# <u>Methods for elimination of double taxation</u>

- Dated: 22.09.2024
- Nalsar University of Law,Hyderabad
- IV Semester- M.A (International Taxation)


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"It was only for the good of his subjects that he collected taxes from them, just as the Sun draws moisture from the Earth to give it back a thousand fold" –

--Kalidas in Raghuvansh eulogizing KING DALIP.

*“Nothing is certain except Death and Taxes”*

# Topic Coverage

- Methods for elimination of Double taxation.
- Exemption Method and credit method.
- Operation and effects of the methods.

# Background

- ***“We all are living in a global village but are we taxed at a global level”***
- Inbound and outbound Investments (FDI, FPI, FII, FVCI, QFI).
- DTAA(Double Taxation Avoidance Agreement)
- Tax Evasion & Tax Avoidance.

# Introduction to Double taxation

- Taxing same income twice in the hands of Assesssee.

- When the **taxpayer 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 the two basic rules that enables the country of residence as well as the country where the source of income exists to impose tax namely,
- (i) the source rule and
- (ii) the residence rule.

# Source Rule & Residence Rule

- **The source rule** holds that 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 **taxpayer resides.**

# What if source & residence rule apply simultaneously?

- If both rules apply simultaneously to a business entity and *it were to suffer 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 view point that Double Taxation Avoidance Agreements (DTAA) become very significant.

- Double taxation is often an unintended consequence of tax legislation. It is generally seen as a negative element of a tax system, and tax authorities attempt to avoid it whenever possible.

# Types of Double taxation

**Types of Double Taxation**

Juridical Double Taxation

Economic Double Taxation

# <u>Juridical Double Taxation</u>

When an income is **taxed twice** in the hands of taxpayers – **once in the country of residence** and **once in the country of source**, it leads to **“juridical double taxation”**. Most of the countries majorly face double taxation on account of income being taxed in more than one country.

Example: Mr X is earning income in UK from fees from technical services and he is resident of India at the same time.

Being a resident his Income is taxable in India. (India follows residence rule to tax global Income).What are the rules in regard to residency in India?

Source of Income is in UK and the FTS is also getting taxed in UK. Source country withholds tax (TDS)

# Reasons for Juridical Double taxation

- Taxation of world-wide income of residents.
- Taxation of world-wide income of citizens.
- Deemed dual residency.
- Triangular cases.

# Taxation of world-wide income of residents

- Many countries tax the global income of its residents. This results in dual taxation of income in the hands of a taxpayer, once in the country of his residence and second time in the source country.

- ***Case Study:***

- A UK subsidiary company remits annual royalty to its Indian parent Company. The Indian Company is taxable on its global income (including royalty) in India under the residence rule and the royalty is taxable in UK under the source rule.

# Taxation of world-wide income of citizens

- Some countries tax global income of its citizens even when the citizens are residents of another country. This gives rise to double taxation, once in the country of citizenship and second in the country of residence.

- ***Case Study:***
- A US citizen who is a tax resident of India would be taxed on its global income in India based on residence rule and in the US based on his citizenship. (USA follows Citizenship rule)

# Deemed dual residency

- A person may be deemed to be a resident of more than one country and accordingly, both the countries might tax the global income of such person.

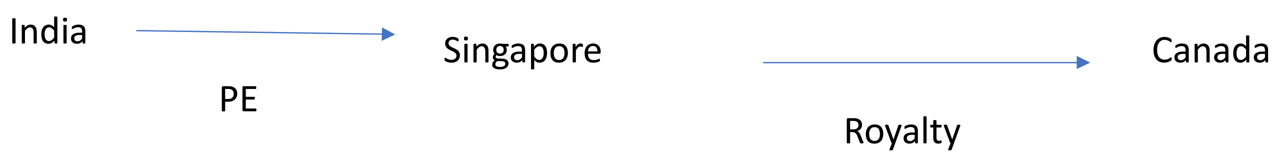
- Case Study

- A person residing in Canada relocates to India and resides in India for 182 days or more during that year, then there might be a situation where he is the resident of two countries, leading to taxation of his income in both the countries.

# Triangular cases

- Double taxation arises when two countries subject the same person, not being resident of both countries to tax on income arising in a country.

- ***Case Study:***
- A company based in India is having a Permanent establishment (PE) in Singapore. If the Singapore PE derives income from Canada, the income of the PE would be taxable in Singapore as well in Canada.



# Three Cases of Juridical Double Taxation

- The three types of Juridical Double Taxation are:

1. There are two states of residence. (Dual Residency)
2. There is a source state and state of residence. (Residence – Source)
3. There are two sources, source state and a state of residence. (Source – Source)

# Dual Residency

- It is possible to be resident for tax purposes in more than one country at the same time. This is known as dual residence; where each contracting state subjects the same person to tax on his worldwide income or capital.

- ***Case Study:***

- If you are resident in India and another country and so are liable to tax on your worldwide income in both, you have to look at the double taxation agreement between the two countries to find out where you should pay tax.

- If you have dual residence with India and another country, then a double taxation agreement should prevent you from being taxed twice on the same income. The conflict in this case is reduced by virtue of Article 4 "resident of a contracting state" of Double Taxation Agreement.

