Black Money Law & Treaty

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Queries:

1. Can one get the Double Tax Avoidance Agreement (DTA) relief under Black Money Law (BML)?

Consider an illustration with several legal issues.

Mr. IR was resident in USA and is citizen of USA. He had investments and earns interest. He has retired and returned to India in the year 2010 so that he is resident but NOR for A.Y. 2011-12 and ROR for 2013-14. He pays full tax on Indian and US income in USA but has not declared US incomes in India.

2. Can he claim to determine residential status under "Tie Breaking Rules – Article 4".

3. Assume that IR has paid US Federal tax @ 40% on his US incomes and US state tax @ 5%. How much credit can he claim in India against his Indian tax liability?

4. Will the answers be different for –

(i) Period prior to 1st July, 2015;
(ii) For VCS; and
(iii) Post VCS where AO is applying BML.

This issue needs to be considered at several stages.

My Submissions:

Note: For the full forms of short forms used in this chapter, please see my chapter on BML analysis.

2. Government View:

Government clearly does not want to give DTA relief where BML is applied. This is apparent from the following provisions/ actions.

2.1 As per the BML Bill presented in the Parliament, **Section 73** made a provision authorising the Government to sign DTA with other countries for avoidance of double taxation. Relevant text is given below:

73(1) *The Central Government may enter into an agreement with the Government of any other country –*

(a) for the ***granting of relief*** *in respect of –*

(i) *income on which tax has been paid both under this Act and under the corresponding law in force in that country; or*
(ii) *tax chargeable under this Act;*

(b) *for the **avoidance of double taxation** of income under this Act and under the corresponding law in force in that country;*

(c) *for **exchange of information** for the prevention of evasion or avoidance of tax on undisclosed foreign income chargeable under this Act or under the corresponding law in force in that country, or investigation of cases of such evasion or avoidance;*

(d) *for **recovery of tax** under this Act and under the corresponding law in force in that country; or*

(e) *for carrying out any other purpose of this Act not expressly covered under clauses (a) to (d) or the corresponding law in force in that country.*

However, when the final law has been passed, original provision has been changed significantly. Section 73 still authorises the GOI to sign agreements with other Governments. However, this authority is only for exchange of information and for recovery of tax. There is no authority to sign an agreement for elimination of double taxation.

2.2 **Section 84** provides a list of provisions under ITA – that will apply to BML. The list includes S.90 (1) (c) & (d) – provisions pertaining to exchange of information and recovery of tax. Clauses (a) & (b) referring to relief from double taxation are specifically excluded. Similar provision is made for S.90 A.

2.3 See FAQ dated 6th July, 2015 – Circular No. 13 of 2015. Question No. 26 is specifically asking whether DTA relief is available or not. GOI's clear answer is that DTA relief will not be available.

Thus Government view is clear. Hence if any person wants to claim the relief, he should be sure of ensuing litigation. With this clarification, let us examine the law further.

3. Voluntary Compliance Scheme:

If an assessee wants to claim DTA relief in the VCS declaration he will have to give full details of his claim of DTA relief. The scheme provides for CIT accepting the declaration and issuing a notice of demand. Quite likely, the CIT will reject the DTA relief claim and ask for full payment of tax. If full tax is not paid, he will not issue Certificate under VCS. Then the relief u/s. 67 won't be available. Assessee's violations will

be on record. GOI can use this form and institute proceedings under BML & FEMA.

Claiming DTA relief under VCS seems to be impractical and unadvisable.

4. BML – Post VCS:

Let us consider a situation where: (i) the assessee has not filed any VCS declaration; or (ii) having filed the declaration; under BML, the AO finds information for some other income. In this situation, possibly, the assessee will use all the arguments available. In such a case, what arguments are possible?

5. BML is part of Taxation:

BML is not an independent law. It doesn't stand on its own. BML is an addition to, an attachment to Income-tax law. This is clear from the following:

BML comes into operation only when – an assessee has/ had income chargeable to tax under the ITA; and that income has remained untaxed. In short, that income and resulting assets are called Black Money.

In absence of Income-tax Act, the whole of BML falls flat.

