B K KHARE & Co
CHARTERED ACCOUNTANTS

Monthly Newsletter

Direct Tax

Thursday, 21st Sep 2023

Volume 9, Issue 4

House Features

Liability in special cases- representative assessees: section 163- agents of non-residents

By itself section 163 is a compact provision, but in the context of the globalized world in which we live and the large amounts of FDI currently pouring into our country (the figure was $85 billion during FY 2021-22,) it has large ramifications: it deals with the question as to who can be declared as an agent of a non-resident - an important question for those deal with such assessee sectionument →

Are non-residents mandatorily required to take PAN in India to avail Treaty benefit?

Guided by the principles of 'reform, perform and transform' the Government of India has brought in several reforms which have furthered ease of doing business in India. Tax reforms have been one of the promoting factors and have led to increased trade with other countries. Tax reforms not only provided for reliefs or benefits to the

taxpayers but also provided for checks and balances when such relief or benefits should not be allowed.

India follows the source rule principle of taxing the income of non-residents i.e., income having nexus with India. Taxation of non-residents is governed by the more beneficial provisions of the Income tax Act, 1961 ('Act') or the applicable Double Taxation Avoidance Agreement ('Treaty') entered into by India with concerned country. Access to the more beneficial provisions of a Treaty is provided by section 90 of the Act. →

Connect with Us

Liability in special cases- representative assessees: section 163- agents of non-residents

By itself section 163 is a compact provision, but in the context of the globalized world in which we live and the large amounts of FDI currently pouring into our country (the figure was $85 billion during FY 2021-22,) it has large ramifications: it deals with the question as to who can be declared as an agent of a non-resident - an important question for those deal with such assessee section

Broad scheme of the Act dealing with non-residents

Section 5 of the Act specifies that unless otherwise exempted, income which is received in India or is deemed to be so received, by a non-resident, is liable to income-tax in India. Likewise, income which accrues or arises or is deemed to so accrue or arise in India, to a non-resident, is also liable to such tax in India. Section 9 specifically deals with the latter-that is, incomes which are deemed to accrue or arise in India. In such cases, where the non-resident is situated abroad, his incomes are often brought to tax through his agent, situated in India and declared as such under section 163. Although a direct assessment on the non-resident can always be made, because of multiple compliances required by the revenue, appointing an agent is a practical solution to the problem, convenient both for the assessee as well as the department.

Who can be appointed as agent-section163(1)

A person who is an agent under the general law of the land may be appointed as an agent for income-tax purposes under this provision. However, a person who is not an agent under general law may still be appointed as an agent for income tax purposes, if he:

a. is employed by or on behalf of the non-resident;
b. he has a business connection with the non-resident;
c. is in receipt of any income from or through the non-resident, either directly or indirectly;
d. is a trustee of the non-resident;
e. has acquired by means of transfer, a capital asset situated in India belonging to a non-resident

The condition precedent with regard to the first four categories stipulated above is that the agent should be situated in India. This condition does not apply to the fifth category *supra*. The transferee is deemed to be an agent regardless of whether he is a resident or a non-resident. Where a resident engages a firm of solicitors situated outside India, the former can be treated as an agent of the latter, if the latter receives its income from the former. Thus, both clauses b. and c. become applicable [*CESC v. DCIT 263 ITR 402*(*Cal*]. Likewise, where a solicitor made an income payment to a non-resident on behalf of a resident client, he was held to be an agent of the non-resident because the latter received a revenue receipt through him *[Ray v. IR 19 TC 164 (HL)*].

An authorized agent, either in fact or in law, may come under clause a above if he receives a salary. If he does not receive a salary, he will be covered by clause b. above, if he has a business connection with the non-resident assessee [*P.V. Raghava Reddi v. CIT 44 ITR 720*(SC)]. It may be noted that an explanation to section163(1), introduced by the Finance Act of 2003, has made the definition of 'business connection' u/s 9(1) applicable to this provision as well.

An agent appointed under this provision is "an agent for the purposes of the Act [*Turner Morrison and Co Ltd. v. CIT23 ITR 152(SC)*]" This implies that he can be appointed as an agent even before the start of the relevant assessment year and thus be made to pay advance tax u/s 210 on the income of the non-resident [*Premier Automobiles v. SECTIONN.Shrivastava 76 ITR 1(SC)].*

Proviso to section163(1)

A broker in India cannot be treated as an agent in respect of transactions where he carries these out only through non-resident brokers and does not deal with a non-resident principal directly [Proviso to section163(1)].

