

**CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL
MUMBAI**

WEST ZONAL BENCH

SERVICE TAX APPEAL NO: 88568 of 2014

[Arising out of Order-in-Original No: 54,55/ST/RN/CMR/MII/13-14 dated 15th May, 2014 passed by the Commissioner of Central Excise, Mumbai – II.]

InfrasoftTech India Ltd
Technosoft Knowledge Gateway Building,
B-14 Road No.1, Wagle Industrial Estate,
Thane (W) – 400 604

... Appellant

versus

Commissioner of Central Excise
Mumbai – II
9th Floor, Piramal Chambers, Jijobhoy Lane, Lalbaug
Mumbai – 400 012

...Respondent

APPEARANCE:

Shri RD Wagle, Advocate for the appellant

Shri Bidhan Chandra, Additional Commissioner (AR) for the respondent

CORAM:

HON'BLE MR C J MATHEW, MEMBER (TECHNICAL)
HON'BLE DR SUVENDU KUMAR PATI, MEMBER (JUDICIAL)

FINAL ORDER NO: A/85342 / 2020

DATE OF HEARING:	04/09/2019
DATE OF DECISION:	26/02/2020

PER: C J MATHEW

In the appeal of M/s InfrasoftTech India Ltd against order-in-
original no. 54,55/ST/RN/CMR/MII/13-14 dated 15th May 2014 of

Commissioner of Central Excise, Mumbai – II, covering the period from May 2008 to March 2011, challenge is to the recovery of ₹3,11,95,070/-, along with interest thereon, and imposition of penalty of like amount on what is claimed to be sale of software developed for their own use and marketed as ‘core banking’ software to their customers which was charged by service tax authorities to be liable as provider of ‘information technology software service’.

2. According to Learned Counsel, the appellant is involved in sale of ‘canned software’ produced by third parties and their own software deployed in the banking industry. He submits, that these activities are not in conformity with the description of the taxable service in section 65(105)(zzzzze) of Finance Act, 1994 and contends that the two show cause notices, dated 3rd October 2011 and 6th March 2012, are not in consonance with the principles of natural justice by having failed to invoke the specific sub-clause within the definition of the ‘taxable service’. Reliance is placed by him on the decision of the Hon’ble Supreme Court in *Gajanan Visheshwar Birjur v. Union of India (UOI) and Ors.* [1994 (72) ELT 788 (SC)], *Amrit Foods v. Commissioner of Central Excise, UP* [2005 (190) ELT 433 (SC)] and *Odyssey Organics P Ltd v. Commissioner of Central Excise, Raigad* [2017 (47) STR 289 (Tri.)]. Further, contending that the impugned order has travelled beyond the show cause notices by fastening liability under sub-clause (v) instead of sub-clause (i), he seeks that the order should be set aside.

3. Challenging the taxability itself under sub-clause (v) of section 65(105)(zzzzze), it is contended that the decision of the Hon'ble Supreme Court in *State Bank of India v. Collector of Customs, Bombay* [2000 (115) ELT 597 (SC)] that

'10. The purpose for the Press Note is two fold: (1) to bring down the prices of the imported software and (2) to save precious foreign exchange outflow on several copies of imported software. With this object in view, Central Government decided to allow duplication/reproduction of imported software in India. That being so duplication will not attract any excise duty. The royalty payable on duplicate copies of the software will be paid with the foreign exchange arranged by the party. No custom duty will be leviable on the royalty paid. But then the Indian party will ensure that the royalty paid for each copy is not more than what is being charged by the manufacturer/owner from other customers elsewhere in the world. Master copy imported for duplication purposes will be assessed to customs duty as per existing procedure. From the reading of the press note, it is apparent that it would apply when there is commercial exploitation of the imported software.'

should apply to them.

