Comprehensive Analysis of Taxation of Royalties

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Section 9 of The Income Tax Act, 1961

Section 9(1)(vi): Royalty Income

The following Income shall be deemed to accrue or arise in India:

Income by way of royalty payable by—

(*a*) the Government ; or

(*b*) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(*c*) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Exception in sub-clause(b) of section (1)(vi) - Source of Income outside India

- **Aktiengesellschaft Kuhnle Kopp & Kausch W. Germany v. BHEL (262 ITR 513)(Madras)**

  The High Court stated that exclusion shall be applied in case of export sales and held that as far as export sales is concerned, that amount is also exempt u/s 9(1)9(vi) of the Act. Though a resident in india paid the royalty, it cannot be said that it was deemed to have accrued or arisen in India as the royalty was paid out of export sales and hence the source of the royalty is the sales outside India. Since the source of the royalty is from the source situated outside India, the royalty paid on export sales is not taxable

- **CIT v. Havells India Ltd. (352 ITR 376)(Delhi)**

  The High Court held that the real question is whether the export sales proceeds received from goods manufacture and exported from India constitute a source inside or outside India. To decide the same we have to take pragmatic and a practical view and not approach the question from a theoretical perspective. We are making a distinction between the source of the income and the source of receipt of the monies. In order to fall within the second exception provided in section 9(1)(vii)(b) [similar to section 9(1)(vi)(b)] of the Act, the source of the income and not the receipt should be situated outside India.

Exception in sub-clause(b) of section (1)(vi)

- Source of Income outside India:
- **Lufthansa Cargo India Pvt Ltd. V. DCIT (92 TTJ 837) (Delhi-ITAT)**

  The payments for repair of aircrafts abroad which were acquired for operating on international routes only was held to fall under the exclusion clause of 9(1)(vii)(b)[similar to 9(1)(vi)(b)]

- **Titan Industries Ltd. V. ITO (11 SOT 206)(Bangalore-ITAT)**

  The ITAT held that the assessee company which was engaged in manufacture and sale of watches under the patent name 'TITAN' having an associate company incorporated in Singapore for promoting sales of watches in APAC region and got its patent registered in Hong Kong could claim the exception clause u/s 9(1)(vii)(b) for the fees paid to register the patent

Section 9 of The Income Tax Act, 1961

- Section 9(1)(vi): Royalty Income

  Royalty Income shall be deemed to accrue or arise in India if:

PAYER	CONDITIONS
Indian Government	No conditions
Resident in India	All cases, Except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India
Non-Resident in India	Only where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India

Explanation 2 to Section 9(1)(vi)

Royalty means consideration (Including a lump-sum consideration other than consideration chargeable under the head "Capital Gains") for:

(i) The transfer of all or any rights (including the granting of a licence) in respect of a
- patent,
- invention,
- model, design,
- secret formula or
- process or
- trade mark or
- similar property.

(ii) The imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iii) The use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;

Explanation 2 to Section 9(1)(vi)

(iv) The imparting of any information concerning
- technical,
- industrial,
- commercial or scientific
- knowledge, experience or skill ;

(iva) The use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;

(v) The transfer of all or any rights (including the granting of a licence) in respect of any
- copyright,
- literary,
- artistic or
- scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting ,

~~*but not including consideration for the sale, distribution or exhibition of cinematographic films*; or~~

(vi) The rendering of any services in connection with the activities referred to in sub-clauses (*i*) to (*iv*), (*iva*) and (*v*).

Explanation 3 to Section 9(1)(vi)

Computer Software means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data.

Explanation 4 to Section 9(1)(vi)

It is clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.

Explanation 5 to Section 9(1)(vi)

It is clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not—

(*a*) the possession or control of such right, property or information is with the payer;

(*b*) such right, property or information is used directly by the payer;

(*c*) the location of such right, property or information is in India.

Explanation 6 to Section 9(1)(vi)

It is clarified that the expression "process" includes and shall be deemed to have always included transmission by

- satellite (including up-linking, amplification, conversion for down-linking of any signal),
- cable,
- optic fibre or
- by any other similar technology,

whether or not such process is secret;

Definition of know-how

As per ANBPPI **know-how** is

all the undivulged technical information,

whether capable of being patented or not,

that is necessary for the industrial reproduction of a product or process,

directly and under the same conditions;

inasmuch as it is derived from experience, know-how represents

what a manufacturer cannot know from

mere examination of the product and mere knowledge of the progress of technique.

Referral Fee – Whether Royalty

- A referral fee did not amount to royalty within the meaning of explanation 2 to Section 9(1)(vi) as there was no information imparted regarding commercial knowledge or experience, providing “bald commercial information was not royalty”

“Use” or “Right to Use”

- The expression “use” is not defined in the Act as well as Article 12 of the Model convention and includes leasing, letting or licensing.
- The oxford English reference dictionary defines “use” as meaning “exploit for one’s own ends, employ for some purpose; apply to one’s own purpose; the act so employing, using, or putting into service’.
- A one-time “use” is sufficient to constitute royalties and repetitive “use” is not necessary.
- The word “right: denotes “entitlement”. The expression “right to use” means “ a grant, whether exercised or not” as opposed to “use” which signifies “a grant as exercised”.

