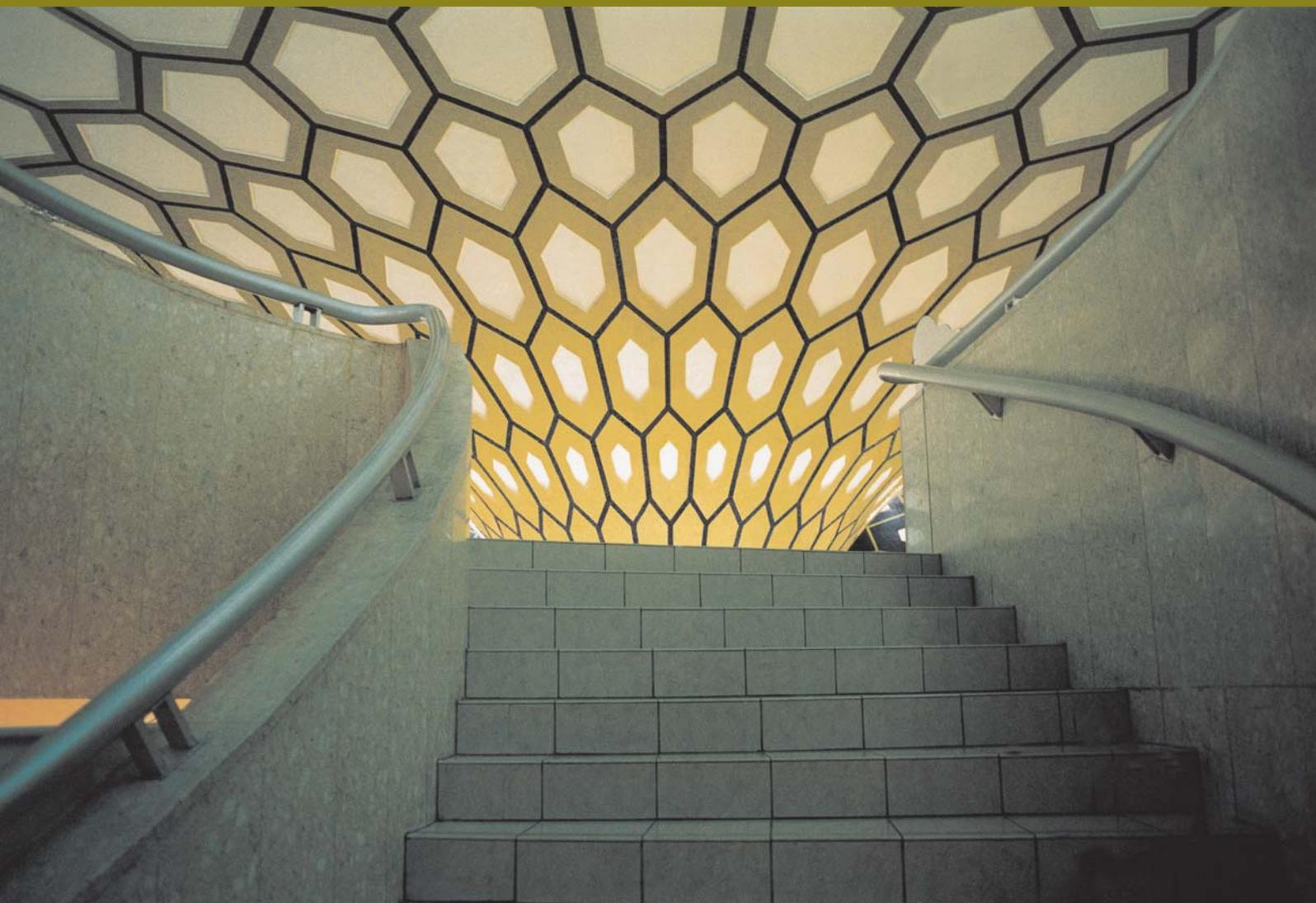


Foreign Nationals Working in India



Foreign Nationals Working in India

PricewaterhouseCoopers
India

August 2005

This booklet is prepared by PricewaterhouseCoopers to provide foreign nationals going to work in India with a broad view of tax laws. It reflects the current tax law or practice in India prevailing in August 2005.

