RESEARCH REVIEW JOURNALS
Volume-03
Issue-12
December -2018

ISSN: 2455-3085 (Online)
RESEARCH REVIEW International Journal of Multidisciplinary
www.rrjournals.com [UGC Listed Journal]

Double Taxation Avoidance Agreement in India: Reliefs, Models and Understanding on recent Judicial Decisions

[1]Arun Kumar D, [2]Nischal Kumar K P & [3]Srikanth B

[1,2,3]B.Com F&A, Department of Professional Studies, Christ University, Karnataka (India)

ARTICLE DETAILS

Article History
Published Online: 10 December 2018

Keywords
DTAA, Bilateral relief, unilateral relief, OECD, UN Model.

ABSTRACT

This research paper is mainly related to double taxation avoidance agreement (DTAA) in which the comparison of Bilateral relief and Unilateral relief has been done based on the provisions of income tax act 1961, which are dealt under section 90, 90A and 91. We found out that there is a major difference in this kind of reliefs as it involves the application of provisions in the presence of agreement and in the absence of agreement between the Countries. Further the study was made on the models of tax convention which are majorly OECD and UN model, in which we found out that in India UN model is most preferably used when compared to the OECD Model. Also the study was conducted on the recent judicial decisions so that we can understand the complication faced by the assessee and the various ambiguity of DTAA can also be understood because of this.

1. Introduction

When an individual is resident in one country but has a source of income situated in another country it gives rise to possible double taxation. This arises from two basic rules that enables the country of residence as well as the country where the source of income exists to impose tax. This two basic rules are (i) the source rule and (ii) the residence rule. The source rule holds that the income is to be taxed in the country in which it originates irrespective of whether the income accrues to a resident or a non-resident whereas the residence rule stipulates that the power to tax should rest with the country in which the tax payer resides. For a business entity if both the rules apply simultaneously and if it suffers tax at both ends, the cost of operating on an international scale would become prohibitive and would deter the process of globalization. It is from this point of view that Double Taxation Avoidance Agreements(DTAA) become significant.

The Double Taxation Avoidance Agreement is a tax treaty signed between India and another country so that taxpayers can avoid paying double taxes on their income earned from the source country as well as the residence country. Currently, India has double tax avoidance treaties with more than 88 countries around the world.

This research paper is about mainly understanding the applicability of the double taxation avoidance agreements with various countries by referring through case studies of those countries as the provisions of DTAA are based on the particular articles as agreed with India and other countries.

2. Review of Literature

1) Double Taxation Avoidance Agreements in India (Annapurna, 2014)

In this paper the author has explained how to claim relief under double taxation avoidance agreements, based on two things i.e. 1) the country of residence. 2) The source country. The country of residence means where the assesse resides and the source country is any foreign country other than where he resides. He has also explained how DTAA works and necessity of it. The rules of the agreement depend on mutual agreement between two states, DTAA can be different from country to country. He told that double taxation can be avoided in following two ways 1) The country where the tax payer resides, can exempt the income which is coming from the foreign countries OR 2) The country where the tax payer resides, grant the credit for the tax paid in another foreign country. He has also briefed about the Double non taxation and Treaty shopping: the misuse of double taxation avoidance agreement and its analysis. Treaty shopping means when an assesse wants to do a transaction through another country which has most beneficial treaty with India in order to reduce his tax liability. Example: Indo Mauritius tax treaty.

2) A critical analysis of the concept of Double Taxation Avoidance Agreement under the income tax act, 1961 (Aayushi, 2015)

In this paper the author has explained about the historical development of Double Taxation Avoidance Agreement. He has explained the models of DTAA such as OECD, UN model. He has briefed about the provisions of DTAA under INCOME TAX act i.e. section 90 and section 91 provide specific relief to the tax payers for them to save from paying the tax twice. He has also explained about the classification, objectives, pattern and Indian policy of DTAA. The DTAA has been classified as comprehensive and limited. Comprehensive provides for taxes on income, capital gains and capital while Limited refer only to income from shipping and air Transport or estates, inheritance and gifts. He concluded that India has a comprehensive Double Taxation Avoidance agreements with several nations.

