SKP

TAX TRENDS

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We are pleased to present the second edition of Tax Trends, SKP's quarterly newsletter that aims to provide a quick snapshot of the key direct tax developments in India. This issue covers developments from July to September 2015.

Since the Modi government assumed office last year, there has been substantial dynamism in the tax environment in India. The government has been actively focusing on curbing tax evasion and at the same time, has made active efforts to reach out to taxpayers to clarify its position on tax matters.

Living up to the promise of curbing tax evasion by means of money and assets stashed overseas, the government has enacted a separate legislation to deal with 'Black Money' stashed abroad. The law is stringent and comprehensive. In *Spotlight*, we discuss the finer aspects of this new legislation.

The levy of Minimum Alternate Tax (MAT) on foreign institutional investors (FIIs) had an adverse impact on investor sentiment. The government was swift in its response and constituted an Expert Committee headed by Justice A P Shah to look into the matter. The Committee was of the view was that levy of MAT on FIIs was not sustainable. The government graciously accepted the decision of the Committee and issued a formal Circular to this effect. This approach marks a significant change compared to the earlier government's reaction to the Vodafone case and is being widely appreciated by the investor community.

Similarly, applicability of MAT to foreign companies other than FIIs was also being widely debated. MAT, which is a tax on accounting profit, is levied at a minimum effective rate of 19.43% and is higher than the special purpose tax rates under most of the DTAAs entered into by India. The government recently issued a press release clarifying that foreign companies that do not have a Permanent Establishment (PE) in India will not be subject to MAT. This benefit is also being extended to taxpayers from non-DTAA countries, which will provide relief to taxpayers from Hong Kong SAR. The government has also specified that it will amend the law with retrospective effect from 1 April 2001. This is a striking development that will provide huge relief to a large number of taxpayers in their ongoing litigations in India on this issue.

It has been equally encouraging to see that the Finance Minister, on his own, has gone on record to state that he will reduce the corporate tax rates next year. Though the exact rate cut is being worked out, the statement of intent marks a stoic difference in approach from the government.

The government is also moving towards increased interlinking and data sharing amongst different government departments to curb tax evasion. There has also been an outstanding improvement in the time taken for issuing tax refunds for individual taxpayers. Earlier, refunds would take over 12 months to be received after filing the return of income. This time has now been reduced to only 15 days and many individual taxpayers who filed their tax returns in July/August 2015 have already received their refunds.

We hope you find our newsletter useful and look forward to your feedback. You can write to us at skptax@skpgroup.com.

Warm regards,

The SKP Tax Team

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Overview of the new Black Money law in India

The government of India has been under immense pressure to tackle the menace of income earned in India but stashed/invested abroad without payment of due taxes. To fulfil its election promise, the government has enacted a new law called The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 (BMA). The BMA became effective from 1 July 2015 and provides for stringent implications, compliances, and penalties.

The BMA covers the following types of incomes/assets:

- Income earned in foreign countries that is taxable in India
- Assets created in foreign countries from income that is taxable in India
- Income derived from assets in foreign countries.

The BMA does not cover domestic undisclosed income/assets as a separate law is being enacted to deal with the same.

The BMA applies to individuals, companies, firms, trusts, etc. and applies to persons who are 'ordinary tax residents of India' as defined under the Income Tax Act, 1961 (ITA). Non-residents and residents who are not ordinarily residents are outside the purview of the BMA. The tax residential status in India is dependent on the period of stay in India and needs to be determined based on the provisions of the ITA and the applicable Double Taxation Avoidance Agreement.

BMA applies to income earned in foreign countries and assets held in foreign countries. Any person, whose income is taxable in India but is not offered to tax in India and is stashed overseas, or whose foreign assets are not disclosed to the Indian tax authorities, is considered an offender under the BMA.

The definition of 'foreign asset' is very wide and covers almost every kind of property. Foreign assets would include:

- Foreign bank accounts held singly or jointly
- Foreign bank accounts where the person is a signing authority
- Financial interest including partnership interest in any entity outside India
- Immovable property
- Any other capital asset
- Interest in any foreign trust (as trustee/beneficiary/settlor).

The BMA provides various stringent measures against offenders such as:

- Tax @ 30% of undisclosed foreign income and value of undisclosed foreign assets
- Penalty @ 90% of the tax amount
- Penalty of INR 1 million for not filing tax return within one year from the end of the fiscal year
- Penalty of INR 1 million for non-furnishing/inaccurate furnishing of particulars of foreign assets
- Prosecution with imprisonment ranging from 3 years to 10 years.

As seen from above, an offender under the BMA will be liable to pay 120% of his undisclosed income/ value of undisclosed assets by way of tax and penalty. Prosecution proceedings will also become applicable. The valuation of undisclosed assets will be governed by separate rules.

