

CTR ENCYCLOPAEDIA ON INDIAN TAX LAWS

ADDITIONAL DIRECTOR OF INCOME TAX (INTERNATIONAL TAXATION) vs. TII TEAM TELECOM INTERNATIONAL (P) LTD.

ITAT, MUMBAI 'E' BENCH

Pramod Kumar, A.M. & Vijay Pal Rao, J.M.

ITA No. 3939/Mum/2010; Asst. yr. 2006-07

26th August, 2011

(2011) 140 TTJ (Mumbai) 649 : (2011) 60 DTR 177 : (2011) 12 ITR 688

Legislation referred to

Section 90, 90(2), 254(1), DTAA between India & Israel, Art. 12,

Case pertains to

Asst. Year 2006-07

Decision in favour of

Assessee

Double taxation relief—Agreement with foreign country—Applicability of DTAA vis-a-vis provisions of IT Act—In view of s. 90(2), the provisions of applicable tax treaty override the provisions of IT Act, except to the extent the latter are more beneficial to the assessee—It is wholly immaterial whether the provisions of the IT Act are later provisions or whether these provisions were legislated prior to entering into the tax treaty—Once a tax treaty is entered into and notified by the Central Government, the provisions of the IT Act have to make way for the provisions of the tax treaty, wherever these provisions are in conflict with the provisions of the tax treaty, unless the provisions of the IT Act are more favourable to the assessee vis-a-vis the corresponding provisions of the tax treaty

Held :

As to the extent to which provisions of the tax treaty will govern the taxability of a non-resident assessee, the law is unambiguous as s. 90(2) provides that "where the Central Government has entered into an agreement with the Government of any country outside India under sub-s. (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee". In other words, in such a case, the provisions of applicable tax treaty will override the provisions of the IT Act, except to the extent the latter are more beneficial to the assessee. As evident from a plain reading of s. 90, it is wholly immaterial whether the provisions of the IT Act are later provisions or whether these provisions were legislated prior to the tax treaty having been entered into. Once a tax treaty is entered into, and is notified by the Central Government, the provisions of the IT Act have to make way for the provisions of the tax treaty, wherever these provisions are in conflict with the provisions of the tax treaty—unless, of course, when the provisions of the IT Act are more favourable to the assessee vis-a-vis the

corresponding provisions of the tax treaty. It is important to bear in mind the fact that this unqualified treaty override is not due to operation of any provisions of the general law or convention, but by the virtue of a specific provision to that effect in the IT Act itself. The Indian IT Act itself restricts its application to a situation covered by the provisions of a tax treaty entered into, and duly notified, under the scheme of s. 90.—[Union of India & Anr. vs. Azadi Bachao Andolan & Anr.](#) (2003) 184 CTR (SC) 450 : (2003) 263 ITR 706 (SC) **followed**; Gramophone Co. of India Ltd vs. V.B. Pandey AIR 1984 SC 667 and Ram Jethmalani vs. Union of India 2011 TIOL SC 57 PIL **distinguished**.

(Paras 8 & 9)

Conclusion :

In view of s. 90(2), the provisions of applicable tax treaty override the provisions of IT Act, except to the extent the latter are more beneficial to the assessee, whether the provisions of the IT Act are later provisions or whether these provisions were legislated prior to entering into the tax treaty.

In favour of :

Assessee

Double taxation relief—Agreement between India and Israel—Royalty vis-a-vis payment for supply of software—Royalty is defined in art. 12(3) of the DTAA to mean 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, any patent, trademark, secret formula or process, etc.—Connotations of "use of copyright" of a work are distinct from the use of a copyrighted article—Meaning of "use of copyright of a work" cannot be treated as extending to "use of a copyrighted work" as this would amount to doing clear violence to the words employed by the treaty—Copyright is one thing and copyrighted article is quite another thing—It is not the Revenue's case that any of the in-built rights which constitute copyright have been transferred by the assessee—Therefore, payment for software cannot be treated as payment for use of copyright in the software—Further, when someone pays for the software he actually pays for a product which gives certain results, and not the process of execution of instructions embedded therein—Thus, the stand of the Revenue to the effect that the payment for software is de facto a payment for process cannot be accepted—Moreover, the expression 'process' appears immediately after and in the company of the expressions "any patent, trademark, design or model, plan, secret formula" which indicate that they are used in their cognate sense—Viewed in this perspective, 'process' has to be understood in the nature of know-how and not a product—Therefore, the payment for software, by no stretch of logic can be treated as a payment for a "process" liable to be taxed as royalty

Held :

It is an admitted position that the assessee did not have any PE in India in terms of the provisions of art. 5 of the tax treaty, and, accordingly, the assessee cannot be held liable to be taxed in respect of business profits, under art. 7, on supply of software in question.

(Para 14)

