

EXPATRIATE TAXATION IN INDIA

India HRM Conference

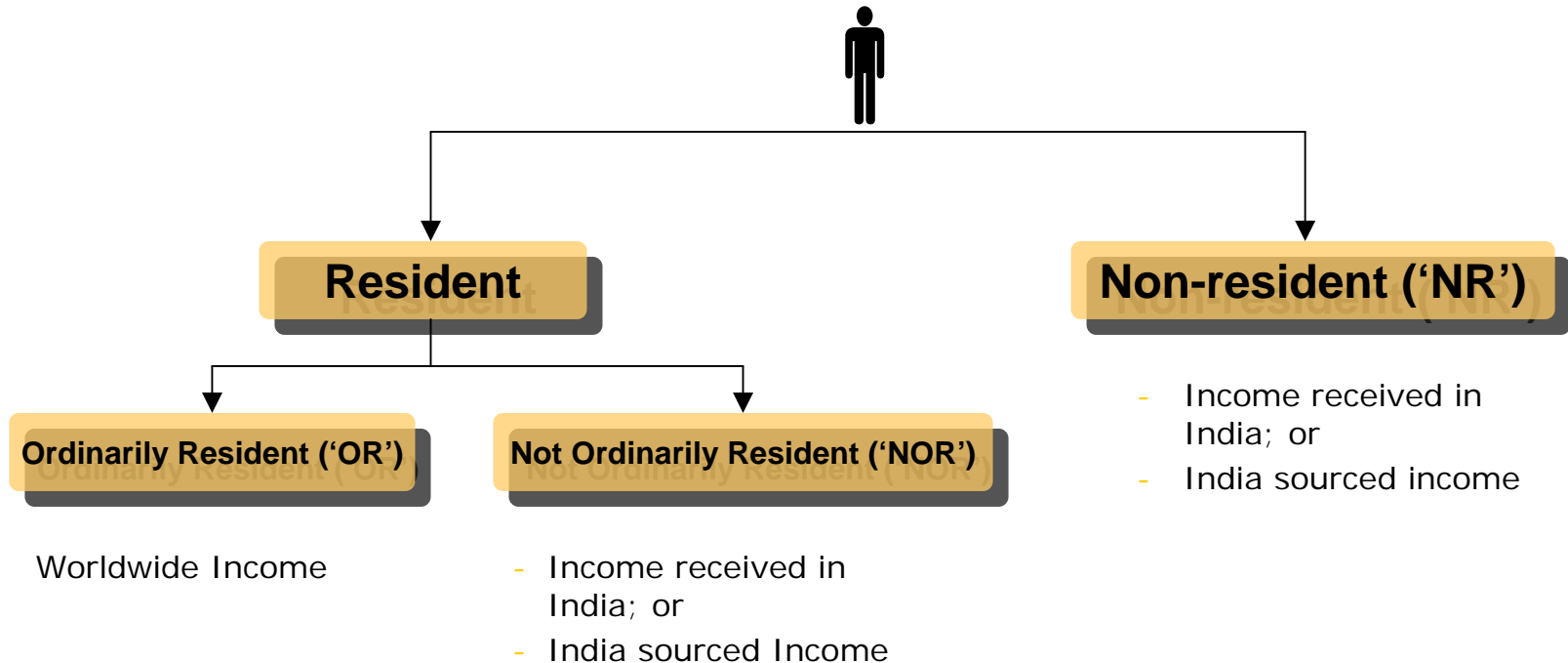
July 7, 2006

Ajay Sethi | Partner |

Presentation

- Residency
- Taxable Income
- Planning Avenues
- Tax Reporting in India
- Tax Assessments

Taxability Under Domestic Law – Scope of taxation



Local Laws vs Double Tax Avoidance Agreement ('DTAA')

PKA & Associates
Chartered Accountants

- DTAA overrides local laws of contracting states
- 'Tax Residency' needs to be tested
- 'Tax Jurisdiction' – Place of tax payment needs to be determined

■ Resident vs. Non-Resident ('NR')

- Primary Condition - Stay of 182 days in a single year **or** 60 days in a single year and 365 days in last four years.
- Secondary Condition - Non residents in nine out of ten preceding years or stayed less than 730 days in India in last seven years.