It is important to note that unlike the provisions of the ITA, the BMA does not have any time limit for the initiation of any proceedings. For instance, if any undisclosed foreign asset was purchased in the year 2000 and the same comes to the notice of the tax office in the year 2025, it would still be liable for tax @ 30% and penalty @ 90% on the value of assets. Thus, an offender would constantly fear being caught by the BMA.

The BMA has not provided any specific exception for the case of expatriate employees of multinational companies working in India. Therefore, any expatriate employee who becomes an ordinary tax resident in India due to his extended deputation to India may get covered under the BMA if there is a lapse on his part to disclose foreign assets acquired from income earned

in India. On similar lines, where the family members of the expatriate employees accompany them to India, such family members may also get covered within the purview of the BMA for lapses to disclose foreign assets acquired from income earned in India.

Once the BMA applies, the expatriate employees have to comply with all the requirements of the BMA. The expatriate employee shall be liable to tax in India on his global income, even if such income is already subject to tax in any other country. Where the expatriate employee has acquired any assets outside India from the income earned by him in India, such assets should be disclosed in his Indian tax returns. However, he may not be required to declare assets that were acquired by him when he was not a tax resident of India.

These requirements already exist under the ITA and the present format of tax returns. Similar to the ITA, the BMA also has provisions for appeals and tax recovery. What has changed under the BMA is, in the case of default, stringent penal consequences will apply.

The BMA additionally provides that any person other than the income-earner could also be considered an offender if such person supports in tax evasion or helps any offender under the BMA in any manner. The employer of expatriate employees may therefore become an offender under the BMA if he does not exercise due diligence to ensure expatriate employees comply with the requirements of the BMA. Furthermore, where any tax or penalty is due from an expatriate employee under the BMA, the tax authorities can require the employer to pay the tax or penalty to the government out of any payments to be made to such expatriate employee.

Expatriate employees and their employers should exercise utmost caution in understanding and complying with the requirements of the BMA. They should ensure the tax residential status in India is correctly determined. Complete disclosure of foreign incomes and foreign assets must be provided in the tax returns. Also, it is equally critical to maintain detailed and robust documentation to demonstrate the source of funds for acquiring foreign assets to justify that the foreign assets were either acquired:

- when the expatriate was not an ordinary tax resident in India, or
- out of income not taxable in India, or
- out of income on which taxes were duly paid in India.

The documentary evidence could be in the form of detailed bank statements, copies of the agreements/deeds for purchase of properties, movement of funds between different bank accounts, particulars of source of income for making investments, copies of invoices/bills for purchase of any other valuables, etc.

Similarly, non-resident Indians who are planning to return to India permanently and have kept assets outside India will need to plan their return properly, keeping this law in mind.

The BMA is a new legislation and it is yet to be seen as to how the government applies the same. So far, the government has issued two sets of frequently asked questions (FAQs) to clarify certain aspects of the BMA. In an unprecedented and welcome initiative, the Chairperson and Revenue Secretary of the Central Board of Direct Taxes (CBDT) held an hour-long Talkathon to explain BMA to the general public.

The BMA is a stringent legislation and is a milestone achievement of India’s resolve to counter the menace of undisclosed income and assets stored in tax havens overseas. It is a part of the multi-pronged strategy pursued by the Modi Government to counter the menace of ‘Black Money’. Simultaneously, the government is also engaging foreign countries for the exchange of information through bilateral and multilateral means to curb tax evasion. India has also been a prominent participant in the global initiative on Base Erosion and Profit Shifting (BEPS).

Foreign Companies not having Permanent Establishment in India not liable to pay Minimum Alternate Tax, clarifies Government of India

Press release dated 24 September 2015

The Government of India has issued a press release to clarify the applicability of MAT for foreign companies with effect from 1 April 2001. According to the press release, a foreign company that is a tax resident of a country with which India has a Double Taxation Avoidance Agreement (DTAA) will not be liable to MAT, if such foreign company does not have a PE in India, as defined in the DTAA. For taxpayers who are tax residents of countries with whom India does not have a DTAA, this benefit will be available if such taxpayers are not required to seek registration under section 592 of the Companies Act, 1956 or section 380 of the Companies Act, 2013. The press release also states that appropriate amendment to the ITA shall be carried out to give effect to this clarification with effect from 1 April 2001.

Consultancy fees paid for review of engineering designs not considered FTS under India-Finland tax treaty as review of designs does not result in *'make available'*, holds Delhi Tribunal

Income Tax Officer, TDS vs Nokia India Pvt Ltd (ITA No. 1941/ Del/2012)

The taxpayer was a tax resident of India and was in the process of setting up a manufacturing facility in India. For the purpose of constructing a manufacturing facility, the taxpayer had appointed a local Indian contractor to undertake the construction activities. Furthermore, the taxpayer also hired a Finland-based consulting company to review the design, construction plans, etc. to ensure the construction was up to the taxpayer's global standards. The issue in contention before the tribunal was whether the payment made to the Finnish vendor was liable to withholding tax in India.

