



International Taxation - IV

All India Chartered Accountants Society
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Agenda

Scope provisions

Significant economic presence

Source rules
Sub-clauses (v), (vi) and (vii)

Royalty

Fees for technical services

Equalisation levy

Ch. VIII of the Finance Act, 2016
as amended by FA 2021

Gifts

Sec 195, TRC and Form 10F

Scope provisions



Scope of total income

For residents [s. 5(1)]

Subject to the provisions of this Act, the **total income** of any previous year of a person who is **a resident** includes all income **from whatever source derived** which

- **is received** or **is deemed to be received in India** in such year by or on behalf of such person; or
- **accrues or arises** or **is deemed to accrue or arise to him in India** during such year; or
- **accrues or arises to him outside India** during such year

NOR exception

- **income which accrues or arises to him outside India shall not be so included unless it is derived from a business controlled in or a profession set up in India.**

For non-residents [s. 5(2)]

Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which

- **is received** or **is deemed to be received in India** in such year by or on behalf of such person; or
- **accrues or arises** or **is deemed to accrue or arise to him in India** during such year

Received, accrue and arise

- Received
 - Only an income receipt
 - The word relates to **first receipt after accrual** of income [*Kamdar (1946) 14 ITR 10 (Bom)*, approved in *Keshav Mills (1953) 23 ITR 230(SC)*]
 - The recipient gets the money under his control
 - Cannot be received more than once [*Keshav Mills (1953) 23 ITR 230(SC)*]
 - Include accrual and **constructive receipt**
 - Adjustment of cross-claims, settlement in account, an exchange effected by a book entry, or a set-off [*Arunachalam 1 ITC 75*]
- Accrue and arise
 - ‘Accrue’ and ‘arise’ not synonymous; used in contradistinction to the word ‘receive’ and indicate a right to receive [*Roger Pyatt Shellac 1 ITC 363*]
 - Accrual **requires a debt to be created** in favour of the assessee by somebody, **a right to receive that is legally enforceable**
 - Arise means (income) coming into existence, or notice or present itself
 - ‘Accrual’ could be notional while ‘*arising*’ is factual, later event [*KNB Inv. 367 ITR 616 (AP)*]

Deemed accrual or arising in India

- **Deeming place of accrual** to be in India
 - Does not deem income to accrue or arise
- Clauses (i) to (viii)
- Applies to both residents and non-residents
- Not relevant where income accrues or arises in India
 - *Mustaq Ahmed (2008) 307 ITR 408 (AAR), Rajiv Malhotra (AAR)*

Business connection, in the classical sense

9(1) The following incomes shall be deemed to accrue or arise in India :—

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

- Business Connection not defined in the Act
- Judicially explained [*R. D. Aggarwal & Co. (1965) 56 ITR 20 (SC)*]
 - Relation between NR's business and some activity in India
 - A real and intimate relation between activity outside and activity inside India – the relation between the two contributing to the earning of the income by NR
 - Implies repeated, continuous activities, occasional activities not covered.
 - Readily established if there exists an element of agency between NR and India

Business connection - Exclusions

- Income only to the extent reasonably attributed to business operations in India
 - Apportionment for operations within India and without – based on economic principles [*Anglo-French Textile Co. (1954) 25 ITR 27 (SC)*], *Ahmedbhai Umarbhai & Co (1950 18 ITR 472 (SC))*
 - Purport of Explanation 1(a)?
- Income from purchase of goods for exports
 - Not excluded – income from
 - Purchase for sale in India
 - Purchase activities in India - for purchase of goods from outside India
 - Purchase of services – not expressly mentioned in exclusion
- Income from collection of news in India for transmission outside India by news agency
- Income from shooting cinematograph films in India
- Income from displaying uncut and unassorted diamonds in specified zones

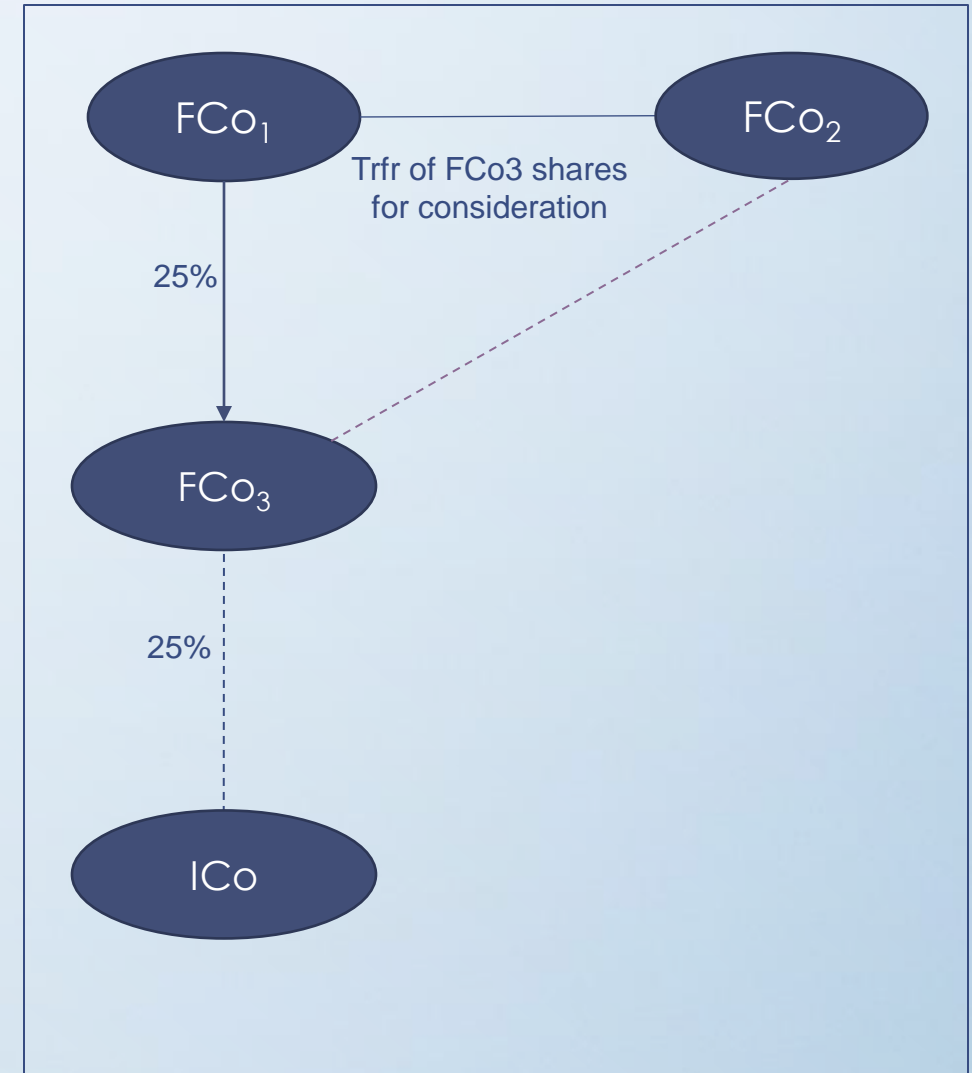
Indirect transfers

9(1) The following incomes shall be deemed to accrue or arise in India :—

(i) **all income accruing or arising**, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or **through the transfer of a capital asset situate in India**.

Explanation 4.—.....the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

Explanation 5: For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be **deemed to have been situated in India**, if the share or interest derives, directly or indirectly, its **value substantially from the assets located in India**:



Indirect transfers – case study

Indirect transfer provisions [sec. 9(1)(i)]

- If FCo₂ shares derive value substantially from assets located in India [Expln 5]
- If assets located in India represent at least 50% of value of total assets on a specified date
 - Preceding year-end date or date of transfer if book value of assets >15%
- Taxable gains -only such part as reasonably attributable to assets located in India [Expln 7(b),rule 11UC]

Specified date	On last day of preceding FY	On date of transfer
Ico FMV	40	40
Add: borrowing	30	0
Total assets	70	40
FCo ₂ share (25%)	17.5	10
FCo₂ FMV	19	19
Add: borrowing	5	5
Total assets	24	24
Income attributable to assets in India(r 11UC)	73%	42%

Assets of ICo	Preceding year-end	On trfr date
Factory land and building	30	30
Liquid assets	40	10
Borrowings	30	0
FMV of ICo	40	40

Assets of FCo ₂	Preceding year-end	On trfr date
Shares of ICo	10	10
Other foreign assets incl. IP	10	10
Liquid assets	4	4
Borrowings	5	5
FMV of FCo ₂	19	19

Under Treaties-

- *No taxing right generally for Source State for gains from Indirect transfers (unless real property co. shares)*
- *MLI Article 9 – 365-day Look-back rule*

Significant economic
presence



BEPS – the road traveled

- Action 1 – Address the tax challenges of the digital economy

*Identify the main difficulties that the digital economy poses for the application of existing international tax rules and develop detailed options to address these difficulties, taking a holistic approach and considering both direct and indirect taxation. Issues to be examined include, but are not limited to, **the ability of a company to have a significant digital presence in the economy of another country without being liable to taxation due to the lack of nexus under current international rules**, the attribution of value created from the generation of marketable location relevant data through the use of digital products and services, the characterisation of income derived from new business models, the application of related source rules.....*

- Action 1 Report (July 2014)

*The Task Force discussed and analysed a number of potential options proposed by delegate countries to address these challenges. **Options discussed** regarding nexus and data in particular range from changes to the definition of PE to the **introduction of a new nexus based on a “significant presence” in a market**, and also include the introduction of a withholding tax on sales of digital goods and services. (Conclusions, on page 158)*

BEPS – the road traveled

- Action 1 Report (2015) – a ‘potential’ option

*This option would **create a taxable presence in a country** when a non-resident enterprise has a significant economic presence in a country **on the basis of factors that evidence a purposeful and sustained interaction with the economy of that country via technology and other automated tools.** These factors would be **combined with a factor based on the revenue derived from remote transactions into the country**, in order to ensure that only cases of significant economic presence are covered, limit compliance costs of the taxpayers, and provide certainty for cross-border activities.*

- Revenue not sufficient in isolation to establish a nexus; **to be combined with-**
 - **digital factors** (local domain name, local digital platform, local payment options) and
 - **user-based factors** (monthly active users, online contracts, data collected)
- A **link required** between the revenue-generating activity of the NR enterprise and its SEP in a country.

