After studying this chapter, you would be able to -

- **appreciate** the need for double taxation relief.
- **identify** the types of double taxation relief available.
- **Integrate, analyse and apply** the provisions relating to double taxation relief contained in the Income-tax Act, 1961 and Income-tax Rules, 1962 in problem solving and addressing related issues.
- **appreciate** the procedure for claiming deduction where there is no double taxation avoidance agreement between India and the other country where the income has been taxed and **compute** the amount of deduction.
- **appreciate** the concept of Permanent Establishment under double taxation avoidance agreements and its relevance.
3.1 CONCEPT OF DOUBLE TAXATION RELIEF

In the present era of cross-border transactions across the globe, the effect of taxation is one of the important considerations for any trade and investment decision in other countries. One of the most significant results of globalisation is the visible impact of one country’s domestic tax policies on the economy of another country. This has led to the need for continuously assessing the tax regimes of various countries and bringing about necessary reforms.

Where a taxpayer is resident in one country but has a source of income situated in another country it gives rise to possible double taxation. This arises from the two basic rules that enables the country of residence as well as the country where the source of income exists to impose tax namely, (i) the source rule and (ii) the residence rule. The source rule holds that income is to be taxed in the country in which it originates irrespective of whether the income accrues to a resident or a non-resident whereas the residence rule stipulates that the power to tax should rest with the country in which the taxpayer resides. If both rules apply simultaneously to a business entity and it were to suffer tax at both ends, the cost of operating on an international scale would become prohibitive and would deter the process of globalisation. It is from this point of view that Double Taxation Avoidance Agreements (DTAA) become very significant.

DTAAs lay down the rules for taxation of the income by the source country and the residence country. Such rules are laid for various categories of income, for example, interest, dividend, royalties, capital gains, business income etc. Each such category is dealt with by separate article in the DTAA.

Double taxation means taxing the same income twice in the hands of an assessee. In India, a person is taxed on the basis of his residential status. Likewise, it may so happen that he is taxed on this basis or some other basis in another country on the same income. However, it is a universally accepted principle that the same income should not be subjected to tax twice. In order to take care of such situations, the Income-tax Act, 1961 has provided for double taxation relief.

3.2 TYPES OF RELIEF

Relief from double taxation can be provided in mainly two ways:

- Bilateral Relief
- Unilateral Relief

(1) **Bilateral Relief**: Under this method, the Governments 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. India has entered into agreements for relief against or avoidance of double taxation with more than 50 countries which include Sri Lanka, Switzerland, Sweden, Denmark, Japan, Federal Republic of Germany, Greece, etc.

Bilateral Relief may be granted in either one of the following methods:

- **Exemption Method**
  - A particular income is taxed in only one of the two countries.

- **Tax Credit Method**
  - Income is taxable in both countries in accordance with their respective tax laws read with double taxation avoidance agreement.
  - The country of residence of the tax payer, however, allows him 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.

**2) Unilateral Relief:** This method provides for relief of some kind by the home country even where no mutual agreement has been entered into by the two countries.

### 3.3 DOUBLE TAXATION RELIEF PROVISIONS UNDER THE INCOME TAX ACT, 1961

Sections 90 and 91 of the Income-tax Act, 1961 provide for double taxation relief in India.

**1) Agreement with foreign countries or specified territories - Bilateral relief [Section 90]**

(i) Section 90(1) provides that 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 income-tax has been paid both in India and in that country or specified territory; or
(ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory 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; or

Accordingly, the Central Government has notified that where such an agreement provides that any income of a resident of India may be taxed in the other country then, such income shall be included in his total income chargeable to tax in India in accordance with the provisions of the Income-tax Act, 1961, and relief shall be granted in accordance with the method for elimination or avoidance of double taxation provided in such agreement [Notification No. 91/2008, dated 28.8.2008].

(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 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.

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

(ii) Where the Central Government has entered into such an agreement with the Government of any country outside India or specified territory outside India 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 this Act shall apply to the extent they are more beneficial to that assessee.

(iii) However, the provisions of Chapter X-A, General Anti-avoidance rule, shall apply to the assessee even if such provisions are not beneficial to him.