Opportunity of being heard-section163(2)

A person cannot be treated as an agent unless he has been provided with a reasonable opportunity of being heard [section163(2)].

Agent chargeable only in respect of income accruing or arising u/s 9(1)

S/s 161 creates a vicarious liability for the person concerned who has been appointed as an agent. Two points need to be emphasised. First, the liability is confined to the income of the non-resident principal. Second, it is limited to the income mentioned u/s 9(1) and

not any other income [*Turner Morrison v. CIT 23 ITR 152(SC)*]. Importantly, section 9(1)(i) covers all income, accruing or arising, either directly or indirectly, through or from:

i. any business connection in India,
ii. any property situated in India,
iii. any asset or source of income situated in India
iv. the transfer of a capital asset situated in India

From a practical point of view, an agent appointed u/s 163, usually becomes liable to pay tax only in respect of the above four categories of income.

SECTION161 specifies that the rights, duties and liabilities of an agent in respect of such income are the same as they would be if the income were received by or accruing to him beneficially. Any assessment made on him however is deemed u/s 161 to be representative in character and tax could be levied and recovered only **in the like manner and to the same extent** as it could be levied and recovered from the principal non-resident. This liability is limited to the incomes indicated u/s 9(1). The purpose of section163 is merely to secure payment from the non-resident, through an agent, of the tax due from him on his income taxable in India.

It follows from the first principles discussed in the preceding paras that in case the person concerned ceases to be non- resident in any year, the question of invoking section163 would not arise. [*Converse Network Systems Pvt Ltd v. CIT 369 ITR 40*]. There may be a situation where a legally correct order has been passed u/s 163 on the basis of a business connection that exists between the non-resident company and the resident company appointed as an agent u/s 163, yet no assessment on the latter, the resident agent, may be possible simply because the business connection itself may not have yielded any income for the non-resident company [*CIT v. Bombay Trust Corporation 4 ITR 323(PC)*].

The statute also makes it amply clear that an agent can only be appointed in respect of a non-resident and not a resident assessee. The agent so appointed u/s 163 may not actually be an agent under general law or in fact. Thus, when the managing agents of a non-resident company opened a branch of that company in India, which imported and sold goods on behalf of the company, and the managing agents received commission on such sales, it was held that the branch was an agent of the managing agents because there was a business connection between the two. This was so, notwithstanding the fact that, in actual fact, the reverse was true-the managing agents were the agents of the non- resident

company that owned the branch. *[In re: Nandlal Bhandari Mills Ltd. v. CIT 7 ITR 452(All)].* But tax on the agent *qua* representative assessee can only be levied on that part of the income that can reasonably be attributed to the profits that can be apportioned to the Indian operations of the non-resident and not those which have arisen abroad [Cl.(a) of the Explanation to section9(1)(a)].

Agent may not necessarily be in receipt of any income on behalf of the non-resident

An agent may not be in receipt of any income on behalf of the non-resident. If he has paid the non-resident the amounts sought to be taxed e.g. dividend or interest on loans that may have accrued to the non-resident, he becomes liable under this section to be treated as an agent and treated as a representative assessee [*Caltex v. CIT 21 ITR 278 (Bom)*].

Liability - personal

The liability of an agent is personal and not dependent upon his possessing funds belonging to the non-resident [*Plunkett v. Narayanan 1 ITC 1( )*]. But, when the assessment is made directly on the non-resident, it is not open to the department to proceed against the personal assets of his agent. The department can, however, proceed against the assets of the non-resident in the possession of the agent (section167).

Assessment on agent possible only in respect income arising from his connection or concern with the income of the non-resident

Even when a connection between the non-resident and a resident exists, it must represent a live link with the income earned by the non-resident. Only then can the resident be treated as an agent of the non- resident: thus where an Indian company was a subsidiary of a subsidiary of a non-resident, and the latter transferred the Indian company to another non-resident without the Indian company being involved in the deal in anyway, such Indian company could not be treated as an agent of the non-resident transferor, as there was no live connection between the capital gain made by such non-resident and the Indian subsidiary [*Wabco India Ltd. V. DCIT 407 ITR 317*(*Mad*)]. A resident borrower may be treated as an agent of a non-resident lender in respect of the loan given to him by the latter, but he cannot be treated as an agent for an immovable property transaction carried out in India by such non-resident, if he has no concern with such income [*CIT v. Currimbhoy Ebrahim and Sons 3 ITR 395(PC)*]. The mere presence of bank account statements of a non-resident in the house of a person would not be enough to establish a business connection between him and the non-resident; accordingly, without more

evidence such a person could not be treated as an agent of the non-resident concerned [*CIT v. Madhavan Bashyam 312 ITR 90].*

