Payments to Non-residents

Practical Issues

Section 195

August 2012

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Setting the context

Importance of tax withholding

Significant growth in Indian economy due to inbound investments in the last two decades

Significant liberalization of Indian economy

Globalization of the world economy

Focused approach of the Tax Authorities on cross-border transactions

Technological revolution and emergence of e-commerce

Objective of Section 195

Circular No. 152 dt. 27-11-1974

- To insure tax is collected at the earliest point of time
- No difficulty in collection of tax at the time of assessment
- Avoiding loss of revenue as non residents may have no assets in India for subsequent recovery

XYZ, In Re: P.No.18 of 1995- 238 ITR 575

"the objective is to ensure, as best as possible, that the tax liability on the income element, on the amount paid is got deducted at source itself so that the department is not put to 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."

Section 195 – Chargeability

Section 195

Any person responsible for paying to a non resident…any interest or ***any other sum chargeable under the provisions of this Act*** shall…deduct income-tax thereon…

Applicability: Section 1

The Act applies to the ***whole of India*** and became effective from ***1 April 1962***

Charging Section: Section 4

Section 4 gives the ***authority*** *to* the government to ***charge Income-tax***

Scope of Total Income of NR: Section 5

- Income received or deemed to be received in India
- Income accrues or arises, or ***deemed to accrue or arise*** in India

Section 9 - Income deemed to accrue or arise

Chargeability to tax governed by provisions of Act or DTAA

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

** Apart from section 5, wherever applicable*

Act or DTAA, whichever is beneficial prevails [Section 90 (2) of the Act]

Overview of Section 195

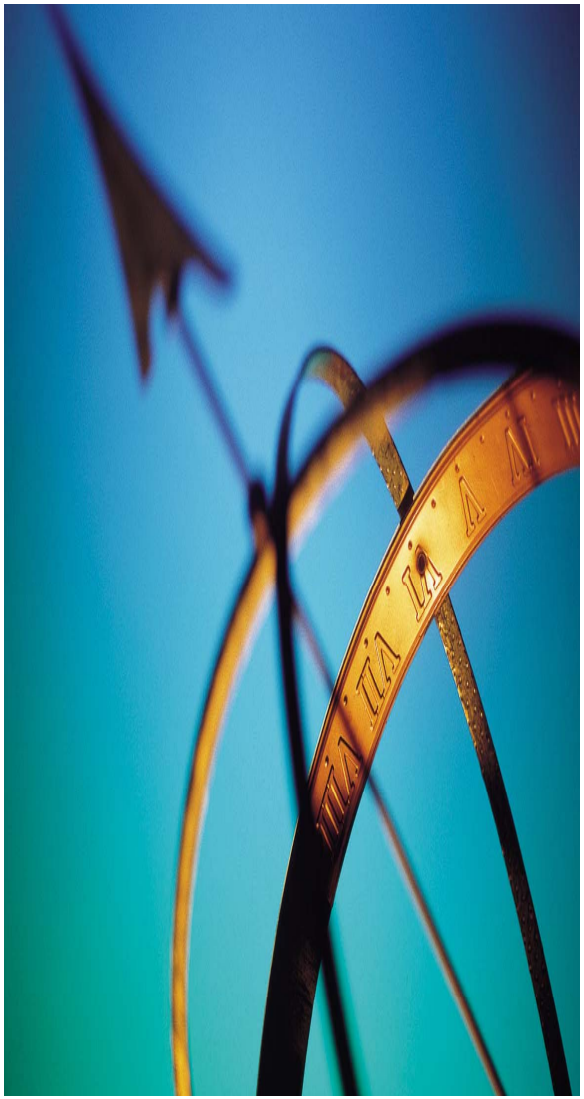
Section 195 – Typical characteristics

- Covers all sum except salaries; dividend as referred to in section 115O and interest* payments
- Deals with deduction of tax at source from payments to Non-residents and F Co.
- No threshold limit prescribed – tax deductible even on a negligible amount
- Tax on the gross amount or income element
- Option provided to approach the AO for determination of income element
- Tax treaty benefit available under section 2(37A)(iii) read with section 90A

** Inserted by Finance Act 2012*

Withholding tax not conclusive, subject to regular assessment

Amendments by Finance Act 2012



- Withholding tax provisions extended to non-residents, regardless of presence in India *(with retrospective effect from 1.4.1962)*
- Residency Certificate in prescribed form made mandatory for claiming Treaty benefits *(with effect from 1.4.2013)*
- Payer not to be considered as 'assessee in default' where the **resident** payee discharges the tax liability on the income, files the tax return and payer furnishes a certificate from accountant in prescribed form

  No disallowance on failure to withhold tax on payments made to resident payee where payer is not considered as an 'assessee in default'
- **Validation clause** – Clause 119 of Chapter VI of Finance Act 2012 provides for validation the proceedings under the Act and the tax levied, collection or imposed in respect of the tax on capital gains arising out of transactions which has taken place outside India

Section 195 – Provisions under the Act

Part	Section Provisions	
1	Section 195(1)	Liability of *'All persons*'* to deduct tax on amounts payable to non-residents / foreign company
2	Section 195 (2) / 195 (3) / 197	Certificate for deduction of tax at Nil / lower rate
3	Section 195 (6)	Certificate of Chartered Accountant
4	Section 195 (7)*	CBDT to notify persons or class of persons to refer matters to AO for determination of withholding tax liability
5	Section 195 A	Income payable "net of tax"
6	Section 206AA	Mandatory furnishing of PAN

(inserted in Finance Act 2012)*

Point of taxation and Rate in Force

Point of withholding

- **The Act:** Credit or payment whichever is earlier
- **Treaty:** "Royalty or FTS arising in a Contracting State and **paid** to a resident of the Other Contracting State may be taxed in that Other State.
- **Flakt (India) Limited [267 ITR 727] AAR** – Taxability adjudged from Treaty/Act, however **tax event** from Domestic provisions.

Rates in force

- **Rates specified in Finance Act or Rates specified in DTAA – whichever is beneficial** *(Section 2(37A)(iii))*
- **Rates under DTAA to be further increased by surcharge and Education Cess?**
  - DTAA uses term "Income-tax"
  - Income-tax includes surcharge and additional surcharge *(CIT v. K. Srinivasan [1972] 83 ITR 346 (SC))*
- **Tax to be deducted @ 20% on failure to furnish PAN** *(Section 206AA inserted w.e.f 1 April 2010)* – unilateral override of the Treaty?

Provisions of section 206AA

Section 206AA stipulates withholding *at higher* of following rates in case PAN of payee is not furnished:

- Rate specified in the relevant provisions of the Income-tax Act, 1961 (varying rates prescribed for different nature of payments); or
- Rates in force (as specified in the Schedule to the Finance Act; relevant tax treaties); or
- 20 percent.

