No TDS on payment for purchase of goods / services through credit card transactions

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Recently, an opinion was sought from me by a client regarding TDS implications under Chapter XVII-B of the Income-Tax Act, 1961 (the Act), in respect of merchant service fees payable in the course of settlement of credit card transactions for the purchase of goods / services.

In the aforesaid transactions, the functions of the relevant entities may be briefly discussed as follows :

(i) The '*Issuing Bank'*, issues credit card to the customer, makes payment to other entities on behalf of the customer and recovers the same from the customer.

(ii) The '*Acquiring Bank'* pays the amount of purchase price of goods / services, purchased by the customer, to the Merchant Establishment, selling such goods / services, after deducting therefrom the agreed discount / commission.

(iii) The '*Credit Card Association'*, viz. VISA International, Master Card International, M/s.American Express, etc, authorizes banks to issue credit card bearing their logos to various persons. They operate a global settlement and payment system for the credit cards issued by the member banks of the Credit Card Association.

(iv) '*Merchant Establishment'* undertakes the sale of goods / services to the credit card holder or the customer and receives payment for the price of the goods / services through the aforesaid route of payment.

As regards the payment for the goods / services to be purchased by the credit card holder, the system followed is described hereinafter :

Through Visa platform or Credit Card Association, net settlement is made by the Issuing Bank to the Acquiring Bank, i.e., the Issuing Bank will make requisite payment to the Acquiring Bank, after deducting its merchant service fees. The daily settlement is done by the Credit Card Association, which makes payment to the Acquiring Bank, after deducting its merchant service fees. The Acquiring Bank makes payment to the Merchant Establishment, in respect of the price of goods / services purchased by the customer, after deducting its merchant service fees.

It may, thus, be seen that in the aforesaid process, merchant service fees is received by the Issuing Bank, the Credit Card Association and the Acquiring Bank. As regards the Merchant Establishment, it is merely provided with the facility to receive the disbursement of the net transactions, after deduction of the aforesaid merchant service fees.

From the aforesaid procedure of payment, it may be seen that the price paid in respect of the goods / services purchased by the customer is recovered by the Issuing Bank from the customer or the credit

card holder. The Issuing Bank makes payment to the Credit Card Association, which makes payment to the Acquiring Bank and which, in turn, makes payment to the Merchant Establishment. **Thus, effectively, the person making the payment for the aforesaid goods / services is the customer and as regards the Issuing Bank, Credit Card Association and the Acquiring Bank, they only render the requisite services, in respect of the payment to the Merchant Establishment for the price of the goods / services purchased by the customer.**

It is, thus, quite clear that the Merchant Establishment only receives payment through the aforesaid route and it does not make any payment to any of the aforesaid entities.

In this connection, the transaction regarding the payment of price of goods / services, requires to be properly understood. From the aforesaid facts, it is quite clear that the Merchant Establishment is selling its goods / services at a slightly lower price, with a view to increasing the volume of sale of such goods / services. As far as the customer is concerned, he is purchasing the goods / services, in question, at the aforesaid lower price only. It may also be understood that the aforesaid reduction in price is shared amongst the aforesaid three entities, viz. the Issuing Bank, the Credit Card Association and the Acquiring Bank, by way of merchant service fees. It must, therefore, be clearly understood that the Merchant Establishment is not making payment for the aforesaid merchant service fees. On the other hand, the Merchant Establishment is the recipient of the purchase price of the goods / services, through the aforesaid route of payment, on behalf of the customer.

Before we proceed to deal with the issue under consideration, it will be appropriate to understand the basic provisions of Chapter XVII-B of the Act. The deduction of tax at source is a convenient method of tax collection, since it effects early realization and is less painful to the person from whose income such tax is deducted. It must be clearly understood here that tax deductible at source (TDS), is deducted from the payment being made to a person by a '*Person responsible for paying'* the said amount. As regards the Government, it saves time on the part of the Income-tax staff in as much as all calculation and other attendant work are performed by the '*Person responsible for paying'*.

In the present context, the expression '*person responsible for paying'*, is very relevant, regarding the provisions of TDS under Chapter XVII-B of the Act. The aforesaid expression is defined under section 204 of the Act. For the sake of ready reference, section 204 of the Act, is reproduced as follows :

Meaning of "person responsible for paying".

