ISSUES OF EMPLOYMENT FACED BY EMPLOYERS HIRING FOREIGN NATIONALS IN INDIA

INTRODUCTION

India is having the world's second largest labour force. However, there is a lot of complicity with regard to employment laws prevailing in India. The labour laws prevailing in India are influenced by the International treaties and conventions. Having regard to foreign judgment, the court many times interprets those foreign laws not being inconsistent with the Constitution and the prevailing domestic laws. Applicability depends on the consistency, competency of courts and Jurisdiction.

SCOPE OF EMPLOYMENT REGULATION

- Laws applicable to foreign nationals

All labour laws regulating employment relationships in India also apply to foreign nationals working in India. These include the Employees' Provident Fund and Miscellaneous Provisions Act 1952 (EPF Act), Employees' State Insurance Act 1948 (ESI Act), Industrial Disputes Act 1947 (ID Act), Maternity Benefit Act 1961 (MBA) and the Payment of Bonus Act 1965 (PBA).

- Laws applicable to nationals working abroad

Indian labour law does not apply to Indian nationals who are employed by foreign entities abroad.

TAXATION OF EMPLOYMENT INCOME

Foreign nationals

Foreign nationals are subject to income tax in India on all their income derived from a source in India or received in India during the relevant tax year (subject to any exceptions under a double taxation treaty).

This income also includes income deemed to be received or deemed to accrue/arise in India. Generally, income from salaries is deemed to accrue or arise in India if the services are rendered in India. However, for an individual who is not a citizen of India, section 10(6)(vi) of the Income Tax Act 1961 (ITA) provides that the remuneration received by him as an employee of a foreign enterprise for services rendered by him during his stay in India will be exempt from income tax subject to the following conditions being fulfilled:

- The foreign enterprise is not engaged in any trade or business in India.

- The foreign national's stay in India does not exceed in the aggregate a period of 90 days during the relevant tax year.
- The remuneration received by the said foreign national is not liable to be deducted from the income of the foreign enterprise chargeable to tax in India.

Where a foreign national comes to India and is present in India for a period of 182 days or more during the relevant tax year, he will be considered resident in India. However, for the initial few years (two or three years, depending on his date of arrival and the number of days stay in India), he will be considered as not ordinarily resident for tax purposes and the following income will be subject to tax in India:

- Income received, or deemed to be received, in India.
- Income accrued or arising, or deemed to accrue or arise, in India.
- Income accrued or arising outside of India in relation to a business controlled, or a profession set up, in India.

Thereafter, once he becomes "ordinarily resident" in India, his global income is taxable in India.

Nationals working abroad

As a general principle, the global income of an individual who is "ordinarily resident" in India is chargeable to tax in India, including all incomes which accrue or arise outside India during the relevant tax year.

However, if this person's stay in India is for less than 182 days in aggregate during the relevant tax year, such person would be considered a non-resident in India for that year. In this case, the person would be liable for tax in India only for income derived from a source in India or received in India during the relevant tax year, including income deemed to be received or deemed to accrue or arise in India (subject to any exceptions under an applicable double taxation treaty).

WHO ARE EXPATRAITES?

The term 'Expatriate' is derived from Latin (ex-patria) which means "out of the country". The Oxford Dictionary defines an expatriate as a 'person living abroad'. Technically, an expatriate is a person temporarily or permanently residing in a country and culture other than that of his/her upbringing or legal residence. Thus, in the Indian context expatriate means a resident of foreign country working in India (inbound) or an Indian resident working abroad (outbound).

ISSUES AFFECTING EXPATS

Taxation of employees working abroad on ship or aircraft

In terms of Articles 8/9 of the applicable DTAAs(Double Taxation Avoidance Agreements) dealing with air transport and shipping business, the remuneration in respect of an employment exercised aboard on a ship or aircraft in international traffic may be taxed in the country of which the person deriving the profits from the operation of the ship or aircraft is a resident.

