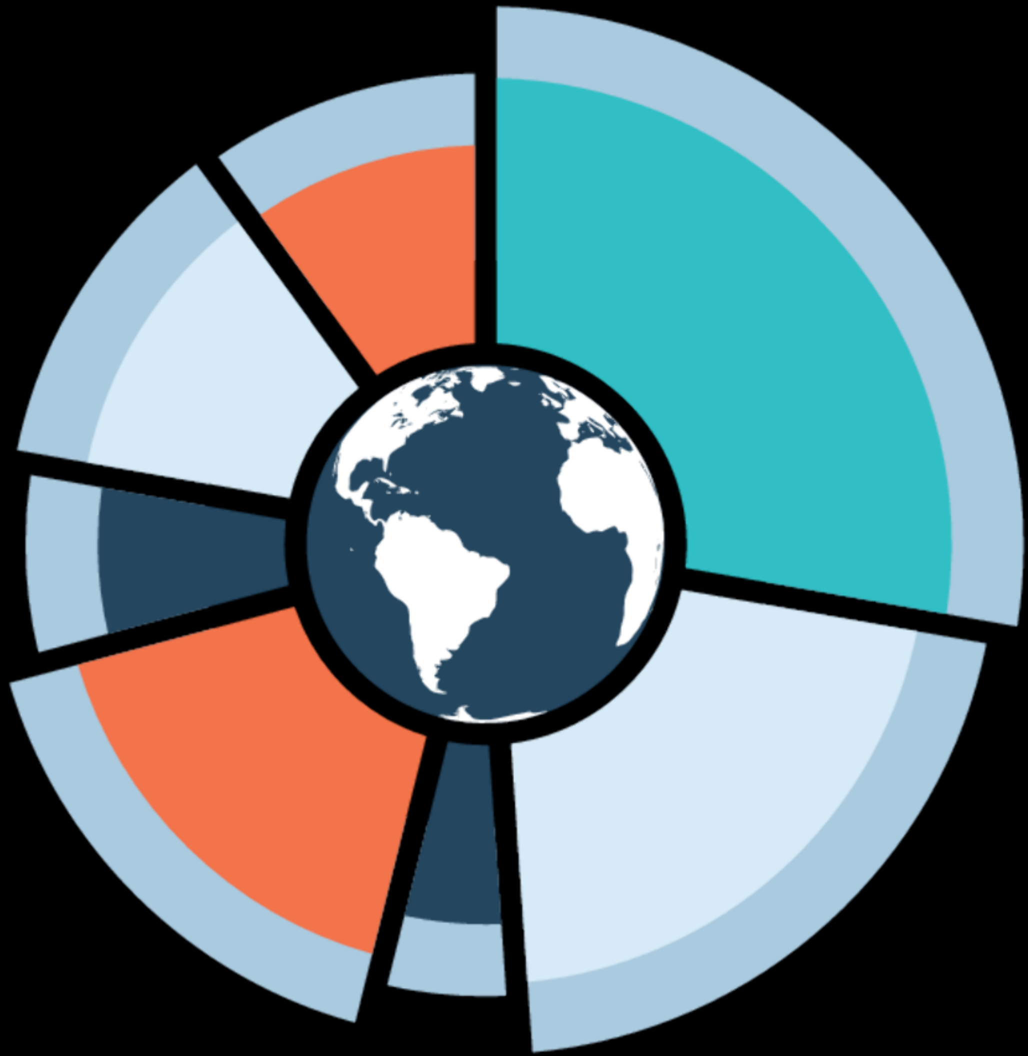


BEPS Action Plans - Future of International Tax Landscape

Rohan K Phatarphekar

8 April 2017

Contents

BEPS Action Plans - implementation status in India

BEPS Action Plans - implementation status in India

BEPS Action Plan	Implementation in India	Effective date
Action Plan 1: Digital economy	Equalisation levy introduced	1 June 2016
Action Plan 2: Hybrid mismatches	No amendment in Indian tax law	Not applicable
Action Plan 3: CFC Rules	Not implemented	Not applicable
Action Plan 4: Interest deductions	Limit on interest deduction	Financial year 2017-18
Action Plan 5: Harmful tax practices	Concessional tax regime for royalty on patents	Financial year 2016-17
Action Plan 6: Prevent treaty abuse	General anti-avoidance rule effective	Financial year 2017-18
Action Plan 7: Artificial Avoidance of PE	Indian tax treaties typically have wider definition of PE	-
Action Plans 8 – 10: Intangibles, Risks and capital & High risk transactions	Intangibles and others	Existing provisions
Action Plan 11: Data collection & analysis	Not implemented	Not applicable
Action Plan 12: Disclosure of aggressive tax planning	Not implemented	Not applicable
Action Plan 13: Transfer pricing documentation	Country-by-country reporting and Master file requirement introduced	Financial year 2016-17
Action Plan 14: Dispute resolution mechanism	Multilateral instrument is signed – to the extent agreed by the participating countries	-
Action Plan 15: Multilateral instrument	India is likely to sign the multilateral instrument	-

