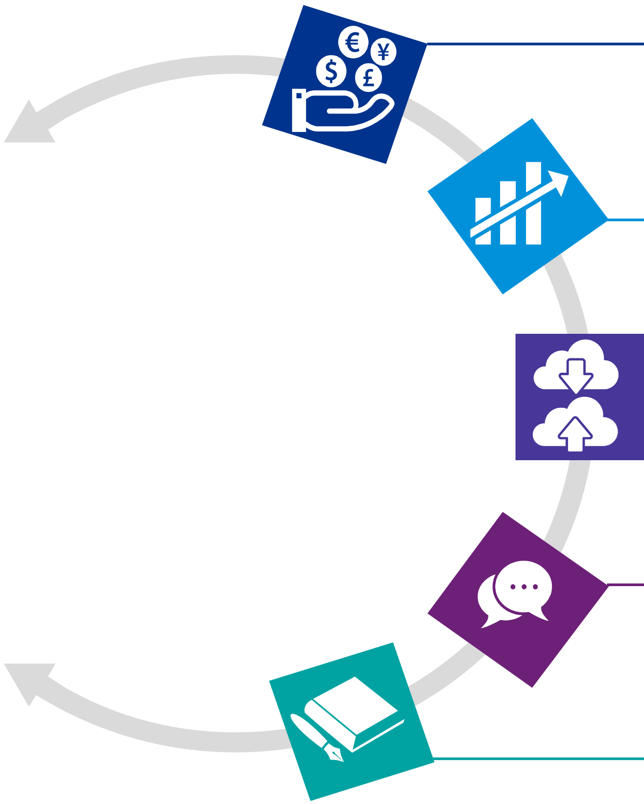
Digital Economy - OECD & MLI perspective

1 September 2018

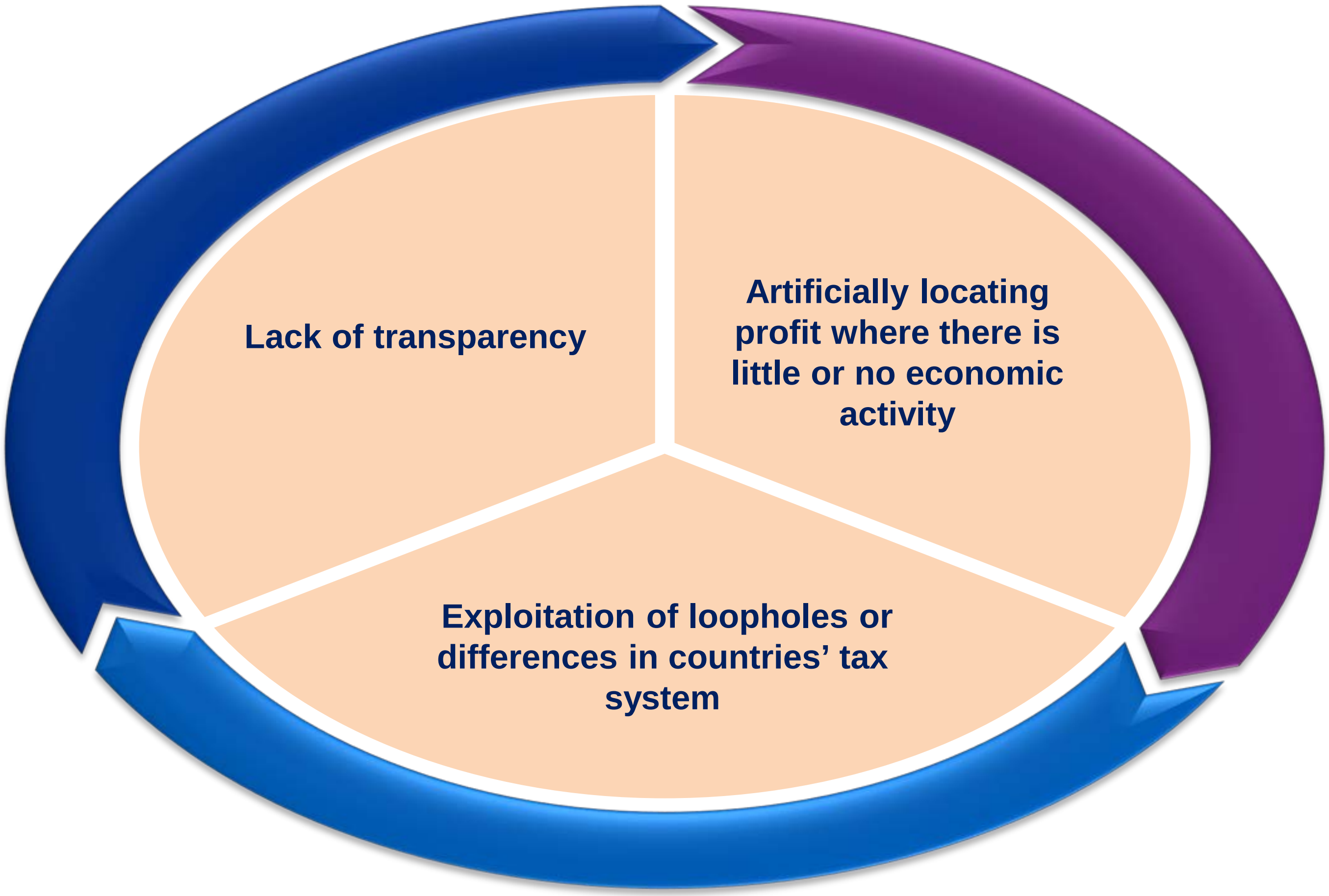
Delving into the nitty-gritty…



- BEPS Initiative
- Objective of actions plans - 3 main pillars
- Digital Economy – challenges, measures
- Case studies
- MLI - An overview

