IN THE ITAT MUMBAI BENCH 'L'

CLSA Ltd.

v.

Income-tax Officer, (International Taxation)-2(1), Mumbai*

D.K. AGARWAL, JUDICIAL MEMBER
AND P.M. JAGTAP, ACCOUNTANT MEMBER
IT APPEAL NO. 2010 (MUM.) OF 2008
[ASSESSMENT YEAR 2004-05]
JANUARY 18, 2013

ORDER

P.M. Jagtap, Accountant Member - This appeal filed by the assessee is directed against the order of learned CIT (Appeals)-31, Mumbai dated 14-01-2008.

2. The issue raised in ground No. 1 of this appeal relates to the addition of Rs. 4,22,23,050/- made by the AO and confirmed by the learned CIT (Appeals) on account of the payment claimed to be received by the assessee towards recovery of overhead expenses from CLSA India Ltd. treating the same as in the nature of "Fees for technical services".

3. The assessee in the present case is a Company incorporated in Hongkong and belongs to the CLSA Group of companies. During the year under consideration, it had received an amount of Rs. 4,22,23,050/- from CLSA India Ltd. which was shown as the recovery of the share of that company in the indirect overhead expenses. The AO, however, found that CLSA India Ltd. had deducted tax at source from the said amount paid to the assessee. Keeping in view this fact as well as the provisions of section 9(1)(vii), he held that the amount in question received by the assessee company from CLSA India Ltd. was in the nature of fees for technical services which was chargeable to tax in the hands of the assessee.

4. The addition of Rs. 4,22,23,050/- made by the AO on account of the amount received from CLSA (India) Ltd. treating the same as fees for technical services was challenged by the assessee in an appeal filed before the learned CIT (Appeals). It was submitted before the learned CIT (Appeals) that the assessee company belongs to CLSA group of companies and as per the practice followed in the said group, a group company contributing to the generation of a particular revenue stream is required to share in such revenue from the other group companies in order to be able to cover its cost. It was submitted that CLSA (India) Ltd. (CLSAI in short), an Indian company, had entered into an indirect overhead expenses reimbursement agreement on 01-04-2003 with CLSA BV, the holding company. In pursuance of the said agreement, CLSA BV had directed different members of the group to perform different functions for the benefit of the group as a whole and CLSAI was required to contribute towards the overhead expenses incurred by the other group companies to perform the functions assigned to them. It was submitted that the sum of Rs. 4,22,23,050/- accordingly was paid by CLSAI to the assessee company as per the said agreement towards its share of expenses on the basis of invoice raised by the assessee. It was contended that the said contribution was thus paid towards reimbursement of various indirect overhead expenses incurred by the assessee company without any markup or service charges and the same being recovery of the overhead expenses actually incurred by the assessee company without any profit element, the same did not constitute income of the assessee company. In support of this contention, reliance was placed on behalf of the assessee on the decision of Hon'ble Supreme Court in the case of *P.H.*

Divecha v. *CIT* [1963] 48 ITR 222 as well as the decision of Hon'ble Calcutta High Court in the case of *CIT* v. *Dunlop Rubber Co. Ltd.* [1983] 142 ITR 493.

5. After considering the submissions made on behalf of the assessee on this issue as well as the material available on record, the learned CIT (Appeals) proceeded to examine the issue as to whether the payment made by the CLSAI to the assessee company was only reimbursement of cost and, therefore, not taxable in India as claimed by the assessee. In this regard, he noted that there was failure on the part of the assessee to prove that the money as was being collected in the name of reimbursement from the group company was actually spent. She also noted that the amount paid by CLSAI to the assessee company was claimed to be in the nature of contribution of its share towards expenses incurred by the assessee and as per the relevant agreement, such share was to be determined on some reasonable basis. The learned CIT (Appeals) held in this regard that the assessee could not produce before her any evidence of the so called reasonable basis for determining the share of contribution of CLSAI. She noted that even the global accounts of the CLSA group were not filed by the assessee and in absence of the same as well as the complete working furnished by the assessee to show that it had charged only the amounts actually spent by it for providing services, its claim for reimbursement of expenses actually incurred could not be accepted. She, therefore, rejected the stand of the assessee on this issue and after referring to the terms and conditions of the relevant agreement and relying on certain judicial pronouncements, she proceeded to hold that the payment from CLSAI was received by the assessee company for providing technical services and the amount so received being in the nature of fees for technical services was rightly brought to tax by the AO in the hands of the assessee.

