IN THE INCOME TAX APPELLATE TRIBUNAL,
AGRA BENCH, AGRA
[Coram : Bhavnesh Saini JM and Pramod Kumar AM]

I.T.A. No.: 393/Agra/2012
Assessment year: 2008-09

Metro & Metro ***……Appellant***
Mathura Road, Agra 282 007
[PAN: AACFM1909J]

Vs.

Additional Commissioner of Income Tax
Range 2, Agra ***……Respondent***

Appearances by:
Naveen Gargh, *for the appellant*
Waseen Arshad, *for the respondent*

Date of concluding the hearing : October 31, 2013
Date of pronouncing the order : November 01, 2013

O R D E R

Per Pramod Kumar:

1. By way of this appeal, the assessee appellant has challenged the correctness of learned Commissioner (Appeals)'s order dated 29th February 2012, in the matter of assessment under section 143(3) of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') for the assessment year 2008-09.

2. The main issue that we are required to adjudicate in this appeal is whether or not the learned CIT(A) was justified in confirming the disallowance of Rs 52,07,883, in respect of leather testing charges paid to TUV Product Und Umwelt GmbH – a tax resident of Germany, under section 40(a)(i) of the Act, on the ground that the assessee failed to discharge his tax withholding obligations in respect of the same.

3. The issue in appeal lies in a narrow compass of undisputed material facts. The assessee before us is a manufacturer and exporter of leather goods. On 14th August 2008, the assessee filed his return of income, declaring taxable income of Rs 5,81,56,220 which was later taken up for the scrutiny assessment proceedings. During the course of this scrutiny assessment proceedings, the Assessing Officer noticed that the assessee has made remittances aggregating to Rs 52,07,883 to a Germany based company, by the name of TUV Product Und Umwelt GmbH (TUV GmbH, in short), in respect of leather testing charges, but did not withhold the applicable taxes from these remittances. The Assessing Officer was of the view that since the assessee has made the remittances without withholding requisite tax deductions, the payments so made are not allowable as deductions in the hands of the assessee. It was in this backdrop that a show cause notice was issued requiring the assessee to show cause as to why these payments not be disallowed under section 40(a)(i) of the Act.

4. It was contended by the assessee that unless TUV GmbH is liable to be taxed in India, in respect of the income embedded in the remittances made to them, the assessee did not have any obligations to deduct the taxes at source. It was also contended that the services rendered by way of leather testing charges were not rendered in India. While stating that, "the intention of introducing the source rule was to bring to tax interest, royalty or fees for technical services by way of creating a fiction in Section 9, the source rule would mean that irrespective of the *situs* of services, the *situs* of taxpayer and the *situs* of utilization of services will determine the tax jurisdiction", assessee referred to the judgment of Hon'ble Supreme Court, in the case of Ishikwajima Harima Heavy Industries Ltd Vs DIT (288 ITR 708) wherein it is said to have been held that there must be sufficient territorial nexus between income sought to be taxed in India and the territory of India. It was thus contended that unless the services are rendered in India, the same cannot be brought to tax in India. As regards amendment in Section 9 post the Hon'ble Supreme Court decision in the case of Ishikwajima (supra), reliance was placed on Hon'ble Karantaka High Court's decision in the case of Jindal Thermal Power Co Ltd Vs DCIT (321 ITR

31) in support of the proposition that the said amendment has not really nullified the impact of Hon'ble Supreme Court's judgment in the case of Ishikwajima (supra). It was submitted that no testing operations were carried out by the TUV GmbH in India, and that, accordingly, income cannot be said to accrue or arise in India. It was also contended that unless TUV GmbH can be said to have a PE in India, which cannot be said in the present case, and unless the services are rendered in India, which is not the case here, the income of the TUV GmbH cannot be brought to tax in India. It was also submitted that the assessee that the testing services for which impugned payments are made donot benefit the assessee in any other way except for compliance with statutory requirements in Germany with regard to the safety of products. With this factual contention, reliance was placed on the decisions of the Authority for Advance Ruling in the cases of Cushman & Wakefields Pvt Ltd In Re (305 ITR 208) and Joint Accreditation Committee of Australia and New Zealand (2010-TII-28-ARA-INTL). None of these submissions, however, impressed the Assessing Officer. He was of the considered view that Explanation to Section 9 clearly states that for accrual of FTS, there is no requirement of residence, place of business or business connection in India. It was observed that if any payment is made by any person resident in India to a non resident person by way of fees for technical services, income is deemed to accrue or arise in India. It was because of this deeming fiction, according to the Assessing Officer, that the income is taxable in India. It was also observed that the double taxation avoidance agreement between India and Germany (Indo German tax treaty, in short) does not come to the rescue of the assessee since this treaty itself provides that the income on account of fees for technical services may be taxed in the source state as well. The Assessing Officer thus concluded that, "on the facts and in the circumstances of the case as discussed above, it is crystal clear that testing charge is payment on account of technical cum consultancy services only and is deemed to accrue or arise in India..and, therefore, leather testing charges paid ....of Rs 52,07,833, without deduction of tax at source as required under section 195, is disallowed under section 40(a)(i) of the Act and added to the income of the assessee". Aggrieved, assessee carried the matter in appeal

