

AAR holds that in case of non-resident companies, filing of return of income in India is mandatory inspite of income not being chargeable to tax in India by applying tax treaty provisions

The Authority for Advance Rulings ('AAR') delivered an important ruling in the case of VNU International BV, deviating from its previous rulings to hold that inspite of income not being chargeable to tax in India by applying tax treaty provisions; a non-resident company is obliged to file a return of income in India.

Facts of the case

- VNU International BV ('the Applicant'), a subsidiary of the Nielsen Company is a tax resident of Netherlands and holds 100 percent of shares of AC Nielsen ONG-MARG Private Limited ('AC Nielsen'), a company incorporated in India.
- ORG-IMS Research Private Limited ('ORG'), an Indian company had entered into a scheme of arrangement with AC Nielsen in the year 2003, whereby the pharmaceutical industry retail research business of AC Nielsen got demerged.
- In the year 2004, the Applicant transferred 50,765 shares of ORG to IMS-AG, a company incorporated in Switzerland.

Issue before the AAR

- Whether any capital gain earned by the Applicant on transfer of 50,765 shares of ORG to IMS-AG would be liable to tax in India as per the provisions of the Income-tax Act, 1961 (the 'Act') and the Double Taxation Avoidance Agreement entered into between India and the Netherlands ('India Netherlands treaty')?
- Whether the transfer of shares by the applicant to IMS-AG would attract transfer pricing provisions under sections 92 to 92F of the Act?
- Whether IMS-AG were liable to withhold tax at source under section 195 of the Act and if so, on what amount should the tax have been deducted?
- If the capital gain is not taxable in India, whether the Applicant is required to file any return of income under section 139 of the Act?

Applicant's contentions

Global Guide to Tax

- [PERE together with Taxand produced the 2011 global guide to tax, advising on real estate investment opportunities. Click here to view guide.](#)
- [BMR Advisors, in association with, IPPAI, has produced a survey report "Impact of Taxation on the Energy Value Chain & Electricity Prices in India", analyzing the present regulatory and policy framework for the energy sector. Click here to view report.](#)

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Contributors

- The Applicant submitted that as ORG is an Indian company, the situs of its shares would be in India. Accordingly, any capital gain earned by the Applicant on the transfer of shares of ORG would be taxable in India.
- However, the Applicant being a tax resident of Netherlands, it was eligible to opt for the provisions of India Netherlands treaty. The Applicant submitted that the transfer of shares of ORG by the applicant would be governed by Article 13(5) of the India Netherlands treaty which states that gains from the alienation of shares shall be taxable only in the country of which the alienator is a resident, ie in Netherlands. The Article further states that if the purchaser of shares is a resident of India then such gains will still not be taxable in India if such gains are realized in the course of a corporate organization, re-organization, amalgamation, division or similar transaction and the buyer or the seller owns at least 10 percent of the capital of the other. As the shares of ORG are transferred to IMS-AG which is a tax resident of Switzerland, any capital gains earned by the Applicant would be taxable only in Netherlands. The said capital gains would not be taxable in India.
- The Applicant further submitted that the transfer pricing provisions are merely machinery sections and would apply only where the transaction entered into by the foreign assessee is liable to tax in India. Accordingly, as the said transfer of shares of ORG by the Applicant is not liable to tax in India, the transfer pricing regulation would not apply.
- Similarly, Section 195 of the Act would have no application as capital gains on transfer of shares of ORG by the Applicant are not taxable in India.
- As regards filing of return of income, the Applicant submitted that as the income is not taxable in India, it is not under any obligation to file the return of income under section 139(1) of the Act. Section 139(1) of the Act is merely a machinery section and would apply only where the transaction entered into by the foreign assessee is liable to be taxed in India. Reliance was also placed in this regard on the AAR Rulings pronounced in the cases of Venenburg Group B V (289 ITR 464), Dana Corporation (321 ITR 178) and Amiantit Intl Holding Ltd (322 ITR 678) ([Click here](#) for BMR analysis of Amiantit AAR ruling).

Revenue's contentions

- The Revenue agreed with the Applicant's contentions on all grounds except the contention raised by the Applicant in response to filing of return of income in India.
- The Revenue contended that the first step is determining whether a particular source of income is taxable in India. If that particular source of income is also taxable in the other country, then the second step is to see whether there is a tax treaty entered into between both the countries and if the same is in affirmative which country is vested with the taxing rights.