# <u>Residence - Source</u>

- ***For Individuals***:
- ***Entities to be considered a Tax Resident (Company, HUF, LLP)***

- The conflict in this case may be solved by allocation of the right to tax between the contracting states. Such allocation may be made by renunciation of the right to tax either by the state of source or situs or of the situation of the PE or by the state of residence or by a sharing of the right to tax between the two states. The provisions of the Chap III and IV of the model convention combined with the provisions of Article 23A or 23B, govern such allocation.

# Source-Source

- Where each contracting state subjects the same person, not being a resident of either contracting state to tax on income derived from, or capital owned in, a contracting state then it would amount to double taxation based on source of income.

- The conflict in this is outside the scope of the convention as under Article 1 it applies only to persons who are residents of one or both of the states. It can however be settled by applying the mutual agreement procedure.

# Economic Double Taxation

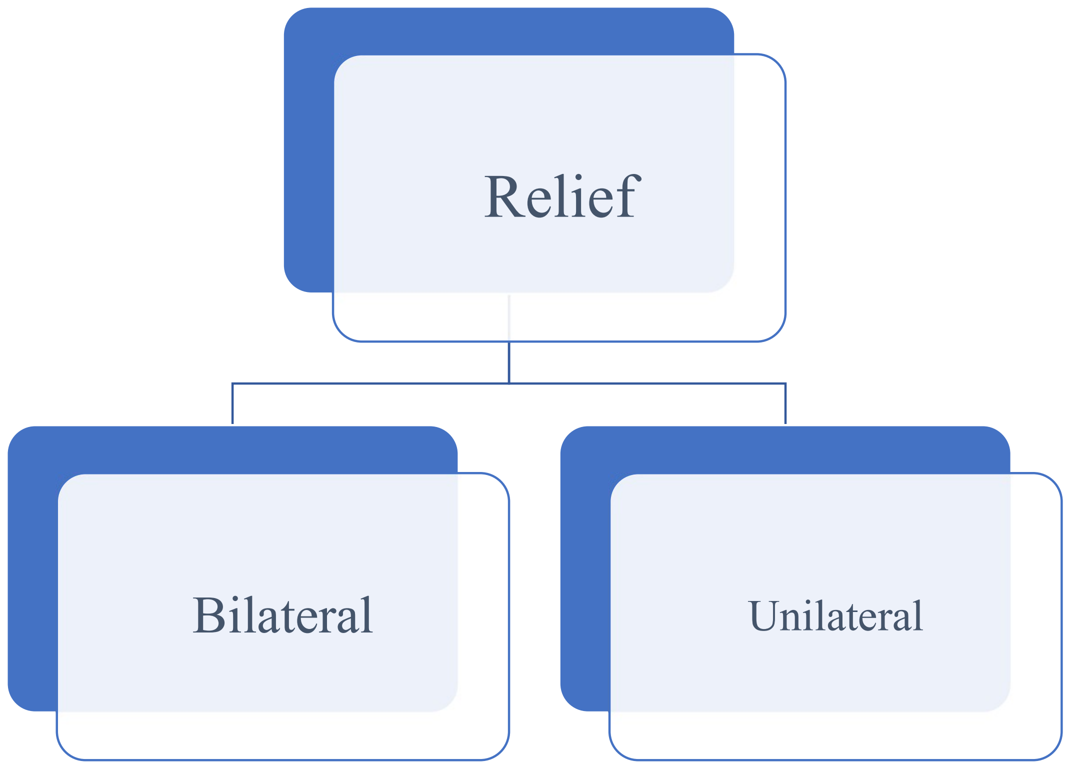
- These are situations where the same income is taxable in the hands of two taxpayers;

- **for example, dividend is taxed in the hands of the corporate as well as in the hands of the shareholder**. This kind of double taxation is known as **'economic double taxation'.**

# Elimination of Double taxation

- Double taxation means taxing the same income twice in the hands of an assessee. A particular income may be taxed in India in the hands of a person based on his/its residence. However, the same income may be taxed in his/ its hands in the source country also, as per the domestic laws of that country. This gives rise to double taxation*. It is a universally accepted principle that the same income should not be subjected to tax twice. In order to take care of such situations, the Income-tax Act, 1961 has provided for double taxation relief.*

# Types of Double Taxation Relief



# Unilateral Tax Relief: (section 91 of Income Tax Act)

- This method provides for double taxation relief unilaterally by a country to its resident for the taxes paid in the other country, ***even where no DTAA has been entered into with that country***.

- Thus, Foreign tax credit relief provided to its residents by a country under the domestic law in the absence of DTAA is referred to as Unilateral relief. ***India grants unilateral relief through credit method under section 91 to its residents for taxes paid in the country, with which India has not signed DTAA***. Such reliefs are provided to eliminate the cascading effect of double taxation.

# Unilateral Tax Relief: (section 91 of Income Tax Act)

- Unilateral relief (which is provided under section 91 of the Act) is available to a resident taxpayer who has satisfied the following conditions:

✓ earned foreign income and

✓ proves that he has suffered tax on such foreign income in any country outside India by way of deduction of tax at source or otherwise in accordance with the laws in force in that country on the same income which is subject to tax in India.

