

INTERNATIONAL TAXATION-AN OVER VIEW

CA.P. SATHEESAN
REGIONAL COUNCIL MEMEBR

Contents

1 What is international tax?

2 Domestic law provisions

3 Double Taxation

4 DTAA

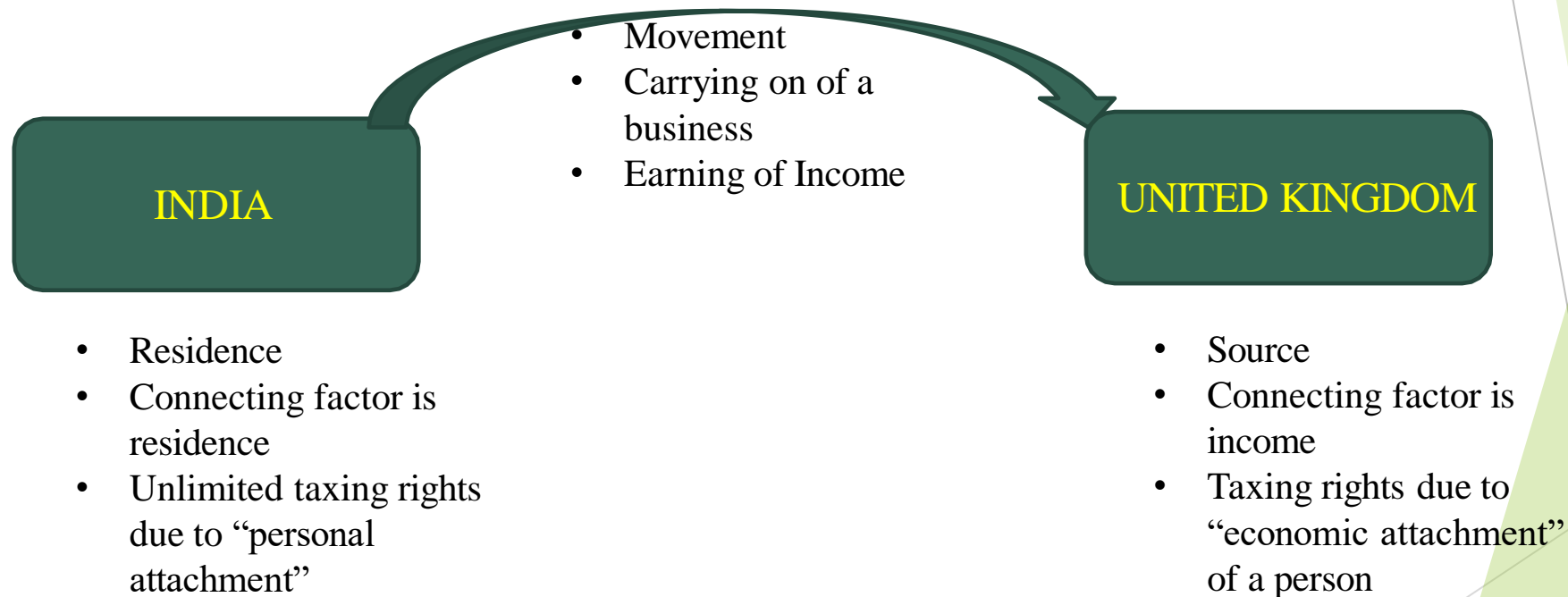
5 Key articles of tax treaties

6 Multilateral Instrument

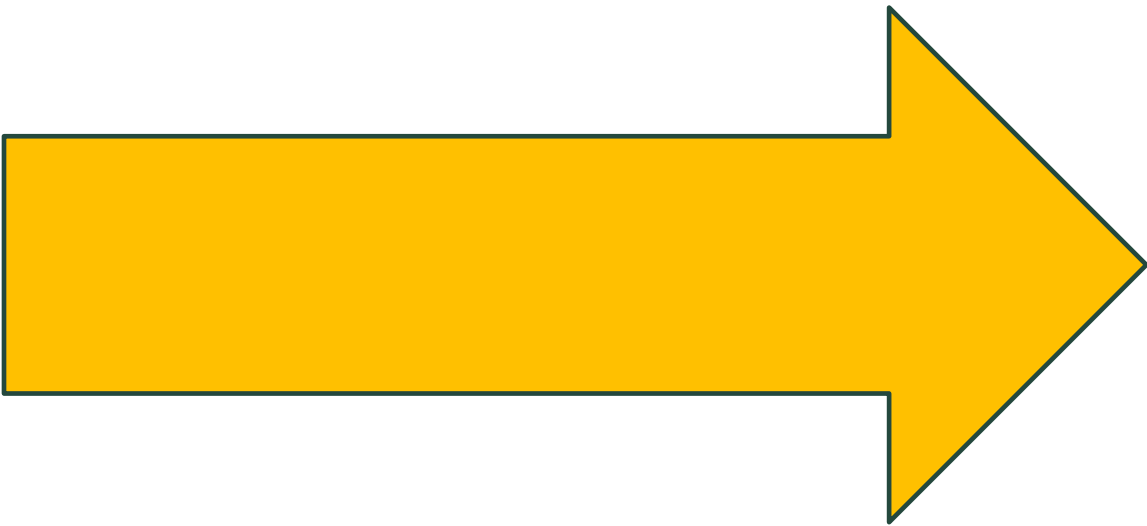
7 Other points

What is international tax?