In terms of the provisions of art. 12(3) of the Indo-Israel tax treaty, royalty is defined, for the purposes of this tax treaty, as "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, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience". The provisions of art. 12(3) specifically provide, what is liable to be treated as royalty is payment for "use of, or the right to use, any copyright of literary, artistic or scientific work", and the connotations of "use of copyright" of a work are distinct from the use of a copyrighted article. The meaning of "use of copyright of a work" cannot be treated as extending to "use of a copyrighted work" as well, as it would amount to doing clear violence to the words employed by the treaty. Copyright is one thing, and copyrighted article is quite another thing. The four rights which, if acquired by the transferee, constitute him the owner of a copyright are : (i) the right to make copies of the computer programme for purposes of distribution to the public by sale or other transfer of ownership, or by rental, lease, or lending; (ii) the right to prepare derivative computer programmes based upon the copyrighted computer programme; (iii) the right to make a public performance of the computer programme; (iv) the right to publicly display the computer programme. It is not even Revenue's case that any of these rights have been transferred by the assessee, on the facts of this case, and, for this reason, the payment for software cannot be treated as payment for use of copyright in the software. Provisions of cl. (v) in Explan. 2 to s. 9(1)(vi) also cover consideration for "transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work"—a provision which is clearly larger in scope than the provision of art. 12(3) of the Indo-Israel tax treaty. The word "of" between 'copyright' and 'literary, artistic or scientific work' is also missing in the statutory provision. The treaty provision are thus certainly not in pari materia with this statutory provision, and, by the virtue of s. 90(2) the provisions of India Israel tax treaty clearly override this statutory provision.—[Motorola Inc. vs. Dy. CIT](#) (2005) 96 TTJ (Del)(SB) 1 **followed**; [Gracemac Corporation vs. Asstt. Director of IT](#) (2010) 134 TTJ (Del) 257 : (2010) 47 DTR (Del)(Trib) 65 : (2010) 42 SOT 550 (Del) **not followed**.

(Paras 15 to 17)

When someone pays for the software, he actually pays for a product which gives certain results, and not the process of execution of instructions embedded therein. As a matter of fact, under standard terms and conditions for sale of software, the buyer of software is not even allowed to tinker with the process on the basis of which such software runs or to even work around the technical limitations of the software. Therefore, the stand of the Revenue to the effect that the payment for software is de facto a payment for process cannot be approved. That is a hyper-technical approach totally divorced from the ground business realities. It is also important to bear in mind the fact that the expression 'process' appears immediately after, and in the company of, expressions "any patent, trademark, design or model, plan, secret formula or process". These expressions are used together in the treaty and as it is well-settled, that when two or more words which are susceptible to analogous meaning are used together they are deemed to be used in their cognate sense. They take, as it were, their colours from each other, the meaning of more general being restricted to a sense analogous to that of less general. This principle of interpretation of statutes, holds equally good for interpretation of a treaty provision. Viewed in this perspective, and taking note of lowest common factors in all the items covered by definition of the expression 'royalty' in art. 12(3), the 'process' has to be in the nature of know-how and not a product. In this view of the matter the payment for software, by no stretch of logic, can be treated as a payment for "a process" liable to be taxed as royalty.—[Asia Satellite Telecommunications Co. Ltd. vs. Director of IT](#) (2011) 238 CTR (Del) 233 : (2011) 51 DTR (Del) 1 : (2011) 332 ITR 340 (Del) **relied on**.

(Paras 17 & 18)

Conclusion :

Payment for supply of software simpliciter can neither be treated as payment for use of copyright in the software nor a payment for a process and, therefore, the amount received by the assessee, an Israeli company, from an Indian company for supply of software is not liable to be taxed as

royalty within the meaning of art. 12(3) of the Indo-Israel DTAA.

In favour of :

Assessee

Appeal (Tribunal)—Precedent—Decision of Co-ordinate Bench—A Co-ordinate Bench decision, which is admittedly contrary to earlier precedents on the issue from other Co-ordinate Benches, does not bind the subsequent Co-ordinate Benches—Further, a decision of Special Bench coming from a Bench of larger strength, prevails over the Division Bench decision—[CIT vs. B.R. Constructions](#) (1993) 113 CTR (AP) 1 : (1993) 202 ITR 222 (AP) applied

(Para 19)

Conclusion :

A Co-ordinate Bench decision, which is admittedly contrary to earlier precedents on the issue from other Co-ordinate Benches, does not bind the subsequent Co-ordinate Benches.

Cases referred to

Ambika Prasad Mishra vs. State of UP AIR 1980 SC 1762

Asia Satellite Telecommunications Co. Ltd. vs. Dy. CIT (2003) 78 TTJ (Del) 489

CIT vs. P.V.A.L. Kulandagan Chettiar (Dead) Through LRs (2004) 189 CTR (SC) 193 : (2004) 267 ITR 654 (SC)

CIT vs. Thana Electricity Supply Ltd. (1993) 112 CTR (Bom) 356 : (1994) 206 ITR 727 (Bom)

Dy. CIT vs. UHDE GmbH (1996) 54 TTJ (Mumbai) 355

Hewlett-Packard (India) (P) Ltd. vs. ITO (2006) 5 SOT 660 (Bang)

ISBC Consultancy Services Ltd. vs. Dy. CIT (2004) 83 TTJ (Mumbai) 597 : (2004) 88 ITD 134 (Mumbai)

Lotus Development (Asia Pacific) Pte Ltd (ITA Nos 564 to 566/Del/2005)

Lucent Technologies Hindustan Ltd. vs. ITO (2004) 82 TTJ (Bang) 163 : (2005) 92 ITD 366 (Bang)

Samsung Electronics Co. Ltd. vs. ITO (2005) 93 TTJ (Bang) 658

Sonata Information Technology Ltd. vs. Addl. CIT (2007) 106 TTJ (Bang) 797 : (2006) 103 ITD 324 (Bang)

Tata Consultancy Services vs. State of Andhra Pradesh (2004) 192 CTR (SC) 257 : (2004) 271 ITR 401 (SC)

Counsel appeared :

C.G.K. Nair, **for the Appellant** : Jitendra Jain, **for the Respondent**

ORDER**Pramod Kumar, A.M. :**

By way of this appeal, the AO has called into question correctness of CIT(A)'s order dt. 24th Feb., 2010, in the matter of assessment under s. 143(3) of the IT Act, 1961, for the asst. yr. 2006-07.

2. In the first ground of appeal, the AO has raised the following grievance :

"On the facts and in the circumstances of the case and in law, the learned CIT(A) erred in holding that the AO wrongly held that the amount of Rs 3,00,44,506 received by the assessee for the supply of software is in the nature of 'royalty' which is liable for taxation in India."

