Volume-89 December -2021 Pages 1-19

SBS Wiki

monthly e-Journal

For Private circulation only

By

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Dear Readers,

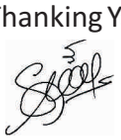
Greetings for the season!

In this edition, we bring you, one of the most complicated classifications under the income tax laws, that is, classification of lease income. Whether the same would be classified under income from house property or profits and gains from business or profession or income from other sources is a complicated issue and we tried to discuss on the same with the help of a case study.

The next article is on the various issues under the residency under Section 6 of Income Tax Act. We have covered the most asked issues, whether the day of arrival is counted for purposes of computation of days present in India for determining the residential status and similar items.

I hope that you will have good time reading this edition and please do share your feedback. I will also urge clients to mail us topics or issues on which you want us to deliberate in our future editions, so that we can contribute to the same.

Thanking You,



Suresh Babu S
Founder & Chairman

DIRECT TAX

LEASE INCOME - IFHP VS PGBP VS IFOS

Contributed by CA Sri Harsha

One of the mysteries of the 21st Century is the taxation of rental income under the IT Act[1] . The classification of such rental income is quite challenging and garnering a unanimous view among tax practitioners itself is impossible, forget about the authorities and courts. In this article, we try to analyse the various judgements on the issue and provide our conclusions about the classification.

Before proceeding to analyse the various judgments, a quick look at the scheme of IT Act is essential. Section 4 of the IT Act deals with charge of income tax on total income earned by the assessee in the previous year. The tax on the total income of the previous year has to be classified under the heads of income as provided in Section 14 of Act and accordingly the liability has to be computed. Each head of income is different from other head and has different entitlements, restrictions and prohibitions in the total scheme of the act. Hence, classifying an income under the appropriate head is important because of different tax consequences. For example, an income which is classified under IFHP[2] is eligible only for a standard deduction of expenditure as against actuals, however, the same income, which if classified under PGBP[3] , does not have any restriction for claiming the expenditure. Hence, it is important to classify the income under appropriate head to avoid any future litigations on the said count.

Case Study:

Let us say, ABC Limited has constructed a building which can be fit for use for a company, say PQR Limited engaged in providing restaurant, banquet, accommodation, and other related services. PQR Limited has approached ABC Limited for the leasing of the said property. As per the contract, ABC Limited must invest in certain plant and machinery (lifts, generator set and others), furniture and fixtures and certain other items. The rent is agreed to be shared based on certain percentage of revenues earned by PQR Limited. Adding another layer of complication (but not hypothetical), let us assume that ABC Limited has taken part of the building on lease from various owners and leased it to PQR Limited.

The question would be, whether the rental income earned by ABC Limited should be offered to tax under IFHP or PGBP or IFOS [4]. Before analysing the same, it is not out of place to mention that classification of income under each of the above head have different tax consequences. For example, if the income is classified under IFHP, ABC Limited can only claim deduction upto 30% of net annual value in terms of Section 24(a) of IT Act. On the other hand, if ABC Limited classifies the said income under PGBP, then there is no restriction on the quantum of expenditure that can be claimed as deduction. Alternatively, if the income is classified as IFOS, then there is no possibility of deduction of any expenditure, either standard as allowed under IFHP or actual as allowed under PGBP. Apart from the above, there is also carry-forward of losses (the quantum and years for which they are allowed to carry forward), which are dependent again upon the classification of income and differ from one head to another. Hence, it is essential to understand under which head of income, the said income gets classified. So, let us proceed to answer the same.

[1]Income Tax Act, 1961
[2]Income from House Property
[3]Profits and Gains from Business or Profession
[4]Income From Other Sources

Discussion on Possibility of Classification under IFHP:

Section 22 to Section 27 deals with IFHP. Section 22 states that annual value of property consisting of any buildings or lands appurtenant there to of which the assessee is the ***owner,*** shall be the income chargeable to the income-tax under the head IFHP. From the above, it is evident that in order to classify an income from property under IFHP, it is mandatory that assessee is the owner of such property. If the assessee is not the owner of the property, the income earned from such property, would not be subjected to tax under the head IFHP. Hence, it is necessary to determine, the ambit of expression 'owner of house property' to decide the possibility of classification under IFHP.

