Overview of a Treaty or DTAA

- ✓ Every nation has a right to tax its residents on their global income.
- ✓ As a result, the income of a person may get taxed in both the countries i.e., in the home country (country of origin) as well as the foreign country (country person operates)
- ✓ In home country tax is an obligation, while in foreign country tax is a cost.
- ✓ Double Tax Avoidance Agreements (DTAA) comes into play to mitigate hardships caused by taxing the same income twice.

Treaty – Meaning:

A tax treaty is form of agreement between two or more national jurisdictions concerning taxes where the main purpose of which is to regulate matters concerning taxes.

The application of the term 'treaty' in the generic sense signifies that the parties intend to create rights and obligation enforceable under international law.

They are agreements between two countries and not two taxpayers. Double taxation is eliminated by allocation of exclusive right to tax or sharing taxing rights.

General terms used in DTAA:

- Contracting state = A country which enters in to a contract
- State of residence = A country wherein a person resides
- State of source = A country wherein income arises/accrues
- Enterprise of a contracting state = Any taxable entity
- Permanent establishment = A fixed base or a business connection (say a branch or an dependent agent) of enterprise in the state of source

For easier understanding replace the words 'Contracting states' by names of the respective countries and read the DTAA.

Types of Double Taxation:

In general it can be either

Juridical double taxation i.e., Two or more countries levy taxes on same entity or person on same income for same period. It is the result of a conflict between two tax systems. This arises due to overlapping claims of tax jurisdictions on interrelated economic activities.

Say for example if a NR assessee comes into India to provide any services from USA. Income from such services may be taxable in India as services are provided in India and also the total income of the NR is taxed in USA which includes the services in India as NR is resident of USA.

Economic double taxation i.e., same transaction or income is taxed in two or more states during the same period but in the hands of different taxpayers.

Say for example a NR Company receives dividend income from an Indian Company wherein such a dividend income is included in the taxable income of the NR. Hence both the Indian Company and the NR Company pays tax on the same income.

Articles of DTAA:

ARTICLE 1 - *General Scope* & ARTICLE 2 - *Taxes covered* – To whom the treaty applies

ARTICLE 3 - *General definitions*

ARTICLE 4 - *Residence*

ARTICLE 5 - Permanent Establishment (PE)

ARTICLE 6 - Income from immovable property

ARTICLE 7 - Business profits

Taxation of net profits by Source Company allowed to the extent that is attributable to PE.

ARTICLE 8 - Shipping and air transport

ARTICLE 9 - Associated enterprises

ARTICLE 10 – Dividends

ARTICLE 11 – Interest

ARTICLE 12 – Royalties and fees for included services

Exclusive taxation by country of residence. However definition of fees for included services has certain exclusions.

ARTICLE 13 – Capital Gains

ARTICLE 14 - Permanent establishment tax

ARTICLE 15 – Independent Personal Services

Taxable if fixed base exists or stayed for more than specified number of days in the other country in the relevant previous year.

ARTICLE 16 - Dependent personal services

Taxation of employment income by source country but exemption if employee is present for less than specified number of days and employer is NR.

ARTICLE 17 - Directors' fees

Directors' fees and similar payments taxed in country of residence.

ARTICLE 18 - Income earned by entertainers and athletes

ARTICLE 19 - ***Remuneration and pensions in respect of Government service***

ARTICLE 20 - ***Private pensions, annuities, alimony and child support***

ARTICLE 21 - ***Payments received by students and apprentices***

ARTICLE 22 - ***Payments received by professors, teachers and research scholars***

ARTICLE 23 - ***Other income***

ARTICLE 24 - ***Limitation on benefits***

ARTICLE 25 - ***Relief from double taxation***

ARTICLE 26 - ***Non-discrimination***

ARTICLE 27 - ***Mutual agreement procedure***

ARTICLE 28 - ***Exchange of information and administrative assistance***

ARTICLE 29 - ***Diplomatic agents and consular officers***

ARTICLE 30 - ***Entry into force; and***

ARTICLE 31 – ***Termination***

Treaty Source Rule:

Income	Rule
Immovable property	Place where situated
Business profits and professional services	Permanent establishment or fixed base
Shipping and air transport	Place of management
Dividend, interest income and directors fees	Residence of the payer
Employment services, artistes and sportsman	Place of work
Government salaries and pensions	Country of the payer
Other income	Residence of the recipient

Q. Can DTAA levy higher tax than domestic rates?

Ans. As per Sec 90(2) an assessee has the option to choose between domestic tax law and DTAA whichever is beneficial to him/her. So in case of a higher tax burden imposed by DTAA an assessee is free to go by domestic favorable tax law as DTAA is not compulsory.