3. While there is no dispute that the grievance so raised by the AO is fully covered by decision of a Co-ordinate Bench in assessee's own case in a preceding assessment year, for the reasons we will set out in a short while, it is perhaps appropriate and desirable to deal with the issue at some length.

4. The relevant material facts, as culled out from the material on record before us, are like this. The assessee is a company incorporated in, and tax resident of, the State of Israel. The assessee company has its registered office at 12 Amal Street, Afek Park, Rosh Ha'ayain, Israel 48092, and it does not have any office, or PE in any other manner, in India. As evident from material on record, there is no dispute also that the assessee is eligible for benefits of India Israel DTAA [(2002) 254 ITR (St) 245; 'Indo-Israel tax treaty', in short]. On 17th Sept., 2002, the assessee entered into an agreement with Reliance Infocomm Ltd. (RIL, in short), for supply and licence of software for RIL's wireless network in India. Under the said agreement, RIL placed the two purchase orders, i.e. PO 13009821 and 13009823—both dt. 17th Sept., 2002, for US \$ 25,84,300 and US \$ 6,65,880 respectively. While the first purchase order for US \$ 25,84,300 was executed in the accounting period relevant to the asst. yr. 2003-04, the second purchase order for US \$ 6,65,880 was executed in the accounting period relevant to this assessment year. This is also not in dispute that by the virtue of the agreement referred to above the assessee has granted to RIL, and its affiliates, a perpetual, irrevocable, non-exclusive, royalty-free, worldwide licence to instal, use, operate or copy the software and the documentation licensed under the agreement solely for implementation, operation, management and maintenance of RIL's network within India. The assessee filed an IT return for the relevant assessment year, disclosing nil income and contending that no part of its income, in the absence of a permanent establishment (PE) in India, is taxable in India. In the course of the assessment proceedings, the AO noted that the assessee has invoiced a sum of US \$ 6,65,880 in the relevant accounting period, which is taxable in this assessment year. The AO noted the contention of the assessee to the effect that the payment received for supply of software was in the nature of business profits which could only be taxed under art. 7 of India Israel DTAA as business income, but since assessee does not have a PE, in terms of art. 5 of India-Israel DTAA, its business profits could not be taxed in India at all. It was also contended that in any event the assessee has merely raised an invoice but, till the end of the relevant accounting period, the assessee has not received any payments for the said invoice. It was also contended that, in view of jurisdictional Tribunal's decision in the case of Dy. CIT vs. UHDE GmbH (1996) 54 TTJ (Mumbai) 355, the amount so invoiced is not taxable in this assessment year. The AO took note of these submissions as also of assessee's reliance on a large number of judicial precedents, including in the cases of Tata Consultancy Services vs. State of Andhra Pradesh (2004) 192 CTR (SC) 257 : (2004) 271 ITR 401 (SC), Sonata Information Technology Ltd. vs. Dy. CIT (2006) 7 SOT 465 (Mumbai), Samsung Electronics Co. Ltd. vs. ITO (2005) 93 TTJ (Bang) 658, Lucent Technologies Hindustan Ltd. vs. ITO (2004) 82 TTJ (Bang) 163 : (2005) 92 ITD 366 (Bang), Hewlett-Packard (India) (P) Ltd. vs. ITO (2006) 5 SOT 660 (Bang), Lotus Development (Asia Pacific) Pte Ltd (unreported Tribunal Delhi Bench decision; ITA Nos 564 to 566/Del/2005), Sonata Information Technology Ltd. vs. Addl. CIT (2007) 106 TTJ (Bang) 797 : (2006) 103 ITD 324 (Bang), ISBC Consultancy Services Ltd. vs. Dy. CIT (2004) 83 TTJ (Mumbai) 597 : (2004) 88 ITD 134 (Mumbai), and the AO further

noted the fact that in the asst. yr. 2003-04, the same issue has been decided in favour of the assessee by the CIT(A). However, as the AO noted, since the order of the CIT(A) is contested in appeal before the higher authorities, the amount in respect of supply of software was considered taxable in the hands of the assessee. Accordingly, this amount of US \$ 6,65,880, which worked out to Rs 3,00,44,506, was brought to tax in the hands of the assessee. Aggrieved by the stand so taken by the AO, assessee carried the matter in appeal before the CIT(A). Learned CIT(A) inter alia noted that the assessee, being a tax resident of Israel, is entitled to the benefits of India Israel DTAA, which override the provisions of the IT Act to the extent the same are beneficial to the assessee. The provisions of the India Israel DTAA were, accordingly, applied. In an erudite and detailed order, following inter alia the Special Bench decision in the case of Motorola Inc. vs. Dy. CIT (2005) 96 TTJ (Del)(SB) 1, learned CIT(A) concluded that under the agreement, the assessee only parted with a copy of software program and not "any copyright over such software as envisaged by s. 14 of the Copyright Act". Under the circumstances, according to the learned CIT (A), payment made by RIL to the assessee could not be said to be a "payment for the use of, or right to use of, copyright". The CIT(A) thus held that the payment amounted to payment for "purchase of copyright material" which does not amount to royalty within the meaning of art. 12(3) of the India Israel DTAA. It was on this basis that the CIT(A) deleted the impugned addition of Rs. 3,00,44,506. The AO is aggrieved of the relief so given by the CIT(A) and is in appeal before us.

