

# Tax Hotline

February 29, 2024

## PAYMENTS MADE TO ACCESS LEGAL DATABASE NOT TAXABLE AS FTS OR ROYALTY

- The Delhi HC affirms the order of ITAT that subscription fees paid for accessing a legal database is neither taxable as royalty nor fee for technical services under provisions of the ITA read with India-USA DTAA.
- High Court highlighted the distinction between transfer of a copyright from a mere right to use a copyrighted article.

## BACKGROUND

Recently, the Delhi High Court (“**HC**”)<sup>1</sup> upheld the order passed by the Income Tax Appellant Tribunal (“**ITAT**”) and affirmed that subscription fees paid to access legal database is neither taxable as royalty nor fee for technical services (“**FTS**”) under section 9 of the Income-tax Act, 1961 (“**ITA**”) read with the India-US double tax avoidance agreement (“**DTAA**”).

## FACTS OF THE CASE

Relax Inc, a US based company (“**Taxpayer**”) maintained an online database titled “Lexis Nexis” that enabled Indian subscribers to access judgments, articles, legislations and other research material relevant to the legal field. The Taxpayer accorded access of the said legal database to the Indian customers in exchange of a subscription fee.

The Taxpayer in the course of assessment proceedings argued that the income earned from subscription fee is in the nature of business income and in the absence of it having a permanent establishment (“**PE**”), it would not be subject to tax as per Article 7 of the DTAA. The Taxpayer also submitted that the access accorded to the Indian consumer was neither a transfer of copyright nor it satisfied the requirement of ‘included service’. Hence, income earned by it would not fall within the ambit of royalty or FTS and consequently would not form subject matter of either section 9(1)(vii) of the ITA or within Article 12 of the DTAA.

In this context, the question before HC’s consideration was whether the subscription fee payable by Indian subscribers is taxable in India or not.

## DECISION OF THE HC

We have summarized the decision of HC below.

### Income was not in the nature of royalty and does not fall within the ambit of Article 12(3) of the DTAA

The HC after examining the text of Article 12(3) of the DTAA held that in order to characterize subscription fee as royalty, the tax authorities would have to establish that the payments received by the Taxpayer was consideration for the use of or the right to use any copyright or a literary, artistic or scientific work as defined by Article 12(3) of the DTAA. Merely granting access to the legal database will clearly not amount to a transfer of a right to use a copyright. The HC relied on *Engineering Analysis Centre for Excellence vs. CIT*<sup>2</sup>, *Director of Income Tax vs. Infrasoftware*<sup>3</sup> and *CIT vs. Microsoft Corporation*<sup>4</sup> that also dealt with this issue and re-emphasized that there exists a clear distinction between the transfer of a copyright and the mere grant of the right to use copyrighted material.

### Income was not in the nature of technical consultancy and does not within the ambit of either section 9(1)(vii) of ITA or Article 12(4) of the DTAA

The HC upheld the order of the ITAT and held that section 9(1)(vii) of the ITA is not applicable in the instant case. On a plain reading of Explanation 2 of section 9(1)(vii) of the ITA which defines FTS, it is clear that consideration should fall within the ambit of rendering of a managerial, technical or consultancy service.

Further, it was held that for subscription fee to fall within the ambit of FTS it is imperative for the tax authorities to establish that the Taxpayer was rendering technical or consultancy services and which included making available technical knowledge, experience, skill, know-how or processes. The Delhi HC stated that access to the legal database in the present case did not constitute the rendering of any technical or consultancy services. In any case, according access to the legal database did not also amount to making available any technical knowledge, experience, skill, know-how or processes by the Taxpayer. Hence, the income in question will not fall within the ambit of either section 9(1)(vii) or Article 12(4) of the DTAA.

## NDA ANALYSIS

This is a welcome decision. Taxation of subscription fees has been a contentious issue in India. The Delhi HC has reaffirmed that according access of the legal database to customers does not constitute a transfer of copyright. Merely enabling a customer to have access to the legal database or information contained therein without any further

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right in the intellectual property does not amount to transfer of right or conferment of right to use the copyright. While the Delhi HC held that payments for accessing legal database does not qualify as FTS under the ITA, in relation to royalty, the Delhi HC relied on the treaty provisions and did not delve into the provisions of ITA.

In another case, the Bangalore ITAT<sup>5</sup> was dealing with a similar question on whether fees paid by the Indian customers to a foreign Ed-tech platform for access to database of online educational video was taxable as royalty. The ITAT held that by subscribing to database, the Indian customers merely got access to the database without any right over the copyright in the database. The ITAT Ahmedabad<sup>6</sup> while considering a similar issue has also held that payment made for access to database which is publicly available to any person interested in availing such information is not in the nature of royalty. Similarly, the ITAT Mumbai<sup>7</sup> has held that maintaining legal databases that merely accumulate and organize publicly available/disclosed information at one place which can be accessed by the customers against payment of subscription fees cannot constitute a copyright or intellectual property to begin with. The decision of the Delhi HC adds to the favourable jurisprudence on this issue.

Lastly, while the Delhi HC has held that subscription fees paid to access online database is neither taxable as royalty nor FTS under provisions of the ITA read with DTAA, it will be essential to analyze applicability of Equalization Levy ("EL") on such subscription fees. EL was introduced in India in 2016 with the intention to tax digital transactions. With effect from 01 April 2020, the scope of EL has been widened to apply EL at rate of 2% on foreign 'e-commerce operators' on online provision of goods or services to residents of India. In case where EL is applicable, the ITA specifically exempts such income from income-tax.

– Avani Maheshwari and Ipsita Agarwalla

You can direct your queries or comments to the authors.

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<sup>1</sup>The Commissioner of Income Tax v. Relx Inc, ITA 630/2023

<sup>2</sup>(2022) 3 SCC 321

<sup>3</sup>2013 SCC OnLine Del 4694

<sup>4</sup>2022 SCC OnLine Del 1514

<sup>5</sup>Pluralsight LLC v. Deputy Commissioner of Income Tax, ITA No. 37/Bang/2023.

<sup>6</sup>Income Tax Officer (International Taxation) v. Cadila Healthcare Limited, ITA No. 486/Ahd/2016

<sup>7</sup>American Chemical Society v Deputy Commissioner of Income-tax (International Taxation), IT appeal Nos. 1520 & 1521 (MUM.) of 2022.

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