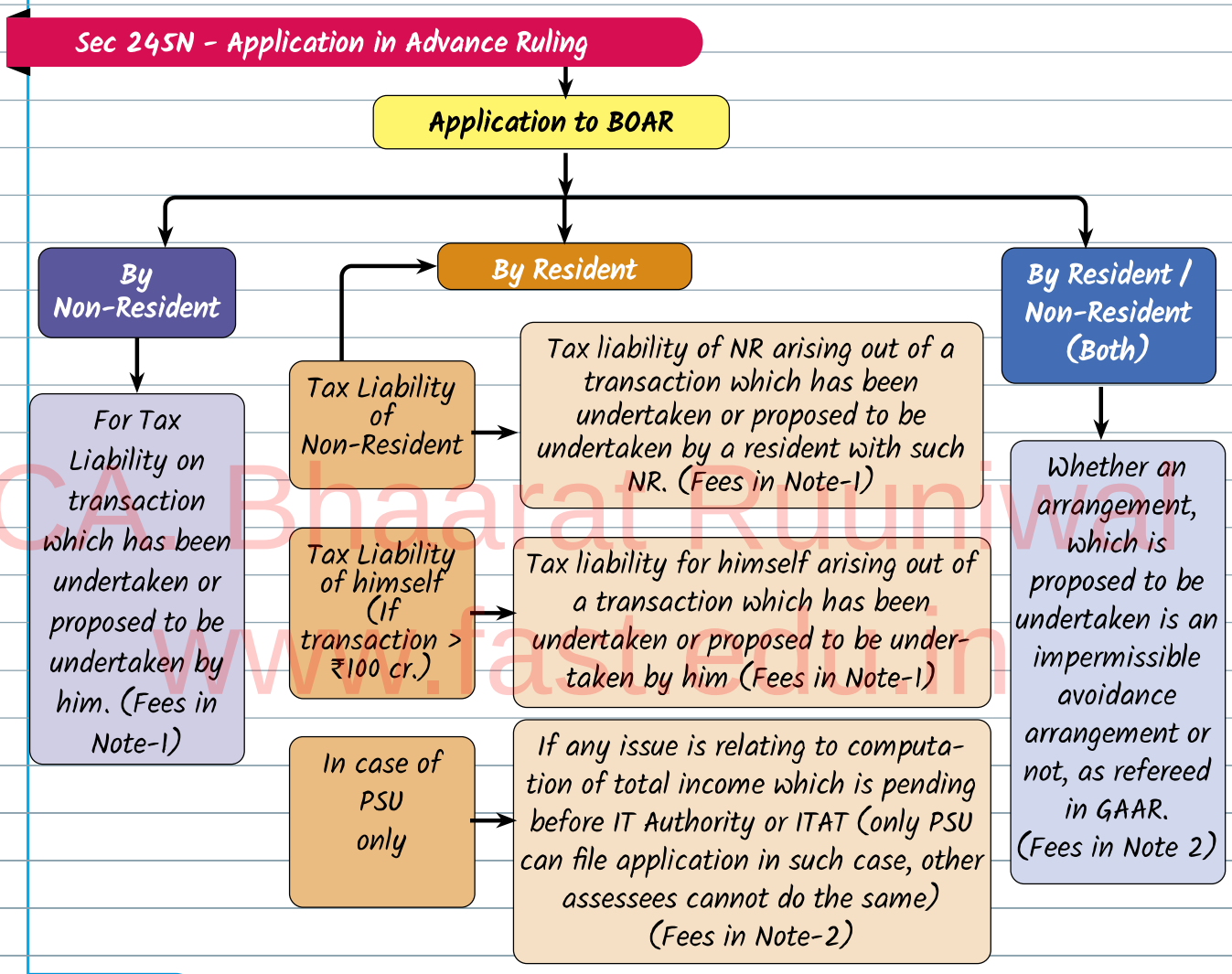
Taxation of Business Process Outsourcing Units in India (Circular No. 05/2004 dated 28.09.2004)

1. A non-resident entity may outsource certain services to a resident Indian entity. If there is no business connection between the two, the resident entity may not be a Permanent Establishment of the non-resident entity, and the resident entity would have to be assessed to income-tax as a separate entity. In such a case, the non-resident entity will not be liable under the Income Tax Act, 1961.
2. However, it is possible that the non-resident entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the Permanent Establishment of the non-resident entity.
3. The non-resident entity or the foreign company will be liable to tax in India only if the IT enabled BPO unit in India constitutes its Permanent Establishment.
4. A non-resident or a foreign company is treated as having a Permanent Establishment in India if the said non-resident or foreign company carries on business in India through a branch, sales office, etc. or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts or regularly delivers goods or merchandise or habitually secures orders on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India by the Permanent Establishment becomes taxable in India.
5. If BPO units becomes Permanent Establishment in India then profit attributed to such Permanent Establishment will be taxed in India. Profits are to be attributed to the Permanent Establishment as if it were a distinct and separate enterprise and dealing wholly independently with the enterprise of which it is a Permanent Establishment.
6. Price of the services rendered by the Permanent Establishment to the Head Office or by the Head Office to the Permanent Establishment on the basis of "Arm's Length principle".

ADVANCE RULING

In Advance Ruling, assessee makes an application to the BOAR (Board of Advance Rulings) and BOAR will give it's ruling (decision/ judgment) in relation to such transaction, which has been undertaken or proposed to be undertaken by the assessee (whether it is a question of law or a question of fact).



Note 1 Fees (along with application) as per Sec 245Q will be

- Transaction upto ₹100 cr. ₹2,00,000
- Transaction > ₹100 cr. but upto ₹300 cr. ₹5,00,000
- Transaction > ₹300 cr. ₹10,00,000

Note 2 Fees (along with application) as per sec 245Q will be 10,000

Note 3 Application can be withdrawn within 30 days from the date of application (after 30 days it can be withdrawn by the applicant if BOAR permit the same – M.K. Jain vs HC)

Note 4- If any issue is relating to computation of total income which is pending before IT Authority or ITAT then no one can file application with BOAR except PSU.

Note 5- Application shall be made in prescribed form (Quadruplicate) & accompanied by prescribed fees.

Sec 245R - Procedure on receipt of application

1. Forward the copy to CIT/PCIT and call upon relevant records (if required)-
On receipt of application, BOAR will forward the copy of application to CIT/PCIT and if necessary, call upon him to furnish relevant records.

2. Action (Accept/Rejection) on application-
After examining the application or records, BOAR may either allow or reject the application but in following cases BOAR will not accept the application-

   i. If any issue is already pending before IT Authority or ITAT (except for PSU)
   However, if any issue is pending before HC/SC then PSU also cannot make an application before the authority)

   ii. Determination of FMV of any property

   iii. Transaction which is designed prima facie for avoidance of tax. (except application which is made by PSU or in relation to a transaction is an impermissible avoidance arragement)

An Opportunity of being heard (OBH) will be given to the applicant before the application is rejected.

3. ***Pronouncement of Ruling-***
If application is allowed then BOAR will pronounce its ruling within 6 months from the date of receipt of application (copy of ruling / judgment will be forwarded to the assessee and CIT/PCIT).

Special Notes

1. The Central Government may, by notification in the Official Gazette, make scheme for the purposes of giving advance rulings under this Chapter by the Board for Ad vance Rulings, so as to impart greater efficiency, transparency and accountability by -

   i. Eliminating the interface between the Board for Advance Rulings and the applicant in the course of proceedings to the extent technologically feasible;

   ii. Optimising utilisation of the resources through economies of scale and functional specialisation;

   iii. Introducing a system with dynamic jurisdiction.

2. Prior to amendments by Finance Act, 2021, the order of Advance Ruling was binding on the assessee as well as the Department. HOWEVER, FINANCE ACT, 2021 has deleted this provision AND THEREFORE AFTER THE AMENDMENTS MADE BY FINANCE ACT, 2021 the OR DER OF BOARD FOR ADVANCE RULINGS (BOAR) SHALL NIETHER BE BINDING ON THE ASSESSEE NOR BE BINDING ON THE INCOME TAX DEPARTMENT. Assessee / Income tax department can file an appeal to High Court against the order of Board for Advance Rulings (BOAR).

SECTION 245RR - Income Tax Appellate Authority Not to Proceed in Certain Cases

No Income-tax Authority or the Appellate Tribunal shall proceed to decide any issue in respect of which an application has been made by an applicant. It shall wait for the decision of BOAR.

SECTION 245W - Appeal to High Court

1. The applicant, if aggrieved by any ruling pronounced or order passed by the Board for Advance Ruling or the Assessing Officer, on the directions of the Principal Commissioner or Commissioner, may appeal to the High Court against such ruling or order of the Board for Advance Rulings within sixty days from the date of the communication of that ruling or order, in such form and manner, as may be prescribed.

   Provided that where the High Court is satisfied, on an application made by the appellant in this behalf, that the appellant was prevented by sufficient cause from presenting the appeal within the period specified in sub-section (1), it may grant further period of thirty days for filing such appeal.

2. The Central Government may make a scheme, by notification in the Official Gazette, for the purpose of filing appeal to the High Court under sub-section (1) by the Assessing Officer so as to impart greater efficiency, transparency and accountability by-

   a. Optimising utilisation of the resources through economies of scale and functional specialisation;

   b. Introducing a team-based mechanism with dynamic jurisdiction.

SECTION 245T- Advance Ruling to be void in certain circumstances

Where the **Board for Advance Rulings (BOAR)** finds, on a representation made to it by the Principal Commissioner or Commissioner or otherwise, that an advance ruling pronounced by it has been obtained by the applicant by fraud or misrepresentation of facts, it may by order declare such ruling to **be void-ab-initio.** Therefore, all the provisions of the Act apply (after excluding the period beginning with the date of such advance ruling and ending with the date of the order declaring the advance ruling as void) to the applicant as if that advance ruling had never been made.

Sec.245-OB – Constitution of Board for Advance Rulings

The Central Government shall constitute one or more Boards for Advance Rulings for giving advance rulings under this chapter.

Accordingly, vide notification no. 96/2021 dated 01.09.2021, Central Government has constituted three Boards for Advance Rulings- Board for Advance Ruling-I and Board for Advance Ruling-II having headquarters in Delhi and Board for Advance Ruling-III having headquarter in Mumbai.

The BOAR shall consist of two members, each being an officer not below the rank of Chief Commissioner, as may be nominated by the Board.

Sec. 245P- Vacancies, etc. not to invalidate proceedings

Any proceeding before or pronouncement of advance ruling by, the BOAR shall not be questioned or be invalid on the ground merely by the existence of any vacancy or defect in the constitution of the BOAR.