Further, PAN to be quoted on all correspondence, bills, vouchers, etc. between payer and payee.

Section 206AA - certain issues

Applicability restricted to transactions where tax is deductible?
Timing for applicability of section 206AA?
Applicability on payments to non residents?
Overriding effect on tax treaties?
Grossing up and determination of income liable to tax in payee's hands in 'net of tax' contracts?
Levy of surcharge and education cess on maximum rate of 20 percent?

Section 195(2) - Application by Payer

Application by the Payer to the AO for determining appropriate portion of sum chargeable

Mandatory to approach AO?

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

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

Fact: Gross trading receipt with income element embedded therein

Section 195(2) – Income not taxable?

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

- **Obligation to withhold tax exists if the income is prima facie taxable, unless a 'nil' TDS order is obtained**

GE India Technology Center
327 ITR 456 (SC)

- **If the payment is not in the nature of income, no obligation to withhold tax or obtain TDS order**

1999 **2009** **2010**

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

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

Post Samsung decisions*

- **Liability to withhold tax does not arise where income is not taxable in India**

  Van Oord ACZ India (P) Ltd

  Prasad Production Ltd.

Procedure for lower withholding - a Snapshot

	195 (2)	195(3)	197
Overview	Payer having a *bonafide* belief that portion (not the whole amount) of any sums payable by him to **Non-resident** is not be liable to tax in India, may make an application to AO to determine taxable portion	Payee may make an application to AO for granting him with a certificate to receive an income without deduction of tax at source. On receipt of such certificate payer shall not deduct taxes till the certificate is valid from the payments made to such payee	AO may grant the certificate of “Nil” or “ Lower” withholding if he is satisfied that income of such non-resident payee is liable for Nil or lower tax
Application by	Payer	Non-resident Payee	Payee
Form	No specific format	Rule 29B - Forms 15C and 15D	Rule 28 - Form 13

Procedure for lower withholding - a Snapshot

	195 (2)	195(3)	197
Purpose	Whole or portion of such sum not chargeable to tax	Nil withholding	Lower / Nil Withholding
Certificate	AO to determine the *appropriate proportion* chargeable to tax and issue certificate accordingly	Rule 29B - Certificate issued by the AO	Rule 28AA - Certificate to be issued by AO
Appealable?	Appeal under section 248 only if tax deductible on income is borne by payer	No Appeal	No Appeal, revision u/s 264 can be done. *(Larsen and Toubro (2010) 326 ITR 514 (Bom HC))*

Application to AO for no deduction – Section 195(3)

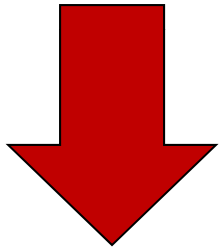
- **Payee satisfying <u>certain conditions</u> can make an application for receipt of any amount without deduction of tax at source**
- **Prescribed conditions provided in Rule 29B are:**
  - Has been regularly assessed to Income-tax in India and accordingly has furnished all the returns before the relevant due date
  - Not in default or deemed to be in default in respect of tax, interest, fine or any sum payable under the Act
  - Has not been subjected to penalty under section 271(1)(iii).
  - Additional conditions for Person other than banking companies
    - Has been carrying on business or profession in India **continuously** for at least 5 years; and
    - Value of Fixed Assets in India exceeds Rs 50 Lacs
- **Certificate issued by the AO valid for the Financial Year mentioned therein**

Above conditions are not required to be satisfied for application by payee under Section 197

Section 195(6) – CA Certificate

Section 195(6) introduced by Finance Act 2008 (w.e.f. 1 April 2008)

Requires the person making payment to NR to furnish the information relating to payment



Furnishing of information - Rule 37BB (w.e.f. 1 July 2009)

- Furnish information to the tax department - Form 15CA
- Obtain CA certificate before making payment to NR - Form 15CB

Procedure - Form 15CA and 15CB

Remitter

Obtains certificate from Accountant (Form 15CB)

Electronically upload the remittance details in Form 15CA on www.tin-nsdl.com

Take printout of filled undertaking form (15CA) with system generated acknowledgement number

Printout of the undertaking form (15CA) is signed

Submit the signed paper undertaking form to the RBI/ AD along with certificate of an Accountant in duplicate

RBI/ AD remits the amount

A copy of undertaking (15CA) & Certificate of Accountant (15CB) forwarded to AO

- Applicable only for remittance purposes
- Not a conclusive proof
- Every remittance required to follow procedure even if not chargeable to tax in India
- Requires the payer to provide PAN of the non resident
- Form 15CB need not be filed with the tax department – information requirement is same as Form 15CA

Practical Issues

NR to NR Payments

NR to NR payments for offshore transactions covered under the ambit of Section 195?

Section 1(2) extends to 'whole of India'. Arguably, such payments should not attract provisions of section 195.

- **Vodafone International Holdings B.V.** (SLP No 26529 of 2010); held that
  - Question of withholding tax would not arise on offshore transfer between the two non-residents not liable to capital gains tax in India
  - For the purposes of Section 195 of the Act, tax presence has to be viewed in the context of the transaction that is subjected to tax, and not with reference to an entirely unrelated matter

Section 195 applies if income chargeable to tax in India

- **Satellite Television Asian Region Ltd (**99 ITD 91 ITAT Mum)
- **AAR Ruling – Bechtel (P No 13 of 1995, 225 ITR 487)**

Finance Act 2012 – Explanation introduced in Section 195

Clarified that liability for deducting tax at source applies to all persons, resident or non resident, regardless of existence of business connection or taxable presence.

After Vodafone….

Vodafone Wins $2 bn Tax Case in Supreme Court

January 20, 2012

Supreme Court held that Indian Tax authorities have no basis to tax the sale of indirect interests held in the Indian Company

Major Transactions impacted by such retrospective amendments

- Mitsui – Vedanta deal – Sale of 51% in Sesa Goa to Vedanta
- SABMiller's acquisition of 100% stake in Fosters India
- Sanofi Aventis' acquisition of majority stake in the Indian vaccine company Shanta Biotech
- Kraft – Cadbury takeover deal

