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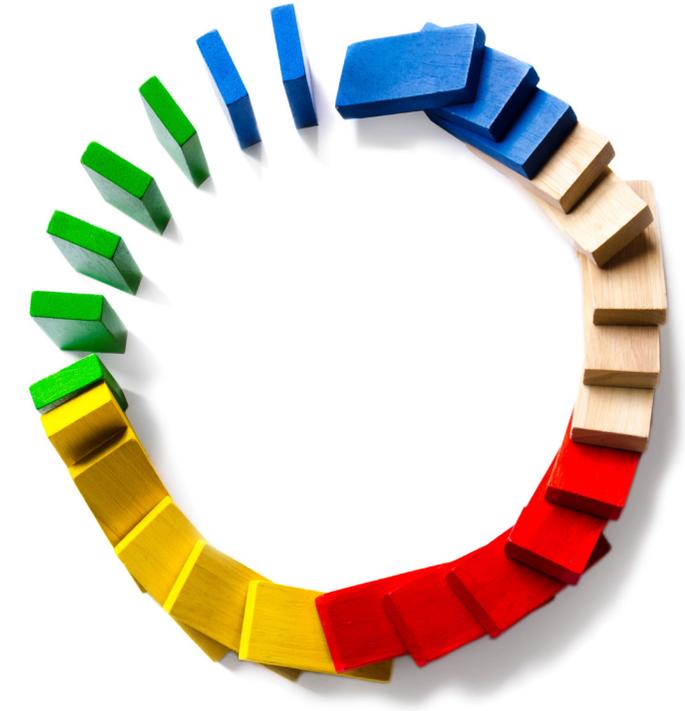
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Payments to Non-Residents and tax returns – to file or not to file?

2016



Typically, MNC Groups regularly recharge software charges and other expenses and also provide management services, licences, brand name, and know-how to the Indian group entities. These transactions in most cases give rise to taxable income under the Income-Tax Act,

Taxability of non-residents in India

- Under the Act, a non-resident is taxable in India on income received/ deemed to be received, or which accrues/ arises or is deemed to accrue/ arise in India. Further, the NRFC can take recourse to the provisions of a Double Taxation Avoidance Agreement [“Treaty”] to the extent they are more favorable where the NRFC qualifies for Treaty benefits.

Withholding tax obligations of Indian entity

- Payers are required to withhold taxes at the time of making payment or credit whichever is earlier where such payments comprise taxable income for a non-resident.
- Tax Treaty benefits available to a foreign entity can be considered to determine the appropriate rate of withholding tax.
- Until recently, the absence of a Permanent Account Number for the NRFC would result in higher rate of withholding tax under the Act. Following recent amendments, instead of a

Consequences of non-compliance for the Indian entity

- Interest payable at 1%/1.5% per month on the tax amount not deducted/not paid.
- Penalty exposure of up to 100% of the tax amount.

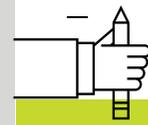
1961 [‘Act’] for the non-resident group entities in India. This document provides an overview of the taxation of Non-Resident Foreign Companies (NRFCs), withholding tax obligations of the Indian entity, tax filing obligation for the NRFCs, and consequences of non-compliance.

- Recently, based on information collated from annual information return data and withholding tax returns (Form 27Q) filed by Indian entities, etc., the Income Tax department has been very active in issuing notices to NRFCs to widen the tax base and ensure compliance in India by MNCs in respect of their non-resident group entities.

PAN, a tax residency certificate, other details can be furnished to avoid the higher rate of tax at the time of withholding.

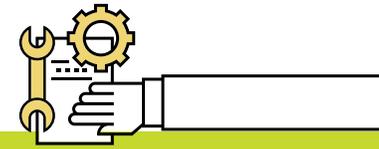
- Filing of withholding tax returns in Form 27Q and compliance with Transfer Pricing rules (disclosure and documentation) is required, where applicable.
- A lower withholding rate can be determined by application to tax officer under section 195 or section 197 of the Act.

- Disallowance of underlying expenses on which tax was required to be deducted/ paid.



Compliance obligations for NRFCs

- Every company (including foreign company) is required to file its return of income and claim credit of taxes paid, if any, in respect of a tax year (i.e., 1 April till 31 March of next calendar year).
- Relaxation from return filing requirements is available where income consists of certain types of interest or dividend income only.
- Where the income arises from an “International Transaction” as defined in TP provisions, the following TP compliances are required:
 - Reporting of international transactions in Accountants Report in Form 3CEB; and
 - Maintenance of TP documentation (if international transactions exceeds INR 10 Million)
- Some non-residents do not file returns in India because the entire tax has been withheld by the Indian entity. However, in addition to penalty of INR.5,000 for non-filing of the return, it should be noted that the penalty provisions for non-compliance has been amended from tax year 2016-17 as per which:
 - Income assessed to tax pursuant to non-filing of return of income would be considered as ‘under-reporting’ of income and penalty at 50% of the tax amount would be leviable on such under-reported income; and
- Income assessed to tax pursuant to non-filing of Accountant’s Report [i.e., TP certificate] would be considered as ‘misreporting’ of income and penalty at 200% of the tax amount would be leviable on such misreported income.
- In cases where no return of income is filed, the Income Tax authorities may issue notices for filing it. In some cases, the notices relate to tax years where it is not possible to file a belated return.
- Further, NRFCs that have a refund position for earlier years (due to excess taxes withheld, etc.) but have not filed tax returns for such years can make a claim for such refunds by way of an application to the Income Tax authorities seeking a condonation of delay. Such an application is processed based on correctness and genuineness of the claim.
- There are conflicting rulings of the Authority of Advance Rulings on the issue of requirement to file return of income where the income is not liable to tax in India, owing to more favorable Treaty provisions. Note that failure to file an income tax return and Form 3CEB could result in interest, penalties, or even prosecution a brief summary of which is provided below.



Due date of filing tax returns

Particulars	Tax Year 2015-16 and before	Tax Year 2016-17 onwards
Filing of tax return (if TP provisions applicable)	30 November following the end of the tax year	30 November following the end of the tax year
Filing of tax return (if TP provisions not applicable)	30 September following the end of the tax year	30 September following the end of the tax year
Belated filing	Up to 2 years from the end of the relevant tax year	Up to 1 year from the end of the relevant tax year

Consequences of non-compliance by NRFC

Nature of Interest/Penalty	Quantum of Interest/Penalty
Interest for delay in filing return of income	1% per month on income-tax payable (less credit for withholding tax & advance tax)
Interest for deferments/ defaults in payment of advance tax	1% per month on shortfall of advance income-tax payable (less credit for withholding tax & advance tax)
Penalty for failure to file return of income	INR 5,000
Penalty for failure to furnish Accountants' Report in Form No. 3CEB	INR 1,00,000
Penalty for failure to report a transaction in Form 3CEB or maintain TP documentation (w.r.t. international transactions exceeding INR 10 million)	2% of the value of international transaction
Penalty for under-reporting/ misreporting of income (from tax year 2016-17 onwards)*	50%/200% of tax payable on under-reported / misreported income
Prosecution for non-furnishing of return of income	3 months to 7 years depending on tax alleged to have been evaded

*Prior to tax year 2016-17, penalty for concealing income or furnishing inaccurate income ranged from 100% to 300% of tax alleged to have been evaded

Note: Levy of penalty/prosecution is not automatic and is subject to issuance of show-cause notice and sufficient opportunity is granted to demonstrate bona fide action for non-compliance