6. We have heard the arguments of both the sides on this issue and also perused the relevant material on record. The learned counsel for the assessee has filed before us the additional evidence in the form of relevant financial statements and working to show that the amount in question was received by the assessee company from CLSAI on account of recovery of indirect overhead expenses actually incurred by it without there being any markup or element of profit. He has also moved an application seeking admission of the said additional evidence as per Rule 29 of the Appellate Tribunal Rules, 1962. As submitted in the said application, the assessee was of the bonafide belief that evidence and submissions made during the course of appellate proceedings before the learned CIT (Appeals) would suffice to justify that the amounts received by it was in the nature of reimbursement of expenses. It is submitted that the understanding of the assessee in this regard was substantiated by the fact that it had submitted additional evidence to learned CIT (Appeals) in respect of another ground involving the issue of reimbursement of direct expenses which was decided by the CIT (Appeals) in favour of the assessee after considering the said additional evidence. It is submitted that the assessee, therefore, had no reason to believe that the learned CIT (Appeals) would not agree with the fact that the indirect overhead expenses were in the nature of reimbursement. It is submitted that the learned CIT (Appeals) also did not specifically require the assessee to furnish the evidence like relevant vouchers, global accounts etc. to further establish that the amounts received by it were in the nature of reimbursement of expenses and this evidence was sought by the learned CIT (Appeals) only on 11th January, 2008 which was Friday and the impugned order was passed on Monday i.e. 14th January, 2008 before the assessee could file the same. It is submitted that the assessee thus was not given sufficient time to collect the required supporting evidence and present the same before the learned CIT (Appeals) for her consideration. It is also submitted that the additional evidence now being filed by the assessee is relevant to support and substantiate its claim that the amount in question received from CLSAI represents a mere reimbursement of cost actually incurred without involvement of any profit element and the same being crucial to the issue under consideration, it should be admitted.

7. The learned DR has raised a strong objection to the admission of additional evidence filed by the assessee. He has submitted that sufficient opportunity was given by the learned CIT (Appeals) to the assessee to establish that the amount in question was received towards reimbursement of expenses actually incurred but the assessee has failed to do so by adducing the relevant documentary evidence.

8. After considering the rival submissions on this preliminary issue and perusing the relevant material on record, we find that the additional evidence filed by the assessee is very much relevant for deciding the issue under consideration. As a matter of fact, the learned CIT (Appeals) has observed in her impugned order that the assessee could not support and substantiate its case that the amount in question received from CLSAI represents reimbursement of expenses actually incurred by producing the relevant supporting evidence and has also identified such documentary evidence which the assessee, according to her, could not produce. As submitted by the assessee in the application filed under Rule 29 of the Appellate Tribunal Rules, sufficient opportunity, however, was not given by the learned CIT (Appeals) to the assessee to produce the said evidence inasmuch as the same was called for on the date of last hearing which took place on Friday i.e. 11th January, 2008 and the order was passed immediately on Monday i.e. 14th January, 2008 leaving hardly any time to collect and file the said evidence. Having regard to all these facts of the case and keeping in view that the additional evidence filed by the assessee goes to the root of the matter and the same is very much relevant to decide the issue under consideration, we are of the view that the same is required to be admitted in the interest of justice. Accordingly, we admit the said additional evidence and remit the matter to the learned CIT (Appeals) in order to give an opportunity to the learned CIT (Appeals) to verify/examine the said additional evidence and decide the issue afresh on such verification/examination. Needless to observe that the learned CIT (Appeals) shall give sufficient opportunity of being heard to the assessee. Ground No. 1 of the assessee's appeal is accordingly treated as allowed for statistical purposes.

9. The issue involved in ground No.2 relates to the addition of Rs. 7,73,58,162/- made by the AO and confirmed by the learned CIT (Appeals) on account of referral fees received by the assessee from CLSAI treating the same to be in the nature of fees for technical services.

10. During the year under consideration, CLSAI had paid an amount of Rs. 7,73,58,162/- to the assessee-company as "Referral Fees". It was explained on behalf of the assessee company before the AO that it has business relationship with various financial institutions outside India which required services of a broker in relation to the investment activities carried out by such Institution in Indian capital market. It was submitted that the assessee referred such overseas institutional clients to CLSAI acting as India stock broker for which it received referral fees from CLSAI. It was contended that such fees received by the assessee from CLSAI was not in the nature of fees for technical services in terms of section 9(1)(vii) and the same, therefore, was not chargeable to tax in India. It was also submitted that the fees was in the nature of commission paid by Indian exporter to foreign agents and as per para 4 of CBDT Circular No. 23 dated 27th July, 1969, it was not taxable in India. The AO did not find merit in these contentions of the assessee. According to him, the amount in question received by the assessee from CLSAI as a referral fees was not in the nature of commission paid by the Indian exporter to a foreign agent and the same, therefore, was not covered by the CBDT Circular No. 23 dated 27th July, 1969. He held that the said amount was in the nature of fees for technical services received by the assessee and the same, therefore, was chargeable to tax in its hands in India.