before the learned CIT(A) but without any success. In broad terms, he rejected the theory of territorial nexus on the basis of analysis in, which he extensively reproduced from, a coordinate bench decision in the case of Ashapura Minichem Ltd Vs ADIT (131 TTJ 291), and held that post 2010 amendment in Section 9(1), this theory of territorial nexus between the *situs* of activity and the tax jurisdiction is no longer relevant. It was also held that the decisions of Hon'ble Supreme Court in the case of Ishikwajima and of Hon'ble Karnataka High Court in the case of Jindal Power are no longer good law, as Section 9(1) itself stands materially altered now. Learned CIT(A) also rejected assessee's contention that since the assessee is a one hundred percent exporter, the source of his income is outside India, and accordingly, by the virtue of exception visualized in Section 9(1)(vii)(b) the said income cannot be brought to tax in India. Learned CIT(A) held that while the sale may have been made to the persons outside India, the business is clearly carried on in India and as such it cannot be said that the source of income was outside India. It was in this backdrop that he distinguished decision of a coordinate bench of this Tribunal, in the case of Havel India Pvt Ltd Vs ACIT (140 TTJ 283) and noted that it was case in which assessee had the customers as also the manufacturing facilities outside India and, therefore, the Tribunal's decision that the business was carried out outside India was on different set of facts. Learned CIT(A) also rejected assessee's reliance on Hon'ble Supreme Court's judgment in the case of GVK Industries Ltd Vs ITO (332 ITR 130), on the ground of that this decision does not hold Section 9(1)(vii) to be unconstitutional and that the observations made by Their Lordships are being read out of context. He also referred to and relied upon the decision of another coordinate bench of this Tribunal, in the case of Indian Summer Vs ACIT [4 ITR (Tribu) 181] in support of the proposition that the only requirement of Section 9(1)(vii) is that the fees paid the fees for technical services paid by a person, who is a resident of India, to a non resident and that such services should not be used in a business carried on the resident person outside India. Learned CIT(A) observed that, " ..in leather testing, for determination of quality, contents in leather, and doing the necessary testing and doing the necessary checking whether the material has any toxic chemicals

or not, before issuing the requisite certificate if its suitability to be used in manufacturing of shoes, an expertise in leather technology is required in which knowledge and skill of a technical expert is used, and, therefore, the leather testing is apparently in the nature of 'technical services'". He then referred to the provisions of Article 12 of Indo German tax treaty, analyzed the same and came to the conclusion that the testing charges , being consideration for technical services of testing leather, were clearly in the nature of technical services within the scope of Article 12(4) of the said tax treaty. Learned CIT(A) also rejected the assessee's plea to the effect that he cannot be expected to discharge the onus of tax deduction when law is amended with retrospective effect , by stating that the amendment was only clarificatory in nature and that, in any event, it was open to the assessee to move application under section 195(2) in case he had any doubts on the issue of taxability. It was also observed that the judicial precedents cited by the assessee, with regard to non applicability of penal provisions in respect of retrospective amendments, were on different facts and not applicable in the present context. In a very erudite and detailed order, thus, learned CIT(A) confirmed, and in fact fortified, the stand of the Assessing Officer. The assessee is not satisfied and is in further appeal before us.

5. We have heard the rival contentions at considerable length, perused the material on record and duly considered factual matrix of the case as also the applicable legal position. We will set out and deal with the arguments of the learned representatives as we take up each of the issues raised before us one by one. These issues can be divided in two broad categories – first, arguments on merits against the taxability of testing charges in the hands of TUV GmbH, and, second, arguments against applicability of legal provisions under section 40 (a)(i) disabling the deduction for testing charges so paid to TUV GmbH.

6. So far as taxability of leather testing fees in the hands of the TUV GmbH, in terms of the provisions of Indo German tax treaty is concerned, while learned

counsel fairly accepts that the issue of testing fees in terms of the treaty provisions is covered against him by a decision of the coordinate bench in the case of Ashapura Mibnichem Ltd *(supra),* he submits one aspect of the matter has been overlooked in this decision. The point is this. While Article 12(1) of the India German Double Taxation Avoidance Agreement does provide for taxation of the 'fees for technical services', it merely states that such fees "may be" taxed in the other contracting states, and that the expression "may" has a connotation much narrower than "shall" which alone can justify levy of taxes in the other contracting state. Learned counsel makes elaborate submissions on the connotations "may", "shall" in the context of the levy of taxes. Learned Departmental Representative, on the other hand, submits that even though the expression used is "may", it does entitle the other contracting state, i.e. the source state, to levy taxes in accordance with its domestic law. It is pointed out that the terminology used in the tax treaties is different from the tax laws but the scheme of taxation of fees for technical services, which are to be taxed in the source state as well, is free from doubt.

7. In our considered view, it is necessary to appreciate the fundamental position with regard to the treaties in the sense that treaties donot, and cannot, provide for taxation of any income; they limit the taxing authority of the contracting states. The tax treaties are primarily instrument allocating between such contracting states, with or without conditions, rights to tax income which have allegiance in more than one tax jurisdiction. A tax treaty does, therefore, only enable a contracting state to levy tax. Once it does so, the domestic law of the tax jurisdiction which has been granted the right to tax comes into play and it comes into play subject to such restrictions as may have been placed thereon, A tax treaty cannot force a contracting state to levy a tax. The expression 'shall only be taxed' in the context of the treaties is used only in the sense of restricting the other state from levying taxes on such income, as in Article 8 for example. The use of expression 'shall' in such situations is not to levy any taxes, since, as we have noted earlier, treaties cannot impose any taxes, but it does only imply that taxability, if at all, can be in the specified jurisdiction

alone. Let us, in this light, take a look at the provision of Article 12 of Indo German tax treaty.