‘USE’

- It was held that the word ‘use’ in relation to equipment occurring in clause (iva) of explanation 2 to section 9(1)(vi) is not to be understood in the broad sense of availing the benefit of an equipment. There must be some positive act of utilization, application or employment of equipment for the desired purpose. The customer must operate or control the equipment in some manner and exercise a certain degree of possession and control.

Royalty Provisions-Model Tax Conventions

Article 12(1)- Resident Taxation Clause

OECD MODEL	US MODEL	UN MODEL
1. Royalties arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State.	1. Royalties arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other Contracting State.	1. Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. 2. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed ___ per cent of the gross amount of the royalties. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation

Royalty Provisions-Model Tax Conventions

Article 12(2)- Royalty Definition Clause

OECD MODEL	US MODEL	UN MODEL
2.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.	4.The term "royalty" as used in this Article means payments of any kind received as consideration for the use of, or the right to use, any copyright of literary, artistic, scientific or other work (including cinematographic films); any patent, trademark, design or model, plan, secret formula or process; or for information concerning industrial, commercial or scientific experience.	3. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or ***for the use of, or the right to use, industrial, commercial or scientific equipment*** or for information concerning industrial, commercial or scientific experience.

Analysis

- The UN model covers the phrase "***for the use of, or the right to use, industrial, commercial or scientific equipment*** ", which is in line with section 9(1)(vi) of the Income Tax Act.

- "The Revision of the Model Convention" adopted by the Council of the OECD on 23 July 1992 removed the above phrase.

- These words still form a part of the UN Model Tax Convention, 2017.

- Hence, as per the UN model such payments constitute to be royalty and as per the OECD model they will fall in the Article 7 (Business Profits)

Analysis Contd…

- However, under the **Article 12** to apply, in case of an equipment the following factors are to be tested:
  1. Who is in physical possession and controls the property/equipment
  2. Who has significant economic or possessory interest in the property
  3. Who bears the risk of substantially diminished receipts or substantially increased expenditure if there is non performance under the contract
  4. Who uses the property/equipment concurrently to provide significant services to entities unrelated to the service recipient
  5. Total payment for the service does not substantially exceed the rental value of the computer equipment for the contact period

Dry Leasing V/s Wet Leasing

- Bareboat charter of equipment results in Royalties, while time charter of equipment does not result in Royalties. The Mumbai Tribunal held that there is no fundamental distinction between 'Dry Leasing' and 'Wet Leasing' and the basis, context and colour of both the transactions are nothing but leasing.*
- **West Asia Maritime Ltd. V. ITO (2007) 109 TTJ 617**

  W an Indian Co., acquired a ship from D, a foreign co., under a "bare boat charter and demise" agreement whereby, it (W, Indian Co) was to pay hire charges to D for 69 months. W also had options to purchase the ship from D by making a balloon payment which depends upon when the option was exercised. The ITAT held that the hire charges were royalties and not sale consideration, even though W had later exercised the option to purchase the ship.

* UN Commentary (2011) on Article 8 (para 11)

ADIT v. Valentine Martime (Mauritius) Ltd. (2011) 45 SOT 34 (Mum)

Caribjet Inc v. DCIT (2005) 4 SOT 18 (Mum)

Tax on Charter of Ship

- The Madras High Court held that even the time charter of a ship would fall under clause (iva) of explanation 2 to section 9(1)(vi). It is held that the term 'use' would include economic exploitation and the fact that the possession and control of the ship remains with the ship owner is irrelevant. It was also held that the charterer is not in possession of the vessel in the case of time charter, he has sufficient control over where the vessel will sail and when it will sail.
- The Madras High Court distinguished its above decision and held that the hiring of dredging equipment will not come within the meaning of royalty.

Container Leasing

Majority of the countries apply Article 12 to leasing of containers. Some countries, however, feel that Article 12 does not apply to container leasing since container industry is a peculiar one where the lease is an instrument rather than an ultimate end.

Certain Indian treaties (e.g. with Malta) provide that profits from the use, maintenance or rental of container (including trailers, barges and related equipment for the transport of containers) used in connection with the operation of ships or aircraft in international traffic would be subject to Article 8.*

* OECD report on "The Taxation of Income Derived from the Leasing of Containers" (Para 12, 40(a), 40(b), 41)

Credit Ratings Reports/Certificate

As per one view payments to a specialised credit rating agency for credit rating are for 'Professional Services'*, whereas as per another view issuance of credit rating by a credit rating agency is supply of commercial information.

Essar Oil Ltd. V. JCIT (2006) 102 TTJ 270 (Mum)

The Hon'ble ITAT held that:

- In general, the term "information" means the act or process of informing, communication or reception of knowledge;

- Any information which has got a commercial value for the user can be termed as "commercial information"

Credit Ratings Reports/Certificate

- If the end result of a service (e.g. Services for providing credit rating) is in the shape of supply of commercial information(e.g. Credit rating) for the user, then the transaction as a whole is of supply of "commercial information" and not merely of rendering of services. However, if the credit rating agency does not assign any credit rating and suggests ways and means to the client so that a suitable credit rating can be given, then there is no supply of "commercial information" and a service is provided
- One of the distinctions between "information" and "services" is that scope of services is narrow in a sense that such services are confined between two or more entities while "information" generally affects large public, directly or indirectly
- The other distinction can be drawn on the basis of the objective or necessity of the transaction i.e., if such services are taken for mandatory compliance with some statutory rules, then payments would be for services, even if, as a result of such exercise, some information is given to the public at large.