204. *For the purposes of the foregoing provisions of this Chapter and section 285, the expression "person responsible for paying" means—*

(i) in the case of payments of income chargeable under the head "Salaries", other than payments by the Central Government or the Government of a State, the employer himself or, if the employer is a company, the company itself, including the principal officer thereof;

(ii) in the case of payments of income chargeable under the head "Interest on securities", other than payments made by or on behalf of the Central Government or the Government of a State, the local authority, corporation or company, including the principal officer thereof;

(iia) in the case of any sum payable to a non-resident Indian, being any sum representing consideration for the transfer by him of any foreign exchange asset, which is not a short-term capital asset, the authorised dealer responsible for remitting such sum to the non-resident Indian or for crediting such sum to his Non-resident (External) Account maintained in accordance with the Foreign Exchange Regulation Act, 1973 (46 of 1973), and any rules made thereunder;

(iii) in the case of credit, or, as the case may be, payment] of any other sum chargeable under the provisions of this Act, the payer himself, or, if the payer is a company, the company itself including the principal officer thereof.

Explanation.—For the purposes of this section,—

(a) "non-resident Indian" and "foreign exchange asset" shall have the meanings assigned to them in Chapter XII-A;

(b) "authorised dealer" shall have the meaning assigned to it in clause (b) of section 2 of the Foreign Exchange Regulation Act, 1973 (46 of 1973).

From the aforesaid definition of the expression '*person responsible for paying'* under the provisions of section 204, it may be seen that for non-government employees, etc, he is the employer in cases of salary income, the borrower in cases of interest income or **payer in cases of other income**. There is, however, one exception, namely, in cases of companies, etc, the aforesaid expression includes the company, etc, itself as well as its principal officer. The law casts an obligation on the '*person responsible for paying'* to deduct tax at source from the relevant amounts / incomes and to pay it to the credit of the Central Government and do other things, in the prescribed manner. **In other words, it must be understood that the tax is to be deducted at source by the person responsible for paying the amount or income to the recipient thereof. It is, thus, quite clear that it is the payer of amount / income to the recipient thereof, who is under the obligation to deduct tax at source there from.**

In the present case, the Merchant Establishment is the recipient of income and therefore, the Merchant Establishment will not be under any obligation to deduct tax at source in respect of the aforesaid service fees.

Further, as regards the Issuing Bank, that itself, receives the payment from the customer and also takes its part of MSF from the aforesaid payment. Besides, as regard the Credit Card Association and the Acquiring Bank, they are a part of the chain in the payment of the sale price of the goods to the Merchant Establishment and therefore, they cannot be treated as persons responsible for making the payment. **In view of the aforesaid reasons, no one out of the aforesaid three entities can be held as responsible for paying the aforesaid sale price of the goods or the merchant service fees and accordingly, there will be no obligation of TDS, in respect of the aforesaid payment on any of the aforesaid three entities.**

We may now examine the relevant provisions of Chapter XVII-B of the Act, as regards the nature of the aforesaid merchant service fees. On closely examining the various sections under Chapter XVII-B of the Act, the only sections which may probably apply to the payment of the aforesaid merchant service fees, could be sections 194C, 194H or 194J. Section 194C deals with TDS from payments to contractors; section 194H deals with TDS from payment of commission or brokerage; whereas section 194J deals with TDS from fees for professional or technical services.

In order to ascertain whether the aforesaid merchant service fees may fall within the purview of the aforesaid sections, viz. sections 194C, 194H or 194J, the said sections are examined one after the other, as follows :

I. Section 194C – Payment to contractors

For the sake of ready reference, section 194C of the Act is reproduced as follows :

Payments to contractors.

194C.*(1) Any person responsible for paying any sum to any resident (hereafter in this section referred to as the contractor for carrying out any work (including supply of labour for carrying out any work) in pursuance of a contract between the contractor and a specified person shall, at the time of credit of such sum to the account of the contractor or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to—*

(i) one per cent where the payment is being made or credit is being given to an individual or a Hindu undivided family;

(ii) two per cent where the payment is being made or credit is being given to a person other than an individual or a Hindu undivided family,

of such sum as income-tax on income comprised therein.

(2) Where any sum referred to in sub-section (1) is credited to any account, whether called "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly.

(3) Where any sum is paid or credited for carrying out any work mentioned in sub-clause (e) of clause (iv) of the Explanation, tax shall be deducted at source—

(i) on the invoice value excluding the value of material, if such value is mentioned separately in the invoice; or

(ii) on the whole of the invoice value, if the value of material is not mentioned separately in the invoice.

(4) No individual or Hindu undivided family shall be liable to deduct income-tax on the sum credited or paid to the account of the contractor where such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.

(5) No deduction shall be made from the amount of any sum credited or paid or likely to be credited or paid to the account of, or to, the contractor, if such sum does not exceed thirty thousand rupees :

***Provided** that where the aggregate of the amounts of such sums credited or paid or likely to be credited or paid during the financial year exceeds seventy-five thousand rupees, the person responsible for paying such sums referred to in sub-section (1) shall be liable to deduct income-tax under this section.*

(6) No deduction shall be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor during the course of business of plying, hiring or leasing goods carriages, on furnishing of his Permanent Account Number, to the person paying or crediting such sum.

