

Budget 2018 – International Tax Proposals

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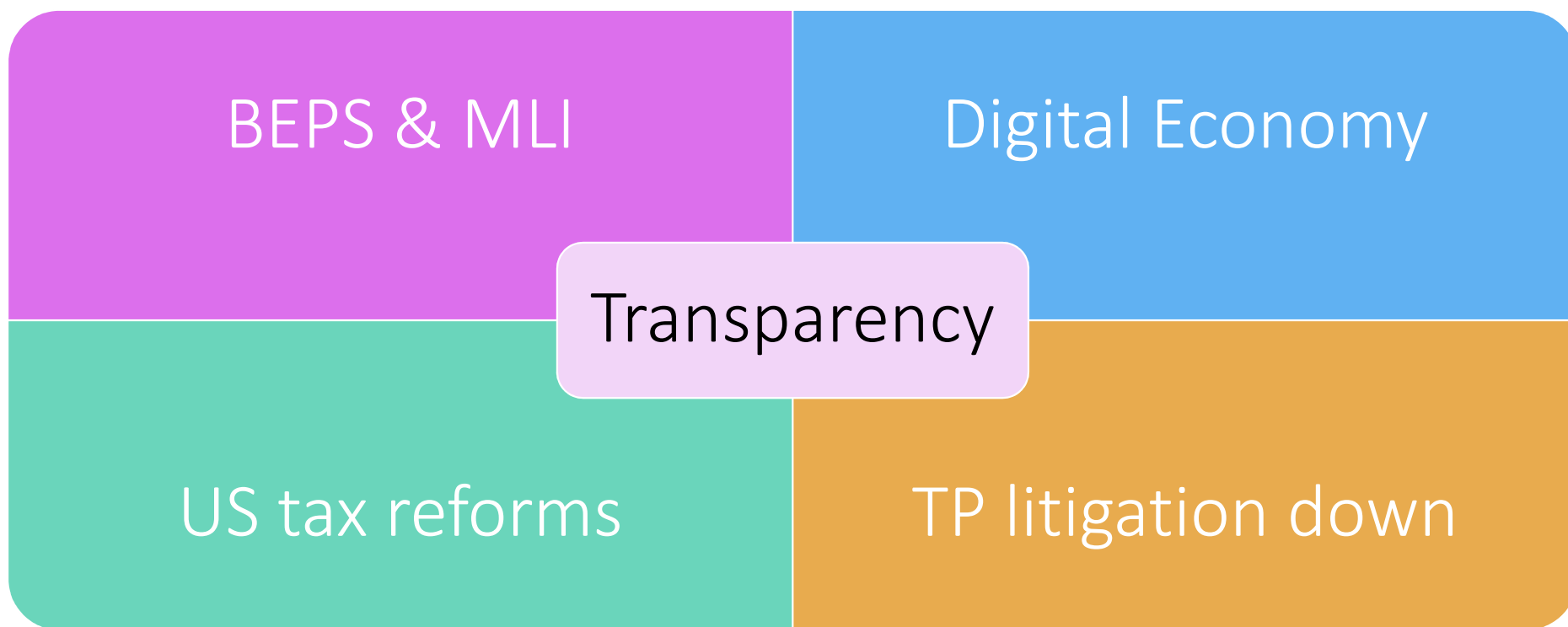
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Pune West CPE Study Circle

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International Tax Landscape



Non-resident tax rates

- No change in the tax rates for NRIs or foreign companies for FY 2018-19
- Increase in cess from 3% to 4% for FY 2018-19
- Tax rate as applicable to foreign companies for FY 2018-19

Corporate Tax rate	40%
MAT rate	18.5%
Surcharge	
Upto Rs 1 crores	NIL
Rs 1 cr to Rs 10 cr	2%
More than Rs 10 cr	5%
Cess (from FY 2018-19)	4%

LTCG & deemed dividend

- Application of DDT on deemed dividend distribution tax – benefit of tax treaty in the hands of recipient not relevant (from FY 2018-19)
- New regime for taxation of long-term capital gains on sale of equity shares
 - Applicable even to non-residents **including FIIs** (for FY 2018-19)
 - *Doubts raised due to the drafting in Sec 115AD*
 - Special tax treatment for income earned by non-resident Indians (NRIs)
Chapter XII-A now relevant for LTCG on shares
 - *Sec 115F provides a special exemption from LTCG if certain conditions on re-investment are met and Sec 115G provides for dispensation from filing a tax return.*

Agency PE – Business connection scope expanded

Inserted from FY 2018-19

Existing Explanation 2 to Sec 9(1)(i)

Explanation 2.—For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, **unless his activities are limited to the purchase of goods or merchandise for the non-resident**; or

Proposed Amendment

Explanation 2.—For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident or **habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by that non-resident and the contracts are—**

- (i) in the name of the non-resident; or**
- (ii) for the transfer of the ownership of, or for the granting of the right to use, property owned by that non-resident or that non-resident has the right to use; or**
- (iii) for the provision of services by the non-resident; or**

Agency PE scope widened – Why?