■ Not Ordinarily Resident ('NOR') - Usually runs for 2-3 years

- Tax Rate is 30 percent *plus* surcharge (10%) and education cess (2%).

Effective tax rate **33.66 percent**

Tax Payer's Residency - Case Study 1

Arrival in India on April 1, 2003

Fiscal Year	Stay in India	Residential Status
2003-04	365 *	NOR
2004-05	365 *	NOR
2005-06	< 60	NR
	≥ 60	Resident

- * If cumulative stay less than 730 days in FY 2003-04 & 2004-05, then NOR in FY 2005-06 even if his stay in 2005-06 exceeds 60 days

Tax Payer's Residency

- Case Study 2

Arrival in India on October 2, 2002

Fiscal Year	Stay in India	Residential Status
2002-03 (<i>Oct 2 – March 31</i>)	181 *	NR
2003-04	365 *	NOR
2004-05	365 *	NOR
2005-06	< 60 *	NR
	≥ 60	Resident

* An expatriate can stay for 970 days (181 + 365 + 365 + 59) without becoming a Resident

Tax Payer's Residency

– Case Study 3

Arrival in India on January 31, 2003

Fiscal Year	Stay in India	Residential Status
2002-03 (<i>Jan 31 – March 31</i>)	60 *	NR
2003-04	330 *	NOR
2004-05	330 *	NOR
2005-06	< 60 *	NR
	≥ 60	NOR

* An expatriate can stay for 1085 days (60 + 330 + 330 + 365) without becoming a Resident

Tax Payer's Residency – DTAA

Rule of Residency – Article 4 of the DTAA

- Applicability of treaty - resident of at least one of the contracting states i. e. India or Singapore
- Based on fiscal residency
- 'Tie breaker' test – when resident of both contracting states

- 'Dependent Personal Service' i.e. Deputation to India on salary basis
(*article 15*) – Non taxable in India when
 - Stay in India \leq 183 days during financial year; **and**
 - Salary not paid by or on behalf of an Indian Co; **and**
 - Salary not borne by any PE of Employer in India

- 'Independent Personal Services' i.e. Contractual engagement to India
(*article 14*) – Non taxable in India when
 - No fixed base in India; **and**
 - Stay in India \leq 90 days during financial year

Tax Protection Clause – Case Study

**“Is it mandatory that proof of tax paid outside
India be shown in order to claim
DTAA benefit?”**

Emmerich Jaegar v CIT (Gujarat HC)

- EJ, a Austrian technician was deputed to India by a Austrian company to work in India. He stayed in India for less than six months and was paid remuneration in foreign currency by the Austrian company
- Since this income was earned in India, even though Mr X was a 'non-resident', was liable to be taxed in India. However, per article 14 of the DTAA between India and Austria, the exemption from tax on such income in India could be claimed only if Mr EJ was 'liable to tax' in Austria.
- The Indian tax officer equated 'liability to tax' with 'payment of tax' and contended that unless tax is paid in Austria, the relief available under article 14 cannot be claimed.
- The tribunal held that once 'liability to tax' is determined per provisions of the articles of the DTAA, the fact that whether tax was actually paid in Austria was not relevant and hence Mr X was eligible for relief under article 14 of the DTAA.

- **Salary & Allowances**
- **Perquisites**
 - Accommodation
 - Social Security Benefits
- **Fringe Benefit Tax** (*Liability in hands of employer*)
- **“Tax on Tax” – Tax Equalisation** - To bridge parity in difference in tax rates of two or more tax jurisdictions

Taxable Income

– Salary & Allowances

- Basic Salary
- Bonus
- Salary in respect of leave immediately prior or post deputation to India
- Hardship Allowance
- Children Education Allowance
- Leave Travel Allowance

Taxable Income - Perquisites

■ Accommodation

- lower of 20 percent of **salary and allowances** (excluding perquisites) **or** actual rent
- Value attributable to furniture, etc.