International taxation is the study or determination of tax on a person or business subject to the tax laws of different countries, or the international aspects of an individual country's tax laws as the case may be.



India is taxing resident Citizens on world wide income generated by them



**Domestic law
provisions**

Charging section and scope of total income

- Charging section (Section 4 of the Income-tax Act, 1961 ('ITA'))
 - Provides that total income of previous year of every person shall be charged at prescribed rates.
- Incidence of tax on income depends upon:
 - Person's resident status
 - Accrual of income based on the place
 - Receipt of income based on place and time
- Income once taxed in accrual / deemed to accrued basis cannot be taxed again on receipt basis

Charging Section 5 and scope of total income

Resident & Ordinary resident

- Income accrued or arising or deemed to accrue or arise in India
- Income received or deemed to be received in India
- Accruing or arising outside India

Resident but not ordinary resident

- Income accrued or arising or deemed to accrue or arise in India
- Income received or deemed to be received in India
- Accruing or arising from outside India from business controlled or profession setup in India

Non-resident

- Income accrued or arising or deemed to accrue or arise in India
- Income received or deemed to be received in India

Residential status

Basic condition

182 days or more in PY

Or

60* days or more in PY
and 365 days or more in 4
PPY

Additional condition

Resident in 2/10 PY

and

Presence for 730 days or
more during 7 PPY

❖ Individuals fulfilling basic and additional conditions will be resident and ordinary resident of India

❖ Individual fulfilling only basic condition will be resident but not ordinary resident of India.

❖ Not fulling conditions will be non-resident

***Replace 60 days with 182 days**

- a) Indian citizen leaving for employment or crew member of India ships
- b) Indian citizen or PIO visiting India

***Replace 60 days with 120 days**

Indian citizen or PIO visiting India having total income (other than income from foreign sources exceeding 15 lakhs)

Residential status

Deemed residency

Condition 1-Citizen of India

Condition 2 – Total income (other than income from foreign sources), exceeding Rs. 15 lakh

Condition 3 – If he is not **liable to tax** in any country or territory by reasons of his domicile, residence or any other criteria of similar nature

Liable to tax

The term liable to tax in relation to a person and with reference to a country, means that there is an income tax liability on such person under the law of that country for the time being in force and shall include a person who has subsequently been exempted from such liability under the law of that country.

Summary of Residential status

Individual	Status	Residential status
Indian citizen not liable to tax on foreign income and having Indian income > 15 Lakhs	Resident	RNOR
Indian citizen leaving India as member of crew of Indian ship or employment purposes and stay in India is more than 182 days	Resident	RNOR / ROR Depending on additional condition
Indian citizen / PIO having Indian income > 15 lakhs and stay in India is more than 120 days but less than 182 days in PY	Resident	RNOR
Indian citizen / PIO having Indian income < 15 lakhs and visits India for more than 182 days	Resident	RNOR / ROR Depending on additional condition

Residency Rules for Companies

Residential status u/s 6(3) of the ITA –

- Either Indian Company

or

- Place of Effective Management (POEM) in India

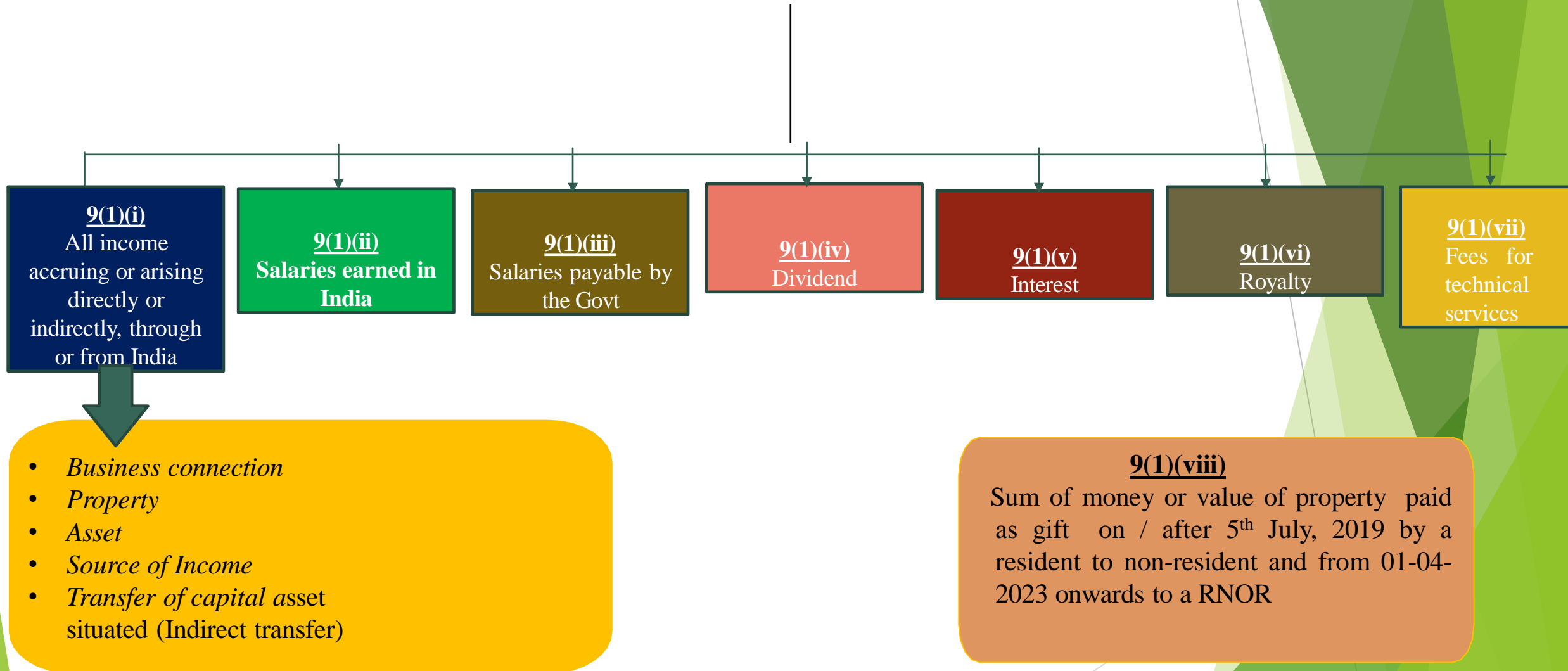
POEM means a place where key management and commercial decisions that are necessary for the conduct of business of an entity as a whole are, in substance made.

