

# **J. B. Nagar CPE Study Circle - ICAI**

**Intensive Course on Income Tax**

**Deemed accrual - Interest, Royalty  
and Fees for Technical Services**

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**Naresh Ajwani  
Partner  
Rashmin Sanghvi & Associates  
Chartered Accountants**

# Scope of the Presentation

## Incomes and taxation

- Interest, Royalties, FTS

## Sections

9(1), clauses (v), (vi) and (vii)

- Taxation of above income

44D, 44DA, 115A

# Scope of the Presentation

- Some basic concepts – briefly.
- Common features of taxation of interest, royalty and FTS.
- Meaning of interest, royalty and FTS.  
Along with the meaning, taxation and some issues with respect to these incomes.

# Accrual of income

- Accrual of income is relevant for:
  - A “resident” to determine the year in which income is taxable.
  - A “non-resident” (and NOR) to determine not only the year, but whether income is taxable in India or not.
  - A person “returning to or leaving India” to determine whether income is taxable and the year.

# Income accruing in India

- Income accruing in India:

Debt should become due to the person.

Place of accrual should be in India.

Income should accrue within the previous year concerned.

# Deemed accrual of income

- Income deemed to accrue in India – section 9.

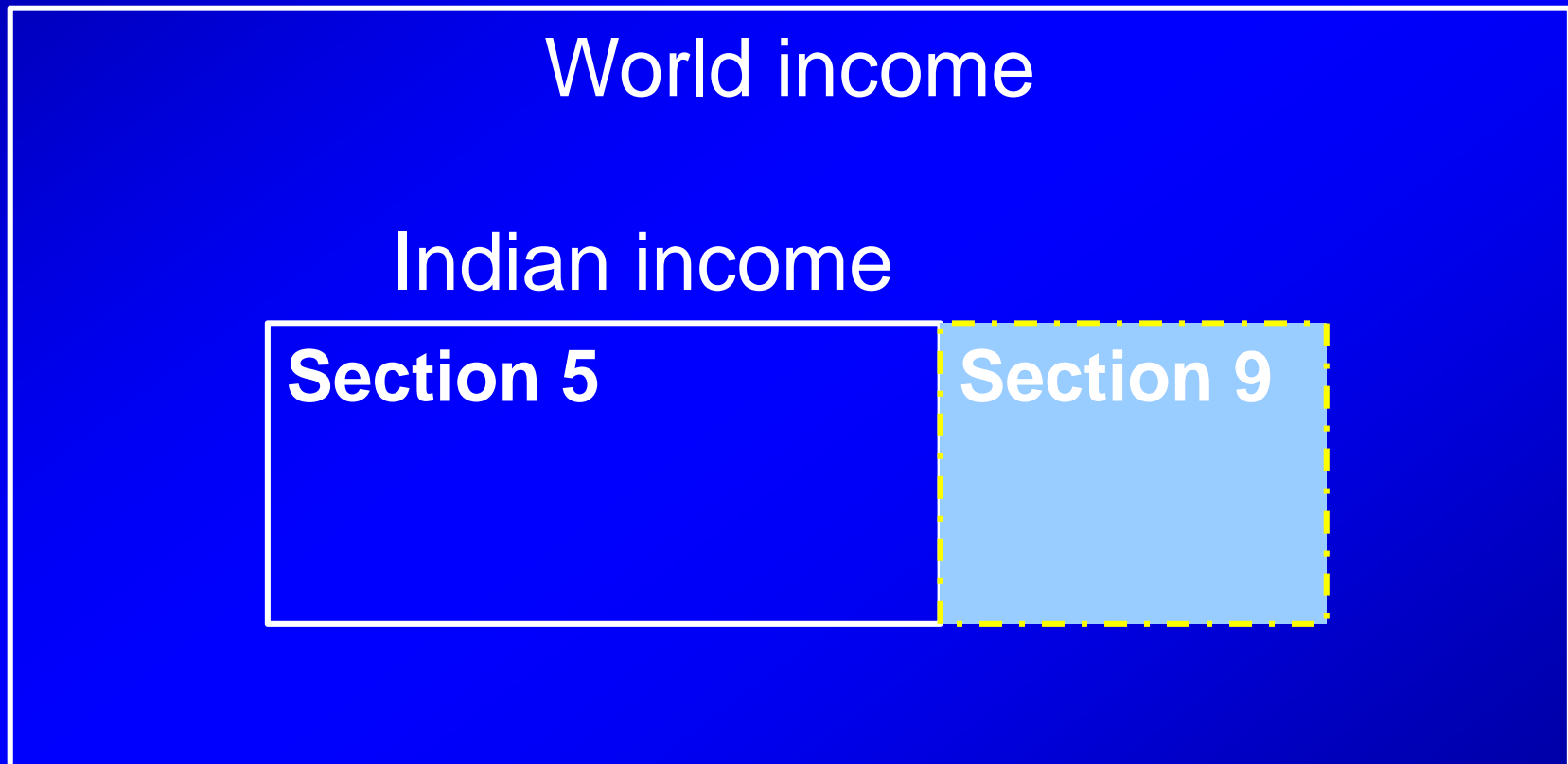
## Deeming Fiction – Section 9:

- Expands the scope of total income.
- Income actually does not accrue, but is fictionally deemed to accrue in India.
- Interpret it strictly. However the scope is so wide .....

# Income deemed to accrue in India

- Deemed to accrue in India – section 9:  
Income is deemed to accrue in India due to:
  - Business connection in India.
  - Property, asset, “source” of income in India.
  - Transfer of Capital asset situated in India.

# Income deemed to accrue in India





# Interest, Royalty, FTS

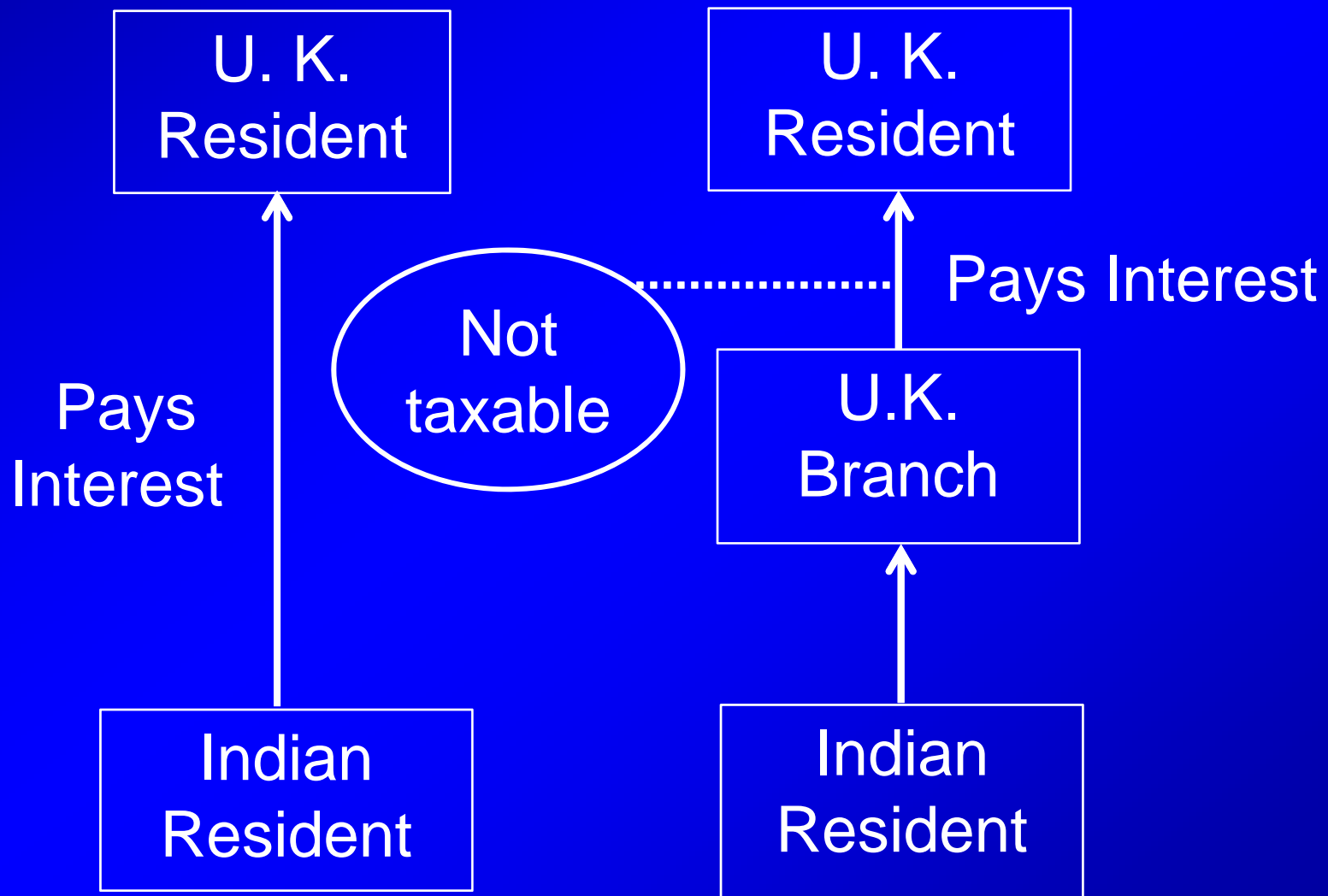
- Income is deemed to accrue in India if payment is by:
  - Government.
  - Indian resident – unless loan, services, property is used for business outside India or for earning income from source outside India.

