

# ***BEPS ACTION PLANS & IMPACT ON INDIA***

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## A. Introduction

Political leaders, media outlets, and civil society around the world expressed growing concern about tax planning by multinational enterprises (MNEs) that makes use of gaps in the interaction of different tax systems to artificially reduce taxable income or shift profits to low-tax jurisdictions in which little or no economic activity is performed.

In response to this concern, and at the request of the G20, the Organisation for Economic Co-operation and Development (OECD) published an Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan, OECD, 2013) in July 2013. The 40 page detailed report, which was negotiated and drafted with the active participation of its member states, contained 15 separate action plans or work streams, some of which were further split into specific actions or outputs. The Plan was squarely focused on addressing these issues in a coordinated, comprehensive manner, and was endorsed by G20 leaders and finance ministers.

In India, the international tax system also changed rapidly as a result of coordinated action by OECD and also as a result of unilateral measures designed by individual countries, both intended to tackle concerns over base erosion and profit shifting (BEPS) and perceived international tax avoidance techniques of high-profile multinationals.

The recommendations of the BEPS Project led by the OECD, culminating into issuance of final BEPS reports in October 2015, are at the root of much of the coordinated activity, albeit, the timing and method of implementation by countries involved in this project of these recommendations may vary. Since issuance of the reports on action plan, the next phase shall be focused on dealing with outstanding or additional work for Action Plans, implementation and monitoring of BEPS reports.

This note provides

- Summary of BEPS Action Plans
- Status of Implementation of BEPS by select Countries
- Implementation of BEPS Actions Plans by India
- Snapshot of implementation of BEPS Action plans by select Countries
- Analysis of impact of BEPS Actions Plans to few sectors at India

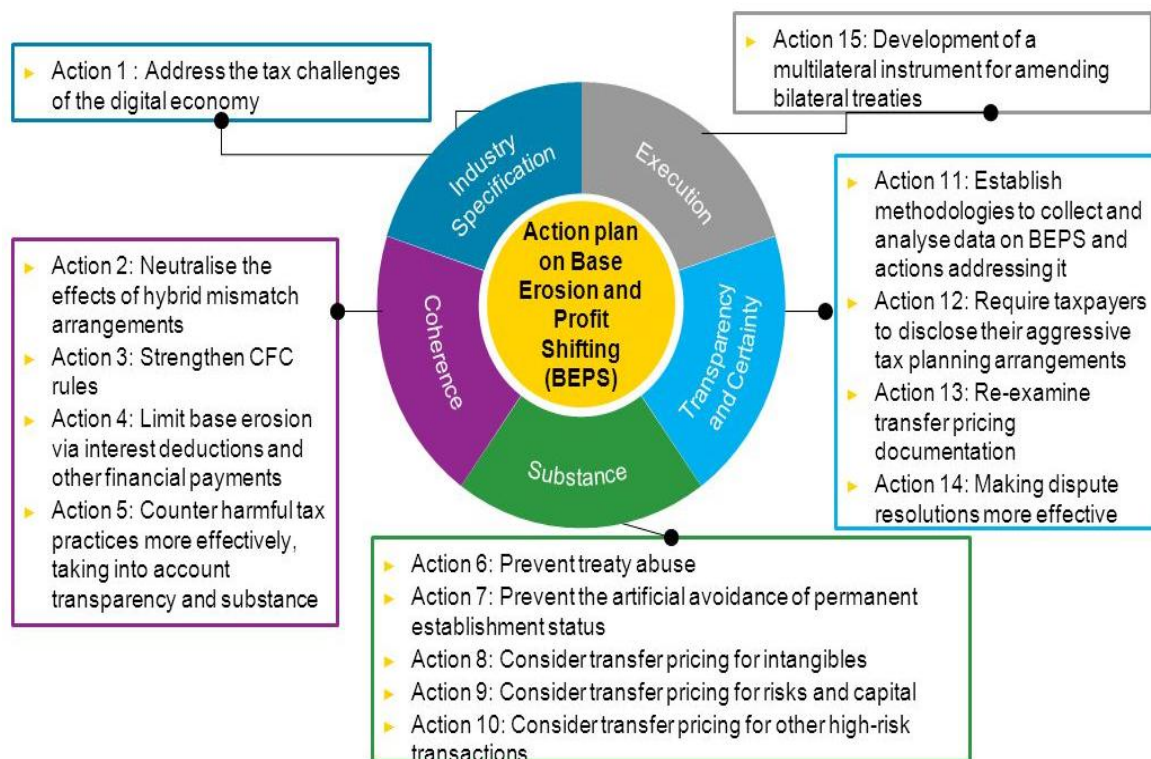
Mumbai  
23<sup>rd</sup> January, 2017

## B. Summary of BEPS & Its Action Plans

### B. 1. Introduction to BEPS

Base erosion and profit shifting (BEPS) is a tax avoidance strategy used by multinational companies, wherein profits are shifted from jurisdictions that have high taxes (such as the United States and many Western European countries) to jurisdictions that have low (or no) taxes (so-called tax havens).

