

## **No TDS on sales commission paid to non-residents for services rendered outside India**

The Hon'ble ITAT, Jaipur in ***Modern Threads India Limited v. ACIT (Income Tax Appeal Nos. 198/JP/2019 and 199/JP/2019 decided on February 15, 2021)*** has held that payment of sales commission by the assessee to non-resident agents for the services rendered outside India will not fall in the category of the income received or deemed to be received in India as well as accrues or arises or is deemed to accrue or arise in India. Hence, there will be no liability to deduct tax at source ("**TDS**") under Section 195(1) of the Income Tax Act, 1961 ("**IT Act**") and the provisions of Section 40(a)(i) of the IT Act that is disallowance of such commission cannot be invoked.

### **Facts:**

Modern Threads India Limited ("**the Appellant**") is a public limited company deriving income from polyester viscose, blended woollen yarn etc., and the company was declared a sick company by the Board of Financial Reconstruction on May 21, 2005.

The Assessing Officer ("**the AO**") while completing the assessment mentioned that the Appellant had paid commission of Rs. 99,84,435/- to foreign agents as sales commission during the year and no TDS was deducted as per the provisions of Section 195 of the IT Act. A show cause notice was issued to the Appellant as to why this commission should not be disallowed under Section 40(a)(i) of the IT Act in view of insertion of Explanation 2 to Section 195(1) of the IT Act vide Finance Act, 2012 with retrospective effect from April 01, 1962. The Appellant in response to show cause notice filed a detailed reply but it was rejected by the AO and the sum was disallowed in terms of Section 40(a)(i) of the IT Act.

The Appellant filed an appeal before CIT(Appeals) but the appeal was rejected and the order of AO was upheld.

The Appellant aggrieved by the order of CIT(Appeals) ("**Impugned order**") filed an appeal before Hon'ble ITAT Jaipur.

### **Issue:**

- Whether TDS should be deducted on the sales commission paid to the non-residents as per the provisions of Section 195(1) of the IT Act?
- Whether Section 40(a)(i) of the IT Act can be invoked?

### **Held:**

The Hon'ble ITAT, Jaipur in ***Income Tax Appeal Nos. 198/JP/2019 and 199/JP/2019 decided on February 15, 2021*** has held as under:

- Referred on the judgement of the Hon'ble ITAT, Jaipur in ***M/S JLC Electromet Pvt. Ltd. v. ACIT (Income Tax Appeal Nos. 1494/JP/2018 and 23/JP/2019 decided on September 4, 2019)*** wherein it was held that:
  - Section 195(1) of the IT Act provides that any person responsible for paying to a non-resident, not being a company or to a foreign company, any interest or any other sum chargeable under the provisions of IT Act shall deduct income tax thereon at the rates in force.
  - Section 195 of the IT Act requires any person to deduct TDS before making payments to a non-resident if the income of such non-resident is chargeable to tax in India.
  - Once the payment in question is commission then the provisions of Section 40(a)(i) of the IT Act are applicable only if such sum is chargeable to tax under IT Act.
  - Commission paid to non-resident outside India for the services rendered outside India will not fall in the category of the income received for deemed or received in India as well as accrues or arises or is deemed to accrue or arise in India.
  - Accordingly, when the amount paid by the assessee is not chargeable to tax in India then the assessee is not liable to deduct TDS and consequently the provisions of Section 40(a)(i) of the IT Act cannot be invoked for making the disallowance.
- Relied on the above-mentioned pari-materia case to hold that the commission paid to non-resident outside India for the services rendered outside India will not fall in the category of the income received or deemed to be received in India as well as accrues or arises or is deemed to accrue or arise in India.
- Found that, out of total commission payment of Rs. 99,84,436/- an amount of Rs. 1,55,867/- has been paid to a resident entity on which TDS has already been deducted which is again out of the ambit of provisions of Section 40(a)(i) of the IT Act.

- Held that, the sales commission payment or part thereof cannot be held chargeable to tax in India and in absence of any income chargeable to tax, there will be no liability to deduct TDS under Section 195(1) of the IT Act and the provisions of Section 40(a)(i) ibid therefore cannot be invoked in the instant case.
- Therefore, directed the AO to delete the disallowance made by invoking the provisions of Section 40(a)(i) of the IT Act.

### **Our Comments:-**

It may be noted that similar views were taken by Hon'ble High Court, Gujarat in the case ***PCIT v. Komal Amin Exports Pvt. Ltd. (R/Tax Appeal Nos. 1397 of 2018 and 1398 of 2018 decided on February 18, 2019)*** wherein it was held that when the commission paid to the non-resident agents was neither received or deemed to be received in India nor accrued or was deemed to accrue in India, no income was chargeable to tax under the provisions of the IT Act, then there is no obligation on the assessee to deduct TDS under Section 195(1) of the IT Act and consequently the provisions of Section 40(a)(i) ibid will not apply.

### **Relevant Provisions:-**

#### **Section 195(1) of IT Act:**

*"195. Other sums.*

*(1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest (not being interest referred to in section 194LB or section 194LC) or section 194LD or any other sum chargeable under the provisions of this Act (not being income chargeable under the head "Salaries") shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force*

*Provided that in the case of interest payable by the Government or a public sector bank within the meaning of clause (23D) of section 10 or a public financial institution within the meaning of that clause, deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode:*

*Explanation.1-For the purposes of this section, where any interest or other sum as aforesaid is credited to any account, whether called "Interest payable account" or "Suspense account" or by any other name, in the books of account of the person liable to*

*pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly.*

*Explanation 2.-For the removal of doubts, it is hereby clarified that the obligation to comply with sub-section (1) and to make deduction thereunder applies and shall be deemed to have always applied and extends and shall be deemed to have always extended to all persons, resident or non-resident, whether or not the non-resident person has-*

*(i) a residence or place of business or business connection in India; or*

*(ii) any other presence in any manner whatsoever in India.”*

**Section 40(a)(i) of the IT Act:**

*“40. Amounts not deductible*

*Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession",-*

*(a) in the case of any assessee-*

*(i) any interest (not being interest on a loan issued for public subscription before the 1st day of April, 1938), royalty, fees for technical services or other sum chargeable under this Act, which is payable,-*

*(A) outside India; or*

*(B) in India to a non-resident, not being a company or to a foreign company,*

*on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid [on or before the due date specified in sub-section (1) of section 139”*

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