Action Plan 1

Digital Economy

Action Plan 1: Digital Economy

India - Equalization levy

- Tax on “specified services” (online advertising), introduced by India Finance Act, 2016
- Inspiration: BEPS Action Plan 1 choices

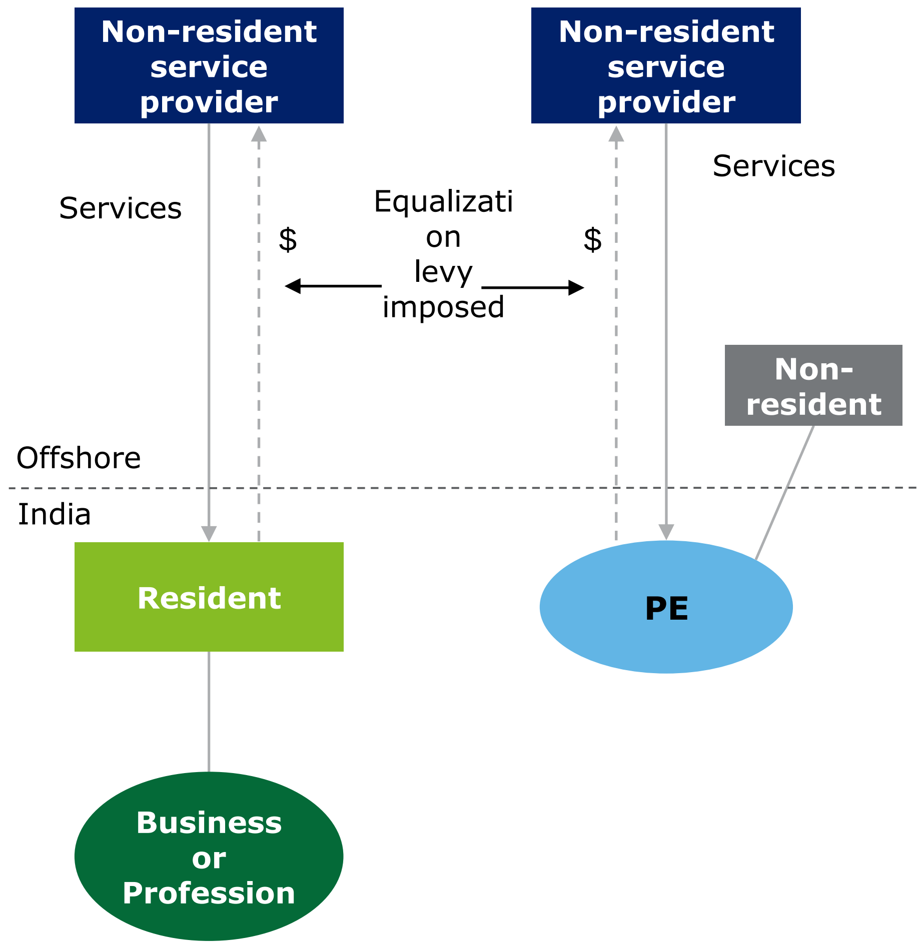
Nexus based on significant economic presence	Withholding tax	Equalization levy

- While not a recommendation, Action Plan 1 discusses characteristics and possible tax design of above options, **provided they respect existing treaty obligations**
- Countries typically have been introducing VAT on digital transactions

Indian jurisprudence on online advertising income - held to be neither royalties or fees for technical services, and not taxable in the absence of a PE in India

