



India Alert on BEPS Incisive Insights

OECD releases BEPS
final reports: A tax
evolution

Issue no: [BEP/SA/01/2015](#)

In this issue:

- Latest update
- Key highlights
- India perspective and area of impact
- Way forward
- Do you know about Dbriefs?
- Contacts

Latest update

On 5 October 2015, ahead of the G20 Finance Ministers' meeting in Lima on 8 October, the Organisation of Economic Co-operation and Development (OECD) has presented the final package on Base Erosion and Profit Shifting (BEPS) measures for a comprehensive, coherent and coordinated reform of international tax rules.

The BEPS measures involved a two-year consultation process between the OECD, G20, developing countries and the stakeholders from business, academia and civil society organisations. Sixty-two countries including India have collaborated in the G20/OECD-led BEPS project and they have agreed to continue working together at least until 2020. Many more participated in shaping the outcomes through regional structured dialogues.

The BEPS plan is structured around the following three fundamental pillars:

- introducing coherence in the domestic rules that affect cross-border activities;
- reinforcing substance requirements in the existing international standards to ensure alignment of taxation with the location of economic activity and value creation; and
- improving transparency, as well as certainty for businesses and governments.

The final BEPS package includes new minimum standards on the following:

- country-by-country reporting - which for the first time will give tax administrations a global picture of the operations of multinational enterprises
- treaty shopping - to put an end to the use of conduit companies to channel investments
- curbing harmful tax practices - particularly in the area of intellectual property and through automatic exchange of tax rulings
- effective mutual agreement procedures - to ensure that the fight against double non-taxation does not result in double taxation.

The BEPS package also redefines the concept of permanent establishment to curb arrangements which avoid the creation of a taxable presence in a country.

Implementation of BEPS would involve amendments being considered in the domestic tax laws and tax treaties by various countries including India. The instrument will be open for signature by interested countries in 2016. There are some more policy developments expected in 2016 and 2017 including a monitoring mechanism on adopted BEPS measures. The monitoring

group could be extended even more widely as other countries outside the project are invited to join.

Key highlights

The 15 BEPS Actions is intended to equip governments with consistent domestic and international instruments to address tax avoidance and ensure that profits are taxed where economic activities generating the profits are performed and where value is created. Highlights of some of the key action points are as follows:

- **Digital economy:** the concept of permanent establishment is proposed to be widened by modifying the exceptions to permanent establishment to ensure that they are available only for activities that are preparatory or auxiliary in nature. Coverage of income from digital sales under CFC is also expected and the collection of VAT/ GST on cross-border B2C transactions will be on a destination principle basis.
- **Hybrid mismatch arrangements:** where differences in the tax treatment of an entity/ instrument under the tax laws of two or more jurisdictions to achieve double non-taxation are intended, the basic approach recommended is to disallow the expense, with a secondary rule to tax the income, where the payer country does not counter the deduction. These recommendations will neutralise hybrid mismatches, by putting an end to multiple deductions for a single expense, deductions without corresponding taxation or the generation of multiple foreign tax credits for one amount of foreign tax paid.
- **Interest deductions and financial payments:** recommends that countries should limit interest deductions to a fixed percentage of earnings before interest, tax and depreciation (EBITDA). The cap should be in the range 10-30%. Countries may optionally offer a fallback to a group-wide ratio of third party net interest expense, should this be higher.
- **Treaty Abuse:** recommends countries to include anti-abuse provisions in their tax treaties, including a minimum standard to counter treaty shopping. It has also recognized that some flexibility in the implementation of the minimum standard is required as these provisions need to be adapted to each country's specificities and to the circumstances of the negotiation of bilateral conventions. A specific anti-abuse rule, the limitation-on-benefits (LOB) rule that limits the availability of treaty benefits to entities that meet certain conditions will be included

in the OECD Model Tax Convention. In other cases which would not be covered by the LOB rule described above, a more general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purposes test or “PPT” rule) will be included.