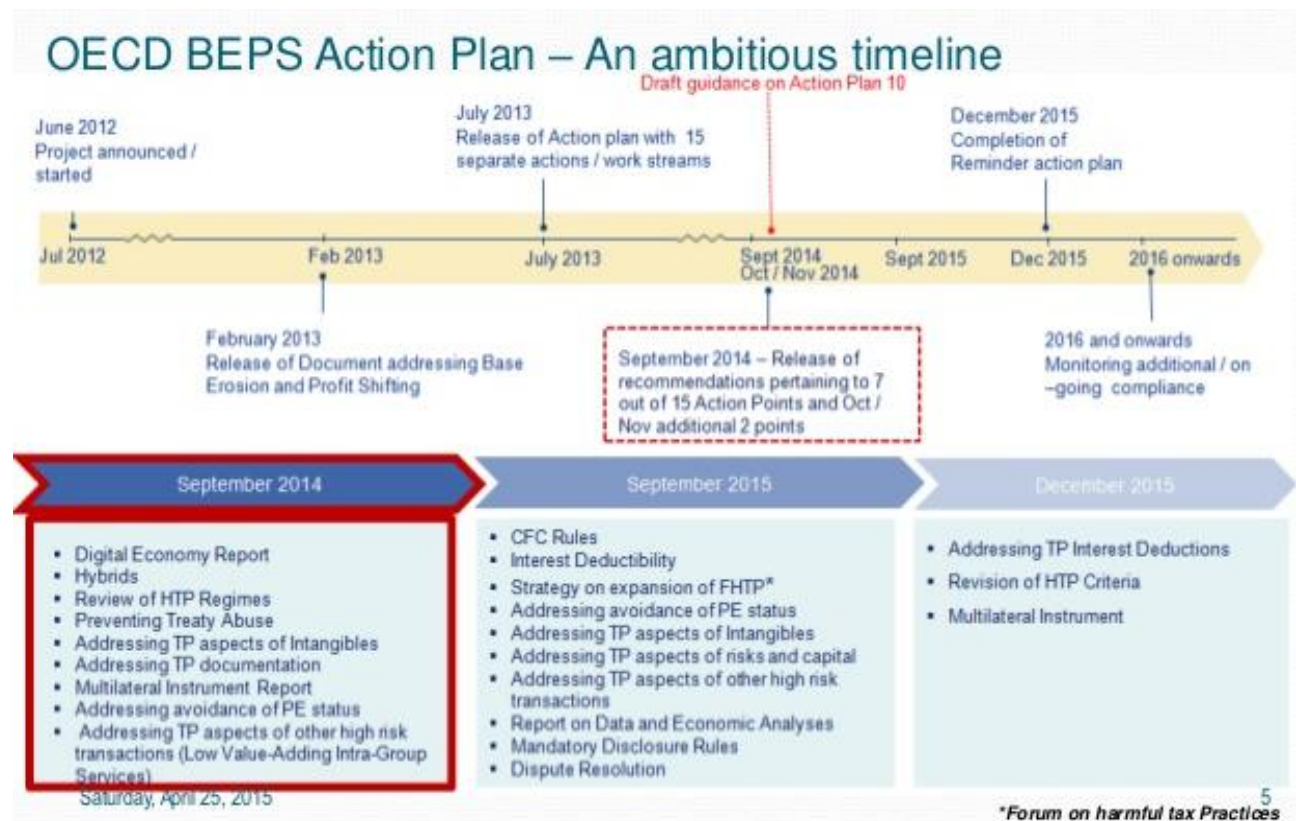
OECD broadly divided the BEPS Action Plans under 5 categories. The diagram below summarises BEPS Action Plans under the said 5 categories.





## B. 2. Journey of BEPS so far

It was in June 2012 that OECD announced the BEPS Project. OECD outlined the timeline of the said ambitious project.



It is heartening to note that the timeline was adhered by OECD in spite of the complexity of the subject & involvement of so many participants in the BEPS Project. 82 countries are participating in the BEPS project including G20 members, developed economies & developing countries.

