EXPATRIATES
— Tax and Regulatory Aspects

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The comments made and the views expressed in this Paper are the author’s personal views. It is advised that separate and specific professional advice is sought on each specific facts/issues.
OVERVIEW

A survey titled ‘Moving people with purpose – Modern mobility survey’¹ conducted in 2014 by PwC indicated that 89% of the organisations plan to increase their internationally mobile population. With every such movement, the company and the expatriate employees not only have to grapple with the tax issues in the home and host countries, but also have to ensure compliance with host country regulations such as immigration laws, exchange control regulations, social security and other labour laws.

From a tax perspective, in what may seem a simple employee movement/secondment, may expose the company to huge costs and risks including the permanent establishment (‘PE’) risk, social security cost, routine but cumbersome tax compliances and even the more recent risk of creating a place of effective management (‘POEM’) in India. Transfer Pricing and Indirect Taxes are also factors that need to be considered while planning any expatriate movement/programme.

Some of the important aspects to be considered in case of expatriate movements (vis-à-vis India) are:

1. **Immigration**: A foreign national visiting India must not only have a valid visa but the right kind of visa (for example employment visa, business visa, project visa, student visa, etc.). For each kind of visa, there are specific eligibility criteria and documentation requirements that need to be met.

   An expatriate employee coming to India under an employment visa valid for more than six months, has to register himself with the Foreigners’ Regional Registration Office (FRRO) within 14 days of his arrival in India. Where the employment visa is valid for less than six months, the registration with FRRO is required only if there is a specific endorsement on the visa for such registration. Under certain circumstances, the registration with FRRO is also required for an expatriate employee coming under a business visa. Please note that each case needs to be analysed separately for immigration requirements in India. A tentative check list of details required for such registration is given in Appendix 1.

2. **Foreign Exchange Management Act, 1999 (‘FEMA’)**: FEMA regulations also need to be looked into at the time of opening a bank account in India as well as to determine the ability to receive, retain and/or remit the salary outside India. The key to this is to determine the residential status of the expatriate employee under FEMA, which contains a definition different from that under the Income-tax Act, 1961 (‘the Act’).

3. **Social Security**: On 1st October, 2008, the Ministry of Labour and Employment, Government of India, notified social security schemes for international workers (‘IW’). Accordingly, every foreign national holding a foreign country passport is mandatorily required to contribute to Provident Fund (‘PF’) in India, provided he is coming to work for an establishment in India to which the PF Act applies (where employee strength is more than 20). Further, if any IW is coming from a country with which India has

a Social Security Agreement (‘SSA’) and he is contributing on reciprocity basis to the
home country social security, either as a citizen or resident and enjoying the status of
a ‘detached worker’ in terms of the SSA, such an IW is excluded from this requirement
provided he obtains the Certificate of Coverage (‘CoC’) from his home country. India
has so far signed SSAs with 18 countries to avoid employers and employees from
making double social security contributions in both the home and the host countries.
However, till date, only 14 SSAs have been made effective. A list of countries with
which India has signed the SSAs is given in Appendix 2.

Every IW has to contribute 12% of his salary to PF and a matching contribution is
made by the employer. Where the employee comes from a country with which India
does not have an operational SSA, the withdrawal of such contribution is not allowed
until the expatriate employee reaches the age of 58. Since most of the expatriate
employees come on net salary terms, this becomes a huge cost to the employer as the
employer has to not only pick up the entire 24% of salary as contributions to PF but
also the cost of tax gross-up on the contribution picked up by the employer.

4. Tax: In this Paper, I have focused on some of the very typical but complex tax issues
that arise from expatriate movements. For the sake of simplicity, wherever there is a
reference to Double Taxation Avoidance Agreement (‘DTAA’), unless otherwise specified,
the reference is to the India-US DTAA. The discussion is limited to the income falling
under the head “Income from salary”.

A lot of tax issues arise on account of the fact that the expatriate employees insist on
continuing their overseas payroll and do not want to take up local employment for fear
of losing continuity of service and social security benefit.

The tax issues that I have covered are broadly divided into individual and corporate
tax issues, some of which are typical to inbound expatriate movement (India being
the host country) and some to outbound expatriate movement (India being the home
country). These issues are:

A. Individual tax issues
   I. Residential status: This is one area, which can have a large number of
issues cutting across complex set of facts in real life expatriate scenarios.

   Since, the taxability of salary of an expatriate employee would depend upon
his residential status, determining his residential status not only under the
Act but under the DTAA as well is of vital importance. Some of the issues
that one may face in this area are on account of:

a) Definition of residential status under the Act;
b) Applicability of DTAA;
c) Tiebreaker Article (Article 4 of the DTAA);
d) Split residency due to a mismatch of tax years in different countries.

   II. Short stay exemption: An expatriate employee may be on a business visit,
a short-term assignment or on a long-term assignment. Depending on the
period of travel and nature of assignment, the tax issues may differ.
In case of a business visit or a short-term assignment, the Act [Section 10(6)(vi) and Section 10(6)(viii)] as well as the DTAA (Article 16) allows for short stay exemption, provided the specific conditions mentioned therein are satisfied. This may create issues and controversies, some of which are discussed in this Paper.

III. **Employee Stock Option:** Under section 17(2)(vi) of the Act, shares/securities received by an employee under an Employee Stock Option Plan (ESOP) or the like, are taxable on allotment of the specified security. However, in the case of an expatriate employee, who renders services in two or more countries during the period between grant and exercise of options, a question arises as to which country and to what extent such a benefit is taxable, if on the date of allotment, the expatriate employee was rendering services in India.

IV. **Hypothetical tax deduction:** Hypothetical tax (hypo tax), like the name suggests, is not an actual tax but a notional tax, which is equivalent to a home country tax, which the expatriate employee would have had to pay, had he remained in the home country with that level of salary. In most expatriate programmes, the employer deducts this hypothetical tax to arrive at the net salary payable to the expatriate employee. What is discussed in this Paper is, whether such hypothetical tax is deductible under the Act while determining the taxable salary of the expatriate employee. Also if so, whether such deduction is to be made from base salary or from perquisite valuation? This is a common and an on-going controversy that is very typical in an expatriate scenario.

V. **Overseas Social Security and Pension Contributions:** Most expatriate employees, while on assignment continue with their home country social security and pension contributions. While some of these social security contributions are mandatory under the laws of that country, some are voluntary. Some are defined contribution schemes and some are defined benefit schemes. In some, there is a one-to-one correlation between the contribution and the benefit, while in some, there is no such correlation. The controversy that surrounds this is whether the employer contribution to social security is taxable in the hands of the expatriate employee or not? Another controversy is whether the employee contribution is tax deductible or not?

VI. **Per diem allowance:** With Indian companies expanding their global footprint, more and more employees are sent on overseas assignments. The employees may be on short-term assignments (on or for a particular project) or on long-term assignments. At times, when projects get extended, their assignment period may also have to be extended. When these employees are sent abroad to work outside their normal place of duty, they are given a per diem or a daily living allowance to meet their ordinary daily charges. This is very typical of Indian IT companies. Section 10(14)(i) of the Act read with Rule 2BB(1)(b) of the Income-tax Rules, 1962 exempts per diem allowance in certain cases. This Paper discusses some of the controversies surrounding the taxability of per diem allowance in different circumstances.
B. Corporate tax issues

VII. Permanent Establishment (PE) exposure for overseas employer: Where the employment or payroll of the expatriate employee continues in the home country, depending on the period of presence, nature of work performed by the expatriate employee and contractual arrangements with host country entity, the overseas employer may trigger a PE exposure in the host country. This gives rise to tax and other compliance obligations, which may be unwarranted. The case study on the subject examines various tax consequences under different fact patterns.

VIII. TDS on salary and DTAA relief: Every employer has to deduct tax under Section 192 of the Act at the time of payment of salary. Many a times, expatriate employees continue to be on their home country payroll while they are seconded/deputed to the host country. The home country employer continues to pay the salary to the expatriate employees on behalf of the host country employer. In addition, the employer also pays the host country tax with gross up. In such a scenario, the question arises as to who should deduct tax and do the corresponding compliances? The other question is whether the benefit available to the expatriate employees under the DTAA (that is, foreign tax credit or income exclusion) can be considered by the employer at the time of deduction of tax from salary? In absence of such credit the tax gross up required increases. Consequently, there are huge funds locked up in refunds. Such refunds take long time to recover. Further, it is even more difficult to recover this back from employees, as employer who has borne the tax should really be entitled to receive it.

The ensuing paragraphs seek to discuss in detail some of the concepts and questions summarised above. The groups may deliberate the questions in the Paper as well as in the case studies at the end of the Paper.

1 Residential Status in India

1.1. The taxability of income in India primarily depends on the person's residential status in India. An expatriate can either be a Resident and Ordinarily Resident (ROR), Resident but Not Ordinarily Resident (RNOR) or Non-Resident (NR) in India.

