SATURDAY INTERNATIONAL TAX GYAN !!!
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Back to Basic Principles

SITG No. 242

Taxpayer can opt for taxability under Act or DTAA, whichever is more beneficial for each stream of income.

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Introduction

- The taxpayer is allowed to choose whether to be taxed under the provisions of the domestic tax law (The Act) or under the relevant provisions of the DTAA.

- The choice depends on which option results in the **lower tax liability**. This provides taxpayers with flexibility and allows them to optimize their tax position.

- Under Indian tax law, **Section 90(2)** of the Income Tax Act, 1961, provides that a taxpayer can apply the provisions of a DTAA if they are more beneficial than the domestic tax law.

- The reference to "each stream of income" means that this choice is applied on an income-by-income basis. A taxpayer might have **multiple sources of income**, such as salary income, rental income, interest, royalties, or capital gains which are taxed at different rates. For each source of income, the taxpayer can independently decide whether to apply the provisions of the Act or the DTAA.

Introduction

- Although the term “stream of income has not been defined under the law. However, based on various case laws it can be derived that if the income is derived from different sources or are taxed at different rates by the statute it will be considered as different stream of income. Although, such income might be under same head of income as per Income tax act but since the source is different they will be considered as different stream of income.

- For eg: STCG earned is taxed under 111A of the Income tax act and LTCG is taxed under 112A of the Act and accordingly both of them will be considered as different stream of income.

Illustration

- **Mr. X, a tax resident of France, has two streams of income namely business income u/s 44BB taxed at 30% and royalty income u/s 115A at 20% in India during the Assessment Year 2023-24**

1. **Income from Offshore Drilling Services (Business Income) under a Contract with ONGC**

- Revenue Rs. 10 Crore
- Eligible for taxation under Article III of the India-France DTAA, which allows taxation based on net business profits instead of the presumptive taxation method under Section 44BB of the Income-tax Act (ITA).
- Under DTAA, net profit after allowable expenses is ₹2 crore, leading to a tax liability at 30% + Surcharge(as applicable) + Cess for non-residents.
- Under Section 44BB, 10% of gross receipts (₹1 crore) would be taxable, leading to a tax liability at 30% + Surcharge (as applicable) + Cess for non-residents.
- Since **Section 44BB results in lower tax liability**, Mr. X opts for ITA for this income.

Illustration

2. Income from Royalties Received from an Indian Company

- Revenue Rs. 1 Crore
- Under the Income-tax Act, royalty income is taxed at 20%+Surcharge(as applicable) + Cess for non-residents.
- Under Article XII of the India-France DTAA, royalty income is taxed at a concessional rate of 10%
- Since **DTAA is more beneficial**, Mr. X opts for DTAA for this income**.**

Illustration

Mr. X strategically chooses the more beneficial provisions for each source of income in the same assessment year:

- For business income (offshore drilling), he opts for ITA (Section 44BB) to reduce taxable income.
- For royalty income, he opts for DTAA to avail a lower tax rate.

This illustrates that **an assessee can apply different tax regimes to different income sources within the same year, as per Section 90(2) of the ITA**.

Judicial Precedents in India

❖ **IBM World Trade Corportaion vs Addl. DIT(IT) [2015] 58 taxmann.com 132 (Banglore – Trib.)**

- Under Indian tax law, **Section 90(2)** of the Income Tax Act, 1961, provides that a taxpayer can apply the provisions of a DTAA if they are more beneficial than the domestic tax law.
- The taxpayer should be able to **choose the most beneficial tax rate for each segment of income separately** (i.e., royalty, software sales, technical services).
- For agreements entered **before 1st June 2005**, the tax rate was **20%** under ITA, but **15% under DTAA**—so DTAA should apply
- For agreements entered **on or after 1st June 2005**, the tax rate was **10% under ITA**, which is lower than DTAA's **15%**, so ITA should apply

Our Comments

- ❖ Various other judgements having the same view as above judgements are as under:
- Indium IV (Mauritius) Holdings Limited vs DCIT (IT) ITA NO. 2423/MUM/2022 (A.Y: 2017-18)
- Director of Income tax, (IT) v IBM World Trade Corporation [2020] 120 Taxmann.com 151 (Karnataka)
- ❖ There is no restriction on the assessee that he can not choose different option for different stream of income, he can adopt the interpretation which is more favourable to the taxpayer for different stream of income.
- ❖ Different stream of income can be considered as different source of income irrespective of the head of income.

Reference of Previous SITG of Back to Basic Principles Series

S.No	Particulars	Link
1.	Right to Choose Between DTAA and IT Act	Click here
2.	If two views possible, view which is favourable to taxpayer should be adopted	Click Here

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