

DOUBLE TAXATION RELIEF

Some key points

Bilateral relief

Under this method, the Government of two countries can enter into an agreement to provide relief against double taxation by mutually working out the basis on which the relief is to be granted. The Government of India has entered into such Double Taxation Avoidance Agreement (DTAA) with more than 70 countries so far.

The DTAA would override the general provisions of the Income-tax Act, 1961 and the assessee may choose the treaty or the regular provisions whichever is beneficial to him.

Bilateral relief may be granted in either one of the following methods.

- (a) **Exemption method** by which a particular income is taxed in only one of the two countries;
- (b) **Tax relief method**, under which, an income is taxable in both the countries in accordance with the agreement. However, the country of residence of the taxpayer would allow him the credit for the tax charged thereon in the country of source.

In India, double taxation relief is provided by a combination of the two methods.

Unilateral relief

This method provides relief of some kind by the home country even where no mutual agreement has been entered into between the two countries.

Question 1

Kalpesh Kumar (aged 50 years) is a musician deriving income of Rs.75,000 from concerts performed outside India. Tax of Rs.10,000 was deducted at source in the country where the concerts were performed. India does not have any double tax avoidance agreement with that country. His income in India amounted to Rs.2,25,000. Compute tax liability of Kalpesh Kumar for the assessment year 2011-12 assuming he has deposited Rs.10,000 in Public Provident Fund and paid medical insurance premium in respect of his father (aged 76 years) Rs.20,000.

Answer

An assessee shall be allowed deduction under section 91 provided all the following conditions are fulfilled :-

- (a) The assessee is a resident in India during the relevant previous year.

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- (b) The income accrues or arises to him outside India during that previous year.
- (c) Such income is not deemed to accrue or arise in India during the previous year.
- (d) The income in question has been subjected to income-tax in the foreign country in the hands of the assessee and the assessee has paid tax on such income in the foreign country.
- (e) There is no agreement under section 90 for the relief or avoidance of double taxation between India and the other country where the income has accrued or arisen.

In view of the aforesaid provisions, deduction under section 91 will be calculated as follows:

Particulars	Rs.	Rs.
Indian Income		2,25,000
Foreign Income		<u>75,000</u>
Gross Total Income		3,00,000
Less: <u>Deduction under section 80C</u>		
PPF Contribution	10,000	
<u>Deduction under section 80D</u>		
Medical insurance premium of father (See Note 2 below)	<u>20,000</u>	<u>30,000</u>
Total Income		<u>2,70,000</u>
Tax on total income		11,000
Add: Surcharge		Nil
Add: Education Cess @ 2%		220
Secondary and higher education cess @ 1%		<u>110</u>
		<u>11,330</u>
Average rate of tax in India [i.e. Rs.11,330/2,70,000 x 100]		4.20%
Average rate of tax in foreign country [i.e. Rs.10,000/ Rs.75,000 x 100]		13.33%
Doubly taxed income		75,000
Rebate under section 91 on Rs.75,000 @ 4.20% (lower of average Indian tax rate and foreign tax rate)		3,150
Tax payable in India [Rs.11,330 – Rs.3,150]		8,180

Notes:

- (1) It has been assumed that Mr. Kalpesh Kumar is a resident.
- (2) In respect of medical insurance premium paid for father Rs.20,000 is allowed in full under section 80D.

Question 2

An assessee, on fulfillment of certain conditions, can claim relief in respect of the income arising in those countries with which India does not have any double taxation agreement. Do you agree?

Answer

The assessee shall be allowed relief in respect of such income under section 91 provided all the following conditions are fulfilled :-

- (a) The assessee is a resident in India during the relevant previous year.
- (b) The income accrues or arises to him outside India during that previous year.
- (c) Such income is not deemed to accrue or arise in India during the previous year.
- (d) The income in question has been subjected to income-tax in the foreign country in the hands of the assessee and the assessee has paid tax on such income in the foreign country.
- (e) There is no agreement under section 90 for the relief or avoidance of double taxation between India and the other country where the income has accrued or arisen.