11. The addition made by the AO on account of referral fees treating the same as fees for technical services was challenged by the assessee in an appeal filed before the learned CIT (Appeals). It was submitted before the learned CIT (Appeals) that CLSA group is a leading

equity brokerage house in the Asia Pacific Market serving about 1200 international clients mainly based in US and Europe. The assessee company belonging to the said group had established, developed and progressively expanded the group operations across the Asia Pacific markets and had contacts with persons outside India who were desirous of dealing in securities listed on NSE. It was submitted that the assessee company secured the business of institutional investors in respect of dealing in securities and referred the same to CLSAI, an Indian stockbroker for which total amount of Rs. 7,73,58,162/- was received by it from CLSAI as referral fees. It was contended that the services rendered by the assessee company to CLSAI thus were not in the nature of any managerial, technical or consultancy services and accordingly the referral fees received by it from CLSAI was not in the nature of fees for technical services as defined in section 9(1)(vii). It was contended that such referral fees received by the assessee from CLSAI was in the nature of income not arisen in India and the same, therefore, was not chargeable to tax in India. It was further contended that such referral fees received by the assessee was in the nature of commission paid by an Indian exporter to the foreign agent which was not taxable in India as per the CBDT Circular No. 23 dated 23rd July, 1969. Reliance was placed on behalf of the assessee on the decision of Hon'ble Supreme Court in the case of *CIT* v. *Toshoku Ltd.* [1980] 125 ITR 525 wherein it was held that the non-resident did not carry on any business operation in the taxable territories as they acted as selling agents outside India. It was held that the commission amount earned by the non-resident for services rendered outside India could not be deemed to be income which was either accrued upon or arisen in India so as to bring the same to tax in India.

12. The learned CIT (Appeals) considered this issue in the light of submissions made on behalf of the assessee as well as material available on record. She referred to the referral fees agreement between the assessee-company and CLSAI and noted the essential features thereof as under :

> "CLSA LTD has in the said agreement stated that it has contacts with a number of persons outside India who desire to purchase, sell or otherwise deal in securities listed or approved for trading on the NSE, and
>
> In the agreement it is also stated that CLSA Ltd. has referred, and may from time to time in the future refer to CLSI such persons outside India.
>
> Such persons referred by CLSA Ltd. to CLSI will require the transactions to be executed by CLSI and settled directly with its custodian.
>
> In consideration of CLSA HK referring these persons to CLSI, CLSI agrees to pay to CLSA Ltd., for each executed transaction in respect of the persons referred to CLSI, a referral fee @ 30% of the amount of commission received by it in respect of each such executed transaction."

After taking note of the essential features of the relevant referral fees agreement, the learned CIT (Appeals) proceeded to examine the issue relating to taxability of the referral fees received by the assessee in India in the light of the provisions of section 5(2) read with section 9(1) of the Indian Income-tax Act. According to her, the situs of the source of relevant income is relevant in this context and the same is required to be determined according to the general principles of law in the light of the peculiar facts of each case. She noted in this context that the referral fees as per the terms and conditions of the agreement was payable to the assessee only after the referred client has executed transactions through CLSAI and has made full and final payment of brokerage for the said transactions to CLSAI. According to the learned CIT (Appeals), the referral fees arose out of the payment of brokerage made by the clients to CLSAI in India and the source of the said income for the assessee thus was execution by the referred clients of transaction in India through CLSAI. She held that although the assessee had rendered services abroad and also pursued and solicited clients there, the right to receive commission/referral fees

arose in India only when the referred clients executed the transactions through CLSAI and made full and final payment to CLSAI in India. She held that the income from referral fees, therefore, was chargeable to tax in India in the hands of the assessee in view of the specific provisions contained in section 5(2)(b) read with section 9(1)(i) of the Act. In support of this conclusion, the learned CIT (Appeals) relied on the decision of Authority for Advance Ruling in the case of *Raju Malhotra* 284 ITR 564 wherein it was held that commission payable to non resident agent for soliciting foreign participant abroad for a trade exhibition to be held in India would be taxable under the Act in view of the specific provisions of section 5(2)(b) read with section 9(1)(i) as the right to receive the commission under the terms of the agency agreement would arise in India only when the exhibitors would participate in the show and make full and final payment to the organizer and the source of income of the agent is the participation of the exhibitors in the exhibition in India.

