TECHNICAL GUIDE
ON
EXPATRIATES TAXATION

Committee on International Taxation
The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

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Foreword to the Second Edition

In the era of innovation, the organisations seek and rewards ideas, irrespective of where they originate and reside. Our country is bestowed with a unique wealth of qualified professionals that gets richer every day. The perennial source of human capital of India has to be tapped and converted into value.

With increasing globalization, wide spectrum of opportunities is available for the human capital and the talent plays a bigger role in the different organizations worldwide. The imprint of excellence of Indian professionals is visible in different fields on wide canvas of the globe. Recently, the Indian talent had hit the headlines of the leading dailies stating that '13 Indians now head major global firms.'

I am pleased that Committee on International Taxation of the Institute of Chartered Accountants of India (ICAI) has done a splendid work and has come out with the second edition of "Technical Guide on Expatriates". I express my appreciation to CA. Dhinal A. Shah, Chairman, Committee on International Taxation of ICAI for the initiative taken to revise the publication.

I am sure that the book will be immensely useful to the readers.

Best Wishes

Place: New Delhi | CA. Subodh K. Agrawal

February 7, 2014 | *President, ICAI*

Preface to the Second Edition

Globalizations of economics and the need to develop a global competitive advantage, an increasing number of companies are transferring personnel between countries. India is on a fast track of development and is a highly promising destination for various kinds of skilled workers and executives to work in India. As of now, there is a considerable chunk of foreign origin people who are employed in India and similarly Indian nations are deputed outside India. They broadly belong to two categories - Foreign Expatriates working in foreign companies which have opened operations in India. Foreign Expatriates who are working in Indian Corporates and Indian Companies.

The law both enacted law as well as judge made law had undergone substantial changes. Therefore, urgent need to update the publication was widely felt.

I am happy to state that CA. Sonu Iyer accepted our request to revise the edition. The revised edition would not have seen light of the day without his untiring efforts. I do not think his efforts can be effectively appreciated through the medium of words.

CA. Sonu Iyer has been actively supported by CA. Preeti Sharma. I place on record our sincere appreciation of the contribution made by each of them.

I express my gratitude to CA. Subodh Kumar Agrawal, President and CA. K. Raghu, Vice-President for their motivation and guidance. I thank CA. Sanjiv Kumar Chaudhary Vice-Chairman, CA. Jay Ajit Chhaira, CA. Tarun Jamnadas Ghia, CA. Nihar Niranjan Jambusaria, CA. Sanjeev Maheshwari, CA. Shiwaji Bhikaji Zaware, CA. S. Santhana Krishnan, CA. G. Sekar, CA. J. Venkateswarlu, CA. Manoj Fadnis, CA. Sanjay Agarwal, CA. Naveen N.D. Gupta, CA. Vijay Kumar Gupta, Shri Manoj Kumar, Shri Bhaskar Chatterjee, CA. T.P. Ostwal, CA. Gurunath Kanathur, CA. Mahesh P. Sarda, CA. Vivek Newatia, CA. Kuntal Dave, CA. Rajneesh Agarwal, CA. Sachin Vasudeva and CA. (Dr.) Girish Ahuja who have contributed by giving valuable inputs in revising this technical guide.

I appreciate the efforts made by Mr. Ashish Bhansali, Secretary, Committee on International Taxation for co-ordination and Mr. Govind Agarwal for rendering secretarial assistance.

Place: New Delhi
Date: 05.02.2014

CA. Dhinal A. Shah
Chairman,
Committee on International Taxation,
ICAI

Foreword to the First Edition

The opening up of the Indian economy and its globalization has resulted in far reaching changes. The inflow of funds from foreign institutional investors and non-residents has led to the emergence of taxation of non-residents as an extremely important topic in the current context.

Income from Employment has also been the most significant component of income derived from personal services in international taxation perspective. Working people from one state have been on the move to other states by taking employment always. Such movements have been increase in the recent past due to opening of global economies and increased cross-border trade. Formation of European Union, SAARC and other regional co-operation group are just a few examples. All these activities have encouraged free movement of people both on temporary and permanent basis.

Realizing the importance of the subject, Committee on International Taxation of ICAI and Taxation Committee of WIRC has taken an initiative to come out with a Technical Guide on “Expatriates Taxation” which provides a detailed study on the subject in a simple language.

I record my appreciation for the initiatives taken by CA. Mahesh P. Sarda, Chairman, Committee on International Taxation of ICAI. I congratulate contribution of CA N.C.Hegde for the hard work put in by him for providing the basic draft and in bringing out this Technical Guide. I also appreciate CA Shriniwas Y. Joshi, Chairman WIRC of ICAI for his coordination of the project.

I am sure that this Technical Guide will be of immense use to the readers.

Date 1st July, 2011
New Delhi

CA. G. Ramaswamy
President
ICAI

Preface to the First Edition

The advent of economic reforms in the form of globalization and liberalization in our country has resulted in the rapid growth of the economy in general and cross border transactions in particular. The process of globalization is set to gain further impetus with the good performance of the economy in recent past. There has been manifold increase in the cross border activities of Indian and MNCs business entities in the manufacturing and service sectors. The movement of manpower is an integral part of the entire process and has substantially increased in the recent past. The international taxations aspects related to income sourced from Expatriate Employment requires greater level of understanding.

Looking to the importance of the subject, the Committee on International of ICAI in collaboration with WIRC of ICAI undertook project to come out with a study addressing issues relating to Expatriates Taxation. Accordingly, CA. N. C. Hegde FCA, Mumbai (Regional Council Member of WIRC) was requested to pilot the project. I am extremely thankful to CA. Shriniwas Joshi, Chairman of the Western India Regional Council and CA. N. C. Hegde for their efforts in bringing out this publication. I place my appreciation on record for the valuable contributions made by CA. Alpana Rao, CA. Arvind Rao and CA. Hiten Shah.

I wish to thank Hon'ble CA. G. Ramaswamy, President, ICAI and Hon'ble CA. Jaydeep N. Shah, Vice President, ICAI for their continuous support and encouragement to the initiatives of the Committee.

I am sure that this study will help all the members in better understanding of the issues involved in Expatriates Taxation.

Date 1st July, 2011

CA. Mahesh P. Sarda
New Delhi
Chairman
Committee on International Taxation
ICAI

Preface to the First Edition

The Industrial Policy of 1991 welcomed both foreign investment and allowed hiring of foreign technicians. Since then, we have seen both Indian subsidiaries of foreign companies as well as Indian corporates having a choice in attracting the best talent that is available globally. The hire of expatriates is no longer a phenomenon which is limited to the major metropolitan cities.

The Government has made it extremely easy for Indian corporates to remunerate them as well as enable the expatriates to repatriate their salaries.

However whilst on hand there is greater operational freedom for residents for hire of expatriates as well complete freedom to remunerate them, the tax treatment of salaries has often been a subject matter of concern both to the Indian employer and the expatriate.

Tax treaties that India has entered into have no doubt provided respite but one still is left with a lot of issues which are often unresolved.

It is in this background that the book on "Taxation of Expatriates" gives a detailed study on the said subject. The study provides for an analysis of the law and a lucid and practical discussion on various connected issues. The study has employed simple language that is easy to comprehend.

I wish to thank the Taxation Committee of WIRC and CA N.C.Hegde to take this important project so as to provide all information related to the subject in a concise form.

I would also like to thank my professional colleagues, CA Alpana Rao, CA Arvind Rao and CA Hiten Shah for having spared the time from their busy schedule to bring out this excellent booklet .

I am confident that the book will immensely useful for members in understanding the subject as well as help them in discharging their professional responsibilities especially in regard to the preparation of tax returns.

CA Shriniwas Y. Joshi
Chairman, WIRC

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Introduction

The term 'Expatriate' is derived from Latin (ex-patria) which means "out of the country". The Oxford Dictionary defines an expatriate as a 'person living abroad'. Similarly the Webster Dictionary defines the term as 'a person residing in a foreign country'. Technically an expatriate is a person temporarily or permanently residing in a country and culture other than that of his/her upbringing or legal residence[1]. The term 'expatriate' in some countries also has a legal context used for tax purposes

The Income-tax Act, 1961 ('ITA') does not define the term 'Expatriate'. But as pointed out above it essentially refers to an employee who is working abroad on deputation or secondment. In terms of the Oxford Dictionary, deputation means 'to appoint someone to perform a task for which one is responsible'. Secondment is defined in the Oxford Dictionary as 'to temporarily transfer a worker to another position'.

The concept of 'deputation' is well understood in service law and has a recognized meaning, as observed by the *Apex Court in State of Punjab and others vs. Inder Singh and Others,* (1997 8 Supreme Court Cases 372). The Apex Court pointed out that:

"'Deputation' has a different connotation in service law and the dictionary meaning of the word deputation is of no help. In simple words "deputation" means service outside the cadre or outside the parent department. Deputation is deputing or transferring an employee to a post outside his cadre, that is to say, to another department on a temporary basis. After the expiry (of) period of deputation the employee has to come back to his parent department to occupy the same position unless in the meanwhile he has earned promotion in his parent department as per the recruitment rules. Whether the transfer is outside the normal field of deployment or not is decided by the authority who controls the service or post from which the employee is transferred. There can be no deputation without the consent of the person so deputed and he would, therefore, know his rights and privileges in the deputation post."

For the purpose of easy understanding, it can be said that an expatriate is a resident of a foreign country working in another country. It presupposes

[1] Wikipedia

reference to a person who, for tax treaty purposes, continues to be a resident in his/her home country.

Thus, in the Indian context expatriate means a resident of foreign country working in India (inbound) or an Indian resident working abroad (outbound)

Depending upon the entry strategy adopted by the foreign employer and work requirements, an inbound expatriate can work in India under any of the below structures:

- Business visit
- Short term assignment
- Medium to Long term assignment
- Permanent relocator
- Consultant

The broad issues involved in a typical assignment structure which an employer and an expatriate need to be aware of are provided below:

(a) Immigration: The expatriate should travel on correct visa type (business visa /employment visa- depending upon the purpose of visit) and should get himself/herself registered with Foreign Regional Registration Office (FRRO) in India within 14 days of arrival in India, if required under his/her visa type.

(b) Taxability of the employee: Salary received by employee for rendering services in India would be liable to tax in India as employment income irrespective of its place of receipt, as the source of the same lies in India. Hence, any salary/ allowance/ benefit paid to an employee outside India which is related to assignment period in India will be subject to tax in India. Employer is required to comply with withholding tax obligation on such payments. The maximum marginal tax rate for the financial year 2013-14 is 33.99%.

A short stay exemption may be claimed for the business travelers subject to satisfaction of conditions provided in the applicable tax treaty.