Supply of drawings and design

- Payments received for the supply of drawings and designs for the construction of a bridge or for providing specialised knowledge for manufacturing a particular commodity or for the supply of know-how and information necessary for setting up a plant or for a license to manufacture and sell certain products and use of patents or for engineering and procurement services and project management services were held to be payments by way of royalty and therefore taxable

  Payment towards technology, technical information and assistance for the purpose of manufacture is royalty. The court held that the grant of the right to use or permission to use intellectual rights and know-how would be covered under the definition of royalty.

1. Leohardt v. CIT 249 ITR 418
2. NV Philips v. CIT 172 ITR 521
3. NV Philips v. CIT 172 ITR 541
4. CIT v. Ahmedabad Calico 139 ITR 806
5. Worley Parsons Services Pty Ltd., In re. (No.1) 312 ITR 273 (AAR)
6. HCL Ltd. V. CIT 372 ITR 441

Case Laws on Bandwith Charges

- **[2014] 361 ITR 0575 (Mad) Verizon Communications Singapore PTE LTD. vs. ITO (IT).** The assessee was a Singapore based company & was engaged in the business of providing international connectivity services, bandwidth services or telecom services. Any customer has to enter into an agreement with the assessee for the overseas leg of services and the same customer has to enter in a similar agreement with VSNL for similar services in India. The payments to the assessee were for 'use of, or right to use equipment' u/s 9(1)(vi). Also, explanation 6 of section 9(1)(vi) defines 'process' to mean and include transmission by satellite (including uplinking, amplification, conversion for downlinking of any signal) cable, optic fibre, or by any other similar technology, whether or not such process is secret. The payment for bandwith charges recevied by the assessee also amount to use of process. The Hon'ble HC affirmed the decision of the ITAT holding that the bandwith charges received by the assessee are in the nature of 'royalty' as per Explanation 2(iva) & (vi) of section 9(1)(vi) of the Income Tax Act, 1961.
- **ISRO satellite centre In re, 307 ITR 59 (AAR) & Asia Satelliite telecommunications Ltd. V. DIT 332 ITR 340**

  It was held that the reservation of a particular capacity or bandwith is only a facility which is offered by the owner of the satellite infrastructure. Such payments will also not be for the use of satellite equipment.

Case Laws on Bandwith Charges Contd...

- **[2019] 73 ITR 194 (Mum-ITAT) DCIT V. Reliance Jio Infocomm Ltd**

  The assessee company is engaged in business of telecom services in India, entered into a 'bandwith-services' agreement with a Singaporean company (RJIPL) which enabled it to establish, install, maintain, operate and provide telecommunication services in Singapore and also provide bandwith services to service recipients across globe. The **process** involved to provide bandwith services was a standard commercial process that was followed by industry players and, therefore, same could not be classified as a '**secret process**' which would have been required for characterising aforesaid payment made by assessee to RJIPL as 'royalty' under India-Singapore DTAA. As amount paid by assessee to RJIPL was **neither towards use of Industrial, commercial or scientific equipment, nor towards use of (or for obtaining right to use) any secret formula or process**, same could not be classified as payment of 'royalty' as per the Article 12 of the India-Singapore DTAA.

Deviation from UN Model Convention

- **Singapore(Article 12)**

  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 a literary, artistic or scientific work, including cinematograph film or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, **including gains derived from the alienation of any such right, property or information ;**

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

- **Germany (Article 12)**

  No difference from UN model.

Deviation from UN Model Convention

- **UK (Article 13)**

  For the purposes of this Article, the term "royalties" means :

  payments of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic or scientific work, including cinematography films **or work on films, tape or other means of reproduction for use in connection with radio or television broadcasting,** any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience; and

  payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial or scientific equipment, **other than income derived by an enterprise of a Contracting State from the operation of ships or aircraft in international traffic.**

- **Italy (Article 13)**

  No difference from UN model

Deviation from UN Model Convention

- **Netherland (Article 12)**

  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, ~~**or films or tapes used for radio or television broadcasting,**~~ any patent, trademark, design or model, plan, secret formula or process, ~~**or for the use of, or the right to use, industrial, commercial or scientific equipment**~~ or for information concerning industrial, commercial or scientific experience.

- **UAE (Article 12)**

  The term "royalties" as used in this Article means payment 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 cinematography films, or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience **but do not include royalties or other payments in respect of the operation of mines or quarries or exploitation of petroleum or other natural resources.**

Deviation from UN Model Convention

- **Canada (Article 12)**

  The term 'royalties' as used in this Article means :

  payment of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic, or scientific work including cinematograph films or work on film tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, **including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof; and**

  payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment, **other than payments derived by an enterprise described in paragraph 1 of Article 8 from activities described in paragraph 3(c) or 4 of Article 8.**

Deviation from UN Model Convention

- **Switzerland (Article 12)**

  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 a literary, artistic, or scientific work, including cinematograph films or **work on film, tape or other means of reproduction for use in connection with radio or television broadcasting**, any patent trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, any industrial, commercial, or scientific equipment, or for information concerning industrial, commercial or scientific experience.