**Scope of Income:**

1.2. Under **Section 5** of the Income-tax Act, 1961 ('Act'), the scope of income subject to tax in India is dependent on the residential status of the individual. Accordingly, taxability of income in India based on residential status is summarized as follows:

<table>
<thead>
<tr>
<th>Residential Status</th>
<th>Income accrued/ deemed to accrue in India</th>
<th>Income received/ deemed to be received in India</th>
<th>Income accrued and received outside India</th>
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<td>ROR</td>
<td>Taxable in India</td>
<td>Taxable in India</td>
<td>Taxable in India</td>
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<tr>
<td>NOR/NR</td>
<td>Taxable in India</td>
<td>Taxable in India</td>
<td>Not taxable in India*</td>
</tr>
</tbody>
</table>

*unless it is derived from a business controlled in India or profession set up in India.*
Determination of residential status under Section 6 of the Act

1.3. Under Section 6 of the Act, the residential status in India of an individual is determined based on his physical presence in India. The wording of section 6 of the Act provides certain challenges when it comes to determining the residential status of an individual under certain circumstances, which the groups may deliberate:

Q 1: In a borderline case, whether a part of the day, day of arrival and/or day of departure should be included for calculating the number of days of physical presence in India?

Q 2: In case of an Indian citizen who leaves India for the purposes of employment, whether the 60 days has to be read as 182 days [Refer Explanation 1(a) and 1(c) to section 6(1) of the Act] if he returns back to India in the same year?

Q 3: A foreign citizen came to India on 1st June, 2012 for the purposes of employment for two years. He was expected to leave India on 27th May 2014, after completion of his assignment (less than 60 days in previous year 2014-15). However, due to an airline strike (which was beyond his control), he had to stay in India for 10 days and due to this reason, he crossed 60 days in the previous year 2014-15. He was in India for 365 days in past two years. Whether the period for which he was forced to stay back for reasons beyond his control need to be considered to reckon his residential status?

Q 4: What does “leave India for the purposes of employment” mean? Does it cover cases where the individual continues his employment with the Indian company but is transferred outside India to work for a year for an overseas branch?

Q 5: Whether for the purpose of computing the period of 60 days as mentioned in Section 6(1)(c), period of vacation to India would need to be excluded?

Q 6: An Indian citizen staying abroad comes to India on work, for a project of his overseas employer on 15th January, 2015 and returns overseas on 15th April 2015. Whether under Explanation 1(b) of section 6(1), this can be considered as a ‘visit’ and the period of 60 days has to be read as 182 days for the previous year 2014-15?

Determination of residential status under the Double Taxation Avoidance Agreement (DTAA)

1.4. In case of every expatriate employee, determining his residential status in India under the Act is the first step. Thereafter, it is equally important to determine his residential status under the DTAA.

1.5. Under the DTAA, taxability is determined on the basis of:

• Characterisation of income
• Source of income
• Residential status (Article 4 of the DTAA)

1.6. For a DTAA to be applicable, an individual has to be a “Resident” in at least one of the contracting States/ countries under the domestic law of the respective country.
1.7. At times, an expatriate employee may be a resident of both treaty countries under the respective country’s domestic tax law. In such situations, Article 4(2) (Tie Breaker Rule) has to be applied to determine residency of the expatriate for the purposes of DTAA.

1.8. The tie breaker test broadly follows the following pattern:

- Permanent home test
- Centre of vital interest test
- Habitual abode test
- Nationality test
- Determination by competent authorities

1.9. The above is explained by way of the following example:

Mr. A is an US citizen and OCI card holder. He came on a three year assignment to India from the US on 1st June 2014. He was present in India for 235 days during the Financial Year 2014-15. Given this, he becomes a resident of India under the Act for the period 1st April, 2014 to 31st March, 2015 and a resident of the US under its domestic tax law, for the calendar years 2014 and 2015.

1.10. In such a scenario, the following sequence of Tie Breaker test will have to be followed to determine his residency under the DTAA:

(a) **Permanent Home test**

Mr. A for the purposes of the DTAA, would be resident of the country in which he has a permanent home. If he has a permanent home in neither of the countries, the habitual abode test will have to be looked into as centre of vital interest test does not apply in such case.

Mr. A owns a house in the US, which is available to him during the years 2014 and 2015. Also, during his employment in India during the financial year 2014-15, he was provided with a rented accommodation exclusively for his use by his employer.

In this case, he has a home available to him in both the states i.e. in India as well as the US and hence, the test of permanent home is not sufficient to determine his residential status. Therefore, what needs to be seen is, in which country he has his centre of vital interest.²

(b) **Centre of vital interests test**

Mr. A will be a resident of the country which is the centre of vital interest for him i.e. where his economic and social ties are closer. In this case, assume that Mr. A has equal economic interest in India as well as in the US. His wife has moved with him to India, but his children continue to stay in the US. As such, his centre of vital interest is also split. In such situation, he will tie break his residency to a country which is his habitual abode.

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² [Manoj Kumar Reddy vs. ITO [2009] 34 SOT 180 (ITAT Bangalore)]

Dr. Rajnikant R. Bhatt vs. CIT {1996} 222 ITR 562/89 Taxman 82 (AAR–New Delhi)
The question arises when there is a tie between social and economic relations, what is to be given more weightage?

(c) Habitual abode test

Ordinarily, the word “habitual” indicates some sort of continuity and is derived from the word “habit”, which implies the tendency to repeat the same action and the word “abode” indicates the place of residence. The place of residence should be more than temporary and need not be permanent. Habitual abode refers to the State/Country in which the longer period of residence occurs.

Professor Klaus Vogel in his book “The Klaus Vogel on Double Taxation Conventions, Third Edition, 2007” on page 252 states that “in order to determine the “habitual abode”, what should be established is where the tax payers lives and not merely where he frequently stays. According to the author, for making such a comparison, a period of adequate length needs to be seen”.

Depending on the stay of an expatriate in the past and the intention of the expatriate to stay in future years “habitual abode” needs to be determined. At times it can be extremely difficult to determine the residency on the basis of this test.

For the purpose of this case, if it has to be assumed that this test is not determinative of his residence, then the nationality test needs to be looked into.

(d) Nationality

Since Mr. A is a national of the US, his residency will ultimately tie break in favor of the US.

In case the residency of an individual cannot be determined by using any of the tests indicated above, the individual can approach the competent authorities to seek guidance on the residency under the DTAA.

3. While there are no clear guidelines available in MC and OECD commentary for specific situations, it is important to note that the OECD Commentary (July 2010) has provided guidance in paragraph 15 to the effect that the circumstances must be examined as a whole and the personal acts of the individual should be given special attention.

Professor Klaus Vogel in his book “The Klaus Vogel on Double Taxation Conventions, Third Edition, 2007” has referred to international decisions where the Courts have held that in case a tie between personal and economic relations exists, personal relations will be given more weightage. However, in some of the cases, the Courts have ruled that the centre of vital interest existed in the Country in which the individual has economic relations.

There are no direct judgements of Indian courts on this issue on what should be given more weightage.
The groups are requested to deliberate on some of the practical challenges that emerge out of Article 4:

Q 7: Whether an individual who is a NOR under the Act is to be considered as Resident in India for the purposes of DTAA? Consequently, is the Tie Breaker Rule required to be considered?

Q 8: If an assignment is for less than one year, whether a rented home available to the expatriate employee in the host country can be considered a ‘permanent home’?

**Tax Residency Certificate (TRC)**

1.11. Under section 90(4) of the Act, an assessee, not being a resident in India, **shall not be entitled to claim** any relief under a DTAA unless a certificate of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory.

However, practically, an expatriate employee may face the following difficulties when it comes to obtaining a TRC:

1.12. **Multiple/ overlapping year**

In few countries, TRC is available for one calendar year. In such situation, if a TRC is required for the previous year 2014-15, then one would need to obtain two TRCs to cover the previous year 2014-15.

1.13. **Timing difference**

The Government authorities of several countries follow different practices with regards to the issuance of TRC for individuals. Where a particular country issues a TRC only after the end of the financial year (i.e. after ensuring compliance with the requirements of a physical stay etc.) the expatriate employee may face practical difficulties in claiming relief under DTAA on income arising during the year and consequently the employer may end up deducting excess tax.

1.14. **Permanent difference**

There may be countries where there is no specific system of issuing a TRC and it would not be possible for the expatriate to obtain a TRC from the home country Government.

1.15. Such difficulties, which are beyond the control of the expatriate employees cannot prevent the expatriate employees from claiming benefits under DTAA. Furthermore, the law cannot compel a person to do something that is impossible.4

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1.16. It is to be noted that as of now, the Act has not prescribed/ suggested any way out for
the non-residents who are resident of other counties but are not able to obtain TRCs
from there.

1.17. Practically, therefore, where circumstances justify, the benefit under the DTAA may
be claimed by placing reliance on any other alternate document, like the copy of the
foreign tax return, which can be furnished to prove the “resident” status in the other
country.