# Interest, Royalty, FTS

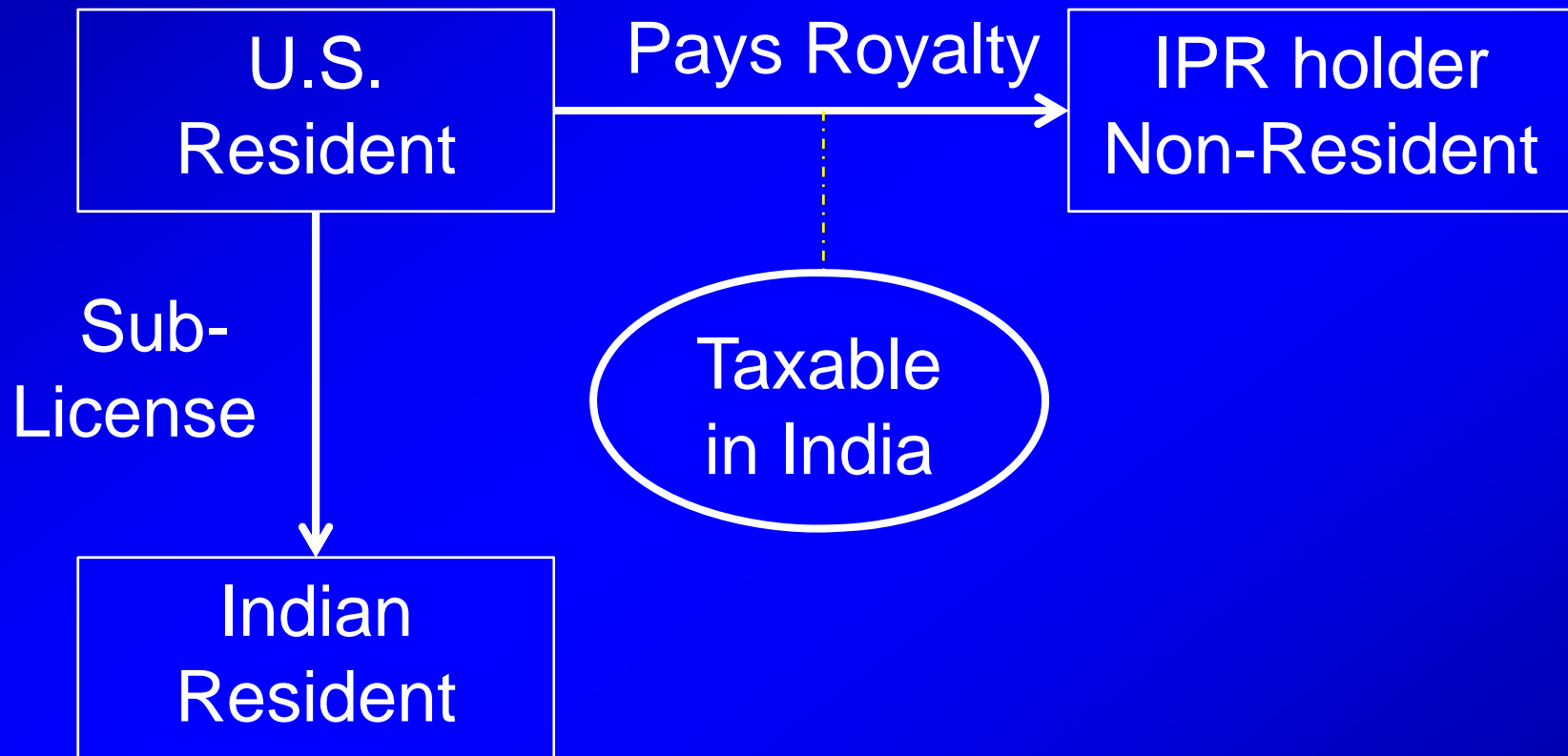
- Non-resident if property, service is used for business in India; or loan, property, service is used for earning income from source in India.