13. The learned CIT (Appeals) then proceeded to consider the issue as to whether the amount received by the assessee as referral fees from CLSAI constituted fees for technical services u/s 9(1)(vii) of the Act. She noted that as per sub-clause (b) of clause (vii) where FTS is paid by a person who is a resident in India, the income shall be deemed to accrue or arisen in India. She then referred to the definition of FTS given in Explanation 2 to section 9(1)(vii) according to which FTS means any consideration including any lump sum consideration for rendering of any managerial, technical or consultancy services. According to the learned CIT (Appeals), the services provided by the assessee in the form of referring clients to CLSAI would amount to rendering market and sales promotion services which are covered in the bracket of managerial and consultancy services and the same, therefore, would fall in the definition of FTS. She held that the amount received by the assessee from CLSAI under the referral agreement thus was chargeable to tax in India as fees for technical services. In support of this conclusion, the learned CIT (Appeals) relied on the decision of Authority for Advance Ruling in the case of *International Hotel Licensing Co.,* In re [2007]288 ITR 534/158 Taxman 231 (AAR - New Delhi) wherein it was held that amount received by non resident applicant from Indian Hotel in connection with marketing and business promotion activity conducted outside India cannot be treated as mere reimbursement of cost and expenses and there being real and intimate relation between the business activities carried on by the applicant outside India and the activities of the hotel owner in India, a business connection exists within the meaning of section 9(1)(i) and the amount received by the applicant from Indian Hotel would be taxable in India being in the nature of fees for technical services as defined in section 9(1)(vii). She also relied on the decision of the Tribunal in the case of *Raymond Ltd.* v. *Dy. CIT* [2003] 86 ITD 791 (Mum.) wherein it was held that services rendered by the managers are managerial or consultancy services within the meaning of section 9(1)(vii) read with Explanation 2 and, therefore, the management commission and the selling commission are income by way of fees for technical services deemed to accrue or arise in India. The learned CIT (Appeals) held that referral fees paid by CLSAI to the assessee in the present case was for services utilized for the purpose of business carried on in India and irrespective of the place where the said services were rendered, the amount of referral fees should be deemed to accrue or arisen in India. For this purpose, she relied on clause (b) of section 9(1)(vii) where the expression used is "fees for services utilized in India". She again referred to the decision of the Tribunal in the case of *Raymond Ltd.* (*supra*) wherein it was held that even if the services are rendered outside India, it is irrelevant for the purposes of section 9(1)(vii) and what is relevant is the place where the services are utilized. It was held that the thrust of the provision is the "source rule" i.e. the source of payment. She also relied on the decision of the Tribunal in the case of *Ranbaxy Laboratories Ltd.* v. *Dy. CIT* [2004] 91 TTJ (Delhi) 831 wherein the payment made by the person carrying on the business of managing drugs in India for services of non-resident availed of for seeking approval for

marketing drugs from regularity authorities of USA and UK was held to be for technical and consultancy services assessable in India being income deemed to accrue or arise in India.

14. The learned CIT (Appeals) held that the decision of Hon'ble Supreme Court in the case of *Toshoku Ltd.* (*supra*) cited on behalf of the assessee was distinguishable on facts since it was a case where the Japanese company did not carry on any activity whatsoever in India and all its activity was outside the Indian territories having no extension in India. She held that the assessee in the present case, on the other hand, was passing on its business to the Indian counter part and collecting referral fees only after the business transaction is matured and executed. She also noted that in the case of *Toshoku Ltd.* (*supra*), the Japanese party was the agent of the assessee whereas the assessee in the present case by its own admission in the referral agreement was not an agent of CLSAI. She held that the assessee, therefore, was not even entitled for the benefit of Board Circulars relied upon by it as the same were applicable only in case of foreign agents of Indian exporters. The learned CIT (Appeals) thus held that the referral fees received by the assessee from CLSAI was in the nature of fees for technical services and the same being income of the assessee arisen in India was rightly brought to tax in India in its hands. She, therefore, confirmed the addition made by the AO on this issue.

15. The learned counsel for the assessee at the outset, invited our attention to the note on referral fees submitted to the AO, a copy of which is placed at page No.18 of his paper book. He submitted that as explained in the said note, the assessee-company was engaged in securing the business of institutional investors in respect of transactions of buying and selling securities and referring the same to CLSA India, an Indian Stockbroker. He submitted that the assessee had business relationship with various financial institutions outside India which required services of a broker in relation to investment activities carried out by such institution in Indian capital market. He submitted that the assessee referred the orders of such overseas institutional clients to CLSAI being Indian stockbroker and received an amount of Rs. 7,73,58,162/- as a referral fees from CLSAI. Relying on this note submitted before the AO explaining the nature of referral fees as well as the contents of referral agreement placed at page No. 19 to 21 of his paper book, the learned counsel for the assessee contended that the services rendered by the assessee to CLSAI for which the referral fees was received by it cannot be said to be in the nature of managerial, technical or consultancy services so as to bring the same within the definition of fees for technical services given in section 9(1)(vii) read with Explanation 2 thereto. He contended that the said amount, on the other hand, was received by the assessee for services rendered outside India and the same being not income accruing or arising, whether directly or indirectly, through or from any business connection in India as contemplated in section 9(1)(i), the same does not constitute income deemed to accrue or arisen in India so as to be taxable in India in the hands of the assessee company. In support of this contention, he relied on the decision of Hon'ble Bombay High Court in the case of *Ceat International S.A.* v. *CIT* [1999] 237 ITR 859/103 Taxman 153 and that of Hon'ble Delhi High Court in the case of *CIT* v. *Eon Technology (P.) Ltd.* [2011] 343 ITR 366/203 Taxman 266/15 taxmann.com 391 (Delhi). He also relied on the decision of Hon'ble Supreme Court in the case of *Carborandun Co.* v. *CIT* [1977] 108 ITR 335 in support of the assessee's case on this issue. As regards the decision of Authority for Advance Ruling in the case of *Ravi Malhotra,* In re [2006] 284 ITR 564/155 Taxman 101 (AAR - New Delhi) relied upon by the learned CIT (Appeals) in his impugned order, he submitted that the same is contrary to the decision of Hon'ble Supreme Court in the case of *Carborandun Co.* (*supra*) as well as to the relevant provisions of the Act and the same, therefore, cannot be relied upon to decide the issues against the assessee.

