Sum received by Irish Co. for providing online access to its e-learning products in India is taxable as royalty

Summary – The Delhi ITAT in a recent case of SkillSoft Ireland Ltd., (the Assessee) held that Consideration paid by an Indian distributor to foreign company for use or right to use confidential programme software (especially designed software) itself constitutes royalty in terms of DTAA between India and Ireland

Facts

- The applicant, an Ireland based company, is engaged in the business of providing SkillSoft products. A SkillSoft product consists of two components. The first is course content and the second is the software through which the course is delivered to the end customer.
- The applicant has entered into a reseller agreement with SkillSoft India. SkillSoft India buys the SkillSoft products from applicant and sells the same to Indian users. Under the reseller agreement SkillSoft India is a distributor and has the right to license, market, promote, demonstrate and distribute SkillSoft products by providing online access to SkillSoft products in India.
- The applicant's argument is that SkillSoft Products are similar to a book, and since payments for books are not regarded as royalty, it is argued that payments for the educational course offerings like SkillSoft Products, being akin to such books, should not be regarded as royalty under the India-Ireland Treaty. The applicant mainly emphasized on the facts that no right in the copyright is transferred to the SkillSoft India or to the Indian end-users. He also made a distinction between copyright and copyrighted article and stated that payment received is in respect of copyrighted article. He further argued that Indian end-users are granted only non-exclusive and non-transferable license and therefore it is not covered under the definition of 'copyright'.

Held

Issues

- The issues to be considered here are : as to whether computer programme and computer database (software) are covered under article 12(3)(a) of DTAA for the purpose of Royalty; whether there is any distinction between copyright and copyrighted articles for the purpose of royalty and whether grant of non-exclusive, non-transferable rights would be akin to transfer of rights in the copyright or copyrighted article.

Software as Literary Work

- As regards coverage of computer programme and computer data base within the ambit of 'literary work' in article 12(3)(a), this Authority in the case of *FactSet Research Systems Inc.*, In re [2009] 317 ITR 169/182 Taxman 268 (AAR - New Delhi) held that the computer data base falls within the scope

© 2015, Tenet Tax & Legal Private Limited

of literary work. Admittedly, SkillSoft products are software as mentioned by the applicant in the application. The issue was settled by the Authority in the case of *FactSet Research Systems Inc.* (*supra*) that 'By an inclusive definition in section 2(o) of Copyright Act, computer programmes and computer databases are included within the ambit of literary work.' The applicant has further tried to say that such software shall be covered under ITES. However, this is a fallacious argument because the notification dated 18-9-2013 issued by CBDT defining ITEA does not apply to the applicant. This notification is only meant for such eligible assessees who have exercised a valid option for application of Safe Harbour Rules. The analogy drawn by the applicant to the on-line banking facility provided by a bank or to an e-library (book) is also not at all appropriate. As mentioned earlier, SkillSoft products consist of the software through which the course content is delivered to the end-customer who gains access to an especially designed software for understanding the content. As per the website of the applicant they are marketing several copyrighted software containing simulation exercises and such software simulations are especially designed by them. Such especially designed software are not available in public domain. It is clearly mentioned by them that these products are 'licensed by the applicant to SkillSoft India under the agreement and further sub-licensed/distributed to end customers in India under the customer agreement.' It is not correct to say that the applicant's case is completely different from the facts of a case surrounding software. The fact is that software and computer databases created by the applicant are included within the ambit of 'literary work' and, therefore, covered under article 12(3)(a).

Copyright v. Copyrighted Article

- The applicant further trie to make a distinction between a copyrighted article and a copyright and said that the payment received by the applicant is only in respect of a copyrighted article and no rights in the copyright are granted to the Indian end-users. In the case of *Citrix Systems Asia Pacific Pty Ltd.*, In re [2012] 343 ITR 1/205 Taxman 320/18 taxmann.com 172 (AAR - New Delhi) the Authority had examined same issue and concluded that such distinction is illusory. It is nothing but an article which incorporates the copyright of the owner, the assignee, the exclusive licensee or the licensee. So, when a copyrighted article is permitted or licensed to be used for a fee, the permission involves not only the physical or electronic manifestation of a programme, but also the use of or the right to use the copyright embedded therein.

Grant of non-exclusive, non-transferable rights in licence

- It is the applicant's main argument that it does not involve provision of the right to use in copyright of a literary, realistic or scientific work, in patent, trademark, design or model plan , etc. The applicant argued that the grant of right to Indian end-users to access the educational content should not be construed as granting a copyright. It is purely a question of fact on the basis of which it can be decided whether the nature of license granted by the applicant would result in royalty or not.

© 2015, Tenet Tax & Legal Private Limited

Similar issue was involved in the case of *Citrix Systems Asia Pacific Ply. Ltd.,* In re (*supra*). The High Court in the case of *Synopsis International Old Ltd.* [2013] 212 Taxman 454/[2012] 28 taxmann.com 162 (Kar.) had examined clause of the agreement entered into between the parties which dealt with grant of rights. It was provided therein that Synopsis granted licensee offering a non-exclusive, non-transferable license, without right of sub-license, of use the software and design technologies only in the quality authorised by a licensee in accordance with the documentation in the use area. In the present case also the reseller agreement grants to customer a non-exclusive, non-transferable license (without the right to sub-license). The High Court had mentioned categorically that merely because the words 'non-exclusive and non-transferable' are used in the said license, it does not take away the software out of definition of 'copyright'. It was further held that even if it is not transfer of exclusive right in the copyright, the right to use the confidential information embedded in the software in terms of the aforesaid license makes it abundantly clear that there is transfer of certain rights which the owner of copyright possess in the said computer software/programme in respect of the copyright owned. It was further held that it is not necessary that there should be a transfer of exclusive right in the copyright. In this case also similar words have been used in the reseller agreement as well as Master License Agreement. Therefore, irrespective of use of the words like non-exclusive and non-transferable in these two agreements, there is definitely transfer of certain rights of which the applicant is the owner.

- As regards definition of 'royalty' under DTAA, it was held by the Karnataka High Court in the case of *Synopsis International Old Ltd.* (*supra*) that under the DTAA to constitute royalty there need not be any transfer or any rights in respect of any copy rights and it is sufficient if consideration is received for use of or the use to any copyright. Therefore, if the definition of 'royalty' in the DTAA is taken into consideration, it is not necessary that there should be a transfer of any exclusive right, and in terms of the DTAA the consideration paid for the use of right to use the said confidential information in form of computer programme software itself constitutes royalty. Thus, the findings of Karnataka High Court in the case of *Synopsis International Old Ltd.* (*supra*) are agreed.
- In view of above, The payment received by the applicant cannot be characterized as fees for technical services under Article 12(3)(b)of the DTAA. The payment received by the applicant are in the nature of royalty under article 12(3)(a) of the DTAA. No permanent establishment is created for the applicant in India under the provision of Article 5 of the DTAA and the payment received by the applicant would be subject to withholding tax in accordance with the provisions of the section 195.
- No permanent establishment is created for the applicant in India under the provision of Article 5 of the DTAA.

© 2015, Tenet Tax & Legal Private Limited