The definition of 'owner of house property' has been defined vide Section 27 of Act. The sub-clause that is relevant to the current issue is the (iiib). Vide Section 27(iiib), a person who acquires any right (excluding any right by way of lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof, by virtue of any such transaction referred in Section 269UA(f), is deemed to be the owner of house property for the purposes of Section 22 to 26.Section 269UA (f), vide sub-clause (i) states that transfer in relation to immovable property referred to in sub-clause (i) of clause (d) of Section 269 UA, means a transfer of such property by way of sale or exchange or lease for a term of not less than 12 years and includes allowing the possession of such property to be taken or retained in part performance of a contract of the nature referred in Section 53A of Transfer of Property Act, 1882. The immovable property referred in sub-clause (i) of clause (d) of Section 269 UA, means any land or building or part of the building, and includes, where any land or any building or part of a building is to be transferred together with any machinery, plant, furniture, fittings or any other things, such machinery, plant, furniture, fittings or other things also.

Hence, on a combined reading of Section 269UA (f) and 269 UA (d)(i), what transpires is, if there is an immovable property which is nature of building together with machinery, plant, furniture or fittings or other things and being transferred ***vide lease for a term not less than 12 years***, the person making such transfer shall be deemed to be owner for the purposes of Section 22 to Section 26. Accordingly, all instances of transfer of immovable property vide lease for a term not less than 12 years, the transferor would still qualify as the owner of the house property for the purposes of IFHP.

However, the ownership of the property is not a conclusive factor for classification of income earned under IFHP. If it can be substantiated that such letting out is not for earning the rent alone but to commercially exploit the property, then there can be said that the income earned shall be taxable under PGBP and not under IFHP. Hence, let us proceed to examine the classification under PGBP.

Discussion on Possibility of Classification under PGBP:

Section 28(i) states that the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year shall be classifiable under PGBP. Let us now, proceed to understand, under what circumstances, such income shall be classifiable under PGBP.

The Supreme Court in the matter of Chennai Properties & Investments Limited[5] held that if the main objective of the company is to let out, then such income can be classified under the head PGBP instead of IFHP. The Supreme Court in the matter of Chennai Properties & Investments Limited (supra),placed reliance on the judgment in the matter of Karanpura Development Co Ltd [6], where in it was held that 'as *has been already pointed out in connection with the other two cases where there is letting out of premises and collection of rents the assessment on property basis may be correct but not so, where the letting or sub-letting is part of trading operation. The dividing line is difficult to find, but in the case of a company* ***with its professed objects and the manner of its activities and the nature of dealing with its property,*** *it is possible to say on which side the operations fall and to what head the income is to be assigned'.*

The Supreme Court in the matter of Chennai Properties & Investments Limited (supra), further distinguished the two judgments which were against the taxpayers classifying income under PGBP. The two judgments were in the matters of East India Housing and Land Development Trust Limited[7] and Constitution Bench in the matter of Sultan Brothers (P) Limited [8]. We shall discuss the same hereunder.

The Supreme Court has distinguished the judgment in the matter of East India Housing and Land Development Trust Limited (supra), stating that, the main objective of the company was to buy and develop properties and promoting and developing markets and not the letting out of properties. Accordingly, the Supreme Court has come to conclusion that since letting was not at all the objective of the company and there was a rental income, such income shall be taxable as IFHP and not PGBP. The court was therefore of the opinion that income which was from the house property had not altered because it was received by company formed with the objective of developing and setting up properties. However, in the matter of Chennai Properties & Investments Limited, the main objective was to let out. Hence, there is a change in facts of the matter between East India Housing and Land Development Trust Limited (supra) and Chennai Properties & Investments Limited and stated that such judgment does not apply.

Further, the Constitution Bench in the matter of Sultan Brothers (P) Limited has held that despite of the fact that objective of the company is to acquire land and buildings and to turn the same into account by construction and reconstruction, decoration, furnishing and maintenance of them and leasing and selling of the same would not by itself turn into the lease as business income. The Constitution Bench has concluded that, ***'We think each case has to be looked at from a businessman's point of view to find out whether the letting was the doing of a business or the exploitation of his property by an owner.*** *We do not further think that a thing can by its very nature be a commercial asset. A commercial asset is only an asset used in a business and nothing else, and business may be carried on with practically all things. Therefore, it is not possible to say that a particular activity is business because it is concerned with an asset with which trade is commonly carried on. We find nothing in the cases referred, to support the proposition that certain assets are commercial assets in their very nature'.*

The Supreme Court in the matter of Chennai Properties & Investments Limited has distinguished the judgment of Constitution Bench of Sultan Brothers (P) Limited by stating that the entire exercise, whether an income falls under IFHP or PGBP should be based on the facts of each case and since in the facts of Chennai Properties & Investments Limited, the objective was to let out and accordingly the decision in Sultan Brothers (P) Limited can be distinguished.