Special Note- As per Explanation 1 to Sec. 153

In computing period of limitation for making assessment or reassessment, following time period shall be excluded from the time period referred to in section 153:

The period commencing from the date on which an application is made before the BOAR under section 245Q and ending on the date on which-

- the order of REJECTING the application; or
- the Advance Ruling PRONOUNCED by BOAR

is received by CIT under section 245R.

Eg.1 Assessment for the Year 2021-22, the assessee made an application to Board for Advance Ruling on 1.12.2021. The BOAR pronounces its Advance Ruling on 30.04.2022 and the Advance Ruling is received by the CIT on 31.05.2022. Upto what time can the Assessing Officer complete the assessment.

Answer Assessment for the Assessment Year 2021-22 can be completed under section 143(3) upto 31.12.2022 + (1.12.2021 to 31.05.2022) i.e. 182 days = 01.07.2023

Eg.2 BRO & Co. filed an application for advance ruling for the A.Ys. 2020-21, 2021-22 and 2022-23 with the Board for Advance Ruling (BOAR). For the assessment years 2020 21 and 2021-22, notice under section 143(2) was issued to the assessee and subsequently, before the date of filing application with BOAR, notice under section 142(1) along with questionnaire was also issued. For the assessment year 2022-23, notice under section 143(2) was issued before the date of filing of application with the BOAR and notice under section 142(1) along with questionnaire was served on the assessee after the date of filing of application with the BOAR. Can the BOAR reject the application on the ground that proceedings are already pending?

Answer The facts of the case are similar to the facts in Hyosung Corporation v. AAR (now BOAR) (2016), wherein the above issue came up before the Delhi High Court. The Court observed that mere issue of notice under section 143(2) in pre-printed format will not amount to proceedings pending for the purpose of applying the proviso to section 245R(2). However, issue of notice under section 142(1) accompanied by a questionnaire before filing of the application by the assessee with the BOAR would tantamount to proceedings pending before an income-tax authority.

Thus, applying the rationale of the Delhi High Court ruling to the case on hand, the application for the assessment year 2022-23 cannot be rejected by the BOAR since notice under section 142(1) issued for the assessment year 2022-23 after the date of filing of application will not result in the proceedings being 'already pending' before an Income-tax authority.

However, for the assessment years 2020-21 and 2021-22, the rejection of the application by BOAR is tenable in law, since notice under section 142(1) along with detailed questionnaire was issued before the date of filing of such application.

CBDT notifies E-Advance Rulings Scheme 2022

The Central Board of Direct Taxes (CBDT) notifies E-Advance Ruling Scheme 2022 vide Notification No. 07/2022 dated 18th January 2022.

The Notification is Given Below :

S.O. 248(E). In exercise of the powers conferred by sub-sections (9) and (10) of section 245R and subsections (2) and (3) of section 245W of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby makes the following Scheme, namely-

1 **Short title and commencement.**

(1) This Scheme may be called the "e-advance rulings Scheme, 2022".

(2) It shall come into force on the date of its publication in the Official Gazette.

2 **Scope of the Scheme.**

This Scheme shall be applicable to applications of advance rulings,-

(a) made to the Board for Advance Rulings under sub-section (1) of section 245Q of the Act; or

(b) transferred to Board for Advance Rulings under sub-section (4) of section 245Q of the Act.

3 **E-advance rulings by Board for Advance Rulings.-**

1 The Board for Advance Rulings shall pronounce eadvance rulings of applications allocated or transferred to it under paragraph 5, in accordance with the provisions of this Scheme;

2 The Board for Advance Rulings shall have such other income-tax Authority, ministerial staff, executive or consultant to assist the members of the Board for Advance Rulings, as considered necessary by the Central Board of Direct Taxes.

4 **Allocation of applications for advance ruling.-**

The Principal Director General of Income-tax (Systems) or the Director General of Income tax (Systems), as the case may be, shall, with the approval of the Central Board of Direct Taxes, devise a process to randomly allocate or transfer the applications for advance ruling, referred to in paragraph 3, to the Board for Advance Rulings through an automated allocation system.

5 **Submission of additional facts before the Board for Advance Rulings.**

(1) The Board for Advance Rulings may at its discretion permit or require the applicant to submit such additional facts as may be necessary to enable it to pronounce its advance ruling.

(2) Where in the course of the proceedings before the Board for Advance Rulings, a fact is alleged which cannot be borne out by, or is contrary to, the record, it shall be stated clearly and concisely and supported by a duly sworn affidavit.

6 **Questions contained in the application.**

The applicant shall not, except by leave of the Board for Advance Rulings, urge or be heard in support of any additional question not set forth in the application, but in deciding the application the Board for Advance Rulings shall, at its discretion, consider all aspects of the questions set forth as may be necessary to pronounce a ruling on the substance of the questions posed for its consideration.

7 **Verification of additional facts**

Where in the course of any proceedings before the Board for Advance Rulings any fact not contained in the application for advance ruling (including the annexure and the statements and other documents accompanying such annexure), referred to in paragraph 3, are sought to be relied upon, they shall be submitted to the Board for Advance Rulings in writing and shall be verified in the same manner as provided for in such application.

Notes

Equalisation Levy

The key aspects related to Equalisation Levy have been discussed below.

1 Meaning of "Equalisation Levy" [Section 164(d) of the Finance Act, 2016]

Equalisation levy means the tax leviable on consideration received or receivable for any specified service or e-commerce supply or services.

2 Charge of Equalisation Levy on 'Specified Services' [Section 165 of Finance Act, 2016]

(i) Equalisation levy @ 6% is leviable on the amount of consideration for specified service received or receivable by a person, being a non-resident from -

a. a person resident in India and carrying on business or profession; or
b. a non-resident having a PE in India.

(ii) Equalisation levy is not chargeable, where –

a. the non-resident providing the specified service has a PE in India and the specified service is effectively connected with such PE;
b. the aggregate amount of consideration for specified service received or receivable in a previous year by the non-resident from a person resident in India and carrying on business or profession, or from a non-resident having a PE in India, does not exceed ₹ 1 lakh; or
c. where the payment for the specified service by the person resident in India, or the PE in India is not for the purposes of carrying out business or profession.

3 Charge of Equalization levy on E-commerce supply or services [Section 165A of the Finance Act, 2016]

(i) **Chargeability of Equalization levy on E-commerce supply or services-**

Equalization levy @ 2% would be chargeable on the amount of consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated by it—

1. to a person resident in India; or
2. to a non-resident in the specified circumstances as provided below; or
3. to a person who buys such goods or services or both using internet protocol address located in India.

(ii) **Non-chargeability of equalization levy- The equalization levy shall not be charged—**

1. where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such PE;
2. where the equalization levy is leviable under section 165;
3. sales, turnover or gross receipts, as the case may be, of the e-commerce operator from the e-commerce supply or services made or provided or facilitated is less than ₹ 2 cr. during the previous year.

(iii) **Meaning of "specified circumstances"-**

1. sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement through internet protocol address located in India; and
2. sale of data, collected from a person who is resident in India or from a person who uses internet protocol address located in India.

(iv) **"Consideration received or receivable from e-commerce supply or services" would include-**

1. consideration for sale of goods irrespective of whether the e-commerce operator owns the goods. However, it shall not include consideration for sale of such goods which are owned by a person resident in India or by a permanent establishment in India of a person non-resident in India, if sale of such goods is effectively connected with such permanent establishment;
2. consideration for provision of services irrespective of whether service is provided or facilitated by the e-commerce operator. However, it shall not include consideration for provision of services which are provided by a person resident in India or by permanent establishment in India of a person non- resident in India, if provision of such services is effectively connected with such permanent establishment.

(a) Definition of "Specified Service", "E-Commerce Operator" and "E-Commerce Supply or Services" [Section 164 of the Finance Act, 2016]

	Term	Meaning
(i)	Specified Services	(i) Online advertisement; (ii) Any provision for digital advertising space or any other facility or service for the purpose of online advertisement; (iii) Any other service as may be notified by the Central Government. Note – 'Online' means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network.
(ii)	E-Commerce Operator	A non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both
(iii)	E-Commerce Supply or Services	(i) online sale of goods owned by the e-commerce operator; or (ii) online provision of services provided by the e- commerce operator; or (iii) online sale of goods or provision of services or both, facilitated by the e-commerce operator; or (iv) any combination of activities listed in (i), (ii) or (iii) above. "Online sale of goods" and "online provision of services" would include one or more of the following online activities (a) acceptance of offer for sale; or (b) placing of purchase order; or (c) acceptance of the purchase order; or (d) payment of consideration; or (e) supply of goods or provision of services, partly or wholly.

4 Provisions of Chapter on Equalisation Levy-

Section	Subject	Provisions
166	**Collection & Recovery of Equalisation Levy on Specified Services**	
	Person responsible for deduction of equalisation levy	Every person, being a resident and carrying on business or profession or a non-resident having a permanent establishment in India shall deduct equalisation levy referred to in section 165(1) from the amount paid or payable to a non-resident in respect of the specified service.
	Rate of Equalisation levy for deduction of equalisation levy	6% of the amount of consideration for specified service paid or payable to a non-resident in respect of specified service by a person resident in India and carrying on business or profession or a non-resident having a PE in India.
		The amount of consideration, the amount of equalisation levy, interest and penalty payable and refund shall be rounded off to the nearest multiple of ten rupees. For this purpose, any part of a rupee consisting of paise shall be ignored and, thereafter, if such amount is not a multiple of ten, then, if the last figure in that amount is five or more, the amount shall be increased to the next higher amount which is a multiple of ten and if the last figure is less than five, the amount shall be reduced to the next lower amount which is a multiple of ten [Rule 3 of Equalisation Levy Rules, 2016].
	Threshold limit	Equalisation levy is deductible if the aggregate amount of consideration for specified service in a previous year exceeds one lakh rupees

Section	Subject	Provisions
	Time period for remittance of equalisation levy	The equalisation levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government by the 7th of the month immediately following the said calendar month. The assessee who is required to deduct and pay equalisation levy, shall pay the amount of such levy, by remitting it into the Reserve Bank of India or in any branch of the State Bank of India or of any authorised Bank accompanied by an equalisation levy challan. [Rule 4 of Equalisation Levy Rules, 2016]
	Consequence of failure to deduct equalisation levy	Any assessee who fails to deduct equalisation levy shall, notwithstanding such failure, be liable to pay the levy to the credit of the Central Government by the 7th of the month immediately following the said calendar month. Thus, if the assessee responsible for deducting equalisation levy, fails to so deduct, he has, in any case, to pay such levy to the credit of the Central Government by the 7th of the month immediately following the said calendar month.
166A	Collection and recovery equalisation levy on e-commerce supply or services	The equalisation levy referred to in section 165A(1), has to be paid by every e-commerce operator to the credit of the Central Government for the quarter of the financial year ending with the date specified in column (2) of the Table below by the due date specified in the corresponding entry in column (3) of the said Table-

S. No.	Date of ending of the quarter of the F.Y	Due date of the F.Y
(1)	30th June	7th July
(2)	30th September	7th October
(3)	31st December	7th January
(4)	31st March	31st March

Section	Subject	Provisions
		The amount of consideration, the amount of equalisation levy, interest and penalty payable and refund shall be rounded off to the nearest multiple of ten rupees. For this purpose, any part of a rupee consisting of paise shall be ignored and, thereafter, if such amount is not a multiple of ten, then, if the last figure in that amount is five or more, the amount shall be increased to the next higher amount which is a multiple of ten and if the last figure is less than five, the amount shall be reduced to the next lower amount which is a multiple of ten [Rule 3 of Equalisation Levy Rules, 2016 as amended by the Equalisation Levy (Amendment) Rules, 2020]. The e-commerce operator who is required to pay equalisation levy, shall pay the amount of such levy, by remitting it into the Reserve Bank of India or in any branch of the State Bank of India or of any authorised Bank accompanied by an equalisation levy challan [Rule 4 of Equalisation Levy Rules, 2016, as amended by the Equalisation Levy (Amendment) Rules, 2020].

