

International taxation proposal of Finance Bill 2021

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Dividend Taxation

Benefit of treaty to FIIs

- Section 196D prescribed flat withholding rate of 20% (plus surcharge and cess)
- Unlike section 195, reference to 'rates in force' was missing resulting in TDS rate from 20.8% to 23.92% depending upon dividend income and categorization of FII
- Proviso inserted to section 196D providing possibility of considering treaty rate for withholding purpose
- Proviso requires satisfaction of both cumulative conditions:
 - Agreement referred to in section 90(1) [DTAA] applies to payee; and
 - Payee has furnished a certificate referred in section 90(4) [TRC]
- Both conditions needs to be satisfied, mere TRC will not suffice
- Amendment applies from AY 2021-22 **[retrospective]**

Benefit of treaty to FIIs

- Apparently, declaration under section 90(5) [Form 10F] is not required but said information will be required to mitigate rigors of section 206AA read with Rule 37BC
- Deductor will have to satisfy FII eligibility to DTAA. This will require consideration of following factors:
 - Treaty residency of FII
 - Satisfaction of GAAR, PPT, LOB test and other anti-abuse provisions
 - Beneficial ownership of recipient of income
- Whether obtaining declarations will meet the test of FII being eligible to treaty benefit?
 - Bombay High Court in Universal International Music in context of India-Netherland treaty held that TRC is sufficient proof of Beneficial Owner

Benefit of treaty to FIIs

- Pitfalls for payer
 - No amendment in section 201/201(1A) to exonerate payer from being assessee in default if payer is not able to prove treaty eligibility beyond declarations
 - Payer can be deemed to be representative assessee under section 163
- Treaty rate of popular FII jurisdiction

Particular	Mauritius	Singapore	Luxembourg	France	US	UK
DDT Rate	5%*	10%*	10%	10%	15%	10%

- FIIs receiving dividend income in Indian bank account held with custodians may be hit by Limitation of Relief provision of India-Singapore DTAA and may not be entitled to treaty benefit

Benefit of treaty to FIIs

- No withholding on dividend income paid to:
 - Central Bank of the United Arab Emirates, Abu Dhabi Investment Authority and Abu Dhabi Fund for Economic Development on account of Article 24 of India-UAE DTAA
 - Monetary Authority of Singapore pursuant to Article 22 of India-Singapore DTAA

Benefit of treaty to FIIs

- Treaty entered by India with few of the countries, i.e, Netherlands, France, Sweden, Switzerland, Hungary provides for application of MFN clause for reducing the withholding tax rate on dividend income, if a more favourable rate is provided in tax treaty entered with another OECD country post signing of the treaty
- Post signing of India-Netherlands treaty, India has signed treaty with OECD countries, Slovenia and Lithuania which provides for withholding tax rate of 5% on payment of dividend
- Accordingly, applying the MFN clause, possible to reduce dividend tax rate from 10% as provided in above treaties to 5% as per the treaty rate provided in tax treaty entered with Slovenia and Lithuania

Proposition is untested – from deductor perspective conservative view may be adopted

Benefit of treaty to FIIs

- Robust safeguards
 - Obtain valid TRC on date of dividend payout – difficulty may arise if COR gives TRC only on filing of tax return or dividend is paid in start of financial year of FII wherein issuance of TRC takes some time
 - Self certification covering:
 - Beneficial ownership of dividend
 - Satisfaction of PPT, GAAR, LOB test
 - No PE declaration
 - Declaration of residential status
 - SEBI FII registration certificate

Benefit of treaty to FIIs

➤ Amendment is effective from 1 April 2021 (AY 2021-22)

➤ Section 294 of the Act

“If on the 1st day of April in any assessment year provision has not yet been made by a Central Act for the charging of income-tax for that assessment year, this Act shall nevertheless have effect until such provision is so made as if the provision in force in the preceding assessment year or **the provision proposed in the Bill then before Parliament, whichever is more favourable to the assessee, were actually in force**”

➤ Should deductor rely on proposed law and grant treaty benefit for dividend proposed to be paid in Feb 21 and March 21?

