

Del HC delineates guiding principles for deciding application for lower/ Nil tax withholding; outlines principles governing DAPE under India-Ireland DTAA

In the recent judgment of *SFDC Ireland Ltd.*¹, the Delhi HC has shed light on an issue of vital importance, viz., *the nature of the duty cast upon the Assessing Officer ('AO') while deciding an application for issuance of lower/ Nil withholding certificate*, u/s 195/ 197(1) of the Income Tax Act, 1961 ('the Act'). While doing so, the Hon'ble Court ventured into a deep dive of various facets such as: (i) relevance of the procedure u/r 28AA of the Income Tax Rules, 1962 ('the Rules'); (ii) chargeability to tax as an essential prerequisite for attracting Section 195; (iii) concept of Dependent Agent Permanent Establishment ('DAPE'), etc.

Brief Factual Matrix

- The assessee, a resident of Ireland having no business presence in India, is offering standardized Customer Relationship Management products ('SFDC Products').
- The assessee, under a Reseller Agreement, appointed its affiliate entity in India as a non-exclusive reseller of such products.
- Under the agreement, the parties were to transact on a principal-to-principal basis, neither acting on behalf of, nor having the authority to bind the other to any contract.
- The reseller was to procure the SFDC Products from the assessee for onward resale in India, in consideration for which the reseller would be entitled to retain operating margin of 2.75% of the Indian Territory revenue.
- Since the revenue from sale of SFDC Products was in the nature of business income, not being chargeable to tax in India in the absence of a PE, the assessee filed an application seeking Nil tax withholding on remittance of such revenue.
- The AO, by way of the **impugned order**, prescribed withholding tax rate of 2% reasoning that: (i) *the reseller was empowered to enter into contracts on behalf of the assessee*; (ii) *the reseller was involved in the price determination process, indicating dependency on the assessee, which was difficult to establish at the stage of 197 proceedings*; and (iii) *grant of Nil Certificate would amount to accepting the stand of the assessee*.

Judgment by Delhi HC

- (1) At the outset, the HC delineated the duty of AO in deciding applications u/s 197 and Rule 28AA of the Rules, stating that the obligation to withhold tax arises only when receipts in the hands of non-resident are chargeable to tax under the Act;² thus, the AO is required to take a view (even though it may not be final) as to the chargeability of receipts to tax

¹ 2025:DHC:977-DB

² (2010) 327 ITR 456 (SC); [2021] 432 ITR 471 (SC); (2012) 6 SCC 613

under the Act. Ergo, before rejecting such application, the AO is required to a prima facie opinion regarding taxability of income in the hands of the non-resident.

- (2) The HC further negated the reasoning and basis assigned by the AO in rejecting the prayer for Nil withholding certificate, holding that:
- a. In the absence of material to indicate otherwise, the provisions of the Reseller Agreement would, *prima facie*, be determinative of the relationship between the parties – accordingly, it is, inter alia, not disputed that parties act on principal-to-principal basis and neither party exercises authority to bind the other;
 - b. The AO accepted that in the absence of PE in India, payments receivable by assessee, being “business income”, would not be chargeable under the Act.
 - c. Although the AO has hinted towards existence of assessee’s DAPE in India, no such finding, even prima facie has been rendered.
 - d. Further, absent definitive material supporting the allegation that reseller exercises authority to conclude contracts on behalf of assessee, the stand of DAPE under Article 5(6) of the DTAA would not sustain; also, even if the reseller is involved in price determination of SFDC products, it would not result in a DAPE; lastly, in the absence of any other features, the revenue model of providing margin of 2.75% on operating cost to the reseller is not indicative of assessee having a DAPE in India.
 - e. In any case, the transactions between the reseller and the assessee, being related parties, would be benchmarked on arm’s length basis.

Accordingly, the HC directed the AO to grant NIL withholding tax certificate to the assessee.

The case was represented by **Mr. Ajay Vohra, Sr. Advocate**, instructed and assisted by the team of ***Vaish Associates Advocates***, comprising of **Mr. Aniket D. Agrawal, Associate Partner** and **Mr. Samarth Chaudhari, Sr. Associate**.

VA Comments

The judgment goes a long way in outlining the duty cast upon the AOs at the stage of deciding applications u/s 197(1) [as also Section 195], and directs that AOs guide their enquiries as per the scheme prescribed in the statute, and do not indiscriminately fling allegations [of some suspected dependency without alleging existence of DAPE (as in the instant case)] *sans* establishing (even prima facie) that receipts in question are chargeable to tax under the Act.

The judgment also explains intricate aspects of a DAPE by referring not only to the provisions of the India-Ireland DTAA, but also that of OECD and UN Model conventions. It also refers to text of Klaus Vogel on Double Taxation Conventions for identifying the rationale for inclusion of DAPE as a category of PE.

Similarly placed assesseees can cite this judgment to apply principles propounded by the HC to their own cases.

For any further information/clarification, please feel free to write to:

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