2) Trends of FDI in India : An Analytical study of 2001 - 2014 (Naveen, 2015)

In this paper the author has explained the FDI inflows on India through various countries. He said that due to DTAA; Mauritius has become most dominant source of FDI contribution in India and it's accounted for 36.25% of FDI investments. He has also tested that there is significance association between GDP and FDI in India

3) A close look into double taxation avoidance agreements with India: some relevant issues in international taxation (Sarbapriya, 2011)In this paper the author has explained about the concept of double taxation avoidance agreement i.e. an agreement entered between India and other countries so that the tax payer can avoid paying double taxes on their income earned from the source country as well as the residence country. He has also explained about the necessity and importance of DTAA. He briefed the salient features of DTAA's between India and other countries.

4) Double tax treaties and their interpretation (klaus, 1986)In this paper the author has explained many things such as the meaning of double taxation and the need of it, the circumstances giving raise to double taxation and its general rules of international law. He has briefed about the avoidance of double taxation particularly through treaties i.e.

1) Unilateral measures to avoid double taxation: Double taxation can be avoided unilaterally if one of the states involved withdraws its tax claim. On behalf of the state of residence, this unilateral move often is achieved pursuant to a method developed under Anglo-American law whereby the state of residence, to the extent it is not simultaneously the source state, allows a credit for the tax levied in the source state up to an amount equal to its own tax charge.
2) The Development of Tax Treaties Consequently, individual states have entered bilateral agreements for the avoidance of double taxation. At first, only federally related or closely allied states were involved, but following World War I an extensive treaty network developed in Central Europe. Germany entered its first double tax agreement with Italy in 1925.
3) The OECD Model, the U.S. Model, and Other Model Treaties

The efforts of the Organization of European Economic Cooperation (hereinafter the OEEC) and its successor organization, the Organization for Economic Cooperation and Development (hereinafter the OECD), to develop a system for the avoidance of double taxation picked up where the preparatory research of the League of Nations left off. The Committee on Fiscal Affairs submitted a series of model treaty articles in four interim reports between 1956 and 1961 and a summary report in 1963 to which the complete model treaty (hereinafter the OECD Model) and an official commentary (hereinafter the Commentary) were appended.

3. Research design

a) Statement Of Problem

Introduction of DTAA has a major impact on international taxation, not only it has its impact on the FDI but also in various other economic factors , but the guidelines of DTAA of various countries are complex, subjective and are different to one another. Hence, this study is done to understand the applicability of these guidelines and its impact with the help of recent judicial decisions of different countries.

b) Sources of data

The data for research has been obtained from secondary sources. The researchers have obtained the data from trusted websites. Research papers, case studies, double tax avoidance agreements and such other relevant information have been studied for the purpose of carrying out the research.

c) Data analysis tools

Researchers have used non statistical methods in studying the data. A background study has been undertaken to understand the double taxation avoidance laws. This research paper is purely prepared on a descriptive basis.

d) Expected outcome

The researchers aim to project the benefit of the tax policies under the agreement using the provisions of the legislatures and also by considering the amendments.

e) Limitations

To conduct a study on the double taxation avoidance agreements, apt data regarding the same is required. Since the data is highly confidential, obtaining the data becomes easier said than done, hence proving to be a constraint while conducting the study.

4. Analysis

❖ **Comparison of Bilateral Relief and Unilateral Relief**:

A. Bilateral relief:

When the government of two countries enter agreement to provide certain specified income so that the double taxation can be avoided by jointly working out the system to grant it.

In India Bilateral relief is provided under the section 90 and 90A of the income tax act 1961.

Bilateral relief are of mainly two types:

a) Exemption method: to mainly avoid overlapping of tax on the same income this method is used that is when India and the other country agrees that income arising on both the countries should be taxed in only one of the country or that each of the two countries should tax only a particular specified portion of the income.

b) Tax credit method: this is a type of bilateral relief where in the single taxability is not provided but some relief is provided. The assesse will be given a deduction has a relief though he is still liable to have his income taxed in both the countries.

B. Unilateral relief:

Unilateral relief is the relief provided by the home country in this case which is India irrespective of any agreement with the country concerned. Bilateral agreements are not sufficient to meet all the cases hence this kind of relief exist.

In India, section 91 of the income tax act ,1961 provides such relief, where in if section 90 does not apply for relief under section 91 will be available. Unilateral relief will be only available in respect of doubly taxed income that is part of income which is included in assessee's total income.