(7) The person responsible for paying or crediting any sum to the person referred to in sub-section (6) shall furnish, to the prescribed income-tax authority or the person authorised by it, such particulars, in such form and within such time as may be prescribed.

Explanation.—For the purposes of this section,—

(i) "specified person" shall mean,—

(a) the Central Government or any State Government; or

(b) any local authority; or

(c) any corporation established by or under a Central, State or Provincial Act; or

(d) any company; or

(e) any co-operative society; or

(f) any authority, constituted in India by or under any law, engaged either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both; or

(g) any society registered under the Societies Registration Act, 1860 (21 of 1860) or under any law corresponding to that Act in force in any part of India; or

(h) any trust; or

(i) any university established or incorporated by or under a Central, State or Provincial Act and an institution declared to be a university under section 3 of the University Grants Commission Act, 1956 (3 of 1956); or

(j) any Government of a foreign State or a foreign enterprise or any association or body established outside India; or

(k) any firm; or

(l) any person, being an individual or a Hindu undivided family or an association of persons or a body of individuals, if such person,—

(A) does not fall under any of the preceding sub-clauses; and

(B) is liable to audit of accounts under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such sum is credited or paid to the account of the contractor;

(ii) "goods carriage" shall have the meaning assigned to it in the Explanation to sub-section (7) of section 44AE;

(iii) "contract" shall include sub-contract;

(iv) "work" shall include—

(a) advertising;

(b) broadcasting and telecasting including production of programmes for such broadcasting or telecasting;

(c) carriage of goods or passengers by any mode of transport other than by railways;

(d) catering;

(e) manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer,

but does not include manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from a person, other than such customer.

From the aforesaid provisions of section 194C(1), it may be seen that any person responsible for paying any sum to any resident contractor for carrying out any work, including supply of labour, in pursuance of a contract, shall deduct an amount equal to –

(i) One per cent where the payment is being made to an individual or HUF;

(ii) Two per cent where the payment is being made to a person, other than an individual or HUF

of such sum as income-tax on income comprised therein.

Further, as per *Explanation (iv)* to section 194C, the term '*Work*' shall include -

(*a*) advertising;

(*b*) broadcasting and telecasting including production of programmes for such broadcasting or telecasting;

(*c*) carriage of goods and passengers by any mode of transport other than by railways;

(*d*) catering.

(*e*) manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer.

- but does not include manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from a person, other than such customer.

From the aforesaid language of section 194C, it is evident that section 194C contemplates that the contract must involve the carrying out of any work including supply of labour. Further, as per *Explanation (iv)* to section 194C, the term "*work*" includes advertising, broadcasting, telecasting, carriage of goods and passengers, catering, manufacturing or supplying a product, etc.

We may also examine the term '*Work*', as used in common parlance. As per the Concise Oxford Dictionary, 9th Edition, "*work*" means application of mental or physical effort to a purpose; the use of energy. "*Work*" also means a thing done or made by work; the result of an action; a thing made.

From the aforesaid discussion, it may be safely concluded that a contract contemplated under section 194C must involve physical effort or use of energy and the result of such work should be a thing done or made.

The aforesaid three entities, viz. Issuing Bank, Credit Card Association or Acquiring Bank are not carrying out any *work*, while routing the payment of the sale price of the goods to the Merchant Establishment, as contemplated under section 194C of the Act. The aforesaid view is further reinforced, vide the following Circulars issued by the CBDT.

(i) As per para 7(iv) of Circular No.681, dated 8.3.1994 of the CBDT, the provisions of section 194C would not apply in relation to payments made to banks for discounting bills, collecting / receiving payments through cheques / drafts, opening and negotiating Letters of Credit and transactions in negotiable instruments.

(ii) Similarly, as per Circular No.713, dated 2.8.1995, the provisions of section 194C will not apply to payments made to the airlines or the travel agents for purchase of tickets for air travel of individuals.

(iii) Vide Answer to Question No.14 of Circular No.715, dated 8.8.1995, Fixed Deposit commission and brokerage cannot be covered by section 194C.

(iv) Vide Answer to Question No.16 of Circular No.715, dated 8.8.1995, rendering of services for procurement of orders is not covered under the provisions of section 194C.

In view of the aforesaid reasons, the aforesaid three entities, viz. the Issuing Bank, Credit Card Association and Acquiring Bank are not carrying out any work as contemplated under section 194C of the Act and accordingly, the provisions of section 194C will not be applicable to the aforesaid merchant service fees received by them.

II. Provisions of section 194H – Payment of commission or brokerage

For the sake of ready reference, section 194H of the Act, is reproduced as follows :

Commission or brokerage.

