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International compliance regime short-changed?

09 August 2014



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Introduction

Meaning of double taxation

- Double taxation is imposition of taxes twice on the same income in the same year on a person.
- Double taxation occurs mainly due to overlapping of taxation jurisdiction based on the following taxation principles:
 - ✓ Resident based taxation - world wide income of a resident is taxed
 - ✓ Source based taxation - income arising from sources within the country is taxed
 - ✓ Citizen based taxation – income of a citizen is taxed irrespective of place of source
- Thus, double taxation occurs when two countries following different principles of taxation try to tax an income

What is Double Taxation Avoidance Agreement

- DTAA is consensus between two countries aiming at elimination of double taxation.
- DTAA allocates jurisdiction of taxation between two countries and wherever double taxation provides mechanism for eliminating or reducing double taxation.
- DTAA provides bridge between the tax laws of two countries – common definition
- DTAA provides methodology for alternate dispute resolution mechanism
- DTAA provides for exchange of information between the treaty partners and mechanism for collection of tax
- India currently has a network of 86 DTAA's across the world. ([Annexure – List of DTAA](#))
- India also provides for unilateral mitigation of double taxation for its residents by providing credit of taxes paid in foreign countries with whom India does not have a DTAA

General taxability of non-resident in India

Types of Income	Under the Income Tax Act, 1961	Under the India and US DTAA
Business profits	<ul style="list-style-type: none"> Taxable if there is business connection in India {Section 9(1)(i)} Taxable on net basis (40%) 	<ul style="list-style-type: none"> Taxable only if there is a permanent establishment in India (restricted) (Article 5) Taxable on net basis (40%)
Royalty	<ul style="list-style-type: none"> For use or right to use IPRs, commercial / scientific information, equipment (wide definition) {Section 9(1)(vi)} Taxable on gross basis (25%) 	<ul style="list-style-type: none"> For use or right to use IPRs, commercial / scientific information, equipment (restricted definition) (Article 12) Taxable on gross basis (15%)
Fee for technical services (“FTS”)	<ul style="list-style-type: none"> For technical, consultancy and managerial services {Section 9(1)(vii)} Taxable on gross basis (25%) 	<ul style="list-style-type: none"> For technical, consultancy and managerial services – (check for make available concept) (Article 12) Taxable on gross basis (15%)
Interest	<ul style="list-style-type: none"> Interest on debt or credit {Section 56} Taxable on gross basis (20%) 	<ul style="list-style-type: none"> Interest on debt or credit (Article 11) Taxable on gross basis (10 / 15%)
Capital Gain	<ul style="list-style-type: none"> Gain arising from transfer of Capital assets in India. {Section 9(1)(i)} Taxable at (10 / 20 / 40%) 	<ul style="list-style-type: none"> No benefit in DTAA with USA and UK etc. DTAA with Mauritius, Singapore etc. provides for taxability of capital gain arising on transfer of shares in Indian company only in the country of residence of foreign company.

Payer is liable to withhold tax on payment of taxable income to non-resident

Prime factors for consideration of PE

Type of PE	Key Factors
Fixed Place PE	Prime Conditions are : <ol style="list-style-type: none">1. Fixed place of business2. Place should be at disposal3. Carry on the business through the PE
Installation / Supervisory PE	Time period for project as specified in the respective DTAA. (Indian treaties generally provide for time period of Six months)
Service PE	<ul style="list-style-type: none">• Rendition of service through employees or other personnel engaged by the enterprise for such purpose.• Time period as specified in the respective DTAA should be considered. Indian DTAA generally provides for time period from 1 to 183 days.
Agency PE	Dependent Agent would generally constitute PE if he: <ul style="list-style-type: none">• Habitually exercise authority to conclude contracts.• Habitually maintain stock of goods, from which goods are generally delivered.• Habitually secured order primarily for the non resident.

Exclusions from Permanent Establishment

PE specifically not 'deemed' to include

- use of facilities solely for the purpose of storage, display or delivery of goods;
- maintenance of stock of goods;
- for the purpose of processing by another enterprise;
- maintenance of a fixed place solely for the purpose of purchasing goods/ collecting info;
- carrying on any other activity of a preparatory or auxiliary character;
- combination of above activities.