Intangible business connection

- *Volkswagen Finance P Ltd (2020) 115 taxmann.com 386 (Mum Trib)*

*Principles laid down in context of rather primitive trade, commerce or services are not of much relevance; business models are constantly evolving, it is time that the law is seen in tandem with the ground realities of the business world, rather than in the strict confines of what was decided in the judicial precedents, in the context of a different business world when these ground realities did not exist. **Today, virtual and intangible business connections are perhaps far more critical, important and commonplace** than the conventional brick and mortar business connections half a century ago...*

*.... when we examine relation between Indian business and participation in an event by the celebrity at Dubai launch event, we have no doubt that **it is because of this relationship between event in Dubai and business of the assessee in India that the income has accrued and arisen to the celebrity making appearance in Dubai launch event.** There cannot be any justification for an assessee in India, doing business only in India, paying money to a celebrity to make an appearance in an event in Dubai unless such an appearance benefits the business of the assessee in India, and the fact that it did benefit the business interests of the assessee in India is not even in doubt or controversy.*

Expenses by payer for holding overseas event is in connection with business in India, a natural corollary that income from participation in this event to a non-resident has a business connection in India.

- *Issues*
 - *Intangible versus tangible business connection – example of tangible BC?*
 - *Echoes of SEP – transaction with a person in India!!*

Pillar 1 Blueprint – Scope & Nexus

Automated digital services (ADS)

- Services that are automated (requiring minimum human involvement) and digital (provided over the Internet or electronic network).
 - Positive list
 - Online advertising services; Sale/alienation of user data; Online search engines; Social media platforms; Digital content services; Online gaming; Cloud computing, etc.
 - Negative list
 - Customised professional services; Customised online teaching services; Online sale of goods and services other than ADS; Revenue from sale of a physical good, irrespective of network connectivity (“Internet of things”); etc.
- Nexus
 - Only a revenue threshold
 - since ADS activities have potential to operate remotely and can be presumed to do so.

Consumer facing Businesses (CFB)

- Businesses that generate revenue from sale of goods and services of a type commonly sold to consumers, i.e. individuals that are purchasing items for personal use and not for commercial or professional purposes.
 - Includes businesses that sell consumer products indirectly through third-party intermediaries, franchise and licensing arrangements
- Nexus
 - A revenue threshold *and*
 - A **Plus factor** indicating significant and sustained engagement with the market
 - Physical presence or a group-PE
 - **A deemed engagement provision**
 - Unlikely that a group will be selling into a market with no supporting activities.
 - Any other factor (unconstrained by physical presence).

BEPS - Taxation of more than digital business

- Action 1 Report 2015

*.... while the **ability of a company to earn revenue from customers in a country without having a PE in that country is not unique to digital businesses**, it is available at a greater scale in the digital economy than was previously the case. Where this ability, coupled with strategies that eliminate taxation in the State of residence, results in such revenue not being taxed anywhere, BEPS concerns are raised [para 185]*

- Interim Report 2018

*.. possibility to reach and interact with customers remotely through the Internet, together with the automation of some business functions have significantly **reduced the need for local infrastructure and personnel to perform sales activities in a specific jurisdiction (ie scale without mass)** [p 267]*

- Public Consultation Document (Feb 2019)

*“**remote**” participation in the domestic economy enabled by digital means but without a taxable physical presence is often seen as the key issue in the digital tax debate [para 12]*

some MNE groups with highly digitalised business models were able to establish local affiliates in market jurisdictions, ... However, the local affiliates are commonly structured to have no ownership interest in intangible assets, not to perform DEMPE functions, and not to assume any risks related to such assets. Accordingly, only a modest return may be allocated to these LRDs [para 13]

- Tax Issues related to Digitalization of the Economy: Comm. Of Experts (Apr 19)(para 7)

*However, with the advent of modern means of telecommunication and the spread of digitalization, **ability to effectively engage in substantial business activities in the market country without a fixed place of business there, or to conclude contracts remotely through technological means with no involvement of individual employees or dependent agents**, raises questions about continuing suitability of existing PE or nexus rules.*

The Parliament's posit for SEP

- Memorandum FB 2018

*“The oranges upon the trees in California are not acquired wealth until they are picked, not even at that stage until they are packed, and not even at that stage until they are transported to the place where demand exists and until they are put where the consumer can use them. **These stages, upto the point where wealth reached fruition, may be shared in by different territorial authorities.**”* (excerpts from a report on double taxation submitted to League of Nations in early 1920s).....

*Taxation of business profits on the basis of economic allegiance has always been the underlying basis of existing international taxation rules. Economists gave **primacy to the economic allegiance rather than physical location** and made it clear that physical presence was important only to the extent it represented the economic location.*

*For a long time, nexus based on physical presence was used as a proxy to regular economic allegiance of a non-resident. However, with the advancement in information and communication technology in the last few decades, **new business models operating remotely through digital medium** have emerged. Under these new business models, **the non-resident enterprises interact with customers in another country without having any physical presence in that country resulting in avoidance of taxation in the source country.** Therefore, the existing nexus rule based on physical presence do not hold good anymore for taxation of business profits in source country....*

The Parliament's posit for SEP

- Memorandum FB 2018

*OECD under its **BEPS Action Plan 1** addressed the tax challenges in a digital economy wherein it has discussed several options to tackle the direct tax challenges arising in digital businesses. One such option is a new nexus rule based on “significant economic presence”. As per the Action Plan 1 Report, a non-resident enterprise would create a taxable presence in a country if it **has a significance economic presence in that country on the basis of factors that have a purposeful and sustained interaction with the economy by the aid of technology and other automated tools.** It further recommended that **revenue factor may be used in combination with the aforesaid factors to determine 'significance economic presence'.***

- Memorandum FB 2020 – discussion of the ongoing G20-OECD BEPS Project

Expln 2A – the chapeaux

*“For the removal of doubts, it is hereby declared that the significant economic presence of a non-resident in India shall constitute “business connection” in India and “significant economic presence” for this purpose, **shall mean-**.”*

- Declaratory not clarificatory, prospective; applies from AY 2022-23.
- SEP in addition to the classical business connection –
- Business with India attracts Indian tax – SEP enhances scope of coverage
- SEP meaning exhaustive
- Clause (a) and (b) operate independently; thresholds to be applied separately
- Transaction with a person in India **need not be through technology and automated tools or other digital means**
- SEP provisions do not have an impact if the NR is entitled to a Treaty
 - Risk of non-entitlement of a Treaty due to GAAR or MLI (Art. 3 Dual residents, Art 6, Preamble, Art. 7 PPT or Art. 10-3rd Country PE)

Expln 2A Limb (a)

“transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed; or”

- The term “in respect of”
 - Equivalent to “attributable”; said words could mean more than “consisting of” or “namely” [Swastik Tobacco Factory, (1966) 3 SCR 79, Engineering Analysis (2021) 125 taxmann.com 42 (SC)];
- Only digital goods or covers physical goods?
 - Invitation for comments for threshold refers to physical goods also [F. No. 370142/11/2018-TPL dt 13th July 2018]
- Rights themselves could qualify as goods or property
- Isolated or sporadic transactions also covered
- ‘Carried out’ meaning
 - to put into operation; execute; to effect or accomplish; complete [Dictionary.com]; to bring to a successful issue : complete, accomplish; to put into execution; to carry out a plan [Merriam Webster]
 - Carried out by NR in India [old Expln 2A since amended]; “attributable to the operations carried out in India” [Expln 1(a)]

Expln 2A Limb (a)

- Aggregate of payments arising from such transactions exceeding Rs. 2 crore p.a.
- Transactions to be carried out by NR **‘with any person in India’**
 - “any person in India”, not “any person resident in India”
 - EL: “to a person resident in India”
 - Situs of the transaction, place of supply or place where consideration received not relevant

✓ SEP ✗ No SEP	Trxn with a person who is a	Resident	Non-resident
	<i>when he is in India at the time of the txn</i>	✓✓✓	✓✓✓
	<i>when he is not in India at the time of the txn</i>	xx	xx
	<i>at any time in India, even if not in India at the time of the txn</i>	x	x
	<i>having a branch in India, though txn not relating to the branch</i>	-	✓x
	<i>having a dependent agent in India, though txn not relating to the branch</i>	-	xx
	<i>having a BC in India, though txn not relating to the BC</i>	-	xxx

Download of data or software

*Includes transaction for **provision of** download of data or software in India*

- Inclusive portion whether expands scope [*in respect of goods, services or property*]?
 - Or it characterizes the transaction in respect of goods, services or property as one **that includes provision of data or software in India!!**
- Provision in India
 - Implies only PUSH operations, not passive websites?
 - ‘Transaction’ implies two parties, consideration
 - Where access to download is available
- Download of data
 - Sold or licensed
 - Transaction ‘in respect of goods, services or property’ – Is data goods?
 - Transaction in respect of copyright in data?
 - Whether data available for download in India, or merely exploited by NR buyer outside India
- Download of software -
 - Not limited to **computer software**

Software payments – Royalty vs SEP

- Expln 4 to s. 9(1)(vi) versus Expln 2A to s. 9(1)(i)
 - right for use or right to use computer software vs. provision of download of software
 - Contract-based as against mode of delivery
 - If sale of software
 - Expln 4 inapplicable, Expln 2A applies if a download
 - If a licence to use software
 - Both Expln 4 and Expln 2A (if download) applies
 - Priority? Clause (vi) *Lex specialis* [*Meteor Satellite* (1979) 2 Taxman 424 (Guj); *Copes Vulcan* (1987) 30 Taxman 549 (Mad)]
 - No bar on applying other clauses of s. 9 when txn falls out of definition [*Neo Sports Broadcast* [2011] 133 ITD 468 (Mum); *Warner Bros* (2014) 39 CCH 247 (Mum-Trib)]

Expln 2A Limb (b)

“systematic and continuous soliciting of business activities or engaging in interaction with such number of users in India, as may be prescribed ~~through digital means~~”

- Systematic and continuous soliciting of business activities
 - With users?
 - Casual or sporadic activities not covered
- Engaging in interaction with users
 - Above a threshold prescribed [300000 users]
 - Casual or sporadic activities, if above threshold?
 - Letter [F.No. 370142/11/2018/TPL] dated 13.7.2018
 - Interaction impliedly two-way
 - passive user or website out of coverage?
 - Automated processes within scope.
 - **‘Through digital means’ - omitted**
 - Not necessarily online; through any means

Inconsequential for SEP

“Provided that the transactions or activities shall constitute significant economic presence in India, whether or not—

- (i) the agreement for such transactions or activities is entered in India; or*
- (ii) the non-resident has a residence or place of business in India; or*
- (iii) the non-resident renders services in India: ”*

- Akin to Explanation to section 9 wrt clauses (v), (vi) and (viii).

