

SECTION 195- TDS ON PAYMENT TO NON RESIDENTS

Section 195 - whether TDS on entire payment or only on income component?

- Any person responsible for paying to a non-resident any interest or any other sum chargeable under the provisions of this Act shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force. –
- **Exclusions**
 - ❖ Interest referred to in section 194LB (infrastructure debt fund or section 194LC (income by way of interest from Indian Company) to a non resident not being a company or section 194LD (income by way of interest on certain bonds and government securities to a FII or qualified foreign investor.
 - ❖ Rate of TDS is 5 % in all the above cases.
 - ❖ Income chargeable under the head "Salaries".
 - ❖ Dividends referred to in section 115-O i.e. Tax on distributed profits of domestic companies.
- **Any Person**
- Includes all taxable entities – individual/HUF, residents /non-residents
- Expln 2 (inserted by FA 2012 w.r.e.f 1.4.1962) which states that -
 - ✓ For the removal of doubts, it is hereby clarified that the obligation to comply with sub-section (1) and to make deduction thereunder applies and shall be deemed to have always applied and extends and shall be deemed to have always extended to all persons, resident or non-resident, whether or not the non-resident person has—
 - ❖ (i) a residence or place of business or business connection in India; or
 - ❖ (ii) any other presence in any manner whatsoever in India.
- Agent u/s 163 not liable to deduct TDS on payment to NR – CIT v Premier Tyres Ltd 134ITR17(Bom).

Section 195 - whether TDS on entire payment or only on income component?

- **Transmission Corpn of AP Ltd v CIT 239 ITR 587 (SC);**
- The scheme of TDS applies not only to the amount paid which wholly bears income character such as salaries, dividends, interest of securities etc., but also to gross sums, the whole of which may not be income or profits of the recipient;
- It is true that in some cases, a trading receipt may contain a fraction of sum as taxable income, but in other cases such as interest, commission, transfer of rights of patents, goodwill or drawings for plant and machinery and such other transactions, it may contain large sum as taxable income under the provisions of the Act.
- Whatever may be the position, if the income is from profits and gains of business, it would be computed under the Act as provided at the time of regular assessment.
- The said provision is for tentative deduction of income-tax thereon subject to regular assessment and by the deduction of income-tax, rights of the parties are not, in any manner, adversely affected.
- To deduct TDS not on gross amount but on income portion of payment made, the payer can make an application under section 195(2) to the assessing officer in such form and manner to determine the appropriate proportion of such sum so chargeable.

Section 195 - whether TDS on entire payment or only on income component?

- **GE India Technology Centre (P) Ltd v CIT 327 ITR 456 (SC)**
- Limited to the appropriate proportion of income chargeable under the Act forming part of the gross sum of money payable to the non-resident. This flows from the words used in section 195(1), namely, 'chargeable under the provisions of the Act'.
- The application of section 195(2) pre-supposes that the person responsible for making the payment to the non-resident is in no doubt that tax is payable in respect of some part of the amount to be remitted to a non-resident but is not sure as to what should be the portion so taxable or is not sure as to the amount of tax to be deducted. In such a situation, he is required to make an application to the ITO(TDS) for determining the amount.
- While deciding the scope of section 195(2), it is important to note that the tax which is required to be deducted at source is deductible only out of the chargeable sum. This is the underlying principle of section 195. Hence, apart from section 9(1), sections 4, 5, 9, 90 and 91 as well as the provisions of the DTAA are also relevant, while applying tax deduction at source provisions.
- Reference to the ITO (TDS) under section 195(2) or 195(3) either by the non-resident or by the resident payer is to avoid any future hassles for both resident as well as non-resident. Section 195(2) and 195(3) are safeguards. The said provisions are of practical importance.
- From this, it follows that where a person responsible for deduction is fairly certain, then he can make his own determination as to whether the tax is deductible at source and, if so, what should be the amount thereof.

Section 195 - whether TDS on entire payment or only on income component?