## B. 3. Key Points / Highlights for Action Plans

OECD released 7 reports<sup>1</sup> in the year 2014 & 6 reports<sup>2</sup> in the year 2015. Each report dealt with the subject quite exhaustively. Having regard to the complexity of the subject & the volume of the information & data available in each of the report, to summarise the same in short version is a challenging & difficult task. However, an endeavor has been made to provide accurate and exhaustive summary of each of the reports issued by OECD on Action Plan 1 to 15.

### Action Plan 1: Addressing Tax Challenges of the Digital Economy

#### Backdrop

In September 2013, the Task Force on the Digital Economy (“TFDE”) was established as a subsidiary body of the OECD Committee on Fiscal Affairs. The TFDE determined that the digital economy is increasingly becoming the economy itself and that attempting to ring-fence the digital economy from the rest of the economy for tax purposes would not be practical. Instead, the TFDE identified some key features of the digital economy that exacerbate the BEPS risks, and work on other actions took these risks into consideration to ensure that the proposed solutions addressed the additional risks of BEPS in the digital economy.

#### Analysis

The digital economy raises broader tax challenges for policy makers. These challenges relate in particular to nexus, data, and characterisation for direct tax purposes, which often overlap with each other. The digital economy also creates challenges for value added tax (VAT) collection, particularly where goods, services and intangibles are acquired by private consumers from suppliers abroad.

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<sup>1</sup> Reports released in 2014: **Action Plan 1:** Addressing Tax Challenges of the Digital Economy, **Action Plan 2:** Neutralising the Effects of Hybrid Mismatch Arrangements, **Action Plan 5:** Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, **Action Plan 6:** Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, **Action Plan 8 - 10:** Aligning Transfer Pricing Outcomes with Value Creation, **Action Plan 13:** Transfer Pricing Documentation and Country-by-Country Reporting, **Action Plan 15:** Developing a Multilateral Instrument to Modify Bilateral Tax Treaties.

<sup>2</sup> Reports released in 2015: **Action Plan 3:** Controlled foreign company (CFC), **Action Plan 4:** Interest Deduction and Other Financial Payments, **Action Plan 7:** Preventing the Artificial Avoidance of Permanent Establishment Status, **Action Plan 11:** Measuring and Monitoring BEPS, **Action Plan 12:** Mandatory Disclosure Rules, **Action Plan 14:** Making Dispute Resolution Mechanisms More Effective.

The digital economy is the result of a transformative process brought by information and communication technology (ICT), which has made technologies cheaper, more powerful, and widely standardised, improving business processes and bolstering innovation across all sectors of the economy.

### **Recommendation**

The TFDE discussed and analysed a number of potential options to address challenges of digital economy, including through an analysis of their economic incidence, and concluded to introduce:

- a new nexus in the form of a significant economic presence,
- a withholding tax on certain types of digital transactions, and
- an equalisation levy.

To these above aims, the work will continue following the completion of the other follow-up work on the BEPS Project. This future work will be done in consultation with a broad range of stakeholders, and on the basis of a detailed mandate to be developed during 2016 in the context of designing an inclusive post-BEPS monitoring process. A report reflecting the outcome of the continued work in relation to the digital economy should be produced by 2020.

It was also suggested that countries could, however, introduce any of these three options in their domestic laws as additional safeguards against BEPS, provided they respect existing treaty obligations, or in their bilateral tax treaties.

### **Action Plan 2: Neutralising the Effects of Hybrid Mismatch Arrangements**

#### **Backdrop**

Hybrid mismatch arrangements exploit differences in the tax treatment of an entity or instrument under the laws of two or more tax jurisdictions to achieve double non-taxation, including long-term deferral. These types of arrangements are widespread and result in a substantial erosion of the taxable bases of the countries concerned. They have an overall negative impact on competition, efficiency, transparency and fairness.

#### **Analysis**

The aim of this action is to simply prevent double non-taxation through interaction of domestic and treaty rules by eliminating tax benefits of mismatches and multiple deductions, deductions without corresponding taxation and multiple tax credits.



## Recommendation

The report recommends countries to adopt both primary and defensive rules; it is not strictly necessary for every country to introduce hybrid mismatch rules for them to be effective. It is more important to the successful operation of the rules that countries' hybrid mismatch rules are consistent with each other, both in their operation and scope. The idea of common approach is that countries that wish to tackle hybrids do so in a way that makes the rules easier for all countries to apply.

The effect of having both a primary and defensive rule is that a country does not need to rely on the domestic laws of another country in order to neutralize hybrid mismatches. The Hybrid report recommendations, once implemented by a country, will neutralize the hybrid mismatch effects of "US check-thebox planning" in those countries.

