IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI E BENCH, MUMBAI
Before Shri Pramod Kumar (Accountant Member)
and Shri Vijay Pal Rao (Judicial Member)

ITA No. 3939/Mum/2010
Assessment year: 2006-07

Additional Director of Income Tax
(International Tax)- Range 2(2), Mumbai ………..………… Appellant

Vs.

TII Team Telecom International Pvt. Ltd. ………………… Respondent
c/oSudit Parekh & co.
Ballard Estate, 2nd floor, ADI Marzban Path,
Ballard Pier, Fort,
Mumbai.
[PAN : AACCT5300M]

Appearances:

C G K Nair, for the appellant
Jitendra Jain, for the respondent

Date of hearing : July 07, 2011
Date of pronouncement : August 26 , 2011

O R D E R

Per Pramod Kumar :

1. By way of this appeal, the Assessing Officer has called into question correctness of CIT(A)'s order dated 24th February 2010, in the matter of assessment under section 143(3) of the Income Tax Act, 1961, for the assessment year 2006-07.

2. In the first ground of appeal, the Assessing Officer 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 Assessing Officer 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 Assessing Officer is fully covered by decision of a coordinate 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 permanent establishment 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 Double Taxation Avoidance Agreement (254 ITR Stat 245; 'Indo Israel tax treaty', in short). On 17th September 2002, the assessee entered into an agreement with Reliance Infocomm Limited (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 dated 17th September 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 assessment year 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 is has granted to RIL, and its affiliates, a perpetual, irrevocable, non-exclusive, royalty free, worldwide licence to install, 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. Theassessee filed an income tax 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 Assessing Officer 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 Assessing Officer 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 Article 7 of India Israel DTAA as business income, but since assessee does not have a permanent establishment, in terms of Article 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 in 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 DCIT Vs UHDE GmbH (54 TTJ 355), the amount so invoiced is not taxable in this assessment year. The Assessing Officer 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 (271 ITR 401 SC), Sonata

Information Technology Ltd Vs DCIT (7 SOT 465), Samsung Electronics Co Ltd Vs ITO (93 TTJ 658), Lucent Technologies Hindustan Limited Vs ITO (92 ITD 366), Hawlett Packard India Pvt Ltd Vs ITO (5 SOT 660), Lotus Development (Asia Pacific) Pte Ltd (Unreported ITAT Delhi bench decision; ITA Nos 564 to 566/Del/05), Sonata Information Technology Ltd Vs ACIT (103 ITD 324), ISBC Consultancy Services Vs DCIT (88 ITD 134), and the Assessing Officer further noted the fact that in the assessment year 2003-04, the same issue has been decided in favour of the assessee by the CIT(A). However, as the Assessing Officer 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 Assessing Officer, 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 Income Tax 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 DCIT (96 TTJ 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 Section 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 Article 12 (3) of the India Israel DTAA. It was on this basis that the CIT(A) delete the impugned addition of Rs 3,00,44,506. The Assessing Officer is aggrieved of the relief so given by the CIT(A) and is in appeal before us.

5. In the meantime, the Assessing Officer’s appeal, in assessee’s own case and on the very same issue for the assessment year 2003-04, came up before a coordinate bench of this Tribunal, and, vide order dated 13th April 2010, the coordinate bench rejected the grievance of the Assessing Officer. 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 coordinate benches have already analysed and noted the difference between the purchase of copyrighted article and transfer of copy rights. 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 Article 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 Assessing Officer and justified the same. Learned counsel for the assese, on the other hand, took us though the order of the coordinate 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 assessment year 2003-04, and the income in the assessment year 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 year – 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 coordinate bench in the case of Gracemac Corporation Vs ADIT (42 SOT 550), 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 coordinate benches as also by the Special Bench decision in the case of Motorla Inc (supra). It was submitted that the issue is directly covered by the said Special Bench decision which overrides the decisions of the coordinate 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 thesame in preference over other decisions from other division benches. Learned counsel took us through the coordinate 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 coordinate bench in assessee's own case, or whether we would follow a later division bench in decision in Gracemac's case (supra). Taking a clue from these proceedings, learned Departmental Representative urged us to f ollow 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 PVAL Kulangadan Chettiar 267 ITR 654) which have greater binding force than the decision of a Special Bench, we must follow the coordinate 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 PVAL Kulangadan Chetiar (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 Assessing Officer and supportive of the line of reasoning adopted by the coordinate bench in Gracemac's case (supra). None of these decisions, learned Departmental Representative pointed out, was considered by the CIT(A) or even the coordinate bench in the preceding year. He also took us through the observations made in Gracemac decision, and the manner in which earlier decisions on the same issue, in favour of the assessee, weredistinguished 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 Assessing Officer.

