

# Overview of Taxation of Non Residents

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# Scheme of Taxation for Non Residents under Income-tax Act, 1961

- ◆ Section 4 (Charge of Income-tax) – Income Tax shall be charged at the rates for that assessment year in accordance with the provisions of the Income Tax Act, 1961 in respect of the total income of the previous year of every person
  
- ◆ Section 2(31) – Person includes
  - ◆ An Individual
  - ◆ HUF
  - ◆ A Company
  - ◆ A Firm
  - ◆ AOP or BOI whether incorporated or not
  - ◆ Local authority and
  - ◆ Every artificial juridical person, not falling above



# Section 5

- ◆ Section 5(2) – The total income of any previous year of a person who is non-resident includes all income which
  - ◆ Is received or deemed to be received in India; or
  - ◆ Accrues or arises or is deemed to accrue or arise to him in India
  
- ◆ Section 2(30) – A non-resident means a person who is not resident and includes the person who is resident but not ordinarily resident

# Scope of Income

	<b>Resident &amp; Ordinarily Resident</b>	<b>Resident but Not Ordinarily Resident</b>	<b>Non Resident</b>
Income accrued or arised in India / received in India	Taxable	Taxable	Taxable
Income accrued outside India but deemed to accrue in India / First receipt in India	Taxable	Taxable	Taxable
Any other income accruing outside India and received outside India	Taxable	Not Taxable*	Not Taxable

\***Exception** - Income received by the individual is taxable only if the business set up is in India



# Section 6 – Residential Status

- ◆ An individual will be treated as a Resident in India in any previous year if he/she is in India for:
  - ◆ At least 182 days in that year, OR
  - ◆ At least 365 days during 4 years preceding that year AND at least 60 days in that year.  
(if the individual leaves India for the purpose of employment or as a member of the crew of an Indian Ship, then the words ‘60 days’ will be substituted with ‘182 days’)

An individual who does not satisfy both the conditions as mentioned above will be treated as "non-resident" in that previous year.

# Section 6 – Residential Status

- ◆ A person is said to be “not ordinarily resident” in India if:
  - ◆ He has been a non-resident for 9 out of 10 previous year preceding that year, or
  - ◆ during seven previous years, preceding that year, has been in India for 729 days or less  
(incase of an HUF the above criteria will be applied to the ‘karta’ of HUF to know the status of the HUF)
  
- ◆ Any HUF, firm or company is said to a be a resident in India if during the previous year the control and management of its affairs is situated wholly in India

# Section 9 vis-a-vis DTAA

<b>Nature of Income</b>	<b>Income-tax Act, 1961</b>	<b>DTAA (OECD model)</b>
<b>Business/ Profession</b>	<b>S.9(1)(i)</b>	<b>Article 5 and Article 7</b>
<b>Salary Income</b>	<b>S.9(1)(ii), S.9(1)(iii)</b>	<b>Article 15</b>
<b>Dividend Income</b>	<b>S.9(1)(iv), S.115A</b>	<b>Article 10</b>
<b>Interest Income</b>	<b>S.9(1)(v), S.115A</b>	<b>Article 11</b>
<b>Royalties</b>	<b>S.9(1)(vi), S.115A</b>	<b>Article 12</b>
<b>Fees for Technical Services</b>	<b>S.9(1)(vii), S.115A</b>	<b>Article 12</b>
<b>Capital Gains</b>	<b>S.9(1)(i)</b>	<b>Article 13</b>

# Section 9

## ◆ Section 9(1)(i)

All income directly or indirectly through or from any business connection, or property, or asset or source of income or through transfer of capital asset situate in India

## ◆ A business connection involves

- ◆ A relation between a business carried on by a non-resident, some activity in India, which contributes directly or indirectly to the earning of the profits or gains.
- ◆ It predicates an element of continuity between the business of the non-resident and the activity in India  
CIT Vs. R.D. Aggarwal & Co. (56 ITR 20)

## ◆ Taxable only if :

- ◆ relates to a source of income or asset in India; or
- ◆ if “business connection” under IT Act / “PE” under the treaty exists.



