



**Taxation of cross border HO – BO business models**  
**The Dbriefs Tax series**

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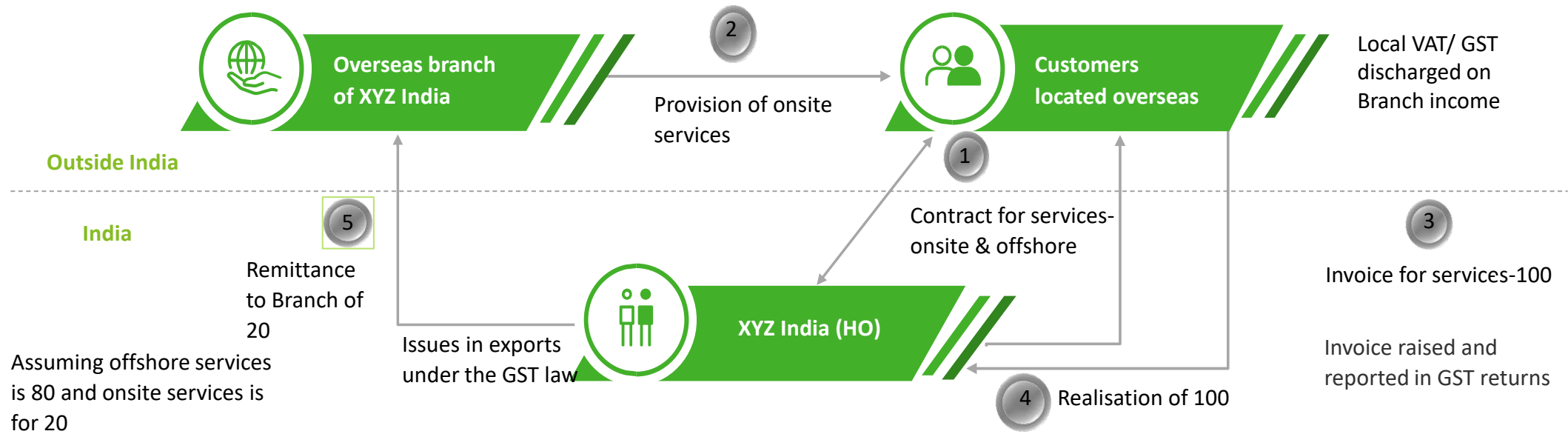
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# Agenda

- Overview of various Head Office(HO)-Branch Office ('BO) business models
- Case studies on HO-BO issue
- Impact on similar companies
- Key aspects to be considered for HO-BO arrangements

# Overview of various Head Office(HO)-Branch Office ('BO) business models

# Case Study 1: Overview of HO-BO business model (Variant 1)



Indian IT companies operate through a global delivery model



While the contractual relationship maybe between the Indian HO and the Overseas BO, some part of the contract is executed between the HO in India and some part by the overseas BO which is in a non-taxable territory

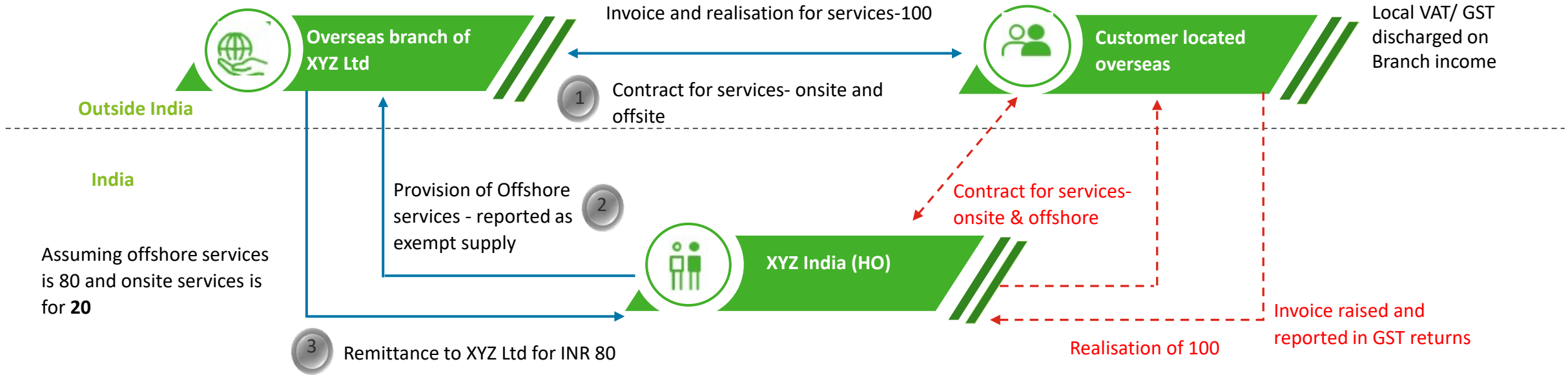
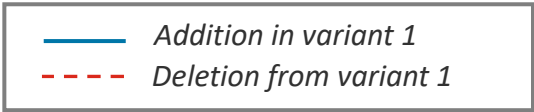



The BO delivers the services directly to the customer outside India, the portion of revenue attributable to the BO is subject to VAT and corporate income tax of the relevant country





As per the terms of the contract, one integrated price may be paid to the Indian HO. Thereafter, the HO in turn transfers funds to the branch for its day-to-day expenses