(c) Social security: Social security in India is governed by Provident Fund Regulation. A foreign passport holder, working for a 'covered establishment' in India and coming from a country with which India has not entered into a Social Security Agreement, is mandatorily required to contribute under Provident Fund Regulation. The employer is required to contribute 24% of "salary" prescribed for provident fund contribution. The employer has a right to recover 12% of such contribution from the employee's salary. There are certain restrictions on withdrawal of contribution for international workers.

(d) Payment of salary outside India: Under the exchange control regulations of India, it is permissible for the employees of a foreign entity seconded to branch, office, joint venture or subsidiary of such foreign entity in India, to receive their entire salary in a bank outside India provided the income tax as per the domestic tax laws of India has been duly paid on the entire salary as accrued in India.

(e) Other issues: The presence of employees of a foreign entity in India may create a permanent establishment exposure for the foreign entity. The arrangement between the foreign entity and the Indian entity to second the employees of the foreign entity to work for the Indian entity needs to be evaluated from service tax perspective. The secondment transaction between related parties would be subject to transfer pricing regulation and hence any cost sharing arrangement should satisfy arm's length principle. Any taxable payment from Indian entity to a non-resident would be subject to withholding tax provisions.

The typical characteristics of various deployment structures and tax implications for the expatriates are indicated below.

Type / Nature of Assignments	Typical Characteristics	India Tax implications
Business visits	• Employee visiting India for short business visits of 20-30 days spread over the financial year • Purely for the limited purpose of attending meetings/ conferences in the capacity of employee of foreign entity	• Employee may be eligible to claim short stay exemption under the ITA or applicable tax treaty subject to satisfaction of given conditions and thus not required to pay taxes in India • A short business visit of 20-30 days may not create tax implications for foreign entity. However, if the transaction is between related parties, it is advisable to evaluate permanent establishment risk for

Type / Nature of Assignments	Typical Characteristics	India Tax implications
		foreign entity
Short-term Assignments	• Employee would be sent to India for short periods of 6-8 months • He/ she would be working in India but as an employee of the foreign entity & would continue to be on its payroll • Normally Indian entity would compensate the foreign counterpart for the services rendered by the expatriate • Generally, such arrangement is made for performing training or supervisory functions	• Employee would be taxable on the salary income earned for services rendered in India. • There could be Permanent Establishment exposure for the foreign entity because of presence of the expatriate employees of foreign entity in India on behalf of foreign entity. • Foreign entity would have to comply with the withholding tax obligation in relation to salary paid to its employees for services rendered in India.
Medium-term & Long-term assignments — Secondment	• Employee would be deputed to India for rendering services to the Indian entity for a period of 2 – 3 years or more • He/ she would be working in India in the capacity of Employee of Indian entity. • He/ she would be on the payroll of Indian entity and the remuneration would be solely borne by the	• Employee would be taxable on the salary income earned for services rendered in India • Indian entity will have to comply with all the regular legal formalities in respect of the employee • The foreign entity may not have any Permanent Establish-ment exposure in India subject to appropriate

Type / Nature of Assignments	Typical Characteristics	India Tax implications
	Indian entity	documentary evidence to substantiate expatriate employees working under the control and supervision of the Indian entity
Permanent Relocation	• Employee will resign from home country entity and join the Indian entity as a local hire.	• Employee would be taxable on the salary income earned for services rendered in India. • Indian entity will have to comply with all regular formalities, just as for local Indian employee • There is no permanent establishment exposure for home country entity

Sometimes, a company may choose to hire independent foreign consultants. The taxability of independent expatriate consultants differs from that of expatriate employees.

Similarly, in case of outbound expatriates the assignment could be in the nature of business visits, short-term, medium-term or long-term assignments.

Type / Nature of Assignments	Typical Characteristics	India Tax implications
Business visits	• Employee visiting foreign country for short business visits of 20-30 days spread over the year • Purely for the limited purpose of attending meetings/conferences in the capacity of	• Employee would remain a resident in India (subject to his physical presence in India) and hence salary in respect of period of foreign visits would continue to be taxable in India

	employee of the Indian entity	
Short-term assignments	• Employee would be sent out of India for short periods of 6–8 months • He/ she would be working outside India but as an employee of the Indian entity & would continue to be on its payroll • Foreign entity may compensate the Indian entity for the services rendered by the expatriate • Generally, such arrangement is made for performing training or supervisory functions	• There could be Permanent Establi-shment exposure for the Indian entityin the foreign country if salary is received in India, the same may be taxable on receipt basis under ITA. • In case the outbound expatriate qualifies as a non-resident in India, possibility of claiming income exemption under applicable tax treaty may be explored • In case the employee continues to be resident in India, short stay exemption may be claimed in the host country. In case the employee is not eligible for short stay exemption in host country, the double taxation can be eliminated by claiming credit of host country taxes in India
Medium-term & Long-term assignments- Secondment	• Employee would be deputed to the foreign entity for rendering services for a period of 2-3 years or more • He/ she would be working abroad in the capacity of employee of the foreign entity • He/ she would be on the	• In case the outbound expatriate qualifies as a non-resident in India, he/she would not be liable to pay tax on salary income received outside India for the period of services rendered outside India • In case the

	payroll of foreign entity and the remuneration would be solely borne by such foreign entity	employee continues to be resident in India, he/she would be liable to pay tax on his/her global income in India. However, at the same time, he/she would be eligible to claim credit of taxes paid in the host country on the salary income related to period of services rendered outside India
Permanent Relocation	• Employee would be deputed to overseas entity on a permanent basis • He / she would no longer be a part of Indian entity • The social ties with India would be detached	• In case the outbound expatriate qualifies as a non-resident in India, he/she would not be liable to pay tax on salary income received outside India for the period of services rendered outside India • In case the employee continues to be resident in India, he/she would be liable to pay tax on his/her global income in India. However, at the same time, he/she would be eligible to claim credit of taxes paid in the host country on the salary income related to period of services rendered outside India

Taxation

I. Basic concepts — Domestic Law

Under the ITA, incidence of tax depends on the residential status of the tax payer as well as on the place and time of accrual or receipt of any income. Each of these components is discussed in the following paragraphs.

Residential status

In India charge of income-tax is not based on domicile or citizenship. The extent of Indian tax liability depends on the residential status of an individual based on the individual's physical stay in India.

Residential status is determined on the basis of the physical presence in India during each previous year i.e. the financial year commencing from 1st April.

For tax purposes, an individual may be Resident and Ordinarily Resident ('ROR'), Resident but Not Ordinarily Resident ('RBNOR') or Non-Resident ('NR'). The conditions to be satisfied to qualify in any of these categories are discussed below:

i. Basic residency test

An individual is regarded as a resident in India in any previous year, if he/she is present in India for:

– 182 days or more during that year; or

– 60 days* or more during that year and 365 days or more during the 4 preceding tax years.

*To be replaced by 182 days in following two cases:

– an Indian citizen who leaves India for the purpose of employment abroad or as a crew member of an Indian ship; or

– an Indian citizen or Person of Indian Origin[2] employed abroad who comes to India on a visit.

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[2] A person shall be deemed to be of Indian origin if he, or either of his parents or any of his grand-parents, was born in undivided India – Explanation to section 115C(e) of ITA.

ii. Non resident

An individual fulfilling neither of the above basic residency test is regarded as a non-resident in India.

iii. Resident but Not Ordinarily Resident and Resident and Ordinarily Resident

A person resident in India may be further classified as ROR or RBNOR based on the below mentioned criteria.

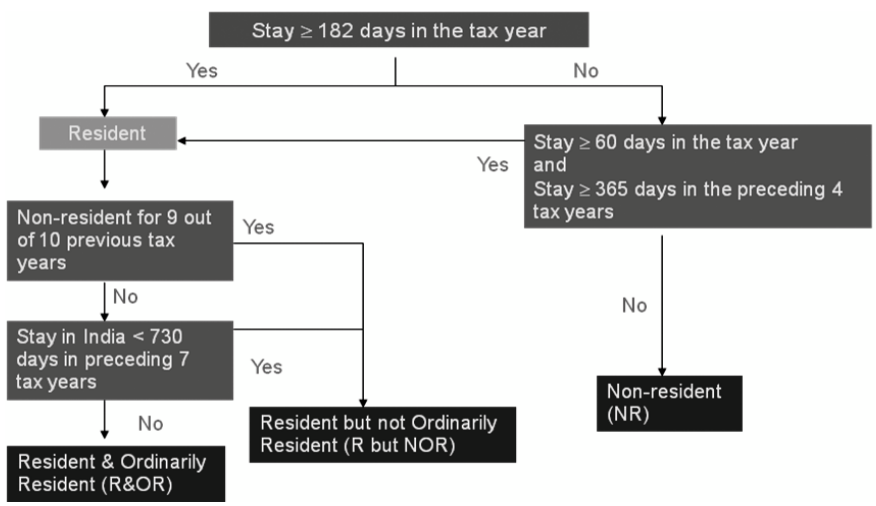
A resident individual (i.e., satisfying the basic residency test specified in clause (i)) would be regarded as a ROR in India in any financial year if **both** the following conditions are satisfied:

– He/ she has been resident in India for at least 2 out of 10 preceding financial years; and

– He/ she has been present in India for a period or periods aggregating to 730 days or more, during the 7 preceding financial years.

A resident individual who does not satisfy any one or both of these additional conditions would be regarded as RBNOR.

The above residency rules are summarized in the below matrix:



The actual number of days an individual is present in India is generally determined on the basis of entries in the passport, taking into account the day of entry as well as the day of exit[3]. Further, stay in the territorial waters of India would also constitute presence in India for the purpose of determining the residential status.

Illustration 1

Mr. ABC, a Canadian citizen, arrives in India for the first time on October 02, 2013. Details of his entry and exit from India as per his passport and his residential status would be as follows:

Year Number	Previous Year	Days present in India	Cumulative stay in preceding previous year	Residential status
1	2013-14	181	0	NR
2	2014-15	366	181	RBNOR
3	2015-16	365	547	RBNOR
4	2016-17	365	912	ROR

Normally, an inbound expatriate coming to India for the first time will become ROR in the third/fourth year from the year of arrival.

Illustration 2

Mr. XYZ, an Indian citizen, who is appointed as a Senior Manager by an Australian company, leaves India for the first time on September 10, 2012. Details of his India visits in the subsequent years and his residential status would be as follows:

Year Number	Previous Year	Days present in India	Cumulative stay in preceding previous year	Residential status
1	2012-13	163	>365	NR
2	2013-14	75	>365	NR
3	2014-15	185	>365	ROR

Normally an outbound expatriate would remain NR in all the years of assignment (except year of return) when the total stay in India is less than 182 days.

[3] P. No. 7 of 1995 – 223 ITR 462 (AAR)

Scope of income

While residents (i.e., tax payers whose residential status is ROR) are taxed on their worldwide income, non-residents are taxed only on income that is received or deemed to be received in India or income that accrues/arises or is deemed to accrue/arise in India. For this purpose a RBNOR is taxed like a NR with the only difference that he/she is also liable to tax on income accruing abroad if it is from a business controlled in or a profession set up in India.

