IN THE INCOME TAX APPELLATE TRIBUNAL,
CUTTACK BENCH, CUTTACK

BEFORE S/SHRI N.S SAINI, ACCOUNTANT MEMBER
AND PAVAN KUMAR GADALE, JUDICIAL MEMBER

ITA No.289/CTK/2014
Assessment Year : 2010-2011

DCIT, Circle 1(1), Bhubaneswar.	Vs.	Paradeep Phosphates Limited, Bayan Bhawan, Pt. Jawaharlal Nehru Marg, Bhubaneswar.
PAN/GIR No. AABCP 327		
(Appellant)	..	(**Respondent**)

ITA No.264/CTK/2015
Assessment Year : 2010-2011

Paradeep Phosphates Limited, Bayan Bhawan, Pt. Jawaharlal Nehru Marg, Bhubaneswar	Vs.	DCIT, Circle 1(1), Bhubaneswar.
PAN/GIR No. AABCP 327		
(Appellant)	..	(**Respondent**)

Assessee by : Shri B.K.Mohapatra
Revenue by : Shri Kunal Singh, CIT DR

Date of Hearing : 31/07/ 2017
Date of Pronouncement : 04/08/ 2017

O R D E R

Per N.S.Saini, AM

These are cross appeals filed by the Revenue and the Assessee against the order of CIT(A)-1, Bhubaneswar, dated 22.4.2014 for the assessment year 2010-2011.

First, we take up the Revenue's appeal in ITA No.289/CTK/2014.

2. In Ground Nos.1, 2 & 3 of the appeal, the grievance of the revenue is that the CIT(A) was not justified in deleting the addition of Rs.21,80,04,41,000/- on account of non-deduction of tax u/s.40(a)(ia) of the Act.

3. The brief facts of the case are that the Assessing Officer observed that during the year, the assessee had made import purchases of Rs.21,80,04,41,000/-. The Assessing Officer analyzed the provisions of section 195(1), 195(2), 195(3) & 197 of the Act and their applicability in the case of the assessee. The Assessing Officer also referred to the CBDT's Circular No.759 dt.18.11.1997 read with RBI Circular No.767 dt.22.5.1998, No.48 dt.29.11.1997 and also the amended CBDT's Circular No.10/2002 dt.9.10.2002. The Assessing Officer further observed that the assessee did not apply to him to determine the appropriate portion of the sum chargeable u/s.195(2) and did not get a certificate u/s. 195(2) or u/s. 197. The Assessing Officer also observed that neither any undertaking nor CA's certificates as envisaged in the aforesaid CBDT's circulars were submitted before him. Therefore, he concluded that in absence of certificate u/s.195(2) or 197, the assessee was required to deduct tax u/s.195(1) in respect of remittances made for purchases from non-resident concerns. The Assessing Officer cited decisions in the case of CIT v. Barium Chemicals Ltd. (1988), 175 ITR 243 (AP), Agarwal Chambers of Commerce Ltd. v. Ganapati Rai Hiralal, (1958) 33 ITR 245

(SC), and decision in the case of Transmission Corpn. of A.P. Ltd. vs CIT, 239 ITR 587. Relying heavily on the decision in the case of AP State Electricity Board which was confirmed by the Supreme Court, the Assessing Officer stated that tax was deductible by the assessee u/s.195(1) on payment to non-resident in respect of import value of machinery & spares, raw materials etc., since no benefit of sections 95(2), 195(3), 197 was availed of. Accordingly, the Assessing Officer held that the assessee has failed to discharge its obligations to deduct tax at source u/s.195(1) for which the provisions of section 40(a)(i) is attracted. Since the assessee has not deducted tax u/s.195(1) of the Act from the said amounts, the Assessing Officer disallowed the same by invoking section 40(a)(ia) of the accordingly addition of Rs.2180,04,41,000/- was made by him.

4. On appeal before the CIT(A) the assessee submitted as under:

> "*(1) The Company is engaged in the business of manufacturing and sale of fertilizers.*
> *(2) For manufacture of fertilizers, the Company mostly imports raw materialsunder CFR (Cost + Freight) basis and makes the payment for such supply of materials.*
>
> *The Company's Transfer Pricing (TP) assessment for the AY 2010-11 has been* completed *on 30.01.2014 with "NIL Adjustment" after going through in detail, the transactions of imports from various parties being associated enterprises within the meaning of Section 92 (C) of the Income Tax Act, 1961. Copy of the aforesaid Order is enclosed and marked as Annexure-1 for your kind reference.*
>
> *The Statutory Audit and the Tax Audit of the Company have been carried out by M/s. S.P. Batliboi & Associates, Kolkata and the Tax Audit report by our auditors clearly specifies that there is no addition required u/s 40 (a) (i) of the Income Tax Act on any violation of TDS u/s 195, while making remittances to the non--resident parties against purchases.*
>
> *The Company has been consistently following such type of imports, manufacture*

and sale of fertilizers over the years with no such issue having been raised by the Income Tax Authorities up to the A.Y. 2005-06.

> *(5) Similar matter i.e. applicability of TDS u/s 195 on payments remitted against purchases was examined by the Ld. AO in response to the Order issued by Ld. CIT u/s 263 relating to the AY 2006-07.*
>
> *On examination the Ld AO, confirmed in his Order that Section 195 is not applicable while making remittances against the imported purchases and hence applicability of Sec 40 (a) (i) is not tenable. Copy of the De-novo assessment order u/s 143(3)/ 263 of I.T. Act for the AY 2006-07 is enclosed and marked as Annexure-2 for your kind reference.*

It may be mentioned here that the Ld. CIT set aside the assessment order for the AY 2007-08 by invoking Section 263 of the Act and directed the AO to do denovo assessment by adding/disallowing an amount of Rs 1344.63 Crore u/s 40 (a) (i) towards import purchases. Being aggrieved with the aforesaid Order, PPL filed an appeal before the Hon'ble ITAT and the Hon'bie ITAT vide Order dtd 13th June, 2013 quashed the direction of CIT for disallowing Rs 1344.63 Crore by referring the landmark decision rendered by the Hon'ble Supreme Court in the matter of GE India Technology Centre P. Ltd v CIT (327ITR 456). Copy of the Order passed by the Hon'ble ITAT is enclosed and marked as Annexure-3 for your kind reference.

On the same issue for AY 2009-10, the Ld. JCIT adjudicated that withholding tax should have been levied on such imports and has disallowed the entire import purchases. In this regard, it may be noted that the company filed an appeal before your Honour and your Honour vide Order dtd 28th October, 2013 quashed the Order of JCIT by mentioning that import purchases are outside the purview of withholding tax by relying upon the landmark decision rendered by the Hon'bie Supreme Court in the matter of GE India Technology Centre P. Ltd v CIT (327 ITR 456). Copy of the Order passed by the Hon'ble ITAT is enclosed and marked as Annexure-4 for your kind reference.

On the same issue for AY 2010-11, the AO has adjudicated that withholding tax should have been levied on such imports and has disallowed the same. In this regard, it may be noted that there has not been any change in the law other than number of judicial pronouncements holding that no tax is to be deducted at source where the amount payable is not chargeable to tax in India. The AO has not followed the well settled judicial principle of consistency which holds that unless there is a material change in facts and circumstances of the case, the revenue authority will not depart from its previous decisions at their own sweet will.

This principle was upheld by Gauhati High Court in case of Dhansiram Agarwalla v Commissioner of Income Tax (217 ITR 4), where it was held that:

" .. having upheld in identical circumstances and accepted the explanation furnished by the assessee, consistency demanded and dictated that the

Tribunal should not have rejected the explanation for the subsequent year which has been rejected simply because the second/alternative explanation regarding the mode of conveyance was not found to be acceptable..."

"..Although it is true that neither the principle of res judicata nor the rule of estoppel is applicable to assessment proceedings, yet the rule of consistency does apply to such proceedings as has been held in CIT v. Godavari Corporation Ltd...."

.... In view of the foregoing discussion and taking into consideration the facts that the Tribunal has omitted to bear in mind the rule of consistency and consider the second explanation from the angle of human probabilities in the totality of circumstances, and the assessment and the findings as recorded in and the assessment order, annexure "B", it cannot be said in the circumstances of the case that the Tribunal was justified in affirming the addition of Rs. 90,000/-.

In the result, our answer to the question referred to is in the negative, i.e., in favour of the assessee and against the Revenue".

Further, in case of Taraben Ramanbhai Patel v. ITO (215 ITR 323), the Hon'ble Gujrat High Court held that:

"It is no doubt true that the strict rule of the doctrine of res judicata does not apply to proceedings under the Income-tax Act. At the same time, it is equally true that unless there is a change of circumstances, the authorities will not depart from previous decisions at their sweet will in the absence of material circumstances or reasons for such departure."

Accordingly, the AO while doing the assessment for the AY 2010-11 should have been followed his earlier orders and not deviate from his previous decision since there has been no change in the facts of PPL's case (purchase of materials from overseas countries) which necessitated such departure.