Points of difference between Section 166 and 166A

- **As per section 166** – Equalisation Levy on Specified Services, the person responsible for collecting the levy is the service recipient availing the specified service(s), who has to deduct Equalisation Levy from the amount paid or payable to a non-resident in respect of such service(s). The service recipient responsible for deduction and remittance is a resident or a non-resident having PE in India.
- **As per section 166A** – Equalisation Levy on e-commerce supply or services, the person responsible for collecting the levy is the recipient of the amount, in case of an e-commerce operator effecting online sale of goods owned by him or online provision of services. There is no deduction obligation on the part of the service recipient/ buyer, in this case. Therefore, in this case, the responsibility for payment of equalisation levy is vested on the non-resident e-commerce operator who does not have a PE in India.

Section	Subject	Provisions
167	**Furnishing of statement**	
	Statement in prescribed form within time	Every assessee or e-commerce operator shall, within the prescribed time after the end of each financial year, prepare and deliver or cause to be delivered to the Assessing Officer or to any other authority or agency authorised by the Board in this behalf, a statement in the prescribed form, verified in the prescribed manner and setting forth the prescribed particulars in respect of all specified services or e-commerce supply or services, as the case may be, during such financial year. The statement in respect of all specified services/ e- commerce supply or services, as the case may be, chargeable to equalisation levy during any financial year is required to be furnished electronically under digital signature or electronically through electronic verification code in Form No. 1, duly verified, on or before 30th June immediately following that financial year [Rule 5 of Equalisation Levy Rules, 2016 as amended by the Equalisation Levy (Amendment) Rules, 2020]
	Time limit for for filing a revised statement	An assessee or e-commerce operator who has not furnished the statement on or before 30th June immediately following the financial year or having furnished a statement within that time, notices any omission or wrong particulars therein, may furnish a statement or a revised statement, as the case may be. Such statement or revised statement has to be filed at any time before the expiry of two years from the end of the financial year in which the specified service was provided, or e-commerce supply or services was made or provided or facilitated.

Section	Subject	Provisions
	Time limit for filing a statement in response to notice issued by the Assessing Officer	Where any assessee or e-commerce operator fails to furnish the statement within the prescribed time, the Assessing Officer may serve a notice upon such assessee or e-commerce operator requiring him to furnish the statement in the prescribed form, verified in the prescribed manner and setting forth the prescribed particulars, within such time, as may be prescribed. The Assessing Officer has been empowered to issue notice for furnishing such statement, which then has to be furnished, within 30 days from date of serving of such notice [Rule 6 of Equalisation Levy Rules, 2016]
168	**Processing of Statement**	
	Manner of processing of statement	Where a statement has been made under section 167 by the assessee or e-commerce operator, such statement shall be processed in the following manner, namely— (a) the equalisation levy shall be computed after making the adjustment for any arithmetical error in the statement; (b) the interest, if any shall be computed on the basis of sum deductible or payable, as the case may be, as computed in the statement; (c) the sum payable by, or the amount of refund due to, the assessee or e-commerce operator, shall be determined after adjustment of interest computed against the equalisation levy paid under section 166(2) or section 166A or interest paid under section 170 and any amount paid otherwise by way of tax or interest; (d) an intimation shall be prepared or generated and sent to the assessee or e-commerce operator, specifying the sum determined to be payable by, or the amount of refund due to him; and

Section	Subject	Provisions
		(e) the amount of refund due to the assessee or e- commerce operator in pursuance of such determination shall be granted to him. However, no such intimation shall be sent after the expiry of one year from the end of the financial year in which the statement or revised statement is furnished.
	Prescribed form for service of notice of demand on the assessee/ e- commerce operator	Where any levy, interest or penalty is payable under the equalisation levy provisions, a notice of demand in Form No. 2 specifying the sum so payable shall be served upon the assessee or e-commerce operator, as the case may be. Further, intimation issued upon processing of the statement or revised statement shall also be deemed to be a notice of demand [Rule 7 of Equalisation Levy Rules, 2016]
	Scheme for centralised processing of statements	For the purposes of processing of statements, the CBDT may make a scheme for centralised processing of such statements to expeditiously determine the tax payable by, or the refund due to, the assessee or e-commerce operator as required thereunder.
169	**Rectification of mistake**	
	Time limit for amending an intimation	With a view to rectifying any mistake apparent from the record, the Assessing Officer may amend any intimation issued under section 168. Such intimation can be amended within one year from the end of the financial year in which the intimation sought to be amended was issued.
	Amendment can be made suo motu or brought to notice by the assessee/ e-commerce operator	The Assessing Officer may make an amendment to any intimation, either suo motu or on any mistake brought to his notice by the assessee or e-commerce operator

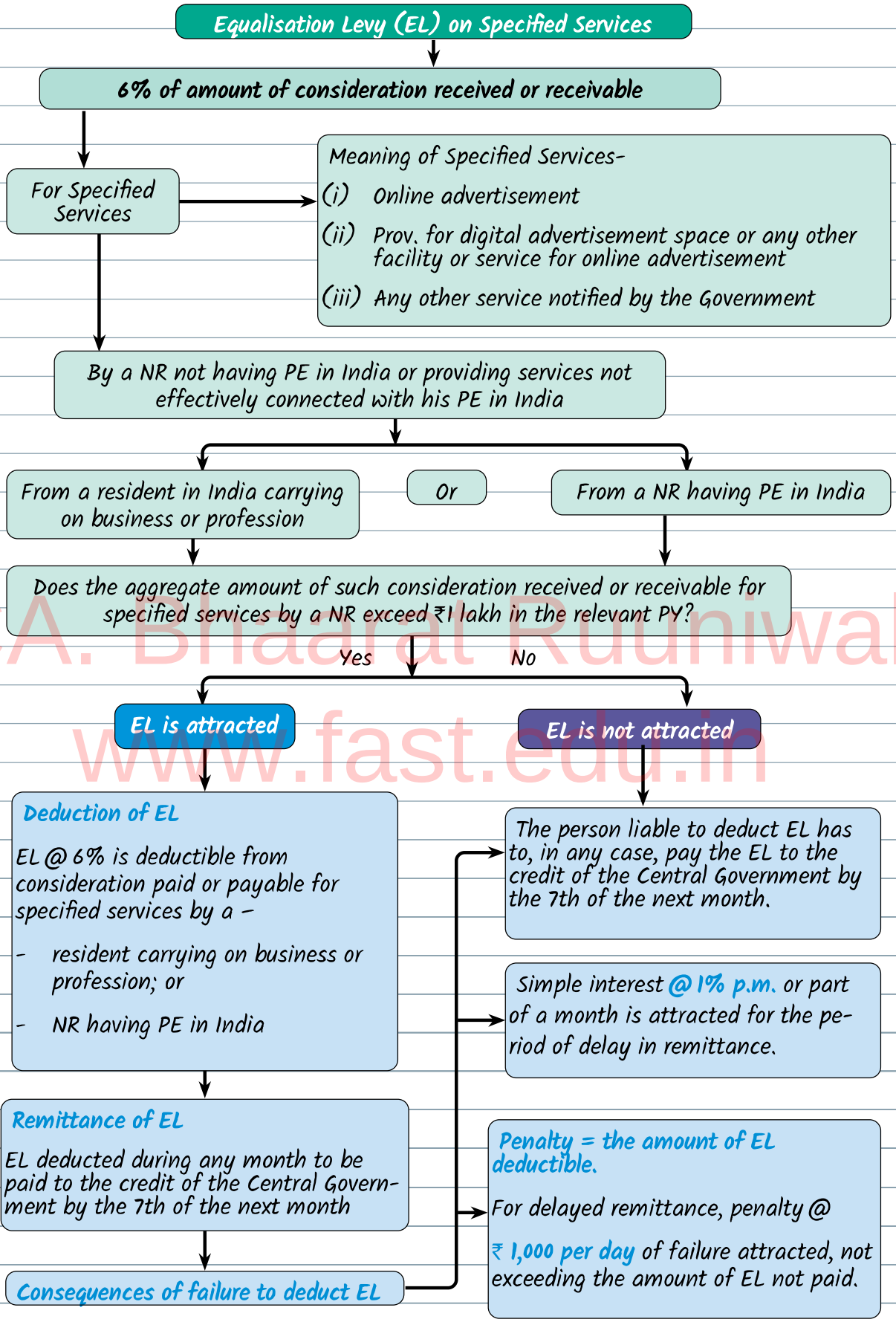
Section	Subject	Provisions	
	Opportunity of being heard to be given by the assessing officer before amending an intimation	An amendment to any intimation, which has the effect of increasing the liability of the assessee or e-commerce operator or reducing a refund, shall not be made unless the Assessing Officer has given notice to the assessee or e-commerce operator of his intention so to do and has given the assessee or e-commerce operator a reasonable opportunity of being heard. Where any such amendment to any intimation has the effect of enhancing the sum payable or reducing the refund already made, the Assessing Officer shall make an order specifying the sum payable by the assessee or e-commerce operator and the provisions of this Chapter shall apply accordingly.	
170	**Interest on delayed payment of equalisation levy**	An assessee or e-commerce operator who fails to credit the equalisation levy or any part thereof within the period specified u/s 166 or 166A, to the account of the Central Government, has to pay simple interest at the rate of 1% of such levy for every month or part of a month by which such crediting of the tax or any part thereof is delayed.	
171	**Penalty for failure to deduct or pay equalisation levy**	**Nature of default**	**Penalty**
		Failure to deduct whole or part of equalisation levy u/s 166	In addition to payment of equalisation levy u/s 166(3) and interest u/s 170, penalty equal to the amount of equalisation levy that he failed to deduct would be leviable
		Failure to pay whole or part of Equalisation levy as required u/s 166A	In addition to equalisation levy u/s 166A and interest u/s 170, penalty equal to the amount of equalisation levy that he failed to pay is leviable