[5]2015 (5) TMI 46 – Supreme Court
[6]1961 (8) TMI 7 – Supreme Court
[7]1960 (11) TMI 7 – Supreme Court
[8]1963 (12) TMI 4 – Supreme Court

From the above discussion, what can be summed up is, there is no straight answer as to whether an income is classifiable under IFHP or PGBP. It depends upon the facts of each case and the intention of the party who lets his property. If the intention is to earna standard rent from the property, then it can be classified as IFHP, but if the intention is to commercially exploit the asset, then such income shall be classified as PGBP.

From the facts in the case study, it is evident that the objective of ABC Limited is not to just earn the rental income, which is evident from the fact that rent is based on the revenues earned by PQR Limited. In other words, ABC Limited has also taken a risk or done an adventure (in case of downside in revenues, ABC Limited would be losing the rentals) by resorting to the rentals based on the revenues instead of standard rentals. Hence, there are brighter chances for ABC Limited to classify the income under PGBP rather than IFHP.

The Supreme Court in the matter of Rayala Corporation Private Limited[9] has stated that the assessee company has only one business and that is leasing of its property and earning rent therefrom and hence concluded that income from leasing is chargeable under PGBP and not under IFHP as claimed by revenue. The Supreme Court in the matter of Raj Dadarkar & Associates[10] has stated that income earned from shopping centre, where the assessee is owner, by virtue of Section 27(iiib) is chargeable to IFHP and not PGBP, ***since the assessee has failed to show any evidence or other material to state that intention was to exploit the property not as owner. Hence, the intention assumes importance to classify the income either as IFHP or PGBP.***

The Delhi High Court in the matter of Francis Wacziarg [11], has held that income earned from leasing out of hotels is to be treated as income from PGBP and not under IFHP as claimed by the Revenue. The Delhi High Court has confirmed the view taken by Commissioner of Income Tax (Appeals) wherein the Commissioner of Income Tax (Appeals) has held that income earned by assessee was taxable under PGBP for the reason that the license fee received by assessee is not a fixed sum of money as in the case of IFHP but is has been varying from year to year as it is based on a revenue sharing agreement, which arises according to the receipts. As stated in the facts of case study, ABC Limited has also entered a similar agreement with PQR Limited, where the lease rental or license fee is charged based on the receipts earned by PQR Limited and accordingly the same may be concluded as income under PGBP and not under IFHP.

The Andhra Pradesh High Court in the matter of Sileman Khan Mahaboob Khan[12] has held that income earned from letting out godowns which is a commercial asset by itself does not make income under PGBP and to be taxed under IFHP. The Andhra Pradesh High Court further stated that the nature of income shall not become PGBP only for the reason that one of the objectives of partnership deed is to undertake activity of construction and to let out them. In the facts of the case, the assessee was an exporter of tobacco and whenever he is not in requirement of godowns, the same were let out and the Andhra Pradesh High Court has held that since letting out of godowns is not a continuous activity and such let out is not without any amenities, the income earned from let out shall be subjected to tax under IFHP and not under PGBP. However, this can be distinguished from the facts of the current case study.

[9] 2016 (8) TMI 522 – Supreme Court
[10] 2017 (5) TMI 586 – Supreme Court
[11] 2011 (11) TMI 19 – Delhi High Court
[12] 2015 (5) TMI 432 – Andhra Pradesh High Court

The Income Tax Appellate Tribunal (for brevity 'ITAT') of Chandigarh in the matter of Enn Zen Enterprises (P) Limited [13] was seized with facts wherein the assessee had leased the building and restaurant along with furniture and fixture and earned income. Such income has been disclosed as income from PGBP. However, the Assessing Officer has raised an objection that such income has to be assessed as IFHP and not as PGBP. The ITAT after perusing the facts has stated that, whether a particular letting is business or not has to be decided based on the facts and circumstances of each case and the same has to be looked from the perspective of the assessee to find out whether letting was done for a business or for exploitation of its property as owner. The ITAT further stated that it is now trite law that merely the fact that a premises is being let out on rent does not mean that income out of it is to be taxed as income from house property. It has to be seen what is, primary object of letting out such property. The object, as it appears, in the present case, is exploitation after the persistent efforts of the assessee at various levels. The development of two such hotels, not only one, in the assessee's case also strengthen the contention of the assessee that is in the business of running hotels and concluded that income shall be treated as PGBP and not as IFHP.

The ITAT of Hyderabad in the matter of Vijay Infotech Ventures[14] , has held that objects of the company to carry on business of leasing out the properties to make profit will be subjected to tax under PGBP and not under IFHP. The facts were that assesse was leasing out the building for software technology and accordingly held that such income is under PGBP and IFHP.

