



# **International Taxation**

## **ICAI Howrah**



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# Issues on International Taxation





# Why International Taxation

- ◆ Globe is called as Global Village
- ◆ Globalization
- ◆ Movement of People – Concurrent Earnings
- ◆ Borderless Global Economy - Internet
- ◆ Resource of Competent and Enterprising Tax Professionals
- ◆ Movement of Cross Border M & A close to consumers and Virgin Untapped Markets
- ◆ Double Taxation Conflicts



# Why International Taxation

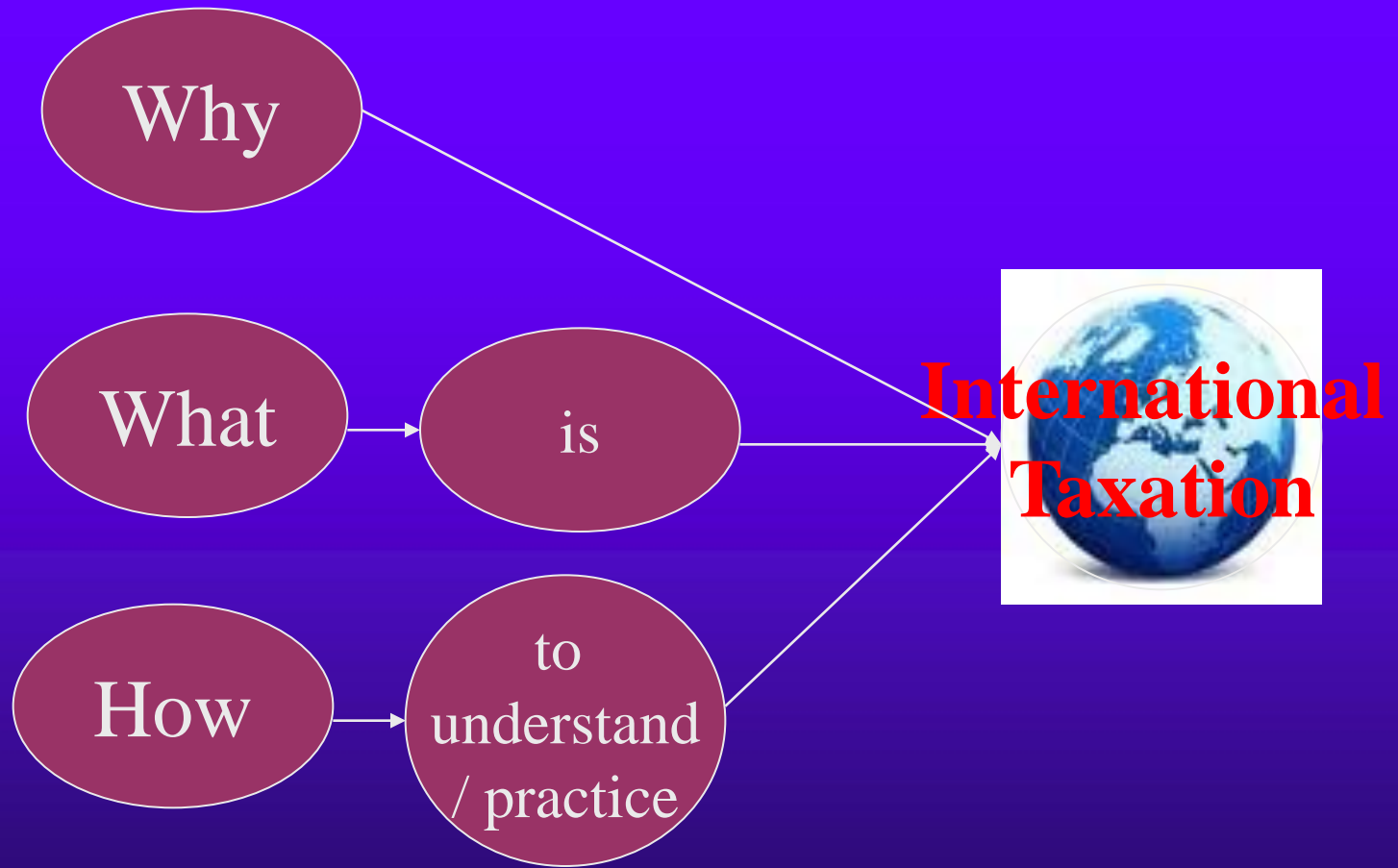
- ◆ **Globalization**
- ◆ **Borderless Global Economy – Internet**
- ◆ **Movement of People – Concurrent Earnings**
- ◆ **Growing Opportunities**
- ◆ **Cross Border M & A**
- ◆ **Growing Opportunities**
- ◆ **Cross Border M & A**
- ◆ **To Define Taxing Rights among the States**
- ◆ **To Avoid Double Taxation Conflict**

