



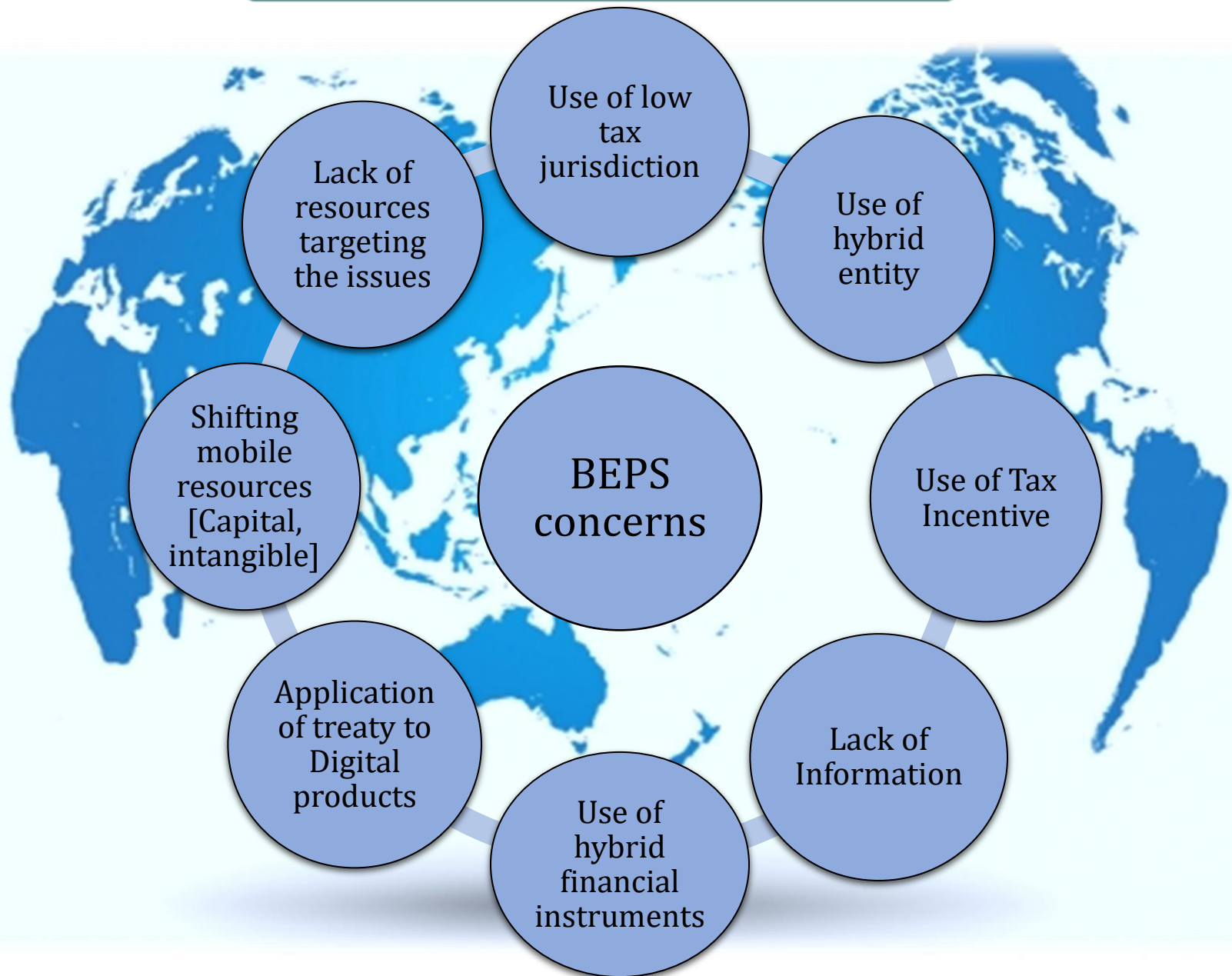
2nd All India Tax Summit
- Achromic Point
09-06-2016

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CA Omar Abdullah S M



WHY BEPS Project ???



Fiscal and economic effects

Global annual CIT revenue



Loss of 4-10%
(USD 100-240 bn)

