

SIRC of ICAI Tirupur Branch

Taxation of Expatriates

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Taxation of Expatriates

- ▶ Issues which can be considered for taxation of Expatriates:
 - Residential Status.
 - Taxation of salary, perquisites, amenities, tax equalisations given abroad, etc.
 - FEMA issues.
 - DTA.
 - FBT.

Taxation of Expatriates

- Stock Options.
- TDS by employers.
- Foreign Tax credits.
- PE issues for foreign employers.
- Tax planning areas.
- ▶ Other issues: (Not discussed.)
 - Visa.
 - Registration with Police.

Expatriate

- ▶ The word “expatriate” is not defined under the Tax laws.
- ▶ Usually it refers to an employee working abroad and who comes to work in a country for a short period (say between 6 months and 5 years). They do not intend to become permanent residents.
- ▶ Under Indian context, it includes NRIs.

Residential Status – Income-tax

- ▶ If a person comes to India & stays for less than 60 days, he will be a non-resident.
- ▶ If a person comes to India & stays for more than 60 days but less than 181 days,

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Within 4 preceding previous years, the number of days stay in India is less than 365 days,

he will be a non-resident.

Residential Status – Income-tax

- ▶ For NRI, the test of 365 days in 4 preceding previous years does not apply if he is on a visit to India. [Expln. (b) to S.6(1)]. i.e. He can be in India upto 181 days if he comes on a visit, and still be a non-resident.

However if the NRI has not come for a visit, will he get the benefit of stay upto 181 days and yet be considered as a NR?

Residential Status – NRI – Income-tax

- ▶ NRI is defined u/s. 115C(e):

It means a person who is:

- (i) a non-resident; and
- (ii) an Indian citizen; or

a person of India Origin (PIO).

PIO means a person who himself, or either of his parents, or either of his grandparents, were born in undivided India.

There is no reference to spouse.

Residential Status – Income-tax

- ▶ Not Ordinarily Resident (NOR):

If a person is a non-resident for nine years, he will be considered as NOR for one year.

If a person is a non-resident for 10 years or more, he will be considered as NOR for 2 years.

If he is in India for less than 730 days in 7 preceding years, he will be a NOR. (This can give NOR status benefit for 3 or 4 years.)

- ▶ As an NOR, foreign incomes are tax free.

Residential Status – FEMA

▶ Section 2(v)(B) -

A person is a resident in India if he stays in India:

- for employment in India.
 - for carrying on business.
 - for any purpose which indicates his intention to stay for an uncertain period.
- ▶ An expatriate would be an Indian resident from the day he comes to India.

Residential Status – FEMA

- ▶ A person is Not permanently resident (NPR) in India if he comes for an employment of specific duration (irrespective of the period), or a specific job for assignment not exceeding 3 years.

FEMA issues

- ▶ Employer can remit its contribution towards Provident fund/ superannuation/ pension fund abroad in case of “Expatriate staff” who are NPR. [FEMA Notification 3, Reg. 5]
- ▶ ‘Expatriate staff’ means a person whose provident / superannuation/ pension fund is maintained outside India by his principal employer outside India.

FEMA Issues

- ▶ His foreign assets and foreign incomes can be kept abroad.
- ▶ Normally full salary has to be brought into India.
- ▶ 25% of foreign salary has to be paid by the foreign employer in rupees in India. 75% can be kept abroad.

[This facility is available if he is on deputation to the Indian office or subsidiary -
FEMA Notification 10, Reg. 7(8).]

FEMA Issues

► Remittance abroad:

A foreign citizen (other than a citizen of Nepal or Bhutan or a PIO) who has retired from an employment in India, can remit US\$ 1 mn. per financial year out of retirement proceeds.

Documentary evidence and a certificate from a CA is required for the remittance.

[FEMA Notification 13, Reg. 4(2)(i)]

► NRIs can remit US\$ 1 mn. per year out of Indian assets.

Residential Status – Income-tax Vs. FEMA

- ▶ A person can have different residential status under Income-tax Act & FEMA.

E.g. A person comes to India on 1st Dec.07. Under FEMA, he will be an Indian resident immediately. Under I.T. Act, he will be a non-resident till 31st March, 08.