Need for separate order

A separate order should ordinarily be passed on a person when he is treated as an agent of a non-resident [*CIT v. Currimbhoy 3 ITR 395(PC*)]. If a non-resident has a business connection with several agents, each of them has be assessed separately in respect of the profits that accrue to the non-resident through each of them. [CIT v. *Ramnarayan 24 ITR 442*(Bom)]. If, an agent represents several non-residents, one order indicating his liability towards each of them may suffice, but it would be better if a separate order were to be passed in respect of his liability in respect of each of the non-residents he representsection

An order treating a person as an agent is appealable to the CIT(A) u/s 246A of the Act.

Reasonable opportunity of being heard

The section does not speak of a formal service of notice before a person is treated as an agent of a non-resident. The requirement u/s 163(2) is of being allowed a reasonable opportunity of being heard. But as a matter of practice, since being appointed as an agent under this section creates an obligation, followed by the possibility of a monetary liability, the department's as well as the assessee's interests would be best protected if a formal notice of the intention treat the assessee as an agent is served on the assessee. This should be followed by a speaking order. The Punjab High Court (*in CIT v. Kanhyalal Gurmukh Singh 87 ITR 476*), the Bombay High Court (in *CIT v. Belapur Sugar and Allied Industries Ltd. 141 ITR 404*) and the Madras High Court (*in CIT v. SECTIONG. Sambandham 242 ITR 708*) have held that before a notice is issued to a person as an agent of a non-resident u/s148, he must first be served with an order appointing him as an agent of the non-resident concerned.

Since each assessment year is separate, a separate determination is required for each assessment year.

Conclusion

This concludes our discussion on one class of representative assesses-liability of agents of non-residents. In the next issue of *Knowledgeware*, we will discuss assessment of trusts whose beneficiaries are indeterminate or unknown.

Are Non-Residents Mandatorily Required To Take PAN In India To Avail Treaty Benefit?

Guided by the principles of 'reform, perform and transform' the Government of India has brought in several reforms which have furthered ease of doing business in India. Tax reforms have been one of the promoting factors and have led to increased trade with other countries. Tax reforms not only provided for reliefs or benefits to the taxpayers but also provided for checks and balances when such relief or benefits should not be allowed.

India follows the source rule principle of taxing the income of non-residents i.e., income having nexus with India. Taxation of non-residents is governed by the more beneficial provisions of the Income tax Act, 1961 ('Act') or the applicable Double Taxation Avoidance Agreement ('Treaty') entered into by India with concerned country. Access to the more beneficial provisions of a Treaty is provided by section 90 of the Act.

It was noticed by the Government that, in a few instances, taxpayers who were not tax resident of a contracting country, claimed benefit under the Treaty entered into by the Government with that country. Thereby, even third-party residents claimed unintended treaty benefits. Therefore, effective from April 1, 2012, the Government made it mandatory for payees to provide Tax Residency Certificate (TRC), containing prescribed particulars, issued by the Government of that country in which the non-resident payee is a resident. The prescribed particulars included: Name, address, legal status, unique identification number (in the country of residence), period etc.

The Finance Ministry, vide Press Release dated 1st March 2013, clarified that the TRC issued by the Government of a foreign country would be accepted as evidence of tax residency and the tax authorities cannot go behind the TRC to question the residential status.

The requirement to obtain TRC from the Government of the residence state in the prescribed manner, turned out to be quite onerous, as the non-resident did not have control over the ways of the issuing authority in the country of his residence. To resolve this issue, the Government, vide amendment in Finance Act 2013 relaxed the requirement

to provide the TRC in the 'prescribed manner' and required that, instead, the non-resident provide a self-declaration in Form 10F of such particulars as were sought in the TRC, earlier along with TRC issued by Government of the country of residence. Rule 37BC(2) provided that TRC be provided where the law of that country or specified territory provided for the issuance of such certificate.