Taxation of director's fees

Director's fee is the remuneration received by an individual, in the capacity of a member of a board of directors of a company. Services are deemed to have been rendered in the country where the company is a resident. Remuneration would cover all payments in cash and kind.

Taxation of accidental expatriates

An accidental expatriate is an employee who has travelled overseas enough so as to trigger taxation in that country. Besides taxation, accidental expatriates may trigger immigration and permanent establishment risks for the employer in that country. For instance, a business visitor to India whose business visits aggregate to a physical presence of more than 182 days in the given financial year would be an accidental expatriate. The employer would be required to comply with the withholding tax requirements in respect of such expatriate and might be exposed to interests and penalties for delay in withholding and deposit of tax.

Tax residency certificate

In order to claim relief under DTAA, Section 90 of the ITA has been amended to provide for an additional requirement. Sections 90 (4) and 90A(4) of the ITA provide a condition for submission of tax residency certificate to avail the benefits under a DTAA. The certificate would have to be obtained from the Revenue Authorities of the host country. Further, a standard format has also been issued for making an application for requesting tax residency certificate from the Indian tax office if the individual qualifies as a resident of India, where the certificate is required by the authorities of another country.

Obligation to pay Gratuity

As per Section 4 of the Payment of Gratuity Act, 1972, gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than five years;

- On his superannuation, or
- On his retirement or resignation, or
- On his death or disablement due to accident or disease.

The expatriates who have already rendered five years of services reserve the right to claim gratuity from the Indian employer at the time of termination.

SOCIAL SECURITY IN INDIA

Provident Fund Obligation in India Social Security in India is governed principally by the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (the PF Act) and is operated through the following schemes:

- Employees Provident Funds Scheme, 1952 (PF Scheme)
- Employees Pension Scheme, 1995 (Pension Scheme)
- Employees Deposit Linked Insurance Scheme, 1976 (EDLI)

The PF Act applies to establishments employing 20 or more persons engaged in a specified industry or notified by the Central Government from time to time or establishments which has opted for voluntary coverage under the PF Act.

Applicability of Indian Social Security Schemes to International Workers

In October 2008, the Government of India issued notifications extending the applicability of PF Act to a new category of workers called 'International Workers' requiring them to mandatorily contribute into its schemes effective 1 November 2008. 'International Worker' has been defined to mean:

- Indian employee having worked or going to work in a foreign country with which India has a Social Security Agreement (SSA) and satisfying the conditions as prescribed in such SSA;
- Non-Indian employees, not holding an Indian passport, working for a covered establishment in India to which the PF Act applies (coming from a country with which India has not entered into a SSA).
- A 'covered establishment' is –

— an establishment employing 20 or more persons engaged in a specified industry or notified by the Central Government from time to time.

— any establishment employing even less than 20 persons that has opted to be covered voluntarily under the PF Act.

Contribution for International Workers

The employer is required to contribute 24% of employee's 'Monthly Pay' under the schemes and has option to recover 12% of 'Monthly Pay' from employee's salary. The 24% contribution in case of International workers will be split as follows:

- 12% of 'Monthly Pay' as employee's contribution to PF Scheme
- 8.33% of 'Monthly Pay' as employer's contribution to Pension Scheme
- 3.67% of 'Monthly Pay' as employer's contribution to PF Scheme. Withdrawal from the Provident Fund Scheme International Workers will be entitled to withdraw accumulated balance in the Provident Fund Scheme in the following circumstances:
- On retirement from service after attaining the age of 58 years;
- On permanent and total incapacity;
- On ceasing to be an employee of a covered establishment in respect of an International Worker covered under a SSA. Accordingly, in case where an International Worker is not covered under a SSA entered into between India and any other country, accumulated balances in Provident Fund account will be not be refundable until the International Worker retires after attaining the age of 58 years (subject to certain exceptions).