# Jurisdiction of Taxation

- ◆ **Source Jurisdiction of Taxation**
- ◆
- ◆ **Residence Jurisdiction of Taxation**



# What we Discuss To-day



# Tax Havens Where Rich Indians Stash Their Money

Rich Indians love to park their wealth offshore, away from the public glare and the scrutiny of Income Tax Department. The Panama Papers Leak is testimony to this fact. Now the world knows how Panama was used by some very influential names across the globe to stash unknown millions. Well, Panama isn't the only tax haven the rich use to hide assets.

Before the leaks, an estimated \$1 trillion of Indian "black" money was believed to be stashed abroad, according to government's estimates. It was more than India's annual GDP. Moreover, only 3% of the population, World Bank estimates show, was actually paying taxes in our country.

Every successive government promises to bring back this black money. The Modi government is hoping to choke India's black-money culture with mandatory tax number declarations for people shopping with large sums, linking biometric identities to every bank account, opening new payment gateways and promoting credit card use, but India's rich still find their ways out, just like they have been for years now. We give you the names of the world's most popular tax havens where the



- Seychelles
- United States
- Switzerland
- Hong Kong
- Cayman Islands
- British Virgin Islands
- Channel Islands
- Cyprus
- Bahamas
- The Netherlands
- Mauritius
- Singapore
- Dubai



# Panama Files

Govt sets up multi-agency body to probe Panama disclosures

» Special Investigation Team (SIT) on black money to also investigate

## THE DISCLOSURES

Over 11.5m documents leaked from law firm Mossack Fonseca based in Panama

The law firm helped set up offshore entities in places like Bahamas & British Virgin Islands

Cases go back almost 40 years

Some could be legal business transactions

## INDIAN CASES

Over 500 Indian names figure in the list



## WHAT NEXT

India is still negotiating an information sharing agreement with Panama

Tax authorities unlikely to get much from Panama

Many offshore entities set up in British Virgin Islands (BVI) & Bahamas

India has an information exchange treaty with BVI

New Delhi had already started receiving information from BVI

It can now seek specific information based on the disclosures

## Our Bureau

**New Delhi:** The government has constituted a multi-agency group to continuously monitor information arising out of disclosures of more than 500 Indian names that used Panama law firm Mossack Fonseca to set up offshore entities, promising action against unlawful accounts.

"The multi-agency group will comprise various government agencies — the CBDT (Central Board of Direct Taxes), FIU (Financial Intelligence Unit), FT&TR (Foreign Tax and Tax Research) and RBI (Reserve Bank of India). They will continuously monitor these (accounts) and whichever accounts are found to be un-

shore companies" in some cases.

The global list includes political leaders, celebrities and prominent sports persons.

Many countries including Australia and New Zealand have also announced investigations.

"I welcome this investigation. I think it is a healthy step that these kind of exposures are being made. I have been repeatedly saying that the world is now going to increasingly become more transparent, countries are cooperating with each other and slowly all this information is going to come out as a result of various global initiatives which have been launched," Jaitley said.

SIT chairman MR Shah said it will look



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# What is Globalization ?

Globalization is the phenomenon of

- ◆ Sourcing Capital from where it is cheapest,
- ◆ Sourcing People from where it is best available,
- ◆ Producing where it is most Cost Effective and
- ◆ Selling where there is Market for.