8. Article 12 provides as follows:

Article 12
ROYALTIES AND FEES FOR TECHNICAL SERVICES

(1) Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

(2) However, such royalties and fees for technical services may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the recipient is the beneficial owner of the royalties, or fees for technical services, the tax so charged shall not exceed 10 per cent of the gross amount of the royalties or the fees for technical services.

(3) The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematograph films or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience.

(4) The term "fees for technical services" as used in this Article means payments of any amount in consideration for the services of managerial, technical or consultancy nature, including the provision of services by technical or other personnel, but does not include payments for services mentioned in Article 15 of this Agreement.

(5) The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties or fees for technical services, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties or fees for technical services arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right, property or contract in respect of which the royalties or fees for technical services are paid is effectively connected with such permanent establishment or fixed base. In such case, the provisions of Article 7 or Article 14, as the case may be, shall apply.

(6) Royalties and fees for technical services shall be deemed to arise in a Contracting State when the payer is that State itself, a Land or a political subdivision, a local authority or a resident of that State. Where, however, the person paying the royalties or fees for technical services, whether he is a resident of a Contracting State or not has in a Contracting State a permanent establishment or a fixed base in connection with which the liability to pay the royalties or fees for technical services was incurred, and such royalties or fees for technical services are borne by such permanent establishment or fixed base, then such royalties or fees for technical services shall be deemed to arise in the State in which the permanent establishment or fixed base is situated.

> (7) Where, by reason of special relationship between the payer and the beneficial owner or between both of them and some other Person, the amount of royalties or fees for technical services paid exceeds the amount which would have been paid in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Agreement.

9. A plain reading of the above provisions show that under the Indo German tax treaty, a source state has the rights to tax an income in the nature of 'royalties' and ' fees for technical services', as defined above, but the tax so levied, by the virtue of taxing rights allocated above, shall not exceed ten percent. In effect, therefore, when a source state taxes the said income at ten percent rate or less, the said levy is in accordance with the scheme of allocation of taxing rights. However, when taxes levied exceed the specified rate, the extent to which such taxes exceed the specified rate, it will be contrary to the scheme of the allocation of taxing rights under the treaty and the taxability will be restricted in terms of the limited rights so allocated to the source state.

10. In all fairness to the learned counsel, however, we are alive to the fact that a coordinate bench of this Tribunal, in the case of Pooja Bhatt Vs DCIT (2008 TIOL 558 ITAT MUM), had indeed drawn a line of demarcation between 'shall ', 'may' and 'may also' and, based on that analysis, held that an income cannot be taxed in the residence country unless it falls in the category where both the contracting states have the right to tax, which, in their esteemed view, will be represented by expression "may also". However, the question that we are called upon to adjudicate in this case did not fall for consideration in the said case, and as is the settled position of law, a judicial precedent is an authority for what it actually decides and not what may even reasonable follow from the same. We leave it at that.

11. In view of the above discussions, in our considered view, the TUV GmbH does not get any benefit from the provisions of the Indo German tax treaty, so far as taxability of its income from leather testing fees is concerned.

12. Coming to the merits of taxability of testing fees in the hands of TUV GmbH under section 9(1)(vii), we find that, in principle, the issue is covered against the assessee by decision of a coordinate bench, in the case of Ashapura Minichem *(supra)* wherein a coordinate bench, speaking through one of us (i.e. the Accountant Member), had observed as follows:

9. The legal proposition canvassed by the learned counsel, however, does no longer hold good in view of retrospective amendment w.e.f. 1st June 1976 in section 9 brought out by the Finance Act, 2010. Under the amended Explanation to Section 9(1), as it exists on the statute now, it is specifically stated that the income of the non-resident shall be deemed to accrue or arise in India under clause (v) or clause (vi) or clause (vii) of section 9(1), and shall be included in his total income, whether or not (a) the non-resident has a residence or place of business or business connection in India; or (b) the non-resident has rendered services in India. It is thus no longer necessary that, in order to attract taxability in India, the services must also be rendered in India. As the law stands now, utilization of these services in India is enough to attract its taxability in India. To that effect, recent amendment in the statute has virtually negated the judicial precedents supporting the proposition that rendition of services in India is a *sine qua non* for its taxability in India.

10. The concept of territorial nexus, for the purpose of determining the tax liability, is relevant only for a territorial tax system in which taxability in a tax jurisdiction is confined to the income earned within its borders. Under this system, any foreign income that is earned outside of its borders is not taxed by the tax jurisdiction, but then apart from tax heavens, the only prominent countries that are considered territorial tax systems are France, Belgium, Hong Kong and the Netherlands, and in those countries also this system comes with certain anti abuse riders. In other major tax systems, the source and residence rules are concurrently followed. On a conceptual note, source rule of taxation requires an income sourced from a tax jurisdiction to be taxed in this jurisdiction, and residence rule of taxation requires income, earned from wherever, to be taxed in the tax jurisdiction in which earner is resident. In the US tax system, this residence rule is further stretched to cover US taxation of all its citizens - irrespective of their domicile, and the source rule is also concurrently followed. It is this conflict of source and residence rules which has been the fundamental justification of mechanism to relieve a taxpayer, whether under a bilateral treaty or under domestic legislations, of the double taxation - either by way of exclusion of income from the scope of taxability in one of the competing jurisdictions or by way of tax credits. Except in a situation in which a territorial method of taxation is followed, which is usually also a lowest common factor in taxation policies of tax heavens, source rule is an integral part of the taxationsystem and any double jeopardy, due to inherent clash of

source and residence rule, to a taxpayer is relieved only through the specified relief mechanism under the treaties and the domestic law. It is thus fallacious to proceed on the basis that territorial nexus to a tax jurisdiction being *sine qua non* to taxability in that jurisdiction is a normal international practice in all tax systems. This school of thought is now specifically supported by the retrospective amendment to section 9.

