

**Provisions of Income-tax Act,
1961 relevant to International Tax
in India & some basic concepts of
International Taxation**

SECTION 5 & 7

- Global income of a **“tax resident”** is taxable in India. It includes income received or accrued or arising or deemed to be received or accruing or arising in India and also includes income accruing or arising outside India.
- Whereas a non resident is liable to pay tax only on income received or accrued or arising or deemed to be received or accruing or arising in India.
- However, in the case of a person not ordinarily resident in India, the income which accrues or arises to him outside India shall not be so included unless it is derived from a business controlled in or a profession set up in India.
- The incomes deemed to be received in the previous year includes the annual accretion in the previous year to the balance at the credit of an employee participating in a recognised provident fund, to the extent provided in rule 6 of Part A of the Fourth Schedule, the transferred balance in a recognised provident fund, to the extent provided in sub-rule (4) of rule 11 of Part A of the Fourth Schedule & the contribution made, by the Central Government or any other employer in the previous year, to the account of an employee under a pension scheme referred to in section 80CCD.

Section 6 – RESIDENCE IN INDIA

- An individual is tax resident in India in any previous year, if –
 - ❖ is in India for 182 days or more; or
 - ❖ Having been in India in the PY for 60 days or more and for 365 days or more within 4 years preceding the PY. However if a citizen of India has left India as crew member of Indian ship or *for the purposes of employment outside India*, than 60 days will be substituted by 182 days. Similarly if a citizen of India or Person of Indian Origin who is outside India and comes on visit to India in any PY, than 60 days will be substituted by 182 days. W.e.f. 01.04.21, if the aforesaid visitor to India earn more than Rs. 15 lakhs excluding the income from foreign source than 120 days will replace 60 days.
 - ❖ W.e.f. 01.04.21, an individual, being a citizen of India, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the PY shall be deemed to be resident in India in that previous year, if he is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature;
- A HUF, firm or AOP non resident, if control and management of its affairs is situated wholly outside India.

Section 6 – RESIDENCE IN INDIA

- A company is said to be resident in India in any PY, if
 - ❖ It is an Indian company; or
 - ❖ Its place of its place of effective management, in that year, is in India. "Place of effective management" means a place where key management and commercial decisions that are necessary for the conduct of business of an entity as a whole are, in substance made.
- An individual or HUF is said to be "not ordinarily resident" in India in any PY if that individual or manager of HUF has been a non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less. W.e.f. 01.04.2021, an Indian Citizen or Person of Indian origin having income exceeding 15 lakhs in the previous year excluding the foreign source of Income, who is in India for more than 120 days but less 182 days in a year is a non ordinary resident and a deemed resident shall also be a non ordinary resident.

Section 9 –Income deemed to accrue or arise in India

- All income accruing or arising, whether directly or indirectly, through or from any *business connection in India*, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India shall be deemed to accrue or arise in India.
- The concept of business connection has been in existence since the commencement of the Act though there is no definition of the same therein.
- Effective April 2004 an Explanation was introduced to clarify that the term business connection shall include any business activity carried out through a person, who acting on behalf of the non-resident, has and habitually exercises in India an authority to conclude contracts on behalf of the non-resident or maintains in India stock of goods which he delivers on behalf of the non-resident or habitually secures in India orders mainly or wholly for the non-resident.
- An exception was also carved out that if the activities of such agent was limited to the purchase of goods or merchandise for the non-resident, the same will not be covered under the ambit of business connection.
- In the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India.

BUSINESS CONNECTION

- The Central Board of Direct Taxes had issued a Circular No. 23 on 23rd July 1969 regarding taxability of income accruing or arising through, or from, business connection in India to a non-resident, under section 9 of the Income-tax Act, 1961 which has been withdrawn by Circular No. 7/2009, dated 22-10-2009. Some illustrative instances of a non-resident having business as per circular are given below :
 - (a) Maintaining a branch office in India for the purchase or sale of goods or transacting other business.
 - (b) Appointing an agent in India for the systematic and regular purchase of raw materials or other commodities, or for sale of the non-resident's goods, or for other business purposes.
 - (c) Erecting a factory in India where the raw produce purchased locally is worked into a form suitable for export abroad.
 - (d) Forming a local subsidiary company to sell the products of the non- resident parent company.
 - (e) Having financial association between a resident and a non-resident company.