(iv) **Meaning of terms used in any DTAA with a foreign country or specified territory**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Meaning of the term</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Term used in any DTAA with a foreign country or specified territory, and not defined in the agreement or the Act but assigned a meaning in the notification issued by the Central Government in the Official Gazette, which is still in force</td>
<td>The term shall have the meaning assigned in the said notification and the meaning shall be deemed to have effect from the date on which the DTAA came into force.</td>
</tr>
</tbody>
</table>
The DTAAs under section 90 are intended to provide relief to the taxpayer, who is resident of one of the contracting country to the agreement. Such tax payer can claim relief by applying the beneficial provisions of either the treaty or the domestic law. However, in many cases, taxpayers who were not residents of a contracting country also resorted to claiming the benefits under the agreement entered into by the Indian Government with the Government of the other country. In effect, third party residents claimed the unintended treaty benefits.

Therefore, section 90(4) provides that the non-resident to whom the agreement referred to in section 90(1) applies, shall be allowed to claim the relief under such agreement if a Tax Residence Certificate (TRC) obtained by him from the Government of that country or specified territory, is furnished declaring his residence of the country outside India or the specified territory outside India, as the case may be.

Therefore, a certificate issued by the Government of a foreign country would constitute proof of tax residency, without any further conditions regarding furnishing of “prescribed particulars” therein. In addition to such certificate issued by the foreign Government, the assessee would be required to provide such other documents and information, as may be prescribed, for claiming the treaty benefits. [See section 90A(5) for CBDT Notification No. 57/2013 dated 1.8.2013, prescribing documents and information to be furnished by the assessee for claiming treaty benefits]

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.

Circular No. 333 dated April 2, 1982, issued by CBDT provides that a specific provision of the DTAA will prevail over the general provisions of the Income-tax Act, 1961. Therefore, where a DTAA provides for a particular mode of computation of income, this mode will take precedence over the Income-tax Act, 1961. However, where there is no specific provision in the treaty, then the Income-tax Act will apply.
Tax treaties are generally based on certain models. The most common ones are:

These models will be discussed in detail in Chapter 6 “Overview of Model Tax Conventions” in Module 2.

Illustration 1

Examine the correctness or otherwise of the following statement with reference to the provisions of Income-tax Act, 1961.

The double taxation avoidance treaties entered into by the Government of India override the domestic law.

Solution

The statement is correct.

Section 90(2) provides that where a double taxation avoidance treaty is entered into by the Government, the provisions of the Income-tax Act, 1961 would apply to the extent they are more beneficial to the assessee.

In case of any conflict between the provisions of the double taxation avoidance agreement and the Income-tax Act, 1961, the provisions of the DTAA would prevail over the Act in view of the provisions of section 90(2), to the extent they are more beneficial to the assessee [CIT v. P.V.A.L. Kulandagan Chettiar (2004) 267 ITR 654 (SC)].

Illustration 2

Cosmos Limited, a company incorporated in Mauritius, has a branch office in Hyderabad opened in April, 2017. The Indian branch has filed return of income for assessment year 2018-19 disclosing income of ₹50 lacs. It paid tax at the rate applicable to domestic company i.e. 30% plus education cess on the basis of paragraph 2 of Article 24 (Non-Discrimination) of the Double Taxation Avoidance Agreement between India and Mauritius, which reads as follows:

"The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in the same circumstances."
However, the Assessing Officer computed tax on the Indian branch at the rate applicable to a foreign company i.e. 40% plus education cess.

*Is the action of the Assessing Officer in accordance with law?*

**Solution**

Under section 90(2), where the Central Government has entered into an agreement for avoidance of double taxation with the Government of any country outside India or specified territory outside India, as the case may be, 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 the assessee. Thus, in view of paragraph 2 of the Article 24 (Non-discrimination of the Double Taxation Avoidance Agreement (DTAA), it appears that the Indian branch of Cosmos Limited, incorporated in Mauritius, is liable to tax in India at the rate applicable to domestic company (30%), which is lower than the rate of tax applicable to a foreign company (40%).

However, Explanation 1 to section 90 clarifies 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. Therefore, in view of this Explanation, the action of the Assessing Officer in levying tax@40% on the Indian branch of Cosmos Ltd. is in accordance with law.

**Illustration 3**

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

**Solution**

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.

**Illustration 4**

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

Section 90(2) makes it clear that where the Central Government has entered into a Double Taxation Avoidance Agreement with a country outside India, 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.