- **Permanent Establishment:** the proposal redefines the term ‘permanent establishment’ and includes recommendations to address commissionaire arrangements. With change in the definition of permanent establishment, arguments previously taken by taxpayers in not having a taxable presence within a commissionaire arrangement will be disregarded unless it is proved that activities are performed in the course of independent business. Moreover, in conclusion of contracts, the PE definition has been widened.
- **Transfer pricing on value creation:** The final reports provide guidance to ensure that transfer pricing outcomes are in line with value creation in relation to intangibles, including hard-to-value ones, to risks and capital, and to other high-risk transactions. The aim is to evaluate whether “transfer pricing rules secure outcomes that see operational profits allocated to the economic activities which generate them.”

For intangibles, the guidance clarifies that legal ownership alone does not necessarily generate a right to all (or indeed any) of the return that is generated by the exploitation of the intangible. This implies that entities must be able to control the risks that give rise to potential rewards and the group companies performing important functions, controlling economically significant risks and contributing assets, will be entitled to an appropriate return reflecting the value of their contributions. The report also adds that “capital-rich entities without any other relevant economic activities (“cash boxes”) will not be entitled to any excess profits”, which includes interest. Further, as part of the Report, a mandate is included for follow-up work to be done on the transactional profit split method, which will be carried out during 2016 and finalised in the first half of 2017.

- **Transfer pricing documentation:** a significant development is reorganising transfer pricing documentation across participating countries to enhance transparency while taking into consideration compliance costs. The final deliverable contains guidance on the transfer pricing documentation (master file and local file) and Country-by-Country (CbC) report. The deliverable provides a fixed CbC template with very clear guidance on its use. Authorities are intended to receive the benefit of additional information for risk assessment, provided they have a double tax treaty or a tax information exchange agreement with the parent company country – or both have signed the multilateral Convention on Mutual Administrative Assistance in Tax Matters.

India perspective and area of impact

As a member of the G20 and an active participant in the BEPS project, India is committed to its outcome. Indian authorities believe that structural changes and mechanisms may need to be adopted as the BEPS project outcome will result in an increased flow of information and exchange of information under treaties. While confidentiality is important, an objective from the Indian perspective is to ensure that relevant information is shared under the exchange of information mechanism. India also believes that mandatory and binding arbitration in tax disputes is not acceptable and should remain as an option. For the BEPS actions to be implemented consistently, the multinational Instrument is a practical way to address treaty related measures.

In relation to the actions itself, some key transactions that may be affected from an Indian perspective include digital transactions, holding structures, permanent establishment (taxable presence) and funding transactions/ structures amongst others.

As regards the prevention of treaty abuse, India has already introduced in its domestic law the consolidated rules in the form of General Anti Avoidance Rule (GAAR) as a measure to address treaty shopping and other forms of treaty abuse by shell companies which is likely to be implemented from 2017. Also, with the proposed change in the definition of PE under BEPS, Indian taxation norms are going to be impacted and existing treaties may have to be renegotiated accordingly. It would be essential to provide greater certainty regarding the constitution of the PE and determining the profits attributable to a PE.

The Indian view on marketing intangibles has largely developed on the basis of judicial precedents. Reviewing and aligning with BEPS guidance may pose challenges. Further, the BEPS proposals on the treatment of assigning profits where value creating activities are undertaken, will have to be aligned with India specific guidance on this matter.

The Indian transfer pricing regulations presently do not provide for maintenance of information contained in the master file and CbC template. Rules may need to be framed to accommodate these and avoid duplicity with domestic compliance norms. To collate the required information, taxpayers, particularly outbound businesses would need to put in place a robust information tracking and collection system, leading to an increase in their transfer pricing compliance

efforts. As a consequence, the larger companies may be required to consider technology solutions to collect, store, analyse, and prepare the CbC template and master file. Further, while the timelines of this guidance being implemented in India is still awaited, considering the OECD proposed timelines on CbC reporting, companies may need to take this on priority.

Way forward

The G20/OECD working group notes that “although measuring the scale of BEPS proves challenging given the complexity of BEPS and the serious data limitations, today we know that the fiscal effects of BEPS are significant. The group estimates that BEPS has cost some 4-10% of annual corporate tax revenues.