Further, the Central Board of Direct Taxes (for brevity 'CBDT') vide Circular 16/2017 dated 25th April 2017 has clarified that income arising from letting out premises/developed space along with other amenities in an Industrial Park/SEZ is to be charged under PGBP and not under IFHP as claimed by Assessing Officers. Even though the above is applicable for industrial parks/SEZ, the intention can be garnered and applied to the current facts to derive that income is subjected to PGBP.

Hence, from the above jurisprudence, if the objective of ABC Limited is to lease out the property and earn income thereon and to commercially exploit the property instead of earning regular income from the property, then it is fit case, the income can be classified as PGBP instead of IFHP despite of the fact that ABC Limited is the owner or deemed owner for the purposes of Section 22 to Section 26. However, the said matter is not free from any litigation.

Discussion on Possibility of Classification under IFOS:

The next issue that may arise is, whether the income earned from PQR Limited can be classified as IFOS instead of PGBP. Section 56(1) of Income Tax Act states that income of every kind which is not to be excluded from the total income shall be chargeable to tax under IFOS, ***if it is not chargeable to income tax under any of the heads as mentioned in Section 14, from A to E.***

Since, we have concluded that the income is chargeable to tax under IFHP or PGBP, the same will not be taxable under IFOS vide Section 56(1).

[13] 2016 (5) TMI 63 – ITAT Chandigarh
[14] 2017 (1) TMI 106 – ITAT Hyderabad

There might arise a question, since the ABC Limited has taken lease from various landowners and given the same commercial complex to PQR Limited, whether such sub-lease is subjected to tax under IFOS. Normally, the income from sub-lease transactions are subjected to tax under IFOS, since under the typical sub-lease, the person who is providing assets on sub-lease is not an owner and thereby failsto satisfy the condition under Section 22 to be called as IFHP. Hence, typical sub-lease transactions are subjected to tax under IFOS. However, in the instant case, as we have concluded that ABC Limited is deemed to be owner by virtue of Section 27(iiib), the income earned shall not be taxable under IFOS, since it satisfies the condition mentioned under Section 22.

Because of the above-mentioned reason, we can conclude though ABC Limited has sub-leased the property, there will not be any classification under Section 56(1) of Act. Hence, let us proceed to examine applicability of any other provisions of Section 56 to call income earned by Subishi or new entity as IFOS.

Section 56(2)(iii) states that, where an assessee lets on hire machinery, plant or furniture belonging to him and also buildings, and the letting of buildings is inseparable from the letting of the said machinery, plant or furniture, the income from such letting, if it is not chargeable to income-tax under the head PGBP. Hence, from the above, it is evident that, income from letting of machinery, plant or furniture belonging to him along with buildings and such letting of machinery, plant or furniture is inseparable from letting of buildings, then such income if not charged under PGBP, then such income will be subjected under IFOS.

Hence, from the above discussion, we wish to conclude that the income earned by ABC Limited can be classified as PGBP. However, as part of their tax policy, they have to keep updating with latest judicial trends to revisit time and again the above stand adopted by them. The below are certain judgments of various courts, where different views were taken qua classification:

S No	Matter	Court	Summary of Outcome	IFHP	PGBP	IFOS
1.	DS Promoters and Developers Private Limited[15]	Delhi (HC)	• The assessee in this case has let out two properties. One of them is owned by the assesse and the other one is leased by assessee and further leased to earn rental income. • The assessee has offered the above income from both properties under PGBP. However, the tax authorities wanted to tax the income from own property under IFHP and income from leased property under IFOS, since the assessee is not owner. • The Delhi High Court after observing the judicial precedents stated that the objective of the assessee is to exploit the commercial property and accordingly held that income should be under PGBP.	No	Yes	No
2.	Harikrishna Family Trust[16]	Gujarat (HC)	• The assessee, a trust after completion of construction work rented out the whole premises to Posts & Telephones Department. • The assessee has leased out the property from another owner and then leased it to the Posts & Telephones Department. The assessee was offering the said income under IFHP. • The tax authorities contention was that since the assessee is not the owner of the property, the income cannot be taxed under IFHP and should be chargeable to PGBP. • The High Court after analysing the facts that the trust was not carrying out any systematic activity, it is hard to classify the income under PGBP and accordingly taxed it under IFOS.	No	No	Yes

