HIGH COURT OF ALLAHABAD

Commissioner of Income-tax, Allahabad

v.

Model Exims Kanpur*

SUNIL AMBWANI AND SURYA PRAKASH KESARWANI, JJ.
IT APPEAL DEFECTIVE NO. 164 OF 2011†
SEPTEMBER 10, 2013

A.N. Mahajan and **D. Awasthi** *for the Appellant.* **S.D. Singh** *for the Respondent.*

ORDER

1. We have heard Shri Dhananjay Awasthi, learned counsel for the appellant. Shri Krishna Dev Vyas appears for the respondent.

2. The explanation of delay of 13 days in presenting the appeal has not been seriously opposed. We have gone through the cause shown for condonation of delay. The explanation is good and sufficient. The delay of 13 days in filing the appeal is condoned.

3. With the consent of parties the matter was heard.

4. This appeal has been preferred by the income tax department under Section 260A of the Income Tax Act, 1961 against the order dated 28.4.2011 passed by the Income Tax Appellate Tribunal (ITAT) in I.T.A. No.754/LKW/2010 for the assessment year 2007-08.

5. The department has preferred following questions of law for consideration in this appeal:—

"1. Whether the Hon'ble Income Tax Appellate Tribunal is justified in law and on facts in putting reliance on the CBDT's **circular no.786 dated 07.02.2000** whereas no cognizance has been taken of the Board's **circular No.30/2009 dated 25.03.2009**. The circular clarifies the ambiguous interpretation of provisions of law. Its nature is clarificatory and is therefore, applicable retrospectively.

2. Whether the Hon'ble Income Tax Appellate Tribunal is justified in law and on facts in ignoring the ratio of judgment of Hon'ble Supreme Court in the *CIT* v. *Moser Baer India (P) Ltd.*, [2009] 315 ITR 460 (SC) wherein it was held that the clarificatory nature of amendment in statute is retrospective in nature.

3. Whether the Hon'ble Income Tax Appellate tribunal is justified in law and on facts in ignoring the Explanation inserted by Finance Act, 2010 respectively w.e.f. 01.06.1976 in sub section (1)(viii) of Section 9 of Income Tax Act, 1961."

6. Brief facts giving rise to this case as stated in the order of the ITAT are quoted as below:—

> 'The facts of the case, in brief, are that the assessee is a partnership and was engaged in the business of manufacturing and export of finished leather, Shoe-uppers and leather products. The assessee was running two units-one at Jajmau and other at Banthar and filed the return on 30.10.2007 declaring an income of Rs.80,16,170, which was processed under Section

143(1) of the I.T. Act. Later on, the case was selected for compulsory scrutiny. During the assessment proceedings, the AO observed that the assessee had paid a sum of Rs.57,49,489 to the claimed overseas entities without deduction of income-tax at source under Section 195 of the income-tax Act, 1961 (In short "the Act"). The AO confronted the assessee with the provisions contained under Section 195 and Section 9 of the Act and called upon to show cause as to why the aforesaid sum be not disallowed under Section 40(a)(ia) of the Act. The assessee objected to the proposed disallowance and submitted that the expenses had been incurred in view of the business expediencies to further the business interest of the assessee overseas by the recipients having expertise in such matters, who were non-residents within the meaning of the relevant provisions of the Act, as such, there was no statutory liability on the part of the assessee to deduct at source under Section 195 of the Act. The submissions of the assessee have been highlighted by the AO at page 25 of the assessment order dated 15.12.2009 which read as under:

"(*a*) Payment of commission has been made to foreign nationals operating from foreign territories,

(*b*) The recipients have no office, branch or any other establishments in India,

(*c*) The commission has been paid in respect of the services rendered by the recipients, outside Indian territory,

(*d*) The payment has been received by the recipients out of India,

(*e*) These payments are squarely covered by the directions issued by the Central Board of Direct Taxes through Circular No.23 of 1969, 163 of 1975 and 786 of 2000,

(*f*) The aforesaid income termed as commission is not taxable under the scheme of Income Tax Act, 1961.

(*g*) There was no liability on the part of the assessee to deduct income tax at source u/s 195 or any other provisions of the Act, and

(*h*) Therefore, the same cannot be disallowed u/s 40(a)(ia) of the Income Tax Act, 1961."