This can be analyzed by following situation:

A. If India is having DTAA with the other country, then tax relief can be claimed u/s 90.
B. If India is having DTAA with the specified associations, then tax relief can be claimed u/s 90A.
C. If India is having DTAA with the other country, then tax relief can be claimed u/s 91.

(A) If India is having DTAA with the other country, then tax relief can be claimed u/s 90

Steps to compute Double Taxation relief:

Step 1) Compute Global Income i.e. aggregate of Indian income and Foreign income;

Step 2) Compute tax on such global income as per the slab rates applicable;

Step 3) Compute average rate of tax (i.e. Global income divided by amount of tax);

Step 4) Compute an amount by multiplying Foreign income with such average rate of tax;

Step 5) Compute Tax paid in Foreign country

The amount of relief shall be lower of step 4 and step 5.

(B) If India is having DTAA with the specified associations, then tax relief can be claimed u/s 90A.

When a specified association in India enters into an agreement with a specified association abroad, the Central Government, may by notification adopt such agreement and provide relief under section 90A of the Income Tax Act, 1961.

The relief can be claimed only by the residents of the countries who have entered into the agreement. If resident of other countries wants to claim the relief, then they have to obtain a Tax Residence Certificate (TRC) from the government of that country.

(C) If India is having DTAA with the other country, then tax relief can be claimed u/s 91.

When there is no DTAA, relief is granted under section 91.

Steps to compute relief

Step 1) Compute tax payable in India

Step 2) Compute lower of Indian rate of tax and rate of tax in Foreign country

Step 3) Multiply the rate obtained in Step 3 by the doubly taxed income

Relief will be the amount as computed in Step 3.

In order to understand the computation, we have taken a hypothetical situation so that the benefit of this relief can be found out.

2) Model taxation conventional treaties used in DTAA of India:

In order to enable various countries, to enter into treaties, which are standardized to some extent, Organization for Economic Cooperation and Development (OECD) and the united nations (UN) have developed certain model tax treaties, which various countries can take as a starting point for negotiations between themselves and other countries. These Models are extensively used by various countries to enter into tax treaties. In some cases, they have been incorporated verbatim with minor changes. However, in other cases, countries have made suitable changes in the draft model according to their economic environment and commercial and tax considerations.

Some of this models can be understood has follows:

(A) OECD model: In 1961, the organization for economic co-operation and development (O.E.C.D) was established, with developed countries as its members, to succeed the Organization for European Economic Co-operation (O.E.E.C), and OECD approved the draft presented to the OEEC. In 1997, the final draft was prepared in the present form which has been revised several times.

OECD Model is essentially a model treaty between two developed nations.

This model advocates residence principle, that is., it lays emphasis on the right state of residence to tax the income.

(B) UN Model: the un model comprise between the source principle and the residence principle. However, it gives more weight to the source principle as against the residence principle of the OECD Model.

UN Model is designed to encourage flow of investments from the developed countries to developing countries. It takes into account sharing of tax revenue with the country providing capital.

By this analysis we found out that in India the UN Model is mainly used in the tax treaties with other countries.

3) Recent Judicial Decisions of DTAA and Its understanding:

This objective was met with reference of recent case studies which relates to DTAA of India and six different countries which these countries are mainly selected based on their FDI in India

1) MAURITIUS:

Case: JRAY McDermott Eastern Hemisphere Ltd. Vs Jt. CIT

This is mainly a case related to Permanent establishment vis-à-vis construction or assembly project.

By referring to this case we found out that during the relevant financial period, the assesse was engaged in certain installation contracts in some offshore fields in the Indian continental shelf. However, according to the assesse, the income so earned from that contracts so executed was in the nature of business profits which could be taxed only under article 7 of the convention, but existence of a permanent establishment, which is defined under the article 5 of the said

convention, was a *sine qua non (*an essential condition; a thing that is absolutely necessary.) for such a taxability. It was further found out that since the assesse did not have any such permanent establishment in India, the income of the assesse could not be brought to tax in India and article 5(2)(i) of the said convention would show that, for the purpose of computing the threshold time-limit what is to be taken into account is activities of a foreign enterprise on a particular site or a particular project, or supervisory activity connected therewith, and not on all the activities in a tax jurisdiction as a whole. It is important to bear in mind the fact that the expressions used in the relevant definition clause are in singular, and there is no specific mention about aggregating the number of days spent on various sites, projects or activities. In other words, each of the building site, construction project, assembly project or supervisory activities in connection therewith is to be viewed on standalone basis

Understanding: what is to be taken in to account is the duration of the activities of the foreign enterprise on a particular site or a particular project or supervisory activity connected therewith, on a standalone basis and not all the activities in a tax jurisdiction as a whole.