Deviation from UN Model Convention

- **USA (Article 12)**

  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 a literary, artistic, or scientific work, including cinematograph films or work on film, tape **or other means of reproduction for use in connection with radio or television broadcasting**, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, **including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof ; and**

  payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment, **other than payments derived by an enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(*c) or 3 of Article 8.***

Software - Goods or Service

- **[2004] 271 ITR 401 (SC) Tata Consultancy Services v. State of Andhra Pradesh**

- It has been held that by sale of the software programme the incorporeal right to the software is not transferred. It is held that the incorporeal right to software is the copyright which remains with the originator. What is sold is a copy of the software. It is held that the original copyright version is not the one which operates the computer of the customer but the physical copy of that software which has been transferred to the buyer. It has been held that when one buys a copy of a copyrighted novel in a book store or recording of a copyrighted song in a record store, one only acquires ownership of that particular copy of the novel or song but not the intellectual property in the novel or song.
- 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, they become 'goods', which are susceptible to sales tax.

Features of a Computer Software

- Can be described as a programme, or a series of programmes, containing instructions for a computer required either for the operational processes of the computer itself (system software) or for the accomplishments of other tasks (application software).
- Can be transferred via variety of media e.g. Tape, disc, fibre, wireless or can be downloaded.
- Can be standardised with a wide range of applications (off the shelf software) or be tailor made (Customised/bespoke software).
- Can be integrated with hardware (e.g. Embedded systems) or in an independent form.
- Is a form of intellectual property
- There maybe a grant of license to develop and exploit the software commercially; or
- Consideration may be received for usage (personal or business); or
- There may be complete or full transfer of ownership rights.

Section 14 of The Copyrights Act, 1957

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);*

Section 14 of The Copyrights Act, 1957 Contd...

(*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

Section 14 of The Copyrights Act, 1957 Contd...

(c) in the case of an artistic work,—

(*i*) to reproduce the work in any material form including—

(*A*) the storing of it in any medium by electronic or other means; or

(*B*) depiction in three-dimensions of a two-dimensional work; or

(*C*) depiction 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);

Section 14 of The Copyrights Act, 1957 Contd...

(d) in the case of a cinematograph film,—

(*i*) to make a copy of the film, including—

(*A*) a photograph of any image forming part thereof; or

(*B*) storing of it in any medium by electronic or other means;]

(*ii*) to sell or give on commercial rental or offer for sale or for such rental, any copy of the film

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

(e) In the case of a sound recording,—

(*i*) to make any other sound recording embodying it [including storing of it in any medium by electronic or other means]

(*ii*) to sell or give on commercial rental or offer for sale or for such rental, any copy of the sound recording

(*iii*) to communicate the sound recording to the public.

Case Laws on Software Payments

- **[2014] 264 CTR 329(Delhi) DIT v. Infra Soft Ltd.**

The assessee was an international software marketing, and development company and its holding company was based in US. The software developed and customized by the assessee was licensed to an Indian customer and the branch office of the assessee in India performed services involving interface to peripheral installation and training. As per the terms of license agreement, the licensee was allowed to make **only one copy** of software and associated support information for backup purposes with a condition that such copyright would include 'Infrasoft' copyright and all copies of software would be exclusive properties of 'Infrasoft'. Software was to be used only for licensee's own business and without consent of assessee it was not allowed to **loan/rent/sale/sub-licence or transfer the copy of software to any third party**, licensing agreement showed that the license is **non-exclusive**, **non-transferable** and the software has to be **used in accordance with the agreemen**t. To be taxable as royalty income covered by article 12 of the DTAA the income of the assessee should have been generated by the "**use of or the right to use of** "any copyright. **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.**

There is a **distinction between 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.

The Hon'ble High Court held that the consideration received was business income and could not be treated as royalty.

Case Laws on Software Payments

- **Zylog Systems Limited vs. ITO, [2020] 415 ITR 311 (Madras HC)**

  The assessee company is engaged in software development, it entered into a license agreement with a US company (M/s Bluestone Software Inc.) which grants it to use the copy of a 'copyright of software'. The assessee was to take copies and develop the same software and they are also permitted to market the product with a trademark and logo of the foreign company. For the purpose of this authorisation to use the software, trademark and logo in the product, the assessee is paying the annual fee, such fees tantamount to royalty as per the article 12(3) of the India-USA DTAA.

- **Quaolcomm India (P.)Ltd. Vs. ADIT (IT), [2017] 162 ITD 493 (Hyd. Trib)**

  The assessee was an Indian Co. It purchased **software support end user license package** from its associates in US and UK, and had made payments for use of such software licenses.Software was for assisting assessee in rendering its services and these software were tool in rendering software development services.

  The issue of license to use the software cannot be construed as granting a right to utilize the copyright embedded in the software. Therefore the payment made was for purchase of copyrighted article and not for the use of copyright itself. The Hon'ble ITAT held that payment for purchase of end user license package cannot be treated as royalty under the India-USA DTAA

Case Laws on Software Payments

- **Aspect Software Inc. vs. ADIT(IT) [2015] 61 taxmann.com 36 (Delhi-ITAT)**

  The assessee is a US company engaged in business of provision of hardware, software and rendering of support services that enable call centre companies. The US co. sold contact solutions to customers in India which was a combination of software and hardware. In which the hardware was sold to the customer and the software was licensed.