For ITA to apply, two connecting factors are necessary. Qua the assessee, he should be resident of India. Qua the income, it should be sourced in India. For a resident, global income is taxable. For Indian sourced income; even non-resident is liable to tax in India.

Now consider a non-resident assessee who has foreign sourced income. ITA has no jurisdiction. Hence BML has no applicability.

Consider another person whose gross total global income is less than Rs. 2,00,000. He is not liable to pay any tax. Harshest provision of BML cannot touch such a person.

Obvious conclusion is that BML is an addition to ITA and is part of complete taxation procedure. (The term taxation includes all the processes – compliance by the assessee, representation by the advisor and assessment/ penalty/ prosecution by the department.) Government believes that the provisions of the ITA have failed in bringing back Indian Residents' black money held abroad. Hence they have brought in BML.

What is imposed u/s. 3 and u/s. 60 of BML is Income-tax (on incomes that have escaped tax under ITA) and nothing else. What is

imposed u/s. 41 & u/s. 61 is penalty for non-payment of tax and nothing else.

Conclusion: BML is an intrinsic part of taxation process.

6. Treaty Supersedes Domestic Law:

6.1 Now it is a settled principle that –

Whenever there is a difference between the provisions of the tax law and the DTA; whichever provision is **more beneficial to the assessee** shall apply. The DTA will override the provisions of the domestic tax law.

6.2 However, OECD and UN commentaries on treaties clarify that **"Anti Avoidance Provisions"** in the domestic law will prevail over the treaty. This is a fair provision. One cannot abuse treaties to avoid tax and then claim that the treaty overrides domestic law.

However, is BML an Anti-Avoidance provision?

This is NOT an anti-avoidance provision aimed at curtailing treaty abuse. BML is simply a penalty provision. A law aimed at people who have evaded tax. Tax evaders don't use treaties. They just hide facts. GOI wants to punish them. Fine – But just as penalty provisions (like Sections 147-148 or 271 etc.) cannot override the treaties; BML cannot override treaty.

BML levies two charges: (i) Tax & (ii) Penalty. Credit for foreign taxes paid should be available under Article 23 of the treaty. No credit will be available against penalty.

Further clarifications:

Anti-Avoidance provisions like GAAR – Sections 95 to 102 will prevail over treaty. S.90 (2A) specifically providing for domestic law overriding treaty is valid.

Section 206AA is a procedural and yet anti-avoidance provision. It forces non-resident recipients to obtain PAN. In absence of PAN, higher TDS is provided. But if the recipient files his tax return; he can claim treaty relief and get a refund. Hence this is a valid provision.

BML is a penalty provision, not anti-avoidance provision. Hence it cannot override treaty.

7. It is a settled principle of law that – if the Parliament makes a **specific provision** [as in S.90 (2A)]; that the domestic law will override treaty; then that specific provision is final.

In the present case, Parliament has not made a specific provision for denying foreign tax credit under treaty. It has just omitted to include S.90 (1) (a) & (b) while including other relevant provisions. This is an act of omission and not an act of commission.

8. No need for new treaty:

Treaties signed under ITA – S.90 are applicable to BML also. There is NO NEED to sign separate treaties under BML. See Article 2 (1) of the treaties. It clearly provides that all kinds of taxes "on Income & on Capital" shall be covered by the treaty. Article 2 (4) specifically provides that any similar taxes imposed after the signing of the treaty will also be covered under the treaty. It also provides that the Competent Authorities of both countries shall inform the other country about changes in tax law. It may be noted that there is a direction to the authorities to inform. But the applicability of the treaty to the new tax law is not subject to information. In other words, the treaty clearly applies to BML. This is a clear and conclusive provision. We can say clearly that there was no need for new treaties – and hence BML sections 73 & 84 do not provide for a treaty to eliminate double taxation. BML makes provision for signing new treaties for exchange of information and for recovery of taxes. Clear reason can be that – so far, GOI has used all treaties for elimination of double tax. We have not seen use of treaties for tax recovery. And even exchange of information is a new activity. Ten years back, no one exchanged information. Alternatively we can say that Section 73 of BML is a surplusage.

