



## **Global Business Tax Alert** Sharp Insights

**The Ahmedabad Bench of ITAT in the case of <sup>1</sup>Saira Asia Interiors (P.) Ltd. has held that royalty income of a non-resident ('NR') is taxable on receipt basis under India-Italy tax treaty**

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## Background / Facts

- Saira Asia Interiors (P.) Ltd. ('the taxpayer') recorded certain liability in its books of accounts on November 22, 2010 towards technical know-how to one of its Italy-based group company.
- Payment was made to the overseas group company on May 12, 2011 after withholding tax @ 10% (plus applicable surcharge and cess). The tax so withheld was deposited with government's treasury on June 20, 2011.
- The Assessing Officer ('AO') was of the view that the taxpayer was liable to deduct tax at source ('TDS') at the time of credit of the technical know-how fee or at the time of actual payment, whichever is earlier. The credit being earlier, the taxpayer should have deducted TDS at the time of credit.
- Accordingly, a tax demand for failure to deduct and pay tax was levied on the taxpayer by the AO.
- Aggrieved by the order of the AO, the taxpayer filed an appeal before the first appellate authority [Commissioner of Income Tax (Appeals) (CIT) (A)], who decided in favour of the revenue.

## Taxpayer's key contentions

The taxability of royalty under the <sup>2</sup>India-Italy tax treaty would arise only at the time when the amount is actually paid/remitted and not at the time when credit was given to the recipient in the books of accounts.

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<sup>2</sup>Article 13 of the Double Taxation Avoidance Agreement between the Government of the Republic of India and the Government of the Republic of Italy

## Revenue's key contentions

- From a plain reading of Section 195 of the Income-tax Act, 1961 ('Act'), it is clear that the liability to deduct tax in the hands of the payee arises at the time of credit to the account of the payee or payment whichever is earlier.
- There is no provision in the Act which empowers the taxpayer to deduct tax at source in respect of the amount payable, in the year in which the same is taxable in the hands of the payee.

## Ruling of the Tribunal

### On timing of the taxable event

- Tax withholding liability under Section 195 is a vicarious liability. It's survival in the hands of the payer is wholly dependent on the existence of tax liability in the hands of the NR recipient.
- Reliance was placed on the Apex Court ruling in <sup>3</sup>'G E Technology Centre Pvt Ltd.' wherein it was held that the tax withholding obligation does not get triggered unless the income embedded in a payment is taxable under the Act.

- Under Article 13 of India-Italy tax treaty, taxability of royalty is dependent on the payment by the resident of a contracting state and receipt of the same by the resident of the other contracting state. Mere fact that an Indian resident credits the amount of royalty payable to an Italian resident, does not trigger taxability under Article 13.
- Reliance for the above proposition was placed on various decisions rendered by the coordinate benches including that rendered in the case of <sup>4</sup>'National Organic Chemical Industries Ltd.'.

### On applicable withholding tax rate

- Having considered taxability of royalty on paid basis under Article 13 of the India-Italy tax treaty, the Tribunal applied beneficial withholding tax rate of 10%, provided under the <sup>5</sup>Act, as against 20% as provided under Article 13.
- Tribunal held that though the taxpayer is covered by the India-Italy tax treaty, the provisions of the Act continue to apply to the extent more beneficial to the taxpayer.

<sup>3</sup> 'G E Technology Centre Pvt Ltd v. CIT' [2010] 327 ITR 456 (SC)

<sup>4</sup> 'National Organic Chemical Industries Ltd.vs. DCIT' [2005] 96 TTJ 765 (Mum)

<sup>5</sup> Section 115A of the Act

## Conclusion

This ruling considers the interplay of the machinery provisions of the Act relating to collection and deposit of TDS with the corresponding substantive provisions. The Tribunal's findings are based on the conjoint reading of the provisions.

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## Contacts

### Ahmedabad

19<sup>th</sup> Floor, Shapath - V  
SG Highway,  
Ahmedabad – 380 015.  
Tel: + 91 (079) 6682 7300  
Fax: + 91 (079) 6682 7400

### Coimbatore

Shanmugha Manram  
41, Race Course,  
Coimbatore  
Tamil Nadu - 641018  
Tel: + 91 (0422) 439 2801  
Fax: +91 (0422) 222 3615

### Kolkata

Bengal Intelligent Park Building  
Alpha, 1st floor, Block EP and GP  
Sector V, Salt Lake Electronics  
Complex,  
Kolkata - 700 091.  
Tel : + 91 (033) 6612 1000  
Fax : + 91 (033) 6612 1001

### Bangalore

Deloitte Centre, Anchorage II,  
100/2, Richmond Road,  
Bangalore 560 025.  
Tel: +91 (080) 6627 6000  
Fax: +91 (080) 6627 6010

### Delhi/Gurgaon

Building 10,  
Tower B, 7th Floor,  
DLF Cyber City,  
Gurgaon 122 002  
Tel : +91 (0124) 679 2000  
Fax : + 91 (0124) 679 2012

### Mumbai

Indiabulls Finance Centre,  
Tower 3, 28th Floor,  
Elphinstone Mill Compound,  
Senapati Bapat Marg, Elphinstone  
(W),  
Mumbai – 400013  
Tel: + 91 (022) 6185 4000  
Fax: + 91 (022) 6185 4101

### Chennai

No.52, Venkatanarayana Road,  
7th Floor, ASV N Ramana Tower,  
T-Nagar,  
Chennai 600 017.  
Tel: +91 (044) 6688 5000  
Fax: +91 (044) 6688 5050

### Hyderabad

1-8-384 and 385, 3rd Floor,  
Gowra Grand S.P.Road,  
Begumpet,  
Secunderabad – 500 003.  
Tel: +91 (040) 6603 2600  
Fax: +91 (040) 6603 2714

### Pune

106, B-Wing, 7<sup>th</sup> Floor,  
ICC Trade Tower,  
Senapati Bapat Road,  
Pune – 411 016.  
Tel: + 91 (020) 6624 4600  
Fax: +91 (020) 6624 4605



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