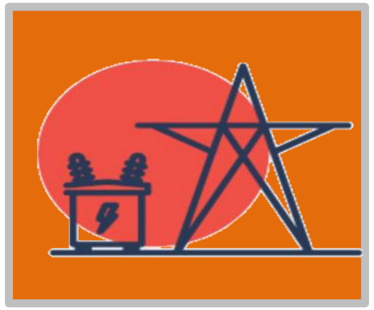
EPC and Manufacturing Sector

16 July 2023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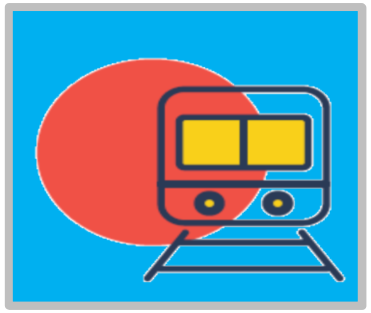
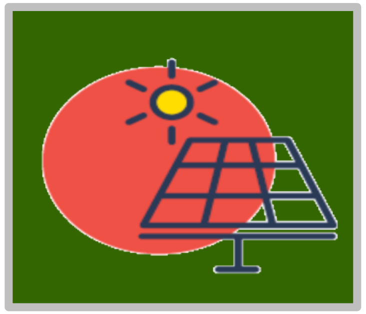

Railways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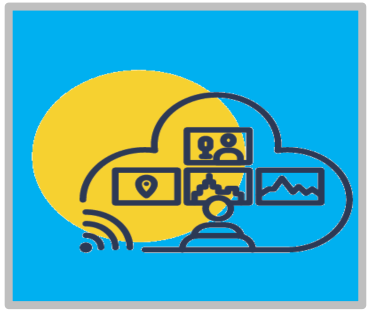
Civil


Smart Infra


Cables

Indian EPC Industry and its contribution to the economy

Highways

Railways

Airport & Port

Power

Telecom

Indian EPC Industry – The backbone for India's growth story and employment generation

- The government has given a massive push to the infrastructure sector by allocating Rs. 10 lakh crore (US$ 130.57 billion) to enhance the infrastructure sector.
- The government allocated Rs. 134,015 crore (US$ 17.24 billion) to National Highways Authority of India (NHAI).
- Enhance infrastructure spending to reach its 2025 economic growth target of US$ 5 trillion.
- Continuing transmission line and capacity addition has helped in increase of Renewable Energy.
- Huge transmission capacity has facilitated seamless transfer of power from power surplus regions/areas to power deficit regions/areas and thus optimizing the use of generation resources.
- Under the National Infrastructure Pipeline (NIP), projects worth Rs. 108 trillion (US$ 1.3 trillion) are currently at different stages of implementation

Points to Ponder – Taxation Related issues

General

- Digital Transformation in Tax Administration

Direct Tax

- Faceless tax assessments and Appeals
- EPC Contract Structuring and taxation issues on supply
- Foreign tax credits
- Mergers and Amalgamations
- Payments for Commission , FTS , Royalty – Form 10F Foreign tax payments

Indirect Tax and GST

- Inverted duty structure and substantial GST credit accumulations
- GST credit – 3B V/s 2A
- GST on advances and GST TDS on Govt contracts.

Digital Transformation in Tax Administration

Direct Taxes

- Almost all processes shifted in faceless mode
- Compliance management and Centralised Processing centre (CPC)
- Analyse pattern and inconsistencies between declared income and expenditure
- Cross verification of data- Books Vs GST reporting Vs 26AS etc.
- Enhances reporting requirements in tax audits (Cl 17 /34 / 44)
- Sharing of information between multiple regulators , MCA, RBI, GSTN,
- Regular surveys / search , information calling u/s 133(6).

Indirect Taxes

- Massive data analytics through GSTN
- Separate section for data analyses – DGARM
- Tracking of the movement of goods through toll booths
- Geo-tagging of the premises of registration
- Identification of the vendors defaulting in GST and fake purchases / sales. (Fake invoices having GST of ~63K Crs identified till date)
- Expanding tax base through lower limits for e-invoicing (5 crs w.e.f 1st Aug 2023).
- Aggressive tax inspections and investigations and recoveries
- Use of arrest powers

Direct Tax - Faceless assessments and Appeals

- Healthy, as no biases, personal gratifications, and cases being decided on merits.
- Literally no disposal of appeals in last couple of years since faceless appeal notified.
- Challenges in explaining the mass data and facts in faceless assessments.
- High pitched assessments due to lack of understanding of business and commercial facts patterns.
- Inadequate time provided for submissions and documents / evidences
- Huge challenges at CPC level - Compliance management and Centralised Processing centre (CPC) – Unreasonable and wrong demands , credits of TDS and advance taxes being denied without any reasons , past demands not corrected in system, AOs are helpless as all powers rests with CPC, no two-way communication process.
- Personal virtual hearings being granted but not very effective.
- Assessee need to be well prepared, data accessibility and needs for use of technologies.
- Keep all reconciliations , factual data, technical submissions of recurring issues ready.