This booklet is not intended as a comprehensive or exhaustive study, but merely as an explanatory guide. We would strongly recommend readers to seek professional advice before making any decisions.

For further information, please contact PricewaterhouseCoopers offices in India (See Appendix E)

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Section 1 Understanding the basic principles

The scope of taxation

1. Tax incidence of an individual solely depends upon his residential status, which in turn depends on his physical presence in India. If an individual is resident and ordinarily resident, worldwide income of the individual is liable to tax in India. If an individual is resident but not ordinarily resident, income received in India or accruing/arising from a source in India or income derived from a business controlled or profession set up in India is liable to tax in India. If an individual is considered non-resident, income received in India or accruing/arising from a source in India is liable to tax in India. There is no special tax regime for expatriates.

The tax year

2. The Indian tax year commences on 1st April and ends on 31st March of the succeeding year.

Method of calculating tax

3. Individuals are taxed on a graduated scale after certain deductions and allowances (See Appendix A).

Determination of residential status

4. Residential status of an individual can be classified as under:
 - i Resident in India
 - Resident and ordinarily resident (ROR) and
 - Resident but not ordinarily resident (RNOR)
 - ii Non-resident in India (NR)

An individual is treated as Resident in India if any one of the following conditions is satisfied:

(a) Individual's stay in India is 182 days or more in any tax year; OR

(b) Individual's stay in India is 60 days or more in the relevant tax year and 365 days or more in aggregate in the 4 tax years immediately preceding the tax year for which residential status is determined.

If none of the above conditions is fulfilled, the individual is treated as NR. It is not essential for the stay in India to be continuous or at the same place.

A resident individual is treated as RNOR in India if he satisfies any one of the following conditions:

(i) The individual is NR in India in at least 9 out of 10 tax years preceding the tax year for which residential status is determined; OR

(ii) The individual is physically present in India for 729 days or less during 7 tax years preceding the tax year for which residential status is determined.

A resident individual not satisfying both the conditions mentioned above [(i) and (ii)] is treated as ROR.

By practical implication, an expatriate coming to India for the first time may enjoy the status of RNOR for the initial 3-4 tax years depending upon the timing of his arrival in India. However, facts and circumstances need to be analyzed for each case for determining the residential status.

In case an individual is a ROR in India in any given tax year, he is taxable in India on his worldwide income. However if such individual is also a resident of a country with which India has entered into a Double Taxation Avoidance Agreement (DTAA), the residency aspect may be resolved under the tie breaker clauses of the relevant DTAA. A detailed analysis needs to be undertaken before finalizing the position in this regard.

Section 2 Understanding the Indian tax system

The taxation of employment income

- 5.1 Remuneration earned by the expatriate employees for rendering services in India is deemed to accrue or arise in India irrespective of the place of payment. Salary includes both cash components and perquisites provided to an employee in connection with his Indian assignment.
- 5.2 Cash components are fully taxable in India. Certain perquisites such as housing and furnishings are taxable on concessional basis. However, there has been a significant amendment to the taxation of perquisites provided to employees consequent to the introduction of 'Fringe Benefit Tax' (FBT) with effect from tax year 2005 - 06.
- 5.3 Prior to the introduction of the FBT regime, perquisites were being concessionally taxed (housing, car, free meals etc.) or were being taxed at the actual cost incurred for providing the benefits. Consequent to the introduction of the FBT regime, perquisite valuation has also undergone a change whereby certain perquisite valuation rules (such as car, free meals, gifts, etc.) have now been omitted. Such benefits are no longer taxable in the hands of the employees but shall be subject to FBT.
- 5.4 Under the FBT regime, an employer is liable to pay FBT at an effective rate of 33.66% on the value of prescribed fringe benefits provided /deemed to be provided to its employees. The fringe benefits/deemed fringe benefits which have been specified in this regard are enclosed as Appendix B. The value of fringe benefits/ deemed fringe benefits so provided to the employees is calculated on the basis of rules prescribed in this regard.
- 5.5 The benefits which are taxable in the hands of the employees as perquisites are not subject to FBT.
- 5.6 FBT will apply to foreign companies [including Liaison Offices (LO)] if it has employees based in India. However, if all the employees of the foreign company who are based in India are not subject to tax in India, there will be no FBT implication on the foreign company.