5. In the meantime, the AO's appeal, in assessee's own case and on the very same issue for the asst. yr. 2003-04, came up before a Co-ordinate Bench of this Tribunal, and, vide order dt. 13th April, 2010, the Co-ordinate Bench rejected the grievance of the AO. While doing so, the Co-ordinate Bench extensively quoted from the order of the CIT(A) and rather succinctly observed as follows :

"9. As can be seen from the above discussion of the CIT(A) the factual position as per the agreements and the legal position with reference to the supply of software for use was analysed in detail. Various Co-ordinate Benches have already analysed and noted the difference between the purchase of copyrighted article and transfer of copyrights. We are in agreement with the findings of the CIT(A), who has correctly come to the conclusion that the supply of software to Reliance does not amount to any transfer of copyright and payment can be only for purchase of copyrighted article and does not amount to royalty within the meaning of art. 12(3) of the DTAA. Consequently the order of the CIT(A) is upheld. Revenue appeal is dismissed."

6. When this appeal was called out for hearing, learned Departmental Representative fairly accepted that the issue is covered in favour of the assessee by Tribunal's order in assessee's own case, but he nonetheless dutifully relied upon the order of the AO and justified the same. Learned counsel for the assessee, on the other hand, took us through the order of the Co-ordinate Bench in assessee's own case and submitted that the issue in appeal before us was squarely covered by the same. It was also pointed out that the contract for supply of software was the same, as in the asst. yr. 2003-04, and the income in the asst. yrs. 2003-04 and 2006-07, i.e. assessment year before us, was on the same set of material facts. It was submitted that there was not even slightest change in facts of the case or in the applicable legal position, and that it cannot indeed be open to the Tribunal to take different views on the income arising to the assessee under the same contract in different assessment years particularly as there was no change in the legal position or the material facts. However, when learned counsel's attention was invited to a later decision of the Co-ordinate Bench in the case of Gracemac Corporation vs. Asstt. Director of IT (2010) 134 TTJ (Del) 257 : (2010) 47 DTR (Del)(Trib) 65 : (2010) 42 SOT 550 (Del), which holds that even the sale of copyrighted software, without sale of or right to use of copyright, could be treated as royalty in terms of materially identical tax treaty provision, it was submitted that the said decision was contrary to the law laid down by a large number of decisions by other Co-ordinate Benches as also by the Special Bench decision in the case of Motorola Inc. (supra). It was submitted that the issue is directly covered by the said Special Bench decision which overrides the decisions of the Co-ordinate Benches, i.e. Division Benches, under the rule of precedence. Learned counsel politely submitted that once there is a Larger Bench decision, which is directly on the issue, and the same

is not overturned by a higher judicial forum, the Division Benches are duty-bound to follow the same in preference over other decisions from other Division Benches. Learned counsel took us through the Co-ordinate Division Bench's decision in the case of Gracemac (supra), read out the operative portion where Motorola decision (supra) is sought to be distinguished, pointed out, what he perceived as, the apparent fallacies in the process of this distinction having been made out, and left it to us to consider whether we would follow the Special Bench and Co-ordinate Bench in assessee's own case, or whether we would follow a later Division Bench decision in Gracemac's case (supra). Taking a clue from these proceedings, learned Departmental Representative urged us to follow the Gracemac decision (supra). He submitted that Gracemac decision (supra), being a later decision, should be followed in preference over earlier decision in assessee's own case. When it was pointed out to him that Gracemac decision (supra) was contrary to the law laid down by Special Bench of this Tribunal in the case of Motorola Inc. (supra), which is a binding precedent for us, learned Departmental Representative submitted that the later Division Bench in Gracemac's case has followed Hon'ble Supreme Court's judgments (in the cases of Gramophone Co. of India Ltd vs. V.B. Pandey AIR 1984 SC 667 and CIT vs. P.V.A.L. Kulandagan Chettiar (Dead) Through LRs (2004) 189 CTR (SC) 193 : (2004) 267 ITR 654 (SC) which have greater binding force than the decision of a Special Bench, we must follow the Co-ordinate Bench's order in Gracemac Corporation's case (supra) in preference over the Special Bench decision in the case of Motorola Inc. (supra). He submits that the law laid down by Hon'ble Supreme Court in these cases, i.e. Gramophone Co of India Ltd. (supra) and P.V.A.L. Kulandagan Chettiar (supra), must prevail over the Special Bench decision. Learned Departmental Representative, who had almost given up his case in his first round of arguments, was now vehement in his reliance on the stand of the AO and supportive of the line of reasoning adopted by the Co-ordinate Bench in Gracemac's case (supra). None of these decisions, learned Departmental Representative pointed out, was considered by the CIT(A) or even the Co-ordinate Bench in the preceding year. He also took us through the observations made in Gracemac decision (supra), and the manner in which earlier decisions on the same issue, in favour of the assessee, were distinguished in detail. A reference was also made about press reports on a recent Supreme Court judgment which is said to have held that despite secrecy clause in Indo-German tax treaty, the information obtained from German tax authorities could not have been withheld from public. He urged us to vacate the order of the CIT(A) and restore that of the AO.

7. We have duly considered all these submissions, carefully perused the material before us and conscientiously deliberated upon the applicable legal position as also factual matrix of the case.