TDS exemption to Business trust

- Exemption on TDS on dividend payment to REITS and InvITs
 - REITs and InvITS are trust registered under SEBI Act 1992
- Deductor to obtain documentation from REITs and InvITs registration with SEBI and declaration that they are governed by section 10(23FC)
- Amendment applies retrospectively from AY 2020-21
- Impact of retrospective amendment:
 - TDS is sunk cost as income of REITs and InvITS are exempt under section 10(23FC)
 - Can deductor listed companies be asked to refund tax withheld on strength of amendment by revising of TDS return?
 - Excess TDS paid can be adjusted against other payments

Relief in advance tax

- Section 234C provides for 1% interest in case of mismatch between installment of advance tax and actual tax
- Amendment proposed to insulate investor from interest levy by providing that interest will be applicable in case of mismatch between installment of advance tax and actual tax only after receipt of dividend income
- Shareholders having large portfolio receiving dividend from numerous company will have to keep detail records

Equalisation levy

Exemption under ITA

- FA 2020 expanded scope of EL provision by providing 2% tax rate on the amount of consideration received or receivable by an e-commerce operator from ecommerce supply or services made or provided or facilitated to specified person effective AY 2020-21
- Section 10(50) exempted above income from AY 2021-22. This raised apprehension on double levy i.e. taxation under Act as also EL provision
- FB 2021 removes this anomaly by providing exemption from AY 2020-21

Taxability under Act and EL

- Considering nature of levy, it is possible that same transaction may fall under Act as also EL provisions
- EL provided for 2% levy whereas taxability under Act was at higher rate. This created following apprehension:
 - Can assessee choose to be governed by Act or EL whichever is beneficial?
 - Whether income will be taxed under both legislatures?
- Explanation 1 to section 10(50) inserted to provide that income which is chargeable to tax as royalty or FTS in India read with DTAA shall not qualify for exemption under section 10(50)
- Thus, income in the nature of royalty or FTS which is taxable either under Act or DTAA is only excluded.

Taxability under Act and EL

- Section 163 of FA 2016 amended to provide EL provision shall not apply to income taxable as royalty or FTS either under Act or DTAA
- Thus, provision of Act will have preference over EL provision if income is taxable
- Partially allays fears on intra group services which on which tax was paid by NR in India either as royalty or FTS
- Arguably, amount taxed under Act should be excluded for computing de-minimus threshold of Rs 2 crs for levy of EL

Taxability under Act and EL

Section 10(50)

Income referred to in this clause shall not include and shall be deemed never to have been included any income which is chargeable to tax as royalty or fees for technical services in India under this Act read with DTAA

Comments

- Clarificatory amendment and retrospective from FY 2020-21
- Income in nature of royalty and FTS only covered by explanation
 - Other income in nature of SEP, business connection not excluded
- Precondition – ‘income which is chargeable to tax’ (see subsequent slides)
- End result to be seen on interpretation of Act and treaty

Possible situations

Situation 1: EL payment chargeable under Act and DTAA

- Exclusion in section 10(50) is for income in nature of royalty or FTS which is chargeable to tax under Act or DTAA. Similar scope exclusion provided in proviso to section 163
- Whether method of accounting followed by NR is of relevance?
 - Charge under section 163 of EL Act is on received or receivable i.e. accrual
 - Arguably, NR can offer income to tax in India on cash basis under Act
 - Exemption provided under section 10(50) is on income without making reference to 'received or receivable' method followed by NR should not be of any relevance

Possible situations

Situation 1: EL payment chargeable under Act and DTAA

- NR has to make its own assessment of chargeability to under Act or EL
- Position adopted by Deductor is irrelevant
- Software payment
 - Matter is before SC with conflicting decisions of High Court
 - Possible that deductor may be deducting tax and NR claiming refund waiting for SC decision
 - Failure to pay EL may invite interest 1% per month and levy of penalty