–Substance over form concept

–Fact specific exercise


–To be checked year on year

Income deemed to accrue or arise in India – Section 9 of the ITA

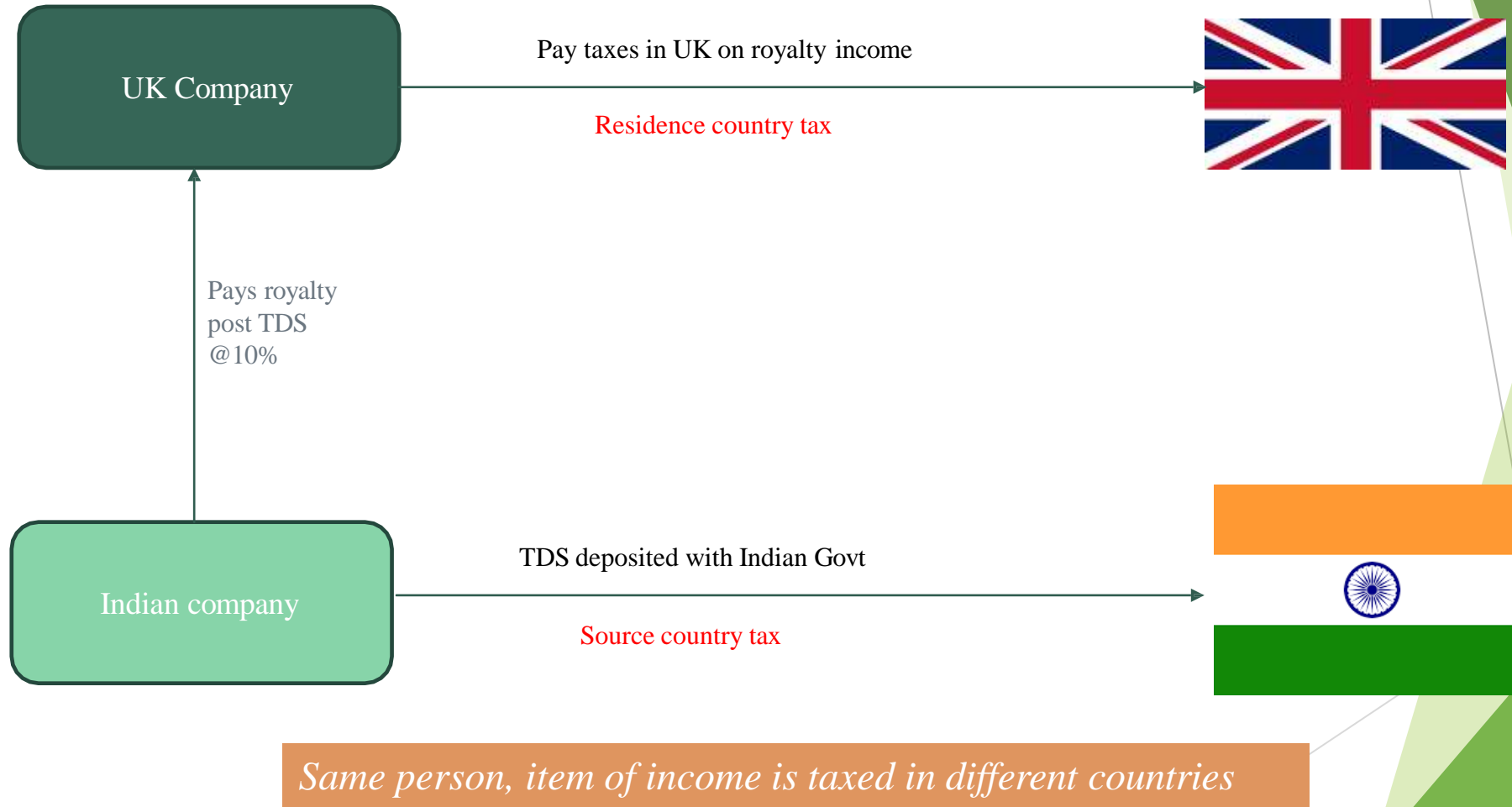


Only income attributable to India shall be deemed to accrue in India

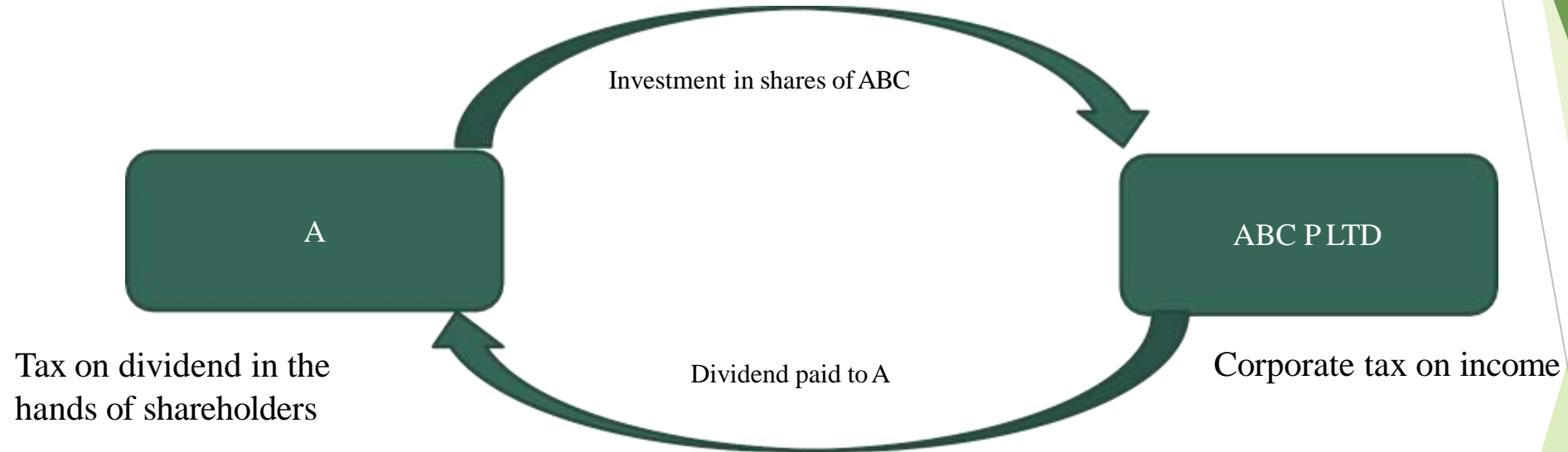
Double Taxation

The background features abstract, overlapping geometric shapes in various shades of green, ranging from light lime to dark forest green. These shapes are primarily located on the right side of the frame, creating a modern, layered effect. The text 'Double Taxation' is centered in a dark blue, sans-serif font.

Types of double taxation – Juridical Double Taxation



Types of double taxation – Economic Double Taxation



Same economic transaction, item of income is taxed in the hands of different taxpayers

Remedy from double taxation in India

- Section 90(2) – Tax payer has the option to be taxed under the provisions of the tax treaty or the domestic tax laws, whichever are more beneficial
- Section 91 –
 - ✓ Relief from double taxation in countries with which India has no tax treaties
 - ✓ Person resident in India is allowed credit for foreign taxes paid (in respect of income accruing or arising outside India) against the Indian taxes as per prescribed rules (Form 67 as per Rule 128)