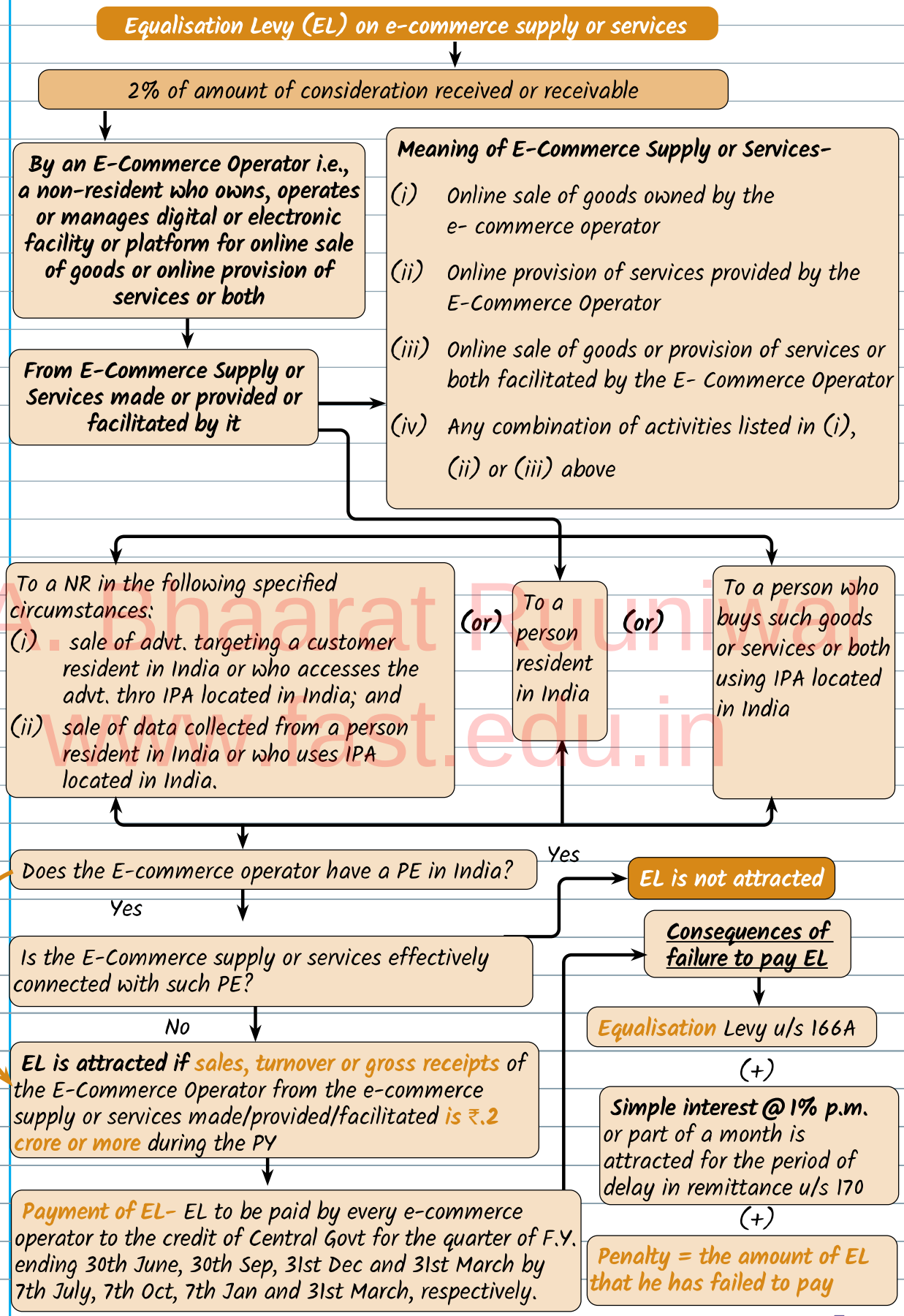
		Nature of default	Penalty
		Failure to remit equalisation levy to the Central Government on or before 7th of the following month, after deduction of the same u/s 165(1)	In addition to paying the equalisation levy on specified services u/s 166(2) and interest u/s 170, a penalty of ₹ 1,000 for every day during which the failure continues is leviable. However, such penalty shall not exceed the amount of equalisation levy that he failed to pay.
172	**Penalty for failure to furnish statement**	For failure to furnish the statement within 30th June of the immediately following year or within 30 days from the date of service of notice by the Assessing Officer, penalty of ₹ 100 for each day during which the failure continues is leviable.	
173	**Circumstances when penalty cannot be imposed under section 171 and 172**	No penalty for failure to deduct or pay equalisation levy or failure to furnish statement shall be imposable, if the assessee or e-commerce operator proves to the satisfaction of the Assessing Officer that there was reasonable cause for the said failure. Further, no order imposing a penalty under this Chapter shall be made unless the assessee or e-commerce operator has been given a reasonable opportunity of being heard.	
174	**Appeal to Commissioner of Income-tax (Appeals)**		
	Time limit for filing of appeal against an order imposing penalty	An assessee or e-commerce operator aggrieved by an order imposing penalty under this Chapter, may appeal to the Commissioner of Income-tax (Appeals) within a period of 30 days from the date of receipt of the order of the Assessing Officer	
	Fee for filing appeal	An appeal shall be in the prescribed form [Form 3] and verified in the prescribed manner. It shall be accompanied by a fee of ₹ 1,000.	

Section	Subject	Provisions
		It may be filed electronically under digital signature or electronically through EVC. Any document accompanying Form No.3 has to be furnished in the manner in which Form No.3 is furnished [Rule 8 of Equalisation Levy Rules, 2016]
	Provisions of the Income-tax Act, 1961 applicable in case of such appeals	Where an appeal has been filed, the provisions of sections 249 to 251 of the Income-tax Act, 1961 would, as far as may be, apply to such appeal. Section 250 specifies the procedure in appeal and section 251 enlists the powers of the Commissioner (Appeals).
175	**Appeal to Appellate Tribunal**	
	Assessee/ e- commerce operator/ CIT may file appeal to Appellate Tribunal against an order passed by Commissioner (Appeals) u/s 174	An assessee or e-commerce operator aggrieved by an order made by the Commissioner of Income-tax (Appeals) under section 174 may appeal to the Appellate Tribunal against such order. The Commissioner of Income-tax may, if he objects to any order passed by the Commissioner of Income-tax (Appeals) under section 174, direct the Assessing Officer to appeal to the Appellate Tribunal against such order.
	Time limit for filing appeal	An appeal shall be filed within 60 days from the date on which the order sought to be appealed against is received the assessee or e-commerce operator or by the Commissioner of Income-tax, as the case may be.
	Fee for filing appeal	The appeal shall be in the prescribed form [Form No.4] and verified in the prescribed manner. In the case of an appeal filed by an assessee or e-commerce operator, it shall be accompanied by a fee of ₹1,000. Also, the form of appeal, the grounds of appeal and the form of verification appended thereto shall be signed by the person specified in Form No.4, as applicable to the assessee or e-commerce operator, as the case may be [Rule 9 of Equalisation Levy Rules, 2016]

	Provisions of the Income-tax Act, 1961 applicable in case of such appeals	Where an appeal has been filed before the Appellate Tribunal under sub-section (1) or sub-section (2), the provisions of sections 253 to 255 of the Income-tax Act, 1961 would, as far as may be, apply to such appeal.
176	**Punishment for false statement**	If a person - (a) makes a false statement in any verification under this Chapter or any rule made thereunder; or (b) delivers an account or statement, which is false, and which he either knows or believes to be false, or does not believe to be true, he shall be punishable with imprisonment for a term which may extend to three years and with fine. An offence so punishable shall be deemed to be non-cognizable within the meaning of the Code of Criminal Procedure. This is irrespective of anything contained in the Code of Criminal Procedure, 1973.
177	**Institution of prosecution**	Prior sanction of the Chief Commissioner of Income-tax is required for instituting prosecution against any person for any offence under section 176.
10(50)	**Income exempt from tax**	Section 10(50) exempts any income arising from providing any specified service on or after the date on which the provisions of Chapter VIII of the Finance Act, 2016 comes into force, or arising from any e-commerce supply or services made or provided or facilitated on or after 01.04.2020 and chargeable to equalisation levy under that chapter.

Section	Subject	Provisions
40(a)(ib)	Non- compliance of the provisions of equalisation levy	If any consideration is paid or payable to a non-resident for a specified service on which equalisation levy is deductible and such levy- · Has not been deducted; or · After deduction, has not been paid On or before the due date u/s 139(1), then, such expenses incurred by the assessee (i.e. advertisement expenses) shall not be allowed as deduction in the current P.Y. However, if the equalisation levy has been deducted in any subsequent year or has been deducted during the P.Y but paid after the due date of return filing then such sum shall be allowed as deduction in the P.Y in which such levy has been paid.
194-O	TDS	Where sale of goods or provision of services of an e-commerce participant is facilitated by an e-commerce operator through its digital or electronic facility or platform, such e-commerce operator is liable to deduct tax at source @ 1% of the gross amount of such sales or services or both at the time of credit of amount or payment thereof to such e-commerce participant, whichever is earlier. Note- No TDS shall be deducted where such e-commerce participant furnishes his PAN/Aadhaar number and such e-commerce participant is an individual or HUF and the gross amount so credited or paid is upto ₹5 lakhs.