BEPS initiative

15 Action Plans Designed to stop countries and companies from competing on the basis of:



Prevent double non-taxation

Objective of actions plans - three main pillars

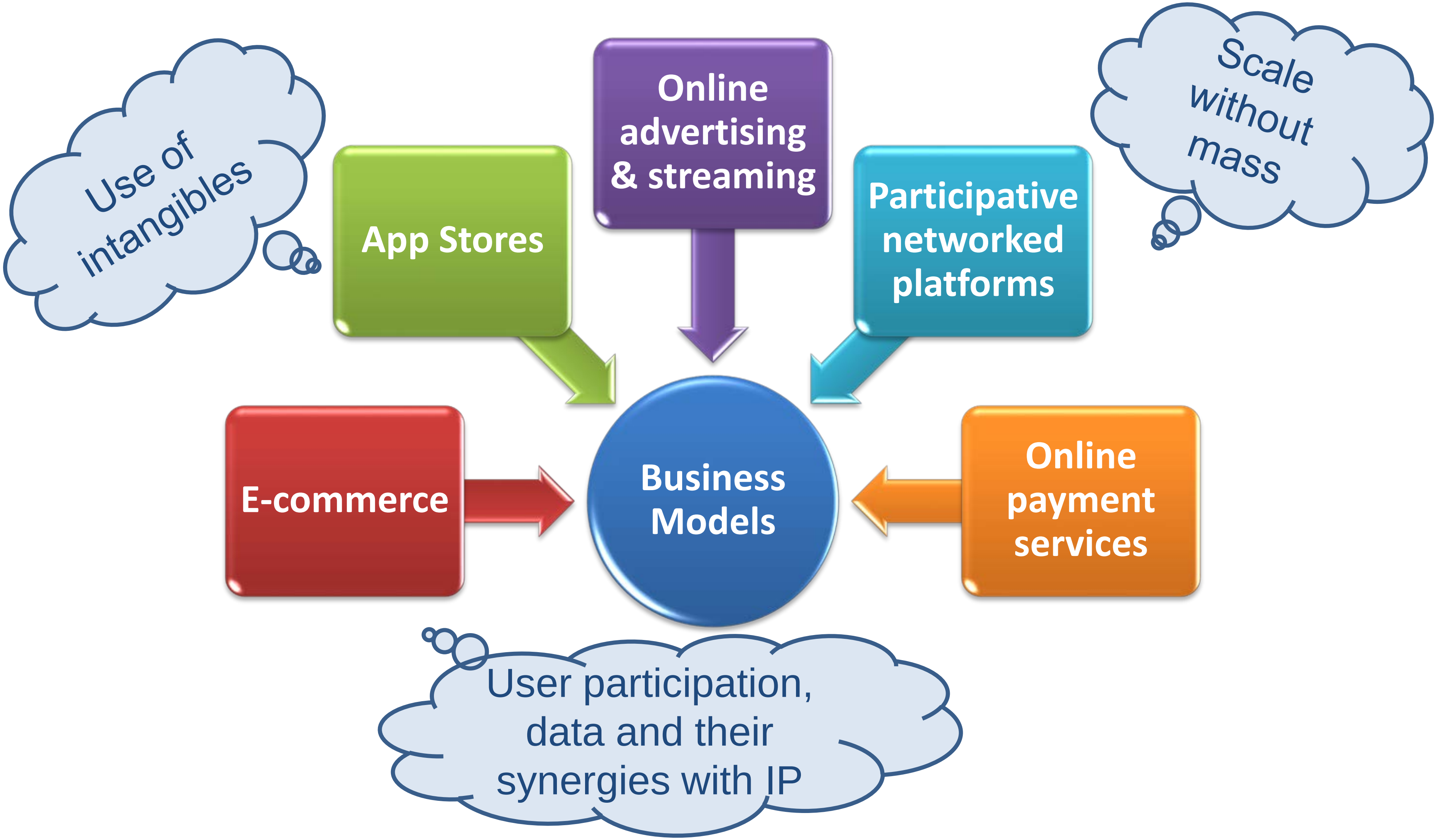
Coherence	Substance	Transparency and Certainty
Hybrid Mismatch Arrangements (2)	Preventing Tax Treaty Abuse (6)	Measuring BEPS (11)
CFC Rules (3)	Avoidance of PE Status (7)	Disclosure Rules (12)
Interest Deductions (4)	TP Aspects of Intangibles (8)	TP Documentation (13)
Harmful Tax Practices (5)	TP/Risk and Capital (9)	Dispute Resolution (14)
	TP/High Risk Transactions (10)	

Digital Economy (1)

Multilateral Instrument (15)

Digital economy

Digital economy



Digital economy

Shifting of IP to low tax jurisdictions

Failure of application of traditional concept of PE under tax treaties which relies on physical presence

