

Interest income need not to be assessed when assessee is a Non-resident

The Income Tax Appellate Tribunal, Mumbai (“**the ITAT**”) in the case of *JCIT v. Rahul Rajnikant Parikh [I.T.A. No. 638,639,640/Mum/2022 dated October 20, 2022]* held that the interest income need not be assessed when assessee is a Non-resident.

Facts:

Rahul Rajnikant Parikh (“**the Respondent**”) was a Non- resident under Income Tax Act, 1961 (“**the IT Act**”). It came to the notice of the Government that the Respondent had a bank account, which he was operating jointly in HSBC Bank, Geneva. It was noticed that some deposits have been made in this bank account during the years relevant to Assessment Years (“**A.Y.**”) 2003-04 & 2004-05. In the three next A.Y. namely 2006-07 to 2008-09 interest has been credited on the deposits so made in the above said bank account.

In the first round, the deposit amounts as well as interest income accrued on the above said deposits were assessed in the hands of the Respondent dividing the same equally. The additions were made of Rs. 89,197, Rs. 99,284 and Rs. 150,139 respectively for the three A.Y respectively. These assessments were challenged by the Respondent before the Commissioner of Income-Tax (Appeals) (“**CIT(A)**”) who deleted these additions.

The Revenue department (“**the Appellant**”) then filed an appeal before the ITAT challenging the order of CIT(A) of deletion of the additions. The ITAT restored the matter and sent back the file to the Assessing Officer (“**A.O.**”) with the direction to make further investigation into the source of deposits made into the bank account. The AO assessed the interest income on the hands of the Respondent on the grounds that interest income shall be “deemed to have accrued” as per Section 9 of IT Act to the Respondent in India since the corresponding deposit amount has been assessed in the hands of the Respondent in A.Y. 2003-04 & 2004-05.

Issue:

Whether the interest income can be assessed in the hands of a Non-resident from deposits made in a Foreign bank?

Held:

The ITAT held as under:

- Section 5(2) of the IT Act defines the scope of total income which can be taxed in India in the hands of “non-resident”. The income accrued in India in the hands of Non-resident can be taxed, however, the issue in the present case is related to the interest on Income accrued. Section 5(2) of the IT Act is limited to extent of income only.
- Section 9 (1)(v) of the IT Act lists out three situations in which an interest income could be deemed to accrue or arise in India, namely:
 - payment of interest income by Government of India;
 - payment of interest by a resident;
 - payment of interest income by a non-resident, where the non-resident has used the borrowed money in India in his business

The first two conditions are not applicable in the present case and even the third is not applicable because it is not the case that the HSBC bank has used the deposits for the purpose of business or profession in India. Therefore, all three conditions are not satisfied.

- Reading Section 5(2) and Section 9(1)(v) of the IT Act reveals that if any income is deemed to accrue or arise in India, then the same could be taxed in the hands of non-residents also. However, the same cannot be applicable to the interest.

- Therefore, the interest income cannot be assessed in the hands of the Respondent since they are Non-residents and the income is actually accrued outside India.

Hence, the Appeal filed by the Revenue was dismissed.

Relevant Provisions:

Income Tax Act, 1961:

Section 9: Income deemed to accrue or arise in India

(1) The following incomes shall be deemed to accrue or arise in India :-

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

Explanation 1.-For the purposes of this clause-

(a) in the case of a business, other than the business having business connection in India on account of significant economic presence, of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India;

(b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export ;

(c) in the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India;

(d) in the case of a non-resident, being-

(1) an individual who is not a citizen of India ; or

*(2) a firm which does not have any partner who is a citizen of India or who is resident in India ;
or*

*(3) a company which does not have any shareholder who is a citizen of India or who is resident
in India,*

*no income shall be deemed to accrue or arise in India to such individual, firm or company
through or from operations which are confined to the shooting of any cinematograph film in
India.*

*(e) in the case of a foreign company engaged in the business of mining of diamonds, no income
shall be deemed to accrue or arise in India to it through or from the activities which are confined
to the display of uncut and unassorted diamond in any special zone notified by the Central
Government in the Official Gazette in this behalf.*

*Explanation 2.-For the removal of doubts, it is hereby declared that "business connection" shall
include any business activity carried out through a person who, acting on behalf of the non-
resident,-*

*(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the
non-resident or habitually concludes contracts or habitually plays the principal role leading to
conclusion of contracts by that non-resident and the contracts are—*

(i) in the name of the non-resident; or

*(ii) for the transfer of the ownership of, or for the granting of the right to use, property owned
by that non-resident or that non-resident has the right to use; or*