16. The learned DR, on the other hand, strongly relied on the impugned order of the learned CIT (Appeals) on this issue submitting that elaborate reasons have been given by the learned CIT (Appeals) while confirming the addition made by the AO on this issue. He submitted that the amount in question on account of referral fees was received by the assessee for providing

market services as rightly pointed out by the learned CIT (Appeals) in his impugned order. He submitted that without any expertise and knowledge in the field, nobody would consult or take advise as has been done in the present case. He contended that whether the services are rendered in India or outside India has become irrelevant after the amendment made in the relevant provisions and what is relevant in the context of fees for technical services is where the relevant services are utilized. He submitted that in the cases relied upon by the learned counsel for the assessee in support of the assessee's case, double tax avoidance treaties were involved whereas in the present case there is no such treaty. As regards the decision of Hon'ble Delhi High Court in the case of *Eon Technology (P.) Ltd.* (*supra*) relied upon by the learned counsel for the assessee, he contended that it was a case of commission paid on export and not the case for fees for technical services and the same, therefore, is not applicable in the present case. He contended that the latter decision of Hon'ble Delhi High Court in the case of Haveli Industries Ltd.(copy filed), on the other hand, is directly applicable to the facts of the present case as the services in that case were rendered and utilized by the Indian Company in India. He also relied on the decision of ITAT Special Bench, Mumbai in the case of *Mahindra & Mahindra Ltd.* v. *Dy. CIT* [2009] 30 SOT 374 to contend that advisory services are clearly covered in consulting services as contemplated in Explanation 2 to section 9(1)(vii).

17. In the rejoinder, the learned counsel for the assessee submitted that in case of fees for technical services covered u/s 9(1)(vii), place of accrual of income is not relevant as rightly contended by the learned DR. He submitted that the stand of the assessee in the present case, however, is that the amount in question received on account of referral fees is not in the nature of fees for technical services and the same not being income accruing or arising either directly or indirectly through or from any business connection in India as contemplated in section 9(1)(i), the same is not taxable in India not being the income deemed to accrue or arisen in India. He submitted that in the case of *Haveli Industries Ltd.* (*supra*) relied upon by the learned DR, the amount in question was admittedly paid for fees for technical services and the only issue was whether the source of that income was in India or outside India. He contended that the case of the assessee in this context is that the amount of referral fees received by it is not in the nature of fees for technical services.

18. The learned counsel for the assessee further submitted when the matter was refixed for clarification before us that the concept of source of income has been explained by the Hon'ble Supreme Court in the case of *Performing Right Society Ltd.* v. *CIT* [1977] 106 ITR 11 at page 22 and 23 of the report. He contended that the decision of the Authority for Advancing Ruling in the case of *Rajiv Malhotra* (*supra*) relied upon by the Revenue in this regard is wrong as Explanation 1(a) to section 9(1)(i) has not been considered while rendering the said decision which clearly envisages that some portion should be carried on in India to say that the corresponding income accrues or arises in India. He submitted that this aspect has been considered by the Mumbai Bench of the Tribunal in the case of *Addl. DIT(IT)* v. *Star Cruise India Travel Services (P). Ltd.* [2011] 46 SOT 173/12 taxmann.com 242 wherein the Tribunal has declined to follow the decision of Authority for Advance Ruling in the case of *Rajiv Malhotra* (*supra*). He contended that what is relevant in this context to decide the source of income is where the services are actually rendered. In this regard, he relied on the decision of Hon'ble Allahabad High Court in the case of *Lakshmipati Singhania* v. *CIT* [1969] 72 ITR 512 at page 519 and 520. He also contended that what is to be seen to ascertain the exact nature of services so as to decide whether they fall u/s 9(1)(i) or 9(1)(vii) is what are the services rendered by the non-resident company qua CLSAI. In this regard, he relied on the decision of the ITAT, Jaipur Bench in the case of *Asstt. CIT* v. *Modern Insulator Ltd.* [2012] 20 taxmann.com 335.