Notes

BEPS

BEPS Action Plan I- Addressing the challenges of the digital economy

	OECD Recommendation	Provision incorporated in Indian Tax Laws
1.	Modifying existing Permanent Establishment (PE) rule to provide whether an enterprise engaged in fully de-materialized digital activities would constitute a PE if it maintained significant digital presence in another country's economy	Equalisation Levy Equalisation levy @ 6% is attracted on the amount of consideration for specified services received or receivable by a non-resident not having PE in India or providing services not effectively connected with PE in India, from: • a resident in India who carries on business or profession or • from a non-resident having PE in India. The resident or non-resident having PE in India has to deduct equalisation Levy @ 6% from consideration for specified services paid to non-resident and remit the same to the Central Government within the prescribed time. **Equalisation levy @ 2% would be chargeable on the amount of consideration received or receivable by an e-commerce operator from e-commerce supply or services** made or provided or facilitated by it— (i) to a person resident in India; or (ii) to a non-resident in the following specified circumstances - (a) sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement
2.	A virtual fixed place of business PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction & carries on business through that website.	
3.	Imposition of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider.	
4.	Imposition of an Equalisation Levy on consideration for certain digital transactions received by a Non-resident from a resident or Non-resident having PE in the other contracting state.	

	OECD Recommendation	Provision incorporated in Indian Tax Laws

though internet protocol address located in India; and

(b) sale of data, collected from a person who is resident in India or from a person who uses internet protocol address located in India; or

(iii) to a person who buys such goods or services or both using internet protocol address located in India

Further, section 194-O provides that where sale of goods or provision of services of an e-commerce participant is facilitated by an e-commerce operator through its digital or electronic facility or platform, such e-commerce operator is liable to deduct tax at source @1% of the gross amount of such sales or services or both.

Significant economic presence

Significant economic presence of a non-resident in India shall also constitute business connection in India. Significant economic presence means-

	Nature of transaction	Condition
(a)	in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India	Aggregate of payments arising from such transaction or transactions during the previous year should exceed ₹ 2 crores.

OECD Recommendation	Provision incorporated in Indian Tax Laws	
	Nature of transaction	**Condition**
	(b) systematic and continuous soliciting of business activities or engaging in interaction with users in India	The number of users should be atleast 3 lakhs.

Action Plan 2- Neutralise the effects of hybrid mismatch arrangements

Hybrid mismatch is an arrangement that exploits a difference in the tax treatment of an entity or an instrument under the laws of two or more tax jurisdictions to achieve double non-taxation.

Some examples of hybrid mismatch are as follows-

1. Creation of two deductions for single borrowers.
2. Taking deductions without corresponding Income inclusion.
3. Misuse of Foreign Tax Credit
4. Participation exemption regime (showing activity in low tax jurisdiction)

OECD Recommendations

1. Change in the domestic law and make rules to neutralise the effect of Hybrid Mismatch Arrangements.
2. Change in tax treaty to deal with dual resident companies, transparent entity, hybrid entity etc.

Recommended general amendments are as follows-

- A rule denying transparency to entities where the non-resident investors' resident country treats the entity as opaque;

Example 1

Let us say, X Co., a parent company in country X indirectly holds Y Co., an operating company in country Y. Between X Co. and Y Co. is a hybrid entity that is treated as transparent or disregarded for country X tax purposes and as non-transparent for country Y tax purposes. X Co. holds all or almost all equity interest in the hybrid entity which in turn holds all or almost all equity interests in Y Co. The hybrid entity

borrows money from a third party and the loan is used to invest equity into Y Co (or to buy the shares in Y Co from either another company of the same group or from an unrelated third party). The hybrid entity pays interest on the loan. Except for the interest, the hybrid entity does not claim any other significant deduction and does not have any significant income.

With respect to Country Y, for tax purposes, Hybrid Entity is subject to corporate income tax. Its interest expenses can be used to offset other country Y group companies' income under the country Y group tax relief regime. On the other hand, country X treats the hybrid entity as transparent or disregarded, with the result that its interest expenses are allocated to X Co, which deducts the interest expense to offset unrelated income. The net effect is that there are two deductions for the same contractual obligation in two different countries. Therefore, by virtue of rule denying transparency to an entity which is treated as opaque in the subsidiary company's country, the double deduction can be avoided.

- A rule denying an exemption or credit for foreign underlying tax for dividends that are deductible by the payer;

Example 2

N Co, a company resident in country N is funded by M Co., a company resident in country M with an instrument that qualifies as equity in country M but as debt in country N. A payment made under the instrument would be deductible as interest expense for N Co under country N tax law. The corresponding receipts are treated as exempt dividends under the tax laws of country M. Consequently, deduction is available under the tax laws of country N without a corresponding income inclusion in country M.

Therefore, by virtue of rule denying an exemption or credit for foreign underlying tax for dividends that are deductible by the payer, exemption of such income in country M would not be possible.

- A rule denying a foreign tax credit for withholding tax where that tax is also credited to some other entity; and
- Amendments to CFC and similar regimes attributing local shareholders the income of foreign entities that are treated as transparent under their local law.

Branch Mismatches

Branch mismatches arise where the ordinary rules for allocating income and expenditure between the branch and head office result in a portion of the net income of the taxpayer

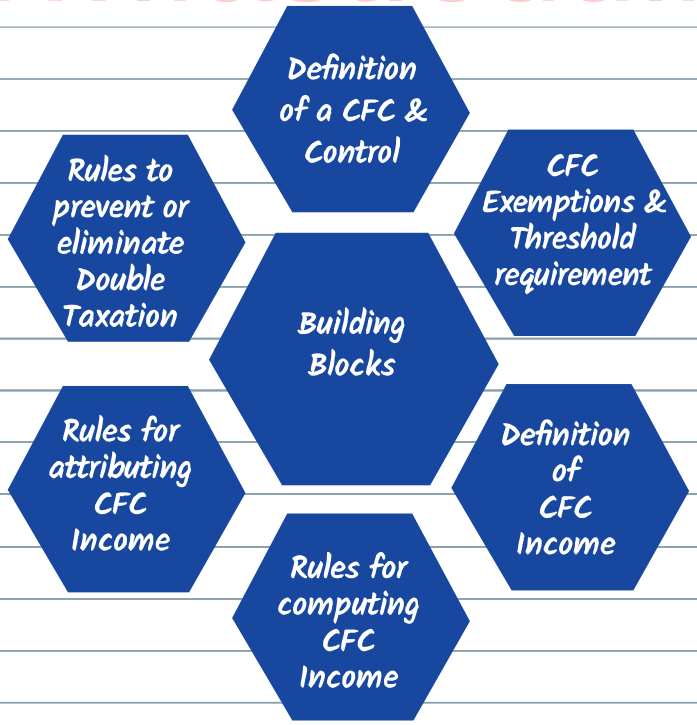
escaping the charge to taxation in both the branch and residence jurisdiction. Unlike hybrid mismatches, which result from conflicts in the legal treatment of entities or instruments, branch mismatches are the result of differences in the way the branch and head office account for a payment made by or to the branch.

Branch mismatches are a product of inconsistencies in the domestic rules for determining the amount of income and expenditure subject to tax in each jurisdiction where the taxpayer operates. Branch mismatches exploit both differences in the domestic rules for determining whether an enterprise is subject to tax in a particular jurisdiction and the amount of income and expenditure to be taken into account in calculating that tax liability.

BEPS Action Plan 3- Strengthen Controlled Foreign Corporation (CFC) rules

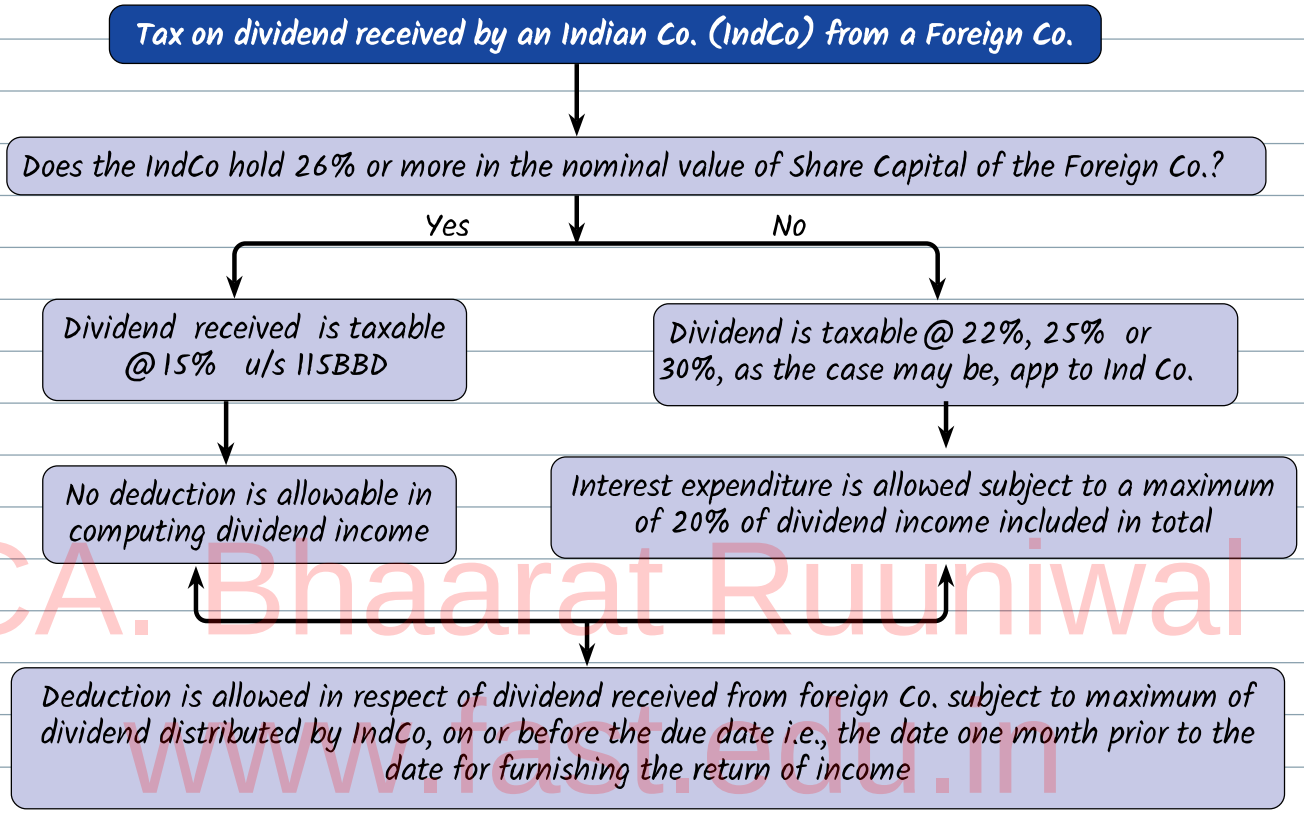
OECD Recommendation

CFCs are foreign subsidiaries in tax havens in which the taxpayer has controlling interest. Since tax is generally levied on distributed dividend, tax in parent country could be avoided until the tax haven country actually paid dividend to the shareholders. The OECD regards CFC Rules as important in tackling BEPS and has made a series of best practice recommendations in relation to the building blocks of an effective CFC regime.