  The consideration received by the assessee for supply of product along with license of software to end user is not considered as royalty under article 12 of the India-USA Tax Treaty. Even where the software was separately licensed to the end users, there was no transfer of any right in respect of copyright by the assessee and it was a case of mere transfer of a copyrighted article. The payment for copyrighted article represents purchase price of the article. The Hon'ble ITAT held that income was business income and could not be treated as royalty.

Case Laws on Software Payments

- **[2019] 70 ITR 0073(Pune-ITAT) John Deere India Pvt. Ltd. (John Deere Equipment merged with John Deere India Pvt. Ltd.) vs. Dy DIT (IT).**

  The assessee being an Indian Co. made payment to its US based Associated Enterprise (AE) on account of software licenses, IT support charges, lease line charges and web based training fees. Purchase of software in the case of assessee being copyrighted article was not governed by the definition of 'royalty' under section 9(1)(vi).It was also held that since the definition of 'royalty' originally defined under DTAA has not been amended, the amended definition of 'royalty' under domestic law could not be extended to cover such cases. Therefore the provisions of DTAA that overrides the provision of IT Act, shall be applicable to the assessee.

  The Hon'ble ITAT held that the payment made to the US AE towards license fees could not be treated as royalty.

- **Qualcomm Incorporated Vs. ADIT (IT) [2015] 56 taxmann.com 179 (Delhi Trib)**

  When royalty is for use of a technology in manufacturing, it is to be taxed at situs of manufacturing product, and, when royalty is for use of technology in functioning of product so manufactured, it is to be taxed at situs of use. Revenue received by an American company, for providing software to Indian company is for copyrighted article and not for copyright itself same would not be taxable under section 9 or under article 12 of Indo-US DTAA

Case Laws on Software Payments

- **Reliance General Insurance Co. Ltd. vs. ITO(IT) [2018] 97 taxmann.com 350 (Mum Trib)**

  The assessee entered into an agreement with a US Co. or acquiring a non-exclusive, non-transferable, non-assignable and a non-sub-licenseable license to use the AE's Software Product *viz.* 'Blaze Advisor' software for its internal business purposes.

  On perusal of the agreement it was clear that assessee was clearly divested of all its rights to either transfer, assign and sub-license the said software The right to use of 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 Hon'ble ITAT held that the remittance made for acquiring the license could not be treated as royalty.

Case Laws on Software Payments

- **Black Duck Software Inc. Vs. DCIT (IT) [2017] 86 taxmann.com 62 (Delhi Trib)**

The assessee is a US co. It was provider of products and services for automating the management, compliance and secure use of open source software in multi source development at enterprise scale. During the year under consideration, the assessee had sold software under a 'Master License and Subscription Agreement'.

From a perusal of the scope of master license agreement, it is quite apparent that the assessee provided to its customers a non-exclusive; non-transferable license within the applicable subscription period. The customer has no right to retain or use the programme after termination of applicable subscription period for any reason.

Thus, the payment, which has been received by the assessee, is purely for copyrighted software product as against payment for giving any right to use any copyright in the software.

The Hon'ble High Court held that the consideration could not be treated as royalty.

Case Laws on Software Payments

- **Cincom System Inc. vs. DDIT (IT) [2016] 71 taxmann.com 258 (Delhi Trib.)**

The assessee is a US co. engaged in business of providing software solution. It entered into a communication agreement with Cincom- India, whereby the assessee would provide access internet by which it provided a gateway that would facilitate call centres to incoming and outgoing calls from India to the people of USA, referred as Cincom gateway. For this purpose assessee used embedded secret software owned by itself.

It is a case of **use of embedded secret software owned by the assessee**-company for the purpose of enabling the customer from India to call the residents of USA or *vice-versa*. The **consideration payable is for the specific programme** through which the Indian company is able to cater to the needs of the group companies. The transaction would be **related to a 'scientific work' and would partake of the character of intellectual property**. Payment is received as **'consideration for the use of, or the right to use design or model, plan, secret formula or process'.**

The Hon'ble ITAT held that the payment were in nature of royalty.

Case Laws on Right to use- Off the Shelf Software

- **Cummins Inc. vs. DDIT (IT) [ITAT-Pune] [2019]111 taxmann.com 197**

  The assessee being a US tax resident was the principal company of group, who procured various software directly from 3rd party vendors with the object of standardization, efficiency, consistency and cost effectiveness, and thereafter it granted user rights in these software to its affiliate company worldwide for their internal use including the JV in India.

  The US company obtained non-exclusive user right and does not have any rights to sub-license/reverse engineer the software. The software supplied by the US Company to the Indian companies was **not customized software but were purchased off-the-shelf. The US company merely provided the Indian JV rights in the copyrighted software and not the rights of use of copyright.** The definition of "royalty" as given in Article 12 of the DTAA is very restrictive as compared to royalty defined under the Act. The consideration received for grant of user rights in software licenses would not amount to royalty income within the purview of DTAA.

Tax on Online access of database

- **[2013] 355 ITR 284 (Karnataka) CIT v. Wipro Ltd.**

  The assessee company made a payment to a US company for obtaining online access to the database maintained by the US company. Though subscription access to journal may seem different from software license, it si in fact nothing but a license to use (right to use) the journal and hence will be construed as royalty u/s 9(1)(vi) of the Act.