MNE effective tax rates



4% – 8.5% lower
ETR than similar
domestic firms

Concentration of investments



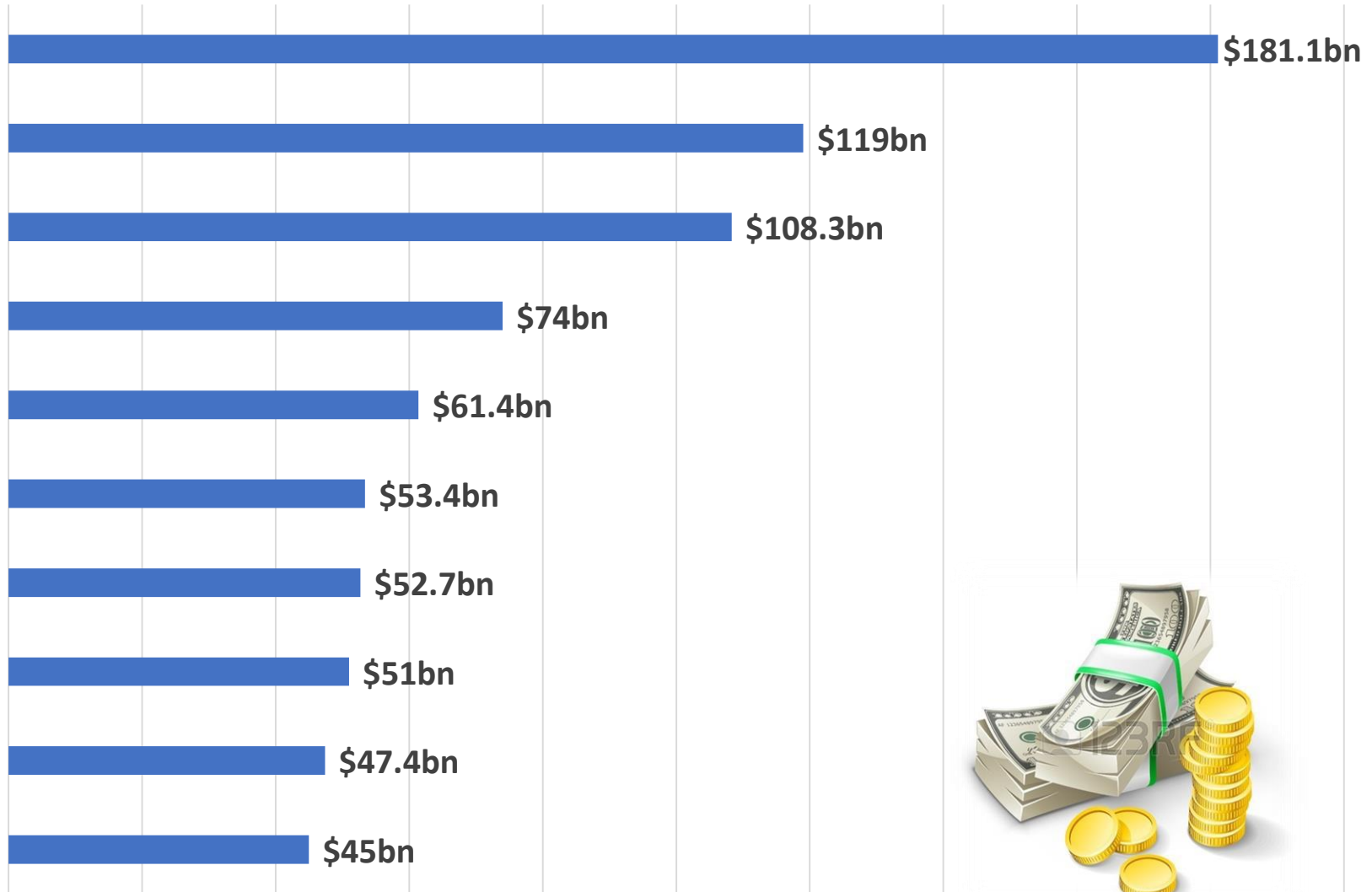
Net FDI to GDP ratios
have increased sharply

Better data is needed

- To assess the effects of BEPS on shifting real economic activity
- To perform statistical analysis based on Country-by-country reports
- To update periodic Corporate Tax Statistics

Key data on BEPS

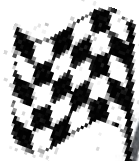
Money held offshore by U.S. companies in 2013 (in billion U.S. dollars)



2013- OECD delivered its first report on BEPS and identified 15 Action Points.

G20 leader's declaration endorses the BEPS project, making it joint project between OECD and G20

2012-The Tax Base Erosion and Profit Shifting (BEPS) Project began.



Oct 2015- OECD launched the 2015 BEPS package.



2014- OECD releases reports, discussion, and draft on all the 15 action topics covered by BEPS.

G20 endorsed the first 7 of 15 actions on BEPS



Nov 2015- G20 leader endorses the BEPS Package.



The background of the slide is a photograph of a series of classical stone columns, likely from a government building or museum. The columns are arranged in a perspective that recedes into the distance. Sunlight filters through the columns, creating strong shadows and highlights on the stone surfaces. The overall tone is warm and formal.

PILLARS OF BEPS PROJECT

**Creating coherence
between
interaction of
domestic laws of
various countries.**

**Emphasis on
substance**

**Need for increased
transparency and
certainty for
business and
government.**

India follow up action on BEPS



Action Plan 1

- Equalization levy Chapter VIII of Finance Act 2016 w.e.f 1st June 2016

Action Plan 5

- Section 115BBF of Income-tax Act, 1961 – Tax on Income from Patent w.e.f 1st April 2017

Action Plan 13

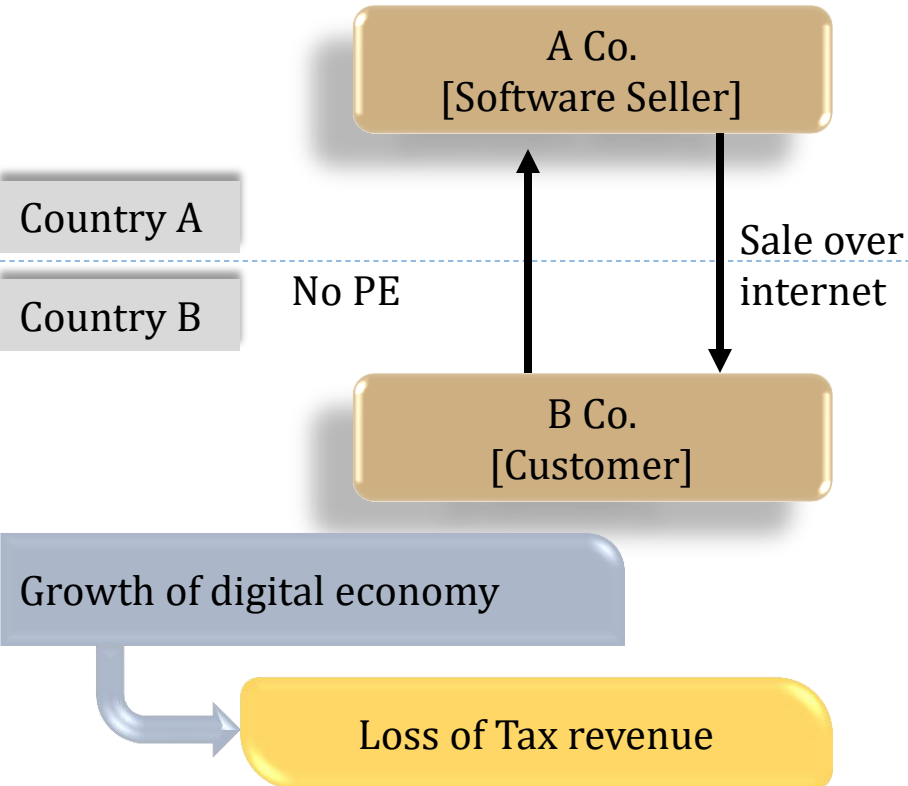
- Section 286 of Income-tax Act, 1961 - Furnishing of report in respect of international group. w.e.f 1st April 2017

Action plan 1 – Digital Economy

Action Plan

1

Digital economy is increasingly becoming the economy itself.