There are two big questions on the BEPS Actions: when will they be implemented and which countries will implement the Actions. The Explanatory Statement sets out the various levels of agreement:

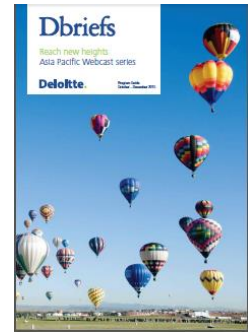
“All OECD and G20 countries commit to consistent implementation in the areas of preventing treaty shopping, Country-by-Country Reporting, fighting harmful tax practices and improving dispute resolution. Existing standards have been updated and will be implemented, noting however that not all BEPS participants have endorsed the underlying standards on tax treaties or transfer pricing [understood to be only Brazil].

The G20/OECD will undertake more work in 2016 on several Actions:

- Harmful Tax Practices: revision of criteria; expanding participation of non-OECD countries.
- Treaty Abuse: treaty entitlement of certain funds.
- Interest: finalise design of group ratio carve-out, special rules for banking, insurance.
- Permanent Establishments: profit attribution rules.
- Transfer Pricing: financial transactions, use of the profit split method.

Do you know about Dbriefs?

Dbriefs are live webcasts that give valuable insights on important developments affecting your business. To register, visit the [Dbriefs page](#)



 Download the report

Contacts

Ahmedabad

Heritage, 3rd Floor,
Near Gujarat Vidyapith,
Off Ashram Road,
Ahmedabad – 380 014.
Tel: + 91 (079) 2758 2542
Fax: + 91 (079) 2758 2551

Coimbatore

Shanmugha Manram
41, Race Course,
Coimbatore
Tamil Nadu - 641018
Tel: + 91 (0422) 439 2801
Fax: +91 (0422) 222 3615

Kolkata

Bengal Intelligent Park Building Alpha,
1st floor, Block EP and GP Sector V,
Salt Lake Electronics Complex,
Kolkata - 700 091.
Tel : + 91 (033) 6612 1000
Fax : + 91 (033) 6612 1001

Bangalore

Deloitte Centre, Anchorage II,
100/2, Richmond Road,
Bangalore 560 025.
Tel: +91 (080) 6627 6000
Fax: +91 (080) 6627 6010

Delhi/Gurgaon

Building 10,
Tower B, 7th Floor,
DLF Cyber City,
Gurgaon 122 002
Tel : +91 (0124) 679 2000
Fax : + 91 (0124) 679 2012

Mumbai

Indiabulls Finance Centre,
Tower 3, 28th Floor,
Elphinstone Mill Compound,
Senapati Bapat Marg, Elphinstone (W),
Mumbai – 400013
Tel: + 91 (022) 6185 4000
Fax: + 91 (022) 6185 4101

Chennai

No.52, Venkatanarayana Road,
7th Floor, ASV N Ramana Tower,
T-Nagar,
Chennai 600 017.
Tel: +91 (044) 6688 5000
Fax: +91 (044) 6688 5050

Hyderabad

1-8-384 and 385, 3rd Floor,
Gowra Grand S.P.Road,
Begumpet,
Secunderabad – 500 003.
Tel: +91 (040) 6603 2600
Fax: +91 (040) 6603 2714

Pune

106, B-Wing, 7th Floor,
ICC Trade Tower,
Senapati Bapat Road,
Pune – 411 016.
Tel: + 91 (020) 6624 4600
Fax: +91 (020) 6624 4605

This material and the information contained herein prepared by Deloitte Touche Tohmatsu India LLP (DTTI LLP) is intended to provide general information on a particular subject or subjects and is not an exhaustive treatment of such subject(s). This material contains information sourced from third party sites (external sites). DTTI LLP is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such external sites. None of DTTI LLP, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this material, rendering professional advice or services. The information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this material.

©2015 Deloitte Touche Tohmatsu India LLP. Member of Deloitte Touche Tohmatsu Limited.

Registered office: 12, Dr. Annie Besant Road, Opp. Shiv Sagar Estate, Worli, Mumbai – 400 018, India.
Deloitte Touche Tohmatsu India Private Limited (U74140MH1995PTC093339), a private company limited by shares, was converted into Deloitte Touche Tohmatsu India LLP (LLP Identification No. AAE-8458), a limited liability partnership, with effect from October 1, 2015.

[Home](#) | [Add Deloitte as a safe sender](#)

Follow us on:

