Levy of DDT subject to Treaty benefits – Bombay High Court Ruling

Until March 31, 2020, a Company paying dividend to its shareholders was subjected to Dividend Distribution Tax (DDT) @ 15% + applicable surcharge and cess u/s. 115-O of the Income Tax Act ("the Act") and such dividend was exempt in the hands of the shareholders. Currently, dividend is taxable in the hands of the shareholders and the Company is liable to deduct TDS on such dividend.

In cases where an Indian company distributes dividend to its non-resident shareholders, the issue whether - DDT discharged by the domestic company shall be eligible to lower Treaty rates has consistently been a subject matter of dispute. In this regard, the Mumbai ITAT (Special Bench) in Total Oil India Pvt. Ltd. & Others[1], held that the Indian company shall not be eligible to lower Treaty rates.

Putting to rest this controversial issue, the Bombay High Court in its recent ruling[2] has reversed the aforesaid Mumbai ITAT decision of Total Oil to hold that DDT is a tax on dividend which is income of the shareholder and hence, eligible to Treaty benefits.

Facts

1. Colorcon Asia Pvt. Ltd. ("the assessee") is a wholly owned subsidiary of its foreign parent, Colorcon Limited, United Kingdom ("Colorcon UK") which is a tax resident of UK, holding a valid TRC.

2. The assessee paid dividend to its UK parent and discharged DDT u/s. 115-O @ 15% plus applicable surcharge and cess (Effective rate ~ @20.36%). It sought an advance ruling to restrict DDT to 10%, as per Article 11 of the India–UK Double Taxation Avoidance Agreement (DTAA/Treaty).

3. The Board for Advance Rulings (BFAR) rejected the claim, holding that DDT is outside the scope of DTAA, relying on Mumbai ITAT Special Bench ruling in Total Oil India Pvt. Ltd. Aggrieved by this, the assessee filed an appeal before the Bombay High Court (Bombay HC) against the BFAR ruling.

Assessee's contentions

1. DDT is nothing but tax on dividend, which is income of the shareholder.

2. The legislative history of Sec. 115-O states that the incidence of tax has shifted from shareholders to company for administrative convenience but there is no change in the substantial provision. Reliance was placed on the Supreme Court's decision of UOI v.

[1] [2023] 104 ITR(T) 1 (Mumbai - Trib.) (Special Bench)
[2] [2025] Colorcon Asia Pvt. Ltd [TS-1623-HC-2025(BOM)

Tata Tea[3] which held that DDT is tax paid on dividend itself.

3. Treaty benefit cannot be denied because of mere change in incidence of tax under the domestic law.

4. DDT is an additional tax which falls within the ambit of charging section 4 of the Act. Such charge is subject to provisions of the Act including Sec 90.

5. The assessee being resident of one of the Contracting States is entitled to seek relief under Article 1 of the Treaty where payment is made to resident of another contracting state.

6. It was further argued that Article 2 of the DTAA has enlisted the taxes covered and it covers "Income Tax" including any surcharge thereon under the definition of "Tax" for the purpose of "Taxes covered in India". Article 2 also provides that the DTAA to apply to any identical or substantially similar tax in addition to or in place of tax.

7. All the four conditions provided in Article 11 for restricting the tax rate to 10% are satisfied, viz –
   - Payment – the payment must be "dividend" as defined in Article 11(3);
   - Payer - Such dividend has been paid by a resident of India;
   - Payee – should be paid to a resident of UK; and
   - Beneficial ownership - Dividend shall be taxable at 10%, if the recipient is the beneficial owner of the dividend. (Colorcon UK admittedly was the beneficial owner of dividend).

8. Any unilateral change made in the Act over the years merely in relation to the incidence of tax cannot alter the beneficial provision of the DTAA.

9. The assessee relied upon the decision of Delhi ITAT in Giesecke & Devrient (India) (P.) Ltd. v. ACIT[4] in support of its contention that the DDT rate is subject to tax rate provided under the DTAA

10. If India is permitted to charge a rate of tax in excess of the rate under the Treaty on items of income, such as dividend as defined under the Treaty, it would not be in accordance with Article 24 and the credit would not be available, resulting in double taxation.

Revenue's contentions

1. DDT is an "additional income tax" on the domestic company and cannot be construed to mean as "tax" in the hands of non-resident shareholder earning dividend income. Reliance placed on Supreme Court's decision in Godrej and Boyce Manufacturing Company Limited vs. DCIT[5].

2. As per ratio of Mumbai ITAT (Special Bench) in Total Oil India Private Ltd, the incidence as well as charge in respect of DDT is only on the domestic company that declares, distributes or has paid the dividend.

3. DDT is explicitly excluded from scope of taxes covered under the DTAA hence the prescribed rate of 10% under Article 11(2) would not apply to DDT.

[3] [2017] 398 ITR 260 (SC)
[4] [2020] 120 taxmann.com 338 (Delhi-Trib.)
[5] [2010] 394 ITR 449 [SC]

4. The bilateral treaty between India and UK is silent and do not contemplate, DDT as a tax on shareholders similar to Indo-Hungarian Treaty and therefore, the tax rate prescribed in Article 11 of the Treaty cannot be applied.