13. Learned counsel, however, submits that the conclusion so arrived at in Ashapura Minichem's case *(supra)* is vitiated in law for the fundamental reason that it overlooks the decision of Hon'ble Supreme Court, in the case of GVK Industries Ltd Vs ITO (supra) which rules against the extra territoriality of the tax laws. As regards the subsequent special bench decision in the case of ADIT Vs Clifford Chance (154 TTJ 537), learned counsel fairly accepts that the special bench decision covers only with the scope of Section 9(1)(i) and the other segments of Section 9(1) have not been dealt with the said decision. The Special Bench has specifically observed that they are concerned with the scope of Section 9(1)(i) which has remained unaffected by the retrospective amendment made by Finance Act 2010. The question that we are, therefore, required to deal with is whether or not the Ashapura Minichem decision holds good law in the light of Hon'ble Supreme Court's decision in the case of GVK Industries *(supra).*

14. As far as Hon'ble Supreme Court's judgment in the case of GVK Industries is concerned, it does not, by any stretch of logic, hold against the constitutional validity of Section 9(1)(vii). The relevant observations made against the constitutional validity of laws having extra territorial implications are as follows:

> **(2) Does the Parliament have the powers to legislate 'for' any territory other than the territory of India or any part of it ?**
>
> **The answer to the above would be 'no'. It is obvious that Parliament is empowered to make laws with respect to aspects or causes that occur, arise or exist, or maybe expected to do so, within the territory of India and also with respect to extra-territorial aspects or causes that have an impact or nexus with India……Such laws would fall within the meaning, purport and ambit of grant of powers of Parliament to make laws "for the whole or any part of the territory of India" and they may not be invalidated on the ground that they require extra territorial operation. Any laws enacted by**

> **the Parliament with respect to extra territorial aspects or causes that have no nexus with India would be ultra vires….. and would be laws made for a foreign territory.**

15. A plain reading of the above observations by Their Lordships clearly indicates that as long as the law enacted by the Parliament has a nexus with India, even if such laws require extra territorial operation, the laws so enacted cannot be said to constitutionally invalid. It is only when the "**laws enacted by the Parliament with respect to extra territorial aspects or causes that have no nexus with India"** that such laws **"would be *ultra vires*".** As to what is acceptable nexus, we find guidance from Prof Michael Lang's rather recent book 'Introduction to the Law of Double Taxation Conventions' (published by Linde, Austria; ISBN 978-90-8722-082-2):

> **In international law practice, there are no significant limits on the tax sovereignty of states. In designing the domestic personal tax law, the national legislator can even tax situations when, for example, only a *"genuine link"* exists. It is only when neither the person nor the transaction has any connection with the taxing state that tax cannot be levied.**

16. There is a clear nexus between the taxability of services rendered to residents of a tax jurisdiction with that jurisdiction itself. As the assessee himself has observed in the written submissions reproduced in the assessment order at page 6 thereof, "the intention of introducing the source rule was to bring to tax interest, royalty or fees for technical services by way of creating a fiction in Section 9, the source rule would mean that irrespective of the *situs* of services, the *situs* of taxpayer and the *situs* of utilization of services will determine the tax jurisdiction". This source rule taxability has not been struck down by the GVK decision. All it says that there has to be reasonable nexus and impact. It is not, and cannot be, anybody's case that there is no nexus between income in the hands of a person providing technical services to India and India the tax jurisdiction. We, therefore, reject learned counsel's reliance on GVK decision.

17. Learned counsel then contends that, in any event, the provisions of Section 9 (1)(vii) will not come into play in this case because the entire testing process is automated. It is submitted that the provisions of Section 9(1)(vii) can come into play only in respect of such a technical service which involves human skills and interplay. Our attention is invited to a decision of the coordinate bench in the case of Siemens Ltd Vs CIT (ITA No 4356/Mum/2010; order dated 12th February 2013) in which it is held that " if a standard facility is provided through a usage of machine or technology, it cannot be termed as rendering of technical services", and it is contended that the leather testing services are rendered with the help of machines and, therefore, the same are not covered as being in the nature of technical services as envisaged under Section 9 (1)(vii). Learned counsel submits that human element, even at all involved, is no more than that of a rather routine process of making the reports while the core analysis work is done by the machines. When it was put to him that even if we assume that the core work is done by the machines, there is still quite a bit of human involvement, learned counsel submits that it is no more than that of a person reading the machine analysis. Learned Departmental Representative, on the other hand, invites our attention to the decision of Hon'ble Delhi High Court, which coordinate bench was presumably following in the Siemens decision (supra), which does indicate that it is only when the process is completely automated and is without any human involvement that the technical services involved could be beyond the scope of technical services envisaged under section 9(1)(vii).

18. While we are inclined to agree with the broad principles canvassed by the learned counsel, we donot think these principles lead to the conclusions he is seeking to justify. It is, if we may say so, classical case of right propositions being used to justify the wrong conclusions.