### Action Plan 3: Controlled foreign company (CFC)

## Backdrop

Controlled foreign company (CFC) rules respond to the risk that taxpayers with a controlling interest in a foreign subsidiary can strip the base of their country of residence and, in some cases, other countries by shifting income into a CFC. Without such rules, CFCs provide opportunities for profit shifting and long-term deferral of taxation.

## Analysis

Since the first CFC rules were enacted in 1962, an increasing number of jurisdictions have implemented these rules. Currently, 30 of the countries participating in the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project have CFC rules, and many others have expressed interest in implementing them. However, existing CFC rules have often not kept pace with changes in the international business environment, and many of them have design features that do not tackle BEPS effectively.

## Recommendation

The recommendation made in the OECD report deals with effective implementation of CFC rules to prevent taxpayers from shifting profits to foreign subsidiaries. It recognises that while implementing CFC rules special treatment needs to be accorded to income from intellectual property, services and digital transactions. It recommends substantive reporting requirement for entities having CFCs.

## **Action Plan 4: Interest Deduction and Other Financial Payments**

### **Backdrop**

It is an empirical matter of fact that money is mobile and fungible. Thus, multinational groups may achieve favourable tax results by adjusting the amount of debt in a group entity. The influence of tax rules on the location of debt within multinational groups has been established in a number of academic studies and it is well known that groups can easily multiply the level of debt at the level of individual group entities via intra group financing.

### **Analysis**

Financial instruments can also be used to make payments which are economically equivalent to interest but have a different legal form, therefore escaping restrictions on the deductibility of interest. Base Erosion and Profit Shifting (BEPS) risks in this area may arise in three basic scenarios:

- Groups placing higher levels of third party debt in high tax countries.
- Groups using intragroup loans to generate interest deductions in excess of the group's actual third party interest expense.
- Groups using third party or intragroup financing to fund the generation of tax exempt income.

### **Recommendation**

The OECD report recommends that the approach to be supported by targeted rules to prevent its circumvention, for example by artificially reducing the level of net interest expense. It also recommends that countries consider introducing rules to tackle specific BEPS risks not addressed by the recommended approach, such as where an entity without net interest expense shelters interest income.

## **Action Plan 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance**

### **Backdrop**

The OECD produced a report in 1998 on “harmful tax practices” that has largely gathered dust since then. It is now proposed to revamp this work. A new suggestion is for

“compulsory spontaneous exchange on rulings related to preferential regimes”, although it is unclear how this would work.

### Analysis

The elements of a strategy to engage with countries other than OECD Members and BEPS Associates in order to achieve a level playing field and avoid the risk that the work on harmful tax practices could displace regimes to third countries is outlined in the Report, together with the status of discussions on the revisions or additions to the existing framework. These aspects of the work will be taken forward in the context of the wider objective of designing a more inclusive framework to support and monitor the implementation of the BEPS measures.

### Recommendation

The report issued by OECD sets out a minimum standard based on an agreed methodology to assess whether there is substantial activity in a preferential regime to claim consequential benefits. In other words, the substantial activity test has been given prime importance in a preferential regime. Also, sharing of tax rulings having BEPS concerns has been suggested as a measure of garnishing transparency.

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### Action Plan 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances

#### Backdrop

International tax issues have never been as high on the political agenda as they are today. The integration of national economies and markets has increased substantially in recent years, putting a strain on the international tax rules, which were designed more than a century ago. Weaknesses in the current rules create opportunities for base erosion and profit shifting (BEPS), requiring bold moves by policy makers to restore confidence in the system and ensure that profits are taxed where economic activities take place and value is created.

## Analysis

Action 6 of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project identifies treaty abuse, and in particular treaty shopping, as one of the most important sources of concerns.

Taxpayers engaged in treaty shopping and other treaty abuse strategies undermine tax sovereignty by claiming treaty benefits in situations where these benefits were not intended to be granted, thereby depriving countries of tax revenues. Countries have therefore agreed to include anti-abuse provisions in their tax treaties, including a minimum standard to counter treaty shopping.

## Recommendation

The following approach is recommended to deal with these:

First, a clear statement states that entering into a tax treaty intended to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements will be included in tax treaties.

Second, a specific anti-abuse rule, the limitation-on-benefits (LOB) rule, which limits the availability of treaty benefits & the said rules are based on the legal nature, ownership in, and general activities of the entity, seek to ensure that there is a sufficient link between the entity and its State of residence. Such limitation-on-benefits provisions are currently found in treaties concluded by a few countries and have proven to be effective in preventing many forms of treaty shopping strategies.