# Case Study 1: Overview of HO-BO business model (Variant 2)



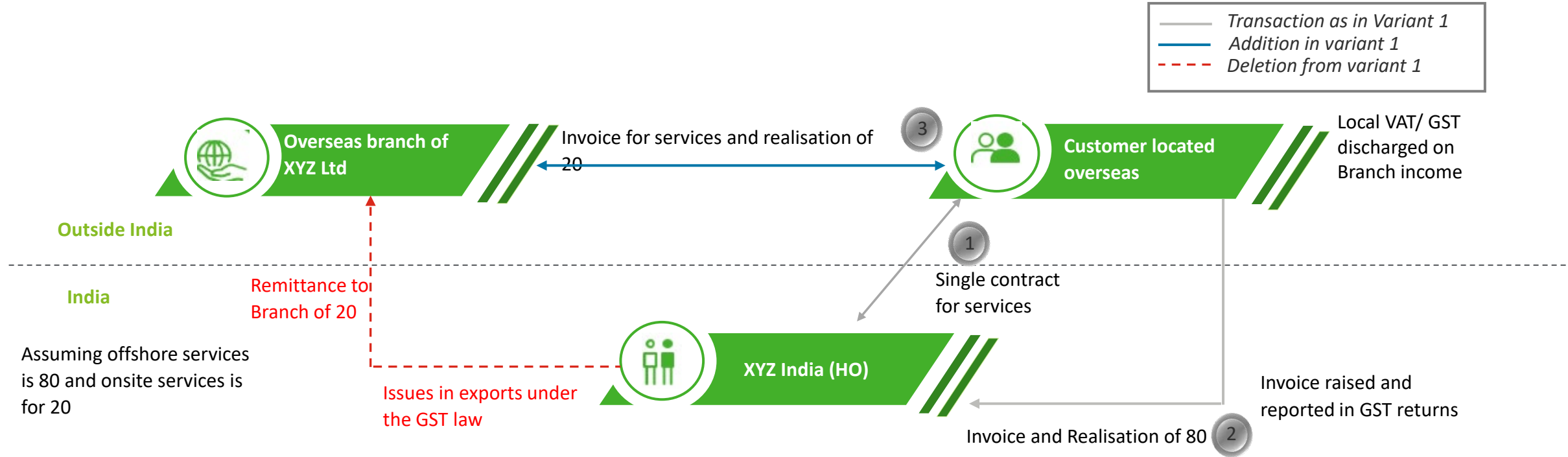
 Indian IT companies operate through a global delivery model

 While the contractual relationship maybe between the overseas BO and overseas customer, some part of the contract is executed between the HO in India and some part by the Overseas BO which is in non-taxable territory

 The HO deliver the services to the overseas branch, the portion of revenue attributable to the HO is exempt from GST by way of a notification No. 15/2018 dated 26-07-2018

 As per the terms of the contract, one integrated price may be paid to the overseas BO. Thereafter, the overseas BO in turn transfers remittance to HO in India

# Case Study 1: Overview of HO-BO business model (Variant 3)



Indian IT companies operate through a global delivery model

For a particular contract, some part of the contract is executed between the HO in India and some part by the Overseas BO which is in non-taxable territory

The BO and HO deliver the services directly to the customer outside India, the portion of revenue attributable to the BO is subject to VAT and corporate income tax of the relevant country

As per the terms of the contract, the price may be paid separately to overseas BO and HO. The portion of revenue attributable to the HO is subject to GST and corporate income tax of the India

# Relevant GST provision and circular

Relevant  
GST provision

Section 7 of the CGST Act 2017, “Supply” includes the activities mentioned in Schedule-I of the CGST Act, made or agreed to be made even **without consideration**

**S. No. 4 of Schedule -I of the CGST Act 2017 states**

Import of services by a person from a related person or from **any of his other establishments outside India**, in the course or furtherance of business shall be considered a supply even if made without consideration

Definition: Import of services

Section 2(11) of the IGST Act 2017 defines the import of services as any services where –

- The supplier of services is located outside India
- The recipient of services is in India
- The place of supply is in India

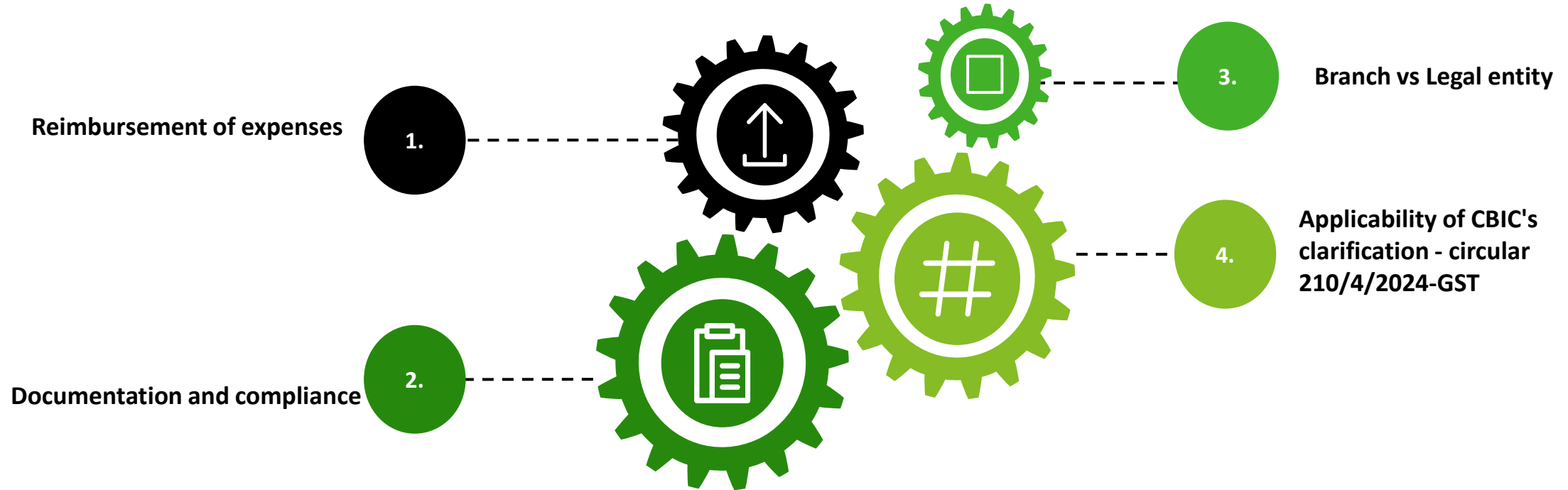
**The supply shall be considered as an import of services only upon the satisfaction of the above three conditions**


Circular No. 210/4/2024-GST


- This circular applies to scenarios involving the import of services between related parties where the recipient is entitled to claim full Input Tax Credit (ITC)
- The circular clarifies that, if the recipient in India is eligible for full ITC, any value declared by the recipient as import, shall be deemed to be the open market value
- Basis the above, even “NIL” value may be deemed to be the open market value