8. We find that the assessee is a tax resident of Israel and, in terms of the Indo-Israel tax treaty, the assessee is covered by the provisions of the said tax treaty. As to the extent to which provisions of the tax treaty will govern the taxability of such an assessee, the law is unambiguous as s. 90(2) provides that "where the Central Government has entered into an agreement with the Government of any country outside India under sub-s. (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee". In other words, in such a case, the provisions of applicable tax treaty will override the provisions of the IT Act, except to the extent the latter are more beneficial to the assessee. In the case of Union of India & Anr. vs. Azadi Bachao Andolan & Anr. (2003) 184 CTR (SC) 450 : (2003) 263 ITR 706 (SC), Hon'ble Supreme Court had an occasion to survey the judicial precedents on this issue and then conclude as follows :

".....A survey of the aforesaid cases makes it clear that the judicial consensus in India has been that s. 90 is specifically intended to enable and empower the Central Government to issue a notification for implementation of the terms of a DTAA. When that happens, the provisions of such an agreement, with respect to cases to which where they apply, would operate even if inconsistent with the provisions of the IT Act. We approve of the reasoning in the decisions which we have noticed. If it was not the intention of the legislature to make a departure from the general principle of chargeability to tax under s. 4 and the general principle of ascertainment of total income under

s. 5 of the Act, then there was no purpose in making those sections 'subject to the provisions' of the Act. The very object of grafting the said two sections with the said clause is to enable the Central Government to issue a notification under s. 90 towards implementation of the terms of the DTAs which would automatically override the provisions of the IT Act in the matter of ascertainment of chargeability to income-tax and ascertainment of total income, to the extent of inconsistency with the terms of the DTAC."

9. As evident from a plain reading of s. 90, as also the esteemed views of Hon'ble Supreme Court, it is wholly immaterial whether the provisions of the IT Act are later provisions or whether these provisions were legislated prior to the tax treaty having been entered into. Once a tax treaty is entered into, and is notified by the Central Government, the provisions of the IT Act have to make way for the provisions of the tax treaty, wherever these provisions are in conflict with the provisions of the tax treaty-unless, of course, when the provisions of the IT Act are more favourable to the assessee vis-a-vis the corresponding provisions of the tax treaty. It is important to bear in mind the fact that this unqualified treaty override is not due to operation of any provisions of the general law or convention, but by the virtue of a specific provision to that effect in the IT Act itself. The Indian IT Act itself restricts its application to a situation covered by the provisions of a tax treaty entered into, and duly notified, under the scheme of s. 90 of the IT Act. We must, at this stage, briefly deal with Hon'ble Supreme Court's judgment in the cases of *Gramophone Co. of India Ltd vs. V.B. Pandey* (supra). In *Gramophone Co.'s case* (supra), Hon'ble Supreme Court had an occasion to deal with the right of transit of goods through India, of our landlocked neighbour Nepal, under the international convention as also under the bilateral treaty, and the precise question which came up for consideration before Their Lordships was whether goods, which cannot be allowed to be imported into India due to copyright infringement law in force in India, could be allowed to be transited through India in deference to the right of passage of imports by Nepal. These basic facts are evident from the following opening observations made by their Lordships in the judgment :

"Nepal is our neighbour. Unfortunately Nepal is land-locked. Nepal's only access to the sea is across India. So, as one good neighbour to another with a view to `maintain, develop and strengthen the friendly relations between our two countries, by treaty and by International Convention, we allow a right of innocent passage in order to facilitate Nepal's international trade. One of the questions before us is the extent of this right : Does the right cover the transit of goods which may not be imported into India ? May goods which may not be brought into India be taken across Indian territory ? What does 'import' mean, more particularly what does 'import' mean in s. 53 of the Copyright Act ? Can an unauthorised reproduction of a literary, dramatic, musical or artistic work or a record embodying an unauthorised recording of a record (which, for short, adopting trade parlance, we may call a pirated work), whose importation into India may be prohibited, but whose importation into Nepal is not prohibited, be taken across Indian territory to Nepal ? These are some of the questions which arise for consideration in this appeal."

(Emphasis, by underlining, italicized in print, supplied by us)

10. It was in this context, and particularly in a situation in which an international convention and a bilateral treaty was being given effect to without there being any enabling provisions for such convention and treaty overriding the domestic legislation, that justice O Chenappa Reddy, in his inimitable manner, observed as follows :

"There can be no question that nations must march with the international community and the municipal law must respect rules of international law even as nations respect international opinion. The comity of Nations requires that rules of international law may be accommodated in the municipal law even without express legislative sanction provided they do not run into conflict with Acts of Parliament. But when they do run into such conflict, the sovereignty and the integrity of the Republic and the supremacy of the constituted legislatures in making the laws may not be subjected to external rules except to the extent legitimately accepted by the constituted

legislatures themselves. The doctrine of incorporation also recognises the position that the rules of international law are incorporated into national law and considered to be part of the national law, unless they are in conflict with Act of Parliament. Comity of Nations or no, municipal law must prevail in case of conflict. National Courts cannot say yes if Parliament has said no to a principle of international law. National Courts will endorse international law but not if it conflicts with national law. National Courts being organs of the National State and not organs of international law must perforce apply national law if international law conflicts with it. But the Courts are under an obligation within legitimate limits, to so interpret the municipal statute as to avoid conformation with the comity of Nations or the well established principles of International law. But if conflict is inevitable, the latter must yield."