- **CIT v. HEG Ltd. 263 ITR 230 (MP)**

  The high court held that payment for a compilation of technical information (Carbon Databank) to a US company cannot be construed as royalty. The high court held that payments made to obtain mere data or calculation sheet could not be treated as royalty payments. In order to withhold tax on payments for information received, the information should have some special features and should not merely be of pure commercial nature

- **[2017] 55 ITR(T) 405 (AHD-ITAT) DCIT(IT) v. Welspun Corporation Ltd.**

  The assessee company obtained access to a database from a UK company. The database contained copyrighted information not available in public domain. As per article 13 of the India-UK DTAA it is only when use is of copyright that taxability can be triggered in source country. The Hon'ble ITAT held that the payment was for use of copyrighted material rather than for use of copyright and hence such payments do not fall in the definition of royalty.

Case Laws on Cloud Hosting Services

- **Rackspace US Inc. vs. DCIT(IT)(ITAT- Mumbai) [2020] 113 taxmann.com 382**

  The assessee being a US based company, earned income from providing cloud services including cloud hosting and other supporting and ancillary services to Indian customers. There was no leasing of any equipment by the US Company and customers were not having physical control or possession over servers and right to operate and manage this infrastructure/servers vested solely with the US company. The US Company's customers only avail hosting services and do not use, possess or control the equipment used for providing hosting services. The payment for hosting services made by Indian customers to US Company does not fall within the ambit of the definition of royalty u/s 9(1)(vi). O**nly after making retrospective amendment in the section by inserting Explanation 4,5 & 6 the payments received by the assessee fall in the definition of royalty.** The amendment in the Act **cannot be read into the treaty** and the definition of royalty under Article 12(3) of the India-USA Tax Treaty in respect of payment for use or right to use equipment is in pari-materia with the pre-amendment definition of royalties in the Act and said definition is exhaustive and not inclusive. The Hon'ble ITAT held that hosting service provided by the assessee could not be taxed in India as Royalty or FTS under section 9(1)(vi) or 9(1)(vii).

Case Laws on Web Hosting Services

- **DDIT (IT) vs. Savvis Communication Corporation [2016] 69 taxmann.com 106 (Mumbai Trib.)**

  The assessee was a US Co. engaged in the business of IT solutions including web hosting services. It earned income from provision of managed hosting services to Indian entities. Distinction between consideration receive/paid for rendition of services even though involving use of scientific equipment and the consideration paid/received for use of scientific equipment analysed. A payment cannot be said to be consideration for use of scientific equipment when person making the payment does not have an independent right to use such an equipment and physical access to it.

  Therefore, even though the services rendered by the assessee to the Indian entities may involve use of certain scientific equipment, the receipts by the assessee cannot be treated as 'consideration for the use of, or right to use of, scientific equipment'.

  The Hon’ble ITAT held that consideration received for rendering web hosting services cannot be treated as royalty.

Case Laws on data access/ link/IPLC charges

- **NetCarcker Technology Solutions Inc. Vs. ADIT [2019] 111 taxmann.com 193 (Mum-ITAT)**

  The assessee was US tax resident and engaged in providing and developing billing information and software, for which it received data access/ link charges also know as IPLC from its Indian subsidiary. International Private Leased Circuits (IPLC) was procured by the US co. from a 3rd party and the cost incurred in this respect attributable to the Indian subsidiary was charged from the Indian co. The payment in the instant case was not for a scientific work nor there was any patent, trademark, design, plan or secret formula or process for which the payment was made. **This facility is a standard facility which is used by other companies as well.**

  The Hon'ble ITAT held that IPLC charges fall out of the purview of the term Royalty as well as FTS/FIS as per the Act and the India-USA DTAA.

Case Laws on data access/ link/IPLC charges

- **ITO vs. Cognizant Technology Solutions India (P.) Ltd [2014] 47 taxmann.com 409 (Chennai Trib)**

  The assessee-company is engaged in the business of software development and export. The assessee made remittances to USA for hire of IPLC. The payment to the US co. includes router rental charges, router management charges, router maintenance charges, software initialization charges, router installation charges.

  Even if the payments were treated as non-relating to the use of equipment, they should be considered as payment for the use of the process provided by the assessee, whereby through the assured bandwidth, the customer is guaranteed the transmission of data and the voice. Thus, the consideration being for the use and right to use of the process, it is 'Royalty', within the meaning of Clause-(iii) of Explanation-2 to section 9(1)(vi) of the Act. The Hon'ble High Court affirmed the findings of the Tribunal on the issue.

Case Laws on Online Educational Service

- **[2012] 51 SOT 356(Delhi) Hughes Escort Communications Ltd. v. DCIT.**

  The assessee had entered into an affiliate agreement with TILS Inc., U.S.A. (eCornell) to market, promote and provide ancillary services in connection with providing distance learning courses offered by eCornell university to students in India and both of them shared payments. Honorable Delhi Tribunal held that the payment made to eCornell was not 'royalty' as payment was not for use or right to use any copyright or literary work, instead it was purely a case of apportioning of fees attributable to eCornell as per affiliate agreement.

- **Regents of University of California UCLA Anderson School or Management Executive education, USA – (AAR) 378 ITR 398 (AAR-New Delhi)**

  Applicant was a US based Non- profit public benefit corporation formed for providing education. The applicant entered into an agreement with an Indian Co. to launch a management program to train senior executives of companies. The applicant during the course provided the participants with programs of Harvard Publishing University which are publishing material for people all over the world. The AAR held that the payments cannot be considered as royalty as per the India-USA DTAA.