One can conclude that – BML is covered under the treaties and no new treaties are required. This is evident from Article 2. It is also very practical. It takes a long time to sign one treaty. If GOI were to again sign eighty treaties for BML; it would probably take another ten years. Considering all these issues, the law has rightly avoided signing of new treaties under BML.

9 Multilateral Treaty:

India has signed multilateral tax treaty with other fifty nine countries. This treaty covers all taxes other than customs duty. The treaty covers direct taxes, VAT & GST and even motor car taxes. All taxes are covered – whether imposed by Central or State Government or a Municipality.

Considering all the issues, in my opinion, BML is covered under treaties. Hence foreign tax paid should be available under the treaty – as a credit against Indian tax payable under BML.

This is one of the several controversies built-in under BML.

10. Answers to the Query: Having considered the theory, now we may apply this view to the query.

10.1 As per Government view, the U.S. tax paid will not be available as credit against the Indian tax payable on U.S. income.

10.2 As per my view, the credit should be available.

10.3 Mr. IR is Indian tax resident under the Indian tax law. He is U.S. citizen and hence U.S. tax resident under the U.S. law. This is dual residential status. For breaking the tie, he can apply Article 4 of the India-U.S. DTA for BML and ITA.

It may also be noted that (i) within USA, there are restrictions on availability of DTA to such assessees, (ii) However, under the U.S. domestic law, he will be considered as having "emigrated". Hence he will have a larger basic limit until which his income may not be liable to tax in USA. If his income is below this limit, he may escape the U.S. tax burden on Indian income.

Balance facts will determine his residential status.

10.4 Assume that he is held to be a tax resident in India. Hence India is the Country of Residence (COR) and USA will be the Country of Source (COS). As COS, U.S. can levy only 15% tax on interest income (Article 11 of India-US DTA). However, IR has paid 40%. India will give credit for only 15%. Balance is excess US tax paid by him on U.S. income.

10.5 State tax paid in USA is not available as credit against Indian tax payable on U.S. incomes. There are tribunal decisions ruling that U.S. State tax should be available as credit against Indian tax. I submit to disagree.

10.6 Pre-BML – Mr. IR has become ROR from A.Y. 2013-14. Hence before A.Y. 2013-14, his foreign income was not liable to tax in India. Hence claiming DTA relief is not relevant.

For A.Y. 2013-14 he cannot revise his Indian tax return.

BML cannot operate for period prior to 1st July, 2015. Hence the income of A.Y. 2013-14 cannot be taxed if the income is spent away or otherwise does not exist as on 1st July, 2015. However, if the income exists in the form of an asset (Bank Balance or any other asset); then that amount is liable to tax under BML.

For his entire asset outstanding as on 1st July, 2015 he has to determine the assessment year to which it pertains. Note a controversial issue:

The asset disclosed under VCS pertains to which "Previous Year"?

Proviso to S.3 (1) provides that – the income shall be charged to tax in the previous year in which it comes to the notice of the AO. However, S.60 simply provides that the undisclosed asset shall be chargeable to tax on the date of commencement of BML. Does it mean previous year 2015-16? Or does it mean that on 1st July, 2015 tax is chargeable for income of all the relevant past previous years? Can the assessee claim treaty relief – for taxes paid abroad in the past; against tax payable now? My submission: If the nexus between the income of the past and the income (converted into asset) being taxed now can be established; the tax credit should be available.

It is a common issue in International Taxation – same income may be taxable in two countries in different accounting years. This may be due to different rules of accounting the income; or due to any other reason.

Present asset being taxed under BML is the result of undisclosed income of past several years. Foreign taxes paid on each of those years should be available as credit against income-tax payable under BML.

For Income pertaining to the year 2013-14; he may claim credit for the 15% tax paid in USA.

10.7 For A.Y. 2014-15, he may revise the Indian IT return and claim credit for U.S. taxes.

10.8 For A.Y. 2015-16, he may have yet to file the return. Disclose U.S. income, pay tax in India and claim credit for U.S. tax.

10.9 For A.Y. 2016-17 and onwards, he may disclose his income properly and claim proper tax credit under ITA. Pay limited tax in USA.

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