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# Double Taxation Conflicts

- ◆ Residence rule due to personal attachment – protection to person etc
- ◆ Source rule due to economic attachment – economic activities within that country
- ◆ Primary right should be on the activity –if all states practice territorial tax no issue- many states follow right to tax worldwide income of their residents



# Double Taxation Conflicts

- ◆ Double Tax is built in the system as part of the Classical tax system of respective country
- ◆ Double Tax is harmful for international trade



# Double Taxation Conflicts

## ◆ Types of Conflicts -

- \* Source-Source conflicts
- \* Residence-Residence conflicts
- \* Residence – Source conflicts
- \* Income characterization conflict
- \* Entity conflicts
- \* Mismatching Tax systems (taxable income and computation of taxes)



# Double Taxation Conflicts Resolution

## ◆ Bilateral Relief

- Negotiated sharing of the tax revenues by two countries sought
  - Developed countries usually have balanced sharing of tax revenues
  - Developing countries may have unbalanced sharing as they are governed by economic, social as well as revenue considerations

## ◆ Unilateral Relief

- Section 91 of the Act



# What is International Taxation

- ◆ Purpose of International Taxation
- ◆ Objectives of International Taxation
- ◆ Legislation of International Taxation





# Purpose of International Taxation

- ◆ Taxing Residents World-Wide Income
- ◆ Taxing Non-Residents National Income

# Purpose of International Taxation



## India

Mr. Patel -  
Indian Resident.  
Indian Income  
Rs. 1,000.

Mr. Smith -  
Indian Interest  
Income Rs. 200.

## Germany

Mr. Patel -  
German Interest  
Income Rs.100.

Mr. Smith -  
German Resident.  
German Income  
Rs. 2,000.

INDIA would want to tax Mr. Patel	Amount (in Rs.)
On his Indian Income – On Source + Residence Basis	1,000
German Income - On Residence Basis	100
Sub Total	1,100
<b>India would also tax Mr. Smith</b>	
on his Indian Interest income on Source Basis	200
Total	1,300

# Purpose of International Taxation

<b>Germany would tax Mr. Smith</b>	<b>Amount (in Rs.)</b>
<b>On his German Income on Source + Residence Basis</b>	<b>2,000</b>
<b>On his Indian Income on Residence Basis</b>	<b>200</b>
<b>Total</b>	<b>2,200</b>
<b>Germany would tax Mr. Patel</b>	
<b>On his German Income on Source Basis</b>	<b>100</b>
<b>Total</b>	<b>2,300</b>
<b>Thus – Domestic Income by a resident causes no problems of Double tax.</b>	<b>Rs. [3,000]</b>
<b>Only when a resident of one country gets income from another country, Double tax issues arise</b>	<b>Rs. [300]</b>