4. It is also contended further that there is no commercial exploitation by the appellant who merely make these available to their customers. Placing reliance on the decision of the Hon'ble High Court of Delhi in *Director of Income Tax v. Infrasoftware Ltd* [(2014) 220 TAXMAN 0273 (Del.)] which follows the decision in *Motorola Inc v.*

Deputy CIT (2005) 96 TTJ Delhi 1 as below

'157. We may first look at the supply contract itself to find out what JTM, one of the cellular operators, can rightfully do with reference to the software. We may remind ourselves that JTM is taken as a representative of all the cellular operators and that it was common ground before us that all the contracts with the cellular operators are substantially the same. Clause 20.1 of the Agreement, under the title "License", says that JTM is granted a non-exclusive restricted license to use the software and documentation but only for its own operation and maintenance of the system and not otherwise. This clause appears to militate against the position, if it were a copyright, that the holder of the copyright can do anything with respect to the same in the public domain. What JTM is permitted to do is only to use the software for the purpose of its own operation and maintenance of the system. There is a clear bar on the software being used by JTM in the public domain or for the purpose of commercial exploitation.

158. Secondly, under the definition of "copyright" in Section 14 of the Copyright Act, the emphasis is that it is an exclusive right granted to the holder thereof. This condition is not satisfied in the case of JTM because the license granted to it by the assessee is expressly stated in Clause 20.1 as a "non exclusive restricted license". This means that the supplier of the software, namely, the assessee, can supply similar software to any number of cellular operators to which JTM can have no objection and further all the cellular operators can use the software only for the purpose of their own operation and maintenance of the system and not for any other purpose. The user of the software by the cellular operators in the public domain is totally prohibited, which is evident from the use of the words in Article 20.1 of the

agreement, "restricted" and "not otherwise". Thus JTM has a very limited right so far as the use of software is concerned. It needs no repetition to clarify that JTM has not been given any of the seven rights mentioned in Clause (a) of Section 14 or the additional right mentioned in Sub-clause (ii) of Clause (b) of the section which relates to a computer programme and, therefore, what JTM or any other cellular operator has acquired under the agreement is not a copyright but is only a copyrighted article.

162. A conjoint reading of the terms of the supply contract and the provisions of the Copyright Act, 1957 clearly shows that the cellular operator cannot exploit the computer software commercially which is the very essence of a copyright. In other words a holder of a copyright is permitted to exploit the copyright commercially and if he is not permitted to do so then what he has acquired cannot be considered as a copyright. In that case, it can only be said that he has acquired a copyrighted article. A small example may clarify the position. The purchaser of a book on income-tax acquires only a copyrighted article. On the other hand, a recording company which has recorded a vocalist has acquired the copyright in the music rendered and is, therefore, permitted to exploit the recording commercially. In this case the music recording company has not merely acquired a copyrighted article in the form of a recording, but has actually acquired a copyright to reproduce the music and exploit the same commercially. In the present case what JTM or any other cellular operator has acquired under the supply contract is only the copyrighted software, which is an article by itself and not any copyright therein.

168. The actual regulations bring out the distinction very clearly between the copyright right and a copyrighted article. They also specify the four rights which, if acquired

by the transferee, constitute him the owner of a copyright right. They 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 publically display the computer programme.*

184. In view of the foregoing discussion, 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 be considered as royalty either under the Income-tax Act or the DTAA.'

it is the contention of Learned Counsel that the detailed exposition should place the activities of the appellant beyond the pale of the said sub-clause. Inviting our attention to circular no. 354/89/TRU dated 4th November 2009 of the Central Board of Excise & Customs clarifying that

'6. Accepting their plea, in Budget 2009, two parallel notifications were issued on the excise and customs side. Vide notification no. 22/2009-C.E., dated 7-7-2009, partial exemption from excise duty was provided to packaged or canned software on that portion of the value which represents

the consideration for the transfer of the right to use for commercial exploitation, as on this portion, service tax would be leviable under the ITSS. Similar exemption from CVD was provided vide notification No. 80/2009-Customs dated 7-7-2009 on such software. These exemptions were notified to ensure that while importing or manufacturing packaged software, the importer/manufacture is spared from paying customs duty/excise duty on the value attributable to transfer of 'right to use'.

as elaboration of the intent to tax, he discountenances the stand of the adjudicating authority.