Artificial avoidance of taxable presence by

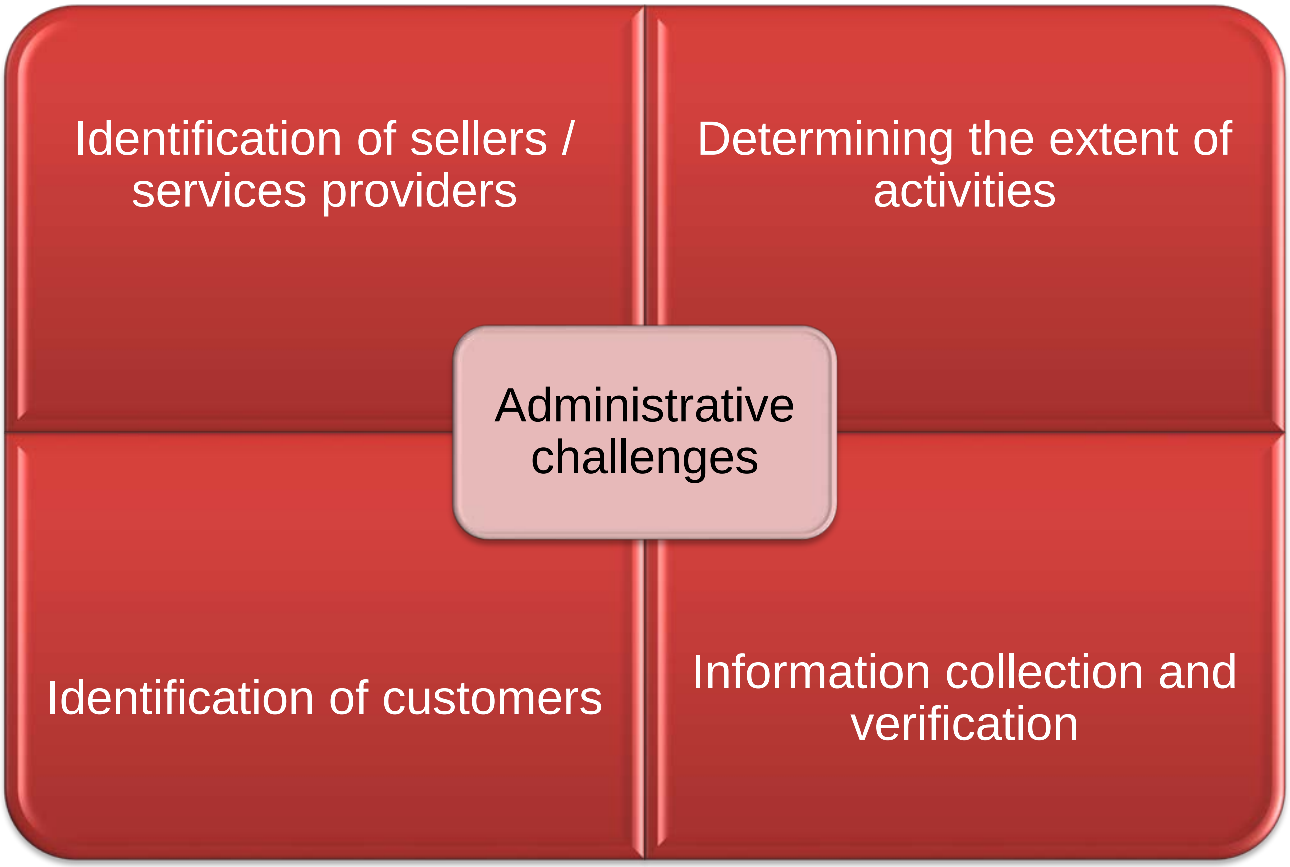
Policy challenges in Digital Economy

Nexus

Data

Characterization

Challenges raised by Digital Economy



BEPS AP 1 - Addressing Tax Challenges of Digital Economy

First report on Action Plan 1	-	Released in October 2015
Interim report on Action Plan 1	-	Released in March 2018
Final report on Action Plan 1	-	To be released in 2020

- *Identified opportunities for tax planning in the digital economy and*
- *Analyzed best measures for tacking BEPS in the digital economy*

Options identified to tackle direct tax issued raised by Digitalization

- **Nexus based on the concept of significant economic presence**
- **Withholding Tax on digital transactions**
- **Introduction of Equalisation levy**