19. We agree that when no human intervention is involved in any services, such services cannot be treated to be of the nature which can be covered by the

scope of Section 9 (1)(vii). The detailed reasoning for this approach, as was noted by another coordinate bench in the case of ITO Vs Right Florists Pvt Ltd (154 TTJ 142), is as follows:

> *24. While there is no specific definition assigned to the technical services, and Explanation 2 to Section 9(1)(vii), as also Article 12(2)(b) merely states that 'fees for technical services' will include considering of "rendering of any managerial, technical or consultancy services".It is significant that the expression 'technical' appears alongwith expression 'managerial' and 'consultancy' and all the three words refer to various types of services, consideration for which is included in the scope of 'fees for technical services'. The significance of this company of words lies in the fact that, as observed by a coordinate bench of this Tribunal in the case of Kotak Securities Ltd Vs DCIT (50 SOT 158), "when two or more words which are susceptible to analogous meaning are used together they are deemed to be used in their cognate sense. They take, as it were, their colours from each other, the meaning of more general being restricted to a sense analogous to that of less general". Just as a man is known by the company he keeps ,a word is also to be interpreted with reference to be accompanying words. Words derive colour from the surrounding words. Broom's Legal Maxims (10th Edn.) observes that "It is a rule laid down by Lord Bacon, that copulation verborum indicate cceptationem in eodem sensu i.e. the coupling of words together shows that they are to be understood in the same sense. It is, therefore, clear on principle that as long as words are used together in a statutory provision, they take colour from each other and restrict its meaning to the genus of these words. In this way, the meaning of words is restricted because of other words in the same group of words, and the meaning is so restricted to the species or genus of those other words. Genus of these words should be clearly discernible from the lowest common factor in those words. The lowest common factor in 'managerial, technical and consultancy services' seems to be the human intervention, because while these three words are of wide scope and are in varied field, the only common thread in these words seems to be that the services, which are essentially professional services in nature, can be rendered with human interface. A managerial or consultancy service can only be rendered with human interface, while a technical service can be rendered with human interface as also without human interface. A technical service, for example, could be automated analysis of a chemical compound without any scope of any human contribution at any stage, and a technical service could also be physical examination by an expert chemical analyst, with or without the help of machines, of the same chemical compound. However, when we try to restrict the meaning of technical services to the services which are covered by managerial and technical services as well, services without human interface will have to*

be taken out of its ambit. It is, therefore, clear on principle that as long as words are used together in a statutory provision, they take colour from each other and restrict its meaning to the genus of these words which is evident by the lowest common factor in those words. The lowest common factor in 'managerial, technical and consultancy services' being the human intervention, as long as there is no human intervention in a technical service, it cannot be treated as a technical service under Section 9(1)(vii).There is one more approach to this issue, even though the results will be the same. The other way of looking at these three words on the basis of the principle of noscitur a sociis is, as was done by Hon'ble Delhi High Court in the case of CIT Vs Bharti Cellular Limited (319 ITR 139), is that the common characteristic of the majority of the words be read as limitation on the scope of the other words. While doing so, Their Lordships had observed as follows:

> *13. ……In the said Explanation [i.e. Explanation 2 to Section 9(1)(vii)] the expression fees for technical services means any consideration for rendering of any managerial, technical or consultancy services. The word technical is preceded by the word managerial and succeeded by the word consultancy. Since the expression technical services is in doubt and is unclear, the rule of* noscitur a sociis *is clearly applicable.*
>
> *The said rule is explained in Maxwell on The Interpretation of Statutes (Twelfth Edition) in the following words:-*
>
> > *Where two or more words which are susceptible of analogous meaning are coupled together,*noscitur a sociis, *they are understood to be used in their cognate sense. They take, as it were, their colour from each other, the meaning of the more general being restricted to a sense analogous to that of the less general.*
>
> *This would mean that the word technical would take colour from the words managerial and consultancy, between which it is sandwiched.*
>
> *The word managerial has been defined in the Shorter Oxford English Dictionary, Fifth Edition as:- of pertaining to, or characteristic of a manager, esp. a professional manager of or within an organization, business, establishment, etc.*
>
> *The word manager has been defined, inter alia, as:- a person whose office it is to manage an organization, business establishment, or public institution, or part of one; a person with the primarily executive or supervisory function within an organization etc; a person controlling the activities of a person or team in sports, entertainment, etc.*

> *It is, therefore, clear that a managerial service would be one which pertains to or has the characteristic of a manager. It is obvious that the expression manager and consequently managerial service has a definite human element attached to it. To put it bluntly, a machine cannot be a manager.*
>
> *14. Similarly, the word consultancy has been defined in the said Dictionary as the work or position of a consultant; a department of consultants. Consultant itself has been defined, inter alia, as a person who gives professional advice or services in a specialized field. It is obvious that the word consultant is a derivative of the word consult which entails deliberations, consideration, conferring with someone, conferring about or upon a matter. Consult has also been defined in the said Dictionary as ask advice for, seek counsel or a professional opinion from; refer to (a source of information); seek permission or approval from for a proposed action. It is obvious that the service of consultancy also necessarily entails human intervention. The consultant, who provides the consultancy service, has to be a human being. A machine cannot be regarded as a consultant.*
>
> *15. From the above discussion, it is apparent that both the words managerial and consultancy involve a human element. And, both, managerial service and consultancy service, are provided by humans. Consequently, applying the rule of* noscitur a sociis, *the word technical as appearing in Explanation 2 to Section 9 (1) (vii) would also have to be construed as involving a human element.*

