

Pre-packaged software supplied to public funded research institutions are eligible for concessional rate of tax at 5% – Karnataka AAR

24 May 2022



## Summary

The Karnataka Authority of Advance Ruling (AAR) has observed that the software supplied is a pre-developed or pre-designed software and made available through the use of encryption keys. Hence, it satisfies all the conditions that are required to be satisfied to cover them under the definition of goods. The goods supplied by the applicant cannot be used without the aid of a computer and hence the goods supplied qualify to be computer software and more specifically covered under application software. The AAR further held that supply of such software licence to public funded research institutions is covered under notification stipulating concessional rate of GST at 5% on scientific and technical equipments.

## Facts of the case

- The applicant<sup>1</sup> is a reseller of software products procured from its principal partner<sup>2</sup> in India. However, the applicant does not own the IPRs for the software supplied.
- The applicant is engaged in supply of scientific and technical equipment and time-based and perpetual software license(s) to Public Funded Research Institutions (PFRI) on which GST at 18% has been charged as a supply of service. The applicant contended that the software supplied are embedded in the computer or equipment and require a licence to be activated through a licence key.
- The applicant further submitted that software licence supplied by them are pre-developed or pre-designed, rather than tailor made and must be loaded in the computer. After activation, the software could be used by the customers in different fields depending on their requirement. Hence, the goods supplied are computer software specifically covered under application software.
- The applicant, placing reliance upon the Supreme Court case<sup>3</sup>, submitted that such supply is treated as supply of goods and is entitled for concessional rate of GST at 5%, as specified in the notification<sup>4</sup>.
- The applicant sought advance ruling on whether supply of software licence shall be treated as computer software resulting in supply of goods and subsequent benefit of notifications will be allowed.

## Karnataka AAR observations and ruling<sup>5</sup>:

- **Supply of pre-developed and pre-packaged software is a supply of goods:** The software supplied by the applicant is a pre-developed or pre-designed which must be loaded on a computer. The software becomes useable only after it is activated through licence key. As per the explanatory note<sup>6</sup>, services of limited end-user

<sup>1</sup> Keysight Technologies India Pvt. Ltd.

<sup>2</sup> Keysight Technologies Inc., USA

<sup>3</sup> Tata Consultancy Services Vs. State of Andhra Pradesh [2004 (178) ELT 22 (SC)]

<sup>4</sup> Notifications No.45/2017-Central Tax (Rate), Notification (45/2017) No. FD48 CSL 2017,

Bengaluru and Notification No.47/2017-IGST (Rate) all dated 14.11.2017

<sup>5</sup> KAR ADRG 11/2022 order dated 21.04.2022

<sup>6</sup> Explanatory Notes to the Scheme of Classification of Services

licence as part of packaged software are excluded from the SAC 997331<sup>7</sup>. Thus, supply of software licence by applicant is supply of goods covered under tariff heading 8523.

- **Benefit of concessional rate:** The purpose of the notification is to offer a reduced rate of GST to certain institutions for the purpose of research. Exclusion of computer software on mere technical grounds would defeat such purpose. In the instant case, the applicant is supplying computer software to a PFRI. Further, the said institute has also furnished a certificate as required to fulfil the required condition of the notification. Thus, the benefit of concessional GST rate is applicable to the applicant.

## Our comments

In the erstwhile regime, the Apex Court in the case of Tata Consultancy Services<sup>8</sup> had held that canned software which is sold in packages/CDs/ DVDs/USB drivers will be classified as goods.

Even, the Karnataka AAR in the case of SPSS South Asia Private Limited<sup>9</sup> had held that the supply of software license made by the applicant is covered under supply of goods. Further, since the applicant was supplying computer software to National Institute of Science Education and Research, therefore, the notifications prescribing concessional GST rates were made applicable to the applicant.

The Karnataka AAR in the present ruling has primarily focused on two areas. First, that as per the scheme of classification, supply of software with limited end-user license is excluded from SAC 997331, and second, if the software would be supplied on a higher GST rate to the research institution, it would defeat the ultimate objective of providing concession to the research institutions. In our view, just an exclusion from a particular SAC cannot be a criteria to determine whether the underlying supply is of goods or service. Further, as far as second part is concerned, the ground that higher rate on software will defeat the purpose of the notification, does not appear to be convincing, as the exemption notifications cannot determine the type of supply (whether it is goods or a service).

Moreover, this ruling might not be relevant to other taxpayers who are not classified as research institutions in terms of the exemption notification.

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<sup>7</sup> Licensing services for the right to use computer software and databases

<sup>8</sup> Civil Appeal No. 2582 of 1998 with C.A. Nos. 2584-2586 of 1998

<sup>9</sup> Advance Ruling No. KAR ADRG 15/2021, Order dated 24 March 2021

# Contact us

To know more, please visit [www.grantthornton.in](http://www.grantthornton.in) or contact any of our offices as mentioned below:

---

## NEW DELHI

National Office,  
Outer Circle,  
L 41, Connaught Circus,  
New Delhi - 110001  
T +91 11 4278 7070

## NEW DELHI

6th Floor, Worldmark 2,  
Aerocity,  
New Delhi - 110037  
T +91 11 4952 7400

## AHMEDABAD

Unit No - 603 B, 6th Floor,  
Brigade International  
Financial Center,  
GIFT City Gandhinagar,  
Ahmedabad - 382355  
T +91 79 6900 2600

## BENGALURU

5th Floor, 65/2, Block A,  
Bagmane Tridib,  
Bagmane Tech Park,  
CV Raman Nagar,  
Bengaluru - 560093  
T +91 804 243 0700

---

## CHANDIGARH

B-406A, 4th Floor,  
L&T Elante Office Building,  
Industrial Area Phase I,  
Chandigarh - 160002  
T +91 172 433 8000

## CHENNAI

9th floor, A wing, Prestige  
Polygon, 471 Anna Salai,  
Mylapore Division, Teynampet,  
Chennai - 600035  
T +91 44 4294 0000

## DEHRADUN

Suite No 2211, 2nd Floor,  
Building 2000, Michigan Avenue,  
Doon Express Business Park,  
Subhash Nagar,  
Dehradun - 248002  
T +91 135 264 6500

## GURGAON

21st Floor, DLF Square,  
Jacaranda Marg,  
DLF Phase II,  
Gurgaon - 122002  
T +91 124 462 8000

---

## HYDERABAD

Unit No - 1, 10th Floor,  
My Home Twitza, APIIC,  
Hyderabad Knowledge City,  
Hyderabad - 500081  
T +91 40 6630 8200

## KOCHI

6th Floor, Modayil Centre Point,  
Warriam Road Junction,  
MG Road  
Kochi - 682016  
T +91 484 406 4541

## KOLKATA

10C Hungerford Street,  
5th Floor,  
Kolkata - 700017  
T +91 33 4050 8000

## MUMBAI

11th Floor, Tower II,  
One International Center,  
SB Marg Prabhadevi (W),  
Mumbai - 400013  
T +91 22 6626 2600

---

## MUMBAI

Kaledonia, 1st Floor,  
C Wing,  
(Opposite J&J Office),  
Sahar Road, Andheri East,  
Mumbai - 400069

## NOIDA

Plot No 19A, 2nd Floor,  
Sector - 16A,  
Noida - 201301  
T +91 120 485 5900

## PUNE

3rd Floor, Unit No 310-312,  
West Wing, Nyati Unitree,  
Nagar Road, Yerwada  
Pune - 411006  
T +91 20 6744 8800

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For more information or for any queries, write to us at [GTBharat@in.gt.com](mailto:GTBharat@in.gt.com)



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