Happy to help compute tax on Flipkart deal, taxman tells Walmart

BY DEEPSHIKHA SIKARWAR, ET BUREAU | UPDATED: MAY 11, 2018, 06.43 AM IST

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NEW DELHI: Walmart can approach the authorities under Section 195(2) of the Income Tax Act to determine the withholding tax liability on its proposed purchase of a 77% stake in Flipkart for $16 billion, the income tax department has told the American retail giant.

The withholding tax rate in the case of long-term capital gains tax is 10-20% depending on the nature of the investment.

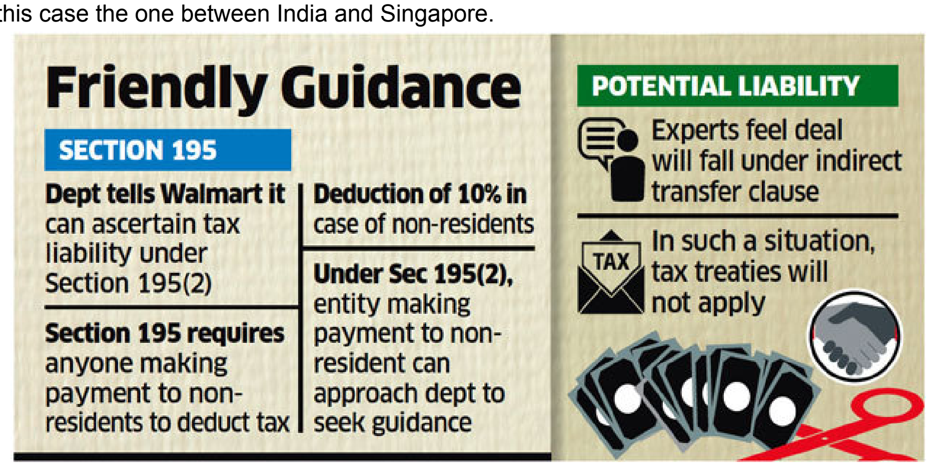
“We have told them that they can approach the income tax officer to ascertain their tax liability,” said a senior income tax official with knowledge of the communication sent to the company on Tuesday. ET had reported May 9 on the letter sent to Walmart regarding the transaction.

Section 195 requires any entity making a payment to a non-resident that’s not interest income or salary to deduct tax as appropriate on the amount. Under Section 195(2), the entity can make a reference to the income tax officer to determine the exact tax liability. The income tax department has sought details of the deal that Walmart announced on Wednesday.

The tax department has told Walmart that it believes it may have withholding tax liability under the law on payments made to non-resident investors in the Indian ecommerce company.

Mandatory to Withhold Tax

“Treaty provisions will not apply on indirect transfers that have Indian assets as underlying,” said another official, referring to double taxation avoidance agreements, in this case the one between India and Singapore.



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Non-resident private equity investors who are selling stakes to Walmart have the option to approach the Authority of Advance Rulings or income tax officer under Section 197 to ascertain their tax liability. The Finance Act, 2012, introduced indirect transfer-related provisions under Section 9(1)(i) of the Income Tax Act. Consequently, the income that nonresidents get directly or indirectly through transfer of a capital asset situated in India is to be taxed here with retrospective effect from April 1, 1962.

The change in the law makes it mandatory for all persons, whether resident or non-resident, having a business connection in India, to withhold tax even if a transaction is executed on foreign soil if the underlying asset is Indian. The previous United Progressive Alliance government had introduced the amendment to overcome a Supreme Court ruling in favour of Vodafone. Income tax authorities had made a significant tax claim on its 2007 deal with Hutchison Whampoa to buy a majority stake in its local telecom subsidiary, levying this on the indirect transfer of an Indian asset.

The withholding tax rate in the case of long-term capital gains tax is 10-20% depending on the nature of the investment. “Under Section 195 of the Income Tax Act, 1961, Walmart will have the obligation to withhold tax from the amount to be paid to the non-resident sellers,” said Amit Maheshwari, partner, Ashok Maheshwary & Associates LLP. “The actual amount of taxability in this transaction may vary in view of the beneficial tax rates available to non-residents and treaty benefits.” To seek a lower rate, Maheswari said Walmart will have to apply for this with related documents and explanations to substantiate the actual amount of gain. Tax officials will then decide whether to issue the certificate for lower withholding tax, he said.

“Such a transaction is taxable under the indirect transfer provisions of domestic tax laws. However, if the seller of such shares is located out of jurisdictions such as Singapore or Mauritius, even under amended treaty scenario, it may be possible to claim such gains to be non-taxable in India under residuary clause of article dealing with capital gains taxation,” said Rakesh Nangia, managing partner, Nangia & Co LLP.

“In any case, the buyer would be required to withhold income tax as per domestic tax provisions under Section 195, and if the tax withholding is to be mitigated, then a ‘nil’ withholding tax order would be required from Indian authorities in advance under Section 195(2) or Section 197,” he added.