The Tribunal observed that according to the India-Finland tax treaty, fees for technical services (FTS) mean payment for provision of services which *'makes available'* technical knowledge, experience, knowhow, process, etc. or results in the transfer of a technical plan or design.

Relying upon the definition of *'make available'* provided in the MoU to the India-US tax treaty, the Tribunal held that the Finnish company did not make available any kind of technical knowledge, experience, etc. to the taxpayer as the services provided did not enable the taxpayer to take any benefit of the technical knowledge inherent to the services independently. Furthermore, the Tribunal also observed that the Finnish company was hired merely to review the work done by the Indian contractor and not to prepare any sort of design, plan, etc. Accordingly, the Tribunal concluded that the services did not result in the transfer of a technical plan either.

It was accordingly held that the payment made to the Finnish company was not in the nature of FTS under the tax treaty and was therefore not liable to withholding tax in India.

Beneficial tax rates under tax treaties can be claimed even in scenarios where recipient does not have a PAN. Provisions of section 206AA cannot override treaty provisions, holds Bangalore Tribunal

Deputy Commissioner of Income Tax and Asst Director of Income Tax vs M/s Infosys BPO Ltd (ITA No. 1143(B)/2013)

The taxpayer was a tax resident of India and had made certain payments to non-residents who did not have a Permanent Account Number (PAN).

The taxpayer deducted taxes at the rates prescribed in the respective tax treaties. However, tax authorities were of the opinion that since the taxpayer had made payments to non-residents who did not have a PAN, the taxpayer was obligated to deduct taxes at 20% as per section 206AA. The question before the Tribunal was, in the case of absence of a non-resident's PAN, can a taxpayer claim the benefit of lower deduction under tax treaties i.e. whether or not the provisions of section 206AA overrides provision of section 90(2).

The Tribunal made the following observations while issuing its order:

- Sections 195 and 206AA are procedural provisions dealing with collection and deduction of tax at source.
- Section 195 which casts the duty for deduction of tax is not a charging section. Treaty provisions are charging sections which will override machinery provisions such as sections 195 and 206AA.
- Accordingly, it would not be logical to construe that section 206AA overrides section 90(2) which is a treaty provision.

The Tribunal therefore held that the tax liability of a non-resident eligible to treaty benefits can never be more than the rate prescribed under the applicable tax treaty.

While taking the above decision, the Tribunal placed heavy reliance on the decision of Serum Institute of India Ltd which was a similar case.

Payment for live coverage of cricket match does not qualify as FTS or royalty under the India-UK tax treaty

IMG Media Ltd vs Director of Income Tax (ITA No. 1513/ Mum/2014)

The taxpayer was a tax resident of UK and was engaged in the business of providing multimedia coverage services for live sports events. The taxpayer received payments from BCCI for capturing and delivering live audio and visual coverage of cricket matches held in India. The question before the Tribunal was whether the income from the taxpayer's activities constituted either FTS or royalty under the India-UK tax treaty.

The Tribunal held that according to the India-UK tax treaty, FTS means payment for provision of services which *'make available'* technical knowledge, experience, know how or process, etc. to the recipient thereof. Relying on the definition of *'make available'* provided in the MoU to the India-US tax treaty, the Tribunal held that the UK company produced the end product using its extensive technical expertise.

However, the Tribunal noted that the taxpayer merely delivers a final product in the form of program content and does not make available any technical expertise to the Indian company which would enable the Indian company to perform such service on its own accord in the future. Hence, the ITAT held that the said payment does not fall within the restricted definition of FTS under the treaty.

The Tribunal further noted that the taxpayer merely applied its technical expertise to produce the feed for live coverage. They did not have any ownership over the final program content that was produced by it. In the absence of any ownership over the program content, the Tribunal held that the said receipt would also not qualify as royalty under the India-UK tax treaty.

Expenses cannot be disallowed if 'nil withholding certificate' was obtained under section 195(2)

Deputy Commissioner of Income Tax vs M/s Carl Zeiss India Pvt Ltd (ITA No. 1251(B)/2014)

The taxpayer was a branch office of a conglomerate headquartered in Singapore. The taxpayer acted as a front office for its group companies in India and undertook sales support activities for them in India. According to a cost-sharing agreement between the taxpayer and its head office, some portion of the salary cost of the senior management personnel of the head office was allocated to the taxpayer and was to be reimbursed to the head office. The taxpayer had obtained a nil withholding certificate under vsection 195(2) for the above remittance. The question before the Tribunal was whether the said remittance was in the nature of FTS and the taxpayer was liable to deduct taxes and also whether a disallowance under section 40(a)(i) could be made after a certificate had already been obtained under section 195(2).

