IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH 'A, HYDERABAD

BEFORE SHRI G.C.GUPTA, VICE PRESIDENT AND SHRI AKBER BASHA, ACCOUNTANT MEMBER

ITA Nos.601 to 604/Hyd/09 : Asst. years 2001-02 to 2004-05

Dy. CIT, Cir-1(1), Hyderabad.	VS	M/s. Divi's Laboratories Ltd., Hyderabad. PAN: AAACD6745J
(Appellant)		(Respondent)

Appellant by: Sri. V. Srinivas
Respondent by: Sri. S. Rama Rao

O R D E R

Per Akber Basha, Accountant Member:

These four appeals by the revenue are directed against the separate orders of CIT(A)-II, Hyderabad all dated 27-2- 2009 and they pertain to the assessment years 2001-02 to 2004-05. Since common & identical issues are involved in all these appeals and the assessee is also same, these are clubbed together and disposed off by this combined order for the sake of convenience.

2. Since the facts are identical in all these appeals, for the sake of brevity, we deal with the facts mentioned in ITA No. 601/Hyd/09 for the assessment year 2001-02. Briefly stated facts of the case are that the assessment under section 143(3) for the year under consideration was completed on 26-2-2004 determining the total income of Rs.6,95,42,210/-. Aggrieved against this assessment order, the assessee filed an appeal before the CIT (A). On appeal, the CIT (A) allowed certain relief to the assessee. Against the order of the CIT (A), the department filed appeal before the ITAT. The Tribunal vide order dated 31-10-2007 allowed the appeal of the department in ITA No.797/Hyd/2004. The Tribunal in the order referred to above set aside the issue relating to disallowance under section 40a (ia) of the Act for the commission payments made by the assessee to the foreign agents. As regards computation of deduction under section 80HHC of the Act when the income is computed under section 115JA, the Tribunal directed to compute the eligible profit for deduction on the basis of adjusted book profit under section 115JA of the Act in terms of the decision of Special Bench in the case of DCIT vs. Syncom Formulations (I) Ltd., (13 SOT 404). The present assessment order has been passed by the assessing officer in pursuance to the direction of the Tribunal. The assessing officer after affording opportunity to the assessee made a disallowance of Rs.33,54,926/- under section 40a(ia) of the Act. The assessing officer also recomputed the deduction under section 80HHC of the Act under the normal provisions and also for the purpose of

computation of book profit under section 115JA of the Act. Being aggrieved against the disallowance made by the assessing officer, the assessee went in appeal before the CIT (A). On appeal, the CIT (A) deleted the disallowance made by the assessing officer under section 40a [ia] of the Act except the payment made to M/s. San International. The CIT [A] also directed the assessing officer to restrict himself to the computation of deduction under section 80HCC of the Act in terms of the Special Bench decision in the case of Synchom Formulations [supra] only for the purpose of working out the book profit under section 115JA of the Act as directed by this Tribunal. Not satisfied with the findings and the decision of the CIT (A), the revenue is in appeal before us.

3. The revenue raised the following grounds in this appeal:-

"1. The order of learned CIT (A) is erroneous on the facts and circumstances of the case.

2. The learned CIT (A) failed to appreciate the fact that the assessment was completed in accordance with the directions of the Hon'ble Tribunal. The learned CIT(A) failed to appreciate the fact that the assessee failed to furnish copies of agreements, correspondence with foreign agents in spite of affording opportunity as directed by Hon'ble ITAT and the assessing officer

concluded the applicability of provisions of section 40a(i) after examination of the material on record.

3. The learned CIT (A) ought to have confirmed the disallowance made by the assessing officer under section 40 a(i) of Rs.33,22,621/-.

4. The learned CIT (A) ought to have confirmed the action of assessing officer in applying the retrospectively amended provisions of section 80HHC for computing deduction under section 80HHC.

5. Any other ground that may be urged at the time of hearing."

4. 1st and 5th grounds are general in nature and no adjudication is required.