BEPS AP 1 - Addressing Tax Challenges of Digital Economy

AP 3: Designing effective CFC Rules

AP 5: Measures related to harmful tax practices

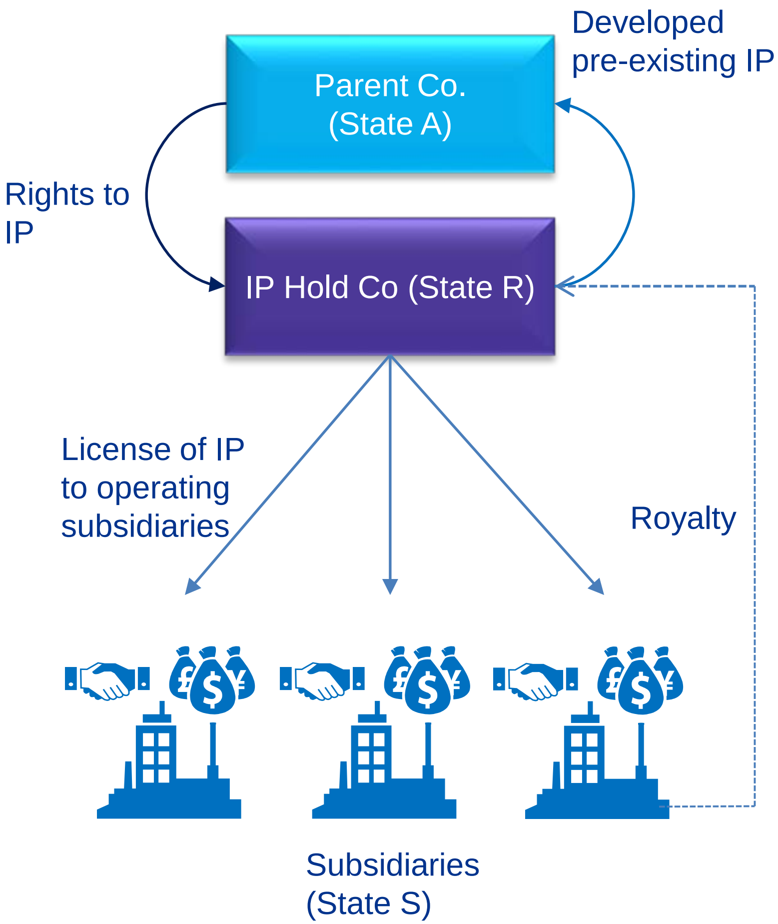
AP 6: New standards on Treaty Abuse – change in the preamble, PPT

AP 7: Changes to definition of PE
Specific activity exemption limited to preparatory & auxiliary services
DAPE even if involved in activities leading to conclusion of contract

AP 8 to 10: designing effective TP rules for rewarding entities contributing to the development, maintenance, production and exploitation of intangibles

Case studies

Case Study 1 - Cash Box



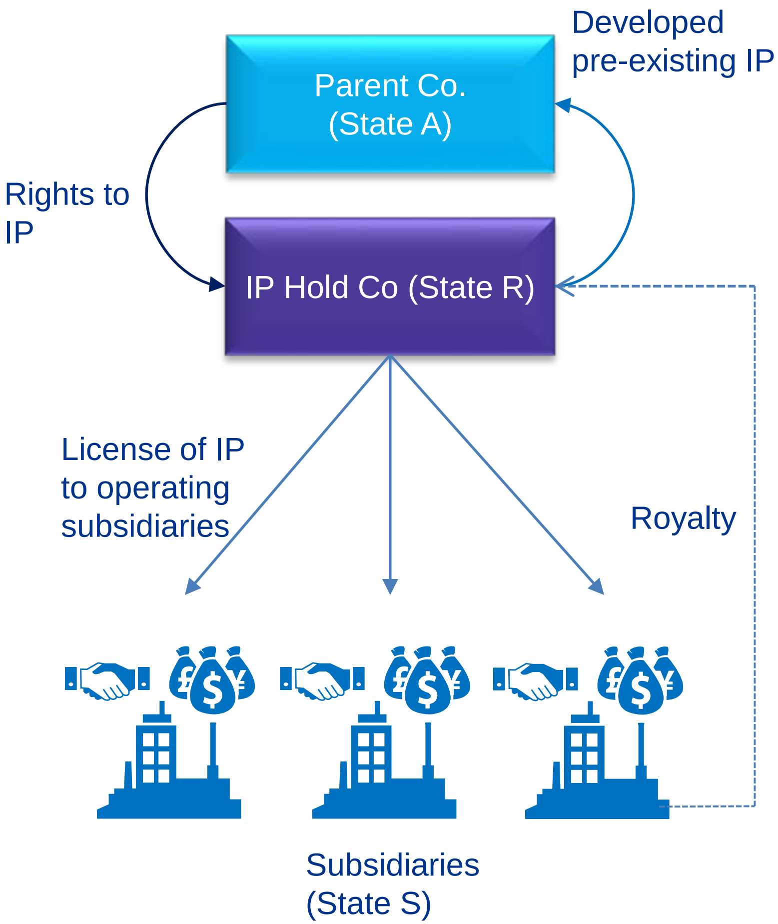
Facts

- Parent Co. develops the IP and performs R&D funded by IP Hold Co. on cost-plus basis
- IP Hold Co. is a capital rich associated enterprise located in State R (low tax jurisdiction)
- IP Hold Co. licenses to other operating subsidiaries engaged in marketing and sales without IP Hold Co. being effectively involved in functions related to IP
- Taxable profits of Subsidiaries are reduced by deduction of royalties

Issues

- Structure enables the group to park bulk of profits in a “cash box” (i.e. IP Hold Co.)
- IP Hold Co. has ownership over the IP even without taking any risks – substance over form

