Un, dos, tres, the tax man bays

- *Daksha Baxi*

They came to India to make beautiful music. Michael Jackson, Diana King, UB40. Ricky Martin blazed a trail across the media not only because of his show but also because of the famous inquisition by tax authorities in the capital. The world has shrunk and even our very own artistes take a trip overseas to satisfy their fans.

This raises the issue of taxation of artistes in the international sphere and brings to the forefront the need for proper planning.

The activities of artistes are essentially of an itinerant nature. As a result, taxation of their income not only poses problem in case of non-residents, but an even greater problem in case of resident artistes. Obtaining information and combating understatement or non-disclosure of income is a major problem. The main concern of tax authorities world-wide has been that income from these activities should be taxed in the same way as income from any other activity.

In case of a non-resident artiste who is resident of a country with which India has double taxation avoidance agreement (the treaty), if the treaty provisions are more beneficial to the artiste than those under the provisions of the Income Tax Act, 1961 (I-T), the non-resident artiste would generally not be liable to tax in India. This is owing to the operation of Articles 14 (independent personal services) or 15 (dependent personal services).

However, to counter this and to ensure that artistes get taxed in the country where they perform Article 17 has been introduced.

Article 17 deals specifically with the income of `Artistes and Athletes'. Paragraph 1 of this Article, however, has not been completely foolproof in enabling tax authorities to garner taxes. This paragraph only enables the source country to tax an artiste for income received by him for his personal activities as an artiste.
The expression `personal activities' seems to indicate that the paragraph applies to income accruing to the individual from his activity as a `performer'. In situations where orchestras, choral societies and sports teams are incorporated, the question is whether only the income received by the individual members of these incorporated entities is covered by this paragraph or whether the company earnings are also covered by it.
The OECD committee has concluded that Article 17(1) applies to income directly or indirectly accruing to the individual. The profit accruing to the corporate entity out of this performance would not be taxable under this paragraph in the country of performance (source country).

Tax planning ingenuity has helped artistes escape tax by interposing a company between the artiste and the country where he performs. The artiste would be employed by a non-resident corporate entity. The artiste would only receive a salary from this corporate entity. The whole of the income for his performance in India would be paid to the foreign company.

Owing to Article 7 (business profits), the income derived by this company as well as the artiste would not be liable to tax in India if the company does not have a permanent establishment (PE) in India. Often such a non-resident corporate entity is either actually owned by the artiste himself or by a related person and it is only used as a vehicle to avoid taxes.

The tax authorities in India could seek to tax the individual artiste on the basis that the company was a sham, or that it lacked business purpose or that the company was merely an agent of the individual or even under an `abuse of law' doctrine.

Paragraph 2 to Article 17 provides that where income in respect of personal activities exercised by an artiste in his capacity as such accrues not to the artiste himself but to another person, that income may, notwithstanding the provisions of Articles 7, 14 and 15, be taxed in the contracting state in which the activities of the artiste are exercised.

The OECD Commentary states that the purpose of Article 17(2) is to counteract certain tax avoidance devices in cases where remuneration for the performance of an artiste is not paid to the artiste himself but to another person (eg: so-called artiste company) in such a way that the income cannot be taxed in the source State either as personal service income of the artiste or as profit of the enterprise in absence of a PE.

Except for certain exemptions which may be available under section 10(6), the deeming provisions of section 9, read with the provisions of section 5 of the I-T Act, enable the Indian tax authorities to tax income received by a non-resident artiste who is not a citizen of India, for his performance as an employee of an event management company in India as also as a performer in his individual capacity. However, in absence of the special provision for taxation of an artiste (such as those in the UK, explained later) due to section 90 (2) of the Act, it may be possible in certain circumstances for the artiste to escape taxation in India. Typically there are three types of situations relating to performance by an artiste, the tax implications of each differ.

Act 1: Here, the artiste receives remuneration or fees directly for the performance in India. While section 5 (2) of the I-T Act which defines the scope of income taxable in India may enable the tax authorities to tax the remuneration received by the artiste in India for his personal performance, it may not be possible to establish business connection.

A business connection is essential if such income is to be deemed to accrue or arise in India under section 9(1)(i). Now, a business connection is not strictly defined in the I-T Act, thus this term is to be understood on the basis of interpretation provided by the courts.

The leading case in this regard is that of R.D. Agarwal v CIT (1965)(56 ITR 20). The SC while determining what constitutes a business connection explained that it predicates an element of continuity between the business of the non-resident and the activity in India. A stray or isolated transaction is normally not regarded as a business connection. Thus if the performance by the artiste in India is a stray act, it will not give rise to a business connection.

In such a situation, even when the income received by the artiste falls within the provision of Article 17 of the treaty between the country of residence of the artiste and India, because of section 90(2) of the ITA, in certain circumstances, the artiste may not be liable to tax in India.
Case 2: The artiste is employed under a `slave contract' by a `shadow company' incorporated outside the source country. This company pays a regular salary to the artiste and arranges for his/her performance world-wide. The company receives the income from the performances.

Here, the artiste's salary may not be taxable in India due to the exemption under section 10(6) (vi). Provided that the conditions under this section are satisfied, even though the income can be taxable under Article 17(1), section 90(2) would enable the artiste to be taxed under the more favourable provisions of the I-T Act. Thus the income of the artiste may escape tax in India altogether
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Furthermore, the income received by the foreign company would be taxable only if the company had a PE in India, unless the treaty between India and the country of residence of the shadow company is covered by Article 17(2), explained earlier.

Case 3: An event management company in India enters into a contract with a `loan-out company' for the performance of the artiste in a source country. The artiste receives a salary from such company, which in turn receives income in the country of performance (source country).

Once again, the artiste may not be liable to tax in India if the exemption under section 10(6) is available to him. The event management company would be required to deduct tax at source while making payment

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to the loan-out company, if the provisions of section 9(1) (i) are satisfied and a business connection exists or if Article 17(2) of the relevant treaty becomes applicable.

In case of certain treaties, there may be limitation in operation of Article 17(2). For example, the Indo-Canadian and the Indo-US treaties provide that paragraph 2 of Article 17 would not apply if it can be established that there is no participation in the profit of the `loan out company'.

In case of the US, the language used covers any sort of participation, including deferred remuneration, bonus, et al. Even the relatives of such artistes should not be participating in the profits of such a company. In such a situation, if the artiste is not a shareholder of the loan-out company and receives only a salary from such a company, both the artiste and the company may not be liable to tax in India. The Indo-US treaty also provides that the income of the artiste may only be taxable if the net amount received (after deduction of expenses incurred in connection with the performance), exceeds US $1,500 or equivalent rupees. There is no such limitation in the operation of paragraph 2 in case of the treaty between India and the UK. However, if the visit of the artiste were supported from the public funds of India or UK, including a political sub-division or local authority of that state, the income would not be taxed under article 17 in the country of performance.

The UK has special provisions in the domestic tax law whereby any payment made to an artiste is subject to a withholding tax which the payer is responsible for deducting while making the payment. In absence of such provisions in the I-T Act, taxability of a non-resident artiste in India remains illusive. Courtesy: Nishith Desai Associates, international legal and tax counsellors

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