[15] 2009 (5) TMI 557 – Delhi High Court
[16] [2008] 306 ITR 303

3.	FGP Limited No. 9 Commercial [17]	ITAT (Mumbai)	• The assessee has developed the property and also made provisions for various services with a view to commercially exploit the property. • The rental income was offered to tax under PGBP, whereas the tax authorities tried to tax under IFHP. • The ITAT placing reliance on SG Mercantile Corporation[18] and distinguishing the Harikrishna Family Trust stated that the assessee has exploited the property on commercial basis and it would be right in law to tax the income	No	Yes	-
4.	Rayala Corporation (P) Limited [19]	Madras (HC)	• The question before the High Court was whether the income from leasing and renting of immovable properties with all infrastructural facilities with providing maintenance and related activities should be subjected to IFHP or PGBP. • The Madras High Court after referring to Rayala Corporation (P) Limited judgment of Supreme Court (supra) held that such income is taxable under PGBP.	No	Yes	-
5.	PSTS Heavy Lift and Shift Limited [20] [Similar judgments in Shri Hardoi Baba Roller Flour Mills Private Limited][21]	Madras (HC)	• The main source of income of assessee is rentals and offered it as PGBP. The tax authorities have rejected the same and tried to tax under IFHP. • The High Court held that when the main income of the assessee is to earn the rental income, it is not fair to tax such income under IFHP and held taxation under PGBP is right.	No	Yes	-

[17] 2012 (10) TMI 559 – ITAT Mumbai
[18] 83 ITR 700
[19] 2020 (3) TMI 883 – Madras High Court
[20] 2020 (2) TMI 213 – Madras High Court
[22] 1019 (3) TMI 1004 – Allahabad High Court

6.	E-City Project Construction Private Limited[22]	Bombay (HC)	• The assessee is built various malls and was in receipt of rent. The same was offered to tax under PGBP. The tax authorities wanted to tax under IFHP. • The High Court stated that since the intention of the assesse was to commercially exploit the property, the income is taxable under PGBP.	No	Yes	-
7.	City Centre Mall Nashik Private Limited[23] [Similar judgments in Krome Planet Interiors Private Limited[24] , Oberon Edifices and Estates Private Limited[25]	Bombay (HC)	• Assessee has built a mall and entered agreements with various shops in the mall to earn income on basis of revenue sharing and rental fee. The assessee has offered the income under PGBP, however the tax authorities wanted to tax it under IFHP. • The High Court held that the revenue sharing arrangements and objective of the assesse indicates the intent to exploit the property in commercial way and hence the same is taxable under PGBP.	No	Yes	-
8.	Cache Properties Private Limited[26] [Similar judgments in Mangala Homes Private Limited[27] and Meeraj Estate and Developers][28]	ITAT (Hyd)	• Assessee has let out properties and offered the rental income under IFHP. The tax authorities wanted to tax the same as PGBP. • The Tribunal stated that since the assessee is not carrying on a systematic and organized activity to exploit the property commercially, the same would be taxable under IFHP and not PGBP.	Yes	No	-

[22]2017 (7) TMI 779 – Bombay High Court
[23]2020 (1) TMI 872 – Bombay High Court
[24]2019 (4) TMI 1388 –Bombay High Court
[25]2019 (3) TMI 1468 – Kerela High Court
[26]2019 (5) TMI 1875 – ITAT Hyderabad
[27]2008 (8) TMI 522 – Bombay High Court
[28]2019 (10) TMI 1002 – Allahabad High Court

9.	Cache Properties Private Limited [29]	ITAT (Hyd)	• Followed the earlier judgement (supra) and also stipulated the tests to be applied for determination whether rental income would be classified as IFHP or PGBP. • The four tests prescribed are the tenure of lease, the objects of company, intention of company and services provided or activities carried on by assessee after letting out of the property.	Yes	No	-
10.	Palmshore Hotels (P) Limited[30] [Similar judgments inDodla International Limited][31]	Kerala (HC)	• Assesse herein had constructed, established and operated a hotel by name 'Hotel Palmshore' but gave the hotel along with its furnishings and equipments on license basis. • The assessee offered the income under PGBP and tax authorities wanted to tax under IFHP. The Court held that the provisions of the agreement indicate that the license that has been granted is that of a fully established running hotel authorising the licensee to operate the hotel for a specified period subject to the terms and conditions incorporated therein and such grant of license is business and cannot be taxed under IFHP.	No	Yes	-

[29] 2021 (11) TMI 768 – ITAT Hyderabad
[30] 2017 (11) TMI 1086 – Kerala High Court
[31] 2021 (2) TMI 421 – ITAT Chennai

DIRECT TAX

VARIOUS ISSUES OF RESIDENCY UNDER SECTION 6

Contributed by CA Sri Harsha & CA Narendra

In our previous article[1] ,the concept of deemed residency under Section 6 of ITA[2] has been discussed in detail. In this part, various issues related to determination of residential status of an individual are aimed for discussion. As per Section 6(1) of ITA an individual shall be treated as resident:

a. If he is in India for a period of 182 days or more during previous year or
b. If he is in India for a period of 365 days within 4 years immediately preceding previous years and 60 days or more during the previous year.