Provisions incorporated in the Income-tax Act, 1961

There are no CFC Rules in the Income-tax Act, 1961. However, section 115BBD has been inserted in Income-tax Act, 1961 to encourage repatriation of profits by Indian companies which have significant voting power in foreign Companies.



BEPS Action Plan 4- Interest deductions and other financial payments

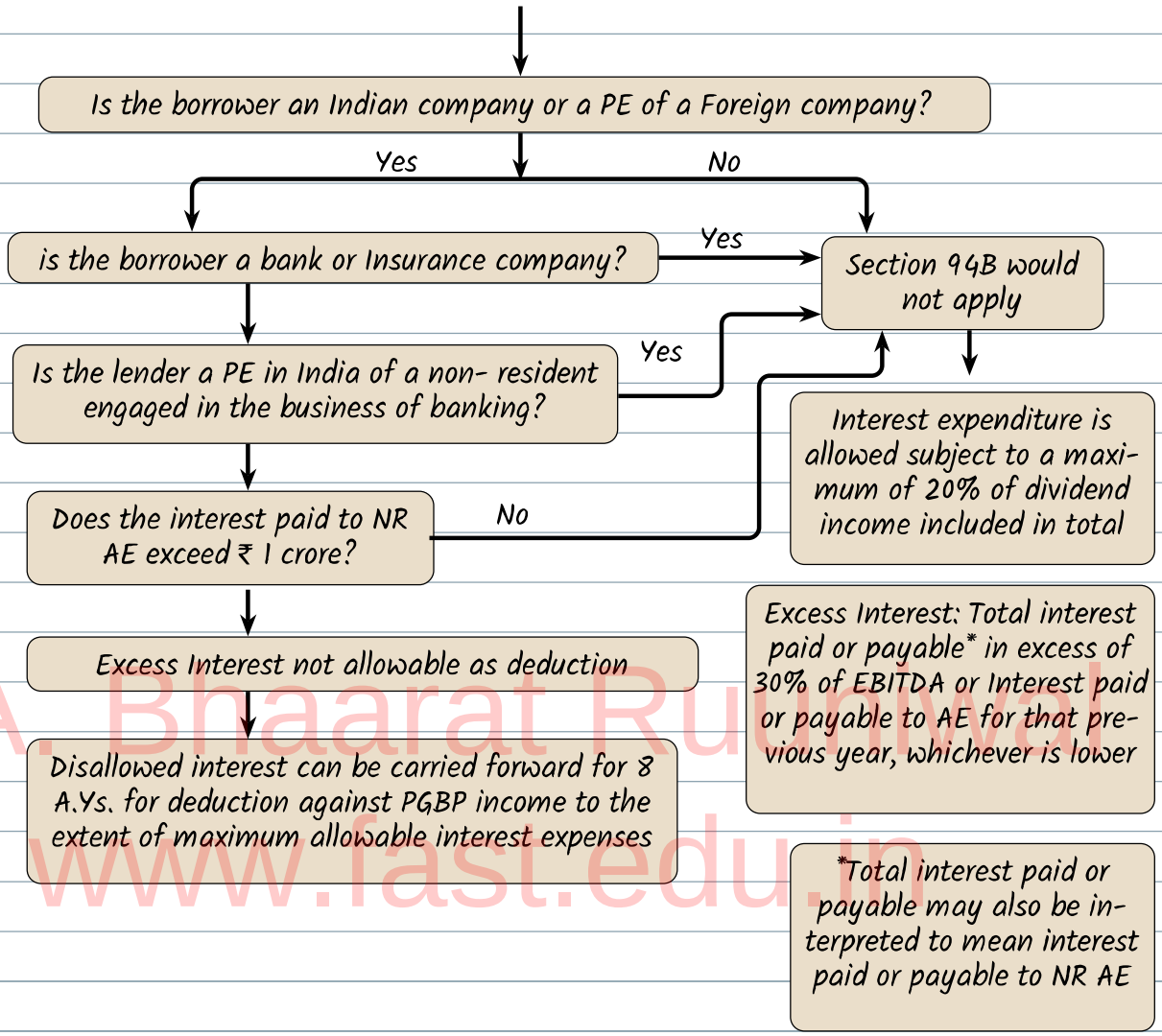
Common Approach in 2015 Report

The common approach which directly links an entity's net interest deductions to its level of economic activity, based on taxable EBITDA includes three elements:

	Rule	Basis
i	Fixed Ratio Rule	based on benchmark net interest/EBITDA Ratio
ii	Group Ratio Rule	allows an entity to deduct more interest expense based on the position of its world wide group
iii	Targeted Rules	address specific risks

Provisions incorporated in the Income-tax Act, 1961

Sec 94B – Limitation of interest deduction [based on Fixed Ratio Rule]



BEPS Action Plan 5- Counter Harmful Tax Practices

OECD BEPS Action 5 Report

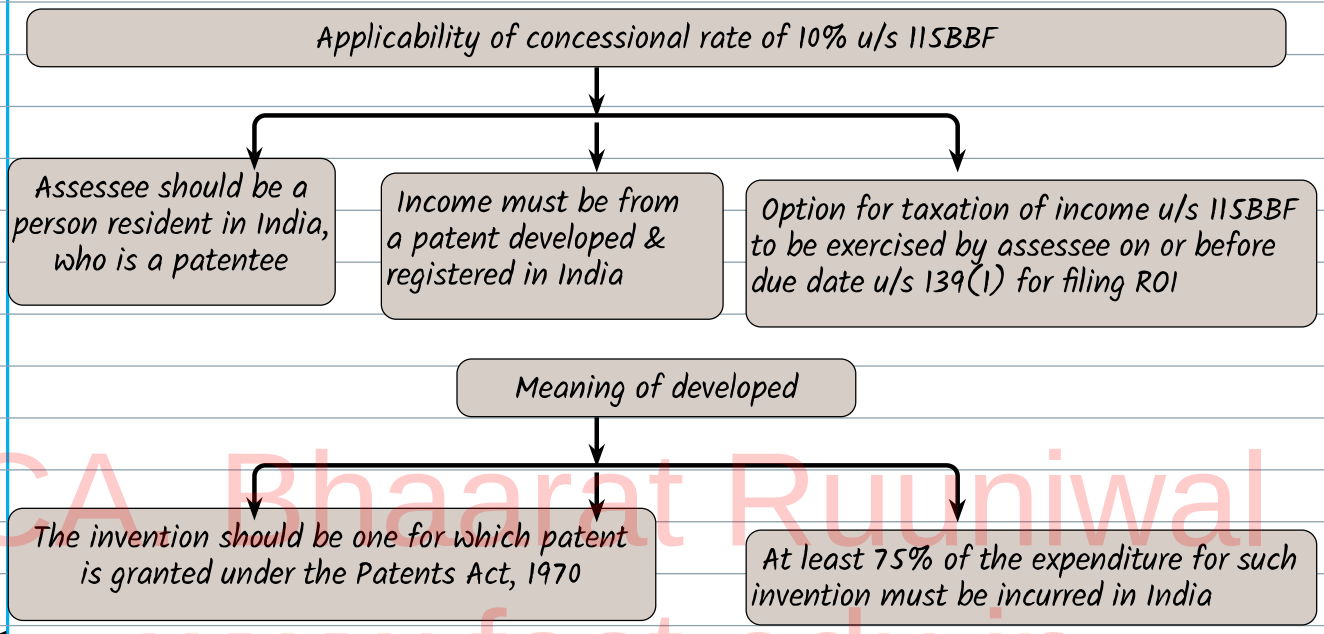
Action 5 report identifies factors for determining a potential harmful tax practice that results in low or no effective tax rate, lack of transparency, negotiable tax rate or base etc.

For instance, in case of R&D activities, the nexus approach recommended by the OECD under BEPS Action 5 requires attribution and taxation of income arising from exploitation of IP in the jurisdiction where substantial R & D activities are undertaken instead of the jurisdiction of legal ownership.

Provisions incorporated in the Income-tax Act, 1961

Sec 115BBF of the Income-tax Act, 1961 – Tax on income from patent

Where the Total Income of the eligible assessee includes any income by way of royalty in respect of a patent developed & registered in India, then, such royalty is taxable @ 10% (plus applicable surcharge & cess).



BEPS Action Plan 6- Preventing treaty abuse

OECD Minimum Standard

Given the risk to revenues posed by treaty shopping, countries have committed to ensure a minimum level of protection against treaty shopping by including in their treaties:

i. the combined approach of Limitation of Benefits (LOB) and Principal Purpose Test (PPT) rule,
ii. the PPT rule alone, or
iii. the LOB rule supplemented by a mechanism that would deal with conduit financing arrangements not already dealt with in tax treaties.

LoB clause incorporated in Indian Tax Treaties

LoB clause in India-Mauritius Tax Treaty

- On 10.5.2016, the India-Mauritius tax treaty was amended and for the first time, it has been provided that gains from the alienation of shares acquired on or after 1.4.2017 in a company which is a resident of India may be taxed in India.