Case Study 1 - Cash Box

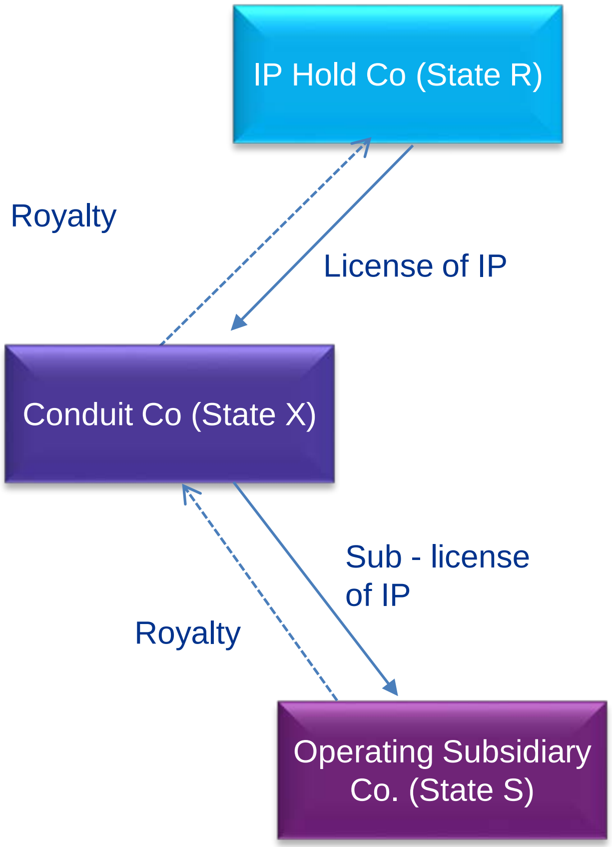


BEPS measures

- **Action Plan 5 provides for better alignment of economic activities and taxation**
- Lays down Substantial Activity test
- Recommends the Nexus approach
- Proportion of expenditure incurred used as measure for substantial activity

India introduced "Patent Box" regime
w.e.f. 1 April 2016
u/s 115BBF

Case Study 2 - Treaty Shopping



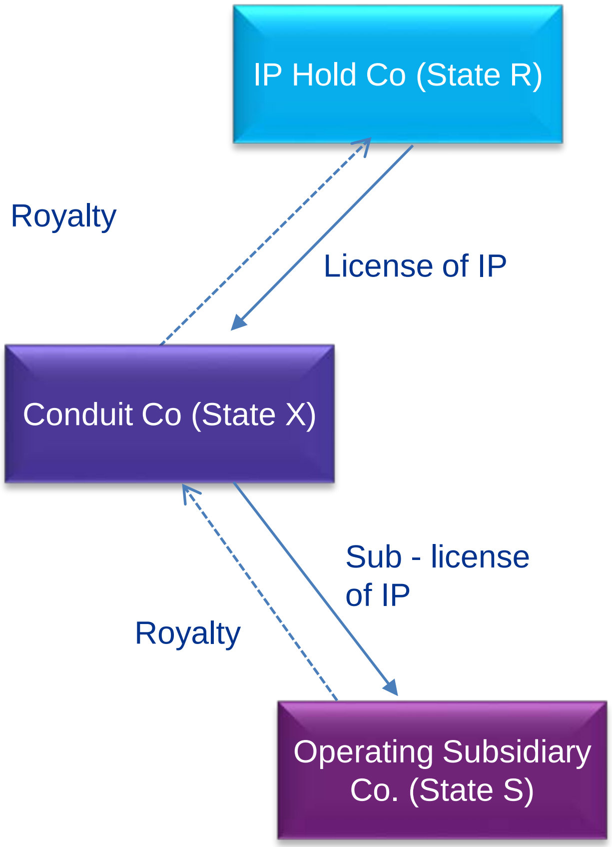
Facts

- IP Hold Co. holds stock of subsidiaries, owns IP and licenses IP to Conduit Company
- Conduit Co. (low substance) sub-licenses to operating subsidiaries and is entitled for favorable tax treaty
- Taxable profits of Subsidiaries are reduced by deduction of royalties

Issues

- No/lower WHT by application of favorable tax treaty between State X and State S