194H. *Any person, not being an individual or a Hindu undivided family, who is responsible for paying, on or after the 1st day of June, 2001, to a resident, any income by way of commission (not being insurance commission referred to in section 194D) or brokerage, shall, at the time of credit of such income to the account of the payee or at the time of payment of such income in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rate of ten per cent :*

Provided *that no deduction shall be made under this section in a case where the amount of such income or, as the case may be, the aggregate of the amounts of such income credited or paid or*

likely to be credited or paid during the financial year to the account of, or to, the payee, does not exceed five thousand rupees :

Provided further *that an individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such commission or brokerage is credited or paid, shall be liable to deduct income-tax under this section:*

Provided also *that no deduction shall be made under this section on any commission or brokerage payable by Bharat Sanchar Nigam Limited or Mahanagar Telephone Nigam Limited to their public call office franchisees.*

Explanation.—For the purposes of this section,—

(i) "commission or brokerage" includes any payment received or receivable, directly or indirectly, by a person acting on behalf of another person for services rendered (not being professional services) or for any services in the course of buying or selling of goods or in relation to any transaction relating to any asset, valuable article or thing, not being securities;

(ii) the expression "professional services" means services rendered by a person in the course of carrying on a legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or such other profession as is notified by the Board for the purposes of section 44AA;

(iii) the expression "securities" shall have the meaning assigned to it in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) ;

(iv) where any income is credited to any account, whether called "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly.

It may, thus, be seen that as per the provisions of section 194H, any person responsible for paying any income by way of commission or brokerage, shall deduct income-tax thereon at the rate of ten per cent.

As per *Explanation (i)* to section 194H, "*commission or brokerage*" includes any payment received or receivable, directly or indirectly, by a person **acting on behalf of another** person for services rendered (not being professional services) or for any services in the course of buying or selling of

goods or in relation to any transaction relating to any asset, valuable article or thing, not being securities.

In the present context, it will be necessary to examine or deal with the following issues / items :

1. **The word "commission", judiciously defined**.

Davey, L.J. defined "*commission*" as follows:

Commission is *prima facie* the payment made to an **agent for agency work,** usually according to a scale, it may be an *ad valorem* scale, but not necessarily an *ad valorem* scale. It is…. the most general word that can be used to describe the remuneration paid to an agent for an agency work other than a salary: - *Drielsma Vs. Manifold* [1894] 3 Ch. 100, 107 (CA).

A '*commission*" is the recompense or reward of an **agent, factor, broker or bailee**, when the same is calculated as a percentage on the amount of his transaction or on the profit to the **principal** – *Sunderland Vs. Day* 145 N.E.2d. 39, 41 12 I11.2d.50.

"*Commission*" is compensation paid to another for services rendered in the **handling of another's business or property** and based proportionately upon the amount or value thereof – *Rubinstein Vs. Rubinstein* 109 N.Y.S.2d.724,734.

Besides, as per Advanced Law Lexicon, 3rd Edition, 2005, by Shri P.R.Aiyar, *In Commercial law,* commission is a compensation to a factor or other agent for services to be rendered in making a sale or otherwise; a sum allowed as compensation to a servant, factor or agent who manages the affairs of others, in recompense for his services. It is an allowance, recompense or reward made to agents, factors, brokers and others for effecting sales or carrying out business transactions. **It is generally calculated as a certain percentage on the amount of the transactions or on the profit to the principal.**

Thus, for payment of commission, **an element of agency is essential**.

2. **The word "brokerage", judiciously defined.**

The law dictionary defines brokers to be "those that contrive, make, and conclude bargains and contracts between merchants and tradesmen, for which they have a fee or reward" – *Milford Vs. Hughes* [1846] 16 M. & W. 174.

A broker is a **mercantile agent** who in the ordinary course of his business is employed to make contracts for the purchase or sale of property or goods of which he is not entrusted with the possession or documents of title [1 Halsbury's Laws (3rd Edition) 151, 152].

A broker for sale is a person making it a trade to find buyers for those who wish to sell, and sellers for those who wish to buy, and to negotiate and superintend the making of the bargain

between them. His duty is to establish privity of contract between the seller and the buyer [34 Halsbury's Laws (3rd Edn.) 27].

From the aforesaid definition, it is clear that for payment of brokerage also, **an element of agency is essential**.