Social Security Agreements

India has currently signed SSA with 17 countries and out of which, as on today agreements with Netherlands, Korea, Belgium, Germany, Switzerland, Luxembourg, France, Hungary and Denmark have been entered into force.

The various advantages of signing an SSA are:

- Ø **Detachment-CoC**

A CoC is a confirmation from home country social security authorities that the individual is covered under home country social security and continues to be covered during the period of assignment. Foreign passport holders can obtain CoC in home country and claim exemption in India. Likewise, Indian passport holders can obtain CoC in India and claim exemption in host country with which India has an SSA. One of the eligibility conditions of detachment is the requirement for the employee to work in the host country on behalf of the home country entity. This could lead to a potential Permanent Exposure.

- Ø **Equality of treatment**

An SSA ensures that persons who ordinarily reside in either country receive equal treatment with the nationals of that country in the application of the social security legislation.

- Ø **Export of benefits**

SSAs contain provision for payment of benefits to the International Workers irrespective of the location (India, home country or a third country).

- Ø **Totalization of periods**

Totalization of periods means aggregation of time spent in home country and host country to determine eligibility to social security benefit. International Workers who contribute to social security in both countries are eligible to aggregate periods covered in both countries to determine eligibility to pension benefits in either country. Aggregation of periods is permissible only for determining eligibility and not for the purpose of determining actual level of benefit payable.

JUDICIAL APPROACH TOWARDS EXPATS

THE COMMISSIONER OF INCOME TAX V. JAYDEV H. RAJA (Income tax appeal No. 87 OF 2000)

FACTS OF THE CASE:

The respondent-assessee a resident but not ordinarily resident individual was an employee of Coca-Cola Inc. USA and had income under the head "Salaries". Under the Tax Equalization Policy framed by the said company, the assessee's tax liability arising out of his foreign assignment was to be borne by the company but restricted only to the extent of liability arising out of such foreign assignment. As the assessee had foreign assignment in India during the assessment year in question, the company under its tax equalization policy was liable to reimburse the tax payable on total salary which the assessee was entitled to receive in India.

ISSUES BEFORE THE COURT :

- Whether on the facts and circumstances of the case and in law, the Tribunal was justified in holding that tax borne by the employee is not part of the pay?
- Whether on the facts and circumstances of the case and in law the Tribunal was justified in holding that notional interest on interest free deposit made for accommodation is not part of perquisite of the assessee?

DECISION:

It was held that though the assessee had paid tax of Rs.50.00 lakhs, since the assesses was entitled to reimbursement of Rs.35.00 lakhs from the Company, the salary income (Rs.77.00 lakhs) received by the assesses had to be enhanced by Rs.35.00 lakhs only and not the balance Rs.15.00 lakhs which is paid by the assesses from the salary income. In these circumstances, the Tribunal was justified in holding that the tax amounting to Rs.15.00 lakhs paid by the assessee from the salary income (not reimbursed by the company) could not be added to that income of

the assessee. Accordingly the first question cannot be entertained. As regards the second question is concerned, the Tribunal has allowed the claim of the assesee by following the decision of this Court in the case of M.A.E. Paes reported in 230 ITR 60 where the court held that it will be open to the Tribunal to accept the fair rental value shown by the assessee which is higher than the municipal valuation or if it is not satisfied about the correctness of the same, to determine the same by applying the principles laid down under the Rent Control Act for fixation of the standard rent. Thus, The Mumbai High Court in the case of a resident but not ordinary resident held that only actual reimbursement of tax by his overseas employer can be treated as his perquisite and taxed accordingly. Any tax which is borne by the assessee cannot be treated as his income. The High Court reaffirms the Delhi High Court ruling on hypothetical taxes not forming part of the taxable salary of an employee.