Features

- Activities so remote from actual realization of profits that difficult to attribute
- 5(4) cannot be invoked where aforesaid activities are undertaken for third parties.

ECB Policy- An Overview

External Commercial Borrowing (ECB)

Automatic Route

Maximum - \$ 750 M (U\$ 200 M Hotel, Hospital, S/W and upto U\$ 10 M by NGO in Micro Finance, International Fin Co upto 75% of its Owned Fund per financial year

Minimum average maturity 3 or 5 years depending on the quantum of ECB

Approval Route

Approval route applicable - when not covered in Automatic route

Short term debt not encouraged

ECB Policy- At a glance

Eligible Lender

- International Banks
- International Capital Markets
- Multilateral Financial Institutions
- Export credit agencies
- Suppliers of equipment
- Foreign collaborators
- Foreign Equity Holders (min. 25%)
- For ECB > USD 5M – Debt-Equity 7:1 (approval route)

Maturity and Interest

- **Minimum avg. maturity period**
USD 20 M – 3 years
>USD 20 upto 750 M – 5 years
- **All in Cost Ceiling**
3-5 years - LIBOR + 350 b.p.
>5 years - LIBOR + 500 b.p.

Eligible Borrowers

- Corporates
- NGOs in Micro Finance
- SEZ Units (except financial intermediaries, individuals, Trusts)
- NBFC-IFC
- NBFC-AFC
- Micro Finance Institution

