



GE INDIA TECHNOLOGY CENTRE PRIVATE LTD. VS COMMISSIONER OF INCOME TAX & ANR (2010) 10 SCC 29

SUPREME COURT JUDGMENT

Decided on: 09.09.2010

RATIO DECIDENDI

Payments to a non-resident or foreign company will be subject to deduction of Tax at Source under section 195 (1) of the Income Tax Act, 1961 only if the sum payable is “chargeable to tax” in India in the hands of the non-resident or foreign company.

FACTS

Supreme Court in this matter clubbed various other petitions on the same issue and proceeded on the basis of facts of the leading case of Sonata Information Technology limited. The appellants were the distributors of imported prepackaged shrink wrapped standardized software from Microsoft and other Suppliers outside India. GE made payments to the aforesaid software Suppliers. The ITO (TDS) held that since the sale of software included a license to use the same, payments made by the GE to the foreign Suppliers constituted royalty, which was deemed to accrue or arise in India. Therefore, Tax at Source (TAS) was liable to be deducted under Section

195 of the Income Tax Act, 1961 (Act). The finding of the ITO (TDS) was upheld by the Commissioner (A).

In second appeal, the Income Tax Appellate Tribunal (ITAT), however, held that the amount paid by GE to the foreign software Suppliers was not “royalty” and the same did not give rise to any income taxable in India, and therefore, the GE is not liable to deduct Tax at Source (TAS). Revenue appealed to the High Court of Karnataka and raised the contention that unless the payer makes an application to ITO (TDS) under Section 195 (2) and obtain permission for non-deduction of TAS, payer cannot contend that the income is not chargeable to tax. Karnataka High Court accepted this contention of department and relying on the Supreme Court decision in *Transmission Corporation's* case held that any payment in the nature of income to a non-resident or a foreign company would require TAS deduction under section 195 (1) of the Act.

ISSUE

Whether under the Income Tax Act, 1961, the obligation to deduct tax at source (TAS) arises the moment there is remittance to non-residents?

OBSERVATIONS AND DECISION OF THE SUPREME COURT

1. The most important expression in Section 195 (1) consists of the words "chargeable under the provisions of the Act". If the contention of the Department that the moment there is remittance the obligation to deduct TAS (TDS) arises is to be accepted then we are obliterating the words "chargeable under the provisions of the Act" in Section 195 (1). 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.
2. That 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. Section 195 (2) is based on the "principle of proportionality". The said

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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.

3. The facts of the *Transmission Corporation's* case were different and the reliance of Karnataka High Court on the same is misplaced.

4. The Supreme Court overruled the Karnataka High Court ruling and held that Payment to a non-resident will be subject to withholding of the tax under section 195 (1) of the Act, only if the sum payable is "chargeable to tax" in India in the hands of the non-resident.

CONCLUSION

The issue of Tax Deduction at Source, when the payment is being made by resident to a non-resident has long been a controversial issue with the various High Courts being of divergent opinions. This ruling of Supreme Court has finally settled the position of law in case of payments to non-residents by stating that if payments in not chargeable to tax in India in the hands of the non-resident then there is no liability to deduct Tax at Source.