The above rules can be broadly depicted as follows:

Nature of income	Taxability in case of		
	ROR	RBNOR	NR
Income received or deemed to be received in India	√	√	√
Income accruing or deemed to be accrued in India	√	√	√
Income from a business controlled from India or from a profession set up in India but not received or accrued in India	√	√	X
Income not received or not deemed to be received in India	√	X	X
Income not accruing or not deemed to be accrued in India	√	X	X

Thus, depending upon its nature, income is taxed in India either on receipt or on accrual basis. Income is said to be received when it actually reaches the tax payer; however, it is said to accrue or arise when the right to receive such income becomes vested to the tax payer.

It may be noted that any income which is taxed on accrual basis cannot again be taxed on receipt of the same. Further, once an amount is received as income, any remittance of such amount to another place does not result in receipt at another place – for instance if a ROR tax payer is receiving income abroad in financial year 2013-14, he cannot be said to have received the same when he brings or remits such income to India in financial year 2014-15.

General scheme of taxation

Under the ITA, income is classified and accordingly taxable under any of the following heads:

- Income from Salaries

  The income arising on account of employee-employer relationship is taxable under this head and inter alia includes salary, allowances, perquisites, provident fund contributions, income received from previous employers, retirement benefits, salary arrears, etc.

- Income from House Property

  Under this head of income there is a charge on the potential of property (i.e., land and/ or building, commercial as well as residential) to generate income not merely on the actual rent received there from. Specific rules are laid down for computing the taxable value of a property for taxation purpose.

- Profits and gains from Business or Profession

  Income earned by a tax payer on exercise of a business or profession is taxable under this head. Generally, business/ profession income is arrived at after deducting from the gross sale/billing all the expenses incidental to such business/ profession, including depreciation. Weighted deduction is available in case of certain specified expenses such as research & development whereas certain expenses are deductible on fulfilment of prescribed conditions (for instance only on actual payment or on compliance with withholding tax procedures).

- Capital Gains

  Capital Gain represents the profit or gain arising to a tax payer on transfer of a capital asset during a year. Generally capital gains are calculated by deducting from the net sale consideration the cost of acquisition and cost of improvement incurred by the transferor on the capital asset. In case of long-term capital assets i.e. those held for a period of more than 36 months (12 months in case of shares of a company/ listed securities in recognized stock exchanges in India), in order to give effect to inflation the cost of acquisition and improvement are indexed using the cost inflation index numbers notified by the Government; however indexation benefit is not available for bonds and debentures.

Long term capital gains are exempt from tax in certain cases if the gains are reinvested within the specified period. For example, capital gains on transfer of residential house held for more than 36 months are exempt if they are reinvested in acquiring or constructing another residential house within a specified period. Similarly capital gains from the sale of any capital asset held for more than 36 months are exempt if the amount of capital gains is reinvested in certain specified assets, being redeemable bonds issued by the National Highways Authority of India or the Rural Electrification Corporation within six months and for a lock-in period of three years.

- Income from other sources

  This is the residual head of income and any income which is not covered under the earlier heads is covered in 'income from other sources' for instance interest, gifts, dividends, lottery winnings, etc.

The computation mechanism for income under each of the above mentioned head is distinct and the total income under all the heads, after setting off brought forward losses, if any, constitutes the Gross Total Income ('GTI') for a particular financial year. From the GTI a tax-payer/ assessee is entitled to claim certain deductions[4] in respect of specific investments and/ or expenses (for instance provident fund investments, insurance premiums, housing loan repayments, etc.) up to the prescribed limits so as to arrive at the Net Taxable Income for the year.

As discussed earlier, expatriate employees are in essence employees working in a country away from their country of legal residence. Thus, for the purpose of easy understanding, normally the income earned by an expatriate working in India would be arising from the employee- employer relationship, irrespective whether he/she is on the payroll of the foreign entity or the Indian entity, and therefore the same would be taxed as their 'Salary income'. The taxability of such salary income and related issues are discussed in the forthcoming topics.

Tax rates

Income tax is payable on the Net Taxable Income at the rates specified for the relevant year. The tax rates for every financial year are proposed and adopted by the Parliament in the Annual Budget. The tax rates for the financial years 2012-13 and 2013-14 are as follows:

[4] Under Chapter VI-A of the ITA

For financial year 2012-13 (assessment year 2013-14)

Income slabs	Tax rates
Taxable income up to ₹ 200,000	Nil
Taxable income between ₹ 200,001 & ₹ 500,000	10%
Taxable income between ₹ 500,001 & ₹ 1,000,000	20% plus ₹ 30,000
Taxable income above ₹ 1,000,000	30% plus ₹ 130,000

The basic exemption limit of ₹ 200,000 is increased to ₹ 250,000 in case of resident tax payers who are 60 years of age or more but less than 80 years of age and ₹ 500,000 in case of resident tax payers who are of the age of 80 years or more.

For financial year 2013-14 (assessment year 2014-15)

Income slabs	Tax rates
Taxable income up to ₹ 200,000	Nil
Taxable income between ₹ 200,001 & ₹ 500,000	10%
Taxable income between ₹ 500,001 & ₹ 1,000,000	20% plus ₹ 30,000
Taxable income above ₹ 1,000,000	30% plus ₹ 130,000

The basic exemption limit has been increased to ₹ 250,000 in case of resident tax payers who are of the age of 60 years or more but less than 80 years and to ₹ 500,000 in case of resident tax payers who are of the age of 80 years or more.

A rebate of up to `2,000 is available to resident individuals whose total income does not exceed `500,000.

A surcharge is applicable to individuals with taxable income exceeding ₹ 10,000,000 equal to 10% of tax payable. Further, marginal relief is allowed to ensure that the additional amount of income-tax payable including surcharge, on the excess of income over ₹ 10,000,000 is limited to the amount by which the income is more than `10,000,000.

The above tax rates are required to be increased by an additional education cess of 3% in all cases.

II. Basic concepts — Tax Treaties

In case resident of one country (home/ residence country) derives income from another country (host/source country) there arises a possibility of 'double taxation' of the same income in the source country and subsequently in the residence country. Such double taxation can also arise due to difference in the definition of tax residency and in the scope of taxation of various countries.

Thus, with respect to an expatriate, double taxation may arise on account of the following reasons:

- He/she is a resident of two countries and each state seeks to tax the individual on worldwide income;
- He/she is a resident of one country deriving income from another country.

In order to prevent such double taxation, governments engage in efforts to avoid double taxation by entering into Double Taxation Avoidance Agreements/ Tax Treaty ('DTAA'). The adoption of a DTAA requires modification to the internal tax laws of the respective state and as such, an enabling Act of Parliament.

Under Section 90 of the ITA, the Central Government of India is empowered to enter into an agreement with any country for granting relief from double taxation, exchange of information, recovery of tax and to make such provisions as may be necessary for implementing the agreement. In India, a DTAA becomes a law without any further legislation having to be enacted[5].

DTAA divide the taxing rights between the countries that are party to the agreement. India has entered into two types of DTAA with other countries:

- Comprehensive DTAA, which covers all income flows; and
- Limited DTAA that covers only shipping and/ or air transport income.

India has concluded comprehensive DTAA with almost 90 countries including major countries like Australia, Belgium, Brazil, Canada, China, Germany, Italy, Japan, Mauritius, New Zealand, Singapore, United Kingdom, United States, etc.

India has also entered into 'Tax Information Exchange Agreements' with few countries namely Bermuda, Bahamas, Isle of Man, British Virgin Islands, Cayman Island, Jersey, Guernsey, Liberia, Macao and Gibraltar.

Section 90 further provides that where the provisions of the DTAA entered into by India with another country are more beneficial to any assessee, the assessee would be governed by such beneficial provisions of the DTAA. This position has been upheld by the Apex Court in the case of UOI vs. Azadi

[5] Supreme Court in Maganbhai vs. Union of India 1969 AIR 783.

Bachao Andolan (263 ITR 706). Hence, in the case of an expatriate the provisions of the treaty need to be examined for the purpose of ascertaining the tax liability.

Residential status under DTAA

Generally, Article 4(1) of a DTAA, defines the term 'resident' of a country to mean any person who, under the laws of that country, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and also includes that State and any political sub-division or local authority thereof. Thus, in order to qualify as a resident under a DTAA entered into by India, an expatriate should be a resident either in the overseas country or in India under the domestic laws. It may be noted that the residential status of the employer is not relevant in determining the status of the expatriate.

However, if by virtue of the above provision, an individual is a resident of both the contracting countries, the distributive rules cannot apply. Therefore, for such cases, clause 2 of the residency article provides the tie breaker test for determining which of the two contracting countries the person would be deemed to be a resident as per the DTAA. The relevant factors to be considered in the tie-breaker test are as follows:

- Permanent home: The country in which he/she has a permanent home available to him/her;
- Centre of vital interest: The country with which his/her personal and economic relations are closer;
- Habitual abode: The country in which he/she has habitual abode;
- Nationality: Country of which he/ she is a national;
- Competent authorities: As determined by mutual agreement between both the countries competent authorities.

III. Taxation of salary

Any salary due or received from the employer or the former employer is charged to tax in India as 'Income from Salary'. Further, it is taxed on due or receipt basis, whichever is earlier.

As discussed earlier, salary income of expatriates would be taxable in India under the provisions of the ITA in case the same is received or deemed to be received in India or in case it accrues or is deemed to be accrued in India.

Further, Section 7 of the ITA provides that the following incomes are deemed to be received in India:

(i) Annual increase in the recognized provident fund balance of an employee, in excess of the prescribed percentage[6]

(ii) Transferred balance in the recognized provident fund to the extent specified[7]

(iii) Contribution made by the employer to the specified employee pension scheme

Section 9 *inter alia* provides that income from salary shall be deemed to be accrued in India in case the same is in respect of:

- services rendered in India; and
- leave period which is preceded and succeeded by services rendered in India and forms part of contract of employment.

Thus, salary income of an expatriate would be deemed to arise in India and hence taxable, if the services are rendered in India, irrespective of the place of entering into the contract of employment or receipt of the income.

A. Inbound Expatriate Employees

An inbound expatriate employee working in India would be liable to tax in India on the salary earned during the period of services rendered in India, whether he/she is on the payroll of the Indian entity or of the foreign entity, subject to certain exemptions provided in the domestic law as well as the respective DTAA.

Salary components

The ITA provides an inclusive definition of the term salary and perquisites. The term 'salary' includes wages, any annuity or pension, gratuity, any fees, commission, perquisites or profits in lieu of or in addition to any salary or wages, advance salary, leave salary, etc. Thus, essentially salary includes all consideration in money or money's worth (cash or kind) for services rendered arising out of an employer-employee relationship. The definition is wide enough to cover all types of payments whether in cash or kind; whether immediate or lump sum and whether from or on behalf of current or past employer.