Case Laws on One time affiliation fees

- **Customer Lab Solutions (P.) Ltd. vs. ITO [2018] 171 ITD 552 (Hyd-ITAT)**

  Assessee being an Indian company entered into an agreement with an US Company for the purpose of its consultancy business and paid two types of fees: 1. Annual Affiliate fee and 2. Fees for consulting and reports. Against the payment of the affiliation fee the assessee got two magazines published by Harvard Business school which cannot be considered as right to use a copyright. Further, the payment of affiliation fee alone does not result in either providing any technical service or use of technical knowledge. Also, there is no transfer or use of any technology, and the payment of fees was simply for affiliation. The Hon'ble ITAT held that the payments made by the assessee could not be considered as royalty under both section 9(1)(vi) and article 12 of India-USA DTAA.

- **[2013] 214 TAXMAN 0317 (Bombay) DIT(IT) vs. WNS Global Services (Uk) Ltd.**

  The assessee company was a resident of UK, it obtained a lease line from an international telecom operator and further this lease line was provided to WNS India on cost to cost basis & the charges of the same were also recovered from WNS India. The Hon'ble HC held that the charges received are in the nature of reimbursement of expenses and will not be classified as royalty or income attributable to PE in India.

- **(2019) 198 TTJ 0546 (Kol-ITAT) Koninklijke Philips Electronics N.V. vs. DCIT(IT).**

  The assessee Co. Was a tax resident of Netherland & it entered into a Research and Development Co-operation agreement (RDCA) with Philips India (PEIL). The remuneration received for providing the R&D services as per the RDCA were mere reimbursement of expenses incurred for such R&D. The assessee used knowledge, experience and skill but did not impart such knowledge, experience and skill to PEIL. The ITAT held that such remuneration does not fall in the ambit of 'royalty' as per article 12(4) of the India-Netherland DTAA and also u/s 9(1)(vi) Explanation 2(iv). Hence, such income is not taxable in hands of assessee in India.

- **CIT v. Maggronic devices pvt ltd 329 ITR 442(HP) & CIT v. Creative infocity Ltd. 397 ITR 165(Gujarat)**

  Payment made for outright purchase of technical know-how (drawing, designs, shelters, etc.) is not royalty

- **K bhagya lakshmi V. DCIT 416 ITR 497(Madras)**

  Payment for assignment of copyright for 99 years-may be treated as perpetual and akin to a sale – not regarded as royalty

- **CIT v. Klayman porcelains Ltd. 229 ITR 735 (AP)**

  A non resident company deputed an expert to supervise the construction and installation of a project in India. The same cannot be held as royalty.

- **CIT v. Neyveli Lignite 243 ITR 459 (Madras)**

  The foreign company supplied machinery to an Indian company and incidentally also supplied the design of the manufacturing machinery and information concerning the working of the machinery. The design was not supplied to enable the Indian company to manufacture the machinery, nor was any license of any patent involved in the transaction. The Hon'ble high court held on these facts that the payment to the foreign company was not covered by ether cl (vi) of (vii) of section 9(1) of therefore not taxable.

- **[2019] 179 ITD 0367(Bangalore-ITAT) M/S. Kingfisher Airlines Ltd. vs. DCIT (IT).**

  The assessee Co. Availed services of a UAE Co. For training its pilots & cockpit crew. In the due course of such training a flight simulator was used, and it was charged to the assessee on hourly basis. The ITAT held that mere charge of simulator on hourly basis does not conclude that the assessee has paid royalty for such use, it was a part of the training program. The same shall be considered as business profits of the foreign entity & due to no PE in India such income is not taxable in India.

- **[2011] 139 TTJ 10(Delhi-ITAT) DCIT vs. MRO (India) (P) LTD.**

  The assessee Co. Entered into an agreement with a New Zealand Co. for liaisoning and co-ordinating the transfer of DNA test reports of a person to the US embassy. Such services do not fall in the ambit of 'royalty' or 'fees for technical services', there is no obligation on assessee to deduct tax.

- **[2018] 194 TTJ 385(Bangalore-ITAT) Google India Pvt Ltd vs. JDIT (IT).**

  The assessee Co. has entered into an arrangement with Google Ireland Ltd.(GIL). As per the agreement (Adword programme) the assessee **bought** advertisement slots from GIL and further sold them to customers, it made remittances to GIL after keeping its share. ***Under the agreement the assessee was give the licence to use the confidential information, technical know-how, trade mark, brand features, derivative works, in order to provide its services efficiently.*** Therefore the consideration paid by the assessee is on account of usage of all these intangibles is certainly in the nature of payment of 'royalty' and is chargeable to tax under section 9(1)(vi) of the Act and under article 12 of the India -Ireland DTAA. The assessee was bound to deduct tax at source from such payments.

- **[2019] 111 taxmann.com 214 (Delhi - Trib.) DLF v. ITO**

  The assessee company, as tax resident of India, made a payment to a company of UAE to hire a charter plane outside India. The Hon'ble ITAT held that the hire of a charter plane outside India was a standard service and do not constitute to be royalty.

