Taxation Of Dividend Received By Foreign Holding Companies From Indian Subsidiary w.e.f 1st April, 2020

Income tax provisions on taxability of Dividend Income

Background: Until 31st March, 2020 (AY 20-21) dividend from an Indian company, was not liable to tax u/s 10(34) of the Income Tax Act, 1961. Consequently, the domestic company was required to pay Dividend Distribution Tax (DDT) under section 115-O. Thus, when DDT was paid by the payer company, and receipt of dividend was exempt in the hands of shareholders being Foreign Companies.

Tax implications in the hands of Foreign companies w.e.f 1.4.2020 - AY 21-22 onwards:

Dividend Income received by a foreign company from an Indian company is taxable under the 'head other sources'. (One exception being dividend is attributable to Permanent Establishment (PE) of foreign company in India). In that case the dividend income will be taxable as Business Income.

This will apply to the dividend distributed on or after 01-04-2020. (Sections 9(1)(iv) read with 5(2)(b) of the Income Tax Act, 1961.)

The tax rate on dividend income will be 20% (plus surcharge and cess as applicable). However, the foreign company can claim the treaty benefits subject to the conditions mentioned in that treaty between India and the country where Investor Company is tax resident.

Section 115A of the Income Tax Act, 1961 deals with the provisions related to determination of tax in respect of dividends, royalty and technical fees in the case of foreign companies. Whereas section 115E of the Income Tax Act, 1961 deals with taxation of dividends on shares held as investments by foreign company at 20% (plus surcharge and cess as applicable) if the shares were purchased in foreign currency.

Tax deducted at source (TDS) on Dividend Income

Indian companies will have to deduct withholding tax (TDS) before payment of dividend to the foreign company. The TDS (without surcharge and cess) will be as under (section 195 read with section 5,9,90,91, 115A and 206AA):

Shareholder Situation	Withholding tax
No PAN, No TRC#	20%
No PAN, TRC available	Treaty Rate (since most countries rate is lower than 40%)
PAN available , No TRC	20%
PAN & TRC available	Beneficial rate as per Income Tax Act and Treaty (generally 10%)

 # TRC: Tax residency certificate provided by the foreign company to prove its tax residential status in home country.

Proofs required in case the foreign company wants to claim the treaty benefit:

Dividend income is generally chargeable to tax in the source country (India) as well as the country of residence (Foreign country) of the foreign company and, consequently, country of residence provides a credit of taxes paid by the taxpayer in the source (India) country. Thus, the dividend income shall be taxable in India as per provisions of the Act or as per relevant DTAA, whichever is more beneficial.

The following documents will be required from the foreign company if it is entitled to treaty benefit:

i. Tax Residency Certificate (TRC) from the foreign company

ii. Self declaration in Form 10F/Letter of Representation

iii. a. that the non-resident shareholder receiving the dividend income is the beneficial owner of such income and that shareholding existed upto minimum of 365 days if the treaty partner has signed MLI (CTA).

b. that Dividend income is not attributable or effectively connected to any Permanent Establishment (PE) or Fixed Base in India.

#(Point iii. is not applicable in case the home country has not opted for Article 8 of MLI since, there will be no impact on Article 10 of the CTA – Dividend Income).

 # The Multilateral Instrument (MLI) is an outcome of BEPS Action 15 of the OECD/G20 Inclusive Framework. It offers a mechanism/ common platform for governments to swiftly transpose results from the BEPS into their bilateral tax treaties worldwide. This has brought significant changes in the existing Double Tax Avoidance Agreements (DTAA) which are now called the Covered Tax Agreements (CTA).

Liability to file Return of Income in India by the foreign company:

The foreign company not required to submit/file its return on income in India if it meets certain conditions.

The condition specifies that; the withholding of taxes on dividend should have been at the rate of 20% (plus surcharge and cess as applicable) and that total income consists of dividend income only. This implies that the withholding tax should be at 20% (plus surcharge and cess as applicable). (Section 115A (5))

Compliance by Indian companies while remitting dividend to Foreign Company

The Indian payer company is required to file **Form 15CB/15CA** stating the information of transaction i.e.

i. Name of the Foreign Company
ii. Nature of payment
iii. Gross amount of dividend
iv. Rate of Withholding Tax
v. Article under of the treaty claimed

The Indian subsidiary company is required to file the return of TDS in Form 27Q.

a) After filing of TDS - return, the Indian company must issue TDS certificate (in Form 16A)
b) This certificate will be the documentary evidence for the Foreign Company to claim tax credit.