

Commission/brokerage paid by Asset Management Company to Mutual Fund distributors does not attract withholding tax provisions

30 July 2013



Background

Recently, the Chennai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Sundaram Asset Management Co. Ltd.¹ (the taxpayer) held that tax need not be withheld on payments by Asset Management Company to distributors of Mutual Fund (MF) units.

The Tribunal recognised that services provided by MF distributors are specifically excluded under Section 194H of the Income-tax Act, 1961 (the Act) as the Section excludes withholding tax/ Tax Deducted at Source (TDS) requirements on commission or brokerage paid on securities.

Further these services are not 'professional services' or 'technical services' for the purpose of Section 194J of the Act.

¹ Sundaram Asset Management Co. Ltd. v. DCIT (ITA No. 1774/Mds/2012, Assessment Year 2008-09, dated 19 July 2013)]

Facts of the case

- The taxpayer, an Asset Management Company, has paid commission/brokerage to its MF distributors.
- The Assessing Officer (AO) disallowed payment made by the taxpayer to the MF distributors under Section 40(a)(ia) of the Act for not withholding tax thereon under Section 194J of the Act, applicable to fees for technical/professional services.
- The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO.
- Aggrieved, the taxpayer preferred an appeal before the Tribunal.

Issue before the Tribunal

- Whether payments by the Asset Management Company to the MF distributors are subject to any withholding tax?

Taxpayer's contention

- The taxpayer contended that the commission/brokerage paid to brokers for sale of various Mutual Funds is covered under the provisions of Section 194H of the Act. Such commission paid to the brokers has been specifically excluded from tax deduction. The AO erroneously applied the provisions of Section 194J of the Act. The taxpayer relied on the decision of the Bombay High Court in the case of Kotak Securities Ltd².

Tax department's contention

- The tax department contended that the payments made to the MF distributors are in the nature of fees for professional and/or technical services and subject to withholding tax/ TDS under Section 194J of the Act.

Tribunal's ruling

- The provisions pertaining to TDS on commission and brokerage are contained in Section 194H of the Act, which also include definitions of "commission or brokerage" and "securities".
- Based on these provisions, the Tribunal observed whereas 'securities' include units of mutual funds; Section 194H of the Act excludes commission or brokerage paid on securities.
- Further, the Tribunal observed that the services rendered by the MF brokers/distributors do not fall within the term 'professional services' or technical services as defined under Section 194J of the Act. The Tribunal recognised that the brokers do not require any special qualification in the field of law, engineering, accountancy or technical consultancy. Even an ordinary graduate from humanities group can be a broker.
- Thus, the Tribunal deleted the disallowance under Section 40(a)(ia) of the Act on account of payment made to MF distributors.

Our comments

Apparently given that commission or brokerage paid on securities are expressly excluded from the scope of Section 194H of the Act (TDS on commission), the tax department, as an alternative, sought to apply the provisions of section 194J of the Act (TDS on fees), not appreciating the nature of service rendered.

In these circumstances, this is a welcome ruling from the Chennai Tribunal.



² CIT v. Kotak Securities Ltd [2012] 340 ITR 333 (Bom)

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