Action Plan 1: Digital Economy

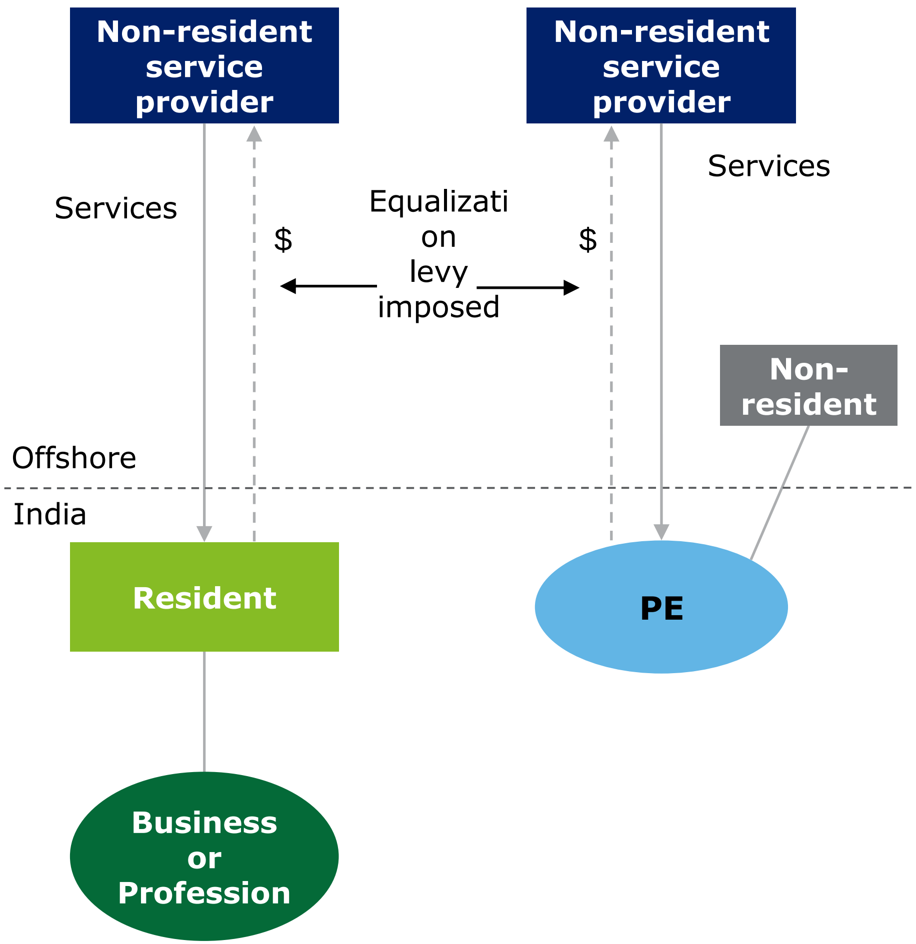
India - Equalization levy



- Levied on
  - Consideration received / receivable
  - **By** non-residents (not having PE in India)
  - **From** Indian tax residents or non-resident having PE in India
  - On account of rendering specified services
  - At 6% of the gross amount
- Specified services
  - Online advertisement, any provision for digital advertising space or any other facility or service for the purpose of online advertisement
  - Any others **to be notified…**
- Applicable with effect from 1 June 2016

Action Plan 1: Digital Economy

India - Equalization levy



- Introduced outside of the income tax law
  - As a separate Chapter to Finance Act
- Exceptions
  - Non–resident recipient has PE in India and specified service is effectively connected to such PE
  - Payment is not for the purpose of carrying out business or profession
  - Aggregate consideration does not exceed INR 100,000 (approx. USD 1,500) in any previous year (April – March)
- Consequences for non compliance
  - Interest, penalty, non deductibility
- Where deducted and paid, **no further tax liability in the hands of non-resident**

Action Plan 4

Interest deductions

Action Plan 4: Interest deductions

India – Limit on interest deduction

- Finance Act 2017 has introduced the limit interest deduction in certain cases – in line with recommendation of OECD BEPS Action Plan 4
- Deduction of interest expense/similar consideration paid/payable to its AE restricted to 30% of its EBITDA
- Coverage - Indian company/PE of a foreign company in India, paying interest/similar consideration on any debt issued by a non-resident AE
- Additional Coverage - Debt from third party's deemed to be debt from AEs where AEs provides an implicit or explicit guarantee to the third party lender
- Threshold - Restriction applicable where interest to the AE's exceeds INR 10 million
- Exemption - For companies engaged in the business of banking or insurance
- Carry forward - Disallowed interest expense carried forward upto 8 years

Action Plan 4: Interest deductions

India – Limit on interest deduction

Illustration

Particulars	Year 1	Year 2
EBITDA	2,000	3,000
Interest expenditure to AE	700	700
Maximum interest deduction allowable (30% of EBITDA)	600	900
Interest allowed in computation of income*	600	800 (700+100)
Interest disallowed & carried forward	100	-

Presuming interest is deductible in computation of income chargeable to tax under the head 'profits and gains of business and profession'

Action Plan 4: Interest deductions

Indian rules v. BEPS Action Plan 4

Indian rules	BEPS Action 4
Apply only to related party debt (or deemed related party debt)	Focuses on interest deductions *per se*
Deal with gross interest expense	Envisages disallowance of net interest expense
Disallowance of interest in excess of 30% of EBITDA	Range of 10-30% of EBITDA suggested
Appears that the disallowance would be with reference to EBITDA based on financial accounting	Envisages using the entity’s EBITDA based on tax numbers
Does not provide for a group ratio rule	Group ratio rule for relief to companies that are highly leveraged with third party debt for non-tax reasons
No transitional provisions or grandfathering of existing financing structures	Give reasonable time to restructure and/or provide for transitional rules

Action Plan 5

Harmful Tax Practices

Action Plan 5: Harmful Tax Practices

India has introduced a concessional tax regime for patents

Royalty income to be taxed at 10% (plus surcharge and cess) on gross basis

- Patent to be developed and registered in India
- Patentee to be true and first inventor and an Indian resident

Restrictive in nature

- Income from exploitation of patent outside India
- Does not cover IPR other than patents

Concessional tax regime vis-à-vis the "nexus approach" as per BEPS Action 5

- India's regime appears to be in line with the nexus approach – prohibitions on acquisition of IP and on outsourcing in place under the regime

POEM vis-à-vis BEPS

The three tier documentation (including the Master File and CbC Report) provides key information about the group's global operations to the tax authorities

- Organisational structure of the group
- Description of group’s business – **Important drivers of profit**
- Group’s intangible – **DEMPE function**
- Groups’ financial activities - Identification of entities in the group that provide a central financing function, **including the PoEM of such entities**
- Group’s financial and tax position
- Group’s income, taxes paid and activity for each subsidiary

