

With Holding Tax

Non Residents



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Habibullah & Co. (HCO) is a professional services firm providing audit, assurance, tax, financial advisory and consulting services to a wide range of publicly traded and privately held companies, guided by core values including competence, honesty and integrity, professionalism, dedication, responsibility and accountability.

At HCO, the interests of our clients are paramount. Our focus on the mid-market means we have a real understanding of the environment in which our clients operate and are ideally placed to help them grow and prosper.

In our continued efforts to provide Tax, Audit & Compliance updated to our clients and international associates we have compiled this guide focusing on Investment opportunities in India with light on establishing business in India. Indian Tax Law has not been discussed in this issue as the same has been separately published.

Who we are and what we stand for

- More than 50 years of professional experience (Established in the year 1962)
- 10 Partners
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- International Representation through “Antea-Alliance of Independent Firms”
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Withholding Tax

Non Residents

The Indian government has become progressively stricter about what is considered income under tax law and who must file an income tax return. In particular, companies required to withhold taxes, and individuals or companies in receipt of income, have found themselves subject to increasingly stringent withholding rules. The topic of withholding taxes can be problematic both for the payer (whether resident or non-resident) and for the recipient of the income (whether resident or non-resident).

Indian companies and non-resident companies with India-sourced income must withhold taxes on any payment to another party that is subject to withholding tax in India. If the payer believes that only a portion of the amount is subject to tax, the payer can apply to the assessing officer of the Tax Authority to determine the appropriate portion that is subject to tax.

However, if the payer fails to comply with the withholding tax requirements, the payer can be assessed interest and penalties. Some of the circumstances in which companies are required to withhold tax from payments to non-residents are:

- Non-residents with a permanent establishment in India;
- Non-residents wishing to claim a refund of tax withheld in India;
- Non-resident investors (i.e., foreign institutional investors) earning India-source income such as interest and capital gains;
- Non-residents receiving India-source royalties or fees for technical services;

- Non-residents deriving capital gains from the sale or transfer of Indian assets;
- Non-residents engaged in offshore transactions involving a transfer of shares in an Indian company;
- Non-residents earning any kind of India-source income.

In each of these circumstances, companies making payments to non-residents must withhold income tax from the payment either at the time when the income is credited to the account of the payee or at the time of payment in cash, check, or bank draft, whichever is earlier. The Income Tax Act provides the rates of withholding. In general, the current withholding rates are:

Nature of payment	Tax rate (%)
Dividend	20
Interest on foreign currency (subject to conditions)	5
Interest on money borrowed in foreign currency under a loan agreement or by way of long-term infrastructure bonds (or rupee denominated bonds) (time period for borrowing is July 2012 to July 2015)	5
Interest on investment in long-term infrastructure bonds issued by Indian company (rupee denominated bonds or government security)	5
Royalty and technical fees	25
Long-term capital gains other than exempt income	20
Income by way of winning from horse races	30
Other income	40

Non-resident individuals and companies are subject to withholding tax on income that arises or accrues or is deemed to arise or accrue in India, or income that is received or deemed to be received in India. Individuals and companies who receive Indian-sourced income are considered to be payees. All of the circumstances outlined above which require payers to withhold tax also require the non-resident payee to file an Indian tax return.

It is important to note that the payee must file an Indian tax return regardless of whether the payee is entitled to the benefits of a tax treaty and/or has zero tax liability.

In the past, the Tax Authority did not require return filing if the concerned income was not taxable in India. However, the burden is now on the payee to demonstrate to the Tax Authority that it is eligible for treaty benefits, and in most cases, this will require filing a return.

Some payees have the misguided impression that they only have to file a return if they have a permanent establishment in India; but, even if the India-sourced income is exempt from tax under a tax treaty, or if the Indian payer has already withheld the tax, the payee must still file an Indian income tax return.

Non-residents can choose to be governed by Indian tax law or by the provisions of an applicable tax treaty. In order to be governed by an applicable tax treaty, non-residents must file a Form 13, "Application by a person for a certificate for no deduction/collection of tax or deduction/collection of tax at a lower rate" if seeking approval for withholding at lower rates.

Form 15C or 15D, "Application by Person for Receipt of Sums Other Than Interest and Dividends without Deducting Tax," is required if seeking authorization

receipt of other sums without tax withholding. Before filing an application for reduced or zero tax withholding, the payee must apply for and receive a permanent account number (PAN) from the Indian government.

Conclusion

As the Indian Government applies more stringent enforcement of withholding rules, foreign companies who are subject to withholding should obtain a PAN in order to reduce the withholding tax burden on payments they receive from their Indian customers. If the payee does not provide a PAN to the payer, the payer must withhold 20% rather than the 10-15%



rate that applies under most treaties. Additionally, payees should know that the Indian Finance Ministry actively seeks to identify PAN holders who have not filed income tax returns in order to ensure that they are complying with Indian tax law.

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