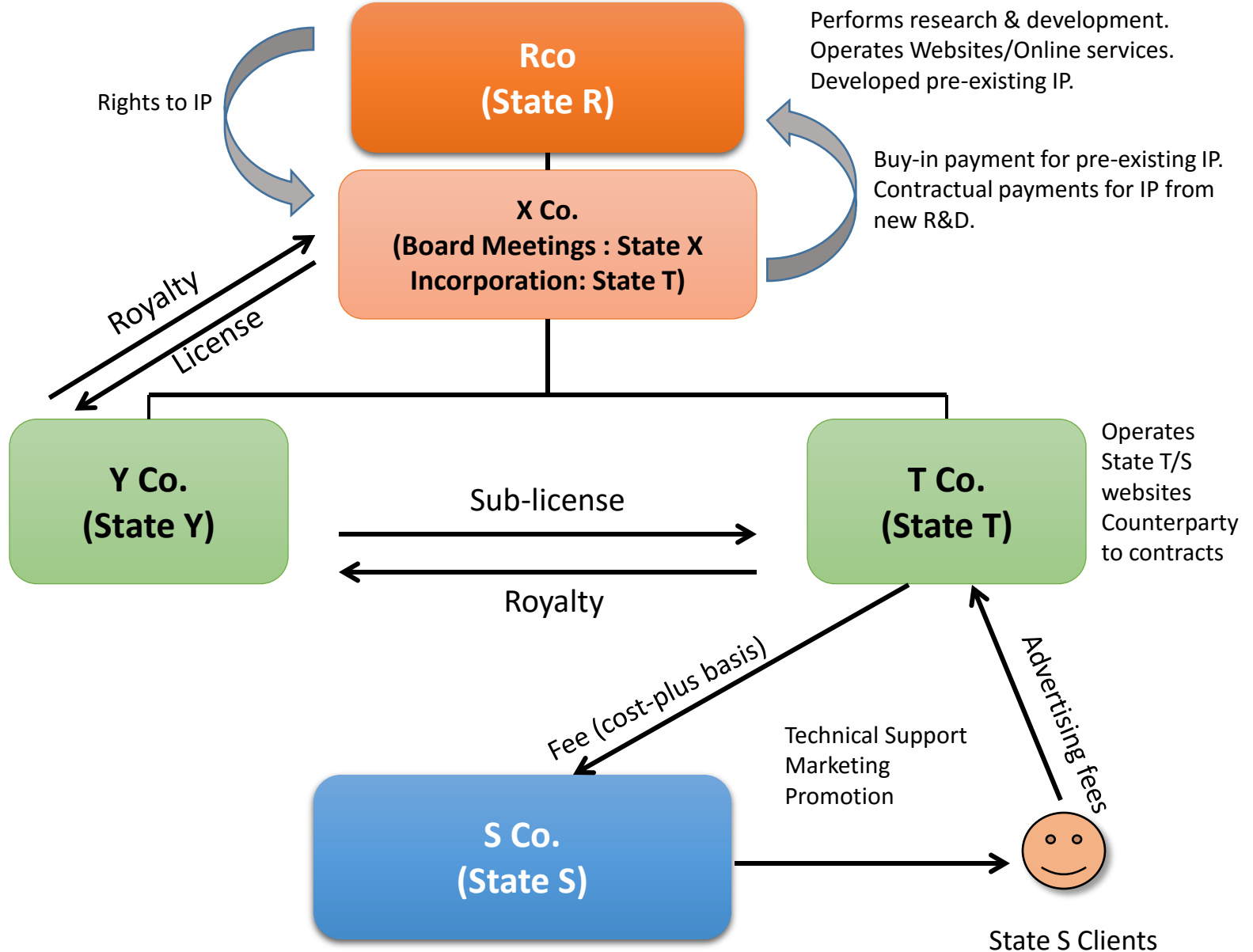


Significant economic presence

Withholding Tax

Equalization Levy

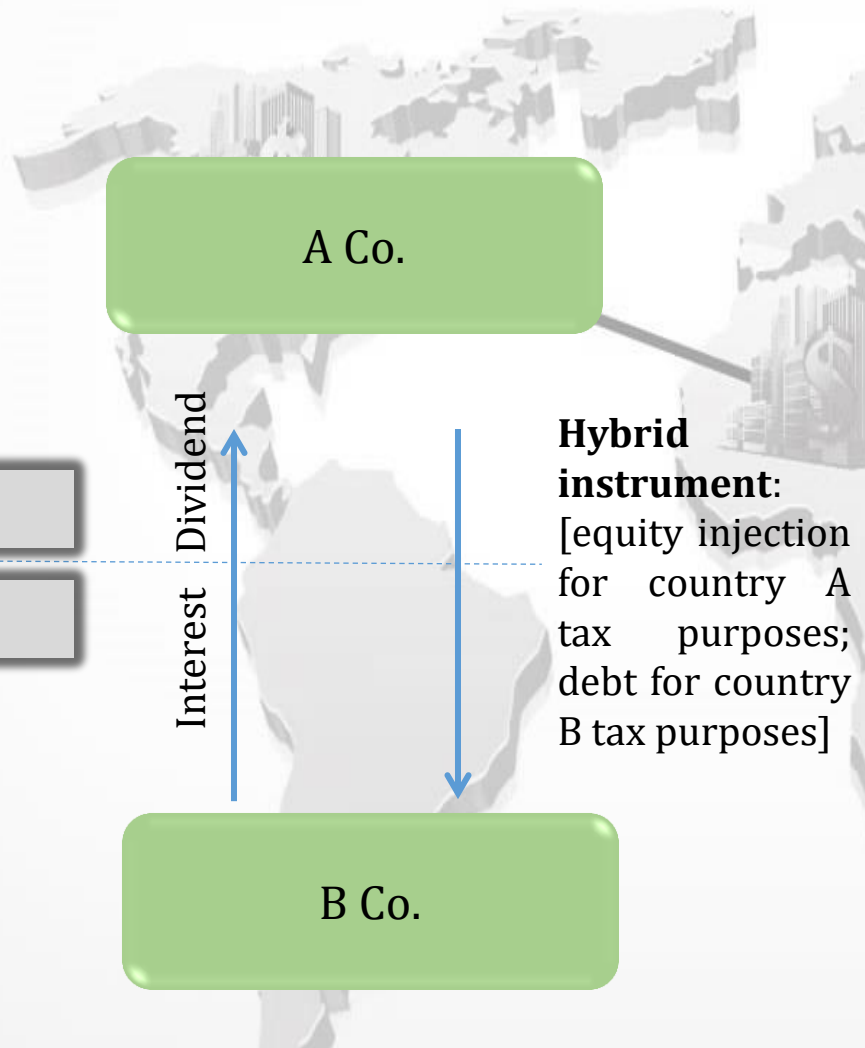
Internet advertising



