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Article

Compelling a non-resident to seek PAN – A vexed question

By **Tapas Misra**

With a view to enhance detection capabilities of the tax department and enforcing better compliance Section 206AA was inserted by Finance (No.2) Act, 2009 with effect from 1-4-2010. This new provision mandated all recipients of income to furnish Permanent Account Number (PAN) and in order to discourage non-compliance it required tax to be deducted at a higher rate than would be ordinarily applicable.

The new section carried a non obstante provision with reference to any other provisions of the Act. As a result, all recipients of income, whether residents or non-residents, appeared to get covered. While no specific reference was made to non-residents, a later amendment by Finance Act, 2013, which inserted sub-section (7) in Section 206AA to exclude payment of interest on long term bonds from this requirement, appears to suggest non-residents were always contemplated to be covered by the mandate to obtain PAN or be subjected to higher rate of tax deduction at source.

For non-residents, apart from the general inconvenience, this new provision posed two problems: (i) under Rule 114C(1)(b) of the Income-tax Rules, 1962 provisions of Section 139A were not applicable to non-residents; and (ii) in cases covered under the double taxation avoidance agreements, the tax rates prescribed therein had a cap *(tax at such rates not exceeding…)*. The question that arose, in several cases, was whether in view of the fact that a non-resident is not required to obtain PAN under Section 139A read with Rule 114C(1)(b), can a non-resident be compelled under section 206AA to obtain PAN? Further, the tax deductor/payer was also faced with the question whether to deduct tax at a higher rate of twenty per cent or stick to the rate of ten or fifteen per cent prescribed in the relevant tax treaty.

Dealing with the primary issue of whether a non-resident is at all required to apply for and obtain PAN, the Bangalore Bench of the Tribunal held, in *Bosch Ltd.* v. *DCIT,* [2013] 141 ITD 38 (Bangalore), as under:

> "…The provisions of sec. 206AA clearly overrides the other provisions of the Act. Therefore, a non-recipient whose income is chargeable to tax in India has to obtain PAN and provide the same to the assessee deductor. The only exemption given is that non-resident whose income is not chargeable to tax in India are not required to apply and obtain PAN. However, where the income is chargeable to tax irrespective of the residential status of the recipients, every assessee is required to obtain the PAN and this provision is brought in to ensure that there is no evasion of tax by the foreign entities.
>
> …In the case of Smt. A. Kowsalya Bai (supra) the recipients of the interest were residents of India and their total income was less than the taxable limit prescribed by the relevant Finance Act. It was in these facts and circumstances that

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the Hon'ble High Court has held that where the recipients of the 'interest income' were not having income exceeding taxable limits, it was not required to obtain the PAN. But in the case before us, the assessees are non-residents and admittedly the income exceeds the taxable limit prescribed by the relevant Finance Act. In the circumstances, the recipients are bound and are under an obligation to obtain the PAN and furnish the same to the assessee. For failure to do so, the assessee is liable to withhold tax at the higher of rates prescribed u/s 206AA of the Income-tax Act i.e. 20%...."

In a recent decision of the Pune Bench of the Tribunal in *DDIT* v. *Serum Institute of India Ltd.* [2015] 56 taxmann.com 1 (Pune - Trib.) the second question, i.e., if tax can be deducted at the rates prescribed in the treaties even if the non-resident has not obtained PAN, came up for consideration. In that case the first question, i.e., if a non-resident was at all required to apply for PAN, was decided against the assessee by the CIT (A) and it did not come up before the Tribunal. After considering the scheme of the Act in so far as Section 90(2) is concerned, the Hon'ble Tribunal held as follows:

"...The CIT(A), in our view, correctly inferred that section 206AA of the Act does not override the provisions of section 90(2) of the Act and that in the impugned cases of payments made to non-residents, assessee correctly applied the rate of tax prescribed under the DTAAs and not as per section 206AA of the Act because the provisions of the DTAAs was more beneficial..."

We are now faced with two decisions of the Tribunal with differing views on the issue, whether tax could be deducted at the rate prescribed in a treaty even when the non-resident does not have a PAN. Whether the non-resident is at all required to apply for PAN is decided against the assessee by the Bangalore Bench while the Pune Bench did not have an occasion to deal with this issue. The assessees, particularly those who are paying to non-residents and face the adverse consequence of disallowance under Section 40(a)(i) and demand under Section 201 for alleged short deduction, are still staring at uncertainty. Perhaps some assessee may challenge the applicability of Section 206AA to non-residents by invoking writ jurisdiction of a High Court. Or, perhaps the legislature may make the law clearer.

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Circular and Notification

CBDT notifies Income Computation and Disclosure standards : By way of notification No. 32/2015 dated 31-3-2015, the income computation and disclosure standards for the purposes of computation of income chargeable to income-tax under the head 'Profit and gains of business or profession' or 'Income from other sources' to be followed from 1-4-2015 onwards. The standards pertain to computation and disclosure and an entity need not maintain separate books of accounts for the same. The major heads covered are income recognition in

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case of valuation of inventories except work in progress under construction contracts, shares and debentures held as stock in trade, producers inventories of livestock and machine spare parts, recognising income in respect of construction contracts when there is reasonable certainty of collection and on accrual basis in case of interest, royalty unless there is a more rational method. Revenue from service transactions should be recognised on percentage completion basis. The notification also contains provisions as regards computation and disclosure standards in case of tangible fixed assets, self-constructed assets, and those relating to effects of changes in foreign exchange rates.

