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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Date of decision : 05.02.2018

\+ W.P.(C) 5908/2015

DANISCO INDIA PRIVATE LIMITED ..... Petitioner

Through Mr. Sujit Ghosh, Ms. Kanupriya Bhargava and Ms. Mannat Waraich, Advs.

versus

UNION OF INDIA & ORS. ..... Respondents

Through Mr. Prasanta Verma, SCGC with Ms.Shalu Goswami, Adv. for UOI/R1.
Mr. Ruchir Bhatia, Sr. Standing Counsel and Mr. Puneet Rai, Jr. Standing Counsel for Income Tax Deptt.
Mr. C. Mukund, Ms.Geetika Matta and Mohd. Farib Ahmed, Advs. for RBI/R4

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE A. K. CHAWLA

HON'BLE MR. JUSTICE S. RAVINDRA BHAT (ORAL)

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The petitioner is aggrieved of Section 206AA of the Income Tax Act ('the Act') (introduced by Finance Bill No. 2 of 2009) that directs a levy of 20% in the case of outward remittances in the hands of the payer (hereafter referred to as 'the deductor') and is applicable

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to assessees that are non-residents of India. Section 206AA to the extent it is relevant, reads as follows :

> *"206AA. (1) Notwithstanding anything contained in any other provisions of this Act, any person entitled to receive any sum or income or amount, on which tax is deductible under Chapter XVIIB (hereafter referred to as deductee) shall furnish his Permanent Account Number to the person responsible for deducting such tax (hereafter referred to as deductor), failing which tax shall be deducted at the higher of the following rates, namely:—*
>
> *(i) at the rate specified in the relevant provision of this Act; or*
> *(ii) at the rate or rates in force; or*
> *(iii) at the rate of twenty per cent.*

2. The petitioner complains that the impugned provision cannot be sustained having regard to the peculiar facts of this case. The petitioner is an Indian assessee, who, in the normal course of its business remits payments to M/s DuPont Singapore, a non-resident company, located in Singapore. DuPont is not a tax assessee in India. Tax relationship between the two countries is regulated in terms of Indo-Singapore Double Taxation Avoidance Agreement (DTAA). The relevant provisions of DTAA mandates a cap of 10% upon the recovery of amounts, in respect of tax incidence that occurs in the concerned host country (Article 12). Article 12 of the DTAA reads, as follows :

> *"ROYALTIES AND FEES FOR TECHNICAL SERVICES*
> *7. Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.*

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[1][2 However, such royalties and fees, for technical services may also be taxed in the Contracting State in which they arise and according to the laws of that Contracting State," but if the recipient is the beneficial owner of the royalties or fees for technical services, the tax so charged shall not exceed 10 per cent.]

3. The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use:

> *(a) any copyright of a literary, artistic or scientific work, including cinematograph film or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right, property or information ;*
>
> *(b) any industrial, commercial or scientific equipment, other than payments derived by an enterprise from activities described in paragraph 4(6) or 4(c) of Article 8.*

4. The term "fees for technical services" as used in this Article means payments of any kind to any person in consideration for services of a managerial, technical or consultancy nature (including the provision of such services through technical or other personnel) if such services :

> *(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received ; or*
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> *(b) make available technical knowledge, experience, skill, know-how or processes, which enables the person acquiring the services to apply the technology contained therein; or*
>
> *(c) consist of the development and transfer of a technical plan or technical design, but excludes' any service that does not enable the person acquiring the, service to apply the technology contained therein.*

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For the purposes of (6) and (c) above, the person acquiring the service shall be deemed to include an agent, nominee, or transferee of such person.

5. Notwithstanding paragraph 4, "fees for technical services" does not include payments :

> *(a) for services that are ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of property other than a sale described in paragraph3(a);*
>
> *(b) for services that are ancillary and subsidiary to the rental of ships, aircraft, containers or other equipment used in connection with the operation of ships or aircraft in international traffic ;*
>
> *(c) for teaching in or by educational institutions ;*
>
> *(d)for services for the personal use of the individual or individuals making the payment;*
>
> *(e) to an employee of the person making the payments or to any individual or firm of individuals (other than a company) for professional services as defined in Article 14;*
>
> *(f) for services rendered in connection with an installation or structure used for the exploration, or exploitation of natural resources referred to in paragraph 2(/) ofArticle5 ;*
>
> *(g) for services referred to in paragraphs 4 and 5 of Article 5.*