Prohibition

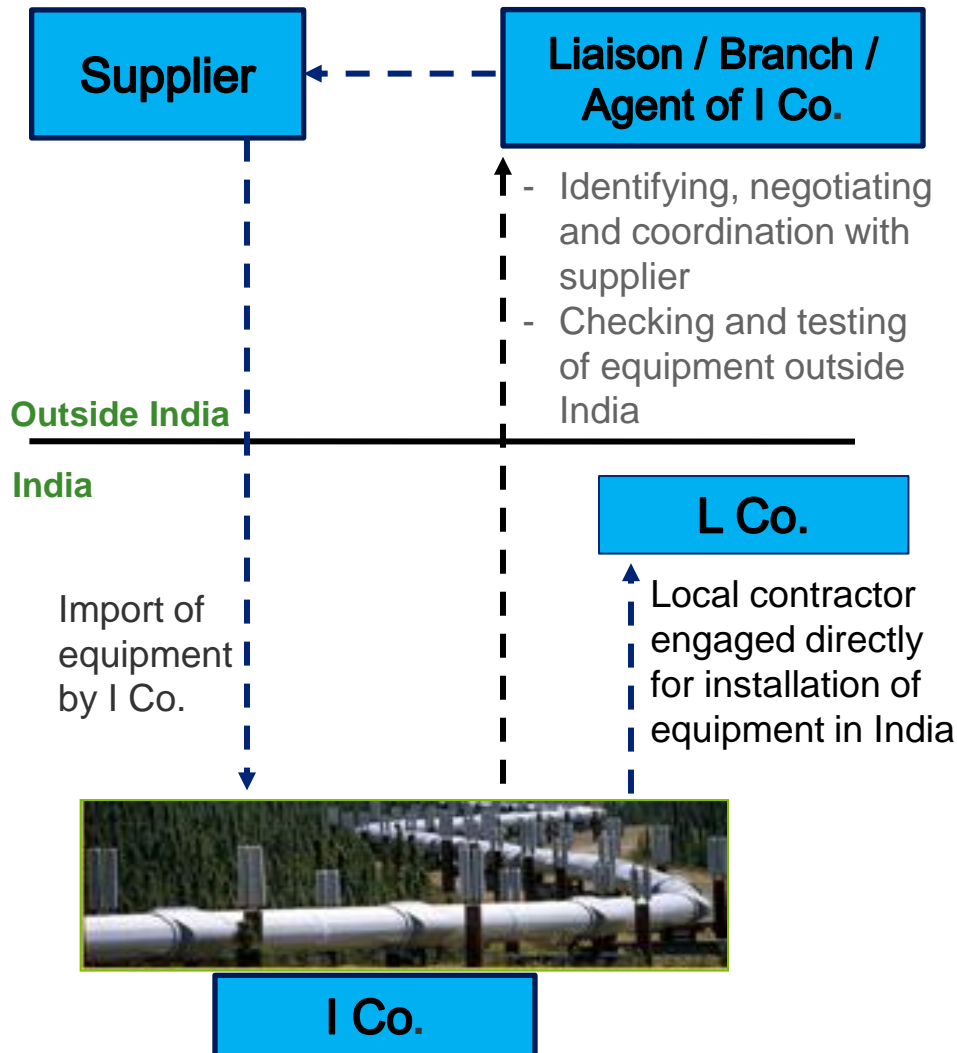


- On lending
- Investment in capital market or acquiring a company in India
- Real Estate

End Use

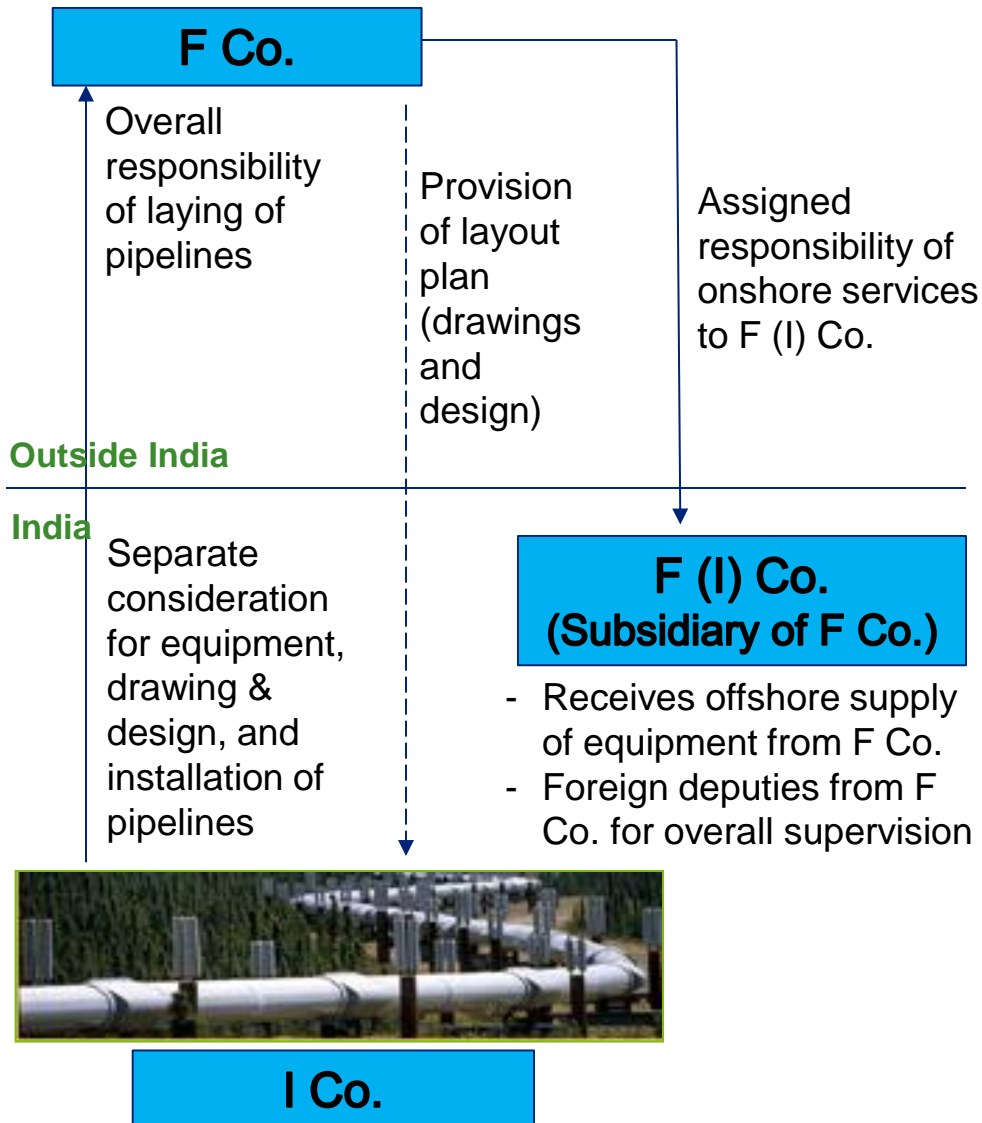
- Real/ Industrial sector (SME)–
 - Import of capital goods,
 - New Projects, Expansion/ modernization of existing units
 - ODI in JV/ WoS abroad
- Payment of Interest During Construction (IDC)
- First stage acquisition of shares in the disinvestment process and also in the mandatory second stage offer under GOIs disinvestment program
- Payment for obtaining License/ permit for 3G spectrum.
- For lending to self help groups or for micro credit by NGO's
- Repayment of rupee loans by companies in infrastructure sector manufacturing and hotel sector (with project cost of NR 250 or more)
- Working capital for Civil Aviation sector
- General corporate purpose (w.e.f. 4 September 2013) for ECB from foreign direct equity holder