5. Ground Nos. 2 and 3 are with regard to the disallowance of commission paid to non-resident agents under section 40a (ia) of the Act. In the present assessment order, the assessing officer observed that, the Tribunal had set aside the issue for re-examination of the issue after considering agreement, if any between the parties and also to find out whether there was any intention to make the payment by cheque or draft. The assessing officer was also directed to reconsider the issue in the light of the judgment of Hon'ble Apex Court in the case of Oagle Glass Works. In response to the notice issued by the assessing officer, the assessee reiterated that the commission was paid by

them to the foreign agents for the services rendered outside India and the payments were remitted through the banking channel as per the requirement of RBI regulations. The assessee also stated that the fact in their case is different from the one referred to the case of Oagle Glass Works. The assessee also relied on the decision of the Tribunal, Hyderabad Bench "B" in the case of Premier Explosives Limited in ITA No.736/Hyd/03 for assessment year 1998-99, wherein, it was held that commission paid to non-resident agents who operate from abroad and not having any permanent establishment in India and the payments are remitted directly abroad is an allowable expenditure and there is no obligation to deduct tax at source. The assessing officer however did not accept the explanation of the assessee and he found that during the year under consideration the assessee had paid commission amounting to Rs.38,81,237/- out of which an amount of Rs.5,26,311/- did not attract the provision of TDS. He accordingly disallowed balance amount of Rs.33,54,926/- paid to non-resident agents since no tax was deducted at source. During the proceedings before the CIT [A], the authorized representative of the assessee reiterated the stand taken earlier before the assessing officer and the assessee relied on the Circular No.23 dated 23-7-1969 and Circular No.786 dated 7-2-2000. Relying on various judicial pronouncements, the assessee stated that the aforesaid circulars issued by the CBDT are binding on the revenue and the assessee also relied on the following decisions before the CIT [A], in support of its contention that the payment of sales

commission to foreign agents do not attract the provisions of section 40a(i) of the Act.

1. JCIT vs. George Williamsons Assam Ltd. (116 ITD 328)
2. DCIT vs. Ardeshi B. Cursetjee & Sons Ltd. (115 TTJ 916)
3. ACIT vs. Premier Explosives ITA No.736/Hyd/03 ITAT, Hyd.
4. Dr. Reddy's Lab vs. ITO (58 ITD 104) ITAT, Hyd.
5. SOL Pharmaceutical vs. ITO (83 ITD 72) ITAT, Hyd.
6. Ind Telesoft Pvt. Ltd. (267 ITR 725) (AAR)
7. Indochem Garments Pvt. Ltd. 86 ITD 102 ITAT, Madras.

The assessee also relied on the decision of Hon'ble Apex Court in the case of CIT vs. Toshoku Limited (125 ITR 525) before the CIT [A]. it was also stated that during the year relevant to the assessment year 2006-07 the assessee had incurred an amount of Rs.1,77,34,622/- as deduction representing commission paid to non-resident agents and during the scrutiny assessments after obtaining explanation from the assessee, the said claim of deduction was allowed by the assessing officer. The assessee also stated before the CIT [A] that commission paid to non-resident agents is not being disallowed under section 40a (i) in other Ranges like Range-3, Range-16 and Range-2, Hyderabad under the AP Charge. The CIT [A] by following several decisions of the Tribunal and in particular, the judgment of the Apex Court in the

case of CIT vs. Toshuku Ltd., reported in 125 ITR 525 held that the payment of commission to non-resident selling agents does not attract the provisions of section 195 and consequently disallowance under section 40a [ia] of the Act would not arise. Accordingly he deleted the said disallowance except in the case of payment made to San International.

6. The learned departmental representative submitted that during the year under consideration, the assessee claimed to have paid commission of Rs.38,81,237/- to 29 non-resident agents. Out of total 25 non-resident agents, the assessee furnished correspondence in respect of 13 agents only. In respect of other agents, the assessee could not substantiate the claim that the provisions of section 40a (ia) are not attracted. Therefore, it is rightly held by the assessing officer that the provisions of section 40a (ia) are attracted. It is further submitted that wherever the assessing officer found that the payment of commission was not liable for deduction of TDS, he allowed the expenses as allowable expenditure and the balance is only disallowed as per the provisions of section 40a (ia) of the Act.

7. The learned counsel for the assessee submitted that the issue is covered in favour of the assessee by the decision of apex court in the case of GE India Technology Centre P. Ltd. Vs. CIT and Another (327 ITR 456). It is submitted that for the assessment year 2006-07 similar payments were made and during the scrutiny

assessments, after obtaining explanation from the assessee, the said claim of deduction was allowed by the assessing officer. It is also submitted that the department is not correct in holding that the moment there is remittance, there is an obligation to deduct TDS arises. Hence, it is prayed that the grounds raised by the revenue on this issue have no merit and the same are to be dismissed.

