Business Laws

Nothing ‘soft’ about this ‘ware’

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In a seminal judgment, SC has held that ownership of copyright in a work differs from the ownership of the physical material in which the copyrighted work may happen to be embedded

An Indian company which purchases television sets for further resale in India is not called upon to deduct tax at source on the payments made to the foreign vendor for the simple reason that the revenue constitutes business income for the foreign manufacturer and the foreign manufacturer does not have a permanent establishment in India.

Unfortunately, since the product is ‘software’ (all other things being the same), controversy erupted as the government took the position that the payment would amount to ‘payment of royalty’. This meant that tax has

to be deducted.

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The assessee's basic argument was that there is a huge difference between 'copyright' and 'copyrighted article'. A software licensed through distributors or resellers or directly is only a 'copyrighted article' and the 'copyright' continues to vest with the foreign software manufacturer / supplier.

Section 9 of the Income Tax Act, 1961 was amended to define 'royalty' in order to cover *transfer of all or any rights including the granting of a license in respect of any copyright.* The definition of 'royalty' under various Double Taxation Avoidance Agreements entered into between India and other countries were not amended.

Assesses relied upon Section 90(2) of the Income Tax Act, 1961 which provides that the provisions of the Act shall apply to the extent they are more beneficial to the assessee and in the instant case, the provisions of the Act were not beneficial.

Appeals before SC

Divergent views resulted in the matter reaching the Supreme Court in a batch of appeals filed by the assessee as well as the Revenue.

The SC in a landmark decision in *Engineering Analysis Centre of Excellence* has settled the issue with absolute clarity and the decision by itself is a treatise on both tax and copyright laws.

The SC has categorically held that there is no obligation to deduct TDS on the amounts paid by resident Indian end-users/distributors to non-resident computer software manufacturers/suppliers as consideration for the resale/use of the computer software through Exclusive User License Agreement or distribution agreements as such payments are not payment of royalty for use of copyright in the computer software.

Copyright

The SC held that ownership of copyright in a work differs from the ownership of the physical material in which the copyrighted work may happen to be embedded.

An example is the purchaser of a book or a CD/DVD who becomes the owner of the physical article but does not become the owner of the copyright inherent in the work – the copyright remaining exclusively with the owner.

A licence from a copyright owner conferring no proprietary interest on the licensee does not involve parting with any copyright and is different from a licence under Section 30 of the Copyright Act. The right to reproduce and right to use computer software are distinct and separate rights where the former amounts to parting of the copyright and the latter not being so.

Income Tax Act

Any ruling on the more expansive language contained in the explanation to Section 9(1)(vi) would have to be ignored if it is wider and less beneficial to the assessee than the definition contained in the DTAA. The SC also held that even if the definition of 'royalty' in the Act alone is considered, it is clear that there has to be a *transfer* of 'all or any rights' which includes the grant of license in respect of any copyright in literary work.

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patent, copyright and trademark laws