- **Instruction No. 02/2014, Dated 26.02.2014**
- Section 201 of the Act inter alia provides that any person who is required to deduct tax in accordance with the provisions of the Act, does not do so, shall be deemed to be an assessee in default and shall also be liable to pay simple interest at the specified rate.
- The Board hereby directs that in a case where the assessee fails to deduct tax under section 195 of the Act, the Assessing Officer shall determine the appropriate proportion of the sum chargeable to tax as mentioned in subsection (1) of section 195 to ascertain the tax liability on which the deductor shall be deemed to be an assessee in default under section 201 of the Act, and the appropriate proportion of the sum will depend on the facts and circumstances of each case taking into account nature of remittances, income component therein or any other fact relevant to determine such appropriate proportion.
- Section 195(7) inserted w.e.f. 01.07.12 which provides that notwithstanding anything contained in sub-section (1) and sub-section (2), the Board may, by notification in the Official Gazette, specify a class of persons or cases, where the person responsible for paying to a non-resident, not being a company, or to a foreign company, any sum, whether or not chargeable under the provisions of this Act, shall make an application in such form and manner to the Assessing Officer, to determine in such manner, as may be prescribed, the appropriate proportion of sum chargeable, and upon such determination, tax shall be deducted under sub-section (1) on that proportion of the sum which is so chargeable.

Section 195(2) & 197 - Application to AO to receive interest/other sum at lower TDS

- Section 195(2) – Application by deductor if he considers that the whole of such sum would not be income chargeable in the case of the recipient, he may make an application in such form and manner to the Assessing Officer, to determine in such manner, as may be prescribed, the appropriate proportion of such sum so chargeable, and upon such determination, tax shall be deducted only on that proportion of the sum which is so chargeable.
- Section 197 – Application by recipient to for certificate for deduction at lower rate. If the AO is satisfied that the total income of the recipient justifies the deduction of income-tax at any lower rates or no deduction of income-tax than the AO give to him such certificate as may be appropriate. Where any such certificate is given, the person responsible for paying the income shall, until such certificate is cancelled by the Assessing Officer, deduct income-tax at the rates specified in such certificate or deduct no tax, as the case may be. The Board may, having regard to the convenience of assesseees and the interests of revenue, by notification in the Official Gazette, make rules specifying the cases in which, and the circumstances under which, an application may be made for the grant of a certificate under sub-section (1) and the conditions subject to which such certificate may be granted and providing for all other matters connected therewith.

Section 195(3) to (5) - Application by payee to AO to receive interest/other sum without deduction of tax

- Application by payee to AO in prescribed form for grant of certificate authorizing receipt of interest/other sum without deduction of tax.
- Upon grant of such certificate, every payer making payment of such sum to payee, during period that certificate in force, shall make payment of interest/other sum without deduction of tax at source.
- Certificate valid till period for which it is granted, or till it is cancelled before expiry of such period
- Board may make rules, having regard to convenience of assesseees and interests of revenue, specifying cases in which and circumstances under which application may be made & conditions subject to which certificate may be granted & all other matters connected therewith.
- **Rule 29B, Forms 15C & 15D.**
- **Specified income**
- Where banking co which is neither an Indian company or a company, which has made prescribed arrangements for declaration & payment of dividends within India, & which carries on operations in India through a branch, income by way of interest (other than interest on securities) or any other sum (other than dividends).
- In case of any other person who carries on business or profession in India through a branch, any sum (other than interest or dividends).
- Interest or other sum should be receivable by branch on its own account – not on account of its head office or other foreign branch, or any other person.

Section 195(3) to (5) - Application to AO to receive interest/other sum without deduction of tax

- **Following conditions to be fulfilled:**
 - ❖ Regularly assessed to tax in India, and filed all returns due before date of application.
 - ❖ Not in default or deemed to be in default of any tax, interest, penalty, fine or any other sum payable under IT Act.
 - ❖ Where the applicant is not a banking company referred to in clause (i) of sub-rule (1)—
 - ✓ Has been carrying on the business/profession in India continuously for period of not less than 5 years immediately preceding date of appln;
 - ✓ Value of fixed assets of such business/profession as per books of account of year preceding date of application exceed Rs.50 lakh.
- Application by banking co in Form 15C, by any other person in Form 15D
- AO may issue certificate if satisfied that all conditions fulfilled, and issue of certificate not prejudicial to interests of revenue
- Certificate valid for financial year specified in certificate, unless cancelled by AO before expiry
- Application for fresh certificate can be made after expiry of earlier certificate, or within 3 months before expiry.

Section 195(6) – Information to be furnished

- Deductor to furnish information relating to payment of any sum whether or not chargeable under the provision of the Act. In terms of Rule 37BB he shall furnish the following:-
- If the payment chargeable under the Act does not exceeds 5 lakh in a FY, information in part A of Form 15CA;
- If the payment chargeable under the Act exceeds 5 lakh in a FY
 - ❖ Information in part B of Form 15CA after obtaining Certificate from AO u/s 197 or Order from AO u/s. 195(2) or 195(3).
 - ❖ Information in part C of Form 15CA after obtaining Certificate in Form 15CB from an accountant.
- If the payment is not chargeable under the Act, information in part D of Form 15CA.
- Information in Form 15CA to be furnished electronically, and signed print-out to be submitted to AD before making remittance.
- The certificate in Form No. 15CB shall be furnished and verified electronically.
- No information, if sum is not taxable, if the payment is by an individual, and does not require prior approval of RBI in terms of section 5 of the FEMA read with Schedule III to the FE (Current Account Transaction) Rules, 2000 or if the remittance is of the nature in specified list.