11. These observations only lay down the principle that the "rules of international law may be accommodated in the municipal law even without express legislative sanction provided they do not run into conflict with Acts of Parliament (emphasis, italicized in print, supplied by us by underlining) "but such an accommodation to rules of international law, by convention or by treaties, does not extend to the situations in which the provisions of domestic law are clearly contrary to the rules of international law. These observations have no bearing on a situation like the one before us, i.e. in the case of the IT Act, in which the Act itself provides that the provisions of a tax treaty, entered into, and duly notified under the scheme of, s. 90 will override the provisions of the Act. The observations made in Gramophone's case (supra) could have been relevant if the provisions of s. 90 were not on the statute book. Even in the absence of the provisions of s. 90, going by the rationale of Gramophone judgment, the provisions of tax treaty would have had application—though only to the extent the same does not come into conflict with the provisions of the IT Act. In the case before us, however, it is because of the provisions of s. 90(2), and not merely on account of the general principles of extending respect to international conventions and treaties, that the provisions of the tax treaty override the provisions of the IT Act. The observations made by Hon'ble Supreme Court, in the case of Gramophone Co. of India Ltd. (supra), are thus wholly irrelevant in the present context. As we say so, we are alive to the fact that a Co-ordinate Bench has indeed observed that "the later domestic tax legislation may override tax treaty provisions wherever there is irreconcilable conflict" and, in support of this proposition, relied upon Gramophone judgment. However, these observations were in the nature of obiter dicta , i.e. things said by the way, inasmuch as the Co-ordinate Bench was only dealing with a situation, as the bench put it, there was no conflict between the provisions of the treaty and the IT Act, but, assuming there was indeed a conflict, "we would like to deal with such a hypothetical situation". It is well settled in law that obiter dicta of Co-ordinate Benches are not binding (unlike the ratio), but they may be regarded as persuasive in a future decision. As observed by Hon'ble Bombay High Court, in the case of CIT vs. Thana Electricity Supply Ltd. (1993) 112 CTR (Bom) 356 : (1994) 206 ITR 727 (Bom), an obiter does not have a binding force, though it "may have some persuasive efficacy". Even as we hold the observations of the Bench with highest respect, though with respectful disagreement, we do not regard the observations made by the Bench as of binding force, in view of the peculiar circumstances in which these observations are made. That is one reason that despite a contrary ruling on this issue by a Co-ordinate Bench, we see no need to refer the matter to the Special Bench. Secondly, we have noted that Gracemac decision (supra) did not have the benefit of guidance by Hon'ble Supreme Court's direct judgment on the issue of treaty override, in the context of the provisions of the IT Act. There cannot obviously be any point in referring an issue to the Special Bench which is clearly covered by a direct decision on that issue by Hon'ble Supreme Court. With respect, but without hesitation, we, therefore, hold that Gramophone Co. of India Ltd's decision (supra), in our humble understanding, does not dilute the principle of treaty override implicit in the scheme of the IT Act and which has the approval of Hon'ble Supreme Court in Azadi Bachao Andolan's case (supra).

12. We may also briefly deal with a rather recent decision of Hon'ble Supreme Court in the case of Ram Jethmalani vs. Union of India 2011 TIOL SC 57 PIL to the extent this judgment deals with limitations on universal applicability of the principles of tax treaty override. One of the issues which came up for the consideration of their Lordships, in this case, was whether in view of the provisions

of art. 26 of India-German DTAA [(1997) 223 ITR (St) 130], Government of India was indeed forbidden from disclosing certain information it has received from the German Government, with regard to Indian account holders in banks based in Liechtenstein. Their Lordships rejected the stand of the Government and held that art. 26 does not prevent Government of India from disclosing this information because (a) the "information" that is referred to in art. 26 is that which is "necessary for carrying out the purposes of this agreement", i.e. the Indo-German DTAA, and this does not extend to "information regarding Indian citizens' bank accounts in Liechtenstein that Germany secures and shares that have no bearing upon the matters that are covered by the double taxation agreement between the two countries"; (b) "there is no absolute bar of secrecy. Instead the agreement specifically provides that the information may be disclosed in public Court proceedings, which the instant proceedings are", and (c) that the last sentence in art. 26(1) permitting disclosure of such secret information "in public Court proceedings or in judicial proceedings" must be so construed as not limiting it to disclosure in the income-tax proceedings only because such an approach will come in conflict with the scheme of the Constitution of India, granting every person a power to seek remedy against infringement of fundamental right under Part III of the Constitution, as "in order that the right guaranteed by cl. (1) of Art. 32 be meaningful, and particularly because such petitions seek the protection of fundamental rights, it is imperative that in such proceedings the petitioners are not denied the information necessary for them to properly articulate the case and be heard, especially where such information is in the possession of the State". Their Lordships further observed that "to deny access to such information, without citing any constitutional principle or enumerated grounds of constitutional prohibition, would be to thwart the right granted by cl. (1) of art. 32". The law so laid down by their Lordships does not, in any way, dilute the principles of tax treaty override, even as their Lordships observe that when Courts have to interpret the provisions of tax treaty, they must not do so in such a manner as to come in conflict with the basic structure of the Constitution of India. This observation cannot, in our humble understanding, be construed as limiting the principles of tax treaty override either. As a matter of fact, their Lordships, later in the judgment, have observed that "we have perused the documents in question, and heard the arguments of Union of India with respect to the double taxation agreement with Germany as an obstacle to disclosure" and rejected these arguments, in the immediately following sentence, by observing that "we do not find merit in its arguments flowing from the provisions of double taxation agreement with Germany". It was on interpretation of the treaty provisions, rather than on rejecting the applicability of treaty provisions, that in Ram Jethmalani's case (supra), the Government of India's stand for non-disclosure of names of persons holding accounts in Liechtenstein. This judgment cannot, therefore, be seen as diluting the principles of tax treaty override.

13. In view of the above discussions, as long as the assessee cannot be subjected to tax on the impugned receipts in terms of the provisions of Indo-Israel tax treaty, the assessee will not have tax liability in India. The provisions of the IT Act, 1961, cannot be put into service in such a situation, because, as we have noticed earlier, these provisions can apply only when they are more beneficial to the assessee vis-a-vis the provisions of the applicable tax treaty.

14. It is an admitted position that the assessee did not have any PE in India in terms of the provisions of art. 5 of the tax treaty, and, accordingly, the assessee cannot be held liable to be taxed in respect of business profits, under art. 7, on supply of software in question. The case of the Revenue really rests on taxability under art. 12 which provides as follows :

"Royalties

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 recipient is the beneficial owner of the royalties, the tax so charged shall not exceed 10 per cent of the gross amount of the royalties.