2) NETHERLAND:

Case: Universal International Music Vs Department of Income Tax

This was mainly a case related to Tax residence certificate

By this case we collected information that The assessee is a company incorporated under the laws of Netherlands. The assessee who was the tax resident of Netherlands within the meaning of Article 4 of Double Taxation Avoidance Agreement (DTAA) signed between India and Netherlands and was engaged in many business activities as per the agreement.

The AO in the assessment order observed that the concessional rate of 10% is applicable only when the assessee is beneficial owner of the royalty. The AO asked for details to claim has beneficial owner. The assessee explained that as per group policy, for any business outside the home territory of the repertoire company, the commercial exploitation rights were transferred to other group company and on request from any universal group company other group companies license the right to them to exploit the same in the home territory of the requesting company. Thus ultimately the group companies were license holders to commercially exploit the rights around the world. The assessee had given such rights of exploitation to Universal Music India Pvt. Ltd. in the Indian territory for which royalty had been received. The AO did not accept this fact and denied beneficial ownership, but at the end it was decided that based on the DTAA between India and Mauritius which it was stated that tax residence certificate issued by the tax authorities of the contracting state would be sufficient evidence for accepting the status of residence in Mauritius and for beneficial ownership. It was accordingly urged that the assessee was the beneficial owner of the royalty and the same should be taxed @ 10% under the provisions of Article 12 of DTAA.

Understanding: Tax residence certificate issued by Tax Authority of the contracting state is a sufficient evidence of the beneficial ownership of royalties.

3) SINGAPORE:

Case: **Signate Singapore Headquarters (p) ltd., in re 2010) 230 CTR 110(AAR)**

This is a case mainly related to a permanent establishment, Applicant a Singapore company having entered in to agreement with independent service providers (ISPs), in India who are obliged to make adequate space available to store applicant's products provide other facilities apart from storage, handling, repacking, etc., and deliver the goods to the customers on behalf of the applicant, as per the article 5 For the purposes of this Agreement, the term "permanent establishment" means a fixed place of business through which the business of the enterprise is wholly or partly carried on. The term 'permanent establishment" includes especially:

a. a place of management;
b. a branch;
c. an office;
d. a factory;
e. a workshop;
f. a mine, an oil or gas well, a quarry or any other place of extraction of natural resources;
g. a warehouse in relation to a person providing storage facilities for others;
h. a farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on;
i. premises used as a sales outlet or for soliciting and receiving orders;
j. an installation or structure used for the exploration or exploitation of natural resources but only if so used for a period of more than 120 days in any fiscal year.

Understanding: Permanent Establishment includes a ware house in relation to a person providing storage facilities for others so the person we will be taxed in India.

Case study on other countries has also been referred to get better understanding.

5. **Findings & Conclusion**

In India DTAA have a major role in foreign direct investments and because of which the tax treaties usually keeps changing according to the benefit of the other countries. DTAA being a part of international taxation becomes difficult for one to understand the subject as a whole. In this research paper we found out how the bilateral relief are made and what are the sections of Income Tax Act 1961 dealing with such kind of relief and also the unilateral relief and the sections dealing with Income Tax Act 1961 relating to this relief and it was possible to make comparison with this relief to know which is beneficial.

This research paper also described the different kind of model tax conventions used by different countries and in which we found out that the UN model was the one used by India for DTAA. The understanding of recent judicial decisions relating to DTAA was done in which the various applications of DTAA could be understood.

References

1. Aayushi, J. (2015). *Journal of legal studies and research* .
2. Annapurna, C. (2014 , 03 05). *https;//www. ssrn.com*.
3. klaus, V. (1986). *Berkeley Journal of International Law*.
4. Naveen, S. (2015). Trends of FDI in India : An analytical study of 2001- 2014. *International journal of commerce and management* .
5. Sarbapriya, R. (2011). Retrieved from www.iiste.org.

