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[2016] 71 taxmann.com 213 (Mumbai - Trib.)/[2016] 49 ITR(T) 73 (Mumbai - Trib.)

IT/ILT: Consideration received by assessee for pure sale of 'shrink wrapped software' off shelf, cannot be considered as a 'royalty' within meaning of Article 12(4) of DTAA as same is consideration for sale of copyrighted product and not for use of any copyright

IT/ILT: If any amendment is carried out under domestic law, same cannot be read into treaty

[2016] 71 taxmann.com 213 (Mumbai - Trib.)

IN THE ITAT MUMBAI BENCH 'L'

ADIT (IT) - 3 (2)

v.

Baan Global BV*

G.S. PANNU, ACCOUNTANT MEMBER
AND AMIT SHUKLA, JUDICIAL MEMBER
IT APPEAL NOS. 7048 (MUM.) OF 2010, 3049 (MUM.) OF 2011 AND 776 & 777 (MUM.) OF 2013
[ASSESSMENT YEARS 2006-07 TO 2008-09]
JUNE 13, 2016

I. Section 9 of the Income-tax Act, 1961 read with article 12 of the DTAA between India and Netherlands - Income - Deemed to accrue or arise in India (Royalty) - Assessment years 2006-07 to 2008-09 - Whether to fall within realm and ambit of right to use copyright in computer software programme, said rights must be given and if said rights are not given, there is no copyright in computer programme or software - Held, yes - Assessee-Dutch company was engaged in business of development and sale of computer software - Assessee entered into a 'Distribution Agreement' with Indian subsidiary INFOR India for supply of its software to Indian customers on which INFOR India would receive a fix percentage sum - Terms of agreement, specifically forbade them from decompiling, reverse engineering or disassembling software - Agreement provided that end user would use software only for operation and would not sub-license or modify software - Whether since consideration received by assessee was for pure sale of 'shrink wrapped software' off shelf, i.e., sale of copyrighted product, and not for use of any copyright itself, it could not be considered as a 'royalty' within meaning of Article 12(4) of DTAA - Held, yes [Para 11] [In favour of assessee]

II. Section 9 of the Income-tax Act, 1961, read with article 3 of the DTAA between India and Netherlands - Income - Deemed to accrue or arise in India (General definitions - Alteration in domestic law, effect on treaty) - Assessment year 2007-08 - DRP decided nature of consideration against assessee by taking additional reasoning that in wake of new Explanation 4 to section 9(1)(vi) enlarged definition of 'royalty' should be read into DTAA by virtue of Article 3(2) - Whether amendment carried out in domestic law with retrospective effect will not automatically alter provisions of DTAA - Held, yes - Whether one contracting State which is a party to a treaty, cannot unilaterally alter its provision

and enlarge scope of any term from prism of its domestic law - Held, yes [Para 21] [In favour of assessee]

FACTS-I

- The assessee-Dutch company was engaged in the business of development and sale of computer software and provides other services in relation to its software product. The assessee in India had entered into a 'Distribution Agreement' with INFOR India which is an Indian subsidiary company for supply of its software to Indian customer on which INFOR India would receive a fix percentage sum. INFOR India was an independent distributor of computer software which sells under the brand name of 'INFOR' and is sold as 'off the shelf' software in the market used by the customers in various businesses, like in connection with financial accounting, inventory management, HR management etc. The customer in India would place an order with INFOR India which in turn passes on the order to the assessee for the purchase of the software. The assessee then had the exclusive right to accept or reject the order. However, once the order was accepted by the assessee, the CD containing the software was sent to India and in turn INFOR India distributes the CD to the customer in India. The assessee also deliverd the license-key for the software directly to the customer and the customers pay the consideration for the sale of software to INFOR India, which in turn after retaining the distributor's margin remits the balance amount to the assessee. The assessee also carried out through INFOR India 'other general services' related to software.
- During the year, the assessee had received a sum of Rs. 3.75 crore as sales consideration for the computer software products supplied by it to IFOR India and sum of Rs. 4.79 crore as 'other general services' (OGS fees) from the said Indian subsidiary. Since the assessee did not have a permanent establishment (PE) in India, only the amount of Rs. 4.79 crore received as 'OGS fee' was offered for tax in India as 'fees for technical services', however, so far as the income from sale of software products of Rs. 3.75 crore was concerned same was treated as business profit. Hence, this amount was not shown chargeable to tax in India in absence of any PE in India. In response to the show cause notice by the AO, as to why the said amount received from sale of computer software should not be taxed in India as 'royalty', the assessee submitted that, the receipts from the sale consideration of computer software cannot be treated as 'royalty' both under the 'Income-tax Act' as well as under the 'Tax Treaty' between India and Netherland.
- The Assessing Officer held that, the payment received by the assessee for sale of software was nothing but 'royalty' not only under the Income-tax Act but also within the meaning of India-Netherland DTAA and accordingly, assessed receipts at the rate of 15 per cent being tax rate applicable to the 'royalty income' as per article 12 of DTAA.
- On appeal, the Commissioner (Appeals) held that the payment received by the assessee emanated only from sale of a copyrighted article and therefore, it does not amount to 'royalty' within the meaning of article 12(4) of the India-Netherland DTAA.
- On appeal to the Tribunal:

HELD-I

- The computer software is sold "off shelf" which is mainly used by the Indian customer in their business for financial accounting, inventory management, HR management etc. INFOR India carries out marketing and sale of the software in India and places order with the assessee. The software supplied is then distributed to the Indian customers through INFOR. The consideration charged by INFOR India is based on terms agreed between the assessee and INFOR India as per the 'distribution agreement'. Under the terms of the agreement, as noted by the Commissioner (Appeals), there is no transfer of any copyright in the software product. The payment received by the assessee is purely towards a copyrighted software product as against the payment for any copyright itself. The assessee does not give any right to use the copyright embedded in the software. In other words, the Indian Customer (or INFOR India) except for the limited right to access the copyright software for its own business purpose does not acquire any kind of right to exploit the copyright in the computer software. These facts have not been controverted by the department and, therefore, what has been incorporated and stated by the Commissioner (Appeals) in his order is reckoned as admitted facts. [Para 10]

- From the plain reading of article 12, it can be inferred that, it refers to payments of any kind received as a consideration for the *use of*, or the *right to use* any *'copyright'* of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience. Thus, in order to tax the payment in question as "royalty", it is *sine qua non* that the said payment must fall within the ambit and scope of Para 4 of Article 12. The main emphasis on the payment constituting 'royalty' in Para 4 are for a consideration for the 'use of' or the 'right to use' any copyright. . . . . . The key phrases 'for the use' or 'the right to use any copyright of'; 'any patent. . . . . .; 'or process', 'or for information. . . . . . . ,'; 'or scientific experience', etc., are important parameter for treating a transaction in the nature of 'royalty'. If the payment doesn't fit within these parameters then it doesn't fall within terms of 'royalty' under article 12(4). The computer software does not fall under most of the term used in the article barring 'use of process' or 'use of or right to use of copyrights' Here first of all, the sale of software cannot be held to be covered under the words 'use of process', because the assessee has not allowed the end user to use the process by using the software, as the customer does not have any access to the source code. What is available for their use is software product as such and not the process embedded in it. Several processes may be involved in making computer software but what the customer uses is the software product as such and not the process, which are involved into it. What is required to be examined in the impugned case as to whether there is any use or right to use of copyright? The definition of copyright, though has not been explained or defined in the treaty, however, the various Courts have consistently opined that the definition of 'copyright' as given in the 'Copyright Act, 1957' has to be taken into account for understanding the concept.

- Thus, the definition of 'copyright' in section 14 is an exhaustive definition and it refers to bundle of rights. In respect of computer programming, which is relevant for the issue under consideration before us, the copyright mainly consists of rights as given in clause (b), that is, to do any of the act specified in clause (a) from (i) to (vii) as reproduced above. Thus, to fall within the realm and ambit of right to use copyright in the computer software programme, the aforesaid rights must be given and if the said rights are not given then, there is no copyright in the computer programme or software. As noted by the Commissioner (Appeals), under the terms of the agreement between the assessee and INFOR India, the agreement specifically forbids them from decompiling, reverse engineering or disassembling the software. The agreement also provides that the end user shall use the software only for the operation and shall not sub-license or modify the software. None of the conditions mentioned in section 14 of the Copyright Act are applicable. If the conclusions of Commissioner (Appeals) are based on these facts and agreement, then he has rightly concluded that the consideration received by the assessee is for pure sale of "shrink wrapped software" off the shelf and hence, cannot be considered as a "royalty" within the meaning of article 12(4) of the DTAA, as the same is consideration for sale of copyrighted product and not to use of any copyright. [Para 11]