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, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

4. The provisions of paras 1 and 2 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a PE situated therein, or perform in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with such PE or fixed base. In such case, the provisions of art. 7 or art. 15, as the case may be, shall apply.

5. Royalties shall be deemed to arise in a Contracting State when the payer is that State itself, a political sub-division, a local authority or a resident of that State. Where, however, the person paying the royalties, whether he is a resident of a Contracting State or not, has in a Contracting State a PE or a fixed base in connection with which the liability to pay the royalties was incurred, and such royalties are borne by such PE or fixed base, then such royalties shall be deemed to arise in the State in which the PE or fixed base is situated.

6. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this article shall apply only to the lastmentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention."

15. In terms of the provisions of art. 12(3) of the Indo-Israel tax treaty, royalty is defined, for the purposes of this tax treaty, as "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, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience". The question then arises whether a payment for computer software cannot be a payment for use of or right to use of 'a copyright of literary, artistic or scientific work, including cinema photographic film', and, while examining this question, it is important to bear in mind the fact that there is a specific mention about the use "of" copyright. The only other clause in which payment for software could possibly fall is "consideration for use of, or right to use of, a "process". Let us examine these two aspects of the definition of 'royalty' under the India-Israel tax treaty.

16. As regards the question whether the payment for software could be treated as payment for "use of, or the right to use, any copyright of literary, artistic or scientific work", we find that this issue directly came up for consideration of a Special Bench of this Tribunal in the case of Motorola Inc. (supra). That was a case in which the Special Bench had an occasion to decide whether payment for software amounts to 'royalty', for the purposes of India Sweden tax treaty [(1998) 229 ITR (St) 11] which incidentally is the same as in Indo-Israel tax treaty and which also defines royalty as "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, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience". The Special Bench, after a very erudite discussion on various facets of the issue before them, concluded that "we hold that the software supplied was a copyrighted article and not a copyright right, and the payment received by the assessee in respect of the software cannot, therefore, be considered as royalty either under the IT Act or the DTAA". Right now we are only concerned with the provisions of the tax treaty, and we have noticed that the provisions of tax treaty as before the Special Bench are exactly the same as before us in this case. The issue, therefore, as to whether payment for supply of software can be viewed as a

payment for copyright or not is no longer *res integra*. The Special Bench has decided this issue in favour of the assessee, and the views so expressed by the Special Bench, being from a higher forum than this Division Bench, are binding on us. In any case, as the provisions of art. 12(3) specifically provide, what is liable to be treated as royalty is payment for "use of, or the right to use, any copyright of literary, artistic or scientific work", and the connotations of "use of copyright" of a work are distinct from the use of a copyrighted article. The meaning of "use of copyright of a work" cannot be treated as extending to "use of a copyrighted work" as well, as it would amount to doing clear violence to the words employed by the treaty. Copyright is one thing, and copyrighted article is quite another thing. To give a simple example, when a person is using a music compact disc, that person is using the copyrighted article, i.e. the product itself, and not the copyright in that product. As held by the Special Bench in Motorola's case (*supra*), the four rights which, if acquired by the transferee, constitute him the owner of a copyright right, and these rights are :

- (i) The right to make copies of the computer programme for purposes of distribution to the public by sale or other transfer of ownership, or by rental, lease, or lending.
- (ii) The right to prepare derivative computer programmes based upon the copyrighted computer programme.
- (iii) The right to make a public performance of the computer programme.
- (iv) The right to publicly display the computer programme.

17. It is not even Revenue's case that any of these rights have been transferred by the assessee, on the facts of this case, and, for this reason, the payment for software cannot be treated as payment for use of copyright in the software. As we hold so, we may mention that in the case of *Gracemac* (*supra*), a contrary view has been taken but that conclusion is arrived at in the light of the provisions of cl. (v) in Explan. 2 to s. 9(1)(vi) which also covers consideration for "transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work" a provision which is clearly larger in scope than the provision of art. 12(3) of the Indo-Israel tax treaty. The word "of" between 'copyright' and 'literary, artistic or scientific work' is also missing in the statutory provision. The treaty provision that we are dealing with are thus certainly not *in pari materia* with this statutory provision, and, by the virtue of s. 90(2) of the Act, the provisions of India Israel tax treaty clearly override this statutory provision. In *Gracemac* decision (*supra*), the Co-ordinate Bench was of the view that the provisions of the applicable tax treaty and the IT Act are "identical"—a position which does not prevail in the situation before us. We, therefore, see no reasons to be guided by *Gracemac* decision (*supra*). The next issue that we need to consider is whether a payment for software can be said to be a payment for "process" as a computer program is nothing but a set of instruction lying in the passive state and this execution of instructions is 'a process' or 'a series of processes'. No doubt, in terms of the provisions of s. 2(ffc) of the Indian Copyright Act, 1957, a computer program, i.e. software, has been defined as "a set of instructions expressed in words, codes, schemes or in any other form, including a machine readable medium, capable of causing a computer to perform a particular task or achieve a particular result", but the moot question is as to what is that a customer pays for when he buys, or to put it in technical terms 'obtains licence to use' the software—for the process of executing the instructions in the software, or for the results achieved on account of use of the software. To draw an analogy, it is akin to a situation in which a person hires a vehicle, and the question could be as to what does he pay for—for the use of the technical know-how on the basis of which vehicle operates, or for the use of a product which carries passengers or goods from one place to another. The answer is obvious. When you pay for use of vehicle, you actually pay for a product which carries the passengers or goods from one place to another and not the technical know-how on the basis of which such a product operates. Same is the case with the software, when someone pays for the software, he actually pays for a product which gives certain results, and not the process of execution of instructions embedded therein. As a matter of fact, under standard terms and conditions for sale of software, the buyer of software is not even allowed to tinker with the process