5. According to Learned Authorised Representative, the product of the appellant is covered by section 65(53a) of Finance Act, 1994 defining 'information technology software' as

'any representation of instructions, data, sound or image, including source code and object code, recorded in a machine readable form, and capable of being manipulated or providing interactivity to a user, by means of a computer or an automatic data processing machine or any other device or equipment;'

and as the show cause notices have enumerated the various activities, all of which lie within the ambit of the said definition, the failure to crystalize the sub-clause is not fatal to the proceedings for which reliance is placed on the decision of the Hon'ble Supreme Court in *Collector of Central Excise, Calcutta v. Pradyumna Steel Ltd [1996 (82) ELT 441 (SC)]*. Further, according to him, perpetual licensing of

software can be inferred from the contract which explicitly permits commercial exploitation and that tweaking of the generic product for use by the banking industry to take care of new requirements constitutes ‘customized software’ which is within the scheme of tax liability. Attention was drawn to the impugned order which has rendered the finding that

‘22.2. From a combined reading of the above restrictions and terms it is obvious that above restrictions imposed on the client are of such a nature that they are restricting the right of free enjoyment of the software in the same way as a purchaser of goods is able to have. Therefore, it is not a ‘transfer of right to use software’ as per Clause 29(A)(d) of Article 366 of the Constitution of India and it can not be treated as deemed sale. It is a simple case of a licence to use and not Transfer of right to use software. It is neither transfer of title nor deemed sale and hence is liable to service tax. Providing the right to use mentioned in cl. (v) of the definition of information technology software is the same thing as providing the license to use. Therefore this activity of providing the license to use software falls under Clause (v) of the definition of ‘Information Technology Service and is taxable.’

6. Citing the decision of the Hon’ble Supreme Court in *Tata Consultancy Services v. State of Andhra Pradesh & Others* [2004 (178) ELT 22 (SC)] that

‘26. Mr. Sorabjee submitted that the High Court correctly held that unbranded software was “undoubtedly intellectual property”. Mr. Sorabjee submitted that the High Court fell in

error in making a distinction between branded and unbranded software and erred in holding that branded software was “goods”. We are in agreement with Mr. Sorabjee when he contends that there is no distinction between branded and unbranded software. However, we find no error in the High Court holding that branded software is goods. In both cases, the software is capable of being abstracted, consumed and use. In both cases the software can be transmitted, transferred, delivered, stored, possessed etc. Thus even unbranded software, when it is marketed/sold, may be goods. We, however, are not dealing with this aspect and express no opinion thereon because in case of unbranded software other questions like situs of contract of sale and/or whether the contract is a service contract may arise.’

and of the Hon’ble High Court of Madras in *Infotech Software Dealers Association v. Union of India* [2010 (20) STR 289 (Mad.)] to the effect that

‘31. From the above, the dominant intention of the parties would show that the developer or the creator keeps back the copyright of each software, be it canned, packaged or customised, and what is transferred to the network subscriber, namely, the members of the association, is only the right to use with copyright protection. By that agreement, even the developer does not sell the software as such. By that Master End-User License Agreement, the members of petitioner-association again enter into an End-User License Agreement for marketing the software as per the conditions stipulated therein. In common parlance, end user is a person who uses a product or utilises the service. An end user of a computer software is one who does not have any significant contact with the developer/creator/designer of the software.

According to Webster's New World Telecom dictionary, an end user is "the ultimate user of a product or service, especially of a computer system, application or network." On a careful reading of the above, we are of the considered view that when a transaction takes place between the members of ISODA with its customers, it is not the sale of the software as such, but only the contents of the data stored in the software which would amount to only service. To bring the deemed sale under Article 366(29A)(d) of the Constitution of India, there must be a transfer of right to use any goods and when the goods as such is not transferred, the question of deeming sale of goods does not arise and in that sense, the transaction would be only a service and not a sale.'

his submission on taxability was elaborated.

