

Transmission Corporation of A.P. Ltd.

Vs

Commissioner of Income Tax, A.P.

Civil Appeal Nos. 594-96 of 1985

(D. P. Wadhwa, M. B. Shah JJ)

17.08.1999

JUDGMENT

M.B. Shah, J. –

1. These appeals are filed by the Assessee against the judgment and order dated 2nd July, 1984 passed by the Andhra Pradesh High Court in deciding three income tax reference partly in favour of the revenue. (Re : *CIT v. Superintending Engineer, Upper Silera, 1985(152) ITR 753*. The Court held that provisions of Section 195 relating to deduction of tax at source come into operation in respect of sums paid to a non-resident, whether or not such sum represents only income or profits if such sums are paid to non-residents during the course of regular trading operation. That finding is challenged in these appeals.

2. Before deciding the question involved, we would refer to a few facts of the matter :-

The appellant the Andhra Pradesh State Electricity Board (hereinafter referred to as "the Board") made certain payments to non-resident against the purchase of machinery and equipment and also against the work executed by the non-residents in India of erecting and commissioning the machinery and equipment. The Board entered into two separate agreement with M/s. Charmilles Engineering Works Ltd., Geneva, Switzerland, one for the purchase of Nos. 95,000 BHP Francis Turbines and another for purchase of 2 Nos. Butterfly Valves. There were two other contracts of the assembly, erection and testing and commissioning of the aforesaid equipments. The payments were made to the non-resident company for the financial year 1966-67 to 1972-73. The Board also entered into an agreement with Oerlikon Engineering Co., Zurich, Switzerland, for the purchase of 2 Nos. 60 MW generators and Indoor Switchgear for the Sileru Hydro Electric Scheme. Another contract was executed for the assembly, erection and testing and commissioning of the above equipments. The payments were made in the financial year 1966-67, 1967-68 and 1968-69. Third contract was entered by the Board with M/s. Sacheron Works Ltd., Geneva, Switzerland for the purchase and erection of 7 nos. power transformers for the Sileru Hydro Electric Scheme. On the basis of the said contract in the financial year 1966-67, the amount was paid to the non-resident company. For the aforesaid payments, the question arose whether the Electricity Board was under an obligation to deduct tax at source from these payments under Section 195 of the Income Tax Act, 1961 (hereinafter referred to as "the Act"). These payments were made by the Electricity Board without deduction of tax at source. Owing to the failure of the Electricity Board to deduct such tax, it was deemed to be an assessee in default in respect of the

tax deductible at source. Hence, Income Tax Officer passed orders determining the tax which, according to him, was deductible at source under Section 195 and the Electricity Board was required to pay such amounts. Against the order of the Income Tax Officer, appeals were filed by the assessee which were allowed by the Appellate Assistant Commissioner with the observation that the words "any other sum chargeable under the provisions of this Act" occurring in Section 195 of the Act do not contemplate inclusion of trade receipts in their ambit and that Section 195 applies only to cases where the sums paid are "pure income profits". The Appellate Assistant Commissioner, therefore, allowed the appeals and set aside the orders passed by the Income Tax Officer. Against the said order, Revenue preferred appeals before the Income Tax Appellate Tribunal. The Income Tax Appellate Tribunal also dismissed the appeals filed by the Income Tax Officer on the ground that the provision of Section 195 of the Act are not applicable to payments of sums to a non-resident, which are not "pure income profits". Thereupon, on the reference applications filed by the Commissioner of Income Tax under Section 256(1) of the Act the Tribunal referred the following question of law for the decision of the High Court for the payments made to the non-resident company :-

R.C. NO. 205 of 1978 :-

"Whether on the facts and in the circumstances of the case, the Superintending Engineer, Civil Circle, Upper Sileru, is liable to deduct income-tax u/s. 195 of the Income-Tax Act, 1961 on the payments made to the non-resident company for the assessment years 1966-67, 1967-68, 1968-69 and 1969-70 ?"

3. Similar questions with regard to payments made to two other non-residents as stated above were also referred in R.C. Nos. 203 and 204 of 1978. 4. At the time of hearing of the matter, the High Court stated that two fundamental question arise for consideration and they were : (a) whether the provisions of Section 195 of the Act are applicable to cases where the sum paid to the non-resident does not wholly represent income; and (b) if Section 195 is applicable in such cases, whether the Income-tax Officer could enforce deduction of tax at source on the gross amount of trading receipts or only in respect of that portion of the trading receipts which may be chargeable as income under the Act ? The Court observed that the question referred to deals with only first aspect mentioned above but the second aspect is an integral part of the first aspect and, therefore, it was necessary to reframe the question in order to bring real controversy between the parties.