EPC Contract Structuring

Key Attributes : Offshore and onshore Engineering, Supply and services/construction

Split Contract V/s Composite Contracts – Commercial as well as tax considerations

Allocation of contract value - Cash flow, repatriation , FC risks, transfer price

EPC Contract Structuring – Key Tax issues

- Projects under SPV's – Project conditions , Prequalification's (PQ's) , JV partner's choice
- Legal Structure – LLP v/s company V/s AOP. – Winding up perspective
- Consortium arrangements and AOP exposure.
- Higher tax rates at AOP level – 35.88% (30% + SC @ 15%+ Cess) Vs 25.17% for corporates.
- Restrictions on payments to AOP partners. { Sec 40 (ba) }
- In case of losses no tax setoff for AOP members.
- Active v/s passive partner
- Tax credits for foreign partner in the home country – may not be available
- Taxability of supplies – Issues both for domestic and offshore projects.
- Taxation issues in case of back-to-back contracts to JV partners – GAAR , TDS and GST
- Tax overreach and disregard of tax treaties by some countries.

Foreign Tax Credits – Offshore projects by Indian EPC companies

- FTC allowed as per Section 90/91 / Rule 128 and applicable tax treaties.
- Credits of taxes withheld as per the domestic laws irrespective of treaty provisions – Whether credits can be claimed in India.
- Tax credit issues in case the due date of filing and payment falls after 30th November due date in India. Revised return timelines also curtailed in India to 31st December.
- Tax Credits availability of BPRT.
- Few countries (Bangladesh , Nepal etc) have WHT on total revenue which are treated as final tax without any refunds (AIT)
- Tax credits of the liabilities in foreign jurisdiction in assessments / appeals.
- Allowability of expenses of unutilised FTC - Reliance infrastructure Limited v. Jt CIT (76 taxmann.com 257).