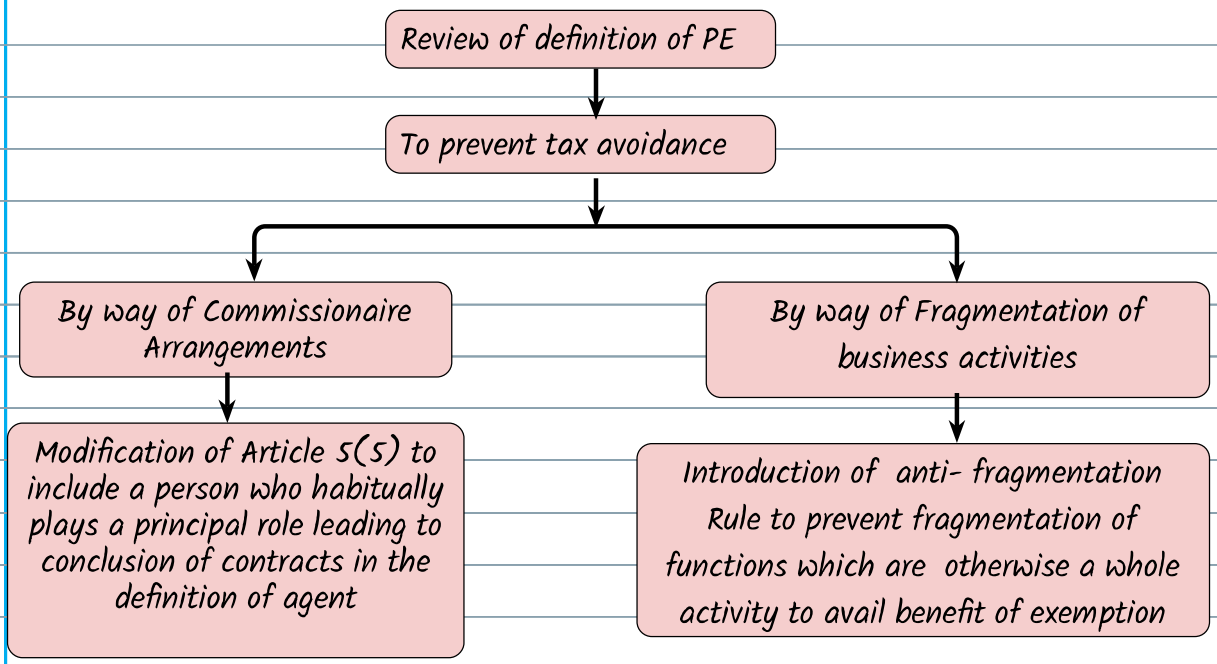
- The tax rate on such capital gains arising from 1.4.2017-31.3.2019 should, however, not exceed 50% of the applicable tax rate on capital gains in India.
- LOB Clause provides that a resident of a Contracting State shall not be entitled to the benefits of 50% of the tax rate applicable in transition period if its affairs are arranged with the primary purpose of taking advantage of concessional rate of tax.
- A shell or a conduit Co. claiming to be a resident of a Contracting State shall not be entitled to this benefit.
- A shell or conduit Co. is any legal entity falling within the meaning of resident with negligible or nil business operations or with no real and continuous business activities carried out in that Contracting State.

LoB clause in India-Singapore Tax Treaty

- Capital gains on sale of shares of an Indian company by a resident of Singapore was taxable only in Singapore, if such shares were acquired before 1.4.2017.
- The India-Singapore tax treaty has been amended to provide that capital gains on alienation of shares acquired on or after 1.4.2017 would be taxable in a similar manner as laid out in India- Mauritius tax treaty, subject to LoB clause.
- The transition period benefit is also similar to that contained in India-Mauritius Tax Treaty.

BEPS Action Plan 7- Prevent the Artificial Avoidance of PE Status

OECD Recommendation



Action Plan 8-10 – Transfer Pricing outcomes in line with value creation/ Intangibles/Risk and Capital and other high-risk transactions.

The aforesaid Action plans represent the OECD's work on transfer pricing which has been a core focus of the BEPS Action Plans. The specific Actions focus on Intangibles, Risks and capital and other high-risk transactions. These are the hard areas of transfer pricing and are summarized together in the Final Report 'Aligning Transfer Pricing Outcomes with Value Creation'.

Action Plan	Details
8	Addresses transfer pricing issues relating to controlled transactions involving intangibles, since intangibles are by definition mobile and they are generally difficult- to-value. Misallocation of the profits generated by valuable intangibles is a significant cause of BEPS.
9	Contractual allocations of risk are respected only when they are supported by actual decision-making and thus exercising control over these risks. Moreover, Action 9 addresses the level of returns to funding provided by a capital-rich MNE group member, where those returns do not correspond to the level of activity undertaken by the funding company.
10	This action focuses on other high-risk areas, which include- • the scope for addressing profit allocations resulting from controlled transactions which are not commercially rational, • the scope for targeting the use of transfer pricing methods in a way which results in diverting profits from the most economically important activities of the MNE group, and • the use of certain type of payments between members of the MNE group (such as management fees and head office expenses) to erode the tax base in the absence of alignment with the value-creation.

OECD Guidelines

- Analysis of contractual relations between associated companies.
- The true nature of the transaction to be determined for transfer pricing purposes when the substances differ from the form.
- Risk and return should be allocated to enterprise having financial capacity to assume the risk. If an enterprise does not have the financial capacity to take risks, these risks should not be assigned to that entity.

- The return should not be attributed to an entity that only has assets, but should be allocated on the basis of the function performed, the risk assumption and the asset used. If an enterprise only provides funding, then that enterprise qualifies for a risk-free return.
- Profits should be allocated to enterprises carrying out the most important activities rather than to low value-added activities. If an enterprise of MNE is engaged in low value added intra group service (back office operation) then profit margin should be limited to 5%.

Action Plan II – Measuring and Monitoring BEPS

Indicators of BEPS activity

Six indicators of BEPS activity highlight BEPS behaviour using different sources of data, employing different metrics, and examining different BEPS channels. When combined and presented as a dashboard of indicators, they confirm the existence of BEPS, and its continued increase in scale in recent years.

i. The profit rates of MNE affiliates located in lower-tax countries are higher than their group's average worldwide profit rate. For example, the profit rates reported by MNE affiliates located in lower-tax countries are twice as high as their group's worldwide profit rate on average.

ii. The effective tax rates paid by large MNE entities are estimated to be lower than similar enterprises with only domestic operations - This tilts the playing-field against local businesses and non-tax aggressive MNEs, although some of this may be due to MNEs' greater utilisation of available country tax preferences.

iii. Foreign direct investment (FDI) is increasingly concentrated - FDI in countries with net FDI to GDP ratios of more than 200% increased from 38 times higher than all other countries in 2005 to 99 times higher in 2012.

iv. The separation of taxable profits from the location of the value creating activity is particularly clear with respect to intangible assets, and the phenomenon has grown rapidly - For example, the ratio of the value of royalties received to spending on research and development in a group of low-tax countries was six times higher than the average ratio for all other countries, and has increased three-fold between 2009 and 2012.

v Royalties received by entities located in these low-tax countries accounted for 3% of total royalties - This provides evidence of the existence of BEPS, though not a direct measurement of the scale of BEPS.

vi Debt from both related and third-parties is more concentrated in MNE affiliates in higher statutory tax-rate countries. The interest-to-income ratio for affiliates of the largest global MNEs in higher-tax rate countries is almost three times higher than their MNE's worldwide third-party interest-to-income ratio.

Action Plan 12 – Disclosure of Aggressive Tax Planning Arrangements

The lack of timely, comprehensive and relevant information on aggressive tax planning strategies is one of the main challenges faced by tax authorities worldwide. Mandatory disclosure regimes can enable countries to quickly respond to tax risks by providing early access to such information.

BEPS Action Plan 12 recognises the advantages of tools designed to facilitate the information flow on tax risks to tax administrations and tax policy makers.

The Report provides a modular framework for guidance drawn from best practices for use by countries without mandatory disclosure rules to design a regime that suits their requirement to get early information on potentially aggressive or abusive tax planning schemes and their users.

Where a country opts for mandatory disclosure rules, the recommendations provide the necessary flexibility to balance a country's need for better and more timely information with the compliance burdens for taxpayers.

It also sets out specific best practice recommendations for rules targeting international tax schemes, as well as for the development and implementation of more effective information exchange and co-operation between tax administrations.

ACTION PLAN 13 – RE-EXAMINE TRANSFER PRICING DOCUMENTATION

The BEPS report recommends that countries adopt a standardised approach to transfer pricing documentation; it mandates the following three-tier structure-

S No.	Document	Information
(1)	Master File	Standardised information relevant for all multinational enterprises (MNE) group members. Master file requires MNEs to provide tax administrations with high-level information regarding their global business operations and transfer pricing policies. The master file is to be delivered by MNEs directly to local tax administrations.
(2)	Local File	Local file requires maintaining of transactional information specific to each country in detail covering related-party transactions and the amounts involved in those transactions. In addition, relevant financial information regarding specific transactions, a comparability analysis and analysis of the selection and application of the most appropriate transfer pricing method should also be captured. The local file is to be delivered by MNEs directly to local tax administrations.
(3)	Country-by-country report	Information relating to the global allocation of the MNE's income and taxes paid; and Indicators of the location of economic activity within the MNE group. CBC report requires MNEs to provide an annual report of economic indicators viz. the amount of revenue, profit before income tax, income tax paid and accrued in relation to the tax jurisdiction in which they do business. CBC reports are required to be filed in the jurisdiction of tax residence of the ultimate parent entity, being subsequently shared between other jurisdictions through automatic exchange of information mechanism.

Advantages of three-tier structure (as per BEPS report)-

- Taxpayers will be required to articulate consistent transfer pricing positions;
- Tax administrations would get useful information to assess transfer pricing risks;
- Tax administrations would be able to make determinations about where their resources can most effectively be deployed, and, in the event audits are called for, provide information to commence and target audit enquiries.

Implementation of international consensus in India

India is one of the active members of BEPS initiative and part of international consensus. For the purpose of implementing the international consensus, a specific reporting regime in respect of CbC reporting and also the master file has been incorporated in the Income-tax Act, 1961. The essential elements have been incorporated in the Income-tax Act, 1961 while remaining aspects would be dealt with in detail in the Income-tax Rules, 1962.

Note – Refer to Chapter I Transfer Pricing, wherein the following have been discussed at length -

i. Elements relating to CbC reporting requirement and related matters which have been incorporated in section 286 of the Income-tax Act, 1961
ii. Maintenance and furnishing of Master file: Consequent provisions incorporated in section 92D of the Income-tax Act, 1961.

Threshold limit of consolidated group revenue for applicability of CbC reporting requirement

The CbC reporting requirement for a reporting year does not apply unless the consolidated revenues of the preceding accounting year of the group, based on consolidated financial statement, exceeds prescribed threshold of ₹6400 cr.

Action Plan 14- Making Dispute Resolution More Effective

The objective of measures developed under Action Plan 14 of BEPS project is to minimise the risks of uncertainty or unintended double taxation, through consistent and proper implementation of tax treaties and effective & timely resolution of disputes regarding their interpretation or application through MAP.

The BEPS Action Plan 14 had suggested a peer review mechanism to ensure adequate implementation of the suggested minimum standard.

As a result, the peer review undertaken for India in 2019 highlighted India's progress on MAP Programme and suggested recommendations for more effective functioning of the MAP.

- That MAP treaty obligations be fully implemented in good faith and that MAP cases be settled in a timely manner.
- That taxpayers can access the MAP if they qualify.
- To promote the prevention and early settlement of treaty disputes through effective administrative processes.

Provision incorporated in the Income-tax Act, 1961

BC is established, inter alia, where a person acting on behalf of NR has and habitually exercises the authority to conclude contracts on behalf of the NR.