5. Thereafter, the Court re-framed and decided the following question :-

"Whether, on the facts and in the circumstances of the case, the Superintending Engineer, Civil Circle, Upper Sileru, is liable to deduct income-tax under Section 195 of the Income-tax Act, 1961 in respect of payments made to non-residents viz., M/s. Charmilles Engineering Works Ltd., M/s. Sacheron Works Ltd., and M/s. Oerlikon Engineering Company and, if so, whether the tax deductible is liable to be determined on the gross sum of money paid to the non-residents ?"

6. Dealing with the contentions raised by the assessee and interpreting Section 195, the High Court held that it should be borne in mind that whatever tax is deducted at source under Section 195 from out of the gross sum is not irretrievably lost to the recipient; it is only a provisional payment which will be made to the Central Government to the credit of the recipient; the provisions of the Act

enable the recipient, whether such recipient is a resident or non-resident, to file a return of income in the regular course and prove to the satisfaction of the ITO the income chargeable under the Act. The Court answered the reframed question as under :-

1. The respondent-assessee, who made the payments to the three non-residents above referred, was under an obligation to deduct tax at source under Section 195 of the Act in respect of the sums paid to them under the contracts entered into.

2. The obligation of the respondent-assessee to deduct tax under Section 195 is limited only to the appropriate proportion of the Income chargeable under the Act forming part of the gross sums of money paid to the three non-residents above referred.

3. While the Income Tax Officer was correct in the determination of tax under Section 195 in respect of the payments made to M/s. Sacheron Works Ltd., in R.C. No. 204, he was in error in determining the tax deductible under Section 195 in respect of the gross sums of money paid to M/s. Charmilles Engineering Works Ltd. in R.C. No. 203 and M/s. Oerlikon Engineering Company in R.C. No. 205.

7. Against the said judgment and order, the appellant-Supreintending Engineer (assessee) has filed these appeals. At the time of hearing of these appeals, learned counsel for the appellant submitted that Section 195 would be applicable where payment to non-resident is 'wholly income' chargeable to tax as it provides that any person responsible for paying to a non-resident "any sum chargeable under the provisions of this Act", shall, at the time of payment, deduct income tax thereon at the rates in force. It is his contention that under the Income Tax Act, tax can be levied and collected on the income but when the payments made to the non-resident were not entirely income, but a trading receipt, there is no question of deduction of income tax at the source as the section does not provide for it. He submitted that the expression "any other sum chargeable under the provisions of the Act" occurring in Section 195 of the Act conveys only one meaning that tax at the source could be deducted when the sum paid is total income 'chargeable' under Section 5 of the Act. If the payment is anything more than or other than income, it does not answer the definition of the total income under Section 5 of the Act. The substance of the contention is what is taxable under the Income Tax Act is pure income or profit and not the gross sum which would include cost of materials and other expenses and hence Section 195 would not be applicable in such cases.

For appreciating the contention raised by the learned Counsel, we would first refer to relevant parts of Sections 190, 195(1), 195(2), 195(3) and 197, as they stood at the relevant time, which are as under :

"190. (1) Notwithstanding that the regular assessment in respect of any income is to be made in a later assessment year, the tax on such income shall be payable by deduction at source or by advance payment, as the case may be, in accordance with the provisions of this Chapter.

(2) Nothing in this section shall prejudice the charge of tax on such income under the provisions of sub-section (1) of Section 4.

195. (1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company which is neither an Indian company nor a company which

has made the prescribed arrangements for the declaration and payment of dividends within India, *any interest* not being "Interest on securities" or *any other sum, not being dividends, chargeable under the provisions of this Act*, shall, at the time of payment, unless he is himself liable to pay any income-tax thereon as an agent, *deduct income-tax thereon at the rates in force*.

