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BEPS
Union Budget 2018

Base Erosion and Profit Shifting

For past few years, the Organisation for Economic Co-operation and Development [OECD] and G20 countries have actively worked on the base erosion and profit shifting [BEPS] project. BEPS refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profit 'disappear' for tax purpose or to shift profits to locations where there is little or no real activity but taxes are low, resulting in little or no overall corporate tax being paid. In light of several such instances resulting in BEPS, the G20 and OECD released their recommendation on 15 BEPS action plans (15 action plans) on 5 October 2015.

The BEPS action plans are structured around three fundamental pillars:

- Introducing coherence
- Reinforcing substance
- Improving transparency

As a member of G20 and an active participant of the BEPS project, India is committed to the BEPS outcome. To implement the BEPS actions, India has been amending its domestic tax law as well as its tax treaties. This document highlights the BEPS related amendments proposed in the Union Budget 2018.



Agency PE

The agency PE rules contained under the Indian tax law and India's tax treaties are broadly similar. Under the Indian tax law, a foreign enterprise would be regarded as having a business connection in India if any person acting on behalf of the foreign enterprise is habitually authorised to conclude contracts for the foreign enterprise.

As per the proposed amendment, a foreign enterprise would be regarded as having a business connection in India if a person acting on behalf of the foreign enterprise is habitually authorised to conclude contracts, or habitually concludes contracts, or habitually plays the principal role leading to conclusion of contracts by the foreign enterprise, and the contracts are:

- in the name of the foreign enterprise; or
- for the transfer of the ownership of, or for the granting of the right to use, property owned by that foreign enterprise or that the foreign enterprise has the right to use; or
- for the provision of services by that foreign enterprise.

The proposed amendment is in line with BEPS action 7, and is modelled on Article 12 of the multilateral instrument (MLI) signed by India and various other jurisdictions. The proposal would ensure that the agency PE rules under the Indian tax law and tax treaties (once the MLI becomes effective) are on the same footing.

It may be noted that many significant treaty partners of India like the UK, Canada, Singapore, Luxembourg and Cyprus have reserved the right for Article 12 of the MLI to not apply. The India-US tax treaty would also stand unchanged as the US is not yet a signatory to the MLI. Treaty partners such as China, Germany and Mauritius have not notified the tax treaty with India as a covered tax agreement. Accordingly, the agency PE clause under India's tax treaties with these countries would stand unchanged, and the agency PE change discussed above would effectively not impact taxpayers who are tax residents of these countries. India's treaty partners that have opted for Article 12 of the MLI include France, Netherlands and Japan, and the agency PE rules would be effectively modified for tax residents of these countries once the MLI is effective.



Digital PE

Taking a cue from BEPS action 1 dealing with the digital economy, the Budget proposes to provide that a 'significant economic presence' shall constitute a business connection of a foreign enterprise in India. The term 'significant economic presence' is defined to mean:

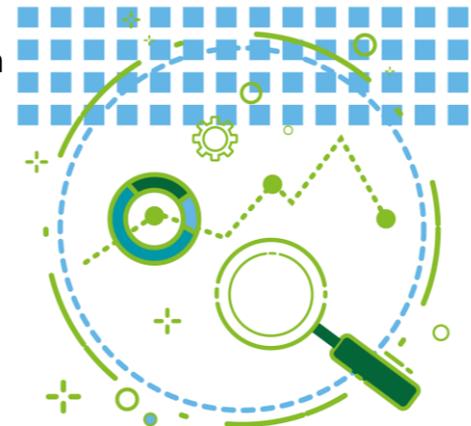
- transaction in respect of any goods, services or property carried out by a foreign enterprise in India, including provision of download of data or software in India if the aggregate of payments arising from such transaction(s) during the year exceeds the prescribed amount; or
- systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.

The threshold of 'revenue' and 'users' in India has not been indicated at present, but will be decided after consultation with stakeholders.

It is further proposed to provide that the transactions or activities shall constitute significant economic presence in India, whether or not the non-resident has a residence or place of business in India or renders services in India.

Generally the business connection rules provide that only such part of the income as is reasonably attributable to the operations carried out in India will be liable to tax in India. However, in the context of 'significant economic presence', the rules provide that only so much of income as is attributable to the transactions or activities shall be liable to tax in India – interestingly, operations carried out in India do not find a mention in respect of a 'digital PE'.

A digital PE or the concept of significant economic presence does not form part of any of India's tax treaties or the MLI. Thus the digital PE would really impact taxpayers who are tax resident of a jurisdiction with which India does not have a tax treaty (example: Hong Kong). The Memorandum explaining the provisions of the Finance Bill however clarifies that the proposed 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 tax treaties.



Country by Country reporting provisions

Being an active member of the BEPS initiative, India was amongst the few jurisdictions that had introduced the three tier transfer pricing documentation requirements as recommended in the OECD BEPS Action Plan 13.

In May, 2016, India introduced core elements of the CbC reporting requirement and the concept of Master File in the Act through Finance Act 2016, effective from 1 April 2016. Recently, the Indian Government released the final rules on CbC reporting and Master File requirements in India.

Certain provisions of the Indian CbC reporting requirements were not aligned with the BEPS Action 13 recommendation. For eg. the OECD recommends that the CbC report be filed within 12 months from the end of the reporting accounting year, whereas India requires filing of CbC report by the due date of filing of the income-tax return. Additionally, various clarifications were required on aspects such as applicability, definition of agreement etc.

The Finance Bill 2018-19 has now proposed certain amendments to the CbC reporting provisions under Section 286, to align with the OECD BEPS Action 13 recommendations. We have analysed below these amendments:

For Indian headquartered International Groups

A parent entity resident in India will be required to file the CBC report in India by the extended due date of 12 months from the end of the reporting accounting year, as against the due date of filing the return of income.

- Due date was already extended to 31 March 2018 for the Financial Year 2016-17, now applicable for all going forward years
- The Master File due date continues to be the due date of filing the return of income i.e. 30th November



Country by Country reporting provisions

For Overseas headquartered International Groups

- An additional condition has been introduced for mandating Indian constituent entities of overseas headquartered group's to file its CbC report in India, where the parent has no obligation to file the CbC report in its jurisdiction.
- As per the original provisions of sec 286(4), an Indian filing requirement was not triggered if there existed either the agreement referred to in section 90 (1) or 90A (1), between India and the parent's jurisdiction or a notified agreement for exchange of the CbC report. The definition of agreement has now been amended to include a combination of both, an agreement such as the DTAA and an agreement for exchange of CbC report (eg. MCAA) notified by the Central Government.
- The due date for furnishing the CbC report has been changed to 12 months from the end of reporting accounting year as against the earlier return filing due date
 - The Master File due date continues to be the due date of filing the return of income i.e. 30th November

- Where an Indian constituent entity is required to file the CbC report in India and the group has appointed an Alternate Reporting Entity (ARE), in addition to satisfaction of the specified conditions, the ARE was required to file the CBC report in its jurisdiction before the India due date to avoid a secondary filing obligation in India. It has now been clarified that if the ARE files the CbC report before the due date prescribed in its own jurisdiction, it would not be required to file the CbC report in India.

The amendments reflect a positive move showing India's intent to align the Indian requirements with the BEPS Action 13 and the global standards. These amendments have been regarded as clarificatory in nature, though few of them are essentially a retrospective amendment resulting in change to the law (applicability, compliance, etc). Thus, these amendments could create their own set of implications and ambiguities for the taxpayers.





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