# Emerging tax issues respect of HO-BO arrangements





 IT/ITeS

 Shipping

 Airlines

 Banks

 Logistics

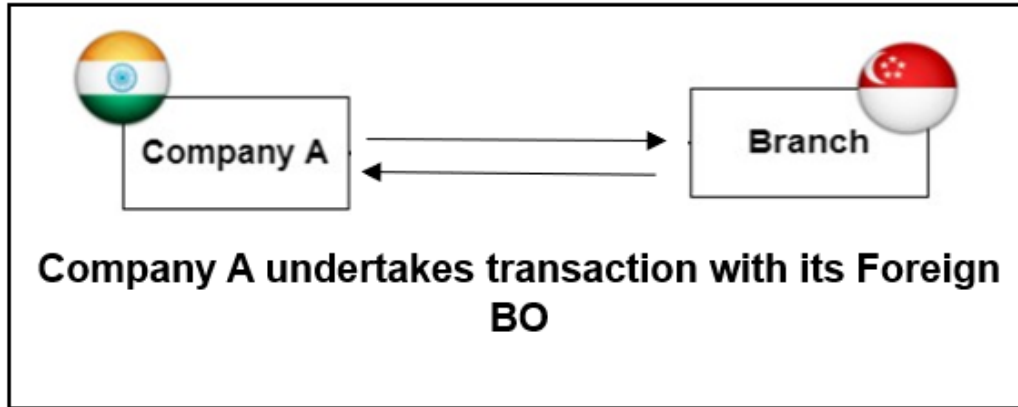
 Infra projects

## Polling question 1

Do you think the recent circular issued under GST on HO-BO transactions and FOC import of services provides sufficient clarity?

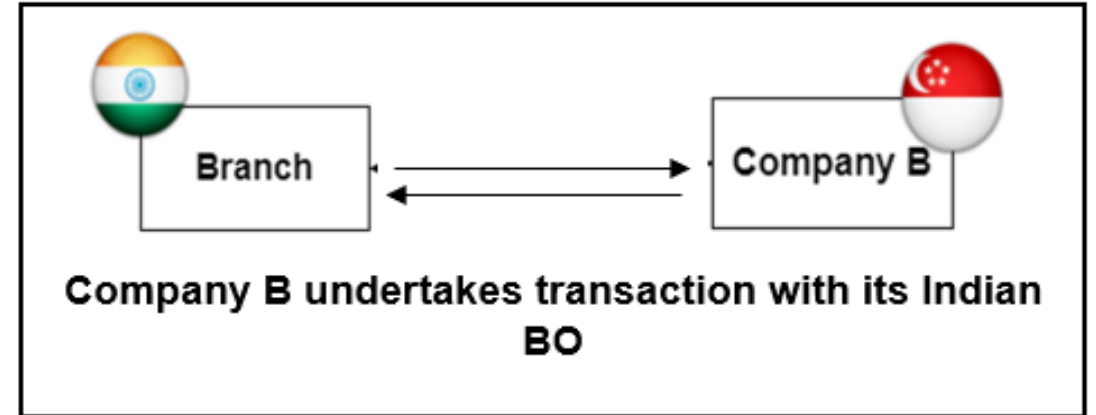
- Yes
- No
- May be

## Transaction between HO and BO



### Will this transaction be an international transaction?

- Section 92B(1) defines, international transaction to mean a transaction between two or more associated enterprises, either or both of whom are non-residents
- BO is considered as a tax resident of India and given that the transaction between Company A and Foreign BO is between two residents, hence, above transaction is not an international transaction
- BO would be subject to requirements of transfer pricing under local country regulations. (using AOA or other regulations as specified)



### Will this transaction be an international transaction?

- The Indian BO is a Non-resident of India being the permanent establishment of a Foreign HO
- Accordingly, as per section 92B (1) read with section 92F (which defines the terms enterprise and starts as any person (including a permanent establishment of such person...))
- The transaction between an Indian BO and Foreign HO is within two non-residents, hence, the said transactions is an international transaction and accordingly, the Indian transfer pricing provisions are applicable to such transactions

# Transfer pricing considerations for HO BO business models

## Variant 1

- Indian HO has an arrangement for subcontracting the services to the Foreign BO, accordingly the Foreign BO shall be characterised as a routine service provider and shall be remunerated accordingly
- In practice, such Foreign BOs are remunerated on a cost-plus markup pricing mechanism
- There is a risk on account of the attribution of appropriate income to the Foreign BO
- The local tax authorities question the remuneration attributable to the Foreign BO and can propose an adjustment

## Variant 2

- Higher risk than variant 1 on account of attribution of income to the Foreign BO
- The local tax authorities may allege that higher revenue should be attributable to the Foreign BO, as the contract is entered by the Foreign BO
- The local authorities may consider recharacterization of the Foreign HO from a routine service provider bearing limited risk to an entrepreneurial entity

## Variant 3

- There is a clear demarcation of the nature and extent of services provided by the HO and BO along with separate consideration for the services rendered
- Least litigative from transfer pricing perspective

For all the above variants a well-articulated documentation discussing appropriate delineation of the functions performed, assets used to provide services and the risk borne; characterisation of the HO and BO, appropriate pricing mechanism should be maintained.

# Direct tax considerations

## Scope of total income of XYZ India

- Under Indian tax laws, XYZ India, being an Indian company will be an India tax resident
- XYZ India will be taxed in respect of its global income (including income of the overseas branch)
- Transactions between the HO & BO will be eliminated in computing taxable profits in India



## Applicability of branch profit tax

- The overseas jurisdiction is likely to treat the branch as a permanent establishment of XYZ India and tax its profits at applicable rates
- Generally, the branch will be considered as a distinct entity for the purposes of computation of the tax
- A branch remittance tax may be levied by some countries (for instance USA) on profits sought to be ploughed back to the HO



## Availability of foreign tax credit and IECR matters

- The Indian tax law read with tax treaties generally provide for a relief from double taxation by allowing XYZ India foreign tax credit
- The Indian exchange control regulations permit opening of a bank account outside India in the name of the branch
- At the time of setup – XYZ India is permitted to remit amounts for initial expenses – upto 15% of average sales/turnover during last two FYs or 25% of net worth of XYZ India, whichever is higher
- For recurring expenses, XYZ India may remit upto 10% of average sales/turnover for last two FYs



## Polling question 2

Are you currently paying tax under reverse charge mechanism on import of services between HO and BO?