It may be mentioned here that, CBDT issued instruction No. 2 u/s 119 of the IT Act on Section 195 on 25.02.2014. The Ld. DCIT passed the Order for the AY 2010-11 on 28.02.2014 ignoring the aforesaid instruction issued by CBDT. Had the instruction been followed by the AO, then the demand on account of Section 195 would not have been raised on PPL. It is worth mentioning here that CBDT has the power to issue instructions to subordinate

authorities' u/s 119 of the IT Act and all such authorities and ait other persons employed in the execution of the Act shall observe and follow such Orders/Instructions/Directions of the Board. Hence the disallowance of import purchases in the pretext of TDS has not been made is not tenable and justified. The copy of the instruction issued by CBDT is enclosed and marked as Annexure-5 for your kind reference.

For the current assessment in progress, the very same issue has been raised by the Ld. AO in the personal hearing held on 10th February' 2014. In this regard, it may be mentioned here that during the AY 2010-11, payment on account of import purchases was Rs. 218004.41 lac. In this regard, the copy of the Annual

Report is enclosed and marked as Annexure-6 for your kind reference. Details of purchases of raw materials, trading goods, capital goods and components and spares are shown hereunder for your kind reference:

The Ld. AO even disallowed the purchase of Capital Goods which is not routed through the Profit and Loss Account.

(8) In regards to the applicability of the section 195 relating to import purchases and disallowances of the same in the pretext of non deduction of tax at source from the remittances under Sec 40(a)(i), our submission is stated below alongwith relevant case laws of Hon'ble Supreme court and other judicial pronouncements:

(8.1) The aforesaid amount of Rs. 218004.41 lacs are in respect of purchase of materials from non-resident (foreign suppliers) for import of goods (Supply of Raw materials/trading goods/capital items/ components and spares). It may be noted that in respect of import of goods, on payments to Foreign non-resident suppliers, no income accrues arises/deemed to accrue or arises in India under the provisions of the IT Act. Further no money is received in India by the foreign parties and therefore no income is chargeable in India u/s 5 and 9 of the I.T. Act.

(8.2) <u>In this regard, the provisions of section 195 of the Act is as under:</u>

"Any person responsible for paying to a non resident, not being a company or to a foreign company, any interest or <u>any other sum chargeable under the provision of this Act</u> (not being the 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 there of in cash or by issue of cheque or draft or by any other mode, whichever is earlier, deduct the income tax there on at the rate in force.

• Since no income is chargeable in India under the provision of the IT Act in respect of the said imports, the question of TDS u/s. 195 of the I.T Act does not arise and therefore we have rightly not deducted any TDS u/s. 195 of the I. T Act on such foreign payments. Thus the aforesaid payments for supply of raw material remains outside the purview of Sec 195 of the Act and therefore there is no scope for any disallowance u/s 40(a)(i) of the Act. This is a well established principle. It is pertinent to mention that the Hon'ble Supreme Court in the case of <u>GE India Technology Cen.(P) Ltd. Vs CIT reported in (2010) 193 Taxman 234(SCT, (2010) 327 ITR 456 (SC)</u> has interpreted the provisions of sec 195 of the Act and has held that payment on supply of goods does not attract TDS u/s 195 of the IT Act and section 195 is applicable to the service components and not to the supply components. The brief facts and the decision is given hereunder:
GE India Technology Cen.(P) Ltd. Vs CIT (supra);

<u>Brief facts and background of the case:</u>

o *The assessee-company was a distributor of imported pre-packaged shrink*

wrapped standardized software from microsoft and other suppliers outside India. During the relevant assessment year, it made payments to the said software suppliers which according to the assessee represented the purchase price of the abovementioned software. The ITO(TDS) held that since the sale of software included a licence to use the same, payments made by the assessee to the foreign suppliers constituted royalty, which was to be deemed to have accrued or arisen in India and, therefore, tax at source was liable to be deducted under section 195. The said finding of the ITO(TDS) was upheld by the Commissioner (Appeals). In second appeal, the Tribunal, however, held that the amount paid by the assessee to the foreign software suppliers was not 'royalty' and the same did not give rise to any income taxable in India and, therefore, the assessee was not liable to Deduct Tax At Source (TAS).
On appeal to the High Court, the revenue for the first time, raised the contention that unless the payer made an application to the ITO(TDS) under section 195(2) and obtained a permission for non-deduction of the TAS, it was not permissible for the payer to contend that the payment made to the non-resident did not give rise to 'income' taxable in India and, therefore, there was no need to deduct any TAS. That argument of the department was accepted by the High Court vide the impugned judgment, by placing strong

reliance on the judgment of the Supreme Court in Transmission Corpn. of A. P. Ltd. v. CIT [1999] 239 ITR 587/105 Taxman 742.

On appeal to the Supreme Court held: o *Section 195 imposes a statutory obligation on any person responsible for paying to a non-resident any interest (not being interest on securities) or any other sum (not being dividend) chargeable under the provisions of the Act, to deduct income-tax at the rates in force unless he is liable to pay income-tax thereon as an agent. Payment to non-residents by way of royalty and payment for technical services rendered in India are common examples of sums chargeable under the provisions of the Income-tax Act to which the afore stated requirement of tax deduction at source applies. The tax so collected and deducted is required to be paid to the credit of the Central Government in terms of section 200, read with rule 30 of the Income-tax Rules, 1962. Failure to deduct tax or to pay tax would also render a person liable to penalty under section 201, read with section 221. In addition, he would also be liable under section 201(1 A) to pay simple interest at 12 per cent ~ per annum on the amount of such tax from the date on which such tax was deductible to the date on which such tax was actually paid. The most important expression in section 195(1) consists of the words 'chargeable under the provisions of the Act'. A person paying interest or any other sum to a non-resident is not liable to deduct tax if such sum is not chargeable to tax under the Act. For instance, where there is no obligation on the part of the payer and no right to receive the sum by the recipient and the payment does not arise out of any contract or obligation between the payer and the recipient but is made voluntarily, such payments cannot be regarded as income under the Act. Section 195 contemplates not merely amounts, the whole of which are pure income payments, it also covers composite payments which have an element of income embedded or incorporated in them. Thus, where an amount is payable to a non-resident, the payer is under an obligation to deduct TAS in respect of such*

Sl. No.	Name of Material	Value of import calculated on CIF basis (Amount	Applicability of TDS	Reason for non deduction of TDS
1	Catalyst	113.33	No	Supply Item
2	Components and	220.31	No	Supply Item
3.	Raw materials	173048.96	No	Supply items
4.	Capital goods	23.84	No	Supply items
5.	Trading goods	44597.97	No	Supply items
	Total	218004.41		

The Ld. AO even disallowed the purchase of Capital Goods which is not routed through the Profit and Loss Account.

(8) In regards to the applicability of the section 195 relating to import purchases and disallowances of the same in the pretext of non deduction of tax at source from, the remittances under Sec 40(a)(1), our submission is stated below alongwith relevant case laws of Hon'ble Supreme court and other judicial pronouncements;

(8.1) The aforesaid amount of Rs. 218004.41 lacs are in respect of purchase of materials from non-resident (foreign suppliers) for import of goods (Supply of Raw materials/trading goods/capital items/ components and spares). It may be noted that in respect of import of goods, on payments to Foreign non-resident suppliers, no income accrues arises/deemed to accrue or arises in India under the provisions of the IT Act. Further no money is received in India by the foreign parties and therefore no income is chargeable in India u/s 5 and 9 of the I. T. Act.

(8.2) In this regard, the provisions of section 195 of the Act is as under:

• "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 provision of this Act (not being the 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 there of in cash or by issue of cheque or draft or by any other mode, whichever is earlier, deduct the income tax there on at the rate in force.

• Since no income is chargeable In India under the provision of the IT Act in respect of the said imports, the question of TDS u/s. 195 of the I.T Act does not arise and therefore we have rightly not deducted any TDS u/s. 195 of the I.T Act on such foreign payments. Thus the aforesaid payments for supply of raw material remains outside the purview of Sec 195 of the Act and therefore there is no scope for any disallowance u/s 40(a)(1) of the Act. This is a well established principle. It is pertinent to mention that the Hon'ble Supreme Court in the case of GE India Technology Cen.(P) Ltd. Vs CIT reported in (2010) 193 Taxman 234fSC): (2010) 327 ITR 456 (SC) has interpreted the provisions of sec 195 of the Act and has held that payment on supply of goods does not attract TDS u/s 195 of the IT Act and section 195 is applicable to the service components and not to the supply components. The brief facts and the decision is given hereunder:

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o *The assessee-company was a distributor of imported pre-packaged shrink wrapped standardized software from Microsoft and other suppliers outside India. During the relevant assessment year, it made payments to the said software suppliers which according to the assessee represented the purchase price of the abovementioned software. The ITO(TDS) held that since the sale of software included a licence to use the same, payments made by the assessee to the foreign suppliers constituted royalty, which was to be deemed to have accrued or arisen in India and, therefore, tax at source was liable to be deducted under section 195. The said finding of the ITO(TDS) was upheld by the Commissioner (Appeals). In second appeal, the Tribunal, however, held that the amount paid by the assessee to the foreign software suppliers was not 'royalty' and the same did not give rise to any income taxable in India and, therefore, the assessee was not liable to Deduct Tax at Source (TA5).*

o *On appeal to the High Court, the revenue for the first time, raised the contention that unless the payer made an application to the ITO(TDS) under section 195(2) and obtained a permission for non-deduction of the TAS, it was not permissible for the payer to contend that the payment made to the non-resident did not give rise to 'income' taxable in India and, therefore, there was no need to deduct any TAS. That argument of the department was accepted by the High Court vide the impugned judgment, by placing strong reliance on the judgment of the Supreme Court in Transmission Corpn. of A. P. Ltd. v. CIT [1999] 239 ITR 587/105 Taxman 742.*

On appeal to the Supreme Court held:

Section 195 imposes a statutory obligation on any person responsible for paying to a non-resident any interest (not being interest on securities) or any other sum (not being dividend) chargeable under the provisions of the Act, to deduct income-tax at the rates in force unless he is liable to pay income-tax thereon as an agent. Payment to non-residents by way of royalty and payment for technical services rendered in India are common examples of sums chargeable under the provisions of the Income-tax Act to which the afore stated requirement of tax deduction at source applies. The tax so collected and deducted is required to be paid to the credit of the Central Government in terms of section 200, read with rule 30 of the Income-tax Rules, 1962. Failure to deduct tax or to pay tax would also render a person liable to penalty under section 201, read with section 221. In addition, he would also be liable^ under section 201(1 A) to pay simple interest at 12 per cent per annum on the amount of such tax from the date on which such tax was deductible to the date on which such tax was actually paid. The most important expression in section 195(1) consists of the words 'chargeable under the provisions of the Act'. A person paying interest or any other sum to a non-resident is not liable to deduct tax if such sum is not chargeable to tax under the Act. For instance, where there is no obligation on the part of the payer and no right to receive the sum by the recipient and the payment does not arise out of any contract or obligation between the payer and the recipient but is made voluntarily, such payments cannot be regarded as income under the Act. Section 195 contemplates not merely amounts, the whole of which are pure income payments, it also covers composite payments which have an element of income embedded or incorporated in them. Thus, where an amount is payable to a non-resident, the payer is under an obligation to deduct TAS in respect of composite payments. The obligation to deduct TAS is, however, limited to the appropriate proportion of income chargeable under the Act forming part of the gross

sum of money payable to the non-resident. This obligation being limited to the appropriate proportion of income flows from the words used in section 195(1), namely, 'chargeable under the provisions of the Act'. It is for this reason that vide Circular No. 728, dated 30-10- 1995, the CBDT has clarified that the tax deductor can take into consideration the effect of the DTAA in respect of payment of royalties and technical fees while deducting TAS. It may also be noted that section 195(1) is in identical terms with section 18(3B) of the 1922 Act. In CIT v. Cooper Engg. Ltd. [19681 68 ITR 457 (Bom.) it was pointed out that if the payment made by the resident to the non-resident is an amount which is not chargeable to tax in India, then no tax is deductible at source even though the assessee may not have made an application under section 18(3B) [now section 195(2)]. The application of section 195(2) pre-supposes that the person responsible for making the payment to the non-resident is in no doubt that tax is payable in respect of some part of the amount to be remitted to a non-resident but is not sure as to what should be the portion so taxable or is not sure as to. the amount of tax to be deducted. In such a situation, he is required to make an application to the ITO(TDS) for determining the amount. It is only when these conditions are satisfied and an application is made to the ITO(TDS), that the question of making an order under section 195(2) will arise.

> *While deciding the scope of section 195(2), it is important to note that the tax which is required to be deducted at source is deductible only out of the chargeable sum. This is the underlying principle of section 195. Hence, apart from section 9(1), sections 4, 5, 9, 90 and 91 as well as the provisions of the DTAA are also relevant, while applying tax deduction at source provisions. Reference to the ITO (TDS) under section 195(2) or 195(3) either by the non-resident or by the resident payer is to avoid any future hassles for both resident as well as non-resident. Section 195(2) and 195(3) are safeguards. The said provisions are of practical importance.*
>
> *From this, it follows that where a person responsible for deduction is fairly certain, then he can make his own determination as to whether the tax is deductible at source and, if so, what should be the amount thereof.*
>
> *If the contention of the department, that the moment there is remittance, the obligation to deduct TAS arises, is to be accepted, then the word's 'chargeable under the provisions of the Act' in section 195(1) will be obliterated. The said expression in section 195fl) shows that the remittance has got to be of a trading receipt, the whole or part of which is liable to tax in India, The payer is bound to deduct TAS only if the tax is assessable in India. If tax is not so assessable, there is no question of TAS being deducted.*

One more aspect needs to be highlighted. Section 195 falls in Chapter XVII which deals with collection and recovery. Chapter XVII-B deals with deduction at source by the payer. On analysis of various provisions of Chapter XVII one finds use of different expressions; however, the expression 'sum chargeable under the provisions of the Act' is used only in section 195. In none of the other provisions, expression 'sum chargeable under the provisions of the Act' is found. Therefore, the Court is required to give meaning and effect to the said expression. It follows, therefore, that the obligation to deduct TAS arises only when there is a sum chargeable under the Act. Section 195(2) is not merely a provision to provide information to the ITO(TDS); it is a provision requiring tax to be deducted at source to be paid to the revenue by the payer who makes payment to a non-resident. Therefore, section 195 has to be read in conformity with the charging provisions, i.e., sections 4, 5 and 9.

This reasoning flows from the words 'sum chargeable under the provisions of the Act' in section 195(1). The fact that the revenue has not obtained any information per se cannot be a ground to construe section 195 widely so as to require deduction of TAS even in a case where an amount paid is not chargeable to tax in India at all. One cannot read section 195, as suggested by the department, namely, that the moment there is remittance the obligation to deduct TAS arises. If such a contention is accepted, it would mean that on mere payment income would be said to arise or accrue in India, If the contention of the department is accepted, it would mean obliteration of the expression 'sum chargeable under the provisions of the Act' from section 195(1), While interpreting a section one has to give weightage to every word used in that section. While interpreting the provisions of the Act, one cannot read the charging sections of that Act de hors the machinery sections. The Act is to be read as an integrated Code. Section 195 appears in Chapter XVII which deals with collection and recovery. The provisions for deduction of TAS which are in Chapter XVII dealing with collection of taxes and the charging provisions of the Act, form one single integral, inseparable Code and, therefore, the provisions relating to TPS apply only to those sums which are 'chargeable to tax' under the Act. Hence, the provisions relating to TPS apply only to those sums which are chargeable to tax under the Act, If the contention of the department is accepted that any person making payment to a non-resident is necessarily required to deduct TAS, then the consequences would be that the department would be entitled to appropriate the moneys deposited by the payer even if the sum paid is not chargeable to tax because there is no provision in the Act by which a payer can obtain refund. Section 237, read with section 199, implies that only the recipient of the sum, i.e., the payee can seek a refund. It must, therefore, follow, if the department is right, that the law requires tax to be deducted on all the payments, the payer, therefore, has to deduct and pay tax, even if the so-called deduction comes out of his own pocket and he has no remedy whatsoever, even where the sum paid by him is not a sum chargeable under the Act. The interpretation of the department, therefore, not only requires the words "chargeable under the provisions of the Act" to be omitted, it also leads to an absurd consequence. The interpretation placed by the department would result in a situation where even when the income has no territorial nexus with India or is not chargeable to tax in India, the Government would nonetheless collect tax. Section 195(2) provides a remedy by which a person may seek a determination of the 'appropriate proportion of such sum so chargeable' where a proportion of the sum so chargeable is liable to tax. The entire basis of the department's contention was based on administrative convenience in support of its interpretation. According to the department, huge seepage of revenue can take place if persons making payments to non-residents are free to deduct TAS or not to deduct TAS. It was the case of the department that section 195(2), as interpreted by the High Court, would plug the loophole as the said interpretation requires the payer to make a declaration before the ITO(TDS) of payments made to non- residents. In other words, according to the department section 195(2) is a provision by which paver is required to inform the department of the remittances he makes to the non-resident by which the department is able to keep track of the remittances being made to non-residents outside India. There was no merit in those contentions. Section 195(1) uses the expression sum chargeable under the provisions of the Act. One needs to give weightage to those words.