Other Explanations to sec. 9(1)(i)

- Limitations from classical BC – applies to SEP as well
 - Purchase of goods for export
 - Shooting of cinematograph film
 - Diamond centre display
 - Sales through independent agent
 - Sales through dependent agent who does not conclude contracts

Attribution to operations in India

“Explanation 1.—*For the purposes of this clause—*

(a) *in the case of business, other than the business having business connection in India on account of significant economic presence, of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India;”*

“Expln 2A, 2nd Proviso - *Provided further that **only so much of income as is attributable to the transactions or activities** referred to in clause (a) or clause (b) shall be deemed to accrue or arise in India.”*

- Income not revenue, essentially net income
- Priority to SEP over Classical BC
 - Classical BC only if not SEP? Or both should co-exist?
- Non-revenue factors indicating remote presence in Action 1 reports absent in law.
 - Can they be read into the provisions?
 - A purposive interpretation restricting attribution only to income accruing or arising **by virtue of digital transactions** of a NR who has an SEP [*Kanga & Palkhivala 11th Edn*].

Expln 3A

*For the removal of doubts, it is hereby declared that the **income attributable to the operations carried out in India**, as referred to in Explanation 1, shall include income from—*

- (i) **such advertisement which targets a customer who resides in India** or a customer who accesses the advertisement through internet protocol address located in India;*
- (ii) **sale of data collected from a person who resides in India** or from a person who uses internet protocol address located in India; and*
- (iii) **sale of goods or services using data collected from a person who resides in India** or from a person who uses internet protocol address located in India.*

Provided *that the provisions contained in **this Explanation shall also apply to the income attributable to the transactions or activities referred to in Explanation 2A.***

- BC scope not expanded, only income from specified activities includible if there is a BC (classical or SEP)

Rule 10 - Determination of income in the case of non-residents

10. In any case in which the Assessing Officer is of opinion that the actual amount of the income accruing or arising to any non-resident person whether directly or indirectly, **through or from any business connection in India** or through or from any property in India or through or from any asset or source of income in India or through or from any money lent at interest and brought into India in cash or in kind **cannot be definitely ascertained**, the amount of such income for the purposes of assessment to income-tax may be calculated :—

(i) **at such percentage of the turnover so accruing or arising** as the Assessing Officer may consider to be reasonable, or

(ii) on any amount which bears **the same proportion to the total profits and gains** of the business of such person (such profits and gains being computed in accordance with the provisions of the Act), as the receipts so accruing or arising bear to the total receipts of the business, or

(iii) in such other manner as the Assessing Officer may deem suitable.”

Profit Attribution to PE

CBDT Committee Draft Report 2019

- Amendment of Rule 10 recommended
 - Possibly could be inserted into the ITA [para 200]
- Shift from supply side to demand side
 - UN Committee of Experts Report (April 2019)
- Formulary apportionment (of global profits) rejected
 - Data relating to global profits unavailable/unverifiable
- NR having Business Connection to be apportioned profits attributable to operations in India
 - Three factors equally weighed-
 - sales, employees (manpower & wages) and assets
- NR having business connection due to SEP constituted due to users beyond threshold
 - Four factors weighed-
 - sales, employees (manpower & wages), assets and users
- Global op margin floor at 2% - losses not recognised
 - *MNE likely to continue operations in India only if they are profitable* [para 160]

Profit Attribution to PE

CBDT Committee Draft Report 2019

- Merits of fractional apportionment-
 - Considers both demand and supply side factors
 - Method simple, avoids litigation
- Modified rule to apply only when-
 - no India-centric accounts available
 - profits of India operations not correctly determinable

Profit attribution – an illustration

Digital models	Case 1 - Low & medium user intensity				Case 2 - High user intensity			
	Weight	In India	Outside India	Product	Weight	In India	Outside India	Product
Sales revenue derived by Indian operations	30%	80	20	0.24	30%	80	20	0.24
Employees with respect to Indian operations	15%	8	2	0.12	12.5%	8	2	0.10
Wages payable to employees with respect to Indian operations	15%	10	10	0.08	12.5%	10	10	0.06
Assets deployed for Indian operations	30%	15	15	0.15	25%	15	15	0.13
For users in India	10%			0.10	20%			0.20
Total	100%			0.69	100%			0.73
Revenue derived from India				80				80
Global Op. Profit Margin* (Min 2%)				5%				5%
Profits derived from India				4.00				4.00
Profit attributable to operations in India				2.74				2.91
Reduce therefrom any profits already taxed in India (eg subco)								

Source rules

Sub-clauses (v), (vi) and (vii)



Source rules (for interest, royalty & FTS)

	Clause (v) - Interest	Clause (vi) Royalty	Clause (vii) FTS
Government			
a person who is a resident except where	the interest is payable in respect of any debt incurred, or moneys borrowed and used , for the purposes of a business or profession carried on by such person outside India or	the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or	the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or
	for the purposes of making or earning any income from any source outside India ; or	for the purposes of making or earning any income from any source outside India ; or	for the purposes of making or earning any income from any source outside India ; or
a person who is a non-resident	the interest is payable in respect of any debt incurred, or moneys borrowed and used , for the purposes of a business or profession carried on by such person in India .	the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or	the fees are payable in respect of services utilised in a business or profession carried on by such person in India or
	Absent	for the purposes of making or earning any income from any source in India	for the purposes of making or earning any income from any source in India

Source rules [clauses (v), (vi) and (vii)]

- On extra-territoriality of the Source rules
 - Law can have an **extra-territorial operation in order to subserve the object and that object must relate to something in India** [*Electronic Corporation of India (1990) 183 ITR 43 (SC)*]
 - **Source rules in consonance with nexus theory**, does not fall foul of extra-territoriality of operation [*GVK Industries (2015) 371 ITR 453 (SC)*]
- Nexus with India *qua* payer
- Limb i and limb ii scope [*Qualcomm Incorporated (2013) 23 ITR(T) 239 (Delhi)*]
 - where right, property or information is used for purposes of business carried on by payer (*limb i*)
 - where right, property or information is **not used by payer himself** for purposes of business carried on by him **but is sub-licensed to another so as to make or earn from a source** (*limb ii*)
- Either limb to be satisfied (for the exception (sub-clause (b)) and the rule (sub-clause (c)))
- ‘Business carried on’ need not be the whole business [*Qualcomm Inc. (2015) 43 CCH 145 (Del)*]
- ‘Utilised’ means ‘*meant to be utilised*’, not *in fact utilised* [*Hindalco Ind. (2004) 91 ITD 64 (Mum)*]
- Burden of proof
 - on assessee to prove the exceptions in sub-clause (b)
 - On Revenue to prove conditions in sub-clause (c)

Source

- What is Source

*“the **spring or fount** from which a clearly defined channel of income flows. It is that which by its nature and incidents constitutes a **distinct and separate origin of income**, capable of consideration as such in isolation from other sources of income, and which by the manner of dealing adopted by the assessee can be treated so.” [Seth Shivprasad (1972) 84 ITR 15 (All.)]*

- Attributes

- For identifying overseas customers for products to be exported from India, locating prospects and promoting assessee’s capabilities to sell their products in India – **sales by payer to customers outside India effected from India – services utilized in India** [Wallace Pharma (2005) 278 ITR 97 (AAR)]
- Testing services for export market – Source of income are export contracts which are concluded in India. **Importer not a source of income, only source of receipt** –services not utilized in earning from a source outside India [Havells India [(2012) 253 CTR 271 (Delhi)]
- Services for acquiring sugar mills in Brazil, a Brazilian subsidiary set up- assessee contemplating to create a source in Brazil- covered within the phrase ‘for the purpose of making or earning outside India’ which **doesn’t require an existing source** [Bajaj Hindustan (2011) 13 taxmann.com 13 (Mum)]
- Legal services connected with a proposal to acquire an overseas business by resident – **not being a pre-existing business, not excluded** [Shriram Capital (2020) 425 ITR 207 (Mad)]

Clauses of section 9(1) - priority

- Clauses (v), (vi) and (vii) *lex specialis* to BC
 - Irrespective of business connection
- Exclusion from definition versus exclusion from the rule
 - If for the purposes of business carried on outside India by a resident [*sub-clause (b)*] or not for business carried on in India by a NR [*sub-clause c*]
 - Rule relating to specified category self-contained, no occasion to apply other clauses
- No bar on applying other clauses of s. 9 when txn falls out of definition
 - *Neo Sports Broadcast* [2011] 133 ITD 468 (Mum); *Warner Bros* (2014) 39 CCH 247 (Mum-Trib)
- **Inconsequential** [Expln to Sec. 9]
 - income of NR under clause (v) or clause (vi) or clause (vii) of s. 9(1) shall be included in the total income of the non-resident, whether or not,—
 - NR has a **residence or place of business or business connection in India**; or
 - NR has **rendered services in India**.

Royalty



Royalty defined

- **Means** consideration (including lumpsum)
- but excluding income of recipient chargeable to capital gains for the following right, property or information viz.
 - Transfer of all or any rights (incl. granting of licence) **in respect of** patent, invention, model, design, secret formula or process or trade mark or similar property or
 - Imparting information concerning their working or use
 - Use of any patent, invention, model, etc
 - Imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
 - Use or right to use industrial, commercial or scientific equipment (excl. amts u/s. 44BB)
 - Transfer of all or any rights (incl. granting of licence) **in respect of** copyright, literary, artistic or scientific work including films or video tapes for television or tapes for radio broadcasting
 - Rendering of any services in connection with the above activities

Royalty – Use of equipment

- Transponder payments – *[Asia Satellite Telecomm. (2011) 332 ITR 340 (Del)]*
 - control or possession not with payer- not use of equipment
 - Not covered under 'secret process'
 - But provision of service
- Insertion of Explanation 5 (wref 1.6.1976)
 - Whether or not
 - possession or control of such right, property or information is with the payer
 - such right, property or information is used directly by the payer
 - location of such right, property or information is in India
 - Expln 5 merely **clarificatory** - *[Poompuhar Shipping (2014) 360 ITR 257 (Mad)]*
- Insertion of Expln 6 (wref 1.6.1976)
 - "process" includes 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.**

Royalty – Use of equipment

- Technology used to provide banking services patented, not known to public- secret process [*Mastercard Asia Pacific (2018) 406 ITR 43 (AAR)*]
- Data storage charges not for use of equipment [*Vishwak Solutions (2015) 38 ITR(T) 522 (Chennai ITAT)*]
- Provision of bandwidth services as **standard services** to transmit voice and data – not royalty under India-Singapore DTAA [*Telstra Singapore (2021) 123 taxmann.com 124(Delhi Trib); Skycell Communications (2001) 251 ITR 53 (Madras)*]

Royalty – Software payments

- Software controversy-
 - Use of computer software amounts to use of copyright in the software, royalty – Citrix Systems, Samsung
 - Copyright to be distinguished from copyrighted article - Infrasoftware (Delhi HC)
- Explanation 4 wref 1.6.76
 - includes right to use or right for use computer software
- Supreme Court in Engineering Analysis Centre of Excellence
 - Four categories of transactions analysed by SC
 - I. Payment by end-user to NR supplier or manufacturer
 - II. Resident distributor purchasing copies from NR suppliers/manufacturers and resells to local distributors/end-users
 - III. NR distributor acquires copies from another NR supplier/manufacturer and resells to local distributors/end-users
 - IV. Software copy affixed onto hardware and sold as integrated unit/ equipment by NR supplier/manufacturer to resident Indian distributors/end-users.