[An NRI will lose exemption on NRE interest - section 10(15)(ii).]

Residential Status – Income-tax Vs. FEMA

- ▶ Indian Ships – if operating beyond India's territorial waters - will not be considered as “in India”. (Territorial waters mean a distance upto 12 nautical miles from appropriate baseline).

Under FEMA – a ship flying an Indian flag is considered as a floating island. Therefore a person is “in India”. (Paul H. Rodriguez V. Director of Enforcement – 45 Taxmann 94).

Residential Status – Income-tax

- ▶ Day of arrival & departure in India.

Advance Ruling (233 ITR 462) – Both days should be counted as “in India”.

Jaipur Tribunal (No. 1230 dt. 22.8.86) (ITO V/s. Dr. R. K. Sharma) – Only day of departure has to be considered as “in India”.

Dual Residence

- ▶ DTA does not prescribe residential status.
- ▶ Only the Domestic Tax law determines residential status.
- ▶ A person can be a resident of two countries (specially in the year of departure / arrival).
- ▶ If there is no DTA, a person may be taxable in both countries on Global income.

Dual Residence

- ▶ If there is a DTA, the tie-breaking rules have to be applied as per hierarchy of tests below:
 - Permanent Home;
 - Centre of vital interests (Personal & economic relations);
 - Habitual Abode;
 - Nationality;
 - Mutual Agreement Procedure.

Dual Non-Residence

- ▶ Due to different fiscal year endings, a person may be a non-resident of both - the home country & the host country.
- ▶ As a non-resident of both countries, he will not be entitled to DTA relief.
- ▶ Domestic relief also may not apply.

Dual Non-Residence

► Example:

A Singapore expatriate comes to India on 1st January, 2007. He will be a NR of Singapore for 2007.

In India, he will be a non-resident upto 31.3.07.

Salary earned in Singapore for January-March, 2007 – will become taxable in both countries.

He will not get credit any where – leading to double tax.

Taxation of Expatriates

- ▶ Resident & ordinary resident → Global income is taxable.
- ▶ Resident but NOR → Indian income is taxable. Foreign income is not taxable – unless received in India.
- ▶ Non-resident → Same as above.

Taxation of Expatriates

- ▶ Employee employed — S.5 - Income accrues in India.

Employee employed — S.9(1)(ii) - Income is abroad, but renders deemed to accrue in services in India. India

- ▶ Indian salary plus foreign salary is taxable in India.

Taxation of Expatriates

- ▶ Foreign perquisites are also taxable in India.
- ▶ Meaning of employment – Max Mueller Bhavan – 268 ITR 31 (Advance Ruling)
- ▶ Duration of employment is not relevant.
- ▶ Tax on Non-monetary perquisite paid by the employer is exempt from grossing up – section 10(10CC).

RBF Rig Corp. Delhi Tribunal Special Bench (2007) – Tax borne by the employer is exempt from grossing up.

Taxation of Expatriates

- ▶ Income received before joining employment (pre-sign-on incentive); or after leaving employment is considered as “profits in lieu of salary” [S.17(3)(iii) w.e.f. A.Y. 2001-02].
- ▶ Salary for rest period before & after services rendered in India is taxable. [S.9(1)(ii), Expln.].
- ▶ If payment is related to services rendered in India, it is taxable.

DTA

- ▶ Article 15 (UN and OECD model) deals with employment income.
- ▶ Primarily salary is taxable in the Country of Residence (say UK) unless, the employment is exercised in the other country (say India). [Article 15(1)].
- ▶ If the employment is exercised in India, then salary is also taxable in India.

DTA

- ▶ Place where the employee renders services is considered as the place of employment.
- ▶ Time of payment of remuneration is immaterial. If it is related to employment in India, remuneration is taxable in India.

If the other country taxes income on receipt basis, then there can be unrelieved double tax. (e.g. salary under S. 9(1)(ii), 17(3)(iii)).

DTA

- ▶ Article 15 applies only to private sector employees. It does not apply to:
 - Director's fees.
 - Artist's & sportsperson's remuneration.
 - Pension.
 - Salary & pension of Government employees.
 - Payments to students, professors & foreign teachers in some cases.

