IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH.

I.T.R. No.162 of 1996
Date of decision: 9.3.2011

Commissioner of Income Tax

-----Petitioner.

Vs.

M/s Swaraj Mazda Ltd.

-----Respondent.

CORAM:- HON'BLE MR. JUSTICE ADARSH KUMAR GOEL
HON'BLE MR. JUSTICE AJAY KUMAR MITTAL

Present:- Ms. Urvashi Dhugga, Sr. Standing Counsel
for the applicant.

Mr. Pankaj Jain, Advocate
for the asessee.

ADARSH KUMAR GOEL, J.

1. Income Tax Appellate Tribunal, Chandigarh has referred for opinion of this Court following questions of law, arising out of its order dated 21.2.1995 in I.T.A. No.1098 of 1989 for the assessment year 1987-88:-

> "1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that payment of Daily Allowance by the assessee-company to the Japanese company and the expenses incurred by the assessee-company on the Japanese engineers during their stay in India were not in the nature of fee

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for technical services as contemplated in Explanation 2 to Section 9(1)(vii) of the Income Tax Act and were not taxable under section 115A(1) of the Act?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the Double Taxation Avoidance Agreement between India and Japan overrides the provisions of the Income Tax Act?"

2. The assessee entered into technical assistance agreement dated 5.10.1984 with a Japanese company M/s Mazda Motor Corporation envisaging transfer of rights to assemble and manufacture certain vehicles in India. As per the said agreement, the assessee was to be given the assistance of Japanese engineers for training the engineers of the assessee. The payment made by the assessee to the Japanese company amounting to about ₹72 lacs for the assessment year 1984-85 was sought to be treated as charges for technical services partaking the character of royalty or fee for technical services. The Assessing Officer treated the assessee as assessee in default under Section 201A of the Act for not deducting tax on the said payment attracting tax. According to the assessee, the said payment was by way of Dearness Allowance as per the said agreement and thus, was not taxable income of the recipient. Further stand of the assessee Company was that it had filed application under Section 195(2) of the Act and the requisite No

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Objection Certificate was granted permitting non deduction of tax at source. In the order of assessment, the Assessing Officer held that payment of Dearness Allowance was merely a device for avoidance of tax. In fact the said payment represented royalty or fee for technical services, on which, the recipient was liable to pay tax and the assessee was required to deduct tax at source. On appeal, the CIT(A) upheld the plea of the assessee and set aside the demand, which view has been upheld by the Tribunal as follows:-

> "9. We have also look to section 9(1)(vi) of the Act, which treats income by way of royalty as income accrued in India. Explanation 2 under the said clause defines royalty as a consideration for the transfer of any rights in respect of a patent, invention, model, design, secret formula or trade mark or similar property. It is also said to be a consideration for the imparting of any information concerning the working of a patent, invention etc. Royalty is also a consideration for imparting of any information concerning technical, industrial commercial or scientific knowledge, experience or skill. Similarly, income by way of fees is also made taxable in clause (vii) of section 9(1) of the Income Tax Act. Here also, Explanation 2 defines "fees for technical services" as consideration for the rendering of any managerial, technical or other consultancy services but did not include consideration for any construction, assembly, minor or like project.
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> 10. From the perusal of the aforesaid two provisions relating to royalty and fees for technical services

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made taxable as income, it would be clear that the nature of payment in the present case has to be determined in the light of aforesaid definitions. We have already seen that imparting of training does not find any mention either in clause (vi) or in clause (vii) of section 9(1) of the Act. Therefore, it would be difficult to assume that the remittance made by the assessee company to meet out of pocket expenses of the engineers was either royalty or fees for technical services. If at all the any surplus money was left with the Japanese Co. The revenue did not collect any information to come to the conclusion that the Japanese Co. did not retain part of the receipt and that surplus became the commercial profit of the Japanese Co. In the absence of any evidence on record, the revenue's plea regarding surplus in the hands of the Japanese Co. it is found to be without basis. Moreover, we have already seen that commercial profits could be treated to be income if the Japanese Co. had permanent establishment in India vide Article III(1) of the Govt. Agreement. In the light of the clear provision contained in Govt. Agreement, which has an overriding effect by virtue of Article XI (1), the commercial profits, if any, available in the hands of the Japanese firm could not be treated to be taxable income. Therefore, the assessee company was not required to deduct tax on such remittance.