- 5.7 An employer is required to pay FBT on a quarterly basis and to file an annual FBT return with the Indian tax authorities in respect of fringe benefits/deemed fringe benefits provided to its employees during the tax year.

Housing

- 6 Housing benefit is generally valued at 20% of salary or rent paid by the employer for the accommodation, whichever is less. Further, in case of furnished accommodation, the value of housing benefit is increased by 10% per annum of the actual cost of furniture owned by the employer and in case of hired furniture, actual hire charges is added. Hotel accommodation is taxable at 24% of salary or hotel rent paid by the employer, whichever is less, except where such accommodation is provided for a period not exceeding 15 days on transfer from one place to another. Accommodation provided in a remote area to employees working in mines, project execution sites etc. is not taxable.

Other perquisites

- 7 Other perquisites such as domestic help, security guards, utilities, free or concessional education are taxable at the actual cost to the employer. Further, benefit from use of moveable assets provided by the employer to its employees (other than laptops and computers) and transfer of such moveable asset to the employee is taxable on concessional basis. The benefit arising to the employee from interest free or concessional loan given by the employer is taxable at notional rate of interest as prescribed under the Indian tax laws.

Social security and pension plans

- 8 India does not have any social security law in place. Certain statutes providing for employee benefits are mandatorily applicable only for employees drawing salary not more than Rs. 6,500 per month. The tax laws in India do not provide for any special provision for taxation of contributions, if any, made by the employer towards social security or other pension/benefit schemes in the home country of the expatriates. A detailed study of such schemes should be carried out to analyze the point of tax incidence of such contributions made by the employer.

Stock options

- 9 Taxation of stock options granted to the employees depends on whether stock option plan/scheme is qualified or non-qualified under the Indian tax laws. Income arising under a qualified stock option scheme is taxable as capital gains at the time of sale of shares by the employee. However, benefit arising under an non-qualified stock option scheme is taxable as employment income at the time when the options are exercised by/allotted to the employee and subsequently as capital gains at the time of sale of shares. A stock option scheme is considered to be qualified under the Indian tax laws if the same is in accordance with the guidelines issued by Indian Central Government in this regard and a copy of the plan along with other documents has been filed with the Indian tax authorities within the prescribed time limit from the date of its implementation. A detailed study of stock option plan is recommended to analyze the tax incidence.

Exemptions and deductions

- 10.1 Remuneration paid to an employee of foreign enterprise who is not a citizen of India for rendering services in India is not taxable if his aggregate stay in India does not exceed 90 days during the relevant tax year and the following conditions are satisfied:
- (a) his employer is not engaged in any trade or business in India and
 - (b) remuneration paid to the individual is not liable to be deducted while computing the taxable income in India of such employer.
- 10.2 An individual being a tax resident of a country with which India has entered into a DTAA (See Appendix D) and who is coming to work in India, may remain liable to tax in the country of his residence even while he is on assignment to India provided the conditions as prescribed under the 'Dependent Personal Services' clause of the relevant DTAA are fulfilled. In most of the DTAA's India has with other countries, the following conditions have generally been prescribed:
- (a) The aggregate stay of the individual in India is less than 183 days in the relevant tax year;
 - (b) The remuneration is not paid by, or on behalf of an employer who is resident in India;
 - (c) The remuneration is not borne/deductible by a permanent establishment or a fixed base of the employer in India.
- 10.3 Tax borne by the employer on behalf of the employee is taxable as additional income in the hands of the employee except for the tax borne by the employer at his option on the non-monetary perquisites provided to the employee. However, the tax borne by the employer on non-monetary perquisites would not be allowed as a deduction in computing the employer's taxable income in India.
- 10.4 Individuals are entitled to a deduction from their gross total income on account of investments in eligible securities, payment of life insurance premium, contribution to provident fund, contribution to certain pension funds, payment towards children tuition fee and other specified payments up to a maximum amount of Rs. 100,000 per annum.