Issue before the Bombay HC

Whether DDT paid by taxpayer is to be governed by DTAA or to be dealt with only in accordance with Sec 115-O of the Act?.

Bombay HC Ruling

1. **Earning of the 'income' attracts the charge**

   The High Court relied extensively on **Apex Court's decision in Tata Tea Company** with respect to constitutional validity of Sec. 115-O wherein it was held that, the source of dividend income becomes irrelevant when it is declared and paid by the company to its shareholder. Once dividend is paid, it takes the character of 'dividend income' in the hands of the shareholder and not the company irrespective of the fact that source of such dividend are the profits of the payer company.

   The High Court overruled BFAR's decision and held that Sec. 4 of the Act levies income-tax, including additional income tax, in respect of the 'total income' of every person. 'Income' as defined u/s/ 2(24) includes 'dividend'. Therefore, Sec 115-O levies additional tax on the "amounts declared, distributed or paid by way of dividends" by the company.

   The High Court observed that the Supreme Court in Tata Tea's case, confirmed Parliament's authority to impose DDT on dividends under Entry 82 of List I (Union List). This fortifies the view that levy of DDT is on the dividend income of the shareholder and not on the profits of the company.

2. **Change in incidence of tax does not change the charge on income**

   The High Court observed that as per the legislative history of Sec. 115-O, the incidence of tax has shifted hands from shareholders to the payer company, however there is no change in the definition income with respect to 'Dividend'. Thus, the substantive provision that - DDT is a tax on dividend income of the shareholders has remained historically unaltered.

3. **DDT rate under the Act is subject to Treaty rates**

   The High Court upheld Delhi ITAT's view in Giesecke & Devrient Ltd that -

   - DDT is a levy of tax on the dividend distributed by a company to its shareholders.

   - As per charging section 4 of the Act, chargeability of income tax shall be at rates which shall be subject to -
     (i) provisions of the Act;
     (ii) provisions for the levy of additional income-tax.

   Thus, by virtue of charging Sec. 4, DDT rate shall be as per rate prescribed u/s. 115-O and this rate shall be restricted to the lower tax rate available under Treaty as per Sec. 90 of the Act.

4. Eligibility under India-UK Treaty

As per Sec. 90(2), DTAA would prevail over the domestic law to the extent it is more beneficial to the assessee who is subjected to tax in India.

Article 1 of the Treaty applies to the persons who are residents of one or both Contracting States. The assessee being resident of one the Contracting States i.e. India is entitled to seek relief under Article 1 where payment is made to resident of another contracting state i.e. UK.

Article 2 of the Treaty covers any identical or substantially similar taxes which are imposed by either Contracting State. This implies that DDT being an additional income tax, is covered by the Treaty under Article 2.

Article 11 of the Treaty restricts the right of India as a source State to levy tax as per domestic laws on dividend paid to resident of UK in excess of 10%.

The nature of income i.e. dividend, is relevant to invoke Article 11, and not the person in whose hands the tax is levied.

5. Excess DDT paid - Unconstitutional

The High Court held that DDT collected under domestic law in excess of 10% as prescribed by India-UK DTAA is contrary to Article 265 of the Constitution of India which states that *"No tax shall be levied or collected except by authority of law".*

Our Comments

This is a great decision is on interpretation of Article 11 of India-UK DTAA and it underscores supremacy of Treaty provisions over domestic law to the extent beneficial, holding that this benefit shall apply to DDT as well.

It relies on Tata Tea [SC] and the entire history of dividend taxation from 1997 to 2020, to hold that undisputedly DDT is paid on dividend being income which can only be of the shareholder.

It rejects reliance on Godrej & Boyce [SC] on the ground that it dealt with question of Sec. 14A and not nature of income being dividend.

Considering the nuances and overall impact of this decision, it is most likely to be challenged before Supreme Court.

Key considerations

1. Dividend being exempt in the hands of the foreign shareholder u/s. 10(34) and 10(35), in India, there is technically no juridical double taxation (which is genesis of Tax Treaties) on such dividend income. Having said that -
   (i) Can one resort to DTAA, in absence of double taxation or;
   (ii) One has to interpret the rationale laid down by this Bombay HC ruling that – under Article 11(2) both countries decided that India's right to tax shall be restricted to 10%, leaving the choice of manner of taxation as per domestic laws of India and once character of income being dividend is seen, the person paying tax in India becomes irrelevant.

2. This decision may support refund claim of excess DDT paid, if the issue has been contested before appellate authorities and is pending in appeals or if no ground is taken, an additional ground may be filed where possible, subject to other DTAA entitlement documents like Tax Residency Certificate, Beneficial Ownership documents. In any case, only the company paying DDT may benefit by getting refund of excess DDT paid.

3. For years where appeal is not pending or time limit of u/s. 264, u/s.154 has expired, relief is doubtful, nonetheless filing a Writ petition may be tested, though it too seems difficult in the absence of live claims. Further, maintenance of a miscellaneous application on the basis of a subsequent superior court ruling may be debatable as per recent Bombay HC ruling[6].

4. Applicability to buyback tax for past years is doubtful as firstly question of buy back being dividend or capital gains under DTAA itself is sub judice and not settled yet.

[6] [2025] 481 ITR 103 [Bom]