# INVESTMENTS OPPORTUNITIES IN AND FROM INDIA

## Tax Imperatives



# TAX TRANSACTION IMPERATIVES

# INVESTMENTS OPPORTUNITIES IN AND FROM INDIA

## TRANSACTION IMPERATIVES



Business Environment

Cultural Issues

Accounting treatment

Inbound Investments

Legal & regulatory framework

Tax regimes & treaties

Identifying and delivering synergies

Business Dynamics



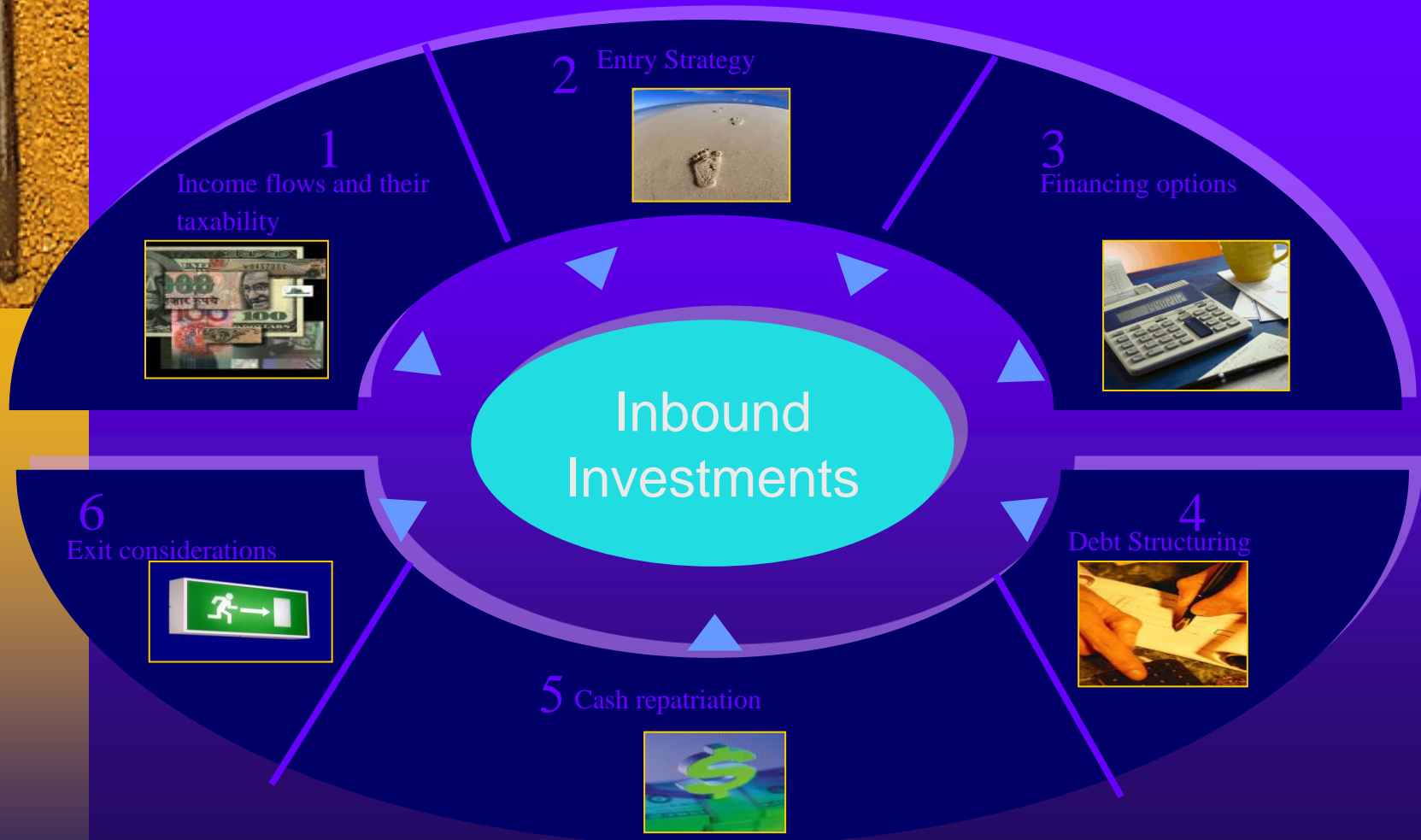
# INVESTMENTS OPPORTUNITIES IN AND FROM INDIA



INDIA INBOUND  
INVESTMENT KEY  
CONSIDERATIONS

# INVESTMENTS OPPORTUNITIES IN AND FROM INDIA

## KEY TAX AND FINANCIAL CONSIDERATIONS



## INDIA INBOUND INVESTMENT STRUCTURES - PRINCIPLES

- Simple to set up and administer
- Minimal ongoing compliance
- Investor friendly
- Upfront addresses the tax planning for future exit
- Ease of winding up
- Overall, is based on sound tax and regulatory positions





# INDIA INBOUND INVESTMENT STRUCTURES - PRINCIPLES

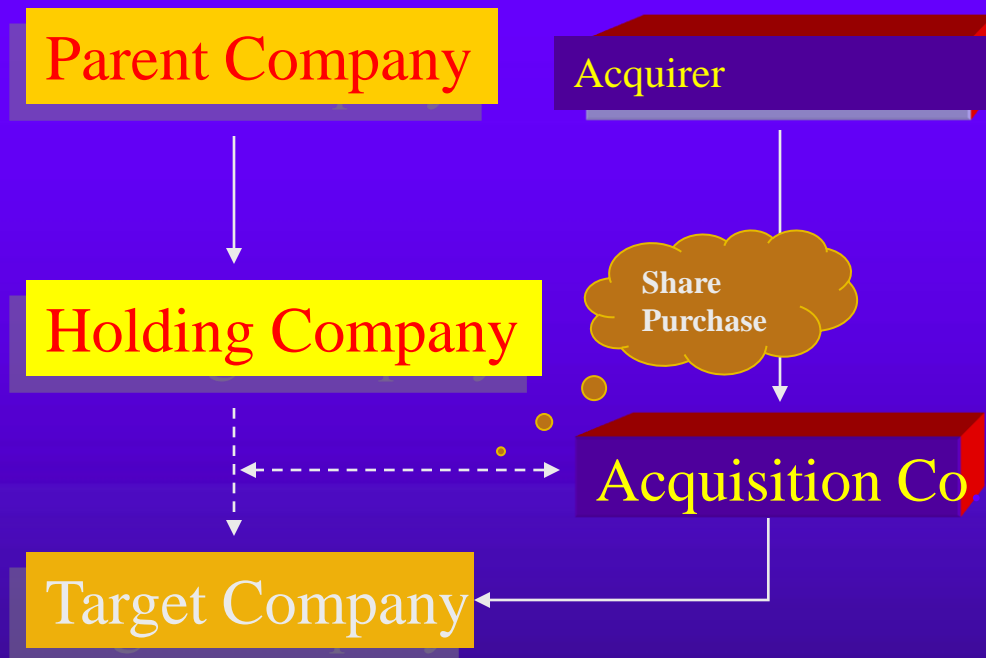


## Share Purchase

### Target Structure



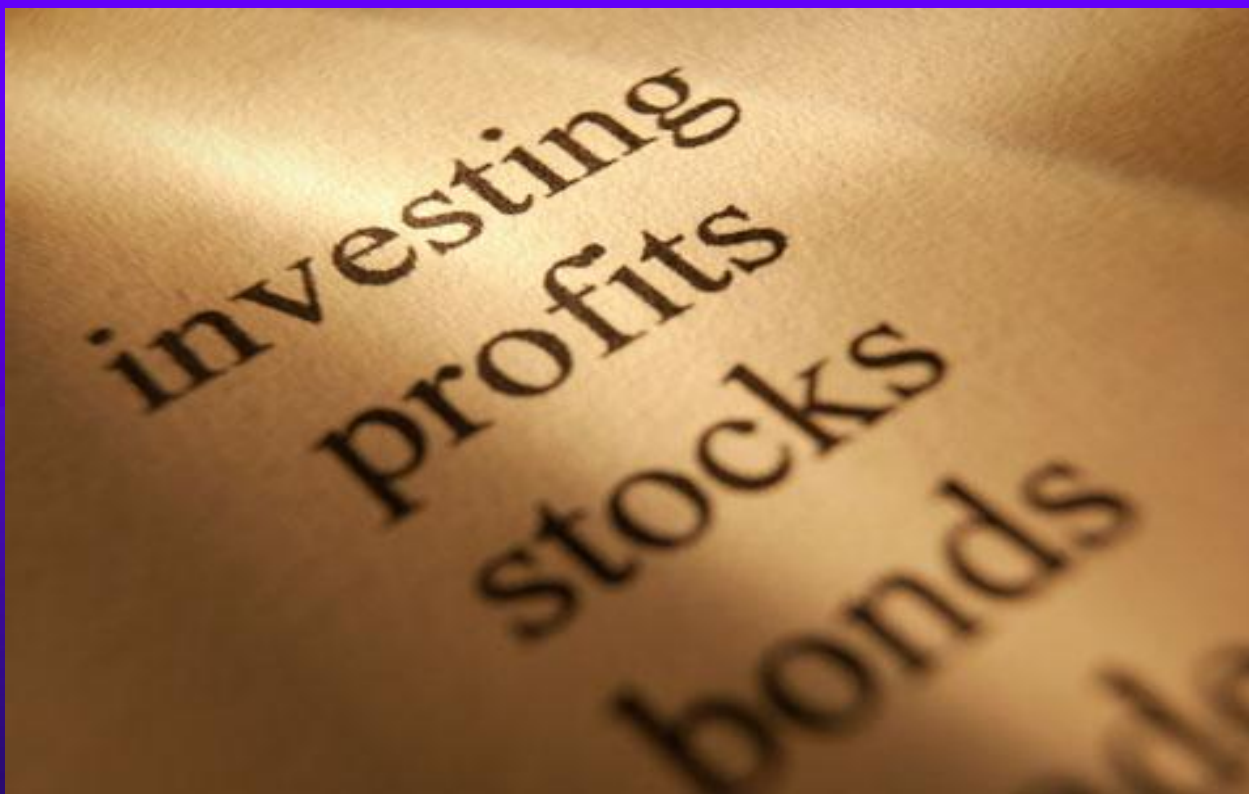
### Acquisition Structure



- Acquirer purchases shares in **Target Company** from **Holding Company** for cash consideration
- **Target Company** becomes a **100% subsidiary** of Acquirer



