



Global Business Tax Alert Sharp Insights

Deeming provision in relation to indirect transfer not applicable to dividend declared and paid by foreign company outside India

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Background

- Section 9 of the Income Tax Act, 1961 (“the Act”) is a deeming provision which provides for the incomes which are deemed to accrue or arise in India. Income accruing or arising, whether directly or indirectly, through the transfer of a capital asset situate in India is one of the income deemed to accrue or arise in India.
- The Finance Act, 2012 inserted Explanation 5 to clause (i) of the sub-section (1) of section 9 which provided that the 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 to be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from assets located in India.
- The said amendment sought to bring into the ambit of taxation the gains from transfer outside India of shares of foreign company deriving substantial value from assets situated in India by deeming the shares of the said foreign company as situated in India.
- However, it was unclear whether the India tax authorities may further seek to tax the dividend declared by such foreign company in lieu of the said amendment on the basis that the company declaring dividend is deemed to be situated in India.
- Representations were therefore made to the Central Board of Direct Taxes to clarify the position in relation to the above.

Clarification by CBDT.

- The CBDT has clarified that Explanation 5 to section 9(1)(i) of the Act would be applicable in relation to deeming any income arising outside India from any transaction in respect of any share or interest in a foreign company or entity, which has the effect to transferring, directly or indirectly, the underlying assets located in India, as income accruing or arising in India.
- Declaration of dividend by such a foreign company outside India does not have the effect of transfer of any underlying assets located in India.

- Therefore, dividend declared and paid by a foreign company outside India in respect of shares which derive their value substantially from assets situated in India would not be deemed to be income accruing or arising in India by virtue of the provisions of Explanation 5 to section 9(1)(i) of the Act.

Comments

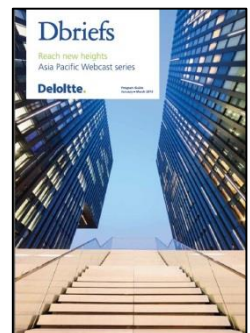
The aforesaid clarification should now put to rest the uncertainty in relation to the taxability of dividend declared and paid by a foreign company outside India, shares of which derive its value substantially from assets situated in India.

Source: Circular No. 4 /2015 dated 26 March 2015 issued by the Central Board of Direct Taxes

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