1.18. The tax return forms that were issued on 23rd June, 2014 require an assessee to declare
whether he has obtained a TRC for claiming relief under the DTAA. This requirement
may become a practical challenge for the assessee as the DTAA benefit may be denied
due to timing and permanent difference in obtaining a TRC, based on the details filled
in the tax return form. An assessee may need to file relevant documents at the time
of assessment proceedings/hearings to support such a claim.

2 Employee Stock Option Plan (ESOP)

2.1 An Employee Stock Option (ESOp) is a common component of remuneration especially
in multinational companies that provide the workforce with an ownership interest
in the company. The taxability of ESOp has seen a lot of changes under the Act. Currently, ESOp is specifically included within the definition of perquisite.

2.2 Under section 17 of the Act, “perquisite” includes:

\[(vi) the value of any specified security or sweat equity share allotted or transferred,
directly or indirectly, by the employer, or former employer, free of cost or at
concessional rate to the assessee.\]

2.3 As such, ESOps are taxable in the year/at the time of allotment of shares by employer.
The following are the basic stages under a typical ESOP:

| Grant Date | Vesting Date | Exercise Date | Allotment Date | Selling Date |

2.4 The vesting period in an ESOP could generally be 2-3 (or more) years. Since the
taxability of salary depends upon the residential status as well as the place of
rendering of services, the taxability of ESOP can be a complex affair.

Non-Resident/ Resident but Not Ordinarily Resident

2.5 For an NR or RNOR in India, income which accrues/arises/is received in India or
deemed to accrue or arise or received in India is taxable in India.

2.6 In the absence of specific provision under the Act, a view has emerged that if at the
date of allotment of shares, the expatriate employee was rendering services in India,
the entire value of ESOP should be taxable in India.

2.7 An alternate view is that, such benefit should be taxed in India proportionately on
the basis of expatriate employee’s presence in India during the grant to vest period.
Reliance can be placed on the following judicial precedents:
2.8 In case of Robert Arthur Keltz (35 taxmann.com 424), the Delhi Tribunal held that only proportionate salary would be taxable in India, if a part of activity done by the assessee has no relation to any India specific job or activity. In this case, “the assessee was in India only for a short period i.e. 1.4.2006 onwards and that prior to it, he had not done any service connected with any activity in India”. It was held that “as the assessee has not rendered services in India for the whole grant period, only such portion of the ESOP perquisite as is relatable to the service rendered by the assessee in India is taxable in India.” For this proposition, Delhi Tribunal relied on the jurisdictional tribunal’s decision in the case of Asstt. CIT vs.Ellin ‘D’Roazario (ITA 2918/D/2005) where similar facts were involved.

2.9 In this regard, attention is also invited to the CBDT Circular 9/2007 dated 20th December 2007 (in the context of Fringe Benefit Tax).

   “Question 4: How will the value of fringe benefit be determined in case where employee was based in India only for a part of the grant year?

   Answer: In a case, where the employee was based in India only for a part of the grant period, a proportionate amount of the value of fringe benefit will be liable to FBT. The proportionate amount shall be determined by applying to the value of the fringe benefit, the proportion which the length of the period of stay in India by the employee during the grant period bears to the length of the grant period.

2.10 Also according to the report by Organization for Economic Cooperation and Development (OECD) on “Cross-Border Income Tax Issues arising from Employee Stock Options Plans”, the proportionate benefit that pertains to the period of services rendered in India between the grant date and vesting date may be taxed in India.

2.11 While, in my opinion, the better view is that that ESOP value should be computed proportionately, it is advisable that whatever approach/view is adopted by the employer/employee, it is followed consistently.

Resident and Ordinarily Resident

2.12 In cases, where an expatriate employee is a ROR, his global income shall be taxable in India under the Act, subject to benefits under the DTAA. Therefore, the value of the ESOP perquisite will be taxed fully in India. Foreign tax credit under the relevant DTAA may be available in India for taxes paid on such ESOP in other jurisdictions.

2.13 If an employee is a resident of a foreign country during the vesting period (after applying Article 4(2) of the DTAA. Tie Breaker clause), it may be possible to take a view that benefits pertaining to employment exercised outside India during such a period would not be taxable in India [under Article 16(1) of the DTAA]

2.14 Apart from some uncertainty on the taxability of ESOP in the hands of an expatriate employee in cross border situations, additional questions also arise while determining the employer’s withholding tax obligations. Some of the issues are discussed in the Case Study section.

3 Short Stay Exemption

3.1 The basic rule of taxation of salary under the Act or DTAA is that salary is taxable in the country where services are rendered (physical presence). However, both provide...
conditional thresholds exempting such income from tax where the presence is for a short duration and specified conditions are satisfied.

**Under the Act**

3.2 Section 10(6)(vi) of the Act provides that remuneration received by a foreign citizen, being an employee of a foreign enterprise, for services rendered by him during his stay in India will not be included in the total income if all the following conditions are fulfilled:

- The foreign enterprise is not engaged in any trade or business in India;
- The employee's stay in India does not exceed in the aggregate a period of ninety days in the previous year;
- Such remuneration is not liable to be deducted from the income of the employer chargeable under the Act.

**Under the DTAA**

3.3 Article 16(2) of the DTAA provides for short stay exemption if the following conditions mentioned therein are met.

a) The recipient is present in the other state for a period or periods not exceeding in the aggregate 183 days in the relevant taxable year;
b) The remuneration is paid by, or on behalf of, an employer who is not a resident of the other state;
c) The remuneration is not borne by a permanent establishment or a fixed base or a trade or business which the employer has in the other State.

**Q 9:** A question that arises is whether the expatriate employee claiming such short stay exemption is required to file income tax return under Section 139(1) of the Act?

While deliberating this question, the groups may consider the following:

3.4 Under Section 139(1) of the Act, an individual is required to file his income tax return, in case his total income assessable under the Act exceeds the basic exemption limit. It can therefore be argued that if the expatriate employee is claiming short stay exemption and his total income does not exceed the basic threshold limit, he is not required to furnish his income tax return.

3.5 Rule 12 of the Income-tax Rules, 1962 (‘the Rules’) was amended to include the manner in which tax return shall be filed by a person claiming relief under Section 90, indicating possibly, that in such cases a return is required to be filed.

3.6 The Act, under some of the provisions such as section 115A(5) and section 115AC(4) specifically exempts the assessee from the obligation of filing of tax return, however, there is no such provision relating to salary income.
3.7 In various judicial precedents, it has been held that if the income received by the assessee before claiming exemptions and deductions (including treaty benefit) exceeds the maximum amount which is not chargeable to income tax, a return of income has to be filed. The assessing officer will then decide whether the deductions/exemptions claimed are allowable or not.

3.8 While analysing the applicability of short stay exemption under Article 16 of the DTAA, there is one more practical challenge that one may face. There may be a case where the foreign employer bears the entire salary cost of the expatriate employee whereas the Indian entity bears a portion of the salary or incurs certain costs of the expatriates such as accommodation costs, travel costs. These costs are not charged to the foreign employer.

Q 10: In such situations, i.e. when the Indian entity bears part of the salary, can the expatriate claim short stay exemption?

Q 11: If yes, whether it has to be restricted to the salary borne by the foreign employer (assuming all the other conditions specified in Article 16(2) of the DTAA are satisfied).

3.9 In case, conditions (a) and (c) mentioned in paragraph 3.3 as specified in Article 16(2) are satisfied but part remuneration is borne by the Indian entity, there can be two approaches to consider:

Approach 1
Condition ‘b’ mentioned under Article 16(2) is not satisfied therefore, Article 16(1) would be applicable and the entire remuneration would be taxable.

Approach 2
As the Indian entity will not claim deduction of the salary paid by the foreign entity, the expatriate can claim short stay exemption attributable to the salary paid by the foreign entity and part of the salary borne by the Indian entity will be taxable in India.

The groups may deliberate as to which is a better approach.

5. XYZ / ABZ Equity Funds vs. CIT (2001) [250 ITR 194]
VNU International B.V., (2011) [334 ITR 56]
Deere and Company (2011) [337 ITR 277]
Castleton Investment Ltd. (2012) [348 ITR 537]
SmithKline Beecham Port Louis Ltd. (2012) [348 ITR 556]

6. Article 16: 1. Subject to the provisions of Articles 17 (Directors’ Fees), 18 (Income Earned by Entertainers and Athletes), 19 (Remuneration and Pensions in respect of Government Service), 20 (Private Pensions, Annuities, Alimony and Child Support), 21 (Payments received by Students and Apprentices) and 22 (Payments received by Professors, Teachers and Research Scholars), salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.
A reference in this regard can be made to Klaus Vogel commentary “The Klaus Vogel on Double Taxation Conventions, Third Edition, 2007” on Article 15:

“Problems will arise whenever part of the remuneration payable to a person employed in a State of which he is not resident is borne in kind (e.g. by the provision of accommodation, subsistence allowance to cover additional cost of board etc.) by an enterprise in the State of employment and enterprise in the State of residence of that person does not refund such costs to the enterprise in the State of employment. Such payment in kind is an additional consideration for the services rendered and therefore, is a wage or salary. However, it is not made by, or on behalf of, and employer who is not a resident of the State of employment. In this connection, the following must be distinguished: If the charges involved represent minor elements of the overall remuneration for the services, they should be treated in the same way as latter (Flick/Wassermeyer/Wingert/Kempermann, Art.15Anm.53). However, if such charges are not minor elements of the overall remuneration, the latter must be availed, so that the actual wage or salary may be taxable only in the employer's state of residence, while the payment in kind may be taxable in the State of employment and generally also in the employer's State of residence.”