SC ruling on end-user payments

- A licence (EULA) does not confer any proprietary interest on the licensee, does not entail parting with any copyright, and is different from a licence u/s 30 of CA 1957
 - a licence which grants the licensee an interest in the rights mentioned in section 14(a) and 14(b) of the CA 1957.
- Where end-user is authorized to have access to and make use of the “licensed” computer software product over which he has no exclusive rights, no copyright is parted with and no infringement as permitted acts [s. 52(1)(aa)].
 - Significance of non-exclusive rights?
- No difference whether software is customized, or otherwise.

SC ruling on distribution agreements

- What is granted to the distributor is **only a non-exclusive, non-transferable licence to resell computer software**, it being expressly stipulated that no copyright in the computer programme is transferred either to the distributor or to the ultimate end-user.
- Distributor does not get to use the software product
- Similar to case of Indian distributor not having right to reproduce a book and then sell copies of the same. On the other hand, if NR publisher were to sell the same book to an Indian publisher with the right to reproduce and make copies, copyright in the book has been transferred *[para 47]*
- What is “licensed” by the foreign, non-resident supplier to the distributor and resold to the resident end-user, or directly supplied to the resident end-user, **is in fact the sale of a physical object which contains an embedded computer programme, and is therefore, a sale of goods** which, as has been correctly pointed out by the learned counsel for the assessee, is the law declared by this Court in the context of a sales tax statute in *Tata Consultancy Services v. State of A.P.*, 2005 (1) SCC 308 *[para 52]*
- On the other hand, in the facts of the case before us, the distributors resell shrink-wrapped copies of the computer programmes that are **already put in circulation by foreign, nonresident suppliers/ manufacturers, since they have been sold and imported into India via distribution agreements** and are thus not hit by section 14(a)(ii) of the Copyright Act. This is made clear by the *explanation* to section 14 of the Copyright Act, which states as follows: “*Explanation.--For the purposes of this section, a copy which has been sold once shall be deemed to be a copy already in circulation.*” *[para 130]*
- *UsedSoft GmbH v. Oracle International Corp.* (Case C-128/11) ECJ relied upon .

SC ruling – other issues

- For meaning of ‘copyright’, one has to refer to CA 1957
 - There is no copyright otherwise than under the CA 1957 [S. 16]
 - The expression “copyright” has to be understood in the context of the statute which deals with it, it being accepted that municipal laws which apply in the Contracting States must be applied unless there is any repugnancy to the terms of the DTAA
- TDS under section 195 subject to chargeability of income
- Explanation 4 not retrospective wef 1976
- A person not obliged to do the impossible (deduct TDS) i.e., apply a provision of statute when not in the statute book.
- Revenue’s Review Petition pending

Google Adwords ruling

- Google India renders certain ITES enabled services and software development services for Google Ireland
- Google India non-exclusive distributor of Google Adwords program for Google Ireland.
- Held:
 - ITES services are enabling the overall business and not directly related to generating revenue from Adword Program in India. Revenue generated by end customers clicking on link and not because of ITES services.
 - Even if agreements interlinked, internal tools / intangibles / software of Google Ireland not transferred to Google India. Google India has only the right to use these for rendering ITES services.
 - None of the copyrights as per section 14(a)/(b) and section 30 of Copyright Act, 1957 transferred by Google Ireland to Google India. Not royalties under India-Ireland Treaty.
 - Use of Google Brand Features etc incidental and ancillary for achieving the main purpose of marketing and distributing the Google Adwords Program.
 - Online advertisement is now covered under EL vide FA 2016.

Royalty – other instances

- Films rights for 99 years– not royalty since **sale, distribution or exhibition of films** [*K Bhagyalakshmi (2013) 416 ITR 497 (Mad)*]
 - Television rights for 25 years- royalty since falls under films or tapes used for television [*Shree Balaji Communications (2013) 140 ITD 687 (Chennai Trib)*]
 - *These words omitted by FA 2020 wef 1-4-2021*
- Database subscriptions
 - **Limited right to use the database** not use of copyright; information supplied in public domain was not payment for ICS experience [*Factset Research Systems (2009) 317 ITR 169 (AAR)*]
 - Information supplied by social media monitoring through web-crawlers – information concerning industrial and commercial knowledge, skill- royalty [*Though Buzz (2012) 346 ITR 345 (AAR)*]
- Domain name registration services
 - **Domain names similar to trade names** and are protected; services in respect thereof royalty u/s 9(1)(vi) [*Godaddy.com (2018) 170 ITD 217 (Delhi)*]
- Use of patented technologies to render services a secret process, hence royalty [*Mastercard Asia Pacific, In Re (2018) 406 ITR 43 (AAR)*]

Fees for technical services



Fees for technical services [Clause (vii)]

- Source rule – fees for technical services payable by-
 - Government
 - Resident **except where** the right, property or information is used or services utilized
 - in a business or profession carried on by such person outside India or
 - for the purposes of making or earning income from any source outside India
 - Non-resident **where** the right, property or information is used or services utilized
 - in a business or profession carried on by such person in India or
 - for the purposes of making or earning income from any source in India

FTS

means

- *any consideration (including any lump sum consideration)*
- *for the rendering of*
- *any **managerial, technical or consultancy services***

- Words to be understood in **common parlance**
- Managerial services
 - Administration management not automatically covered
 - Leadership training not managerial service [Sandvik AB (2021) 85 ITR(T) 593 (Pune)]
 - Managerial services even if of technical or consultancy nature [(2019) Hyva Holdings 106 taxmann.com 24 (Mum)]
- Technical services
 - Requires expertise in technology
 - To be read in a narrow sense- **to take colour from 'managerial' and 'consultancy'** - requires **human intervention** [Bharti Cellular (2009) 319 ITR 139 (Delhi)]
 - Human intervention test not an effective basis- Service that caters to special needs of an user is technical service as distinct from a facility available to all [Kotak Securities Ltd (2016) 95 CCH 95]

FTS

means

- *any consideration (including any lump sum consideration)*
- *for the rendering of*
- *any **managerial, technical or consultancy services***

- Consultancy services
 - Include advisory service without technological expertise; could also be a technical service [*P No. 28 of 1999, In Re (2000) 242 ITR 208 (AAR)*]
 - Instances-
 - Advice to procure loan/strengthen finances–consultancy [*GVK Ind Ltd 371 ITR 453 (SC)*]
 - Credit evaluation, expert advice on quality standards, market research, advice on market development [*Guangzhou Usha Intl, In Re (2015) 280 CTR 412 (AAR)*]
 - Development of overseas markets requiring special expertise in the field [*Wallace Pharmaceuticals (2005) 278 ITR 97 (AAR)*]

FTS - inclusions and exclusions

- **Provision of services of technical or other personnel** included
 - Takes meaning from the preceding part, services provided by such personnel to be managerial, technical or consultancy character
 - Covers rendering of FTS through personnel; inclusion clarificatory [*Zuari Agro Chemicals (2012) 253 CTR 529 (Bombay)*]
- Consideration for any **construction, assembly, mining or like project undertaken by the recipient** excluded
 - Exclusion to be established by the person claiming such exclusion [*Orissa Synthetics (1993) 203 ITR 34 (Ori)*]
 - Only supervisory services without undertaking the specified project not covered [*SMS Schloemann Siemag Aktiengesellschaft (1996) 57 ITD 254 (Hyd)*]
 - Activities covered u/s 44BB (income from exploration of mineral oils) *lex specialis*, not FTS, s. 9(1)(vii) does not apply [*Corpro Systems, In Re (2016) 389 ITR 29 (AAR)*]
 - Installation of equipment belonging to the customer covered [*Technip Singapore (2016) 385 ITR 408 (Del)*]
- Fee for use of standard facility not FTS [*Skycell Communications (2001) 251 ITR 53 (Mad)*]

Treaties – Fees for Included Services

- India – UK Treaty
 - *Make available technical knowledge, experience, skill, know how or processes or*
 - *consist of the development and transfer of a technical plan or technical design*
- More restricted scope as compared to FTS under the Act
- To be of technical nature- Boston Consulting (2005) 94 ITD 31 (Mum)
- What is not ‘make available’
 - Software maintenance, testing services, certification, strategic consultancy, group support, general training
- Development and transfer of technical plan/design
 - Make available does not extend to this limb; transfer of plan or design for mere use also covered [*SNC Lavalin (2011) 332 ITR 314 (Delhi)*]
 - In contrast, India – Singapore Treaty Art. 12(3)
*“...consist of the development and transfer of a technical plan or technical design, **but excludes any service that does not enable the person acquiring the service to apply the technology contained therein.**”*

Royalty and FTS -taxation under the Act

- Sec. 115A –
 - If payer Govt or Indian concern
 - Gross tax rate 20%, no deduction
 - If TDS deducted at the rates u/s 115A, no obligation to file return
- Sec. 44DA
 - If payer Govt or Indian concern
 - If NR has a PE in India and royalty /FTS effectively connected with that PE - Net basis taxation
- Sec 195 TDS obligation

FTS vs Royalty

- FTS article absent in some treaties
- Services in connection with activities in Explan 2 to s. 9(1)(vi) – royalty
 - Lanka Hydraulic Institute (2011) 337 ITR 47 (AAR)
 - NR provided services of (i) field data collection, ii) desk study & mathematical model study to arrive at suitable solution, and (iii) technology transfer involving procurement & installation of software with perpetual licence and support and maintenance for two years and training.

