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The limitation of relief clause under the India-Singapore tax treaty is not applicable to income which is offered to tax on an accrual basis in Singapore

Background

Recently, the Rajkot Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Alabra Shipping Pte Ltd, Singapore/GAC Shipping India Pvt Ltd (agent)[1] held that the benefit of the India-Singapore tax treaty (tax treaty) is not to be denied to the taxpayer by applying provisions of the Limitation of Benefit (LOB)[2] clause since such income has already been offered to tax on an accrual basis in Singapore. The Tribunal observed that such LOB provisions can only be triggered when two conditions are satisfied i.e. (a) low or no taxability in the source jurisdiction and (b) taxability on a receipt basis in the residence jurisdiction. In the present case, the taxpayer had remitted its freight income to the U.K. account; however, the Tribunal has given the benefit of the tax treaty to the taxpayer.

Facts of the case

- GAC Shipping India Pvt Ltd (the taxpayer), filed a return of income in India in respect of MT Alabra, which is owned by Alabra Shipping Pte Ltd of Singapore, a freight beneficiary, as an agent of such a Singapore company under Section 172(3) of the Income-tax Act, 1961 (the Act). The taxpayer claimed the benefit of India-Singapore tax treaty and treated such freight income as exempt from tax in India. The taxpayer remitted the funds to the freight beneficiary's account with 'The Bank of Nova Scotia in the U.K.'.
- The Assessing Officer (AO) observed that the taxpayer remitted freight to a country other than Singapore and the remittance to Singapore is a *sine qua non* for availing the benefits of the India-Singapore tax treaty. The AO on the basis of the LOB clause in Article 24 of the tax treaty declined the tax treaty benefit.
- Aggrieved by the order of the AO, the taxpayer filed an appeal before the Commissioner of Income-tax (Appeals) [CIT(A)]. The taxpayer contended that the freight receipts were taxable in Singapore as the taxpayer was a tax resident of Singapore. The taxpayer produced a certificate from the Singapore Inland Revenue Service as well as from the Independent Public Accountant in Singapore. The taxpayer contended that provisions of Article 8 of the India-Singapore tax treaty will apply and, accordingly, the freight receipts cannot be brought to tax in India.
- The CIT(A) relied on the decision of the Mumbai Tribunal in the case of Abacus International Pvt. Ltd.[3] where it was observed that a requirement of Article 24 of the tax treaty is that the taxpayer must have received the interest income in Singapore. Accordingly, the CIT(A) upheld the order of the AO.

Tribunal's ruling

- In this case, since the taxpayer seeks a benefit of tax treaty protection, in terms of its shipping income covered by Article 8 of the tax treaty, the only LOB provision which comes into play is the provision set out in Article 24 of the tax treaty.

[1] Alabra Shipping Pte Ltd./Singapore GAC Shipping India Pvt. Ltd (As agents) v. ITO (ITA No. 392/RJT/2014) – Taxsutra.com
[2] Article 24 – Limitation of Relief of India-Singapore tax treaty
[3] Abacus International Pvt. Ltd. v. DDIT [2013] 34 taxmann.com 21 (Mum)

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While the tax treaty does contain certain other significant LOB clauses[4], such LOB clauses are relevant only for the purposes of the tax treaty protection related to Article 1 of the protocol to the tax treaty.

- On perusal of Article 24(1) of the tax treaty, it indicates that LOB clauses come into play when:
  - Income sourced in a contracting state is exempt from tax in that source state or is subject to tax at a reduced rate in that source state;
  - The said income is subject to tax by reference to the amount remitted to, or received in, the other contracting state, rather than with reference to the full amount of such income

  In such a situation, the tax treaty protection will be restricted to the amount which is taxed in the other contracting state.

- The benefit of the tax treaty protection is restricted to the amount of income which is a subject matter of taxation in the source country. This is more relevant in a situation in which a territorial method of taxation is followed by the tax jurisdiction and the taxation of income from activities carried out outside the home jurisdiction is restricted to the income repatriated to such tax jurisdiction. In the case of Singapore, the tax treaty protection must remain confined to the amount which is actually subject to tax.

- Any other approach could result in a situation in which income, which is not a subject matter of taxation in the residence jurisdiction, will anyway be available for tax treaty protection in the source country. Therefore, the scope of the LOB provision in Article 24 of the tax treaty needs to be appreciated.