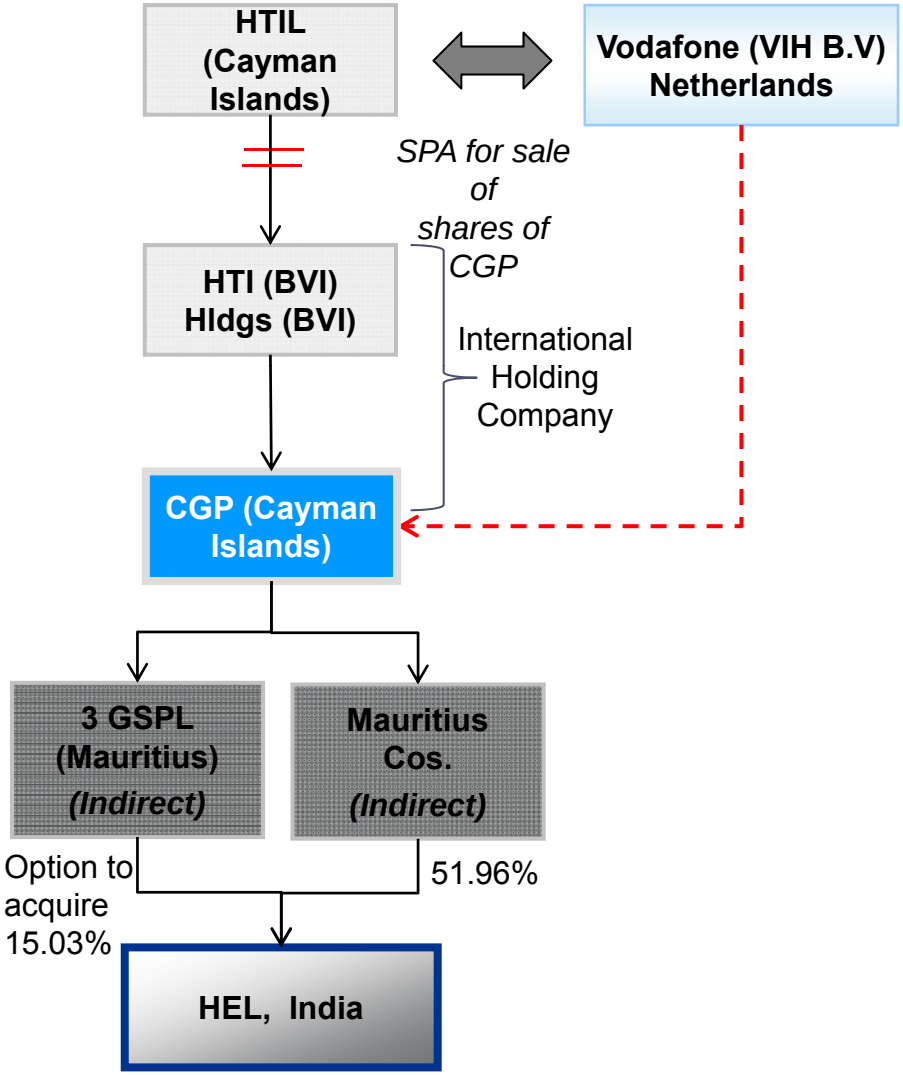
Dampened Enthusiasm for International Investment in India

Finance Act 2012- India Imposes Tax on indirect transfer of Indian assets

May, 2012

- India makes retrospective changes to the law that would effectively reverse the decision of the Supreme Court in the Vodafone case
- Allows India to tax non-residents on gains arising from the disposal of share or interest if such share or interest derives its value "substantially" from Indian assets
- A validation clause has been introduced to legitimise recovery of tax on such indirect transfers (Clause 119 of the Finance Act)
- Withholding tax obligation to extend to all persons, resident or non-resident, irrespective of the presence of non-resident in India

Vodafone: The Transaction



The Transaction

In February 2007, VIH B.V acquired 100% shares in CGP Holdings, Cayman Islands for USD 11.1 billion from HTIL

CGP through various intermediate companies/contractual arrangements controlled 67% of HEL, India

The acquisition resulted in VIH acquiring control of CGP and its downstream subsidiaries including HEL

HEL was a joint venture between Hutchinson Group & Essar Group

Vodafone: Background

2006-2007

- Open offer made by Vodafone for HTIL's stake in HEL
- VIH gave binding offer for acquiring entire shareholding in CGP
- VIH entered into SPA with HTIL through which VIH would own 42% direct interest in HEL. Through CGP it would own indirect interest in HEL

September 2007

- Notice was issued by the Tax Authorities to VIH for failure to withhold tax u/s 195 on payment made to HTIL indirectly
- Notice also included claim that VIH be treated as agent of HTIL u/s 163

October 2007

- Writ Petition filed stating that the Tax Authorities do not have jurisdiction over sale of shares between two non-residents
- Claimed it to be Not-Taxable in India

December 2008

In relation to the petition filed, the Bombay High Court held that the tax authorities had made out a *prima facie* case that the transaction was one of transfer of capital asset situated in India

January 2009

- In response to Writ filed with Supreme Court, the Supreme Court directed the tax to first determine the jurisdictional challenges raised by Vodafone
- It also permitted Vodafone to challenge the decision of the tax authorities on the preliminary issue of jurisdiction before the High Court

September 2010

- Bombay High Court dismissed petition of VIH
- Vodafone files appeal with Supreme Court
- Supreme Court directs Vodafone to discharge tax demand of INR.2500 crores
- ***3 member bench led by Chief Justice of India pronounced order with majority in favor of Vodafone on 20th January 2012***

Vodafone: Key Issues & SC Observations

Presently, indirect transfer of an asset in India is not Taxable under the Income Tax Act

Key Issues	SC Observations
Whether any source of Income or Capital Asset said to be situated in India?	Section 9(1)(i) of the Income Tax Act ("IT Act") does not have 'look through' provisions, and it cannot be extended to cover indirect transfers of capital assets/ property situated in India
Whether transfer of rights is incidental to a share transfer and only the situs of such shares should prevail?	The situs of the shares would be where the company is incorporated and where its shares can be transferred. A controlling interest is an incident of ownership of shares, which flows out of the holding of shares and hence is not an identifiable or distinct capital asset independent of the holding of shares
Whether Courts can lift the corporate veil in the absence of any look through provisions in the law or in the absence of a fraud?	Interposing foreign holding / operating companies is a common practice. Before lifting corporate veil, transaction should be looked at in a holistic manner viz. time duration for which the holding structure exists, period of business operations in India etc

Contd…..

Vodafone: Key Issues & SC Observations

Key Issues	SC Observations
Whether the sale of CGP share can be said to be a transaction which was designed to avoid tax in India?	Sole purpose of CGP was not only to hold shares in subsidiary companies but also to enable a smooth transition of business. Therefore, it could not be said that CGP had no business or commercial substance
Does section 195 have extra territorial jurisdiction?	Applies only to payments made from a resident to a non-resident
Whether India Mauritius treaty would be applicable where Vodafone had divested directly at Mauritius level?	In the absence of LOB clause and presence of CBDT circular 789 of 2000 and TRC, tax department cannot deny benefits of treaty to Mauritius Cos. TRC can be ignored if treaty is abused for the fraudulent purpose of tax evasion

Supreme Court ruled that the transaction was structurally valid and the tax authorities in India had no jurisdiction to tax such an overseas transaction

Finance Act - Rewrites legislation retrospectively

Non-residents are liable to tax on indirect transfers of Indian assets, including transfers of shares in companies which derive their value "substantially from assets located in India", and covering transfers back to 1 April 1962...

