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DIRECT TAX UPDATE

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No obligation to deduct TDS u/s 195 if income is not chargeable to tax in India.

- **DCIT Vs. Sahara India Commercial Corporation Ltd. (IT Appeal Nos. 488 to 492, 517 to 521 and 540 to 544 of 2009- Lucknow Tribunal)**

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Payment towards 'publicity' bears the character of 'advertisement" for the purpose of deduction of tax at source u/s 194C and no penalty could be imposed on assessee for non-deduction of tax at source if recipient was a loss making entity.

- **XL India Business Services Pvt Ltd Vs. ACIT (IT Appeal No. 16/Del/13)**

Reference to the TPO, in absence of any proceedings pending before AO is unsustainable in law

- **CIT Vs. REPCO Home Finance Ltd (T.C. (A.) No. 601 of 2014)**

Interest u/s 234C to be calculated on date of presentation of cheque for payment of advance tax

Recent Circular

- The CBDT has released Circular No. 17/2014 which contains the rates of deduction of income-tax from the payment of income chargeable under the head "Salaries" during the Financial Year 2014-15 and explains certain related provisions of the Act and Income-tax Rules, 1962.

1. Transfer Pricing

a. Birla Corporation Ltd. Vs. ACIT (IT Appeal Nos. 251 and 252 (Jabalpur) of 2013)

Payments of incidental services for installation and commissioning of machines are not liable to be tax as fee for technical services

Facts of the case:

During the scrutiny, the Assessing Officer (AO - TDS) noticed that the assessee has made certain foreign remittances without deducting tax at source. When assessee was asked the reasons of doing so, it was explained to the AO-TDS that the income embedded in these payments was not chargeable to tax in India as these payments were for imports of plant, equipment and machinery. It was also contended that as the payments were made for purchases, which did not give rise to taxability of

related income in India, there was no requirement of tax withholding requirement from these payments.
The AO-TDS was of the view that the payment was not only for purchases but also for incidental services in connection with installation and commissioning of these machines, and, accordingly, the assessee was required to deduct tax at source from these payments.

On appeal, the Commissioner (Appeals) upheld the order of the AO-TDS.

Assailing the said order passed by CIT(A), the assessee filed an appeal in the Tribunal.

Decision of the Tribunal:

The Hon'ble Tribunal Court while giving relief to assessee held as under:

- The assessee, had fairly submitted that the taxability of such payments as FTS or FIS was taken as granted, without appreciating this nuance of the matter, so far as standalone payments for these services were concerned, but neither such a conduct on the part of the assessee can constitute estoppel against the correct legal position nor would it imply that the a part of sale consideration can be fictionally treated as towards such services and then treated as FTS or FIS while the scope of such payments, under the tax treaties, is confined to amounts actually paid as FTS or FIS. The taxability of an income is to be decided on the basis of the provisions of law and not conduct of the parties. Just because the assessee has accepted a taxability in respect of some other transaction, no matter howsoever related, the legal remedies available to the assessee cannot be negated. There cannot be, and there is no, estoppel against the law. In view of the above discussions, in a situation in which there are specific PE clauses in relation to a particular type of services, which are covered in the scope of services covered by the scope of the 'fees for technical services' or 'fees for included services', the taxability of consideration for such services must remain confined to taxability of profits under the relevant specific PE clause. The provisions for taxability as FTS or FIS will not come into play in such cases.

- By no stretch of logic, installation or assembly activities

even involve transfer of technology in the sense that recipient of these services can perform such services on his own without recourse to the service provider, nor has it been the case of the authorities below. For this short reason alone, the installation, commissioning or assembly activities cannot constitute fees for technical services, or fees for included services- as these are termed in Indo-US tax treaty.

- The same is the position with regard to the Indo Belgium tax treaty by the virtue of following MFN (most favoured nation) clause.

- Installation, commissioning or assembly of a plant, machinery or equipment, or any supervision activity connected therewith, is ancillary and subsidiary, as well as inextricably and essentially linked, to sale of such a plant equipment or machinery; therefore, any consideration for such installation, commissioning or assembly activities, or supervision services cannot be included in fees for included services under Indo-Swiss tax treaty. Accordingly, even if there be any income embedded in such payments, same cannot be brought to tax, in view of provisions of Article 12(5)(a) of Indo Swiss tax treaty, in hands of Swiss vendors as well.

- As corresponding provisions also find place in Indo-UK [Article 13(5)(a)] and Indo-US [Article 12(5)(a)] tax treaties, for this reason as well and for material facts being similar, consideration for installation, commissioning or assembly activities, or supervision services in respect thereof, can also not be subjected to tax in India in hands of UK and US based vendors either.