However, as per section 90(4), the assessee, in order to claim relief under the agreement, has to obtain a certificate [Tax Residence Certificate (TRC)] from the Government of that country, declaring the residence of the country outside India. Further, he also has to provide the following information in Form No. 10F:

(i) Status (individual, company, firm etc.) of the assessee;
(ii) PAN of the assessee, if allotted;
(iii) Nationality (in case of an individual) or country or specified territory of incorporation or registration (in case of others);
(iv) Assessee’s tax identification number in the country or specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which the assessee claims to be a resident;
(v) Period for which the residential status, as mentioned in the certificate referred to in section 90(4) or section 90A(4), is applicable; and
(vi) Address of the assessee in the country or specified territory outside India, during the period for which the certificate, as mentioned in (v) above, is applicable.

However, the assessee may not be required to provide the information or any part thereof, if the information or the part thereof, as the case may be, is already contained in the TRC referred to in section 90(4) or section 90A(4).

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, 1961. Mr. X is, therefore, not liable to pay tax on the income earned by him provided he submits the Tax Residence Certificate obtained from the government of the other country, and provides such other documents and information as may be prescribed.

Illustration 5

Arif is a resident of both India and another foreign country in the previous year 2017-18. He owns immovable properties (including residential house) in both the countries. He earned
income of ₹ 50 lacs from rubber estates in the foreign country during the financial year 2017-18. He also sold some house property situated in foreign country resulting in short-term capital gain of ₹ 10 lacs during the year. Arif has no permanent establishment of business in India. However, he has derived rental income of ₹ 6 lacs from property let out in India and he has a house in Lucknow where he stays during his visit to India.

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 examine 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.

Solution

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 shall be 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. 2018-19.
INTERNATIONAL TAXATION

The fact of the case and issues arising therefrom are similar to that of CIT vs. P.V.A.L. Kulandagan Chettiar (2004) 267 ITR 654, 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.

However, as per section 90(4), in order to claim relief under the agreement, Arif has to obtain a certificate [Tax Residency Certificate (TRC)] declaring his residence of the country outside India from the Government of that country. Further, he also has to provide such other documents and information, as may be prescribed.

Therefore, in this case, Arif is not liable to income tax in India for assessment year 2018-19 in respect of business income and capital gains arising in the foreign country provided he furnishes the Tax Residency Certificate and provides such other documents and information as may be prescribed.

(2) **Double taxation relief to be extended to agreements (between specified associations) adopted by the Central Government [Section 90A]**

(i) Section 90A provides that any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may, by notification in the Official Gazette, make the necessary provisions for adopting and implementing such agreement for -

a) grant of double taxation relief,

b) avoidance of double taxation of income,

c) exchange of information for the prevention of evasion or avoidance of income-tax, or

d) recovery of income-tax.

Section 90A(1) provides that an agreement may be entered into by any specified association in India with any specified association in the specified territory outside India which may be adopted by the Central Government by way of notification in the Official Gazette, for granting relief of tax or, as the case may be, for avoidance of double taxation.

The Central Government has, vide Notification No.90/2008 dated 28.8.2008, notified that where such an agreement provides that any income of a resident of India may be taxed in the other country then, such income shall be included in his total income chargeable to tax in India in accordance with the provisions of the Income-tax Act, 1961, and relief shall be granted in accordance with the method for elimination or avoidance of double taxation provided in such agreement.

(ii) In relation to any assessee to whom the said agreement applies, the provisions of the Income-tax Act, 1961 shall apply to the extent they are more beneficial to that assessee.
(iii) However, the provisions of Chapter X-A, General Anti-avoidance rule, shall apply to the assessee even if such provisions are not beneficial to him.

