



TAX TREATMENT OF DIVIDEND RECEIVED FROM A FOREIGN COMPANY

Dividend received from an Indian company which has suffered dividend distribution tax is exempt from tax under section 10(34). Exemption under section 10(34) is granted to dividend received from an Indian company and not to a dividend received from a foreign company. Thus, dividend from a foreign company received by an Indian resident is taxable. In this part you can gain knowledge about tax treatment of dividend received from a foreign company.

Meaning of dividend

In common parlance 'dividend' means the profits distributed by a company to its shareholders. Apart from that, i.e., dividend paid by a company to its shareholders, section 2(22)(e) gives the definition of deemed dividend. Hence, under the Income-tax Act, dividend includes deemed dividend. As per section 2(22), "dividend" includes following payments or distribution to the extent of accumulated profits of the company [i.e. whether capitalised profit or not for section 2(22)(a) to (d) excluding capitalised profit in case of section 2(22)(e)] :

- (a) any distribution if such distribution entails the release of all or any part of the assets of the company ;
- (b) any distribution of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest, and any distribution to its preference shareholders of bonus shares ;
- (c) any distribution made on liquidation of a company except where the shareholder is not entitled to participate in the surplus asset in the event of liquidation and shares were issued to him for full cash consideration.
- (d) any distribution on the reduction of capital of a company except where the shareholder is not entitled to participate in the surplus asset in the event of liquidation and shares were issued to him for full cash consideration.
- (e) Any payments in the form of loans or advances made by a closely-held company (i.e. a company in which public are not substantially interested) to its shareholder who is the beneficial owner of shares holding not less than 10% of voting power in such company or to any concern in which such shareholder is a member or a partner and which he has a substantial interest or any payment made by on behalf of such shareholder for his/her individual benefit. However, such payment would not amount to dividend, if such payment is made in the ordinary course of business and money lending is substantial part of the company's business.

However, "dividend" does not include—

- (i) any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956;





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- (ii) any distribution of shares made in accordance with the scheme of demerger by the resulting company to the shareholders of the demerged company whether or not there is a reduction of capital in the demerged company.
- (iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off.

Head of taxability and applicable tax rate

Dividends are charged to tax under the head “Income from other sources” and hence dividend received from a foreign company is charged to tax under the head “Income from other sources”. Dividend received from foreign company will be included in the total income of the taxpayer and will be charged to tax at the rates applicable to the taxpayer.

Relief from double taxation

Dividend received from a foreign company is charged to tax in India as well as in the country to which the foreign company belongs. If the foreign dividend has suffered double taxation, then the taxpayer can claim double taxation relief either as per the provisions of Double Taxation Avoidance Agreement (if any) entered into with that country (if any) by the Government of India or can claim relief as per section 91 (if no such agreement exists).

To understand the tax treatment of the dividend received from a foreign company, the taxpayer should keep in mind the provisions of Income-tax Law as well as the provisions of Double Taxation Avoidance Agreement (DTAA) (if any) entered into with that country (if any).

Concessional rate of tax to dividends received from foreign specified company

As discussed earlier, dividend received from a foreign company is taxed in the hands of a resident taxpayer at the normal rates applicable to his income. Normal tax rate applicable to an Indian company is 30% (plus surcharge and cess as applicable), hence, dividend received from a foreign company is charged to tax at 30% in the hands of an Indian company. However, section 115BBD provides a concessional rate of tax in respect of dividend received by an Indian company from a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital.

By virtue of section 115BBD, dividends [as defined in section 2(22) except dividend as defined in section 2(22)(e)] received by an Indian company from a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital is charged to tax at a flat rate of 15% (plus surcharge and cess as applicable).

It should however be noted that, in the above case no deduction on account of any expenditure or allowance will be allowed from the amount of the dividend covered under section 115BBD. In other words, the gross amount of dividend (without deducting any expenditure/allowance) will be taxed at the rate of 15% (plus surcharge and cess as applicable).





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MCQ ON TAX TREATMENT OF DIVIDEND RECEIVED FROM A FOREIGN COMPANY

Q1. Dividend received from an Indian company which has suffered dividend distribution tax is exempt from tax under section _____.

- (a) 10(32) (b) 10(33)
(c) 10(34) (d) 10(38)

Correct answer : (c)

Justification of correct answer :

Dividend received from an Indian company which has suffered dividend distribution tax is exempt from tax under section 10(34).

Thus, option (c) is the correct option.

Q2. Exemption under section 10(34) is granted to dividend received from an Indian company as well as from a foreign company.

- (a) True (b) False

Correct answer : (b)

Justification of correct answer :

Exemption under section 10(34) is granted to dividend received from an Indian company and not to a dividend received from a foreign company. Thus, dividend from a foreign company is taxable in the hands of the shareholder.

Thus, the statement given in the question is false and hence, option (b) is the correct option.