Typical transactions in a project – Scenario: 1



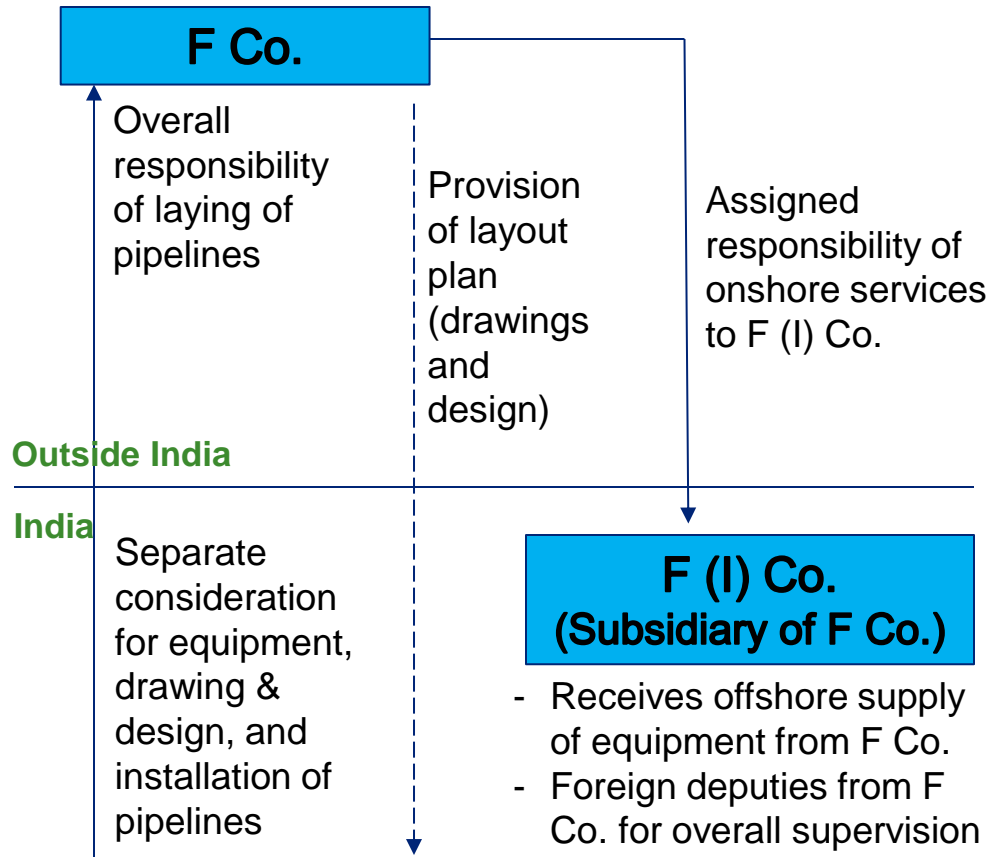
- Will I Co. have Fixed PE, Agency PE outside India ?
- Can revenue received by the Liaison / branch / Agent be taxed in India?
- Is I Co. liable to withhold tax in India from payments to be made to Liaison / branch / Agent ?
- Arm's length pricing?
- Will consideration received by supplier for off shore supply of equipment be taxable in India?
- Timelines for payment to supplier?
- Is commission to LO/BO/Agent is freely permitted under FEMA?

Typical transactions in a project – Scenario: 2



- Will consideration received by F Co. for overall project be taxable in India?
- Will separate consideration for different activities have different tax treatment?
- Will off-shore supply of equipment be taxable in India?
- Will F Co. have a fixed place PE, installation / supervisory PE or service PE in India?
- Will income from provision of design and drawing be considered as Royalty or FTS?
- Whether employees deputies to F (I) Co. by F Co. need to file return of income in India?
- Is I Co. liable to withhold tax in India from payments to be made to F Co. ?

Typical transactions in a project – Scenario: 2 (Contd.)

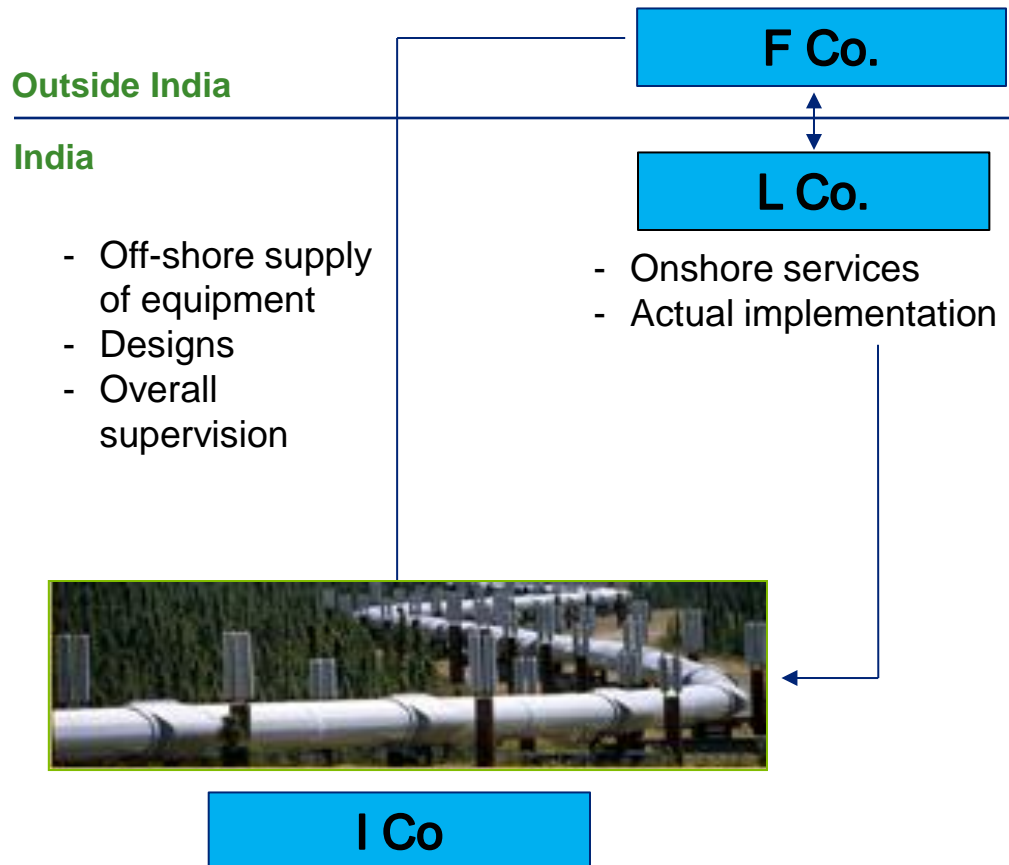


I Co.

- Timeline for payment to F Co?
- Timeline for payment to F(I) Co?
- Can F(I) Co collect money on behalf F Co.
- Can F Co pay salary to foreign deputies in his bank account outside India?

