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and understanding



WHITE PAPER - WHETHER NON-RESIDENT FOREIGN COMPANIES ARE REQUIRED TO FILE RETURN OF INCOME IN INDIA

THE POWER OF BEING UNDERSTOOD



1.0 BACKGROUND

- 1.1** Taxation of non-residents has been a vexed issue for a long time. Applicability of tax laws of different countries makes it difficult to ascertain taxability of non-residents who have global presence.
- 1.2** In case where non-residents are liable to tax in country other than their resident country, they may have to adhere to various compliances required by tax law of the other country. One of such important compliance is filing of Income Tax Return.
- 1.3** Generally, in India, any person earning income from India which is taxable in India has to file return of income in India. Nowadays, there are frequent transactions amongst the foreign companies and Indian companies related to various payments such as software, royalty, fees for technical services, management fees, reimbursements, etc. There may be withholding taxes being withheld by Indian entities while making payments to such foreign entities.
- 1.4** In most of the cases, Non-resident foreign companies in general do not file return of Income in India as taxes were withheld on their income in India.
- 1.5** Recently, based on information collated from withholding tax returns (Form 27Q) filed by Indian entities, etc., the Income Tax authorities have been issuing notices to foreign companies and asking them to file return of income in India.

2.0 TAXATION OF NON-RESIDENT COMPANIES

- 2.1** In case of non-residents, India follows source based taxation. Sub-section (2) of section 5 of the Income Tax Act, 1961 ('IT Act') which provides for the scope of total income, states that following incomes shall be chargeable to tax in India in case of a non-resident.
 - Income which is received or deemed to be received in India and;
 - Income which accrues or arises or is deemed to accrue or arise in India

3.0 REQUIREMENT OF FILING OF RETURN U/S 139

3.1 Provisions of the Act

- 3.1.1** As per section 139(1) of the Act, following persons shall be required to furnish return of income before the prescribed due date;
 - Company or firm; or;
 - Any person other than company or firm where total income of such person exceeds the basic exemption limit.

Further, definition of "company" as per section 2(17) of the Act, includes a foreign company.
- 3.1.2** In case of non-resident foreign companies, it may so happen that income earned by the companies from India is exempt either under the Act or under the beneficial provisions of the Double Tax Avoidance Agreements (DTAA). Ambiguity revolves around that whether, in such a case it is mandatory for such company to file return in India. Also practically, it may become difficult for non-resident foreign companies to file return of income in India due to requirement of Director's digital signature and PAN registration requirements.

3.1.3 Judicial view on requirement to file return by non-residents

- As far as judicial view point is concerned, there are various conflicting judgements by Authority of Advance Rulings (AAR). Relevant judgements of AAR are tabulated as under:

Judgement	Case	Basis for judgement
Do not have to file return of income.	Venenburg Group B.V. [2007] 159 Taxman 219	<ul style="list-style-type: none"> Liability to pay tax is founded upon sections 4 and 5 of the Act, which are the charging sections. Section 139 and other sections are merely machinery sections to determine the amount of tax. There would be no occasion to call a machinery section in aid where there is no liability at all Reference in this connection was made to Chatturam v. CIT
	Factset Research Systems Inc [2009] 182 Taxman 268	Here is no obligation to file the return in view of our finding that there is no royalty income and on the facts stated by the applicant, there is no PE.
	Dow Agro Sciences Agricultural Products Ltd [2016] 65 taxmann.com 245	Reliance placed on judgements in case of Factset Research Systems Inc and Vanenburg Group BV.
Have to file return of income.	VNU International B.V. (2011)	<ul style="list-style-type: none"> In section 139(1), there is no expression as 'exceeded the maximum amount which is not chargeable to income-tax'. As per the third proviso, every company is required to file its return of income, whether it has an income or a loss. Foreign company is covered within the definition of a company under section 2(17) of the Act.
	Deere & Co. [2011] 11 taxmann.com 388 (AAR)	<ul style="list-style-type: none"> Assessee placed reliance on AAR rulings on Factset Research Systems Inc and Vanenburg Group B.V. However, it was held that return is to be filed notwithstanding that no tax may be payable as per DTAA. Reliance was placed on rulings in VNU International B.V.
	SmithKline Beecham Port Louis Ltd [2012] 24 taxmann.com 153	Once there is chargeability to tax under the Act, the return of income will have to be filed under section 139, even if the benefit of the DTAC is claimed or a ruling is given on that basis. The applicant will therefore have the obligation to file a return of income in terms of section 139.
	XYZ [2012] 20 taxmann.com 88	Since the income would have been taxable in India under section 9, but for the intervention of the respective DTAA, the applicants are bound to file returns in India under section 139.

