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TAX FLASH NEWS

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Salary received by a non-resident in India is taxable in India on receipt basis

Background

The Income-tax Act, 1961 (the Act) brings different classes of income within the ambit of taxation[1] based on the residential status of each taxpayer. Recently, the Kolkata Bench of the Income Tax Appellate Tribunal (the Tribunal) in the case of Tapas Kr. Bandopadhyay[2] (the taxpayer) held that the income received in India by a non-resident taxpayer is taxable in India by virtue of such income received in India.

Facts of the case

- The taxpayer was employed as a marine engineer and had worked in international waters during the relevant FY and received remuneration from two entities.
- The taxpayer's employment contracts with overseas shipping entities were through an Indian agent, and the contracts were executed in India.
- The taxpayer was on international waters rendering services during the course of the voyage and had stayed for less than 182 days in India during the relevant FY. Hence, he qualified as a non-resident in India for the relevant FY.
- Based on his residential status, he claimed the incomes received from both these entities as exempt from tax in India on the basis that such incomes were earned outside India in foreign currency and were merely remitted to his NRE accounts in India on his instructions.
- Based on the passport of the taxpayer and other details submitted by the taxpayer, the Assessing Officer (AO) accepted the residential status of the taxpayer as 'non-resident'. However, the AO sought to tax the incomes claimed exempt by the taxpayer on the ground that the said incomes were received in India and hence, were taxable in India under Section 5(2)(a) of the Act, irrespective of the residential status of the taxpayer. As the taxpayer was not a resident of any other state as already stated by him, tax treaty benefits will not be applicable on his income. The AO further observed that these incomes were credited in to the NRE bank accounts by the employers, and therefore, the taxpayer had control over such amounts for the first time in India and added such sums as incomes taxable in India.
- On an appeal before the Commissioner of Income Tax (Appeals) [CIT(A)], the taxpayer argued as under:
  - He qualified as non-resident, entire services were rendered outside India, and neither of the employers for which services were rendered had a permanent establishment in India.
  - Payment for services rendered outside India was made by the entities in foreign currency which was in turn remitted to the NRE accounts in India.
  - 'Received in India' under the Act[3] should be interpreted as income received in India in Indian currency. Remittance made in foreign currency to NRE account cannot be considered as 'income received in India'.

[1] Section 5 of the Act
[2] Tapas Kr. Bandopadhyay v. DDIT (ITA No. 70/Kol/2016)
[3] Section 5(2)(a) of the Act

- Where a foreign company makes payment to non-residents for services rendered outside India, point of receipt of income by the non-resident taxpayer should be considered as outside India and not in India.

- The CIT(A) was not convinced by the arguments put forth by the taxpayer and therefore, upheld the AO's order, inter alia applying the decision of the Mumbai Tribunal in the case of Captain A L Fernandez[4]. In that case, the Mumbai Tribunal had held that:
  - The salary for services rendered aboard a ship outside the territorial waters of any country would be taxable in India if it were received in India as per Section 5(2)(a) of the Act.
  - When salary income received by the taxpayer has accrued or arisen in India under Section 5(2)(a) of the Act, it is not necessary to examine whether the salary is also deemed to accrue or arise in India by applying Section 9(1) of the Act and the Explanation thereto.
- Aggrieved by the order of the CIT(A), the taxpayer preferred an appeal before the Tribunal inter alia stating that the decision in the case of Captain A L Fernandez does not apply in his case and seeking to rely on other decisions and to delete the addition made by the AO.
- The taxpayer relied on the following judgements:
  - Prahlad Vijendra Rao[5] where the High Court of Karnataka had held that:
    - Salary received by the non-resident marine engineer for services rendered by him on a foreign going Indian ship which mainly remained away from the Indian coast accrued outside India and was not taxable in India.
    - The criteria for applying the definition of Section 5(2)(b) of the Act would be such income which is earned in India for the services rendered in India and not otherwise.
    - Under Section 15 of the Act even on an accrual basis salary income is taxable, i.e., it becomes taxable irrespective of the fact whether it is actually received or not; only when services are rendered in India it becomes taxable by implication. However, if services are rendered outside India such income would not be taxable in India.
    - Income earned by the non-resident taxpayer while working outside India has not accrued in India and is not deemed to accrue in India.
  - Avtar Singh Wadhwan[6] where the High Court of Bombay had held that
    - In the case of a non-resident, if income accrues outside India, the same is not taxable.
    - Under Section 9(1)(ii) of the Act, where the salary is earned in India, it shall be regarded as income arising in India. Explanation to that Section declares that income of the above nature payable for services rendered in India shall be regarded as income earned in India. This Explanation clearly indicates that where the salary is payable for services rendered in India, the same shall be regarded as income earned in India. Therefore, the relevant test to be applied is where the services have been rendered. If the services were rendered in India, then the salary income shall constitute income arising in India.
  - Arvind Singh Chauhan[7] where the Agra Tribunal held that
    - The connotation of income having been received and an amount having been received are qualitatively different. Salary amount was received in India, but the salary income was received outside India.
    - Income cannot be taxed at every point of receipt. Salary had accrued outside India and, by arrangement, was remitted to India. Hence, it will not constitute receipt of a salary in India to trigger taxability under Section 5(2)(a) of the Act.
- The tax department contended that the charging section[8] of the Act does not specify the term 'in India' and does not have a bias based on the residential status of the taxpayer. Further, as per Section 15 of the Act, salary can be due to a taxpayer anywhere in the world and the location where salary is received is of no consequence in respect of taxability in India as in the decision of the Supreme Court of India (the Supreme Court) in the case of L W Russel[9].