[Section 9(1) – clauses (v), (vi), (vii)]

# E.g. Business outside India



# E.g. Source in India



# Interest, Royalty, FTS

- Concessional tax rate is specified under Section 115A.  
No deduction of expenses is allowed.
- If Section 115A is not applicable, normal provisions apply.
- For royalty and FTS, if there is a PE, then under section 44DA, net profit is taxable.

# Interest, Royalty, FTS

- Income is deemed to accrue in India whether the non-resident:
  - has residence or place of business or business connection in India, or
  - has rendered services in India.

[Explanation to S. 9]

# Interest - meaning

- Interest is defined in S. 2(28A). It means:
  - interest on debt of any kind.
  - service fee or other charge in respect of debt, or unutilised credit facility.

# Interest

- Loan given in **rupees** by non-resident –  
No tax relief. Regular tax is payable.
- Loan given in **foreign currency** – lower rate of tax u/s. 115A on GROSS interest.
- No expenses are allowed.



# Tax on Interest – S. 115A

## I. Normal foreign currency loan:

- Loan should be borrowed in Foreign Currency.

Foreign Currency  $\neq$  Foreign Exchange.

- Interest is received from Government or Indian concern.
- Tax is payable @ 20% [plus SC & EC] on GROSS interest.

# Tax on Interest – S. 115A

## II. Loan by infrastructure debt fund:

- Tax is payable @ 5% [plus SC & EC] on GROSS interest.

# Tax on Interest – S. 115A

## III. Specific Loans:

- Loan is borrowed between 1.7.2012 and 30.6.2015 in foreign currency.
- There is a loan agreement or Long term infrastructure bonds have been issued.
- Government approval is obtained.
- Tax = 5% on GROSS interest payable upto rate approved.

Tax on the excess interest?

# Tax on Interest – S. 115A

- Income-tax return not to be filed if:
  - Income comprises only of interest.
  - Full tax has been deducted at source.
- “Indian concern” – not defined.