Key Amendments	Key Impact
'Capital Asset' to include management & control rights	Transfer of shares (at any level) which result in transfer of controlling interest of an Indian Company could give rise to a taxable event in India
'Transfer' to include parting with or creation of right, notwithstanding that such transfer flows from transfer of shares of an offshore entity	Transfer would now include indirect transfer of shares if rights in such shares are effected and dependent upon transfer of shares even of a foreign company
Scope of term 'through' clarified to include 'by means of', 'in consequence of', or 'by reason of'	Widens the scope of taxation of income under Section 9 of the ITA and bring into tax net, the gains derived from transfer of share or interest if such share or interest derives either directly or indirectly its value substantially from assets located in India
Witholding tax provisions applicable to non-residents irrespective of residence/ place of business/ connection in India	The amendment widens the withholding tax provisions of Section 195 of the ITA by applying it to all persons whether resident or non- resident

Finance Act - Rewrites legislation retrospectively

Key Amendments	Key Impact
Retrospective Amendment applicable from 1962	Despite the fact that the law is amended retrospectively from 1961, the Revenue authorities can go back only 7 years to initiate proceedings against a company. In other words, only transactions from 1 April 2005 will be open to scrutiny after 31 March 2012, unless proceedings have already been initiated in the past.
Tax authorities allowed to issue notice to examine the taxability in India, of income arising in respect of "Financial interest in an entity" located outside India for an extended period of sixteen years	This amendment could enable the tax authorities to reopen cases for the aforesaid extended period.

Clarification Provided by CBDT

- The Central Board of Direct Taxes ("CBDT") has issued clarification with regards to the reopening of completed assessments on account of clarificatory amendments introduced by the Finance Act 2012 viz. Section 2(14), Section 2(47), Section 9 and Section 195 with retrospective effect
- The Board has directed that in case where assessment proceedings have been completed under section 143(3) of the Act, before 1st April 2012, and no notice for reassessment has been issued prior to that date, then such cases shall not be reopened under section 147/148 of the Income Tax Act on account of the abovementioned clarificatory amendments introduced by the Finance Act, 2012`

Finance Act - Rewrites legislation retrospectively

Clarifications Required……

- No threshold defined to determine what constitutes “substantial” with regards to taxing offshore transfers with substantial asset base in India
- Computation mechanism not prescribed
  - Taxability based on the proportion of the value of the India business to the global value
  - Whether gross or net value of India assets to be considered?
- Applicability of Treaty provisions?

Fees for Technical Services

'Make available' concept

- Some of India's tax treaties with other countries, have the 'make available' clause under FTS article
- The 'make available' clause narrows down the definition of FTS i.e. if the services do not "make available" technical knowledge, etc., then, they are outside the ambit of Article on FTS, hence not taxable
- Accordingly, it is possible to argue that withholding tax under section 195 should not apply *(CIT v. GE India Technology Cen. (P.) Ltd. (SC) - [2010] 327 ITR 456)*

- **Bharati AXA General Insurance Co. Ltd** *(AAR No. 845 of 2009)*
- **Ernst & Young (P) Limited ('EYPL')** *(AAR No. 820 of 2009)*
- **Intertek Testing** *(307 ITR 418)*
- **Anapharm Inc** *(305 ITR 394)*
- **De Beers India Minerals Pvt Ltd** *(Kar HC) (ITA No. 549 of 2007)*

In all the above cases, since services did not 'make available' technical knowledge - held to be outside the purview of FTS, hence not taxable.

…Fees for Technical Services

- **Perfetti Van Melle Holding B.V.** *(AAR no 869 of 2010)* – held that 'specified services' are inextricably linked / attached to Trademark License and Know-how agreements from which consideration is flowing in the form of taxable 'Royalty', hence taxable.
- **Shell India Markets Pvt Ltd** *(AAR no 833 of 2009)* – held that payment received by SIPCL is chargeable to tax in India as the employees of applicant are continuously supported and advised by SIPCL.
- **Mersen India Private Limited** *(AAR No 774 of 2010)* – Make available clause interpreted for 'Managerial services' in light of MFN clause in India-France DTAA, held taxable

- **Conflicting Decisions**
- **Aggressive position by Revenue Authorities**

Withholding tax implications on Technical services *not making available* technical knowledge??

Reimbursement of Expenses

Cost to Cost reimbursement does not attract TDS – Key Principles

- There should be direct nexus between the actual cost incurred and amount reimbursed
- There should be no element of profit embedded in the payments so made
- Payment made should be for pure reimbursement of expenses and not for rendering services

No TDS on cost allocation/Reimbursements

- Ernst & Young (P) Ltd vs. Commissioner of Income tax, Kolkata [2010-TIOL-18-ARA-IT]
- ABB Limited vs. Commissioner of Income tax, Bangalore [2010-TIOL-16-ARA-IT]
- M/s Invensys Systems Inc. vs. Director of Income tax (International Tax), Chennai [2009-TIOL-21-ARA-IT]
- CIT v. Dunlop Rubber Co. Ltd. [1983] 142 ITR 493 (Cal) -

TDS on cost allocation/ Reimbursements

- Mahindra and Mahindra Ltd. v DCIT [2009] 313 ITR 263 (Mum SB)
- CSC Technology Singapore Pte Ltd (Del ITAT) – ITA No. 5604/Del/2010
- Timken India Ltd. 193 CTR 610 (AAR)
- Danfoss Industries (India) Ltd., In re [2004] 268 ITR 1 (AAR)

Reimbursement of salary of Deputed employees

Reimbursement to non-resident of salaries of the foreign technicians seconded to Indian co's operations as employees

Reimbursement <u>considered not</u> taxable:

- *DIT v. HCL Infosystems Ltd. [2004] 274 ITR 261 (Del) – section 192 v. 195*
- *Cholamandalam MS General Insurance Co. Ltd. In re [2009] 309 ITR 356 (AAR)*
- *IDS Software Solutions India (P) Ltd. vs ITO [2009] 122 TTJ 410 (Ban)*

Reimbursement <u>considered</u> taxable:

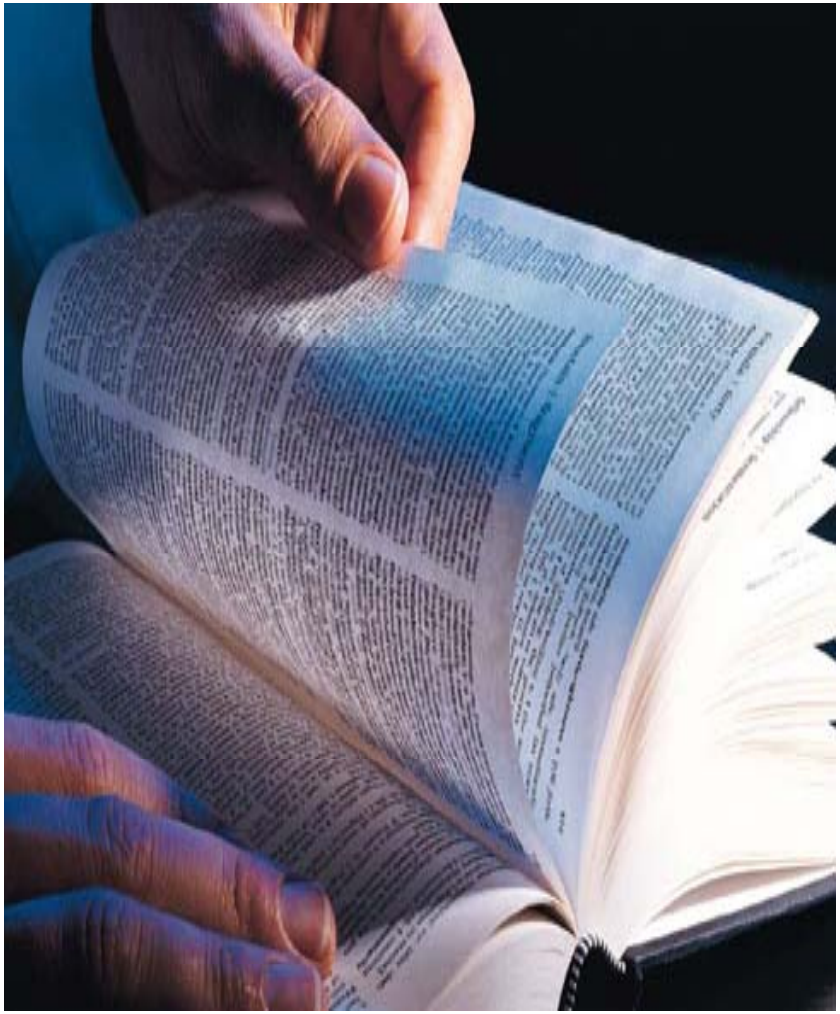
- *Centrica India Offshore Pvt Ltd (AAR)*
- *Verizon Data Services India Private Limited (AAR)*
- *AT & S India (P) Ltd. v. CIT [2006] 287 ITR 421 (AAR)*

Transactions having some linkage with 'Provision of services' likely to fall under tax net….

Software Taxation

Payment for supply of shrink wrap software is not royalty:

- Consideration is not for the use of the copyright but for the use of a copyrighted article
- No right given to the buyer to commercially exploit the software such as right to make copies or sub-license the software
- Software when put onto a media (like CD) and sold becomes goods like an audio cassette or book
- No royalty where the purchase is an integrated purchase, inextricably linked to the hardware



Software Taxation – Conflicting decisions

- Ericsson *(2011) 16 taxmann.com 371 (Del HC)*
- Novell Inc v. DDIT *(2011) 16 taxmann.com 186 (Mum ITAT)*
- Motorola Inc*, (95 ITD 269)(Delhi SB)*
- ADIT v. Tata Communications Ltd. *(ITA 1473/Mum/2009)*
- Dassault Systems K.K. *[2010-TIOL-02-ARA-IT]*

- Samsung Electronics *(2011) 16 taxmann.com 141 (Kar HC)*
- Millennium IT Software Ltd. *(2011) 14 taxmann.com 17*
- Sunray Computers *(2011) 16 taxmann.com 268 (Kar HC)*
- CIT v. Synopsys International Old Ltd *(Kar HC)*
- Acclerys KK, In re *(2012-TII-10-ARA-INTL)*
- Citrix Systems Asia Pacific Pty. Ltd*. (AAR)*
- Microsoft Corporation vs. ADIT *(2010-TII-141-ITAT-DEL-INTL)*

Copyright Vs Copyrighted Article???

Software Taxation – Amendment in Finance Act 2012

Expansion of Royalty definition retrospectively w.e.f. AY 1977-78

- **Explanation 4 added to s. 9(1)(vi)**
  - *For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a **computer software** (including granting of a license) irrespective of the medium through which such right is transferred*

- **As per Memorandum to Finance Bill**
  - *Some judicial decisions have interpreted this definition in a manner which has raised doubts as to whether consideration for use of computer software is royalty or not …. **Considering the conflicting decisions of various courts in respect of income in the nature of royalty and to restate the legislative intent, it is further proposed to amend the Income-tax Act ….***

Controversies put to rest by the amendment with retrospective effect…
Question continues on payments made in past without withholding taxes???

Satellite/Transponders payment

Conflicting Decisions

- Asia Satellite Telecommunications Co Ltd *(2011) 332 ITR 340 (Del)*
- PanAmSat International Systems Inc *(2006) 103 TTJ 861 (Delhi) 8)*
- Raj Television Networks Limited *(IT Appeal Nos. 1827 and 1828/Mds./199)*
- ISRO Satellite Centre*, In re (2008) 307 ITR 59 (AAR)*

- Sanskar Info TV Pvt Ltd
- New Skies Satellite NV *[2009] 121 ITD 1 (Delhi)*
- Asianet Communications Ltd *(2010) 38 SOT 158 (Mad)*

Applicability of withholding tax on Transponder Payments???

Satellite/Transponders payment

Expansion of Royalty definition retrospectively w.e.f. AY 1977-78

- **Explanation 5 added to s. 9(1)(vi)**
  - *For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, **property** or information, **whether or not***

    (a) the possession or control of such right, property or information is with the payer;