- Under the scheme of allocation of taxing rights under the related tax treaties, India does not have the right to tax income, even if any, in respect of rendition of installation, commissioning or assembly services, embedded in the invoice value of the related equipment, plant or machinery.

- In case the Assessing Officer brings any material on record which can demonstrate that the vendors had a PE in India, and the income embedded in the impugned payments was indeed liable to be taxed in India, to that extent and in accordance with the provisions of law, the Assessing Officer will be at liberty to raise the fresh demand under section 201 r.w.s. 195.

Therefore, the payments made by the assessee to foreign parties for incidental services in connection with installation and commissioning of machines are not liable to be taxed in India as fee for technical services and assessee is not required to deduct tax at source from these payments.

b. ACIT Vs. Track Shoes (P.) Ltd (ITA No. 541 of 2014-Chennai-Tribunal)

Commission paid by the assessee to its foreign agent on export sales does not fall within definition of 'fee for technical services'

Facts of the case:

During relevant year, the assessee paid commission to foreign agents on export sales. The Assessing Officer opined that the amount paid by the assessee to non-resident agent was fee for technical services and since the assessee did not deduct TDS under section 195 the said expenditure was not allowable under section 40(a)(i). The Commissioner (Appeals) deleted said disallowance.

Decision of the Tribunal:

On revenue's appeal, the Hon'ble tribunal held as under:

- The AO while completing the assessment disallowed commission payments made to foreign agents on the ground that assessee has not deducted TDS. The AO was of the view that sales commission paid by the assessee shall be deemed to accrue or arise in India, if such income is accrued or arisen from any business connection in India. According to the AO in the instant case, payments were made for assessee's business purposes which is carried on in India and therefore such commission paid to non-residents abroad is deemed to have been arisen in India. The AO is not disputing that the commission paid by the assessee is not for export sales. Further he has not brought on record to suggest that non-residents provided technical services to the assessee. The Commissioner (Appeals) in respect of sales commission paid to Calzados Jose and M.G. Diffusion International deleted the disallowance relying on the decision of this Tribunal in the case of **ITO v. Faizan Shoes (P.) Ltd. [2013] 58 SOT 245** where the facts were identical as foreign agents have no permanent establishments in India, no part of their services have been

rendered in India and in such situation there is no obligation on the assessee to deduct tax at source under section 195. The decision relied on by the Commissioner (Appeals) has been after affirmed by the Madras High Court in the case of **ITO v. Faizan Shoes (P.) Ltd. [2014] 367 ITR 155 (Madras)**

- The High Court held that the services rendered by the non-resident agent can at best be called as a service for completion of export commitment, therefore commission paid to non-resident agents will **not** fall within the definition of fees for technical services. Further it was also held that commission amounts earned by non-resident assessees for services rendered outside India **cannot be deemed** to be incomes which have either accrued or arising in India.

Thus, commission paid by the assessee to its foreign agent on export sales would not fall within definition of 'fee for technical services' and there is no need to deduct TDS while making said payment.

2. Domestic Taxation

a. ACIT Vs. Vilas N. Tamhankar (I.T.A. No. 4522/Mum/2013)

No obligation to deduct TDS u/s 195 if income is not chargeable to tax in India.

Facts of the case:

The assessee made the payment to a resident of Canada for sales and marketing support outside India. No part of the services, toward which payment had been made to the payee, was rendered in India. The payee had no place of business or establishment in India. Thus, the assessee made payment without deducting tax at source. No application u/s.195(2) of the Income Tax Act, 1961 ("the Act") was made to the Assessing Officer (A.O.), in whose view there was thus a contravention of section 195 of the Act and, consequently, the non-obstante provision of section 40(a)(i) would get attracted, where tax is deductible at source thereon. Accordingly, the AO relying on the decision in the case of ***Transmission Corpn. of A.P. Ltd. vs. CIT [1999] 239 ITR 587 (SC)*** disallowed the expense of sales and marketing support u/s.40(a)(i) for non-deduction of TDS.

The assessee filed an appeal before CIT(A). The ld. CIT(A) relying on the decision rendered by the apex court in the case of ***GE India Technology Centre (P.) Ltd. vs. CIT [2010] 327 ITR 456 (SC)*** deleted the disallowance.

