/-. The case was taken up for scrutiny subsequently. The assessee had received a sum of Rs. 29,24,244/- towards payment for seconded employees. The AO, after a detailed discussion held this payment to be in the nature of Fees for Technical Services both under the Income-tax Act,1961 ['the Act' for short] as well as the India-Singapore DTAA.

3.2 During the year under consideration, the assessee had sold software licenses to its associated enterprises and to other Indian customers, as detailed below:

1	IBM India Pvt. Ltd.	Rs.521,66,10,39
2	Non-Associated Enterprises	Rs.9,99,95,503

3.3 The AO treated the amounts received by the assessee from the sale of software to its Indian AE i.e. IBM India and

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other non-AEs as royalty; both under the Act as well as the treaty. The findings of the AO are summarized below:

- Since the use of a computer programme involves the use of a process, it is covered by the definition of royalty u/s 9(1)(vi), as far as the users are concerned.
- Explanation 4 to section 9 (1)(vi) which was inserted by the Finance Act, 2012 w.e.f. 1.4.1976, clarified that consideration for use or the right to use computer software is royalty. In particular, the Memorandum to the Finance Bill, 2012, clarified the legislative intent behind taxing the sale of software as royalty.
- Since the DTAA had been entered into force after 7th Sept, 1990, this position of the Indian Government that use of software under license amounts to royalty, was already known to other treaty partners, at the time of entering to DTAA, hence it was wrong on the part of the assessee to plead that the Explanation 4 was unilaterally overriding the DTAA.
- As per Article 12 of the DTAA payment for the use of, or the right to use any copyright of literary work, including, consideration for alienation of such right, is royalty. Since a computer programme is a literary work, payment for the use of or the right to use of copyright in it (computer programme), including consideration for alienation of copyright right in it, is royalty under the DTAA also.
- The software is an embodiment of the knowledge, skill, experience and expertise of its (Software's)

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developer. In the case of software, a right in the software is the just or legal claim of its developer to it and such right is called the 'Copyright'. Thus, the right is not embodied in the software but it subsists in it. The very nature of the software is that it, being a computer programme, cannot be sold without the transaction involving some transfer of copyright.

- Copyright as defined in Section 14 of Copyright Act is not an indivisible right but a bundle of rights. Further, the bundle of rights comprising copyright is also not an indivisible bundle, but consists of discreet rights bundled together.
- Sec.14(b)(ii) of the Copyright Act which deals specifically with computer programme makes the right of selling or renting out a copy of the computer programme a copyright. Such a right is not a copyright in the case of a book, which can be sold as a chattel without transferring any copyright. But the software (computer programme) cannot be sold as a chattel without the transaction involving some transfer of copyright, which in turn is the bundle of rights defined in Sec.14(a) of the Copyright Act.
- While the original copyright owner has the option to retain the exclusivity and keep all the rights to himself, he also has the option under the Copyright Act to assign one or more of these rights. The licensee does not become the owner of one or more rights comprised in the copyright as in the case of an assignee but gets an interest in the right. Such interest in the right which is not the right itself is

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usually the right to use the copyright without becoming the owner of the copyright.

- The assessee has not parted with or been divested of its exclusive right to do or to authorize others to do the acts specified in Sec.14(b) of the Copyright Act in respect of the software developed by it. All it has done is, by exercising its right as the owner of copyright in the software, is just authorizing IBM India to sell or offer for sale that software to various remarketers and/or end-users. This is done in terms of an agreement entered between the assessee and IBM India, called IBM Software Remarketer Agreement (SRA). Since, as per the Software Remarketer Agreement, IBM India was only authorized (licensed) to sell or offer for sale the software in question, and the software is not sold to it, the consideration paid by IBM India to the assessee is for granting of license (authorization) to use the copyright in the software as specified in Sec.14(b)(ii) and not for the sale of such software.
- There is a transfer of copyright right, though non-exclusive, between the assessee and IBM India and not sale of software as claimed by the assessee. The legal title of the computer program is not transferred to IBM India & others. It still lies with the supplier only i.e. the assessee.
- The transaction by which the end user is authorized to store the software is in terms of an agreement between the end user and IBM Singapore which is called Software License Agreement.