Equalisation levy

Ch. VIII of the Finance Act, 2016
as amended by FA 2021



Background

- BEPS Action 1 Report 2013 – Addressing Tax Challenges of Digital Economy

*Identify the main difficulties that the **digital economy** poses for the application of existing international tax rules and develop detailed options to address these difficulties, taking a holistic approach and considering both direct and indirect taxation.*

Issues to be examined include, but are not limited to,

the ability of a company to have a significant digital presence in the economy of another country without being liable to taxation due to the lack of nexus under current international rules,

the attribution of value created from the generation of marketable location relevant data through the use of digital products and services,

the characterization of income derived from new business models,

application of related source rules, effective collection of VAT/GST wrt cross-border supply of digital goods/ services.

- Action 1 Report (2015)

None of the other options analysed namely (i) a new nexus in the form of a significant economic presence, (ii) a withholding tax on certain types of digital transactions, (iii) an equalisation levy, recommended.

- ‘**Digital economy**’ to ‘**Digitalised economy**’ in 2019

Indian developments

- Rulings
 - Services for uploading and displaying advertisement on Portal outside India not taxable [*Yahoo India (2011-TII-94-ITAT-Mum-INTL)*]
- E-commerce Committee Report Feb 2016
 - Report recommended a flat 6-8% levy on several types of digital transactions
- **EL 1.0** vide Finance Act 2016
 - Chapter VIII of Finance Act 2016, separate from the Income-tax Act
 - To deny treaty protection to the levy
 - 6% rate on specified services
- **EL 2.0** vide Finance Act 2020
 - Separate from provisions of EL 2016
 - Expanded the scope of EL
 - 2% rate
- Introduction of **SEP (Expln 2A)** vide FA 2018 wef 1.4.19 (now wef 1.4.22)

EL 1.0 – The charge

- Consideration for **specified service** received or receivable by a NR from
 - A person resident in India carrying on business or profession
 - Specified service need not be utilised in that business/profession; [but see s. 165(2)(c)]
 - A NR having a PE in India
- ‘Specified service’ means
 - **online** advertisement,
 - any provision for **digital advertising space** or
 - any other facility or service **for the purpose of** online advertisement
 - other service to be notified (none notified yet)
- online“ defined
 - a facility or service or right or benefit or access obtained through the internet or any other form of digital or telecommunication network

EL 1.0 – Specified services

- Online Advertisement
 - Charges to list on review websites like Tripadvisor
- Provision for digital advertising space
 - Charges for listing offerings on marketplaces
 - For online advertisement or display for sale?
 - Charges paid for higher listing
- **Production and creative fees** for creating advertisement?

EL 1.0 – Other provisions

- Exclusions
 - NR service provider **has a PE in India**
 - Service effectively connected to that PE
 - Aggregate consideration for specified services in a previous year **≤ INR 1 lac**
 - Payment for specified service by Resident or PE in India **not for the purpose of carrying out business/profession**
 - PE not defined, 'Includes a fixed place of business' As per s. 92F(iia) of ITA
- EL Collection and recovery
 - **Deductible by payer** if aggregate **consideration > INR 1 lac**
 - No grossing up necessary if payer bears the levy
 - Failure to deduct EL –
 - Payer liable to pay the levy
 - Disallowance of consideration u/s 40(ib) of ITA

EL 2.0 – The charge

- *EL @ 2%*
 - Of the *amount of consideration*
 - *received or receivable*
 - *by an ecommerce operator*
 - *from ecommerce supply or services*
 - *made or provided or facilitated by it*
 - *to*
 - *A person resident in India; or*
 - *To a NR in specified circumstances*
 - *To a person who buys such goods or services by using an IP address located in India*
- *Consideration*
 - not defined; Contract Act meaning- a *quid pro quo*
 - receivable vs due
 - *'from' and not 'for'*
- *Person resident in India*
 - Defined in ITA
 - Need not carry on business (as in EL 1.0)
 - *Contrast with*
 - *'Person in India' in Explan 2A (SEP) & 'who resides in India' in Explan 3A (profit attribution)*

EL 2.0 – Ecommerce operator

- *Sec. 164(ca)*
 - *Ecommerce operator (ECO) 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.*
- 'Platform' not defined
 - A facility which can be used for online supply or services
- Not covered
 - Passive websites disseminating information
- Mere use of third-party platform not ECO
- Platform *for* online activities specified
- Online sale of goods
 - The words '*sale of goods*' nomen juris (Gannon Dunkerley (1959) SCR 379(SC))
 - Rental not covered
 - A service? Service-tax/GST law?
 - 'supply of goods' [s. 194-O Expln (a)]
- Social media platforms covered
 - Sale of advt (EL 1.0) & Sale of data (EL 2.0)

EL 2.0 – Ecommerce supply or services

Sec. 164(cb)

e-commerce supply or services" means—

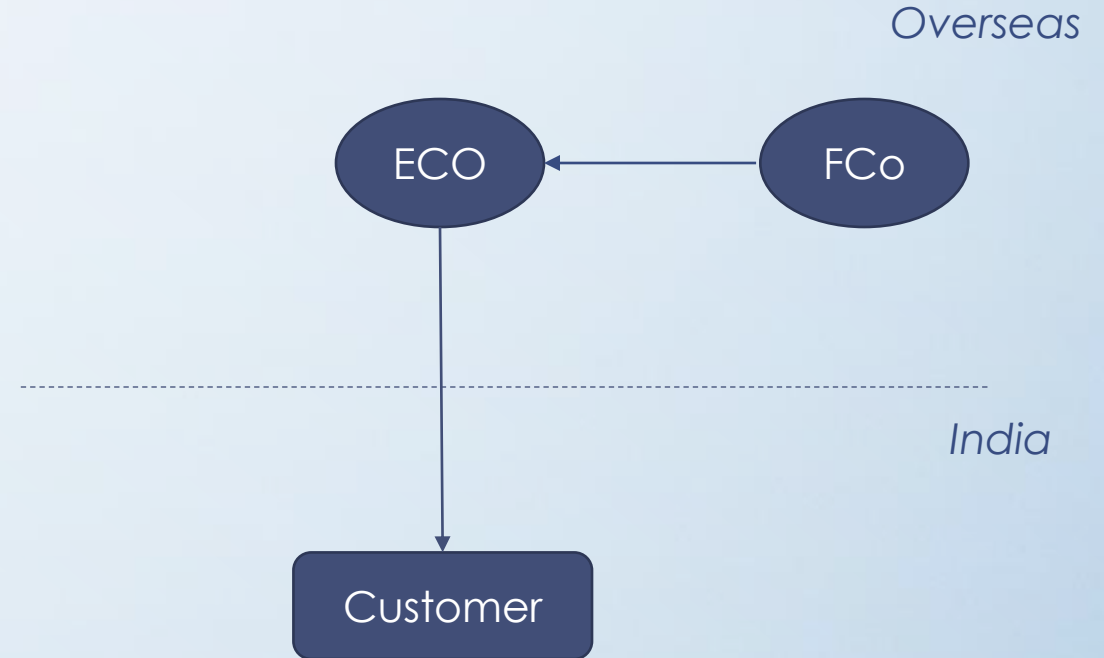
- (i) online sale of goods **owned by the ECO** ; or*
- (ii) online provision of services **provided by the ECO**; or*
- (iii) online sale of goods or provision of services or both, **facilitated by the ECO**; or*
- (iv) any combination of activities listed in clause (i), (ii) or clause (iii);*

*Explanation.—For the purposes of this clause, “online sale of goods” and “online provision of services” **shall include one or more of the following online activities**, namely:—*

- (a) acceptance of offer for sale; or*
- (b) placing of purchase order; or*
- (c) acceptance of the purchase order; or*
- (d) payment of consideration; or*
- (e) supply of goods or provision of services, **partly or wholly**;*

EL 2.0 – Consideration (1/2)

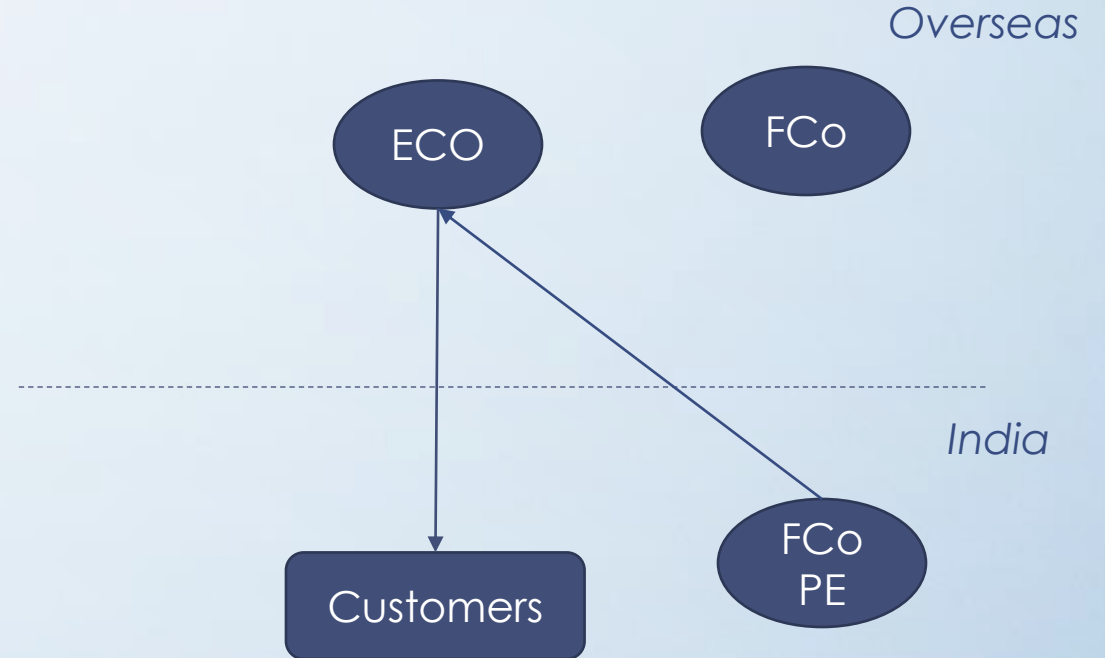
- **Sec. 163(3)**
It shall apply to to consideration recd or receivable **for** e-comm. supply or services...
- **Sec. 165A(1)**
Consideration recd or receivable by an ECO **from** ecomm. supply or services made or provided or facilitated by it to a person resident in India
- **Sec. 165A(3)(b)(i)**
Consideration recd or receivable from ecomm. Supply or services **shall include**
 - consideration for sale of goods irrespective of whether the ECO owns the goods*
 - consideration for provision of services irrespective of whether service is provided or facilitated by the ECO*
 - Does not deem something to be received; only ensures if recd, it shall be included!
- Contrast with Explan to sec. 194-O(1)



Case 1		Case 2		Case 3	
Customer - ECO	102	Customer - FCo	100	Customer - FCo	102
ECO - FCo	100	Customer - ECO	2	FCo - ECO	2
EL on	102	EL on	2	No EL	0

EL 2.0 – Consideration (2/2)

- Consideration received or receivable by ECO from ecomm. supply or service made or provided or facilitated by it to – (i) a person resident in India [s. 165A(1)]
- consideration received or receivable from ecomm. supply or services shall include—
 - (i) consideration for sale of goods irrespective of whether the ECO owns the goods, so, however, that it shall not include consideration for sale of such goods which are owned by a person resident in India or by a PE in India of a person non-resident in India, if sale of such goods is effectively connected with such PE
 - (ii) consideration for provision of services irrespective of whether service is provided or facilitated by the ECO, so, however, that it shall not include consideration for provision of services which are provided by a person resident in India or by PE in India of a person non-resident in India, if provision of such services is effectively connected with such PE.