Question 3

Mr. Bansal, a resident Indian and aged 67 years, has derived the following income during the previous year 2010-11:

	Rs.
(i) Income from business in India	2,50,000
(ii) Commission (Gross) from a company in Hong Kong (Tax paid in Hong Kong Rs.60,000)	3,00,000
(iii) Dividend (Gross) from a company in Hong Kong (Tax paid in Hong Kong Rs.18,000)	90,000
(iv) Interest on fixed deposit and savings account with banks in India	2,00,000

India has no double tax avoidance agreement with Hong Kong. Compute the income and tax payable by Mr. Bansal for assessment year 2011-12.

Answer

Mr. Bansal is entitled to relief under section 91, since :-

- (i) He is a resident in India during the relevant previous year.

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- (ii) Income, by way of commission and dividend, accrues or arises to him outside India (in Hong Kong) during the previous year.
- (iii) Such income is not deemed to accrue or arise in India during the previous year.
- (iv) The income in question, namely, commission and dividend, has been subjected to income-tax in Hong Kong in the hands of Mr. Bansal and he has paid tax on such income in Hong Kong.
- (v) There is no agreement under section 90 for the relief or avoidance of double taxation between India and Hong Kong.

Therefore, he is entitled to the deduction under section 91, from the Indian income-tax payable by him, of a sum, calculated on such doubly taxed income at the Indian rate of tax or at the Hong Kong rate of tax, whichever is lower.

Computation of total income and tax liability of Mr. Bansal for A.Y.2011-12

Particulars	Rs.
Income from business in India	2,50,000
Commission received from a company in Hong Kong	3,00,000
Dividend received from a company in Hong Kong	90,000
Interest on fixed deposits and savings account with banks in India	2,00,000
Total Income	8,40,000
Tax on the above:	
Upto Rs.2,40,000	Nil
Over Rs.2,40,000 & upto Rs.5,00,000 @ 10%	26,000
Over Rs.5,00,000 & upto Rs. 8,00,000 @ 20%	60,000
Over Rs.8,00,000 @ 30%	12,000
	98,000
Education cess @ 2% and secondary and higher education cess @ 1%	2,940
Total tax liability	1,00,940
Average rate of income-tax in India: (1,00,940/8,40,000 x 100)	12.02%
Average rate of income-tax in Hong Kong (78,000/3,90,000 x 100)	20%
Double tax relief under section 91 shall be @12.02% or 20% of foreign income, whichever is less [i.e., 3,90,000 x 12.02%]	46,878
Net tax liability (Rs.1,00,940 – Rs.46,878)	54,062

Question 4

An individual resident in India, having income earned outside India in a country with which no agreement under section 90 exists, asks you to explain whether the credit for the tax paid on the foreign income will be allowed against his income-tax liability in India.

Answer

The assessee is a resident in India and accordingly, the income accruing or arising to him globally is chargeable to tax in India. However, section 91 specifies that if a person resident in India has paid tax in any country with which no agreement under section 90 exists, then, for the purpose of relief or avoidance of double taxation, **a deduction is allowed from the Indian income-tax payable by him, of a sum calculated on such doubly taxed income at Indian rate of tax or the rate of tax of such foreign country, whichever is lower, or at the Indian rate of tax, if both the rates are equal.** Accordingly, the assessee shall not be given any credit of the tax paid on the income in other country, but shall be allowed a deduction from the Indian income-tax payable by him as per the scheme of section 91.

Question 5

The Income-tax Act, 1961 provides for taxation of a certain income earned by X. The Double Taxation Avoidance Agreement, which applies to X, excludes the income earned by X from the purview of tax. Is X liable to pay tax on the income earned by him? Discuss.

Answer

Section 90(2) makes it clear that where the Central Government has entered into a Double Taxation Avoidance Agreement, then **in respect of an assessee to whom such agreement applies, the provisions of the Act shall apply to the extent they are more beneficial to the assessee.** This means that where tax liability is imposed by the Act, the Double Taxation Avoidance Agreement may be resorted to for reducing or avoiding the tax liability.

The Supreme Court has held, in *CIT v. P.V.A.L. Kulandagan Chettiar (2004) 267 ITR 654*, that in case of any conflict between the provisions of the Double Taxation Avoidance Agreement and the Income-tax Act, 1961, the provisions of the Double Taxation Avoidance Agreement would prevail over those of the Income-tax Act. X is, therefore, not liable to pay tax on the income earned by him.

Question 6

What is the circumstance in which it is not necessary for a non-resident Indian, whose total income is above the taxable limit, to file his return of income under section 139(1)?

Answer

Section 115G of the Income-tax Act, 1961 provides that it is not necessary for a non-resident Indian to furnish a return of income under section 139(1) if his total income only consisted of

investment income or long-term capital gain or both and the tax deductible at source under Chapter XVII-B has been deducted from such income.

Question 7

Arif is a resident of both India and another foreign country in the previous year 2010-11. He owns immovable properties (including residential house) in both the countries. He earned income of Rs. 50 lakhs from rubber estates in the foreign country during the financial year 2010-11. He also sold some property situated in foreign country resulting in short-term capital gain of Rs. 10 lakhs during the year. Arif has no permanent establishment of business in India. However, he has derived rental income of Rs. 6 lakhs from property let out in India and he has a house in Lucknow where he stays during his visit to India.

The Article 4 of the Double Taxation Avoidance Agreement between India and the foreign country where Arif is a resident, provides that “where an individual is a resident of both the Contracting States, then he shall be deemed to be resident of the Contracting State in which he has permanent home available to him. If he has permanent home in both the Contracting States, he shall be deemed to be a resident of the Contracting State with which his personal and economic relations are closer (centre of vital interests)”.

You are required to state with reasons whether the business income of Arif arising in foreign country and the capital gains in respect of sale of the property situated in foreign country can be taxed in India.

Answer

Section 90(1) of the Income-tax Act, 1961 empowers the Central Government to enter into an agreement with the Government of any country outside India for avoidance of double taxation of income under the Indian law and the corresponding law of that country. Section 90(2) provides that where the Central Government has entered into an agreement with the Government of any other country for granting relief of tax or for avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of the Income-tax Act, 1961 shall apply to the extent they are more beneficial to that assessee.

Arif has residential houses both in India and foreign country. Thus, he has a permanent home in both the countries. However, he has no permanent establishment of business in India. The Double Taxation Avoidance Agreement (DTAA) with foreign country provides that where an individual is a resident of both the countries, he shall be deemed to be resident of that country in which he has a permanent home and if he has a permanent home in both the countries, he is deemed to be resident of that country, which is the centre of his vital interests i.e. the country with which he has closer personal and economic relations.

Arif owns rubber estates in a foreign country from which he derives business income. However, Arif has no permanent establishment of his business in India. Therefore his personal and economic relations with foreign country are closer, since foreign country is the place where –

(a) the property is located and

(b) the permanent establishment (PE) has been set-up

Therefore, he shall be deemed to be resident of the foreign country for A.Y. 2011-12.

The fact of the case and issues arising therefrom are similar to that of *CIT vs. P.V.A.L. Kulandagan Chettiar (2004) 137 Taxman 460*, where the Supreme Court held that If an assessee is deemed to be a resident of a contracting State where his personal and economic relations are closer, then in such a case, the fact that he is a resident in India to be taxed in terms of sections 4 and 5 would become irrelevant, since the DTAA prevails over sections 4 and 5.

Therefore, in this case, Arif is not liable to income tax in India for assessment year 2011-12 in respect of business income and capital gains arising in the foreign country.