Aggrieved by the order Revenue filed an appeal in the Tribunal:

Decision of the Tribunal:

The Hon'ble Tribunal while giving relief to the assessee held as under-

- As explained by the Apex court in ***GE India Technology Centre (P.) Ltd (supra)***, if the interpretation being accorded by the Revenue to section 195, i.e., that the moment payment to a non-resident is made, the obligation to deduct the tax at source arises, is accepted, the same would imply obliterating the words 'chargeable under the provisions of the Act' occurring in section 195(1). Section 195 falls under Part B of Chapter XVII of the Act, titled 'collection and recovery of tax'. As explained by the Apex court, the Act forms one integrated code, and the charging sections cannot be read *de hors* the machinery sections. Due weight has to be given to every word in the section. The interpretation by the Revenue was, in its view, guided more by administrative convenience, and which would though imply deduction of tax even on payments *qua* which there was no territorial nexus with India or otherwise were not chargeable to tax in India. Administrative considerations could not be the basis of the interpretation of the statutory provisions, even as the law contemplates adequate safeguards in the form of section 40(a)(i) and section 195(6);

- There is a requirement and an essential ingredient to invoke s. 40(a)(i) by AO, which is in fact obliged in law to render a finding as to the chargeability of the sum to tax under the Act, which is absent in the case of assessee's case; and

- The edifice of the assessee's case is the rendering of the services outside India. Therefore, though for a consideration for marketing and sale support services and only in the nature of commission or service charges, the same has no nexus with India.

Therefore, the assessee is bound to deduct TDS u/s 195 from the payment made to non-resident only if income is

chargeable to tax in India.

b. DCIT Vs. Sahara India Commercial Corporation Ltd. (IT Appeal Nos. 488 to 492, 517 to 521 and 540 to 544 of 2009- Lucknow Tribunal)

Payment towards 'publicity' bears the character of 'advertisement" for the purpose of deduction of tax at source u/s 194C and no penalty could be imposed on assessee for non-deduction of tax at source if recipient was a loss making entity.

Facts of the Case:

M/s Sahara India Commercial Corporation Limited ("the assessee") is engaged in the business of real estate development, construction and media activities etc. and it entered into a business arrangement with M/s Sahara Airlines Ltd. (SAL) in the nature of subsidy, reciprocatory to which, the deductee was entrusted with the job of printing of logo, colour scheme, etc. on its ticket, aircraft, brochure etc. No tax was deducted on the above payments.

The AO contended that the act of publicizing assessee's business would come under the preview of advertisement and, therefore, payment made for the same was to be subjected to TDS u/s 194C. Consequently, the AO treated assessee as an assessee-in-default u/s 201(1) and levied penalty on it u/s 271C.

The assessee took a stand that deductee has not undertaken any advertisement activity for and on behalf of the assessee which could have a contractor-contractee relationship to invoke provisions of section 194C. The AO's order was set aside by CIT(A) against which AO filed the instant appeal before the ITAT.

Issues involved:

- Whether the payment made by the assessee to the deductee is in nature of advertisement?
- Whether the provisions of section 201(1A) and section 271C can be invoked in cases where the deductee is incurring losses?

Decision of Tribunal:

The Hon'ble Tribunal held as under:

- Relying on the CBDT Circular No. 714, dated 08-08-1995 and by interpreting the word 'advertisement' from various dictionaries, the Hon'ble ITAT held that "advertisement" includes publicity; however,*vice-versa* may not be possible. When publicity brings commercial benefit either apparent or hidden, it will give publicity the character of "Advertisement";

- It was confirmed by the Tribunal that publicizing the business of assessee indirectly would give a commercial benefit to it. Hence, tax was required to be deducted under Section 194C;

- The Tribunal observed that SAL had filled all its returns including payment received from assessee and had declared huge losses in all such years. Therefore, there was no loss to the revenue on account of non-deduction of taxes by the assessee because SAL was a loss making company. Hence, assessee couldn't be treated as an assessee-in-default u/s 201(1A) for non-deduction of tax.

Therefore, the subsidy paid by assessee for the purpose of publicizing the logo by displaying the logo on ticket, aircraft, brochure etc is treated as amount paid for advertisement and liable to TDS under section 194C. However, no penalty could be imposed on assessee for non-deduction of TDS if recipient was a loss making entity and it filed all its returns including the amount so received.

c. XL India Business Services Pvt Ltd Vs. ACIT (IT Appeal No. 16/Del/13)

Reference to the TPO, in absence of any proceedings pending before AO is unsustainable in law

Facts of the Case:

The assessee filed the Return of Income on October 29, 2007 and the time limit for issuance of notice, u/s 143(2), for selecting the case for scrutiny assessment expired on September 30, 2008. On December 24, 2009 the AO made a reference, under section 92CA(3), to the TPO for determination of arm's length price of the international transactions entered into by the assessee with its associated enterprises. The reference made to the TPO and the resultant proceedings resulted into a transfer pricing adjustment of Rs. 2,80,91,619/-

The assessee objected to this initiation of re-assessment proceedings. It was contended that the time limit for issuance of notice under section 143(2) had expired. It was also pointed out that reference to the TPO was invalid as it was made before the initiation of re-assessment proceedings under section 147, at a time when no proceedings were pending before the AO.

