IN THE COURT OF APPEAL OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

In the matter of an application for mandates in the nature of writs of certiorari and prohibition in terms of Article 140 of the Constitution of the Democratic Socialist Republic of Sri Lanka.

BC Computers Ltd
"Bartleet House",
No.65, Braybrooke Place,
Colombo 02.

PETITIONER

C.A. Application No. 764/07 (Writ)

Vs.

1. U.S. Wickramasinghe
   Assistant Superintendent of Customs
   Department of Customs
   Times Building, Colombo 01.

2. Wasantha Wimalaweera
   Assistant Superintendent of Customs
   Department of Customs
   Times Building, Colombo 01.

3. A. Kulenthiran
   Deputy Director of Customs
   Department of Customs
   Times Building, Colombo 01.

4. The Director General of Customs
   Sri Lanka Customs
   Times Building, Colombo 01.

RESPONDENTS

BEFORE	:	**S. SRISKANDARAJAH, J (P/CA)**
COUNSEL	:	Riad Ameen
		for the Petitioner.
		F.Jameel,D S G
		for the Respondents
Argued on	:	22.02.2012 & 30.05.2012
Written Submission	:	31.10.2012 Petitioner
		30.10.2012 Respondent
Decided on	:	29.01.2013

S.Sriskandarajah, J

The Petitioner is a company, and it was awarded a tender consequent to a competitive bidding by the National Savings Bank of Sri Lanka for the supply, installation and implementation of automated tele-machine software and, as such, the Petitioner engaged the services of two specialists companies in India and Singapore to develop and provide the said software to the Petitioner. The Petitioner entered into a licensed agreement with the said companies, viz., Financial Software (F.S.S.) of India and A.C.I. Worldwide (Asia) Pvt., Limited of Singapore, to procure the licence and price to supply and implement the said software solutions in the National Savings Bank for its automated tele-machines. Pursuant to the said licensed agreement, in January 2006, the Software Engineers of F.S.S. travelled to Sri Lanka from India and installed the aforesaid software on the Petitioner's computer system. The Petitioner submitted that the aforesaid software was brought into Sri Lanka in compact discs (CDs) by Software Engineers of F.S.S. Some of the components of the software were downloaded from internet by the F.S.S. Software Engineers and the said software was developed and customized to suit the requirements of the National Savings Bank. The Software

Engineers of F.S.S. installed the software in the Petitioner's computer system and took away the C.D. containing the software brought by them to Sri Lanka, since the said C.D. contained the source code and the F.S.S. Engineers took the contents of the source code. The Petitioner transferred the software installed in their computer system on to its own CDs and supplied the said software solution to the National Savings Bank for it's ATM transactions, as aforesaid. The Petitioner contended that in C.A. Application No.218/2001 filed by the Commercial Bank Limited, reported in 2002/3 SLR 86, it was held that in terms of Section 10 of the Customs Ordinance, Customs duty was payable on goods, wares and merchandise, licensed customised software as intangible property and the carrier media, i.e., CDs containing licensed software are tangible property. On this basis the carrier media, i.e., CDs containing licensed customised software could be levied Customs duty, but only in respect of the value of the carrier media, and it was held, the value of licensed customized software itself contained in such carrier media, viz., CDs, would not be liable for Customs duty. This decision of the Court of Appeal was set aside by the Supreme Court in S.C. Appeal 43 of 2004, S.C. Minutes 27/04/2006, where the Supreme Court held:

I. All tangible goods, wares and merchandise imported into Sri Lanka are subject to Customs duty;

II. Discs, magnetic tapes and CDs containing software imported into Sri Lanka constitute wares or merchandise;

III. The focus of the Customs investigation is on software imported as part of the tangible carrier media, such as discs, tapes and CDs;

IV. In ascertaining the value of such goods, the value of any tangible component thereof, is taken into account in conformity with the express provisions laid down in 2.8.2. of Schedule (e) of the Customs Ordinance regarding intellectual property. (The said Schedule has now been repealed by Customs (Amendment Act No.2 of 2003); and

V. It must be noted that the said taxation is tangible unit and not intangible component, per se, and the relevant item is taken as a whole for the purpose of valuation.

The position of the Petitioner is that the Petitioner only received software from software engineers of F.S.S., and the software, per se, received by the Petitioner is not subject to Customs duty as it is intangible property and does not constitute goods. The Petitioner further contended that the Petitioner was not in possession of the C.D. containing the software that was brought into Sri Lanka by the Software Engineers of F.S.S. The Customs duty, in terms of the judgment of the Supreme Court, could only be imposed on the CDs containing software brought into Sri Lanka. The Petitioner submitted that the 1st and 2nd Respondents commenced an investigation into software brought into Sri Lanka by Software Engineers of F.S.S. of India in January 2006, and during the course of the investigation, the 1st and 2nd Respondents alleged that the Petitioner had imported software without paying Customs duty. After an inquiry, the 3rd Respondent made an order dated 10/08/2007 imposing a mitigated forfeiture of Rs.6.5 million in terms of Sections 47, 107, 129 and 162 of the Customs Ordinance. The Petitioner contended that the said decision of the 3rd Respondent dated 10/08/2007 is ultra vires for the reasons that the said decision is contrary to the provisions of the Customs Ordinance, and the said forfeiture is unclear, unreasonable and irrational. The Petitioner also further contended that the said 3rd Respondent has erroneously acted on the premise that software, per se, is goods liable for Customs duty when in law software, per se, is intangible property that does not constitute goods. It is the position of the Petitioner that the Petitioner was not obliged to make a declaration as the Petitioner had never received the CDs containing the software, and the said CDs were brought into Sri Lanka by the F.S.S. software engineers and taken back to India by F.S.S. engineers after the installation of the software was completed. In those circumstances the Petitioner contended that the Petitioner never imported the software. The Petitioner also submitted that the 3rd Respondent has failed to ascertain the value of the