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 Section 90 (2) provides that "where the Central Government has entered into an agreement with the Government of any country outside India under sub-section (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 Income Tax Act, except to the extent the latter are more beneficial to the assessee. In the case of Union of India Vs Azadi Bachao Andolan (263 ITR 706), Hon'ble Supreme Court had an occasionm 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 Double Taxation Avoidance Agreement. 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 theprinciple 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 Section 90, as also the esteemed views of Hon'ble Supreme Court, it is wholly immaterial whether the provisions of the Income Tax 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 Income Tax 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 Income Tax Act are more favourable to the assessee vis-à-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 Income Tax Act itself. The Indian Income Tax 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 Section 90 of the Income Tax Act. We must, at this stage, briefly deal with Hon'ble Supreme Court's judgments in the cases of Gramophone Co. of India Ltd Vs V B Pandey AIR 1984 SC 667. 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 neighbor 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 tothe 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 Sec. 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 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 legislatives anction 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 recognizes 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 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 nternational law. These observations have no bearing on a situation like the one before us, i.e. in the case of the Income Tax Act, in which the Act itself provides that the provisions of a tax treaty, entered into, and duly notified under the scheme of, Section 90 will override the provisions of the Act. The observations made in Gramophone’s case (supra) could have been relevant if the provisions of Section 90 were not on the statute book. Even in the absence of the provisions of Section 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 Income Tax Act. In the case before us,

however, it is because of the provisions of Section 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 Income Tax Act. The observations made by Hon'ble Supreme Court, in the case of Gramophone Company of India Ltd (supra), are thus wholly irrelevant in the present context. As we say so, we are alive to the fact that a coordinate 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 coordinate bench was only dealing with a situation, as the bench put it, there was no conflict between the provisions of the treaty and the Income Tax 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 coordinate benches are not binding (unlike the ratio), but they may be regarded as persuasive in a future decision. In observed by Hon'ble Bombay High Court, in the case of CIT Vs. Thana Electricity Supply Co Ltd (206 ITR 727), 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's one reason that despite a contrary ruling on this issue by a coordinate bench, we see no need to refer the matter to the special bench. Secondly, we have noted that Gracemac decision 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 Income Tax Act. There cannot obviously be any point in referring an issue to the Special Bench which is clearly covered by a direct decisions on that issue by Hon'ble Supreme Court. With respect, but without hesitation, we, therefore, hold that Gramophone Company of India Ltd's decision, in our humble understanding, does not dilute the principle of treaty override implicit in the scheme of the Income Tax 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 Article 26 of India German Double Taxation Avoidance Agreement (223 ITR Stat 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 Article 26 does not prevent Government of India from disclosing this information because (a) the "information" that is referred to in Article 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 Article 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 Clause (1) of Article 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 anyconstitutional principle or enumerated grounds of constitutional prohibition, would be to thwart the right granted by Clause (1) of Article 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 limited 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 Income Tax 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-à-vis the provisions of the applicable tax treaty.

14. It is an admitted position that the assessee did not have any permanent establishment in India, in terms of the provisions of Article 5 of the tax treaty,

and, accordingly, the assessee cannot be held liable to be taxed in respect of business profits, under Article 7, on supply of software in question. The case of the revenue really rests on taxability under Article 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, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

4. The provisions of paragraphs 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 permanent establishment 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 permanent establishment or fixed base. In such case, the provisions of Article 7 or Article 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 permanent establishment or a fixed base in connection with which the liability to pay the royalties was incurred, and such royalties are borne by such permanent establishment or fixed base, then such royalties shall be deemed to arise in the State in which the permanent establishment 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 suchb relationship, the provisions of this Article shall apply only to the last mentioned 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 Article 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, trade mark, 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 (229 ITR Stat 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, trade mark, 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 Article 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 clause (v) in Explanation 2 to Section 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 Article 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 Section 90(2) of the Act, the provisions of India Israel tax treaty clearly override this statutory provision. In Gracemac decision (supra), the coordinate bench was of the view that the provisions of the applicable tax treaty and the Income Tax 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 a 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 Section 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 knowhow 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 knowhow 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 Ltd Vs DCIT

(78 TTJ 489), a coordinate bench of this Tribunal did take the view that when an assessee pays for transponder hire, he actually pays for the a process inasmuch as transponder amplifies and shifts the frequency of each signal, and, therefore, payment for use of transponder is infact a payment for process liable to be treated as 'royalty' within meanings of that expression under Explanation 2 to Section 9 (1)(vi) of the Income Tax 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 DIT (332 ITR 340), Their Lordships, after a very erudite and detailed discussion, concluded that "we areunable to subscribe to the view taken by the Tribunal in the impugnedjudgment on the interpretation of Section 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, trade mark, 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 common-sense 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 Article 12(3), the 'process' has to be in the nature of knowhow and not a product.In this view of the matter, and in view of Hon'ble Delhi High Court's declining to uphold the

coordinate 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 coordinate 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 has come to a different conclusion by opining that payment for software is infact a payment for a process, but the view so expressed, being contrary to earlier decisions of the other coordinate 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 (202 ITR 222) does not constitute a binding judicial precedent. In our considered view, even a coordinate bench decision, which is admittedly contrary to earlier precedents on that issue from other coordinate benches, does not bind the subsequent coordinate benches. We have all the respect and admiration for the coordinate 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 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 Commissioner (Appeals) and decline to interfere in the matter.

21. In the result, the appeal is dismissed. Pronounced in the open court today on 26th day of August, 2011.

Sd/- sd/-

(Vijay Pal Rao) (Pramod Kumar)
Judicial Member Accountant Member
Mumbai; 26th day of August, 2011.

Copy forwarded to:
1. The appellant
2. The respondent
3. Director of Income Tax (International Taxation) , Mumbai
4. Commissioner (Appeals) II , Mumbai
5. Departmental Representative, E bench, Mumbai
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By Order etc.

Assistant Registrar
Income Tax Appellate Tribunal
Mumbai benches, Mumbai