Third, in order to address other forms of treaty abuse, including treaty shopping situations that would not be covered by the LOB rule described above, a more general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purposes test or “PPT” rule) will be included in the OECD Model Tax Convention.

### Action Plan 7: Preventing the Artificial Avoidance of Permanent Establishment Status

## Backdrop

This Action is focused on the need to update the OECD tax treaty definition of permanent establishment (‘PE’) (Article 5 in the OECD model treaty) in order to prevent abuses of the threshold allocating taxing rights for trading activities to different jurisdictions. As part of

this work the OECD is considering the modernisation of the PE threshold in relation to digital cross-border business, in line with the work on Action 1.

### **Analysis**

Tax treaties generally provide that the business profits of a foreign enterprise are taxable in a State only to the extent that the enterprise has in that State a permanent establishment (PE) to which the profits are attributable. The definition of PE included in tax treaties is therefore crucial in determining whether a non-resident enterprise must pay income tax in another State.

### **Recommendation**

This OECD action plan includes the changes that will be made to the definition of PE in Article 5 of the OECD Model Tax Convention, which is widely used as the basis for negotiating tax treaties, as a result of the work on Action 7 of the BEPS Action Plan. Together with the changes to tax treaties proposed in the Report on Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, OECD, 2015), the changes recommended in this report will restore taxation in a number of cases where cross-border income would otherwise go untaxed or would be taxed at very low rates as result of the provisions of tax treaties. Taken together, these tax treaty changes will enable countries to address BEPS concerns resulting from tax treaties, which was a key focus of the work mandated by the BEPS Action Plan.

## **Action Plan 8 - 10: Aligning Transfer Pricing Outcomes with Value Creation**

### **Backdrop**

Over several decades and in step with the globalisation of the economy, world-wide intra-group trade has grown exponentially. Transfer pricing rules, which are used for tax purposes, are concerned with determining the conditions, including the price, for transactions within an MNE group resulting in the allocation of profits to group companies in different countries.

The impact of these rules has become more significant for business and tax administrations with the growth in the volume and value of intra-group trade. As the Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan, OECD, 2013) identified, the existing international standards for transfer pricing rules can be misapplied so that they result in outcomes in which the allocation of profits is not aligned with the economic activity that produced the profits. The work under Actions 8-10 of the BEPS Action Plan

has targeted this issue, to ensure that transfer pricing outcomes are aligned with value creation.

### Analysis

Action 8 looked at transfer pricing issues relating to controlled transactions involving intangibles, since intangibles are, by definition, mobile and they are often hard to value. Misallocation of the profits generated by valuable intangibles has heavily contributed to BEPS. Under Action 9, contractual allocations of risk are respected only when they are supported by actual decision-making and thus exercising control over these risks. Action 10 has focused on other high-risk areas, including 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 multinational group, and the use of certain type of payments between members of the multinational group (such as management fees and head office expenses) to erode the tax base in the absence of the alignment with the value creation. The combined report contains revised guidance which responds to these issues and ensures that transfer pricing rules secure outcomes that better align operational profits with the economic activities which generate them.

### Recommendation

Following recommendations cement the importance of underlying substance and value creation over legal ownership/funding:

The new guidelines emphasise the need to accurately delineate a transaction so that the conduct of parties will replace contractual arrangements where they are incomplete or out of line with the conduct. Transactions can be disregarded for TP purposes where they lack commercial rationality.

A safe harbour for low value adding services recommended, with a light touch benefits test and prescribed net cost plus margin of 5%.

### Action Plan 11: Measuring and Monitoring BEPS

### Backdrop

The adverse fiscal and economic impacts of base erosion and profit shifting (BEPS) have been the focus of the OECD/G20 BEPS Project since its inception. Although measuring the scale of BEPS proves challenging given the complexity of BEPS and the serious data



limitations, today we know that the fiscal effects of BEPS are significant. The findings of the work performed since 2013 highlight the magnitude of the issue, with global corporate income tax (CIT) revenue losses estimated between 4% and 10% of global CIT revenues, i.e. USD 100 to 240 billion annually. Given developing countries' greater reliance on CIT revenues, estimates of the impact on developing countries, as a percentage of GDP, are higher than for developed countries.

### **Analysis**

Empirical analysis indicates that BEPS adversely affects competition between businesses, levels and location of debt, the location of intangible investments, and causes fiscal spillovers between countries and wasteful and inefficient expenditure of resources on tax engineering.