8. We have considered the submissions of both the parties and perused the relevant material available on record. The moot question that arises out of these appeals is whether the payment of commission made to the overseas agents without deduction of tax is attracted disallowance under section 40a(ia) of the Act or not. Whether the payment in dispute made by way of cheque or demand draft by posting the same in India would amount to payment in India and consequently whether mere payment would be said to arise or accrue in India or not?. First we will take up the issue whether the payment of commission to overseas agents with out deduction of tax is attracted disallowance under section 40a (ia) of the Act or not. We find that the CBDT by its recent Circular No.7 dated 22nd October, 2009 withdrawn its earlier Circulars Nos.23 dated 23-7-2009, 163 dated 29th May, 1975 and 786 dated 7-2-2000. The earlier circulars issued by the CBDT have clearly demonstrated the illustrations to explain that such commission payments can be paid without deduction of tax. Thus, the main thrust in such a situation is whether the commission made to

overseas agents, who are non-resident entities, and who render services only at such particular place, is assessable to tax. Section 195 of the Act very clearly speaks that unless the income is liable to be taxed in India, there is no obligation to deduct tax. Now, in order to determine whether the income could be deemed to be accrued or arisen in India, section 9 of the Act is the basis. This section, in our opinion, does not provide scope for taxing such payment because the basic criteria provided in the section is about genesis or accruing or arising in India, by virtue of connection with the property in India, control and management vested in India, which are not satisfied in the present cases. Under these circumstances, withdrawal of earlier circulars issued by the CBDT has no assistance to the department, in any way, in disallowing such expenditure. It appears that an overseas agent of Indian exporter operates in his own country and no part of his income arises in India and his commission is usually remitted directly to him by way of TT or posting of cheques/demand drafts in India and therefore the same is not received by him or on his behalf in India and such an overseas agent is not liable to income-tax in India on these commission payments. This view is fortified by the judgment of Apex Court in the case of CIT vs. Toshoku Limited reported in 125 ITR 525.

9. It is pertinent to note that the section 195 of the Act has to be read along with the charging sections 4, 5 and 9 of the Act. One should not read section 195 to mean that the moment

there is a remittance; the obligation to deduct TDS automatically arises. If we were to accept such contention, it would mean that on mere payment in India, income would be said to arise or accrue in India. These are the observations made in the judgment of Apex Court in the case of GE India vs. CIT reported in 327 ITR 456, relied on by the learned counsel for the assessee, for the proposition that provisions relating to deduction of tax applies only to those sums which are chargeable to tax under the Income-tax Act. If the contentions of the department, are to be taken as correct, that any person making payment to a non resident is necessarily required to deduct tax, then the consequence would be that the department would be entitled to appropriate the monies deposited by the payer even if the sum paid is not chargeable to tax because there is no provision in the Income-tax Act by which a payer can obtain refund. As per section 237 read with section 199 of the Act implies that only the recipient of the sum i.e., payee would seek a refund. In view of the above, hence, no tax is deductible under section 195 of the Act on commission payments and consequently the expenditure on export commission payable to non-resident for services rendered outside India becomes allowable expenditure and the same is outside rigors of the section 40a(ia) of the Act.

10. The judgment of the Karnataka High Court in the case of Samsung Electronics reported in 320 ITR 209, relied on by the department, dealt on whether tax is to be deducted at source,

under section 195 of the Act, in respect of payment made to non-resident, on import of software. The judgment of the Karnataka High Court is largely based on the judgment of Supreme Court in the case of Transmission Corporation of AP Ltd. vs. CIT reported in 239 ITR 587. However, the Karnataka High Court not followed the subsequent binding judgment of the Supreme Court in the case of Vijay Ship Breaking Corporation vs. CIT reported in 314 ITR 309 wherein the Apex Court has categorically held that, the resident is not required to deduct TDS under section 195(1) of the Act, if the income of non-resident recipient is not taxable in India. Given this binding precedent, the judgment of Karnataka High Court in the case of Samsung Electronics (supra) would not apply to the cases where the non-resident recipient is not taxable in India. We also find that the judgment of Apex Court in the case of Ishikawajima Harima Heavy Industries Limited vs. Director of Income-tax, Mumbai reported in 288 ITR 408 wherein it was held that for section 195 is to be attracted, the services rendered by the non-resident should have been rendered in India and also should have been used in India and that, this twin tests has to be satisfied for section 195 is to be attracted. We find that the Legislation introduced the Explanation to section 9(2) of the Act, after this judgment, with retrospective effect from 1-6-1976 in the Finance Act, 2007. Despite this introduction of Explanation to section 9(2) of the Act, the Karnataka High Court in the case of Jindal Thermal Power Co. Ltd., vs. DCIT reported in 321 ITR 31 held that the law laid down by the Apex Court in the case of Ishikawajima Harima

Heavy Industries Limited (supra) still holds good despite the retrospective amendment to section 9 of the Act. In our opinion, the requirement of services of the non-resident being rendered in India and being utilized in India is still valid, despite the judgment of the Karnataka High Court in the case of Samsung Electronics (supra) and withdrawal of earlier circulars issued on this subject by CBDT.

