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Delhi ITAT allows US LLC to avail of India-US tax treaty benefits

Updated - October 10, 2024 at 10:44 PM. | Mumbai

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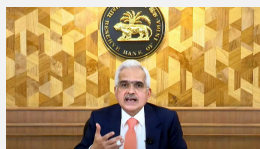


The decision can have a bearing on S Corporations which desire to avail India-US tax treaty benefits

The Delhi Income Tax Appellate Tribunal (ITAT) has allowed a limited liability corporation (LLC) and a tax resident of US to avail of the India-US tax treaty benefits. The residential status of a US LLC and its eligibility to take treaty benefits has been a subject matter of litigation, making this a landmark judgment on the subject.

“This is a positive ruling for US LLCs as well as fiscally transparent entities (FTEs) in other jurisdictions having a tax treaty with India with similar provisions. It is necessary to assess the tax treaty eligibility from a holistic standpoint after considering all its specific provisions, the tax laws of respective jurisdictions and the availability of a valid tax residency certificate,” said Bijal Ajinkya, Partner, Khaitan & Co, in a note.

A US LLC is a hybrid entity which can be treated in the US as a pass-through or a FTE yet continue to be treated as a company for Indian tax purposes.



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The matter

General Motors Company USA (taxpayer), incorporated as an LLC under US laws, offered to tax income by way of fees for technical or included services (FTS/FIS) at the rate of 15 per cent as per Article 12 of the India-US tax treaty. The income tax authorities, however, felt that the income ought to be taxed at the rate of 25 per cent under Indian tax laws. Since the taxpayer was an FTE — not liable to tax in US — it should not be treated as a US resident for the purpose of tax treaty.

The taxpayer claimed that ‘liable to tax’ should be inferred to mean that a person is treated as a taxable person in the relevant jurisdiction and does not require actual payment of taxes for the purpose of Article 4 of the treaty. It furnished a valid tax residency certificate issued by US authorities along with form 10F in accordance with section 90 of the IT Act.

Wider implications

According to Harshal Bhuta, Partner, PR Bhuta & Co., the decision can have a bearing on S Corporations which desire to avail India-US tax treaty benefits. An S Corporation is a business entity that passes business income and losses to its shareholders.

Bhuta, however, believes that the issue of accessing treaty by an LLC and S Corporation will not remain free from litigation since the ITAT ruling disregards the express provisions of the India-US DTAA, which limits treaty access to only some forms of fiscally transparent entities.

The latest judgment relies on the Mumbai Tribunal decision in the case of Linklaters LLP, which had taken a similar sympathetic view to grant treaty benefits to the income earned by a UK partnership under the pre-amended India-UK DTAA, he said. The India-UK DTAA was amended to accord DTAA benefits to income earned by UK LLPs treated as pass-through for tax purposes in the UK. Similarly, US and Germany too revised their DTAA in the year 2006 to explicitly grant treaty access to income earned by fiscally transparent entities. “India should consider similar treaty revisions with the US to clarify its stand on this issue,” Bhuta said.

“Entities adopting a pass-through regime in host jurisdictions should evaluate classification under the laws of incorporation and determine eligibility to claim tax treaty benefits accordingly,” added Ipsita Agarwalla, Leader - International Tax, Nishith Desai Associates.

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Published on October 10, 2024

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