component of the software installed from the CDs for the purpose of imposing Customs duty, and the value of other downloaded items from the internet that is not liable for Customs duty. In the above circumstances the Petitioner has sought a Writ of Certiorari to quash the forfeiture imposed by the order dated 10/08/2007 marked P10.

The Supreme Court in S.C. Appeal No.43 of 2004 in *Luxman Perera and 2 others Vs. Hatton National Bank, S.C. Minutes 27th November 2006* held: "The fundamental proposition, as laid down in Section 10 of the Customs Ordinance is, that all intangible goods, wares and merchandise, whether imported or exported, is liable to Customs duty. The Respondent Bank had taken up the position that the type of software used by the Bank in its Bank installations are all custom made software, programmed specially for the Respondent Bank, all needs of such software is not available in the open market and, in consideration for the use of the software, a licence fee is paid to the provider as opposed to a price where there is an outright transfer of property in the goods.

The Respondent-Appellant contended that software is a copyright material and comes within the ambit and scope of paragraph 2.8.2 of Schedule (e), and when goods are valued, there is an underlying assumption that the right to use a copyright shall be included in the normal price. Thus, the issue is whether the customised software used by the Respondent Bank under licence for its bank's purpose is duty payable under the Customs Ordinance.

Paragraph 1 of Schedule (e), which is the umbrella provision of the Schedule, reads as follows:-

"The value of any imported goods shall be the normal price, i.e., the price which they would fetch at the time of importation on a sale in the open market between a buyer and a seller independent of such other than as indicated in paragraph 27".

The Court of Appeal consideration of Schedule (e) will reveal that it contains a series of rules and assumptions which are a reflection of accepted international trade and practice. It is borne from the foregoing that there is no dispute:-

(a) That all tangible goods, wares and merchandise imported into Sri Lanka are subject to Customs duty; and

(b) That books, periodicals, diskets, mechanical tapes and compact disks containing relevant software imported into Sri Lanka constitute goods, wares of merchandise.

The dispute however is in respect of the proper value to be placed upon the goods which have been used as the carrier media for software in terms of directions found in Schedule (e). Such goods must be valued with reference to the right to use that software, and they cannot be treated for valuation purpose in the same manner as for blank disks.

In terms of the provisions of Schedule (e) of the Customs Ordinance, there is no basis to draw a distinction between the value of the carrier media and the value of software. It is to be noted that the practice of Customs investigations is on software imported as part of tangible carrier media such as diskets, tapes and compact discs. The jurisdiction for such Customs investigation is set out in Sections 51 and 52 with paragraph 2.8.2 of Schedule (e) of the Customs Ordinance.

In ascertaining the value of such goods, the value of any intangible component thereof is taken into account in conformity with the express provisions laid down in paragraph 2.8.2 of Schedule (e) which provides for the inclusion of the value of any intellectual property components. It must be noted that the subject of taxation is tangible unit and not it is intangible component, per se, and the relevant item is taken as a whole for the purpose of valuation.

The Inquiring Officer of the said Customs investigation had come to the conclusion that BC Computers Limited had remitted by way of T.T. the full charges for the software and received in their computer system the said software and therefore he had considered them as the Importer. It is the position of the BC

Computers that the software that was brought to Sri Lanka in the CD form by F.S.S., have subsequently taken it back by them and, therefore, they claim that there cannot be any value attached by the Customs for the recovery of Customs duty and other levies. The officer who conducted the inquiry has considered this aspect and had come to the conclusion in his order that the Customs value for the recovery of Customs levy of and the other levies are amounts actually paid for the subject transaction. The software licence agreement entered into between BC Computers Limited and F.S.S. for the software has given the transaction value as US$ 40,000 and the modules of all the software products are "object code modules", and in para 2 of the said agreement, the Petitioner has accepted responsibility for procurement, installation, administration and maintenance of all hardware and system software required for the running of the application software. The application software was handed over to the Petitioner with the object code. The submission of the Petitioner that the source code was not handed over to the Petitioners and, therefore, the software is not in fact sold to the Petitioner is untenable, as source code is a trade secret and that will not be handed over in any software transaction. The object code with is necessary for the running of the software was handed over to the Petitioner and, in these circumstances, the property of the software is now handed over to the Petitioner even though the carrier media, the CDs were taken back to India by F.S.S. Company. In those circumstances the transacted value between the parties are clearly borne out by their licence agreement and the Inquiring Officer has considered the above factors and had imposed a mitigated forfeiture of Rs.6.5m. Under these circumstances I see no reason to interfere with the decision of the Inquiring Officer and, therefore, I dismiss this Application without cost.

President of the Court of Appeal