Constituents of BEPS Master File / CbC

- Tax authorities would have visibility of operations and structure of the group
- Tax authorities can identify companies that could have PoEM in India, based on passive income in such companies
- IP structures would be visible through analysis of DEMPE function
- Highlight group companies enjoying high income with low ETR

Potential risk for PoEM

General anti-avoidance rule applicable from 1 April 2017

The Concept

- To deny tax benefit in an arrangement which:
  - Has been entered into with the main purpose to obtain tax benefit
  - Which lacks commercial substance
  - Creates rights and obligations which are not at arm's length principle
  - Results in misuse of tax law provisions or is carried out by means or in a manner which are not ordinarily employed for bona fide purposes
- Such an arrangement is termed as "impermissible avoidance agreement"
- As regards foreign investors, GAAR provisions would mainly impact those investors who claim treaty benefits to eliminate or minimise tax outgo in India

Application & exemption

- Under the current provisions, GAAR not applicable to:
  - Arrangements where tax benefit does not exceed INR 30 million
  - Investors in FPIs
  - FPIs if they do not claim treaty benefits
- Investments made prior to 1 April 2017 will be grandfathered

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- GAAR is akin to principal purposes test (PPT) envisaged under BEPS action 6 dealing with tax treaty abuse
- GAAR is very wide in nature and applies in a variety of situations, i.e. even when tax treaty benefit is not claimed

Action Plan 8-10

TP aspects of intangibles and others

Action Plan 8: TP aspects of intangibles

India Overview

BEPS Definition

"Something which is not a physical asset or a financial asset, and which is capable of being owned or controlled for use in commercial activities and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances."

Issues impacting India

- Research, development, and process improvement arrangements
- Development and enhancement of marketing intangibles
- Location specific advantages, local market features, workforce, etc. considered as intangibles by Indian tax authorities

Action Plan 8: TP aspects of intangibles

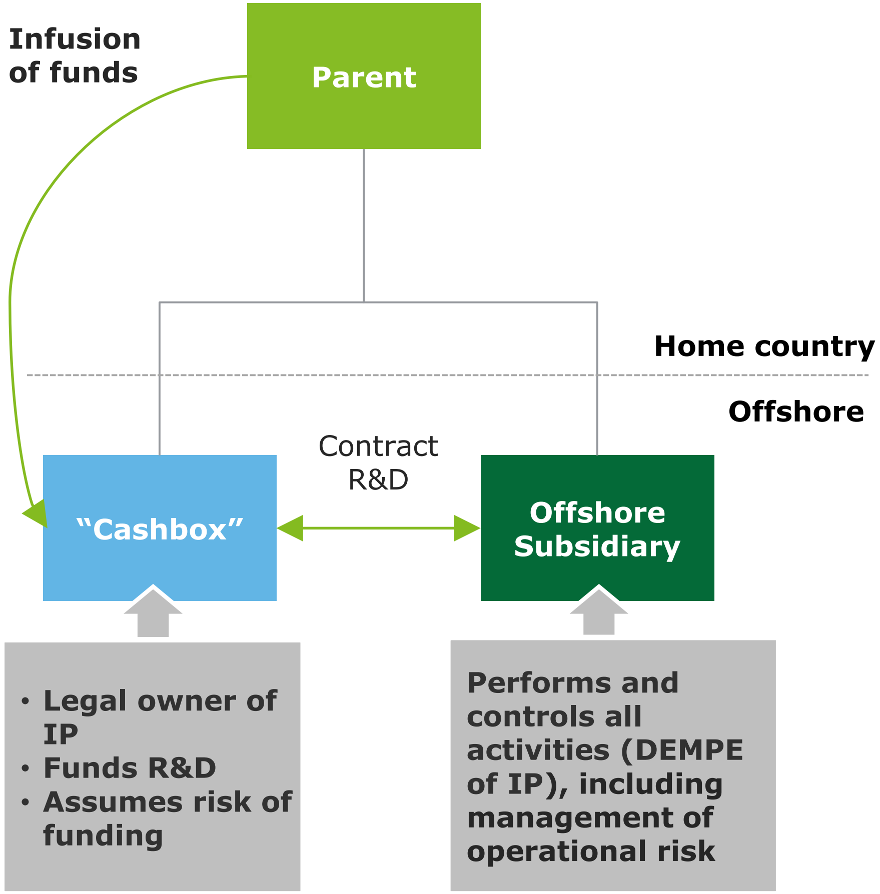
India Overview

Several aspects of the BEPS guidance are in line with view of the Indian tax authorities

BEPS	India- CBDT Circular No. 6/ 2013 ('Circular')
• Contracts are the starting point of the analysis, however, conduct of the parties are the ultimate determinants • Focus on functions, risks and costs • Fact specific analysis to be done while examining the DEMPE functions • The alignment of functional contributions and financial investment with legal rights • Direct exercise of **all important functions** and control over service providers performing outsourced activities	• Circular Classifies R&D centres of overseas MNEs into three broad categories based on functions, assets and risk assumed by the centre established in India • Guidelines laid down to identify the R&D centres as a contract R&D service provider assuming insignificant risk • Emphasis on the functions/conduct of parties rather than the contractual arrangement • Emphasis on nature and quantum of risk borne by R&D centres • Alignment of functional contributions and financial investment with legal rights recommended by circular as well.