Obligations of the employer-regulatory

- 11.1 Under the provisions of Foreign Exchange Management Act, 1999 (FEMA), a Foreign Company is required to obtain approval from Reserve Bank of India (RBI) for setting up a LO or Branch Office (BO) in India. Establishment of a Project Office (PO) in India ordinarily does not require RBI approval. However, certain post facto filings are required to be completed with the concerned Regional Office of RBI (under whose jurisdiction the Project Office is set up). All Foreign Companies intending to depute their expatriate employees in India must review their business model to evaluate whether such deputation will tantamount to setting up an office in India. If that is the case, RBI approval (for a LO/ BO)/ post facto filings with RBI (for a PO) would need to be undertaken.
- 11.2 After the office is set up, the Foreign Company is required to be registered with the Tax and Company law authorities [Registrar of Companies (RoC)]

within the prescribed time period.

- 11.3 Representative offices of Foreign Companies operating in India are required to open and maintain a bank account in India through the inward remittances brought from Head Office and meet all the expenses of Indian office from this account.
- 11.4 The local offices are required to maintain books of accounts in India and get them audited on an annual basis. Further, there are annual reporting requirements that are required to be undertaken with RBI and RoC.

Obligations of the employer-tax

- 12.1 Under the provisions of Indian tax laws, the employers are required to deduct tax at source from the employees' salary income and deposit the same with the government treasury on a month to month basis. Delay in depositing tax attracts interest for delay and may also result in penal consequences. As soon as employee commences his assignment, tax based on estimated income for the relevant tax year should be calculated and deposited with the government treasury on a monthly basis.
- 12.2 The requirement of deduction and deposit of taxes is applicable in all circumstances even where the employer company has not set up an office in India.
- 12.3 Certain reporting obligations have been imposed on the employer :
- To file quarterly tax withholding return in the prescribed form (form 24Q) in respect of salary paid and taxes deducted during the quarter.
 - To issue annual tax withholding certificate (form 16) outlining the salary paid and taxes deducted along with a statement in form 12BA disclosing the benefits provided to the employees.
 - To file annual tax withholding return in the prescribed form (form 24) in respect of salary paid and taxes deducted during the relevant tax year.

Section 3 What to do before you arrive in India

Work permit/ Employment visa

- 13.1 Foreign nationals arriving in India for employment must hold a valid employment visa. The Indian Embassy/High Commission located in various Countries issues employment visa to foreign nationals. There are no work permit requirements to work in India. Business/tourist visas are usually not convertible into employment visa while in India.
- 13.2 Current exchange control regulations do not permit the remittance of salary outside India by the employees unless they come on an employment visa.

Section 4 What to do after you arrive in India

Seek registration with FRRO

14.1 Foreign nationals including their family members who intend to stay in India for more than 180 days or have visa for more than 180 days, have to get themselves registered with the Foreigners' Regional Registration Office (FRRO) within 2 weeks of their first arrival in India. For the purposes of registration, the persons are required to make an application in the prescribed form and be present in person at the time of registration. The following documents are required to be submitted along with application:

- Application form in quadruplicate (Form A)
- Passport and visa in original
- 4 passport size photographs
- Proof of residence in India
- Copy of employment contract and undertakings by the employer

Once the FRRO is satisfied about the above documents, a "Residential permit" to stay in India is issued to the foreign national.