25. We may also point out that while this judgment did not meet approval of Hon'ble Supreme Court, in the judgment reported as CIT Vs Bharti Cellular Limited (330 ITR 239), on the short factual aspect regarding fact of human intervention. It was for recording the factual findings on this aspect that the matter was remitted to the file of the Assessing Officer. However, so far as the principle laid down by Hon'ble Delhi High Court on the application of principle of noscitur a sociis *in restricting the scope of 'technical services' to 'technical services with a human interface' was concerned, Their Lordships of Hon'ble Supreme Court took note of the said principle and left it intact. The stand taken by Hon'ble Delhi Court, in our humble understanding, stands approved. Of course, what constitutes a technical service without human interface is essentially a question of fact and each case will have to be examined on its own facts. However, as long as there is no human intervention in a technical service, in the light of law so laid down, it cannot be treated as a technical service under Section 9(1)(vii).*

20. The principle of law, as clearly discernable from the observations made by Hon'ble Delhi High Court in Bharati Cellular's case (supra), is that "***the word technical as appearing in Explanation 2 to Section 9 (1) (vii) would also have to be construed as involving a human element."*** In other words, when services have no human element involved, such services cannot be treated as 'technical services' for the purposes of Section 9(1)(vii). Let us also not forget that these observations were made in the context of inter connect and port access facility which is facility to use the gateway and the network of other cellular operator. This is a completely automated process with no human involvement at all, and yet , when the matter reached Hon'ble Supreme Court, Their Lordships, in the judgment reported as CIT Vs Bharati Cellular Ltd (330 ITR 239), did remit the matter back to the Assessing Officer by observing as follows:

> ***The problem which arises in these cases is that there is no expert evidence from the side of the Department to show how human intervention takes place, particularly, during the process when calls take place, let us say, from Delhi to Nainital and vice versa. If, let us say, BSNL has no network in Nainital whereas it has a network in Delhi, the Interconnect Agreement enables M/s. Bharti Cellular Limited to access the network of BSNL in Nainital and the same situation can arise vice versa in a given case. During the traffic of such calls whether there is any manual intervention, is one of the points which requires expert evidence. Similarly, on what basis is the "capacity" of each service provider fixed when Interconnect Agreements are arrived at?***
>
> ***For example, we are informed that each service provider is allotted a certain "capacity". On what basis such "capacity" is allotted and what happens if a situation arises where a service provider's "allotted capacity" gets exhausted and it wants, on an urgent basis, "additional capacity"?***
>
> ***Whether at that stage, any human intervention is involved is required to be examined, which again needs a technical data. We are only highlighting these facts to emphasise that these types of matters cannot be decided without any technical assistance available on record.***
>
> ***There is one more aspect that requires to be gone into. It is the contention of Respondent No.1 herein that Interconnect Agreement between, let us say, M/s. Bharti Cellular Limited and BSNL in these cases is based on obligations and counter obligations, which is called a "revenue sharing contract". According to Respondent No.1, Section 194J of the Act is not attracted in the case of "revenue sharing contract". According to Respondent No.1, in such contracts there is only sharing of revenue and, therefore, payments by revenue sharing cannot constitute "fees" under***

Section 194J of the Act. This submission is not accepted by the Department. We leave it there because this submission has not been examined by the Tribunal.

In short, the above aspects need reconsideration by the Assessing Officer. We make it clear that the assessee(s) is not at fault in these cases for the simple reason that the question of human intervention was never raised by the Department before the CIT. It was not raised even before the Tribunal; it is not raised even in these civil appeals. However, keeping in mind the larger interest and the ramification of the issues, which is likely to recur, particularly, in matters of contracts between Indian Companies and Multinational Corporations, we are of the view that the cases herein are required to be remitted to the Assessing Officer (TDS).

Accordingly, we are directing the Assessing Officer (TDS) in each of these cases to examine a technical expert from the side of the Department and to decide the matter within a period of four months. Such expert(s) will be examined (including cross-examined) within a period of four weeks from the date of receipt of the order of this Court. Liberty is also given to Respondent No.1 to examine its expert and to adduce any other evidence

21. In Siemens case *(supra),* however, the coordinate bench went much beyond what was held by the Hon'ble Courts above. The coordinate bench has concluded that, "Thus if a standard facility is provided through a usage of machine or technology, it cannot be termed as rendering of technical services. Once in this case it has not been disputed that there is ***not much of*** **the human involvement** for carrying out the tests of circuit breakers in the Laboratory and it is ***mostly*** **done by machines and is a standard facility**, it cannot be held that ……..(the assessee) is rendering any kind of technical services to assessee" . These observations are not only based on erroneous analysis of the legal position but directly contrary to the law laid down by Hon'ble Supreme Court wherein it is held that even in a case of completely automated process like interconnect and port access facility, which is facility to use the gateway and the network of other cellular operator, the Assessing Officer is still required to examine **"whether at any stage, any human intervention is involved".** It is not a question of more of, or less of, human involvement. It is, in our humble understanding, the question of presence of or absence of human involvement. Our distinguished colleagues clearly erred in reading the unambiguous mandate

of law laid down by Hon'ble Courts above. However, even as we disagree with the coordinate bench decision, for the reasons we will set out in a short while, we see no need to remit the matter to the larger bench. That would be, as we will see a little later, an academic exercise on the facts of the present case. Suffice to say, we are not inclined to accept this plea of the assessee. In any event, there is nothing on records to even demonstrate the precise process of leather testing, the actual steps involved in the process and parameters involved, nor these aspects of the matter have been examined by any of the authorities below.

