

Tax Hotline

September 05, 2006

WITHHOLDING TAX ON PURCHASE OF SOFTWARE

The Authority for Advance Rulings ("**Authority**") has recently held that in the case of an Indian company there exists a legal obligation to withhold taxes while making payments for the software purchased from a foreign company.

The applicant, Headstart Business Solutions Pvt. Ltd. ("**Headstart**"), an Indian company had entered into a Solution Provider Agreement with Microsoft Sales Corporation, Singapore ("**Microsoft**") for the purchase of business software solutions. It had sought a ruling from the Authority on whether it was required to withhold taxes while making payments for the purchase of such software from the foreign company.

The applicant contended that the payments for software would be taxable as royalty only if the software imported was accompanied by copyright thereby enabling the applicant to replicate the software. In the present case, as the imported software did not confer any copyright on the applicant, the remittance made by the applicant to the foreign company for the purchase of software did not entail deduction of taxes. Further, the income arising in India to the foreign company from the sale of such software is business income and in the absence of any linkage to a 'permanent establishment' of the foreign company in India, the same is not liable to tax.

For the purposes of determining the obligation to withhold taxes, the Authority did not take the nature of payment into consideration and did not find it necessary to deliberate over the issue as to whether any copyright had been conferred on the applicant. The Authority said: "The arguments advanced by the learned counsel for the applicant with regard to there being no royalty income or the statement that MRSC has no PE (Permanent Establishment) in India are beyond the scope of consideration and subject matter of this application." The Authority solely relied on Section 195 (1) of the Income Tax Act, 1961 ("**ITA**"), holding that the expression "any other sum chargeable under the provisions of this Act" brings within its ambit not only the amounts, the whole of which are taxable without deduction, but also amounts of a mixed composition, where only a part of it may be liable to tax, as well as other disbursements which are of the nature of gross revenue receipts.

Thus, the Authority ruled that there was indeed a legal obligation to withhold taxes when making payment for the purchase of software from a foreign company, as such a payment falls within the scope of section 195 (1) of the ITA.

Impact: The rulings of the AAR are private and binding only on the applicant and tax authorities, in the case of the applicant. However, they do have persuasive value. This ruling will have an impact on many Indian companies, which buy off-the-shelf software products from abroad. The ruling does not discuss the India-Singapore tax treaty provisions and their overriding effect on the ITA.

- Bijal Ajinkya & Archana Rajaram

Source: AAR/103/2005-06/349

DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

Research Papers

Horizon Technologies

January 21, 2025

Compendium of Research Papers

January 11, 2025

FAQs on Setting Up of Offices in India

December 13, 2024

Research Articles

INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

Key changes to Model Concession Agreements in the Road Sector

January 03, 2025

The Revolution Realized: Bitcoin's Triumph

December 05, 2024

Audio

Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

Renewable Roadmap: Budget 2024 and Beyond - Part I

August 26, 2024

NDA Connect

Connect with us at events, conferences and seminars.

NDA Hotline

Click here to view Hotline archives.

Video

"Investment return is not enough" Nishith Desai with Nikunj Dalmia (ET Now) at FI18 event in Riyadh

October 31, 2024

Analysing SEBI's Consultation Paper

on Simplification of registration for
FPIs

September 26, 2024

Scope of judicial interference and
inquiry in an application for
appointment of arbitrator under the
(Indian) Arbitration and Conciliation
Act, 1996

September 22, 2024