In Transmission Corpn. of A.P. Ltd.'s case (supra), it was held ,that TAS was liable to be deducted by the payer on the gross amount if such payment included in it an amount which was exigible to tax in India. It was held that if the payer wanted to deduct TAS not on the gross amount but on the lesser amount on the footing that

only a portion of the payment made represented "income chargeable to tax in India", then it was necessary for him to make an application under section 195(2) to the ITO(TDS) and to obtain his permission for deducting TAS at lesser amount. Thus, it was held bv the Court that if the paver had a doubt as to the amount to be deducted as TAS, he could approach the ITO(TDS) to compute the amount which was liable to be deducted at source. Section 195(2) is based on the 'principle of proportionality'. The said sub-section gets attracted only in cases where the payment made is a composite payment in which certain proportion of payment has an element of 'income' chargeable to tax in India, It is in this context that the Supreme Court stated, 'If no such application is filed, income-tax on such sum is to be deducted and it is the statutory obligation of the person responsible for paying such sum to deduct tax thereon before making payment. He has to discharge the obligation to TDS'. If one reads the observation of the Supreme Court, the words 'such sum' clearly indicate that the observation refers to a case of composite payment where the payer has a doubt regarding the inclusion of an amount in such payment which is exigible to tax in India, The above observations of the Supreme Court in Transmission Corpn, of A.P, Ltd.'s case (supra) have been completely misunderstood by the Karnataka High Court to mean that it is not open for the paver to contend that if the amount paid by him to the non-resident is not at all 'chargeable to tax in India' ,then no TAS is required to be deducted from such payment. This interpretation of the High Court completely loses sight of the plain words of section 195(1) which in clear terms lay down that tax at source is deductible only from "sums chargeable" under the provisions of the Income-tax, i.e. chargeable under sections 4, 5 and 9.

o *In the instant case, on facts, the ITO (TDS) had taken the view that since the sale of the concerned software included a licence to use the same, the payment made by the assessee to foreign suppliers constituted 'royalty' which was deemed to accrue or arise in India and, therefore, TAS was liable to be deducted under section 195(1). The said finding of the ITO(TDS) was upheld by the Commissioner (Appeals). However, in the second appeal, the Tribunal held that such sum paid by the assessee to the foreign software supplier was not a 'royalty', and that the same did not give rise to any 'income' taxable in India and, therefore, the assessee was not liable to deduct TAS. However, the High Court did not go into the merits of the case and it went straight to conclude that the moment there is remittance, an obligation to deduct TAS arises, which view stood overruled,*

o *Since the High Court did not go into the merits of the case on the question of payment of royalty, the impugned judgment of the High Court was to be set aside and cases were to be remitted back to the High Court for de novo consideration of the cases on merits. A copy of the aforesaid Judgment in the said case of GE India Technology Cen.(P) Ltd. Vs CIT is enclosed and marked as Annexure-7 for your kind reference.*

It is pertinent to mention that as per Article 141 of the Constitution of India the law declared by the Supreme Court shall be binding on all courts within the territory of India. Therefore, the law pronounced by the Hon'ble Supreme Court in the aforesaid case of GE India Technology is squarely applicable to PPL's aforesaid payments to foreign suppliers for import of materials / goods.

o *Further, a law which is settled in the country through the highest Court ought not to be interfered with to unsettle the same through improper interpretation of*

the Law. Hence, our prayer before your Honour to allow the entire imported purchase by deleting the addition made u/s 40 (a) (i) of the IT Act by applying Section 195 to the imported purchases of raw materials and remittances thereof to the foreign suppliers.

(8.3) It may kindly tie noted that majority of the purchases of imported raw materials, trading goods and components and spares are from countries covered under Double Taxation Avoidance Agreement (DTAA) with India wherein it is dearly specified that any "Business Profits" are liable to taxation in the country from where the purchases have been made during the course of business. Purchase being the business transactions are concluded when the goods along with the Bill of lading are handed over to the shipper in the country of origin.

(9)The provisions of Section 40(a)(i) of the IT Act is as under:

"Amounts not deductible.

40. 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 during the previous year, or in the subsequent year before the expiry of the time prescribed under sub- section (1) of section 200 :

Provided that where in respect of any such sum, tax has been deducted in any subsequent year or, has been deducted in the previous year but paid in any subsequent year after the expiry of the time prescribed under sub-section (1) of section 200, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Explanation.—For the purposes of this sub-clause,—

(A) "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9;
(B) "fees for technical services" shall have the same meaning as in Explanation 2 to clause (vii) of sub-

section (1) of section 9"

(10)Contentions of the Ld. AO while disallowing payments on account of imports for non deduction of taxes and it's non applicability in the present case

The AO has held that the provisions of section 195(1) of the Act were applicable to the Assessee and in the event that certificates under section 195(2) or 195(3) or section 197 of the Act were applied for by neither parties, the Company has failed to discharge its obligations for tax deduction.

It has already been decided in the matter of GE Technology that the provisions of section 195 are applicable to any payments to non residents only when they are chargeable to tax in India. The Supreme Court in case of GE Technology (supra) has already settled the matter wherein, it was held that any sum remitted to the non resident which is not taxable under the provisions of the Act does not require the payer to withhold tax at source. The said case was also relied on by us in our submissions before the AO, however, the AO has completely disregarded the submissions and has plainly resorted to disallowing the import payments on the premise that PPL should have applied for a withholding tax order for determining the tax rate of such withholding before making payment. In doing so, he has completely disregarded the fact that these payments are not chargeable to tax in India and there was no obligation on PPL to withhold any taxes or apply for a lower or NIL withholding tax order on such payments.
There has been no attempt from the AO to substantiate that the import transactions are chargeable under the Act or distinguish the contentions of PPL.
The order is thus not a speaking order and is bad in law.

The AO has observed that undertakings or certificates (i.e.,Form 15CA / 15CB) were not furnished by the Company to the Authorized Dealers / Bankers before making import payments.

In this regard, the PBI had issued A.P. (DIR Series) Circular No. 03 dated 19 July 2007 which clarified that the Chartered Accountant's certificate needs to be obtained for import transactions also. However, RBI has issued a notification no.E.CO.FID.5759/22.20.001/2007-08 dated 11 September 2007 whereby RBI has highlighted the difficulties faced by the remitter at the time of making remittance outside India and accordingly, clarified that the procedure laid down in A.P. (DIR Series) Circular No. 56 dated 26 November 2002 may be continued to be followed till further clarification from CBDT.

It can thus be seen from the above that the intention of introducing such compliances was never to bring all remittances under the purview of the above compliances, such compliance was introduced to avoid any payments which are taxable under the Act to escape being taxed in India. Subsequently, taxpayers were facing difficulties while undertaking compliances with respect to the foreign remittances and certain relaxation were provided by the RBI in complying with

these provisions.

Even if the provisions apply to import transactions, non compliance could not be treated as a ground for disallowing the import transactions under section 40 (a) (i) of the Act.

Separately, section 195(6) of the Act requires a person referred to in section 195 (1) of the Act to furnish the required information. Accordingly, if the amount remitted is, not chargeable to tax, the remitter is no a person referred to in section 195(1) of the Act and is not therefore required to comply with section 195(6) of the Act.

- *The case decisions relied upon by the AO on the basis of which he had contended that the provisions of section 195 are applicable to import transactions as well are not applicable to the facts of PPL.*

CIT vs Barium Chemicals Ltd. (175 ITR 243)

In the facts of this case, the assessee-company, Barium Chemicals Limited, Ramavaram, entered into an agreement with a foreign company, viz. Chemicals and Technical Service limited, on July 9, 1967, where under, the assessee-company undertook to > remit certain amount to the foreign company. No tax was deducted at source by the assessee-company as required under section 195 of the Act. For that reason, the Income Tax officer added the tax component and worked out the total taxable income at a particular figure.

On appeal, the Appellate Assistant Commissioner determined the income accruing to the non-resident company at £ 2,000 and held and directed the Income Tax Officer to value the perquisite on this basis (taking it as tax on tax and including this amount) and computing the business income and allow relief accordingly.)

In the above facts, a portion of income taxable in India had been determined and there was no dispute, as whether such income needed to be grossed up for the purpose of withholding taxes. Whereas in PPL's case, the basic issue, in dispute is whether the payments for imports are taxable in India or not. It is also relevant to note that the High Court relied on the case decision of the AP High Court in Commissioner of Income-tax vs Superintending Engineer (1985) 152 ITR 753 while pronouncing its decision on grossing up.

- Agarwal Chamber of Commerce Ltd. vs Ganpati Rai Hiralal (33 ITR 245)

In the facts of this case, the appellant carried on the business of commission agency for dealing in forward transactions in various kinds or grain other commodities. The respondent-firm Ganpat Rai Hira Lal of Narnaul-besides being a shareholder of the appellant company had dealings with it and entered into several forward transactions of sale and purchase of grain and other commodities. The appellant, acting as a commission agent of the respondent and its other constituents entered into several transactions of forward delivery at Hapur with Firm Parallel Musaddi Lal, who were carrying on commission agency business at Hapur (and will hereinafter be termed the Hapur firm). The total profits

of the transactions entered into by the appellant with the Hapur firm was Ps.48,250 on which the Hapur firm paid Rs.14,730-8-0 as income-tax. The profits accruing on the transaction entered into on behalf of the respondent amounted to Rs.29,275-2-6 on which the proportionate income-tax claimed to have been paid was Rs.9,314-13-4.

