

TAX FLASH NEWS

Payment to retailers under the trade discount scheme is treated as sales promotion and not commission and therefore tax is not to be deducted under Section 194H of the Income-tax Act

Background

Recently, the Visakhapatnam Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of United Breweries Ltd.¹ (the taxpayer) has held that the payment made by the taxpayer under the trade discount scheme would constitute sales promotion expenditure and would not be treated as a commission under Section 194H of the Income-tax Act, 1961 (the Act). The Tribunal observed that the sale between the taxpayer, another Indian company and the retail dealers was on 'principal to principal' basis. The retail dealers have not provided any service to the taxpayer since there is no direct connection between the taxpayer and retail dealers.

Facts of the case

- The taxpayer is engaged in manufacture and sale of beer to Andhra Pradesh Beverages Corporation Ltd (APBCL) and is a group concern of United Beverages India Pvt. Ltd. It had entered into a 'Brewing and Distribution Agreement' with another group company.
- The tax department conducted a survey in the premises of the taxpayer to verify the compliance of the Tax Deduction at Source (TDS) provisions of the Act. From the information gathered during the course of the survey, the Assessing Officer (AO) noted that the taxpayer had not deducted tax at source on the payments made under the head 'Trade Schemes and Discounts'.

- The AO felt that these payments are in the nature of commission and would attract the provisions of Section 194H of the Act. The AO held that the taxpayer had defaulted by not deducting tax at source on these payments and hence, it would be treated as 'assessee in default' in terms of Section 201(1) of the Act and also levied interest as per Section 201(1A) of the Act.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.

Tribunal's ruling

- On perusal of Section 194H of the Act, it is clear that the payment received by a person for 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 etc. falls under the category of commission or brokerage.
- Provision of service by a person acting on behalf of another person signifies the existence of a principal-agent relationship between the payer and payee since the agent acts on behalf of the principal. If the relationship between the payer and payee is in the nature of principal to principal, then it cannot be considered as a service provided by one person on behalf of another person and hence the said payment cannot fall under the definition of commission.

¹ United Breweries Ltd. v. ITO (ITA Nos.103, 104 & 105/Viz/2014) – Taxsutra.com

- In the present case, the taxpayer supplies beer to APBCL, which in turn, sells beer to various retail dealers. Hence, in effect, there is no direct relationship between the taxpayer and the retail dealers. However, since the turnover of the taxpayer would be dependent upon the sales effected with the retail dealers, the taxpayer had promoted a sales promotion scheme, under which incentives are given to retail dealers upon achievement of targets in sales.
- Under this promotional scheme, the retail dealers would be motivated to purchase more quantity of beer manufactured by the taxpayer, which in turn would increase the turnover of the taxpayer. In order to market the trade discount scheme and to promote the sales of its products, the taxpayer had appointed del credere agents.
- There was no dispute with regard to the fact that the payment made to the del credere agents for the services provided to the taxpayer was treated as commission by the taxpayer and tax was deducted at source under Section 194H of the Act. The incentives payable under the trade discount scheme were disbursed by the taxpayer to the retail dealers through del credere agents who have opened separate bank accounts for the said purpose.
- The Tribunal relied on the decision of the Supreme Court in the case of Bhopal Sugar Industries Ltd² wherein the Supreme Court had explained about 'contract of sale' and 'contract of agency'. The Supreme Court observed that the essence of the 'contract of agency' is that the agent does not sell the goods as his own but sells the same as the property of the principal under his instructions and directions. The agent always acts on behalf of his principal only and the benefits of the activities done by the agent would be reaped by the principal. Since the agent is not the owner of goods, loss, if any, suffered by the agent is to be borne by the principal and the agent shall be indemnified by the principal. The payment received by the agent for the services rendered to the principal is understood as 'commission'. Thus, the 'element of agency' is an essential requirement in order to characterise a payment made for services provided as 'commission'.
- The decision of the Bombay High Court³ relied on by the CIT(A) also observes that the 'commission' is in the nature of recompense or reward for the services rendered. The decision of the Bombay High Court and the CBDT Circular⁴ make it clear that the discount need not be adjusted against the sale price and that it may be paid separately.
- The Tribunal relied on the decision of the Visakhapatnam Tribunal in the case of Pearl Bottling (P) Ltd.⁵ wherein it was held that the relationship between the taxpayer and its distributor was on 'principal to principal' basis. Therefore, the reimbursement of discount given to the retailers and promotional discount given to the distributors does not amount to a commission.
- There is no dispute that the sale between the taxpayer and APBCL and the sale between APBCL and the retail dealers was on a 'principal to principal' basis, since the property and risk attached with the goods got transferred from the seller to the buyer under both occasions.
- It cannot be said that retail dealers have provided any service to the taxpayer since there is no direct connection between the taxpayer and retail dealers. Further, the del credere agents cannot be considered as 'payees' in these transactions since they had only acted as conduits.
- The payment was actually made to the retail dealers. Accordingly, the payment made by the taxpayer under such scheme would constitute as sales promotion expenditure and would not fall under the category of the commission under Section 194H of the Act. Accordingly, the order of the CIT(A) was set-aside, and the AO was asked to delete the demand raised under Section 201(1) and 201(1A) of the Act.

Our comments

The Visakhapatnam Tribunal in the present case held that sales promotion discounts given to retailers is not a 'commission' in the absence of a principal-agent relationship and hence provisions of Section 194H of the Act are not applicable.

The provisions of Section 194H deal with the deduction of tax at source on payments in the nature of commission or brokerage. The Gujarat High Court in the case of Ahmedabad Stamp Vendors Association⁶ had held that these provisions are not applicable to trade discounts. A commission is paid for selling, buying, and the collection of payment or any mercantile activity while trade discount is given for enhancing sales.

In the case of Idea Cellular Ltd⁷ the Hyderabad Tribunal held that a discount allowed on outright purchase is not commission since there is no principal-agent relationship and transactions are done on principal to principal basis.

² Bhopal Sugar Industries Ltd v. STO AIR 1977 SC 1275

³ Harihar Cotton Processing Factory v. CIT [1960] 39 ITR 594 (Bom)

⁴ CBDT Circular No. 8/2005, dated 29 August 2005

⁵ ACIT v. Pearl Bottling (P) Ltd. [2011] 46 SOT 133 (Visakhapatnam)

⁶ Ahmedabad Stamp Vendors Association v. Union of India [2002] 257 ITR 0202 (Guj)

⁷ Idea Cellular Ltd. v. DCIT [2010] 123 ITD 620 (Del)

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