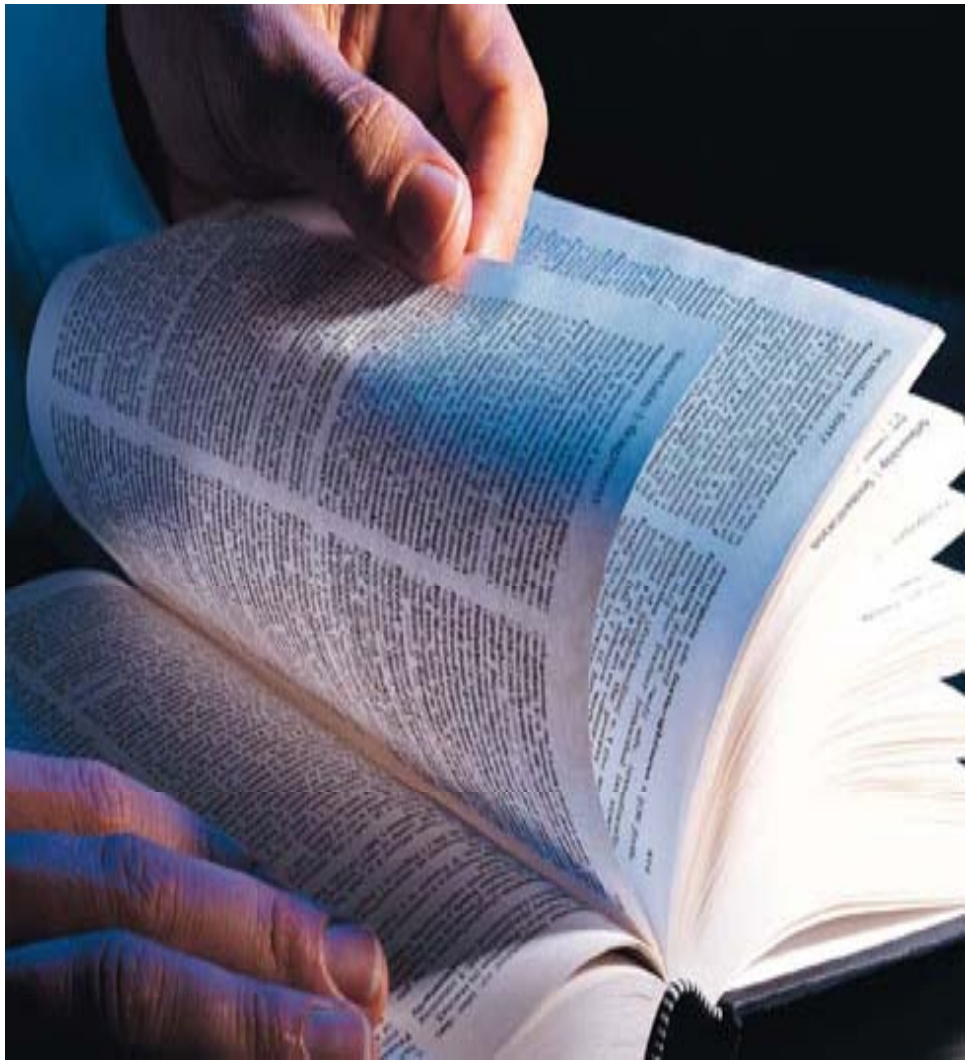
    (b) such right, property or information is used directly by the payer;

    (c) the location of such right, property or information is in India

- **Use of Process : Explanation 6 added to s. 9(1)(vi)**
  - *For the removal of doubts, it is hereby clarified that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret*

Ruling in Asia Sat case overturned…Transponder payments are now brought to the tax net…Withholding tax under 195 apply with retrospective effect

Implications



- Revision of tax returns
- Pending litigation at AO / CIT(A) / DRP / ITAT / AAR / HC / SC level
- To affect both residents (Sec 194J) as well as non-residents (Sec 195)
- Disallowance u/s 40(a)(i) in the hands of payer (or defaulting deductor)
- Liability of payee / deductee to pay interest u/s 234B.
- Liability of defaulting payer / deductor to pay interest u/s 201(1A)
- Recovery of withholding tax from defaulting payer / deductor u/s 201(1)

Amendment to section 90 and section 90A

- Where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act,
- but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued there under being in force, then,
- the meaning assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.

EPC Contracts

When the procurement and commissioning contract are covered by common contract – AO should be approached u/s 195(2) in view of Transmission corporation

- **DIT v L G Cables** (2011 – TII – 02 – HC – DEL – INTL) – Offshore supply of equipments will not be chargeable to tax in India merely if it is interlinked with the satisfactory performance of the on shore contract
- **Technip Italy SPA v ACIT** (Del ITAT) – Income from offshore supply contract under composite contract is not taxable in India

- **Linde AG, Linde Engineering Division** [2012] (AAR) – Consortium formed by applicant with another non-resident, for bidding for a turnkey contract, liable to be taxed as Association of Persons (AOP). Internal division of responsibility by Consortium members not to alter indivisibility of contract or formation of AOP. AAR relies on SC's observations in Vodafone ruling, rejects "dissecting approach" of assesssee. Hence, entire contract was taxable in India

Conflicting decisions…what should be our approach towards withholding tax???

Refund of Tax

Refund of tax in certain situations

Situations under which tax paid under section 195 can be refunded.

- Contract cancelled and remittance not made
- Remittance made, contract cancelled and amount returned
- Contract cancelled, partial execution in event of no or full remittance for non-executed part to the non-resident
- Exemption by amendment in law or notification under income-tax provisions
- Order passed under section 154/248/264 reducing tax deduction liability of the deductor
- Double deduction of tax by mistake
- Inadvertent grossing up of tax, not required under the Act
- Availability of benefit of lower rate under relevant DTAA

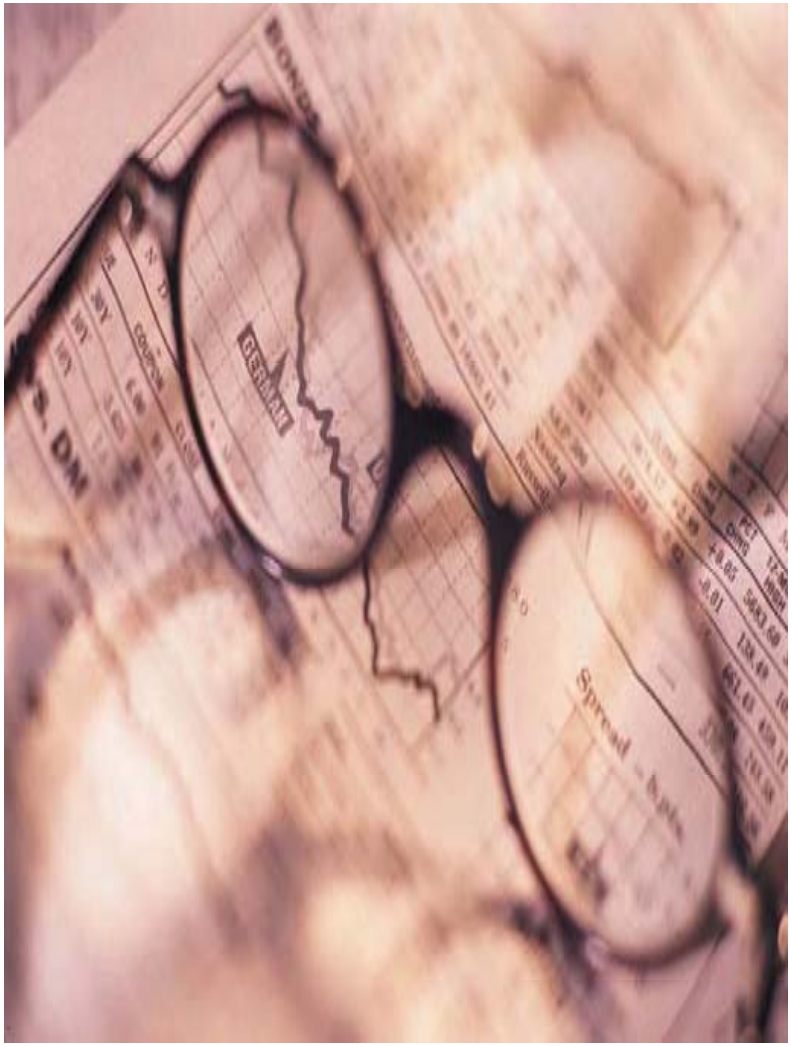
(Circular No. 790 dated 20 April 2000 as superseded by Circular 7/2007 dated 23 October 2007)