The CBDT vide notification No. 57 dated August 1, 2013 amended Rule 21AB with regard to prescribed information required u/s 90(5) and 90A(5). As per the amended Rule 21AB (1), the assessee would be required to provide the following information: Legal status, Nationality (in case of individual), Country or specified territory of incorporation or registration, Tax identification number or unique identification number of the Government, Period for which the residential status mentioned in the TRC is applicable, and the address outside India during the period covered by the TRC.

The amended sub-rule (2) to Rule 21AB exempted the assessee from providing aforesaid information if the same is already contained in the TRC. However, the new sub-rule 2A to Rule 21AB required the assessee to keep and maintain such documents as are necessary to substantiate the information provided and an income-tax authority may require the assessee to provide the said documents in relation to a claim / relief claimed by the assessee. Thus, the requirements of sub-rule 2A appear to be contrary to the clarification vide Press Release dated 1st March 2013 (supra) that the tax authorities shall not challenge the residency once a TRC is issued.

While this process had settled over the years, the Government, with a view to further digitise the income filings for ease in accessing / processing of information, vide notification no. 3/2022 dated July 16, 2022, made it mandatory that certain forms, including Form 10F, were required to be furnished electronically, in the manner prescribed under Rule 131(1) of the Rules. This notification left the non-residents and resident payers grappling for the reasons discussed below.

Obtaining PAN mandatory for non-resident?

Electronic filing of Form 10F required an assessee to create an account on the income tax portal. This is only possible after the assessee obtains a PAN. Thus, effectively this

notification requires all the non-resident payees to obtain a PAN if they desired to be covered by the beneficial provisions of a Tax Treaty.

Section 139A *inter-alia* requires every person to obtain a PAN if his total income (including as a representative assessee) was 'assessable' under the Act. The term 'assessable under this Act' has not been defined under the Act and should therefore be interpreted contextually. The Act uses two expressions distinctly – 'person' and 'assessee'. Every person [section 2(31) being a class of entities] need not be an assessee. An assessee [section 2(7)] means a person 'by whom any tax or any other sum of money is payable under this Act'. By implication, only when a person (section 2(31) has income in respect of which he is liable to pay tax such person is reckoned as an assessee. It would be safe to conclude that only when a person is liable to pay tax under the Act can he be said to be assessable under the Act. He would be so liable to pay tax only when he meets the conditions of Chapter II containing provisions dealing with 'charge of tax'. Needless to say, these would be subject to the other provisions of the Act.

The process of determining the amount of tax (after the basic charge has been established) starts with computation of income (Chapter IV to Chapter VII) and includes provisions dealing with rebates and reliefs from income tax (Chapter VIII). Chapter IX thereafter provides for 'Double taxation Relief' whereby a taxpayer is saved the agony of paying tax simultaneously in India and another country.

It would appear that a person who seeks to claim double taxation relief would have to establish to the satisfaction of the Indian tax authorities that he is entitled to such relief. The process for doing so would be by providing TRC and Form 10F.

Since section 195 provides for deduction of tax at source on all income chargeable to tax under the provisions of the Act (apart from other specified classes of income) the entry of a recipient of income into the net of taxation is determined at this point of time and which is where the payee has to submit TRC and Form 10F to claim double taxation relief.

Chapter XIV contains procedure for assessment which includes provision for filing of income tax returns in respect of income assessable under this Act. There are provisions in the Act which dispense with the requirement for the payee to file income tax returns in

respect of income chargeable to tax in India where tax has been deducted at source e.g. 115A(5).

On a combined reading of the above scheme of the Act it would appear that where the income of a non-resident was taxable under the Act but was not taxable by virtue of the beneficial provisions of a Tax Treaty, the non-resident should not be required to obtain PAN and not be put through the onerous requirement of electronically filing of Form 10F. Such interpretation is equitable, logical, practical and supports the ideology of ease of doing business in India but based on the assumption that the position of non-taxability (under tax treaty) was acceptable to tax authorities.

But the issue that arises is whether should not the tax authorities have a right to examine the claim for relief from taxation under Chapter IX in respect of income chargeable to tax as stated hereinabove. And, if they have such a right, should not the taxpayers obtain PAN, and TRC/Form 10F.

Needless to say, obtaining PAN, TRC and submission of 10F, duly supported by relevant documents is an onerous task. Of course, where income earned from a resident of India, by applying normal interpretive provisions to the obvious facts of a case, cannot be said to be chargeable to tax under the Act, even without invoking provisions of Chapter IX, then there should be no obligation to file form 10F.

