TAXABILITY OF SALARY IN INDIA FOR WORK DONE ABROAD

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BACKGROUND

Owing to the process of globalisation and demand for know-how, it is common that individuals move abroad for exercising employment. The salary is paid to such person being the compensation to the employee for his services made available to the employer. If such Salary income of an assessee, who is a Non-Resident Indian, is paid in India for the employment exercised abroad, various facets involved in determining the point of taxability of such income with respect to provisions of Income Tax Act and the Tax Treaty are discussed below.

For **Example**, Mr.X is an Indian Resident working in Company 'A' in India. Later, he gets seconded to another Company ' B' situated in Switzerland. He works there for more than 200 days in the Previous Year and qualifies as a Resident of Switzerland but he remains in the payroll of Company A and receives his salary credited to his Indian Bank Account.

The question is whether the salary of Mr. X is qualified for exemption in India with respect to tax paid in Switzerland referring to provisions of the act and the tax treaty.

TAXABILITY OF SALARY INCOME

For determining the point of taxability of any income the primary test is whether or not the assessee is a Resident in India for which Section 6 provides a clear picture as to its ascertainment. The premise here is that of the status of the assessee as a Non- Resident Indian.

Application of Income Tax Act

The computation of total income of a Non-Resident has been stated in Section 5(2) of the Act and reproduced below:

***"5. Scope of total income**:-*

(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."

The other relevant provision in the act involved with the point of taxability is Section 9(1) (ii) of the act which deals with income deemed to accrue or arise in India and it reads as follows:

"*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;"

From the plain reading of the above quoted sections, it can be concluded that the salary income being received in India is subject to tax only in India.

Explanation 2 to Section 5 clarifies that income will not be treated to be received in India solely on the basis that such income was received or deemed to be received in India. Therefore, it has to be found out where the income to the person concerned had accrued for ascertaining its taxability.

There is an alternate and a right view that arises which can be obtained while reading Section 5(2) with Section 9(1) (ii) as Section 5 should be interpreted and effected in reconciliation with other provisions of the act since it starts with an expression 'subject to the provisions of the act.'

If Section 5(2), as stated in the act, is read with Section 9(1) (ii), the subsequent conclusion flows to the effect that the salary cannot be taxed in India only for the reason that it was received in India but it is said to be taxed at the place of its accrual which would be India if, and only if, the services are rendered in India otherwise in the place where such services were rendered.

The Calcutta High Court in the case of *Commissioner Of Income-Tax v. Nippon Yusen Kaisha*[1] placed its view with respect to interpretation of Section 5(2) of the act in as much as if other provisions of the act are contrary to Section 5(2), then such provisions will have an overriding effect over the Section.

The Apex court also held that the location where salary is received is of no consequence with respect to taxability in India in *CIT v. LW Russel*[2].

Therefore the view established is that the relevant criterion for determining the point of taxation of salary income in India should be based on right to receive and not on receipt of such income.

Place of accrual of Income

In order to determine the point of taxability, it is essential to find where the income to the person concerned has accrued which is equated to the place where services were rendered. This was affirmed by the Calcutta High Court in *Utanka Roy v. DIT*[3].

Reading section 9(1) (ii) clearly tells that the situs of accrual of salary income is the situs of service rendered. The ITAT, Agra in *Arvind Singh Chauhan vs. ITO*[4] asserted this view thereby affirming the ruling given in *Avtar Singh Wadhwan case*[5] and further held that mere signing of the contract in India does not mean that the salary accrued in India. Therefore, for the purpose of better understanding, the need for classification between 'income being received' and 'amount being received' arises which is determined on the basis of character of income received.

Income cannot be taxed at every point of receipt. Salary can be accrued outside India and by arrangement be remitted to India. Only when services are rendered in India, it becomes

1 1998 233 ITR 158 Cal.
2 1965 AIR 49.
3 390 ITR 109(Calcutta)
4 (2014) 147 ITD 409.
5 2001 247 ITR 260 (Bom.)

taxable by implication. However, receipt cannot become the only criteria to trigger taxability u/s 5(2) (a). Right to receive salary accrued at the place where services were rendered and transfer of money to India was for a matter of convenience.