(iv) **Meaning of terms used in any agreement which any specified association in India may enter into with any specified association in the specified territory outside India for double taxation relief**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Meaning of the term</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Term used in any such agreement, and not defined in the agreement or the Act but assigned a meaning in the notification issued by the Central Government in the Official Gazette, which is still in force</td>
<td>The term shall have the meaning assigned in the said notification and the meaning shall be deemed to have effect from the date on which the agreement came into force.</td>
</tr>
<tr>
<td>(2) Term used in any such agreement, which is defined in the agreement itself</td>
<td>The term shall have the same meaning assigned to it in the said agreement</td>
</tr>
<tr>
<td>(3) Term used in any such agreement, which is not defined in the said agreement, but defined in the Income-tax Act, 1961</td>
<td>The term shall have the meaning assigned to it in the Income-tax Act, 1961 and explanation, if any, given to it by the Central Government</td>
</tr>
</tbody>
</table>

(v) The DTAAs under section 90A are intended to provide relief to the taxpayer, who is resident of one of the contracting country to the agreement. Such taxpayer can claim relief by applying the beneficial provisions of either the treaty or the domestic law. However, in many cases, taxpayers who were not residents of a contracting country also resorted to claiming the benefits under the agreement entered into by the Indian Government with the Government of the other country. In effect, third party residents claimed the unintended treaty benefits.

Therefore, section 90A(4) provides that the non-resident to whom the agreement referred to in section 90A(1) applies, shall be allowed to claim the relief under such agreement if a Tax Residence Certificate (TRC) obtained by him from the Government of that country or specified territory is furnished, declaring his residence of the country outside India or the specified territory outside India, as the case may be.

(vi) Therefore, a certificate issued by the Government of a foreign country would constitute proof of tax residency, without any further conditions regarding furnishing of “prescribed particulars” therein. In addition to such certificate issued by the foreign Government, section 90A(5) requires the assessee to provide such other documents and information, as may be prescribed, for claiming the treaty benefits.
### Documents and information, to be furnished by the assessee for claiming treaty benefits, prescribed by CBDT vide Notification No. 57/2013 dated 01.08.2013:

1. **Status (individual, company, firm etc.) of the assessee;**
2. **Nationality (in case of an individual) or country or specified territory of incorporation or registration (in case of others);**
3. **Assessee's tax identification number in the country or specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which the assessee claims to be a resident;**
4. **Period for which the residential status, as mentioned in the certificate referred to in section 90(4) or section 90A(4), is applicable; and**
5. **Address of the assessee in the country or specified territory outside India, during the period for which the certificate, as mentioned in (iv) above, is applicable.**

However, the assessee may not be required to provide the information or any part thereof, if the information or the part thereof, as the case may be, is already contained in the TRC referred to in section 90(4) or section 90A(4).

The assessee shall keep and maintain such documents as are necessary to substantiate the information provided. An income-tax authority may require the assessee to provide the said documents in relation to a claim by the said assessee of any relief under an agreement referred to in section 90(1) or section 90A(1), as the case may be.

7. **The charge of tax at a higher rate for a company incorporated in the specified territory outside India as compared to a domestic company would not be considered as less favourable charge or levy of tax in respect of such company.**

8. **For the purpose of this section, the ‘specified association’ means any institution, association or body, whether incorporated or not, functioning under any law for the time being in force in India or the laws of the specified territory outside India and which may be notified as such by the Central Government and ‘specified territory’ means any area outside India which may be notified by the Central Government.**

### (3) Countries with which no agreement exists – Unilateral Agreements [Section 91]

In the case of income arising to an assessee in countries with which India does not have any double taxation agreement, relief would be granted under Section 91 provided all the following conditions are fulfilled:

a. **The assessee is a resident in India during the previous year in respect of which the income is taxable.**
(b) The income accrues or arises to him outside India.
(c) The 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.
(e) The assessee has paid tax on the income in the foreign country.
(f) There is no agreement for relief from double taxation between India and the other country where the income has accrued or arisen.

In such a case, the assessee shall be entitled to a deduction from the Indian income-tax payable by him. The deduction would be a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax in the said country, whichever is lower, or at the Indian rate of tax if both the rates are equal.

**Deduction in respect of tax paid on agricultural income in Pakistan [Section 91(2)]**

Where a person who is resident in India in any previous year has any agricultural income in Pakistan in respect of which he has paid the income tax payable in that country, he shall be entitled to a deduction from the Indian income-tax payable by him to the following extent:

(i) of the amount of tax paid in Pakistan on such income which is liable to tax under this Act, also; or
(ii) of a sum calculated on that income at the Indian rate of tax, whichever is less.