- Yes
- No
- Not applicable

## Case Study 2 : Overview of FOC supplies between HO and BO

### Brand, logo, trademark, fixed assets and/or other intellectual property

- IP typically used by the companies located in India for the limited purpose for provision of services to the overseas group companies
- Fixed assets / goods received by the Indian entity from its overseas related party



### Technology (Software or IT) services

- Software licenses held by overseas entity and used in India
- Software or IT services provided to Indian company for providing services back to overseas entities or to Indian customers



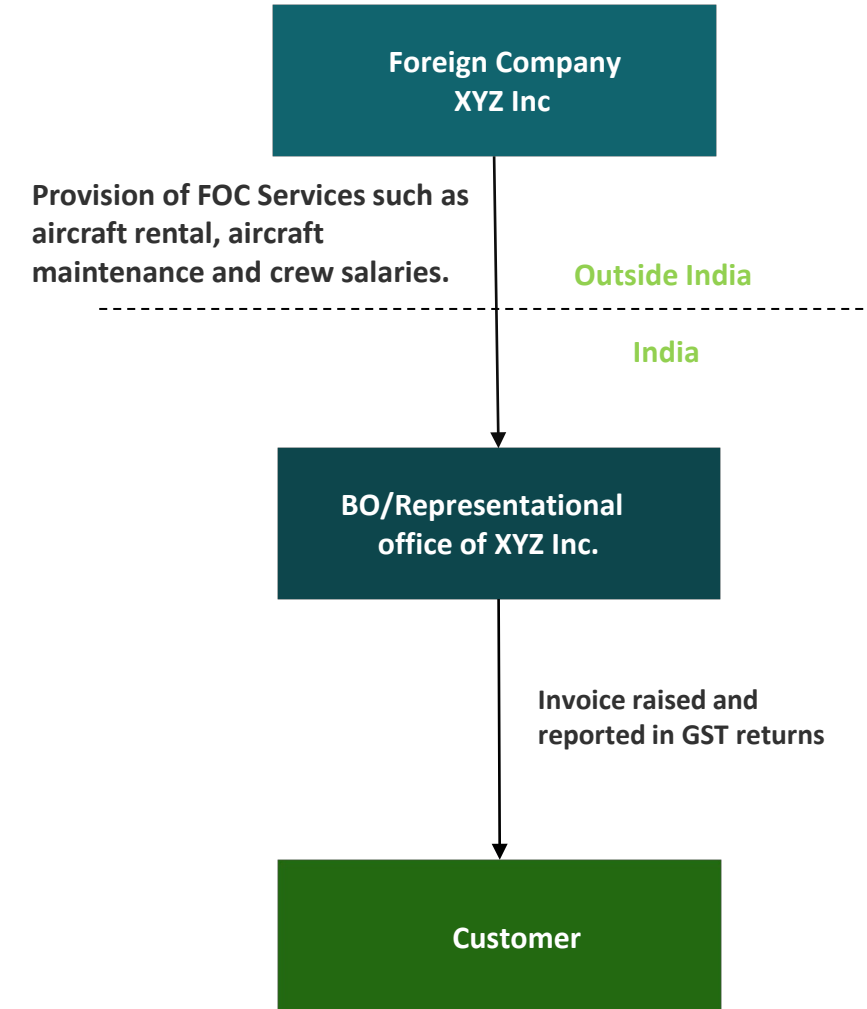
### Financial transactions

- Loans granted by group companies without any notional fees/ charges



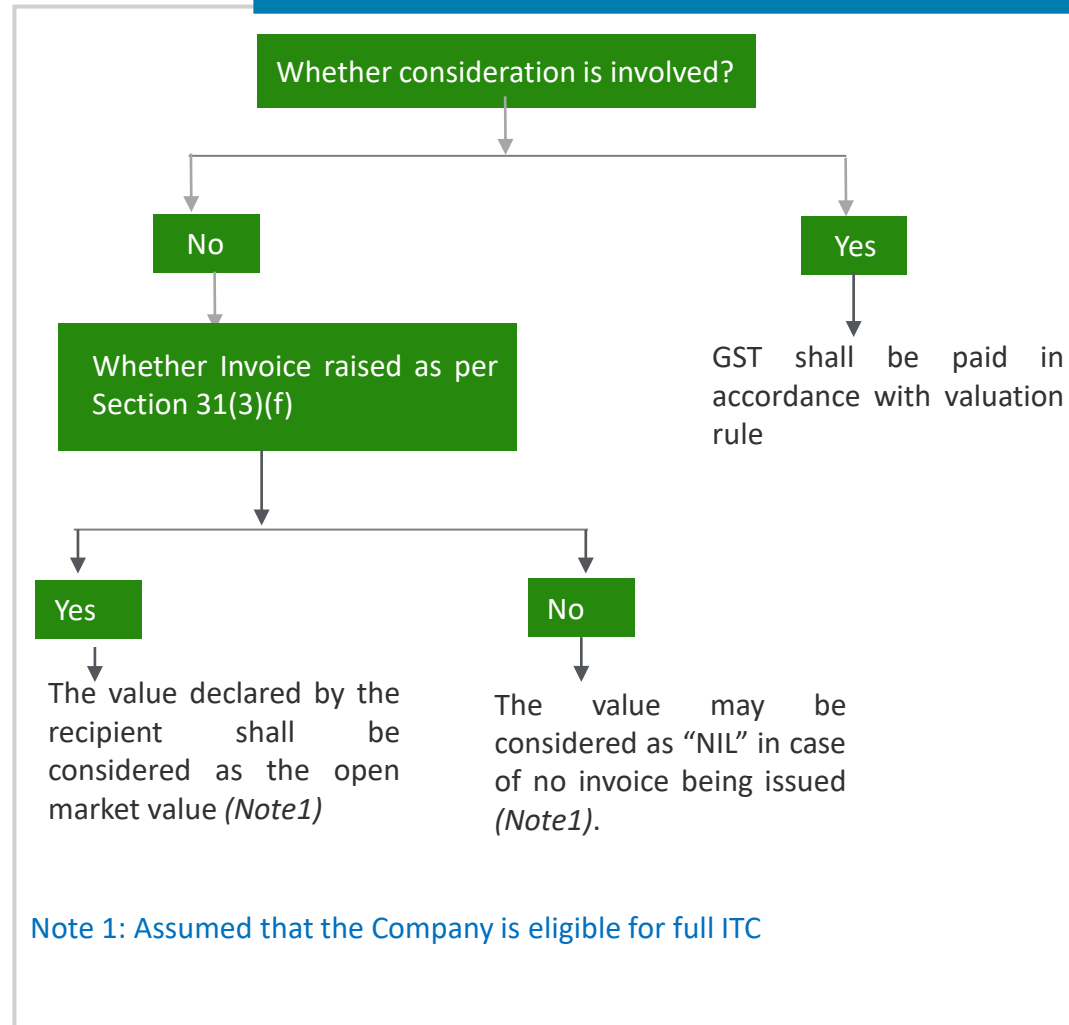
### Support services

- Activities performed by overseas entity in day-to-day functions of the Branch/ Shareholder activities/ Intra-group services performed by overseas related party/HO
- Legal services, tax service, cash flow management, accounting, auditing and budgetary control, etc.
- Ground handling, crew expense, aircraft leasing, aircraft maintenance etc. in case of airline industry



# Impact of GST on “free of cost” (FOC) transactions between HO and BO

## Current tax environment



Activities undertaken between related parties **without consideration** (FOC supplies) are deemed to be 'supply' - Schedule 1, Entry 4

