



Global Business Tax Alert Sharp Insights

The Government of India and Republic of Singapore have signed the third protocol for amendment of the Double Taxation Avoidance Agreement between the two countries.

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Executive Summary

The Central Board of Direct Taxes (CBDT), has issued a press release dated December 30, 2016, towards third Protocol for amendment of the Double Taxation Avoidance Agreement ("DTAA") between India and Republic of Singapore ("India-Singapore DTAA").

The above amendment is in line with India's treaty policy to prevent double non-taxation, curb revenue loss, streamline flow of investments and check the menace of black money through automatic exchange of information, as reflected in India's recently revised treaties with Mauritius and Cyprus and the joint declaration signed with Switzerland.

Third Protocol amending the DTAA

The India-Singapore DTAA was signed at India on January 24, 1994, as amended by the Protocol signed at India on June 29, 2005 and by the second Protocol signed at India on June 24, 2011. On December 30, 2016, both the Governments have signed the third Protocol amending the India-Singapore DTAA.

Summary of important changes provided in the third Protocol are as follows:

1. Mutual Agreement Procedure (MAP)

- The Protocol introduces Article 9(2), hitherto not available in the DTAA which would enable taxpayers of both countries to get arm's length price determined through MAP. This is in line with India's commitments under Base Erosion and Profit Shifting (BEPS) Action Plan.

2. Source-based taxation of capital gains on shares

- The Third Protocol amends the DTAA with effect from April 1, 2017 to provide for source based taxation of capital gains arising on transfer of shares in a company.
- Investments in shares made before April 1, 2017 have been grandfathered subject to fulfillment of conditions in Limitation of Benefits clause ("LoB") as per 2005 Protocol.
- A two year transition period from April 1, 2017 to March 31, 2019 has been provided during which capital gains on shares will be taxed in source country at half of normal tax rate, subject to fulfillment of conditions in LoB clause.

3. Limitation of Benefits

LoB article is present in the existing India-Singapore DTAA which is applicable for residence-based taxation for capital gains. Following amendments are proposed in the new LoB Article:

- The benefit of resident-based taxation for investments made before April 1, 2017 and 50% reduction in tax rate during the transition period from April 1, 2017 to March 31, 2019, shall be subject to LoB Article, whereby a resident of a contracting state (including a shell / conduit company) will not be entitled to benefit of 50% reduction in tax rate, if it fails the main purpose test and bonafide business test.

- A resident would be deemed to be a shell/ conduit company, if its total expenditure on operations in the contracting state is less than Rs.5,000,000 (Singapore Dollars 200,000) -
 - for each of the 12-month periods in the immediately preceding 24 months from the date the gains arise, in the case of benefit of resident-based taxation for investments made before April 1, 2017.
 - for the immediately preceding 12 months from the date the gains arise, in the case of benefit of 50% reduction in tax rate during the transition period from April 1, 2017 to March 31, 2019,.
- A resident is deemed not to be a shell or Conduit Company if it is listed on the recognized stock exchange of the Contracting State or its annual expenditure on operation is equal to or more than the amounts specified above.

4. Others

- The Protocol enables application of domestic law and measures concerning prevention of tax avoidance or tax evasion.

5. Entry into Force

The Protocol shall come into force after completion of due procedural requirements in both the countries and is notified each other about the completion of the procedures. If this Protocol does not enter into force as at March 31, 2017 due to either of the aforesaid notifications remaining pending, this Protocol shall enter into force on April 1, 2017.

Conclusion

The benefits of residence-based taxation of capital gains, on sale of shares under the India-Singapore DTAA, are linked to the India-Mauritius DTAA. Pursuant to the amendment to the India-Mauritius DTAA, uncertainty was created for capital gains taxation under the India-Singapore DTAA.

The Protocol amending the India-Singapore DTAA rests the uncertainty and brings the capital gains taxation including grand fathering provisions in line with the amendments made in the India-Mauritius DTAA.

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