Short visits

► Exemption for short visits:

Income-tax – S.10(6)(vi) – salary is exempt if:

- Foreign enterprise is not engaged in trade or business in India,
- Employee does not stay for more than 90 days in a previous year in India, and
- Salary is not deductible from the employer's income chargeable under Income-tax Act.

[These are cumulative conditions.]

Short visits

► Exemption for short visits:

DTA - Article 15(2) - Salary is exempt if:

- Employee does not stay in India for more than 183 days in a 12 month period commencing or ending in a fiscal year,
- Remuneration is paid by a non-resident employer, and
- Remuneration is not borne by PE or FB of employer in India.

[These are cumulative conditions.]

Short visits

- ▶ In other words, under a DTA, India can tax the employment income, if any of converse conditions are satisfied. i.e.
 - if number of days of employee in India exceed 183, or
 - if remuneration is paid by an Indian resident, or
 - if remuneration is borne by the employer's PE or FB in India.

Short visits

- ▶ Some DTAs use the words “deductible”.
(Indian DTAs with Australia, Belgium, UK.)
- ▶ What is the meaning of “borne by”?
 - Debiting accounts.
 - Payment by a PE.
 - Deduction from profits for taxation.
 - Attributed to the PE.
- ▶ Living allowance paid by Indian company.

Short visits

- ▶ In case of presumptive tax, can we say that salary is “borne by” the PE?