Taxation of dividend income declared by a foreign company outside India: It has been clarified vide Circular No. 4/2015 dated 26-3-2015 that dividends 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 (I) (i) of the Income Tax Act, 1961. The circular clarifies that declaration of dividend by such a foreign company outside India does not have the effect of transfer of any underlying assets located in India.

Ratio decidendi

Section 10 and Section 11 of the Act, are mutually exclusive: The appellant, the department, challenged the order passed by the Tribunal, that whether the respondent trust can claim that the income which is otherwise exempt under Section 10(33) and 10(38) of the Income Tax Act, 1961 (the Act) has to be excluded while computing the income under Section 11 of the Act. On this question the High Court held that, there is nothing in the Sections 10 or 11 which brings out that what is provided by section 10 or dealt with is not to be taken into consideration or omitted from the purview of Section 11. It opined that if the argument was accepted, it would amount to reading into the provisions something which is expressly not there. Thus, the income which is not included by virtue of Section 10, cannot be considered under Section 11 of the Act. [*DIT (E)* v. *Jasubhai Foundation*, ITA No. 1310 of 2013, Order dated 1-4-2015]

For Section 80HHC deduction, there must be profits from export business: The appellant, engaged in the business of export of marine products, financial consultancy and trading in equity shares, incurred losses in export business and earned profits from the domestic business as a result there were net profits of the business as a whole, and claimed deduction under Section 80HHC. On these facts, the Supreme Court held that, from the scheme of Section 80HHC, it is clear that deduction is to be provided under sub-section (1) thereof which is 'in respect of profits retained for export business'. Therefore, the pre-requisite is that there are profits from the export business. Sub-section (3) is only a computation mechanism, however, that would not mean that even if there are losses in the export business, benefit under Section 80HHC would still be available. In the present case, since there are losses in the export business, question of providing deduction

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under Section 80HHC would not arise. [*Jeyar Consultant & Investment Pvt. Ltd.* v. *CIT*, Civil Appeal No. 8912 of 2003, Judgement dated 1-4-2015]

Section 80HHC - Exporters having a turnover of less than and more than Rs 10 crore to be treated at par : Section 80HHC (3) was amended with retrospective effect from April 1, 1992, by which certain benefits were extended to the exporters who were entitled to claim benefit under the said section. This amendment also carved out two categories of exporters, those whose export was less than and those with more than Rs. 10 crore per year. For the latter category the amendment prescribed two conditions contained in third and fourth proviso, (a) he had an option to choose either the duty drawback or the DEPB scheme, being the Duty Remission Scheme; and (b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the DEPB Scheme, being Duty Remission Scheme. The conditions mentioned in third and fourth proviso to Section 80 HHC (3) were challenged on the contention that these conditions were severable and therefore they should be declared *ultra vires* and severed. The High Court had earlier decided the issue in favour of the writ petitioners. The Supreme Court, substituting the High Court order directed that, having seen the twin conditions and since Section 80HHC benefit is not available after 1 April, 2005, the cases of exporters having a turnover below and those above 10 crore rupees should be treated similarly. [*CIT* v. *Avani Exports & Anr.*, SLP No. 9273 of 2013, Supreme Court Order dated 30-3-2015]

Tax need not be deducted on subsequent payment on account of foreign exchange loss : The appellant, an automobile company, acquired technical know-how in respect of some automobile models and capitalized the same as ‘intangible asset’. Due to currency fluctuation subsequently at the time of payment, the appellant suffered exchange loss which was capitalized along with the original cost of the asset as per the mandate of Section 43A of the Act. The appellant deducted tax at source only on the initial payment and not on the subsequent payment made on account of exchange loss. The Tribunal held that the stage of deduction has been set out in the Section 195 of the Act itself, which requires that the deduction of tax at source is required to be made only on one occasion, either at the time of credit or the time of payment, whichever is earlier. Rule 26 of the Rules also clarifies this position and thus the appellant could be called upon to deduct tax at source on the additional liability on account of exchange loss. [*Honda Motorcycle & Scooters India (P.) Ltd.* v. *ACIT*, ITA No. 1020 (Del) of 2015, ITAT Delhi decision dated 13-4-2015]

No penalty where income declared under wrong head under bonafide belief: The taxpayer disclosed income from letting out of the premises under the head ‘Profit and gains from business or profession’ and claimed depreciation on it. When pointed out by the department to treat it as taxable under Income from house property, the taxpayer accepted and paid additional tax. The High Court held that there was no deliberate suppression of income by the taxpayer nor was it a case of furnishing of inaccurate particulars of income. The High

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court set aside the penalty order in the absence of a clear and unambiguous direction for levy of penalty. [*CIT* v. *Chandrasekaran* [2015](56 taxmann.com 210)]

Limitation of 60/90 days prescribed under Rule 34(5)(c) of ITAT Rules is not absolute: The Tribunal pronounced the order after a period of 60days from date of closure of the hearing. A Miscellaneous Application was filed in terms of Section 254(2) of the Income tax Act, 1961 to treat the order passed as barred by limitation prescribed under Rule 34(5) and thus, bad in law. The Tribunal held that even where the order is passed beyond 90 days, the same would not be barred by limitation in special circumstances due to specific usage of the word 'ordinarily' in Rule 34(5)(c). In terms of section 255(5) of the Income tax Act, the Tribunal has the power to regulate its own procedure for discharge of its functions. It has also been held that the function of 'pronouncement of orders' is not like of a nature such as 'actionable legal claim' which if not claimed within a period of 60 days or 90 days can be said to have been barred by limitation. [*Times Guaranty Ltd* v. *ACIT* [2015] (56 taxmann.com 272)(Mumbai Tribunal)]

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