Other conditions:

- Undertaking from the Deductor that no TDs certificate has been issued to NR Deductee
- The Deductee has not filed the return of income and the time limit for filing tax return has expired
- If refund has been claimed by the Deductor, no deduction of corresponding expense should be allowed
- Claim should be made within 2 years from the end of the financial year in which tax is deducted

Net of Tax Arrangement

Net-off tax arrangements



- Section 195A – ‘Grossing up’, if tax borne by payer
- Tax payable at the appropriate rate on the aggregate of the costs paid plus the tax thereon
- Section10(6A) – tax paid by Indian company on the income derived by foreign company, shall not be treated as income of foreign company *(Hyderabad Industries Ltd Vs ITO 188 ITR 749 (Kar HC))*
- Payer to furnish certificate for the tax deducted at source to the payee within the prescribed time *- Circular 785 dated 29 Nov 1999*
- Payments in kind - Section 195 covers payments ‘by any other mode’

  (Kanchanganga Sea Foods Ltd v CIT [2010] 192 Taxmann 187 (SC))

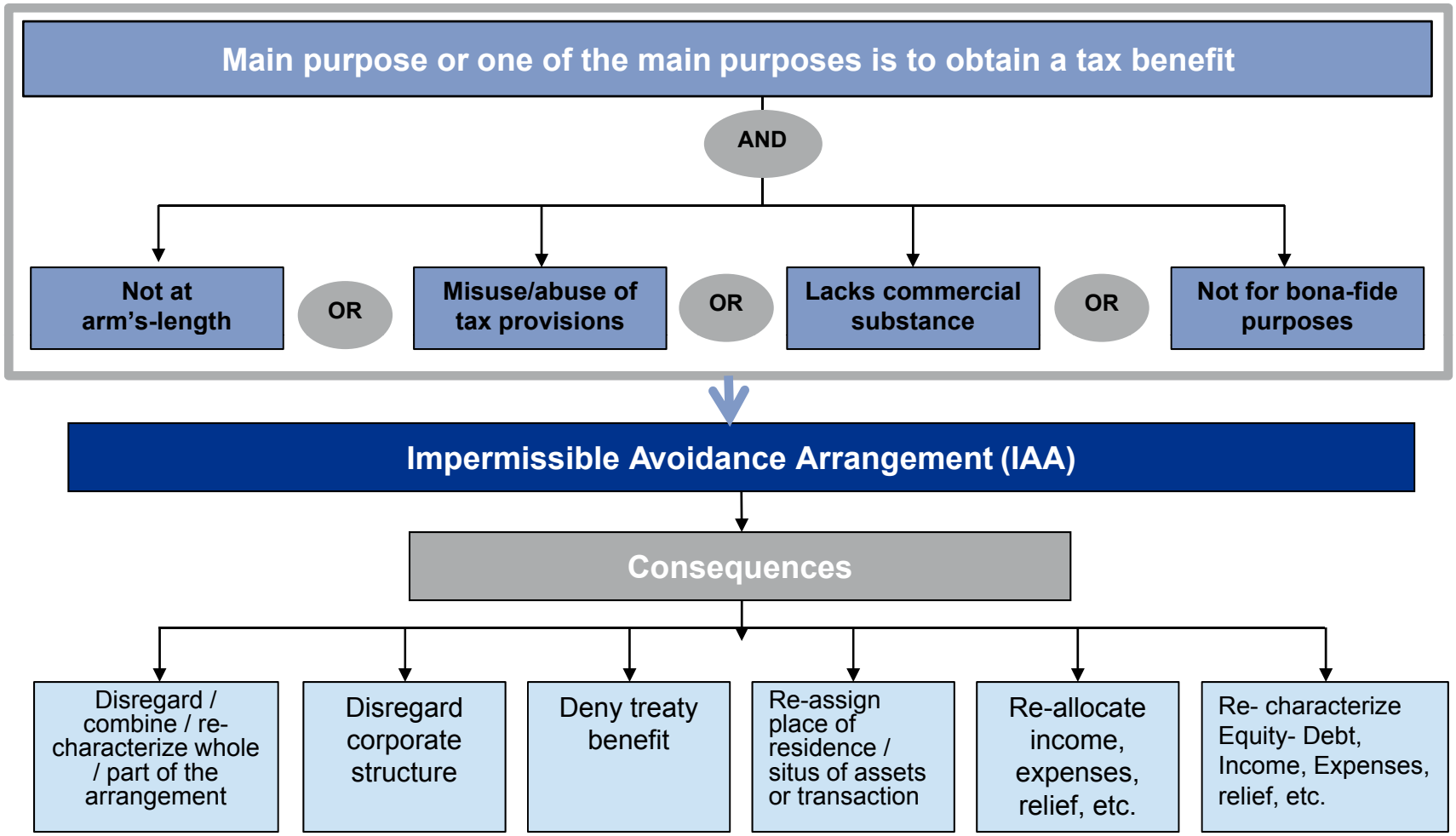
Consequences of Non-compliances

Consequences of Non-compliances

Consequence	Section	Quantum
Interest	201(1A)	Simple interest leviable @1.5 percent / 1 percent p.m. as applicable date tax was deductible to the date tax was paid
Penalty	221 / 271C	Amount equal to tax in arrear
Prosecution	276B	Failed to deposit tax without sufficient cause Rigorous imprisonment of minimum 3 months may extend to 7 years with fine
Disallowances	40(a)(i)	Disallowance of the sums paid on which tax deduction was required