# Section 9(1)(i) - Amendment

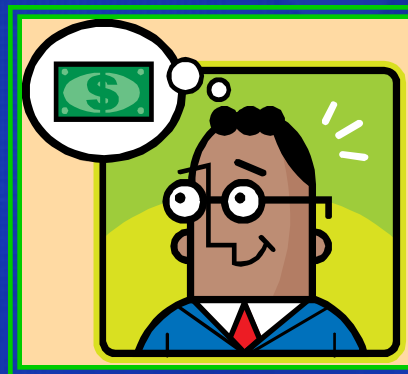
- ◆ Revenue lost the 11,000 crore battle to Vodafone which led to Retrospective amendment
- ◆ Explanation 4
  - ◆ 'through' to retrospectively to mean 'by means of', in consequence of' and 'by reason of'
- ◆ Explanation 5 :
  - ◆ Capital asset to be situated in India, if share or interest derives directly or indirectly its value substantially from assets located in India

# Section 9 - Salaries

Section 9 (1)(ii) –

Income from salaries, if earned in India

- ◆ The term 'earned in India' obviates the difficult question which arises regarding the place of accrual of salaries.
- ◆ The main effect of the clause is to charge non-residents on salary or pension earned in India even where it actually accrues abroad and is received abroad.



# Section 9 – Royalty & Fees for Technical Services

<b>Payer</b>	<b>Deemed to accrue or arise in India</b>
<b>Government</b>	<b>In all cases without exception</b>
<b>Resident</b>	<b>In all cases, except where payable for the purpose of / in business or profession carried on by such person outside India, or for the purposes of <u>making or earning any income from any source outside India</u></b>
<b>Non-resident</b>	<b>Only in cases where it is payable for the purpose of a business or profession carried on by such person in India, or for the purposes of <u>making or earning any income from any source in India</u></b>

# Royalty

## ◆ Means –

- ◆ the transfer of all or any rights (including the granting of a license) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;
- ◆ the imparting of any information concerning the working of the above mentioned assets or intellectual properties
- ◆ the use of any of the above mentioned assets or intellectual properties
- ◆ the imparting of any information concerning about the above mentioned assets or intellectual properties
- ◆ the transfer of all or any rights (including the granting of a license) in respect of any copyright, literary, artistic or scientific work...

# Section 9(1)(vi) - Amendment

## ◆ Explanation 4

- ◆ Transfer of rights retrospectively includes transfer of **right for use / right to use** a computer software irrespective of the medium of transfer

## ◆ Explanation 5

- ◆ Royalty includes consideration whether possession is with payer / such right is used by payer / location of such right is in India

## ◆ Explanation 6

- ◆ **Process** shall retrospectively include transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or other similar technology



# Fees for Technical Services

## ◆ Means –

- ◆ Any consideration (including lumpsum) for rendering of any
  - ◆ Managerial
  - ◆ Technical or
  - ◆ Consultancy services

## ◆ Excludes

- ◆ Construction, assembly, mining or any like project and income chargeable under the head salaries



# Section 9 - Amendment

- ◆ After the decision of Ishikawajima Harima (SC)
- ◆ Explanation was retrospectively inserted by Finance Act, 2007
  - ◆ Income of non-resident shall be deemed to accrue or arise in India whether or not
    - ◆ Non-resident has a place of business or **business connection** in India
    - ◆ Non-resident has **rendered services** in India
- ◆ However, Karnataka High Court in Jindal Thermal Power has upheld that Ishikawajima-Harima is still a good law despite retrospective amendment

# Section 9 - Synopsis

<b>Nature of Income</b>	<b>Taxability</b>
<b>Business / Profession Sec. 9(1)(i)</b>	<b>Taxable if direct or indirect Business Connection in India or property or asset or source in India or transfer of a capital asset situate in India</b>
<b>Capital Gains Sec. 9(1)(i)</b>	<b>Taxable if situs of Shares / Property in India or derives its value substantially from assets in India</b>
<b>Interest Income Sec. 9(1)(v)</b>	<b>Taxable if sourced in India</b>
<b>Royalties Sec. 9(1)(vi)</b>	<b>Taxable if sourced in India</b>
<b>Fees for Technical Services ('FTS') Sec. 9(1)(vii)</b>	<b>Taxable if sourced in India</b>

# Types of double taxation

## ◆ Economic double taxation

- ◆ Same income taxed in hands of two different persons (Transfer pricing)

## ◆ Juridical double taxation

- ◆ Two or more states tax same income
- ◆ Overlapping claims of tax jurisdictions (PE taxation)



# Double Taxation Avoidance Agreement

- ❖ DTAA is an agreement between the two sovereign governments, concerning taxes, the main purpose of which is to regulate tax matters
- ❖ Under the Act, the government has been delegated the power to enter into a DTAA with any country or specified territory or adopt the agreement between specified association of any specified territory by notifying in the official gazette



# Section 90

- ❖ Section 90(2) – Where the DTAA has been entered into by the Government of India with the Government of other country/specified territories for granting relief of tax, or avoidance of double taxation, for promoting mutual economic relations, trade and investment as the case may be, provisions of the domestic law i.e. the Income-tax Act or the DTAA shall apply to the extent that they are more beneficial to the assessee
- ❖ Circular No 333 [F. No. 506/42/81-FTD], dated 2-4-1982 – Where a DTAA provides for a particular mode of computation of income, the same should be followed, irrespective of the provisions of the Income-tax Act