11. The Ld. Counsel for the assessee has invited our attention to an order of the Tribunal (Bombay Bench) in the case of Siemens Aktiengesellschaft Vs ITO (Bom.) (SB), (22 ITD 87), for the proposition that the payments made by the assessee company did not fall under the term "royalty" as defined in Article IX of

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the Govt. Agreement. Our attention has also been drawn to another decision of the Tribunal (Delhi Bench) in the case of ITO V Vidogum & Chemicals Ltd. (23 ITD 235) in support of the plea that where a lump-sum payment was made to a foreign company for securing deputation of their experts in India, that was reimbursement of wages for foreign technicians and not fees for technical know-how. In Jaipur Udyog Ltd. vs CIT (155 ITR 476), the Rajasthan High Court had also an occasion to examine a matter regarding a case of default u/s 201 of the Act. It was held that it was not open to the department to withdraw certificate issued u/s 197(3) of the Act if the assessee had acted upon the determination and had paid the dividend to the shareholders. The Ld. counsel has contended that in the present case of the assessee, no objection certificate has been issued by the AO u/s 195(2) but no recourse was taken to cancel that certificate as required in subsection (4) of the said section. Instead action 201 of the Act was taken deeming the assessee to be a defaulter in respect of the tax. It is contended that the assessee could not be treated/deemed to be an assessee in default in respect of tax u/s 201(1) of the Act unless the certificate granted under sub-section (2) of section 195 was cancelled by the AO under sub-section (4) of that section. The Ld. Counsel has, therefore, vehemently agued that the order of the AO was invalid and unsustainable. We find force in the argument and the revenue has not been able to show as to why no action was taken u/s 155(4) of the Act before deeming the assessee to be an assessee in default u/s 201(1) of the Act.

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12. Looking to the entire facts of the case, we are of the view that whatever payments are made by the assessee to the Japanese Co. these were to meet out of pocket expenses of the Japanese engineers sent by the Japanese Co. for training the workers and technicians of the assessee company. Therefore, these payment did not partake the character of royalty or fees for technical services. There is no evidence on record to substantiate the assumption that be part of the remittance was retained by the Japanese Co. as a surplus which amounted to commercial profits. In the absence of any evidence on record, it would not be appropriate to assume that the entire money received from the assessee was not dispersed among the Japanese engineers. Even if there was some surplus left in the hands of the Japanese Co. that could not be subject to tax by way of commercial profits in the light of Article III(1) of Government Agreement. Article XI(1) of the Govt. Agreement requires that the laws in force will govern the taxation of income except where the provisions have been made to the contrary in the Govt. Agreement. Therefore, it is clear that the Govt. Agreement shall prevail over the provision of law. Looking in the entire facts of the case, we find that the First Appellate Authority has taken correct view in the matter by ordering the refund of the amount by the Department."

3. We have heard learned counsel for the parties.

4. Learned counsel for the assessee points out that the Tribunal has recorded a clear finding that the certificate granted under Section 195(2) was never cancelled under Section 195(4),

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in absence of which the assessee was not required to deduct tax at source and could not be treated as assessee in default. On the said finding, no question of law has been claimed or referred. If the assessee was not required to deduct tax at source and could not be declared assessee in default, question whether the payment was in the nature of fee for technical services or in the nature of reimbursement for the expenses incurred or whether Double Taxation Avoidance Agreement overrides the provisions of the Act, need not be gone into.

5. Learned counsel for the revenue has not been able to dispute the fact that there is no challenge to the finding that certificate issued to the assessee under Section 195(2) was never cancelled and in absence thereof, the assessee could not be treated as assessee in default. In view of the said unchallenged finding, the order of the Tribunal has to be sustained. Once it is so, we are of the view that the questions referred need not be gone into.

The reference is disposed of accordingly.

(ADARSH KUMAR GOEL)
JUDGE

March 09, 2011 **(AJAY KUMAR MITTAL)**
ashwani **JUDGE**

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