(2) *Where the person responsible for paying any such sum chargeable under this Act (other than interest including interest on securities, dividends and salary) to a non-resident considers that the whole of such sum would not be income chargeable in the case of the recipient, he may make an application to the Income Tax Officer to determine, in the prescribed manner the appropriate proportion of such sum so chargeable, and upon such determination, tax shall be deducted under sub-section (1) only on that proportion of the sum which is so chargeable.*

(3) Subject to rules made under sub-section (5), *any person entitled to receive any interest or other sum on which income-tax has to be deducted under sub-section (1) may make an application in the prescribed form to the Income Tax Officer for the grant of a certificate authorising him to receive such interest or other sum without deduction of tax under that sub-section, and where any such certificate is granted, every person responsible for paying such interest or other sum to the person to whom such certificate is granted shall, so long as the certificate is in force, make payment of such interest or other sum without deducting tax thereon under sub-section (1).*

197. Where, in the case of any income of any person other than a company -

(a) income-tax is required to be deducted at the time of credit or, as the case may be, at the time of payment at the rates in force under the provisions of sections 192, 193, 194A, 194D and 195.

(b) being a non-resident, income-tax is required to be *deducted at the time of payment at the rates in force* under the provisions of Section 194, the Assessing Officer is satisfied that the total income of the recipient justifies the deduction of *income-tax at any lower rates or no deduction of income-tax, as the case may be, the Income Tax Officer shall, on an application made by the assessee in this behalf, give to him such certificate as may be appropriate.*

(2) Where any such certificate is given, the person responsible for paying the income shall, until such certificate is cancelled by the Income-tax Officer, deduct income-tax at the rates specified in such certificate or deduct no tax, as the case may be.

(2A)"

8. Before considering Section 195, it is to be stated that the said section is in Chapter XVII containing provisions for collection and recovery of tax. Said chapter is divided into various parts as (A) to (F). Part A - General - deals with deduction at source and advance payment. Section 190, *inter alia*, provides that notwithstanding that the regular assessment in respect of any income is to be made in a latter assessment year, the tax on such income shall be payable by deduction or collection at source or by advance payment, as the case may be, in accordance with the provisions

of the Chapter. Hence, before a regular assessment is made, tax on income shall be payable by deduction or collection at source or by advance payment in accordance with the other provisions. Section 191 provides for direct payment of income-tax by the assessee where provisions is not made under the chapters for deducting income tax at the time of payment. Thereafter, Part (B) of the said Chapter contains group of sections which provides for 'deduction of tax' at source. Section 912 provides for deduction of income tax on the income chargeable under the head "Salaries" by any person responsible for paying such salaries. Section 193 provides for deduction of income tax by the person responsible for paying any income by way of 'interest on securities'. Similarly, Section 194 provides for deduction of income-tax by the company paying 'dividends'. Section 194(A), Section 194(B), Section 194(BB) provides for deduction of income-tax on the income of interest other than interest on securities, winning from lotteries or crossword puzzle and winning from horse race respectively. Even with regard to the payments to contractors and sub-contractors, specific provision is made for deducting the tax specified on the basis of payment thereof in cash or by issue of cheque or draft or by any other mode at the rate of 1% or 2% as the case may be of such sum as income tax on income comprised therein. Section 194(c) reveals the intention of the Legislature to enforce tax deduction at source even in respect of gross sums, the whole of which do not represent income chargeable under the Act. Similar provisions are made in Section 194(D), Section 194(E), Section 194(EE), Section 194(F), Section 194(G), Section 194(H), Section 194(I), Section 194(J) and Section 194(K) which case an obligation to deduct tax on the person responsible for paying such sum which may not represent income. In all these cases, what is deducted is the amount specified in the said sections without their being any actual assessment. Thereafter, Section 195 deals with deduction of tax in cases where payment is to be made to a non-resident which *inter alia* provides :-

- (a) Any person responsible for paying to a non-resident, any interest, or any sum, chargeable under the provisions of this Act (other than interest on securities and salary), shall, at the time of payment, deduct income-tax thereon at the rates in force. Sub-Section (1) of Section 195 excludes from its operation the sum which is to be paid as interest on securities or the sum which is chargeable under the head "Salaries" as the deduction on such sum would be governed by other sections, namely, Sections 192 and 193.
- (b) Where the person responsible for paying any sum chargeable under the Act to a non-resident considers that the whole or such sum would not be chargeable in the case of the recipient, he may make an application to the Assessing Officer to determine "the appropriate proportion of such sums so chargeable", upon such determination, tax shall be deducted under sub-section (1) only on that portion of the sum which is so chargeable.
- (c) Not only this, but Sub-Section (3) provides that any person entitled to receive any interest or other sum on which income-tax is to be deducted under Sub-Section (1) may make an application in the prescribed form to the Assessing Officer for the grant of certificate authorising him to receive such interest or other sum without deduction of tax under the sub-section.
- (d) Further, section 197 provides that recipient can file an application to the Assessing Officer for a certificate that the total income of the recipient justify the deduction of income-tax at any lower rates or no deduction of income tax and the Assessing Officer, if satisfied, can grant such certificate as may be appropriate.