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[6] As per Rule 6 of Part A of the Fourth Schedule of the ITA

[7] As per Rule 11(4) of Part A of the Fourth Schedule of the ITA

In addition to the normal components included in salary structure of any employee, some typical components of the remuneration package of an expatriate employee and the tax treatment of the same are discussed below:

1. Daily allowance / Per Diem - Daily allowance / per diem is generally paid to employees in addition to their regular salary in order to meet their daily living expenses.

Such daily allowance/ per diem is includible in the taxable salary income of employees. However, exemption from tax in some cases, particularly in case of short term business travelers, may be claimed in respect of the actual expenses incurred by the expatriate towards ordinary daily charges on account of absence from the normal place of duty.

2. Relocation allowance - The employees may be paid an allowance to meet relocation/ transfer expenses, shipment cost, excess baggage cost, etc. In case such allowance is actually used by the employees for travel and shipment purposes and the same can be substantiated by adequate documentation, the amount of allowance which is actually used to meet such expenses can be claimed as exempt. Any cash relocation allowance which cannot be substantiated with actual proof of expenditure (limited to travel and shipment of goods) is fully taxable.

3. House Rent Allowance ('HRA') – In case the employee has taken accommodation on rent in India, the HRA paid by the employer would not be taxable to the extent of lower of the following:

- Actual HRA received for the period during which the rented accommodation was occupied; or
- Excess of rent paid over 10% of salary for the period; or
- 50% of the salary, in case accommodation is situated in Mumbai, Delhi, Kolkata or Chennai, or 40% in all other cases

Salary for the purpose of computing the aforesaid exemption means basic salary, dearness allowance if terms of employment so provide and commission earned by the employee based on a fixed percentage of turnover achieved.

4. Provident Fund – Any contribution made by the employer to Provident Fund up to 12% of 'salary' as defined for the purpose of Provident Fund contribution is exempt from tax. However, any contribution in excess of 12% or the employee's contribution paid by the employer is taxable in the hands of the employee.

5. <u>Perquisites</u> – The term perquisite is defined widely to include all the benefits/concessions received by an employee from an employer. It includes both, monetary as well as non-monetary perquisites. Rules have been prescribed for valuing the perquisites and the same are discussed below:

5.1.<u>Accommodation</u> Free or concessional accommodation provided by the employer constitutes a taxable perquisite under the ITA. In terms of the valuation rules such accommodation perquisite is valued as follows:

Accommodation perquisite	Valuation Rules prescribed	
	Where accommodation is unfurnished	Where accommodation is furnished
A Provided by Central/ State Government	License fee determined by Central/State Government reduced by rent recovered from employee	Value of unfurnished accommodation to be increased by 10% of the cost of furniture, in case owned, or actual hire charges where it is hired as reduced by any charges paid for the same by the employee
B Provided by any other employer who owns the accommodation	– 15% of salary in cities having population above 2.5 million as per 2001 census – 10% of salary in cities having population exceeding 1 million but not exceeding 2.5 million as per 2001 census – 7.5% of salary in other case Less: Rent recovered from employee	Value of unfurnished accommodation to be increased by 10% of the cost of furniture, in case owned, or actual hire charges where it is hired as reduced by any charges paid for the same by the employee

Accommodation perquisite	Valuation Rules prescribed	
	Where accommodation is unfurnished	Where accommodation is furnished
C Provided by any other employer who has taken the accommodation on lease or rent	Actual amount of lease rental paid or payable by the employer or 15% of salary whichever is lower Less: Rent recovered from employee	Value of unfurnished accommodation to be increased by 10% of the cost of furniture, in case owned, or actual hire charges where it is hired as reduced by any charges paid for the same by the employee
D Provided in a hotel – Up to 15 days on transfer of the employee – For more than 15 days	Nil Lower of actual hotel charges or 24% of salary for the period of stay as reduced by the rent, if any, actually paid by the employee	

5.2. <u>Vehicle</u>

	Nature of perquisite	Valuation Rules prescribed	
		Small car (engine cc up to1.6 litres)	Big car (engine cc above 1.6 litres)
A	In case car is provided by employer		
A.1	Used exclusively for official purposes	Nil (see note)	Nil (see note)
A.2	Used exclusively for private purposes of employee and expense reimbursed by employer	Actual expenditure incurred	Actual expenditure Incurred
A.3	Used partly for official	₹ 1,800 p.m.	₹ 2,400 p.m.

	Nature of perquisite	Valuation Rules prescribed	
		Small car (engine cc up to1.6 litres)	Big car (engine cc above 1.6 litres)
	purpose and partly for private purpose and the running and maintenance expenses are reimbursed by the employer	(plus ₹ 900 if driver is provided)	(plus ₹ 900 if driver is provided)
A.4	Used partly for official purpose and partly for private purpose and the running and maintenance expenses for private use are fully met by the employee	₹ 600 p.m. (plus ₹ 900 if driver is provided)	₹ 900 p.m. (plus ₹ 900 if driver is provided)
B	In case car is owned by employee and employer reimburses running and maintenance expenses		
B.1	Used exclusively for official purposes	Nil (see note)	Nil (see note)
B.2	Used partly for official purpose and partly for private purposes	Actual expenses reimbursed reduced by ₹ 1,800 p.m. (plus ₹ 900 if driver is provided)	Actual expenses Reimbursed reduced by ₹ 2,400 p.m. (plus ₹ 900 if driver is provided)

Note:

A log book containing details of journey undertaken, viz. date of journey, destination, mileage and the amount of expenditure incurred, for official purpose needs to be maintained.

A certificate from the employer to the effect that expenses were incurred wholly and exclusively for the performance of official duties should be obtained.

5.3. Employee Stock based incentives

A company may reward its employees through any of the following forms of stock based incentives:

- Employee Stock Option Plans (ESOPs)
- Stock Appreciation Rights
- Restricted Stock Plans
- Employee Stock Purchase Plans

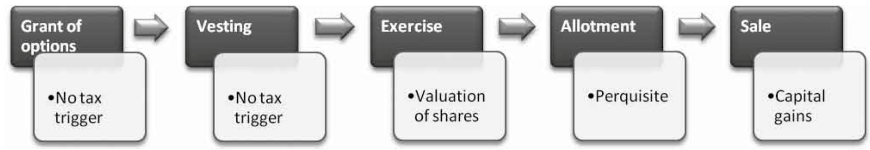
Securities allotted to employees under ESOP or similar share settled programmes constitute benefit derived by the employee and is taxed as salary income in the year of allotment of shares to the employees.

The taxable value is the Fair Market Value ('FMV') of the specified securities on the date on which the option is exercised by the employee as reduced by the exercise price recovered from the employee.

The FMV of the securities is determined as follows:

	Type of securities	FMV on date of exercise
Listed securities	Traded on one Indian stock exchange	Average of the opening and closing price
	Traded on more than one Indian stock exchange	Average of the opening and closing price on the stock exchange that recorded highest trading
	Not traded on date of exercise	Closing price of the share on a closest date preceding the date of exercise
Unlisted securities		As determined by a Category I Merchant banker: – on date of exercise or – any date not more than 180 days preceding the date of exercise

The flow of events and the relevance of the same in determining the levy of taxation on ESOP can be depicted as follows:



In case of cash settled stock based incentive plan , the cash payout is taxable as salary income.

The employer is required to withhold tax at the time of allotment of securities (in case of stock settled incentive plan) and at the time of cash payout (in case of cash settled incentive plan) to the employees. In case of global stock option plans, it is the responsibility of the Indian entity to withhold tax on the perquisite value of such stock options under Section 192 of ITA.

Further, individuals qualifying as NR or RBNOR in India are liable to tax only on their India sourced income. ITA does not specifically provide for apportionment of stock based income in relation to mobile employees. However, guidance may be drawn from the Delhi Income Tax Appellate Tribunal in the case of United Technologies International Operation, according to which if an employee is based in India only for a part of the grant period (i.e. period beginning with the date of grant of the stock options and ending with the date of vesting of the stock options), then proportionate amount of the value of benefit will be liable to tax in India. The proportionate value shall be determined by applying to the value of benefit, the proportion which the length of the period of stay in India by the expatriate during the grant period bears to the length of the total grant period.

Hence, in case of NRs and RBNORs, only that benefit which is attributable to the period of services rendered in India during the grant period shall be taxable in the financial year in which taxable event occurs.

5.4. Other perquisites

Perquisite	Valuation
Sweeper, gardener, watchman, personal attendant	Actual cost to the employer Less: Amount recovered from the employee for services
Supply of gas, electric energy, water	Actual amount of expenditure incurred or reimbursed by such employer on that account Less: Amount, if any recovered from the employee for such benefit or

Perquisite	Valuation
	amenity Note: Where supply of gas, electric energy, water is made from resources owned by the employer, without purchasing them from any outside agency then the value of perquisite would be manufacturing cost per unit incurred by the employer
Fee or concessional educational facilities for any member of employee's household	Actual amount of expenditure incurred or reimbursed by such employer on that account Less: Amount, if any recovered from the employee for such benefit or amenity
Interest free concessional loan for housing	Interest calculated using State Bank of India rates on maximum outstanding monthly balance Less: Interest paid by employee The provision is not applicable on petty loan up to ₹ 20,000 or loan for medical treatment in respect of specified diseases
Free food and non-alcoholic beverages	Amount of expenditure incurred by the employer Less: Amount recovered from the employee Except if employer provides free food and Non-alcoholic beverages during the office working hour at office premises or through paid meal voucher and amount of expenditure not exceeding ₹ 50 per meal.
Gifts, Vouchers or token to employees	Actual amount of expenditure incurred

Perquisite	Valuation
	However, such value to be considered Nil, if the value of gift per employee during the previous year in aggregate is below ₹ 5,000
Memberships and annual fees	Actual amount of expenditure incurred or reimbursed by such employer on that account Less: Amount, if any recovered from the employee for such benefit or amenity. Note: However, there will be no perquisite in the hands of employees if complete detail in respect of such expenditure are maintained by the employer & the employer gives the certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties
Use of movable assets (other than Laptops)	10% of actual cost of the asset or the amount of rent paid or payable Less: Amount, if any recovered from the employee for such benefit or amenity
Home Leave	Any expense incurred by the employer on the home leave travel for journey outside India for employee and his/her family is fully taxable
Telephone facility	Any expense reimbursed by Employers to the employee on account of telephone expenses incurred by an employee is exempt under Section 17(2) read with Rule 3 (7)(ix) of the Income-tax Rules, 1962. landline phone
Transfer of movable asset to the	Actual cost of movable asset

Perquisite	Valuation
employee directly or indirectly	Less: 10% of depreciation for each completed year which such assets was put to use by the employer (the depreciation rate to be used In case of computer and electronic items is 50% and in case of motor car is 20% by reducing balance method Less: Amount, if any recovered from the employee for such benefit or amenity
Any other benefits or amenities, services, rights or privilege	Cost to employer Less: Amount, if any recovered from the employee

5.5. <u>Medical expenses</u>

The ITA provides for the exemption of the following medical perquisites provided by an employer to its employees:

- Medical treatment provided to employee or his/ her family member in a hospital maintained by the employer;
- Amount paid by the employer towards expenditure incurred on medical treatment of employee or his/ her family member in an approved hospital and in respect of prescribed ailments;
- Premium paid by the employer for medical insurance of its employees under scheme approved by Insurance Regulatory Development Authorities of India (IRDA) or reimbursement of such insurance premium to employees;
- Reimbursement of medical expenses up to ₹ 15,000 per annum;
- Actual expenditure incurred on stay and medical treatment abroad of the employee or his/ her family member plus stay abroad of one companion to the extent permitted by the Reserve Bank of India.