- The retrospective amendment brought into statute with effect from 1-6-1976 in form of insertion of in Explanation 4 to section 9(1)(vi) cannot be read into the DTAA, because the treaty has not been correspondingly amended in line with new enlarged definition of 'royalty'. The alteration in the provisions of the Act cannot be *per se* read into the treaty unless there is a corresponding negotiation between the two sovereign nations to amend the specific provision of "royalty" in the same line. The limitation clause cannot be read into the treaty for applying the provisions of domestic law like in article 7 in some of the treaties, where domestic laws are made applicable. Here in this case, the 'royalty' has been specifically defined in the treaty and amendment to the definition of such term under the Act would not have any bearing on the definition of such term in the context of DTAA. A treaty which has entered between the two sovereign nations, then one country cannot unilaterally alter its provision. Thus, there is no merit in the contention of the revenue that the amended and enlarged definition should be read into the Treaty. [Para 12]

- The payment received by the assessee for sums amounting to Rs. 3.75 crores does not amount to 'royalty' within the meaning of article 12(4) of Indo-Netherland DTAA and accordingly, the same is not taxable in India. Since, admittedly, the assessee has no PE in India; therefore, same cannot be taxed as business income under article 7. Accordingly, ground raised by the revenue stands dismissed. [Para 13]

- A non-exclusive, non-transferable license (without any right to sub-lease or sub-license) with a very limited right has been given for right to use the component system and there is no covenant to grant any copyright or right to use. Limited right to operate the copyrighted article cannot be reckoned as royalty within the scope of article 12(4); and *secondly,* the use source code is also for a particular component system to modify such component system for its own internal computing operations. This right is again is with the riders and limitations given therein. There is no right given for the 'use of copyright' or any kind of copyright has been given. Thus, nothing turns on with this observation as made by the DRP that source code is some kind of process and, accordingly, the finding given will apply *mutatis mutandis* in this appeal also. Thus, the impugned issue is decided in favour of the assessee and the amount which has been taxed as 'royalty' is held to be non-taxable in India in terms of DTAA. [Para 22]

CASE REVIEW-I

DIT v. *Infrasoft Ltd.* [2013] 39 taxmann.com 88/[2014] 220 Taxman 273 (Delhi) and *CIT* v. *Alacatel Lucent* [2015] 372 ITR 476/231 Taxman 37/56 taxmann.com 413 (Delhi) (para 13) *followed*.

CASE REVIEW-II

CIT v. *Siemens Aktiongesellschaft* [2009] 177 Taxman 81/310 ITR 320 (Bom.) (para 20) *followed*.

CASES REFERRED TO

Tata Consultancy Services v. *State of A.P.* [2004] 271 ITR 401/141 Taxman 132 (SC) (para 3), *Samsung Electronics Co. Ltd.* v. *ITO* [2005] 94 ITD 91 (Bang.) (para 3), *Hewlett Packard (India) (P.) Ltd.* v. *ITO (International Taxation)* [2006] 5 SOT 660 (Bang.) (para 3), *Sonata Information Technology Ltd.* v. *Dy. CIT* [2006] 7 SOT 465 (Bom.) (para 3), *Sonata Information Technology Ltd.* v. *Addl. CIT* [2006] 103 ITD 324 (Bang.) (para 3), *ACC Ltd.* v. *CC* 2001 (128) ELT 21 (SC) (para 3), *IMP Power Ltd.* v. *ITO* [2006] 9 SOT 156 (Bom.) (para 3), *Dy. DIT* v. *Alcatel USA International Marketing Inc.* 2009 taxmann.com 1014 (Mum. - Trib.) (para 6), *Infrasoft Ltd.* v. *Asstt. CIT* [2009] 28 SOT 179 (Delhi) (para 6), *Lucent Technologies Hindustan Ltd.* v. *ITO* [2005] 92 ITD 366 (Bang.) (para 6), *Hewlett Packard (India) (P.) Ltd.* v. *ITO* [2006] 5 SOT 660 (Bang.) (para 6), *Sonata Information Technology Ltd.* v. *Addl. CIT* [2006] 103 ITD 324 (Bang.) (para 6), *Motorola Inc.* v. *Dy. CIT* [2005] 95 ITD 269 (Delhi) (SB) (para 6), *Mphasis BFL* v. *ITO* [2006] 9 SOT 756 (Bang.) (para 6), *CIT* v. *Samsung Electronics Co. Ltd.* [2012] 345 ITR 494/[2011] 203 Taxman 477/16 taxmann.com 141 (Kar.) (para 8), *CIT* v. *Synopsis International Old Ltd.* [2013] 212 Taxman 454/28 taxmann.com 162 (Kar.) (para 8), *DIT* v. *Reliance Info Com Ltd.* [2014] 64 SOT 137/[2013] 39 taxmann.com 140 (Mum. - Trib.) (para 8), *Pr. CIT* v. *M. Tech India (P.) Ltd.* [2016] 381 ITR 31/238 Taxman 178/67 taxmann.com 245 (Delhi) (para 9), *CIT* v. *Dynamic Vertical Software India (P.) Ltd.* [2011] 332 ITR 222/201 Taxman 78/12 taxmann.com 431 (Delhi) (para 9), *DIT* v. *Infrosoft Ltd.* [2013] 39 taxmann.com 88/[2014] 220 Taxman 273 (Delhi) (para 9), *CIT* v. *Alacatel Lucent* [2015] 372 ITR 476/231 Taxman 37/56 taxmann.com 413 (Delhi) (para 9), *DIT* v. *Ericsson AB* [2011] 16 taxmann.com 371/[2012] 204 Taxman 192/343 ITR 470 (Delhi) (para 9), *Asstt. DIT (Int. Tax.)* v. *Locuz Enterprise Solutions Ltd.* [2015] 61 taxmann.com 47/154 ITD 808 (Hyd. - Trib.) (para 9), *Infotech Enterprises Ltd.* v. *Addl. CIT* [2014] 41 taxmann.com 364/63 SOT 23 (Hyd. - Trib.) (para 9), *Sonic Biochem Extractions (P.) Ltd.* v. *ITO* [2013] 35 taxmann.com 463/59 SOT 4 (URO) (Mum.) (para 9), *Daimler Chryler AG* v. *DIT* [2012] 28 taxmann.com 413 (Mum. - Trib.) (para 9), *DIT (Int. Tax.)* v. *TII Team Telecom International Ltd.* [2011] 12 taxmann.com 502/47 SOT 76 (URO) (Mum.) (para 9), *Jt. CIT* v. *Intec Billing American Inc.* [IT Appeal No. 3196 (Mum.) of 2007] (para 9), *Channel Guide India Ltd.* v. *Asstt. CIT* [2012] 25 taxmann.com 25/139 ITD 49 (Mum.) (para 9), *Rich Graviss Products (P.) Ltd.* v. *Addl. CIT* [2014] 49 taxmann.com 531/66 SOT 24 (Mum. - Trib.) (para 9), *Rajasree Motors (P.) Ltd.* v. *Asstt. CIT* [2016] 61 taxmann.com 270 (Cochin - Trib.) (para 9), *Dy. CIT* v. *Subhotosh Majumdar* [2016] 65 taxmann.com 42/156 ITD 708 (Kol. - Trib.) (para 9), *Sterling Abrasive Ltd.* v. *Asstt. CIT* [2011] 44 SOT 652/10 taxmann.com 65 (Ahd.) (para 9), *TTK Prestige Ltd.* v. *ACIT* [TS-555-ITAT-2014] (para 9), *DIT* v. *Ericson* [2012] 343 ITR 470/204 Taxman 192/[2011] 16 taxmann.com 371 (Delhi) (para 10), *DIT* v. *Nokia Networks OY* [2013] 358 ITR 259/212 Taxman 68/25 taxmann.com 225 (Delhi) (para 10) and *CIT* v. *Siemens Aktiongesellschaft* [2009] 177 Taxman 81/310 ITR 320 (Bom.) (para 21).

Rajendra Kumar *for the Appellant.* **Sunil M. Lala** *for the Respondent.*

ORDER

Amit Shukla, Judicial Member - The aforesaid appeals have been filed by the revenue as well as by the assessee, against separate impugned orders. Since the major issue involved in all the appeals relates to taxability of sale of software as "Royalty" with similar facts permeating through, therefore, all the appeals were heard together and are being disposed off by way of this consolidated order for the sake of convenience.

2. To understand the facts and its implication thereof on the issue of taxability of sum received from sale of computer software by the assessee in India as "Royalty" or not, we will first take-up revenue's appeal in ITA No.7048/Mum/2010 which has been filed against order dated 30th July, 2010 passed by CIT (Appeals)-10, Mumbai for the quantum of assessment passed under section 143(3) for the assessment year 2006-07. In the grounds of appeal, the revenue has raised following grounds:

> 'On the facts and in the circumstances of the case and in law, the ld. CIT (A) has erred in holding that consideration received on sale of computer software programme i.e. C D Rom as business income instead of "Royalty Income" treated by the AO after detailed reasoning'.