A person being an individual is treated as resident in India if any of the conditions i.e., (a) or (b) above is satisfied. Otherwise, such person is treated as non-resident.Further, Explanation 1 to Section 6(1) states that in case of an individual:

a. being a citizen of India who leaves in India in any previous year as a member of crew member of an Indian ship or for the purposes of employment outside India, the period of stay for that year specified above as 60 days is to be replaced with 182 days.
b. being a citizen of India or person of Indian origin, who is staying outside India, comes to India on a visit to India in any previous year.

    i. the period of stay specified above as 60 days is to be replaced with 182days.
    ii. In the case of such person having total income, other than income from foreign sourced income, exceeding INR 15 lakhs, the period of stay specified above as 60 days is to be replaced with 120 days.

A plain reading of Section 6 seems to be easy to understand. However, each and every aspect of Section 6 needs to be analyzed carefully, as many practical difficulties would arise while interpreting the provisions.

Let us proceed to analyze various aspects of provisions of Section 6.

For the purposes of employment:

Explanation 1(a) to Section 6(1) states that in the case of an individual being a citizen of India who leaves India for the purposes of employment outside India, such person is treated as resident in India only when such person stays in India for a period of 182 days or more during the year under consideration instead of general rule of 60 days.

However, the term 'for the purposes of employment' is not expressly defined under the provisions of Section 6. Hence, it triggers interpretational issues.

[1]Deemed Residency - Concept and Issues Thereof
[2]Income Tax Act, 1961

The individual may leave India for obtaining employment outside India, may leave India to exercise employment outside India, may leave India on deputation to other country or may leave India for self-employment outside. The question arises is whether every illustration stated above is covered under the ambit ***'for the purposes of employment'?***

While the first two instances are undoubtedly covered under the term 'for the purpose of employment' outside India, the uncertainty is left with other two instances which is tried to be resolved by various judicial fora.

Deputation:

The AAR in case of British Gas India (P.) Ltd., In re[3] has held that the requirement of Explanation 1(a) to Section 6(1) is not leaving India for employment but ***it is leaving India for the purposes of employment outside India.*** For the purpose of the Explanation, an individual need not be an employed person who leaves in India for employment outside India. Accordingly, the AAR has held that when a person being individual who is under the employment in India leaves on deputation is also covered under Explanation 1(a) to Section 6(1).

Self-Employment:

Circular[4] amending the provisions of Section 6(1) through the Finance Act, 1982 states that "with a view to avoiding hardship in the case of Indian citizens, *who are employed or engaged in other avocations outside India*…". From the above extract of circular, it is evident that individuals engaged in other avocations were also intended to be covered.

The Kerala High Court in the case of O. Abdul Razak[5] has held that even self-employment is also covered under Explanation 1(a) to Section 6(1). The High Court has referred to CBDT [6] Circular 346 (supra) and held that going abroad for the purpose of employment only means that the visit and stay abroad should not be for other purposes such as a tourist, or for medical treatment or for studies or the like. Accordingly, the High Court ***held that going abroad for the purpose of employment therefore means going abroad to take up employment or any avocation as referred to in the Circular, which takes in self-employment like business or profession.***

[3][2006] 155 TAXMAN 326 (AAR – New Delhi)
[4]Circular No 346, dated 30-6-1982
[5][2011] 198 Taxman 1 (Kerala)
[6]Central Board of Direct Taxes

Following the Kerala High Court judgement in the case of O. Abdul Razak (supra), the Delhi Tribunal in the case of Jyotinder Singh Randhawa[7] has held that assessee being a professional golfer is a self-employed professional and hence for such citizen period of stay has to be increased to 182 days as per Explanation 1 (a) to Section 6(1).

The Hyderabad Tribunal in case of K. Sambasiva Rao[8] has referred the decision of the Supreme Court in the case of Aditya V. Birla[9] wherein the Supreme Court has held that employment does not mean salaried employment but also includes self-employed/professional work. Considering the Supreme Court judgement and Kerala High Court judgement in the case of O. Abdul Razak (supra), the Tribunal has held that going abroad for the purpose of employment therefore, means going abroad to take-up employment ***or any avocation*** as referred to in the circular.

Hence, the explanation covers not only the straight employment scenarios but also self-employment scenarios.

Various Situations vis-à-vis Explanation 1:

An act of going abroad and coming to India by an individual may be divided into three phases. First phase - leaving India for various purposes, second phase - visiting India on regular intervals and third phase - coming to India permanently.