**Deduction in respect of a non-resident’s share in the income of a registered firm assessed as resident in India which includes income accruing or arising outside India during the previous year [Section 91(3)]**

Relief to a non-resident assessee in respect of his share in the income of a registered firm assessed as resident in India in any previous year, provided all the following conditions are fulfilled –

(i) The share income from the firm should include income accruing or arising outside India during that previous year;
(ii) Such income should not be deemed to accrue or arise in India;
(iii) The income should accrue or arise in a country with which India has no agreement under section 90 for the relief or avoidance of double taxation;
(iv) The assessee should have paid income-tax in respect of such income according to the law in force in that country.

In such a case, the assessee will be entitled to a deduction from the Indian income-tax payable by him. The deduction will be 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 lower, or at the Indian rate of tax, if both the rates are equal.

Meaning of important terms:

(i) “Indian rate of tax” means the rate determined by dividing the amount of Indian income-tax after deduction of any relief due under the provisions of the Act but before deduction of any double taxation relief due to the assessee.

(ii) “Rate of tax of the said country” means income-tax and super-tax actually paid in that country in accordance with the corresponding laws in force in the said country after deduction of all relief due, but before deduction on account of double taxation relief due in the said country, divided by the whole amount of income assessed in the said country.

(iii) The expression “income-tax” in relation to any country includes any excess profits tax or business profits tax charged on the profits by the Government of any part of that country or a local authority in that country.

Illustration 6

Nandita, an individual resident retired employee of the Prasar Bharati aged 60 years, is a well-known dramatist deriving income of `1,10,000 from theatrical works played abroad. Tax of `11,000 was deducted in the country where the plays were performed. India does not have any Double Tax Avoidance Agreement under section 90 of the Income-tax Act, 1961, with that country. Her income in India amounted to `5,10,000. In view of tax planning, she has deposited `1,50,000 in Public Provident Fund and paid contribution to approved Pension Fund of LIC `32,000. She also contributed `28,000 to Central Government Health Scheme during the previous year and gave payment of medical insurance premium of `26,000 to insure the health of her father, a non-resident aged 84 years, who is not dependent on her. Compute the tax liability of Nandita for the Assessment year 2018-19.

Solution

Computation of tax liability of Nandita for the A.Y. 2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indian Income</td>
<td>5,10,000</td>
</tr>
<tr>
<td>Foreign Income</td>
<td>1,10,000</td>
</tr>
<tr>
<td><strong>Gross Total Income</strong></td>
<td><strong>6,20,000</strong></td>
</tr>
<tr>
<td>Less: Deduction under section 80C</td>
<td></td>
</tr>
<tr>
<td>Deposit in PPF</td>
<td>1,50,000</td>
</tr>
</tbody>
</table>
DOUBLE TAXATION RELIEF

### Under section 80CCC

<table>
<thead>
<tr>
<th>Contribution to approved Pension Fund of LIC</th>
<th>32,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1,82,000</td>
</tr>
</tbody>
</table>

### Under section 80CCE

| The aggregate deduction under section 80C, 80CCC and 80CCD(1) has to be restricted to ₹ 1,50,000 | 1,50,000 |

### Under section 80D

| Contribution to Central Government Health Scheme ₹ 28,000 is also allowable as deduction under section 80D. Since she is a resident senior citizen, the deduction is allowable to a maximum of ₹ 30,000 (See Note 1) | 28,000 |
| Medical insurance premium of ₹ 26,000 paid for father aged 84 years. Since the father is a non-resident in India, he will not be entitled for the higher deduction of ₹ 30,000 eligible for a senior citizen, who is resident in India. Hence, the deduction will be restricted to maximum of ₹ 25,000. | 25,000 |

### Total Income

| 4,17,000 |

### Tax on Total Income

| Income-tax (See Note below) | 5,850 |
| Add : Education cess @2% | 117 |
| Add: SHEC @1% | 58 |

| Average rate of tax in India (i.e. ₹ 6,025/ ₹ 4,17,000 × 100) | 1.445% |
| Average rate of tax in foreign country (i.e. ₹ 11,000/ ₹ 1,10,000 ×100) | 10% |

| Rebate under section 91 on ₹ 1,10,000 @ 1.445% (lower of average Indian-tax rate or average foreign tax rate) | 1,589 |

### Tax payable in India (₹ 6,025 – ₹ 1,589)

| 4,436 |

**Notes:**

1. Section 80D allows a higher deduction of up to ₹ 30,000 in respect of the medical premium.
paid to insure the health of a senior citizen. Therefore, Nandita will be allowed deduction of ₹ 28,000 under section 80D, since she is a resident Indian of the age of 60 years.