19. In reply to the arguments raised by the learned counsel for the assessee at the time of clarification, the learned DR submitted that the amount in question on account of referral fees

was paid by CLSAI to the non resident company for referring the clients. He submitted that this reference was made by CLSAI while advising their clients to go to CLSAI using their experience and expertise in the field. He submitted that the transactions were to be executed ultimately by CLSAI in India which gave rise to the payment of referral fees. He contended that the source of income of the referral fees thus was in India and the payment of such fees to the extent of 30% of the commission received was made by CLSAI not just for referring the clients but mainly because of the expertise of CLSA as a result of which the clients had approached it for making a reference. He contended that the income on account of referral fees thus accrued to CLSA only when the corresponding transactions were completed in India and the source of referral fees being in India, the income on account of the said fees had accrued and arisen in India as held by the Authority for Advancing Ruling in the case of *Rajiv Malhotra* (*supra*) as well as by the Hon'ble Delhi High court in the case of *CIT* v. *Havells India Ltd.* [2012] 208 Taxman 114/21 taxmann.com 476 (Delhi) (*supra*). As regards the various judicial pronouncements cited by the learned counsel for the assessee, he submitted that the facts involved therein are entirely different from the facts involved in the present case inasmuch as element of consultancy services is very much involved in the services rendered by CLSA on the basis of its experience and expertise in the field. He submitted that there being no treaty between India and Hongkong, the matter involved in the present case has to be decided with reference to the relevant provisions of domestic law and not on the basis of treaty as done in the various judicial pronouncements cited by the learned counsel for the assessee.

20. We have considered the rival submissions and also perused the relevant material on record. We have also gone through the various judicial pronouncements cited by the learned representatives of both the sides in support of their respective stand. The issue that is involved in this case for our consideration is whether the referral fees received by the assessee who is a non-resident in India from CLSAI is chargeable to tax in India. In this regard, the learned CIT (Appeals) has relied on the provisions of section 5(2) read with section 9(1) of the Act to hold that the source of the referral fees being the execution of transactions in India through CLSAI on behalf of the referred clients, the right to receive the referral fees arose in India only and the income on account of the referral fees thus was chargeable to tax in India in the hands of the assessee as per the specific provisions contained in section 5(2)(b) read with section 9(1)(i) of the Act being the income deemed to accrue or arise in India. In support of this conclusion, the learned CIT (Appeals) has relied on the decision of Authority for Advance Ruling in the case of *Rajiv Malhotra* (*supra*). As per section 4 of the Act, the basis of Income-tax is the total income of the assessee of the previous year and section 5(2) defines the scope of such total income in case of a person who is a non-resident to include all income from whatever source derived which is received or is deemed to be received in India by or on behalf of such person or accrues or arises or is deemed to accrue or arise to him in India during the relevant previous year. By virtue of clause (i) of section 9(1), all income accruing or arising whether directly or indirectly through or from any business connection in India or source of income in India, inter alia, are treated as income which is deemed to accrue or arise in India. The learned CIT (Appeals) has relied on the provisions of section 5(2) and section 9(1)(i) as also the decision of the Authority for Advance Ruling in the case of *Rajiv Malhotra* (*supra*) to hold that the right to receive the referral fees having arisen to the assessee in India, the income on account of such referral fees was deemed to accrue or arise in India and the same was thus taxable in India in the hands of the assessee-company.

21. In the case of *Star Cruise India Travel Services (P.) Ltd.* (*supra*) cited by the learned counsel for the assessee, a similar issue arose for the consideration of coordinate bench of this Tribunal relating to taxability of cruise package money received by the non-resident assessee from India through Star India. The stand taken by the Revenue in this regard was that the non-resident was having a business connection in India and the same was sufficient to invoke the

tax liability of a non-resident in India in view of the provisions of section 9(1)(i) read with section 5(2). In support of this stand, reliance was placed by the Revenue on the decision of Authority for Advance Ruling in the case of *Rajiv Malhotra* (*supra*). The Tribunal, however, did not find merit in the stand taken by the Revenue and declined to rely on the decision of Authority for Advance Ruling in the case of *Rajiv Malhotra* (*supra*) on the ground that the impact of Explanation 1(a) to section 9(1)(i) of the Act was not considered by the Authority for Advance Ruling. The relevant observations as recorded by the Tribunal in paragraph No. 20 of its order are reproduced below :

> "However, the observations so made by Prof. Land, and the ruling rendered Authority for Advance Ruling in the case of *Rajiv Malhotra* (284 ITR 564), did not have the benefit of examining the impact of Explanation 1(a) to section 9(1)(i) of the Act. As a matter of fact, in *Rajiv Malhotra,* In re [2006] 155 Taxman 101 (AAR - New Delhi), the Authority for Advance Ruling does observe that "the facts that the agent renders services abroad in the form of pursuing and soliciting the participants and that the commission is remitted to him abroad are wholly irrelevant for the purpose of determining the situs of his income" but then this observation overlooks the fact that in terms of Explanation 1(a) to section 9(1)(i), "in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India" but then since no part of the operations was carried out in India, no part of assessee's income could have been thus taxable in India. It would thus seem to us that when no business operations are carried out in India, even if a non-resident has a business connection in India, no part of income of such business can be deemed to have accrued or arisen in India. The views expressed by the learned Authority for Advance Ruling, which do not fetter our independent opinion anyway in view of its limited binding force under section 245S of the Act, do not impress us, and we decline to be guided by the same. Revenue thus derives no support from these observations either. In view of these discussions, and bearing in mind entirely of the case, we uphold the relief granted by the learned Commissioner (Appeals) and decline to interfere in the matter. This conclusion is also in harmony with the conclusions arrived at by a Coordinate Bench in assessee's own case for the assessment years 2002-03 to 2005-06, reported in *Dy. DIT* v. *Star Cruises India Travel Services (P.) Ltd.* [2010] 39 SOT 18 (Mum.) and *vice versa*."