Important to analyse following aspect as the GST law provides for an inclusive definition of supply:

- Whether transaction qualifies to be a 'supply',
- Whether the recipient of 'supply' is commercially exploiting such transactions

Activities being performed by the overseas entities for Indian subsidiaries on FOC basis may be under an agreement or otherwise

Notices have been issued to taxpayers on FOC transactions. GST Authorities seek documents such as APA at the time of audits to ascertain value of the FOC transactions

All the examples illustrated in the previous slides have been picked up by tax authorities

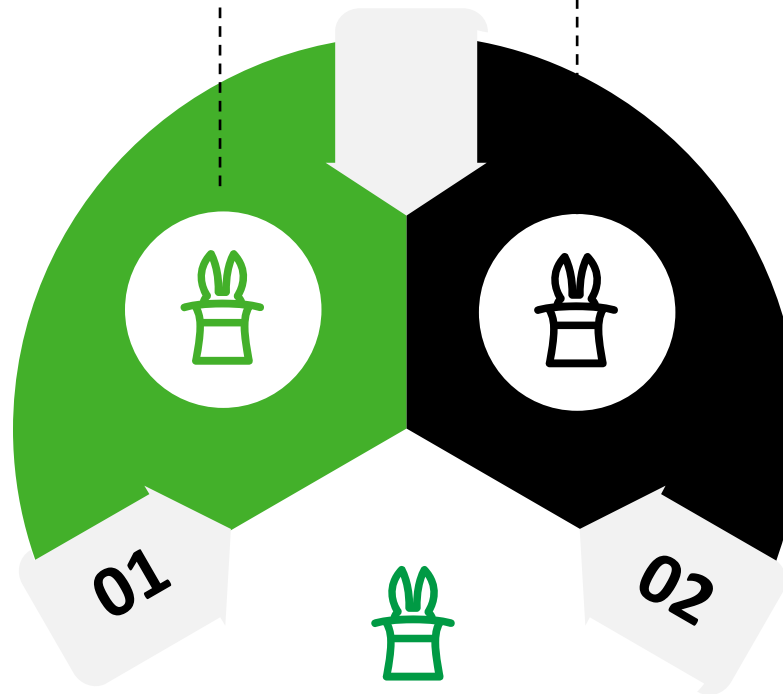
The GST Council in 54<sup>th</sup> council meeting has recommended to exempt the import of services on a FOC by **foreign airline establishments** from related persons outside India  
**\* For past periods, council has recommended regularizing on "as is where is" basis**



# Direct tax considerations

## Scope of taxable income in India and foreign tax credit

- Branch will be considered as a PE of the foreign company
- Under Indian tax laws read with the tax treaties, profits attributable to the Indian branch (after providing for a deduction of expenses) will be taxed in India @ 38.22%
- A credit of this is likely to be available in the home jurisdiction of the foreign company