Possible situations

Situation 2: EL payment not chargeable under Act or DTAA

- Essence lies in meaning of words 'which is chargeable to tax' (see subsequent slides)
- Following payments may be subject to EL if otherwise requirement of EL provisions are met
 - Services which satisfies requirement of make available under various treaty (e.g. India – USA, India – Singapore, India – UK etc)
 - Consideration for rendering of construction, assembly, mining or like project undertaken by recipient [exclusion provided in Exp 2 to section 9(1)(viii)]
 - Issue will arise if such services are otherwise taxed under section 44AB. Exclusion provided is limited to royalty and FTS? Can in such case assessee pick and choose
 - Services utilised in respect of business or profession carried out by such person outside India or for the purposes of making or earning any income from any source outside India

Possible situations

Situation 2: EL payment not chargeable under Act or DTAA

- Following payments may be subject to EL if otherwise requirement of EL provisions are met
 - Services of following nature specifically exempt under select treaties (See Article 12(5) of India – US DTAA)
 - for services that are ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of property other than a sale described in paragraph 3(a)
 - for services that are ancillary and subsidiary to the rental of ships, aircraft, containers or other equipment used in connection with the operation of ships or aircraft in international traffic
 - for teaching in or by educational institutions
 - for services for the personal use of the individual or individuals making the payments
 - to an employee of the person making the payments or to any individual or firm of individuals (other than a company) for professional services as defined in Article 15 (Independent Personal Services)

Chargeable to tax

➤ **Black's Law Dictionary**

“Chargeable : This word, in its ordinary acceptance, as applicable to the imposition of a duty or burden, signifies capable of being charged, subject to be charged, liable to be charged or proper to be charged”

➤ **IMT Labs (India) (P.) Ltd., In re (2006) 157 TAXMAN 213 (AAR)**

“The expression "any other sum chargeable under the provisions of this Act" **would mean a sum on which income-tax is leviable. In other words, the said sum is chargeable to tax and could be assessed to tax under the Act.**”

➤ **Maharashtra State Electricity v. DCIT, (2004) 90 ITD 793 (Mum)**

“The expression 'chargeable under the provisions of this Act' cannot include an income, which in terms of the specific provisions of the applicable Double Taxation Avoidance Agreement, is not exigible to tax in India.”

Definition of ESS

E-Commerce supply or services

"e-commerce supply or services" means—

- i. **online sale of goods** owned by the e-commerce operator; or
- ii. **online provision of services** provided by the e-commerce operator; or
- iii. **online sale of goods or provision of services or both**, facilitated by the e-commerce operator; or
- iv. any combination of activities listed in clause (i), (ii) or clause (iii)

Explanation by FB 2021

Online sale of goods and online provision of services shall include one or more of following online activities:

- i. acceptance of offer for sale
- ii. Placing of purchase order
- iii. Acceptance of the purchase order
- iv. Payment of consideration
- v. Supply of goods or provision of services partly or wholly

Charge of EL

Charge of EL [Section 165A]

There shall be charged an EL at 2% of the amount of **consideration received or receivable** by an EOP **from ESS made or provided or facilitated by it:**

- Indian resident
- NR in respect of specified circumstances
- Person who buys goods or services using IP address located in India

Explanation by FB 2021

- Consideration received or receivable from ecommerce supply or services shall include –
 - Consideration for sale of goods irrespective of whether the e-commerce operator owns the goods
 - Consideration for provision of services irrespective of whether service is provided or facilitated by the e-commerce operator

Impact on NR to NR

Charge of EL [Section 165A]

- Specified circumstances -
 - Sale of advertisement which targets a customer who is Indian resident or customer who accesses the advertisement though IP address located in India **and**
 - Sale of data, collected from a person who is Indian resident or from a person who uses IP address located in India