### **Recommendation**

The Action Plan recommends that the OECD work with governments to report and analyse more corporate tax statistics and to present them in an internationally consistent way. For example, statistical analyses based upon Country-by-Country Reporting data have the potential to significantly enhance the economic analysis of BEPS. These improvements in the availability of data will ensure that governments and researchers will, in the future, be better able to measure and monitor BEPS and the actions taken to address BEPS.

## **Action Plan 12: Mandatory Disclosure Rules**

### **Backdrop**

The lack of timely, comprehensive and relevant information on aggressive tax planning strategies is one of the main challenges faced by tax authorities worldwide. Early access to such information provides the opportunity to quickly respond to tax risks through informed risk assessment, audits, or changes to legislation or regulations. Action 12 of the Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan, OECD, 2013) recognised the benefits of tools designed to increase the information flow on tax risks to tax administrations and tax policy makers.

### **Analysis**

Mandatory disclosure regimes should be clear and easy to understand, should balance additional compliance costs to taxpayers with the benefits obtained by the tax administration, should be effective in achieving their objectives, should accurately

identify the schemes to be disclosed, should be flexible and dynamic enough to allow the tax administration to adjust the system to respond to new risks (or carve-out obsolete risks), and should ensure that information collected is used effectively

### Recommendation

The recommendations for this action plan do not represent a minimum standard and countries are free to choose whether or not to introduce mandatory disclosure regimes. Where a country wishes to adopt 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 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: Transfer Pricing Documentation and Country-by-Country Reporting

#### Backdrop

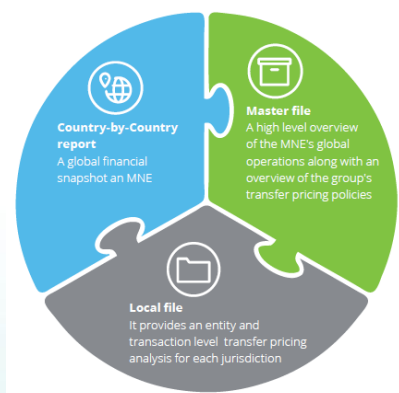
Action 13 of the Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan, OECD, 2013) requires the development of “rules regarding transfer pricing documentation to enhance transparency for tax administration, taking into consideration the compliance costs for business. The rules to be developed will include a requirement that MNEs provide all relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template”.

#### Analysis

Implementation of BEPS leads to improved and better coordinated transfer pricing documentation and increases the quality of information provided to tax administrations and hence limit the compliance burden on businesses.

### Recommendation

In order to implement BEPS, a three-tiered standardised approach to transfer pricing documentation has been developed.



- A **master file** containing standardized information relevant for all multinational enterprises (MNE) group members;

- A **local file** referring specifically to material transactions of the local taxpayer; and
- A **Country-by-Country (Cubic) report** containing certain information relating to the global allocation of the MNE's income and taxes paid together with certain indicators of the location of economic activity within the MNE group.

#### **Action Plan 14: Making Dispute Resolution Mechanisms More Effective**

##### **Backdrop**

Eliminating opportunities for cross-border tax avoidance and evasion and the effective and efficient prevention of double taxation are critical to building an international tax system that supports economic growth and a resilient global economy. Countries agree that the introduction of the measures developed to address base erosion and profit shifting pursuant to the Action Plan of BEPS should not lead to unnecessary uncertainty for compliant taxpayers and to unintended double taxation. Improving dispute resolution mechanisms is therefore an integral component of the work on BEPS issues.

##### **Analysis**

The report on Action 14 is more in the nature of pre-meditated work that may be required as a consequence of implementation of the BEPS project. There is an apprehension that implementation of the BEPS project may result in increased double taxation. Recognising the importance of removing double taxation as an obstacle to cross-border trade and investment, countries have committed to a minimum standard with respect to the resolution of treaty-related disputes. In this respect, mutual assessment procedures (MAPs) have been recognised in particular, as a tool for timely resolution of disputes.

##### **Recommendation**

Minimum standards recommended by OECD for this action plan are as follows:

- Ensure that treaty obligations related to the mutual agreement procedure are fully implemented in good faith and that MAP cases are resolved in a timely manner;
- Ensure the implementation of administrative processes that promote the prevention and timely resolution of treaty-related disputes; and
- Ensure that taxpayers can access the MAP when eligible.

## **Action Plan 15: Developing a Multilateral Instrument to Modify Bilateral Tax Treaties**

### **Backdrop**

Quick implementation of tax treaty-related BEPS measures has been recognised as a need of the day for the BEPS project to be successful. Amendment of thousands of bilateral tax treaties may be time-consuming and may not result in consistent implementation of BEPS measures which may result in the failure of the BEPS project.

### **Analysis**

Action 15 of the BEPS Action Plan provides for an analysis of the tax and public international law issues related to the development of a multilateral instrument to enable countries that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties. On the basis of this analysis, interested countries will develop a multilateral instrument designed to provide an innovative approach to international tax matters, reflecting the rapidly evolving nature of the global economy and the need to adapt quickly to this evolution.

### **Recommendation**

The BEPS report concludes that a multilateral instrument is desirable and feasible, and that negotiations should be convened quickly. This report also explores the questions raised by the use of a targeted multilateral instrument to modify tax treaties, and provides a high-level analysis of both the technical (public international law and international tax law) and political issues that arise. It highlights the feasibility of a multilateral approach as the way to streamline the implementation of the BEPS Action Plan with a view to responding to the current state of urgency, and also to improve efficiency. It concludes that a multilateral instrument is desirable and feasible and it should be negotiated through an International Conference open to G20 countries, OECD members and other interested countries and convened under the aegis of the OECD and the G20.

#### **B. 4. Way ahead for BEPS**

BEPS action plans to improve the coherence of international tax rules reinforce its focus on economic substance and ensure a more transparent tax environment. Having regard to the BEPS recommendations, business models are likely to be subjected to increased scrutiny by tax authorities, especially assertion of permanent establishment on accessibility of websites from source country, presence of marketing or sales personnel in source country or for presence of some equipment. It is likely that the revenue authorities may attempt to tax on account of 'significant digital presence' in source country.

Further, there is a likelihood of increased focus on withholding tax implications on digital products and services to non-residents. It is imperative that MNEs in this space align their tax models in line with the OECD BEPS action plans and also need to track tax policy changes as regards assertion of PE and taxation of digital products.

The work on BEPS shall continue in the year 2017 which will include the additional work on implementation and monetary of BEPS Action Plans.

## C. Status of Implementation of BEPS by select Countries

OECD published Action Plans with the aim to address BEPS concerns by establishing international coherence of corporate income tax systems. For this purpose, countries and jurisdictions were invited to express their interest to join this framework as Associates, to participate on equal footing and to commit to implement the comprehensive BEPS Package. Accordingly, many countries have participated and started implementing some of the action plans. Following is the summary of the status of implementation of BEPS Action Plans on select countries:

### C. 1. Australia

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>VAT on business to customers digital services (Action 1)</b>	The law imposing GST on supplies of digital products and other imported services by non-residents to Australian customers has been enacted.	Taxable supplies attributable to tax periods starting on or after 1 July 2017
<b>Hybrids (Action 2)</b>	Following a consultation initiated by the Board of Taxation on the implementation of anti-hybrid rules, the government released a report on 3 May 2016 as part of the 2016-17 federal budgets, and has confirmed that Australia will introduce anti-hybrid rules modelled on the OECD approach. However, legislation has not yet been drafted.	Payments made on or after 1 January 2018 or six months after the relevant law is enacted, whichever is later
<b>CFCs (Action 3)</b>	The Australian CFC rules are considered to be stronger than the OECD standards. No action is expected.	N/A
<b>Interest deductions (Action 4)</b>	The government has indicated that it is unlikely to change the existing thin capitalisation rules (based on debt-to-asset ratios) at this time (the rules were tightened in 2014).	N/A
<b>Harmful tax practices (Action 5)</b>	The Australian Taxation Office already has started exchanging rulings with other jurisdictions.	Occurring
<b>Prevent treaty abuse (Action 6)</b>	The government has indicated that Australia will include G20/OECD recommendations in all future bilateral tax treaty negotiations.	Occurring



Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Permanent establishment status (Action 7)</b>	Australia has taken unilateral action on PE issues through the enactment of the Multinational Anti-Avoidance Law (MAAL).	01-Jan-16
<b>Transfer pricing (Actions 8-10)</b>	The OECD's transfer pricing guidelines are incorporated in Australia's transfer pricing law (currently referring to the 2010 guidelines). The government confirmed in the May 2016 federal budget that it intends to give effect to the 2015 OECD transfer pricing recommendations with effect from 1 July 2016. However, legislation has not yet been drafted.	Once enacted, the law would apply as from 1 July 2016
<b>Disclosure of aggressive tax planning (Action 12)</b>	A government consultation is underway on the implementation of mandatory disclosure rules for taxpayers and tax advisers.	Not yet known
<b>Transfer pricing documentation (Action 13)</b>	Laws requiring CbC reporting and master and local file reporting have been enacted. The Australian approach broadly is in line with the G20/OECD approach.	01-Jan-16
<b>CbC reporting (Action 13)</b>	Australia has signed the multilateral competent authority agreement for the automatic exchange of CbC reports.	01-Jan-16
<b>Dispute resolution (Action 14)</b>	Australia is committed to binding arbitration.	Not yet known