[4] Captain A L Fernandez v. ITO [2002] 81 ITR 203 (Mum) (TM)
[5] DIT v. Prahlad Vijendra Rao [2011] 198 taxman 551 (Kar)
[6] CIT v. Avtar Singh Wadhwan [2001] 115 Taxman 536 (Bom)
[7] Arvind Singh Chauhan [2014] 42 Taxman.com 285 (Agra)
[8] Section 4 of the Act
[9] CIT v. L W Russel [1964] 53 ITR 91 (SC)

Tribunal's ruling

- The Tribunal observed that the Supreme Court in the case of L W Russel had determined the term 'due' as qualified by 'whether paid or not' in respect of salary income as connected with the contractual right of the employee to receive his salary and has no relation to location or place of services rendered or where the salary becomes 'due'.
- There was no evidence in the present case to support the submission of the taxpayer that the salary income was received outside India and then brought to India for the sake of convenience. The fact that the employers and not the taxpayer had directly remitted the sum to India shows that the taxpayer had control over the said sum only in India.
- If not taxed in India by virtue of receipt in India, such salary income would not suffer tax anywhere in the world. Accepting the taxpayer's argument would render Section 5(2)(a) of the Act redundant. It is elementary that a statutory provision is to be interpreted to make it workable rather than redundant.
- If income should first accrue or arise in India and then should be received in India, to be included under Section 5(2)(a) of the Act, then there would be no need for having the said Section in the statute.
- The judgements relied upon by the taxpayer were distinguishable on the following basis:
  - The cases of Avtar Singh Wadhwan and Prahlad Vijendra Rao are factually distinguishable, since the question raised was not in relation to Section 5(2)(a) of the Act.
  - The decision in the case of Arvind Singh Chauhan followed the decision in the case of A P Kalyankrihsnan[10] where income had suffered tax outside India and then was received in India for the sake of convenience. In the present case, the income had neither suffered tax nor been received in any other jurisdiction. In the case of Arvind Singh Chauhan, the Agra Tribunal took a view that the taxpayer had a lawful right to receive a salary at the location of the foreign employer and the transfer of money to India was only a matter of convenience. However, as per Section 5(2)(a) of the Act, the relevant criterion is not the right to receive a salary but the receipt of salary income which is in India.
- The decision in the case of Captain A L Fernandez clearly lays down that salary for services rendered aboard a ship outside the territorial waters of any country would be taxable in India if it was received in India as per Section 5(2)(a) of the Act. This decision was not brought to notice to the Agra Tribunal in the case of Arvind Singh Chauhan. Following the decision of the Mumbai Tribunal in the case of Captain A L Fernandez, the salary income received by the non-resident taxpayer in the present case were held as taxable in India by virtue of receipt in India as per Section 5(2)(a) of the Act.

Our comments

This decision upholds the significance of Section 5(2)(a) of the Act on taxability of income in India by virtue of receipt in India. Salary income earned aboard a ship on international waters can otherwise go tax-free if not taxed in the place of receipt of such salary income. This decision hinges on the difference between receipt of funds over which a person has control for the first time and transfer of funds by a person between his own accounts.

[10] CIT v. A P Kalyankrishnan [1992] 195 ITR 534 (Mad)

www.kpmg.com/in

Ahmedabad
Commerce House V, 9th Floor,
902 & 903, Near Vodafone House,
Corporate Road,
Prahlad Nagar,
Ahmedabad – 380 051
Tel: +91 79 4040 2200
Fax: +91 79 4040 2244

Bengaluru
Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala, Bangalore 560 071
Tel: +91 80 3980 6000
Fax: +91 80 3980 6999

Chandigarh
SCO 22-23 (Ist Floor)
Sector 8C, Madhya Marg
Chandigarh 160 009
Tel: +91 172 393 5777/781
Fax: +91 172 393 5780

Chennai
No.10, Mahatma Gandhi Road
Nungambakkam
Chennai 600 034
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

Delhi
Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurgaon, Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

Hyderabad
8-2-618/2
Reliance Humsafar, 4th Floor
Road No.11, Banjara Hills
Hyderabad 500 034
Tel: +91 40 3046 5000
Fax: +91 40 3046 5299

Kochi
Syama Business Center
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682019
Tel: +91 484 302 7000
Fax: +91 484 302 7001

Kolkata
Unit No. 603 – 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata 700 091
Tel: +91 33 44034000
Fax: +91 33 44034199

Mumbai
Lodha Excelus, Apollo Mills
N. M. Joshi Marg
Mahalaxmi, Mumbai 400 011
Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

Noida
6th Floor, Tower A
Advant Navis Business Park
Plot No. 07, Sector 142
Noida Express Way
Noida 201 305
Tel: +91 0120 386 8000
Fax: +91 0120 386 8999

Pune
703, Godrej Castlemaine
Bund Garden
Pune 411 001
Tel: +91 20 3050 4000
Fax: +91 20 3050 4010

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