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- The license is granted to the end user by the copyright holder in respect of copyright mentioned in Sec.14(a)(i). That means the programme is licensed to the end user, not sold. Neither the agreement nor the invoices consider the transaction concerned as 'Sale'.
- Since the software in question is only licensed and not sold as per the Software License and Maintenance Agreement, any transaction in terms of this agreement through which the license is granted is not a purchase/sale transaction and the consideration paid by the end user is for granting of license to use the copyright.
- The fact that the IBM India does not duplicate the software acquired from the assessee prior to its sale to the customers does not alter the fact that in the instant case there is a transfer of copyright right from the assessee to IBM India within the purview of Sec.9(1)(vi) of the Income Tax Act.
- Further, licensing of copyright in respect of right to use is inextricably linked to the transaction of sale of software with licenses for resale since the distributor cannot in turn sell the license to use the intellectual properties without being licensed as a distributor. In fact, the license to sell enables the distributor to transact the right to use the intellectual property.

3.4 However, the AO treated the payment for software as royalty. Against this assessee went in appeal before Id. CIT(A) who placed reliance on the judgement of Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. Vs. CIT 432 ITR

471 and decided the issue in favour of assessee. Against this revenue is in appeal before us for both assessment years.

4. After hearing both the parties, we are of the opinion that similar issue came for consideration before this Tribunal in assessee's own case for assessment years 2009-10, 2010-11 & 2012-13 in ITA Nos.1311 to 1313/Bang/2018, wherein the Tribunal vide order dated 3.9.2021 held as under:

Ground No.3 relate to the assessment of sale proceeds received on sale of software licenses as "Royalty income".

Coordinate bench of this Tribunal in assessee's own case for assessment year 2014-15 (supra) decided this issue as under:

"4. The assessee is a Singapore based company engaged in the business of dealing in software & hardware products. Under the provisions of Indian Income Tax Act, the assessee is a non-resident. During the year under consideration, the assessee has sold software licenses to its Associated Enterprise (AE) and also to other Indian customers. The assessee did not offer any income on such sale for taxation in India. The ld. AR submitted that the AE of the assessee, viz., M/s. IBM India Pvt. Ltd is the authorized distributor of software licenses sold by the assessee. In respect of sales made to Non-Associated enterprises, the 14 A.R submitted that majority of sales were made to "other distributors" and in few eases, it was sold to End users also. The details of sales effected by the assessee during the year under consideration in India are tabulated as under by the A.O.

SI. No.	Name of the Party	Sale value (in Rs.)	Offered for taxation or not
1.	IBMIndia Pvt. Ltd.	416,00,24,	No
2.	Non Associated	2514,40,45	No
Total		441,94,65,	

5. The A.O. took the view that the above said aggregate sale consideration of Rs.441.94 Crores constitute "royalty" in the hands of the assessee both under section 9(1)(vi) of the Income-tax Act,1961 ['the Act' for short] and under Double Taxation Avoidance Agreement (DTAA) entered between. India and Singapore. Accordingly, he made addition of Rs.441.94 crores to the total income returned by the assessee. The A.O. placed his reliance onthe decision rendered by Hon'ble Karnataka High Court in the case of Samsung Electronics Company Ltd. (345 ITR 494) and Synopsis International Old Limited (ITA Nos.11-15/2008). The Ld. CIT(A) also confirmed the addition. and hence the assessee has filed this appeal before us.

6. The Ld. A.R. submitted that the assessee has sold only licenses to use the software and it did not part with any of its right over the products within the meaning of Copy right Act. He further submitted that the

provisions of DTAA entered between India and Singapore shall govern these transactions and as per the provisions of DTAA, the sale receipts of software licenses cannot be taxed as "royalty". For all these propositions, the Ld A.R placed his reliance on the decision rendered by Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. (2021) 125 Taxmann.com 42.