On 20 May 1943, the appellant was ordered to be wound up and Udmi Ram Aggarwal, a pleader of the old Patiala High Court, was appointed its liquidator. The official liquidator applied under section 186 of the Patiala Companies Act, for a payment order for Rs.12,204-12-3 against the respondent and in support of his claim be filed, with this application, copies of the respondent's account I the books of the appellant showing how the amount claimed was due from the respondent. This amount included the sum of Rs.9,476-13-0, on account of income-tax paid b the Hapur firm for and on behalf of the respondent on the profits of the forward transactions at Hapur and the commission of the Hapur firm.

The sole point for decision before the HC was whether the respondent is liable for income-tax, which has been paid by the Hapur firm on the transactions, which were entered into by the appellant with the Hapur firm for and on behalf of the respondent.

It could be seen from the above facts that they are entirely different from the facts of PPL and reliance on such decision is totally misplaced. The issue before the Court was to decide whether TDS provisions were applicable on payments made to the non resident Appellant whose global income was a loss. There was no dispute on the fact that tax was deductible on such commission income. However, in PPL's case, the basic issue to decided is whether tax is deductible on import payments, i.e., whether payments made by PPL to the non resident suppliers are chargeable to tax in India or not.

CIT Andhra Pradesh - III vs Superintending Engineer Uper Sileru (SC)

The Andhra Pradesh State Electricity Board (for short 'the Electricity Board'), the respondent in these references, made certain payments to non-residents against the purchase of machinery and equipment and also against the work executed by the non-residents in India if erecting .and commissioning the machinery and equipment. The question arose whether the Electricity Board was under an obligation to deduct tax at Source from these payments under section 195 of the Act.

The payments were made by the Electricity Board without deduction of tax at source. The Income Tax Officer held that the Electricity Board was under an obligation to deduct tax at source under s.195. Owing to the failure of the Electricity Board to deduct such tax, the Electricity Board was deemed to be an assessee in default in respect of the tax deductible at source under section 195. Consequently, the Income Tax Officer passed orders determining the tax, which, according to him, was deductible at source under section 195 and required the Electricity Board to pay such amounts.

The SC in the present case has upheld the order of the Joint

Commissioner which held that the taxpayer was under an obligation to deduct taxes at source under section 195 of the Act and the obligation is limited only to the portion chargeable under the Act.

The above case is distinguishable on the following points:

In the judicial pronouncement relied upon by the learned AO, the payments were made by the assessee in respect of purchase of machinery and equipment and also against the work executed by the non-residents in India for erecting and commissioning such machinery and equipment. Since some part of the composite contract(s) had accrued in India, the Hon'ble Supreme Court has held that the assessee should have obtained certificate under section 195(2) of the Act. However, in PPLs case, there is no uncertainly in respect of withholding tax under the provisions of the Act since the payments are not chargeable to tax in India.

The above judicial pronouncement has been relied on by the SC in the case of Transmission Corporation of A.P. Ltd. & Anr vs. CIT [(1999) 239 ITR 587 (SC)] which has ultimately been settled by the SC in GE India Technology's case (supra). It thus follows that the principles laid down by this judgement are no longer relevant to determine the obligations of a payer while making payments to non residents that are no chargeable under the Act as in the present case.

(11) In view of the above, the aforesaid amount of Rs. 218004.41 lacs is fully allowable and the claim of PPL is legally correct and nothing is disallowable under Section 40(a)(i) of the I.T. Act in respect of the aforesaid remittances to foreign suppliers for import of materials / goods since the same is outside the purview of Sec 195 of the IT Act."

5. The CIT(A) after considering the submissions of the assessee held as under:

"I have carefully gone through the observations of the AO for concluding that the appellant was liable to deduct tax at source u/s.195(1), detailed submissions of the appellant, relevant decisions and various facts on record. The dispute has arisen when the appellant purchased machinery, raw materials, components & spares, capital goods and traded goods from non-resident concerns for a total cost of Rs.2180,04,41,000/- (including all other expenses, duty and taxes)' out of which the total cost of raw materials is Rs. 1730,48,96,000/-. The issue was decided by me in the appellant's own case under similar facts and circumstances for earlier assessment year 2009-2010 as under:

"3.2 ... As per provisions of sec.195(1) of the Act, any person responsible for paying (Payer) to a Non- Resident or Foreign Company (Payee) any interest or 'any other sum chargeable under the provision of the Act', is required to deduct tax at source. The provision applies to all the Payers, including individual and

HUF. The only specific exclusion provided is in respect of payment of dividend which is exempt by virtue of payment of Dividend Distribution Tax. The scope of the provision is wide and therefore, the implications thereof have far-reaching effect in Large numbers of cases as the number of such payments has increased manifold with the development of the economy and growth of cross border transactions in the last decade.

As per provisions of sec.195(2) of the Act, if the Payer considers that the whole of such a sum would not be chargeable to tax in the hands of the Payee, he may make an application to the Assessing Officer (AO) to determine the appropriate portion of such taxable income by passing a general or special order and upon such determination, the Payer is obliged to deduct tax only on the portion so determined.

As per provisions of sec.l95(3)/(5) read with Rule 29B of the Act the specified recipient of such a sum can also make an application to the AO in the prescribed form for grant of a certificate authorising him to receive such sum, without TDS and upon grant of such a certificate, the Payer is required to make payment without TDS. These provisions are largely used by foreign banks operating in India for receiving payments from their customers without TDS.

Section 195(6) was introduced by the Finance Act, 2008 (with effect from 1.-4-2008) providing that the Payer shall furnish the information relating to payments of such sums in the prescribed form and manner. For this Rule 37BB was introduced and the procedure for making remittances is provided for which the certificate of Chartered Accountant in the prescribed Form 15CB is required to be obtained by the Payer before making remittance to the Payee (New Procedure for Remittance). Earlier, there was a requirement for obtaining certificate of Chartered Accountant for making remittance to the Non-Resident, but the same was operating under
the Circulars issued by CBDT.

The Apex Court in the case of Transmission Corporation of A.P. Ltd. (239 ITR 597) has held that the expression 'taxable income' used in S. 195(1) applies^ to any sum payable to the Non-Resident even if such a sum is a trading receipt in the hands of the payee, if, the whole or part thereof is chargeable to tax under the Act. These provisions are only limited to the sums which are of 'Pure Income' nature. Based on this judgment, it was felt by the Payers of such income that the TDS is required to be made u/s. 195(1) only if, the income is chargeable to tax (partly or wholly) under the Act and in cases where, the income itself is not chargeable to tax (Non- taxable income) question of making any TDS should not arise. However, because of the interpretation that it is not for the assesses to decide whether the income is chargeable in the hands of the Payee or not, the litigation on the obligation to make TDS continues, even after the decision of the Apex Court in Transmission Corporation of A.P. Ltd and particularly in view of interpretation of this judgement by the Hon'ble Karnataka High Court in the case of CIT (International Taxation) v. Samsung Electronics Co. Ltd, [2009] 185 Taxman 313 (Kar.)/ [2010] 320 ITR 209 in the case of M/s. Samsung Electronics Co. Ltd. and other cases in the context of obligation to make TDS in respect of payments made to Non-Resident Payees for supply of shrink wrapped standardised software. The Hon'ble Karnataka High Court held as under:

66. If one is allowed the liberty of giving a rough and crude comparison to the manner in which the provisions of section 195 of the Act operates on a resident payer who makes payment to a non-resident recipient and if the payment bears the character of a semblance of an income receipt in the hands of the non-resident recipient, then the obligation on the part of the resident payer who makes such a payment to the non-resident recipient is like a guided missile which gets itself attached to the target, the moment the resident assessee makes payment to the non-resident recipient and there is no way of the resident payer avoiding the guided missile zeroing on the resident payer whether by way of contending that the amount does not necessarily result in the receipt of an amount taxable as income in the hands of the non-resident recipient under the Act or even by contending that the non-resident recipient could have possibly avoided any liability for payment of tax under the Act by the overall operation of different provisions of the Act or even by the combined operation of the provisions of a double taxation avoidance agreement and the Act as is sought to be contended by the respondents in the present appeals.

67. The only limited way of either avoiding or warding off the guided missile is by the resident payer invoking the provisions of section 195(2) of the Act and even here to the very limited extent of correcting an incorrect identification, an incorrect, computation or to call in aid the actual determination of the tax liability of the non-resident which in fact had been determined as part of the process of assessing the income of the non-resident and by using that as the basis for claiming a proportionate reduction in the rate at which the deduction is required to be made on the payment to the non-resident. Except for this method, there is no other way of the resident payer avoiding the obligations cast on it by the provisions of section 195(1) of the Act and as a consequence of such default when is served with a demand notice in terms of section 201 of the Act."