From A.Y.2019-20

BC also includes any business activity carried through a person who, acting on behalf of the NR, habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by the NR. Such contracts should be-

i. in the name of the NR; or
ii. for transfer of ownership of, or for the granting of right to use, property owned by that NR or that the NR has the right to use; or
iii. for provision of services by that NR

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BEPS Action Plan 15 Developing a Multilateral Instrument (MLI)

BEPS Report

The MLI helps fight against BEPS by implementing tax treaty- related measures developed through the BEPS Project in existing bilateral treaties in a synchronized and efficient manner to –

- prevent treaty abuse,
- improve dispute resolution
- prevent the artificial avoidance of PE status
- neutralize the effects of hybrid mismatch arrangements. The MLI is flexible instrument which modifies tax treaties that are "Covered Tax Agreements". A Covered Tax Agreement is an agreement for the avoidance of double taxation that is in force between Parties to the MLI and for which both Parties have made a notification that they wish to modify the agreement using the MLI.

Entry into Force of MLI

- The Multilateral Convention to implement tax treaty related measures to prevent Base Erosion and Profit Shifting (BEPS) was signed by India at Paris, France on 7th June, 2017.
- India had ratified the said Convention and had deposited the instrument of ratification along-with the list of Covered Tax Agreements, reservations and notifications (India's Position under the said Convention) to the Depositary on 25th June, 2019.
- The date of entry into force of the said Convention for India is 1st October, 2019, being the first day of the month following the expiry of a period of three calendar months beginning on 25th June, 2019, being the date of deposit by India of the instrument of ratification.
- The earliest date when the provisions of this Convention can take effect in India is 1st April, 2020 (six months from 1st October, 2019, the date of entry into force for India)

Notes

Notes

TEST YOUR KNOWLEDGE

Question 1

What do you understand by base erosion and profit shifting? Describe briefly its adverse effects.

Answer

Base Erosion and Profit Shifting (BEPS) refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profits 'disappear' for tax purposes or to shift profits to locations where there is little or no real activity but the taxes are low, resulting in little or no overall corporate tax being paid.

Adverse Effects of BEPS:

1. Governments have to cope with less revenue and a higher cost to ensure compliance.
2. In developing countries, the lack of tax revenue leads to significant under-funding of public investment that could help foster economic growth.
3. BEPS undermines the integrity of the tax system, as reporting of low corporate taxes is considered to be unfair. When tax laws permit businesses to reduce their tax burden by shifting their income away from jurisdictions where income pro ducing activities are conducted, other taxpayers, especially individual taxpayers in that jurisdiction bear a greater share of the burden. This gives rise to tax fairness issues on account of individuals having to bear a higher tax burden.
4. Enterprises that operate only in domestic markets, including family-owned businesses or new innovative businesses, may have difficulty competing with MNEs that have the ability to shift their profits across borders to avoid or reduce tax. Fair competition is harmed by the distortions induced by BEPS.

Question 2

What are the significant OECD Recommendations under Action Plan 1 of BEPS? Which recommendation has been adopted in Indian tax laws?

Answer

The OECD has recommended several options to tackle the direct tax challenges which include:

1. Modifying the existing Permanent Establishment (PE) rule to provide that whether an enterprise engaged in fully de-materialized digital activities would constitute a PE, if it maintained a significant digital presence in another country's economy.
2. A virtual fixed place of business PE in the concept of PE i.e., creation of a PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website.
3. Imposition of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

Taking into consideration the potential of new digital economy and the rapidly evolving nature of business operations, it becomes necessary to address the challenges in terms of taxation of such digital transactions.

The concept of 'Significant Economic Presence' (SEP) which is similar to the virtual fixed place PE as recommended in the 2015 BEPS Action Plan 1 report is being introduced vide Explanation 2A to section 9(1)(i). This is effective from A.Y.2022-23.

Significant economic presence of a non-resident in India shall also constitute business connection in India. Significant economic presence means-

	Nature of transaction	Condition
(a)	in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India	Aggregate of payments arising from such transaction or transactions during the previous year should exceed ₹ 2 crores.
(b)	systematic and continuous soliciting of business activities or engaging in interaction with users in India	The number of users should be atleast 3 lakhs.

Further, the above transactions or activities shall constitute significant economic presence in India, whether or not,—

i. the agreement for such transactions or activities is entered in India;
ii. the non-resident has a residence or place of business in India; or
iii. the non-resident renders services in India:

However, where a business connection is established by reason of significant economic presence in India, only so much of income as is attributable to the transactions or activities referred to in (a) or (b) above shall be deemed to accrue or arise in India.

In order to address the challenges of the digital economy, Chapter VIII of the Finance Act, 2016, titled "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India. This is provided for in section 165 of the Finance Act, 2016.

Meaning of "Specified Service"

1. Online advertisement;
2. Any provision for digital advertising space or any other facility or service for the purpose of online advertisement;

Specified Service also includes any other service as may be notified by the Central Government.

Further, in order to reduce burden of small players in the digital domain, it is also provided that no such levy shall be made if the aggregate amount of consideration for specified services received or receivable by a non-resident from a person resident in India or from a non-resident having a permanent establishment in India does not exceed ` 1 lakh in any previous year.

The Finance Act, 2020 has expanded the scope of equalisation levy by inserting new section 165A in the Finance Act, 2016 to include within the ambit of Chapter VIII thereto, consideration received or receivable for e-commerce supply or services made or provided or facilitated on or after 1.4.2020. Accordingly, on and from 1st April, 2020, equalisation levy @ 2% would be chargeable on the amount of consideration received or receivable by an e-commerce operator from e- commerce supply or services made or provided or facilitated by it—

(i) to a person resident in India; or

(ii) to a non-resident in the following specified circumstances -

(a) sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement though internet protocol address located in India; and

(b) sale of data, collected from a person who is resident in India or from a person who uses internet protocol address located in India; or

(iii) to a person who buys such goods or services or both using internet protocol address located in India.

However, equalisation levy would not be chargeable —

(i) where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such permanent establishment;

(ii) where the equalisation levy is leviable on specified services under section 165; or

(iii) sales, turnover or gross receipts, as the case may be, of the e-commerce operator from the e-commerce supply or services made or provided or facilitated is less than ` 2 crores during the previous year.

However, the consideration received or receivable for specified services and for e-commerce supply or services would not include the consideration, which are taxable as royalty or fees for technical services in India under the Income-tax Act, 1961 read with the DTAA notified by the Central Government under section 90 or section 90A.

Question 3

Discuss the provision incorporated in the Income-tax Act, 1961 in line with the OECD recommendations under Action Plan 4 of BEPS.

Answer

In line with the recommendations of OECD BEPS Action Plan 4, section 94B has been inserted in the Income-tax Act, 1961 by the Finance Act, 2017 to provide a cap on the interest expense that can be claimed by an entity to its associated enterprise. The total interest paid in excess of 30% of its earnings before interest, taxes, depreciation and amortization (EBITDA) or interest paid or payable to associated enterprise for that previous year, whichever is less, shall not be deductible.

The provision is applicable to an Indian company, or a permanent establishment of a foreign company, being the borrower, who pays interest in respect of any form of debt issued by a non- resident who is an 'associated enterprise' of the borrower. Further, the debt is deemed to be treated as issued by an associated enterprise where it provides an implicit or explicit guarantee to the lender, being a non-associated enterprise, or deposits a corresponding and matching amount of funds with such lender.

The provision allows for carry forward of disallowed interest expense for 8 assessment years immediately succeeding the assessment year for which the disallowance is first made and deduction against the income computed under the head "Profits and gains of business or profession" to the extent of maximum allowable interest expenditure.

In order to target only large interest payments, it provides for a threshold of interest expenditure of

₹ 1 crore in respect of any debt issued by a non-resident associated enterprise exceeding which the provision would be applicable. Banks and Insurance business are excluded from the ambit of the said provisions keeping in view of special nature of these businesses. Also, section 94B would not be attracted on interest paid in respect of debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking.

Question 4

Describe the three tier structure for transfer pricing documentation mandated by BEPS Action Plan 13.

Answer

Action 13 contains a three-tiered standardized approach to transfer pricing documentation which consists of:

a. **Master file:** Master file requires MNEs to provide tax administrations with high-level information regarding their global business operations and transfer pricing policies. The master file is to be delivered by MNEs directly to local tax administrations.

b. **Local file:** Local file requires maintaining of transactional information specific to each country in detail covering related-party transactions and the amounts involved in those transactions. In addition, relevant financial information regarding specific transactions, a comparability analysis and analysis of the selection and application of the most appropriate transfer pricing method

should also be captured. The local file is to be delivered by MNEs directly to local tax administrations.

(c) **Country-by-country (CBC) report:** CBC report requires MNEs to provide an annual report of economic indicators viz. the amount of revenue, profit before income tax, income tax paid and accrued in relation to the tax jurisdiction in which they do business. CBC reports are required to be filed in the jurisdiction of tax residence of the ultimate parent entity, being subsequently shared between other jurisdictions through automatic exchange of information mechanism.

Question 5

Explain the nexus approach recommended by OECD in BEPS Action Plan 5 which has been adopted in the Income-tax Act, 1961.

Answer

In India, the Finance Act, 2016 has introduced a concessional taxation regime for royalty income from patents for the purpose of promoting indigenous research and development and making India a global hub for research and development. The purpose of the concessional taxation regime is to encourage entities to retain and commercialise existing patents and for developing new innovative patented products. Further, this beneficial taxation regime will incentivise entities to locate the high-value jobs associated with the development, manufacture and exploitation of patents in India.

The nexus approach has been recommended by the OECD under BEPS Action Plan 5. This approach requires attribution and taxation of income arising from exploitation of Intellectual property (IP) in the jurisdiction where substantial research and development (R & D) activities are undertaken instead of the jurisdiction of legal ownership. Accordingly, section 115BBF has been inserted in the Income-tax Act, 1961 to provide that where the total income of the eligible assessee (being a person resident in India who is the true and first inventor of the invention and whose name is entered in the patent register as the patentee in accordance with the Patents Act, 1970 and includes every such person, being the true and the first inventor of the invention, where more than one person is registered as patentee under Patents Act, 1970 in respect of that patent.) includes any income by way of royalty in respect of a patent developed and registered in India, then such royalty shall be taxable at the rate of 10% (plus applicable surcharge and cess). For this purpose, developed means atleast 75% of the expenditure should be incurred in India by the eligible assessee for any invention in respect of which patent is granted under the Patents Act, 1970.

Question 6

What are the ways in which hybrid mismatch arrangements are used to achieve unintended double non-taxation or long-term tax deferral?

Answer

Hybrid mismatch arrangements are sometimes used to achieve unintended double non-taxation or long-term tax deferral in one or more of the following ways -

1. Creation of two deductions for a single borrowal;
2. Generation of deductions without corresponding income inclusions;
3. Misuse of foreign tax credit; and
4. Participation exemption regimes.

Notes

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