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

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

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

3. The services rendered by DuPont-it is not disputed, are covered by the expression 'fees for technical services'. Thus, on an application of the principle of law enunciated in *Azadi Bachao Andolan Vs. Union of India,* (2003) 263 ITR 706 (SC), even if the tax rate for the activity which would form part of the expression 'fees for technical services' is higher, not more than 10% can be recovered by the Indian Tax Authorities. The petitioner contends that Section 206AA (i) has the effect of undoing the provisions of DTAA, besides being in violation of Article 265 of Constitution of India. The petitioner in support of its contention that the levy of 20% rate is

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unconstitutional relies upon the recommendations of Justice Easwar's Committee's report of 2016 made to the Central Government. Upon a review of existing tax laws, Justice Easwar's Committee made the following specific recommendations:

> *"Under the current provisions of Section 206AA, tax is required to be deducted by the deductor at a higher rate as prescribed under the said section, where the deductee does not furnish his Permanent Account Number (PAN). This section was introduced with the objective that the furnishing of PAN was important with a view to trail the taxability of the payments in the hands of a non-resident. As regards non-residents, the Committee noted that in view of the specific provisions of Section 115A and the provisions under the respective Double Tax Avoidance Agreements (DTAAs) prescribing specific rates for tax deduction at source u/s. 195, there was no justification for providing deduction of tax at a higher rate than as prescribed under Section 115A or under the respective DTAA. In fact, this provision has proved to be an impediment in terms of ease of business, as many non-residents prefer not to do business with Indian residents, if obtaining of PAN is insisted from them. The Committee was of the view that it should suffice if the concerned non-resident furnished to the deductor, in lieu of such Permanent Account Number, his tax identification number in the country or the specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which such person claims to be a resident.*

4. It is contended that acting upon the recommendations, the Central Government moved an amendment, which Parliament effected through Finance Act of 2016, that, in effect, neutralized the existing

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provision by substituting Sub-section (7). The newly added Sub-section 206AA(7) w.e.f. 1.6.2016 reads as follows :

> *"(7) The provisions of this section shall not apply to a non-resident, not being a company, or to a foreign company, in respect of —*
>
> > *(i) payment of interest on long-term bonds as referred to in section 194LC; and*
> > *(ii) any other payment subject to such conditions as may be prescribed."*

5. Learned counsel for the respondents urges that with the passage of the amendment, the effect, if any, of pre-existing provision has been neutralized. Learned counsel also points out Rule 37BC of the Income Tax Rules introduced after the amendment does away with the mandatory requirement of the overseas company intending to possess an Indian PAN and instead demands a specific identification number or code as provided. It is also pointed out that Section 206AA was interpreted by a Bench of the Income Tax Tribunal in *Dy. Director of Income Tax Vs. Serum Institute of India Ltd.* (ITA 792/PN/2013, decided on 30.3.2015)

6. After hearing the counsel for the parties, it is quite apparent that the issue urged has been rendered largely academic on account of corrective amendment made by the Parliament-which substituted pre-existing Sub-section (7) with the present Section 206AA (7). The amendment is mitigating to a large extent, the rigors of the pre-existing laws. The law, as it existed, went beyond the provisions of

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DTAA which in most cases mandates a 10% cap on the rate of tax applicable to the state parties. Section 206AA (prior to its amendment) resulted in a situation, where, over and above the mandated 10%, a recovery of an additional 10%, in the event, the non- resident payee, did not possess PAN.

7. In this context, the ITAT in *Serum Institute of India* (Supra) discussed this very issue in some detail and stated, as follows:

> "*...........The case of the Revenue is that in the absence of furnishing of PAN, assessee was under an obligation to deduct tax @ 20% following the provisions of section 206AA of the Act. However, assessee had deducted the tax at source at the rates prescribed in the respective DTAAs between India and the relevant country of the non-residents; and, such rate of tax being lower than the rate of 20% mandated by section 206AA of the Act. The CIT(A) has found that the provisions of section 90(2) come to the rescue of the assessee. Section 90(2) provides that the provisions of the DTAAs would override the provisions of the domestic Act in cases where the provisions of DTAAs are more beneficial to the assessee. There cannot be any doubt to the proposition that in case of non-residents, tax liability in India is liable to be determined in accordance with the provisions of the Act or the DTAA between India and the relevant country, whichever is more beneficial to the assessee, having regard to the provisions of section 90(2) of the Act. In this context, the CIT(A) has correctly observed that the Hon'ble Supreme Court in the case of Azadi Bachao Andolan and Others v. UOI, MANU/SC/1219/2003 : (2003) 263 ITR 706 (SC) has upheld the proposition that the provisions made in the DTAAs will prevail over the general provisions contained in the Act to the extent they are beneficial to the assessee. In this*