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- The Revenue further contended that both the steps mentioned above are a part of an exercise carried out under the Act. While doing so, compliance to machinery provisions under Section 139(1) of the Act assumes importance especially when the questions raised before the AAR by the Applicant are on the basis of a single transaction.

Ruling of the AAR

- The AAR noted that while casting obligation to file return of income by a company, the legislature in its wisdom has omitted to include the expression 'exceeded the maximum amount which is not chargeable to income-tax' under the provisions of Section 139(1) of the Act. Further, as per the third proviso of Section 139(1), every company is required to file its return of income, whether it has an income or a loss.
- The AAR further noted that the Applicant being a foreign company, is covered within the definition of a company under section 2(17) of the Act. There is also no dispute that the income arising from the sale of shares is liable to be taxed in India by virtue of section 5 (2) of the Act, although the right to tax the same is vested with Netherlands by virtue of the India Netherlands treaty.
- The AAR observed that if power to tax is granted it is difficult to appreciate the argument that when the resulting income is nil, there is no obligation to file return of income. It further observed that where it is not necessary for a non-resident to furnish return of income under section 139(1) of the Act, the statute has specifically provided so, as in the case under Section 115AC(4) of the Act.
- Section 245S of the Act states that the ruling pronounced by the AAR is binding unless there is a change in law or facts on the basis of which the advance ruling has been pronounced. Thus, it is necessary to have all the facts connected with the question on which ruling is sought or is proposed to be sought by way of return of income as against merely filing of an application seeking advance ruling in the prescribed form. Given this, the Applicant has to file a return of income to substantiate the facts based on which an application is made to the AAR.
- The AAR finally ruled after taking the above into consideration that the Applicant would be obliged to file a return of income under Section 139(1) of the Act even if its income is not chargeable to tax in India by virtue of the provisions of the India Netherlands treaty. It further stated that instead of causing inconvenience, the process of filing of return of income would facilitate the Applicant in all future interactions with the Income tax department.

BMR comments and analysis

This is a key ruling rendered by the AAR for return filing obligation in case of non-resident companies whose income is not chargeable to tax in India by applying tax treaty provisions.

The AAR had earlier delivered a similar ruling in the case of XYZ / ABC Equity Fund vs CIT (116 Taxman 719) wherein it had held that the assessee cannot be allowed to prejudge the issues and decide for himself not to file a return of income if he is of the view that he will not have any taxable income at all in India.

However, the AAR in the recent past in the cases of Venenburg Group BV (289 ITR 464), Dana Corporation (321 ITR 178) and Amiantit Intl Holding Ltd (322 ITR 678) had delivered rulings which are in contrast to the above holding that Section 139(1) of the Act is merely a machinery section and would apply only where the transaction entered into by the foreign taxpayers is liable to be taxed in India.

This ruling again sparks off the debate on whether filing of a return of income by non-resident companies is mandatory when there is no income chargeable to tax in India by virtue of the provisions of the tax treaty agreement entered into by two countries. This ruling may cause genuine inconvenience / hardship to non-resident companies who have income chargeable to tax in India but the same is not brought to tax in India by virtue of the tax treaty agreements.

The AAR rulings are binding on the department and the Applicant who had sought it. However, the same do have persuasive value. Based on this ruling, the Indian revenue authorities may seek to issue notices to non-resident companies who have had chargeable income in India in the past but the same had not been brought to tax in India by virtue of the tax treaty provisions. This ruling will increase the compliance burden for non-resident companies in India.

Position under the DTC

Section 144(1) of the DTC Bill, 2010 states that every person shall furnish a return of tax bases on or before the due date to the Assessing Officer or such other authority or agency as may be prescribed.

Sub-section (2) of Section 144 lists down the persons in relation to whose income they are liable to file a return of tax bases. A company is included amongst various other persons. However, it is pertinent to note that the expression 'exceeds the threshold limit' is assigned specifically to an individual, or Hindu undivided family or an artificial juridical person. It is not assigned to a company.

Thus the provisions related to filing of return of income are similarly worded in the DTC Bill, 2010 as well.

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