Section 195 - Miscellaneous issues

- Reimbursement of Cost -No TDS.
- The rate of exchange for the calculation of the value in rupees of such income payable to an assessee outside India shall be the telegraphic transfer buying rate of such currency as on the date on which the tax is required to be deducted at source. "Telegraphic transfer buying rate", in relation to a foreign currency, means the rate of exchange adopted by the SBI for buying such currency. (Rule 26 of IT Rules).
- In the case of a remittance to a country with which a Double Taxation Avoidance Agreement is in force, the tax should be deducted at the rate provided in the Finance Act of the relevant year or at the rate provided in the DTAA, whichever is more beneficial to the assessee. - CBDT Cir No 728 dt 30.10.1995.
- Education cess is only a surcharge and surcharge is only a tax and therefore, education cess or any other surcharge should not be added separately to tax rate as per DTAA.
- Payment of "sum" in kind is also covered. It was held in the case of **Kanchanganga Sea Foods Ltd v CIT 325 ITR 540 (SC)** wherein fishing co chartered 2 fishing vessels from NR Co and gave 85% of fish catch as charter fees.
- In case of **Biocon Biopharmaceuticals (P) Ltd v ITO 144 ITD 615 (Bang)** TDS u/s 195 was held to be deductible even on allotment of shares in exchange for use of technology.

Section 195A - Income payable "net of tax"

- Grossing up where amount payable net of tax.
- Where under an agreement or other arrangement, the tax chargeable on any income referred to in the foregoing provisions of this Chapter is to be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon at the rates in force for the financial year in which such income is payable, be equal to the net amount payable under such agreement or arrangement.
- For example, consider a company has an agreement to pay fees for technical services to a non resident wherein in terms of the contract tax is to be borne by the Indian Company and withholding tax rate as per DTAA is 10% . The formula for grossing up is as follows:
 - Gross Fees for Technical Service = net payment / (1 - tax rate);
 - If fees to be paid is \$100,000 then in order to account for the required 10% TDS deductible on net fees, it will have to be grossed up as follows:-
 - $\$100,000 \times (1 - 0.10) = \$100,000/0.90 = \$1,11,111$
 - Net amount payable after applying rate of TDS @ 10% on an amount of \$111,111 will be \$100,000 after deducting TDS of \$11,111.

Section 195 – Refund of Excess TDS

- **CBDT Cir No 7 dt 23.10.2007**
- Circumstances under which refund claimed:
- contract cancelled and no remittance made to the NR.
- Remittance duly made to the NR, but contract cancelled and remitted amount has been returned to payee
- Contract cancelled after partial execution and no remittance made to the NR for the non-executed part;
- Contract cancelled after partial execution & remittance related to non-executed part made to NR returned to payee, or no remittance made but tax deducted & deposited when amount was credited to account of NR;
- Remitted amount gets exempted from tax either by amendment in law or by notification
- Order passed u/s 154 or 248 or 264 reducing the TDS liability of the payee;
- Deduction of tax twice by mistake from the same income;
- Payment of tax on account of grossing up which was not required;
- Payment of tax at higher rate under domestic law while lower rate prescribed in DTAA;
- Where no income accrued to NR due to cancellation of contract ,or where income has accrued but no tax due on that income, or tax due at lesser rate, amount deposited u/s 195 cannot be said to be tax;
- Where tax deducted at DTAA rates, where DTAA rates higher than IT Act rates.

Section 195 – Refund of Excess TDS

- Amount can be refunded to deductor with prior approval of CCIT/DGIT.
- No interest u/s 244A admissible, since amount is not tax.
- Refund to be granted after obtaining undertaking that no TDS certificate issued to NR.
- Where certificate issued, deductor should obtain it or indemnify IT Dept from possible loss on account of claim of refund by NR.
- Refund to be issued only if NR has not filed return and time limit for filing return expired.
- AO needs to disallow corresponding transaction amount if claimed as expense by deductor .
- Claim for refund to be made within 2 years from end of financial year in which tax deducted at source.
- Form 26B prescribed.