22. The next plea of the assessee is whether the fees paid by the assessee, on account of leather testing charges, is in the nature of technical services within meanings of Section 9(1)(vii) or not is absolutely academic on the facts of this case because the assessee being a one hundred percent exporter, and the source of income thus being outside India, the exception visualized in Section 9(1)(vii)(b) will come into play.

23. Learned counsel's next argument is that since assessee is one hundred percent exporter, we have to proceed on the basis that the source of assessee's income, for which testing services are used, is outside India, and, accordingly, by the virtue of exception visualized in Section 9(1)(vii)(b), the fees for technical services paid to TUV GmbH will not be taxable in India.

24. In order to deal with this plea, let us take a fresh look at Section 9 (1)(vii) first:

> ***Section 9 (1) (vii)***
>
> ***The following income shall be deemed to accrue or arise in India***
>
> ***(vii) income by way of fees for technical services payable by—***
> ***(a) the Government; or***
> ***(b) a person who is a resident, except where the fees are payable in***

respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or

(c) a person who is a non-resident, where the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India:]

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government.]

[Explanation 1 : For the purposes of the foregoing proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date.]

Explanation[2] : For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".

25. Section 9(1)(vii)(b) makes it clear that the exception in respect of taxability of fees for technical services paid by an Indian resident is that when such fees is paid in respect of " services utilized in a business or profession carried on by such person outside India or for the purpose of making or earning any income from any source outside India". This exception thus has two distinct segments- first, in respect of services utilized in a business or profession carried on by Indian resident outside India, and – second, in respect of services utilized in respect of earning any income from a source outside India. No doubt whether an India based business is one hundred percent export oriented unit or not, it is still a business carried on in India, and it cannot, therefore, be covered by the first limb of exception envisaged in Section 9(1)(vii)(b). Even if entire products are sold outside India, the fact of such export sales by itself does not make

business having been carried outside India. What matters really, in this perspective, is whether or not business is carried on in India or not, and once it is an undisputed position that business is set up and carried on India, irrespective of where the end consumers are, the business is carried on outside India. However, the scope of second limb of this exception is rather narrow. As against use of expression 'profession or business carried on …….outside India', this exception refers to use of service in 'making or earning any income from any source outside India'. In order to be covered by this exception, what is material is that, irrespective of where the business is situated, the services need to be used for earning or making income from any source outside India. A business outside India and a source outside India are used together in contrast, and can be viewed as reflecting relatively active and passive activities. For example, if technical service is used in a business activity outside India, it could be covered by the first category, while technical service used in an asset which gave on lease could be in the second category. The question, however, is whether the customers being outside India could be viewed as source of income. In our considered view, the source of income, whether customers are inside India or outside India, continues to be business in India. A customer is an important part of the business but no matter how important a segment of business is, such a part of the business cannot be the business itself. The assessee has all along claimed that the leather testing services were required under instructions from importers and so as to enable its products to enter the German markets. All it indicates is that the services were required because of the foreign importers, but, as the mandate of the law, is that aspect itself is not decisive and sufficient for the purpose of exclusion from the scope of Section 9(1)(vii). The services should be for the purpose of earning an income from a source outside India. A customer is not the source of income, he is an important part of the business, which, in turn, is the source of income. As regards the decision of coordinate bench in Havel's case, that was a case in which not only the customers but also certain manufacturing facilities were outside India. We agree that once the manufacturing facilities are outside India and the customers

are also outside India, such a situation will indeed be covered by the exception visualized in Section 9(1)(vii)(b).

26. Learned counsel's argument that the factual plea of the assessee that the business source was outside India has not been rejected by the authorities below, and should, as such, be taken as correct, does not impress us at all. That will be too superficial an approach for a judicial forum which is a final fact finding forum as well.

27. In view of the above discussions, as also bearing in mind entirety of the case, we reject this plea of the assessee as well. Just because the user of services is a one hundred percent export unit, in our considered view, it cannot be said that the technical services are used "for the purpose of making or earning any income from any source outside India", and, accordingly, outside the ambit of income taxable as fees for technical services under section 9(1)(vii).

28. In the light of the foregoing discussions, in our considered view, the payments made to TUV GmbH were taxable in India, and, accordingly, it cannot be said, based on the material on record and arguments before us, that the assessee did not have obligation to withhold taxes from the remittances made to TUV GmbH for leather testing charges. However, as hold so, we are alive to the fact that right now we are not dealing with the penal, recovery or other consequences of non deduction of tax at source, which are of different dimensions and import, and therefore, our findings above donot foreclose any plea or arguments that the assessee may like to take in the course of such proceedings, if any.

29. Learned counsel, however, submits that even if it is assumed, though he does not admit so, that the income embedded in leather testing charges paid to the TUV GmbH was taxable in India, since entire amount was paid during the relevant previous year itself and since no part of the same remaining outstanding at the year end, the disallowance under section 40(a)(i) cannot be

made in the light of Special Bench decision in the case of Merlyin Shipping & Transport Vs ACIT (136 ITD SB 23) which is said to have been approved by Hon'ble jurisdictional High Court in the case of CIT Vs Vector Shipping Services (ITA No 122 of 2013; judgment dated 9th July 2013).