14.2 No registration fee is charged by the FRRO for registration of the foreign nationals. However, if the application for registration with the FRRO is not made within 2 weeks from the first arrival in India, a nominal fine is levied.

Registration with income tax authorities

15 Employees are required to seek tax registration (Permanent Account Number) with the Indian Income tax authorities upon their arrival in India. This is a one time registration which is required to be quoted in various correspondences with the tax authorities.

Advance tax

16 A foreign national having income other than salary income taxable in India, is required to pay advance tax in three installments, which are as follows :

- On or before September 15, each year, 30% of total annual tax
- On or before December 15, each year, 60% of total annual tax, as reduced by amount of previous installment
- On or before March 15, each year, 100% of annual tax, as reduced by the amount of previous installments

Annual tax for this purpose is estimated annual tax liability as reduced by the tax deductible at source. Delay or failure to pay taxes in the aforesaid manner attracts penal interest liability.

Section 5 What to do at the end of the tax year

- Filing of income tax return** 17 Employee must file a tax return with the Indian tax authorities on or before 31st July of each tax year even if all the taxes have been deducted at source.

Section 6 What to do at the time of departure

- Tax clearance** 18 At the time of departure from India, employee is required to furnish to the Income tax authorities, an undertaking from the employer to the effect that the tax payable by employee shall be paid by employer. On the basis of said undertaking income tax authority will grant a “No Objection Certificate” to the employee to leave India.

Section 7 Other matters requiring consideration

- Scope for tax planning** 19 Professional advice may help to optimize your India tax burden. It is therefore, important that before coming to India you seek professional advice on the preparation of your employment contract and also the date and time of arrival in India.

- Payment of salaries outside India** 20 Foreign nationals/ Indian citizens who are not permanently resident in India and have been deputed by a foreign company to its office / branch / subsidiary / JV in India are allowed to make recurring remittances abroad for family maintenance up to 100% of their net salary. Further, up to 75% of salary of a foreign national/ Indian citizen deputed by a foreign company to its Indian office / branch / subsidiary / JV can be paid abroad by the foreign company subject to the foreign national / Indian citizen paying applicable taxes in India.

- Acquisition of immovable property** 21 Generally non residents are not permitted to acquire immovable property except in certain cases, where the property is required for the business of the Indian branch / office / subsidiary of the foreign entity. NRI/ PIOs are also permitted to acquire certain properties.

Foreign nationals retiring from employment in India are free to transfer the immovable property acquired in India and remit the sale proceeds thereof up to US\$ 1 million per calendar year. There is a lock-in-period of 10 years in case the property has been acquired in India out of Rupee funds. Citizens of

Pakistan, Bangladesh, Sri Lanka, Afghanistan, China, Iran, Nepal and Bhutan are not permitted to acquire or transfer immovable property in India without prior RBI approval.

Investment in shares/ debentures	22	Foreign nationals can invest in shares / convertible debentures of Indian Companies in accordance with the Foreign Direct Investment policy.
Remuneration ceiling	23	Expatriates seconded to India are sometimes appointed as managing director or directors of Indian Companies. Under the Indian Companies Act, there are ceilings on the appointment of and salary paid to managing director or directors of Public Companies. Prior approval is required in case managerial remuneration is to be paid to such individuals beyond the prescribed limits.

Income tax rates for Tax Year 2005-06

1 Individual Tax

ROR / RNOR / NR

Income	Tax Rate ⁽²⁾
Upto Rs. 100,000 *	NIL
Rs. 100,001 to Rs. 150,000	10%
Rs. 150,001 to Rs. 250,000	20%
Above Rs. 250,000	30%

* Basic exemption to resident women is Rs. 135,000 and to resident citizens above 65 years of age is Rs. 185,000.