2. The basic exemption limit for senior citizens is ₹ 3,00,000 and the age criterion for qualifying as a “senior citizen” for availing the higher basic exemption limit is 60 years. Accordingly, Nandita is eligible for the higher basic exemption limit of ₹ 3,00,000, since she is 60 years old.

3. 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.
(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 this case, since all the above conditions are satisfied, Nandita is eligible for deduction under section 91.

Illustration 7

Mr. Kamesh, an individual resident in India furnishes you the following particulars of income earned in India, Country "X" and Country "Y" for the previous year 2017-18. India has not entered into double taxation avoidance agreement with these two countries.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income from profession carried on in India</td>
<td>7,50,000</td>
</tr>
<tr>
<td>Agricultural income in Country &quot;X&quot; (gross)</td>
<td>50,000</td>
</tr>
<tr>
<td>Dividend received from a company incorporated in Country &quot;Y&quot; (gross)</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Royalty income from a literary book from Country &quot;X&quot; (gross)</td>
<td>6,00,000</td>
</tr>
<tr>
<td>Expenses incurred for earning royalty</td>
<td>50,000</td>
</tr>
<tr>
<td>Business loss in Country &quot;Y&quot; (Proprietary business)</td>
<td>65,000</td>
</tr>
<tr>
<td>Rent from a house situated in Country &quot;Y&quot; (gross)</td>
<td>2,40,000</td>
</tr>
<tr>
<td>Municipal tax in respect of the above house (not allowed as deduction in country “Y”)</td>
<td>10,000</td>
</tr>
</tbody>
</table>

Note: Business loss in Country "Y" not eligible for set off against other incomes as per law of that country.
The rates of tax in Country "X" and Country "Y" are 10% and 25%, respectively.

Compute total income and tax payable by Mr. Kamesh in India for Assessment Year 2018-19.

Solution

**Computation of total income of Mr. Kamesh for A.Y.2018-19**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income from House Property [House situated in country Y]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross Annual Value(^1)</td>
<td>2,40,000</td>
<td></td>
</tr>
<tr>
<td>Less: Municipal taxes (assumed as paid in that country)</td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td>Net Annual Value</td>
<td>2,30,000</td>
<td></td>
</tr>
<tr>
<td>Less: Deduction under section 24 – 30% of NAV</td>
<td>69,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,61,000</td>
<td></td>
</tr>
<tr>
<td><strong>Profits and Gains of Business or Profession</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from profession carried on in India</td>
<td>7,50,000</td>
<td></td>
</tr>
<tr>
<td>Less: Business loss in country Y set-off(^2)</td>
<td></td>
<td>65,000</td>
</tr>
<tr>
<td></td>
<td>6,85,000</td>
<td></td>
</tr>
<tr>
<td><strong>Income from Other Sources</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agricultural income in country X</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Dividend received from a company in country Y</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Royalty income from a literary book from Country X (after deducting expenses of ₹ 50,000)</td>
<td>5,50,000</td>
<td>7,50,000</td>
</tr>
<tr>
<td><strong>Gross Total Income</strong></td>
<td>15,96,000</td>
<td></td>
</tr>
<tr>
<td>Less: Deduction under Chapter VIA (^3)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Under section 80QQB – Royalty income of a resident from literary work</td>
<td></td>
<td>3,00,000</td>
</tr>
<tr>
<td><strong>Total Income</strong></td>
<td></td>
<td>12,96,000</td>
</tr>
</tbody>
</table>

\(^1\) Rental Income has been taken as GAV in the absence of other information relating to fair rent, municipal value etc.

\(^2\) As per section 70(1), inter-source set-off of income is permitted.

\(^3\) It is assumed that the royalty earned outside India has been brought into India in convertible foreign exchange within a period of six months from the end of the previous year.
## Computation of tax liability of Mr. Kamesh for A.Y.2018-19

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax on total income [30% of ₹ 2,96,000 + ₹ 1,12,500]⁴</td>
<td>2,01,300</td>
</tr>
<tr>
<td><strong>Add:</strong> Education cess @2%</td>
<td>4,026</td>
</tr>
<tr>
<td>Secondary and higher education cess @ 1%</td>
<td>2,013</td>
</tr>
<tr>
<td><strong>Less:</strong> Rebate under section 91 (See Working Note below)</td>
<td>69,360</td>
</tr>
<tr>
<td>Tax Payable</td>
<td>1,37,979</td>
</tr>
<tr>
<td>Tax payable (rounded off)</td>
<td>1,37,980</td>
</tr>
</tbody>
</table>

### Working Note: Calculation of Rebate under section 91

<table>
<thead>
<tr>
<th>Particulars</th>
<th>₹</th>
<th>₹</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average rate of tax in India [i.e., ₹ 2,07,339 / ₹ 12,96,000 x 100]</td>
<td>16%</td>
<td></td>
</tr>
<tr>
<td><strong>Average rate of tax in country X</strong></td>
<td>10%</td>
<td></td>
</tr>
<tr>
<td><strong>Doubly taxed income pertaining to country X</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agricultural Income</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Royalty Income [₹ 6,00,000 – ₹ 50,000 (Expenses) – ₹ 3,00,000 (deduction under section 80QQB)]⁵</td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td><strong>Rebate under section 91 on ₹ 3,00,000 @10% [being the lower of average Indian tax rate (16%) and foreign tax rate (10%)]</strong></td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td><strong>Average rate of tax in country Y</strong></td>
<td>25%</td>
<td></td>
</tr>
<tr>
<td><strong>Doubly taxed income pertaining to country Y</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from house property</td>
<td>1,61,000</td>
<td></td>
</tr>
<tr>
<td>Dividend</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>3,11,000</td>
<td></td>
</tr>
</tbody>
</table>

---

⁴ It is assumed that Mr. Kamesh is not a senior citizen or very senior citizen

⁵ Doubly taxed income includes only that part of income which is included in the assessee’s total income. The amount deducted under Chapter VIA is not doubly taxed and hence, no relief is allowable in respect of such amount – CIT v. Dr. R.N. Jhanji (1990) 185 ITR 586 (Raj.).
### 3.4 CONCEPT OF PERMANENT ESTABLISHMENT

In order to determine the taxability of business income of foreign enterprises operating in India, it is important to determine the existence of a Permanent Establishment (‘PE’). Article 5(1) of the DTAA provides that for the purpose of this convention the term ‘Permanent Establishment’ means a fixed place of business through which the business of an enterprise is wholly or partly carried on. The term ‘Enterprise’ has been defined in section 92F(iii) [Read the discussion under section 92A in Chapter 1 Transfer Pricing].

Permanent establishment means a fixed place of business through which the business of an enterprises is wholly or partly carried on. Every DTAA has a specific clause, which will deal with an explanation of permanent establishment for the purpose of such DTAA. Business Income of a non-resident will not be taxed in India, unless such non-resident has a permanent establishment in India.

According to Article 5(2), the term PE includes -

<table>
<thead>
<tr>
<th>Less: Business loss set-off</th>
<th>65,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Rebate under section 91 on ₹ 2,46,000 @16% (being the lower of average Indian tax rate (16%) and foreign tax rate (25%))</td>
<td>39,360</td>
</tr>
<tr>
<td><strong>Total rebate under section 91 (Country X + Country Y)</strong></td>
<td><strong>69,360</strong></td>
</tr>
</tbody>
</table>

**Note:** Mr. Kamesh shall be allowed deduction under section 91, since the following conditions are fulfilled:-

(a) He is a resident in India during the relevant previous year (i.e., P.Y.2017-18).

(b) The income in question accrues or arises to him outside India in foreign countries X and Y during that previous year and such income is not deemed to accrue or arise in India during the previous year.

(c) The income in question has been subjected to income-tax in the foreign countries X and Y in his hands and it is presumed that he has paid tax on such income in those countries.