# Unilateral Tax Relief: (section 91 of Income Tax Act)

- In such a scenario, tax deduction is computed as under:
- Ascertain the amount of income which has been subject to double taxation
- On the above income which is taxed twice, tax shall be calculated at the Indian rate of tax as well as at the foreign rate of tax
- Tax relief is granted by allowing deduction from the tax liability of an amount equal to the lower of the following:
  - The amount of tax calculated at the Indian rate of tax on the doubly taxed income or
  - The amount of tax calculated at the foreign rate of tax on the doubly taxed income.
  - ***As aforesaid discussed, the provisions of the Act allow to claim credit of taxes paid in foreign country if the same income (which is taxed in foreign country) is chargeable to tax in India.***

# Unilateral tax relief- case study

- Mr.X resident of India, has received salary from country Isle of man / British Islands. India does not have signed any treaty with Isle of Man/ British islands. Tax has been deducted by Isle of Man/British Islands. Whether Mr. X can claim tax relief of taxes deducted?

# Bilateral Tax Relief (section 90 of The Income Tax Act)

- ***Under this method, the government of two countries can enter into an agreement to provide relief against double taxation by mutually working out the basis on which the relief is to be granted***.

- When two countries enter into a DTAA, then the method of relief is provided in the treaty. The treaty provides for ***the manner, mode and quantum of tax relief*** to be allowed in relation to the doubly taxed income in the hands of the taxpayer.

# Methods of claiming Tax Relief

**Exemption Method**

- A particular Income is taxed in only one of the two countries.

**Tax Credit Method**

- Income is taxable in both countries in accordance with their respective tax laws read with double taxation avoidance agreement.
- The Country of residence of the tax payer, however, allows him credit for the tax charged thereon in the country of source.

# Exemption Method

- Under this method, the residence country does not impose any taxes on the income, which may be taxed in the source country. The principle of exemption can be applied in any of the ways explained below:
- **Full exemption:** The income which may be taxed in source country is not at all considered by residence country for the purposes of its taxation. In other words, residence country, apart from exempting such income from its taxation, does not even factor such income for determining the tax on the rest of the income (viz. even for ascertaining tax slab rates etc.).
- **Exemption with progression:** As against the full exemption method, residence country retains the right to consider such income when determining the tax to be imposed on the rest of the income.

# Credit method

- Under this method, the residence country levies tax on the basis of taxpayer's total income which arises from a different source country and later, allows a deduction from its own tax for the tax paid in the other state. Contrasting to the 'exemption method' where 'income' is the subject matter, the credit method prioritizes the 'tax' on such income. The principle of credit can be applied in any of the two ways explained below:
- Full credit: Residence country allows a deduction of entire amount of tax paid in source country on such income, which is doubly taxed (i.e., in source and residence country).
- Ordinary credit: Residence country allows a deduction restricted to that part of its own tax which is appropriate to the income which may be taxed in the other State.

# Methods for the elimination of double taxation

- Article 23 of the UN and OECD Model Tax Conventions respectively provides two alternatives to eliminate double taxation → Exemption method and Credit method
- Under these methods, the residence country is obligated to eliminate double taxation
- Under the **exemption method**, the foreign income is exempt from taxation in the residence country.
- Under the **credit method**, the residence country first determines the income-tax payable on global income and then provides a credit or deduction from its income-tax for income-tax paid in the foreign country
- DTAAs provide the mechanism to eliminate double taxation of the same income in two countries (bilateral relief)
- In addition, many countries provide unilateral relief from double taxation through domestic tax law. India provides unilateral relief through sec 91 of Income-taxAct, 1961
- A claim for refund of taxes in the source country is not elimination of double taxation, but refund of excess income-tax paid

# Case Study

- The total income of Mr. A, resident in India is INR 10,00,000/- comprising of
- Salary earned in India - INR 7,50,000/-
- Dividend income from UK Co. - UKP 2500 (Consider 1 UKP as INR 100)
- In India, the rate of tax on an income of INR 10,00,000/- is 30% and on an income of INR 7,50,000/- is 20%.
- In UK, the rate of tax is 40%.

# Solution to case study: Full exemption method

| Particulars | Amount |
|---|---|
| Income taxable in the source Country(UK) | 2,50,000 |
| Applicable tax rate | 40% |
| Taxes payable in UK | 1,00,000 |
| | |
| Income taxable in Residence Country(India) | 7,50,000 |
| Applicable tax rate | 20% |
| Taxes payable in India | 1,50,000 |
| | |
| Total taxes payable | 2,50,000 |

# Solution: Exemption with progression

| Particulars | Amount |
| --- | --- |
| Income taxable in the source Country(UK) | 2,50,000 |
| Applicable tax rate | 40% |
| Taxes payable in UK | 1,00,000 |
| | |
| Income taxable in Residence Country(India) | 7,50,000 |
| Applicable tax rate | 30% (for tax rate income is Rs.10,00,000) |
| Taxes payable in India | 2,25,000 |
| | |
| Total taxes payable | 3,25,000 |