ACIT

ROBERT ARTHUR KELTZ (3452/DEL/2011)

FACTS OF THE CASE:

An employee of United Technologies International Operation, a company based in the USA ("**UTIO**"), was granted ESOP for 34,000 shares in January 2004 with a vesting period of 3 (three) years from the date of grant. He was sent on secondment to UTIO's Indian liaison office in April 2006. He exercised the stock options in February 2007 while on his assignment in India.

The employee filed his income tax return for the financial year 2007-2008 as an RNOR and offered to tax such fraction of the ESOP perquisite equal to the fraction of the vesting period for which he excised employment in India. However, the Income-tax Assessing Officer ("**AO**") ruled that Employee's taxable income would include the total ESOP perquisite. In appeal, the Commissioner of Income Tax (Appeals) reversed the AO's order.

DECISION:

In further appeal, the ITAT noted that Employee's operation from outside India during the remainder of the vesting period of the ESOP (which was prior to Employee R's deputation to India) did not involve the performance of any service connected with any India-specific job or activity. Hence, the Delhi Tribunal held that as the employee has not rendered service in India for the whole grant period of stock option, only such proportion of the stock options as is relatable to the service rendered in India during the grant period is taxable in India.

DIT

SEDCO FOREX INTERNATIONAL DRILLING INC (TS-603-HC-2012)

FACTS OF THE CASE:

The employer entered into an agreement with its employees pursuant to which the employer agreed to bear the income tax payable by the employees on their salary. The question was

whether such tax payment was "income" in the nature of a perquisite, not provided for by way of monetary payment, within the meaning of clause (2) of Section 17 of the ITA and hence eligible for exemption under Section 10(10CC) of the ITA.

DECISION:

The High Court held that the tax on the salary paid by the employer was a "perquisite" under Section 17(2)(iv) of ITA because it was paid in respect of the employees' obligation and it was not by way of monetary payment to the employees concerned but for or on their account to the Income-tax department. Consequently, "non-monetary" payment of a perquisite to the employee which is eligible for exemption under Section 10(10CC).

YOSHIO KUBO vs COMMISSIONER OF INCOME TAX (ITA No 441/2003/Del)

ISSUES:

- Whether the amounts paid towards income tax by the employer on behalf of the assessee non-monetary perquisites, and do they consequently fall within the scope of Section 10 (10CC) of the Act?
- Whether social security, pension and medical insurance contributions to be analysed in regard to expats?
- Whether taxes are to be excluded while computing the perquisite value of rent free accommodation provided to an employee, in view of Rule 3 of the Income Tax Rules, 1962?
- Hypothetical Tax
- Whether the tax is to be subject to multiple stage grossing up process under Section 195-A of the Finance Act ,2002?
- Assessability of TDS refunds received by the employee.
- Legal expenses incurred

DECISION:

The Court answering each of the issue , held that:

- Amounts paid by the employer, directly to the Indian income tax authorities, in discharge of an employee's income tax liability do not fall into the category of monetary benefits. Hence, the same is eligible for exemption under Section 10(10CC) of the ITA.
- Employer contributions to overseas social security, pension and medical insurance plans are not taxable if such contribution does not result in any direct present benefit to the employee but assures him/her of a future benefit subject to certain contingencies.

- Tax paid the by employer is excluded from the definition of salary for the purpose of valuing accommodation benefits provided by the employer.
- A deduction on account of hypothetical taxes is allowed from the salary income of employees covered under the employer's tax equalization policy.
- The tax paid by the employer on behalf of the employee is a non-monetary perquisite. In other words, taxes paid by the employer can be added only once in the salary of the employee. Thereafter, tax on such perquisites is not to be added again. Whenever tax is deposited in respect of a non-monetary perquisite, the provision of Section 10 (10CC) applies, thus excluding multiple stage grossing up. Thus, Section 195-A would be inapplicable.
- A refund of excess tax ultimately due to the employer is not treated as a taxable benefit for the employee since the employee is obliged to repay the refund back to the employer and does not derive any benefit from it.
- Fees paid by an employer to a tax consultant for tax compliance for expatriates are not considered to be a taxable benefit.

