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## Sovereign right to tax shipping income only by resident state upheld

The Chennai Bench of the Income-tax Appellate Tribunal (ITAT) rendered its decision that under the provisions of India-Singapore tax treaty, the 'Sovereign right' to tax shipping income vests only with the resident state and the limitation of benefits [LOB] provisions are not applicable in such cases.

### Background:

- The taxpayer[1] is a tax resident of Singapore and involved in the business of operation of ships in international traffic.
- The taxpayer was the freight beneficiary in respect of various vessels which sailed from ports in the Indian sub-continent and South East Asia during the Financial Year (FY) 2014-15, corresponding to Assessment Year (AY) 2015-16. The taxpayer did not have a permanent establishment in India.
- The AO had issued a double income-tax (DIT) relief certificate for the relevant AY 2015-16, where relief was granted to the taxpayer in respect of the shipping income from operation of ships in international traffic which was not taxable in India by virtue of Article 8 of the India-Singapore tax treaty.

  Article 8 of the India-Singapore tax treaty provides that, the income from shipping operation is taxed only in the country of residence (i.e. Singapore in the current case).
- For the FY 2014-15, corresponding to AY 2015-16, the taxpayer filed its tax return in India, claiming exemption from tax on income received from shipping operations in India pursuant to Article 8 of the India-Singapore tax treaty.
- During the assessment proceedings, the Assessing Officer (AO) rejected the taxpayer's contention that shipping income was not taxable in India by virtue of Article 8 of the India-Singapore tax treaty and brought to tax the shipping income attributable to Indian operations. The contentions of the AO were as under:
  - Article 8 of the India-Singapore tax treaty should be read with Article 24 of the India-Singapore tax treaty (as per which only such income could be given treaty benefit in India which had suffered tax in Singapore, i.e. an income which was not taxed in Singapore could not be granted tax exemption in India).
  - The purpose of the treaty was avoiding double taxation and not to facilitate double non-taxation;

[1] Bengal Tiger Line Pte Ltd. v. DCIT (ITA No. 11/CHNY/2020) (Chennai ITAT)

- The said income was not taxed in Singapore by virtue of Section 13F of the Singapore Income-tax Act (Singapore ITA). The taxpayer had claimed exemption of the income in both the countries. Therefore, there was no income which was being doubly taxed in order to invoke the provisions of the India-Singapore tax treaty and hence, the said income was taxable in India.

  The AO also rejected the certificate / letter issued by the Inland Revenue Authority of Singapore (IRAS) stating that international shipping income was taxable in Singapore on accrual basis.

- On objections filed by the taxpayer, the Dispute Resolution Panel (DRP) upheld the AO's order and the AO finalised the order based on DRP's directions.
- Aggrieved by the final order of the AO, the taxpayer filed an appeal before the Chennai Bench of the Income-tax Appellate Tribunal (ITAT).

## Decision of the ITAT:

- The ITAT noted the following:
  - The taxpayer was a tax resident of Singapore and did not have a permanent establishment in India.
  - As per Article 8 of the India-Singapore tax treaty, profits derived by an enterprise of a Contracting State (i.e. Singapore in the current case) from the operation of ships or aircraft in international traffic were taxable only in that state (i.e. Singapore in the current case).
  - Article 24 of the India-Singapore tax treaty contemplated twin conditions for its applicability. The first condition was that income was sourced in a Contracting State and such income was exempt or taxed at a reduced rate by virtue of any Article under the India-Singapore tax treaty. The second condition that was required to be looked into before applying Article 24 of India-Singapore tax treaty was income of the non-resident should be taxable on 'receipt' basis in state of residence.
- After noting the above and the detailed arguments put forth by the taxpayer and the Revenue, the ITAT held that:
  - Article 8 of the India-Singapore tax treaty did not provide exemption, it vested the exclusive right of taxation of shipping income to the country of residence. India, by entering into tax treaty with Singapore, had given up its right to taxation of shipping income of a non-resident in India.

    The provisions of Article 24 of the India-Singapore tax treaty were applicable for income which was exempt from tax as per the India-Singapore tax treaty.
  - The twin conditions of Article 24 of the India-Singapore tax treaty [i.e. limitation of benefits (LOB) clause] were not satisfied in the taxpayer's case. Firstly, Article 8 of the India-Singapore tax treaty contemplated the taxation rights of a particular income in a particular state and did not provide for exemption or reduced rate of taxation of such income. Secondly, the letter dated 17 September 2018 of the Inland Revenue Authority Singapore, clarified that the income of a

Singaporean company from the operation of ships in international traffic was taxable in Singapore on 'accrual' basis.

- Section 13F of the Singapore ITA was already in existence since 1 April 1991 even before the India-Singapore tax treaty came into existence (i.e. on 27 May 1994). Accordingly, the competent authorities of both the contracting states, after being fully aware of the local income-tax exemption in Singapore, chose not to alter the taxation right of shipping income which was generally available to the country of residence.
- Although profits derived by an international shipping enterprise was exempted from taxation as per section 13F of the Singapore ITA, but such income was always liable to tax in Singapore. The liability to taxation was not dependent on whether taxes were actually paid in the said jurisdiction – the ITAT placed reliance on the earlier Supreme Court's case[2] in this regard.
- In order to give ordinary meaning to the terms in their context, the whole treaty should be read as it is without giving any meaning which was not the purpose intended by the Articles. In the current case the AO had misunderstood the general rules of interpretation in the Vienna Convention by stating that preamble should be read to understand the object and purpose.
- The two sovereign nations had entered into a bilateral agreement and specifically agreed on the taxing rights of particular streams of income, the provisions of such agreement were to be merely given effect to. As such, the action of the AO to claim taxing right over the said income which was not provided in the India-Singapore tax treaty was ultra vires the power of the AO and amounted to dishonouring the bilateral agreement between two sovereign nations.

  Once the country of residence was having exclusive rights to tax a particular income by way of a separate Article, then limiting or denying such benefit by interpreting the other Articles which were provided for limiting the benefit in case such income was exempt or taxed at reduced rate in the other Contracting State, was contrary to the purpose and object of the tax treaty.
- The AO had also ignored the fact that DIT relief certificate had been issued by the tax department for the subject AY, where the AO after considering the tax residency certificate and supporting documents, held that Article 8 of the India-Singapore tax treaty was applicable to the taxpayer and income from operation in international traffic was not taxable in India. Since no change in law or in facts had been brought on record by the AO, no contrary view could be taken.

Accordingly, the ITAT held that shipping income of the taxpayer was not taxable in India, whereas taxable only in Singapore by virtue of Article 8 of the India-Singapore treaty and allowed the appeal in favour of the taxpayer.

[2] Union of India vs. Azadi Bachao Andolan [2003] 132 Taxman 373 (SC)

## Comment:

This ruling reaffirms the principle that:

- Article 8 of the India-Singapore tax treaty allocates the taxation rights of a particular income to a particular state which is different from exemption or reduced rate of taxation.
- No extraneous conditions can be imposed for application of the provisions of a tax treaty when two sovereign nations have entered into a bilateral agreement and specifically agreed on the taxing rights of a particular stream of income.
- The liability to taxation is not dependent on whether taxes are actually paid in the said jurisdiction.

This ruling is comprehensive and it has considered various judicial pronouncements on interpretation of tax treaties including the Vienna Convention while interpreting the LOB clause.

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