



Newsflash: Revised Tax rate for FTS and Royalties as per Indian domestic tax law and E-filing of Form 10F

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Revised Tax rate for FTS and Royalties as per Indian domestic tax law and E-filing of Form 10F

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1.0 BACKGROUND:

- 1.1** The Indian Budget 2023 vide Finance Bill was presented on 1 February 2023 by the Hon'ble Finance Minister of India, Mrs. Nirmala Sitharaman. Recently, on 24 March 2023, the finance minister announced certain amendments to the originally proposed Finance Bill and the amended Bill was then passed by the Hon'ble Parliament of India which was further ratified into Finance Act 2023 on 31st March 2023.
- 1.2** One of the key amendments amongst the amended Finance Bill is increase in tax rate in respect of Royalty / Fees for Technical Services ('FTS') earned by the Non-resident taxpayers or Foreign Company in India. The existing provisions of Section 115A of the Income-tax Act (hereinafter referred to as 'the Act') lay down special tax provisions such that the Royalty and FTS income earned by non-residents from India would be chargeable to tax at the rate of 10%.
- 1.3** The Indian government vide amendment to the Indian Budget 2023 proposed to increase the special tax rate on Royalty income and FTS earned by a non-resident or a foreign company from the existing 10% to 20% [plus Surcharge and Health and Education Cess as applicable] provided that such royalty or fees is not connected to any Permanent Establishment or a fixed place of such non-resident in India. This amendment will come into force w.e.f. 1 April 2023.
- 1.4** In this connection, the non-resident taxpayers may explore the tax benefits provided by virtue of tax treaties entered by Indian Government with various other countries. Majority of tax treaties between India and various other countries inter alia provides for a lower tax rate i.e., 10% / 15% on the Royalty income and Fees for Technical (included) Services earned by Non-resident / Foreign Company in India.
- 1.5** Now there is a considerable rate disparity between the tax rates as per the Act and the tax rates as per majority of the tax treaties. Consequently, availing tax benefits under the tax treaties becomes critical for non-residents to reduce their tax costs in India. However, the benefits under the tax treaties can be claimed only on satisfaction of various anti-abuse provisions of the treaty such as Principal Purpose Test ('PPT'), Limitation of Benefits ('LOB'), beneficial ownership test etc.
- 1.6** Further, to claim benefit of any Tax treaty in respect of any income earned in India, a non-resident is required to furnish certain details in Form 10F along with the Tax Residency Certificate ('TRC'),

as per Section 90(5) of the Act read with Rule 21AB of the Income Tax Rules, 1962 (hereinafter referred to as 'the IT Rules'). This benefit can be claimed at tax withholding stage by furnishing prescribed documents to the person responsible for paying the income or at the time of filing of Return of income by the non-resident deductee.

1.7 Rule 21AB of the IT Rules provides for the details to be furnished in Form 10F as follows:

- Status (Individual, Company, Firm, etc) of the assessee.
- Permanent Account Number (PAN)* of the assessee
- Nationality (in case of an individual) or Country or specified territory of incorporation or registration (in the case of others).
- Tax Identification Number of the assessee, in the country of Residence or Unique Tax Identification Number.
- Period for which residential status is applicable.
- Address of the assessee in country of residence.

**In Form 10F there is a specific requirement to provide PAN details, but it is notable that Rule 21AB does not prescribe furnishing of PAN details*

2.0 PROCEDURE TO FURNISH FORM 10F ELECTRONICALLY:

2.1 Earlier Form 10F which is in the nature of a self-declaration by the non-resident payee, had to be prepared in a physical (offline) manner and furnished to the tax deductor making foreign remittance. However, the Directorate of Income Tax (Systems) – Central Board of Direct Taxes (CBDT) vide the **Notification No. 03 2022 w.e.f. 16th July, 2022**, has added Form 10F to the prescribed list of forms to be furnished electronically.

2.2 Therefore, Form 10F would now be required to be filed via the e-filing account of Non-resident on Income Tax e-filing portal. The non-resident assessee (deductee) would be required to furnish Form 10F through the e-filing portal by following the below steps. It may kindly be noted that for log-in to the income-tax portal, PAN is mandatory:

- Log in to income-tax portal account at <https://www.incometax.gov.in/iec/foportal>
- On e-file tab, select '**Income Tax Forms**' and then click on '**File Income Tax Forms**'
- Select '**Persons not dependent on any Source of Income (Source of Income not relevant)**'
- Select Form 10F from the list of forms available.
- Select the relevant Assessment Year (AY)** in the tab and click on '**Continue**'.

- The assessee would be required to furnish the required details (as mentioned in Para 1.7 above) and **mandatorily attach a copy of TRC**.
- Signing of Form 10F can be done either through digital signature, (usually if the return of income is required to be furnished under digital signature) or through electronic verification code in accordance with Rule 131 of the IT Rules.