2 Capital Gains Tax

Particulars	Tax Rates ⁽²⁾	
	Resident	Non-residents
Short term ¹ capital gain (from transfer of assets mentioned in note 5 below)	10%	10%
Other Short term capital gains	Normal rates per (1) above	Normal rates per (1) above
Long term capital gains (from transfer of assets mentioned in note 5 below)	NIL	NIL
Other long term capital gains	20%	20%

Notes:

- 1 Short-term capital asset is an asset which is held for a period of not more than three years (one year in case of shares/ listed securities).
- 2 Surcharge would also be applicable (@ 10% of tax, in case of individuals whose taxable income exceeds Rs. 1,000,000/-). Further, education cess @ 2% of the tax including surcharge is also payable (irrespective of the level of income)
- 3 Resident investors are entitled to indexation benefit as a relief against inflation in computing long term capital gains.
- 4 In case of non resident investors, relief from fluctuations in foreign currency is available in computing capital gains arising from sale of shares/debentures of an Indian company.
- 5 Securities Transaction Tax (STT) is applicable in respect of purchase and sale of equity shares in a company listed on a recognized stock exchange in India and units of an equity oriented mutual fund provided the transaction is undertaken through a recognized stock exchange in India.

Benefits/Amenities covered by Fringe Benefit Tax

Fringe Benefits

Any consideration for employment provided by way of -

- (a) any privilege, service, facility or amenity, directly or indirectly, provided by an employer, whether by way or reimbursement or otherwise, to his employees (including former employee or employees);
- (b) any free or concessional ticket provided by the employer for private journeys of his employees or their family members; and
- (c) any contribution by the employer to an approved superannuation fund for employees.

Deemed Fringe Benefits

Nature of expenditure	Percentage of expenditure deemed to be Fringe Benefit
■ Entertainment	20%
■ Hospitality <i>excluding</i>	
(i) Food or beverages provided to employees in office	
(ii) Payment through non transferable food vouchers (5% in case of an employer engaged in the business of Hotel)	20%
■ Conference <i>excluding</i> participation fee of employee	20%
■ Sales Promotion <i>including</i> publicity but <i>excluding</i> certain specified advertising expenditure	20%
■ Employees' Welfare <i>excluding</i>	
(i) Payment to fulfill any statutory obligation	
(ii) Payment to mitigate occupational hazards	
(iii) Payment for first aid facilities in hospital run by employer	20%
■ Conveyance, tour and travel including foreign travel (5% in case of employer engaged in business of construction, manufacture or production of Computer software and pharmaceuticals)	20%
■ Use of Hotel, Boarding and lodging facilities (5% in case of employer engaged in manufacture or production of Computer software and pharmaceuticals)	20%
■ Repair, running (including fuel), maintenance and depreciation on Motor cars/aircrafts (5% in case of employer engaged in the business of carriage of passengers or goods by Motor car. The benefit shall be nil in case of employer engaged in the business of carriage of passengers or goods by aircraft)	20%

Nature of expenditure	Percentage of expenditure deemed to be Fringe Benefit
■ Use of Telephone (including mobile phones) but excluding expense on leased telephone lines	20%
■ Maintenance of any accommodation in nature of guest house <i>excluding</i> accommodation for training purposes	20%
■ Festival Celebrations	50%
■ Use of health club and similar facilities	50%
■ Use of any other club facilities	50%
■ Gifts	50%
■ Scholarships	50%

Illustration of computation of income and tax thereon

Individual - Computation of Income Financial year ending 31st March 2006

Particulars	Amount (Rs.)
Base Salary and allowances	1,000,000
Bonus	500,000
	<hr/> 1,500,000
Perquisites	
Rent free accommodation	300,000
Utilities	90,000
Total	<hr/> 1,890,000
Less: Deduction in respect of investments	100,000
Taxable Income	<hr/> 1,790,000
Rounded off	1,790,000
Tax thereon	<hr/> 487,000
Add: Surcharge @ 10%	48,700
Total	<hr/> 535,700
Add: Education Cess @ 2%	10,714
Total tax liability	<hr/> 546,414

Notes:

1 Rent free accommodation

The individual is entitled for rent-free accommodation. The taxable value of the perquisite is considered as under.