Hypo Tax

One of the significant criteria for the expatriate employee to be comfortable in moving to a different jurisdiction to work would be need for tax neutrality. The tax cost for the expatriate could be higher or lower in the host country compared to his home country. To tackle this issue, employers implement tax equalisation policy to ensure that the expatriate will neither be worse off nor better off as far as tax costs are concerned.

Typically, under tax equalisation policy, when an employee moves from a home to a host location, hypothetical tax (i.e. hypo tax) is calculated. Hypo tax, as the name suggests is not the actual tax but a notional tax which is equivalent to home country tax which the expatriate employee would have had to pay, had he remained in the home country with that level of salary. The salary of the expatriate employee is determined after reducing this hypo tax. Correspondingly, the employer undertakes to bear the entire host country tax on the employee’s salary. As a result, the employee is guaranteed a net take home salary (in addition to any other allowances attributable to his global movement).

Often such hypo tax is estimated at the beginning of the year/assignment and deducted from monthly salary. At the end of the year, true up/down calculations are made and the difference is paid/collected from the employee, based on the home country tax liability on actual remuneration for the year (tax equalisation settlement calculation).

The question that arises is whether this hypo tax is deductible from the salary and only the net salary is taxable. The tax authorities have been taking a position that no deduction is allowed while computing income under the head salary, except those specified under section 16 of the Act and therefore, hypo tax should not be allowed as a deduction.

The argument in favour of allowing hypo tax as a deduction is that this amount was never payable to the expatriate employee and is actually a reduction from the home country salary base to arrive at net salary payable to the expatriate employee.
4.6 Also, there have been several judicial precedents wherein it has been held that hypo tax should be allowed as a deduction.

4.7 The next question that arises is whether this hypo tax needs to be reduced from the base salary of the expatriate employee or from the tax perquisite. The important consideration in this regard would be how the contract between the expatriate and the employer is worded.

4.8 In the case of Jaydev Raja, the ITAT held that the difference on whether it should be deducted from base salary or perquisite is academic and as such, ruled that it should be reduced from base salary. In the case of Lukas Fole (35 SOT 8) as well, the Pune ITAT held that the difference between reducing hypo tax from the base salary and tax perquisite is purely academic. However, it held that hypo tax needs to be reduced from tax perquisite.

4.9 I wish to highlight that this issue is not academic as in certain scenarios the deduction of hypo tax from the base salary may have a different impact as against the hypo tax deducted from tax perquisite. The difference in the approaches becomes more relevant when valuation of other perquisites (e.g. rent free accommodation) or computation of certain exemptions (e.g. HRA) depend upon the amount of base salary.

4.10 This is explained in the following example:

The gross salary of Mr. A is ₹ 100 and tax payable in the home country is assumed to be 20%, i.e. ₹ 20. The average tax rate in the host country is assumed to be 30%.

**Approach 1**
- Deduct hypo tax from the base salary.
- Include the perquisite value of the Indian tax borne by the employer in the taxable salary.

**Approach 2**
Do not deduct hypo tax from the base salary; deduct hypo tax from the tax perquisite value.

Please note that the valuation of housing perquisite is affected depending upon the approach adopted.

Please see workings under both approaches on the following page.

7. LW Russel [1964] 53 ITR 91 (SC)
Garrick D’Silva vs. JCIT [2006] 5 SOT 132 (Delhi ITAT)
ITO vs. Lukas Fole [2010] 35 SOT 8 (Pune ITAT)
### Workings:

<table>
<thead>
<tr>
<th></th>
<th>Approach 1 (hypo tax deducted from base salary)</th>
<th>Approach 2 (hypo tax deducted from perquisite)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base salary before start of the assignment</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Home country tax</td>
<td>20</td>
<td>20</td>
</tr>
<tr>
<td>Host country tax</td>
<td>30</td>
<td>30</td>
</tr>
</tbody>
</table>

#### Tax computation

<table>
<thead>
<tr>
<th></th>
<th>Approach 1 (hypo tax deducted from base salary)</th>
<th>Approach 2 (hypo tax deducted from perquisite)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base salary receivable before the start of assignment</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Less: hypo tax</td>
<td>20</td>
<td>-</td>
</tr>
<tr>
<td>Base salary for tax purposes [A]</td>
<td>80</td>
<td>100</td>
</tr>
<tr>
<td>Accommodation perquisite: 15% of base salary [B]</td>
<td>12</td>
<td>15</td>
</tr>
<tr>
<td>Total Salary [C]=(A+B)</td>
<td>92</td>
<td>115</td>
</tr>
<tr>
<td>Tax on above at 30% [D]</td>
<td>28</td>
<td>35</td>
</tr>
<tr>
<td>Less: Hypo tax [E]</td>
<td>-</td>
<td>20</td>
</tr>
<tr>
<td>Net Tax [F]=(D-E)</td>
<td>28</td>
<td>15</td>
</tr>
<tr>
<td>Tax perquisite = [H] (i.e. tax gross up of ‘F’ at average tax rate of 30%)</td>
<td>39</td>
<td>21</td>
</tr>
<tr>
<td>Gross salary [G]= (C+H)</td>
<td>131</td>
<td>136</td>
</tr>
<tr>
<td><strong>Tax on ‘G’ at average tax rate of 30%</strong></td>
<td>39</td>
<td>41</td>
</tr>
</tbody>
</table>

Note: Similarly, depending upon the approach and the contract wording, the provident Fund contribution required to be made and consequent tax gross up could change.

4.11 As can be seen, if hypo tax is reduced from base salary, the tax amount is 39, whereas, if it is reduced from tax perquisite, the tax amount is 41.

4.12 Given that hypo tax is reduction in salary, it is better to have a local employment letter starting at the net level of salary. Also, where possible, the salary slips should not reflect the hypo tax deduction.

### 5 Social Security and Provident Fund

5.1 Any foreign national holding foreign passport (international worker) coming to India to work for an Indian establishment to which the Employees Provident Funds and Miscellaneous Provisions Act, 1952 applies, is required to contribute to the employee’s provident fund in India. However, international workers (IW) coming from a country with which India has a social security agreement (SSA) and he is contributing to the social security of the home country and enjoys the status of a detached worker is excluded from this requirement provided he obtains a certificate of coverage (COC) from the home country.
5.2 The accumulated balance in the provident fund in India can generally be withdrawn by the IW on retirement or attaining 58 years of age, whichever is later.

5.3 The expatriate employees coming to India on secondment may also have their social security policies active in their home country. They may be mandatorily required under the statute of their home country to contribute to the overseas social security even while on assignment in India.

5.4 The question that arises is whether the employer contribution to overseas social security is taxable in India and whether the employee contribution to overseas social security should be allowed as a deduction while calculating the taxable salary of the expatriate in India.

**Employer contribution to overseas social security and pension**

5.5 Foreign expatriates seconded to India for assignment continue to contribute to social security/pension in their respective home countries, and their employers in home country may also contribute to such schemes. Different countries have diverse rules regarding social security and pension schemes. Some may require contribution on the basis of employment, while others may require such contribution on the basis of residency or citizenship. Furthermore, these contributions may be mandatory in some countries and not in others.

5.6 Generally, when contributions to social security/pension schemes are made by the employer in the home country of the expatriate employee, payments from the scheme are contingent on certain events like retirement, termination of employment, attaining a certain age, etc. Where such payments are contingent in nature and where the employee has no right to claim the amount of such payment till the contingency occurs, the contribution made by the employer to such scheme is not due to and does not give a vested right to the employee over such contributions.

5.7 In cases where it can be established that an employer's contribution to social security/pension scheme of the overseas country does not confer any immediate rights/benefits to the expatriate employee in the year of contribution, and as such, the right of the employee to get the benefit of employer's contribution is contingent and is not a vested right at that stage, it should be possible for the employee to contend that the employer contribution to such social security/pension scheme in the home country should not be treated as taxable under the Act at that stage. Such a contribution becomes taxable only in cases where under the relevant scheme, the employee has a vested right with regards to the benefits of such contribution at that stage.

5.8 The question whether the expatriate employee at the stage of contributions is having a vested right in such benefits of the scheme should ultimately be decided on the basis of the overall terms of the relevant social security/pension scheme and on the basis of facts of each case.