9. The scheme of sub-section (1), (2) and (3) of Section 195 and Section 197 leaves no doubt that the expression "any other sum chargeable under the provisions of this Act" would mean 'sum' on which income-tax is leviable. In other words, the said sum is chargeable to tax and could be assessed to tax under the Act. Consideration would be whether payment of sum to non-resident is chargeable to tax under the provisions of the Act or not? That sum may be income or income hidden or otherwise embedded therein. If so, tax is required to be deducted on the said sum would be the income is to be computed on the basis of various provisions of the Act including provisions of computation of the business income, if the payment is trade receipt. However, what is to be deducted is income tax payable thereon at the rates in force. Under the Act, total income for the previous year would become chargeable to tax under Section 4. Sub-section (2) of Section 4 *inter alia*, provides that in respect of income chargeable under Sub-section (1), income tax shall be deducted at source where it is so deductible under any provision of the Act. If the sum that is to be paid to the non-resident is chargeable to tax, tax is required to be deducted. The sum which is to be paid may be income out of different heads of income provided under Section 14 of the Act, that is to say, income from salaries, income from house property, profits and gains of business or profession, capital gains and income from other sources. The scheme of tax deduction at source applies not only to the amount paid which wholly bears "income" character such as salaries, dividends, interest of securities etc., but also to gross sums, the whole of which may not be income or profits of the recipient, such as payments to contractors and sub-contractors and the payment of insurance commission. It has been contended that the sum which may be required to be paid to the non-resident may only be a trading receipt, and, any contain a fraction of sum as taxable income. It is true that in some cases, a trading receipt may contain a fraction of sum as taxable income, but in other cases such as interest, commission, transfer of rights of patents, goodwill or drawings for plant and machinery and such other transactions, it may contain large sum as taxable income under the provisions of the Act. Whatever may be the position, if the income is from profits and gains of business, it would be computed under the Act as provided at the time of regular assessment. The purpose of sub-section (1) of Section 195 is to see that the sum which is chargeable under Section 4 of the Act for levy and collection of income tax, the payee should deduct income tax thereon at the rates in force, if the amount is to be paid to a non-resident. The said provision is for tentative deduction of income tax thereon subject to regular assessment and by the deduction of income-tax, rights of the parties are not, in any manner, adversely affected. Further, the rights of payee or recipient are fully safeguarded under Sections 195(2), 195(3) and 197. Only thing which is required to be done by them is to file an application for determination by the Assessing Officer that such sum would not be chargeable to tax in the case of recipient, or for determination of appropriate proportion of such sum so chargeable, or for grant of certificate authorising recipient to receive the amount without deduction of tax, or deduction of income-tax at any lower rates or no deduction. On such determination, tax at appropriate rate could be deducted at the source. 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 of tax deduction at source.

10. The High Court of Calcutta considered and interpreted similar provision Section 18(3B) of the Income Tax Act, 1922, in the case of *Ray and Co. (India) Private Limited v. Mukherjee, ITO 1959(36 ITR 365*, and rightly held :

"if 'chargeable under the provisions of this Act' means actually liable to be assessed to tax, in other words, if the sum contemplated is taxable income a difficulty is undoubtedly created as to complying with the provisions of the section."

11. The High Court further held that section 18(3B) contemplated not merely amounts, the whole of which was taxable without deduction, but amounts of a mixed composition, a part of which only might turn out to be taxable income, as well; and the disbursement, which were of the nature of gross revenue receipts, were yet sums chargeable under the provisions of the Income Tax Act and came within the ambit of Section 18(3B) of the Act.

12. Hence, in our view there is no substance in the contention of the learned Counsel for the Appellant that the expression "any other sum chargeable under the provisions of this Act" would not include cases where any sum payable to the non-resident is a trading receipt which may or may not include 'pure income'. The language of Section 195(1) for deduction of income tax by the payee is clear and unambiguous and casts an obligation to deduct appropriate tax at the rates in force. We make it clear that the learned counsel for the parties have not advanced any submissions with regard to other findings given by the High Court.

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

14. In the result, these appeals fail and are dismissed, accordingly with costs.