# Full credit method

| Particulars | Amount |
|---|---|
| Income taxable in the source Country(UK) | 2,50,000 |
| Applicable tax rate | 40% |
| Taxes payable in UK | 1,00,000 |
| | |
| Income taxable in Residence Country(India) | 10,00,000 |
| Applicable tax rate | 30% |
| Taxes payable in India | 3,00,000 |
| Less: Full tax credit | (1,00,000) |
| Tax payable in India | 2,00,000 |
| Total taxes payable | 3,00,000 |

# Ordinary credit Method

| Particulars | Amount |
|---|---|
| Income taxable in the source Country(UK) | 2,50,000 |
| Applicable tax rate | 40% |
| Taxes payable in UK | 1,00,000 |
| | |
| Income taxable in Residence Country(India) | 10,00,000 |
| Applicable tax rate | 30% |
| Taxes payable in India | 3,00,000 |
| Less: tax credit | (75,000)<br>#2,50,000*30% |
| Net tax payable in India | 2,25,000 |
| Total taxes payable | 3,25,000 |

# Special forms of tax credit

- **Underlying tax credit:**
- Ordinarily, Foreign tax credit is allowed in the residence country in respect of taxes paid in source country *as agreed mutually between them, which will mitigate juridical double taxation*. On the other hand, a predominant way of elimination of economic double taxation is by granting ‘Underlying tax credit’. As already discussed, economic double taxation arises when the same income is subjected to tax in the hands of different persons in two different countries. A classic example is the taxation of business profits in the hands of company and taxation of dividends paid out of such profits in the hands of shareholders, which gives rise to double taxation of the same profits. Such scenario is avoidable by inclusion of UTC clause in DTAAs

# Case study: Underlying tax credit

- Blue Ray Co., is a company incorporated in UK. The company earned a profit of INR 100 crores for the FY 2021-22, which is subjected to a corporate tax rate of 20%. The company distributed entire profits available after taxes as dividends to its shareholders, resident in India. The tax rate for dividends in UK and India is 10% and 20% respectively. India-UK DTAA provides for the benefit of UTC. Now, the effect of UTC can be evidenced by comparing the Effective tax payable under situations - with UTC and without UTC as tabulated below

| Particulars | Without UTC | With UTC |
|---|---|---|
| Profits earned by Blue Ray Company (In UK) | 100 | 100 |
| Less: Corporate tax | (20) | (20) |
| Distributable profits | 80 | 80 |
| Profits distributed as dividends | 80 | 80 |
| Less: taxes at UK @10% | (8) | (8) |
| Amount paid to shareholders | 72 | 72 |
| | | |

| Particulars | Without UTC | With UTC |
|---|---|---|
| Amount received by SH in India | 72 | 72 |
| Less: taxes paid in India @20% | (16) | (16) |
| Add: ordinary tax credit | 8 | 8 |
| Add: UTC | 0 | 8(upto 20 of corporate tax) |
| Amount available in hands of SH | 64 | 72 |
| Taxes paid | 36 | 28 |

# Tax Sparing (tax credit method)

- Another special form of tax credit that can be evidenced from DTAAs is 'Tax sparing credit'. The idea behind its introduction is to provide economic incentives for investing in developing nations. Such provision in a tax treaty *allows FTC for the taxes that have been 'spared' under the incentive programme of the source country*. (like 80IAB and other SEZ incentives)
- For instance, the residence country will allow as a deduction the amount of tax which the source country could have imposed in accordance with its local laws even if source country has waived all/ part of that tax under special provisions for the promotion of its economic development, similar to tax holiday regimes.
- Indian tax treaties with various jurisdictions such as Australia, Belgium, Bangladesh, Canada, Malaysia, Singapore, Philippines, Russia, Oman, Jordan etc. have a provision of claiming tax sparing credit.

# Case study- tax sparing

- Seashore Limited, a company incorporated in India has set up a branch office in tax free zone in Russia, by virtue of which no income taxes are payable in Russia. The branch earned a profit of 1,000,000 Russian Rubles (1 Russian Ruble = INR 1.20). The tax rate in Russia and India is 13% and 25% respectively. The tax sparing credit shall be computed by reference to the Article 23 - METHODS OF ELIMINATION OF DOUBLE TAXATION of India – Russia DTAA:

# Solution to tax sparing credit case study

- Foreign taxes deemed to be paid = (INR 12,00,000 * 13%) – (INR 12,00,000 * NIL) = INR 1,56,000/-