Double Taxation Avoidance Agreement



Double Taxation Avoidance Agreements

- **Indian tax laws**

Section 90 – Empowers GOI to enter into a DTAA for avoidance of double taxation

- **Statutory objective**

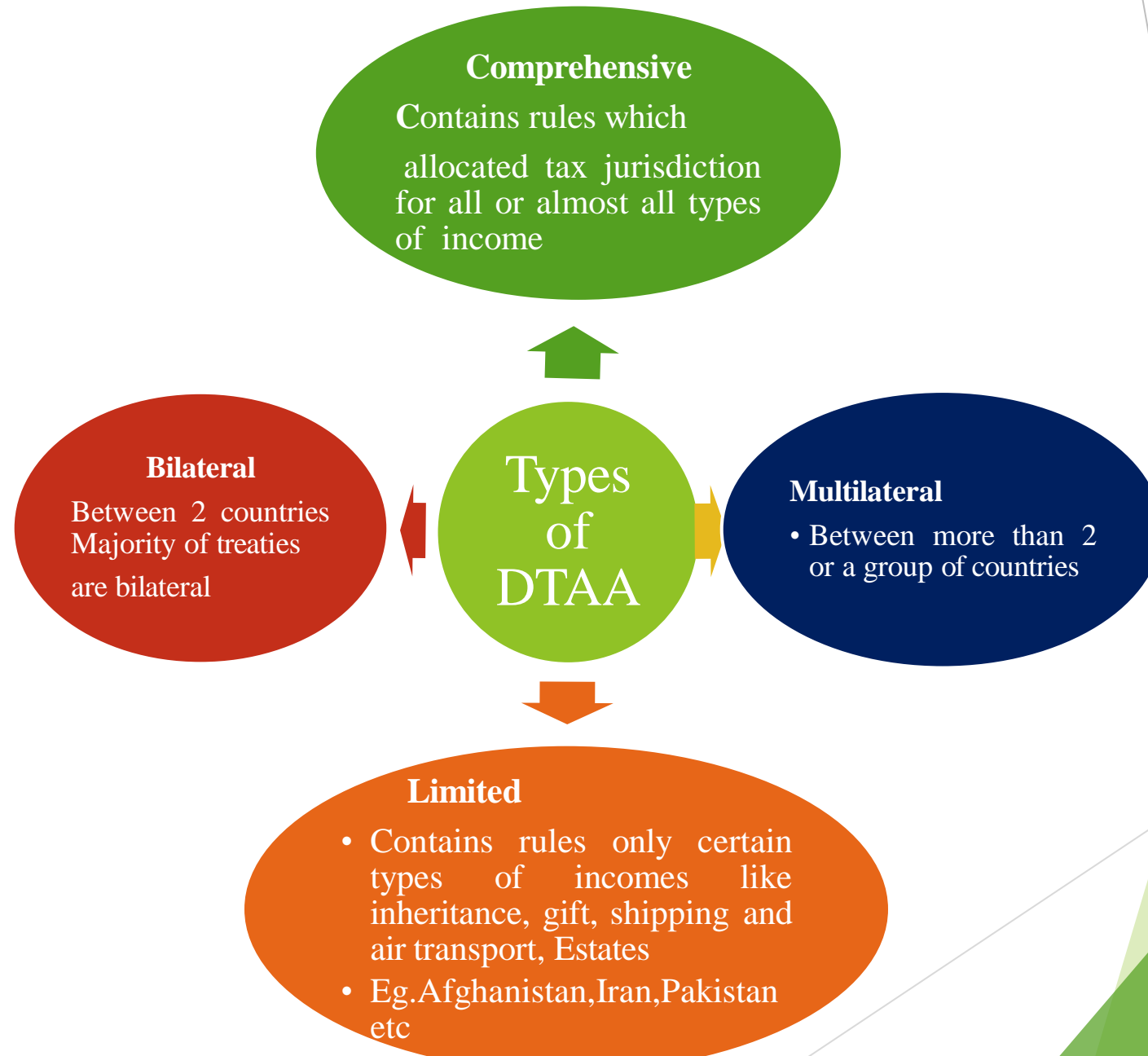
- ✓ Relief on doubly taxed income
- ✓ Promotion of mutual economic relations, trade and investment
- ✓ Avoidance of double taxation
- ✓ Exchange of information
- ✓ Recovery of tax

- **Parties to tax treaties: Section 90(1)**

- ✓ Countries outside India
- ✓ Specified territories outside India

Double Taxation Avoidance Agreements

- International Agreements between two or more sovereign nations to avoid double taxation, exchange of goods and services and the movement of capital and persons
- Also known as Tax Treaty / Convention / Charter
- Following are an integral part of DTAA
 - ✓ Exchange of notes / protocol
 - ✓ Memorandum of understanding



Tax Treaty Models



**UN Model – Source based-
India is following**



**OECD (Organization for Economic
Cooperation and Development)-Model –
Residence based**



US model – for US treaties

Fourth model is Andean Model which is a regional level model convention adopted by lesser and medium developed Latin American countries namely Bolivia, Columbia, Chile, Ecuador, Peru and Venezuela.

Interpretation of Tax Treaties

Protocol / exchange of notes

- Clarifies /elaborates Treaty text
- Binding force – equal to treaty
- No limit to no. of protocols
- May be entered into even after treaty is concluded

Model Commentaries

- OECD Model
- UN Model
- US Technical explanation

Interpretation of Tax Treaties

Sources of Interpretation

Public International law

- The Vienna Convention on the Law of Treaties (VCLT) applies to all international treaties including tax treaties -
 - ✓ *Article 26 - Every treaty in force is binding upon the parties to it and must be performed by them in good faith*