- In addition to above judicial pronouncements, due regard should also be given to the fact that Finance Act 2001 brought an amendment in section 139(1) whereby it was made mandatory for companies to file return of income even if they are incurring loss. Prior to the amendment, section 139 (1) read as “*every person, if his total income, or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeded the maximum amount which is not chargeable to income tax, is required to file a return of such income on or before the due date in the prescribed form and manner*”. Hence, intention of the department is that the companies must file return of income even if their total taxable income is made exempt under the provisions of the Act or as per the provisions of the relevant tax treaty.
- In addition to above, if the transactions are between associated enterprises, then the foreign company also is required to file Form 3CEB (Transfer Pricing Audit Report) in relation to the transactions being entered with its Indian associated enterprises.

4.0 CONSEQUENCES OF NON-FILING OF RETURN OF INCOME

- 4.1 It is pertinent to note that, if an obligation arises on non-resident to file return of income, then non-filing of return would attract penalty provisions.
- 4.2 As per section 234F, penalty will be levied for delay in filing return of income beyond the due date. If return of income is filed after the due date but before 31 December, the penalty will be Rs. 5,000. Whereas if return is filed after 31 December, the amount of penalty will be Rs. 10,000.
- 4.3 As per section 270A, introduced vide Finance Act, 2016, non-filing of return of income may also be construed as under reporting of income. Under reported income will be the amount of income as assessed by income tax authorities and the tax calculated on such income will be payable. Along with tax payable on such under reported income, a penalty will be levied at 50% of the amount of tax payable on the under reported income.
- 4.4 Also if the Transfer Pricing Report in Form 3CEB is applicable to the said authority and if the same is not filed, then the tax authorities may levy penalty of Rs. 100,000 for non-filing of Form 3CEB and penalty of 2% of value of international transactions for failure to report a transaction in Form 3CEB and for not maintaining of TP Study report (if value of transactions exceed INR 10 Million).
- 4.5 The penalty to be levied is at the discretion of the tax authorities and sufficient opportunity is being provided to the tax payers to justify and explain their reasons for not levying the penalty.
- 4.6 Also there are prosecution provisions for non-filing of tax return which may be initiated by the tax authorities subject to prescribed conditions under Section 276CC of the IT Act and the term may range from 3 months to 7 years along with penalty.

5.0 OUR INFERENCE

- 5.1 It can be said that **requirement of filing of return for non-residents arises when income earned by such non-resident comes within the scope of income under the Act** (i.e. Section 5 or 9). Further relief allowed as per DTAA by virtue of section 90 is in nature of exemption and **such exemption must not be considered for determining the requirement for filing of return on income**.
- 5.2 In furtherance to the same, any foreign company which is having permanent establishment in India, also has to file return of income in India and have to comply with the Indian tax compliances as may be applicable.
- 5.3 Also the foreign entity has to file Form 3CEB in relation to international transactions with its Indian associated enterprises. Form 3CEB has to be certified by a Chartered Accountant.
- 5.4 Due date for filing of return of income for companies to whom transfer pricing provisions are applicable is 30 November of relevant assessment year and in case of other companies, due date is 30 September of relevant assessment year.
- 5.5 Considering the aforesaid penal provisions, it is advisable to file return of income and claim the credit for taxes withheld in India.

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The purpose of this White Paper ('Paper') is to provide a brief overview of the whether non-resident Companies are required to file return of income in India as per Income Tax Act 1961. This White Paper is subject to professional advise. After review of this Paper, the same should be discussed with us to determine the final course of action. No part of this Paper shall be reproduced without our prior written consent. The Paper is prepared for general use and our views as stated above would be required to be revalidated vis-à-vis the facts of each case. The Government or judicial authorities may or may not subscribe to the views expressed herein. Under no circumstances, the above should be used as any tax avoidance scheme. It may be noted that nothing contained in this white paper should be regarded as our opinion and facts of each case will need to be analyzed to ascertain applicability or otherwise of the said notification and appropriate professional advice should be sought for applicability of legal provisions based on specific facts. We are not responsible for any liability arising from any statements or errors contained in this white paper.

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