## Branch remittance tax in India

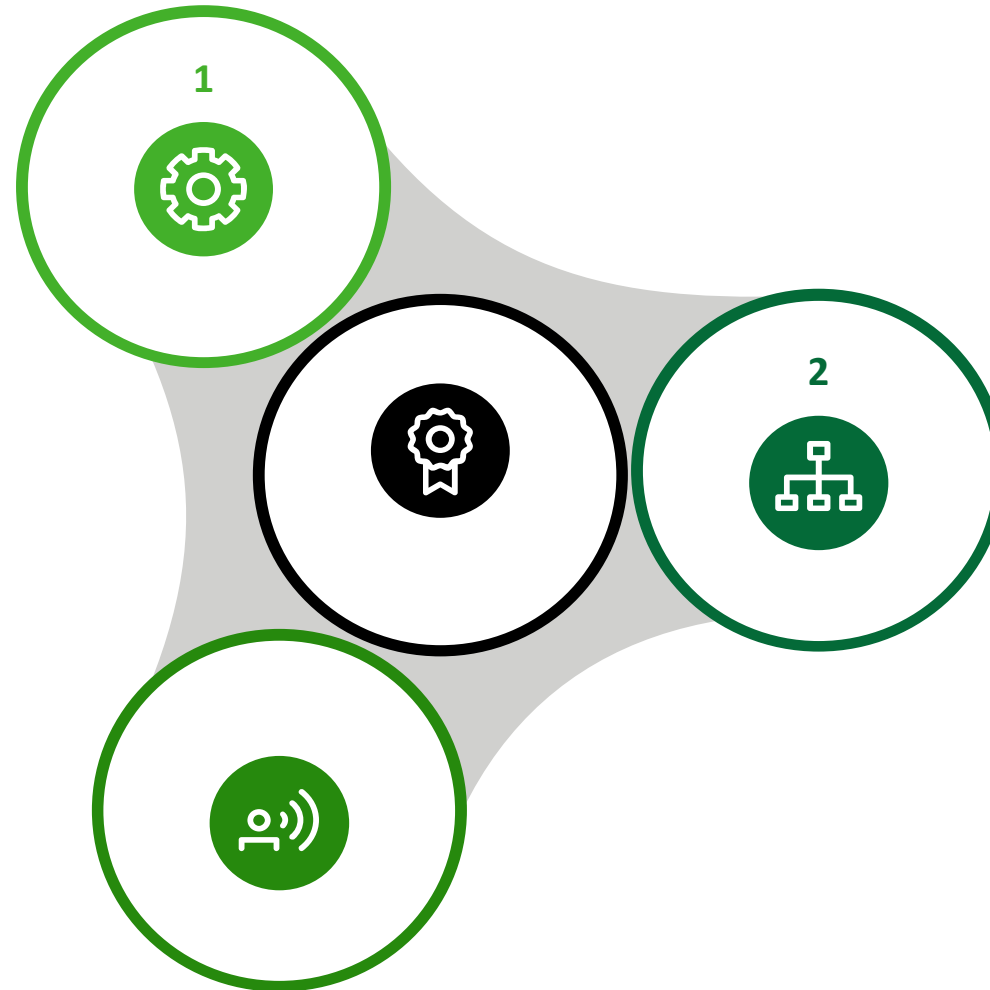
There is no branch remittance tax on profits repatriated by the Indian branch to its head office

Accordingly, no income tax would arise in India on repatriation of surplus profits to the home country of the foreign company

# Transfer pricing considerations

## Free of cost supplies by HO to BO

Free of cost goods/ services, transaction has to be reported in Form 3CEB, further where amounts are recognized on a notional basis in the books of accounts, the same should be in conformity with arm's length principle.



**For intra group services** by the Foreign HO to the Indian BO following has to be analyzed:

- Whether an intra-group service that should be charged for has been provided; and
- What the charge should be in accordance with the arm's length principle

Further, in case the services are in the nature of low value added intra group services, safe harbour option is available wherein cost including a mark-up not exceeding 5 per cent could be charged

## Polling question 3

Should the value of goods/ services/ FOC between the related party transactions as per GST be harmonized with the transfer pricing regulations?

- Yes
- No
- May be

## Case Study 3: Overview of scenarios where supplies are made from multiple locations (branches in different States) to the recipient under a single contract.

### Agreement executed between main branch/ HO and customer

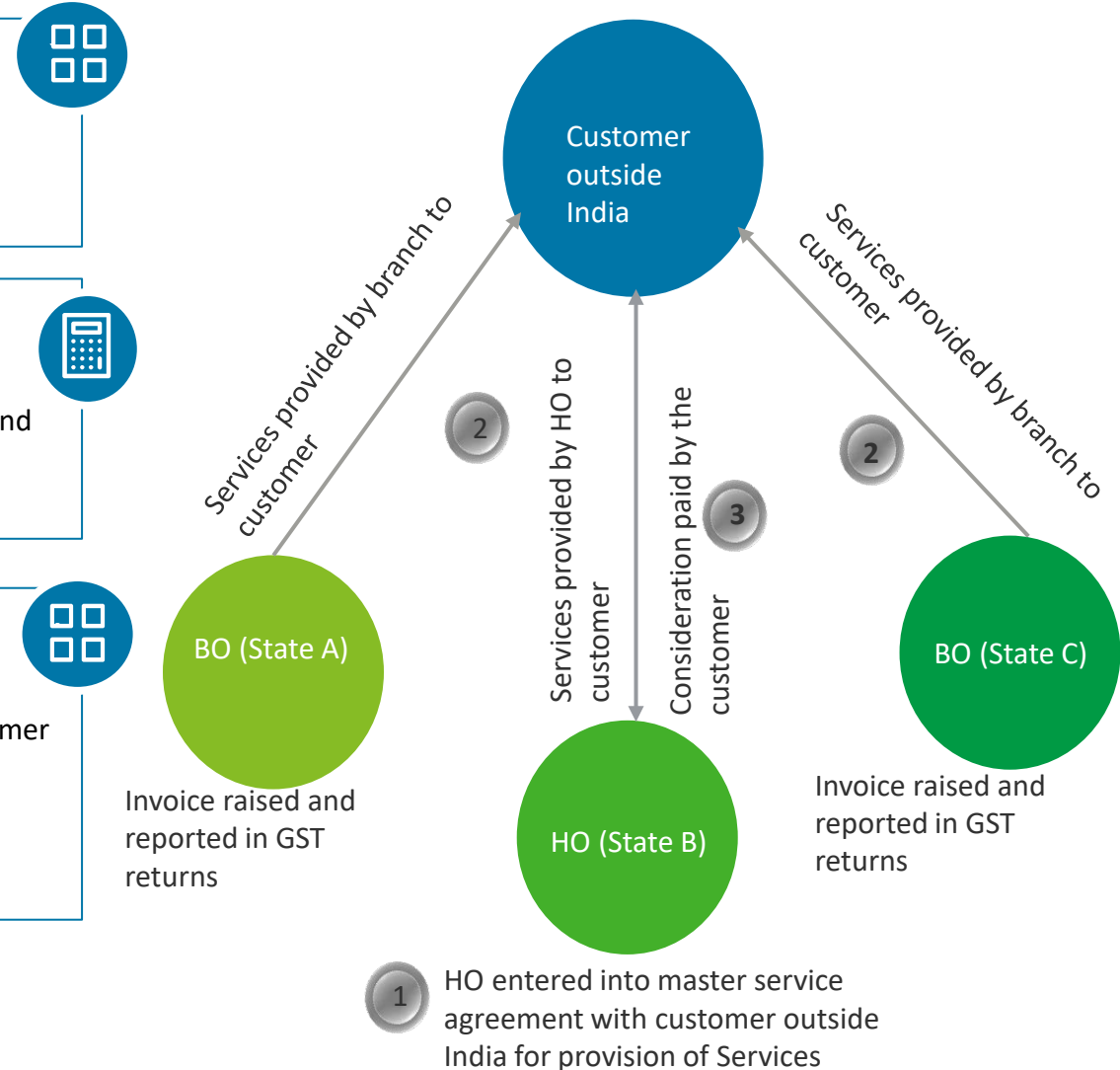
- The agreement for provision of services entered between the HO in State B and the customer located outside India