Impact of amendment

- FB 2021 has amended ESS definition to expand scope of online sale and online services
- FB 2021 expanded meaning of consideration received or receivable
- No amendment in specified circumstances
- Threshold for EL continues same

Impact on NR to NR

Charge of EL [Section 165A]

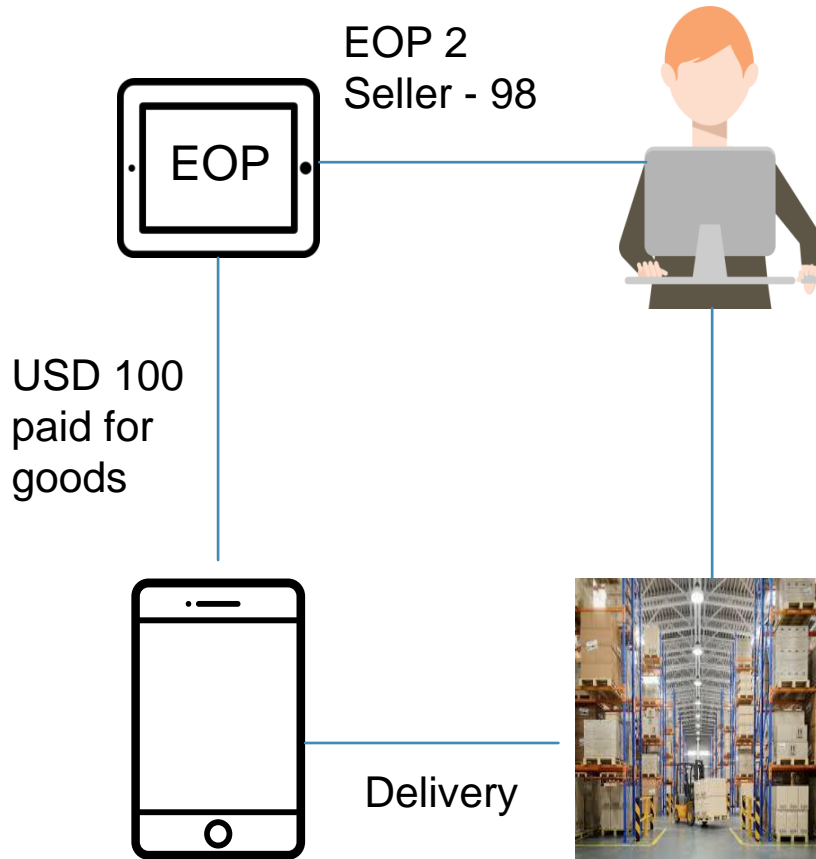
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Marketplace Model



Facts:

- User browses EOP app wherein various sellers have listed its produce
- User selects product, agree for delivery date and makes payment online
- EOP retains commission and makes payment to seller

Issues:

- Who is EOP in this case?
- Impact of amendment in ESS definition
- What is the consideration on which EL should be charged?

Marketplace Model

EOP:

- EOP means a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both
- Seller merely lists his products and does not have specified infrastructure to elevate itself to EOP

Amendment in ESS:

- Appropriate clause seems clause (iii) - online sale of goods or provision of services or both, facilitated by the e-commerce operator
- Amendment in ESS by FB 2021 will ensure that sale continues to be online if one of the specified activity is done online

Marketplace Model

Consideration for levy of EL:

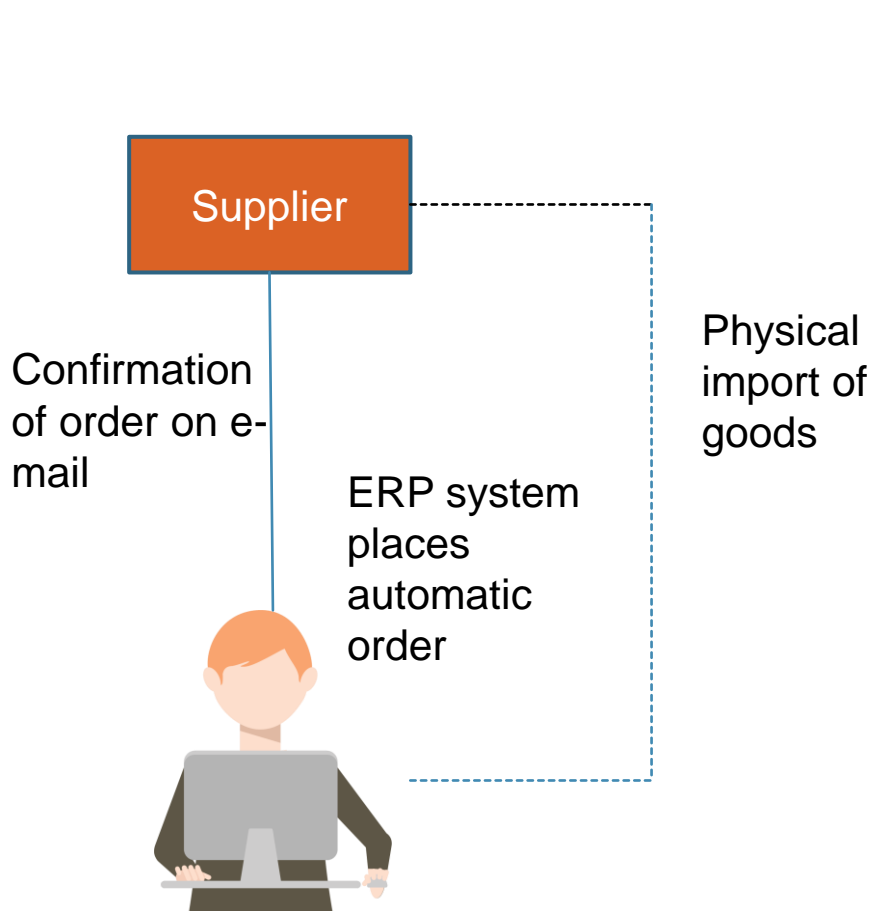
- Section 165A provides 2% levy on amount of consideration received or receivable by EOP from ESS made or provided or facilitated
- There are three limbs i.e consideration from ESS a) made or b) provided or c) facilitated
- Amendment by FB 2021 only deems to include “Consideration for sale of goods irrespective of whether the e-commerce operator owns the goods” (**Limb 1**). This is materially different from other clause “Consideration for provision of services irrespective of whether service is provided or facilitated by the e-commerce operator” (**Limb 2**)
- Unlike Limb 2, Limb 1 does not include words “irrespective of whether service (goods for Limb 1) is provided or facilitated by the e-commerce operator”

Marketplace Model

Consideration for levy of EL:

- Word 'from' in section 165A would indicate nexus or link between consideration and purpose for which consideration is received
- Words 'consideration received or receivable' by EOP would indicate consideration received by EOP is its own right and not something which he has to pass on to seller
- Since EOP is facilitating sales, can it still be said that consideration for levy of EL should be net?

Import of goods - distributor



Facts

- ICO is distributor of FCO
- Both adopts Just In Time inventory model
- Once inventory reduces a benchmark level, ERP system automatically places order

Issue:

- Is Supplier EOP?
- Whether transaction is subjected to EL – online sale of goods?

Definition of EOP

E-Commerce Operator (EOP)

"e-commerce operator" means a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both;

Online

"online" means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network

Analysis

- Words qualifying 'online sale of goods' and 'online provision of services' continues
- Amendment in ESS is only restricted for the purpose of section 165(cb) which defines e-commerce supply or services
- Can it be said that 'for' online sale would mean digital or electronic platform should be ment for online sale and not just for one of the activities now specified in amended ESS definition?