Case Study 2 - Treaty Shopping

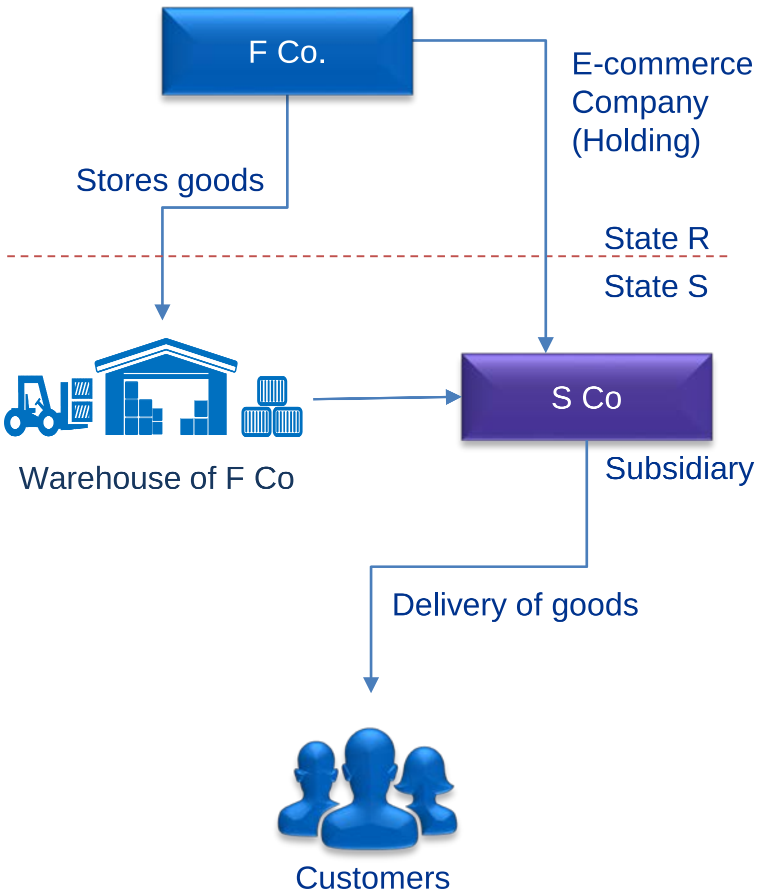


BEPS measures

- **Action Plan 6 recognizes tax treaty abuse and in particular, treaty shopping**
- Anti abuse provisions introduced
- PPT rule – Benefit of tax treaty is denied if one of the principal purpose is to obtain tax benefit
- **MLI – PPT is a minimum standard**
- India has opted - not to grant treaty benefits when PPT invoked

India's CTA may be amended

Case Study 3 - Warehousing



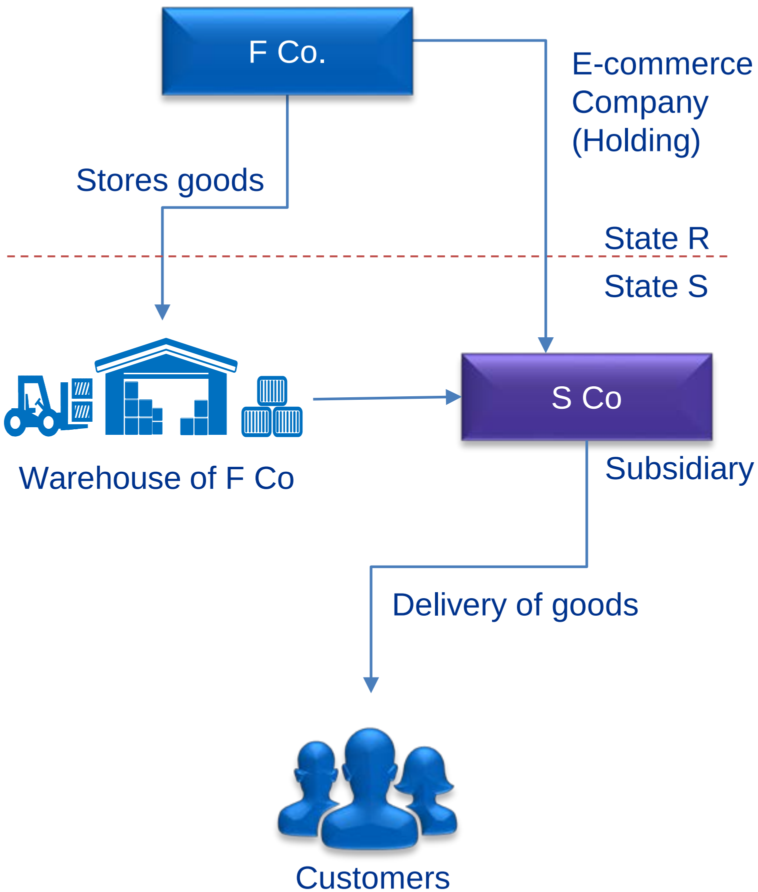
Facts

- F Co. is a B2C e-commerce company in State R
- F Co. has a subsidiary S Co. in State S, which is also provides marketing and support services
- When a customer buys an item through F Co.'s portal/App, S Co.'s employees arrange to deliver goods to the customer from F Co.'s warehouse
- S Co. is remunerated by F Co. on arms length basis for facilitating delivery of goods
- F Co. maintains a warehouse in State S

Issues

- Artificially avoiding PE status in State S by
    1. not concluding contracts on behalf of F Co.'s customers
    2. By applying exemption of warehouse as specific exemption under Article5(4) of the treaty
    3. By fragmenting core activities

Case Study 3 - Warehousing



BEPS Measures

- **Action Plan 7 aims to prevent artificial avoidance of PE status**
- **Scope of PE expanded which is also implemented in MLI**
- **MLI** broadens the scope of DAPE by including activities involving a principal role in concluding contracts
- **MLI** would restrict the applicability of specific exemption under Article 5(4) of the treaty only if preparatory and auxiliary in character
- **MLI** introduces anti-fragmentation rule