# Relief under the Act

## ◆ Section 90

- ◆ Regulates a case where India has a tax treaty
- ◆ Taxpayer has the option to be taxed as per tax treaty or domestic tax laws, whichever is more beneficial [S.90(2)]
- ◆ Domestic law provisions can, at times, be more beneficial

## ◆ Section 91

- ◆ Relief from double taxation if India has no agreements
- ◆ Credit of doubly taxed Income; lower of
  - ◆ Indian rate of tax; or
  - ◆ Foreign countries rate of tax

# Credit of taxes

## ◆ EXEMPTION METHOD

- ◆ Full Exemption
- ◆ Exemption with progression – taken into account for rate purposes

## ◆ CREDIT METHOD

- ◆ Full credit – No restriction
- ◆ Ordinary credit – restricted to the extent of tax payable in residence – qua “Income”
- ◆ Underlying tax credit
- ◆ Tax sparing
  - ◆ Sparing w.r.t. certain income
  - ◆ Sparing w.r.t. tax payable

# Need for Rational Cross Border Taxation

- ◆ Multi country taxation injures flow of cross border activities
- ◆ Double Tax Avoidance Agreement (DTAA) eliminates or mitigates hardship caused by multi level taxation
- ◆ Home country tax is obligation; host country tax is a cost
  - ◆ Home country is country of residence (COR)
  - ◆ Host country is country of source (COS)
- ◆ Usual for COR to provide unilateral relief
- ◆ Mitigation can result in relief from double taxation, but, not refund by COR

# Double Taxation Avoidance Agreement....

- ◆ Basic Tenets of DTAA
  - ◆ Elimination of Double Taxation
  - ◆ Certainty of Tax Treatment
  - ◆ Reduced Tax Rates
  - ◆ Lower Compliance Cost
  - ◆ Prevention of Fiscal Evasion
  - ◆ Prevention of Tax Discrimination
  - ◆ Resolution of Tax Disputes
  - ◆ Provide for Tax Sparing
  - ◆ Exchange of Information



# Double Taxation Avoidance Agreement....

## ◆ Basic Structure:

- ◆ Article 1 & 2 – Persons Covered and Taxes Covered
- ◆ Article 3 – Definitions governing the DTAA
- ◆ Article 4 – Rules of Residence
- ◆ Article 5 – Defines the meaning of term Permanent Establishment
- ◆ Article 6 to 21 – Provides for Distributive Rule regarding Income Taxes
- ◆ Article 22 – Taxes on Capital
- ◆ Article 23 – Elimination of Double Taxation
- ◆ Article 24 to 29 – Special Provisions
- ◆ Article 30 & 31 – Final Provisions

# Section 94A

- ◆ Recently CBDT has notified **Cyprus** as “Notified Jurisdictional Area” as an anti-avoidance measure
- ◆ Impact
  - ◆ Transfer Pricing provisions shall apply as if the transaction is between associated enterprises
  - ◆ Withholding tax @ 30% on any payment made to entity placed in Cyprus
  - ◆ No deduction of payment made unless certain conditions are fulfilled



# Section 163 – Agent of Non-Resident

## ◆ Vicarious liability of the Representative

### ◆ Instances

- ◆ A person from whom non-resident receives any income, directly or indirectly is an agent
- ◆ Even a non-resident can be treated as agent - *A.P. Damodara Shenoy v. CIT* [1954] 26 ITR 650 (Bom.)
- ◆ Simultaneous proceedings against non-resident and agent are barred *CIT v. Alfred Herbert (India) (P.) Ltd.* [1986] 159 ITR 583 (Cal.)
- ◆ Agent is not liable to deduct tax at source on payments to non-resident *CIT v. Premier Tyres Ltd.* [1982] 134 ITR 17 (Bom.)

