

Sum paid for right to use software is deemed as 'royalty' and not sum paid for purchase of software

Summary – The High Court of Delhi in a recent case of M. Tech India (P.) Ltd., (the Assessee) held that Payments made for purchase of software as a product would be treated as a payment for purchase of software rather than payment for use or right to use software to be considered as royalty

Facts

- The assessee-company was a Value Added Reseller (VAR) of software related to healthcare and hospitality. During the relevant assessment year it purchased certain softwares from two foreign companies and resold same to various end users in India. For such purchases the assessee had made certain payments to foreign companies.
- The Assessing Officer held that the said payments were in the nature of 'royalty' and since the assessee had not withheld any tax therefrom, he disallowed the same under section 40(a)(i).
- On appeal, the Commissioner (Appeals) held that the payments made by the assessee for purchase of the software from the foreign companies were not royalty and the assessee was not obliged to deduct any tax at source on such payments. Consequently, he deleted the additions made by the Assessing Officer.
- On appeal by the revenue, the Tribunal concurred with the decision of the Commissioner (Appeals).
- On appeal to the High Court:

Held

- In the cases where an assessee acquires the right to use a software, the payment so made would amount to royalty. However, in cases where the payments are made for purchase of software as a product, the consideration paid cannot be considered to be for use or the right to use the software. It is well-settled that where software is sold as a product, it would amount to sale of goods. Thus, it is necessary to make a distinction between the cases where consideration is paid to acquire the right to use a patent or a copyright and cases where payment is made to acquire patented or a copyrighted product/material. In cases where payments are made to acquire products which are patented or copyrighted, the consideration paid would have to be treated as a payment for purchase of the product rather than consideration for use of the patent or copyright.
- In the aforesaid view, the Tribunal was justified in deleting disallowance made by the Assessing Officer under section 40(a)(i) and 40(a)(ia).