7. It would appear from the submissions that the case of Revenue relies upon the definition of the 'taxable service' which is the provision of service in relation to 'information technology service' comprising

'65(105) (zzzzz) "taxable service" means any service provided or to be provided,-

to any person, by any other person in relation to information technology software including,-

- (i) development of information technology software,*
- (ii) study, analysis, design and programming of information technology software,*
- (iii) adaptation, upgradation, enhancement,*

implementation and other similar services related to information technology software,

- (iv) providing advice, consultancy and assistance on matters related to information technology software, including conducting feasibility studies on implementation of a system, specifications for a database design, guidance and assistance during the startup phase of a new system, specifications to secure a database, advice on proprietary information technology software,*
- (v) providing the right to use information technology software for commercial exploitation including right to reproduce, distribute and sell information technology software and right to use software components for the creation of and inclusion in other information technology software products,*
- (vi) providing the right to use information technology software supplied electronically;'*

and that instead of 'canned software' which is considered to be goods, the appellant herein is alleged to have supplied 'customized software'.

8. It is an admitted fact that the appellant is in the business of

perpetual licensing and software licence, sale of third-party software, customization of software as per requirement of customers and implementation and maintenance of software. The taxability of ‘information technology software service’ has had its own share of teething problems with various clarifications having been issued pursuant to representation from the trade. The software that is sold on physical media comprises the inherent contents therein along with right to use and the incorporation of the above activity in the enumeration of taxable service appears to have been intended to levy tax on the ‘intellectual property right’ component as is evident from the two notifications, issued under Central Excise Act, 1944 and Customs Act, 1962, to provide for abatement to the extent of taxability under Finance Act, 1994 on certain portion of the consideration. It is the claim of the appellant that they are not in the business of customizing software and that their developed software is directly utilized by the banking industry which may or may not make adjustments for their own use. The original authority appears to have come to the conclusion of taxability by interpreting the commercial exploitation, in the definition of ‘taxable service’, with reference to its lexicographical meaning. Against this, the contention of the appellant is that the licence can be utilized only by the recipient of the software who is barred from transferring, or subletting, the software to anyone else. As the scope of usage by the customers did not extend to commercial exploitation, the classification of the activity as

‘information technology software service’ would not be in order. It also not in dispute that the grant of licence, covered by a separate agreement of the customers, is the effective ‘right to use’ envisaged in section 65(105)(zzzze) of Finance Act, 1994.

9. There is no doubt that the appellant is in the business of developing software and that such software is used by the banking industry. We do not find any evidence of such software being designed according to the requirements of, or standards prescribed by, customers. There is no doubt that the licence, provided along with the media containing the software, represents the right to use; however, this is a general industry wide practice that is not alien to ‘canned software’. In *re Tata Consultancy Services*, the Hon’ble Supreme Court has held that ‘canned software’ are goods and being liable to value added tax is precluded from coverage under Finance Act, 1994.

10. From a perusal of the circular dated 4th November 2009, it is seen that the scope of ‘commercial exploitation’ has been examined at length by the Central Board of Excise & Customs; undoubtedly, this was in the context of duties of customs which was leviable on imports. It is seen from the findings of the original authority that the impugned order appears to have been guided entirely by the expression ‘commercial exploitation’. The commercial exploitation of the competencies and expertise of the customers which is supplemented by the software provided by the appellant is not the

same as ‘commercial exploitation’ of the software; while the former can be treated as an ‘input’ or ‘input service’, for the latter, ‘commercial exploitation’ of ‘information technology software’ would mean the transfer of producer’s own right to distribute and sell the software itself to the ultimate market. The agreement does not provide for such an eventuality.

11. In the absence of facts that establish otherwise or of any evidence that such was the transaction between the appellant and the customers, it was not appropriate for the adjudicating authority to conclude that sale of banking software to a bank is ‘commercial exploitation’ merely because the bank deploys the software in its normal business activities. The specific connotation of ‘right to use’ and the ‘intellectual property rights’ enshrined within it mandates commercial exploitation to be ascertained in an entirely different context, viz., that of reproduction or distribution.

12. Accordingly, we find no merit in the impugned order which is set aside. Appeal is allowed.

(Order pronounced in the open court on 26/02/2020)

(C J Mathew)
Member (Technical)

(Dr. Suvendu Kumar Pati)
Member (Judicial)