3. **The judgement in the case of *Ahmedabad Stamp Vendors Association Vs. Union of India* [2002] 257 ITR 202 (Guj.)**

In this case, the Honourable High Court had to deal with the meaning of "*commission or brokerage"*. It was held in this case that in respect of payment of commission or brokerage, an **element of agency is essential.** The ratio of the aforesaid judgement may be summarized, as follows:

By the Finance Act, 2001, S.194H of the IT Act, 1961, was inserted in the Act with effect from June 1, 2001. Section 194H provides for deduction of tax from income by way of commission or brokerage. The definition of "commission or brokerage" as contained in the Explanation to S.194H is not so wide that it would include any payment receivable, directly or indirectly, for services in the course of buying or selling of goods. In order to fall within the aforesaid Explanation, the payment received or receivable, directly or indirectly, is ***by a person acting on behalf of another person*** *(i) for services rendered (not being professional services), or (ii) for any services in the course of buying or selling of goods, or (iii) in relation to any transaction relating to any asset, valuable article or thing.* ***The element of agency has to be there in case of all services or transactions contemplated by Explanation (i) to S. 194H.*** *There is a distinction between a contract of sale and a contract of agency by which the agent is authorized to sell or buy on behalf of the principal. The essence of contract of sale is the transfer of title to the goods for a price paid or promised to be paid. The transferee in such a case is liable to the transferor as a debtor for the price to be paid and not as agent for the proceeds of the sale. The essence of agency to sell is the delivery of the goods to a person who is to sell them, not as his own property but as the property of the principal who continues to be the owner of the goods, and will therefore be liable to account for the sale proceeds.*

Thus, in the context of provisions of section 194H, payment should be made to a person who acts on behalf of another person, for rendering services in the course of buying and selling goods or in relation to any transaction relating to any asset. In other words, transactions on principal to principal basis are not covered by section 194H. **If element of "*agency*" is absent, section 194H is not applicable, even if a payment is termed as "*brokerage*" or "*commission*"**. For instance,

discount allowed by a manufacturer to a dealer for bulk purchases or for prompt payment is outside the purview of section 194H.

In view of the functions performed by the aforesaid three entities, there is no relationship of principal and agent between them and the customer. As already pointed out, the aforesaid three entities are only rendering services for payment of sale price of the goods to the Merchant Establishment.

Therefore, there is absolutely no element of agency involved in the aforesaid transactions. Accordingly, the provisions of section 194H of the Act, will also not be applicable in respect of the merchant service fees receivable by the aforesaid three entities.

III. Provisions of section 194J – Fees for professional or technical services

For the sake of ready reference, section 194J of the Act is reproduced as follows :

Fees for professional or technical services.

194J. *(1) Any person, not being an individual or a Hindu undivided family, who is responsible for paying to a resident any sum by way of—*

(a) fees for professional services, or

(b) fees for technical services, or

(c) royalty, or

(d) any sum referred to in clause (va) of section 28,

shall, at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to ten per cent of such sum as income-tax on income comprised therein :

Provided *that no deduction shall be made under this section—*

(A) from any sums as aforesaid credited or paid before the 1st day of July, 1995; or

(B) where the amount of such sum or, as the case may be, the aggregate of the amounts of such sums credited or paid or likely to be credited or paid during the financial year by the aforesaid person to the account of, or to, the payee, does not exceed—

(i) thirty thousand rupees, in the case of fees for professional services referred to in clause (a), or

(ii) thirty thousand rupees, in the case of fees for technical services referred to in clause (b), or

(iii) thirty thousand rupees, in the case of royalty referred to in clause (c), or

(iv) thirty thousand rupees, in the case of sum referred to in clause (d) :

Provided further *that an individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such sum by way of fees for professional services or technical services is credited or paid, shall be liable to deduct income-tax under this section :*

Provided **also** *that no individual or a Hindu undivided family referred to in the second proviso shall be liable to deduct income-tax on the sum by way of fees for professional services in case such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.*

(2) [***]

(3) [***]

Explanation.—For the purposes of this section,—

(a) "professional services" means services rendered by a person in the course of carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or advertising or such other profession as is notified by the Board for the purposes of section 44AA or of this section;

(b) "fees for technical services" shall have the same meaning as in Explanation 2 to clause (vii) of sub-section (1) of section 9;

(ba) "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9;

(c) where any sum referred to in sub-section (1) is credited to any account, whether called "suspense account" or by any other name, in the books of account of the person liable to pay such sum, such crediting shall be deemed to be credit of such sum to the account of the payee and the provisions of this section shall apply accordingly.

It may be seen from the aforesaid provisions of section 194J that any person, not being an individual or a Hindu undivided family, who is responsible for paying to a resident any sum by way of –

(a) fees for professional services, or

(b) fees for technical services, or

(c) royalty, or

(d) any sum referred to in clause (va) of section 28

- shall deduct an amount equal to ten per cent of such sum, as income-tax on income comprised therein.

As regards the aforesaid MSF, the same cannot partake the nature of royalty or any sum under an agreement, for not carrying out any business or for not sharing know-how, patent, etc., as referred to in section 28(va). Therefore, consideration of the aforesaid items in clauses (c) and (d) is ruled out.