2.3 However, on consideration of the practical challenge being faced in making compliance as per the above notification, the CBDT has exempted the non-resident taxpayers who were not having PAN in India from mandatory electronic filing of Form 10F till March 31, 2023. This timeline is further extended till September 30, 2023 vide ***CBDT Notification dated 28 March 2023*** considering the continued practical challenges being faced by non-resident taxpayers and to mitigate the genuine hardship being faced by such category of taxpayers.

2.4 Accordingly, it is now mandatory to furnish Form 10F electronically via the Income Tax e-filing portal w.e.f. 16th July 2022. However, the non-resident taxpayers who does not have PAN in India may continue to furnish physical Form 10F till 30 September 2023 to avail relevant tax treaty benefits.

3.0 CONSEQUENCES OF NON-COMPLIANCE

3.1 The aforementioned amendment provides that the tax rate change is effective from 1 April 2023. i.e., FY 2023-24 which apparently means any payment made by the Indian concern/ Indian Government to the non-resident taxpayer or foreign company on or after 1 April 2023 would attract tax at the rate of 20% (plus Surcharge and Health and Education cess as applicable) and the resident payer is bound to withhold taxes u/s 195 read with Sec 115A of the Act.

3.2 In case of any failure to

- (i) withhold such taxes or
- (ii) depositing the taxes with the tax authorities or
- (iii) withholding or payment of taxes at lower rate;

there may be interest and penal implications in the hands of resident payer.

3.3 Further, the Act does not specifically provide for any consequences for non-furnishing of electronically filed Form 10F nor any consequences on deductor.

3.4 However, non-furnishing of Form 10F electronically may result in withdrawal of beneficial Treaty rates by the Income-Tax Authorities since Form 10F has to be furnished along with valid TRC for claiming any treaty benefit. Thus, not furnishing online Form 10F may create issues in claiming the treaty benefits for the non-resident and also may have tax and penal consequences on the

Indian resident remitter/deductor for shortfall/nil deduction of tax as the case may be by treating him as “assessee in default”.

4.0 OTHER IMPORTANT ASPECTS

4.1 In order to address the practical hardships that would be faced by non-residents, the government vide Finance Act 2020, had granted an exemption from filing of return of income to non-residents whose only source of income from India is in the nature of royalty and FTS provided the tax has been withheld on such income at a rate not lower than that specified under Section 115A.

4.2 However, pursuant to the aforementioned amendment in the Finance Bill 2023, the tax rate on royalty and FTS under majority of the tax treaties would be lower than the rate prescribed under the Act. Therefore, non-residents desirous of obtaining treaty protection in the form of lower tax rates would now be required to obtain PAN in India and file their return of income in India as well as undertake transfer pricing compliances.

4.3 In the light of increased tax rate on Royalty / FTS income, many non-resident taxpayers who are having Royalty or FTS income from India would like to evaluate benefits under relevant DTAA and it is pertinent to note that furnishing various documentation such as Tax Residency Certificate, No PE Declaration and Form 10F with the Indian payer is a mandatory requirement to avail benefit under the relevant DTAA.

4.4 The non-resident taxpayer intending to avail tax treaty benefits must furnish Form 10F electronically (in the manner prescribed above) on the Income-tax portal. However, the Non-resident taxpayers who currently does not have PAN registration in India may file Form 10F manually to avail tax treaty benefits till 30 September 2023.

5.0 OUR OBSERVATIONS

5.1 With this notification in effect, additional annual compliance/obligation casted on non-resident to mandatorily file Form 10F electronically and upload TRC while there is already an obligation on the remitter / deductor to deduct tax while paying income to non-resident. Also, the e-filing of Form 10F enforces the non-resident taxpayer to obtain PAN in India.

5.2 The non-resident taxpayers who are having Royalty or FTS income in India are also required to file Corporate Tax Return in India within the timelines as prescribed under the Indian tax laws if they are availing any tax benefits under relevant tax treaty. With this amendment, the government seeks to bring as many non-residents as possible within the scope of compliance for better monitoring of their Indian sources of income.

5.3 We would also like to highlight that as per sub rule (2) of rule 21AB of IT Rules, if the information or any part thereof as required in Form 10F is present in the TRC, then such information or part thereof is not required to be submitted in Form 10F. Accordingly, in case all the details such as

status, nationality, Tax Identification Number/Unique number, period of residency and address are present in the TRC, a stand can be taken that furnishing of Form 10F is not mandatory in those cases for claiming the treaty benefit.

In this connection, it is pertinent to note that, in absence of justifiable commercial rationale and adequate documentation, the tax authorities in India may deny the treaty benefits. This may cause an additional outflow on the non-resident taxpayer and lead to litigation costs.

For further information please contact:

RSM Astute Consulting Pvt. Ltd.

8th Floor, Bakhtawar, 229, Nariman Point, Mumbai - 400021.

T: (91-22) 6108 5555/ 6121 4444

F: (91-22) 6108 5556/ 2287 5771

E: emails@rsmindia.in

W: www.rsmindia.in

Offices: Mumbai, New Delhi - NCR, Chennai, Kolkata, Bengaluru, Surat, Hyderabad, Ahmedabad, Pune, Gandhidham, and Jaipur, Vijayanagar.



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