India has no reservations on the proposed MLI amendments

India's CTA may be amended

Multilateral Instrument - MLI

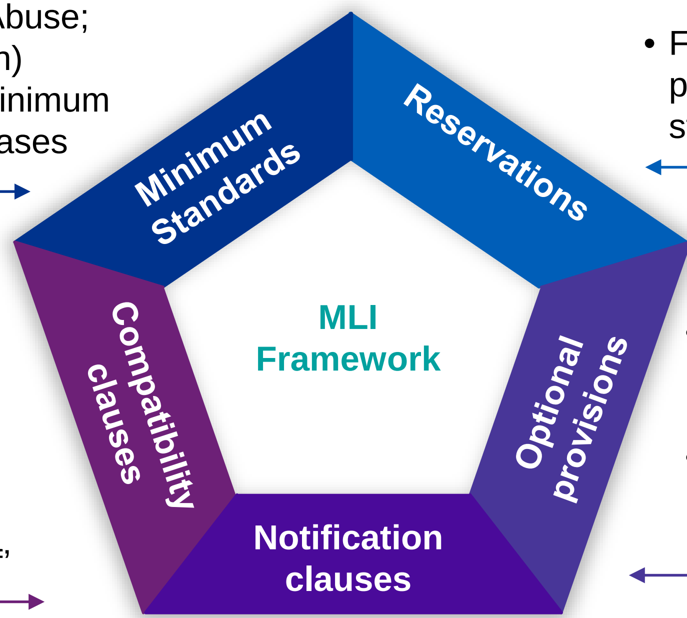
MLI - Background

What is MLI its objectives	• Single instrument that modifies bilateral tax treaties in a synchronised, fast and consistent manner • One negotiation, one signature, one ratification
Impact	• To modify 1200+ tax treaties in first signing; intended to cover 3000+ tax treaties
Actions implemented	• Action 2 (Hybrid mismatches) • Action 6 (Treaty abuse) ***Minimum standard*** • Action 7 (Permanent Establishment) • Action 14 (Dispute resolution) ***Minimum standard***
Legal status	• MLI does not function as protocol, needs to be read with existing tax treaties • Does not replace existing tax treaties but modifies them

MLI - Framework

- All countries to meet certain minimum standards (Action 6 - Treaty Abuse; Action 14– Dispute Resolution)
- No leeway to opt out of the minimum standards, except in limited cases

- Flexibility to opt out of a provision if it is not a minimum standard



- Defines the relationship / addresses conflict between the MLI and the provisions of a CTA
- MLI provision applies –
  - ‘in place of’
  - ‘applies to’ or ‘modifies’
  - ‘in the absence of’
  - ‘in place of or in the absence of’

- Option to choose among alternative provisions intended to address the same issue
- Both the countries to choose the same option in order for it to apply

- Notify choice of optional provision
- Also, notify the existing provision of CTA to be modified / replaced

Process timeline for entry in force

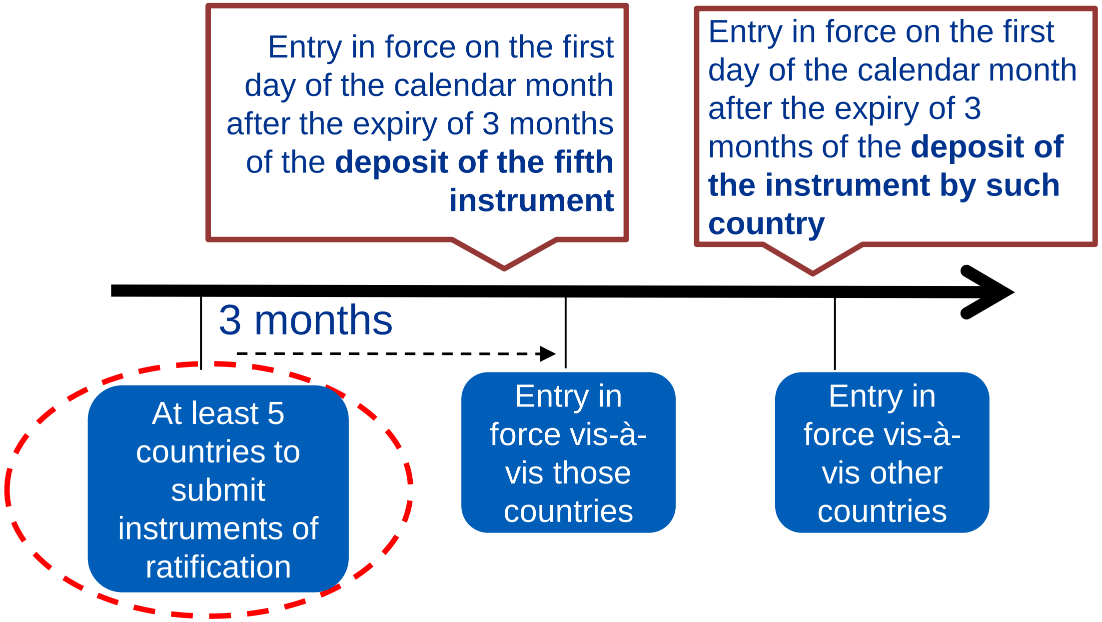


Illustration:

Date of deposit of instrument

India – September 2018

Singapore – October 2018

Date of entry into force:

India – January 2019

Singapore – February 2019

Countries that have ratified and deposited the instrument with the OECD:

1. Republic of Austria (22 September 2017),
2. Isle of Man (19 October 2017)
3. Jersey (15 December 2017)
4. Poland (23 January 2018)
5. Slovenia (22 March 2018)

MLI has enter into force on 1 July 2018

Process timeline for entry into effect for respective CTA

Entry into effect for the respective CTA:

- Computed from the latest date of entry into force for each of the treaty partners of a CTA – referred as " relevant date" ***(i.e. March 2019[#])***

Provisions related to	Date of entry into effect	Date as per illustration
Withholding taxes	1st day of next calendar year that begins on or after the relevant date	For India - 1 April 2019* For Singapore - 1 January 2020
Other taxes	Taxable period that begins on or after expiry of 6 calendar months from the relevant date	For India – FY 2020-21 Singapore – 1 January 2020

[#]India has opted for optional provision pursuant to which the 'relevant date' is 30 days from latter of the dates on which OECD receives notification from India and its treaty partner about completion of its respective internal procedures
*India has chosen to replace 'taxable period' for 'calendar year' for the purpose of its own application of MLI to withholding taxes