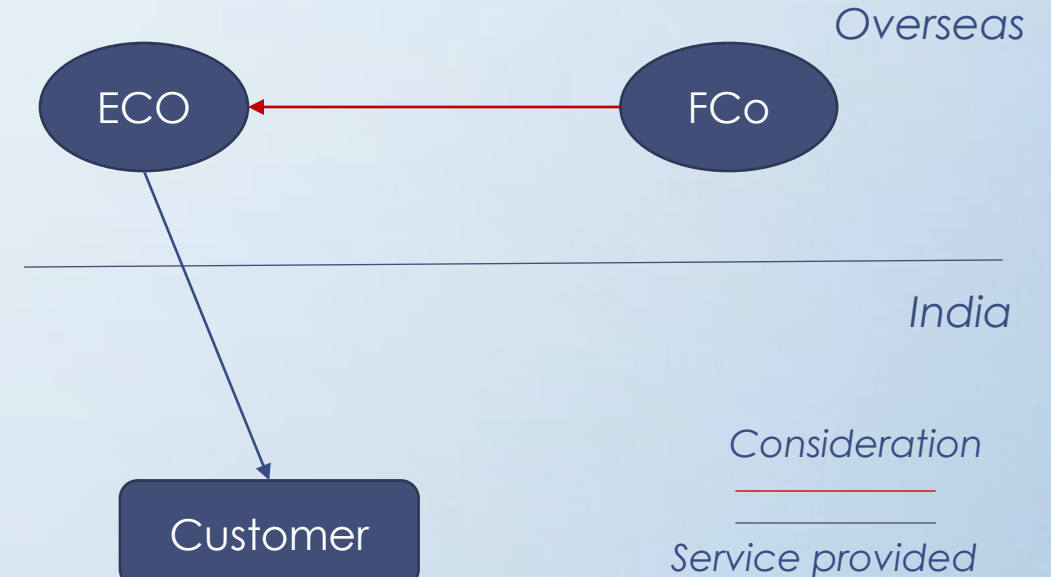
Case 4	
Customer- ECO	102
ECO – FCo PE	100
EL on	2

EL 2.0 – ‘to a person resident in India’

- Sec. 165A(1)
 - **Consideration** recd or receivable by an ECO
 - **from** ecomm. supply or services
 - made or provided or facilitated by it
 - **to a person resident in India**
- *ecomm. supply or services*
 - (i) online sale of goods **owned by the ECO** ;
 - (ii) online provision of services **provided by the ECO**;
 - (iii) The above **facilitated by the ECO**; or
 - (iv) any combination thereof
- **Beneficiary or contracting party**
 - *Vodafone Essar Cellular (2013) 33 taxmann.com 358 (Mum-CESTAT)*
 - *Paul Merchants Ltd (2013) 38 STT 702 (New Delhi CESTAT)*

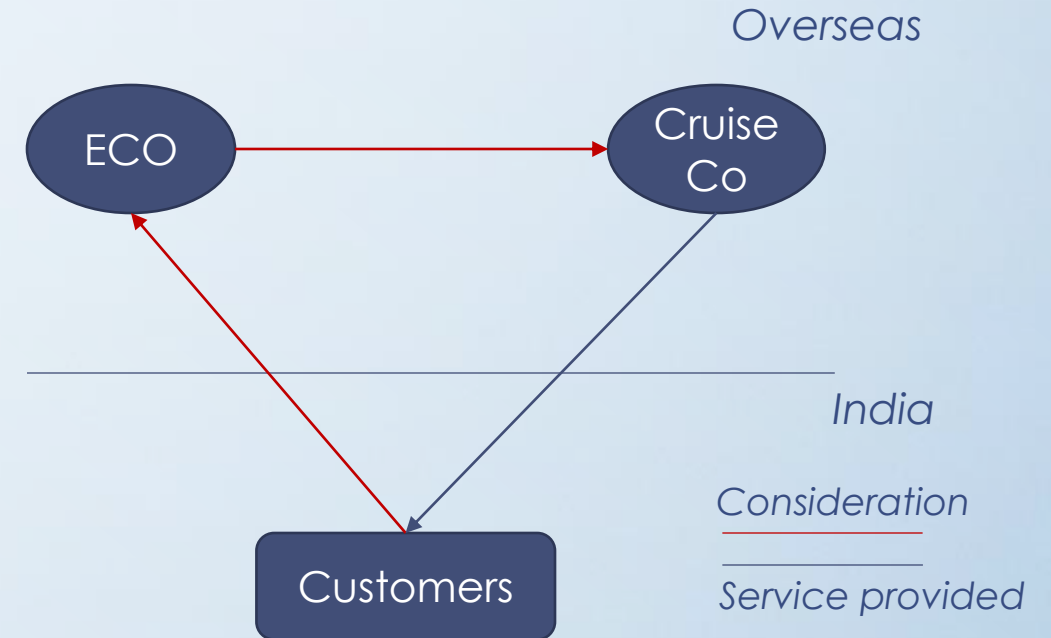
Case study

FCo engages ECO to provide online tech support for devices sold by it to customers in India. FCo pays charges to ECO.



EL 2.0 – Ecommerce supply or services

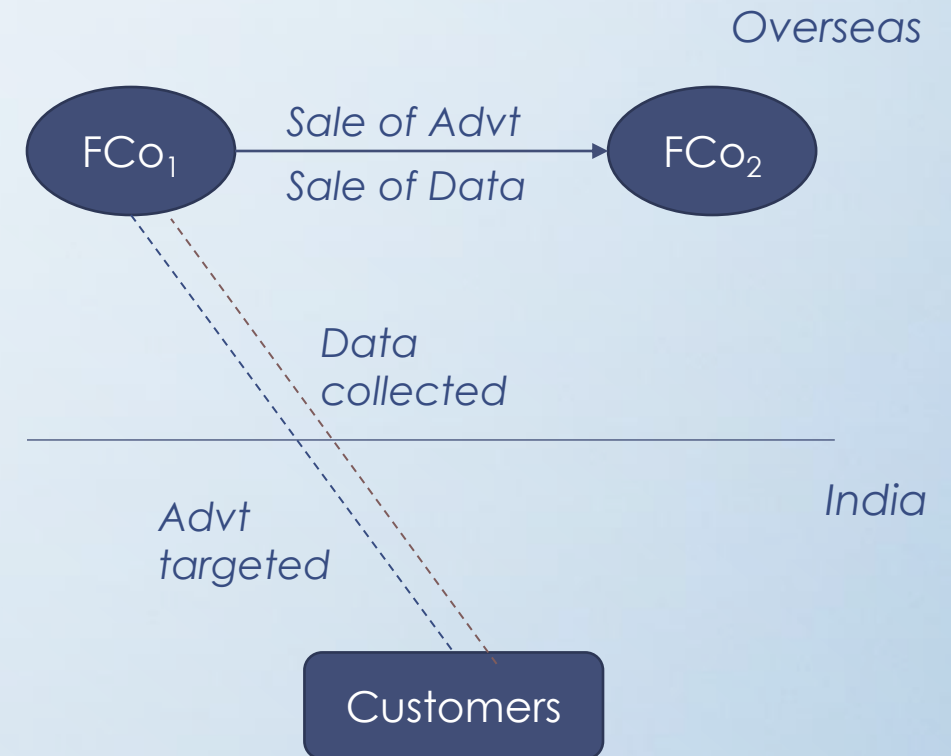
- *Ecomm Supply or services means-*
 - Online sale of goods owned by ECO
 - Online provision of services by ECO
 - Online sale of goods or provision of services facilitated by ECO
 - Any combination of the above
- *Online sale of goods or online provision of services shall include foll. online activities (s. 164(cb) Expln)*
 - acceptance of offer for sale; or
 - placing of purchase order; or
 - acceptance of the purchase order; or
 - payment of consideration; or
 - supply of goods or provision of services, partly or wholly



	Case	EL on
a	Full cost of cruise to ECO	On Full Cost
b	Booking amount to ECO + balance on Cruise	On booking amt only or on full cost?
c	Full cost to ECO + addl exp on Cruise	On Addl Exp on Cruise?

EL 2.0 – NR to NR payments in specified circumstances

- S. 165A(3)(a)(i)
 - sale of advertisement **which targets a customer**,
 - who is resident in India or
 - a customer who accesses the advertisement though IP address located in India
 - No overlap with EL 1.0
- S. 165A(3)(a)(ii)
 - sale of data, **collected from**
 - a person who is resident in India or
 - from a person who uses IP address located in India
 - Origin of data to be from India, subsequent processing immaterial
 - ‘Data collected from’ not ‘data of’
 - Sale vs. licence of data
 - Onward sale of data?