# INVESTMENT & TAX DECISIONS



# Tax Treaties - Objectives





# Tax Treaties - Formation

## ◆ Formation of Tax Treaties –

A DTA develops in six stages, which follow a fairly well established procedure

- (1) Negotiation
- (2) Initialling
- (3) Signature
- (4) Ratification
- (5) Entry into force
- (6) Effective Date



# Tax Treaties - Types

## ◆ Types of Tax Treaties –

Comprehensive Agreements – This is wider in scope addressing all sources of income.

Limited Agreements – which has limited scope and covers

- a) **income from operation of aircrafts and ships,**
- b) **estates,**
- c) **inheritance and**
- d) **gifts.**



# Concepts of International Taxation

- ◆ Controlled Foreign Companies { CFC } –

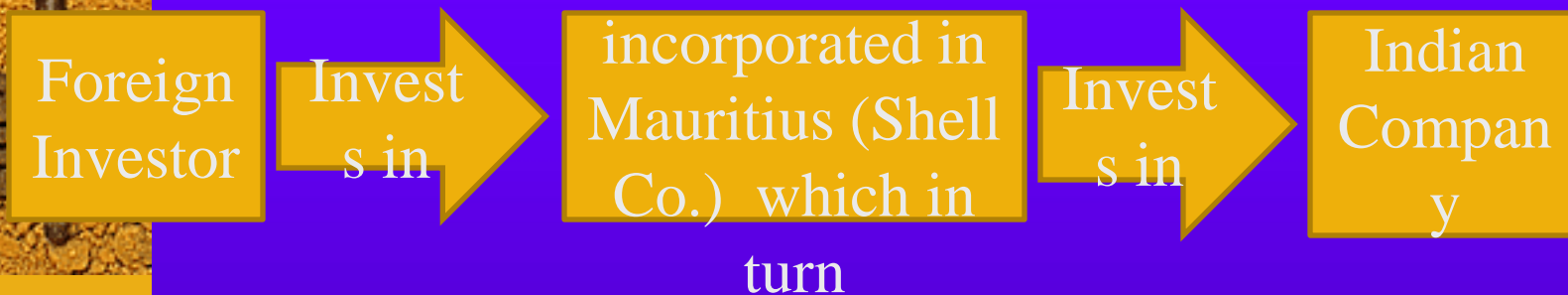
This is a legislation to tax foreign sourced income on an accrual basis, instead of on a receipt basis

To explain – for eg. Company P (Parent Co.) a resident in Country R incorporates a subsidiary (Company S) in a tax heaven country. Income is diverted to Co., S. To avoid this circumstances, Country R may tax Co., P for income earned by Company S.

# Concepts of International Taxation

## • Treaty Shopping -

What does it Mean?



Tax Evasion Vs Tax Avoidance

*“There are many principles in fiscal economy which, though at first blush might appear to be evil, are tolerated in a developing economy, in the interest of long term development.”*





# INTRODUCTION

## *RELEVANCE :*

### ◆ Revenue Authorities :


Obtain fair share of revenue in respect of economic activities carried within its jurisdiction

### ◆ Management:

Decision making, group's performance evaluation, fair profit of an enterprise, etc