22. The similar issue came up for consideration before the Hon'ble Delhi High court in the case of *Eon Technology (P.) Ltd.* (*supra*) wherein the assessee company in India which was engaged in the business of development and export of software had paid commission to its holding company in U.K., namely, ETUK on sales and amounts realized on export contracts procured by ETUK for the assessee. The issue involved for the consideration of Hon'ble Delhi High Court was that whether the commission income earned by ETUK was taxable in India being income accrued or deemed to accrue in India and whether the assessee was liable to deduct tax at source therefrom failing which disallowance u/s 40(a)(ia) was warranted. In this context, it was held by the Hon'ble Delhi High Court that since ETUK was not rendering any service or performing any activity in India itself, commission income could not be said to have accrued, arisen to or received by ETUK in India merely because it was recorded in the books of the assessee in India or was paid by the assessee situated in India. Reliance was placed by the Hon'ble Delhi High Court in this regard on the decision of Hon'ble Supreme Court in the case of *Toshoku Ltd.* (*supra*) wherein the term "business connection" was interpreted by the Hon'ble Supreme Court to mean something more than mere business and is not equivalent to carrying on business, but a relationship between the business carried on by non-resident, which yields profits and gains and some activity in India, which contributes directly or indirectly to the earning

of those profits or gains. It was held that the business connection must be real and intimate from which the income had arisen directly or indirectly.

23. The learned CIT (Appeals) in her impugned order has also treated the referral fees received by the assessee from CLSAI as fees or technical services u/s 9(1)(vii) of the Act. In this regard, she has relied on the definition of the term "fees for technical services" given in Explanation 2 to section 9(1)(vii) according to which FTS means any consideration including any lumpsum consideration for the rendering of any managerial, technical or consultancy services. She has also held that the services provided by the assessee in the form of referring clients to CLSAI amount to marketing and self promotion services which are in the nature of managerial and consultancy services. In support of this conclusion, she had relied on the decision of Hon'ble Authority for Advancing Ruling in the case of *International Hotel Licensing Co.* (*supra*). While supporting this conclusion of the learned CIT (Appeals), the learned CIT-DR at the time of hearing before us, has relied on the decision of Hon'ble Delhi High Court in the case of *Havells India Ltd.* (*supra*). On a careful perusal of both these judicial pronouncements relied upon by the Revenue, we find that the same are distinguishable on facts and the reliance of the Revenue thereon is clearly misplaced.

24. In the case of *Havells India Ltd.* (*supra*), the issue before the Hon'ble Delhi High Court in the context of disallowance u/s 40(a)(ia) of the Act was whether the testing fee paid to the US Company was chargeable to tax in India. The US Company had specialized knowledge and facilities for carrying out the type of testing and the necessary certification, which was required by the assessee. According to the AO, the testing report and certification given by the US Company represented technical services which made available technical knowledge, experience and skill to the assessee because they were utilized in the manufacture and sale of the products in the business of the assessee carried on in India. The stand of the assessee was that the testing and certification were necessary for the export of its products and thus the relevant services provided by the US Company were actually utilized for such export and were not utilized for the business activities of production in India. The assessee thus made an attempt to cover its case in the exception provided in clause (b) of section 9(1)(vii) which deals with the fees payable by resident in respect of services utilized in a business or profession carried on by such resident outside India or for the purposes of making or earning any income from any source outside India. This stand of the assessee was not accepted by the Hon'ble Delhi High Court holding that the export activity having taken place or having been fulfilled in India, the source of income was located in India and not outside India. The issue involved before the Hon'ble Delhi High Court in the case of *Havells India Ltd.* (*supra*) as well as the material facts relevant thereto thus were entirely different from that of the present case. In the case of *International Hotel Licensing Co.* (*supra*) decided by the Authority for Advancing Ruling and relied upon by the learned CIT (Appeals) in her impugned order, the applicant was a non-resident company. It was a subsidiary of Luxembourg entity engaged in the business of promoting enterprises by conducting international advertising/marketing and sales programs for Marriot chains of hotel to promote them in the foreign markets. While Marriot entered into various agreements with an Indian Company (owner) for setting up its hotel projects in India, the applicant also entered into an agreement with the owner called International Marketing Program Participation Agreement (IMPPA).The IMPPA provided that the owner would participate in the marketing business promotion programmes and the applicant would provide, inter alia, space in magazines, newspaper and other printed/electronic media outside India. The consideration that the owner would pay to the applicant was described as an annual contribution equal to 1.5% of the gross revenues of the hotel by way of reimbursement of expenses that the applicant would incur for conducting and coordinating the international marketing activities for Marriot chains of hotel. Pursuant to the IMPPA, the applicant was also to provide certain special programmes to all hotels in the Marriot chains known as Marriot's winning guest loyalty program for which the