For the above purposes, family means spouse, children and dependent parents and siblings of the individual.

Any insurance premium paid by the employer on a foreign medical insurance plan which is not approved by IRDA is not eligible for exemption as mentioned above. In absence of any specific exemption provided under ITA the same would be subject to tax. However, there are judicial precedents[8] stating that the any contribution to medical insurance plans may not be taxable if such contribution does not result in any direct present benefit to the employee but assures him/her of a future benefit subject to certain contingencies.

6. Tax equalization and Hypothetical tax - Most of the companies follows a principle wherein an expatriate should be neither better off nor worse off by taking up an international assignment and therefore he/she should pay no more or no less tax on the salary income than what would have been payable had the employee continued in the home country.

This principle is known as ‘tax equalization’ which means that a hypothetical tax is deducted from the salary and actual taxes in respect of income from employment in India would be borne by the employer and not by the employee.

Hypothetical tax is a part of the tax equalization policy under which the expatriate employee is responsible during the assignment for "hypothetical" or "stay-at-home" tax, which would be calculated on the remuneration the expatriate employee would have earned if he continued to live and work in the home location.

Hypothetical tax is withheld from the assignee's normal pay and is retained by the employer as a "tax reserve". The company would then pay all required home and host country taxes on employment income (including taxes on expatriate benefits) during the assignment.

There are judicial precedents to support the position that the hypothetical tax deducted from the salary does not constitute income in the hands of the expatriate and therefore cannot be treated as part of the employee’s taxable salary. This has also been re-affirmed by the Bombay High Court in the case of Jaydev H. Raja (ITA No 87/2000).

The tax so borne by the employer, would form part of the expatriate’s salary and therefore in computation of the ‘income from salaries’ the taxes so borne by the employer have to be grossed up and included therein.

As per the ITA[9], the employer could, at his option pay taxes on the non-monetary perquisites provided to employees, and such taxes need not be

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[8] Yoshio Kubo & Ors. vs Commissioner Of Income Tax (Delhi High Court) (ITA No 441/2003/Del)

[9] Section 10(10CC) of the ITA

grossed up. Considering that normally expatriate employees are tax equalized, the benefit of this could be availed. However, there would be a disallowance of expense under Section 40(a)(v) of the ITA, in the corporate tax return of the employer to this extent.

The Uttarakhand High Court in case of Sedco Forex International Drilling Inc.(TS-603-HC-2012) and the Delhi High Court in case of Yoshio Kubo & Ors. (ITA No 441/2003/Del) have held that amounts paid by the employer, directly to the Indian income tax authorities, in discharge of an employee's income tax liability do not fall into the category of monetary benefits and hence eligible for exemption under Section 10(10CC). The impact of the exemption is that, instead of applying for multiple gross-up, the employer can pay tax on employee's behalf on the value of non-monetary benefits with a single stage gross up.

It may however be noted that the above said position will receive finality after an affirmative decision by Supreme Court only.

The table below shows the total cost for an employer where the tax liability borne by it is calculated with multiple stage gross up and with single stage gross up relying on the High Court judgment.

	Particulars	Tax liability (without multiple stage grossing up) `	Tax liability (with multiple stage gross up)`
(a)	Total Income	100	100
(b)	Tax Perquisite (tax liability borne by the employer)#	31	45[100*31/ (100-31)]
(c)	Total Income including perquisite	131	145
(d)	Tax payable (@ 31%)	41	45
(e)	Total cost for the employer (a) + (d)	141	145

#assuming tax rate @31% for simplicity

Please note that the exemption under section 10(10CC) is a trade off with the corporate tax deductibility of such amount which is claimed as exempt (refer section 40(a)(v) of the ITA).

7. <u>Foreign social security</u>- There is no specific provision under ITA that governs the tax treatment for social security contributions made by an

employer to the overseas social security scheme on behalf of its employees. It has been held in various judicial pronouncements that in order to attract liability under Section 15 of ITA, the employee should have some vested interest in the amounts paid by the employer. Mere contingency of getting some benefits from the payments made by the employer would not justify them being taxed under these provisions. The Mumbai Income Tax Appellate Tribunal ('ITAT'), in the case of Gallotti Raoul v. Assistant Commissioner of Income-tax, Mumbai, 61 ITD 453 (1997), has held that only the net salary was to be taxed in India after adjustment of the French social security charges. Based on the interpretation of relevant section and judicial precedents on the taxability, employer's contribution may be considered as exempt if following conditions are satisfied:

- The contribution made is an obligation of the employer;
- The contribution made is not an obligation of the employee being met by the employer;
- It is not actually paid to the employee or allowed to the employee or due / accrued to the employee from the employer;
- The employee does not have a vested right at the time when contribution is made;
- The benefit from the contributions made to the funds is contingent in nature;
- The employees do not have any right to claim the amount payable under the policy on the date on which the contribution is being made until happening of such contingency.

Fact specific evaluation of social security scheme / system is required in order to determine the taxability of any contribution made by the employer to such scheme/ system.

Exemptions

Short-stay exemption

The ITA[10] provides for a short stay exemption in case of an individual who is not a citizen of India. The remuneration received by him/ her as an employee of a foreign entity, for services rendered by him/ her during his/ her stay in India is exempt from tax subject to fulfilment of all the following conditions:

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[10] Section 10(6)(vi) of the ITA

- The foreign enterprise is not engaged in any trade or business in India;
- His/her stay in India does not exceed in the aggregate a period of 90 days in such previous year; and
- Such remuneration is not deductible from the income of the employer chargeable under the ITA.

Similarly, India's DTAAs with different countries also provide for a short stay exemption for DTAA residents of other countries in respect of employment exercised in India. Generally, Article 15 or 16 (dependent personal services) of the DTAAs, deal with taxation of employment income.

The said Article provides that salaries, wages and other similar remuneration derived by a resident in respect of employment exercised in the host country would be taxable in the host country; however such income would be taxed exclusively in the home country/ country of residence provided:

- The employee is present in the host country for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned depending upon the relevant clause of the respective DTAA;
- The remuneration is paid by, or on behalf of, an employer who is not a resident of the host country; and
- The remuneration is not deductible in computing the profits of an enterprise chargeable to tax in the host country. In other words, such remuneration is neither deductible nor borne by the PE of the foreign employer in the host country or any other entity which has taxable presence in India.

The aforesaid conditions may differ from country to country and the relevant DTAA should be referred to before application. A claim for the beneficial provisions under this Article should also be substantiated with evidence.

Thus, it could be concluded that inbound expatriates whose presence in India is for a short-term duration could be exempt from tax in India under the relevant DTAA subject to fulfilment of all the conditions mentioned in the relevant clause of the respective DTAA.

Further, in order to claim any benefit under the applicable DTAA by a resident of other country, the person is required to obtain a tax residency certificate from the revenue authorities of the other country.

Tax credits

An inbound expatriate earning income in India may be liable to tax in India under the 'source' rule and may also be taxable in respect of the same income in his/ her home country as per the 'residence' rule. This scenario can lead to double taxation of the same income and in order to avoid the same DTAAs provide for specific provisions for elimination of such double taxation. The most common methodology for avoidance of double taxation used in Indian DTAAs are:

- Exemption method — income or capital that is taxable in the country of source may be fully exempted in the country of residence or vice versa. Alternatively, the country of source limits its right to tax income from sources in its country.
- Credit method — income or capital that is taxable in the country of source may be subject to tax in the country of residence. However, the tax levied in the country of source is credited to the extent of tax levied by the country of residence on such income or capital.

Generally, in terms of the DTAAs income arising to an expatriate is taxed with or without limitation in the source country and therefore the country of residence has the obligation to eliminate double taxation through credit method.

In case there is no DTAA, signed between India and the home country, the tax payer can take benefit under Section 91 of ITA. The above relief is available to the individuals who qualify as resident of India in any tax year. The individual will be entitled to the deduction from the Indian income-tax payable by him/her of a sum calculated on the doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

Conversion of home country salary in Indian rupees in order to calculate Indian taxes

Generally, expatriates receive part of their salaries in foreign currency especially when they continue to remain on the payroll of the foreign employer. In such cases, the salary denominated in foreign currency is to be converted to Indian rupees using the telegraphic transfer buying rate of such foreign currency as on the following dates:

- In case where tax is deductible at source by the employer-the date on which tax is required to be deducted at source i.e. at the time of payment of such salary[11]
- In other cases — the last day of the month immediately preceding the month in which the salary is due, or is paid in advance or in arrears[12].

Telegraphic Transfer Buying Rate in relation to a foreign currency means the rate of exchange adopted by the State Bank of India for buying such currency having regard to the guidelines specified from time to time by the Reserve Bank of India.

Withholding tax implications on the employer

Section 192 of ITA governs withholding tax provisions for payments in the nature of "Salaries". It casts an obligation on the 'person responsible for paying' salary to deduct and deposit withholding taxes at the appropriate rates of tax, as prescribed by ITA.

Based on Section 192 (1) of the ITA, the employer, being a person responsible to pay salary is under an obligation under Section 192(1) of ITA to deposit withholding taxes (on an average basis) at the applicable rates, on the salary payments to the expatriates. Failure to withhold appropriate taxes would expose the employer to interest and penalties under ITA.

In this regard, it is pertinent to note that the Supreme Court of India[13] has ruled that in case salary paid to the expatriate is for rendition of services in India, with no part of such services being performed for the foreign entity, tax has to be deducted at source from salaries of expatriate employees working in India even in cases where such salaries were paid abroad. In other words, salary payable for services rendered in India should be subject to tax deducted at source/ withholding tax provisions, even on that part of the salary which is paid in the home country to the expatriate employee.

The sum of all the salary components, after considering the exemptions and including the value of monetary as well as non- monetary perquisites, would constitute the total salary income chargeable to tax in India.

Service tax Implications

The Finance Act, 2012 has introduced a shift in the manner in which service tax shall be levied post 1 July 2012. The transition involves shift from

[11] Rule 26 of the Income-tax Rules, 1962
[12] Rule 115 of the Income-tax Rules, 1962
[13] Eli Lilly & Company (India) Pvt. Ltd. (178 Taxman 505)

taxation of specified services to a new regime wherein all the services provided in the taxable territory is taxed unless they are excluded from the definition of 'Service' or are covered by any of the entries specified in the negative list.