7. The Ld A.R submitted that the tax authorities have placed their reliance on the decisions rendered by Hon'ble Karnataka High Court in the case of Samsung Electronics Co Ltd (supra) and Synopsis International Old Ltd (supra). However, both the decisions have been reversed by the Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence P Ltd (supra).

8. The Ld A.R further submitted that the Hon'ble Supreme Court has delivered its decision holding that the software licenses cannot be taxed as royalty under the provisions of DTAA unless copy rights are parted with. The Hon'ble Supreme Court has examined some agreements entered by software suppliers with the Distributors/ end users on sample basis in this regard. It included the agreements entered by the assessee with its distributors (referred as "re-marketecs")/ End users and also the End User's License Agreement (EULA) entered between the distributors and the end users.

(a) The agreement entered by the assessee with End users has been extracted in paragraph 44(i) of the order of Hon'ble Supreme Court.

(b) The agreement entered by the assessee with IBM India (re-marketeer) has been extracted in paragraph 44(ii)a of its order by Hon'ble Supreme Court and

(c) The agreement entered by IBM India (r-marketeer) with the end users has been extracted in. paragraph 44(ii)b of the order.

The Ld.AR submitted that the very same terms and conditions of granting license to use software continue during this year also. The Hon'ble Supreme Court has concluded that the payments made by the distributors and end-users to the non-resident software supplier placed in Singapore, is not "royalty" within the meaning of the provisions of DTAA and hence the distributors/ end users are not liable to deduct tax at source u/s 195 of the Act from the payments made to the non-resident software supplier located in Singapore on the reasoning that the distributor's agreement and end-user's license agreement in the facts of cases before Hon'ble Supreme Court do not create any interest or right in such distributors/end-users, which would amount to use or right to use any copy right.

9. The Ld A.R submitted that the assessee herein is a Singapore resident governed by the DTAA entered between India and Singapore.

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On the examination of very same DTAA provisions, the Hon'ble Supreme Court has held that the payments given by the distributors/ end users to the assessee are not "royalty" within the meaning of provisions of DTAA and hence there was no liability to deduct tax at source from those payments u/s 195 of the Act, since no income is chargeable to tax in India. In the instant case, the AO has assessed the sale proceeds received on sale of licenses as "royalty". In view of the above cited decision of Hon'ble Supreme Court, the sale proceeds received on sale of software licenses cannot be assessed as "royalty". Accordingly, the Ld.AR submitted that the impugned addition made by the AO and confirmed by Ld CIT(A) is liable to be deleted.

10. *The Ld. D.R. on the contrary, placed his reliance on the decision rendered by Ld. CIT(A).*

11. *We heard the parties on this issue and perused the record. As submitted by Ld. A.R., the Hon'ble Supreme Court has examined the issue whether the payments received by non-resident suppliers for selling software licenses are royalty or not in the case of Engineering Analysis Centre of Excellence (P) Ltd (supra). The Hon'ble Supreme Court examined this question considering four types of situations, which has been narrated as under:-*

"4. The appeals before us may be grouped into four categories:

(i) The first category deals with cases in which computer software is purchased directly by an end-user, resident in India, from a foreign, non-resident supplier or manufacturer.

(ii) The second category of cases deals with resident Indian companies that act as distributors or resellers, by purchasing computer software from foreign, non-resident suppliers or manufacturers and then reselling the same to resident Indian end-users.

(iii) The third category concerns cases wherein the distributor happens to be a foreign non-resident vendor, who, after purchasing software from a foreign, non-resident resells the same to resident Indian distributor or end-users.

(iv) The fourth category includes cases wherein computer software is affixed onto hardware and is sold as an integrated unit/equipment by foreign, non-resident suppliers to resident Indian distributors or end-users.