The AO was not satisfied with the explanation of the assessee and made the disallowance of Rs.57,49,489 for the reason stated at pages 25 to 34 of the assessment order dated 15.12.2009. For the sake of repetition, the same are not repeated here. The AO, while making the disallowance, held as under:

" ...there there was mandatory liability on the part of the assessee under section 195 of the Income Tax Act, 1961 read with section 9(1)(vii) thereof to deduct income tax at source from the sum of Rs. 35,41,082/- which he has debited in his books of accounts as commission to his claims overseas agents. Since he has failed to deduct income tax at source, the consequent provision contained under section 40a(ia) of the Act are squarely applicable to the facts of the case and accordingly,, a sum of Rs.57,49,489/- is disallowed".'

7. In appeal the CIT(A) held that AO has not brought anything on record, which could demonstrate that there agents had been appointed as selling agents, designers & technical advisers. In absence of any such evidence, this observation of the AO is mere conjecture and

therefore, no cognizance of the same can be taken. The Circular No.7 of 2009 dated 22.10.2009 withdrawing Circular No.23 of 1969, 163 of 1975 and 786 of 2000 will be operative only from 22.10.2009 and not prior to that date. The withdrawal of earlier circulars w.e.f. 22.10.2009 has no bearing to the instant assessment.

8. The ITAT considered the submissions of both the parties and held relying upon its earlier decision in *Dy. CIT* v. *Sanjiv Gupta* that where a circular issued earlier created a vested right in the tax-payer and such right is sought to be curtailed or withdrawn by a subsequent circular, then such subsequent circular will not have a retrospective effect. The ITAT confirmed the order of CIT(A) and dismissed the appeal.

9. Shri Dhananjay Awasthi submits that liability to deduct tax arises out of Section 195 of the Act. The disallowance was made by A.O. under Section 40(a)(i) for non-deduction of tax at source under Section 195. The liability has to be determined in accordance with the provisions of law and not of the circular. Even if earlier circulars did not make it obligatory on the part of assessee to deduct TDS since by Circular No.7 of 2009 all earlier circulars were withdrawn, the assessee would be liable as the withdrawal of the earlier circulars would be retrospective in nature and further that the assessment has to be made after withdrawal of the circular in accordance with law. The Circulars did not create any vested right and were only by way of clarification, which were withdrawn. The observations made by the A.O. under Section 40(a)(i) for non-deduction of tax at source under Section 195 was justified.

10. Shri Dhananjay Awasthi has relied upon *CIT* v. *Moser Baer India Ltd.* [2009] 315 ITR 460 (SC) in which considering the provisions of Explanation 4 to Section 271(1)(c)(iii) the Supreme Court held that the amendment is only clarificatory and would apply even to earlier assessment years.

11. In the present case we are concerned with the circulars, which did not oblige the assessee to deduct TDS. The assessment in question for the assessment year 2007-08 would be governed by Circular, which was operative at the relevant time. The assessee was not entitled to deduct TDS. The department could not have taken different stand in subsequent years or assessment year 2007-08, when the circulars were operative and were not withdrawn. Circular No.7 of 2009 dated 22.10.2009 withdrawing earlier circulars became operative only from 22.10.2009.

12. We also do not agree with learned counsel for the income tax department that there was obligation to deduct tax at source under Section 195 on the commission paid to non-resident recipient, who was not liable to pay tax in India. In such case the assessee payer was not liable to deduct tax at source under Section 195(1).

13. Learned counsel for the respondent assessee submits that apart from argument based on Circular, the CIT(A) also observed as a matter of fact that the A.O. has not brought anything on record, which could demonstrate that non-resident agents had been appointed as selling agents, designers or technical advisers. The payment of commission to foreign agents did not entitle such foreign agents to pay tax in India and thus the TDS was not liable to be deducted.

14. Having carefully considered the submissions, we are of the view that the circulars in the relevant year was binding upon the department and assessee can challenge the affect of the Circular but that the A.O. did not have any right to ignore the circulars and to disallow non-deduction of tax at source under Section 195 and under Section 40(a)(i) of the Act.

15. The questions of law are thus decided in favour of the assessee and against the revenue. The income tax appeal is dismissed.