(d) There is no agreement under section 90 for the relief or avoidance of double taxation between India and Countries X and Y where the income has accrued or arisen.
3.20 INTERNATIONAL TAXATION

Taxability of income of a non-resident: Business connection vis-a-vis permanent establishment

Income of a Non-resident

- Taxability under the Income-tax Act, 1961
  - Governed by Section 9
    - With or without business connection

- Taxability under the DTAA
  - Governed by DTAA
    - Only with permanent establishment

A mine, an oil or gas well, a quarry, or any other place of extraction of natural resources (not exploration)

A place of management

A branch

An office

A warehouse

A sales outlet

A factory

A workshop
3.5 TAXING FOREIGN INCOME

Income earned outside India

Residential Status Test

- Resident
  - Agreement with foreign Country exists
    - Section 90 & Section 90A
      - Taxability Test
        - Non-taxable
        - Taxable
          - DTAA vs. Income-tax Act, 1961, whichever is more beneficial
            - Final Tax payable
  - No agreement with foreign country exists
    - Section 91
      - Compute normal tax on total income
      - Compute the average tax on foreign income
      - From the total tax, reduce rebate under section 91, applying the lower of average Indian tax rate and foreign tax rate, on the doubly taxed income.
      - Final Tax payable
- Non-resident
  - Not taxable

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Illustration 8

The concept of Permanent Establishment is one of the most important concepts in determining the tax implications of cross border transactions. Examine the significance thereof, when such transactions are governed by Double Taxation Avoidance Agreements (DTAA).

Solution

Double Taxation Avoidance Agreements (DTAAs) generally contain an Article providing that business income is taxable in the country of residence, unless the enterprise has a permanent establishment in the country of source, and such income can be attributed to the permanent establishment.

As per section 92F(iii), the term “Permanent Establishment” includes a fixed place of business through which the business of an enterprise is wholly or partly carried on.

As per this definition, to constitute a permanent establishment, there must be a place of business which is fixed and the business of the enterprise must be carried out wholly or partly through this place.

Section 9(1)(i) requires existence of business connection for deeming business income to accrue or arise in India. DTAAs however provide that business income is taxable only if there is a permanent establishment in India.

Therefore, in cases covered by DTAAs, where there is no permanent establishment in India, business income cannot be brought to tax due to existence of business connection as per section 9(1)(i).

However, in cases not covered by DTAAs, business income attributable to business connection is taxable.

3.6 TAXATION OF BUSINESS PROCESS OUTSOURCING UNITS IN INDIA

The provisions containing taxation of IT-enabled business process outsourcing units are not contained in the Income-tax Act, 1961 but are given in Circular No.5/2004 dated 28.9.2004 issued by CBDT. The provisions are briefed hereunder -

(a) A non-resident entity may outsource certain services to a resident Indian entity. If there is no business connection between the two, the resident entity may not be a Permanent Establishment of the non-resident entity, and the resident entity would have to be assessed to income-tax as a separate entity. In such a case, the non-resident entity will not be liable under the Income-tax Act, 1961.

(b) However, it is possible that the non-resident entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the Permanent Establishment of the non-resident entity.

(c) The non-resident entity or the foreign company will be liable to tax in India only if the IT enabled BPO unit in India constitutes its Permanent Establishment.
(d) A non-resident or a foreign company is treated as having a Permanent Establishment in India if the said non-resident or foreign company carries on business in India through a branch, sales office etc. or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts or regularly delivers goods or merchandise or habitually secures orders on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India by the Permanent Establishment becomes taxable in India.

(e) If a foreign enterprise carries on business in another country through a Permanent Establishment situated therein, the profits of the enterprise may be taxed in the other country but only so much of them as is attributable to the Permanent Establishment.

(f) Profits are to be attributed to the Permanent Establishment as if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a Permanent Establishment.

(g) In determining the profits of a Permanent Establishment there shall be allowed as deduction, expenses which are incurred for the purposes of the Permanent Establishment including executive and general administrative expenses so incurred, whether in the State in which the Permanent Establishment is situated or elsewhere.

(h) The expenses that are deductible would have to be determined in accordance with the accepted principles of accountancy and the provisions of the Income-tax Act, 1961.

(i) The profits to be attributed to a Permanent Establishment are those which that Permanent Establishment would have made if, instead of dealing with its Head Office, it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the “arm’s length principle”.

(j) Hence, in determining the profits attributable to an IT-enabled BPO unit constituting a Permanent Establishment, it will be necessary to determine the price of the services rendered by the Permanent Establishment to the Head office or by the Head office to the Permanent Establishment on the basis of “arm’s length principle”.