 - ✓ *Article 27 - Internal law not to be invoked to perform the treaty*
 - ✓ *Article 28 – Do not apply to act or fact which took place prior to entry into force of the relevant tax treaty*
- Growing number of decisions in international courts refer to the rules in the Vienna Convention
- India is not a signatory to Vienna Convention

Other sources

- Multilateral instrument
- Mutual Agreement procedure
- Judicial decision
- Advance ruling
- Practices of tax authorities of both states

Key Articles of DTAA

Composition of DTAA

Scope of Provisions

Article 1 – Personal scope

Article 2 – Taxes covered

Article 29 – Entry into force

Article 30 - Termination

Article 6 – Immovable properties

Article 7 – Business profits

Article 8 – Shipping etc.

Article 10 – Dividends

Elimination of double

Article 23 - Elimination of double taxation

Article 25 - Mutual Agreement

Composition of DTAA

Miscellaneous Provisions

Article 24 – Non-discrimination

Article 27 – Diplomates

Article 28 – Territorial extension

Substantive Provision

Article 11- Interest

Article 12 – Royalties & FTS

Article 13-Capital gains

Article 14 – Independent personal services

Article 15 - Dependent personal services

Article 16 – Directors

Article 17 – Artistes and sports persons

Article 18 – Pensions

Article 19 –Government services

Article 20 –Students

Article 21 – Other income

Article 22 - Capital

Access to DTAA

▪ **ARTICLE 1 – PERSONS COVERED**

- ✓ DTAA applies to ‘persons who are residents of one or both of the Contracting States

• **ARTICLE 2 – TAXES COVERED**

- ✓ Covers income tax and surcharge
- ✓ Does not cover indirect taxes

• **ARTICLE 3 – DEFINITIONS**

- ✓ “Person” includes an individual, a company and any other body of persons
- ✓ “Company” means any body corporate or any entity that is treated as a body corporate for tax purposes

