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Global Tax Update

India

Deloitte Tohmatsu Tax Co.

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1. Reserve Bank of India tightens norms for issue of Rupee-Denominated Bonds (or Masala Bonds) overseas

In 2015, Reserve Bank of India (RBI[1]) permitted Indian entities to issue Rupee-Denominated Bonds (RDBs)/ Masala bonds overseas, so as to access funds from foreign investors in Indian currency. With a view to align the various elements of the External Commercial Borrowings (ECB) framework, RBI has, on 07 June 2017, made amendments[2] to the provisions in respect of maturity period, all-in-cost ceiling and recognized lenders (investors) of RDBs. The highlights of the amendments are summarized below.

1	Review of proposals by RBI, Mumbai	Proposals with regard to borrowing by eligible Indian entities by issue of RDBs will be examined by the Foreign Exchange Department, Central Office of RBI, Mumbai and shall be forwarded through Authorised Dealer bank (earlier there was no such requirement of RBI approval)
2	Maturity period	■ Minimum original maturity period of 3 years for RDBs raised up to $50 million equivalent in INR per financial year; and ■ Minimum original maturity period of 5 years for RDBs raised above $50 million equivalent in INR per financial year. (earlier it was 3 years)
3	Recognized Investors	Entities permitted as investors should not be a 'related party' as defined under Indian Accounting Standard (IND-AS) 24 and accordingly, they cannot subscribe or invest in or purchase RDBs. (earlier related parties were considered as eligible investors)
4	All-in cost ceiling	300 basis points over and above prevailing yield of government of India securities having corresponding maturity. (earlier condition stated that it should commensurate with the prevailing market conditions)

2. Central Board of Direct Taxes notifies rule for secondary adjustments

Central Board of Direct Taxes (CBDT) has issued a notification[3], issuing rule for secondary adjustment legislation[4] introduced through the Finance Act 2017.

The Rule covers two aspects of computation of interest on secondary adjustment. It was mentioned in the new legislation[5] that certain factors would be prescribed later, namely, time limit for repatriation of excess money and imputed per annum interest on excess money.

1 India's Apex Bank

2 RBI A.P. (DIR Series) Circular No.47 dated June 07, 2017

3 Notification, dated 15 June 2017

4 The law attempts to remove the imbalance between the actual profit allocation (consistent with the arm's length principle) vis-àvis the cash account of the taxpayer. Taxpayer in India is required to receive cash in case a primary adjustment to transfer price has been made suo-moto/ by tax or appellate authority and it is accepted, else a secondary adjustment (notional interest) is imputed deeming the adjustment as advance.

5 Section 92CE of the Income-tax Act, 1961

① With respect to the time limit for repatriation of excess money, the rule mentions the time limit to be within or on 90 days – (1) from the due date of filing return of income in cases of suo-moto adjustment, Mutual Agreement Procedure (MAP) settlement and safe harbour, (2) from the date of the order determining the transfer price in case of adjustment by the assessing officer or appellate authority and accepted by the taxpayer, and (3) from the due date of filing modified return or the due date of filing return of income, as the case may be, in case of Advanced Pricing Agreement (APA).

② For the imputed per annum interest income on excess money, the new rule provides for two options – rupee denominated international transaction or foreign currency denominated international transaction. In the case of rupee denominated transaction, the annual interest rate would be one-year marginal cost of fund lending rate of SBI prevalent as on April 1st of the relevant previous year plus 325 basis points, and for foreign currency denominated transaction, it will be 6 month LIBOR as on September 30th of the relevant previous year plus 300 basis points.

An explanatory memorandum issued with the above rule mentions that the provision shall be applicable to primary adjustments exceeding Rs. 10 million made in respect of the assessment year 2017-18 (Financial Year 2016-17), and onwards.