Action Plan 8: TP aspects of intangibles

Funding and intangibles - Cashbox- India impact



BEPS

- Affirmation that capital-rich entities without relevant economic activities ("cash boxes") will not be entitled to any excess profits
- Three scenarios possible:
  - No management of funding risk: entitlement to no more than risk-free return
  - Management of funding risk: entitlement to risk adjusted return
  - Management of funding risk and operational risk: not a cash box!

India Impact

- Investment in India through "cash boxes" may trigger non cost- plus outcomes
- Indian offshore subsidiary performs and controls all DEMPE functions including risk management
- From the routine return currently received by Indian subsidiary, they would now be entitled to a significant allocation of profits
- Guidance akin to Circular No. 6/ 2013 issued to classify the contract Research and Development (R&D) centers of overseas multinationals enterprises (MNEs) and R&D centers bearing insignificant risks

Location savings

Divergent view - India perspective

OECD guidance

- Comparables provide the best evidence of location saving

India's historical perspective

- Mere comparability may not consider the benefit of location savings. Need to take into account the cost difference in the low cost country and in the high cost country from where the business activity was relocated

India's evolving perspective

- The revised India chapter of the proposed UN TP Manual states that compensation for location savings is in-built in the arm's length price determined based on availability of good local comparables

OECD guidance on workforce in place

- Not an intangible since work force cannot be owned or controlled by a single enterprise

India perspective on workforce in place

- Trained and organized work force is an intangible. Also included in the definition of intangible

Action Plan 13

Transfer pricing documentation

Action Plan 13 : Transfer pricing documentation

Documentation requirements introduced in India

Master file

- Finance Act 2017 has introduced the concept to maintain Master File
- Rules for maintaining and furnishing Master File are expected soon
- Penalty for non-furnishing of prescribed information and document is ₹ 500,000
- No threshold prescribed as yet, Master File requirements in India may ne independent of CbC reporting requirement

CbC Reporting

Requirements	Threshold	Timeline	Penalty
• Filing CbC report in India or notification of parent entity • Effective from Financial Year 2016-17	• MNE group having consolidated revenue exceeding € 750 million (in line with BEPS) • Threshold in Indian currency – to be computed based on exchange rate as on the last day of previous year. E.g. threshold for FY 2016-17 - ₹5395 crores	• CbC report to be filed in prescribed format on or before due date of filing return of income i.e. 30 November following the end of the Financial Year	Graded penalty structure from ₹ 5,000 to ₹ 50,000 per day for: • Non-furnishing of CbC report • Non- submission of required information Penalty of ₹ 500,000 for: • Furnishing of inaccurate particulars • Non-furnishing of master file data

Local file

- Existing local transfer pricing documentation requirements retained
- Possibility of further alignment with BEPS Action 13 resulting in additional disclosures

Action Plan 13: Transfer pricing documentation

Contents of Master File

Organizational Chart

- Legal and ownership structure and geographical location of operating entities.

Description of Company's Business

- Drivers of business profit
- Supply chain chart for the five largest products and service offerings plus other products or services amounting to more than 5% of MNE Group's sales
- Information regarding important service agreements
- FAR Analysis, describing principal contributing to value creation
- Business restructuring, acquisitions

Company's Intangible

- List of important of intangibles and agreements with AEs
- MNE Group's strategy for the development, ownership and exploitation of intangibles, including location of principal R&D facilities and location of R&D management.
- Transfer Pricing policy description of important transfers of interest in intangibles

Inter-Company Financial Instruments

- Details of financial arrangements of MNE group
- Information pertaining to central financing function undertaken for the group and the place of effective management of such entities

Financial & Tax Positions

- MNE Group's annual consolidated financial statement
- Information on unilateral APAs and other tax rulings relating to allocation of income among countries

Action Plan 13: Transfer pricing documentation

Contents of Country by Country report - Table 1, Table 2 and Table 3

Table 1: Information included in CbC

Revenues (related, unrelated, total)	Profit/loss before income tax
Income tax paid (cash)	Income tax accrued
Stated capital	Accumulated earnings
Number of employees	Tangible assets other than cash and cash equivalents

Table 2: Information included in CbC – for each tax jurisdiction

Tax Jurisdiction of organization or incorporation if different

Main business activity of each of the entity

Main business activity(ies)

- Research and development
- Holding or managing intellectual property
- Purchasing or procurement, Manufacturing or production
- Sales, marketing or distribution
- Provision of services to unrelated parties
- Internal financial services
- Holding shares or equity instruments, Dormant, Others

Table 3:
To include any further brief information or explanation that taxpayer may consider necessary or that would facilitate the understanding of the compulsory information provided in the CbC Report.