Access to DTAA

- **ARTICLE 4 – RESIDENCE**

- ✓ Lays down criteria for determining residence of person
- ✓ “Resident of one of the States” means any person who, under the laws of that State, is **liable to tax** therein by reason of his domicile, residence, place of management or any other criterion of a similar nature
- ✓ Certain treaties expression used is subject to tax [e.g. India – Sweden tax treaty, India US tax treaty] - Liable to tax v/s subject to tax
- ✓ In case a person is resident of both countries
 - ▶ In the case of an individual -- tie breaker rule determines residency (discussed in subsequent slide)
 - ▶ In any other case -- the place of effective management determines residency

Article 4 – Dual Residency

Tie-breaker applies if a person is resident in both States under Art. 4(1)

For individuals

Other than individuals

Rule 1 – Permanent home / centre of vital interest

Rule 2 – Habitual abode

Rule 3 – Nationality

Rule 4 – Mutual Agreement by competent authorities

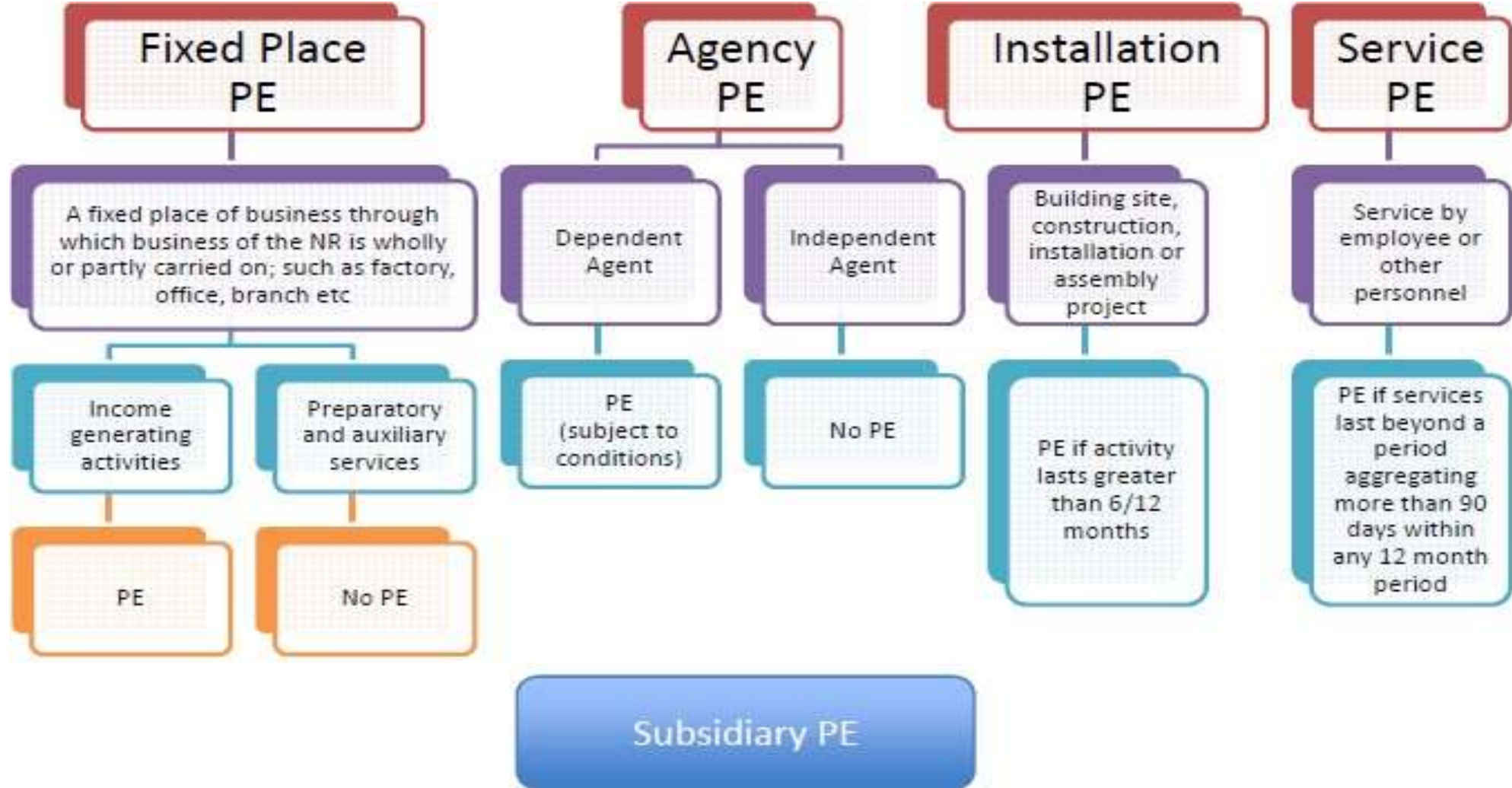
Person is resident of State where **Place of Effective Management ('POEM')** is situated.