### Provision of services by the branch

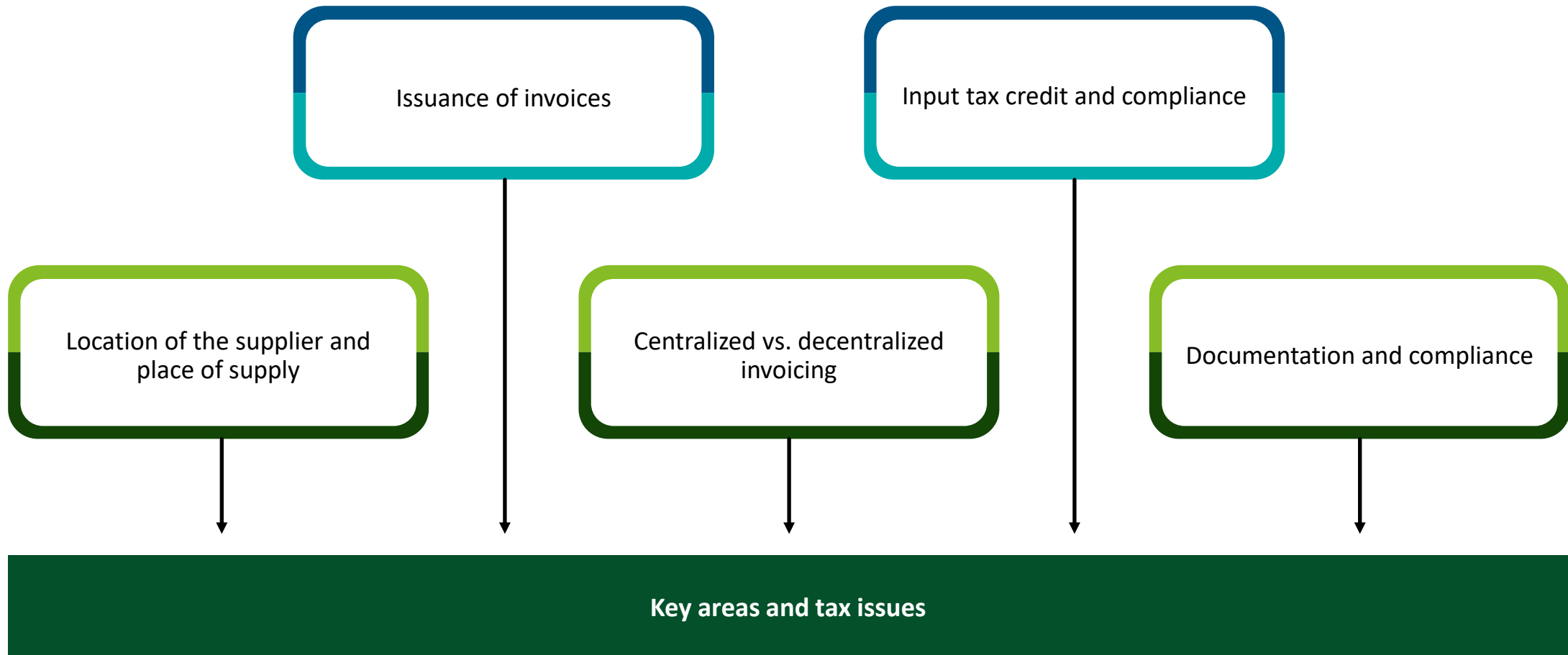
- The provision of the services may be done by the branch in another state (let say State A and C) and the invoice for the service has been raised by the branch

### Issue Involved

- The revenue has taken the view that the invoice should be issued by the Head Office to the customer
- Given that the customer has entered into an agreement directly with the Head Office
- Consequently, the invoice should be reported in the GSTR-1 and GSTR-3B returns of State B registration



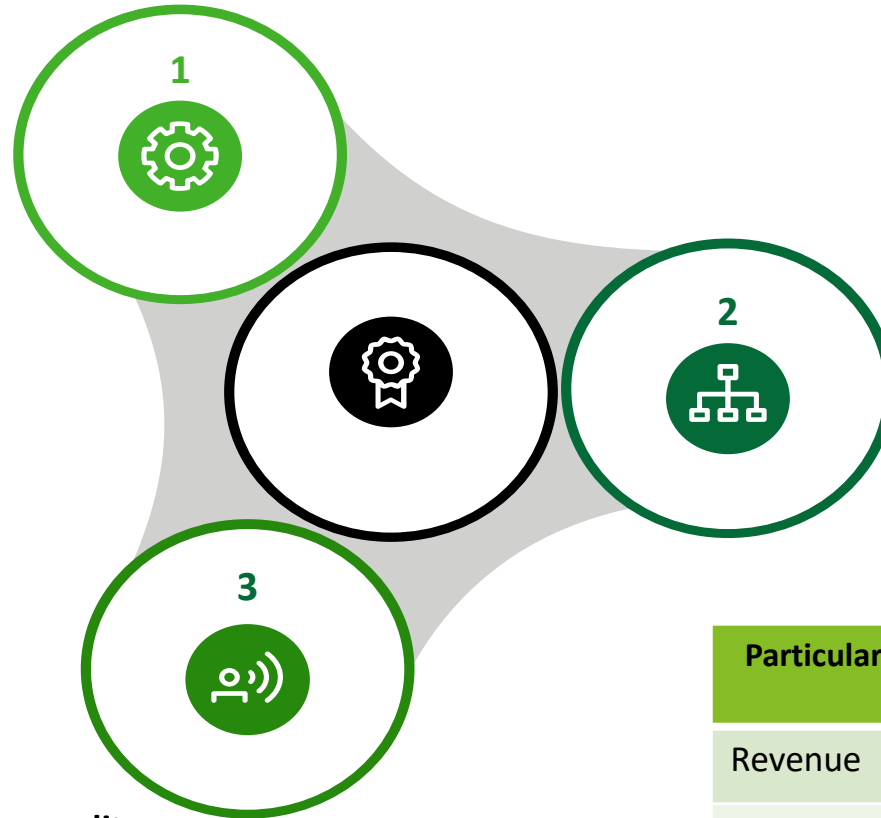
# Impact of GST where supplies are made from multiple locations (branches in different States) to the recipient under a single contract