3. The facts in brief as culled from the impugned order of CIT (A) are that, assessee-company is a non-resident company registered under the laws of Netherlands. It is engaged in the business of development and sale of computer software and provides other services in relation to its software product. The assessee in India had entered into a 'Distribution Agreement' with INFOR Global Solutions India Pvt. Ltd. (herein after referred to as INFOR India), which is an Indian subsidiary company for supply of its software to Indian customer on which it receives a fix percentage sum as per the agreement. INFOR India is an independent distributor of computer software which sells under the brand name of "INFOR" and is sold as "off the shelf" software in the market used by the customers in various businesses, like in connection with financial accounting, inventory management, HR management etc. The customer in India places an order with INFOR India which in turn passes on the order to the assessee for the purchase of the software. The assessee then has the exclusive right to accept or reject the order. However, once the order is accepted by the assessee, the CD containing the software is sent to India and in turn INFOR India distributes the CD to the customer in India. The assessee also delivers the license-key for the software directly to the customer and the customers pay the consideration for the sale of software to INFOR India, which in turn after retaining the distributor's margin remits the balance amount to the assessee. Assessee also carries out through INFOR India "other general services" related to software. During the year, the assessee had received a sum of Rs.3,75,25,291/- as sales consideration for the computer software products supplied by it to IFOR India and sum of Rs.4,79,36,944/- as "other general services" (OGS fees) from the said Indian subsidiary. Since the assessee does not have a permanent establishment (PE) in India, therefore, only the amount of Rs.4,79,36,944/- received as 'OGS fee' was offered for tax in India as 'fees for technical services', however, so far as the income from sale of software products of Rs.3,75,25,291/- is concerned same was treated as business profit. Hence, this amount was not shown chargeable to tax in India in absence of any PE in India. In response to the show cause notice by the AO, as to why the said amount received from sale of computer software should not be taxed in India as "royalty", the assessee submitted that, the receipts from the sale consideration of computer software cannot be treated as 'royalty' both under the 'Income-tax Act' as well as under the 'Tax Treaty' between India and Netherland. In support, various decisions were relied upon, which for sake of ready reference are reproduced hereunder:—

S. No.	Case Law	Citation
1	*Tata Consultancy Services* v. *State of A.P.*	[2004] 271 ITR 401/141 Taxman 132 (SC)
2	*Samsung Electronics Co. Ltd.* v. *ITO*	[2005] 94 ITD 91 (Bang.)
3	*Hewlett Packard (India) (P.) Ltd.* v. *ITO (International Taxation)*	[2006] 5 SOT 660 (Bang.)
4	*Sonata Information Technology Ltd.* v. *Dy. CIT*	[2006] 7 SOT 465 (Bom.)
5	*Sonata Information Technology Ltd.* v. *Addl. CIT*	[2006] 103 ITD 324 (Bang.)
6	*ACC Ltd.* v. *CC*	[2001] 128 ELT 21 (SC)

7	*IMP Power Ltd.* v. *ITO*	[2006] 9 SOT 156 (Bom.)

4. The Ld. AO examined the legal aspect in detail and ultimately held that, the payment received by the assessee for sale of software is nothing but "royalty" not only under the Income Tax Act but also within the meaning of India-Netherland DTAA and accordingly, assessed receipts @ 15% being tax rate applicable to the 'royalty income' as per Article 12 of DTAA. However, before coming to this conclusion, he has passed a very detailed order dealing with the various legal aspects like, the meaning of software as defined in Explanation 3 to section 9(1)(vi); *explanation* to section 80HHE; guide lines under OECD Commentary; etc. He also dealt, whether the sale of software can be treated as sale of goods or not and for this proposition he also distinguished the decision of Supreme Court in the case of *Tata Consultancy Services* (*supra*) as relied upon by the assessee and also interpreted the concept of 'royalty' based on certain decisions. He also took note of definition and scope of royalty and its taxation within section 9(1)(vi) in great detail after explaining and interpreting the various terms and phrases used in section like "process", "similar property", "patent", "design", "trademark" etc. He also took note of various commentaries and meaning of royalty in various copyright acts. After referring to all such concepts used in section 9(1)(vi) and commentaries, which are running from pages 2 to 19 of the assessment order, he concluded that, not only the said payment falls within the ambit of "royalty" under the Domestic Law but also under the India-Dutch Treaty.

5. However, in the entire assessment order, AO has not uttered a whisper either about the facts of the present case or terms and clauses used in the agreement, scope of work and functions defined between the assessee and the distributor INFOR. Whether under the terms of the said agreement, there was any transfer of any copyright, knowhow, patent, process, etc or not or whether it is purely towards a copyrighted software product only has not been discussed. Further, he has not examined whether the customers have the right to use the copyright embedded in the software or it was a sale of copyrighted article. These was very crucial facts and key factors which AO should have analyzed before coming to his conclusion rather than taking pain in explaining the theory and the concepts on various aspects of definition of "royalty" under the Act, commentaries and judgments. He has not examined the scope and definition of "royalty" under the DTAA and how on facts it is applicable in the case of assessee, when treaty benefit has been invoked. Thus the entire order of the AO is quite general *sans* any specific finding given on the material facts placed before him.

6. In the First appeal, the assessee has specifically stated that, it is involved purely in sale of "Off the Shelf Software" to INFOR. It has a distribution agreement with INFOR which carried out all the marketing and sale of the software. Under the agreement, there is no transfer of any copyright or any right to use of any copyright, knowhow has been given to the customers or INFOR. None of the conditions or terms falls within the definition and scope of 'royalty' in Explanation 2 to section 9(1)(vi). The payment made by the Indian customer to the assessee is towards copyrighted software product as against the payment of or any copyright itself as contemplated in the definition of 'royalty' under the Act. The customer does not have a right to use the copyright embedded in the software. In other words, Indian customer is not permitted to make copies and sell the software except for limited right to access the copyrighted software for his own business purpose and not to acquire any right to exploit the copyright in the said software. The term "use of copyright" enforces or encompasses the exploitation of a right embedded in the copyright and here in this case merely a user right has been given in a limited manner and consideration paid for such limited right cannot be reckoned as *use of right to use a copyright.* Thus, in terms of Article 12(4) also, the said payment does not fall within the scope of royalty. Further, the assessee referred to the definition of term of copyright given in the Copyright Act, 1957 and drew specific attention to section 14 to contend that under the definition of Copyright Act also there cannot be any right to use copyright. Besides this, the assessee relied upon following decisions:

S. No.	*Case Law*	*Citation*
1	*Dy. DIT* v. *Alcatel USA International Marketing Inc.*	2009 taxmann.com 1014 (Mum. - Trib.)
2	*Infrasoft Ltd.* v. *Asstt. CIT*	[2009] 28 SOT 179 (Delhi)
3	*Samsung Electronics Co Ltd.*	(*supra*)
4	*Lucent Technologies Hindustan Ltd.* v. *ITO*	[2005] 92 ITD 366 (Bang.)
5	*Hewlett Packard (India) (P.) Ltd.* v. *ITO*	[2006] 5 SOT 660 (Bang.)

6	*Sonata Information Technology Ltd.* v. *Addl. CIT*	[2006] 103 ITD 324 (Bang.)
7	*Motorola Inc.* v. *Dy. CIT*	[2005] 95 ITD 269 (Delhi) (SB)
8	*Mphasis BFL* v. *ITO*	[2006] 9 SOT 756 (Bang.)

7. The Ld. CIT (A) after considering the facts and various contentions raised by the assessee and also analyzing the various decisions referred, held that the payment received by the assessee emanated only from sale of a copy righted article and therefore, it does not amount to "royalty" within the meaning of Article 12(4) of the India-Netherland DTAA. His relevant observations are reproduced hereunder:—

> '1.3.8 I have considered the arguments of the AR and I have also examined the facts. The appellant had entered in to distribution agreement with its infor India its Indian subsidiary company for supply of its software to Indian customer on which it has to receive a fixed percentage sum as per agreement. The appellant had entered into an agreement with Infor India for sale and distribution of computer software. The examination of the agreement for the computer software reveals that the software provided to the Indian customer through Infor India is for mere use of the customer in India. The appellant does not have the right to use the copyright embedded in the software. The customer's are not permitted to make copies and sell the software. Except for the limited right to access the copyrighted software for its own business purpose, the customer does not acquire any right to exploit the copyright in the software. Whereas use of copyright encompasses explanation of the right embedded in a copyright, a mere user right is a limited right and consideration paid for such user rights cannot be regarded as consideration for use or right to use a copyright. Therefore, payment/consideration received for sale of software by appellant is for allowing mere use of copy righted article cannot be held as payment for royalty.
>
> ** ** **
>
> He also analyzed the definition and scope of royalty under Article 12(4) of DTAA, which reads as under:-
>
> Payment of any kind received as consideration for the use of or right to use any copyright of a literary, artistic, or scientific work including cinematographic films, any patent, Trade mark, design or model, plan secret formula or process or for information concerning industrial, commercial or scientif ic experience"
>
> And held that:-
>
> 1.4.6 In view of above, it can clearly be seen that the definition of royalty in Article -12 of the DTAA is more restrictive than what is provided in Section 9(1)(vi) of the Act.
>
> 1.4.7 The appellant is a tax resident of Netherlands and therefore is entitled to the benefit of the India - Netherlands DTAA over the provisions of the Income-tax Act. The definition of royalty in Article 12(4) of the India-Netherlands DTAA states that any "payment of any kind received as consideration for the use of or right to use, any copyright of a literary, artistic, or scientific work including cinematographic films, any patent, Trade Mark, design or model, plant secret formula or process or for information concerning industrial, commercial or scientific experience" would qualify as royalty.
>
> 1.4.8 Definition of copyright is not provided in the India - Netherlands DTAA and therefore definition of copyright provided in the Copyright Act, 1957 is an exhaustive definition since the words used are copyright means. Copyright is a bundle of rights mentioned in section 14 of Copyright Act. This right consists of the work in public, making translation, adaptation, etc. in respect of computer programme relevant for the issue under consideration, copyright mainly consists of following rights
>
> (*a*) to reproduce the work in any material form
>
> (*b*) to issue copies of the work to the public
>
> (*c*) to sell or give on commercial rental or offer for sale or for commercial rental any copy of computer programme.

1.4.9 Examination of the agreement of the appellant with infor India reveals that the agreement forbids the appellant from transferring or modifying the software. The agreement also forbids them from decompiling, reverse engineering or disassembling the software. The agreement also provides that the end user shall use the software only for the operation and shall not sublicense or modify the software. The perusal of the agreement clearly reveals that the appellant has got no right as envisaged in section 14 of the Copyright Act to duplicate the software, to issue copies of software in public or to reverse engineer, de compile or modify the software. Thus, the current transaction under consideration cannot be considered as the transfer of the copyright either in part or in whole. Thus, consideration record by the appellant for sale and distribution of software computer software is not for the use of copyright or transfer of right to use of copyright. As mentioned above, copyright is different from the work in respect of which copyright subsists, the appellant has only got a copy of software without any part of the copyright of the software. Thus, payment received by the appellant for usage of software does not amount to royalty within the definition of Article 12(4) of the DTAA.

1.4.10 Similar issue of whether the supply of a copy of software programme without transfer of any part of copyright amounts to royalty or not has been considered by various Courts.

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1.4.20 It is therefore very apparent from several decisions of Hon'ble ITAT that in the case of sale of copyrighted article, a copy of computer programme, payment received is not royalty if there is no transfer of copyright partly or wholly. Hence, for reasons stated as above and on the basis of the various decisions cited above, it is held that the Indian customer have acquired only a copy of software and did not acquire any copyright over such software as envisaged by section 14 of the Copyright Act. Under these circumstances, payment/consideration received by the appellant cannot be said to be payment for the use of or right to use of copyright. Thus, payment received amounted only for sale of copyrighted article and does not amount to royalty within the meaning of Article 12(4) of the India-Netherlands DTAA. Accordingly, it is held that the AO has not justified in holding the payment/consideration received by the appellant in the nature of royalty. The payments under consideration are therefore in the nature of business income of the appellant. Since the appellant has no PE in India the consideration received by it is not taxable in India. In the light of these facts the addition of Rs.3,75,25,291/- made by the AO is therefore deleted."

Thus, he held that the consideration received by the assessee on sale of computer software in India cannot be taxed as "royalty".'

8. Before us, the Ld. DR relying upon the order of the AO submitted that, exactly on the same issue, Hon'ble Karnataka High Court in the case of *CIT* v. *Samsung Electronics Co. Ltd.* [2012] 345 ITR 494/[2011] 203 Taxman 477/16 taxmann.com 141 had decided this issue in favour of the Department by holding that, payment to a foreign software suppliers for procurement of 'shrink wrap software' amounts to payment of 'royalty' not only within the Article 12(3) of Indo-US DTAA but also in terms of section 9(1)(vi). Similar view was taken by the same High Court in the case of *CIT* v. *Synopsis International Old Ltd.* [2013] 212 Taxman 454/28 taxmann.com 162 (Kar.). The co-ordinate Bench of Mumbai Tribunal in the case of *Dy. DIT* v. *Reliance Info Com Ltd.* [2014] 64 SOT 137/[2013] 39 taxmann.com 140 (Mum. - Trib.) has also relied upon principle laid down by the Hon'ble Karnataka High Court in deciding the issue against the assessee. He further submitted that now in wake of new *Explanation* 4 in section 9(1)(vi) brought by Finance Act 2012 w.r.e.f. 1.06.1976, the scope and definition of "royalty" has been enlarged to include any kind of software. This definition is to be read into Treaty also, as the definition given in domestic law is to be read into.

9. On the other hand, Ld. Counsel, Shri Sunil M Lala after explaining the facts emanating from the order of the CIT (A), submitted that it is a case of a payment made by a distributor to a foreign company for supply of software to Indian customers. These are "off the shelf" sale of software, which are sold to Indian customers as copyrighted software product. No copyright or license in any form is given either to the distributor or to the Indian customer. The facts which have been noted by the CIT (A) have not been controverted either by the AO or by the Department at any stage. The assessee, being a tax resident of Netherland, is governed by Indo-Dutch DTAA and accordingly, the definition of royalty in Article 12(4) shall apply. After referring to the definition of "Royalty" as given in para 4 of Article 12, he submitted that the main criteria for examining the concept of 'royalty' under the article is that, it should be for 'use of' or 'right to use' any copyright etc. For the definition of copyright, section 14 of copyright of 1957 which is an exhaustive definition has to be looked into. The Ld. CIT (A) has examined this aspect in detail and has held that, in the present terms of the agreement, it is not the right to use of any copyright but only a sale of copyrighted article. Regarding reliance placed by the Ld. DR on Karnataka High Court decisions in *Synopsis International Old Ltd.* (*supra*) and *Samsung Electronics Co. Ltd.* (*supra*), he submitted that, Hon'ble Delhi High Court on several occasion had a chance to dealt with these decisions of the Hon'ble Karnataka High Court and their lordships have not only distinguished the same, but have not followed the ratio after detailed reasoning. He also filed a separate compilation of various Delhi High Court and ITAT decisions and submitted that the payments made to acquire software products either independently or embedded in a hardware or any product or sale of any copyrighted article, the consideration received would have to be treated as payment for purchase of the product rather than consideration for the use of the patented or copyright itself and, therefore, cannot be considered as royalty. The lists of the decisions filed are as under:—

S. No.	*Name*	*Citation*
1	*Pr. CIT* v. *M. Tech India (P.) Ltd.* (Delhi High Court)	[2016] 381 ITR 31/238 Taxman 178/67 taxmann.com 245 (Delhi)
2	*CIT* v. *Dynamic Vertical Software India (P.) Ltd.*	[2011] 332 ITR 222/201 Taxman 78/12 taxmann.com 431 (Delhi)
3	*Tata Consultancy Services*	(*supra*)
4	*DIT* v. *Infrasoft Ltd.*	[2013] 39 taxmann.com 88/[2014] 220 Taxman 273 (Delhi)
5	*CIT* v. *Alacatel Lucent*	[2015] 372 ITR 476/231 Taxman 87/56 taxmann.com 413 (Delhi)
6	*DIT* v. *Ericsson AB*	[2011] 16 taxmann.com 37/[2012] 204 Taxman 192/343 ITR 470 (Delhi)
7	*Asstt. DIT (Int. Taxn)* v. *Locuz Enterprise Solutions Ltd.*	[2015] 61 taxmann.com 47/154 ITD 808 (Hyd. - Trib.)
8	*Infotech Enterprises Ltd.* v. *Addl. CIT*	[2014] 41 taxmann.com 364/63 SOT 23 (Hyd. - Trib.)
9	*Sonic Biochem Extractions (P.) Ltd.* v. *ITO*	[2013] 35 taxmann.com 463/59 SOT 4 (Mum. - Trib.)
10	*Daimler Chryler AG* v. *DIT*	[2012] 28 taxmann.com 413 (Mum. - Trib.)
11	*Addl. DIT (Int. Tax)* v. *TII Team Telecom International Ltd.*	[2011] 12 taxmann.com 502/47 SOT 76 (Mum.) (URO)
12	*Jt. CIT* v. *Intec Billing American Inc.*	[IT Appeal No. 3196 (Mum.) of 2007]

Referring and relying upon these decisions, he submitted that, the Hon'ble Delhi High Court in the case of *M. Tech India (P.) Ltd.* (*supra*) has dealt with the decisions of Karnataka High Court in the case of *Samsung Electronics Co. Ltd.* (*supra*) and clearly expressed that it is not in agreement with the decision of Karnataka High Court. Not only once, but in the case of *Infrasoft Ltd.* (*supra*) and *Alacatel Lucent* (*supra*) the Hon'ble High Court has given a similar observation. In other decisions also the Hon'ble Courts have echoed the same view that payment for license to use copyrighted software which are sold 'off the shelf' or the software which are embedded in the hardware cannot be regarded as payment by way of 'royalty'. Lastly, ld. counsel submitted that it could not be held there was any liability to deduct tax at source on account of retrospective amendment brought subsequently that is, Explanation 4 to section 9(1)(vi). In support, of this contention he relied upon following cases:—

S. No.	*Name*	*Citation*

1	*Channel Guide India Ltd.* v. *Asstt. CIT*	[2012] 25 taxmann.com 25/139 ITD 49 (Mum.)
2	*Rich Graviss Products (P.) Ltd.* v. *Addl. CIT*	[2014] 49 taxmann.com 531/66 SOT 24 (Mum. - Trib.)
3	*Rajasree Motors (P.) Ltd.* v. *Asstt. CIT*	[2016] 61 taxmann.com 270 (Cochin - Trib.)
4	*Dy. CIT* v. *Subhotosh Majumdar*	[2016] 65 taxmann.com 42/156 ITD 708 (Kol. - Trib.)
5	*Sterling Abrasive Ltd.* v. *Asstt. CIT*	[2011] 44 SOT 652/10 taxmann.com 65 (Ahd.)
6	*TTK Prestige Ltd.* V. *ACIT*	[TS -555-ITAT-2014] (Bang.)

10. We have heard the rival submissions, perused the relevant finding given in the impugned order and also the various decisions, cited before us. The sole issue involved before us is, whether the payment received by the assessee on sale of computer software product is to be treated as income by way of "royalty" or business income. In case, if it is a 'business' income, then admittedly, assessee being a non-resident company with no permanent establishment in India, the same will not be taxable in India and if it is a "royalty", then it has to be taxed at the rate of 15% as provide under the treaty. Thus, the only issue for consideration is, whether the said payment falls within the terms of "royalty" under Article 12(4) of India-Netherland DTAA or under 9(1)(vi) of Income Tax Act. Here again, it is an undisputed fact that, assessee being a tax resident of Netherland has sought benefit under Indo-Netherland DTAA, therefore, the payment received by the assessee from its Indian Subsidiary, INFOR India has to be examined under the treaty provisions. Briefly recapitulating the relevant facts for the purpose of our adjudication emanating from the impugned order is that, Assessee Company is engaged in the business of development and sale of computer software and also provides "other general services" in relation to the software. For both the activities, it has entered into a "distribution agreement" with its Indian subsidiary INFOR India which mainly functions as a distributor of computer software. So far as payments received from "other general services" of Rs.4,79,36,944/-, same has been offered to tax in India as 'fee for technical services' on which there is no dispute. The dispute is with regard to the payment of Rs.3,75,25,291/- received by the assessee company as a sale consideration for the computer products supplied by it. The computer software is sold "off shelf" which is mainly used by the Indian customer in their business for financial accounting, inventory management, HR management etc. INFOR India carries out marketing and sale of the software in India and places order with the assessee. The software supplied is then distributed to the Indian customers through INFOR. The consideration charged by INFOR India is based on terms agreed between the assessee and INFOR India as per the 'distribution agreement'. Under the terms of the agreement, as noted by the CIT (A), there is no transfer of any copyright in the software product. The payment received by the assessee is purely towards a copyrighted software product as against the payment for any copyright itself. The assessee does not give any right to use the copyright embedded in the software. In other words, the Indian Customer (or INFOR India) except for the limited right to access the copyright software for its own business purpose does not acquire any kind of right to exploit the copyright in the computer software. These facts have not been controverted by the department and, therefore, what has been incorporated and stated by the CIT (A) in his order is reckoned as admitted facts.

11. Now, on these facts, we have to decide, whether the payment received by the assessee can be reckoned as "royalty" within the terms of article 12(4) of DTAA. Before that, the relevant paragraph of Article 12 dealing with the definition of "royalty" reads as under:—

> '4. 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, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience'.

From the plain reading of the article it can be inferred that, it refers to payments of any kind received as a consideration for the *use of*, or the *right to use* any *'copyright'* of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience. Thus, in order to tax the payment in question as "royalty", it is *sine qua non* that the said payment must fall within the ambit and scope of Para 4 of Article 12. The main emphasis on the payment constituting 'royalty' in Para 4 are for a consideration for the 'use of' or the 'right to use' any copyright. . . . . . . .The key phrases "for the use" or "the right to use any copyright of"; "any patent. . . . . .; "or process", "or for information. . . . .,"; "or scientific experience", etc., are important parameter for treating a transaction in the nature of "royalty". If the payment doesn't fit within these parameters then it doesn't fall within terms of "royalty" under Article 12(4). The computer software does not fall under most of the term used in the Article barring "use of process" or "use of or right to use of copyrights" Here first of all, the sale of software cannot be held to be covered under the word "use of process", because the assessee has not allowed the end user to use the process by using the software, as the customer does not have any access to the source code. What is available for their use is software product as such and not the process embedded in it. Several processes may be involved in making computer software but what the customer uses is the software product as such and not the process, which are involved into it. What is required to be examined in the impugned case as to whether there is any use or right to use of copyright? The definition of copyright, though has not been explained or defined in the treaty, however, the various Courts have consistently opined that the definition of "*copyright"* as given in the 'Copyright Act, 1957' has to be taken into account for understanding the concept. Section 14 of the said Act defines the 'copyrights' to mean 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 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 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.

(*c*) in the case of an artistic work,-

(*i*) to reproduce the work in any material form including depiction in three dimensions of a two dimensional work or in two dimensions of a three dimensional work;

(*ii*) to communicate the work to the public;

(*iii*) to issue copies of the work to the public not being copies already in circulation;

(*iv*) to include the work in any cinematograph film;

(*v*) to make any adaptation of the work;

(*vi*) to do in relation to an adaptation of the work any of the acts specified in relation to the work in sub-clauses (i) to (iv);

(*d*) In the case of cinematograph film, —

(*i*) to make a copy of the film, including a photograph of any image forming part thereof;

(*ii*) to sell or give on hire, or offer for sale or hire, any copy of the film, regardless of whether such copy has been sold or given on hire on earlier occasions;

(*iii*) to communicate the film to the public;

(*e*) In the case of sound recording, -

(*i*) to make any other sound recording embodying it;

(*ii*) to sell or give on hire, or offer for sale or hire, any copy of the sound recording regardless of whether such copy has been sold or given on hire on earlier occasions;

(*iii*) to communicate the sound recording to the public. Explanation: For the purposes of this section, a copy which has been sold once shall be deemed to be a copy already in circulation'.

Thus, the definition of 'copyright' in section 14 is an exhaustive definition and it refers to bundle of rights. In respect of computer programming, which is relevant for the issue under consideration before us, the copyright mainly consists of rights as given in clause (b), that is, to do any of the act specified in clause (a) from (i) to (vii) as reproduced above. Thus, to fall within the realm and ambit of right to use copyright in the computer software programme, the aforesaid rights must be given and if the said rights are not given then, there is no copyright in the computer programme or software. As noted by the CIT (A), under the terms of the agreement between the assessee and INFOR India, the agreement specifically forbids them from decompiling, reverse engineering or disassembling the software. The agreement also provides that the end user shall use the software only for the operation and shall not sublicense or modify the software. None of the conditions mentioned in section 14 of the Copyright Act are applicable. If the conclusion of Ld, CIT (A) are based on these facts and agreement, then he has righty concluded that the consideration received by the assessee is for pure sale of "shrink wrapped software" off the shelf and hence, cannot be considered as a "royalty" within the meaning of Article 12(4) of the DTAA, as the same is consideration for sale of copyrighted product and not to use of any copyright.

12. One of the issue which was raised by the Ld. DR before us is that, the Explanation 4 to section 9(1)(vi) which has been with brought by Finance Act 2012 with retrospective effect in section 9(1)(vi), therefore, the meaning and definition of 'royalty' as given therein should be read into the DTAA. We are unable to appreciate this contention of the Ld. DR because the retrospective amendment brought into statute with effect from 01.06.1976 cannot be read into the DTAA, because the treaty has not been correspondingly amended in line with new enlarged definition of 'royalty'. The alteration in the provisions of the Act cannot be *per se* read into the treaty unless there is a corresponding negotiation between the two sovereign nations to amend the specific provision of "royalty" in the same line. The limitation clause cannot be read into the treaty for applying the provisions of domestic law like in Article 7 in some of the treaties, where domestic laws are made applicable. Here in this case, the 'royalty' has been specifically defined in the treaty and amendment to the definition of such term under the Act would not have any bearing on the definition of such term in the context of DTAA. A treaty which has entered between the two sovereign nations, then one country cannot unilaterally alter its provision. Thus, we do not find any merit in the contention of the Ld. DR that the amended and enlarged definition should be read into the Treaty.

13. Now, we come to the various decisions relied upon by the parties. Before us, the Ld DR has heavily relied upon the two decisions of Karnataka High Court, one in the case of *Synopsis International Old Ltd.* (*supra*) and other in the case of *Samsung Electronics Co Ltd.* (*supra*). Both these decisions, admittedly, are against the assessee. However, we find that Hon'ble Delhi High Court in series of decisions have specifically disagreed with the ratio and the conclusion of Hon'ble Karnataka High Court. In the case of *Infrosoft Ltd.* (*supra*), the Hon'ble Delhi High Court precisely on similar nature of agreement and the issue before it has dealt and decided the mater in the following manner:—

"87. In order to qualify as royalty payment, it is necessary to establish that there is transfer of all or any rights (including the granting of any licence) in respect of copyright of a literary, artistic or scientific work. In order to treat the consideration paid by the Licensee as royalty, it is to be established that the licensee, by making such payment, obtains all or any of the copyright rights of such literary work. Distinction has to be made between the acquisition of a "copyright right" and a "copyrighted article". Copyright is distinct from the material object, copyrighted. Copyright is an intangible incorporeal right in the nature of a privilege, quite independent of any material substance, such as a manuscript. Just because one has the copyrighted article, it does not follow that one has also the copyright in it. It does not amount to transfer of all or any right including licence in respect of copyright. Copyright or even right to use copyright is distinguishable from sale consideration paid for "copyrighted" article. This sale consideration is for purchase of goods and is not royalty.

88. The license granted by the Assessee is limited to those necessary to enable the licensee to operate the program. The rights transferred are specific to the nature of computer programs. Copying the program onto the computer's hard drive or random access memory or making an archival copy is an essential step in utilizing the program. Therefore, rights in relation to these acts of copying, where they do no more than enable the effective operation of the program by the user, should be disregarded in analyzing the character of the transaction for tax purposes. Payments in these types of transactions would be dealt with as business income in accordance with Article 7.

89. There is a clear distinction between royalty paid on transfer of copyright rights and consideration for transfer of copyrighted articles. Right to use a copyrighted article or product with the owner retaining his copyright is not the same thing as transferring or assigning rights in relation to the copyright. The enjoyment of some or all the rights which the copyright owner has is necessary to invoke the royalty definition. Viewed from this angle, a non-exclusive and non-transferable licence enabling the use of a copyrighted product cannot be construed as an authority to enjoy any or all of the enumerated rights ingrained in Article 12 of DTAA. Where the purpose of the licence or the transaction is only to restrict use of the copyrighted product for internal business purpose, it would not be legally correct to state that the copyright itself or right to use copyright has been transferred to any extent. The parting of intellectual property rights inherent in and attached to the software product in favour of the licensee/customer is what is contemplated by the Treaty. Merely authorizing or enabling a customer to have the benefit of data or instructions contained therein without any further right to deal with them independently does not, amount to transfer of rights in relation to copyright or conferment of the right of using the copyright. The transfer of rights in or over copyright or the conferment of the right of use of copyright implies that the transferee/licensee should acquire rights either in entirety or partially co-extensive with the owner/transferor who divests himself of the rights he possesses pro tanto.

90. The license granted to the licensee permitting him to download the computer programme and storing it in the computer for his own use is only incidental to the facility extended to the licensee to make use of the copyrighted product for his internal business purpose. The said process is necessary to make the programme functional and to have access to it and is qualitatively different from the right contemplated by the said paragraph because it is only integral to the use of copyrighted product. 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.

91. There is no transfer of any right in respect of copyright by the Assessee and it is a case of mere 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 either under the Income Tax Act or under the DTAA.

92. The licensees are not allowed to exploit the computer software commercially, they have acquired under licence agreement, only the copy righted software which by itself is an article and they have not acquired any copyright in the software. In the case of the Assessee company, the licensee to whom the Assessee company has sold/licensed the software were allowed to make only one copy of the software and associated support information for backup purposes with a condition that such copyright shall include Infrasoft copyright and all copies of the software shall be exclusive properties of Infrasoft. Licensee was allowed to use the software only for its own business as specifically identified and was not permitted to loan/rent/sale/sub-licence or transfer the copy of software to any third party without the consent of Infrasoft. 93. The licensee has been prohibited from copying, decompiling, de-assembling, or reverse engineering the software without the written consent of Infrasoft. The licence agreement between the Assessee company and its customers stipulates that all copyrights and intellectual property rights in the software and copies made by the licensee were owned by Infrasoft and only Infrasoft has the power to grant licence rights for use of the software. The licence agreement stipulates that upon termination of the agreement for any reason, the licencee

shall return the software including supporting information and licence authorization device to Infrasoft.

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94. The incorporeal right to the software i.e. copyright remains with the owner and the same was not transferred by the Assessee. The right to use a copyright in a programme is totally different from the right to use a programme embedded in a cassette or a CD which may be a software and the payment made for the same cannot be said to be received as consideration for the use of or right to use of any copyright to bring it within the definition of royalty as given in the DTAA. What the licensee has acquired is only a copy of the copyright article whereas the copyright remains with the owner and the Licensees have acquired a computer programme for being used in their business and no right is granted to them to utilize the copyright of a computer programme and thus the payment for the same is not in the nature of royalty.

95. We have not examined the effect of the subsequent amendment to section 9 (1)(vi) of the Act and also whether the amount received for use of software would be royalty in terms thereof for the reason that the Assessee is covered by the DTAA, the provisions of which are more beneficial.

96. The amount received by the Assessee under the licence agreement for allowing the use of the software is not royalty under the DTAA.

97. What is transferred is neither the copyright in the software nor the use of the copyright in the software, but what is transferred is the right to use the copyrighted material or article which is clearly distinct from the rights in a copyright. The right that is transferred is not a right to use the copyright but is only limited to the right to use the copyrighted material and the same does not give rise to any royalty income and would be business income.

98. We are not in agreement with the decision of the Andhra Pradesh High Court in the case of *Samsung Electronics Co. Ltd.* (*supra*) that right to make a copy of the software and storing the same in the hard disk of the designated computer and taking backup copy would amount to copyright work under section 14(1) of the Copyright Act and the payment made for the grant of the licence for the said purpose would constitute royalty. The license granted to the licensee permitting him to download the computer programme and storing it in the computer for his own use was only incidental to the facility extended to the licensee to make use of the copyrighted product for his internal business purpose. The said process was necessary to make the programme functional and to have access to it and is qualitatively different from the right contemplated by the said provision because it is only integral to the use of copyrighted product. The right to make a backup copy purely as a temporary protection against loss, destruction or damage has been held by the Delhi High Court in *DIT* v. *M/s Nokia Networks OY* (*supra*) as not amounting to acquiring a copyright in the software".

The ratio of the above decision clearly clinches the issue which is applicable in the case of the assessee also. This ratio and principle has been followed and reiterated again in the case of *M. Tech India Pvt Ltd.* (*supra*) and again in the decisions of *Alacatel Lucent* (*supra*), wherein Hon'ble Delhi High Court relying upon its earlier two decisions in the case of *DIT* v. *Erisson* [2012] 343 ITR 470/204 Taxman 192/[2011] 16 taxmann.com 371 (Delhi) and *DIT* v. *Nokia Networks OY* [2013] 358 ITR 259/212 Taxman 68/25 taxmann.com 225 (Delhi) concluded that, when assessee supplies the software which is incorporated on CD, it has applied only a tangible property and payment made for acquiring such a property cannot be regarded as payment by way of royalty. The relevant observation of the High Court in *Alcatel Lucent* (*supra*) in this regard reads as under:

'We have noticed, at the outset, that the ITAT had relied upon the ruling of this Court in Director of Income Tax V. Ericsson A.B. (2012) 343 ITR 470 wherein identical argument with respect to whether consideration paid towards supply of software along with hardware rather software embedded in the hardware amounted to royalty. After noticing several contentions of the revenue, this Court held in *Ericsson A.B.* (*supra*) as follows:

"54. It is difficult to accept the aforesaid submissions in the facts of the present case. We have already held above that the assessee did not have any business connection in India. We have also held that the supply of equipment in question was in the nature of supply of goods. Therefore, this issue is to be examined keeping in view these findings. Moreover, another finding of fact is recorded by the

Tribunal that the Cellular Operator did not acquire any of the copyrights referred to in Section 14 (b) of the Copyright Act, 1957.

55. Once we proceed on the basis of aforesaid factual findings, it is difficult to hold that payment made to the assessee was in the nature of royalty either under the Income-Tax Act or under the DTAA. We have to keep in mind what was sold by the assessee to the Indian customers was a GSM which consisted both of the hardware as well as the software, therefore, the Tribunal is right in holding that it was not permissible for the Revenue to assess the same under two different articles. The software that was loaded on the hardware did not have any independent existence. The software supply is an integral part of the GSM mobile telephone system and is used by the cellular operator for providing the cellular services to its customers. There could not be any independent use of such software. The software is embodied in the system and the revenue accepts that it could not be used independently. This software merely facilitates the functioning of the equipment and is an integral part thereof. On these facts, it would be useful to refer to the judgment of the Supreme Court in *TATA Consultancy Services* v. *State of Andhra Pradesh* (2004) 271 ITR 401 (SC), wherein the Apex Court held that software which is incorporated on a media would be goods and, therefore, liable to sales tax. Following discussion in this behalf is required to be noted:-"In our view, the term "goods" as used in Article 366(12) of the Constitution of India and as defined under the said Act are very wide and include all types of movable properties, whether those properties be tangible or intangible. We are in complete agreement with the observations made by this Court in *Associated Cement Companies Ltd.* (*supra*). A software programme may consist of various commands which enable the computer to perform a designated task. The copyright in that programme may remain with the originator of the programme. But the moment copies are made and marketed, it becomes goods, which are susceptible to sales tax. Even intellectual property, once it is put on to a media, whether it be in the form of books or canvas (In case of painting) or computer discs or cassettes, and marketed would become "goods". We see no difference between a sale of a software programme on a CD/floppy disc from a sale of music on a cassette/CD or a sale of a film on a video cassette/CD. In all such cases, the intellectual property has been incorporated on a media for purposes of transfer. TAXPUNDIT.ORG Sale is not just of the media which by itself has very little value. The software and the media cannot be split up. What the buyer purchases and pays for is not the disc or the CD. As in the case of paintings or books or music or films the buyer is purchasing the intellectual property and not the media i.e. the paper or cassette or disc or CD. Thus a transaction sale of computer software is clearly a sale of "goods" within the meaning of the term as defined in the said Act. The term "all materials, articles and commodities" includes both tangible and intangible/incorporeal property which is capable of abstraction, consumption and use and which can be transmitted, transferred, delivered, stored, possessed etc. The software programmes have all these attributes. . . . .

In *Advent Systems Ltd.* v. *Unisys Corpn,* (925 F. 2d 670 (3rd Cir. 1991)), relied on by Mr. Sorabjee, the court was concerned with interpretation of uniform civil code which "applied to transactions in goods". The goods therein were defined as "all things (including specially manufactured goods) which are moveable at the time of the identification for sale". It was held:

"Computer programs are the product of an intellectual process, but once implanted in a medium are widely distributed to computer owners. An analogy can be drawn to a compact disc recording of an orchestral rendition. The music is produced by the artistry of musicians and in itself is not a "good," but when transferred to a laser-readable disc becomes a readily merchantable commodity. Similarly, when a professor delivers a lecture, it is not a good, but, when transcribed as a book, it becomes a good. That a computer program may be copyrightable as intellectual property does not alter the fact that once in the form of a floppy disc or other medium, the program is tangible, moveable and available in the marketplace. The fact that some programs may be tailored for specific purposes need not alter their status as "goods" because the Code definition includes "specially manufactured goods."
56. A fortiorari when the assessee supplies the software which is incorporated on a CD, it has supplied tangible property and the payment made by the cellular operator for acquiring such property cannot be regarded as a payment by way of royalty."

6. This Court also noticed that the ITAT had in addition relied upon other judgment of this Court i.e. *Director of Income Tax* v. *M/s. Nokia Networks,* (2013) 358 ITR 259 (Delhi)'.

Similar view has been reiterated in other decisions also as relied upon by the Ld. Counsel. Now that there are catena of decisions and case laws in favour of the assessee including that of the Delhi High Court on several occasions, we are inclined to follow the decision and proposition laid down by the Hon'ble Delhi High Court. Thus, in view of the finding given above, we uphold the order of the CIT (A) that the payment received by the assessee for sums amounting to Rs. 3,75,25,291/- does not amount to "royalty" within the meaning of Article 12(4) of Indo-Netherland DTAA and accordingly, the same is not taxable in India. Since, admittedly, the assessee has no PE in India; therefore, same cannot be taxed as business income under Article 7. Accordingly, ground raised by the revenue stands dismissed.

14. Now, we shall take ITA No.3049/Mum/2011; The aforesaid appeal is arising against the impugned order dated 25.02.2011 passed by CIT (A)-11, Mumbai in relation to the order passed under section 201/201(1A) in the grounds of appeal the assessee has raised following ground:

> 'On the facts and circumstances of the case and in law, the ld. CIT (Appeals) erred in holding that consideration received on sale of computer software programme i.e. C.D. Rom is not a "Royalty Income" as per the Article 12(4) of DTAA between India and Netherlands ignoring the facts of the case and detailed reasoning given by AO'.

15. As admitted by both the parties, issue involved in this appeal is exactly the same. Accordingly, our finding given in the aforesaid appeal will apply *mutatis mutandis* in this appeal also and accordingly, the ground raised by the revenue is treated as dismissed.

16. Now, we shall take up assessee's appeal in ITA No.776/Mum/2013 for the AY 2006-07 arising out of Final Assessment order dated, 11.10.2012 passed under section 144C(5) r.w.s. 148 in pursuance of the direction given by the DRP-I, Mumbai under section 144C(5).

17. At the outset, it is noted that appeal filed by the assessee is barred by limitation by 33 days. In the application for condonation of delay, the assessee has stated following reasons:—

- "The Company is a foreign Company based out of the Netherlands with no operations and presence in India;
- On receipt of the final assessment order, the Company took time to understand the order and to discuss internally the same, which led to the delay in preparation of the appeal documents;
- Since the Company is a foreign company and none of its directors are based in India, the appeal documents had to be sent outside India for signatures. Further, the directors of the Company were travelling on business exigency and therefore, their signatures could not be obtained in due time;
- The fact that the courier had to be dispatched from outside India further added to the delay in receipt of the signed appeal documents in India;
- In view of the above, the Company would like to submit that given the above mentioned situations, the Company, inspite of its best efforts could not obtain the necessary signatures on the appeal documents before the due date for filling the subject appeals".

18. After hearing both the parties and on perusal of the reasons stated in the petition, we find that, there was a reasonable cause for not filing the appeal in time and delay is not on account of any latches on the part of the assessee. Accordingly, we condone the delay.

In the grounds of appeal the assessee has raised the following grounds:—

"1. The order passed by the Learned Deputy Director of Income Tax (International Taxation)-3(1) (AO) and the Hon'ble Dispute Resolution Panel ('DRP') is in gross violation of the principles of natural justice. The order does not take reference of facts and legal principles and is therefore liable to be quashed as bad in law.

2. The Ld. AO and the DRP erred in treating the income from the sale of software products at an income taxable in India. The Ld. AO and the Hon'ble DRP erred in treating the same as in the nature of royalty as per the provisions of the Income Tax Act, 1961 (the 'Act') as well as the Double Taxation Avoidance Agreement between India and Netherlands ('DTAA').

3. The Ld. AO and the Hon'ble DRP failed to appreciate the Appellant's arguments and submissions explaining that the software products sold by the Appellant are goods.

4. The Hon'ble DRP erred in holding that the licensee obtains a "right to make a copy of the software of the equipment in the object code form", without appreciating the fact that the Appellant does not have a right to create copies of the licensed software as specifically stated in the Agreement.
5. The Hon'ble DRP erred in holding that the Appellant had exercised the right which amounts to exercise of a copyright provided under the Copyright Act, without appreciating the fact that the Appellant doesn't have the right to access or copy the unique license key that is required to make the software functional/operative.
6. The Ld. AO and the Hon'ble DRP erred in law in treating the software as a secret process and a property similar to patent, invention, design, secret formula, thereby treating the sale of software products as transfer of rights in the software.
7. The Ld. AO and the Hon'ble DRP has erred in treating the sale of the software products which is a copyrighted article as 'use or right to use of a copyright'.
8. The Ld. AO and the DRP further erred in law in passing the order based on the above contention without considering the various judicial precedents cited by the Appellant in its written submissions and during the course of the hearing, including the binding precedent of the Hon'ble ITAT, Mumbai.
9. The Ld. AO and the Hon'ble DRP has erred in passing the order without considering the order passed by the Commissioner of Income Tax (Appeals) ['CIT (A)'] in Appellant's own case for the FY 2005-06 wherein the CIT (A) held that the consideration received by the Appellant on account of sale of software products is not in the nature of royalty. The Ld. AO and the DRP failed to appreciate the explanations provided by the Appellant that the facts in the subject year are not different from the facts in the FY 2005-06 and hence the decision of CIT (A) in Appellant's case for FY 2005-06 should be applicable to it in the subject year.
10. The Ld. AO and the Hon'ble DRP further erred in passing the order without considering the order passed by the learned CIT (A) in the case of its Indian subsidiary company, *Infor Global Solutions (India) Pvt. Ltd.* ('Infor India') for FY 2006-07 wherein the ld. CIT (A) held that the payment made by Infor India to the Appellant for software products is not in the nature of royalty.
11. The Ld. AO and the Hon'ble DRP followed a pre-decided and biased approach to treat the transaction of sale of software products by the Appellant as royalty, thereby causing the Appellant undue hardship on a matter already decided in the Appellant's own case.
12. The Ld. AO and the Hon'ble DRP did not take reference of facts and legal principles and were purely based on conjectures and surmises and therefore the orders are liable to be quashed as bad in law.
13. The Hon'ble DRP erred in making a reference to Explanation 4 to section 9(1)(vi) of the Act for the purpose of determining the meaning of the term 'royalty' without appreciating that a specific definition of the term as concluded by the Hon'ble DRP.
14. The Ld. AO erred in passing the order without considering the tax deducted at source on the income of the Appellant, and ignored the submissions made by the Appellant stating this fact".

19. From the perusal of the above grounds, it is quite evident that, in this case also the sole issue revolves around taxability of "Royalty" under the DTAA read with section 9(1)(vi) except for the fact that, now the assessee's name has been changed to "INFOR Global Solutions (Barneveld) BV'. In this case the disputed amount for taxability of "royalty" payment is Rs.4,65,46,164/- received towards sale consideration for computer software products supplied by the assessee to its Indian subsidiary. The said sale consideration of CD Rom has been treated as 'royalty' by the AO by and large on the same footing and reasoning as has been discussed in the appeal herein above and accordingly the same has been taxed under the DTAA. As admitted by the parties the facts remain *pari materia.*

20. However in this year Ld. DRP has raised certain additional points, in this appeal which reads as under:-

'The assessee's submission has been considered. As regards the royalty under the domestic law the provisions of section 9(1)(vi) have been amended by the Finance Act, 2012 and explanation 4 has been Inserted therein. The said explanation specifically provides that use of computer software would amount to royalty. As regards application of the DTAA it is relevant to refer to pare 2 of article 3 Indian Netherland DTAA, The said article provides that for interpreting any provision of the convention, when any term is not defined therein, the term shall have same meaning that it carries under the domestic law of the stale applying the convention, concerning the taxes to which the convention applies. Thus, unless the context otherwise requires, for interpreting the DTAA, reference to domestic law is mandated by article 3(2) of the said treaty. Though the term royally has been defined in article 12 para 4 as the consideration for "the use of or the right to use any copyright of literary artistic or scientific work, the terms use of or right to use any copyright' has not been defined in the DTAA. Further, the term "copyright" under the DTAA has to be considered in the context of copyright laws prevailing in the contracting state administering the tax. thus, in order to interpret the term of use of or the right to use one can refer to the explanation 4 to section 9(1)(vi) of the Act. The term any "right, property or Information in the explanation refers to the various kinds intangible property refereed in pare 4 of article 12 including copyright, Hence, even under the provision DTAA, consideration for the use computer software amounts to use of royalty."

6. "While these are legal arguments, it is also necessary to refer to the actual software agreement entered into by the assessee. A reference to the agreement shows that the computer software in this case was not sold as an article on a disk or any other such medium. Clause (e) of para 1 of the licence agreement shows that the software can be downloaded with the process code. Hence the arguments based on the reasoning that it is a sale of copy righted article is not correct in the facts of this case.

7. It is also observed that, Clause (e) to pare 3 of the licence agreement provides for provision of the source code and grants right to make changes. This shows clearly that the case Is not merely of use of software but in fact provides for sharing the source code which could fall within the terms knowhow, secret formula or process.

8. It is also seen that the licensee under para 3 of the licence agreement has right to make a copy of the software of the equipment in the object code form. This itself is adequate to conclude that the assessee has exercised the right which is provided under the Copyright Act as the exercise of a copyright. Under the provision of Indian copyright act making of a copy of a computer software programme will amount to infringement of copyright unless said right is granted by the copyright holder to the user. For all (he above reasons, the facts of this case shows that this is not the case of a sale of copyrighted article but a case of use of computer software resulting in exercising of copyright. For all the above reasons, the action of the AO to tax the same as royalty is upheld.'

21. After considering the direction of the DRP and also the order of the AO, we find that the issue involved herein is exactly same as has been decided in ITA No.7048/Mum/2010, except that the Ld. DRP has decided the issue against the assessee, by taking additional reasoning that now in wake of new *Explanation 4* to section 9(1)(vi) that has the enlarged the definition of "royalty" should be read into DTAA by virtue of Article 3(2). On this aspect we have already dealt with and have given our reasons that, the amendment carried out in the domestic law with retrospective effect will not automatically alter the provisions of DTAA. Article 3(2) of DTAA provides that, *as regards the application of the Convention by one of the States any term not defined herein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which the Convention applies*. This envisages that, if a particular term has not been defined in the treaty but the same has been defined in the domestic law, then the definition given in the domestic law will be considered for analyzing the transaction under the treaty. However, if a particular term has been specifically defined in the treaty, then any reference to the domestic law or any amendment carried out in the definition of such term under such law will have no bearing on the definition of such term in the context of the convention, unless DTAA is also correspondingly amended by the parties. We have already observed above that, one contracting state which is a party to a treaty cannot unilaterally alter its provision and enlarge the scope of any term from the prism of its domestic law. If there is no amendment in the treaty and if any amendment is carried out under the domestic law then same cannot be read into the treaty. This proposition now stands well settled by umpteen number of judgments including that of jurisdictional High Court in the case of *CIT* v. *Siemens Aktiongesellschaft* [2009] 177 Taxman 81/310 ITR 320 (Bom.). Thus, we are unable to accept the finding and direction of the DRP that in absence of any amendment in the provisions of the treaty the amended act should read into by virtue of Article 3(2).

21.1 Regarding other observations of the DRP, like sharing of the source code amounts to process, we have already dealt this issue in our earlier part of this order. Moreover, 'source code' refers to computer programmes written in higher level programming languages and readable by humans. Before us, Mr. Sunil M Lala has given a specimen of 'software license agreement' between the assessee and Indian subsidiary wherein under the term "license", following conditions have been stipulated:—

> 'License. Subject to the terms and conditions of this Agreement and the applicable Order Form (including, without limitation, with respect to termination), Infor grants Licensee a perpetual (unless otherwise specified on the Order Form), non-exclusive, non-transferable license (without the right to sublease or sublicense) to use the Component Systems (including any updates, enhancements or modifications to such Component Systems that Infor provides under the Support Agreement) on the Equipment for Licensee's own, internal computing operations. The computer readable media containing the Component Systems may also contain software programs for which Licensee is not granted a license for use. Licensee may not make any use of any such software programs for which Licensee is not expressly obtaining a license for use under this Agreement. Any rights not expressly granted in this Agreement are expressly reserved. Licensee also has the right to use the Component Systems, in Object Code form temporarily on the Equipment, for disaster recovery of Licensee's computer operations (i.e., loaded on a separate, non-production, off-powered server).
>
> "Source Code". Unless otherwise explicitly provided in an Order Form, Licensee has no license to access or use, or any other rights in or to, the Source Code for a particular Component System. If the Order Form grants Licensee a license to use Source Code for a particular Component System, then Licensee has the limited right to use such Source Code to modify such Component System for its own, internal computing operations. Subject to the foregoing, Licensee will not disclose all or any part of the Source Code for a Component System to any person except Licensee Employees who, before obtaining access to the Source Code, have been informed by Licensee in writing of the non-disclosure obligations imposed on both Licensee and such Licensee Employees under this Agreement. Infor will own all right, title and interest to all derivative works of the Component System ("Derivative Works"), even if solely created by Licensee pursuant to a license to use Source Code hereunder. Licensee hereby assigns to Infor absolutely all of its rights, title and interest in and to any Derivative Works created by the Licensee together with all Intellectual Property Rights therein. Subject to the terms and conditions of this Agreement, Infor grants Licensee (if licensed to use Source Code hereunder) a perpetual (unless otherwise specified in the Order Form), non-exclusive, non-transferable license (without the right to sublease or sublicense) to use and copy for use the Derivative Works created by Licensee or created by Infor at Licensee's request and payment, for Licensee's own, internal computing operations. Upon Infor's request, Licensee will provide Infor with a copy (including all documentation related thereto) of all Derivative Works created by Licensee and will execute and deliver to Infor any documents reasonably necessary to vest in Infor all right, title and interest therein'.

22. From the reading of the above terms of license, it is seen that, first of all, a non-exclusive, non-transferable license (without any right to sublease or sublicense) with a very limited right has been given for right to use the component system and there is no covenant to grant any copyright or right to use. Limited right to operate the copyrighted article cannot be reckoned as royalty within the scope of Article 12(4); and *Secondly*, the use source code is also for a particular component system to modify such component system for its own internal computing operations. This right is again is with the riders and limitations given therein. There is no right given for the 'use of copyright' or any kind of copyright has been given. Thus, nothing turns on with this observation as made by the Ld. DRP that source code is some kind of process and accordingly, our finding given hereinabove in the earlier appeal will apply *mutatis mutandis* in this appeal also. Thus, the impugned issue is decided in favour of the assessee and the amount which has been taxed as "royalty" is held to be non-taxable in India in terms of DTAA, resultantly appeal of the assessee is allowed.

23. Now, we will come to assessee's appeal in ITA No.777/Mum/2013 for AY 2008-09. This appeal is again arising out of Final assessment order dated 11.10.2012 passed in pursuance of direction given by the DRP vide order dated 29.09.2012 wherein exactly the similar grounds have been raised. However, before deciding the appeal, we find that like assessee's appeal for AY 2007-08, this appeal is also time barred by

33 days and the reasons given by the assessee are the same as given in appeal for AY 2007-08. Accordingly, in view of our finding given therein, the delay is hereby condoned.

24. At the outset, it has been admitted by the either parties that the grounds and issues are identical which have been dealt and deliberated upon in this order while deciding the in revenue's appeal for AY 2006-07 and also while deciding the assessee's appeal for AY 2007-08, therefore, the same finding will apply *mutatis mutandis* in this appeal also and accordingly, the impugned issue is decided in favour of the assessee and against the revenue.

To sum-up:

Both the appeals of the revenue stands dismissed and that of the assessee stands allowed.

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*In favour of assessee.