

DIRECT TAX CODE 2009

Impact on Cross Border Transactions

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Building Business Partnerships

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PRESENTATION OUTLINE

- ▲ General Provisions
- ▲ International Tax Provisions
- ▲ Corporate Tax Provisions
- ▲ Mergers and Acquisitions
- ▲ Transfer Pricing Provisions
- ▲ Tax Withholding

General Provisions

General

- ▲ The Direct Tax code ('DTC') will come in to force on **April 1, 2011**
- ▲ **Tax rate for Companies** (foreign and domestic) reduced to 25%
- ▲ **Foreign Companies** doing business in India to suffer an additional 'branch profit tax' at 15% of Profit after Tax ('PAT')
- ▲ New **Rates** of Tax for Individuals
- ▲ Capital gains tax **rates** enhanced and distinction between short term and long term capital gains removed

General

- ▲ Preferred status of 'Not Ordinarily Resident' abolished
- ▲ Residents to be taxed on Global Income
- ▲ Non residents to be taxed only on India sourced income
- ▲ Foreign companies to be treated as '**resident**' in **India** even when **part** control and management situated in India (*Impact*)
- ▲ Time Limits for tax filings, Initiations & Completion of tax assessments revised

International Tax Provisions

General

FOREIGN COMPANY		
Category	Existing	As per DTC
Corporate tax rate	40%	25%
Additional 'branch profit' tax	Nil	15% Not linked to repatriation
Allowances for Head Office Expenditure	5% of net profit	0.5% of sales/turnover/gross receipts
Royalty and Fees for Technical Services- Presumptive	10% on gross income	20% on gross income
Royalty and Fees for Technical Services- Net Income basis	Permitted u/s 44DA of the IT Act	No specific provision
Tax Residency Certificate	Not mandatory	Mandatory

Relief from Double taxation

- ▲ As earlier, power has been given to Central Government to enter in to an agreement with the government of any country to avoid the Double taxation
- ▲ Provisions of DTAA and DTC have been brought at par
- ▲ In case of conflict, **provisions of code would override existing tax treaties**

GAAR

- ▲ **General Anti Avoidance Rules (GAAR)** introduced to give sweeping discretionary powers to the Commissioners of Income-tax (CIT) to declare an arrangement as ‘impermissible’ if the same has been entered for obtaining tax benefit **and** lacks commercial substance. The CIT may suggest amendments or completely **disregard or re-characterize such arrangement**
- ▲ Onus to establish **commercial substance** shifted to the tax-payer
- ▲ GAAR /Anti avoidance measures to override provisions of Tax Treaty
- ▲ **GAAR Examples:** Thin Capitalization, Treaty Shopping, Transfer of IPR’s

Impact of GAAR provisions

- ▲ Sweeping powers with Commissioners of Income tax to question any transaction
- ▲ Time taken to execute transactions would enhance significantly
- ▲ Element of uncertainty will likely discourage investors

Corporate Tax Provisions

Tax Rates

RESIDENT COMPANY

Category	Existing Rate	As per DTC
Income Tax	30%	25%
Minimum Alternate Tax	18% of adjusted book profits	<p>Linked to gross assets</p> <ul style="list-style-type: none"> • 0.25% of gross assets for Banking companies • 2% of gross assets for other companies.
Dividend Distribution Tax	15% (dividend exempt for recipients)	15% (dividend exempt for recipients)

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General

Category	Existing	As per DTC
Carry forward of Business losses	Allowed up to end of 9 years from relevant fiscal year	Unlimited Carry forward of Business losses
MAT Credit	Allowed up to 11 years from relevant fiscal year	No credit for MAT in subsequent years.
Approach for calculating taxable profit	Taxable Profit = Business Profit +/- specific adjustments	<u>Income- Expenses model</u>

Tax Incentive

- ▲ Area/ profit linked incentives replaced with Investment linked incentives
- ▲ **All investments in the form of capital & revenue expenditure** will be deducted while determining taxable profit
- ▲ Loss shall be allowed to be carried forward till it is absorbed completely
- ▲ **Incentives vs. MAT**
DTC allows deduction of investment in capital assets and conversely tax those assets through MAT

Mergers & Acquisitions

General

Category	Existing	As per DTC
Taxability of sale of business assets	Income from Capital gains	Profits and gains of business and profession
Taxability of slump sale	Income from Capital gains	Profits and gains of business and profession
Capital gains on transfer of capital assets between a holding company and a subsidiary	Tax free, provided that holding company holds the 100% capital of latter for 8 years	Tax free, provided that holding company holds the 100% capital of latter (8 year requirement eliminated)

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Reorganisation

- ▲ **Business reorganisation within resident entities**, through a demerger or amalgamation would be tax neutral
- ▲ **Gains involving a foreign company** may not be tax neutral unless such company is regarded as resident under the expanded definition (i.e. control & management)
- ▲ Accumulated losses of the predecessor deemed to be the loss of successor if the successor satisfies the test of continuity of business