Without going into characterisation of the payment, the Tribunal observed that provisions of section 40(a) can be applied only when there is a failure on the part of the assessee to comply with Chapter XVII-B. However, since the taxpayer had obtained a nil deduction certificate under section 195(2), the taxpayer had complied with the provisions of section 195. Accordingly, the Tribunal held that a disallowance under section 40(a)(i) could not be made in this case.

Finance Ministry to issue Guidance Note on Accounting Standards to be followed for computation of Minimum Alternate Tax

[Excerpts from an article published in The Financial Express, dated 3 September 2015]

The confusion on the accounting standard to be used for determining MAT applicability has cropped up due to the coexistence of multiple accounting standards.

The finance ministry is set to issue a guidance note on what accounting standard should be used by firms to determine whether they are liable to pay 18.5% minimum alternate tax (MAT) on their book profits or not.

Government to announce list of tax exemptions to be phased out to help lower the corporate tax rate starting next year

[Excerpts from an article published in The Indian Express, dated 10 September 2015]

The finance minister, Arun Jaitley, said that the government will start reducing the corporate income tax rate from next year onwards to bring it down from 30% to 25% over a period of four years, in line with the plan announced in the Union Budget 2015-16.

The government will also soon announce the list of exemptions that will be phased out. Mr Jaitley also said that the phasing out of tax exemptions will help simplify tax assessments.

Tax liability of Indian companies increases due to the Income Computation and Disclosure Standards made effective from 1 April 2015

[Excerpts from articles published in The Financial Express, dated 7 September 2015 and in Business Standard, dated 12 September 2015]

The Financial Express has reported that since the Income Computation and Disclosure Standards (ICDS) have been made effective, corporates are finding their flexibility to defer tax outgo has been significantly curtailed. Taxpayers have found that the accounting treatments that they follow in many areas are different compared to the requirements of ICDS. It was also reported that the industry at large is still in the process of understanding the precise impact of the ICDS.

The Business Standard has reported that the tax outgo of Indian companies rose faster than their profit before tax in the quarter ended June this year. Data on the BSE-200 companies show the total tax outgo of the constituents rose by 12.7% during the June quarter whereas their profit before tax rose by 5.6%.

Compliance Calendar (October–December 2015)

Month	Due Date	Compliances
October	7	TDS payment for TDS deducted in September 2015
October	15	TDS statements for the quarter of July to September 2015
October	30	Issuance of TDS certificates for the quarter of July to September 2015
October	31	Submission of Annual Documents to the Department of Scientific and Industrial Research of taxpayers enjoying weighted deduction for Research and Development Expenditure under section 35(2AB) of the ITA
November	7	TDS payment for TDS deducted in October 2015
November	30	Submission of Tax Audit Report for FY 2014-15 for taxpayers to whom Transfer Pricing provisions are applicable
November	30	Submission of Chartered Accountant's certificate in Form 3CEB regarding arm's length nature of international transactions for FY 2014-15
November	30	Submission of Chartered Accountant's certificate in Form 29B certifying the calculation of books profits under Minimum Alternate Tax provisions for taxpayers to whom Transfer Pricing provisions are applicable
November	30	Return of Income for FY 2014-15 for taxpayers to whom Transfer Pricing provisions are applicable
November	30	Return of Wealth for FY 2014-15 for taxpayers to whom Transfer Pricing provisions are applicable
December	7	TDS payment for TDS deducted in November 2015
December	15	Advance tax for third instalment for corporate taxpayers (75% of estimated tax liability to be deposited on cumulative basis)
December	15	Advance tax for second instalment for non-corporate taxpayers (60% of estimated tax liability to be deposited)

Corporate Tax Myth

The Tax Audit Report captures all the adjustments to be made in the computation of taxable income and the return of income can be filed exclusively on the basis of particulars reported in the Tax Audit Report.

If you would like us to help you understand the implications, please write to skptax@skpgroup.com.

About SKP

SKP is a long established and rapidly growing professional services group located in six major cities across India. We specialise in providing sound business and tax guidance and accounting services to international companies that are currently conducting or initiating business in India as well as those expanding overseas. We serve over 1,200 active clients including multinationals, companies listed on exchanges, privately held and family-owned businesses from more than 45 countries.

From consulting on entry strategies to implementing business set-up and M&A transactional support, the SKP team assists clients with assurance, domestic and international tax, transfer pricing, corporate services, and finance and accounting outsourcing matters, all under one roof. Our team is dedicated to ensuring clients receive continuity of support, right across the business lifecycle.

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