# Direct tax considerations

## Tax when both HO-BO are DTA units

- The Indian entity with the head office in Karnataka will have one direct tax registration
- Its income earned from all the branches (including the Maharashtra branch) will be taxed on a consolidated basis under the above direct tax registration
- Expenses incurred by the HO in Karnataka and BO in Maharashtra (other than inter-branch transactions) will be allowable as deduction in computing taxable income



## Tax credits

Taxes withheld by the customers of XYZ India will be available as a credit against the corporate income tax payable by XYZ India in its tax return

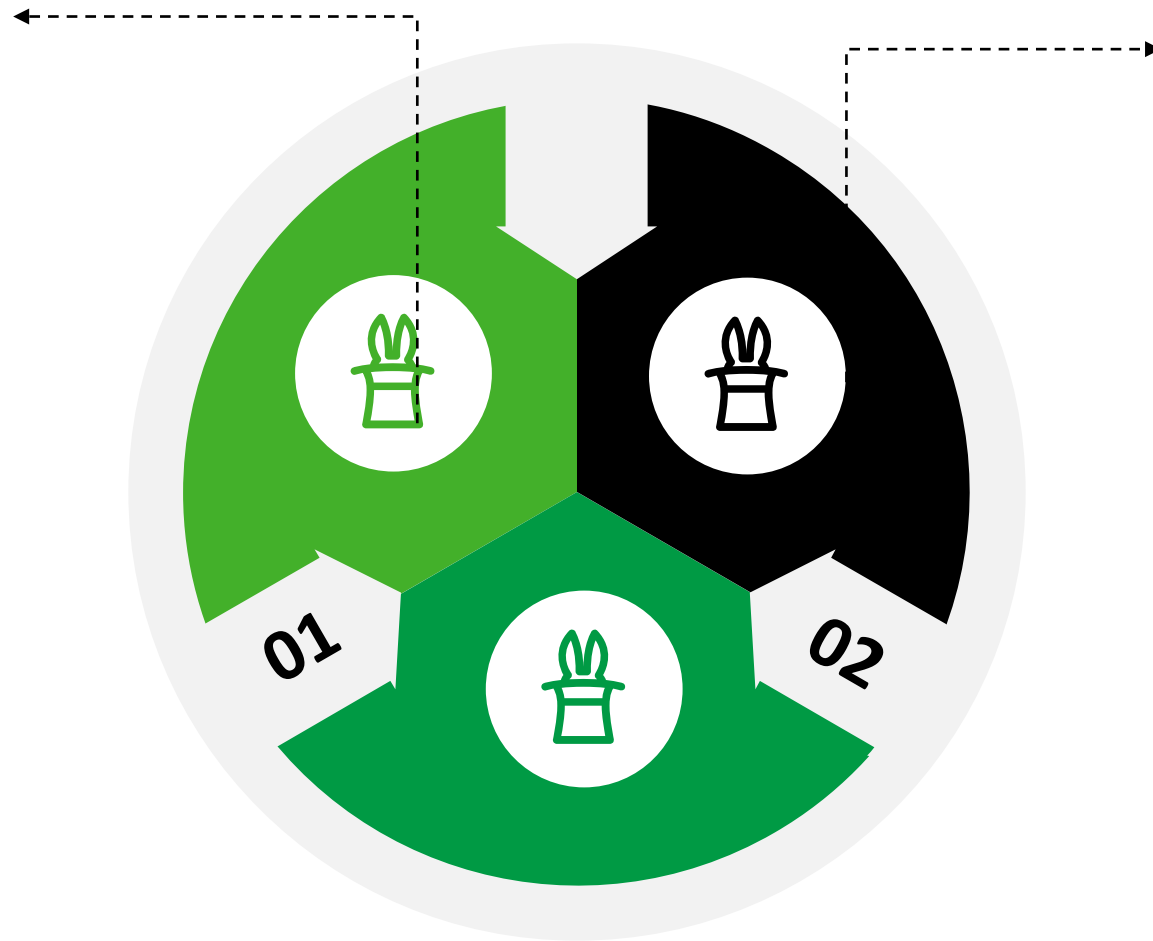
## Tax when either of them is an SEZ unit

- Where the taxpayer has SEZ and DTA unit, the transactions between them should be arranged on an arm's length basis
- The transactions between them should not be arranged in a manner to produce extra-ordinary profits to the SEZ unit (to maximize exemption)
- Profits will be calculated with respect to the SEZ and DTA units respectively
- Profits of SEZ unit will be eligible for an exemption in terms of the tax laws
- Profits of DTA units will be taxable

Particulars	State A – BO – DTA – 10%	State B – HO – SEZ – 80%	State C – BO – DTA – 10%	Total
Revenue	30	240	30	300
Less: Expenses	24 (10%)	192 (80%)	24 (10%)	240
Profit	6	48	6	60
Tax rate	25.17%	-	25.17%	-
Tax	1.5	-	1.5	3

# Transfer Pricing considerations

- In case where the HO/ BO claims benefit under section 10AA or section 80IA, **specified domestic transaction (SDT)** provision needs to be analysed
- The entity claiming benefit under section 10AA or section 80IA has to obtain report from CA for its transaction with the other unit



The transactions between the HO and BO [where either of them claiming benefit under 10AA or for any transfer of goods/ services as referred in section 80IA (8)] are subject to the specified domestic transaction has to be in accordance with the arm's length principle

## Polling question 4

Do you prepare transfer pricing documentation for a Foreign BO?

- Yes
- No
- Depends on the audit and local requirements



# Question and answers

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