Recent ruling given by the Authority for Advanced Ruling, New Delhi in the case of *Texas instruments (India) Pvt Ltd*[6] stated that salary received in India by a Non- Resident employee in respect of services rendered outside India is said to be accrued outside India and cannot be taxable in India.

The Hon'ble Bombay High Court also stresses on the point that the relevant criteria for deciding the place of taxability is the place where the services are rendered and not the place of execution of contract as in the case of *Avtar Singh Wadhwan*[7] wherein the facts pertained to the assessee working in an Indian ship that floated in international waters qualified as a Non-Resident but was employed by and received his salary from Shipping Corporation of India.

Also Circular 13 of 2017 holds that "salary accrued to a Non-Resident seafarer for services rendered outside India on a foreign going ship shall not be taxed in India merely because the amount was credited to NRE Account maintained with an Indian Bank by the sea-farer.

The Hon'ble Madras High Court took a similar view on the matter in the case *CIT v. AP Kalyanakrishnan*[8] stating that the pension of the assessee (RNOR) which was accrued in Malaysia and remitted to India has suffered tax in Malaysia and hence exempt from being taxable in India.

While Hon'ble Karnataka High Court in *Prahlad Vijendra Rao*[9] asserted that the application of Section 5(2) (b) demands the criteria that the income is earned in India for the services rendered in India and not otherwise. Salary derived by an assessee for working abroad for 225 days has been held as not accrues nor deemed to have been accrued in India.

Hence, these cases hold that place of accrual depends on where the services are rendered which gives rise to such payment. Also that income accrued outside India should be taxed in such country and be exempted in India.

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6 A.A.R. No 1299 of 2012
7 *Supra* Note 5
8 195 ITR 534 (Mad.).
9 2011 198 Taxman 551

On the other hand, the Bombay High Court took a contrary view in *A. L. Fernandez v. ITO*[10] by laying down that the receipt of salary in a country is sufficient to give that country the right to tax on such salary income which was highlighted in the case of *Shri Tapan Krishna Pattanaik v. DDIT*[11] by ITAT, Kolkata. But such an inference was made considering two essential elements: (1) income did not suffer taxation in any jurisdiction (2) receipt of salary in NRE Account in India was the initial point of receipt by assessee and he had no control over such funds before being credited to such NRE account.

With reference to Paragraph I of 2005 Model OECD commentary, the general rule with respect to taxation of salary income is that it is taxable in the state where the employment is actually exercised. This again leads to a question where the employment is said to be exercised. This can be traced to the place the employee is physically present while performing activities in course of employment for which salary is paid.

Applicability of DTAA

The income tax act allows for adoption of provisions of the act or of the treaty, whichever stands beneficial to the assessee according to Section 90(2). Being a resident of other country makes an assessee eligible for claiming tax exemption in India under the relevant tax treaty as according to the case of *Raman Chopra*[12].

The relevant Articles in the current issue are **Article 15** (Dependent Personal Services) and **Article 23** (Elimination of Double Taxation) in the agreement between the Republic of India and the Swiss Confederation for the avoidance of double taxation with respect to taxes on income as per the **example** taken above.

The provisions of Article 23 of India- Switzerland DTAA at the outset state that "*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 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.*

10 (2002) 75 TTJ Mumbai 714
11 ITA No.68/Kol/2016
12 [2016] 69 Taxmann.com 452 (Del.)

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 any 12 month period commencing or ending in the fiscal year concerned, and

(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 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 operated in international traffic, by an enterprise of a Contracting State may be taxed in that State."