OECD Commentary says:

- Place where key management and commercial decisions that are necessary for conduct of business are in substance made
- An entity may have more than one place of management, but it can have only one POEM

BEPS (Base Erosion and Profit Shifting) action plan and MLI (Multilateral Convention to Implement) provides to resolve tie breaking by competent authorities for other than individuals

Article 5 – Permanent Establishment



Key substantive provisions

- **DTAA categorizes income under different heads, some of which are as follows:**
 - ✓ Immovable property
 - ✓ Business income
 - ✓ Dividend, Interest, royalties and fees for technical services
 - ✓ Independent personal services
 - ✓ Dependent personal services
 - ✓ Capital gains
 - ✓ Other income

ARTICLE 6 & 7

- **Article 6- Income from immovable property**
- Primary right to tax has been provided to the state where the property is situated

- **Article 7- Business profits**
 - ✓ Business profits of an enterprise is taxable in the state of residence, unless it carries on business in the other state through a PE.
 - ✓ Profits may be taxed in the state of PE but only to the extent attributable to
 - PE
 - Arising from the sale of goods or merchandise in the country which are same or of a similar to those sold through the PE
 - Arising from other business activities carried on in the country which are the same or of a similar kind as those effected through a PE (**Force of attraction**)
 - ✓ Attribution rule- Profits it might be expected to make if it were a separate and distinct enterprise
 - ✓ Deduction of allocable head office expenses allowed subject to provisions of the domestic law
 - ✓ Deduction/income for royalty, commission, management services, interest on Moneys lent not to be considered in computing profits

Article 10, 11 and 12

- Dividend, (Article 10) Interest (Article 11) , Royalties and Fees for technical services (Article 12)
 - ✓ DTAA applies to ‘persons who are residents of one or both of the Contracting States
 - ✓ Recipient must be the beneficial owner.
 - Anti-avoidance measures -”Substance over form”
 - ✓ Taxable on a gross basis.
 - ✓ Income from dividends, interest, royalty and fees for technical services, if attributable to a PE shall be taxable on a net basis as business profits/independent personal services
 - ✓ Source rules under these articles restricted than under the domestic law

Article 10, 11 and 12

Nature of income	Indicative rates	Remarks
Dividend	5%/ 10%/ 15%	Lower rate if holding $\geq 10\%$
Interest	0%/ 10%/ 15%	Lower rate for payments to specific institutions, banks or financial institutions
Royalty	0%/ 10%/ 15%	Lower rate for use of industrial, commercial or scientific equipment
Fees for included services	0%/ 10%/ 15%	Lower rate for services ancillary and subsidiary to the lease of equipment

Article 10, 11 and 12

▪ Royalties

- ✓ Definition under the treaty similar to that under the ITA [Section 9(1)(vi)]. **Inclusion of computer software in UN model**
- ✓ Certain treaties do not have Definition under the treaty similar to that ICS equipment clause [e.g. Sweden, Israel]

▪ Fees for technical services

- ✓ under the Act [Section 9(1)(vii)]
- ✓ Restricted Source rule under certain treaties [e.g. US, Canada, UK]
 - Payments for rendering of any technical or consultancy services, if such services:
 - are ancillary and subsidiary to application or enjoyment of right, property, or information plan for which royalty is received, or
 - **make available** technical knowledge, experience, skill, know-how, or processes, or consist of development and transfer of a technical or technical design.
- ✓ Key exclusions
 - Services for the personal use of individual
 - Teaching in or by educational institutions; etc

Article 13 – capital gains

Sr. No.	Nature of property alienated	Right of taxation
1.	Immovable property	Country in which property is situated
2.	Capital stock/ shares of company, interest in firm, trust estate property of which principally consists of immovable property	Country in which property is situated -Principally - > 50% Certain treaties – specifically exclude listed companies
3.	Shares (other than those in 2 above) of a company resident in other state	Country in which company is resident
4.	Any property forming part of business property of a PE (including on disposal of PE)	Country in which PE is situated
5.	Any other property	Country in which alienator is resident

Article 14 and Article 21

- **Independent personal service**
 - ✓ Deals with taxation of income in respect of professional services or other activities of independent character
 - ✓ Taxable in source state
 - If regular fixed base available in that state or
 - Stay exceeds 183 days in any 12 months period
 - Amount taxable – only amount attributable to fixed base or activities carried out in source state
 - ✓ OECD model convention deleted this article in 2001
 - ✓ Calculation of number of days
- **Other income**
 - ✓ Income not dealt with any of articles of the treaty
 - State in which income arises
 - Amount taxable – only amount attributable to fixed base or activities carried out in source state
 - ✓ Such income could also be taxed in other State
 - If the Income is effectively connected with right/ property of the PE or fixed base is the other state
 - If the income arises in the other state

Most Favoured Nation (MFN) Clause

- Normally benefit under this clause is restricted to a specific group like OECD countries or developing countries
- Benefit provided is normally with respect to following -
 - ✓ Rates of taxes
 - ✓ Liability to tax
 - ✓ Deductions permissible
- Attempts to avoid discrimination between residents of different countries
- MFN clause usually found in Protocols and Exchange of notes
- Ensures equal treatment between a subset of countries
- Extends similar benefits to one country as extended to certain other countries