3.2.1 The AO is of the opinion that the decision of the AP High Court in the case of Transmission Corporation of AP Ltd. v. CIT, which was approved by the Supreme Court in 239 ITR 587 (SC) is applicable and accordingly the assessee was liable to deduct tax u/s. 195(1). In this case the AO considered that the person making payments to a non-resident cannot take a unilateral decision that the payments made by him are not sums chargeable to income tax, and therefore he cannot make such payments without deducting tax at source unless he gets the concurrence of the Assessing Officer as provided in section 195(2) or an exemption certificate under section 195(3). However, as per the High Court's decision the obligation of the assessee is limited to deduct tax u/s.195 on the appropriate portion of the income chargeable under the Act in respect of sums paid under the contract. Accordingly, tax was deductible in respect of income imbedded in the contract amount. In the Instant case, the appellant has purchased raw materials from non-resident business entities and no income can be said to have accrued in India in respect of cost of raw materials. The income, if any, earned by the non-resident seller of the raw materials is earned in foreign soil and not taxable under the Indian Income Tax Law. Further, application u/s.195(2) was required to be made in case the appellant was having any doubt about the proportion of income embedded in the remittance and in case the income itself was not assessable in India, there was no requirement to make any

application u/s.195(2). In any case, not making an application u/s.195(2) before remittance could at best be considered as a violation and would not attract the provisions of section 40(a)(i).

It was held by the Hon'ble ITAT, Hyderabad, in the case of SOL Pharmaceuticals Ltd. v. ITO [2002] 83 ITD 72 (Hyd.) that Section 195(2) is attracted only in a case where at least a portion of the payment to non resident is chargeable as income. If no portion is chargeable, then section 195(2) is not attracted.

It was held by the Hon'ble ITAT, Madras, in the case of Indopel Garments (P.) Ltd. v. DOIT, 86 ITD 102 (Mad), that no tax was deductible from the commission paid to the non-residents. Where there is no chargeable income, it is not necessary for assessee to get concurrence of AO u/s. 195(2).

In the case of Graphite Vicarb Ind. Ltd. v. ITO [1986] 18 ITD 58 l(Cal.), it was held that section 195(2) envisages application for determining appropriate proportion of the sum which would be chargeable to tax; but does not envisage a case where the assessee claims that no profits of the sum to be remitted is liable to tax at all.

3.2.2 Under similar circumstances for the AY 2006-07, the AO has given a finding that no tax is deductible u/s. 195(1) in respect of payment made by the assessee for import of goods. The AO's observations and conclusions in the assessment order u/s,143(3)/263 dt.28.12.2011 is as under:

" <u>Non deduction of TPS:</u>

Assessee PPL has made payment of Rs.14,479.93 lakhs to non-resident for import of goods. Asesesee was asked whether TDS provision is applicable to them or not. A. R. of the assessee stated stat:

Since no income is chargeable in India under the provision of the IT Act in respect of the said imports, the question of TDS u/s.195 of the I.T.Act does not arise and therefore the assessee has rightly not deducted any TDS u/s.195 of the I.T.Act on such foreign payments. Thus the aforesaid payments for Supply of raw material remain outside the purview of of the Act and therefore there is no scope for any disallowance u/s.40(a)(i) of the Act. This is a well established principle. It is pertinent to mention that the Hon'ble Supreme Court in the case of GE India Technology Cen. (P) Ltd. Vs CIT reported in (2010) 193 Taxman 234(SC); (2010) 327 ITR 456 (SC) has interpreted the provisions of Section 195 of the Act and has held that payment on supply of goods does not attract TDS u/s.195 of the IT Act and section 195 is applicable to the service components and not to the supply components."

Argument of the assessee is accepted because of the following reason.

1. *According to the provisions of Sec. 195(1) and 195(2), the TDS is required to be made on "any other sum chargeable under the provisions this Act". Changeability is relevant in this case. As per decision of Hon'ble Supreme*

Court in the case of CWT Vellis Bridge Gymkhan (1998) 229 ITR 1 (SC), if a person has not been brought in the ambit of Section by clear words, he cannot taxed at all.

2. *In this case, the above payments are made towards purchase of goods on principal to principal basis. Assessee has not entered into any contract with foreign parties rather assessee has procured the goods at its own cost like payment of customs duty, freight, handling charges etc. i.e. on CIF basis.*

3. *In case of CIT vs. R.D. Agrawal & Co. (1965) 56 ITR 20(SC), Hon'ble Apex Court has stated that 'In the case of assessee company the purchases are made by placing the purchase order and delivery are made on CIF basis, payment is remitted to foreign sellers in advance, hence, question the taxing the foreign exporters do not arise in India'. Thus, in the case of the assessee, when the sum paid to foreign companies are not chargeable to tax in India, applicability of section 195(1) & 195(2) is not sustainable.*

4. *Trading activities are duly covered under Article 7 of DTAAs of which all related provisions are also in operation and according to DTAAs, the payment made by assessee are not taxable in India. Being specific provisions, DTAAs will prevail other sections of the Act.*

5. *In Circular No. 17 (XXXVII-1) of 1953, No.26 (26)-IT/53 dated 17.07.1953, CBDT has clarified that if transaction is on principal to principal basis no tax liability will be arise in the foreign companies.*

6. *In case of Vijay Ship Breaking Co. Vs. CIT (Ahmedabad) 314 ITR 309 (SC), Hon'ble Apex Court has stated that provision of Sec. 195 is not applicable in case where income is not chargeable to tax in India (Also see Veneburg Group B. V. 289 ITR 466 AAR New Delhi).*

7. *In a recent judgment, in case of Van Oord ACZ (India) Vs. CIT (Delhi) dtd.24.03.2010, Hon'ble High Court has stated that the obligation to deduct tax at source u/s. 195(1) arises only when the payment to chargeable to tax in India.*

8. *In case of Transmission Corporation of AP Ltd. Vs. CTT (1999) 239 ITR 587 (SC) (cited by RAP), Hon'ble Supreme Court has given its findings as below:-*

"in this view of the matter, the answer given by the High Court that (i) the assessee who made payments to the three non-residents was under obligation to deduct tax at source u/s.195 of the I.T.Act in respect of the sums paid to them under the contracts entered into and (ii) the obligation" of the respondent assessee to deduct tax u/s.195 is limited only to the appropriate proportion of income chargeable under the Act, are correct".

By the above findings of Hon'ble Supreme Court, it is clear that provisions of section Sec. 195 are applicable where assessee enters into a contract with non-resident. In this very case, no contract was made by the assessee. Trading transaction was covered under the Sale of Goods Act not under Contract Act."

3.2.3 Under similar circumstances, the Hon'ble IT AT, Cuttack Bench in case of the appellant for AY 2007-08 has quashed the order of CTT, Bhubaneswar u/s. 263 on the ground that the CTT did not consider the direction of Hon'ble Apex Court in GE India Technology case which has been reproduced earlier in the submission of the appellant. Accordingly, in view of the detailed submission of the appellant, the decision of the Hon'ble Supreme Court in the case of GE India Technology which have been referred by the TTAT in appellant's own case for the AY 2007-08 and by the AO for AY 2006-07, it is clear that no tax is deductible u/s,195(l) in respect of remittance made by the appellant for purchase of raw materials amounting to Rs.4491,86,39,189/-

3.2.4 The case of the appellant is squarely covered by the judgment of e Hon'ble Supreme Court in the case of GE India Technology Cen. (P) |&/. v. CIT (2010) 327 ITR 456 (SC) which has been quoted by the appellant in its submissions. The Hon'ble Supreme Court in GE India technology Cen. (P) Ltd. has also considered the judgment in the case of Transmission Corporation of AP Ltd. (supra), support of which was taken 'by the AO in holding that assessee was required to deduct tax u/s. 195(1). The Hon'ble Supreme Court has observed that every remittance would not result in deduction of tax but only in respect of the amount taxable under the provisions of the Income Tax Act. The application u/s. 195(2) is required only when the remitter has no doubt that tax is deductible but not sure of the amount of tax to be deducted. In case no tax is deductible on the remittance, no application u/s. 195(2) or no certificate u/s. 197 is necessary. The Hon'ble Supreme Court In GE India Technology Cen. (P) Ltd. v. CTT (supra), observed as under:

"10. ... In Transmission Corpn. of A.P. Ltd.'s case (supra) it was held that TAS was liable to be deducted by the payer on the gross amount if such payment included in it an amount which was exigible to tax in India. It was held that if the payer wanted to deduct TAS not on the gross amount but on the lesser amount, on the footing that only a portion of the payment made represented "income chargeable to tax in India", then it was necessary for him to make an application under section 195(2) of the Act to the ITO(TDS) and obtain his permission for deducting TAS at lesser amount. Thus, it was held by this Court that if the payer had a doubt as to the amount to be deducted as TAS he could approach the ITO(TDS) to' compute the amount which was liable to be deducted at source. In our view, section 195(2) is based on the "principle of proportionality". The said sub-section gets attracted only in cases where the payment made is a composite payment in which a certain proportion of payment has an element of "income" chargeable to tax in India. It is in this context that the Supreme Court stated, "If no such application is filed, income-tax on such sum is to be deducted and it is the statutory obligation of the person responsible for paying such "sum' to deduct tax thereon before making payment. He has to discharge the obligation to TDS". If one reads the observation of the Supreme Court, the words "such sum" clearly indicate that the observation refers to a case of composite payment where the payer has a doubt regarding the inclusion of an amount in such payment which is exigible to tax in India. In our view, the above observations of this Court in Transmission Corpn. of A.P. Ltd.'s case (supra) which i$ put in italics has been completely, with respect, misunderstood by the Karnataka High Court to mean that it is not open for the payer to contend that if the amount paid by him to the non-resident is not at all "chargeable tp *tax in India", then no TAS is required to be deducted from such payment. This Interpretation of the High Court completely*

loses sight of the plain words of section 195(1) which in clear terms lays down that tax at source is deductible only from "sums chargeable" under the provisions] of the Income-tax Act, i.e., chargeable under sections 4, 5 and 9 of the Income-tax Act."