- There was no dispute about the fact that the business was carried on by the taxpayer in Singapore and that the taxpayer was a tax resident of Singapore. By a letter dated 31 December 2013, the Inland Revenue Authority of Singapore confirmed that, in the case of Albara Shipping Pte Ltd, 'freight income has been regarded as a Singapore sourced income and brought to tax on an accrual basis (and not a remittance basis) in the year of assessment'.

- The taxpayer had also filed a confirmation from its public accountant that the freight earned from the port in India had been included in the global income offered to tax by the company in Singapore. On these facts, the provisions of Article 24 of the tax treaty cannot be put into service as these can only be triggered when the twin conditions of treaty protection, by low or no taxability, in the source jurisdiction and taxability on receipt basis, in the residence jurisdiction, are fulfilled.

- There is nothing on the record which suggests that the freight receipts were taxable only on a receipt basis in Singapore. On the contrary, there was reasonable evidence to demonstrate that such income was taxable on an accrual basis, in the hands of the taxpayer.

- The decision of the Mumbai Tribunal in the case of Abacus International Pvt. Ltd. relied on by the lower authorities, was in the context of interest income of the taxpayer and there was nothing on record to suggest that such an income was to be taxed in Singapore on an accrual basis, rather than on a receipt basis.

- In order to come out of the mischief of Article 24 of the tax treaty, the onus is on the taxpayer to show that the amount is remitted to, or received in Singapore; but then such an onus is confined to the cases in which income is taxable in Singapore on a limited receipt basis rather than on a comprehensive accrual basis. However, in a case where it can be demonstrated that the related income is taxable in Singapore on an accrual basis and not on a remittance basis, such an onus does not get triggered.

- It has been observed that the only reason for declining the India-Singapore tax treaty benefits was the applicability of Article 24 of the tax treaty and that there is no other dispute on the claim of the tax treaty protection of shipping income under Article 8(1) of the tax treaty which provides that, 'Profits derived by an enterprise of a contracting state from the operation of ships or aircrafts in international traffic shall be taxable only in that state'.

- Accordingly, the entire freight income of the taxpayer, which was only from the operation of ships in international traffic, was taxable only in Singapore. The AO was thus in error in bringing the same to tax in India.

Our comments

In the present case, the Rajkot Tribunal has held that LOB provisions under the tax treaty can only be triggered when two conditions i.e. (a) low or no taxability in the source jurisdiction and (b) taxability on a receipt basis in the residence jurisdiction, are fulfilled. In this case, the income of the taxpayer was offered to tax in Singapore on an accrual basis.

[4] As set out in protocol dated 29 June 2005 [(2005) 196 CTR (Stat) 177]

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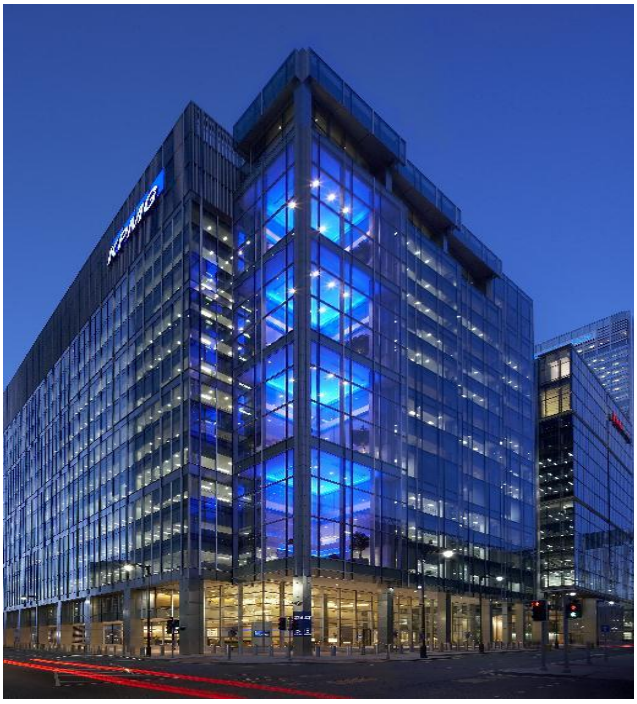
Therefore, the LOB provisions under Article 24 of the India-Singapore tax treaty are not applicable even though income was remitted to the U.K. account.

This ruling provides guidance for applicability of LOB provisions under the India-Singapore tax treaty. It is stated that such LOB provisions will be applicable to income which are taxable on a receipt/remittance basis in Singapore. In a case where it can be demonstrated that the related income is taxable in Singapore on an accrual basis and not on a receipt/remittance basis, such LOB provisions may not apply.



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