Salary received by a non-resident in India for services rendered outside India not eligible for exemption under the tax treaty

Background

The tax treaties provide relief from taxation in case the same income is taxable in more than one jurisdiction. Typically, under most treaties, two kinds of benefits are provided in respect of salary income - exclusion benefit [where salary earned by a resident of a country is taxable only in the country of his/her tax residency, unless services are rendered in the other country, in which case salary for such services may be taxable in both countries] and foreign tax credit (FTC) [credit of taxes paid overseas from the tax liability in the home country in order to eliminate double taxation]. The Income-tax Act, 1961 (the Act) permits that the beneficial provisions of the treaties would apply in order to avoid double taxation. Recently, the Chennai Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Swaminathan Ravichandran 1 (the taxpayer) held that a non-resident is not eligible to claim any benefit under the tax treaty.

Facts of the case

• As per Article 15(1) of the India-China tax treaty, a resident of China receiving the salary for services rendered in China was taxable only in China. Accordingly, in his India Tax Return (ITR), the taxpayer had claimed benefit under Article 15(1) of the tax treaty and claimed a refund 2 of Tax Deducted at Source (TDS) by the Indian employer on such salary.

• The Assessing Officer (AO) had inter-alia disallowed the claim of exemption under Article 15(1) of the tax treaty on the following basis:
  ➢ Article 23 of the tax treaty allows only residents to claim relief under the tax treaty
  ➢ As the taxpayer qualified as a non-resident in India, he was not eligible to claim relief under Article 15(1) of the tax treaty.

• On an appeal by the taxpayer, the Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order of the AO in denying an exemption under Article 15(1) of the tax treaty to the taxpayer.

• Aggrieved by the CIT(A)’s order, the taxpayer went on appeal before the Tribunal relying on the following judicial precedents where claim of exemption under the relevant treaty was allowed for non-residents of India in respect of

1 Swaminathan Ravichandran v. ITO (ITA No. 299/Mds/2016)
Taxpayer’s appeal before the Tribunal also includes issues dealing with income from house property. However, this Flash News is prepared only on the issues relevant to a claim of exemption of salary income in India under the India-China tax treaty.

2 On applying beneficial provisions under Section 90 of the Act
3 Bholanath Pal v. ITO (ITA No.10/Bang/2011)
salary received in India for services rendered outside India by virtue of the respective Articles in the treaties which were worded similar to Article 15(1) of the India-China tax treaty:

- Bholanath Pai\(^3\) under Article 15(1) of the treaty between India and Japan.
- Neeraj Badaya\(^4\) under Article 16(1) of the treaty between India and the USA.
- Arjun Bhowmik\(^5\) under Article 16(1) of the treaty between India and Philippines.

**Tribunal’s ruling**

- The Tribunal observed that the judicial precedents relied upon by the taxpayer were not applicable as they were factually different from the case of the taxpayer as the taxpayer was a non-resident in India who qualified as a tax resident of China.
- As the Article 23 of the India-China tax treaty applies only to residents of India, the taxpayer, by virtue of being a non-resident in India, was not eligible to claim exemption under Article 15(1) of the treaty.
- The Chennai Tribunal upheld the order of the CIT(A) and denied an exemption under Article 15(1) of the tax treaty to the taxpayer.

**Our comments**

This decision assumes significance as it has denied an exemption under the tax treaty in respect of salary received in India for services rendered abroad, in spite of judicial precedents in which such benefit was granted under similar fact patterns. It is a well-settled principle that such income is eligible for the benefit of exclusion under the tax treaty. By virtue of denial of the claim, the income earned outside India suffers additional taxation in India despite the benefits provided in the tax treaties to eliminate double taxation.

This decision is divergent to other judicial precedents\(^6\) which have upheld the principle that salary received in India for services rendered outside India are not taxable in India. Considering that Article 15(1) and Article 23 do not have any specific nexus, the applicability of this decision would need to be evaluated.

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\(^4\) Neeraj Badaya v. ADIT (ITA No. 308/JP/2014)
\(^6\) Decisions relied on by the assessee and DIT v. Prahlad Vijendra Rao [2011] 198 Taxman 551 (Kar)
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