(iii) for the provision of services by the non-resident; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business :

Provided further that where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal non-resident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

Explanation 2A.-For the removal of doubts, it is hereby declared that the significant economic presence of a non-resident in India shall constitute "business connection" in India and "significant economic presence" for this purpose, shall mean-

(a) transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed; or

(b) systematic and continuous soliciting of business activities or engaging in interaction with such number of users in India, as may be prescribed:

Provided that the transactions or activities shall constitute significant economic presence in India, whether or not-

(i) the agreement for such transactions or activities is entered in India; or

(ii) the non-resident has a residence or place of business in India; or

(iii) the non-resident renders services in India:

Provided further that only so much of income as is attributable to the transactions or activities referred to in clause (a) or clause (b) shall be deemed to accrue or arise in India.

Explanation 3.-Where a business is carried on in India through a person referred to in clause (a) or clause (b) or clause (c) of Explanation 2, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India;

Explanation 3A.—For the removal of doubts, it is hereby declared that the income attributable to the operations carried out in India, as referred to in Explanation 1, shall include income from—

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(i) such advertisement which targets a customer who resides in India or a customer who accesses the advertisement through internet protocol address located in India;

(ii) sale of data collected from a person who resides in India or from a person who uses internet protocol address located in India; and

(iii) sale of goods or services using data collected from a person who resides in India or from a person who uses internet protocol address located in India.

Provided that the provisions contained in this Explanation shall also apply to the income attributable to the transactions or activities referred to in Explanation 2A.

Explanation 4.-For the removal of doubts, it is hereby clarified that the expression "through" shall mean and include and shall be deemed to have always meant and included "by means of", "in consequence of" or "by reason of".

Explanation 5.-For the removal of doubts, it is hereby clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.;

Provided that nothing contained in this Explanation shall apply to an asset or capital asset, which is held by a non-resident by way of investment, directly or indirectly, in a Foreign Institutional Investor as referred to in clause (a) of the Explanation to section 115AD for an assessment year commencing on or after the 1st day of April, 2012 but before the 1st day of April, 2015:

Provided further that nothing contained in this Explanation shall apply to an asset or capital asset, which is held by a non-resident by way of investment, directly or indirectly, in Category-I or Category-II foreign portfolio investor under the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2014 34prior to their repeal, made under the Securities and Exchange Board of India Act,1992.". (15 of 1992.)

Provided also that nothing contained in this Explanation shall apply to an asset or a capital asset, which is held by a non-resident by way of investment, directly or indirectly, in Category-I foreign portfolio investor under the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2019, made under the Securities and Exchange Board of India Act, 1992. (15 of 1992.);

Provided also that nothing contained in this Explanation shall apply to-

(i) an assessment or reassessment to be made under section 143, section 144, section 147 or section 153A or section 153C; or

(ii) an order to be passed enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154; or

(iii) an order to be passed deeming a person to be an assessee in default under sub-section (1) of section 201,

in respect of income accruing or arising through or from the transfer of an asset or a capital asset situate in India in consequence of the transfer of a share or interest in a company or entity registered or incorporated outside India made before the 28th day of May, 2012:

Provided also that where-

(i) an assessment or reassessment has been made under section 143, section 144, section 147 or section 153A or section 153C; or

(ii) an order has been passed enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154; or

(iii) an order has been passed deeming a person to be an assessee in default under sub-section (1) of section 201; or

(iv) an order has been passed imposing a penalty under Chapter XXI or under section 221,

in respect of income accruing or arising through or from the transfer of an asset or a capital asset situate in India in consequence of the transfer of a share or interest in a company or entity registered or incorporated outside India made before the 28th day of May, 2012 and the person in whose case such assessment or reassessment or order has been passed or made, as the case

may be, fulfils the specified conditions, then, such assessment or reassessment or order, to the extent it relates to the said income, shall be deemed never to have been passed or made, as the case may be:

Provided also that where any amount becomes refundable to the person referred to in fifth proviso as a consequence of him fulfilling the specified conditions, then, such amount shall be refunded to him, but no interest under section 244A shall be paid on that amount.