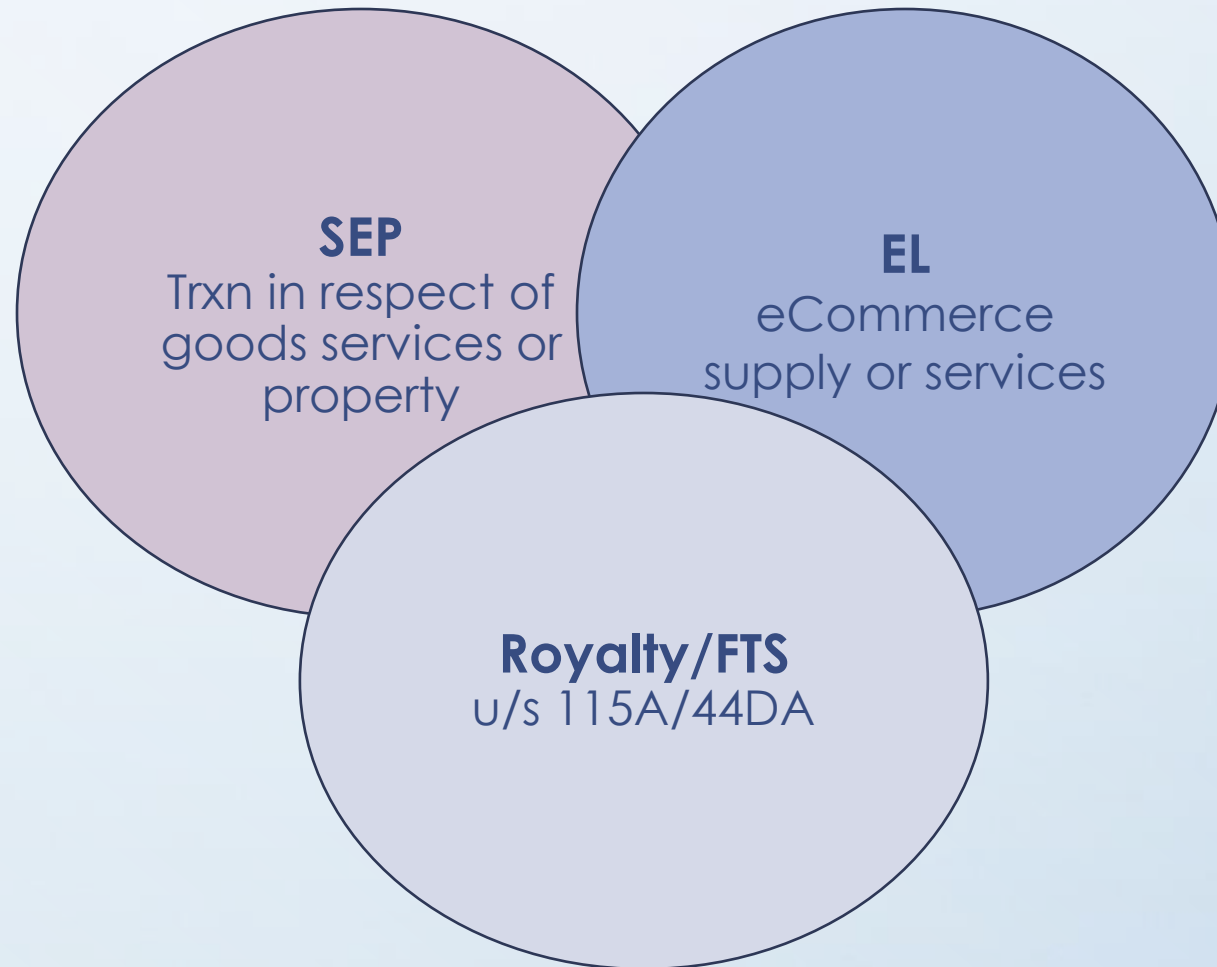
EL 2.0 - Exclusions

- Sec. 165A(2)
 - *ECO has a PE in India to which the ecomm. supply or services effectively connected*
 - *Where EL 1.0 is leviable on specified services*
 - *Sales, turnover or gross receipts of ECO from ecomm supply or services is < INR 2 crores during the previous year*
- PE defined inclusively in ITA
- ‘Effectively connected’
 - Attributable
- Sales, turnover or gross receipts
 - Annual limit
 - To exclude what is covered under
 - EL 1.0
 - Royalty/FTS taxable under ITA

Other provisions

- Annual return EL
 - Payer (for EL 1.0) and Ecom Operator (for EL 2.0) responsible
 - Can be revised within 2 years from the end of the FY
 - Return to be processed, no assessment
- Penalty
 - for non deduction (for EL 1.0)/ non-payment
 - Equal to the amount of EL not deducted/not paid
 - For deduction and non-payment
 - Liable to pay the deducted EL plus INR 1000 /day till the default continues
 - No penalty if assessee proves reasonable cause
- Appeal lies against penalty to CIT (A) and thereafter to ITAT
- Application of provisions of ITA
 - Ch XV of the Act – liability of representative assessee
 - No order prescribed for determining EL- whether fatal?

Royalty/FTS, EL and SEP scope



Royalty & FTS - SEP & Equalisation levy

	Royalty/FTS u/s 115A/44DA	Not covered u/s 115A/ 44DA	SEP
Treaty allocates taxing rights to India (u/Art. 12, 13 or 21, no PE)			
R to NR: Royalty/FTS article applies	Under Act rw Treaty; EL NA	-	9(1)(vi) or (vii) lex specialis; SEP NA
NR to NR: Royalty/FTS NA; Possibly, Other Income article	-	EL applies	S. 10(50), SEP NA
Treaty does not allocate taxing rights to India (u/Art. 12, 13 or 21, or 7 or 14)			
R to NR: Royalty/FTS article NA	EL applies	-	S. 10(50); SEP NA
NR to NR: Royalty/FTS/Other income article NA	-	EL applies	
Treaty allocates taxing rights to India (u/Art. 7 or 14, PE)			
R to NR: Royalty/FTS article to Art. 7	Under Act rw Treaty; EL NA	-	9(1)(vi) or (vii) lex specialis; SEP NA
NR to NR: Art 7	-	EL NA	Direct accrual, SEP NA

- FA 2016, Sec. 163 Proviso
*Provided that consideration received or receivable shall not include consideration which are **taxable as royalty or fees for technical services** in India under the IT Act, read with the **agreement notifiedu/s 90 or 90A ...***
- Sec. 10(50) Expn
*.... income referred to in this clause shall not include ... any income which is **chargeable to tax as royalty or fees for technical services** in India under this Act **read with the agreement notified u/s 90/ 90A....***
- Taxable vs. chargeable to tax
 - **Taxable as royalty versus royalty taxable**
 - Taxable u/s 115A or 44DA
- **'Read with treaty'** meaning
 - Allocation of taxing rights to India; whether falls under royalty/FTS Articles not relevant

EL 1.0 and 2.0 – What the future holds

- Unilateral levies to be withdrawn on culmination of Taxation of Digitalised businesses (Pillar 1 and 2 proposals)
- Meanwhile
 - Number of interpretational challenges in the law for the taxpayer and the Courts
 - USTR investigations of the levy as discriminatory; possible action by the US
 - Possible challenge to the levy under trade laws

Gifts



Clause (viii) - Gifts

(viii) income arising outside India, being any sum of money, ~~or any property situate in India transferred~~, referred to in sub-clause (xviiia) of clause (24) of section 2, paid by a person resident in India to

- *a ~~non-resident~~, not being a company, or to a foreign company (on or after 5-7-2019).*
- *a person ~~not ordinarily resident~~ in India u/s 6(6) (on or after 1-4-2023) (vide FA 2023)*

• Memorandum to Finance Bill 2019

.....Under the existing provisions of the Act, a gift of money or property is taxed in the hands of donee, except for certain exemptions provided in clause (x) of sub-section (2) of section 56. It has been reported that gifts are made by persons being residents in India to persons outside India and are claimed to be non-taxable in India as the income does not accrue or arise in India. To ensure that such gifts made by residents to persons outside India are subject to tax,.....

Receive, accrue, and arise

- Accrue and arise in the context of gifts?
 - Accrual implies a legally enforceable right – unlikely for gifts
 - Income arising from any sum of money paid [s. 9(1)(viii)]
 - Income arising when a sum of money or property received [s 56(2)(x) read with s. 2(24)(xviiia)]
 - Receipt of gift and arising of income **simultaneous**

Sum of money

- Medium of exchange for making payment
- ...currency has always been considered as "money". ... currency whether local or foreign exchange would always amounts to money and cannot be considered as "goods" in the legal sense as defined in the Sale of Goods Act, 1930 [*Thomas Cook (India) Ltd (2006) 103 ITD 119 (Mum)*]
- ...amount has to be definite and exact and it should not be subject to individual valuation....the term “sum of money” shall include cash, cheques, drafts, etc. Money does not include stocks (Shelmer Gilb, In re Eq. Rep 202), jewellery, immovable properties. [*Komal Kumar Bader, (2009) 33 SOT 58 (JP)*]
- India Millennium Deposit Certificates not money [*Anuj Agarwal (2010) 130 TTJ49 (Mum)*]
- Does not include debt

Gifts deemed as income of recipient

- Scope of total income for NR and RNOR
 - Gifts of sum of money received in India [s. 5(2)(a)]
 - Gifts of sum of money received from a resident anywhere [s. 5(2)(b) rws 9(1)(viii)]
- Where received
 - Post office whether agent of the sender or receiver
 - Where the gift was accepted by the donee
 - Indian Post Office Act does not apply beyond Indian territory except to citizens of India outside India [UOI v Moh Nazim AIR 1980 SC 431]
 - For gift of drafts sent from USA to India, necessary to look at US Postal Rules [P D Kumaresan (1998) 230 ITR 605 (Madras)]
- Gift of property – clause (viii) inapplicable
 - Property **situs when received** – the place of receipt
 - situated outside India – outside scope
 - situated in India - Import of omission of words from Finance Bill 2019 [s. 5(2)(b) rws 9(1)(i)?]
 - Situs of intangibles where the owner is – *mobilia sequuntur personam* [CUB Pty Ltd (2016) 71 taxmann.com 315 (Delhi)]