- Indian taxes payable = INR 12,00,000 * 25% = INR 3,00,000/-

- Tax sparing credit (Lower of the above) = INR 1,56,000/

# International concepts to relieve double tax – Exemption Method

| | Art 23A(1) Exemption | Art 23A(2) Exemption | Art 23A(3) & (4) Exemption |
|---|---|---|---|
| UN MODEL | ..resident of a Contracting State derives income or owns capital which may be taxed in the other Contracting State, in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the first-mentioned State **shall, subject to the provisions of paragraphs 2 and 3, exempt such income or capital from tax**.. | ..resident of a Contracting State derives items of income which, in accordance with the provisions of Articles 10, 11, 12, and 12A may be taxed in the other Contracting State, the first-mentioned State shall allow as a deduction from the tax on the income of that resident an amount equal to the tax paid in that other State. Such deduction **shall not, however, exceed that part of the tax, as computed before the deduction is given, which is attributable to such items of income which may be taxed in that other State**.. | ..income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital. ..paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of this Convention **to exempt such income or capital from tax or** applies the provisions of paragraph 2 of Article 10, 11, 12 or 12A to such income; in the latter case, the first-mentioned State **shall allow the deduction of tax provided for by paragraph 2..** |
| OECD MODEL | ..a resident of a Contracting State derives income or owns capital which may be taxed in the other Contracting State in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the firstmentioned **State shall, subject to the provisions of paragraphs 2 and 3, exempt such income or capital from tax**.. | ..a resident of a Contracting State derives items of income which may be taxed in the other Contracting State in accordance with the provisions of Articles 10 and 11 (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State), the firstmentioned State **shall allow as a deduction from the tax on the income of that resident an amount equal to the tax paid in** that other State. Such deduction shall not, however, exceed that part of the tax, as computed before the deduction is given, which is attributable to such items of income derived from that other State.. | ..income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital.....provisions of paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of this Convention to **exempt such income or capital from tax or applies the provisions of paragraph 2 of Article 10 or 11 to such income**.. |

## International concepts to relieve double tax – Credit Method

| | Art 23B(1) Credit | Art 23B(2) Credit |
|---|---|---|
| **UN MODEL** | ..a resident of a Contracting State derives income or owns capital which **may be taxed in the other Contracting State**, in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the first mentioned State shall allow: (a)as a deduction from the tax on the income of that **resident an amount equal to the income tax paid in that other State;** (b) as a deduction from the tax on the capital of that **resident, an amount equal to the capital tax paid in that other State..** | ..any provision of this Convention, income derived or capital owned by a resident of a Contracting State is **exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital..** |
| **OECD MODEL** | ..resident of a Contracting State derives income or owns capital which **may be taxed in the other Contracting State** in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the firstmentioned State shall allow: a)as a **deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State;** b) as a **deduction from the tax on the capital of that resident, an amount equal to the capital tax paid in that other State**.. | ..income derived or capital owned by a resident of a Contracting State is **exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital.**. |

# Rule 128 of The Income Tax Rules 1962

- **128.** *(1) An assessee, being a resident shall be allowed a credit for the amount of any foreign tax paid by him in a country or specified territory outside India, by way of deduction or otherwise***, in the year in which the income corresponding to such tax has been offered to tax or assessed to tax in India***, in the manner and to the extent as specified in this rule :*
- **Provided** *that in a case where income on which foreign tax has been paid or deducted, is offered to tax in more than one year, credit of foreign tax shall be allowed across those years in the same proportion in which the income is offered to tax or assessed to tax in India.*
- *(2) The foreign tax referred to in sub-rule (1) shall mean,—*
- (a) *in respect of a country or specified territory outside India with which India has entered into an agreement for the relief or avoidance of double taxation of income in terms of section 90 or section 90A, the tax covered under the said agreement;*
- *(b) in respect of any other country or specified territory outside India, the tax payable under the law in force in that country or specified territory in the nature of income-tax referred to in clause (*iv*) of the* Explanation *to section 91.*

# Rule 128

- *(3) The credit under sub-rule (1) shall be available against the amount of tax, surcharge and cess payable under the Act* ***but not in respect of any sum payable by way of interest, fee or penalty.***
- *(4) No credit under sub-rule (1) shall be available in respect of* ***any amount of foreign tax or part thereof which is disputed in any manner by the assessee:***
- **Provided** *that the credit of such disputed tax shall be allowed for the year in which such income is offered to tax or assessed to tax in India if the assessee* ***within six months*** *from the* ***end of the month*** *in which the dispute is finally settled, furnishes evidence of settlement of dispute and an evidence to the effect that the liability for payment of such foreign tax has been discharged by him and furnishes an undertaking that no refund in respect of such amount has directly or indirectly been claimed or shall be claimed.*

# Rule 128

- *(5) The credit of foreign tax shall be the aggregate of the amounts of* ***credit computed separately for each source of income*** *arising from a particular country or specified territory outside India and shall be given effect to in the following manner:—*
- *(i) the credit shall be the lower of the tax payable under the Act on such income and the foreign tax paid on such income :*
- **Provided** *that where the foreign tax paid exceeds the amount of tax payable in accordance with the provisions of the agreement for relief or avoidance of double taxation, such excess shall be ignored for the purposes of this clause;*
- *(ii) the credit shall be determined by conversion of the currency of payment of foreign tax at the telegraphic transfer buying rate on the last day of the month immediately preceding the month in which such tax has been paid or deducted*

# Rule 128

- *(6) In a case where any tax is payable under the provisions of section 115JB or section 115JC, the credit of foreign tax shall be allowed against such tax in the same manner as is allowable against any tax payable under the provisions of the Act other than the provisions of the said sections (hereafter referred to as the "normal provisions").*
- *(7) Where the amount of foreign tax credit available against the tax payable under the provisions of section 115JB or section 115JC exceeds the amount of tax credit available against the normal provisions, then while computing the amount of credit under section 115JAA or section 115JD in respect of the taxes paid under section 115JB or section 115JC, as the case may be, such excess shall be ignored.*

