
Export Commission paid to Indian agent of NR, taxable in India; Disallowance of commission in hands of payer under section 40(a)(i)

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In brief

In a recent decision¹ the Madras High Court (HC) has held that commission paid to an Indian agent of a non-resident (NR) was taxable in India as business income. Consequentially, such payment shall be subject to withholding tax under section 195 of the Income-tax Act, 1961 (the Act) and non-compliance of the same was liable for disallowance of such payments under section 40(a)(i) of the Act.

In detail

Facts

- The appellant (taxpayer), an exporter of garments, entered into an agreement with T Limited (a Hong Kong based company) for procurement of export orders. During the year, commission was paid to the Indian agent of T Limited and it was claimed as a business expense by taxpayer.
- Claim of commission paid to the Indian agent in India was disallowed by invoking the provisions of section 40(a)(i) of the Act.
- On appeal before the Commissioner of Income-tax (Appeals) [CIT(A)], the taxpayer contended that since, the services were

rendered outside India, the payment of commission was not liable for tax in India and relied on Central Board of Direct Taxes Circular No. 786 dated 07 February, 2000. Accordingly, it was claimed that tax was not required to be withheld under section 195 of the Act. CIT(A) held that Circular No. 786 was not applicable in this case since, commission was paid to an India recipient. CIT(A)'s decision was also upheld by the Income-tax Appellate Tribunal (Tribunal).

Issue before the High Court

Whether the payment of commission made to the Indian agent of the NR was liable for withholding tax under section 40(a)(i) ignoring that sub-section (ia) was

introduced only with effect from financial year 2004-05?

Taxpayer's Contention

Section 40(a)(ia) of the Act has been inserted with effect from 01 April, 2004 and the same would not be applicable to the assessment year (AY) 2002-03.

Revenue's Contention

The amount represented commission paid to Indian agent of T Limited. Thus, it was taxable in India and was liable for withholding tax as per section 195 of the Act.

High Court's ruling

- HC noted that Circular No. 786 was not applicable since, the commission was received by the Indian agent of T Limited (instead of foreign agent of Indian exporters) in India

¹ T.C. (Appeal) No.121 of 2009

and there was nothing on record to show that the Indian agent transmitted it to Hong Kong. It was also noted that since, disallowance in the present case had been effected in terms of sub clause (i) of section 40(a) of the Act relating to NR, accordingly, the argument raised by the taxpayer that section 40(a)(ia) of the Act had been inserted

with effect from 01 April, 2004 and the same would not be applicable to the relevant AY did not hold good, and further, this ground was not raised by the taxpayer before the TO and CIT(A).

- The HC held that accordingly, there was no infirmity in the orders passed by the lower authorities and confirmed the disallowance of commission.

The takeaways

Commission paid to an Indian agent of the NR in India is chargeable to tax in India, and accordingly liable for withholding tax under section 195 of the Act.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor

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