Requirement to obtain a Digital Signature Certificate (DSC)?

Rule 131 requires verification of Form 10F using a DSC (if the return were to be filed using DSC) or through electronic code verification (ECV). ECV verification could only be made through bank account in India or through generation of Aadhar OTP. Thus, taxpayer who cannot avail the ECV facility shall be mandated to obtain DSC. Obtaining a DSC is also a complicated process for the non-resident, as it requires apostilled identity proof and address along with an Indian mobile number. The requirement of obtaining a DSC could be surpassed by providing a specific power of attorney but also entails legal formalities.

Relief to the taxpayers / non-residents

Having regard to the difficulties faced in electronically filing form 10F, the Government of India, vide notification no. F. No. DGIT(S)-ADG(S)-3/e-Filing Notification/Forms/2023/13420

dated March 28, 2023, relaxed the requirement for those non-resident taxpayers, who did not have a PAN and were not required to have a PAN as per the provisions of the Act. This relaxation of filing form 10F electronically was initially provided until March 31, 2023, and subsequently extended to September 30, 2023. While this was a fair relaxation, its time is running out. It is vital to note that the relaxation is applicable only to those non-residents who are not 'assessable under the Act' in India and for other category of non-residents the requirement to file form 10F electronically prevailed, even if there was a requirement to obtain PAN in India to comply with the process.

As discussed, the interpretation of 'assessable under the Act' could be controversial and debatable.

The relaxation provided was an interim measure to deal with practicalities and no further guidelines or modification in the processes have been provided till date.

Consequences of non-compliance with electronic filing of form 10F

Denial of Treaty benefit? In substance, Form 10F is a self-declaration by the non-resident of his residential status and is in support of TRC (as TRC does not include certain desired information). TRC is the primary document to avail the Treaty benefit. This proposition has been widely accepted by various Courts and Tribunals. The need for fuller details in the form of Form 10F arose because of misuse of treaty provisions, as stated at the start of this write-up.

Having said so, non-compliance with the laid down procedure i.e., not furnishing Form 10F electronically or even furnishing Form 10F manually, may not go well with the tax authorities, who may proceed to deny treaty benefit to non-residents resulting in litigation and locking up of funds in tax demands.

A cursory look at Form 10F would suggest that it is not so incapable of compliance since the information called for is not difficult to provide.

No specific penalty has been provided for not furnishing Form 10F electronically or otherwise. The penal consequences are built in by virtue of application of a higher withholding rate as per the provisions of the Act. It is vital to note that effective April 1, 2023, the rate to tax royalties and fee for technical services (FTS) has been increased from

10% to 20%, whereas many treaties seek to tax royalty & FTS at a lower rate. This indirectly requires non-resident to comply with the documentation compliance (including furnishing of form 10F as prescribed) to avail a lower rate provided in the Treaty. This would bring more taxpayers into the tax net of the department. So long as they are not subjected to uncalled for harassment, this should not be a grievance.

Exposure for resident payers deductor? Resident payers, while dealing with the non-residents, are obligated to withhold tax before remittance. Thus, resident payer/deductor are required to evaluate the applicable withholding tax rate and also collate and maintain documentation to support the position. Thus, Form 10F becomes one of the key documents and was being collated manually quite easily. However, the requirement of furnishing the form 10F electronically has impacted resident payers as the non-residents do not wish to take Indian tax registration out of fear of compliance issues. Because of this the resident payer could be considered to be a representative assessee of the non-resident, requiring them to discharge the tax liability of the non-resident payee. For, they would not be able to prove the eligibility to Treaty benefit absent a valid Form 10F.

Thus, practically and to avoid any dispute, this has forced the resident payers to bear higher tax liability without considering the eligible treaty benefit. This increases cost of ultimate goods and services etc.

Conclusions

The objective of digitisation of Form 10F is to provide a seamless database of the non-resident taxpayer which would help the Government to evaluate and curb the ineligible treaty benefits, which would otherwise be going unnoticed. This should also increase the taxpayers and eventually widen the tax base of the country. This is a laudable move.

As stated above, digitisation of Form 10F is leading to unintended hardship and cost of compliance which, with some practical measures, can be done away with.

The taxpayers wait with bated breath for a practical workable solution to this issue post September 30 2023 when the concession period ends.