Action plan 2 –Hybrid Mismatch Agreement

Action Plan

2



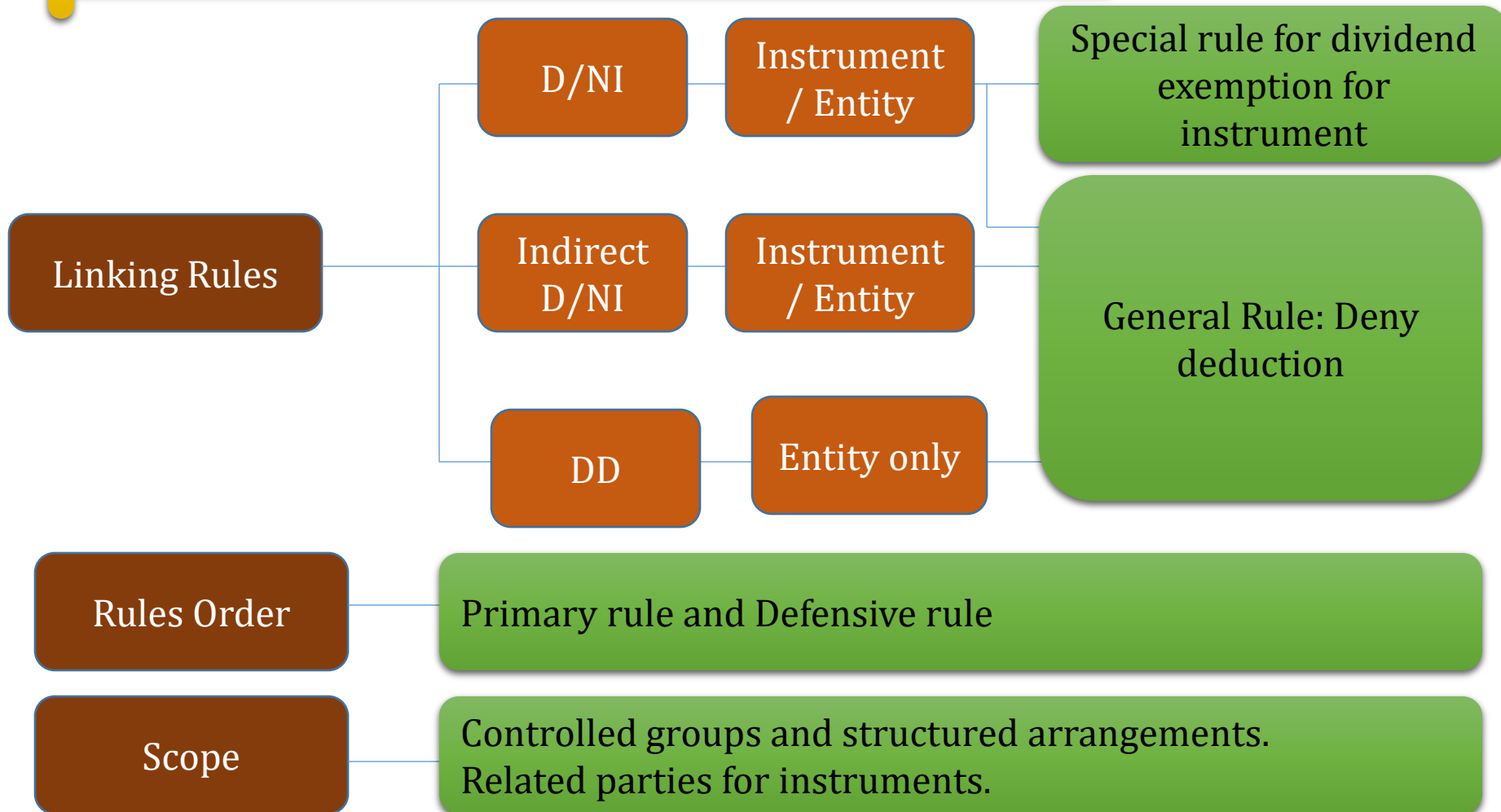
DEDUCTION IN ONE COUNTRY WITHOUT TAXATION IN ANOTHER:

- B Co issues a hybrid financial instrument to A Co, which shall be characterized as debt in Country B and as equity in Country A
- Country A treats the payment as 'dividend', which is entitled to participation exemption
- Country B allows deduction to B Co for interest payments made on the instrument

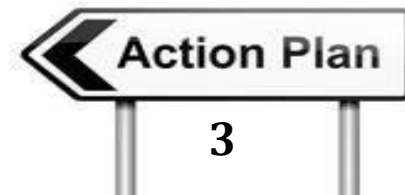
BEPS Recommendations:

- Country B to deny deduction to Payer (B Co)
- *Primary rule:* Country A to treat receipt as ordinary income of A Co

Action plan 2 – Over view of proposed rule



Action plan 3 – CFC Rules



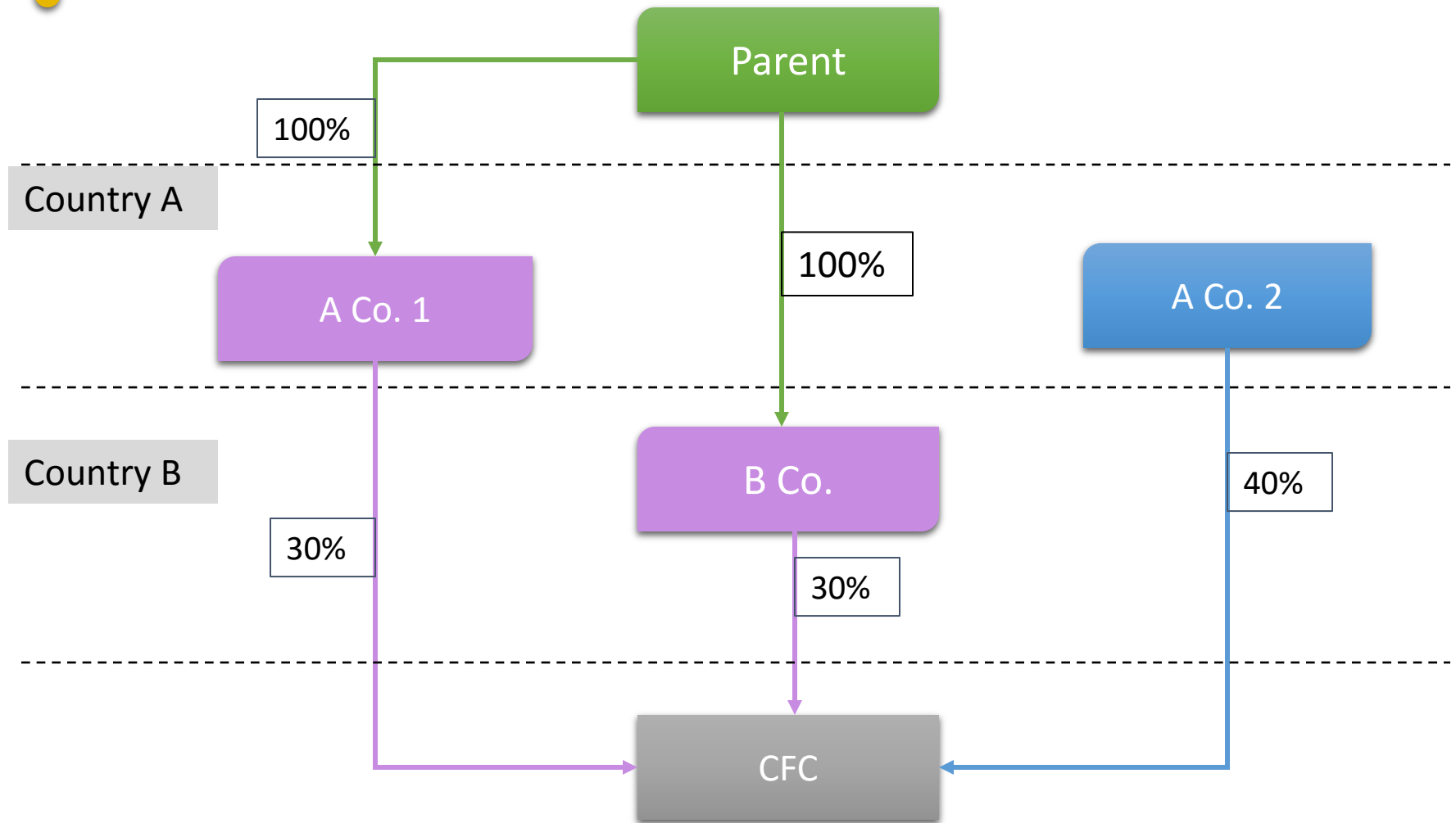
Need for CFC Rules:-

Creation of affiliated non-resident taxpayers and routing income of a resident enterprise through the non-resident affiliate

Objectives :

- Need to strengthen the CFC rules prevailing in the countries
- Develop recommendations regarding the design of CFC rules
- CFC rules lead to inclusions of passive undistributed income in the residence country of the ultimate parent
- A positive spillover effect in source countries as taxpayers have no (or much less) incentive to shift profits into a third, low-tax jurisdiction

Action plan 3 – CFC Rules



Action plan 4 – Limit Base erosion via interest deductions and other financial services

Action Plan

4

Recommendation to eliminate base erosion like

Through the use of related-party and third-party debt to achieve excessive interest deductions

To finance the production of exempt or deferred income

Other financial payments that are economically equivalent to interest payments

FIXED RATIO RULE

Net Interest Expense Allowed

Benchmark Net Interest/EBITDA ratio

Relevant factors help a country set its benchmark ratio within a corridor of 10%-30%

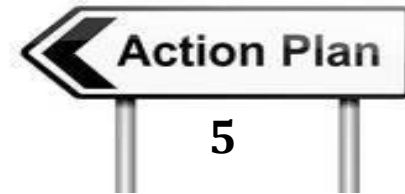
GROUP RATIO RULE

Net Interest Expense Allowed

Groups Net Interest/EBITDA ratio

where this is higher than the benchmark fixed ratio
 Option for a country to apply an uplift to a group's net third party interest expense of up to 10%

Action plan 5 – Harmful tax practices



Plans

Revamp the **work** on harmful tax practices with a **priority** on improving **transparency**

Compulsory **spontaneous exchange on rulings** related to preferential regimes

Rules that require **substantial activity** for any preferential regime

Holistic approach to evaluate preferential tax regimes

Engage with non-OECD members to consider revisions or additions to the existing framework

Expected Results

Finalize review of member country regimes

Strategy to expand participation to non-OECD members

Revision of existing criteria

Action Plan 5-Nexus Ratio

$$\begin{aligned}
 & - \frac{\text{Qualifying expenditures incurred to develop IP asset}}{\text{Overall expenditures incurred to develop IP asset}} \times \text{Overall income from IP asset} = \text{Income receiving tax benefits}
 \end{aligned}$$

Action plan 6 – Prevent treaty abuse

Action Plan

6

Country 1

Country 1

A Ltd

Royalty income
subject to 25%
withholding
tax

Country 2

B Ltd

No tax treaty between Country 1 and
Country 2

A Ltd

No tax
implication

Country 3

C Ltd

Royalty income
subject to no
withholding tax

Country 2

B Ltd

- Tax treaty between Country 1 & Country 3
- Tax treaty between Country 2 & country 3

Issues

Low taxed branches of a foreign company

Conduit companies/ regimes

Multiple layers of legal entities

Artificial shifting of income through transfer pricing arrangements

Recommendations

design of domestic rules to prevent the granting of treaty benefits

Clarify tax treaties are not intended for generating double non taxation

Identification of important tax consideration that country need to take care while entering into treaty.

Plans

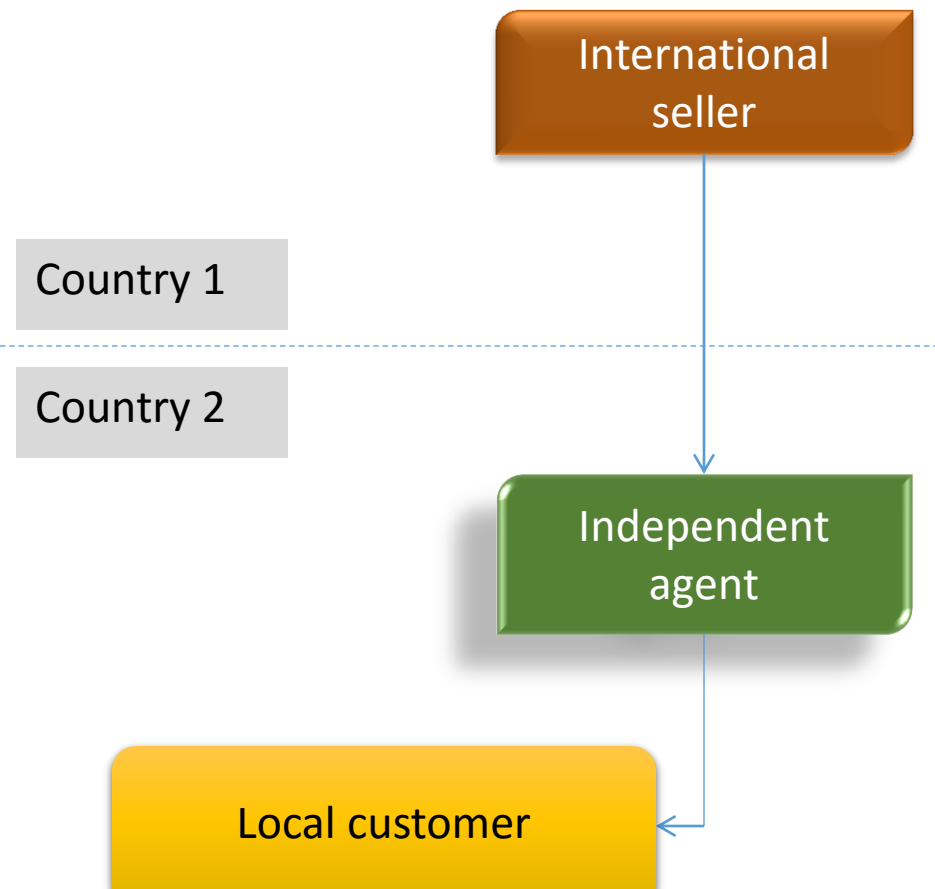
PPT rule

LOB rule

Action plan 7 – PE AVOIDANCE

Action Plan

7

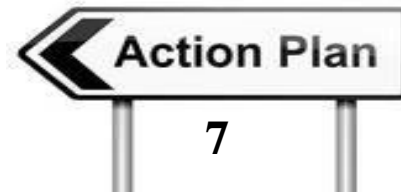


- The independent agent sells the product to the local customer for arm's length remuneration.
- This commissionaire agreement between agent and international principal will give rise to non taxation of source income in country of agent.

Country - A



Company A



Habitually plays the principal role leading to the conclusion of the contract

contract conclusion

Country - B



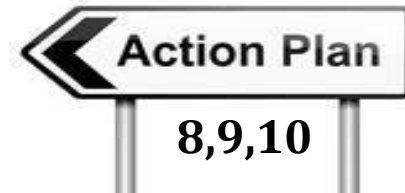
Company B

Contract Negotiation



Customer

Action plan 8,9 & 10 – Aligning Transfer Pricing Outcomes with Value Creation



Multinationals have been able to use and/or misapply arm's length principle to separate income from the economic activities that produce that income and to shift it into low-tax environments. For example:-

Transfers of intangibles and other mobile assets for less than full value

The over-capitalization of lowly taxed group companies.