# Rule 128

- *(8) Credit of any foreign tax shall be allowed on furnishing the following documents by the assessee, namely:—*
- (i) a ***statement of income from the country*** *or specified territory outside India offered for tax for the previous year and of foreign tax deducted or paid on such income in* ***Form No.67*** *and verified in the manner specified therein;*
- *(ii)* ***certificate or statement specifying the nature of income*** *and* ***the amount of tax deducted*** *therefrom or paid by the assessee,—*
- *(a) from the tax authority of the country or specified territory outside India or*
- *(b) from the person responsible for deduction of such tax*
- *(c)* ***signed by the assessee***
- *Provided that the statement furnished by the assessee in clause (c) shall be valid if it is accompanied by:*
- *(A)* ***an acknowledgement of online payment or bank counter foil or challan for the payment of tax where payment has been made by the assessssee***
- ***(B) proof of deduction where tax has been deducted.***

# Rule 128

- [*(9) The statement in Form No. 67 referred to in clause (*i*) of sub-rule (8) and the certificate or the statement referred to in clause (*ii*) of sub-rule (8) shall be* ***furnished on or before the end of the assessment year relevant to the previous year*** *in which the income referred to in sub-rule (1) has been offered to tax or assessed to tax in India and the return for such assessment year has been furnished within the time specified under sub-section (1) or sub-section (4) of section 139:*
- **Provided** *that where the return has been furnished under sub-section* ***(8A) of section 139(updated return)****, the statement in Form No. 67 referred to in clause (*i*) of sub-rule (8) and the certificate or the statement referred to in clause (*ii*) of sub-rule (8) to the extent it relates to the income included in the updated return, shall be* ***furnished on or before the date on which such return is furnished****.*]
- *(10) Form No.67 shall also be furnished in a case where the* ***carry backward of loss of*** *the current year results in refund of foreign tax for which credit has been claimed in any earlier previous year or years.*
- *Explanation.—For the purposes of this rule 'telegraphic transfer buying rate' shall have the same meaning as assigned to it in Explanation to rule 26.***]**

**FORM NO. 67**

[*See* rule 128]

**Statement of income from a country or specified territory outside India and Foreign Tax Credit**

**PAQRT A**

1. Name of the assessee ..........................................................................................
2. *Permanent Account Number or Aadhaar Number* | | | | | | | | | | |
3. Address ..........................................................................................
..........................................................................................
4. Assessment year ..........................................................................................
5. Details of income from a country or specified territory outside India and Foreign Tax Credit claimed

| *Sl. No.* | *Name of the country/ specified territory* | *Source of income* | *Income from outside India* | *Tax paid outside India* | | *Tax payable on such income under normal provisions in India* | *Tax payable on such income under section 115JB/JC* | *Credit claimed under section 90/90A* | | | *Credit claimed under section 91 Amount* | *Total foreign tax credit claimed* |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | *Amount* | *Rate* | | | *Article No. of Double Taxation Avoidance Agreements* | *Rate of tax as per Double Taxation Avoidance Agreements* | *Amount* | | |
| (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) | (11) | (12) | (13) |
| | | Salary | | | | | | | | | | |
| | | House property | | | | | | | | | | |
| | | Business/ professional income | | | | | | | | | | |
| | | Long term capital gain | | | | | | | | | | |
| | | Short term capital gain | | | | | | | | | | |
| | | Interest income | | | | | | | | | | |
| | | Dividend | | | | | | | | | | |
| | | Royalty not being part of business income | | | | | | | | | | |
| | | Fees for technical services not being part of business income | | | | | | | | | | |

**PART B**

| | | |
|---|---|---|
| 1.(*a*) | Whether any refund of foreign tax has been claimed in any prior accounting year as a result of carry backward of losses | Yes/No |
| (*b*) | If reply to (*a*) above is Yes, furnish the following details:— | |
| (*i*) | the accounting year to which such loss pertains | ............ |
| (*ii*) | the accounting year(s) in which set off of carry backward of loss has been undertaken | ............ |
| (*iii*) | refund claimed for the accounting year(s) | ............ |
| (*iv*) | previous year to which refund referred to in (*iii*) relates | ............ |
| 2.(*a*) | Whether credit for any foreign tax has been claimed which is under dispute | Yes/No |
| (*b*) | If reply to (*a*) above is Yes, furnish the following details:— | |
| (*i*) | the nature and amount of income in respect of which tax is disputed | ............ |
| (*ii*) | the amount of such disputed tax | ............ |

***Verification***

I, ............................................................ son/daughter of .............................................................., holding [*Permanent Account Number or Aadhaar Number*] .............................. solemnly declare that to the best of my knowledge and belief, the information given in Part A and Part B of the statement above is correct and complete and is truly stated.

I further declare that I am making this statement in my capacity as ......................... and I am also competent to make this statement and verify it.

Verified today the .................. day of .................. 20 ..........

Place: ......................

*(Signature)*

**Note:** Attach certificate or statement and proof of payment/deduction of foreign tax as referred to in clause (*ii*) of sub-rule (8) of rule 128.

# Carry backward of losses

- Some countries provide for carry backward of losses. For instance, Netherlands provide for carry backward of losses for one year; USA provides for carry backward of losses for upto 2 years. Where carry backward of losses of current year in source country results in refund of foreign tax paid in prior years, which has been claimed as FTC in India, Form 67 shall be filed.