participant would charge 3.5% of Marriot Reward Program members, room charges. The applicant filed the application seeking advance ruling of the authority on the question as to whether the amounts of contribution of 1.5% and 3.5% received by it from the Indian hotel owner in connection with the marketing and business promotion activities conducted outside India would be taxable in India. In this regard, it was held by the Authority for Advancing Ruling that the terms of the IMPPA and the relevant facts of the case were sufficient to show that the real and intimate relationship did exist between the business activities carried on by the applicant outside India and the activities of the owner in India, namely, running of hotel business and paying the contribution to the applicant. It was held that there was a direct nexus between the business of the applicant outside India and the activities of the owner in India and the existence of business connection was clearly established attracting the provisions of section 9(1)(i) to the amounts in question. It was also noted by the Authority for Advance Ruling that advertising on TV in foreign channels was very much accessable in India and such advertisement having the effect in India, payment by the owner for the purposes of service of advertisement had the relation to the activities of the applicant which generated activities of the owner of the hotel business. The Authority for Advance Ruling held that the applicant thus had a source of income in India. It was also held by the Authority that the services provided by the applicant both within and outside India in the form of advertising, marketing promotion, sales program and special services and other programs for which payments were made by the owner, would amount to rendering managerial and consultancy services and the requirements of the definition of FTS as given in Explanation 2 to section 9(1)(vii) were duly satisfied. Accordingly it was ruled that the amounts received by the applicant from the Indian hotel owner in connection with the marketing and business promotion activities said to be conducted outside India would be taxable in India. In our opinion, the facts involved in the present case are entirely different from the facts involved in the case of *International Hotel Licensing Company* (*supra*) inasmuch as the amount in question was paid to the assessee by CLSAI on account of referral fees for referring the international clients and going by the nature of services rendered by the assessee qua CLSAI, it cannot be said that the real and intimate relation exists between the activities carried on by the assessee outside India and the activities of CLSAI in India. Moreover, going by the nature of services rendered by way of referring the international clients to CLSAI, the assessee cannot be said to have rendered any technical, managerial or consultancy services as envisaged in Explanation 2 to section 9(1)(vii) as held by the Authority for Advance Ruling in the case of *Cushman and Wakefield (S) Pte Ltd.,* In re [2008] 305 ITR 208/172 Taxman 179 (AAR - New Delhi) cited by the learned counsel for the assessee wherein a similar issue was involved.

25. In the case of *Cushman and Wakefield (S) Pte. Ltd.* (*supra*), the applicant was a foreign company incorporated in Singapore. It was engaged in the business of rendering services in connection with acquisition, sales and dealings in real estate and other services such as, advisory and research facilities management, project management etc. in the field of real estate. It had developed certain international clients' relationship and under the agreement entered into in Singapore with CWI, a subsidiary company in India, the applicant was to refer potential customer desirous of obtaining real estate consultancy and associated services in India to CWI. The Indian company was liable to pay to the applicant the percentage of the amount charged by it to the referred clients after it had realized in full the amount from the customers. On these facts which are similar to the facts of the present case, application was filed seeking advance ruling from the authority on whether the referral fees received by the applicant from CWI could be characterized as business income or income by way of fees for technical services and whether any tax was liable to be deducted by CWI from the payment of referral fees to the applicant. The Authority ruled that no activity except that by making a referral fees from Singapore to the Indian company had been done in India and, therefore, the referral fees remitted by CWI to the applicant was neither received nor deemed to be received by the

applicant in India. It was also held that there did not exist any real and intimate relation between the activities carried on outside India by the applicant and the activities in India that contributed to the earning of income. The authority ruled that it was the prerogative of the customers to decide whether it wanted to avail of the services of CWI or not and even CWI was not bound to enter into a deal with the referred customer. It was held that there was thus no business income in India of the applicant u/s 9(1)(i) of the Income-tax Act, 1961 nor even the deemed income as per Explanation 2 to section 9(1)(i). It was further ruled that there was no expertise or knowhow which was made available to CWI by the applicant by reason of rendering service of managerial, technical or consultancy nature and in the absence of any sort of durability or permanency of result of rendering of services, the referral fees paid by the Indian company was not fees for technical services u/s 9(1)(vii). Since the issue involved in the present case as well as all the material facts relevant thereto are similar to that of the case of *Cushman and Wakefield (S) Pet. Ltd.* (*supra*) and we agree with and endorse the views expressed by the Authority for Advance Ruling as well as the reasons given in support while deciding the said issue, we hold that the referral fees received by the assessee is not taxable in India. Accordingly, the addition made by the AO and confirmed by the learned CIT (Appeals) on this issue is deleted and ground No. 2 of the assessee's appeal is allowed.

26. In the result, the appeal of the assessee is allowed as indicated above.