The term 'service' has been defined under the Service tax law to mean any activity undertaken by one person for another, for a consideration.

The reimbursement of secondment costs by Indian entity to a foreign entity is not covered under the negative list. Hence, the secondment arrangement and relationship between the foreign entity, Indian entity and the expatriate needs to be evaluated to ascertain any service tax obligation.

Transfer pricing

Under the Indian transfer pricing regulations (provided under Sections 92, 92A to 92F of the ITA and the rules there under), any "international transactions" between two or more Associate Enterprises (AEs) would need to satisfy the arm's length principle. The term "international transaction" is defined as a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

The transfer pricing regulations also requires taxpayers to maintain specified contemporaneous transfer pricing documentation to establish the arm's length nature of its international transaction with the AEs, and also to report all such transactions to the Indian tax authorities in the specified form (i.e. Form 3CEB – Accountants Report) to be filed along with corporate income-tax return.

The secondment transaction between related parties would be subject to transfer pricing regulation and hence any cost sharing arrangement should satisfy arm's length principle.

B. Outbound Expatriate Employees

An overview of the significant issues arising in case of an outbound assignment and the general taxability in such cases are discussed below:

Residential Status and taxability of income under ITA

NR/RBNOR in India

An outbound expatriate employee who is a person of Indian origin shall qualify for the non-resident status if the total stay in India is less than 182 days during the year of departure and any subsequent year of assignment outside India and in such a case, he/ she would be liable to tax in India only in respect of the following:

- Salary actually received in India;
- Salary deemed to be received in India i.e. annual accretion to the recognized provident fund in excess of the prescribed percentage[14] and employer's contribution to notified pension scheme;
- Salary in respect of services rendered in India;
- Salary in respect of rest or leave period which is preceded or succeeded by service in India.

ROR of India

Outbound expatriate employees qualifying as resident (ROR) in India would be subject to tax on their worldwide income under the ITA and eligible for foreign tax credit on foreign sourced income.

Taxability of income under applicable DTAA.

DTAA resident of India

Further, in terms of DTAA, an outbound expatriate employee would be deemed to be a resident in India, if he/she is resident under the ITA and accordingly may be entitled to claim the short stay exemption in the host/source country subject to fulfilment of all the conditions prescribed in the dependent personal service article of respective DTAA.

DTAA resident of host country

An outbound expatriate employee who qualifies as a NR in the relevant financial year under ITA and a resident of host country under its domestic tax laws, may claim the income received in India for services rendered in the host country as exempt in India under Article 15 /16 (the Dependent Personal Services) of the applicable DTAA. In order to claim any such exemption, tax

[14] Presently the prescribed percentage is at 9.5% in case of interest and 12% of salary in case of employer's contribution

residency certificate issued by the Revenue Authorities of host country is required.

Taxability of Income

The tax treatment of the various salary components and computation of the taxable salary in case of outbound expatriate employees would be similar as in the case of inbound expatriate employees, discussed above. However, there are few typical issues in case of outbound expatriate employees which have been discussed below:

- Generally, an outbound expatriate employee who is a person of Indian origin would qualify for the beneficial provisions for determination of residential status and therefore can continue to enjoy non-resident status as long as total stay in India does not exceed 181 days.
- Even though the services are rendered outside India, in case the outbound expatriate employee continues to receive salaries in India under a short-term assignment, such salary would be taxable in India. However, if the outbound expatriate employee satisfies the conditions as provided in the sub article 1 of Article 15/16 of the DTAA, the same may not be taxed in India. Accordingly the Indian employer may not deduct tax in respect of such salary payments upon a satisfaction that the resulting tax liability has been discharged in the host country[15].
- Outbound expatriate employees contributing to foreign social security scheme pursuant to their posting to a foreign country can still contribute to Provident Fund in India if they continue to be employees of Indian employer during the period of their assignment.

C. Issues

Taxation of employees working abroad on ship or aircraft

In terms of Articles 8/9 of the applicable DTAAs dealing with air transport and shipping business, the remuneration in respect of an employment exercised aboard on a ship or aircraft in international traffic may be taxed in the country of which the person deriving the profits from the operation of the ship or aircraft is a resident.

Taxation of director’s fees

Director’s fee is the remuneration received by an individual, in the capacity of a member of a board of directors of a company.. Services are deemed to

[15] British Gas India Ltd. (AAR) (285 ITR 218)

have been rendered in the country where the company is a resident. Remuneration would cover all payments in cash and kind. It is pertinent to mention here that the OECD definition restricts itself to only

'Directorial remuneration in his capacity as a member of the board of directors of a company' and excludes all payments made to a Director in any other capacity.

Taxation of accidental expatriates

An accidental expatriate is an employee who has travelled overseas enough so as to trigger taxation in that country. Besides taxation, accidental expatriates may trigger immigration and permanent establishment risks for the employer in that country.

For instance, a business visitor to India whose business visits aggregate to a physical presence of more than 182 days in the given financial year would be an accidental expatriate. The employer would be required to comply with the withholding tax requirements in respect of such expatriate and might be exposed to interests and penalties for delay in withholding and deposit of tax.

Tax residency certificate

In order to claim relief under DTAA, Section 90 of the ITA has been amended to provide for an additional requirement. Sections 90 (4) and 90A(4) of the ITA provide a condition for submission of tax residency certificate to avail the benefits under a DTAA. The certificate would have to be obtained from the Revenue Authorities of the host country.

Further, a standard format has also been issued for making an application for requesting tax residency certificate from the Indian tax office if the individual qualifies as a resident of India, where the certificate is required by the authorities of another country.

Reporting requirements for payments made to non-residents

With effect from 1 October 2013, any payment made to a non resident which is "chargeable to tax in India" is required to be reported electronically in Form 15CA and Form 15CB. Thus salary payments made to non resident expatriates are required to be reported in case they are chargeable to tax in India.

Obligation to pay Gratuity

As per Section 4 of the Payment of Gratuity Act, 1972, gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than five years;

- on his superannuation, or
- on his retirement or resignation, or
- on his death or disablement due to accident or disease.

The expatriates who have already rendered five years of services reserve the right to claim gratuity from the Indian employer at the time of termination.

IV. Other heads of income & deductions

As discussed earlier, apart from salary, income arising to a tax payer in India can be classified into four heads. Each of these heads of income and the distributive rights for taxation of the same are discussed below:

Income from house property

An expatriate who is NR/RNOR in India, shall be taxable in India in respect of income from immovable property provided either such income is received in India or the underlying property is situated in India. However, in case the expatriate is ROR in India, his/her global income would be liable to tax in India and accordingly, income arising from immovable property situated outside India would also be taxable in India.

In this regard, Article 6 of India's DTAAs, dealing with income from immovable property generally provide that such income 'may be taxed in the country where the property is situated' (i.e., the source country).

Hence in case of double taxation, country of residence can provide the credit of taxes paid in the country of source i.e. in the country where the property is situated.

Income from Business or profession

In terms of India's DTAAs, business income derived by a non- resident shall be taxable in India provided such business is carried on in India through a 'permanent establishment' situated in India. A permanent establishment ('PE') primarily means an industrial or commercial establishment that is equipped with sufficient resources to operate as an independent business unit ('fixed base PE') and includes within its ambit a PE arising on account rendition of services by a non-resident ('service PE') as well as an agency permanent establishment ('agency PE'). It would basically mean a 'virtual projection' of the resident of a foreign country into India.

Thus, in case a person resident abroad is carrying on a business in India through a PE, income attributable to such PE shall be taxable in India.

Income from profession

In terms of India's DTAAs, income derived by a non-resident in India in respect of professional services shall be taxable in India provided the non-resident professional has a fixed base available to him/her in India or his/her stay in India is equal to 183 days or more in the relevant financial year.

For the purpose of this Article 'professional services' includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

Capital gains

Under the ITA, non-resident expatriates are subject to tax only on gains from the transfer of capital assets situated in India or from the transfer abroad of foreign assets if sales proceeds are received directly in India.

Generally, the Article dealing with capital gains in India's DTAAs also provide for the source based taxation in case of immovable properties, movable properties forming part of the business assets of a permanent establishment as well as for shares. For all other assets taxation would be in the country of residence of the tax payer.

Income from other sources

Any residual income not covered in the earlier heads of income is taxable as Income from other sources and basically includes interest, dividend (excluding exempt dividend under Section 10 of the ITA), royalties, fees for technical services, etc. Generally, in terms of tax treaties, non-resident expatriates would be taxable in India in respect of such income provided the same is arising in India. The tax rates for the same are specified in the respective Article of the DTAAs.

Under the domestic tax law the following interest income are exempt from tax:

- Interest on Non-resident (external) account in the hands of individual non-resident under the Foreign Exchange Management Act[16]

[16] Section 10(4)(ii) of the ITA

- Interest on FCNR deposits exempt in the hands of individual who are non-resident or resident but not ordinarily resident[17]
- A deduction of up to ₹ 10,000 may be claimed by individuals with respect to interest on deposits in a savings account with a banking company, specified co-operative society or post office in India.

The total of income under each of the heads discussed above would constitute the gross total income from which the expatriate can claim certain deductions on account of investments in eligible securities, payment of life insurance premium, contribution to provident fund, contribution to certain pension funds, payment towards children tuition fee and other specified payments up to a maximum amount of `100,000 per annum[18].

V. Procedural Compliances

An expatriate coming to India has to comply with the following procedural formalities in India

A. Entry procedures – inbound employees

Before arrival:

Foreign nationals arriving in India must hold a valid visa. The Indian Embassy/High Commission located in various countries issue the correct type of visa to foreign nationals based on the proposed activities of foreign nationals in India. Foreign nationals can secure visas to enter India in the applicable categories listed below:

Nature of visa	Purpose
Employment visa Project visa	Individuals intending to take up employment For executing projects in power and steel sectors
Business visa	Visiting India on business visits
Tourist visa	Visiting India on tourism
Student visa	Pursuing studies/academic courses
Entry visa	Other purposes not covered elsewhere (including accompanying families of foreign nationals)
Research visa	Pursuing research in any field
Transit visa	Travellers passing through the country

[17] Section 10(15)(iv)(fa) of the ITA
[18] Section 80C of the ITA

Missionary visa	Missionaries of registered charitable trusts
Journalist visa	Media representatives
Conference visa	Event organizers and visitors
Sports visa	For professional and amateur sportspeople, judges and adjudicators who want to come to India to participate in their field of sport
Medical visa	For seeking medical treatment in India at recognized and specialized hospitals and treatment centres

The Government of India has issued guidelines on the grant of visa to foreign nationals visiting India for business or employment. The guidelines specify the conditions for issuing a business or employment visa. Further, the guidelines also stipulate the activities for which the business or employment visa may be required.