# Global TP Rules & Enforcement

1996 & Prior	1997/1998	1999/2000	2001/2002	2003/2004	2005/2006
Japan					
Italy					
New Zealand					
Mexico					
Korea					
France					
Czech Republic					
Spain					
Australia					
South Africa					
USA					
	China				
	Slovakia				
	Brazil				
	Japan				
	Italy				
	New Zealand				
	Mexico				
	Korea				
	France				
	Czech Republic				
	Spain				
	Australia				
	South Africa				
	USA				
		Germany			
		Kazakhstan			
		Russia			
		Denmark			
		Belgium			
		Venezuela			
		Argentina			
		Canada			
		UK			
		China			
		Slovakia			
		Brazil			
		Japan			
		Italy			
		New Zealand			
		Mexico			
		Korea			
		France			
		Czech Republic			
		Spain			
		Australia			
		South Africa			
		USA			
			Thailand		
			Portugal		
			Poland		
			Peru		
			India		
			Netherlands		
			Germany		
			Kazakhstan		
			Russia		
			Denmark		
			Belgium		
			Venezuela		
			Argentina		
			Canada		
			UK		
			China		
			Slovakia		
			Brazil		
			Japan		
			Italy		
			New Zealand		
			Mexico		
			Korea		
			France		
			Czech Republic		
			Spain		
			Australia		
			South Africa		
			USA		
				Hungary	
				Colombia	
				Malaysia	
				Thailand	
				Portugal	
				Poland	
				Peru	
				India	
				Netherlands	
				Germany	
				Kazakhstan	
				Russia	
				Denmark	
				Belgium	
				Venezuela	
				Argentina	
				Canada	
				UK	
				China	
				Slovakia	
				Brazil	
				Japan	
				Italy	
				New Zealand	
				Mexico	
				Korea	
				France	
				Czech Republic	
				Spain	
				Australia	
				South Africa	
				USA	



# INDIAN TRANSFER PRICING REGULATION : A BIRD'S EYE VIEW

- ◆ Chapter X –Special provision relating to avoidance of tax (prior to 1.4.2002 – section 92)
- ◆ Pre TPR provisions – Section 40A(2), Section 10A/B , Section 80 IA
- ◆ Based on Raj Narain committee – Finance Act 2001 incorporated detailed TP provisions in INCOME TAX ACT,1961
- ◆ CBDT has set up new post of Director General , International Tax














## Types of transactions considered appropriate for adoption of TNMM

- ◆ Provision of services
- ◆ Distribution of finished products where resale price method cannot be adequately applied
- ◆ Transfer of semi finished goods

In India, in majority cases, method selection process would lead to selection of TNMM as MAM, due to Non Availability of requisite data for other methods.

# Computation Related Documents

Degree of Similarity Required Under Various Methods:

Methods to be used	PRODUCT	FUNCTIONS	RESOURCES	RISKS	COMPLEXITY
CUP					
CPLM/RPM					
TNMM					
PSM					

# Computation Related Documents

## Degree of Similarity Required Under Various Methods (Contd.):

- CUP - High comparability of Products and Risks.
- CPLM and RPM – High comparability of Functions and Risks.
- TNMM – High Comparability of Risk and Resources. Functions also important.
- PSM – Exceptionally used in complex cases, such as presence of intangibles.

In India, in majority cases, method selection process would lead to selection of TNMM as MAM, due to Non Availability of requisite data in other methods.



***Most appropriated method ( MAM) for ALP***  
**Factors for Selection of MAM [Rule 10C R.W. S. 92C]:**

*Rule 10C provides for following factors for selecting MAM:*

- Nature of International Transaction
- Class of Associated Enterprise  
(e.g. Distributor, Contract Mfgr. Etc.)
- Functions Performed, Assets Employed, Risks Assumed.
- Availability, Coverage and Reliability of Data
- Extent to Which Reliable and Accurate ,Adjustments Can Be Made.
- Nature, Extent and Reliability of Assumptions Required.

**Most Appropriate Method must be Reliable Measure of ALP**



# Most appropriate Method - Rule 10C

In selecting the most appropriate method as specified in sub-rule (1) of Rule 10 C, the