# Carry backward of losses

- Glass Ltd., a company incorporated in India (Residence country), has a branch office in USA (source country), which earned income/ incurred losses as tabulated below:

| Year | Income/(loss) | Tax paid |
|---|---|---|
| Year 1 | $10,00,000 | $2,50,000 |
| Year 2 | ($15,00,000) | NIL |

- In Year 1, the company paid taxes in USA of $ 250,000 and claimed the same as FTC in its tax return filed in India. Later, the company opted to carry back the losses incurred in Year 2 for set off against Year 1 and claimed a refund of $ 250,000 in USA. In this case, the company has claimed a refund of taxes paid in USA, while also claiming FTC in India, which amounts to double deduction. Hence, Form 67 is required to be filed in India, mentioning the details of carry backward of losses. While the rule mandates filing of Form 67 in the year in which such carry forward of losses is claimed/ opted (viz. in Year 2), the provisions of the Act is silent on the year in which such FTC shall have to be claimed. Practically, it might be simpler in offering FTC claimed to tax in year 2, rather than year 1 (where due date for filing revised return could have elapsed).

# Case study

**Mr. Krishna, a citizen of Country X, stays in India during the months of April to August and in Country X during the months September to March every year. As per the domestic laws of Country X, an individual has to stay in Country X for 200 days to be treated as a resident of that country.**

**India has a DTAA with Country X in line with UN Model Convention, 2017.**

**Krishna owns immovable properties (including residential house) in both India and Country X. He earned income of Rs. 72 lakhs from coffee estates in the Country X during the financial year 2021-22. He does not have any business in India; nor does he have any permanent establishment in India. He sold a house property situated in Country X which had resulted in short-term capital gain of Rs. 15 lakhs during the year to him and was subject to tax in Country X. He also has a residential house at Pune which was used by him for his stay when he visits India.**

**Determine the residential status of Mr. Krishna for A.Y. 2022-23 and examine with reasons as to whether the business income arising in Country X from the coffee estate and the capital gains in respect of sale of the property situated in Country X can be taxed in India in the hands of Mr. Krishna during the A.Y. 2022-23.**

# Solution to case study

- Section 90(2) provides that where the Central Government has entered into an agreement with the Government of any other country for granting relief of tax or for avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of the Income-tax Act, 1961 shall apply to the extent they are more beneficial to that assessee. In effect, the provisions of the Income-tax Act, 1961 or the DTAA, whichever is more beneficial would be applicable.
- First of all, we have to determine Mr. Krishna's residential status under the provisions of the Income-tax Act, 1961 for A.Y. 2022-23. He stays in India for 153 days in each previous year and for 612 days (153 days x 4) in aggregate in the four immediately preceding previous years. Since he stays in India for a period of 60 days or more in the P.Y. 2021-22 and a total period of 365 days or more during the four immediately preceding previous years, he is resident in India as per the provisions of section 6(1) of the Income-tax Act, 1961 for A.Y. 2022-23.

- Krishna is resident in India in all the ten immediately preceding previous years (P.Y. 2011-12 to P.Y. 2020-21) and his stay in India in the seven immediately preceding previous years (i.e., from P.Y. 2014-15 to P.Y. 2020-21) is 1071 days. Accordingly, since he is resident in all the ten immediately preceding previous years and his stay in India in the seven immediately preceding previous years exceeds 729 days, Krishna would be resident and ordinarily resident for A.Y.2022-23 under the provisions of the Income-tax Act, 1961,

- Krishna is also a resident in Country X in the P.Y. 2021-22, since he has stayed there for 212 days in that previous year. Since his stay in Country X exceeds 200 days, he is a resident in Country X as per the domestic laws of that country. Thus, Krishna is a resident of India as well as Country X in the P.Y. 2021-22, as per the domestic laws of the respective countries.

- India's DTAA with Country X is based on UN Model Convention. Article 4(2) of the India Country X DTAA provides that where an individual is a resident of both India and Country X, he shall be deemed to be resident of that country in which he has a permanent home and if he has a permanent home in both the countries, he shall be deemed to be resident of that country, which is the centre of his vital interests i.e., the country with which he has closer personal and economic relations.

- Krishna has residential houses both in India and in Country X. Thus, he has a permanent home in both the countries. Krishna owns coffee estates in Country X from which he derives business income. He has no business or permanent establishment of his business in India. Therefore, his personal and economic relations with Country X are closer, since Country X is the place where –
- (a) the property is located and
- (b) the business of coffee estates is being carried on.

- Therefore, he shall be deemed to be resident of Country X for A.Y. 2022-23.

- The facts of the case and issues arising there from are similar to that of **CIT vs. P.V.A.L. Kulandagan Chettiar (2004) 267 ITR 654**, where the Supreme Court held that if an assessee is deemed to be a resident of a Contracting State where his

- personal and economic relations are closer, then in such a case, the fact that he is a resident in India to be taxed in terms of sections 4 and 5 of the Income-tax Act, 1961 would become irrelevant, since the DTAA prevails over sections 4 and 5.