Taxable Income – Perquisites

Case Study

“Whether tax liability borne by employer is ‘salary’ or ‘perquisite’ for valuing house perquisite ?”

Valuing Accommodation - *Conflicting Views*

- Part of salary
 - **CIT vs. H. D. Dennis & Others (135 ITR 1) - Mum**
- Being perquisite not to be included in salary
 - **T.P.S. Scot. vs. CIT (232 ITR 475) – Del**
 - **Frank Beaton vs CIT (156 ITR 16) – Del**
- Definition of salary as per new rule 3 specifically excludes perquisites

Taxable Income – Perquisites

Case Study

“Whether contribution to overseas retirement plans (Pension, Annuity) and towards medical/accidental insurance is a taxable perquisite ?”

Taxable Income – Perquisites

Case Study

Social Security Contribution by Employer - Not taxable, if employee do not acquire vested right

- SC in CIT vs. L. W. Russel (53 ITR 91)
- CIT vs. Lala Shrihar (84 ITR 192) – Del
- CIT vs. Vinay Bharat Ram (129 ITR 128) – Del

Taxable Income – Employee Stock Option Plan ('ESOP')

“If an expatriate is provided Stock options, what are the taxability issues included?”

Taxable Income – Employee Stock Option Plan ('ESOP')

- If ESOP scheme not within Indian Government guidelines taxable as perquisite at market value at the point of vesting of right
- Not taxable as perquisite, if ESOP scheme is within Indian Government Guidelines
- No capital gain taxation on sale as long as expatriate is not a resident in India

Taxable Income – Specific Issues

- **Daily allowance provided by third party customer to expatriate**
 - Exempt u/s 10(14) of the Act
 - CIT vs. Goslino Mario (241 ITR 312) - SC

- **Tax borne by employer on non-monetary perquisites viz. accommodation**
 - Exempt u/s 10(10CC) of the Act, provided such tax is not deducted from taxable income of employer

- Tax on Employer for Providing Employee Benefits or Perks
- Taxation on Fringe Benefits at 33 percent
- Non Tax Deductible Expense to Employer Company
- No Tax Credits Against Corporate taxes
- Compliance Issues

Fringe Benefits Tax – Valuation

Taxable Value	5 %	20 %	50 %	100 %
Fringe Benefits	<ul style="list-style-type: none"> Hospitality (<i>Hotel, Airline and shipping business</i>) Conveyance, tour & travel including foreign travel Repair, running & maintenance of Motor Cars (<i>Carriage of goods or passengers by motor cars</i>) Conveyance, tour & travel including foreign travel (<i>Construction/Pharmaceutical/Computer Software</i>) Use of Hotel, boarding & lodging (<i>Pharmaceutical/Computer Software</i>) 	<ul style="list-style-type: none"> Entertainment Hospitality Maintenance of Guest House Employee Welfare Telephone (<i>including mobile</i>) Repair, running & maintenance of Motor Cars & Air Crafts (including depreciation & fuel) Hotel, boarding & lodging 	<ul style="list-style-type: none"> Festival Celebration Gifts Club Facility Health Club, Sports, etc Scholarship to Children 	<ul style="list-style-type: none"> Free or concessional tickets for Private Journey Contribution to Superannuation Fund beyond Rs 100,000 per employee Any other Reimbursement (<i>not specifically covered otherwise</i>)

“ An expatriate, when deputed to India is affected by a higher rate of tax.

What planning is possible so that he does not pay tax higher than what would be charged on his income in Singapore?”