Business and employment visas cannot be converted into any other kind of visa during a foreign national's stay in India. However, such business and employment visas may be converted into "X" visa (dependent visa)/"Medical" visa, subject to the prescribed conditions and the prior approval of the Ministry of Home Affairs of India.

After arrival:

Foreign nationals visiting India on employment visa are required to get themselves registered with concerned Foreigner's Regional Registration Office ('FRRO') within 14 days of his/her first arrival, irrespective of the duration of their stay[19]. However, foreigners holding Overseas Citizenship of India ('OCI') or Person of Indian Origin ('PIO') are exempted from FRRO registration.

Further, foreigners visiting India on other categories of long- term visa including Business visa would not require registration with the concerned FRRO if duration of his/her stay does not exceed 180 days on a single visit. In case a foreigner intends to stay for more than 180 days on a single visit he should get himself/ she registered well before the expiry of 180 days.

Registration facilities are not provided at the airport and are carried out in the office of FRRO or District Superintendents of Police.

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[19] See http://boi.gov.in/ for further details

At the time of registration every foreigner, shall furnish, such information in registration report, as may be in his possession for the purpose of satisfying the Registration Officer and shall, on being required, sign the registration report in the presence of the said officer and shall thereupon be entitled to receive a certificate of registration. For the purpose of the registration the following needs to be submitted:

- Four recent passport size photographs;
- Photocopy of photo page and valid Indian Visa page of the passport;
- Proof of residential address in India;
- Documents of identification and;
- In case of Employment Visa, request letter, undertaking, contract agreement from employer;
- In case of Business Visa, business related papers on the authenticity of the business, copy of permission from Reserve Bank of India and approval of Government of India in case of joint venture/collaboration;

Nominal fee of ₹ 100 is charged for registration within the prescribed time. A penalty in Indian currency equivalent to US$ 30/- in case of late registration is charged.

B. Permanent Account Number ('PAN')

PAN is akin to an Income-tax registration number and any person earning taxable income in India has to obtain the PAN. The application is to be made in Form 49AA to the National Securities Depository Ltd. Facilitation centres together with a copy of prescribed documents.:

The documents accepted as proof of identity and proof of residence is stipulated under Rule 114 of the Income tax Rules, 1962.

PAN application can also be made online on the website of

National Securities Depository Ltd[20].

The PAN is to be quoted on all tax returns, correspondence with the tax authorities and on all documents relating to prescribed categories of transactions.

C. Advance Tax

Where the total tax liability after TDS exceeds ₹ 10,000, advance tax is

[20] https://tin.tin.nsdl.com/pan/form49AA.html

payable within the same financial year on the principle of pay-as-you-earn. The due dates for payment of advance tax and the amount payable are:

Due Date	Amount Payable
On or before 15th September of the year	30% of estimated tax
On or before 15th December of the year	60% of the estimated tax less earlier installment
On or before 15th March of the year	Whole of the estimated tax less earlier installments

Failure to pay advance tax invites interest liability under sections 234B and 234C of ITA. Interest is payable at 1% per month for three months in case of deferral of tax payment which is due on 15th September and 15th December and for one month in case of deferral of payment of the last instalment i.e. tax which is due on 15th March. No interest is charged in respect of advance tax on capital gains and windfall gains if the tax on such income is paid in subsequent installments due when the gain arises before 15th March. If such gain arises after 15th March, no interest will be charged if the tax is paid on or before 31st March.

If the total amount of advance tax amounts to less than 90% of the tax payer's actual liability after Tax Deducted at Source (including foreign tax credit), interest is payable at the rate of 1% per month from 1st April following the year in which the tax is due until full payment of the tax occurs.

The amount paid after 15th March but on or before 31st March is also treated as advance tax paid. Thus, if estimated income is likely to exceed the amount estimated on or before 15 March, then additional advance tax can be paid and penal interest can be saved.

D. <u>Self-assessment Tax</u>

Any remaining tax due after claiming credit for Tax Deducted at Source/Tax Collected at Source, advance tax payments and foreign tax credits is to be paid by way of self assessment tax. Self-assessment tax is a tax paid after the end of the tax year by an individual and generally at the time of filing the tax return.

E. <u>Tax return filing</u>

Every expatriate earning taxable income in India is required to furnish a return of income, in the prescribed form, giving details of his/her income under different heads, tax liability thereon, deductions claimed, etc. The due date for filing such tax return is 31st July of the assessment year i.e. the following financial year. For instance, the tax return for the financial year ended 31st March, 2014 is required to be filed by 31st July, 2014.

A return of income filed within the due date, can be revised at any time, before the expiry of one year from the end of the relevant assessment year (i.e., till 31st March, 2016 in the above instance) or before completion of the assessment by the tax department, whichever is earlier.

Effective financial year 2011–12, RORs in India who have assets (including financial interest in any entity) located outside India or a signing authority on any account located outside India, are mandatory required to file a tax return electronically in India (irrespective of their level of income). This provision will apply even to individuals accompanying expatriates to India as it is unrelated to whether the individual has taxable income in India. The income tax return forms also require information relating to such assets (along with other disclosures) to be set out in the forms.

Further effective financial year 2012-13 tax returns must be filed electronically by all taxpayers with taxable income exceeding ₹ 500,000 and by the taxpayers claiming a foreign tax credit on their Indian tax return.

F. Tax clearance certificates

The ITA provides for procedures to be followed by any person leaving India to obtain a no-objection certificate and the same are summarized below:

For foreign nationals

In terms of section 230(1) of the ITA a foreign national who has come to India in connection with business, profession or employment and has derived income from any source in India has to furnish an undertaking in the prescribed Form 30A to the tax authorities. The said form is basically an undertaking to be given by the employer of the expatriate to the effect that any future tax liability arising in case of the expatriate would be paid by the employer. The purpose of the undertaking is that the Indian Government should not be at loss in terms of collection of taxes in case any tax liability arises in India after repatriation of the expatriate. The tax authorities upon receipt of the undertaking and verification of the documents filed shall issue a no objection certificate in Form No. 30B to the expatriate. Such certificate issued by the tax authorities is valid for the period specified in the certificate from the date of issue. Due to any reason, if the expatriate has to defer his departure date beyond the period stated in the certificate, he is required to obtain a fresh certificate from the tax authorities.

The above compliance procedure is not applicable to a foreign national who visits India as a foreign tourist or for any other purpose not connected with business, profession or employment.

For individuals domiciled in India – outbound employees

In case of a person domiciled in India, leaving India the relevant information needs to be furnished to the tax authorities in Form No. 30C which is a self-declaration by the outbound expatriate that includes his/her details such as PAN, passport details, purpose of visit outside India and estimated period of stay outside India, etc.

Thus, it may be seen that an inbound expatriate shall file Form No.

30A and obtain No Objection Certificate in Form 30B from the tax authorities in India while an outbound expatriate shall furnish his/her information in Form No. 30C to the tax authorities.

Social Security in India

Provident Fund Obligation in India

Social Security in India is governed principally by the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (the PF Act) and is operated through the following schemes:

- Employees Provident Funds Scheme, 1952 (PF Scheme)
- Employees Pension Scheme, 1995 (Pension Scheme)
- Employees Deposit Linked Insurance Scheme, 1976 (EDLI)

The PF Act applies to establishments employing 20 or more persons engaged in a specified industry or notified by the Central Government from time to time or establishments which has opted for voluntary coverage under the PF Act.

Applicability of Indian Social Security Schemes to International Workers

In October 2008, the Government of India issued notifications extending the applicability of PF Act to a new category of workers called 'International Workers' requiring them to mandatorily contribute into its schemes effective 1 November 2008.

'International Worker' has been defined to mean:

- Indian employee having worked or going to work in a foreign country with which India has a Social Security Agreement (SSA) and satisfying the conditions as prescribed in such SSA;
- Non-Indian employees, not holding an Indian passport, working for a covered establishment in India to which the PF Act applies (coming from a country with which India has not entered into a SSA).
- A 'covered establishment' is –
    - an establishment employing 20 or more persons engaged in a specified industry or notified by the Central Government from time to time.
    - any establishment employing even less than 20 persons that has opted to be covered voluntarily under the PF Act.

Contribution for International Workers

The employer is required to contribute 24% of employee's 'Monthly Pay' under the schemes and has option to recover 12% of 'Monthly Pay' from employee's salary. The 24% contribution in case of International workers will be split as follows:

- 12% of 'Monthly Pay' as employee's contribution to PF Scheme
- 8.33% of 'Monthly Pay' as employer's contribution to Pension Scheme
- 3.67% of 'Monthly Pay' as employer's contribution to PF Scheme.

Withdrawal from the Provident Fund Scheme

International Workers will be entitled to withdraw accumulated balance in the Provident Fund Scheme in the following circumstances:

- On retirement from service after attaining the age of 58 years;
- On permanent and total incapacity;
- On ceasing to be an employee of a covered establishment in respect of an International Worker covered under a SSA.

Accordingly, in case where an International Worker is not covered under a SSA entered into between India and any other country, accumulated balances in Provident Fund account will be not be refundable until the International Worker retires after attaining the age of 58 years (subject to certain exceptions).

Social Security Agreements

India has currently signed SSA with 17 countries and out of which, as on today agreements with Netherlands, Korea, Belgium, Germany, Switzerland, Luxembourg, France, Hungary and Denmark have been entered into force.

The various advantages of signing an SSA are:

Detachment-CoC

A CoC is a confirmation from home country social security authorities that the individual is covered under home country social security and continues to be covered during the period of assignment. Foreign passport holders can obtain CoC in home country and claim exemption in India. Likewise, Indian passport holders can obtain CoC in India and claim exemption in host country with which India has an SSA. One of the eligibility conditions of detachment is the requirement for the employee to work in the host country on behalf of the home country entity. This could lead to a potential Permanent Exposure.

Equality of treatment

An SSA ensures that persons who ordinarily reside in either country receive equal treatment with the nationals of that country in the application of the social security legislation.

Export of benefits

SSAs contain provision for payment of benefits to the International Workers irrespective of the location (India, home country or a third country).

Totalization of periods

Totalization of periods means aggregation of time spent in home country and host country to determine eligibility to social security benefit. International Workers who contribute to social security in both countries are eligible to aggregate periods covered in both countries to determine eligibility to pension benefits in either country. Aggregation of periods is permissible only for determining eligibility and not for the purpose of determining actual level of benefit payable.

Exchange Control

A. Residential status

The Foreign Exchange Management Act, 1999 (FEMA) defines a non-resident/ person resident outside India as a person who is not resident in India.

In terms of the aforesaid definitions an individual shall be deemed to be a non-resident in case he/she is residing in India for a period of not more than 182 days during the preceding financial year and includes:

- A person who has gone out of India or who stays outside India either for employment outside India, or for carrying business outside India, or for any other purpose as would indicate his/ her intention to stay outside India for an uncertain period; and
- A person who has come to or stays in India for purposes other than for taking up employment in India, or for carrying on business in India, or for any other purpose as would indicate his/her intention to stay in India for an uncertain period.