Leaving India:

The next aspect in Section 6(1) is whether the provisions of Explanation 1(a) are applicable to subsequent previous years or applicable in the year in which such individual leaves India. Explanation 1(a) states that'*being a citizen of India, who* ***leaves India in any previous year****.....the provisions of sub-clause (c) shall apply in* ***relation to that year*** *as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted."*

[7][2014] 46 taxmann.com 10 (Delhi - Trib.)
[8][2014] 42 taxmann.com 115 (Hyderabad - Trib.)
[9][1988] 170 ITR 137/36 Taxman 9

The reading of Explanation 1(a) shows that these provisions are applicable to the year in which such individual leaves for the purpose of employment outside India.

This aspect has been dealt with by the Bangalore Tribunal in the case of Manoj Kumar Reddy[10] (the decision of the Bangalore Tribunal has been upheld by the Karnataka High Court[11]) where in the Tribunal held that the word 'that year' refers to the previous year in which the assessee has left India for the purpose of employment outside India. Accordingly, the Tribunal has held that Explanation 1(a) to Section 6(1) is applicable to the previous year in which the assessee leaves India for the purpose of his employment.

Visit to India:

The word 'visit to India' too makes significant impact on determination of residential status of an individual. Direct Tax Laws (Second Amendment) Act, 1989, by which period of stay for COI[12] or PIO[13] has been increased to 150 days, throws some light on provisions of Explanation 1 (b) to interpret the term 'visit to India'.
The statement of objects and reasons states that amendment to Section 6 will liberalize the criterion for determining the residential status so as to facilitate non-resident Indians to stay in India for a longer period in order to look after their investments without losing their 'non-resident' status.

Further, CBDT Circular No 684 dated June 10, 1994, explaining the amendments through Finance Act, 1994 states that non-resident Indians who have made investments in India, find it necessary to visit India frequently and stay here for the proper supervision and control of their investments. Accordingly, the period of stay for determining the residential status has been increased to 182 days.

Going through the legislative intent of the Explanation 1 to Section 6, it can be concluded that the purpose of incorporating such Explanation is to encourage NRIs to visit India on regular intervals to look after the investment made them.

[10][2009] 34 SOT 180 (Bangalore)
[11][2011] 12 taxmann.com 326 (Karnataka)
[12]Citizen of India
[13]Person of Indian Origin

Permanent return:

Having said that the period of stay in the case of visit has to be increased to 182 days, the question arises is whether permanent return to India is also covered under Explanation 1(b) to Section 6(1)?

The Bangalore Tribunal in the case of Manoj Kumar Reddy (supra) has held that one has to consider the entry of a person into India and if such entry is for the purpose of visit, then, period of stay 60 days has to been increased to 182 days. However, if in the previous year, the assessee has come to India permanently after leaving his employment outside India, then the Explanation (b) will not be applicable.

In this case, the assessee has come to India on visit and went back to foreign country. Subsequently, the assessee has come to India permanently in the same financial year. By quoting this fact, assessee has argued that once there is a visit to India, period of stay has to be increased to 182 days notwithstanding to the subsequent return to India permanently. However, the High Court considering the legal background of Explanation 1(b) has negated the arguments of the assessee.

Further, an interesting argument has been made the assessee that while computing the period of stay on permanent return to India, period of stay on visit has to be excluded. The assessee has explained his contention with an example '*In Example A, the learned AR submitted that a person comes on visit and his stay in India on visit is 120 days. He will be treated as non-resident as per clause (b) of the Explanation. In Example B, if a person comes on visit and stays in India for 90 days and returns abroad and, later on, comes back to India permanently and he stays in India for a period of 30 days, he will become a resident according to the Assessing Officer. This is because his stay in India has exceeded 60 days if period of visit is also included. In both the cases, stay is only 120 days. However, in Example B, a person becomes a resident while in Example A, he remains non-resident'.*This time, the High Court has agreed with the contention of the assessee and excluded the period of visit to India while computing the period of stay in India.

The AAR in the case of Mrs. Smita Anand, China, In re[14] has, after the detailed analysis, held that as the assessee has returned to India after the resignation hence, such return to India cannot be equated with 'visit to India' under Explanation 1 (b) to section 6(1).

[14][2014] 42 taxmann.com 366 (AAR - New Delhi)

Considering the judicial analysis to Explanation 1 to Section 6(1), it can be understood that intention of the assessee to stay in India whether on visit or permanent makes significant impact on determination of the residential status. Even in the case of leaving India, the term 'purposes of employment' has been interpreted by keeping mind the legislature intention behind the incorporation of such Explanation to Section 6(1).

i. In the case of leaving India for the purposes of employment, the period of stay has to be increased to 182 days.

ii. In the case of coming to India on visit, the period of stay has to be increased to 182 days.

iii. In the case of coming to India permanently, period of stay cannot be increased to 182 days and 60 days has to be computed for determining the residential status of an Individual.