  Also, it entered into an agreement with a UAE based company for obtaining ground rights in respect of India-Pakistan Friendship Series Cricket Matches played in UAE, the said payments were made by the assessee to the UAE company to secure ground rights for the cricket match and to find other sponsors for the event. The term **'equipment'** has not been defined in the Act or in the DTAA, however The Merriam Websters dictionary defines an equipment as **"All fixed assets other than land and building"** used in a business enterprises. As per AS-10 issued by the ICAI a fixed asset is an asset held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business. The cricket ground is land and building and hence cannot be regarded as equipment, further, it is not used in business of the appellant, who is engaged in real estate business. The honorable tribunal held that since the cricket ground can not be described as equipment nor there is use or right to use of it, the payments made by the appellant for taking sponsorship of cricket series can not be characterized as royalty u/s 9(1)(vi) of the Act.

- **[2017] 166 ITD 329 (Bang-ITAT) ABB-FZ LLC v. DCIT(IT)**

  The assessee company a tax resident of UAE has provided services to it AE in india. The services agreement gave opportunity to ABB Ltd (Indian AE) of using information pertaining of industrial/commercial/scientific experience belonging to the assessee which was not available in public domain . Assessee had merely provided access to such specialised knowledge, skill and expertise and had not done anything more, for rendering services. The Hon'ble ITAT held that activities allegedly rendered by assessee were in form of sharing or permitting to use special knowledge, expertise and experience of assessee and thus it fell within realm of 'royalty', as defined in article 12(3) of the India-UAE DTAA

- **Warner Bros. Distributing Inc. vs. ADIT (IT) [2014] 44 taxmann.com 237 (Mumbai)**

  The assessee, a US based company, engaged in distribution of cinematographic films, received certain amount from its divisional office on account of distribution of films in India, which could not be held as payment of royalty as per the DTAA**.**

Case Laws on Professional fees for strategic counselling

- **Marck Biosciences Ltd. Vs. ITO(IT), [2017] 164 ITD 205 (Ahd-Trib.)**

  The assessee an Indian Company made payment to a US company on account of professional fee for global biopharmaceutical strategic counseling and advisory services. According to the lower authorities such services were held to be royalty as per explanation 2 to section 9(1)(vi) and Article 12(3) of the DTAA, considering it as parting with the "information concerning industrial, commercial and scientific experience" gained by the US entity over a period of time. The services received included, business promotion, marketing, publicity and financial advisory. Further, the service did not include the use of any information concerning industrial, commercial or scientific information. **While characterizing the nature of payment, the activity triggering in consideration of which the payment is made is relevant. In the present case the activity was rendition of services, the fact that in the process of availing these services, the assessee benefits from rich experience of the service provider is wholly irrelevant.** The Hon'ble ITAT held that the fees paid could not be treated as royalty as per the Act and the India-USA DTAA

Case Laws on Subscription fees

- **American Chemical Society Vs. DCIT (IT) [2019] 106 taxmann.com 253 (Mumbai)**

  Assessee is US based non-profit corporation, established to promote and support development of knowledge in the field of chemistry. It received subscription fees for chemical abstract services (CAS) and publication (PUBS).

  The US Corporation merely accumulates and organizes information already available in public domain/publicly disclosed information, and organizes the same at one place, thereby creating a database which is accessed by its customers against payment of subscription fee termed as CAS fee. The subscriber/customer did not get a copyright nor any full-fledged right to use, but only a limited right to use the copyrighted article. The corporation itself did not have any copyrights in respect of the contents of the database. The customers got only the right to search, view and display information (whether online or by taking a print) and reproducing or exploiting the same in any manner and its use for purposes other than personal use was strictly prohibited.

  In order to be understood as 'royalty', the payment must be for information which is exclusively possessed or secret under the ownership of the grantor of such information. The Indian customers did not pay the US co. for its experience of creating a database, rather they paid for the information contained in that database. The Hon'ble HC held that CAS and PUBS could not be treated as royalty as per the India-USA DTAA

Case Laws on Advertising & Marketing Service

- **Marriot International Inc. vs. DDIT (IT) [2016] 69 taxmann.com 347 (Mumbai Trib)**

  The assessee is a US co. and belongs to "Marriott" group, which is engaged in the business of operating hotels worldwide. Some of the Indian hotels entered into an agreement with the assessee titled as "International Sales and Marketing Agreement" (ISIM), as per which, the assessee has agreed to carry out "sales and marketing services" outside India. The services mainly consisted of advertisements, marketing, publicity, purchasing add slots in magazines and radio, etc. Based on these advertisements the Indian hotels were able to sell their rooms abroad.

  The Hon'ble ITAT held that the amount so received was to be taxed as royalty in India in terms of article 12 of India-USA DTAA

No surcharge or cess on DTAA rates

- **[2019] 199 TTJ 0273(Hyd-ITAT) R.A.K. Ceramics, UAE (c/o R A K Ceramics India Pvt Ltd.) vs. DCIT(IT).**

  The assessee Co. A resident of UAE received interest and royalty income from an Indian Co., tax was duly deducted as per the rates specified in article 12(2) & 11(2)(b) of the India-UAE DTAA. The ITAT held that there can be no levy of surcharge and educational cess over and above of the rates specified in DTAA as, as per article 2(2) of the DTAA the taxes covered include 'income Tax including any surcharge thereon'.

THANK YOU

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