Action Plan 13: Transfer pricing documentation

Country by Country Model Templates

A model template for the Country-by-Country Report

Table 1. Overview of allocation of income, taxes and business activities by tax jurisdiction

Name of the MNE group: Fiscal year concerned:										
Tax Jurisdiction	Revenues			Profit (Loss) Before Income Tax	Income Tax Paid (on cash basis)	Income Tax Accrued – Current Year	Stated capital	Accumulated earnings	Number of Employees	Tangible Assets other than Cash and Cash Equivalents
	Unrelated Party	Related Party	Total							

GUIDANCE ON TRANSFER PRICING DOCUMENTATION AND COUNTRY-BY-COUNTRY REPORTING © OECD 2014

Table 2. List of all the Constituent Entities of the MNE group included in each aggregation per tax jurisdiction

Name of the MNE group: Fiscal year concerned:																
Tax Jurisdiction	Constituent Entities resident in the Tax Jurisdiction	Tax Jurisdiction of organisation or incorporation if different from Tax Jurisdiction of Residence	Main business activity(ies)													
			Research and Development	Holding or Managing intellectual property	Purchasing or Procurement	Manufacturing or Production	Sales, Marketing or Distribution	Administrative, Management or Support Services	Provision of Services to unrelated parties	Internal Group Finance	Regulated Financial Services	Insurance	Holding shares or other equity instruments	Dormant	Other[2]
	1.														
	2.														
	3.														
	1.														
	2.														
	3.														

[2] Please specify the nature of the activity of the Constituent Entity in the "Additional Information" section.

Table 3. Additional Information

Name of the MNE group: Fiscal year concerned:
Please include any further brief information or explanation you consider necessary or that would facilitate the understanding of the compulsory information provided in the country-by-country report.

Action Plan 13: Transfer pricing documentation

Indian rules vs. OECD documentation requirements

Indian rules (i.e. Rule 10 (D))	**OECD documentation requirements**
Ownership structure	Requirements of Master File
Profile of MNE group	Requirements of Master File
Description of business and industry	Requirements of Master File
Details of international transaction	Requirements of Local File
Functional, asset and risk analysis	Requirements of Local File
Financial estimates	Requirements of Local File
Uncontrolled transactions	Requirements of Local File
Comparability of uncontrolled transactions with relevant transaction	Requirements of Local File
Arms length price	Requirements of Local File
Not specified under existing Rule 10D requirement	Requirements of Local File: • Local management and organization chart • Copy of existing APAs and other tax rulings which are related to the controlled transactions (but don’t involve the local entity)

Actions Plan 13: Transfer pricing documentation

Global perspective - CbC reporting implementation

Final CbC legislations enacted

Countries following OECD recommendations*

- Ireland
- Poland
- France
- Denmark
- Netherlands
- Italy
- UK
- Portugal
- India
- Spain
- New Zealand
- Canada
- Norway
- China
- Austria
- Belgium
- Brazil
- Cyprus
- Finland
- Germany
- Indonesia
- Luxembourg

Countries deviating on threshold/ differing applicable date

- Australia – Threshold AUD 1 billion (EUR 680 million approx.)
- Japan – Threshold JPY 100 billion (EUR 825 million approx.)
- US - Applicable from 1 July 2016, voluntary filing allowed for prior year
- Malaysia – Applicable from 1 January 2017
- Singapore - Applicable from 1 January 2017
- South Africa – Threshold of ZAR 10 billion (EUR 650 million approx.)

* Threshold of EUR 750 million and CbC filing for Fiscal year beginning on or after 1 January 2016

Actions Plan 13: Transfer pricing documentation

Global perspective – Master File implementation – Final rules

Country	First year applicability	OECD MF required	Threshold
Australia	1 Jan 2016	Yes	Global AUD 1 billion turnover (EUR 685 million approx.)
Austria	1 Jan 2016	Yes	EUR 50 million turnover is exceeded for two consecutive fiscal years
Belgium	1 Jan 2016	Yes	Staggered threshold – 3 levels
China	1 Jan 2016	Yes	Related party transactions over CNY 1 billion (EUR 137 million approx.) or if foreign headquartered has prepared a Master File
Denmark	1 Jan 2017	Yes	No threshold – to be prepared by all taxpayers
Finland	1 Jan 2017	Yes	Staggered threshold – 3 levels
France	Already required	No, Existing rules	More than EUR 400 million of gross annual turnover or gross assets
Germany	1 Jan 2017	Yes	Revenues in the previous fiscal year exceeded EUR 100 million
Greece	Already required	No, Existing rules	Annual IG transactions exceed 100k for small companies and 200k for large companies
Indonesia	1 Jan 2016	Yes	Staggered threshold – 4 levels
Italy	Already required	No, Existing rules	Not mentioned
Japan	1 April 2016	Yes	¥100 billion turnover (EUR 815 million approx.)
Korea	1 Jan 2016	Yes	Annual sales revenue of KRW 100 billion (EUR 80 million approx.) or more and intercompany transactions of KRW 50 billion or more
Mexico	1 Jan 2016	Yes	686,252,580 Mexican pesos turnover (EUR 31 million approx.)
Netherlands	1 Jan 2016	Yes	EUR 50 million turnover
Peru	1 Jan 2017	Yes	PEN 81 million revenue (EUR 23 million approx.)
Poland	1 Jan 2017	Yes	Revenue or costs - EUR 20,000,000 in the year preceding the tax year
South Africa	1 Oct 2016	Yes	ZAR 100 million (EUR 7 million approx.)
Spain	1 Jan 2016	Yes	EUR 45 million of revenues