On the basis of the nationality and residential status of the individual under the foreign exchange laws, an individual may be categorized as a Non Resident Indian (NRI) or a Person of Indian Origin (PIO) or a Foreign National.

A non-resident Indian ('NRI') is defined as a non-resident who is citizen of India whereas a Person of Indian Origin ('PIO') means a citizen of any country other than Bangladesh or Pakistan who had (a) at any time held Indian passport or (b) he or either of his parents or any of his grandparents was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 or (c) the person is a spouse of an Indian citizen or a person referred to in (a) or (b).

B. Bank accounts

Banks offer two types of accounts to NRIs, based on whether funds available in the account are repatriable i.e. whether such funds can be transferred or repatriated abroad.

- Repatriable Accounts:
  - Non-Resident (External) Rupee ('NRE') Accounts –

Both Principal and Interest can be repatriated / transferred out of India. Savings rate on NRE accounts is at par with savings rates in resident accounts.

Term deposits can be made for 1 to 3 years.

The interest rates on Non-Resident (External) Rupee (NRE) Deposits are deregulated. Accordingly, banks are free to determine their interest rates on both term deposits of maturity of one year and above under Non-Resident (External) Rupee (NRE) Deposit accounts.

– FCNR (B) Accounts –

Similar to NRE accounts, in FCNR (B) Accounts both principal and interest are repatriable. Presently, deposits can be made in 6 specific foreign currencies (US Dollar, Pound Sterling, EURO, Japanese Yen, Australian Dollar and Canadian Dollar).

Interest rate — On maturity period of 1 to less than 3 years it shall be LIBOR/SWAP plus 200 basis points and for maturity period 3 – 5 years it shall be LIBOR /SWAP plus 400 basis points. For floating rate deposits, the interest reset period shall be six months.

– NRO Accounts –

In NOR Account, only current earnings are repatriable. Savings NRO accounts are normally operated to credit rupee income from shares, interest, rent from property in India, etc.

In case of term deposits, banks are allowed to determine their own interest rates.

Banks can allow remittance up to USD 100,000 per financial year for bona fide purposes from balances in the NRO accounts once taxes are paid out without any prior approval from Reserve Bank of India.

This limit includes the sale proceeds of immovable properties held by NRIs and PIOs.

– Resident Foreign Currency (RFC) Account –

NRIs and PIOs returning to India can maintain an RFC account with an authorized bank in India to transfer funds from their NRE/ FCNR (B) accounts.

Proceeds of assets held outside India before their return to India can be credited to the RFC account.

These funds are free from all restrictions as to their utilization or in investment in any form outside India.

- *Non-Repatriable Accounts:* Non-repatriable funds are those which cannot be taken out of India.

  These have to be maintained in a separate bank account i.e. a Non Resident Ordinary ('NRO') account. Investments made from non-repatriable accounts cannot be repatriated but have to be maintained in a Non-Repatriable Demat account. Money once transferred from an NRE account to an NRO account cannot be transferred back to an NRE account.

  Generally when a resident becomes an NRI, his existing savings account is designated as a NRO account. The NRO accounts could be maintained in the nature of current, saving, recurring or term deposits. NRIs can also open NRO accounts for depositing their funds from local transactions. The interest earned from NRO accounts is fully taxable in India. NRO accounts can be opened in the name of NRIs who have left India to take up employment or business temporarily or permanently in a foreign country. Funds from NRO accounts are not repatriable or transferred to NRE accounts without the prior approval of the RBI.

  However, NRIs, PIOs, Foreign Nationals, retired employees or non-resident widows of Indian citizens can remit, through the Authorized Dealer, up to USD one million per calendar year from the NRO account or from income from sale of assets in India.

It may be noted that the RBI *vide* its recent circular dated 9th June 2011[21] has permitted foreign nationals to re-designate their resident account maintained in India as NRO account on leaving the country after their employment in order to enable them to receive their pending bonafide dues such as income tax refunds, Provident Fund withdrawals, etc. subject to certain conditions.

C. Remittance of salary

A citizen of a foreign state resident in India, being an employee of a foreign entity and on deputation to India with the office/ branch/ subsidiary / joint

[21] RBI/2010-11/560 A.P. (DIR Series) Circular No. 70

venture of foreign entity or being an employee of an Indian entity, may open, hold and maintain a foreign currency account with a bank outside India and receive/remit the whole salary payable to him/her for the services rendered, by credit to such account, provided that income tax chargeable under the ITA is paid on the entire salary as accrued in India.

Similarly a citizen of India, employed by a foreign entity outside India and on deputation to India, may open, hold and maintain a foreign currency account with a bank outside India and receive the whole salary payable to him/her for the services rendered in India, by credit to such account, provided that income tax chargeable under the ITA is paid on the entire salary as accrued in India.

D. Permissible investments

The permissible investments for different categories of individuals under the foreign exchange laws in India are tabulated as under:

Status of individual	Investments	General / Special permission
NRI	Shares, convertible debentures*, real estate (other than an agricultural land, plantation or farm house) etc.	General Permission granted
PIO	Shares, convertible debentures*, real estate (other than an agricultural land, plantation or farm house) etc.	General Permission granted
Foreign national	Shares, convertible debentures* etc.	General Permission granted
	Real Estate (including an agricultural land, plantation or farm house)	Not permitted**

*The foreign exchange regulations provide that an Indian entity shall issue any security (eg. shares, convertible debentures etc.,) to a non- resident only with the prior permission of Reserve Bank of India (RBI). A foreign national, being a person resident outside India, may acquire shares listed on an Indian stock exchange only through a registered foreign institutional investor route under the portfolio investment scheme. Similarly a NRI/PIO, being a person resident outside India, may acquire shares listed on an Indian stock exchange under the portfolio investment scheme. It may be noted here that once the individual gains the status of being a resident as per the exchange control regulations, the individual may acquire securities through a recognized stock exchange in India.

** A foreign national is generally not permitted to acquire any property or invest in real estate in India. However, he may acquire a residential property in India by obtaining a prior permission from the RBI. The RBI may grant permission to the foreign national after satisfying certain conditions, on a case to case basis.

Hence, it may be observed that a NRI/PIO may be privileged to make investments into most forms of investments, whereas certain restrictions are applicable in case of investments made by foreign nationals.

Gist of Important Case Laws

UOI vs. Azadi Bachao Andolan (SC) (263 ITR 706)

Circular No. 789 dated 13-4-2000 providing that FIIs, etc. which are resident of Mauritius would not be taxable in India on income from capital gains arising by sale of shares is valid and efficacious — the double taxation agreement between India and Mauritius is valid in law and an attempt by resident of third party to take advantage of existing provision of DTAA is not illegal.

ACIT vs. Robert Arthur Keltz (represented by United Technologies International Operation) (3452/DEL/2011) (Delhi ITAT)

The Delhi Tribunal held that as the employee has not rendered service in India for the whole grant period of stock option, only such proportion of the stock options as is relatable to the service rendered in India during the grant period is taxable in India.

CIT vs. Jaydev H. Raja (Mumbai High Court) (Income tax appeal No. 87 OF 2000)

The Mumbai High Court in the case of a resident but not ordinary resident held that only actual reimbursement of tax by his overseas employer can be treated as his perquisite and taxed accordingly. Any tax which is borne by the assessee cannot be treated as his income. The High Court reaffirms the Delhi High Court ruling on hypothetical taxes not forming part of the taxable salary of an employee.

DIT vs. Sedco Forex International Drilling Inc (Uttarakhand High Court). (TS-603-HC-2012)

The employer entered into an agreement with its employees pursuant to which the employer agreed to bear the income tax payable by the employees on their salary. The question was whether such tax payment was "income" in the nature of a perquisite, not provided for by way of monetary payment, within the meaning of clause (2) of Section 17 of the ITA and hence eligible for exemption under Section 10(10CC) of the ITA. In this case High Court held that the tax on the salary paid by the employer was a "perquisite" under Section 17(2)(iv) because it was paid in respect of the employees' obligation and it was not by way of monetary payment to the employees concerned but for or on their account to the Income-tax department. Consequently, it is a "non-monetary" payment of a perquisite to the employee which is eligible for exemption under Section 10(10CC).

Yoshio Kubo & Ors. vs Commissioner Of Income Tax (Delhi High Court) (ITA No 441/2003/Del)

This common judgment disposes a bunch of appeals in which the High Court ruled on a number of issues related to expatriate employees. The ruling includes:

- Amounts paid by the employer, directly to the Indian income tax authorities, in discharge of an employee's income tax liability do not fall into the category of monetary benefits. Hence, the same is eligible for exemption under Section 10(10CC) of the ITA.
- Employer contributions to overseas social security, pension and medical insurance plans are not taxable if such contribution does not result in any direct present benefit to the employee but assures him/her of a future benefit subject to certain contingencies.
- Tax paid the by employer is excluded from the definition of salary for the purpose of valuing accommodation benefits provided by the employer.
- A deduction on account of hypothetical taxes is allowed from the salary income of employees covered under the employer's tax equalization policy.
- A refund of excess tax ultimately due to the employer is not treated as a taxable benefit for the employee since the employee is obliged to repay the refund back to the employer and does not derive any benefit from it.
- Fees paid by an employer to a tax consultant for tax compliance for expatriates are not considered to be a taxable benefit.

Eli Lilly & Company (India) Pvt. Ltd. (SC) (178 Taxmann 505)

The withholding tax provisions relating to salary payments are distinct from with the withholding tax provisions on other income. If the salary paid by the foreign entity abroad was for rendition of services in India and if no work was found to have been performed for the foreign entity, such payments would be subject to withholding tax provisions in India. The Indian entity was required to comply with the withholding tax provisions even in case of salary paid overseas by the foreign entity.

Interest will be charged only in cases where no taxes have been paid on foreign salary or where there is a gap between the date on which tax was deductible and the date of actual tax remittance of salary.

British Gas India Ltd. (AAR) (285 ITR 218)

The Authorities for Advance Ruling (AAR) was of the view that the requirement under Explanation (a) to Section 6(1) of the ITA was not leaving India for employment but it was leaving India for the purposes of employment outside India and a person who was leaving India for employment outside India need not be an unemployed person in order to be entitled to claim the beneficial provisions of the said Explanation. Accordingly the salary paid by the Indian entity to such non- resident employee shall not be taxable in India, if the same has been offered for tax in the foreign country.

Gallotti Raoul vs. ACIT (Mumbai ITAT) (61 ITD 453)

Mandatory contribution by the employer towards the social security in the home country of the employee (foreign national), wherein no benefit/ right gets vested in the year of contribution should not be considered as a taxable perquisite in hands of such employee. Also see *ACIT vs. Harashima Naoki Tashio,* ITA No. 4634/Del)