GAAR Provisions

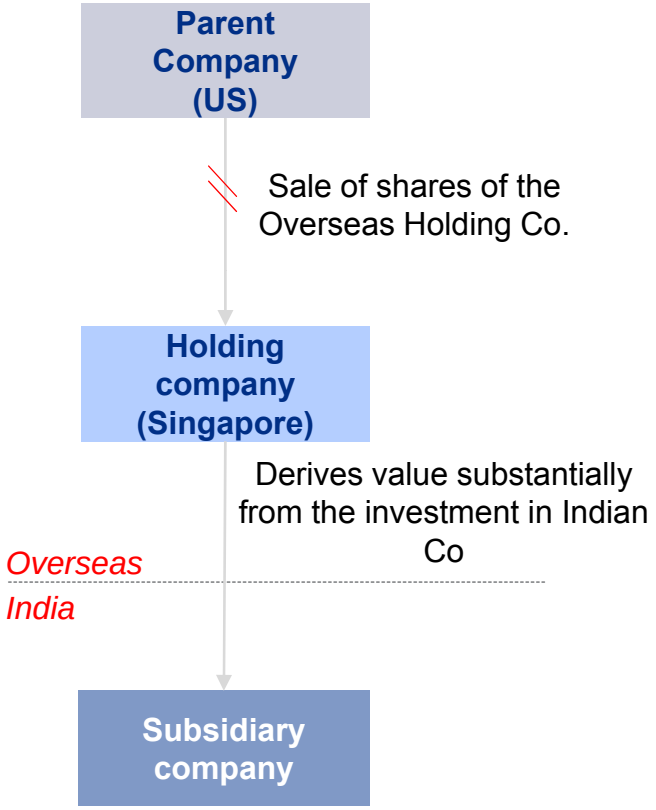
GAAR – Basic Provisions



Detailed guidelines to be prescribed – critical parameter

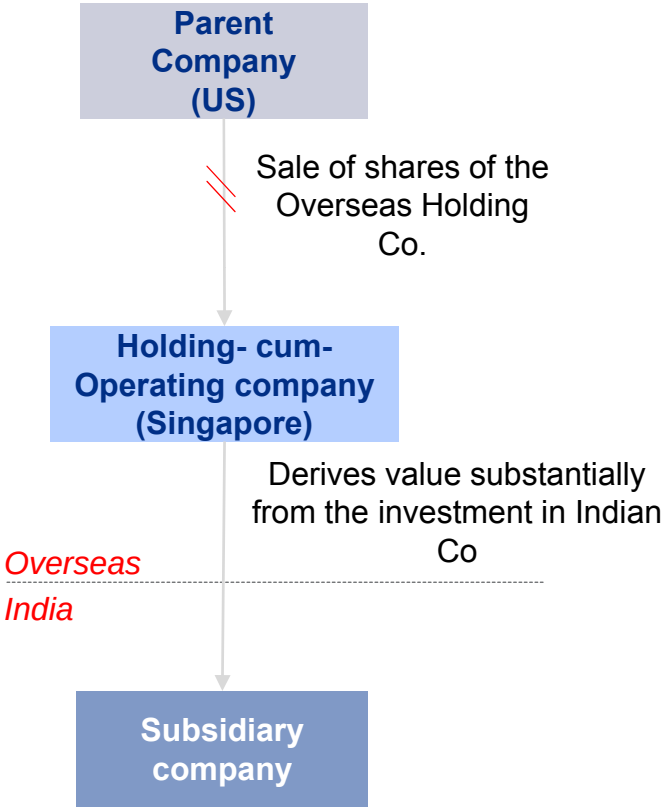
Indirect Transfers (*Diagrammatic representation)*

Earlier Provisions



Such share sale has been held not to be taxable by the SC based on the present interpretation of the law

Current Law



Such share sale is proposed to be made taxable in India subject to Treaty provisions

GAAR Provisions – (*Diagrammatic Representation*)

Key Takeaways

Key Takeaways

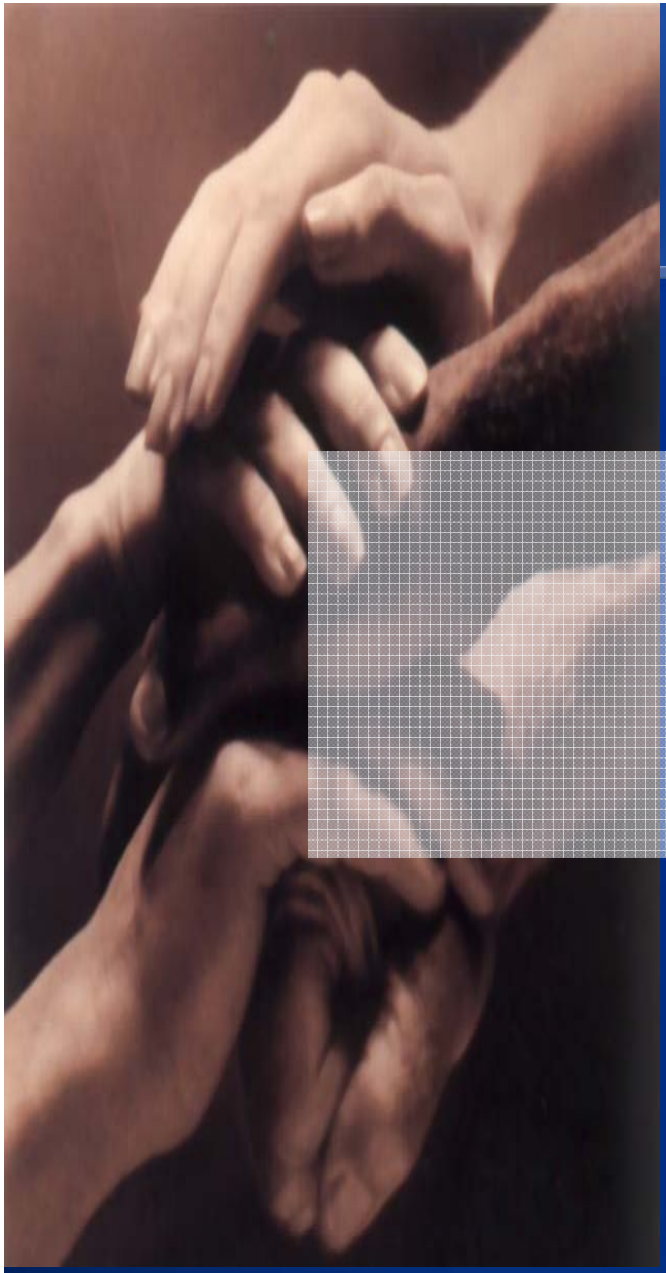
- **Non-residents payers are now brought to the tax net of Section 195**
- **TRC certificate made mandatory for availing treaty benefits**
- **Tax planning, investment structuring through Tax Havens are under the scanner of Tax Authorities**
- **Unlimited powers bestowed on AO by introduction of 'Validation clause' in the Finance Act 2012**
- **Availing tax benefits under treaty should be analyzed closely in the light of GAAR provisions to be applied**

Tax withholding from cross-border transactions is critical

Questions

&

Answers



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