Most Favoured Nation (MFN) Clause

Generally worded MFN clause in the protocol -

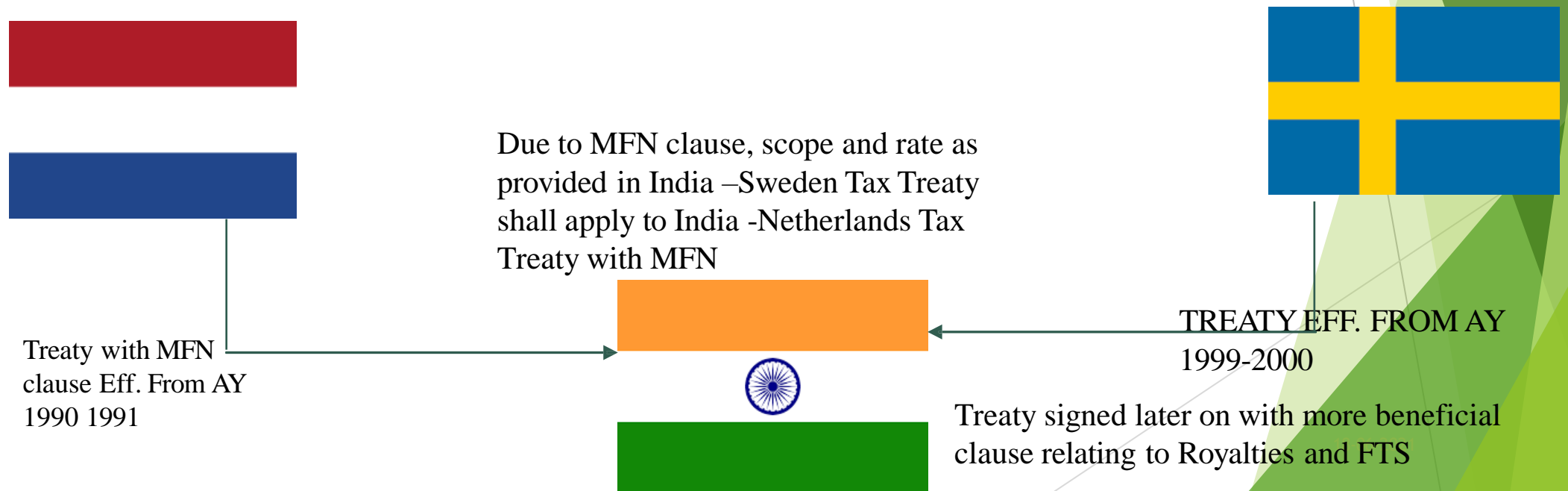
“In respect of Dividends, Interest, Royalties, FTS and payment for use of equipment's if under the Convention,

Agreement or Protocol signed after 1st Sept 1989 between India and a third State which is a member of the OECD, India limits its taxation at source to a rate lower, or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention on the said items of income shall also apply under this Convention..”

Most Favoured Nation (MFN) Clause

Applying the MFN Clause -

Example In a MFN situation, generally, one of the contracting states (say India) to the Double Tax Avoidance Agreement (“Tax Treaty”) grants the residents of the other contracting state (say Netherlands), the same beneficial treatment made available by it (that is, by India) to the resident of a third country (say Sweden) with whom it has entered into a Tax Treaty



Anti-avoidance provisions

- Article 26 - Exchange of Information
 - ✓ The competent authorities shall exchange information concerning taxes covered for the prevention of fraud or
 - ▶ evasion of such taxes.
- Article 9 - Associated Enterprise
 - ✓ Any profits which, would have accrued to one of the enterprises, but by reason of conditions in their
 - ▶ commercial or financial relations have not so accrued, may be included in the profits of that enterprise
 - ✓ Corresponding adjustments – provision exists in certain treaties
 - ✓ Secondary adjustments – not provided under domestic laws of India

Anti-avoidance provisions (contd.)

▪ Limitations of benefits

- ✓ Prevention of treaty shopping i.e. setting up of shell entities simply to take advantage of beneficial treaty provisions Corresponding adjustments – provision exists in certain treaties
- ✓ Provides for fulfillment of certain conditions/ tests by resident companies in order to be eligible to claim benefits of treaty
 - In the India – US treaty (Article 24)
 - Beneficial ownership test i.e. who are actual owners holding more than 50% of the company's shares and
 - Base erosion test i.e. income is not used directly or indirectly to meet liabilities outside the contracting states of a DTAA
 - Exclusion for active entities and listed entities

Anti-avoidance provisions (contd.)

- Protocol to India-Singapore treaty
 - Shell or conduit company set-up or where the affairs are arranged with a primary purpose to take the benefit of favorable capital gains clause

Elimination of double taxation

- **Relief from Double Taxation**

- ✓ Exemption method

- Full exemption; and
 - Exemption by progression

} Looks at income

- ✓ Credit method

- Full credit
 - Ordinary credit

} Looks at tax

- ✓ India follows mostly credit method

- ✓ Underlying tax credit

- ✓ Tax sparing

**Other
points**

Way forward

- Reaching a global consensus on how exactly to tax the digital economy
- Redefining “nexus” and PE concept
- Indian Significant Economic Presence related threshold – appropriate or too wide? How the same is effective till treaties are not amended?
- Operationalization of the Principal Purpose Test under the DTAAs amended by MLI
- Reaching a global consensus on Global minimum tax

THANK YOU

Phone : 9446360080

Email: satheesanregionalcouncil@gmail.com

Disclaimer

The information provided in this presentation is for informational purposes only, and should not be construed as legal advice on any subject matter. No recipients of this presentation, clients or otherwise, should act or refrain from acting on the basis of any content included in this presentation without seeking the appropriate legal or other professional advice on the particular facts and circumstances at issue. The presenter expressly disclaims all liability in respect to actions taken or not taken based on any or all the contents of this presentation.