11. It is well settled law that the provisions of Double Taxation Avoidance Agreement would prevail over the provisions of the Income-tax Act, would seem to have been completely not followed by Karnataka High Court while rendering the judgment in the case of Samsung Electronics (supra). Therefore, in our considered opinion, the law related to deduction of tax at source under section 195 has not been changed consequent to the judgment of Samsung Electronics (supra) or withdrawal of earlier Circulars, on this issue by the CBDT and therefore the rigors of section 40a (ia) of the Act, disallowance of expenditure, is not attracted for the payments made to the overseas agents by the assessee without deduction of TDS. In the case under consideration, the CIT [A] observed that the assessing officer has not been able to establish that there are specific intention of the payee to receive the payment within the territory of India as per the decision in the case of Oagle Glass Works [supra], therefore, in our opinion, the CIT (A) rightly did not agree with the view taken by the assessing officer with regard to the addition made on this

issue and hence, the CIT (A) is justified in directing the assessing officer to delete the said addition. After considering the totality of facts and the circumstances of the case, we are not inclined to interfere with the order of the CIT (A) on this issue and accordingly the same is upheld. Hence the grounds raised by the revenue for all the years under consideration are rejected.

12. The only other remaining ground of appeal is with regard to deduction under section 80HHC of the Act. It is contention of the assessee that the assessing officer erred in reworking the deduction under section 80HHC of the Act which is not part of the remand order passed by the Tribunal vide its order dated 31-10-2007. It is submitted that the assessing officer traveled beyond the direction of the Tribunal in addressing the issues in respect of deduction under section 80HHC of the Act. It is the case of the assessee that the assessing officer cannot make any adjustment to the deduction to the 80HHC under the normal provisions of the Act since that was not part of the remand order of the Tribunal. In this connection, he relied on the decision of the Pune Bench of the Tribunal in the case of Bhagwandas Associates vs. ITO reported in 119 TTJ 663. It is also submitted that the CIT(A) only directed the assessing officer to restrict himself to the computation of deduction under section 80HHC in terms of Special Bench decision of ITAT in the case of DCIT vs. Syncome Formulations (I) Ltd., (13 SOT 404).

13. The learned departmental representative submitted that the deduction under section 80HHC of the Act is to be recomputed as per the directions of the Tribunal in view of the amended provisions of section 80HHC. Assessee was given deduction as per the amended provisions since the turnover of the assessee is more than Rs.10 crores and the assessee could not furnish any details. Therefore, the assessing officer rightly not allowed proportionate deduction on 90% export incentive to the assessee. Since the issue was entirely restored to the file of the assessing officer by the Tribunal, the assessing officer has to make any adjustment under section 80HHC under the normal provisions of the Act.

14. We find that the Tribunal in its order directed that –

> " The next ground of appeal in all the appeals except ITA No.772/Hyd/2000 is regarding computation of deduction u/s 80HHC when the income is computed under section 115JA. We have heard the learned departmental representative and the learned counsel for the assessee. This issue was considered elaborately by a Special Bench of this Tribunal at Mumbai in the case of DCIT vs. Syncome Formulations (I) Ltd. (2007) 13 SOT 414. The Special Bench held when the income is computed under section 115JA, deduction under section 80HHC has to be computed under section 115JA deduction under section 80HHC has to be computed on the adjusted book profit computed under section 115JA. By following the decision of the Special Bench, we direct the

assessing officer to compute the eligible profit for deduction on the basis of the adjusted book profit under section 115JA as held by the Special Bench."

Considering the above, the CIT [A] justified in directing the assessing officer to restrict himself to the computation of deduction under section 80HHC of the Act in terms of Special Bench in the case of DCIT vs. Syncome Formulations (I) Ltd. (supra) only for the purpose of working out the book profit under section 115JA of the Act as directed by the Tribunal. Hence, we do not see any infirmity in the order of the CIT (A) and the same is upheld and ground raised by the Revenue for all the years under consideration is rejected.

15. In the result, all the appeals filed by the department stand dismissed.

Order was pronounced in the Court on 25- 03-2011.

Sd/-	sd/-
(G.C. Gupta) Vice President	(Akber Basha) Accountant Member

Dt. 25– 03-2011.

Copy forwarded to:

1. DCIT, Cir-1(1), Hyderabad.

2. M/s Divi's Laboratories Ltd., Divi Towers, D.K. Road, Ameerpet, Hyderabad.

3. CIT (A)-II, Hyderabad.

4. CIT, A P, Hyderabad.

5. The D.R., ITAT, Hyderabad

Jmr*