

SC: Tax is to be deducted under Section 194H of the Income-tax Act, 1961, on supplementary commission earned by agents on sale of airline tickets

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Summary

The Supreme Court (SC) in its recent decision¹ has held that airlines are required to withhold tax under Section 194H of the Income-tax Act, 1961 (the Act), on supplementary commission earned by the travel agents.

Since the agents had offered the supplementary commission to tax in their return of income, the SC remanded the matter back to the assessing officer to compute interest on delayed payment of tax deducted at source (TDS).

Further, considering the contrary High Court (HC) decisions on the matter, the SC held that the taxpayer had a reasonable cause for not deducting TDS and quashed the penalty proceedings².

Background

- The taxpayer was an airline company. During the relevant period, for airline companies, the International Air Transportation Association (IATA) decided the ceiling price of air tickets (base fare). Airlines could decide the ticket price to be either lower or equal to such base fare, and such price was considered as the net fare.
- The IATA also provided blank tickets to agents to sell tickets in the market.
- Arrangement between the airlines and the agents were governed by the Passenger Sales Agency Agreement (PSA), which was signed by IATA on behalf of the airline.
- However, the agents could sell tickets to customers at a price higher than the net fare decided by the airline. Such additional amount was the agent's income, i.e., the supplementary commission (SPC).

Base fare	Net fare	Fare charged by agent	SPC
120	90	100	10 (i.e. 100-90)

- Once tickets were sold, the agents received a 7% commission (standard commission) on the base fare set by IATA. Airlines deducted TDS³ on such amount.
- Details of the final sale price charged by the agent was provided to an organisation known as Billing and Settlement Plan (BSP)⁴. The BSP stored financial information, including the net amount payable to the aviation companies, discounts, and commission payable to the agents.
- The dispute in this case was regarding the characterisation of SPC and whether the said amount would be subject to TDS³.

¹ In the case of Singapore Airlines Ltd [TS-880-SC-2022] (AY 2001-02)

² Under section 271C of the Act

³ Under section 194H of the Act

⁴ BSP is an organisation that functions under the control of IATA and manages *inter alia* logistics vis-à-vis payments and acts as a forum for the agents and airlines to examine details of sale of air-tickets.

- This batch of appeals⁵ arises from a judgement of the Delhi HC, wherein the HC allowed the revenue's appeal and held that taxpayers (i.e. the airlines) were required to deduct TDS on the SPC. Further, the taxpayers were regarded as "assesseees in default"⁶ and subject to payment of interest⁷ and penalty⁸.

Taxpayer's contentions

- The taxpayer contended that it is oblivious to the amount of SPC received by the agent. Accordingly, it would not be feasible to deduct TDS on such amount, which is paid directly by customer to agents.⁹
- Standard commission and SPC are two different transactions by virtue of two distinct legal relationships. SPC arises on account of the relationship between the agent and the customer, and hence cannot be regarded as commission.
- With respect to the Delhi HC's observation regarding access of information via BSP, the taxpayer contended that IATA sends the final bill to the taxpayer after aggregating the amounts on a bi-monthly basis (and not after each transaction).
- The PSA does not govern the dealings between the agent and the customer.
- As per Section 194H of the Act, commission is payment in the course of services rendered. However, there is no service provided by the agent to the taxpayer for SPC.

- Agents included the amount of SPC in their return of income and paid tax thereon. Accordingly, no TDS was required to be deducted on SPC since it would lead to double taxation.¹⁰

Revenue's contentions

- The taxpayer's argument regarding two different purported legs of the ticket selling process is irrelevant. The overall relationship between the taxpayer and agent is that of principal-agent.
- Each activity carried out by the agent for selling the tickets was on behalf of the taxpayer.
- The relationship between the taxpayer and agent is not that of principal-principal because the title in the tickets remains with the taxpayer¹¹.
- The taxpayer could have made comprehensive tax deduction at the end of the month based on the data maintained by BSP.
- The language of Section 194H of the Act is inclusive and covers direct and indirect payments to the agent¹².
- Default by taxpayer cannot be cured on the premise that agents offered the amount of SPC to tax in their return of income.

Key observations of SC

- Section 194H of the Act and Section 182 of Contract Act, 1872, are interlinked.
- The SC observed that there is a distinction between a contract of agency and a contract of sale¹³.