Article 23 of the said DTAA reads as follows:

"*1. - (a) Subject to any provisions of the law of India which may from time to time be in force and which relates to the relief of taxes paid in a country outside India, where a resident of India derives income which, in accordance with the provisions of this Agreement, may be taxed in Switzerland, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income-tax paid in Switzerland 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 Switzerland.*

(b) Where a resident of Switzerland derives gains from the alienation of shares which may be taxed in India according to Article 13, paragraph 5, sub-paragraph (b), India shall allow as a deduction from tax on that income, an amount equal to the income-tax paid in Switzerland on these capital gains. The deduction shall not, however, exceed that part of the Indian income-tax, which is imposed on these capital gains.

2. (a) Where a resident of Switzerland derives income which, in accordance with the provisions of this Agreement may be taxed in India, Switzerland shall, subject to the provisions of sub-paragraphs (b), (c) exempt such income from tax but may, in calculating tax on the remaining income of that resident, apply the rate of tax which would have been applicable, if the exempted income had not been so exempted : provided, however, that such

exemption shall apply to gains referred to in paragraph of Article 13 only if actual taxation of such gains in India is demonstrated.

(b) Where a resident of Switzerland derives dividends, interest, royalties or fees for [technical] services which, in accordance with the provisions of Articles 10, 11 and 12, may be taxed in India, Switzerland shall allow, upon request, a relief to such resident. The relief may consist of,

(i) a credit from the Swiss tax on the income of that resident of an amount equal to the tax levied in India in accordance with the provisions of Articles 10, 11 and 12, such credit shall not, however, exceed that part of the Swiss tax, as computed before the credit is given, which is appropriate to the income which may be taxed in India; or

(ii) a lump sum reduction of the Swiss tax; or

(iii) a partial exemption of such dividends, interest, royalties or fees for technical services from Swiss tax, in any case consisting at least of the deduction of the tax levied in India from the gross amount of the dividends, interest, royalties or fees for technical services.

Switzerland shall determine the applicable relief and regulate the procedure in accordance with the Swiss provisions relating to the carrying out of international Conventions of the Swiss Confederation for the avoidance of double taxation."

From reading Article 15, we can infer that the assessee can claim exemption for the taxes paid abroad (in this case, Switzerland) for his salary income earned there.

But there arose an issue with the interpretation of provisions in DTAA which lead to the conclusion that the provisions of DTAA is applicable only to Resident Indians and does not work to the benefit of NRI while Article 15(1) is read with Article 23. It sounds clear that Article 23 pertains to grant of Foreign Tax Credit on income of a Resident which is also subject to tax in another country while Article 15(1) specifically provides that salary derived by a resident of Switzerland is taxable only in Switzerland in respect of employment exercised in Switzerland which has no specific nexus with each other.

The recent case of *Shri Swaminathan Ravichandran*[13] pertaining to this issue was brought up before ITAT, Chennai in the year 2016 which washed away the trail left by the previous

13 ITA No.299/Mds./2016

judicial precedents by declaring the scope of DTAA to the effect that it is applicable only to the Resident of India. In my considered opinion, this conclusion seems to have been arrived at by wrongly interpreting the language of relevant provision in DTAA by connecting Dependent Personal Service (DPS) clause with Elimination of Double Taxation clause which has no specific nexus. This ruling has got a wide repercussion as the benefits given to Non-Residents becomes meaningless and absurd thereby rendering the DTAA otiose. Also such an interpretation taken by the judiciary is also repugnant to the very Article I of the DTAA agreement as they read that provisions are applicable to the residents of either of contracting state or both the contracting states.

Therefore, this decision has caused grievance to the assessee who becomes disentitled to get exemption for such income which has already suffered tax in the other contracting state thereby leading to double taxation.

CONCLUSION:

The primary task of the judiciary lies in its interpretation of the provisions engraved in the statutes. There has been a tremendous and phenomenal wide ranging interpretation with respect to taxing statutes that has been laid down in plethora of cases. There is a need to remove the scepticism involved in triggering taxability of salary of a Non-Resident who receives his salary in India but which accrued abroad and also as to the criteria involved to determine place of accrual. In light of above quoted assertions and judicial precedents involving settled principles of law, it is just and proper to hold that salary income of an NRI received in India for the work done abroad should be taxed in the contracting state where he rendered such work and such income should be allowed as an exemption in India.