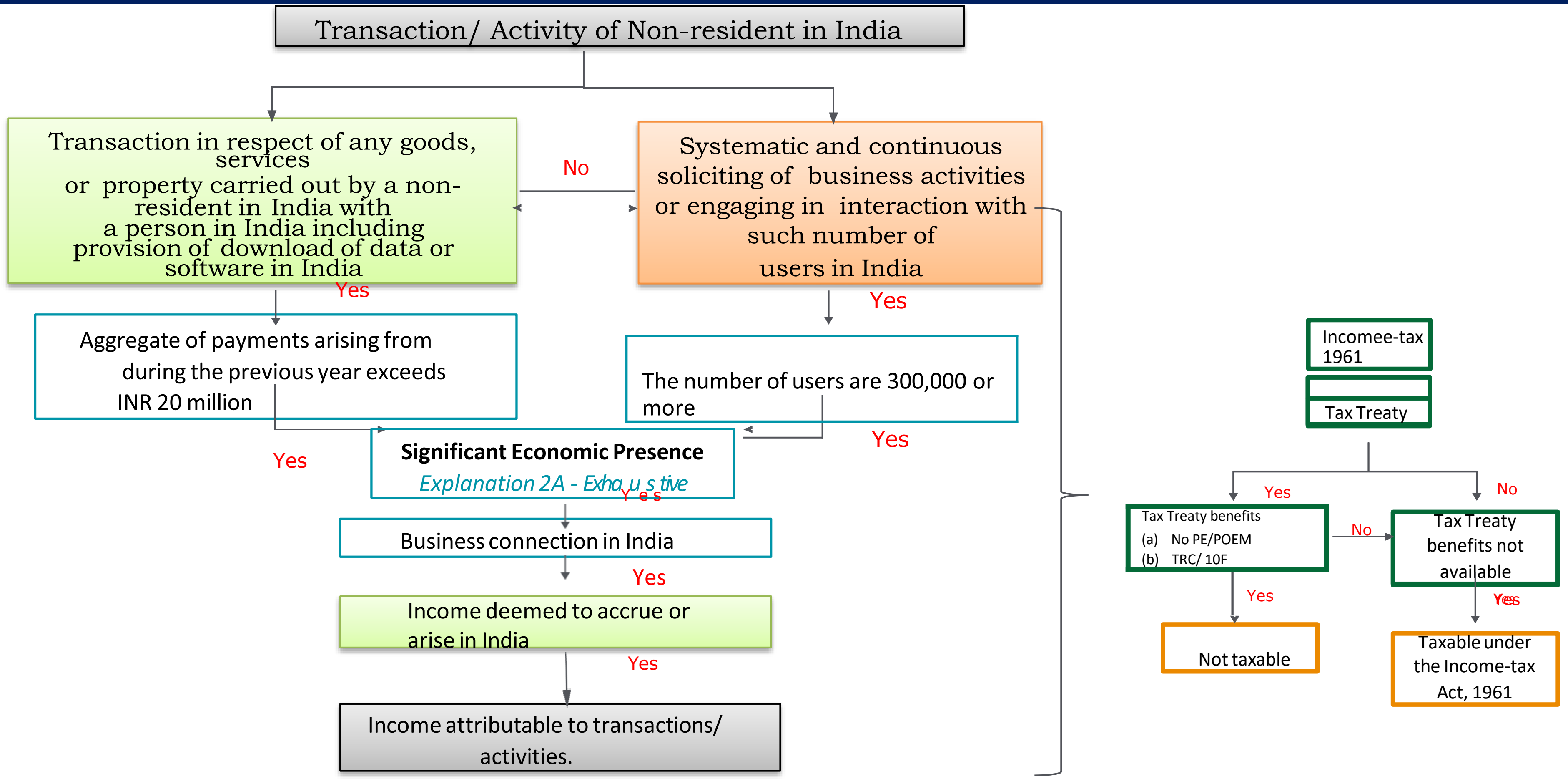
Merger and Amalgamations

- Provisions of section 72A of the Income tax Act permit carry forward of loss and accumulated depreciation in case of amalgamation only to certain specific types of companies such as those owning an industrial undertaking, banking companies, etc. (EPC not covered)

- With the advent of globalization and liberalization resulting in the influx of foreign entities into India, the increasing competition has resulted in a pressing need for small companies in the service and to consolidate their resources to survive.

- There are safeguards to ensure continuity of business in case of manufacturing sector in terms of achieving production of 50% of installed capacity and maintenance of 75% of assets post-merger. Such safeguards may not be feasible for service Sector but other safeguards like continuity of headcount (number of employees) can be considered.

Significant Economic Presence – Explanation 2A of Section 9(1)(i)



- Until March 2021, foreign persons taxed – through physical presence / activities carried on in India.
- Effective April 2021 - Indian Government introduced nexus-based taxes 'Equalization levy' and 'Significant economic presence'.
- SEP not restricted to only digital companies or digital transactions but applies to all goods and services transactions e.g. imports, professions / legal / support services.
- Income attribution Rules are vague – no clarity on how much income to be taxed based on the nexus. (Rule 10 needs amendment)

International Taxation –Revised documentation for foreign remittance – Form 10F

Current process

- Co. being a remitter needs to submit Form 15CA and Form 15CB (CA certificate) to the authorised remittance banks. Various details / documents like invoices, agreements, Tax Residency Certificate ('TRC'), manual Form 10F and client declaration are collected from non-resident service providers to avail relevant Tax treaty benefits.

- The Directorate of Income Tax (Systems) has issued Notification No. 03/2022 dated 16th July 2022 mandating electronic furnishing of Form 10F by non-resident service providers. A relaxation is granted till September 30 2023, if service providers don't have a Permanent Account Number ('PAN') and are not required to have a PAN in India.

Vendors

Foreign remittances not availing treaty benefits

– Amendment not applicable

Foreign remittances availing treaty benefit

Documents Submitted under existing law

- TRC (Tax Residency Certificate)
- No PE (covering MLI aspects as well)
- Manual Form 10F

Changes as per Circular
Electronic filing of Form 10F

Vendor to obtain PAN for electronic filing

- Above changes could entail additional compliance burden to non-resident service providers.
- If PAN not obtained, 20% withholding tax applicable for FTS and for business income, due to SEP provisions tax @40% applicable.
- If vendors don't discharge tax obligations, then ICO , being the payer may be called upon as 'representative agent' to discharge.

Business impact areas

Impact on:

- Foreign remittances exceeding the thresholds of SEP – to be analyzed whether taxable or not.
- 'Import of goods' above the thresholds – Now to be analyzed for SEP provisions and buyer to withhold taxes.
- To avail Tax Treaty benefits – now non-resident's PAN mandated for online filing of Form 10F.
- Enhanced tax risks being the payer – failure for vendor to provide adequate documents – due to commercial grossing up arrangement.
- Enhanced Tax scrutiny being the payer – Risk of regarded as 'representative assessee'.

GST related issues for EPC Industry – Inverted Duty Structure

- The applicable GST rates (up to July 22) on Railways and Govt Contracts – 12% while inputs rate was mostly 18% and Cement still taxed @ 28 % - resulting into huge accumulations of GST credits for most of the EPC players.

- State level GST balances – No facility for transfer of credits within states. One state may have input deficit v/s excess credits in other states. – causing huge cash flow issue.

- Refunds of inverted duty was allowed on goods portion, now the part refunds on services also allowed – No clarity on the past refunds already sanctioned considering only goods input credits.

- In case of SPV's – Excess input credits shall become a permanent cost without any recourse.

GST on Advances and GST TDS

- GST is payable on advances received against service portion. – Cash flow issues if the govt clients do not agree to pay.
- Though the taxes on advances are collected credit not available to recipients – Timing issue.
- 2% GST TDS applicable on payment from Govt clients.
- Huge reconciliation issues of GST TDS as returns do not provide invoice wise data. Commons working for same client on multiple project further aggravate the problem.

THANK YOU

Global Footprint in
100 countries*

*Includes EPC and Supply