	Amount (Rs.)
Lease rent @ Rs 50,000 per month	600,000
20% of salary	300,000
Lower of 20% of salary or rent paid for accommodation is taxable.	300,000

Countries with which India currently has Double Taxation Avoidance Agreements

I – Comprehensive Tax treaties

Australia	Netherlands
Austria	New Zealand
Armenia	Norway
Bangladesh	Oman
Belarus	Philippines
Belgium	Poland
Brazil	Portugal
Bulgaria	Qatar
Canada	Romania
China	Russia
Cyprus	Republic of Slovenia
Czech Republic	Singapore
Denmark	South Africa
Finland	Spain
France	Sri Lanka
Germany	Sweden
Greece	Switzerland
Hungary	Syria
Indonesia	Sudan
Israel	Tanzania
Italy	Thailand
Ireland	Trinidad & Tobago
Japan	Turkey
Jordan	Turkmenistan
Kazakhstan	UAE
Kenya	UAR (Egypt)
Korea	Uganda
Kyrgyzstan	USA
Libya	UK
Malaysia	Ukraine
Malta	Uzbekistan
Mauritius	Vietnam
Mongolia	Zambia
Morocco	
Namibia	
Nepal	

II – Limited Purpose Treaties

Afghanistan	Ethiopia
Kuwait	Lebanon
Pakistan	Iran
Saudi Arabia	Yemen

PricewaterhouseCoopers offices and contacts

PricewaterhouseCoopers is currently operating at Mumbai, New Delhi, Bangalore, Kolkatta, Chennai, Hyderabad and Pune. The firm specializes in business advisory services and provides professional services to a wide range of clients in both public and private sectors. Our office addresses along with details regarding contact persons are given below:

New Delhi

PricewaterhouseCoopers Pvt. Ltd.
Sucheta Bhawan, 11-A,
Vishnu Digambar Marg,
New Delhi – 110 002
Tel: 91-11-2321 0891

Contact Person: Nityanand Gupta
Email : nityanand.gupta@in.pwc.com

Mumbai

PricewaterhouseCoopers Pvt. Ltd.
252, Veer Savarkar Marg
Shivaji Park, Dadar,
Mumbai – 400 028
Tel: 91-22-5669 1500

Contact Person: R. D. Hingwala
Email : r.d.hingwala@in.pwc.com

Kolkatta

PricewaterhouseCoopers Pvt. Ltd.
Suite 9, 3rd Floor,
20-A, Park Street
Kolkatta – 700 016
Tel: 91-33-22263275/22295784

Contact Person: Somnath Ballav
Email : somnath.ballav@in.pwc.com

Bangalore

PricewaterhouseCoopers Pvt. Ltd.
14th Floor, 'C' Wing,
Mittal Tower, 47/6 M G Road,
Bangalore – 560 001
Tel: 91-80-2558 6362/6345

Contact Person: Indraneel R Chaudhury
Email : indraneel.r.chaudhury@in.pwc.com

Chennai

PricewaterhouseCoopers Pvt. Ltd.
PwC Center, IInd Floor32,
Khader Nawaz Khan Road, Nungambakkam
Chennai 600 006
Tel: 91-44-5228 5000

Contact Person: Natesan Sivasubramanian
Email : natesan.sivasubramanian@in.pwc.com

Pune

PricewaterhouseCoopers Pvt. Ltd.
305-307, Century Arcade, 243-244
B/2, Narangi Baug Road
Off Boat Club Road, Pune – 411 001
Tel: 91-20-26123271/3287

Contact Person: Sandip Mukherjee
Email : sandip.mukherjee@in.pwc.com

Hyderabad

PricewaterhouseCoopers Pvt. Ltd.
6-3-550, IInd Floor, LB Bhawan
Somajiguda, Hyderabad 500087
Andhra Pradesh
Tel: +91 40 5566 6081/82

Contact Person: Ashlesh Ch. Verma
Email : ashlesh.ch.verma@in.pwc.com