Contractual allocations of risk to low-tax environments in transactions that would be unlikely to occur between unrelated parties.



Company - P

Rights in
inventions
assigned to
Company - S



Company - S

Wholly - owned
subsidiary

- Fund R & D
- Perform ongoing R & D Function
- Written contract with Company S licensing IP

- Company S agrees to compensate parent P
- Parent Co. P performs negotiations with third-party customers to achieve sales for Company - S
- Parent Co. P provides regular technical services support to Company S



Who controls business risk ?

Action plan 8,9 & 10 – Aligning Transfer Pricing Outcomes with Value Creation

Develop rules to prevent BEPS by moving intangibles among group members which involve:-

Adopting a broad and clearly delineated definition of intangibles

Ensuring that profits associated with the transfer and use of intangibles are appropriately allocated in accordance with (rather than divorced from) value creation

Updating the guidance on cost contribution arrangements

Developing transfer pricing rules or special measures for transfers of hard-to-value intangibles



Company - A

Rights in
inventions
assigned to
Company - B



Company - B

Wholly - owned
subsidiary

- Fund R & D
- Perform ongoing R & D Function

- Employs three lawyers to perform its patent administration work and no other employees
- Grants licenses of its patents to AE's and Independent third parties under instructions from Company - A to earn royalties

Action plan 8,9 & 10 – Aligning Transfer Pricing Outcomes with Value Creation

The MNEs should be prevented from Base Erosion and Profit Shifting by transferring risk among, *or allocating excessive capital to, group members.*

Adopting TP rule that ensure inappropriate return do not accrue to entity because of contractual assumed risk or has provide capital.

The rules will ensure alignment of return with value creation.

Co-ordinate work with the Action plan 4 [Limiting interest deduction and other financial payments]

Action plan 8,9 & 10 – Aligning Transfer Pricing Outcomes with Value Creation

Develop rules to prevent BEPS by engaging in transactions which would not, or very rarely, occur between third parties. This involve

Clarify the circumstance in which transactions can be recharacterised

Clarify the application of transfer pricing methods, in particular profit splits, in the context of global value chains

Provide protection against common types of base eroding payments, such as management fees and head office expenses.

The Action Plans would consider the application of both the principles :-

- (i) Arm's Length Price (ALP) principle and
- (ii) Potential special measures required to address concerns identified in Action Plan

Identifying the commercial and financial relations

Identifying risks in commercial and financial relations

Interpretation

Non recognition

Specific considerations

Guidance
for Applying
ALP
principle

Action 11: Establish methodologies to collect and analyze data on BEPS and the actions to address it

Action Plan

11

Develop outcome based techniques which seeks to allocate income across jurisdictions

Recommendations regarding economic impact of BEPS

Ensuring tools are available to evaluate effectiveness of actions taken on BEPS

Identify new types of data in addition to existing data to analyze both at aggregate and micro-level

Balance above objectives with taxpayer confidentiality and administrative costs

Action Plan 12: Mandatory Disclosure Rules

Action Plan

12



Need for Action Plan 12:

Comprehensive & Relevant information on tax planning strategies often unavailable

Audit suffers from number of constraints of tool for early detection of aggressive tax planning Techniques

- ✓ Recommendations regarding the design of mandatory disclosure rules
- ✓ Focus on international tax schemes to explore
- ✓ Enhancing models of information sharing for international tax schemes



Action Plan 13 : Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting

Action Plan

13



Three - tier TP Documentation

Country-by-Country report

Master File

Country-by-Country Report

Local File

TP Documentation

Contains information relating to MNE group's income and taxes along with other indicators of economic activity for each of their country of operation

The parent entity is required to submit the report to the prescribed authority in its country of residence.

This report shall be shared among the countries vide an automatic IEA



Action Plan 13 : Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting

Matters relating to the implementation of the CbC Report



Timing of preparation & Filing of CbC Report

The CbC report shall be filed no later than 12 months after the last day of the Reporting Fiscal Year of the MNE Group

Which MNE groups are required to file CbC Report

All MNE groups be required to file the CbC Report each year except for MNE groups with annual consolidated group revenue in the immediately preceding fiscal year of less than € 750 million or a near equivalent amount in domestic currency.