3. Welcome amendments in Indian safe harbour rules

The CBDT has made amendments in the existing safe harbour rules. In this respect, CBDT issued a notification on June 7, 2017. The amendments in the Notification are primarily in the applicable safe harbour rates. It also brought within the ambit of safe harbor rules, the receipt of low value-adding intra group services. Safe harbour rules were first introduced in September 2013 and were applicable for five years from Financial year (FY 2012-13 to FY 2016-17). The amended safe harbour rules will be applicable for only three years, from FY 2016-17 to FY 2018-19. Accordingly, FY 2016-17 is the overlapping year. The Notification specifically provides that for the overlapping year, the taxpayer will have the option to apply the old safe harbour rates or the new safe harbour rates whichever is more beneficial.

The comparative analysis of the pre and post amendment safe harbour rates are given below for few transactions, for more details, refer the notification or reach out to us:

For provision of software development services and information technology enabled services

Threshold for Value of international transactions (INR in billions)		Circumstances (minimum operating margin on cost)	
Pre amendment	Post amendment	Pre amendment	Post amendment
Up to 5	Up to 1	20%	17%
More than 5	1-2	22%	18%

For manufacture and export of auto components

Particulars	Circumstances (minimum operating margin on cost)	
	Pre amendment	Post amendment
Manufacture and export of core auto components	12%	12%
Manufacture and export of non-core auto components	8.5%	8.5%

For provision of contract research and development services

Particulars	Circumstances (minimum operating margin on cost)	
	Pre amendment	Post amendment
Provision of contract R&D services wholly or partly relating to software development	30% (no threshold)	24% (international transaction up to INR 2 billion)
Provision of contract R&D services wholly or partly relating to pharmaceutical drugs	29% (no threshold)	24% (international transaction up to INR 2 billion)

For receipt of low value-adding intra-group services

Particulars	Circumstances (Minimum operating margin on cost)	
	Pre amendment	Post amendment
Low value adding intra group services	Not an eligible transaction	Up to 10 crore (including maximum mark-up of 5%)

4. CBDT notifies[6] transactions for availing long term capital gains tax exemption on sale of shares on stock exchange

The ITA[7] exempts long term capital gains arising from transfer of equity shares, where transfer of shares is on or after 1 October 2004 and the transaction of sale is chargeable to Securities Transaction Tax ('STT')[8].

Vide Finance Act 2017, a proviso was inserted to provide that the aforesaid exemption would not be available if the transaction of acquisition of such equity shares is entered into on or after 1 October 2004, and such acquisition is not chargeable to STT.

However, to protect the exemption for genuine cases (where STT could not have been paid), it was proposed to notify list of transactions for which the condition of chargeability to STT on acquisition shall not be applicable.

The CBDT has released the notification[9] which would come into force and shall accordingly apply to Financial year 2017-18 onwards. The notification notifies all the transactions of acquisition of equity shares entered into on or after 1 October 2004, which are not chargeable to STT, other than the following;

① Acquisition of listed equity share through a preferential allotment in a company whose equity shares are not frequently traded in stock exchange.

② Acquisition of listed equity shares not through a recognized stock exchange with certain exceptions.

③ Acquisition of equity shares of a company during the period of its delisting.

Note: The summary is high level and therefore, please refer to the notification / contact us for more details.

5. Every outstanding "receivables" does not constitute an international transaction.

Delhi High Court recently pronounced an important ruling[10] on the treatment of outstanding receivables as international transaction for Indian transfer pricing regulations perspective.

The High Court held that every outstanding invoice beyond the credit free period cannot be classified as a separate international transaction for the purposes of the Indian transfer pricing regulations / domestic tax law. Further, once the taxpayer has factored in the impact of working capital requirement due to outstanding receivables in its pricing/profitability, no further adjustment on account of outstanding receivable is required.

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6 Notification No. S.O. 1789(E) dated 5th June, 2017

7 Section 10(38) of the Income-tax Act, 1961

8 STT is chargeable under Chapter VII of the Finance (No. 2) Act, 2004 for transactions generally entered on stock exchange

9 Notification No. S.O. 1789(E) dated 5th June, 2017

10 Pr. CIT vs Kusum Healthcare Pvt. Ltd. (I.T.A. No. 765/ 2016)

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