However, the AO rejected the objections filed by the assessee against initiation of re-assessment proceedings.

On appeal, the Hon'ble DRP upheld the order of the AO holding that once the TPO's report was available to the AO and the said report indicated that an adjustment was required to be made to the arm's length price of international transaction entered into by the assessee, there was indeed sufficient material on record to form a belief that income of the assessee had escaped assessment.

Decision of the Tribunal:

On appeal to Tribunal:

The Hon'ble tribunal placed reliance on following judgements and held as under:

- As held by the **Hon'ble Karnataka High Court**, in case of **CIT Vs SAP Labs Pvt Ltd [ITA Nos. 842 of 2008 and 339 of 2010]**, unless an income tax return, in respect of which notice under section 143(2) can be issued, is pending before AO, a reference to the TPO cannot be made by the AO;

- Further, the Tribunal referred to the **Hon'ble Bombay High Court's** judgment in case of **CWT Vs Sona Properties (327 ITR 592)**, wherein it was held that when reference itself is invalid, the report received as a result of the said reference cannot constitute material for forming the belief that an income or wealth tax escaped assessment.

- Placing reliance on the above decisions and since there were no decisions holding anything contrary to these decisions by any of the courts above, the very initiation of re-assessment proceedings, on the facts of this case, are not sustainable in law. Accordingly, the re-assessment proceedings are set aside. The re-assessment order thus

stands quashed.

Therefore, the re-assessment proceedings held legally unsustainable in law.

d. CIT Vs. REPCO Home Finance Ltd (T.C. (A.) No. 601 of 2014)

Interest u/s 234C to be calculated on date of presentation of cheque for payment of advance tax

Facts of the Case:

The AO charged a sum as interest u/s 234C for late payment of advance tax. On appeal, the Commissioner (Appeals) held that the date of presentation of cheque should be treated as date of payment of tax and, if so considered, no interest u/s 234C was to be charged. On cross appeal, the Tribunal confirmed the order passed by the Commissioner (Appeals) and dismissed the appeal. Revenue filed an appeal to High court.

Issue before High Court:
Whether the Tribunal was right in holding that the date of presentation of cheque in the bank is to be reckoned as the date of payment of advance tax and not the date on which the cheque is cleared?

Decision of the High Court:

The Hon'ble High court while giving relief to the assessee held as under:

- The issue raised in this appeal is no longer *res-integra* in view of the decision of the Supreme Court in ***CIT v. Ogale Glass Works Ltd.[1954] 25 ITR 529***, where it is held that the position, is that in one view of the matter an implied agreement under which the cheques were accepted unconditionally as payment and on another view, even if the cheques were taken conditionally, the cheques not having been dishonoured but having been cashed, the payment related back to the dates of the receipt of the cheques and in law that dates of payments were the dates of the delivery of the cheques; and

- It is not the case of the department that the cheque issued by the assessee was dishonoured. Once the cheque issued by the assessee is en-cashed, in the light of the decisions

referred (*supra*), the payment relates back to the date of receipt of the cheque.

Thus, interest u/s 234C to be calculated on date of presentation of cheque for payment of advance tax and not on date of clearing of cheque.

3. Circular No. 17/2014 issued by CBDT dated December 10, 2014.

The CBDT has released Circular No. 17/2014 which contains the rates of deduction of income-tax from the payment of income chargeable under the head "Salaries" during the Financial Year 2014-15 and explains certain related provisions of the Act and Income-tax Rules, 1962.

This Circular provides the amended slab rates for taxation incorporated in the Finance (No.2) Act, 2014, applicable for the Assessment Year 2015-16. It contains various illustrations which explain the method of deducting tax at source on the income of an employee falling under various slab rates. It also offers an exorbitant explanation on perquisites and profits in lieu of salary.

A small glimpse of computing income under the head "Income from house property" is provided in the Circular highlighting the recent amendments in respect thereof.

Alongwith above, the Circular also clarifies various compliances in respect of deduction of tax at source, due date of depositing the same to the government and penalties for failure in compliances.

Though this Circular is mandatory only on the Department, the assessee can follow the provisions beneficial to him mentioned therein.