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8. Supreme Court in case of CIT vs. L.W. Russel (1964)[53 ITR 91]; Delhi High Court in case of CIT vs. Mehar Singh Samparan Singh Chawla (1973)[90 ITR 219]; Kerala High Court in case of P. Newcome vs. CIT (1961)[45 ITR 52]; Patna High Court in case of ACIT vs. Dr. Jan Nuyten (2000) [112 Taxman 238]; Delhi High Court in case of Yoshio Kubo vs CIT (2013) [357 ITR 452]
Employee contribution to overseas social security

5.9 While computing income chargeable to tax under the head ‘Salaries’, only the deductions permissible under Section 16 of the Act are allowed. As such, the employee’s contribution to social security/pension scheme in his home country (‘employee contribution’) is not deductible while computing the salary income in hands of the employee. Therefore, it may be necessary to examine whether such a deduction towards the employee’s contribution should be regarded as the mere application of income or whether it could be regarded as diversion of income by overriding title (‘diversion of income’). If it is regarded as diversion of income then it may be possible to contend that it is the amount of salary after deduction of such employee’s contribution – “the net salary” – which should be considered for the purposes of computing income chargeable under the head “Salaries”.

5.10 If the contribution made by the employee is voluntary in nature or is towards a fund which is in nature of savings scheme or if the contribution is made to a fund that is similar to a provident fund or pension fund, established in India, it may be difficult to take a position that such contribution is a prior charge over the salary income i.e. it is diversion of income by overriding title at the stage of earning the salary income itself.

5.11 In certain cases, the employee’s contribution to a social security/ pension scheme in the home country is mandatory. It is retained by the foreign employer and handed over to the authorities concerned. In such cases, the employee has no right to receive it as income. In all these cases, where it is possible to establish that such contribution is in the nature of diversion of income by overriding title at the stage of earning salary income itself, the employee could contend that ‘net salary’ should be considered for the purposes of computing income under the head “Salaries”. As such, effectively, the amount of such contribution should not be liable to tax in India.

6 Whether benefit under the DTAA should be considered at the time of TDS?

6.1 Often companies in India depute employees to overseas jurisdictions but continue to pay their salaries in India. Under the Act, they also continue to deduct tax at the source even when the employee becomes NR.

The groups are requested to deliberate the following question:

Q 12: An employee is NR in India and is entitled to claim the benefits of the India-US DTAA. In terms of Article 16 of the DTAA, his salary is not subject to tax in India. Whether the benefits available to the employee under the DTAA should be considered by the employer for the purposes of TDS, at the time of payment of salary?

6.2 According to the CBDT Circular\textsuperscript{10}, the employer should require the employee to obtain a certificate from the Indian tax authorities under section 197(1) authorizing no deduction or deduction at lower rates as may be prescribed in said certificate.

**Q13:** The question that therefore arises as to whether the employer can himself determine the chargeability of salary income at the time of TDS?

7 **Foreign Tax Credit (FTC)**

7.1 In case of overseas assignments where the employee remains on Indian company’s payroll and continues to be a ROR in India, the Indian company is required to deduct tax under section 192 of the Act on the assignment remuneration (i.e. salary, assignment related allowances benefits) provided to the employees.

7.2 Further, during the period of assignment, the employee may also be liable to tax in the host country on the above-mentioned assignment remuneration.

7.3 In such a situation, the employee may be eligible to claim a Foreign Tax Credit (‘FTC’) in respect of tax paid/due on income that has been taxed in the host country.

7.4 Depending on the host country, FTC can be availed in accordance provisions under DTAA or in accordance with section 91 of the Act where no tax DTAA exists.

7.5 Section 91 (1) of the Act:

> If any person who is resident in India in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India), he has paid in any country with which there is no agreement under section 90 for the relief or avoidance of double taxation, income-tax, by deduction or otherwise, under the law in force in that country, he shall be entitled to the deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

7.6 **Relevant Article** (i.e. Article 25(2) of the India-USA DTAA):

> “....2. (a) Where a resident of India derives income which, in accordance with the provisions of this Convention, may be taxed in the United States, \textit{India shall allow as a deduction from the tax on the income of that resident an amount equal to the income tax paid in the United States,} whether directly or by deduction. Such deduction shall not, however, exceed that part of the income tax (as computed before the deduction is given) which is attributable to the income which may be taxed in the United States.....”

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\textsuperscript{10} Circular No 147 [F No. 275/80/74-ITJ] dated 28-10-1974
Q 14: The question arises whether an employer can consider FTC while deducting tax at source on salary paid to resident employees who are on assignment outside India?

7.7 One view is that since section 192 of the Act is silent as to whether FTC may be considered at the time of TDS, the employer cannot consider such FTC.

7.8 However, there is an alternative view as per which, the employer can consider FTC at the time of TDS under section 192.

The groups may deliberate as to which view is better.

7.9 There are some challenges which an employee may face with while calculating FTC at the time of filing his tax return. One such challenge is explained by way of a case study.

Q15: Questions are also asked on the method to be adopted for calculating the quantum of foreign tax eligible for credit. Say, Mr. A earns salary income which is taxed both in India and the US. His salary of US D 100 comprises of an allowance of US D 30 which is exempt from tax in the US. Whether, while calculating credit for the US tax against the India tax under the DTAA, tax on exempted income of US D 30, has to be excluded to calculate on the remaining doubly taxed income of US D 70?

8 Per diem allowance

8.1 Often companies send their employees on overseas assignment under an arrangement with their overseas clients. Such employees work at the client locations for a duration ranging from a few days to a few years. The employees continue to be on home country payroll. The employees also receive a per-diem allowance over and above the normal home country salary. Per diem allowance may also be referred to as daily overseas allowance, living allowance, cash allowance, etc. in expatriate terminology.

8.2 Any special allowance granted to an employee would be covered within the definition of ‘income’ under section 2(24)(iiia) of the Act. What is being dealt with in this Paper, later as part of case study is the taxability of per diem allowance in the case of employees who qualify to be a ROR in India.

8.3 For this purpose reference may be made to section 10(14)(i) of the Act read with Rule 2BB(1)(b) of the Rules.

8.4 Section 10(14)(i) of the Act provides that;

“any such special allowance or benefit, not being in the nature of a perquisite within the meaning of clause (2) of section 17, specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, as may be prescribed, to the extent to which such expenses are actually incurred for that purpose;”

8.5 Pursuant to above, Rule 2BB(1)(b) of the Rules, inter alia provides that the following is exempt from tax:

“Any allowance whether granted on tour or for the period of journey in connection with transfer, to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty.”
8.6 The groups are advised to go through the decision of Kolkata Tribunal in case of *ITO vs. Saptarshi Ghosh (48 SOT 522)* in this context.

8.7 Generally, in the context of per-diem, the following questions are asked, some of which are covered in the Case Studies:

Q 16: What is the maximum duration of assignment for an expatriate to claim the amount of per-diem spent by him as exempt under the Act and Rules?

Q 17: What is the maximum amount of per diem that can be claimed as exempted and whether it is conditional upon proper documents being provided evidencing the incurrence of expense?

9 Permanent Establishment (PE)

9.1 Often when overseas companies second their employees to India, their salaries continue to be paid outside India through the overseas companies’ payroll. This classically creates a PE exposure for the overseas company in India.

9.2 While a classic solution to mitigate PE exposure in India is to transfer the payroll to Indian entity, this often becomes a challenge due to:

- Social security of expatriate employees in home country
- Personal requirements/financial commitments of expatriate employees in their home country
- Foreign exchange laws and fluctuations
- Continuity of employment with overseas employer

9.3 Based on the contractual arrangement between foreign company and Indian company and cross charge of the salary payments, the foreign company may or may not create a PE in India.

9.4 Depending on differing facts and circumstances of each case (as described below), there may be different results/implications, not only from a PE perspective but also from the perspective of Transfer Pricing, Service Tax, withholding tax requirement, social security etc.

- Differing arrangements for cross charge of salary cost:
  - No cross charge;
  - Cross charge without markup;
  - Cross charge with markup;
  - Cross charge markup only for administrative overheads;
  - Part cost recharge
- Payroll continues with foreign entity or is shifted to Indian company
- Supervision and control of the work of expatriate employee
- Which entity has rights and obligations related to employment (i.e. termination rights, obligation to pay salary etc.)
9.5 Prominent case laws on these matters are developed based on Morgan Stanley\textsuperscript{11} and Centrica\textsuperscript{12} judgements. Groups are requested to go through these decisions.

9.6 I have covered this issue in the last case study. Groups to deliberate various tax consequences under different fact patterns.

\textsuperscript{11} DIT (International Taxation) vs. Morgan Stanley And Co. Inc. (And vice versa) [2007] 292 ITR 416 (SC)
\textsuperscript{12} AAR No. 856 of 2010
Case Study : 1

Shri Vapasaayaram
Indian Citizen

FACTS

• He travelled to the US on 1st November 2012 to take up employment with an US employer
• His family moved to the US on 1st April 2013
• He returned to India after his US assignment on 1st September 2014, along with his family
• He was in India for 365 days in 4 previous years preceding the previous years 2012-13 and 2014-15;
• His stay in India during the 7 years preceding the previous years 2012-13 and 2014-15 was 730 days;
• He was also a resident in India during the previous years 2009-10, 2010-11, 2011-12 and 2012-13
• He did not have any other income or assets in India and the US, during his US assignment
• Tax resident status in the US under the US tax law:
  • For Calendar Year 2012 - NR
  • For Calendar Years 2013 and 2014 – Resident
• He owned a home, which was available to him in India at all times.
• For the assignment period in the US, he was provided with a rented housing facility by the US employer

QUESTIONS

Q18 What will be the residential status of Shri Vapasaayaram, under the Act and DTAA:
  for the departure year 2012-13
  for the arrival year 2014-15

Q19 In his India tax return form, for previous year 2014 -15, whether he has to declare his status as a Resident or as a Non-Resident?