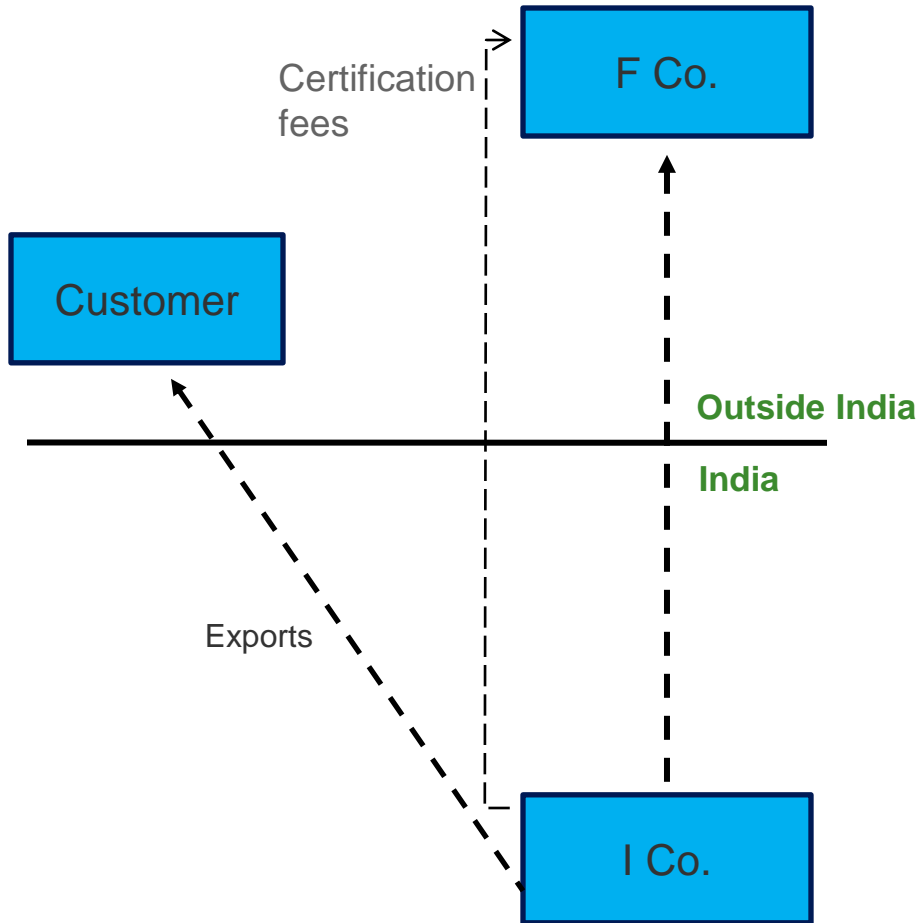
Typical transactions in a project – Scenario: 3

- Turnkey Project
- Bid as a consortium of F Co. & I Co.
- Joint and several liability
- F Co. to be the lead partner
- I Co. can sue either party for performance of contract



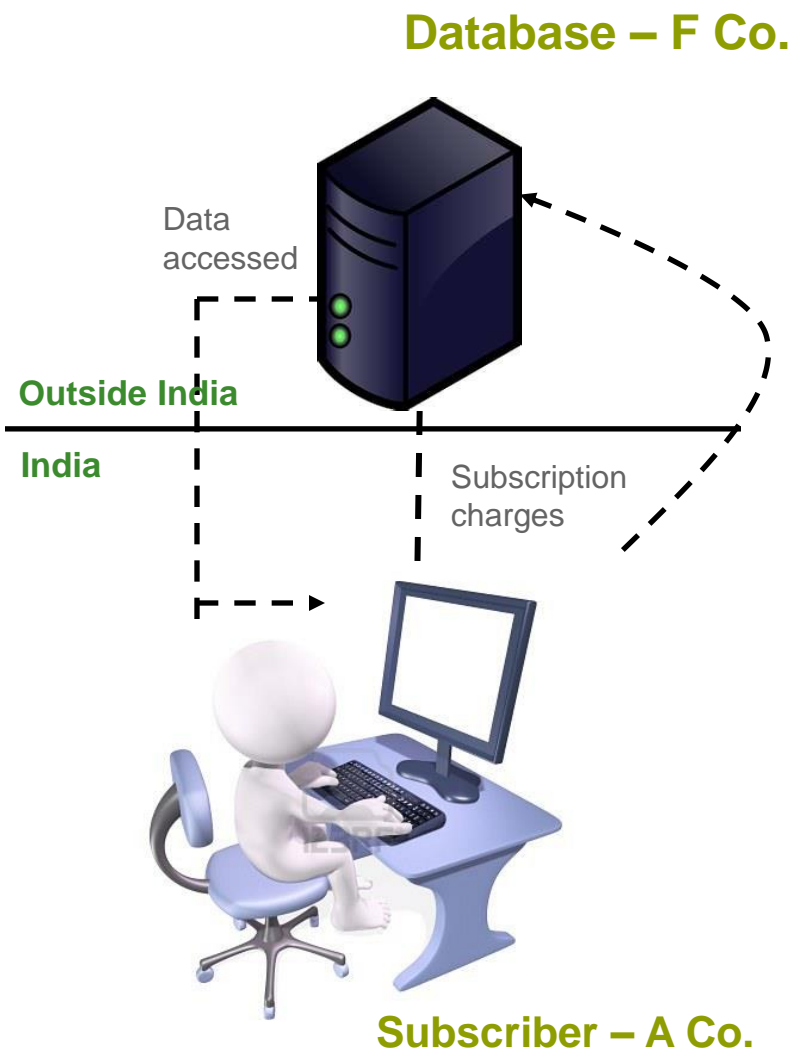
- Will F Co. and L Co. constitute an Association of Person (separate taxable entity)?
- If yes, then:
 - what will be the residential status of AOP
 - how consideration will be distribute
 - availability of credit of taxes paid by AOP to consortium members?
- In whose name tax is required to be withheld by I Co.?
- What are the ways to mitigate AOP exposure?