⁵ Singapore Airlines Ltd. (Civil Appeal No. 6964-6965 Of 2015); KLM Royal Dutch Airlines (Civil Appeal No. 6966-6967 Of 2015); British Airways PLC (Civil Appeal No. 6968 Of 2015)

⁶ As per section 201 of the Act

⁷ Under section 201(1A) of the Act

⁸ Under section 271C of the Act

⁹ Reliance was placed on Bombay HC's decision in the case of CIT v. Qatar Airways [2012] (20 taxmann.com 598) (Bombay)

¹⁰ Reliance placed on SC's decision in the case of Hindustan Coca Cola Beverages Pvt. Ltd. v. CIT (2007) (8 SCC 463)

¹¹ Reliance was placed on Gujarat HC's decision in the case of Ahmedabad Stamp Vendors Ass. v. Union of India (2002) (SCC Online Guj 135), which was affirmed by SC in the case of 16 SCC 114.

¹² Reliance placed on SC's decision in the case of Director, Prasar Bharati v. CIT (2018) (7 SCC 800)

¹³ Reliance placed on SC's ruling in the case of Gordon Woodroffe & Co. v. Sheikh M.A. Majid & Co.

- With respect to taxpayers' arguments regarding bifurcation of the transaction in two parts (i.e. standard commission and SPC), the SC held that the following aspects need to be considered:
 - whether title in tickets passed from the taxpayer to agents.
 - whether sale of the tickets by the agent was done by considering it as the property of the agent or that of the taxpayer.
 - whether the taxpayer or agent is liable for any breach of terms and conditions in the tickets and failure to fulfil contractual rights accrued to the customer on purchase of tickets.
- As per the terms of PSA and based on judicial pronouncements¹⁴, the SC observed that tickets sold by the agent remained the property of the taxpayer and there was no contract of sale between them.
- Various elements of a “contract of agency” are satisfied by the clauses of PSA. Following observations were made based on the review of the PSA:
 - Every action taken by the agent is on behalf of the taxpayer.
 - The taxpayer indemnifies the agent against liabilities arising on account of failure to provide transportation services.
 - The taxpayer retains title over the ticket and is responsible for services provided to the end customer.
 - The taxpayer is responsible to provide compensation to the agent for acts carried out as per the PSA.
- Further, the SC observed that the contract does not distinguish in terms of stages of the transactions in selling tickets. SC upheld the observation of the

Delhi HC that the arrangement between the customer and agent is part of the package of activities pursuant to the PSA.

- SC observed that the ambit of Section 194H of the Act is expansive and it does not distinguish between direct and indirect payments¹⁵. Accordingly, taxpayers' contention regarding point of origin of the amount does not impair the applicability of Section 194H of the Act.
- SC observed that lack of control of the taxpayer on the price charged by the agent cannot absolve it from liability to withhold tax.
- The benefit gained by an agent is incidental and has nexus with the PSA, and hence, is on account of the principal-agent relationship.
- SC also observed that the agent holds the payments in the fiduciary capacity for the taxpayer until proper accounting is made.
- The amount of SPC is reflected on the BSP separately, and hence, the taxpayer can withhold tax thereon.

SC's verdict

- SC held that tax is required to be deducted on the SPC under Section 194H of the Act.
- No recovery of TDS from the taxpayer is required since agents have included the amount of SPC in their tax return and paid tax thereon.
- Interest under Section 201(1A) of the Act can be levied on the amount of shortfall in TDS, for the period of default¹⁶. SC remanded the matter back to the assessing officer for calculating such interest.
- Further, SC held that if any agent has not paid taxes on the amount of SPC, the Revenue can recover the shortfall in TDS from the taxpayer.

¹⁴ (i) Gordon Woodroffe & Co. v. Sheikh M.A.Majid & Co.(1966) (Supp SCR 1)

(ii) Bhopal Sugar Industries Ltd. v. STO, Bhopal (1977) (3 SCC 147)

¹⁵ Prasar Bharati v CIT (2018) 7 SCC 800

¹⁶ i.e., from the date of default in TDS till the date of payment of tax by the agent

- In light of Section 273B of the Act¹⁷, SC held that there were contrary HC decisions on the issue under

consideration, and hence, the taxpayer had reasonable cause for non-deduction of TDS. Accordingly, penalty proceedings were quashed.

Our comments

Withholding tax on SPC has been a litigative issue and there have been contrary HC rulings on the matter. With this decision, the SC has finally settled this matter and held that such amounts would be regarded as commission and would be subject to TDS. Impacted taxpayers would need to assess the impact of this decision basis the facts of their case.

¹⁷ Reliance was placed on SC's decision in the case of CIT v. Eli Lilly & Co. (India) (2009) (15 SCC 1)

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