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context, it would be worthwhile to observe that the DTAAs entered into between India and the other relevant countries in the present context provide for scope of taxation and/or a rate of taxation which was different from the scope/rate prescribed under the Act. For the said reason, assessee deducted the tax at source having regard to the provisions of the respective DTAAs which provided for a beneficial rate of taxation. It would also be relevant to observe that even the charging section 4 as well as section 5 of the Act which deals with the principle of ascertainment of total income under the Act are also subordinate to the principle enshrined in section 90(2) as held by the Hon'ble Supreme Court in the case of Azadi Bachao Andolan and Others (supra). Thus, in so far as the applicability of the scope/rate of taxation with respect to the impugned payments make to the non-residents is concerned, no fault can be found with the rate of taxation invoked by the assessee based on the DTAAs, which prescribed for a beneficial rate of taxation. However, the case of the Revenue is that the tax deduction at source was required to be made at 20% in the absence of furnishing of PAN by the recipient non-residents, having regard to section 206AA of the Act. In our considered opinion, it would be quite incorrect to say that though the charging section 4 of the Act and section 5 of the Act dealing with ascertainment of total income are subordinate to the principle enshrined in section 90(2) of the Act but the provisions of Chapter XVII-B governing tax deduction at source are not subordinate to section 90(2) of the Act. Notably, section 206AA of the Act which is the centre of controversy before us is not a charging section but is a part of a procedural provisions dealing with collection and deduction of tax at source. The provisions of section 195 of the Act which casts a duty on the assessee to deduct tax at source on payments to a non-resident cannot be looked upon as a charging provision. In-fact, in the

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context of section 195 of the Act also, the Hon'ble Supreme Court in the case of CIT v. Eli Lily & Co., MANU/SC/0487/2009 : (2009) 312 ITR 225 (SC) observed that the provisions of tax withholding i.e. section 195 of the Act would apply only to sums which are otherwise chargeable to tax under the Act. The Hon'ble Supreme Court in the case of GE India Technology Centre Pvt. Ltd. v. CIT,MANU/SC/0688/2010 : (2010) 327 ITR 456 (SC) held that the provisions of DTAAs along with the sections 4, 5, 9, 90 & 91 of the Act are relevant while applying the provisions of tax deduction at source. Therefore, in view of the aforesaid schematic interpretation of the Act, section 206AA of the Act cannot be understood to override the charging sections 4 and 5 of the Act. Thus, where section 90(2) of the Act provides that DTAAs override domestic law in cases where the provisions of DTAAs are more beneficial to the assessee and the same also overrides the charging sections 4 and 5 of the Act which, in turn, override the DTAAs provisions especially section 206AA of the Act which is the controversy before us. Therefore, in our view, where the tax has been deducted on the strength of the beneficial provisions of section DTAAs, the provisions of section 206AA of the Act cannot be invoked by the Assessing Officer to insist on the tax deduction @ 20%, having regard to the overriding nature of the provisions of section 90(2) of the Act. The CIT(A), in our view, correctly inferred that section 206AA of the Act does not override the provisions of section 90(2) of the Act and that in the impugned cases of payments made to non-residents, assessee correctly applied the rate of tax prescribed under the DTAAs and not as per section 206AA of the Act because the provisions of the DTAAs was more beneficial. Thus, we hereby affirm the ultimate conclusion of the CIT(A) in deleting the tax demand relatable to difference between 20% and the actual tax

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rate on which tax was deducted by the assessee in terms of the relevant DTAAs. As a consequence, Revenue fails in its appeals.

8. Having regard to the position of law explained in *Azadi Bachao Andolan* (supra) and later followed in numerous decisions that a Double Taxation Avoidance Agreement acquires primacy in such cases, where reciprocating states mutually agree upon acceptable principles for tax treatment, the provision in Section 206AA (as it existed) has to be read down to mean that where the deductee i.e the overseas resident business concern conducts its operation from a territory, whose Government has entered into a Double Taxation Avoidance Agreement with India, the rate of taxation would be as dictated by the provisions of the treaty.

The writ petition is partly allowed in the above terms.

S. RAVINDRA BHAT, J

A. K. CHAWLA, J

FEBRUARY 05, 2018
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