From Tax Relief to FEMA Limitation: Capital Gains Tax Conundrum for SGP NRIs?

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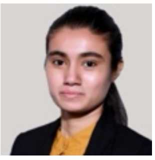

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In an era where Singapore is attracting entrepreneurs from India with various incentives, lifestyle etc., Indian taxman's approach towards capital gains tax from their Indian ventures has increasingly been aggressive. A frequently contested issue is the denial of treaty benefits on the disposal of grandfathered shares by NRIs often on grounds of treaty abuse or lack of commercial/ economic substance. One provision that has gained prominence in this context is Limitation of Relief **("LOR")** clause under Article 24(1) of the India – Singapore tax treaty, which has now become a recurring battleground for NRIs residing in SGP.

While taxman generally acknowledges that capital gains income earned on sale of grandfathered shares by SGP NRIs is not taxable in India under Article 13(4A) of the India-SGP DTAA based on TRC and requisite documents, the consequent contention is invocation of Article 24(1) to assert that such benefit is restricted upto the amount actually remitted to Singapore. NRIs often hold such investments on a non-repatriable basis under FEMA and hence the remittance of such money overseas is allowed only upto USD 1 million per annum which may be insignificant as compared to the actual realized proceeds. Accordingly, such a situation warrants a deeper interpretive analysis of Article 24(1).

Article 24(1): A Twofold Test

Article 24(1) imposes a twofold test in order to invoke the LOR clause:

1. Income is either **exempt or taxed at a reduced rate in India** under the India-SGP tax treaty; **and**
2. such **income is taxable in Singapore only** upon **remittance or receipt basis**.

Article 13(4A) provides that the **"income shall be taxable only in the Contracting State in which the alienator is a resident** ". It is critical to understand that Article 13(4A)[1] as well as similarly worded provisions like Article 7 or 8, do not grant an exemption in India. Rather, these provisions merely vest taxing rights exclusively with SGP, thereby precluding India from exercising any taxing rights altogether over such income. It acts as a jurisdictional bar and categorically **denies the source state (India) the right to tax the income, even if it arises from Indian sources** . Hence, when India lacks taxing rights altogether, the question of claiming an "exemption" or a "reduced rate" in India becomes irrelevant – the income simply falls outside India's taxing jurisdiction.

Additionally, the trigger for second limb arises only when the income in question is subject to tax in SGP on a remittance or receipt basis, rather than on an accrual basis. If it can be demonstrated that the income is not taxed in SGP on a remittance basis, then also Article 24(1) becomes inapplicable.

Indian courts and tribunals[2] have consistently upheld the aforesaid interpretation, affirming that these provisions do not grant an exemption in India. The usage of **word "*only*" in these articles debars India to tax the income, even if it is sourced from India**. When India does not have any taxing rights over the income of a non-resident entity, the question of any kind of exemption or reduced rate of taxation in India does not arise. Further, in these rulings, the courts/ tribunals have noted that **assessees' income was not taxed in SGP on remittance basis, albeit was liable to taxed in-principle on accrual basis** as such income under the income tax laws of SGP was regarded as "accruing in or derived from SGP". To substantiate this position, reliance was placed on certificates issued by Inland Revenue Authority of Singapore (IRAS), which confirmed that the assessee was liable to pay tax in Singapore on its worldwide income on accrual basis and not on remittance basis.

Interestingly, in these rulings, the income was ultimately taxed in Singapore irrespective of such money was actually remitted and did not address situations where NRIs hold passive investments in India.

Prashant Kothari Ruling[3]: A Turning Point

Recently, the Mumbai Tribunal in the case of *Prashant Kothari*, ruled-out applicability of Article 24(1) due to non-fulfillment of the very first condition that Article 13(4)[4] does not provide an exemption in India even though the assessee was unable to furnish a certificate from IRAS. While the Tribunal did not examine the second limb of Article 24(1), it nonetheless raises a question whether this condition will ever be applicable considering the Singapore taxation provisions on capital gains on sale of passive investments in India held by NRIs.

Singapore capital gains tax provisions

Singapore does not impose tax on capital gains (whether foreign or domestic one), except where the gains are deemed to fall under the criteria of 'badges of trade'. Moreover, the newly incorporated provision[5] which introduces capital gains tax from disposal of foreign assets w.e.f. January 01, 2024, does not apply to individuals.

So, if NRIs residing in Singapore derive capital gains on disposal of their passive investments in India, such gains are not subject to tax in Singapore, regardless of whether such money is remitted or not. In such a situation, it is logical to argue that when Singapore does not tax capital gains at the first place, the question of whether taxation is on a remittance or accrual basis becomes immaterial.

A Glimpse into Article 24A

Apart from invoking Article 24(1), the taxman often invokes Article 24A, alleging that the NRIs have structured their affairs primarily to claim treaty benefits. Indian courts/ tribunals, in several rulings[6], have recognized the meeting of minimum expenditure thresholds[7] in the resident state as one of the factors to rebut allegations of treaty abuse. However, such thresholds are prescribed only for corporate entities and there is limited guidance on how similar principles will be applied to individuals in demonstrating that their migration was not solely tax driven.

In the absence of clearly defined benchmarks for NRIs, the test of “substance” becomes more nuanced and a fact driven exercise. To counter such allegations, NRIs need to demonstrate genuineness of their relocation and economic engagement in the resident state through a combination of various factors such as shift in employment to a foreign entity from an Indian entity, active involvement in business development or entrepreneurial activities abroad, relocation of immediate family (spouse and children), shift of economic interest abroad etc. These indicators, taken together, can support the position that NRIs move was motivated by legitimate personal and economic reasons, rather than being a tax avoidance strategy.

Concluding remarks

Sale of Indian shares by NRIs are subject to Indian tax and FEMA provisions. Though FEMA provides a limitation on repatriation of funds, NRIs residing in Singapore are well-placed to challenge any denial of treaty benefits arising from the invocation of the LOR clause. To further strengthen their position, NRIs may consider obtaining a certificate from IRAS clearly stating that such capital gains are not subject to tax in Singapore on remittance basis. It is also interesting to note that the LOR clause is only incorporated in India-SGP tax treaty and does not find place in treaties with Mauritius or Cyprus which also provide that capital gains on sale of grandfathered shares are not taxable in India. As more Indians move abroad for various purposes, it will be interesting to see how jurisprudence evolves on this very important aspect.

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[1] Gains from the alienation of shares acquired before 1 April 2017 in a company which is a resident of a Contracting State shall be taxable only in the Contracting State in which the alienator is a resident

[2] APL Co. Pte Ltd, ITA No. 4435 (Mumbai) of 2013 affirmed by Bombay High Court vide ITA No. 429 of 2018; Citicorp Investment Bank (Singapore) Ltd., ITA No. 793/Mum/2015 affirmed by Bombay High Court vide ITA No. 256/2018; D.B. International (Asia) Ltd., ITA No. 992/Mum/2015

[3] [TS-693-ITAT-2025(Mum)]

[4] Pre-amended

[5] Section 10L of Singapore Income Tax Act, 1947

[6] Tiger Global [TS-5784-HC-2020(Delhi)-O], now pending before Supreme Court; Tyco Electronics Singapore Pte Limited, [TS-6384-ITAT-2024(Delhi)-O]; SC Lowy P.I. (LUX) S.A.R.L., ITA No. 3568/Del/2023

[7] S$200,000 or INR 5,000,000