on the basis of which such software runs or to even work around the technical limitations of the software. In *Asia Satellite Telecommunications Co. Ltd. vs. Dy. CIT* (2003) 78 TTJ (Del) 489, a Co-ordinate Bench of this Tribunal did take the view that when an assessee pays for transponder hire, he actually pays for the process inasmuch as transponder amplifies and shifts the frequency of each signal, and, therefore, payment for use of transponder is in fact a payment for process liable to be treated as 'royalty' within meaning of that expression under Explan. 2 to s. 9(1)(vi) of the IT Act. However, when this decision came up for scrutiny of Hon'ble Delhi High Court, in the case reported as *Asia Satellite Telecommunications Co. Ltd. vs. Director of IT* (2011) 238 CTR (Del) 233 : (2011) 51 DTR (Del) 1 : (2011) 332 ITR 340 (Del), their Lordships, after a very erudite and detailed discussion, concluded that "we are unable to subscribe to the view taken by the Tribunal in the impugned judgment on the interpretation of s. 9(1)(vi) of the Act". It cannot, therefore, be open to us to approve the stand of the Revenue to the effect that the payment for software is de facto a payment for process. That is a hyper-technical approach totally divorced from the ground business realities. It is also important to bear in mind the fact that the expression 'process' appears immediately after, and in the company of, expressions "any patent, trademark, design or model, plan, secret formula or process". We find that these expressions are used together in the treaty and as it is well-settled, as noted by Maxwell in *Interpretation of Statutes* and while elaborating on the principle of *noscitur a sociis*, that when two or more words which are susceptible to analogous meaning are used together they are deemed to be used in their cognate sense. They take, as it were, their colours from each other, the meaning of more general being restricted to a sense analogous to that of less general. This principle of interpretation of statutes, in our considered view, holds equally good for interpretation of a treaty provision. Explaining this principle in more general terms, a very distinguished former colleague of ours Hon'ble Shri M.K. Chaturvedi, had, in an article 'Interpretation of Taxing Statutes' (AIFTP Journal: Vol. 4 No. 7, July, 2002, at p. 7), put it in his inimitable words as follows :

"Law is not a brooding omnipotence in the sky. It is a pragmatic tool of the social order. The tenets of law being enacted on the basis of pragmatism. Similarly, the rules relating to interpretation are also based on commonsense approach. Suppose a man tells his wife to go out and buy bread, milk or anything else she needs, he will not normally be understood to include in the terms 'anything else she needs' a new car or an item of jewellery. The dictum of *ejusdem generis* refers to similar situation. It means of the same kind, class or nature. The rule is that when general words follow particular and specific words of the same nature, the general words must be confined to the things of same kind as specified. *Noscitur a sociis* is a broader version of the maxim *ejusdem generis*. A man may be known by the company he keeps and a word may be interpreted with reference to the accompanying words. Words derive colour from the surrounding words."

18. Viewed in this perspective, and taking note of lowest common factors in all the items covered by definition of the expression 'royalty' in art. 12(3), the 'process' has to be in the nature of know-how and not a product. In this view of the matter, and in view of Hon'ble Delhi High Court's declining to uphold the Co-ordinate Bench's decision in the case of *Asia Satellite Telecommunication Co Ltd.* (supra), we are of the considered view that the payment for software, by no stretch of logic, can be treated as a payment for "a process" liable to be taxed as royalty. This is precisely what was held by a Co-ordinate Bench of this Tribunal in the case of *Sonata Information Technology* (supra), though for different reasons.

19. On this aspect of the matter also, *Gracemac* decision (supra) has come to a different conclusion by opining that payment for software is in fact a payment for a process, but the view so expressed, being contrary to earlier decisions of the other Co-ordinate Benches and in accordance with the law laid down by Hon'ble Andhra Pradesh High Court in the case of *CIT vs. B.R. Constructions* (1993) 113 CTR (AP) 1 : (1993) 202 ITR 222 (AP) does not constitute a binding judicial precedent. In our considered view, even a Co-ordinate Bench decision, which is admittedly contrary to earlier precedents on that issue from other Co-ordinate Benches, does not bind the subsequent Co-ordinate Benches. We have all the respect and admiration for the Co-ordinate Bench decision, but, in our considered view, this decision does not constitute a binding judicial

precedent, and we leave it at that. The other aspect of the matter is that the issue of taxability of software, as a copyrighted article, is directly covered by a Special Bench of this Tribunal and the said decision, coming from a Bench of larger strength, prevails over the Division Bench decision. As laid down by the apex Court in the case of Ambika Prasad Mishra vs. State of UP AIR 1980 SC 1762 (p. 1764 of AIR 1980 SC) "every new discovery nor argumentative novelty cannot undo or compel reconsideration of a binding precedent. A decision does not lose its authority merely because it was badly argued, inadequately considered or fallaciously reasoned....". Therefore, whatever be the points, right or wrong, which can be put against the Special Bench decisions, the Special Bench decision continues to have a binding force on this Division Bench. In our humble understanding, the Special Bench decision in Motorola's case (supra) binds us and we have to respectfully follow the same. Respectfully following this Special Bench decision, as also a series of other Division Bench decisions on the same lines, we must approve the conclusions arrived at by the CIT(A).

20. In view of the above discussions, respectfully following Special Bench decision in Motorola's case (supra) as also a large number of Division Bench decisions on the issue, including in assessee's own case for one of the preceding assessment years, we approve the conclusions arrived at by the CIT(A) and decline to interfere in the matter.

21. In the result, the appeal is dismissed.

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