Fee for technical services



- I Co., exports its products to overseas country.
- Sale of products in country F is allowed only if such products are certified to be fit for use as per the specified certification procedures.
- I Co. availed certification services from F Co.
- Employees of F Co. visit India and certify the goods before exports.
- Export contracts concluded in India, goods manufactured and exported from India.
- Does the above mentioned services will be taxable as FTS?
- Is I Co. liable to withhold tax in India from payments to be made to F Co. ?
- Is there a cap prescribed or payment of FTS?

Royalty



- A Co. subscribes to 'database' of F Co. which is located outside India and which contains financial and economic information including fundamental data of a large number of companies worldwide.
- F Co. collects and collates the information / data available in public domain and puts them all in one place in a proper format.
- Rights of subscriber:
 - Right to view and make use of the data for internal purpose.
 - No right to distribute the data downloaded by it or provide access to others.
 - No right to reproduce or adapt the work.
- Is there a cap prescribed or payment of Royalty?

Payment to F Co. may be chargeable to tax In India as royalty (*check for DTAA benefit*)

Compliance Requirement in India

Non resident

- Once a foreign enterprise formed permanent establishment in India, then it may be required to undertake following compliances in India:
 - Annual filing of return of income;
 - Maintain separate books of accounts of the PE in India;
 - Quarterly filing of withholding tax returns considering payments related to the PE;
 - Employees of the company who are working in India will be taxed in India;
 - Arms length attribution of income to the PE so established etc.

Resident

- Withholding of taxes at rate in force for payment of every income to the non resident.
- Quarterly filing of separate withholding tax return for payments made to Non resident
- He may be considered as representative assessee for Non – resident.

Questions



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Annexure I – List of Indian DTAA

Armenia	Cyprus	Hashemite Kingdom of Jordan	Kuwait	Morocco	Portuguese Republic	Sudan	UAR (Egypt)
Australia	Czech Republic	Hungary	Kyrgyz Republic	Mozambique	Qatar	Sweden	UGANDA
Austria	Denmark	Iceland	Latvia	Myanmar	Romania	Swiss Confederation	UK
Bangladesh	Egypt	Indonesia	Libya	Namibia	Russia	Syrian Arab Republic	Ukraine
Belarus	Estonia	Ireland	Lithuania	Nepal	Saudi Arabia	Tajikistan	United Mexican States
Belgium	Ethiopia	Israel	Luxembourg	Netherlands	Serbia	Tanzania	USA
Botswana	Finland	Italy	Malaysia	New Zealand	Singapore	Thailand	Uzbekistan
Brazil	France	Japan	Malta	Norway	Slovenia	Trinidad and Tobago	Vietnam
Bulgaria	Georgia	Kazakstan	Mauritius	Oman	South Africa	Turkey	Zambia
Canada	Germany	Kenya	Mongolia	Philippines	Spain	Turkmenistan	
China	Greece	Korea	Montenegro	Poland	Sri Lanka	UAE	