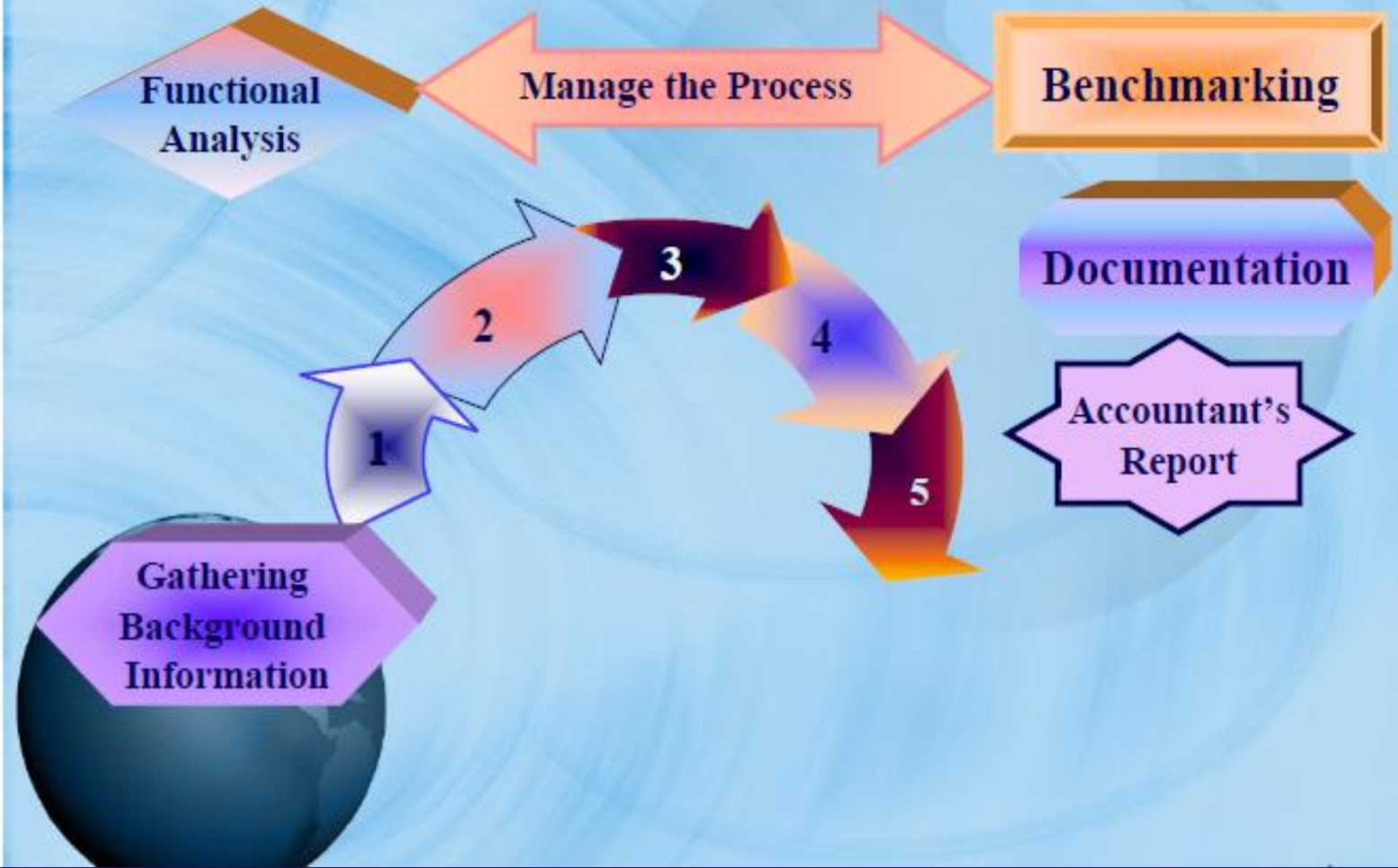
following factors shall be taken into account, namely:—

- the nature and class of the international transaction;
- the class or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises;
- the availability, coverage and reliability of data necessary for application of the method;
- the degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions;
- the extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction and the comparable uncontrolled transaction or between the enterprises entering into such transactions;
- the nature, extent and reliability of assumptions required to be made in application of a method.





# Transfer Pricing Process



# Practical issues in TNMM – Search process

## ◆ Secondary filters

- Salary costs being  $< 25\%$
- R & D costs greater than  $5\%$
- Forex filter
- Trading activity filter
- Asset filter when assets  $>$  revenues

**THANKS**

A scenic view of a body of water at sunset or sunrise, with a curved pier in the foreground and mountains in the distance. The sky is filled with soft, golden light, and the water reflects the warm tones. The pier is dark and curves from the bottom right towards the center. In the far distance, a range of mountains is visible under the hazy sky.