ANSWERS

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Case Study : 2

Mr. Tom Cruise
US Citizen

FACTS

• Tom is a citizen of the US. He does not have any home available to him in the US
• He is employed by a Japanese Company (J Co) and is paid salary in Japan
• During the period between 1st February 2012 and 31st March 2012, he came to India for business purpose and look-see trips. He spent 50 days in India.
• From 1st April 2012, he was seconded by J Co to its Indian JV (I Co)
• Upon secondment to India, he started receiving salary in India by J Co
• He was a NR in India during the previous year 2011-12
• He was a NR in Japan during the calendar year 2012
• His assignment to India finished on 31st January 2015 and he left India for Japan on 1st February 2015
• He was a ROR in India during the previous year 2014-15 and was a resident in Japan for the calendar year 2015

QUESTIONS

Q20 Whether he will be eligible to claim a short stay exemption in India for his salary income pertaining to previous year 2011-12?

Q21 In which country will his salary for the month of January 2015 be taxed? How will the FTC be taken?

Q22 In which country will his salary for February 2015 to March 2015 be taxed? How will the FTC be taken?

Notes:
1) Japan-India DTAA does not have a Tie Breaker Rule
2) Assume that Japan and the US will seek to tax global income on residence basis
3) Tax Rates:
   India – 30%
   Japan – 31%
   US – 35%

ANSWERS:

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Case Study : 3

Mr. George Clooney
US Citizen

FACTS

- George a US Citizen was seconded to India in April 2010 as MD of Indian Group Company (I Co) for 3 years till March 2013
- On 31 March 2011, he was granted stock options by the US company (US Co) [free of cost], with a vesting period of 3 years. No costs were cross charged by the US Co to I Co
- Out of 3 years of vesting period, he was in India for 2 years (i.e. 1st April 2011 to 31st March 2013) and outside India for 1 (1st April 2013 to 31st March 2014)
- He exercised his option and was allotted shares when he was outside India in May 2014
- During the previous year 2014-15 he is Non Resident in India and a Resident of the US

QUESTIONS

Q23 Whether the value of ESOP benefit would be taxable in India?
Q24 If yes, to what extent?
Q25 Who will undertake the TDS compliances in India?
Q26 Whether any short stay exemption can be claimed by Mr. Clooney?
Q27 Would the answer to questions 23 to 26 above be different, if the US company cross charged the entire cost to Indian subsidiary?

ANSWERS

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Case Study : 4

Mr. Santos
US Citizen

FACTS

• Mr. Santos is a US citizen. His global income is subject to tax in the US.
• During the previous year 2014-15, he was an ROR in India and therefore, his global income is chargeable to tax in India.
• Based on his fact pattern, his residency tie breaks in favour of India under Article 4(2) of India-US DTAA
• Mr. Santos is employed by an Indian company during the previous year 2014-15.
• His taxable salary income for the period 1st April 2014 to 31st March 2015 is US $ 365,000. He has US $ 100,000 as interest income in the US which became due and was received in the US on 31st December 2014
• The tax rate in India is 30% and tax rate in the US is 40%. (Please assume that there are no deductions available)

QUESTIONS

Q28 How much tax is payable in India and/or in the US after taking the corresponding tax credit?

Q29 In the above example assume that US $ 30,000 deduction is available in the US against interest income but in India the entire US $ 100,000 is taxable. Which country will have the right to tax such income(s) and to what extent can credit be claimed in respect of such tax(es) in the other country?

ANSWERS
**Case Study : 5**

Shri Gayaram  
Indian Citizen

**FACTS**

- He was seconded to a foreign subsidiary of his Indian employer (F Co.) for 2 years in November 2014 to work on a project for his Indian employer.
- He left India to move overseas with his family on 31st October 2014.
- Apart from his payroll being transferred to F Co, he was provided with housing by overseas subsidiary and a fixed per diem of $6,000 per month (@ US $200 per day).
- $2,000 out of the $6,000 was to cover his personal taxes in the overseas jurisdiction. The balance was to meet his expenses towards conveyance, telephone, internet, meals, laundry, and other personal expenses.
- He was an ROR in India for the previous year 2014-15 and a Non-Resident in the foreign country.
- He could not produce any bills to his employer towards his actual expenses, but gave a declaration to the employer that the entire $6,000 was actually incurred by him. As per statistics published in this foreign country’s government publication, the average expenditure per day of a person living in this country for the basic necessities (excluding housing) was $75.

**QUESTIONS**

Q30 Whether the per-diem allowance granted to Shri Gayaram is exempt under section 10(14)(i) of the Act?

Q31 If yes, what would be the amount of exemption?

Q32 Would it make a difference if:

The overseas assignment was to be for 9 months (starting from 1st March 2015) to a branch of I Co.

- His family did not move.
- His payroll remained in India but the housing and per diem was paid overseas by the branch.

Q33 On facts as in Q 32, what would be the tax treatment in previous year 2015-16 as he would have spent more than 183 days outside India?

**ANSWERS**

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Case Study: 6

Facts:

- Employees of ABC US are seconded to work in ABC India for a period of two years, after which they would go back to their employment with ABC US (or other group companies as per the group needs)
- Seconded employees to work in India for the benefit of ABC India
- Payroll of seconded employees is with ABC US and they are being paid salary outside India by ABC US
- ABC US continues contribution to overseas social security
- ABC US has no obligation to replace the seconded employee in case someone returns before the agreed period
- ABC US cross charges entire salary and social security contribution cost to ABC India (without any markup)
- Under local employment letters between seconded employee and ABC India, the seconded employees are brought at par with other local employees – in terms of rights, risks, responsibilities, rewards, termination, etc.
- ABC India has undertaken all tax compliances in India related to salary payment (i.e. withholding tax, filing e-TDS statements, issuance of Form 16, etc.)

QUESTIONS

Q34 What would be the implications from the perspective of the following:

- PE Risk
- TDS on cross charge of salary cost
- Transfer Pricing
- Service Tax

ANSWERS

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The groups are also requested to deliberate this *vis-à-vis* different fact patterns tabulated below:

Change in facts of secondment arrangement

| Q35 | If there is no cross charge of cost by ABC US to ABC India |
| Q36 | If there is a cross charge of cost with markup (for administrative overheads) by ABC US to ABC India |
| Q37 | If ABC US has obligation to replace the seconded employee in case someone returns before the agreed period |
| Q38 | If payroll is shifted to ABC India and the employees do not have lien on employment with ABC US |
| Q39 | If the seconded employees are working under the supervision and control of ABC US |
| Q40 | If part salary cost of seconded employees is borne by ABC US (only part cost cross charged to ABC India) |
APPENDIX 1

Illustrative list of documents required for registration with FRRO where expatriate employee has come on employment visa:

- Online Application Form
- A letter from Indian employer requesting FRRO officials for expatriate employee’s registration
- An undertaking from Indian employer to the effect that it shall take full responsibility for the activities and conduct of expatriate employee
- Copy of passport of the signatory to the above undertaking
- Copy of passport of expatriate employee
- Copy of PAN card
- Copy of visa of expatriate employee
- Copy of employment/assignment letter between Indian employer and expatriate employee
- Copy of lease agreement along with police verification report. If the expatriate employee stays in hotel, then a letter and Form ‘C’ from the hotel
- Expatriate employees photographs (certain specification)

Additional documents required for FRRO registration of family members:

- Copy of passport and visa
- Copy of Birth certificate, in case of registration of accompanying child
- Copy of Marriage certificate, in case of registration of accompanying spouse

Caution: The above list of documents may vary from time to time and jurisdiction to jurisdiction. It is advisable to look up latest on website of Ministry of Home Affair at http://mha1.nic.in/ or Bureau of Immigration at http://boi.gov.in/ or jurisdictional FRRO.