Process timeline for entry into effect - Illustration

Withholding taxes

Jan 2019	Date of entry into force for India
Feb 2019	Date of entry into force for Singapore
Feb 2019	Date of completion of internal procedures by both the countries
Mar 2019	Expiry of 30 days for date of completion of internal procedures (Relevant date)
1 April 2019	Date of entry into effect for India (i.e. taxable year)
1 Jan 2020	Date of entry into effect for Singapore (i.e. Calendar year)

Other taxes

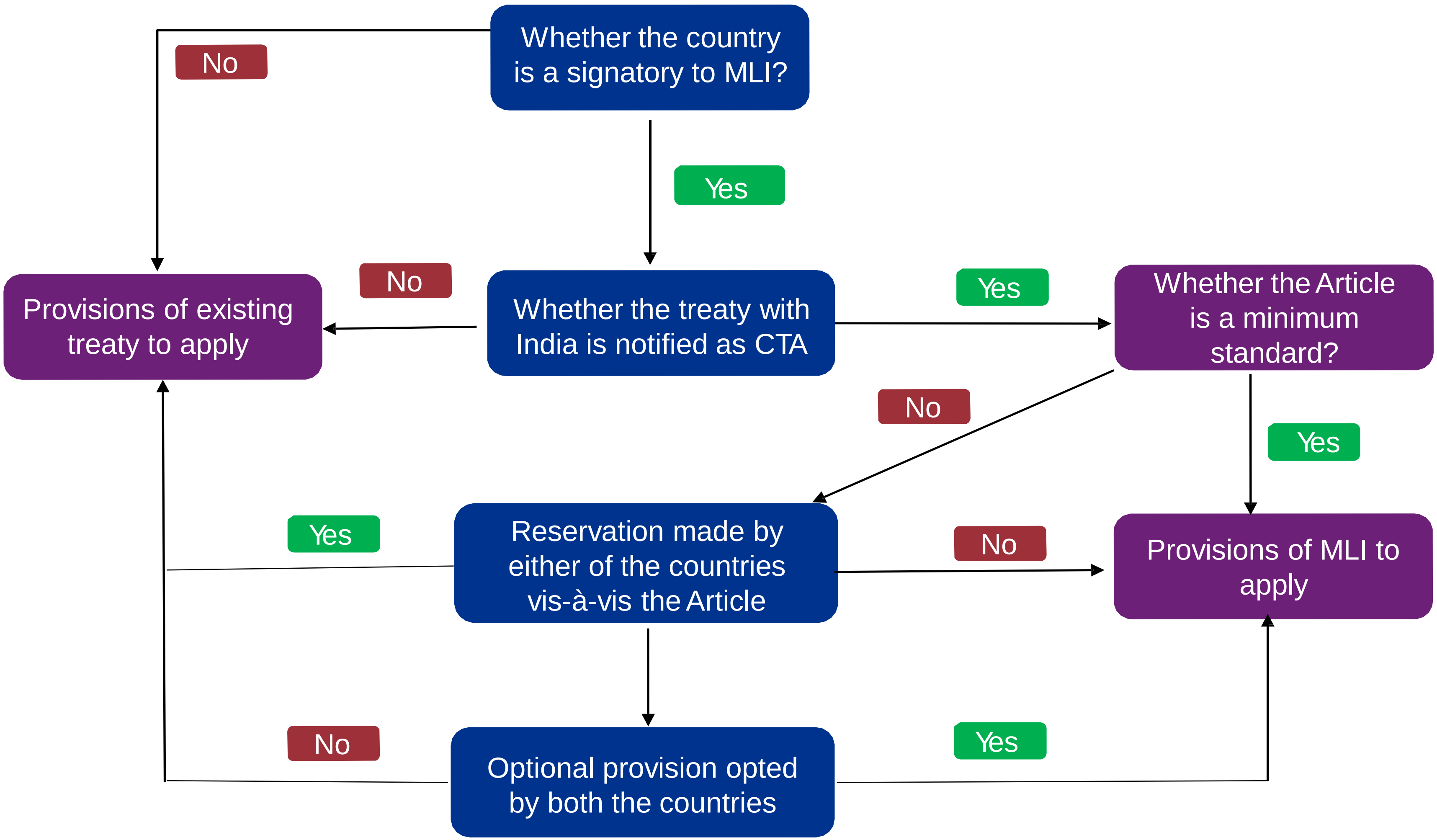
Jan 2019	Date of entry into force for India
Feb 2019	Date of entry into force for Singapore
Feb 2019	Date of completion of internal procedures by both the countries
Mar 2019	Expiry of 30 days for date of completion of internal procedures (Relevant date)
Oct 2019	Expiry of 6 months from 30 day extension period
1 April 2020	Date of entry into effect for India
1 Jan 2020	Date of entry into effect for Singapore

Status of other countries

Some countries which have included India in their CTAs	Countries that have signed MLI but which have not included India in their CTAs	Some countries which have not signed MLI
• Singapore • Netherlands • Australia • United Kingdom • France • Canada • Cyprus • Japan • Sweden • Luxembourg • Spain • Belgium • Korea • UAE	• China • Germany • Mauritius	• U.S.A. • Philippines • Saudi Arabia • Brazil • Thailand*

*Expressed intent to sign MLI

MLI - A snapshot



Thank You