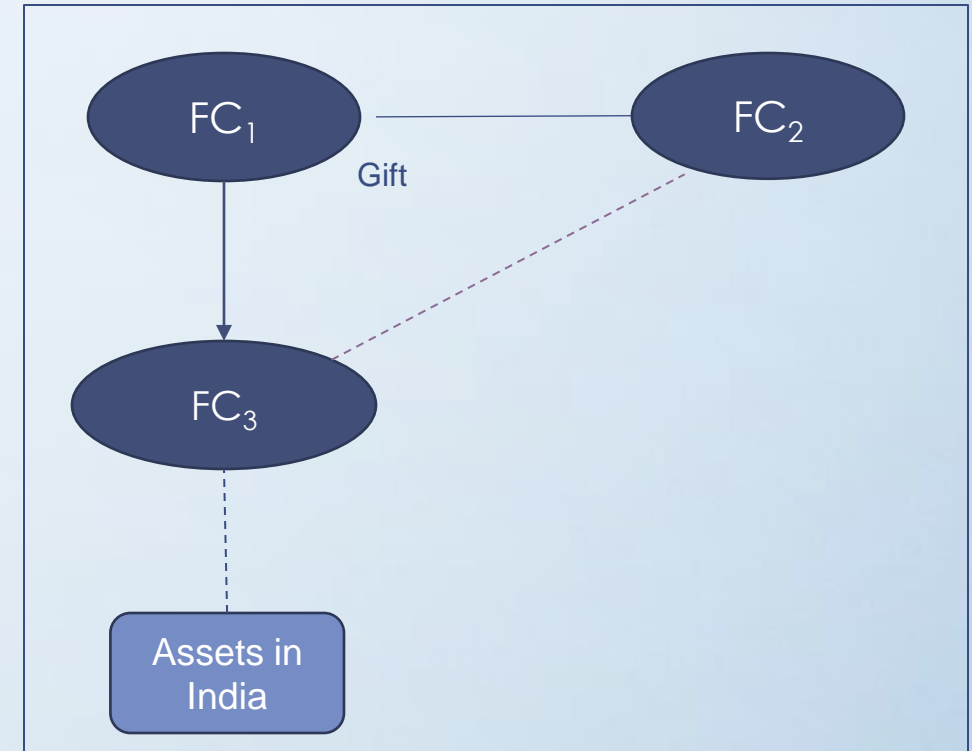
Case study - Gift of property outside India

9(1) The following incomes shall be deemed to accrue or arise in India :—

(i) **all income accruing or arising**, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or **through the transfer of a capital asset situate in India**.

Explanation 4.—.....the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

Explanation 5: For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be **deemed to have been situated in India**, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India:



- CG exempt for transferor [s. 47(iii)]
- For recipient – taxability u/s 56(2)(x)?
- Under Treaty-
 - No taxing right generally for Source State for gains from Indirect transfers
 - Art. 21 Other Income for recipient

Excess or short consideration

- Where concession received
 - Interest charged at lower rate – no transfer of debt –not a gift [*Rukmani & Co Ltd (1981) 5 Taxman 104 (Mad)*]
 - *No receipt of sum of money*
- Where **excess consideration paid**
 - *A sum of money*
- *Under Treaties*

*Where, owing to a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of interest paid exceeds for whatever reason the amount which would have been paid in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In that case, the **excess part of the payments shall remain taxable according to the law of each Contracting State, due regard being had to the other provisions of this Convention** [India – UK DTC, Art. 12(8)]*

Sec 195, TRC and Form 10F



Scope of s. 195

- Payer - Any person

- Retrospective amendment – Explanation 2 to S. 195(1)
 - Obligation to deduct whether or not NR has any presence in India
- Vodafone (SC) ruling nullified – Expln 2
 - Act extends to transactions which have a nexus with India – deduction obligation rests with NR

- Payee

- Non-residents (other than companies); or
- Foreign Co - whether or not NR [*Notn No. 3039(E) dt 11-6-2018 u/s 115JH*]

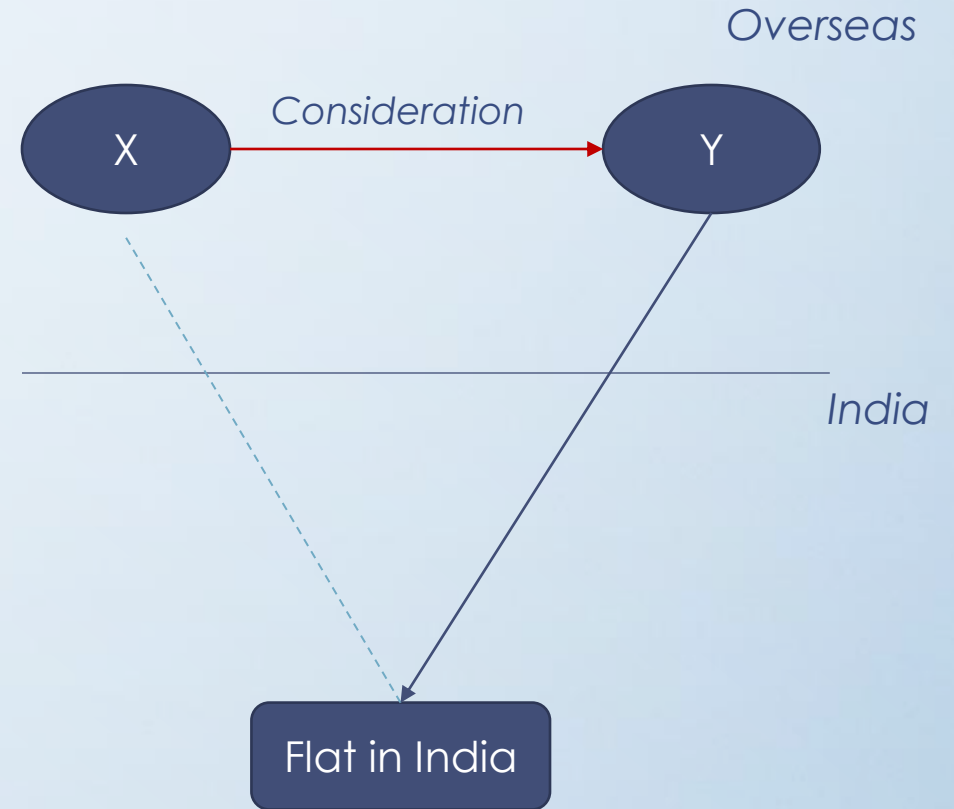
Sums chargeable to tax under the Act

- Income element
 - Where a payment contains **no element of income chargeable to tax – no TDS** [*GE India Technology Centre (2010) 327 ITR 456 (SC)*]
 - Where a payment contains **an element of income embedded** therein, and the **deductor has doubt regarding inclusion of amount in such payment which is chargeable to tax**, to apply u/s 195(2) [*Transmission Corporation 239 ITR 587 (SC) as explained in GE India Technology Centre (SC)*].
 - **DTAA relief to be considered** to arrive at income chargeable under the Act [*GE India Technology Centre (2010) 327 ITR 456 (SC)*]
- Assessee **in default for non-deduction only to the income portion** [*Circular 2/2014 dated 26-2-2014*]
- Exempt from income-tax
 - E.g., Payments covered under Equalisation Levy [S. 163 of FA 2016 as amended by FA 2020]
- Particular sections apply, not s. 195
 - e.g. Salaries (s. 192); specific payments of Interest (s. 194LB, 194LC, 194LD), payments to sportsmen, entertainers or sports associations (s. 115BBA), etc.
- No threshold for deduction of tax

Case study

Mr. X, an NRI wants to purchase a flat from Mr. Y, another NRI.

- **Issue 1** - Being an NRI, should he deduct tax at source? Does TDS obligation apply to NR?
- **Issue 2** – Should it be deducted from the full sale consideration, or from the capital gain only?
- **Issue 3** - Can the payer himself determine the amount of TDS? Can CA issue certificate in Form 15CB for capital gains?



Scope of s. 195 – Rates

- Rate or rates in force [s. 2(37A)(iii)]
 - Part II to the First Schedule of Finance Act
 - DTAA rate – WHT cap in Source State [*Bhavin Shah (2017) 81 taxmann.com 176 (Ahd Trib)*]
 - Surcharge not to be added [*Sunil V Motiani [2013] 33 taxmann.com 252 (Mumbai - Trib.)*]
 - Education Cess not to be added [*DIC Asia Pacific Pte Ltd [2012] 22 taxmann.com 310 (Kol.)*]
- Section 44DA r.w. Section 115A
 - Only applicable for final payment of tax
 - Deductibility as per Schedule I, Part II to FA
- Grossing up (s. 195A)
 - Not applicable for s. 44B, BB, etc.
 - ONGC (2004)264 ITR 340 (Uttaranchal)

	Without Gross Up of Tax (A)	With Gross up of Tax (B)
Invoice Amount	100	100
TDS rate	10	10
Net Amount payable	90	100
Amount/Grossed up amount	100	$100 + 100 / [(100/10) - 1] = 111.11$
Less: Tax deducted	10	11.11
Net Payment	90	100

Tax Residency Certificate

- Whether necessary
 - NR denied treaty relief unless TRC from his State of Residence is obtained [S. 90(4) effective from 1-4-2013]
 - S. 90(4) does not override treaty [Skaps Industries (2018) 94 tamann.com 448 (Ahmedabad Trib)]
 - NR entitled to treaty relief on providing sufficient circumstantial evidence [Sreenivasa Reddy Cheemalamarri (ITA No. 1463/Hyd/2018)]
- Whether sufficient
 - TRC conclusive evidence of residence in the other State – Azadi Bachao
 - Contrary to Govt.'s repeated assurances to foreign investors by way of CBDT circulars, press releases and decisions of courts [Blackstone Capital Partners (WPC 2562/2022 Delhi HC)]
 - Treaty relief can be denied where the transaction is a sham or a colourable device to avoid tax [*Indostar Capital* [2019] 105 taxmann.com 96 Bombay)]

Tax Residency Certificate - Issues

- If TRC is not available at the time of deduction?
 - Benefit of treaty provisions not available; once the TRC is obtained, the treaty benefit would be available for the whole period.
- If the TRC is available, but it is for a different period?
 - The deductor can rely on the TRC for the period during which the income is earned, not necessary to cover the entire tax period concerned.
- Is TRC required in case tax is not payable under the Act itself?
 - As DTAA provisions are not employed, provisions of Sections 90(4), 90(5) and the relevant rules will also not be applicable; Helpful where NR does not have business connection in India – however now check SEP provisions too.

Other prescribed information – Form 10F

- S. 90(5) – The assessee to provide such other details as may be prescribed
 - R. 21AB specifies the information to be provided
 - In Form 10F (self-attested) if required information not contained in the TRC
 - TRC and Form 10F go together, Form 10F alone is not sufficient
 - Form 10F to be submitted online- PAN required
 - Relaxation upto 30-9-2023 to 'a' not having PAN and not required to have PAN (s. 139A)

Thank you!