In the instant case, the amounts have been paid towards purchase of raw material on principal to *principal basis and the appellant has procured the goods from the non-resident seller at its own cost after making payments of custom duty, freight, handling charges etc. on CIF basis. The raw material is sold by the non-resident seller in foreign soil, hence, no income accrues to the non-resident seller in the Indian territory. The AO has not brought any facts on record nor it is apparent that income in respect of transactions arises in favour of the nonresident sellers in the Indian territory or that the income of such nonresidents in respect of transactions is assessable under Indian Income tax Law.*

3.2.5 In view of the judgment of the Apex Court in the case of GE India Technology Cen. (P) Ltd. v. CIT (supra), it is the clear that if the payment is made to a non-resident, which is not a taxable income in India, then no tax is required to be deducted u/s.195. Accordingly, the addition u/s.40(a)(i) made by the AO is hereby deleted, Ground No.2 is thus allowed."

Since the addition made u/s.40(a)(i) for the AY 2009-10 was deleted and the facts and circumstances of the case remain similar in the impugned AY 2010-11, the addition made by the AO for Rs.2180,04,41,000/- u/s.40(a)(i) is hereby, deleted."

6. Ld D.R. relied on the order of the Assessing Officer whereas ld A.R. supported the order of the CIT(A).

7. After considering the rival submissions and perusing the materials available on record, we find that in the instant case, the assesse has made import of materials amounting to Rs.2180,04,41,000/-. The Assessing Officer disallowed the deduction for the same on the ground that the assessee has not deducted TDS u/s.195(1) of the Act by invoking the provisions of section 40(a)(ia) of the Act.

8. On appeal, the CIT(A) allowed the deduction by following his order for the assessment year 2009-2010.

9. Before us no specific error in the order of the CIT(A) could be pointed out by ld D.R. Further, ld D.R. could not point out whether the order of the CIT(A) passed in assessment year 2009-2010 was varied in appeal by any higher forum. The Hon'ble Supreme Court in the case of CIT vs. Excel Industries Ltd, 358 ITR 295(SC) has held that where a consistent view had been taken in favour of the assessee on the question raised, there was no reason for the court to take a different view unless there were very convincing reasons, which there were not.

10. Therefore, respectfully following the above decision of Hon'ble Supreme Court and keeping in view the fact no change in facts has been brought on record by the revenue during the year under appeal, we confirm the order of the CIT(A) and dismiss the ground of appeal of the revenue.

11. In Ground Nos.4 & 5, the grievance of the revenue is that the CIT(A) is not justified in deleting the addition of Rs.26,55,760/- made by the Assessing Officer on account of prior period expenses.

12. The brief facts of the case are that the Assessing Officer made addition of Rs.26,55,760/- under the head "prior period expenses" in respect of price difference on account of IOCL (Rs.26,54,640/-) and other (Rs.1,120/-). According to the Assessing Officer, the assessee was following hybrid system of accounting, which was not permissible and

relying on the decision of Hon'ble Kerala High Court in the case of CIT vs. Travancore Titanium Products Ltd., 183 ITR 73(Ker) disallowed the claim of prior period expenses as the assessee was not maintaining its account on mercantile basis.

13. Before the CIT(A), the assessee has submitted as under:

"The learned AO has disallowed an amount of Rs.26,55,760/- under the nomenclature "Prior period adjustments" solely on the ground of assessee is maintaining books of accounts on mercantile basis.

In every mercantile system of accounting, the Prior. Period Expenses are bound to be there as because every expenses can not be accurately measured and provided in the accounts. The term PPE is only applicable in a mercantile system of accounting as because the difference in provision at one stage and finalization of the actual expenditure at a later stage. The term PPE is not applicable in cash system of accounting, where expenses as and when incurred are debited in the accounts irrespective of the year to which it relates.

Even if the accounts are maintained on mercantile system, certain expenses are bound to be incurred in subsequent years, which can not be anticipated in which it relates due to various reasons like estimated liability differing from actual liability, crystallization of a liability during the subsequent /period, enactment of statute with retrospective effect etc.

The ld. AO neither called for the justification/clarification for such PPE nor called for the vouchers and other supporting documents for verification and without proper examination of the documents disallowed the entire PPE, which is against principles of natural justice and bad in law.

It may be mentioned here that during the relevant AY 2010-11, an amount of Rs 3,17,78,216/- was booked under PPE, whose details is given below:

Details of Prior Period Expenses

Pl No.		*Amount*
1	*Towards Service Tax on differential Port variable charges*	*1,81,90,008/-*
2	*Towards differential port variable charges*	*1,09,32,448/-*
3	*Towards price difference on account of IOCL*	*26,54,640/-*
4	*Others*	*1120/-*
	Total	*3,17,78,216/-*

Out of the above, Service Tax on differential Port variable charges and differential

port variable charges amounting to Rs 1,81,90,008/- and Rs 1,09,32,448/- (mentioned against SI. No. 1 and 2 above) has already been offered to tax under the other heads in the computation of income and accordingly not disallowed by the AO.

However as far as, disallowance of Rs 26,55,760/- is concerned, we would like to bring the following facts for your kind consideration:

During the AY 2010-11, an amount of Rs 26,54,640/- was booked towards differential expenses on account of purchase of furnace oil from IOCL. PPL uses furnace oil for it's granulators to make the fertilizer into granules forms.

PPL purchased FO from IOCL and the provisional billing and settlement of bills is being continued till a final reconciliation has been arrived at, During the relevant AY 2010-11, an amount of Rs 25,54,640/- was derived to be payable to IOCL based on a mutual reconciliation done between PPL and IOCL.

The reason for reconciliation is primarily attributable to change in rate of FO with retrospective effect and the difference in invoiced quantity vis-a-vis receipt quantity. Since IOCL is a Central Govt. PSU and PPL, wholly dependent on IOCL for uninterrupted supply of FO, both the organizations went for a reconciliation for the period 1.4.2005 to 31.03.2009 and arrived at a figure of Rs 26,54,640/- to be payable by PPL to IOCL. Copy of the signed reconciliation statement is attached and marked as Annexure-8 for your kind reference. This expense was never claimed in any of the Return of Income filed for past years.

Since the expense is relating to past period, the statutory auditors insisted to book the same under 'Prior Period Expenses'. Since the expense has been crystallized during the AY 2010-11, the entire amount is allowable as business expenses."

14. The CIT(A) after considering the submissions of the assessee held as under:

"I have gone through the submissions of the appellant and facts on record. The disallowance made by the AO on account of prior period adjustment consists of items as under:

Price difference on account of IOCL	:	Rs.26,54,640/-
Others		Rs. 1,120/-
	Total :	Rs.26,55,760/-

The prior period adjustment is mainly on account of price difference with IOCL which has been recognised in the F.Y. 2009-2010 relevant to the assessment year. The IOCL is public sector undertaking on which the appellant is critically dependent. The billing disputes have been

> settled by mutual discussion and reconciliation as per minutes of joint reconciliation of accounts drawn on 17.2,2010, a copy of which has been filed as per which further net amount of Rs.26,54,639.51 was determined payable by the appellant to the IOCL. The price differential is mainly due to change of rate of FO with retrospective effect and difference in invoice quantity and receipt quantity. Accordingly, the amount of Rs.26,54,640/- has been crystallized in the FY 2009-10 relevant to the impugned assessment year. Accordingly, the addition of Rs.26,55,760/- on account of prior period adjustment is deleted."

15. Ld D.R. relied on the order of the Assessing Officer and ld A.R. supported the order of the CIT(A).

16. After considering the rival submissions and perusing the orders of lower authorities, we find that ld D.R. could not controvert the findings of the CIT(A) that IOCL is a public sector undertaking on which the assessee is critically dependent. The billing disputes have been settled by mutual discussion and reconciliation as per minutes of joint reconciliation of accounts drawn on 17.2,2010, a copy of which has been filed as per which further net amount of Rs.26,54,639.51 was determined payable by the appellant to the IOCL. The price differential is mainly due to change of rate of FO with retrospective effect and difference in invoice quantity and receipt quantity. Therefore, the amount of Rs.26,54,640/- has been crystallized in the FY 2009-10 relevant to the impugned assessment year. Hence, we confirm the order of the CIT(A) and dismiss the grounds of the revenue.

17. In the result, appeal filed by the revenue is dismissed.

Now we take up the Assessee's appeal in ITA No.264/CTK/2014.

18. Ground Nos.1 & 4 are general in nature, hence, requires no separate adjudication by us.

19. In Ground No.2 of the appeal, the grievance of the assessee is that the CIT(A) erred in confirming the disallowance of Rs.1,74,85,684/- under school expenses.

