

Payment-based taxation by India

Introduction

- Non-residents are taxable on income either
 - received in India or
 - income accruing or arising in India
- S 9 states that certain incomes are “deemed” to accrue or arise in India.
- However, interpretation by Courts and amendments (often retrospective) have led to a situation where mere payment from India is taxed in India.

Situs of shares

- Explanation

- Situs is where registered office of a company or where share register is located
 - (1943) 13 Com Cas 265 (Cal – FB)
- Situs for share is where registered office is located
- Situs for foreign shares of an Indian company is where substantial assets are located.

- Company registered and listed in the stock exchange in Japan.
- Substantial value of assets in India.
- Situs of shares in India.
- Shares sold in Tokyo Stock Exchange liable to capital gains tax.
- Impact of Section 195 (retrospective amendment)

Explanation 4 to Section 9 (1) (vi)

- Transfer of all or any rights in respect of any
 - right
 - property
 - information
- licence is deemed to be transfer

Explanation 5 to Section 9(i) (vi)

- Royalty includes consideration.
- Location of such right, property or information is immaterial
- Use of right, property or information can be outside India.
 - taxable in India.

Explanation 6 to Section 9 (1) (vi) - Definition and “process”

- Patent, invention, model, design, secret formula or process, or trademark or similar property.
- Process akin to intellectual property.
- Process includes transmission by satellite
- Process includes up linking , amplification, conversion for down linking of any signal.

Explanation to Sections 9 (1) (v), 9 (1) (vi) or 9 (1) (vii)

- Non resident need not have
 - residence
 - place of business
 - business connection (in India)
- Non resident need not
 - render services in India
- Residence or source not necessary

Explanation 2 to Section 195

- Non resident to non resident
- Non resident need not have
 - residence
 - place of business
 - business connection
- non resident need not have
 - “any other presence” in “any other manner whatsoever” in India.

Part II

CASE LAWS

Commission example

- Indian company – appoints a Pakistani agent.
- Agent concludes a contract in Pakistan.
- Is paid commission by the Indian company.
- Whether taxable in India?
- AAR held: income “accrues” in India. No need to look into s 9.
- DTAA not referred to.

*(In re SKF Boilers and Dryers Pvt. Ltd. 343 ITR 385 (AAR).
Contra CIT v Eon Technology P. Ltd. 343 ITR 366 - however,
relying on Circular No. 786 dated 7.2.2000 which was
withdrawn by Circular No. 7/2009 dated 22.10.2009.)*

Commission example

- Income accrues *when* the assessee has a right to receive the amount. (*ED Sassoon v CIT 26 ITR 27*)
- Applying the same logic, income accrues *where* the assessee has the right to receive the amount.
- The correct answer to the question would depend on the contract between the parties.
- Private international law – the “proper law of the contract” will determine *where* the debt exists.
- The question is not *where* the agent can sue to recover, but what law the court will apply to the contract.
- If the AAR’s ruling is correct, s 9(1)(vi)(b) will become otiose.

Payment for transponder hire

- It had been held in *Asia Satellite 332 ITR 340* that payments for transponder hire are not accruing or arising in India.
- This has been nullified by amendments to s 9.
- Explanation 6 defines “process” and shockingly includes transmission by satellites.
- The fact that the person knows nothing of the process or is not in control of the process is irrelevant now.
- The mere fact that the payment has been made from India is enough for taxation.

Ships – time-charter

- In a time charter, there is no transfer of a right to use a ship. (*Essar Shipping 47 VST 209*).
- However, Madras High Court has now held that mere “use” is sufficient for cl (iva) of Explanation 2 to s 9(1)(vi). *Poompuhar Shipping Corporation Ltd. v ITO, T.C. (A) No. 2206 to 2208 of 2006 (Madras High Court)*.
- Even “economic” use of equipment is covered. No need for “control” over the equipment.
- This leads to absurd situations where if a non-resident uses a piece of equipment to do some job-work for a resident, merely because he is paid from India, he will be taxable here.

Sub-contracts

- Indian parent company sub-contracts work in Australia to its Australian subsidiary.
- AAR held: liable to tax in India for “fees for technical services”.
- No part of the service performed in India.
- Client is Australian. No link with India whatsoever. (*In re, Infosys Technologies Ltd. 350 ITR 178 (AAR).*)
- Again, ruling fails to take into consideration s 9(1)(vii)(b).
- Again, this is a move towards payment based taxation.

Sub-contracts

- However, when client is Indian, understandable that amount is liable to tax in India.
- Since amount is received towards “Indian business”.
- See: *In re, XYZ 348 ITR 31; In re, XYZ 348 ITR 45; In re, XYZ 348 ITR 20*

Only exception - designs

- Designs delivered by non-resident outside India
- To be used by resident in business outside India.
- Was held to be not taxable in India: *Grasim Industries Ltd. v CIT 332 ITR 276.*
- More the exception than the rule.