CBDT circular 740 dated 17.4.1996 - interest payable by an India branch of a foreign bank is taxable @ 20% - Indian branch is a separate entity.

# Tax on Interest

- Can one earn interest out of own self?
- ABN Amro – Kolkata Tribunal.  
Interest payable by branch to HO is not deductible.
- Dresdner Bank – Mumbai Tribunal.  
Interest earned by branch from HO is taxable.

# Royalty - meaning

- Consideration including lumpsum consideration for various kinds of uses of properties as under:
- i) Patent, etc. (generally IPR is patented).
  - Transfer of all or any rights (including grant of a licence)
  - Imparting of information concerning the working of, or the use of the properties.
  - Use of the properties.

# Royalty - meaning

- ii) Technical, industrial, commercial or scientific **knowledge, experience or skill**:
  - Imparting of information concerning the above.
- iii) Industrial, ... **equipment** (excluding S.44BB payments – oil exploration related):
  - Use or right to use the above.

# Royalty - meaning

- iv) Copyright, literary, artistic or scientific work including films, .... (**generally there is a copyright**):
  - Transfer of all or any rights (including grant of a licence).However sale, distribution or exhibition of cinematograph films is excluded.
- v) Rendering of any **services** in connection with the activities referred to above.



# Royalty - meaning

- What is not royalty?  
Capital Gain.  
Outright purchase of design, etc.

# Royalty - meaning

- **Finance Act 2012 – Explanations 4,5 and 6 inserted with effect from 1.6.1976.**
- **Right to use software irrespective of the medium.**

# Royalty - meaning

- Finance Act 2012 contd...
- It is not relevant whether right, property or information:
  - is in possession or control of payer.
  - is used directly by the payer.
  - is located in India or not.
- Process shall mean transmission by satellite ... whether the process is secret or not.

# FTS - meaning

- Consideration including lumpsum consideration for:
  - rendering managerial, technical or consultancy services.
  - provision of services of technical or other personnel.
- However it does not include consideration:
  - for any construction, etc.
  - which amount to salaries.

# Tax on Royalty/FTS – S.115A

- Income is earned from Government or an Indian concern.
- It should not be connected to the PE – u/s. 44DA.
- There should be an agreement with Indian concern which should be:
  - approved by Central Government, or
  - be in accordance with the Industrial Policy.

# Tax on Royalty/FTS – S.115A

- Tax rate:
  - 30% - if agreement is entered into upto 31.5.1997.
  - 20% - if agreement is entered into between 1.6.97 to 31.5.2005.
  - 10% - if agreement is entered into on or after 1.6.2005.

# Tax on Royalty/FTS – S.115A

- Royalty for license of book or computer software to an Indian resident – condition of Government approval, or Industrial policy is not applicable.

Books and software should be permitted to be imported under import policy.

Software – defined in Explanation (b) to S.80HHE. It includes customised data or product or service as notified.

# Tax on Royalty/FTS – S.115A

- No deduction of expenses is allowed.
- Deduction is available under Chapter VI-A (unlike interest provisions).
- There is however no exemption from filing a return even if full tax is deducted at source (unlike interest provisions).



# Royalty & FTS - PE

- If there is a PE or fixed place of profession; agreement is entered into on or after 1.4.2003;  
Royalty & FTS is effectively connected with the PE;  
then the net profits are taxable @ normal rates.

# Royalty & FTS - PE

- Expenses incurred wholly & exclusively are allowed as deduction.
- Expenses paid by PE to HO are not deductible (unless it is reimbursement of actual expenses).
- Audit & Accounts are mandatory as per S.44AA and 44AB.

# Royalty & FTS - PE

- PE includes a fixed place of business through which business is wholly or partly carried on.
- Fixed place of business – not defined.

**Thank you for a patient hearing.**

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**Questions & Comments are welcome.**

**Naresh Ajwani**  
**naresh@rashminsanghvi.com**