Conditions for obtainment & use of report by jurisdiction

Confidentiality

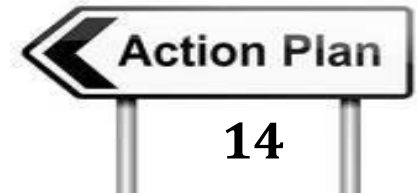
Appropriate Use

Consistency

Model Template for CbC Report

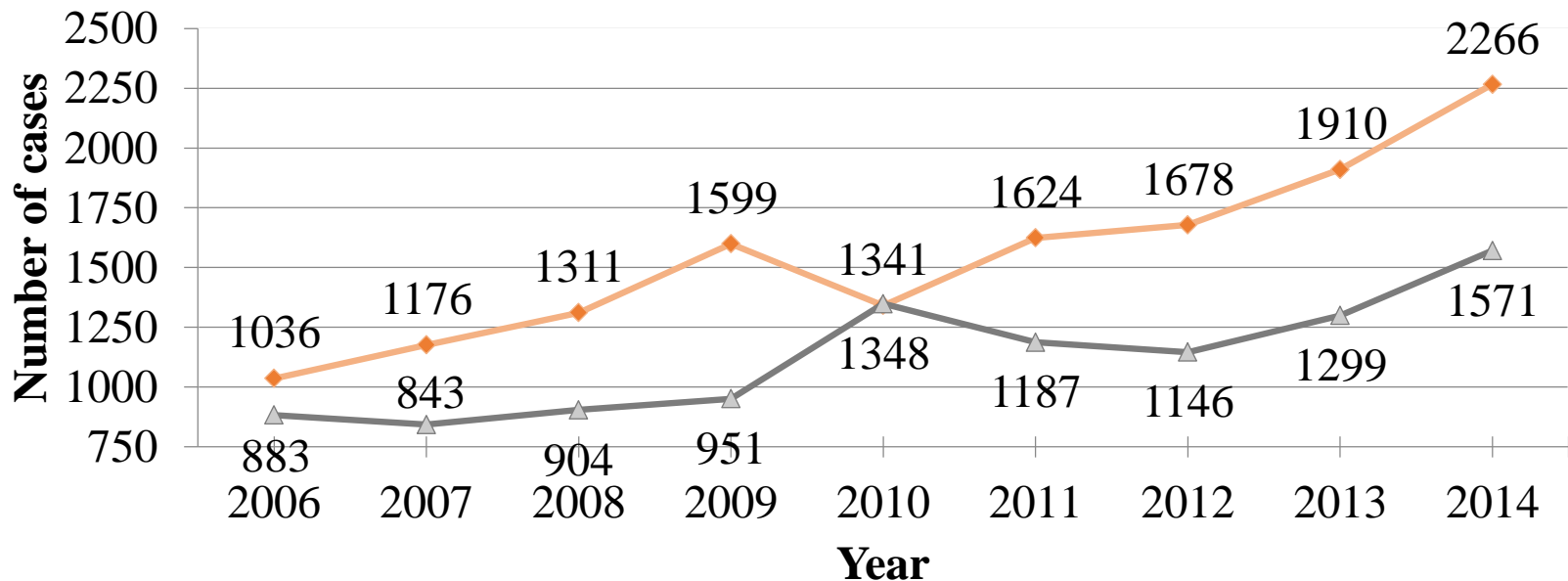


Action Plan 14: Make Dispute Resolution Mechanisms more effective



Action Plan 14 - “Develop solutions to address obstacles that prevent countries from [re]solving treaty-related disputes under MAP, including the absence of arbitration provisions in most treaties and the fact that access to MAP.”

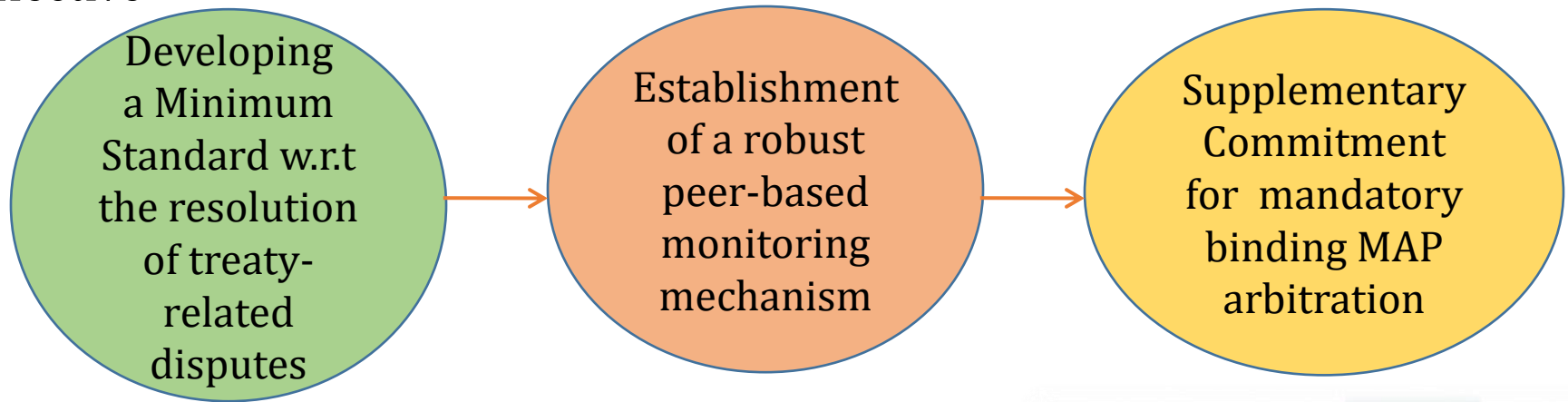
MAP cases initiated / completed by year





Action Plan 14: Make Dispute Resolution Mechanisms more effective

Important changes in the approach to dispute resolution to make it more effective



Action Plan 14: Make Dispute Resolution Mechanisms more effective

Minimum standard comprising 17 specific measures to improve the effectiveness, efficiency and timeliness of the **MAP process, with 3 general objectives**

- Ensuring that treaty obligations related to the MAP are fully implemented in good faith and that MAP cases are resolved in a timely manner.
- Ensuring the implementation of administrative processes that promote the prevention and timely resolution of treaty-related disputes.
- Ensuring that taxpayers that meet the requirements of Article 25(1) of OECD Tax model can access the MAP.



Action Plan 15: Multilateral Instruments

Action Plan

15

Action 15 of the BEPS Action Plan provides for an analysis of the tax and public international law issues related to the development of a multilateral instrument to enable countries that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties.

Need for multilateral instruments

- Updating the current tax treaty network highly burdensome, time consuming and will require substantial resources due to multiple number of bilateral tax treaties
- Without mechanism to swiftly implement them, changes to model only makes gap between content of model and content of actual tax treaties wider. This contradicts the political objective

Action Plan 15: Multilateral Instruments



Objectives

- Analyze the tax and international law issues for development of a multilateral instrument to enable jurisdictions to implement measures and provide a foundation for amendment of bilateral tax treaties.
- Develop a multilateral instrument to provide an innovative approach to international tax matters-reflecting rapidly evolving nature of global economy and adapt quickly to it.
- Streamline the implementation of tax treaty related BEPS measure



Thank
You