Transfer Pricing Provisions

General

- ▲ Concept of Advance Pricing Agreement (APA) introduced.
- ▲ The threshold limits prescribed for consideration two enterprises as related have been revised
- ▲ Modifications have been made in the procedures
- ▲ The determination of arm's length price shall be subject to **safe harbour rules**
- ▲ Penalties have been rationalised
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Impact of TP Provisions

- ▲ APA provides certainty on the issue of TP and prevents time consuming litigations
- ▲ Right to Information (RTI) will not be applicable to Income Tax so the tax authorities are not obliged to disclose the criteria chosen for selecting the case for scrutiny
- ▲ The threshold limits for declaring an entity as an associated enterprise is certainly unfair (e.g. 10% holding in the foreign entity may not give a shareholder even minimum control over its activities and DTC declaring them as ‘associated’)

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Tax Withholding

General

- ▲ Rates of Withholding tax at source for resident and non resident deductees have been revised
- ▲ Scope of Withholding tax at source has been widened by covering all categories of income in case of residents unless specifically exempted (e.g. Non compete fees, Compulsory acquisition of immovable property)
- ▲ Discontinued lower tax withholding certificate
- ▲ **Non compliance to TDS provisions** will result into disallowance of payment. To be allowed subsequently only if TDS is paid within 2 years
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Tax Rates

Old Income Slab (Rs)	New Income Slab (Rs)	Tax Rates
Upto 160,000 (1)	Upto 160,000 (1)	NIL
160,000 – 500,000	160,001 – 1,000,000	10%
500,001 – 800,000	1,000,001 – 2,500,000	20%
Above 800,000	Above 2,500,000	30%

(1) – Rs 190,000 for women and Rs 240,000 for senior citizens

General

Category	Existing	As per DTC
Due Date for filing the return of Income	-31 st July of the A.Y for non business/ non corporate assessee	-30 th June following the F.Y for non business/ non corporate assessee
	- 30 th September of the A.Y for other assessee	- 31 st August following the F.Y for other assessee
Assessment	No cases shall be reopened after 6 years from the end of the relevant A.Y	No cases shall be opened after 7 years from the end of the relevant F.Y

AE's

Criteria	Current Threshold	Proposed Threshold
Shareholding	26% or more voting power	10% or more voting power
Loan by one enterprise (as a % of BV of assets of other)	51% or more	26% or more
No of directors appointed in other company	More than half	More than one-third
Supply of Raw Materials	90% or more in value	Two third or more in value

Procedures

Particulars	Current	Proposed
Filing of Accountant report with	Assessing Officer (AO)	Transfer Pricing Officer (TPO)
Time period for filing the Accountant report	30 th September of the Assessment Year	31 st August following the Financial Year
Time Limit for Selection of TP Cases	Selected as part of assessment proceedings	Within 2 M from the end of FY in which TP certificate is filed
Time Limit for Completion of TP Assessment	43 M from the end of the relevant FY	42 M from the end of the relevant FY

Income - Expense Model

Profits from Business = Gross Earnings – Business Expenditure

Business Expenditure = Operating Expenditure + Permitted Financial Charges + Capital Allowances

Gross Earnings	Operating Expenditure	Capital Allowances
<ul style="list-style-type: none"> -Income from each business to be computed separately and later aggregated - Assets of the business equal to Business assets and Investment assets 	<ul style="list-style-type: none"> -Any expense wholly and exclusively for business purposes -Specific payments only allowed as deduction on payment basis. 	<ul style="list-style-type: none"> -Depreciation including initial depreciation -Scientific research deduction and development allowances

APA

- ▲ APA is an agreement between tax-payer and tax authorities for upfront determination of Arm Length Price of an international transaction. Involves negotiation
- ▲ Validity of the APA is limited to 5 consecutive financial year
- ▲ APA is binding on Taxpayer and Income Tax Authorities.

Meaning

Reorganisation of business means reorganisation of business of two or more residents involves:

- Amalgamation
- Demerger
- Merger under a scheme sanctioned by the Central Government under the Banking Regulation Act 1949

Impact

- ▲ The enlarged definition may impact global organizations having corporate head-quarters in India
- ▲ A foreign company as well as Indian companies having subsidiaries abroad, whose control and management partly lies in India
- ▲ What is “Part Control and management” add to litigation

Tax Withholding

Tax Withholding Rates – Resident Deductees

Nature of Payment	Current Rate	Proposed Rate
Payment for contracts	Individual/HUF – 1% Others – 2%	1%
Rent for Plant/Machinery/Equipment	2%	1%
Non Compete Fee/Compulsory Acquisition of Immovable Property/Other Income	-	10%

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Tax Withholding

Tax Withholding Rates – Non - Resident Deductees

Nature of Payment	Current Rate	Proposed Rate
Salary	Average Rate of Income Tax	No rate Prescribed
Capital Gains	20%/15%/10%	30%
Royalty/FTS	10%/20%	20%
Any Other Income	30%/40%	35%

Rates

- ▲ For corporate assessee – 20% to 25%
- ▲ For non corporate assessee – 20% to 30%

THANK YOU

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