EMIL WEBBER V. COMMISSIONER OF INCOME TAX, V&M, NAGPUR AIR 1993 SC 1466 (200 ITR 483)

ISSUE:

Whether the amount of tax paid by Ballarpur on behalf of the assessee in assessment years 1974-75 and 1975-76 is income tax are under the heading 'other sources'?

DECISION:

It was held that the tax liabilities actually borne by an employer on behalf of an employee would form part of the salary base of the employee by virtue of being accrued income of the employee (as it the employee's obligation for which it is applied).

GALLOTTI RAOUL V. ACIT (MUMBAI ITAT) (61 ITD 453)

ISSUES:

- Whether the salary for the period when the assessees were out of India should be treated as salary earned in India and brought to tax on that basis ?
- Whether the social charges which these foreign nationals are liable to contribute in France should be treated as if the French national has an over-riding title on the income from salary of French nationals and thereby it is only the net of salary be taxed or the gross salary without adjustment of the social charges?

DECISION:

It was held that:

- The salaries of the assessees should be taxed in India only to the extent of the period of stay in India based on "Article XIV(1)of DTAA with France, subject to the provisions of Article XII salaries, wages or other similar remuneration for services as an employee performed in one of the contracting States by an individual who is a resident of the other Contracting State may be taxed only in the Contracting State in which such services are rendered."
- The Mandatory contribution by the employer towards the social security in the home country of the employee (foreign national), wherein no benefit/ right gets vested in the year of contribution should not be considered as a taxable perquisite in hands of such employee. The affiliation being compulsory, making the social security organisation an earning partner alongside of the assessee, i.e.., the assessee earns not only for himself but also for the social security organisation, the extent of the amount relatable to social security organisation, the assessee has no right over it at all and thereby no domain on it. Hence the social security charges are to be deducted from the salary income as a prior charge by overriding title and it is only the net salary after such deduction that should be treated as gross salary within the meaning of Section 16of the I.T. Act.

Commissioner of Income-tax, New Delhi V. M/s Eli Lilly & Company (India) Pvt. Ltd.(2009)

ISSUE:

Whether Tax deductions provisions in Chapter XVII-B, which are in the nature of machinery provisions to enable collection and recovery of taxes, are independent of the charging provisions which determines the assessability of income chargeable under the head "Salaries" in the hands of the recipient?

DECISION:

The Court held that:

The TDS(tax deduction) provisions in Chapter XVII-B relating to payment of income chargeable under the head "Salaries", which are in the nature of machinery provisions to enable collection and recovery of tax forms an integrated Code with the charging and computation provisions under the 1961 Act, which determines the assessability/taxability of "salaries" in the hands of the employee-assessee. Consequently, Section 192(1) has to be read with Section 9(1)(ii) read with the Explanation thereto. Therefore, if any payment of income chargeable under the head "Salaries" falls within Section 9(1)(ii) then TDS provisions would stand attracted. In this batch

of civil appeals, identification of the recipient of salary is not in dispute. Therefore, the tax-deductor- assessee were duty bound to deduct tax at source under Section 192(1) from the Home Salary/special allowance(s) paid abroad by the foreign company, particularly when no work stood performed for the foreign company and the total remuneration stood paid only on account of services rendered in India during the period in question.

CONCLUSION

In international relations it is common for foreign employees being transferred from one country to another for certain projects or contract. Such that now in public relations many agreements are entered into by the nations as to safeguard and protect such employees. Yes , it can be argued that rate of employment in India is already in crisis hence what's the need to import employees, but that's the way transfer of technology can be done , thus improving the economic growth of India. It's the duty of Government to take care of the employees and resolve the issues arising with their entry in India. Laws should be framed as well as require to be flexible as to permit to work only , not to stay and increase the population of India.