

**Office of the Commissioner of Commercial Taxes,  
Andhra Pradesh, Hyderabad**

**CCT's Ref.No. I.I(2)/669/1997**

**Dated: 09-05-2007**

Smt. Ranjeev R. Acharya, I.A.S., Commissioner of Commercial Taxes

**CIRCULAR**

Sub:- APVAT Act - Levy of tax on software - certain clarifications - issued - Reg.

Ref:- DC (CT), Hyd (Rural) vide Ref.No. S9/194/07, dt.21-04-2007.

The DC (CT), Hyderabad (Rural) Division vide reference cited has requested for certain clarifications on levy of tax on software products and services. The clarifications sought for are . . .

1. Whether software developed as per customer requirements i.e., custom made software for the clients exclusive use is goods/services.
2. Whether consultancy charges for software services rendered by software Engineers at clients premises is goods/services in view of the transfer of intellectual property.
3. Whether implementation charges of existing software is goods/service.

Since the issues involved in these matters relate to software industry in general, the clarifications sought for are issued in the form of a circular.

The term %software programme+ or %software+ in short essentially refers to the series of commands issued to a computer to perform certain functions. The software programmes are usually recorded on floppy drives or CDs or hard drives. The programmes on these floppy drives on CDs are installed onto the hard disc of the computer in order that the programme can function. The Honourable Supreme Court in the case of TATA Consultancy Services Vs. State of A.P. (39 APSTJ 205 (SC) examined at length the question as to whether computer software on floppy drives or CDs is goods for the purpose of levy of sales tax and finally held that it is goods and attracts sales tax when transferred to a buyer or user for a price. The Honourable Supreme Court further held that both branded and unbranded software are goods because in both cases the software is capable of being abstracted, transmitted, transferred, delivered, stored, possessed, consumed. The Honourable Supreme Court however did not express any opinion on unbranded software only because of the necessity to examine other questions like situs of sale and / or whether the contract is service contract etc.

The Honourable Supreme Court prima facie held that both branded and unbranded software recorded on floppies and CDs are goods. There is no difficulty in levying tax on branded or canned software because it is sold for a price across the counter. In the cases of unbranded software there will be usually written contracts elaborately specifying the nature of software, its price, the time period within which it should be developed and delivered etc. There is a thinking in certain quarters that development and installation of unbranded software is works contract. But, it must be remembered that in a works contract it is by way of accretion/accession transfer of property in goods takes place. For accretion/accession to take place there must be a nucleus belonging to the customer. Around the nucleus the contractor builds by using his own materials. The transfer of property in the material used by the contractor takes place by way of accretion/accession and is taxable as one of the mutated sales after 46th Constitutional amendment. A contract without a nucleus belonging to the customer cannot be termed as a works contract. It is a case of chattel and is a sale simpliciter taxable under the sales tax Acts. In the cases of unbranded software the customer generally does not supply any nucleus. He only specifies his requirements and the software developer develops the software as per those specifications

either at his premises or at the customers premises, makes copies of the software on floppies or CDs and delivers to the customer or installs on the computer of the customer. These transactions therefore are simple sales. It is however necessary to examine the contracts meticulously to decide whether they confirm to the general pattern of development and delivery of unbranded software described here above or are there any deviations and assess the software developer accordingly.

With regard to the %Consultancy charges+referred to be the DC(CT) (Rural) Division, they are usually the charges collected by the software developer from the customer from time to time at different stages of developing the software. All these charges therefore form part of the sale price once the sale fructifies by delivery of the floppy or Cd containing the required software. They are all pre-sale receipts and add to the sale value of the software. There may however be post-sale receipts also in case they are received for maintaining the software after it is sold. Even in the case of maintenance, the actual service rendered may involve development of a new software programme which plugs the bugs that are discovered in the original software in the course of its usage. In such cases again the transactions actually sale of software but ostensibly termed %consultancy+or %maintenance+etc. It may also be a case of simple service without involving any development and delivery of software.

All the assessing and revisional authorities in the State are therefore requested to examine the cases of software companies in the light of the observations of the Honourable Supreme Court and with reference to the contract agreements between the customers and the software companies to ascertain to true nature of the transactions, the situs of sale etc and take appropriate action accordingly and report compliance.

Smt. RANJEEV R. ACHARYA  
Commissioner of Commercial Taxes

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