Payments made to non-resident freight forwarders not chargeable to tax u/s 9(1)(vii) of the Income – Tax Act, 1961 hence the payer not liable to withhold tax u/s 195.

Recently in the case of **ACIT v. Indair Carriers Pvt. Ltd.**[I.T.A. No. 1605 (Del) of 2010], the Delhi Income-tax Appellate Tribunal, held that payments made to non-resident freight forwarders are not chargeable to tax under section 9(1)(vii) of the Income-tax Act, 1961 and hence the payer is not liable to withhold tax under section 195 of the Act. Consequently, there is no question of disallowance of the amounts paid to non-resident freight forwarders under section 40(a)(i) of the Act.

Facts

The assessee was engaged in the business of handling cargo, i.e., booking of cargo received by it, mainly from exporters in India and air transportation of that cargo to various countries of the world as per client requirements.

During the year under consideration, the assessee made certain payment on account of freight forwardingfunctions done by UTI Network Inc. outside India in respect of cargo exports from India to foreign destinations. During the assessment proceedings, along with certain other disallowances, the assessing officer ("AO") disallowed the amount paid to UTI Network Inc. for the reason that Indair had failed to withhold tax. According to the AO, services rendered by UTI Network Inc. were in the nature of managerial services covered under the definition of 'Fees for technical services' under section 9(1)(vii) of the Act, and hence, liable to tax in India.

Before the Commissioner of Income-tax (Appeals) ("CIT(A)"), the assessee submitted that the services rendered by UTI Network Inc. were not managerial services in nature, but commercial services. Reliance was placed by the assessee on Circular No. 715 dated 8 August, 1995 issued by the Central Board of Direct Taxes ("CBDT"), which clarified that payments to resident clearing and forwarding agents for carriage of goods were subject

to withholding tax under section 194C of the Act. Accepting the arguments of the assessee, the CIT(A) held that the services rendered were not managerial services in nature and that these services were recognized as general orcommercial services and not technical services as understood under section 194J of the Act. Furthermore, the CIT(A) also noted that the services had been rendered outside India and hence, were not taxable in India under section 9(1)(vii) read with section 195 of the Act.

The Revenue filed an appeal before the Tribunal against the order of the CIT(A).

Issue – Whether the CIT(A) had erred in holding that the services rendered were not in the nature of managerial services under the provisions of section 9(1)(vii) of the Act and hence, not subject to withholding tax under section 195 of the Act?

Assessee's contentions

- Amount in question was paid purely towards services rendered by UTI Network Inc.
- Services were rendered in the field of freight forwarding functions, i.e., those functions that were generally done by a freight forwarding agent, which were purely business services
- Managerial services would mean services in the field of managing the affairs or laying down policies, procedures, evaluation of the existing system or evaluation of some new policies or strategies in place of a new system
- Drawing an analogy with the services of domestic clearing and forwarding agents rendered for carriage of goods, it was contended that just as the provisions of section 194C (concerning work and service contracts) were applicable and not section 194J (concerning fees for professional or technical services), the services rendered by UTI Network Inc., could not be considered as managerial services under section 9(1)(vii) of the Act

Tribunal ruling

The Tribunal decided the appeal in favour of the assessee and held that:

- There was no dispute about the fact that payment was made to UTI Network Inc. outside India for freight forwardingfunctions.
- The payment made to the freight forwarding agent as held by the CIT(A) was covered by Circular No. 715 (above), and, therefore, the payment could not be treated to be in respect of managerial services.
- The payment for the said services was not taxable in India under section 9(1)(vii) of the Act.
- The expenditure was in the nature of business expenses.

As the amount was not chargeable to tax under section 9(1)(vii) of the Act, it was therefore not subject towithholding tax provisions under section 195 of the Act. When the amount is not subject to withholding tax, the provisions of section 4 o(a)(i) of the Act are rendered inapplicable. In this respect, the Tribunal reiterated the principles as regards the obligation to withhold tax as laid down in the recent decisions of **CIT v. Eli Lilly Co. P. Ltd** [2009] 312 ITR 225 (SC), **Van Oord ACZ India P. Ltd. v. CIT** [2010] 323 ITR 130 (Delhi), and **ITO v. Prasad Production Ltd** [2010] 129 TTJ 641 (Chennai), which has further been approved by the Supreme Court in the caseof **GE India Technology Centre (P.) Ltd. v.CIT** [2010] 327 ITR 456 (SC).

Conclusion - It may be noted that, though the Tribunal held that the payments made were in the nature of business expenses, it has not examined whether or not there existed a business connection or permanent establishment of UTI Network Inc. in India. Nevertheless, this ruling should be helpful to Indian companies making freight forwarding payments outside India. Since the payment was held not chargeable to tax in India under section 9(1)(vii) of the Act, it was accordingly not subject to withholding tax under section 195 of the Act. Consequently, there was no question of disallowance of the amounts paid to non-resident freight forwarders as the provisions of section 4o(a)(i) of the Act were not applicable.