Case Study – Tax Equalisation

Particulars	Amount (S\$)	
Salary from Employer in Singapore (In Cash)		100,000
Add: Value of Perquisites viz		
- Accommodation (20% of salary)		20,000
Total/Taxable Income		120,000
Tax on Total Income		38,230
Bifurcated Into -		
Tax on Salary	31,500	
Tax on Perquisites	6,730	

Case Study – Tax Equalisation

Take Home Pay

Salary (In Cash)	100,000
Less: Tax on Salary	31,500
Desired Take Home Pay	68,500

Tax On Perquisites – Reimbursed by Employer

Salary (In Cash)	100,000
Add: Tax on Perquisites reimbursed	6,730
Total Salary (In Cash)	106,730
Add: Value of Benefits/Perquisites	20,000
Revised Taxable Income	126,730
Revised Tax Liability	40,500
Actual Take Home Pay (Cash Salary less Tax Liability)	66,230

Case Study – Tax Equalisation

Take Home Pay

Salary (In Cash)	100,000
Less: Tax on Salary	31,500
Desired Take Home Pay	68,500

Tax On Perquisites – Reimbursed by Employer

Salary (In Cash)	100,000
Add: Tax on Perquisites reimbursed	6,730
ADD: ADDITIONAL COMPENSATION	3,420
Total Salary (In Cash)	110,150
Add: Value of Benefits/Perquisites	20,000
Revised Taxable Income	130,150
Revised Tax Liability	41,650
Actual Take Home Pay (Cash Salary less Tax Liability)	68,500

Planning Avenues – Servicing India plus Adjoining Regions

ASA & Associates
chartered accountants

“What will be the impact on tax of an expatriate posted to India with responsibility to service adjoining regions as well viz. Nepal, Bhutan, Sri Lanka, etc.?”

Case Study – Servicing Adjoining Regions

Stephen Brandon v CIT (ITAT Delhi)

- Mr S, a foreign national was a Not Ordinarily Resident ('NOR') in India. His contract included servicing the entire South East Asia region and his remuneration was paid in foreign currency by the parent company. His company's Asia office was headquartered in India.
- Per terms of his contract, besides servicing in India, he made visits to adjoining countries viz. Nepal, Pakistan, Sri-Lanka to perform work assignments and offered proportionate salary to tax in India.
- However, the AO held that since the company was headquartered in India, Mr S continued to render services in India even when he performs assignments in adjoining countries. Accordingly, his entire salary is taxable in India.
- The tribunal held that the Indian tax laws consider salary earned for services rendered in India as taxable in India. Since Mr S also earned for servicing in adjoining regions, salary for that period cannot be taxed in India

Case Study – Servicing Adjoining Regions

Experience Based Advice

- Maintain travel log with details of services rendered in adjoining regions
- Calculation of exact days outside India reconciled to passport entries
- Personal visits / holidays – not eligible for benefit

Planning Avenues – Converting to Resident from Not Ordinary Resident

- ▶ On becoming Resident, global income taxable in India viz.
 - Salary
 - Dividend
 - Interest on Deposits
 - Rent
- ▶ Tax credit allowed for tax withhold outside India on above
- ▶ Capital Gains on immovable assets not taxable in India
- ▶ Plan and shift investment to Growth Funds (when deputation likely > 3 years)

Other Planning Avenues

- Advance Rulings
- 183 days rule under DTAA
- Avoid Permanent Establishment ('PE') trap

Tax Payment in India

■ Tax Withholding ('PAYE') - Salary Deputation

- Employer Responsible
- Monthly deduction & deposit. Quarterly reporting
- Government Notification – specific guidelines that salaried persons to follow tax withholding mechanism

■ Advance tax – Contractual Deputation

- Employee Responsible
- Quarterly Installments

Tax Reporting in India

- Fiscal Year – April 1 to March 31
- Employer Company
 - Quarterly tax reporting –*tax withholding and fringe benefit tax*
- Employee
 - Annual tax declaration by July 31st
 - Obtain No Objection Certificate ('NOC') prior to final departure

- Scrutiny / Assessments i.e. Verification of submission and accessing information namely bank accounts, assets etc.
- Interest & Penalty

THANK YOU