The only other items left for our consideration, are, therefore, fees for professional services or fees for technical services.

As regards the term '*Professional services'*, the same is defined under *Explanation (a*) to section 194J. For the sake of ready reference, the aforesaid *Explanation (a)* is reproduced as follows :

Explanation.—For the purposes of this section,—

(a) "professional services" means services rendered by a person in the course of carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or advertising or such other profession as is notified by the Board for the purposes of section 44AA or of this section;

From the aforesaid *Explanation (a),* it may be seen that '*Professional services'* means services rendered by a person in the course of carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy, etc. From the nature of the aforesaid services being rendered by the aforesaid three entities in the present case, it is quite obvious that the same will not fall within the definition of the term '*Professional services'* under the aforesaid *Explanation (a).*

As regards the expression, '*Fees for technical services'*, as per *Explanation (b)* to section 194J, it shall have the same meaning as in *Explanation 2* to section 9(1)(vii) of the Act. For the sake of ready reference, *Explanation 2* to section 9(1)(vii) is reproduced as follows :

Explanation 2.—For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like

project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".

From the aforesaid *Explanation 2* to section 9(1)(vii), it may be seen that the expression '*Fees for technical services'* means any consideration for rendering any managerial, technical or consultancy services, etc.

In this connection, a judgement of Madras High Court, in the case of *Skycell Communications Ltd Vs Dy.CIT [2001] 251 ITR 53 (Mad)* is very relevant. It was held in this case that provision of cellular mobile telephone facility to subscribers was not a technical service and therefore, no tax was required to be deducted at source under section 194J of the Act, in respect thereof.

In this connection, a part of the Head-Note, on page 54 of the Report is very relevant, which is reproduced as follows :

Fees for technical services is not defined in section 194J of the Income-Tax Act, 1961. Explanation (b) in that section provides that that expression shall have the same meaning as in Explanation 2 to clause (vii) of sub-section (1) of section 9. This definition shows that consideration paid for the rendering of any managerial, technical or consultancy service, as also the consideration paid for the provision of services of technical or other personnel, would be regarded as fees paid for "technical service". The definition excludes from its ambit consideration paid for construction, assembly, or mining or like project undertaken by the recipient, as also consideration which would constitute income of the recipient chargeable under the head "Salaries". Thus while stating that "technical service" would include managerial and consultancy services, the Legislature has not set out with precision as to what would constitute "technical" service to render it "technical service". Having regard to the fact that the term is required to be understood in the context in which it is used, "fees for technical services" could only be meant to cover such things technical as are capable of being provided by way of service for a fee. ***The popular meaning associated with "technical" is "involving or concerning applied and industrial science". "Technical service" referred to in section 9(1) contemplates rendering of a "service" to the payer of the fee. Mere collection of a fee for use of a standard facility provided to all those willing to pay for it does not amount to the fee having been received for technical services.*** *When a person decides to subscribe to a cellular telephone service in order to have the facility of being able to communicate with others, he does not contract to receive a technical service. What he does agree to is to pay for the use of the airtime for which he pays a charge. The fact that the telephone service provider has*

installed sophisticated technical equipment in the exchange to ensure connectivity to its subscriber, dies not on that score, make it provision of a technical service to the subscriber. What applies to cellular mobile telephone service is also applicable in fixed telephone service. Neither service can be regarded as "technical service" for the purpose of section 1941. [Emphasis added]

From the aforesaid Head-Note, it may be seen that the expression '*Fees for technical service'* could only be meant to cover such things technical as are capable of being provided by service for a fee. Further, the popular meaning associated with "*technical*" is "**involving or concerning applied and industrial science". Besides, the aforesaid merchant service fees receivable for use of standard facility provided by the aforesaid three entities will not amount to the fee having been received for technical services.**

In the light of the aforesaid reasons, the aforesaid merchant service fees receivable by the aforesaid three entities, viz. Issuing Bank, Credit Card Association and Acquiring Bank will not fall within the purview of the provisions of section 194J also.

IV. Besides, the aforesaid credit card transactions will mostly be used by the individuals or HUFs and if the aforesaid payment is made exclusively for personal purposes of such individuals or HUFs, then no tax is deductible at source therefrom, under section 194C, 194H or 194J of the Act.

In the present context, it may also be stated that most of the aforesaid credit card transactions for the purchase of goods will be for personal purposes of the aforesaid customers / individuals, which may be individuals or Hindu undivided families (HUFs). As already pointed out, the aforesaid MSF may, at the most, be considered to fall within the purview of sections 194C, 194H or 194J of the Act. It will, therefore, be relevant to refer to certain provisions of the aforesaid sections in this connection. The same are discussed as follows :

1. Section 194C(4)

In this regard, section 194C(4) is relevant, which is reproduced as follows :

Payments to contractors.