12. *The Hon'ble Supreme Court analysed sample agreements in respect of all the four categories and gave the following finding:-*

"45. A reading of the aforesaid distribution agreement would show that what is granted to the distributor is only a non-

exclusive, nontransferable 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 sublicense 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 art 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 art 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.

13. *After analysing the provisions of Income tax Act, provisions of DTAA, the relevant agreements entered by the assesseees with non-resident software suppliers, provisions of Copy right Acts, the circulars issued by CBDT, various case laws relied upon by the parties, the Hon'ble Supreme Court concluded as under:-*

"CONCLUSION

168. *Given the definition of royalties contained in Article 12 of the DTAA's mentioned in paragraph 41 of this judgment, it is clear that there is no obligation on the persons mentioned in section 195 of the Income-tax Act to deduct tax at source, as the distribution agreements/ EULAs in the facts of these cases do not create any interest or right in such distributors/end-users, which would amount to the use of or right to use any copyright. **The provisions contained in the Income-tax Act (section 9(1)(vi), along with explanations 2 and 4 thereof), which deal with royalty, not being more beneficial to the assesseees, have no application in the facts of these cases.***

169. *Our answer to the question posed before us, is that the amounts paid by resident Indian end-users/distributors to non-resident computer software manufacturers/ suppliers, as consideration for the resale/use of the computer software through EULAs/ distribution-agreements, is not the payment of royalty for the use of copyright in the computer software, and that the same does not give rise to any income taxable in India, as a result of which the persons referred to in section 195 of the Income-tax Act were not liable to deduct any TDS under section 195 of the Income-tax Act. The answer to this question will apply to all four categories of cases enumerated by us in paragraph 4 of this judgment."*

14. *We also notice that the decision rendered by Hon'ble Karnataka High Court in the case of Samsung Electronics Co Ltd (supra) has been reversed by Hon'ble Supreme Court in paragraph 101-102 of its order. Similarly, the decision rendered in the case of Synopsis International Old Ltd. (supra) Ltd (supra) by Hon'ble Karnataka High Court has been reversed in paragraph 103 - 109 of its order. Before us, the Ld. A.R. submitted that the terms of agreements remain the same during the year under consideration also. Accordingly, as per the decision rendered by Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. (supra), sale proceeds received by the assessee on sale of software licenses cannot be categorized as "Royalty" within the meaning of provisions of DTAA. Accordingly, we set aside the order passed by Ld. CIT(A) on this issue and direct the A.O. to delete the addition made as "royalty" income.*

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We heard the Ld. DR on this issue and perused the_ record. We find merit in the submissions of the Ld.AR Respectfully following the aforesaid view we direct the Ld.AO to delete the addition made as royalty income.

Accordingly, ground No.3 raised by assessee stands allowed.”

4.1 Further, Hon’ble jurisdictional High Court in assessment years 2006-07 to 2008-09 in ITA No.301 of 2019 and Others vide judgement dated 8th September, 2021 held as under:-

“Learned Counsel for the appellant – assessee submits that the substantial questions of law raised herein are squarely covered by the ruling of the Hon’ble Apex Court in the case of Engineering Analysis Centre of Excellence Private Limited Vs. The Commissioner of Income Tax and another reported in (2021) 432 ITR 471 (SC).

2. *Learned counsel for the respondents revenue could not dispute the same.*

3. *In view of the aforesaid submissions, the substantial questions of law are answered in favour of the assessee and against the revenue.*

The appeal stands disposed of accordingly.”

4.2 In view of the above order of the Tribunal, we find no infirmity in the order of ld. CIT(A) in these two assessment years. Accordingly, the grounds raised by revenue in both these assessment years i.e. 2015-16 & 2016-17 are dismissed.

5. In the result, both the appeals of the revenue are dismissed.

Order pronounced in the open court on 03rd May, 2023

Sd/-
(Chandra Poojari)
Accountant Member

Sd/-
(Beena Pillai)
Judicial Member

Bangalore,
Dated 03rd May, 2023.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(Judicial)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

**Asst. Registrar,
ITAT, Bangalore.**