# Withholding of Tax





# Withholding tax obligation under Section 195

## ◆ Section 195 (1)

- ◆ *Any person* responsible for making payment to a non-resident shall withhold tax
- ◆ Only in respect of interest or other *sum chargeable* under the Income Tax Act, 1961
- ◆ At the time of *credit* or *payment* whichever is earlier
- ◆ At the '*rates in force*'

**Does not apply to salaries and exempt dividends**



# Objective of section 195

- ◆ The objective of section 195 is to ensure, as far as possible, that the tax liability on the income element of the amount paid is deducted at source itself, so that the Department is not put through the hassles of recovering it from a non-resident whose connection with India may be transient or whose assets in India may not be sufficient to meet the tax liability



# Any Person - Whether includes Non-Resident

- ◆ Any person - whether includes non resident –
  - ◆ Favourable View - Not Included
    - ◆ Provision of the Act cannot have extra territorial jurisdiction
  - ◆ Contrary View - Non residents included
    - ◆ Definition of person under the Act includes non residents/foreign company
    - ◆ Liability to deduct tax at source from the payments made by the Foreign TV channels to the Foreign Transponder owner is fastened on them by virtue of the provisions of section 195 (Asia Satellite v DCIT) (85 ITD 478)(Del)
    - ◆ Provisions of Section 195 encompass payment made by HO overseas AAR (1995) 228 ITR 487: Bechtel Ruling

# Rates of deduction

## ◆ At the rates in force:-

- ◆ Section 2(37A) defines 'rates in force' as rates as per Finance Act or Treaty whichever is applicable
  - ◆ Reference to rates as per DTAA included from 1.6.1992
  - ◆ CBDT vide Circular No. 728 dated 30.11.95 , rates as per DTAA to be applied where they are more favorable to the assessee
  - ◆ Conditions for applying beneficial rate laid down u/s. 115A
- ◆ Issue – Whether surcharge to be levied on Treaty rates
  - ◆ If tax Treaty defines tax include surcharge, and
  - ◆ Rates of tax for royalty, Fee for technical services and interest given as not to exceed a specified percentage in DTAA

# Certificate to be obtained

- ◆ Sec. 195(6) - Person referred to in sec. 195(1) shall furnish the information relating to payment of any sum in Form No. 15CA, after obtaining a certificate from a Chartered Accountant in Form No. 15CB. [read with Rule 37BB]
- ◆ Information to be furnished electronically. [rule 37BB]
- ◆ Amended Form 15CA / 15CB vide Notification dated August 5, 2013 (S.O. 2363 E)



# Section 197

## ◆ Section 197 – Certificate for deduction at lower rate

On an application made by the assessee, the assessing officer on being satisfied that the total income of the recipient justifies the deduction of income-tax at any lower rates or no deduction of income tax, may give the assessee the certificate.



# Synopsis

	<b>195 (2)</b>	<b>195(3)</b>	<b>197</b>
Application by	Payer	Payee under Rule 29 B	Payee Rule 28 – Application in Form 13
Scope	Whole of such sum not chargeable to tax	No deduction of tax	No deduction / Deduction at Lower rate
Appealable	Order under Section 195(2) can be appealed under Section 248, provided the payer is liable to bear the taxes and has paid such taxes	No Appeal 260A	No Appeal 260A

# Progress of Jurisprudence

Transmission Corporation of AP Ltd. 239 ITR 587 (SC)

1999

Once income is chargeable to tax, withholding on gross sum unless order obtained from AO



Samsung Electronics Co. Ltd. 227 CTR 335 (Kar)

2009

Obligation to withhold tax exists at all times, unless a 'nil' TDS order is obtained



GE India Technology Center 327 ITR 456 (SC)

2010

If the payment is not in the nature of income, no obligation to withhold tax

# Section 206AA

- ◇ Any person entitled to receive any sum on which tax is deductible under the Act
- ◇ Deductee furnish its PAN to the deductor.
- ◇ On failure in providing PAN, the deductor is required to withhold taxes at higher of the following rates:
  - ◇ **Rates provided under relevant provisions of the Act or**
  - ◇ **Rate or rates in force (i.e. rate provided under the Act or the tax treaty)**
  - ◇ **Rate of 20 percent**
- ◇ Applicable with effect from 1 April 2010.
- ◇ The above provision will be applicable to all payments made to residents / non-residents on which tax is required to be deducted under the Act.
- ◇ Further, the certificate for deduction at lower rate or nil rate of deduction shall not be given by the Assessing Officer (AO) unless the application bears PAN of the applicant / Deductee.

# Authority for Advance Rulings

## ◆ Who can apply?

- ◆ A non-resident
- ◆ A resident undertaking a transaction with a non-resident

## ◆ Who shall be the members?

- ◆ Retired judge of SC
- ◆ IRS officer, qualified to be a member of CBDT
- ◆ Officer of Indian Legal Services, qualified to be an Additional Secretary to the GOI

## ◆ Fees

- ◆ INR 10,000 at the time of application

## ◆ Binding nature

- ◆ Binding only on the applicant who sought it
- ◆ Commissioner, the income-tax authorities subordinate to him

## ◆ Time limit for disposal

- ◆ 6 Months



# Thank You

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