194C.*(4) No individual or Hindu undivided family shall be liable to deduct income-tax on the sum credited or paid to the account of the contractor where such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.*

From the aforesaid provisions of section 194C(4), it may be seen that no individual or Hindu undivided family (HUF) is liable to deduct income-tax at source, where such sum is paid exclusively for personal purposes of such individual or HUF.

2. Second proviso to section 194H

In this regard, the second proviso to section 194H is relevant, which is reproduced as follows :

Provided further *that an individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such commission or brokerage is credited or paid, shall be liable to deduct income-tax under this section:*

From the aforesaid second proviso to section 194H, it may be seen that only individuals or HUFs engaged in a business or profession, in respect of commission or brokerage, will be liable to deduct tax at source from such commission or brokerage.

In other words, if the aforesaid commission or brokerage is paid exclusively for personal purposes of such individuals or HUFs, then the provisions of section 194H of the Act, will not apply and accordingly, no tax will be required to be deducted at source from the aforesaid payment in such cases.

3. Third proviso to section 194J(1)

In this regard, the third proviso to section 194J(1) is relevant, which is reproduced as follows :

Provided also *that no individual or a Hindu undivided family referred to in the second proviso shall be liable to deduct income-tax on the sum by way of fees for professional services in case such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.*

From the aforesaid third proviso to section 194J(1) of the Act, it may be seen that no individual or HUF shall be liable to deduct tax at source on the sum, by way of fees for professional services, if such sum is paid exclusively for personal purposes of such individual or any member of HUF.

In the light of the aforesaid discussion, it is quite clear that most of the aforesaid credit card transactions for the purchase of goods / services will be for personal purposes of the individuals or

HUFs and in view of the aforesaid provisions of sections 194C, 194H and 194J, no tax will be required to be deducted at source under the aforesaid sections, in such cases.

V. No TDS under section 195 also, even if the aforesaid entities are non-resident in India.

In this context, it may also be understood that the aforesaid credit card transactions have global reach. In other words, in respect of global transactions for the purchase of goods / services, at times the aforesaid entities may also be non-resident in India.

It will, therefore, be necessary to examine whether any tax at source will be deductible under section 195 of the Act, in respect of any income / sums payable to the aforesaid non-resident entities.

In view of the aforesaid reasons, it will be necessary to examine the relevant provisions of the Income-Tax Act, 1961 (the Act).

The same are discussed as follows :

1. *Section 195 – TDS from other sums*

For our purpose, section 195(1) is relevant and the same is reproduced :

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195 Other sums.

(1) Any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest or any other sum chargeable under the provisions of this Act (not being income chargeable under the head 'Salaries') shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force :

***Provided** that in the case of interest payable by the Government or a public sector bank within the meaning of clause (23D) of section 10 or a public financial institution within the meaning of that clause, deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode :*

***Provided further** that no such deduction shall be made in respect of any dividends referred to in section 115 –O.*

From the aforesaid provisions of section 195(1), it may be seen that any person responsible for paying to a non-resident, including a foreign company, any interest or any other sum chargeable under the provisions of the Act, except income from "*Salaries*", shall deduct income-tax thereon, at the rates in force.

In other words, deduction of tax at source, is required to be made only if the payment is chargeable to tax n India.

In order to examine whether a certain payment to a non-resident entity is chargeable to tax in India, we will have to examine the provisions of section 5(2) of the Act.

2. *Section 5 – Scope of total income*

For our purpose, provisions of section 5(2) of the Act are relevant. The same read as follows :

Scope of total income

5. *(1) ……*

(2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which –

(a) is received or is deemed to be received in India in such year by or on behalf of such person ; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year.

Explanation 1 – Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Explanation 2 – For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India."

From the aforesaid provisions of section 5(2), it may be seen that the income of a person who is a non-resident, includes income from whatever source derived, which (a) is received or deemed to be received in India in such year by or on behalf of such person ; or (b) accrues or arises or is deemed to accrue or arise in India during such year. As regards receipt of income, it has to be contrasted with remittance. It may be understood here that all direct first receipt of income in India will be taxable in respect of all taxpayers whether resident or non-resident in India. Even for non-residents, it will be treated as Indian income liable to tax, if received in India, though accruing outside India. However, the income first received abroad but remitted to India, cannot be taxable on receipt basis, unless it is otherwise taxable. For example, foreign pension directly received in India will be taxed as a receipt in India; but a sum credited to a bank account abroad and remitted to India thereafter, does not amount to income received in India.

As regards deemed receipt, this charge is applicable to all assesses irrespective of their residential status, even as charge on '*actual receipt'* basis is applicable to both residents and non-residents. It is by virtue of fictional deeming that the sums in question are treated as

income or treated as receipts in India. One of the examples of such fictional receipt is section 7(i) – annual accretions in the previous year to the balance of an employee in a recognized provident fund. The other example may be any sum received or benefit obtained under section 41(1) of the Act.