Action Plan 13 : Transfer pricing documentation

List of signatories to the Multilateral Competent Authority Agreement (MCAA)

57 countries **including India** are signatories to the MCAA on exchange of CBC reports as on January 2017

S. No.	Country	S. No.	Country	S. No.	Country	S. No.	Country
1	Argentina	16	France	31	Jersey	46	Poland
2	Australia	17	Gabon	32	Korea	47	Portugal
3	Austria	18	Georgia	33	Latvia	48	Russian Federation
4	Belgium	19	Germany	34	Liechtenstein	49	Senegal
5	Bermuda	20	Greece	35	Lithuania	50	Slovak Republic
6	Brazil	21	Guernsey	36	Luxembourg	51	Slovenia
7	Canada	22	Hungary	37	Malaysia	52	South Africa
8	Chile	23	Iceland	38	Malta	53	Spain
9	Costa Rica	24	**India**	39	Mauritius	54	Sweden
10	Curacao	25	Indonesia	40	Mexico	55	Switzerland
11	Cyprus	26	Ireland	41	Netherlands	56	United Kingdom
12	Czech Republic	27	Isle of Man	42	New Zealand	57	Uruguay
13	Denmark	28	Israel	43	Nigeria		
14	Estonia	29	Italy	44	Norway		
15	Finland	30	Japan	45	Peoples Republic of China		