APPENDIX 2 - LIST OF COUNTRIES WITH WHICH INDIA HAS SSA, AS ON 10TH JULY 2015:

<table>
<thead>
<tr>
<th>Sr No</th>
<th>Country Name</th>
<th>Effective Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Belgium</td>
<td>1 September 2009</td>
</tr>
<tr>
<td>2.</td>
<td>Germany</td>
<td>1 October 2009</td>
</tr>
<tr>
<td>3.</td>
<td>Switzerland</td>
<td>29 January 2011</td>
</tr>
<tr>
<td>4.</td>
<td>Luxembourg</td>
<td>1 June 2011</td>
</tr>
<tr>
<td>5.</td>
<td>France</td>
<td>1 July 2011</td>
</tr>
<tr>
<td>6.</td>
<td>Denmark</td>
<td>1 May 2011</td>
</tr>
<tr>
<td>7.</td>
<td>Korea</td>
<td>1 November 2011</td>
</tr>
<tr>
<td>8.</td>
<td>Netherlands</td>
<td>1 December 2011</td>
</tr>
</tbody>
</table>
### Sr No | Country Name | Effective Date
--- | --- | ---
9. | Hungary | 1 April 2013
10. | Finland | 1 August 2014
11. | Sweden | 1 August 2014
12. | Czech Republic | 1 September 2014
13. | Norway | 1 January 2015
14. | Austria | 1 July 2015
15. | Canada | Not yet notified
16. | Japan | Not yet notified
17. | Portugal | Not yet notified
18. | Australia | Not yet notified

**APPENDIX 3 – RELEVANT EXTRACT OF INCOME-TAX ACT AND INCOME-TAX RULES**

#### Definitions

**Section 2** In this Act, unless the context otherwise requires,—

(24) “income” includes—

(iiiia) any special allowance or benefit, other than perquisite included under sub-clause (iii), specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit;

#### Scope of total income

**Section 5**

(1) Subject to the provisions of this Act, the total income of any previous year of a person who is a resident includes all income from whatever source derived which—

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year;

or

(c) accrues or arises to him outside India during such year:

Provided that, in the case of a person not ordinarily resident in India within the meaning of sub-section (6)* of section 6, the income which accrues or arises to him outside India shall not be so included unless it is derived from a business controlled in or a profession set up in India.

(2) Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which—

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year.
Explanation 1.—Income accruing or arising outside India shall not be deemed to be received in India within the meaning of this section by reason only of the fact that it is taken into account in a balance sheet prepared in India.

Explanation 2.—For the removal of doubts, it is hereby declared that income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.

Residence in India

Section 6. For the purposes of this Act,—

(1) An individual is said to be resident in India in any previous year, if he—

(a) is in India in that year for a period or periods amounting in all to one hundred and eighty-two days or more; or

(b) [* * *]

(c) having within the four years preceding that year been in India for a period or periods amounting in all to three hundred and sixty-five days or more, is in India for a period or periods amounting in all to sixty days or more in that year.

[Explanation 1].—In the case of an individual,—

(a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act, 1958 (44 of 1958), or for the purposes of employment outside India, the provisions of sub-clause (c) shall apply in relation to that year as if for the words “sixty days”, occurring therein, the words “one hundred and eighty-two days” had been substituted;

(b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to clause (e) of section 115C, who, being outside India, comes on a visit to India in any previous year, the provisions of sub-clause (c) shall apply in relation to that year as if for the words “sixty days”, occurring therein, the words “one hundred and eighty-two days” had been substituted.

[Explanation 2.—For the purposes of this clause, in the case of an individual, being a citizen of India and a member of the crew of a foreign bound ship leaving India, the period or periods of stay in India shall, in respect of such voyage, be determined in the manner and subject to such conditions as may be prescribed.]

........

(5) If a person is resident in India in a previous year relevant to an assessment year in respect of any source of income, he shall be deemed to be resident in India in the previous year relevant to the assessment year in respect of each of his other sources of income.

(6) A person is said to be “not ordinarily resident” in India in any previous year if such person is—
(a) an individual who has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less; or

(b) a Hindu undivided family whose manager has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less.

Income deemed to accrue or arise in India

Section 9. (1) The following incomes shall be deemed to accrue or arise in India:

(ii) income which falls under the head “Salaries”, if it is earned in India.

Explanation.—For the removal of doubts, it is hereby declared that the income of the nature referred to in this clause payable for—

(a) service rendered in India; and

(b) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment, shall be regarded as income earned in India;

Incomes not included in total income

Section 10. In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

6) in the case of an individual who is not a citizen of India,—

(vi) the remuneration received by him as an employee of a foreign enterprise for services rendered by him during his stay in India, provided the following conditions are fulfilled—

(a) the foreign enterprise is not engaged in any trade or business in India;  
(b) his stay in India does not exceed in the aggregate a period of ninety days in such previous year; and  
(c) such remuneration is not liable to be deducted from the income of the employer chargeable under this Act

………..

(14) (i) any such special allowance or benefit, not being in the nature of a perquisite within the meaning of clause (2) of section 17, specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, 39 as may be prescribed, to the extent to which such expenses are actually incurred for that purpose;

(ii) any such allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at the place where he ordinarily resides, or to compensate him for the
increased cost of living, as may be prescribed and to the extent as may be prescribed 40:

Provided that nothing in sub-clause (ii) shall apply to any allowance in the nature of personal allowance granted to the assessee to remunerate or compensate him for performing duties of a special nature relating to his office or employment unless such allowance is related to the place of his posting or residence;

Prescribed allowances for the purposes of clause (14) of section 10

Rule 2BB. (1) For the purposes of sub-clause (i) of clause (14) of section 10, prescribed allowances, by whatever name called, shall be the following, namely:

(a) any allowance granted to meet the cost of travel on tour or on transfer;

(b) any allowance, whether, granted on tour or for the period of journey in connection with transfer, to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty;

(c) any allowance granted to meet the expenditure incurred on conveyance in performance of duties of an office or employment of profit:

Provided that free conveyance is not provided by the employer;

(d) any allowance granted to meet the expenditure incurred on a helper where such helper is engaged for the performance of the duties of an office or employment of profit;

(e) any allowance granted for encouraging the academic, research and training pursuits in educational and research institutions;

(f) any allowance granted to meet the expenditure incurred on the purchase or maintenance of uniform for wear during the performance of the duties of an office or employment of profit.

Explanation: For the purpose of clause (a), “allowance granted to meet the cost of travel on transfer” includes any sum paid in connection with transfer, packing and transportation of personal effects on such transfer.

A.—Salaries

Salaries

Section 15. The following income shall be chargeable to income-tax under the head “Salaries”:

(a) any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not;

(b) any salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer though not due or before it became due to him;

(c) any arrears of salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer, if not charged to income-tax for any earlier previous year.
Explanation 1.— For the removal of doubts, it is hereby declared that where any salary paid in advance is included in the total income of any person for any previous year it shall not be included again in the total income of the person when the salary becomes due.

Explanation 2.—Any salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from the firm shall not be regarded as “salary” for the purposes of this section.

“Salary”, “perquisite” and “profits in lieu of salary” defined.

17. For the purposes of sections 15 and 16 and of this section,—

(2) “perquisite” includes—

(vi) the value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the assessee.

Explanation.—For the purposes of this sub-clause,—

(a) “specified security” means the securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) and, where employees’ stock option has been granted under any plan or scheme therefor, includes the securities offered under such plan or scheme;

(b) “sweat equity shares” means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called;

(c) the value of any specified security or sweat equity shares shall be the fair market value of the specified security or sweat equity shares, as the case may be, on the date on which the option is exercised by the assessee as reduced by the amount actually paid by, or recovered from, the assessee in respect of such security or shares;

(d) “fair market value” means the value determined in accordance with the method as may be prescribed;

(e) “option” means a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price.

Agreement with foreign countries or specified territories

90. (1) The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India,—

(a) for the granting of relief in respect of—

(i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or

(ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or
(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory, as the case may be, or

(c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be,

and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

(2) Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

Following sub-section (2A) shall be inserted after sub-section (2) of section 90 by the Finance Act, 2013, w.e.f. 1-4-2016:

(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee even if such provisions are not beneficial to him.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

(4) An assessee, not being a resident, to whom an agreement referred to in sub-section (1) applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory.

(5) The assessee referred to in sub-section (4) shall also provide such other documents and information, as may be prescribed.

Explanation 1.—For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

Explanation 2.—For the purposes of this section, “specified territory” means any area outside India which may be notified as such by the Central Government.

Explanation 3.—For the removal of doubts, it is hereby declared that where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued thereunder being in force, then, the meaning
assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.

**Countries with which no agreement exists**

91. (1) If any person who is resident in India in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India), he has paid in any country with which there is no agreement under section 90 for the relief or avoidance of double taxation, income-tax, by deduction or otherwise, under the law in force in that country, he shall be entitled to the deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

(2) If any person who is resident in India in any previous year proves that in respect of his income which accrued or arose to him during that previous year in Pakistan he has paid in that country, by deduction or otherwise, tax payable to the Government under any law for the time being in force in that country relating to taxation of agricultural income, he shall be entitled to a deduction from the Indian income-tax payable by him—

(a) of the amount of the tax paid in Pakistan under any law aforesaid on such income which is liable to tax under this Act also; or

(b) of a sum calculated on that income at the Indian rate of tax;

whichever is less.