Explanation.-For the purposes of fifth and sixth provisos, the specified conditions shall be as provided hereunder:-

(i) where the said person has filed any appeal before an appellate forum or any writ petition before the High Court or the Supreme Court against any order in respect of said income, he shall either withdraw or submit an undertaking to withdraw such appeal or writ petition, in such form and manner as may be prescribed;

(ii) where the said person has initiated any proceeding for arbitration, conciliation or mediation, or has given any notice thereof under any law for the time being in force or under any agreement entered into by India with any other country or territory outside India, whether for protection of investment or otherwise, he shall either withdraw or shall submit an undertaking to withdraw the claim, if any, in such proceedings or notice, in such form and manner as may be prescribed;

(iii) the said person shall furnish an undertaking, in such form and manner as may be prescribed, waiving his right, whether direct or indirect, to seek or pursue any remedy or any claim in relation to the said income which may otherwise be available to him under any law for the time being in force, in equity, under any statute or under any agreement entered into by India with any country or territory outside India, whether for protection of investment or otherwise; and

(iv) such other conditions as may be prescribed.

Explanation 6.-For the purposes of this clause, it is hereby declared that-

(a) the share or interest, referred to in Explanation 5, shall be deemed to derive its value substantially from the assets (whether tangible or intangible) located in India, if, on the specified date, the value of such assets-

(i) exceeds the amount of ten crore rupees; and

(ii) represents at least fifty per cent. of the value of all the assets owned by the company or entity, as the case may be;

(b) the value of an asset shall be the fair market value as on the specified date, of such asset without reduction of liabilities, if any, in respect of the asset, determined in such manner as may be prescribed;

(c) "accounting period" means each period of twelve months ending with the 31st day of March:

Provided that where a company or an entity, referred to in Explanation 5, regularly adopts a period of twelve months ending on a day other than the 31st day of March for the purpose of-

(i) complying with the provisions of the tax laws of the territory, of which it is a resident, for tax purposes; or

(ii) reporting to persons holding the share or interest,

then, the period of twelve months ending with the other day shall be the accounting period of the company or, as the case may be, the entity:

Provided further that the first accounting period of the company or, as the case may be, the entity shall begin from the date of its registration or incorporation and end with the 31st day

of March or such other day, as the case may be, following the date of such registration or incorporation, and the later accounting period shall be the successive periods of twelve months:

Provided also that if the company or the entity ceases to exist before the end of accounting period, as aforesaid, then, the accounting period shall end immediately before the company or, as the case may be, the entity, ceases to exist.

(d) "specified date" means the-

(i) date on which the accounting period of the company or, as the case may be, the entity ends preceding the date of transfer of a share or an interest; or

(ii) date of transfer, if the book value of the assets of the company or, as the case may be, the entity on the date of transfer exceeds the book value of the assets as on the date referred to in sub-clause (i), by fifteen per cent:

Explanation 7.- For the purposes of this clause,-

(a) no income shall be deemed to accrue or arise to a non-resident from transfer, outside India, of any share of, or interest in, a company or an entity, registered or incorporated outside India, referred to in the Explanation 5,-

(i) if such company or entity directly owns the assets situated in India and the transferor (whether individually or along with its associated enterprises), at any time in the twelve months preceding the date of transfer, neither holds the right of management or control in relation to such company or entity, nor holds voting power or share capital or interest exceeding five per cent. of the total voting power or total share capital or total interest, as the case may be, of such company or entity; or

(ii) if such company or entity indirectly owns the assets situated in India and the transferor (whether individually or along with its associated enterprises), at any time in the twelve months

preceding the date of transfer, neither holds the right of management or control in relation to such company or entity, nor holds any right in, or in relation to, such company or entity which would entitle him to the right of management or control in the company or entity that directly owns the assets situated in India, nor holds such percentage of voting power or share capital or interest in such company or entity which results in holding of (either individually or along with associated enterprises) a voting power or share capital or interest exceeding five per cent. of the total voting power or total share capital or total interest, as the case may be, of the company or entity that directly owns the assets situated in India;

(b) in a case where all the assets owned, directly or indirectly, by a company or, as the case may be, an entity referred to in the Explanation 5, are not located in India, the income of the non-resident transferor, from transfer outside India of a share of, or interest in, such company or entity, deemed to accrue or arise in India under this clause, shall be only such part of the income as is reasonably attributable to assets located in India and determined in such manner as may be prescribed;

(c) "associated enterprise" shall have the meaning assigned to it in section 92A;

(ii) income which falls under the head "Salaries", if it is earned in India.