Action 14

Dispute Resolution Mechanism

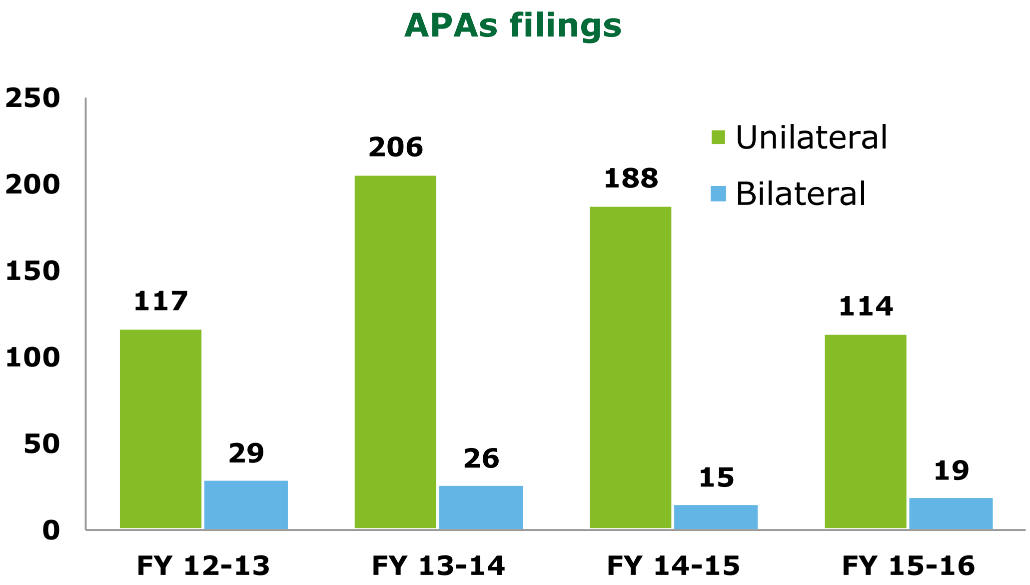
Action 14: Dispute Resolution Mechanism

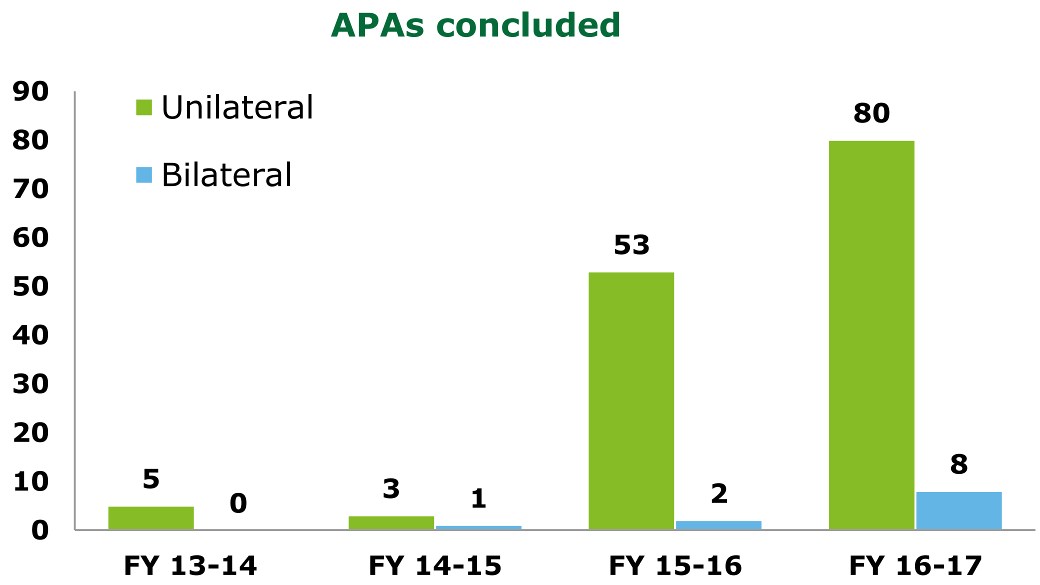
- **All OECD and G20 countries have agreed on a minimum standard regarding MAP**
- **Minimum standard contains 17 commitments, including:**
  - Commitment to seek to resolve MAP cases within an average of 24 months
  - Provide timely and complete reports of MAP statistics
  - Commitment to have their compliance with the minimum standard reviewed by their peers
  - Commitment to not use performance indicators for their competent authority functions and staff in charge of MAP processes based on the amount of sustained audit adjustments or maintaining tax revenue
  - **20 countries have agreed to adopt mandatory binding MAP arbitration**
  - **India has expressed that it is unlikely to accept the mandatory binding MAP arbitration**

India MAP Resolutions Update

- Indian competent authority (CA) team been resolving MAP cases at a brisk pace over last two years
- Indian Government signed framework agreement with the US in January 2015 to resolve transfer pricing disputes between the two countries, with a focus on IT and ITeS segments - more than 100 cases recently resolved
- The two CAs have also recently resolved more than 60 cases which are not covered under the framework agreement.
- The relationship between the Indian CA and the US CA has been strengthen over the last year
- Overall, the Indian Government has resolved more 250 MAP cases till date covering both TP and non TP cases with various countries. MAP negotiations have primarily been with US, UK, China and Japan
- The total income amount locked up in these disputes was upwards of US$ 1.5 billion (Rs.10,000 crore).

India APA update





- Total 714 APA applications filed in the last 4 rounds of filings – 625 unilateral and 89 bilateral
- Significant litigations and lack of effective dispute resolution mechanism lead to a phenomenal response to the Indian APA scheme
- Rollback option heightened the interest in the APA scheme. It provided 9 years of tax certainty – 5 advance years and 4 roll back years
- Judicial authorities – High courts and Tax Tribunal, off late, have placed reliance on the APA results even for the years beyond the APA period

- 152 applications – 141 unilateral and 11 bilateral, concluded so far during the 4 years. Current year has so far more signings than last year
- Pace in the first 2 years was slow and that could be due to meeting the procedural requirements, developing a general understanding on the likely arm's length margin, and more important, bridging of the trust-gap
- The signing of 88 APAs in a single year (F.Y 2016-17) is a significant achievement. The progress of the APA Scheme strengthens the Government's resolve of fostering a non-adversarial tax regime

Action Plan 15

Multilateral Instrument

Action Plan 15 – Multilateral Instrument
Draft of the instrument released on 24 November 2016

- Action 15 culminating the BEPS project
- Not to function as a protocol, but instead will be applied alongside existing tax treaties so as to modify their application
- Consists of seven parts
  - Scope and interpretation of terms
  - Hybrid mismatches
  - Treaty abuse
  - Avoidance of PE status
  - Improving dispute resolution
  - Arbitration
  - Final provisions
- Target signing date by key countries at G20 meeting in June-July 2017
- Ratification procedures would need to follow – so may be in effect from late 2017 or in 2018

Action Plan 15 – Multilateral Instrument

Approach taken

Agreed to a minimum level standard for implementation

- Action 6 – Treaty abuse
- Action 14 – Dispute resolution

High level of flexibility still available to member states

- Covered tax agreements
- Minimum standard alternates
- Opt out for all or part provisions for covered tax agreements

Action Plan 15 – Multilateral Instrument

General structure of main operative provisions

- **Substantive rule**
  - BEPS compliant rule (e.g., Principal Purpose Test (PPT) and optional Limitation on Benefits (LOB) for treaty abuse, revisions to PE definition)
- **Compatibility clause**
  - Resolves conflicts between substantive rules that overlap with existing treaty rules
- **Reservations**
  - Opt outs from substantive rules, where permitted
- **Notifications**
  - Of opt ins, where substantive rules permit a choice among alternatives
  - Of existing treaty rules that are superseded or modified by substantive rules as a result of the compatibility clause

Action Plan 15 – Multilateral Instrument

Next steps

- Key issues for governments
  - Sign?
  - Decide which treaties to cover
  - Determine positions on options and reservations, make notifications, and determine position regarding binding arbitration
  - Domestic law ratification processes
- OECD to act as Depositary
- Planned signing from June/July 2017
- Is the MLC a one-shot BEPS fix or a permanent part of the international tax landscape?

Questions & Answers