30. We are unable to accept this plea. There is no dispute that the Special Bench decision is in the context of Section 40(a)(ia) which is of recent origin and the majority view therein heavily relied upon the wordings originally proposed in the enactment of Section 40(a)(ia) which were in sharp contrast with the wordings actually used in the enactment of Section 40(a)(ia), as also certain other issues which donot touch upon the scope Section 40(a)(i). Section 40(a)(i) debars the deduction of "any interest , royalty, fees for technical services or other sum chargeable under this Act, which is payable outside India, on which tax has not been paid or deducted under Chapter XVII- B" In contrast with these words, Section 40(a)(ia) used the expression "payable to a resident". Obviously, the scope of setting of the words 'payable' in these two situations is materially different and there can indeed be a school of thought, howsoever detached from the reality as it may be, that amount payable to a resident, in the context of Section 40(a)(ia), reflects amount remaining payable. We are not concerned with that aspect of the matter nor do we need to deal with the same. Suffice to say that what is decided in the context of Section 40(a)(ia) does not apply to Section 40(a)(i) and the assessee thus does not derive any advantage from the decisions in the context of Section 40(a)(i). In our considered view, the provisions of Section 40(a)(i) cannot be interpretated in such a manner so as to restrict the scope of section to only amounts remaining payable at the end of the year, because, apart from the difference in wording of Section 40(a)(i) vis-a-vis Section 40(a)(ia) and other factors, such an interpretation will make the section redundant and it is one of the fundamental principles of interpretation is to interpret is *ut res magis valeat quam pereat*, i.e., in such a manner as to make it workable rather than redundant, and to understand the words with reference to the subject-matter, i.e., *verba accopoenda sunt secundum subjectum*

materiam. It is also an elementary legal principle, as was also held by Hon'ble Bombay High Court in the case of CIT Vs Sudhir Jayantilal Mulji (214 ITR 154) that a judicial precedent is an authority for what it actually decides and not what may what come to follow from some observations made therein.

31. Learned counsel also submits in any event, it is because of a retrospective amendment in law . It is submitted that the retrospective amendment was brought about by the Finance Act 2010 which was nowhere in sight at the material point of time, i.e. previous year relevant to the assessment year 2008-09. Learned counsel submits that the assessee cannot be penalized for performing the impossible task of deducting tax at source in accordance with the law which was brought on the statute book much after the point of time when tax deduction obligations were to be discharged. Our attention is invited to the decisions of a coordinate bench in the case of Channel Guide India Ltd Vs ACIT (139 ITD 49), wherein, following the views expressed by Ahmedabad bench in the case of Sterling Abrasives Ltd Vs ITO (ITA No. 2234 and 2244/Ahd/2008; order dated 2008), it is held that law cannot cast the burden of performing the impossible task of performing tax withholding obligations with retrospective effect, and, accordingly, the disallowance under section 40(a)(i) cannot be made in a situation in which taxability is confirmed only as a result of retrospective amendment of law. Learned counsel has also cited several other decisions in support of the proposition that in the case of retrospective amendment, the assessee cannot be punished for not complying with the law as it did not exist at the material point of time.

32. Even as we donot think that the provisions of Section 40(a)(i) are penal provisions in nature, particularly as the related deduction is allowed even in a subsequent period when tax withholding obligation is discharged, and even as we are alive to the fact that we are not dealing with consequences of non tax deduction of tax at source under section 201, as was the position in the case of Sterling Abrasives Ltd (supra), once there is a coordinate bench decision on this issue in favour of the assessee as in the case of Channel Guide *(supra)*, and such

a decision is not a manifestly erroneous decision, we see no reasons to take any other view of the matter than the view so taken by the coordinate bench. It is hardly necessary to emphasize that considerations of judicial propriety and decorum require us to normally follow the coordinate bench decision unless there are very strong and compelling reasons to refer the matter to larger bench. It is not one of those cases. We are inclined to agree with this view which also seems to be reasonable and justified. In the case of Channel Guide (supra), the coordinate bench has observed that the amount paid to the foreign enterprise was not taxable in India in the light of the legal position as it prevailed at that point of time, and it became taxable in India only as a result of the retrospective amendment in Section 9(1), the said payment cannot be disallowed by invoking section 40(a)(i). The situation is the same here. It is only as a result of the amendment in Section 9(1), by the virtue of Finance Act 2010, that the training fees paid to the TUV GmbH can be said to be taxable in India. As for the earlier period, even though the amendment is said to be merely clarifiactory in nature, in view of Hon'ble Supreme Court's judgment in the case of Ishikwajima *(supra)* and in view of the fact that services were rendered outside India – even if utilized in India, the impugned leather testing fees was not taxable in India. Such being the position, and respectfully following the decision of coordinate bench in the case of Channel Guide (supra), we hold that the disallowance under Section 40(a)(i) cannot be invoked on the facts of this case.

33. In the light of the above discussions, and for the reasons set out above, we delete the disallowance of Rs 52,07,883. The assessee gets the relief accordingly.

34. In the result, ground no. 1 is allowed in the limited terms indicated above. The other grounds of appeal, i.e. ground nos. 2 and 3, because of the smallness of the amounts were not really pressed before us. That fact however cannot be put against the assessee in the subsequent years or in penalty proceedings. With these observations, the ground no. 2 and 3 are dismissed.

35. In the result, the appeal is partly allowed in the terms indicated above. Pronounced in the open court today on 1st day of November, 2013.

Sd/-	Sd/-
Bhavnesh Saini	**Pramod Kumar**
(Judicial Member)	(Accountant Member)

Agra, the 1st day of November, 2013

Copies to : *(1) The appellant*
(2) The respondent
(3) CIT
(4) CIT(A)
(5) The Departmental Representative
(6) Guard File

By order etc

Senior Private Secretary
Income Tax Appellate Tribunal
Agra bench, Agra