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Tax Flash News

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Payment received for sharing a third-party shrink-wrapped software with a group company is not 'royalty' in the absence of transfer of copyright

Executive summary

The Delhi bench of the Tribunal in the case of *Saxo Bank A/S*[1] held that the payment received by a foreign company from its Indian group company for sharing a third-party shrink-wrapped software is not taxable as a royalty. The foreign company merely provided access to the software and no copyright was transferred to the Indian company.

The Tribunal relied on the Supreme Court decision in the case of *Engineering Analysis*.

[1] *Saxo Bank A/S* v. *ACIT* (ITA No. 2010/Del/2023) - Source: Taxsutra

Facts of the case

The taxpayer (a foreign company) and its group companies provided capital market platform, and other services through their online platform to the traders and investors.

They required various licensed software for carrying out their business.

The taxpayer entered into a global agreement with a third-party for centrally procuring various shrink-wrapped software for all its group companies.

The taxpayer cross charged the cost of software to the group companies including an Indian group company (SGIPL) for sharing access of software.

The tax officer held that the taxpayer aligned such software with its IT Infrastructure and provided the infrastructure to SGIPL. The payment received for providing access to the IT infrastructure including various software was taxable as equipment royalty under clause (iva) of Explanation 2 to section 9(1)(vi) of the Income-tax Act, 1961.

The taxpayer argued before the Dispute Resolution Panel that it did not maintain any IT infrastructure. The software were either installed on the laptops of the end-users or accessible over the cloud infrastructure of the third-party. Thus, the payment received from SGIPL was not taxable as equipment royalty.

The taxpayer also contended that the software were for its own captive use and use by its group companies for their business operations.

There was no transfer of any copyright while providing access of software to the group companies and thus the payment received was not taxable as software royalty.

Tribunal's decision

The payment made by SGIPL to the taxpayer was not taxable as a royalty as there was no transfer of copyright in the software.

A copyright is not transferred if the licence does not confer any proprietary interest on the licensee or where the core of a transaction is to authorise the end-user to have access to and make use of the licenced software over which the licensee has no exclusive rights.

The software granted to the taxpayer by the third-party was an object code version only and on a non-exclusive, non-sub-licensable basis. It was provided only for taxpayer's and its group companies' internal business purposes.

Neither the taxpayer nor SGIPL can sub-license, transfer, modify, reproduce the software.

Our comments

The Supreme Court in the case of *Engineering Analysis Centre of Excellence Pvt. Ltd*.[2] held that the payment for the shrink-wrapped computer software either by the end-user or by the distributor did not constitute royalty.

Following this decision, the High Courts and the Tribunal have ruled in the favour of taxpayers in the cases involving the shrink-wrapped software.

The Revenue has filed a review petition against the Supreme Court's decision and the petition is still pending.

It is also interesting to see the approach followed by the Revenue to tax the receipt as equipment royalty. The facts of each case need to be analysed to determine the applicability of such an argument.

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[2] *Engineering Analysis Centre of Excellence Pvt Ltd.* v. *CIT* [2021] 432 ITR 471 (SC)

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