(3) If any non-resident person is assessed on his share in the income of a registered firm assessed as resident in India in any previous year and such share includes any income accruing or arising outside India during that previous year (and which is not deemed to accrue or arise in India) in a country with which there is no agreement under section 90 for the relief or avoidance of double taxation and he proves that he has paid income-tax by deduction or otherwise under the law in force in that country in respect of the income so included he shall be entitled to a deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income so included at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

**Deduction at source**

**Salary**

192. 40(1) Any person responsible for paying any income chargeable under the head “Salaries” shall, at the time of payment, deduct income-tax on the amount payable at the average rate of income-tax computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the assessee under this head for that financial year.

(1A) Without prejudice to the provisions contained in sub-section (1), the person responsible for paying any income in the nature of a perquisite which is not provided for by way of monetary payment, referred to in clause (2) of section 17, may pay, at his option, tax on the whole or part of such income without making any deduction therefrom at the time when such tax was otherwise deductible under the provisions of sub-section (1).
(1B) For the purpose of paying tax under sub-section (1A), tax shall be determined at the average of income-tax computed on the basis of the rates in force for the financial year, on the income chargeable under the head “Salaries” including the income referred to in sub-section (1A), and the tax so payable shall be construed as if it were, a tax deductible at source, from the income under the head “Salaries” as per the provisions of sub-section (1), and shall be subject to the provisions of this Chapter.

(2) Where, during the financial year, an assessee is employed simultaneously under more than one employer, or where he has held successively employment under more than one employer, he may furnish to the person responsible for making the payment referred to in sub-section (1) (being one of the said employers as the assessee may, having regard to the circumstances of his case, choose), such details of the income under the head “Salaries” due or received by him from the other employer or employers, the tax deducted at source therefrom and such other particulars, in such form and verified in such manner as may be prescribed41, and thereupon the person responsible for making the payment referred to above shall take into account the details so furnished for the purposes of making the deduction under sub-section (1).

APPENDIX 4

INDIA-USA DTAA

ARTICLE 4 : RESIDENCE

1. For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, citizenship, place of management, place of incorporation, or any other criterion of a similar nature, provided, however, that

(a) this term does not include any person who is liable to tax in that State in respect only of income from sources in that State; and

(b) in the case of income derived or paid by a partnership, estate, or trust, this term applies only to the extent that the income derived by such partnership, estate, or trust is subject to tax in that State as the income of a resident, either in its hands or in the hands of its partners or beneficiaries.

(2) Where by reason of the provisions of paragraph 1, an individual is a resident of both Contracting States, then his status shall be determined as follows:

(a) he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (centre of vital interests);

(b) if the State in which he has his centre of vital interests cannot be determined, or if he does not have a permanent home available to him in either State, he shall be deemed to be a resident of the State in which he has an habitual abode;

(c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident of the State of which he is a national;
(d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where, by reason of paragraph 1, a company is a resident of both Contracting States, such company shall be considered to be outside the scope of this Convention except for purposes of paragraph 2 of Article 10 (Dividends), Article 26 (Non-Discrimination), Article 27 (Mutual Agreement Procedure), Article 28 (Exchange of Information and Administrative Assistance) and Article 30 (Entry into Force).

4. Where, by reason of the provisions of paragraph 1, a person other than an individual or a company is a resident of both Contracting States, the competent authorities of the Contracting States shall settle the question by mutual agreement and determine the mode of application of the Convention to such person.

ARTICLE 16 : DEPENDENT PERSONAL SERVICES

1. Subject to the provisions of Articles 17 (Directors’ Fees), 18 (Income Earned by Entertainers and Athletes), 19 (Remuneration and Pensions in respect of Government Service), 20 (Private Pensions, Annuities, Alimony and Child Support), 21 (Payments received by Students and Apprentices) and 22 (Payments received by Professors, Teachers and Research Scholars), salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State, if:

   (a) the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in the relevant taxable year;

   (b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and

   (c) the remuneration is not borne by a permanent establishment or a fixed base or a trade or business which the employer has in the other State.

3. Notwithstanding the preceding provisions of this Article, remuneration derived in respect of an employment exercised aboard a ship or aircraft operating in international traffic by an enterprise of a Contracting State may be taxed in that State.

ARTICLE 25 - RELIEF FROM DOUBLE TAXATION

1. In accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the general principle hereof), the United States shall allow to a resident or citizen of the United States as a credit against the United States tax on income—

   (a) the income-tax paid to India by or on behalf of such citizen or resident; and

   (b) in the case of a United States company owning at least 10 per cent of the voting stock of a company which is a resident of India and from which the United States
company receives dividends, the income-tax paid to India by or on behalf of the distributing company with respect to the profits out of which the dividends are paid.

For the purposes of this paragraph, the taxes referred to in paragraphs 1(b) and 2 of Article 2 (Taxes Covered) shall be considered as income taxes.

2. (a) Where a resident of India derives income which, in accordance with the provisions of this Convention, may be taxed in the United States, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income-tax paid in the United States, whether directly or by deduction. Such deduction shall not, however, exceed that part of the income-tax (as computed before the deduction is given) which is attributable to the income which may be taxed in the United States.

(b) Further, where such resident is a company by which a surtax is payable in India, the deduction in respect of income-tax paid in the United States shall be allowed in the first instance from income-tax payable by the company in India and as to the balance, if any, from surtax payable by it in India.

3. For the purposes of allowing relief from double taxation pursuant to this article, income shall be deemed to arise as follows:

(a) income derived by a resident of a Contracting State which may be taxed in the other Contracting State in accordance with this Convention [other than solely by reason of citizenship in accordance with paragraph 3 of article 1 (General Scope)] shall be deemed to arise in that other State;

(b) income derived by a resident of a Contracting State which may not be taxed in the other Contracting State in accordance with the Convention shall be deemed to arise in the first-mentioned State.

Notwithstanding the preceding sentence, the determination of the source of income for purposes of this article shall be subject to such source rules in the domestic laws of the Contracting States as apply for the purpose of limiting the foreign tax credit. The preceding sentence shall not apply with respect to income dealt with in article 12 (Royalties and Fees for Included Services). The rules of this paragraph shall not apply in determining credits against United States tax for foreign taxes other than the taxes referred to in paragraphs 1(b) and 2 of article 2 (Taxes Covered).

APPENDIX 5

INDIA-JAPAN DTAA

ARTICLE 4

1. For the purposes of this Convention, the term ‘resident of a Contracting State’ means any person who, under the laws of that Contracting State, is liable to tax therein by reason of his domicile, residence, place of head or main office or any other criterion of a similar nature.

2. Where by reason of the provisions of paragraph 1 a person is a resident of both Contracting States, then the competent authorities of Contracting States shall determine
by mutual agreement the Contracting State of which that person shall be deemed to be a resident for the purposes of this Convention.

ARTICLE 15
1. Subject to the provisions of articles 16, 18, 19, 20 and 21, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that Contracting State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other Contracting State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned Contracting State, if:
   
   (a) the recipient is present in that other Contracting State for a period or periods not exceeding in the aggregate 183 days during any taxable year or ‘previous year’, as the case may be; and
   
   (b) the remuneration is paid by, or on behalf of, an employer who is not a resident of that other Contracting State; and
   
   (c) the remuneration is not borne by a permanent establishment or a fixed base which the employer has in that other Contracting State.

3. Notwithstanding the provisions of paragraphs 1 and 2, remuneration in respect of an employment exercised aboard a ship or aircraft operated in international traffic by an enterprise of a Contracting State may be taxed in that Contracting State.

ARTICLE 23
1. The laws in force in either of the Contracting States shall continue to govern the taxation of income in the respective Contracting State except where express provisions to the contrary are made in this Convention.

2. Double taxation shall be avoided in the case of India as follows:

   (a) Where a resident of India derives income which, in accordance with the provisions of this Convention, may be taxed in Japan, India shall allow as a deduction from the tax on the income of that resident an amount equal to the Japanese tax paid in Japan, whether directly or by deduction. Such deduction in either case shall not, however, exceed that part of the income-tax (as computed before the deduction is given) which is attributable, as the case may be, to the income which may be taxed in Japan. Further, where such resident is a company by which surtax is payable in India, the deduction in respect of income-tax paid in Japan shall be allowed in the first instance from income-tax payable by the company in India and as to the balance, if any, from surtax payable by it in India.

   (b) Where a resident of India derives income which, in accordance with the provisions of this Convention, shall be taxable only in Japan, India may include this income in the tax base but shall allow as a deduction from the income-tax that part of the income-tax which is attributable, as the case may be, to the income derived from Japan.
3. Subject to the laws of Japan regarding the allowance as a credit against Japanese tax of tax payable in any country other than Japan:

(a) Where a resident of Japan derives income from India which may be taxed in India in accordance with the provisions of this Convention, the amount of Indian tax payable in respect of that income shall be allowed as a credit against the Japanese tax imposed on that resident. The amount of credit, however, shall not exceed that part of the Japanese tax which is appropriate to that income.

(b) Where the income derived from India is a dividend paid by a company which is a resident of India to a company which is a resident of Japan and which owns not less than 25 per cent either of the voting shares of the company paying the dividend, or of the total shares issued by that company, the credit shall take into account the Indian tax payable by the company paying the dividend in respect of its income.

(c) 1[***]