



Direct Tax Update - India



Hon'ble High Court clarifies on the Limitation Period for TDS Proceedings Involving Non-Resident Payees

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Hon'ble Telangana High Court rules in favor of tax department by reading a limitation period of 7 years (currently prescribed for residents) into the law relating to TDS proceedings for non-resident payee(s) under section 201(1) of the Income-tax Act, 1961.

Background of the case

Recently in the case of Dr. Reddys Laboratories Limited ('the Assessee') the Hon'ble High Court of Telangana expounded on the issue that what should be the limitation period for TDS proceedings involving non-resident payees under section 201 of the Act. The Assessee is a pharmaceutical company incorporated in the year 1984 and is engaged in manufacturing and selling pharmaceutical products. It is also engaged in research and development of drug products.

The assessee had entered into a Trademark Assignment Agreement (TAA) with two foreign companies viz., USB Farchim SA, Switzerland (for short 'USB Switzerland') and USB Biopharma SPRL, Belgium (for short 'USB Belgium') for the purchase of certain trademarks for identical

territories including India for which it has paid an amount of Rs.115,04,00,000/- to USB Switzerland and an amount of Rs.244,16,00,000/- to USB Belgium during the financial year 2015-2016 relevant to the assessment year 2016-2017 for purchase of the said trademarks.

¹ W.P. No. 1513 of 2019

¹ [2014] 48 taxmann.com 150 (Bombay)

¹ [2016] 76 taxmann.com 256 (Delhi)

On 30.12.2015 survey operation under Section 133A of the Act was carried out to verify Tax Deducted at Source (TDS) liability of the petitioner with respect to payments made to Non-residents. During the survey, it was found that the assessee had not deducted TDS on the remittances made by it during the financial year 2015-2016 to the two foreign companies.

On 20.01.2016, the tax department-initiated proceedings under Section 201(1)/(1A) of the Act by issuing a notice to the assessee to show cause as to why it

should not be construed to be an assessee in default for failure to deduct TDS on payments made by it to the two foreign companies. on 11.02.2016 assessee submitted that the payments made to the two foreign companies were not taxable in India.

Further, on 03.10.2018, the assessee became aware that the two foreign companies had filed applications before the Authority for Advance Ruling (briefly 'AAR' hereinafter) seeking a ruling on the tax liability of the payments made to them on account of the transfer of the trademarks and requested for keeping proceedings in abeyance. The assessee objected as to limitation i.e., initiation of proceedings was barred by limitation and that the reasonable period for passing an order under Section 201 of the Act had lapsed.

On 14.12.2018, the department passed the impugned order declaring that since the assessee did not deduct TDS as required under Section 195 of the Act on the taxable payments made to the two foreign companies during the financial year 2015-2016, it is deemed to be an assessee in default under Section 201(1) of the Act.

Further, penalty proceedings under Section 271C of the Act vide show cause notice dated 21.12.2018.

The assessee filed a writ before the Hon'ble HC for seeking relief. The HC noted that following two issues had arisen for its consideration –

1. whether the period of limitation stipulated in Section 201(3) of the Act would apply to the assessee especially when the same uses the expression 'a person resident in India'.
2. Impact of double taxation avoidance agreement.

Assessee's contentions

As far as limitation is concerned, the assessee contended that the impugned order having been passed on 14.12.2018, the show cause notice being issued on 20.01.2016, is well beyond the reasonable period and therefore, the same should be set aside.

The assessee relied on the judgement of Bombay High Court in case of **Mahindra & Mahindra Limited** and Delhi High Court in **Bharti Airtel Limited** where it was held that going by the same logic as is evident from Section 153(2) of the Act, completion of proceedings under Section 201(1) of the Act that is passing of the order under the said provision has to be within one year from the end of the financial year in which those proceedings under Section 201(1) were initiated.

Revenue's contentions

The department contented that order under Section 201(1) of the Act came to be passed on 14.12.2018 i.e., within three years. Therefore, in such circumstances, it cannot be said that the order passed under Section 201(1) of the Act was passed belatedly or was beyond limitation.

It further argued that all this while, Parliament consciously did not provide for any limitation insofar non-resident Indians are concerned. This clearly reflects the legislative intent that there can be no

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limitation insofar passing of an order under Section 201(1) of the Act qua non-residents is concerned.

Court's Findings:

- Initially the statute did not provide for any limitation, be it a resident Indian or a non-resident Indian. Subsequently, by way of amendment, sub-section (3) was inserted in Section 201 of the Act. Presently, the limitation for passing of an order under Section 201(1) of the Act post the last amendment is seven years insofar a person resident in India is concerned. The present case covers the assessment year 2016-2017, which is well after the last of the amendments were made and when limitation period qua resident Indians is seven years.
- The legislature has consciously not prescribed any time limit for an order under Section 201(1) of the Act insofar a non-resident is concerned; the reason being that if the deductee is a non-resident, it may not be administratively possible to recover the tax from the non-resident. Therefore, it would be wrong to read into Section 201(3) of the Act a period of limitation insofar non-resident is concerned; doing so would amount to legislating by the Court which is not permissible.
- At the same time, it must also be kept in mind that even though there is no limitation prescribed by the statute, the order under Section 201(1) of the Act qua non-resident has to be passed within a reasonable period.
- On **what is a reasonable period** in the absence of any statutory limitation? The Hon'ble HC held that there cannot be a straight jacket answer to such a question. What is a reasonable period would depend upon the facts and circumstances of each case. Therefore, as a general principle it may not be possible as well as feasible on the part

of the Court to say definitely that a period of four years or one year would be the period of limitation for passing an order under Section 201(1) or 201(1A) of the Act when the legislature has consciously not prescribed any such limitation. The HC further held that one thing is very clear, that is, when the legislature has prescribed a period of seven years as the limitation for a resident Indian, it would not be justified to read a limitation of less than seven years in the case of a non-resident. Thus the HC opined that limitation period of seven years prescribed for a resident Indian would be a useful guide to determine what would be a reasonable period in the case of a non-resident Indian.

- The HC thus noted that the survey conducted on 30.12.2015, show cause notice was issued on 20.01.2016 and the proceedings came to be concluded on 14.12.2018 was within a reasonable time.
- The HC refrained from the expressing any opinion on second issue framed by it i.e., impact of double taxation avoidance agreement.

Our comments

Section 201(3) of the Income Tax Act, 1961 specifies that in case of payment made to a Person resident in India, the proceedings under section 201 must be concluded within seven years. At the same time in the case involving non-residents payees, no time limit has been prescribed in the statute. This had created difficulties and uncertainty as to what should be the reasonable time limit for completion of TDS proceedings in such cases.

Contrary to the Hon'ble Delhi High Court's decision in Bharti Airtel's case [which prescribed one year as limitation period], the Hon'ble Telangana High Court held that a period of seven-years prescribed for

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resident Indians can be used to determine what would be a reasonable period for a non-resident. A limitation of less than seven years would not be justified for a non-resident.

Thus, the Hon'ble Court has attempted to bring parity between residents and non-residents as far as the limitation period for completion of TDS proceedings under section 201 of the Act is concerned. This will surely come to aid of the tax authority as they might get a longer period to assess the TDS non-compliance even in cases involving non-residents.

Contributions / Inputs:

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