Q3. As per section 2(22), "dividend" includes any distribution if such distribution entails the release of all or any part of the assets of the company to the extent of accumulated profits of the company [i.e. whether capitalised profit or not except in case dividend is covered by section 2(22)(e)]

- (a) True (b) False

Correct answer : (a)

Justification of correct answer :

As per section 2(22), "dividend" includes following payments or distribution to the extent of accumulated profits of the company [i.e. whether capitalised profit or not for section 2(22)(a) to (d) excluding capitalised profit in case of section 2(22)(e)] :

- (a) any distribution if such distribution entails the release of all or any part of the assets of the company ;





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- (b) any distribution of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest, and any distribution to its preference shareholders of bonus shares ;
- (c) any distribution made on liquidation of a company except where the shareholder is not entitled to participate in the surplus asset in the event of liquidation and shares were issued to him for full cash consideration.
- (d) any distribution on the reduction of capital of a company except where the shareholder is not entitled to participate in the surplus asset in the event of liquidation and shares were issued to him for full cash consideration.
- (e) Any payments in the form of loans or advances made by a closely-held company (i.e. a company in which public are not substantially interested) to its shareholder who is the beneficial owner of shares holding not less than 10% of voting power in such company or to any concern in which such shareholder is a member or a partner and which he has a substantial interest or any payment made by on behalf of such shareholder for his/her individual benefit. However, such payment would not amount to dividend, if such payment is made in the ordinary course of business and money lending is substantial part of the company's business.

Thus, the statement given in the question is true and hence, option (a) is the correct option.

Q4. As per section 2(22), dividend does not include _____.

- (a) Any distribution if such distribution entails the release of all or any part of the assets of the company to the extent of accumulated profits of the company
- (b) Any distribution made on liquidation of a company to the extent of accumulated profits of the company
- (c) Any distribution on the reduction of capital of a company to the extent of accumulated profits of the company
- (d) Any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956

Correct answer : (d)

Justification of correct answer :

With effect from assessment year 2000-01, "dividend" does not include—

- (i) any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956;
- (ii) any distribution of shares made in accordance with the scheme of demerger by the resulting company to the shareholders of the demerged company whether or not there is a reduction of capital in the demerged company.
- (iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off.





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Thus, option (d) is the correct option.

Q5. Dividend received from a foreign company is charged to tax under the head _____.

- | | |
|---|--------------------------|
| (a) Profits and gains of business or profession | (b) Capital gains |
| (c) Income from other sources | (d) Income from salaries |

Correct answer : (c)

Justification of correct answer :

Dividend received from a foreign company is charged to tax under the head “Income from other sources”.

Thus, option (c) is the correct option.

Q6. Dividend received from foreign company will be included in the total income of the taxpayer and will be charged to tax at _____.

- | | |
|---------|---|
| (a) 15% | (b) 20% |
| (c) 30% | (d) Normal rate of tax applicable to the assessee |

Correct answer : (d)

Justification of correct answer :

Dividend received from foreign company will be included in the total income of the taxpayer and will be charged to tax at the rates applicable to the taxpayer.

Thus, option (d) is the correct option.

Q7. A foreign company in which the Indian company holds _____ in nominal value of the equity share capital will be treated as foreign specified company for the purpose of section 115BBD of the Act.

- | | |
|-----------------|-----------------|
| (a) 25% or more | (b) 26% or more |
| (c) 50% or more | (d) 51% or more |

Correct answer : (b)

Justification of correct answer :

A foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital will be treated as foreign specified company for the purpose of section 115BBD of the Act.

Thus, option (b) is the correct option.

Q8. Section _____ provides a concessional rate of tax in respect of dividend received by an Indian company from a foreign specified company.

- | | |
|------------|------------|
| (a) 115A | (b) 115B |
| (c) 115BBD | (d) 115BBE |

Correct answer : (c)



Justification of correct answer :

Section 115BBD provides a concessional rate of tax in respect of dividend received by an Indian company from a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital (*i.e.*, a foreign specified company).

Thus, option (c) is the correct option.

Q9. By virtue of section 115BBD, dividends [as defined in section 2(22) except dividend as defined in section 2(22)(e)] received by an Indian company from a foreign specified company is charged to tax at a flat rate of 15% (*plus* surcharge and cess as applicable).

(a) True

(b) False

Correct answer : (a)

Justification of correct answer :

By virtue of section 115BBD, dividends [as defined in section 2(22) except dividend as defined in section 2(22)(e)] received by an Indian company from a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital is charged to tax at a flat rate of 15% (*plus* surcharge and cess as applicable).

Thus, the statement given in the question is true and hence, option (a) is the correct option.

Q10. No deduction on account of any expenditure or allowance will be allowed from the amount of the dividend covered under section 115BBD.

(a) True

(b) False

Correct answer : (a)

Justification of correct answer :

No deduction on account of any expenditure or allowance will be allowed from the amount of the dividend covered under section 115BBD. In other words, the gross amount of dividend (without deducting any expenditure/allowance) will be taxed at the rate of 15% (*plus* surcharge and cess as applicable).

Thus, the statement given in the question is true and hence, option (a) is the correct option.