Explanation.-For the removal of doubts, it is hereby declared that the income of the nature referred to in this clause payable for-

(a) service rendered in India; and

(b) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment,

shall be regarded as income earned in India ;

(iii) income chargeable under the head "Salaries" payable by the Government to a citizen of India for service outside India;

(iv) a dividend paid by an Indian company outside India ;

(v) income by way of interest payable by-

(a) the Government ; or

(b) a person who is a resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(c) a person who is a non-resident, where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India ;

Explanation.-For the purposes of this clause,-

(a) it is hereby declared that in the case of a non-resident, being a person engaged in the business of banking, any interest payable by the permanent establishment in India of such non-resident to the head office or any permanent establishment or any other part of such non-resident outside India shall be deemed to accrue or arise in India and shall be chargeable to tax in addition to any income attributable to the permanent establishment in India and the permanent establishment in India shall be deemed to be a person separate and independent of the non-resident person of which it is a permanent establishment and the provisions of the Act relating to computation of total income, determination of tax and collection and recovery shall apply accordingly;

(b) “permanent establishment” shall have the meaning assigned to it in clause (iiia) of section 92F;

(vi) income by way of royalty payable by-

(a) the Government ; or

(b) a person who is a resident, except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(c) a person who is a non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum consideration for the transfer outside India of, or the imparting of information outside India in respect of, any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process or trade mark or similar property, if such income is payable in pursuance of an agreement made before the 1st day of April, 1976, and the agreement is approved by the Central Government :

Provided further that nothing contained in this clause shall apply in relation to so much of the income by way of royalty as consists of lump sum payment made by a person, who is a resident, for the transfer of all or any rights (including the granting of a licence) in respect of computer software supplied by a non-resident manufacturer along with a computer or computer-based equipment under any scheme approved under the Policy on Computer Software Export, Software Development and Training, 1986 of the Government of India.

Explanation 1.-For the purposes of the 10first proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date; so, however, that, where the recipient of the income by way of royalty is a foreign company, the agreement shall not be deemed to have been made before that date unless, before the expiry of the time allowed under sub-section (1) or sub-section (2) of section 139 (whether fixed originally or on extension) for furnishing the return of income for the assessment year commencing on the 1st day of April, 1977, or the assessment year in respect of which such income first becomes chargeable to tax under this Act, whichever assessment year is later, the company exercises an option by furnishing a declaration in writing to the 11Assessing Officer (such option being final for that assessment year and for every subsequent assessment year) that the agreement may be regarded as an agreement made before the 1st day of April, 1976.

Explanation 2.-For the purposes of this clause, "royalty" means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains") for-

(i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(ii) the imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iii) the use of any patent, invention, model, design, secret formula or process or trade mark or similar property ;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill ;

(iva) the use or right to use any industrial, commercial or scientific equipment but not including the amounts referred to in section 44BB;

(v) the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting; or

(vi) the rendering of any services in connection with the activities referred to in sub-clauses (i) to 13(iv), (iva) and (v).

Explanation 3.-For the purposes of this clause, "computer software" means any computer programme recorded on any disc, tape, perforated media or other information storage device and includes any such programme or any customized electronic data;

Explanation 4.-For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.

Explanation 5.-For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not-

(a) the possession or control of such right, property or information is with the payer;

(b) such right, property or information is used directly by the payer;

(c) the location of such right, property or information is in India.

Explanation 6.-For the removal of doubts, it is hereby clarified that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret;'

(vii) income by way of fees for technical services payable by-

(a) the Government ; or

(b) a person who is a resident, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or

(c) a person who is a non-resident, where the fees are payable in respect of services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India :

Provided that nothing contained in this clause shall apply in relation to any income by way of fees for technical services payable in pursuance of an agreement made before the 1st day of April, 1976, and approved by the Central Government.

Explanation 1.-For the purposes of the foregoing proviso, an agreement made on or after the 1st day of April, 1976, shall be deemed to have been made before that date if the agreement is made in accordance with proposals approved by the Central Government before that date.

Explanation 2.-For the purposes of this clause, "fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".

(viii) income arising outside India, being any sum of money referred to in sub-clause (xviiia) of clause (24) of section 2, paid on or after the 5th day of July, 2019 by a person resident in India to a non-resident, not being a company, or to a foreign company.

(2) Notwithstanding anything contained in sub-section (1), any pension payable outside India to a person residing permanently outside India shall not be deemed to accrue or arise in India, if the pension is payable to a person referred to in article 314 of the Constitution or to a person who, having been appointed before the 15th day of August, 1947, to be a Judge of the Federal Court or of a High Court within the meaning of the Government of India Act, 1935, continues to serve on or after the commencement of the Constitution as a Judge in India.

Explanation.-For the removal of doubts, it is hereby declared that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India under clause (v) or clause (vi) or clause (vii) of sub-section (1) and shall be included in the total income of the nonresident, whether or not,-

(i) the non-resident has a residence or place of business or business connection in India; or

(ii) the non-resident has rendered services in India.

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