- However, as per section 90(4), in order to claim relief under the agreement, Krishna has to obtain a certificate [Tax Residency Certificate (TRC)] declaring that he is a resident of Country X from the Government of Country X. Further, he also has to provide such other documents and information, as may be prescribed.

- Therefore, in this case, Krishna would not be liable to income tax in India A.Y. 2022-23 in respect of business income and capital gains arising in Country X provided he furnishes the Tax Residency Certificate and such other documents and information as may be prescribed.

# Case study

- Mr. Hari, a resident Indian aged 37 years is a salaried employee employed with Delta P Ltd. He received the following components of his salary income during the previous year 2021-22.
- Basic Salary Rs. 60,000 p.m.
- Dearness allowance 12% of basic salary
- Transport allowance Rs. 10,000 p.m.
- Medical allowance Rs. 5,000 p.m.
- He contributed Rs. 18,000 to approved approved Pension Fund of LIC. He also paid Rs. 2,00,000 by crossed cheque for mediclaim premium to insure the health of his mother, a resident aged 61 years, who is not dependent on him as a lumpsum payment for 5 years including the current previous year.
- He also delivered guest lectures in a reputed university in Country X during the year. He received Rs. 8,00,000 from such university after deduction of tax of Rs. 2,00,000 in Country X. India does not have any double taxation avoidance agreement under section 90 of the Income-tax Act, 1961, with Country X. Compute the tax liability of Mr. Hari for the A.Y. 2022-23, assuming that he does not opt for section 115BAC for A.Y 2022-23?

| Particulars | Rs. | Rs. |
|---|---|---|
| **Salaries [Indian Income]** | | |
| Basic Salary (Rs. 60,000 * 12 months) | 7,20,000 | |
| Dearness Allowance<br>(12% of Basic Salary of Rs. 7,20,000) | 86,400 | |
| Transport Allowance (Rs. 10,000 * 12) (Fully Taxable) | 1,20,000 | |
| Medical Allowance (Rs. 5,000 * 12) (Fully Taxable) | 60,000 | |
| **Gross Salary** | **9,86,400** | |
| *Less:* Standard Deduction u/s. 16(ia)<br>*Lower of actual salary or Rs. 50,000* | 50,000 | |
| **Net Salary** | | 9,36,400 |
| **Income from other sources [Foreign Income]** | | |
| Income from lectures in foreign university<br>[Rs. 8,00,000 plus tax deducted at source of Rs. 2,00,000] | | 10,00,000 |
| **Gross Total Income** | | **19,36,400** |
| ***Less:* Deduction under Chap VIA** | | |
| **Under section 80CCC –** Contribution to approved Pension Fund of LIC | 18,000 | |
| **Under section 80D –** Medical Insurance premium of mother, being a senior citizen for the year 20-21<br>Rs. 40,000 [being 1/5$^{th}$ of the lumpsum premium of Rs. 2,00,000 paid for 5 years] fully allowable, even though she is not dependent on him, since the same does not exceed Rs. 50,000 | 40,000 | 58,000 |
| **TOTAL INCOME** | | **18,78,400** |

# Computation of tax liability of Mr.Hari for AY 2022-23

| Particulars | | Rs. |
|---|---|---|
| Tax on Total Income [Rs. 2,63,520 (i.e., 30% of Rs. 8,78,400) plus Rs. 1,12,500 (Tax on income of Rs. 10 Lakhs)] | | 3,76,020 |
| Add: Health and education cess @ 4% | | 15,041 |
| Tax Liability | | 3,91,061 |
| Average rate of tax in India [i.e., Rs. 3,91,061 / Rs. 18,78,400 * 100] | 20.82% | |
| Tax rate in Country X [200,000/10,00,000]*100 | 20% | |
| **Deduction under section 91** on Rs. 10,00,000 being the doubly taxed income @ 20% [being the lower of Indian rate of tax (20.82%) and Country X tax rate (20%)] | | 2,00,000 |
| **Tax Payable** | | **1,91,061** |
| Tax Payable (rounded off) | | 1,91,060 |

# MLI(Multilateral Instrument & DTAA)

- Under the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), more than 145 countries have collaborated to put an end to tax avoidance strategies that exploit gaps and mismatches in tax rules to avoid paying tax
- Multilateral Instrument (MLI) is an outcome of BEPS Action Plan 15. MLI allows governments to modify existing bilateral tax treaties in a synchronised and efficient manner without the need to renegotiate each treaty bilaterally
- MLI, ratified by the Indian government, enters into force for India from 01.10.2019 and is effective for 93 Indian bilateral tax treaties
- Article 5 of MLI recommends three options for elimination of double taxation. Options A and B modifies the application of the exemption method to prevent double non-taxation.
- "Option C" prescribes application of ordinary credit method. India has chosen to apply Option C (i.e., credit method) to all its Covered Tax Agreements for its own residents • India's DTAAs with Bulgaria, Egypt, Greece and Slovak Republic contains exemption method. It is to be replaced by "credit method"

# Conclusion

- Whether FTC is allowed from MAT (Minimum Alternate tax)?
- What about EQL (Equilisation levy)?
- Whether foreign tax credit is given at the time of issuance of Form 16?
- Foreign tax credit – Residence country
- Beneficial to assessee
- Form 67 compliances


Best Regards:

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