Hospitality industry



Online
Booking on
hotel website



Facts

- Mr A books hotel room online from India
- Hotel Co sends email for booking reservation
- Following payment made at the time of check-out
 - Room tariff (Based on online booking)
 - Dinning (not included in room tariff)
 - SPA and recreation (50% discount provided based on room tariff)

Issue

- Whether 'online sale' or 'online provision of service'?
- EL levied on what amount?

Liable to tax

Liable to tax

- Term 'liable to tax' is used in section 6, section 10(23FE) and various tax treaties entered by India
- Section 2(29A) inserted to define liable to tax as:

“The term liable to tax in relation to a person means that there is a liability of tax on that person under the law of any country and will include a case where subsequent to imposition of such tax liability, an exemption has been provided”
- Explanation 4 to section 90 provides where any term is not defined in DTAA but is defined in Act, it shall have same meaning as assigned to it in the Act
- Article 3(2) of permits reference to domestic law for undefined terms in treaty only when context otherwise requires

Treaty definition of residence

➤ Article 4 of UN Model 2017

“4(1) For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of incorporation, place of management or any other criterion of a similar nature, and also includes that State and any political sub-division or local authority thereof. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated t herein.”

Interplay with treaty

- For claiming residence under treaty following conditions needs to be satisfied:
 - First: Assessee is liable to tax under law of Resident State
 - Second: liable to tax is by reason of his domicile, residence, place of incorporation, place of management or any other criterion of a similar nature
 - Third: Deems State and any political sub-division or local authority as resident irrespective of whether it is liable to tax
 - Fourth: any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein
- Amendment only deals with first requirement and other requirement needs to be satisfied on standalone basis
- Thus, paying tax in COR which is not akin to residential based taxation (comprehensive tax liability) does not entitle NR to claim treaty benefit relying on section 2(29A)

Analysis of definition

- New provision requires analysis of domestic law of country of residence to reach conclusion whether NR meets requirement of liable to tax
- Liability to taxation is not the same as payment of tax. Liability to taxation is a legal situation; payment of tax is a fiscal fact [UOI v. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC)]
 - This interpretation seems to be intact in section 2(29A)
- Can TRC issued by government of resident state be implied approval that NR meets treaty requirement of liable to tax?
 - Circular 789 in context of India-Mauritius treaty

Analysis of definition

Situation
If there is no income tax in a country or even if there is an Income-tax Act, the individual is not covered by the said Act, he could not be treated as a resident of that country.
Meera Bhatia v. ITO [2010] 38 SOT 95 (Mum.)
ITO v. Rameshkumar Goenka [2010] 39 SOT 132 (Mum.)
DDIT v. Mushtaq Ahmad Vakil, 2010-TII-184-ITAT-DEL-INTL

Comments:

- Liable to tax as per section 2(29A)

Analysis of definition

Situation
Expression 'liable to tax' does not necessarily imply that the person should actually be liable to tax in the other country and that it is enough if other country state has right to tax such person, whether or not such a right is exercised
Cyril Eugene Pereira, In re (1999) 105 Taxman 273 (AAR - New Delhi);
Abdul Razak A. Meman, In re (2005) 146 Taxman 115 (AAR);
Gutal Trading Est, In re (2005) 149 Taxman 498 (AAR - New Delhi)

Comments:

- Not liable to tax as per section 2(29A)

Specific treaty residency rules

- Amendment will not impact cases where treaty specific rule of residency

India UAE DTAA: Individual and Companies

- An individual who is present in the UAE for a period or periods totalling in the aggregate at least 183 days in the calendar year concerned, and a company which is incorporated in the UAE and which is managed and controlled wholly in UAE

India – UK – Fiscally transparent entity

- in the case of income derived or paid by a partnership, estate, or trust, this term applies only to the extent that the income derived by such partnership, estate, or trust is subject to tax in that State as the income of a resident, either in its hands or in the hands of its partners or beneficiaries

Thank You

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