As regards receipt of income, such income will naturally be received by a non-resident in a place outside India. Therefore, any such payment to a non-resident outside India will not fall under clause (a) of section 5(2) of the Act.

We will now deal with the provisions of clause (b) of section 5(2) of the Act.

The first limb of the aforesaid clause (b) relates to accrual or arisal of income. The place of accrual or arisal of income is the place where the right to receive that income accrues or arises in respect of any payment made to a non-resident. Ordinarily the right to receive the same by a non-resident accrues or arises outside India. Therefore, the same will not be liable to tax in India.

As the services to be rendered by the aforesaid entities, in case they are non-residents in India, will be rendered outside India, the right to receive the payment in respect of the aforesaid services shall accrue or arise in the foreign countries wherefrom such services are rendered. In view of the aforesaid reasons, the payment in respect of the impugned services, rendered by the aforesaid entities, will not be liable to tax in India.

3. Section 9 – Income deemed to accrue or arise in India

We have now to examine whether the element of income embedded in the payment to the Merchant Establishment or the merchant service fees payable to the other three entities, could be treated as income deemed to accrue or arise in India, as per the provisions of section 9 of the Act.

The provisions of section 9(1) comprise seven clauses, viz. clauses (i) to (vii). These clauses deal with different types of income. The aforesaid clauses are briefly discussed as follows :

(i) Clause (i)

Clause (i) relates to income accruing or arising through or from a business connection or from any property in India or from any asset or source of income in India or through the transfer of capital asset located in India.

Obviously, none of the aforesaid non-resident entities will have a business connection with the customer or the credit card holder in India. Therefore, the aforesaid clause (i) will not apply in the present case.

(ii) Clause (ii)

Clause (ii) relates to income under the head "*Salaries*"

Therefore, clause (ii) will also not apply to the present case.

(iii) Clause (iii)

Clause (iii) relates to income under the head "*Salaries payable by the Government to a citizen of India for service outside India*".

Obviously, clause (iii) will also not apply to the present case

(iv) Clause (iv)

Clause (iv) relates to dividend paid by an Indian company outside India.

Obviously, clause (iv) will also not apply to the present case.

(v) Clause (v)

Clause (v) relates to income by way of interest.

Therefore, clause (v) will also not apply to the present case

(vi) Clause (vi)

Clause (vi) relates to income by way of royalty.

As already explained in the earlier para (III), the income embedded in the payment to the Merchant Establishment or merchant service fees cannot be treated as royalty, by any stretch of imagination.

Therefore, clause (vi) will also not apply to the present case.

(vii) Clause (vii)

Clause (vii) relates to income by way of fees for technical services.

As already explained in the aforesaid para (III), the aforesaid income / amount will also not fall within the purview of "*Fees for technical services* ".

In view of the aforesaid reasons, none of the income / amount payable to the aforesaid non-resident entities will fall within the mischief of section 9(1) of the Income-Tax Act, 1961.

In the light of the aforesaid reasons, any income / sums payable to any of the aforesaid entities, even if they are non-resident in India, will not be liable to tax in India. Therefore, no tax will be required to be deducted at source therefrom under section 195 of the Act also.

VI. Conclusion

In the light of the discussion in the preceding paragraphs, it is clearly established that –

1. The TDS provisions under Chapter XVII-B will apply only to a *person responsible for paying* the income / amount, in question.
2. The aforesaid Merchant Establishment can, in no way, be regarded as the person responsible for paying the sale price of the goods purchased by the customer from such Merchant Establishment.

In view of the aforesaid reason, there will be no obligation of TDS on the Merchant Establishment in the present context.

3. Further, as discussed in detail, in the aforesaid paras (I) to (III), the merchant service fees receivable by the aforesaid three entities, viz. Issuing Bank, Credit Card Association and Acquiring Bank, do not fall within the purview of the probable sections under Chapter XVII-B, viz. sections 194C, 194H and 194J of the Act.
4. Besides, as discussed in aforesaid para (IV), most of the aforesaid credit card transactions for the purchase of goods will be for personal purposes of the customers, which may be individuals or HUFs and in such cases, no tax will be required to be deducted at source, in respect of payments made for the purchase of goods.
5. No tax will be deductible at source under section 195 of the Act, in respect of the income / sums payable to such entities, even if they are non-resident in India.

In view of the aforesaid reasons, there will be no obligation of TDS in respect of the payment of the aforesaid price of the goods / services and the merchant service fees, on the customer / credit card holder, the Merchant Establishment, the Issuing Bank, the Credit Card Association or the Acquiring Bank.

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