20. The brief facts of the case are that the Assessing Officer disallowed Rs.1,74,85,684/- u/s.40A(9) of the Act being amount paid to DAV School by the assessee for running the School in the plant premises. The assessee before the Assessing Officer submitted that payment of DAV school management was neither falling under 'setting up' nor 'formation of' nor under "as contribution to" any fund/trust etc, and, therefore, the same was allowable as business expenditure which was not accepted by the Assessing Officer. According to the Assessing Officer, the claim was covered under the provisions of section 40A(9) of the Act and, accordingly disallowed the same.

21. Before the CIT(A), the assessee submitted as under:

> "*In this regard it may be mentioned here that, the learned AO on irrelevant considerations and presumptions has disallowed/ added an amount of Rs. 1,74,85,684/- towards school expenses by invoking Sec 40A (9) of the IT Act in holding that the same is not eligible as expenses .*
>
> *The aforesaid amount of Rs. 1,74,85,684/- is for the welfare of employees being the expenses of the school (DAV school), which has been established within the*

plant premises and all the expenses are wholly met by the company during the year and has been incurred wholly and exclusively for the purpose of business and therefore ought to be fully allowable as deduction u/s.37 of the Act.

In this regard, we would humbly submit that, for the welfare of the employees, a school has been established within the plant premises and the school is managed by DAV. All the expenses of the school are met directly by the company. It may be mentioned here that, during the AY 2010-11, an amount of Rs 1,74,85,684/- has been booked towards school expenses. Since the entire expenses had been incurred for the staff welfare, the same is an allowable business expenditure. Section 40A(9) provides that "No deduction shall be allowed in respect of any sum paid by the assessee as an employer towards the setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individuals, society registered under the Societies Registration Act, 1860 (21 of 1860), or other institution for any purpose, except where such sum is so paid, for the purposes and to the extent provided by or under clause (iv) 58a [or clause (iva)] or clause (v) of sub-section (1) of section 36, or as required by or under any other law for the time being in force."

Since, payment to DAV school Management is neither falling under "Setting up" nor under "Formation of" nor under "as Contribution to" any fund /trust etc, the same is outside the purview of Sec 40 A (9) of the IT Act. Although the aforesaid fact was appreciated by the Ld. AO in the assessment order, but disallowed the expenses on a flimsy ground. Without considering the basic criteria laid down in the Sec 40 A (9) i.e. "towards the setting up or formation of, or as contribution to, any fund, trust entire amount of school expenses u/s 40 A (9).

the Ld. AO disallowed the

That the aforesaid amount of Rs. 1,74,85,684/- being the amount incurred during the year for the school (DAV school) does not fall under the ambit of provisions of section 40A(9) of the I.T Act and therefore the said disallowance u/s 40A (9) of the Act is legally untenable.

In this regard reliance can be placed on the case of CIT vs Madras Refinery Limited [(2004) 266 ITR 170(Mad)], where the High Court adjudicated that the expenditure incurred for public welfare was in relation to promoting the business in the local community, thereby was incurred for the purpose of business. It may be mentioned here that the Hon'ble ITAT Delhi Bench in the case of CIT V Gujarat Guardian Ltd [2006] 152 Taxman 37 (Delhi) (Mag) held that school expenses can not be disallowed u/s 40 A (9) of the IT Act, Copy of the aforesaid judgement along with detail of school expenditure is enclosed and marked as Annexure-9 for your kind consideration."

22. After considering the submissions of the assessee, the CIT(A) confirmed the disallowance by observing as under:

"I have considered the matter carefully. The appellant's submissions are that the amounts spent in running the school is business expenditure

since the school is run for staff welfare. The appellant is entitled to look after welfare of its employees which helps in running the business smoothly and also to raise profit and productivity. However, the staff welfare cannot be an excuse to justify running of a school or college and claiming expenditure as business expenses. There has to be a reasonable basis for expenditure on staff welfare activity. Under the guise of staff welfare activities, the employer could not take over every aspect of an employee's private life and day-to-day existence. Running of a school has become a business in itself. In view of the same, the expenditure incurred in running of a school is not business expenditure and hence the AO is correct in disallowing the same, The addition of Rs.1,74,85,684/- made by the AO is confirmed."

23. Ld A.R. relied on the decision of Delhi Benches of the Tribunal in the case of DCIT vs. Gujarat Guardian Ltd., (2006) 152 Taxman 37 (Del) (Mag), wherein, the assessee had incurred an expenditure of Rs.10 lakhs towards contribution to a school and the Assessing Officer disallowed the same u/s.40A(9) of the Act, which bars deduction of contribution made by an employer to any fund, trust, etc, for the benefit of employees. On appeal, the CIT(A) allowed the deduction by following the decision of the Delhi Benches of the Tribunal in the case of Modi Rubber Ltd vs IAC(IT Appeal Nos.6227 (Delhi) of 1986 and 142 (Del) of 1987 dated 29.1.1993. On further appeal, the Tribunal confirmed the order of the CIT(A).

24. Further, ld A.R. relied on the decision of Hon'ble Kerala High Court in the case of CIT vs N.Radhakrishnan, (2000) 243 ITR 284 (Ker) where the assessee a public sector undertaking engaged in the manufacture and sale of certain chemicals claimed in the assessment year 1985-86, deduction for payment of Rs.5,34,406/- made to FACT school where children of its employees were studying by way of reimbursement

of the school's proportionate expenditure on the ground that the same was allowable under section 40A(10) and section 37(1) of the Act as expenditure was incurred for welfare of the employees and for business purposes. However, the Assessing Officer disallowed the claim observing that the payment had no direct relation with the business activity of the assessee and was more or less in the nature of a donation. The CIT (A) confirmed the disallowance. On appeal, the Tribunal accepted the assessee's claim on the ground the said contribution was for business purposes. On further appeal, Hon'ble High Court held that the expenditure met by the assessee was wholly and exclusively for the welfare of its employees and also for carrying on business of the assessee company more efficiently by having a contended labour force. It was neither a donation covered under section 40A(9) nor a capital in nature not covered by section 37(1) of the Act.. Hence, the Tribunal was justified in allowing the above expenditure towards contribution for the running of the FACT School, as an expenditure for the smooth functioning of the business of the assessee and an expenditure wholly and exclusively for the welfare of the employees of the assessee and thus, allowable under section 37(1) as well as section 40A(10) of the Act.

25. Ld D.R. though relied on the orders of lower authorities but could not cited any contrary decisions before us.

26. After considering the rival submissions and perusing materials available on record, we find that the issue at hand is squarely covered by the decision of Hon'ble Kerala High Court in the case of N.Radhakrishnan quoted above. Respectfully following the same, we set aside the orders of lower authorities and delete the disallowance of Rs.1,74,85,684/- made u/s.40A(9) of the Act and allow the ground of appeal of the assessee.

27. In Ground No.3 of the appeal, the grievance of the assessee is that the CIT(A) erred in confirming the order of the Assessing Officer in disallowing the claim of post-retirement medical benefit of Rs.1,37,82,763/-.

28. The brief facts of the case are that the CIT(A) observed that it was submitted before him that the Assessing Officer rejected the claim of post retirement medical benefit of Rs.1,37,82,763/-, which was incurred wholly and exclusively for the purpose of business and allowable as deduction u/s.37 of the Act. During the course of appeal hearing, it was submitted that a fresh claim was lodged during the course of assessment proceedings for deduction of Rs.1,37,82,763/- for post retirement medical benefit which was not claimed in the return of income.

29. The CIT(A) held that the issue of claim of post retirement medical benefit has not been discussed by the Assessing Officer in the assessment order. There is no evidence to support the contention that the fresh claim was made during the assessment proceedings, which has not been made

in the return of income. In view of the same, the CIT(A) held that the claim of Rs.1,37,82,763/- on account of post retirement medical benefit cannot be entertained at the appellate stage and dismissed the ground of appeal of the assessee.

30. Before us also, ld AR also failed to produce any evidence to show that fresh claim was made during the assessment proceedings for deduction of Rs.1,37,82,763/- for post-retirement medical benefit which was not made in the return of income. Therefore, we find no good reason to interfere with the order of the CIT(A) which is hereby confirmed and the ground of appeal of the assessee is dismissed.

31. In the result, appeal filed by the revenue is dismissed and that of the assessee is partly allowed.

Order pronounced in the open court on 04 /08/2017.

Sd/- sd/-

(**Pavan Kumar Gadale)** **(N.S Saini)**
JUDICIALMEMBER **ACCOUNTANT MEMBER**

Cuttack; Dated 04 /08/2017
B.K.Parida, SPS

Copy of the Order forwarded to :

1. The Assessee: Paradeep Phosphates, Bhubaneswar
2. The Revenue : DCIT, Circle -1(1), B**hubaneswar.**
3. The CIT(A)-1, Bhubaneswar
4. Pr.CIT-1, Bhubaneswar
5. DR, ITAT, Cuttack
6. Guard file.

//True Copy//

BY ORDER,

SR.PRIVATE SECRETARY
ITAT, Cuttack