- Change driven by OECD's BEPS project and more specifically Action Plan 7 on artificial avoidance of PE
- Scope of PE under treaties to be expanded to stop base erosion due to the activities of agents
- MLI or Multilateral Convention (Article 12) also signed by India carries out changes relating to expanding scope of agency PE under treaties
- Domestic law (under Sec 9) on agency PE would have been narrower post MLI effect
- Domestic law (Sec 9) proposed to be amended to align with MLI

Business connection vs BEPS AP 7

LANGUAGE IN BEPS ACTION PLAN 7

- ...habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are...

PROPOSED AMENDMENT

...habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by that non-resident and the contracts...

Agency - Business connection: Some issues

- Activities limited to the purchase of goods or merchandise for the non-resident earlier were excluded from the scope of business connection
 - Budget 2018 does not retain the exclusion
- Assuming no profit attribution, non-resident may not have a tax risk
- Impact on Indian agents promoting the products/services for Group companies

Significant Economic Presence - Business connection scope expanded

Inserted from FY 2018-19

Significant Economic Presence

- 'Significant economic presence' in India shall also constitute 'business connection'
- “Significant economic presence” means-

Value based test: (i) any transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India if the aggregate of payments arising from such transaction or transactions during the previous year exceeds the amount as may be prescribed; or

Digital test: (ii) **systematic and continuous** soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.

Significant Economic Presence

- Income as is attributable to such transactions or activities shall be deemed to accrue or arise in India
- Residence or place of business in India or **rendering of services in India not a pre-requisite**
- The threshold of “revenue” and the “users” in India to be notified after public consultation.
- Unless corresponding modifications to PE rules are made in the DTAA's, the cross border business profits will continue to be taxed as per the existing treaty rules

Rationale – Digital PE

- Existing business connection provides for physical presence-based nexus rule for taxation of business income of non-resident in India
- Non-resident enterprises interact with customers in another country without having any physical presence in that country resulting in avoidance of taxation in the source country. Therefore, the existing nexus rule based on physical presence do not hold good anymore for taxation of business profits in source country
- References to BEPS Action Plan 1
- Amendment in the domestic law will enable India to negotiate for inclusion of the new nexus rule in the form of 'significant economic presence' in the Double Taxation Avoidance Agreements

Digital PE – Some issues

- Proposed Clause (i) - any transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software
 - merely refers to the monetary threshold and does not require reasonable continuity of non-resident's activities in India
 - “Systematic and continuous” threshold absent
 - Digital test not mentioned
- Conflict with Clause (b) of Explanation 1 to Sec 9(1)(i) which carves out exception for non-resident's activities confined to purchase of goods in India for the purpose of export.
- Would a solitary transaction of say sell of machine by non-resident create a business connection?
 - Is the ratio of SC ruling in R.D. Aggarwal & Co. [(1965) 56 ITR 20] diluted?

Digital PE – Some issues

- Significant economic presence and equalisation levy – both introduced by India (no overlap)
- Explanation - Residence or place of business in India or **rendering of services in India not a pre-requisite**
 - Conflict with “in India”
- Digital PE versus scope of royalty or FTS u/s 9(1)(vi) or (vii)
- Emerging global trends to tax digital economy transactions
- Profit attribution will be a challenging area

Indian Judicial trends - 2017

SC : Formula One World Championship Ltd. [TS-161-SC-2017]

- Formula 1 race in India created a PE...ruling on disposal test

ITAT : ABB FZ-LLC [TS-256-ITAT-2017(Bang)]

- Services without employee's physical presence in India relevant in Service PE conclusion...virtual communication modes relevant.

ITAT : Google India Private Ltd [TS-468-ITAT-2017(Bang)]

- Google's Adwords distribution agreement not mere sale of advertisement space; Upholds royalty taxation

Other changes

CBCR alignment with OECD

- Constituent entity resident in India, having a non-resident parent, to furnish CbCR in case its parent entity outside India has no obligation to file the CBCR in the latter's country or territory;
- Time allowed for furnishing the Country-by-Country Report (CbCR), in the case of parent entity or Alternative Reporting Entity (ARE), resident in India, to be extended to twelve months from the end of reporting accounting year;
- The time allowed for furnishing the CbCR, in the case of constituent entity resident in India, having a non-resident parent, shall be twelve months from the end of reporting accounting year;
- The due date for furnishing of CbCR by the ARE of an international group, the parent entity of which is outside India, with the tax authority of the country or territory of which it is resident, will be the due date specified by that country or territory;
- Terms reporting period and agreement are clarified

Other proposals

- MAT not applicable to foreign companies earning income subject to special taxation regime
 - Clarificatory amendment with retrospective effect from FY 2000-01
 - *44B - shipping business; 44BB - business of exploration, etc., of mineral oils; 44BBA - business of operation of aircraft; 44BBB - business of civil construction, etc., in certain turnkey power projects*
- Penalty increased to ensure compliance of reporting obligations
 - Penalty on failure to furnish the statement of financial transaction or reportable account is proposed to be increased from Rs 100 to Rs 500 for each day of continuing default.
 - Further, the penalty for failure to furnish the report pursuant to a notice issued by the income tax department to be increased from Rs 500 to Rs 1,000, for each day of continuing default.
- Royalty and FTS payment by NTRO to a non-resident to be tax-exempt

Thank You

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Views are personal. Presentation for academic discussion only.