Day of Arrival to be Included in Computation?

As discussed earlier, in order to treat a person resident in India, such person shall be in India for specified number of days in the previous year. The next aspect of Section 6 is, how to compute number of days for which an individual is present in India.

The issue that created lot of discussion at various fora is ***whether day of arrival to India or day of leaving India needs to be included or excluded while computing the number of days in India?***

As this issue has not been dealt with by the provisions of Section 6, judicial fora have analyzed the issue at length and the summary of various decisions are discussed hereunder.

The Jaipur Tribunal in case of Dr. R.K. Sharma[15] has held that fraction of day need not be computed for the purpose determining period of stay in India. In this case, the assessee has arrived in India at 10:30PM. In this regard, the Tribunal has pointed that prime hour of work having expired the assessee could not have done any useful work for the one and a half hours.

The Bangalore Tribunal in the case of Manoj Kumar Reddy (supra) has held that when one has to compute the period for which an assessee is in India, one has to start the counting from a particular day and to end the same with specific day. The period is to be counted from the date of arrival of the assessee in India to the date he leaves India. Thus, the words 'from' and 'to' are to be inevitably used for ascertaining the period though these words are not mentioned in the statute. The Tribunal has further referred to section 9 of General Clauses Act which states that

(1) In any (Central Act) or Regulation made after the commencement of this Act, it shall be sufficient, for the purpose of excluding the first in a series of days or any other period of time to use the word "from", and, for the purpose of including the last in a series of days or any other period of time, to use the word "to".

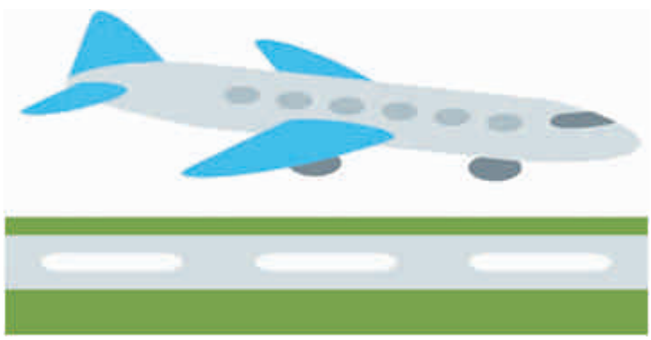
(2) This section applies also to all (Central Acts) made after the third day of January, 1868, and to all Regulations made on or after the fourteenth day of January, 1887.

Which means that while computing a period first day in a series has to be excluded when the 'from' is used in the context. In this regard, even though Section 6 does not use the word 'from', the Tribunal has opined that for computing the period, one has to necessarily import the 'from'. Accordingly, the Tribunal has held that when once the word 'from' is used for computing the period, first day in the series has to be excluded.

Following the decision of Bangalore Tribunal in the case of Manoj Kumar Reddy (supra) and Jaipur Tribunal in the case of Dr. R.K. Sharma (supra), the Mumbai Tribunal in the case of Fausta C. Cordeiro[16] has held that fraction of day must be excluded while computing the period of stay in India.

[15][1987] 0 SOT 1 (Jaipur)[22-08-1986]
[16][2012] 24 taxmann.com 193 (Mum.)

Recently, the Ahmedabad Tribunal in the case of Pradeep Kumar Joshil (Late) Represented by his Wife And L/H. Smt. Sangeeta P. Joshi[17] after the considering the other Bench judgements held that 'We do not find any reason to deviate from the ratio laid down by the Honb'le Bangalore Bench as narrated therein above and relying upon the identical facts in the case in hand we exclude the date of arrival in counting the days of stay in India in the case of the assessee.'



From the above judicial precedents, it can be understood that the day of arrival needs to be excluded for computing the period of stay in India. The question arises whether such day of arrival needs to be excluded when there are multiple visits to India. In this regard, the Ahmedabad Tribunal in the case of Pradeep Kumar Joshi (supra) has held that day of arrival in each visit has to be excluded. The intention behind such decision would be that in order to consider a day, such day needs to be a full day of stay in India and partial/fraction of day need not be considered as day for computing period of stay in India.

We shall conclude this part which has dealt with the aspect of determination of residential status of an Individual on various occasions. In the next part, the aspect related to determination of residential status of an individual who is working in a ship/vessel or aircraft would be discussed.

[17] I.T.A. No. 452/Ahd/2020

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