BUSINESS CONNECTION

- It is frequently argued that the legislature has deliberately not chosen the words to define this concept to keep this phrase wide open for uncertain import. *Hira Mills Ltd. v. I.T.O.* [1946] 14 ITR 417 (All.); *Bangalore Woollen, Cotton & Silk Mills Co. Ltd. v. CIT* [1950] 18 ITR 423 (Mad.).
- Various court rulings including the Supreme Court have interpreted this term considering *the facts and circumstances of a given case*.
- **Tax Treaty position**
- The business presence equivalent in a Tax Treaty is the Permanent Establishment concept.
- **General attributes of a BC**
 - ❖ Real and intimate connection - something more than the sale or purchase of goods is required.
 - ❖ Common control .
 - ❖ The non-resident performing some well-defined business operation in India which contributes directly or indirectly to the earnings of the non-resident.
 - ❖ Continuity – A continuity of relationship and not a mere isolated or stray nexus between the business of the non-resident outside India and the activity in India.

BUSINESS CONNECTION

- An analogous provision in Section 42 of the IT Act, 1922 contemplated 'business connection. The Hon'ble Supreme Court in the case of **C.I.T. v. R.D. Aggarwal & Co. AIR 1965 SC 1526** observed that connotation of 'business income' had to be determined on the facts and circumstances of each case and asserted it something more than the understanding of the term 'Business' as provided in the Act.
- In this case, the assessee RD Aggarwal & Co., was involved with Italy-Belgium settled non-resident exporters as importers and commission agents. It was held that there was no business connection because RD was not authorized to accept orders but was canvassing orders in taxable territories for the other party and no operations like arranging raw material or manufacturing of finished product executed within the taxable territories, the Court interpreted 'business connection' comprehensively and laid down conditions to constitute a business as under-
 - ❖ An element of Continuity;
 - ❖ Facts and circumstances of each case determinative of the existence of Business connection;
 - ❖ Real and intimate connection.

BEPS AND MLI

- In this world of digital economy, the conventional manner of doing business has changed significantly. We are in the age of technological advancement where exists no boundaries. Internet, e-commerce, smart phones etc. have changed the way of doing business.
- In current age taxation based on physical presence results in no or low taxes for such digital businesses.
- Base Erosion and Profit Shifting (BEPS) action plan 15, under the Organisation for Economic Co-operation and Development (OECD) /G20 framework introduced Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) which offers solutions for governments to plug loopholes in international tax treaties by transposing results from the BEPS project into bilateral tax treaties worldwide. At present more than 125 countries are part of this inclusive framework. The intent of the MLI is to make amendments in the treaty agreements to tackle the loopholes in international taxation by incorporating measures suggested by BEPS action plans. One such measure is emergence of concept of Digital Permanent Establishment ('PE').

Business Connection - Significant Economic Presence

- W.e.f. 01.04.2019, significant economic presence(SEP) of a non-resident in India constitutes "business connection" in India. [Explanation 2A to Section 9(1)(i) inserted]
- It means transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed or systematic and continuous soliciting of business activities or engaging in interaction with such number of users as may be prescribed, in India through *digital means*.
- The aforesaid activities constitute significant economic presence in India irrespective of the fact whether the agreement for such transactions or activities is entered in India, the non-resident has a residence or place of business in India or the non-resident renders services in India.
- The Income Tax Rules, 1962 were silent on the threshold pertaining to the aggregate amount of payments arising from specified transactions and the number of users.
- Finance Act, 2020 has deferred concept of SEP to AY 2022-23 by omitting it only for AY 2021-22 due to on-going discussions on G20-OECD/BEPS project.
- However, the reference to 'digital means' in the current provision has been deleted and accordingly, the scope of significant economic presence has been expanded to cover systematic and continuous soliciting of business or engaging with such number of users as may be prescribed.

Widening the scope of business connection

- W.e.f. 01.04.21, explanation 3A has been inserted in Section 9(1)(i) to declare that income attributable to the operations carried out in India, shall include income from—
 - ❖ (i) such advertisement which targets a customer who resides in India or a customer who accesses the advertisement through internet protocol address located in India;
 - ❖ (ii) sale of data collected from a person who resides in India or from a person who uses internet protocol address located in India; and
 - ❖ (iii) sale of goods or services using data collected from a person who resides in India or from a person who uses internet protocol address located in India.”;
- Thus, any non-resident earning income through advertisement, sale of data or e-commerce activities from a person residing in India or a person using Indian IP address shall constitute business connection in India.

Section 9 –Income deemed to accrue or arise in India w.r.t. salary, dividend, interest

- Income from salaries earned in India or salary payable by the Government to a citizen of India for service outside India.
- Dividend paid by an Indian company outside India.
- Income by way of interest payable by the Government, or a person who is a resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India ; or
- Income by way of interest payable by a person who is a non-resident, where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person in India.
- In case of a Foreign bank, interest paid by branch to its head office in addition to any income attributable to such branch.
- Interest income is taxable irrespective of non resident having a residence or place of business or business connection in India.