Lloyd Helicopter – 249 ITR 162

Dhv Consultants – 277 ITR 97

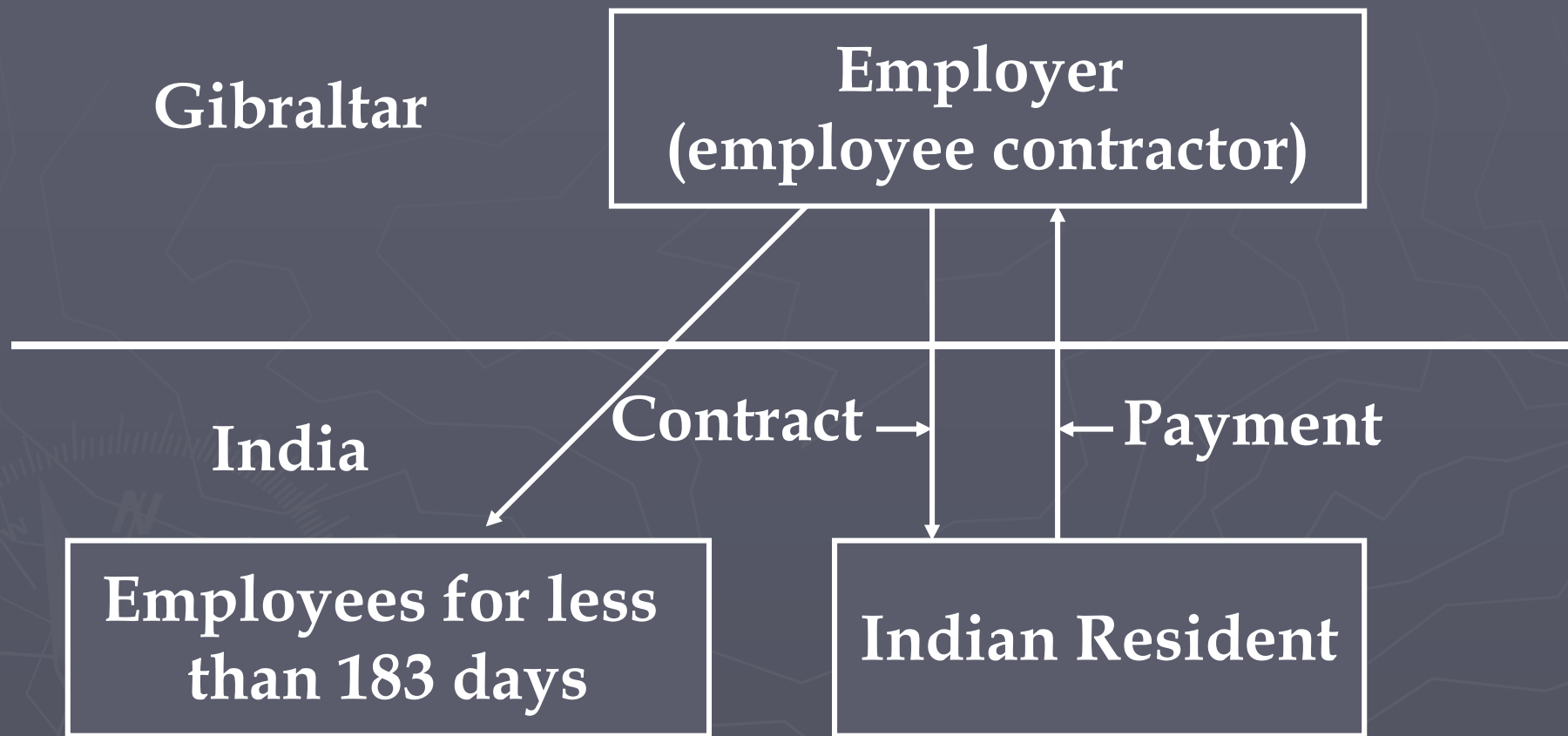
Ensco – 91 ITD 459

- ▶ Reimbursement of costs by PE – Does it mean PE has “borne” the salary?
- ▶ The “base erosion” principle is important. If the PE has claimed salary as a deduction, it should be considered as “borne by”.

Employment on ships

- ▶ If the employee, is employed on a foreign ship, and his stay in India is upto 90 days in a year, salary is not taxable in India [S.10(6)(vii)].
- ▶ Employee on a ship or aircraft operating in international traffic is taxable on his salary where the employer is situated. [Art. 15(3) of a DTA].

International Hiring – Out of labour



Employees work under supervision of Indian client. All conditions of article 15(2) are satisfied.

International Hiring – Out of labour

- ▶ Meaning of employer- One who bears responsibility & risks of employees;

One who directs & supervises the work of employees;

One who enjoys the fruits of employee's work.

- ▶ Substance over form should prevail.
- ▶ Software people working on site – who is the employer?

Expatriates – some issues

- ▶ The employee will not be liable to tax on his foreign incomes, till he is a NOR.
- ▶ What about his other active income?

Examples:

- If he trades in shares over a website?
- His retirement account (e.g. 401-K account in USA) where he has the power to manage the investments? (Advance ruling P-12 – 228 ITR 61)

Is it a source in India (partly or fully)?

Expatriates – some issues

► Wealth-tax:

- Assets as defined u/s. 2(ea) outside India are taxable in case of an ordinary resident.
- S. 6(i) – Assets outside India of foreign citizen and NOR, are exempt from wealth-tax.

Expatriates – some issues

- ▶ Foreign employers may be liable to FBT.
- ▶ Foreign employers will have to comply with TDS provisions.
- ▶ Stock Options.
- ▶ PE exposure for foreign employers.

Residents going abroad

- ▶ **Residential status:**

60 days test applies.

For Indian citizens going for employment abroad, or as members of crew of Indian ships, the person can be in India for upto 181 days and still be an Indian resident. [Expln. (a) to S.6(1)].

Residents going abroad

- ▶ Sometimes initial period of posting abroad may be as a consultant. Benefit of 181 days may not be available.
- ▶ In the first year, he may be an Indian resident. Foreign salary is taxable in India. He will get foreign tax credits.
- ▶ Different fiscal years may cause rectifications.

Residents going abroad

- ▶ Indian employees sent abroad:
 - On payroll of foreign branch or foreign subsidiary,
 - On short visits.

Indian company pays salary in India and abroad in foreign country. Is the Indian salary and foreign salary taxable in India?

British Gas – 287 ITR 462

S Mohan – 294 ITR 177.

Residents going abroad

- ▶ TDS by Indian Co.:
 - Is it creditable abroad?
 - Is it refundable in India?
- ▶ Living allowance for visit abroad.

Fringe Benefit Tax

- ▶ FBT is payable by an employer on any fringe benefit provided to employees. Fringe benefit includes:
 - Actual benefit to employees.
 - Deemed benefit to employees.
- ▶ Circulars clarify the intention of the Government. Some issues in the circulars are not covered under the I.T. Act.

