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#section 115BBDA #POEM #Dividend #tax #DDT #tax credit #DTAA #domestic company

Foreign companies under loop of section 115BBDA: Intended or unintended consequence

1. Introduction of new law and its amendment

Before section 115BBDA insertion, there was loss to revenue, as high dividend income recipients (individual, HUF or firm) who would have been taxed at 30% had their tax liability discharged through DDT in hands of the company @ around 15%. Hence, to plug this loss of revenue, Finance Bill 2016 inserted section 115BBDA to the Income Tax Act, 1961 ('***Act***') with effect from 1st April 2017. Section 115BBDA provides that any income by way of dividend in excess of INR 1,000,000 [equivalent to USD 14,705] shall be chargeable to tax in the hands of shareholders, being individual, resident and HUF resident in India, at the rate of ten percent.

Finance Act 2017 amended section 115BBDA to provide that its applicability to extend to all resident assessee's except domestic company and certain funds, trusts, institutions, etc.

2. Analysis of applicability

A foreign company that is deemed to be resident of India by virtue of Place of Effective Management ('***POEM***') provisions would be subjected to s.115BBDA, being a resident assessee other than the excluded category (i.e domestic company and certain funds, trusts, institutions, etc).

3. Practical scenario

Practically, application of s. 115BBDA to a foreign company cannot be suo motu. Such a situation may arise generally after a prolonged litigation between the foreign company and the revenue authorities, where the assessee is not able to discharge its onus in establishing that POEM of the foreign company is outside India. In this scenario also, the revenue authorities would require to initiate demand u/s 115BBDA, if conditions are met and tax litigation may ensue consequently.

4. Availability of tax credit

In case of dividend subjected to section 115-O, the dividend is tax-free in the hands of recipient of dividend under section 10(34) of the Act. In the context of dividend covered under provision of section 115BBDA of the Act, dividend is taxable in the hands of recipient as specified under proviso to section 10(34) of the Act. Under section 115BBDA, the recipient of the dividend is the person *liable to pay tax* and discharges such tax liability and hence, to be entitled to tax credit under tax treaty provisions as tax resident.

5. Concluding views

The above analysis is indicative that though at the time of drafting of the provisions of section 115BBDA, the situation of invoking tax demand on a foreign company deemed to be tax resident of India by virtue of POEM may or may not have been an envisaged scenario but surely is on lines of the recent government endeavors to curb tax avoidance practices. This intended or unintended tax net on the foreign companies would help in curbing tax avoidance practices as it penalizes foreign companies incorporated outside India by Indian residents, thereby, being on the lines of BEPS action plans and recently introduced GAAR provisions.

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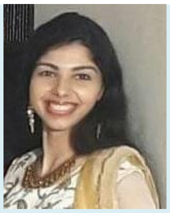

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