FBT – Cross Border

- ▶ Foreign employers are liable to FBT if they have employees based in India.
- ▶ Indian employers are not liable to FBT if they have employees based outside India.
- ▶ What is the meaning of employees based in India and employees based outside India?

Foreign employers – India employees

- ▶ FBT is payable if employees are based in India.
- ▶ Foreign employer may not have a PE in India, or its income may be exempt from tax under a DTA, still FBT is payable if there are employees based in India.
- ▶ Expenses attributable to operations of the PE are to be considered for charging FBT.
- ▶ Short duration stay in India of employees – FBT is payable if salary is taxable in India.

Foreign employers – India employees

- ▶ If none of the employees are taxable in India, FBT is not payable.
- ▶ Thus, FBT is not payable if:
 - there are no employees based in India, or
 - none of the employees are taxable in India.

Foreign employers – India employees

- ▶ 3 tests for levying FBT:
 - Employees are based in India.
 - Employees' salary is chargeable to tax in India.
 - Expenses are attributable to Indian PE.

Indian employers – Foreign employees

- ▶ FBT is payable on expenses attributable to operations in India.

What is the meaning of Operations in India?

- ▶ If there are separate books of account for Indian & foreign operations, FBT is payable on expenses reflected in Indian books.

Indian employers – Foreign employees

- ▶ If there are no separate books of account, FBT is payable on proportionate amount of Global expenditure.

$$\text{Proportionate Amount} = \frac{\text{No. of Indian Employees}}{\text{No. of Global employees}} \times \text{Global expenditure}$$

FBT credit

- ▶ Will the foreign employee get credit for FBT against his home country tax?
- ▶ Will the foreign employer get credit for FBT against its home country tax?

Stock Options

- ▶ Upto A.Y. 2007-08, employees were chargeable to tax.

From A.Y. 2008-09, employer is liable to FBT.

- ▶ If allotment or transfer of specified security or sweat equity takes place after 1.4.07, employer is liable for FBT.

Stock Options by Foreign Company

- ▶ Shares allotted to Indian subsidiary's employees – FBT payable by Indian company.
- ▶ If during the period between “grant” and “vesting” of option (grant period) the employee was in India, FBT is payable by Indian company.
- ▶ If employee is in India for part of the grant period, value of fringe benefit will be divided proportionately between his presence in India and presence outside India.

Stock Options by Foreign Company

- ▶ Employee of foreign company deputed to India
– FBT is payable based on the proportionate period of grant period – if employee is based in India.

What if salary is not taxable in India?

- ▶ Valuation of shares has to be done by SEBI registered Category-I Merchant Banker.

Stock Option granted by Indian Co.

- ▶ If employees are based abroad, then no FBT is payable.
- ▶ However if the employees are in India during the grant period, FBT will be payable.

Stock Appreciation Rights

- ▶ As per CBDT circular, FBT applies even to “Employee Appreciation Rights”.

TDS

- ▶ Foreign employer is required to deduct tax at source u/s. 192.
- ▶ Excess TDS – refund can be made to the employer – circular 285[F.No. 275/77/79-IT (B) dt. 21.10.80].
- ▶ If tax is to be borne by employer (usually for short visits), refund can be given to employer if authorisation has been given by the employee – circular 707 dt. 11.7.95.

Foreign Tax Credit

- ▶ Indian employees earning foreign salary & paying taxes abroad –
Credit for foreign taxes will be available provided that the salary is taxable in foreign country.
- ▶ Foreign tax be credited against Indian tax on salary only, and not against tax on any other income.

Permanent Establishment

- ▶ Presence of employees in India can amount to a PE.

Profits attributable to the PE can be taxable in India.

- ▶ If there is an office in India from where the employees work, the place could become a PE.
- ▶ If the employees' stay in India exceeds the threshold stated in the DTA, it could become a service PE.

Permanent Establishment

- ▶ Motorola, Ericsson and Nokia – Delhi Tribunal Special Bench (2005).

The manner of operations in India by the employee, gave an impression that there is a PE.

- ▶ UAE Exchange Centre (269 ITR 9) Advance Ruling – The liaison office's activities were substantial activities of the company. Therefore it was held to be a PE.

Questions & Comments are welcome.

Thank You.

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