## C. 2. Brazil

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>VAT on business to customers digital services (Action 1)</b>	Not yet known.	Not yet known
<b>Hybrids (Action 2)</b>	Brazil's tax authorities have introduced a cap limit on the deductibility of Interest on Net Equity (maximum interest rate limited to 5% per year). No further changes on hybrids are expected	CY 2015 N/A

Action	Notes on local country implementation	Expected timing/ Implemented date
	in the near future.	
<b>CFCs (Action 3)</b>	Brazil's CFC rules have been modified. No further changes are expected in the near future.	1 January 2015 (with an early adoption election for 1 January 2014) N/A
<b>Interest deductions (Action 4)</b>	Brazil's introduced thin capitalization rules that apply to intercompany foreign loans. The rules are based on debt- to-equity ratios, with more stringent rules applying to intercompany loans with a party resident in a tax haven jurisdiction. Transfer pricing rules require that foreign loans between related parties observe minimum/maximum market rates (Brazilian sovereign debt bonds and/ or LIBOR) plus a spread defined in the tax legislation. No further changes are expected in the near future.	2011 2012 N/A
<b>Harmful tax practices (Action 5)</b>	Brazilian legislation provides for rules disallowing deduction for payments made to tax havens ("black list") or tax privileged regimes ("grey list") jurisdictions where the payments do not satisfy "substance" requirements. Normative Ruling (NR) No. 1,658 enacted on 15 September 2016 addresses the concept of substantive economic activities of holding companies in the context of Brazil's grey list of privileged tax regimes. The NR may be considered an initial action by Brazil in the context of transparency and substance.	1 October 2016
<b>Prevent treaty abuse (Action 6)</b>	Not yet known.	Not yet known
<b>Permanent</b>	Not yet known.	Not yet known

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>establishment status (Action 7)</b>		
<b>Transfer pricing (Actions 8-10)</b>	Brazil's transfer pricing legislation diverges significantly from the current OECD guidelines. However, Brazil has adopted minimum/ maximum mark-ups for certain transfer pricing methods (e.g. resale price, cost plus methods). Intellectual property is not subject to transfer pricing scrutiny. No further changes to the transfer pricing rules are expected in the near future.	N/A
<b>Disclosure of aggressive tax planning (Action 12)</b>	In 2015, the tax authorities tried to introduce a mandatory disclosure regime, which was rejected by the Brazilian congress.	Not yet known
<b>Transfer pricing documentation (Action 13)</b>	Brazil's transfer pricing legislation diverges significantly from the current OECD guidelines, although Brazil has adopted extensive documentation and reporting requirements. Global studies and economic models are not accepted as documents since the country uses a transaction approach. No further changes to the transfer pricing rules are expected in the near future.	N/A
<b>CbC reporting (Action 13)</b>	Decree # 8,842, enacted on 30 August 2016, approves the Convention on Mutual Administrative Assistance on Tax Matters, originally signed by Brazil on 11 November 2011, which will support the CbC implementation. The next step will be signing the Multilateral Competent Authority Agreement on the Exchange of CbC Reports and the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information.	Announced October 2016 Current status Not available

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Dispute resolution (Action 14)</b>	A draft Normative Instruction contains guidance on the mutual agreement procedure under Brazil's tax treaties. Enactment is expected in the near future.	Not yet known

### C. 3. China

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>VAT on business to customers digital services (Action 1)</b>	No action currently is expected in relation to Action 1.	N/A
<b>Hybrids (Action 2)</b>	Under review by the tax authorities (SAT).	Not yet known
<b>CFCs (Action 3)</b>	China already has CFC rules, which are being reviewed as part of changes to current guidance (i.e. Circular 2).	Expected during 2016. Present status not found.
<b>Interest deductions (Action 4)</b>	China uses the thin capitalisation and transfer pricing rules to limit interest deductions, although these rules only cover interest paid between related parties. The Enterprise Income Tax (EIT) law uses a debt-to-equity ratio, rather than an interest expense-based ratio, as the relevant criteria.	N/A
<b>Harmful tax practices (Action 5)</b>	The government is reviewing relevant regimes to ascertain whether they are affected by the action 5 conclusions. The reduced EIT rate for high and new technology enterprises has been reviewed by the OECD and is regarded as not harmful, so no change is expected in the short term.	Ongoing
<b>Prevent treaty abuse (Action 6)</b>	The recommendations in the action 6 report are broadly in line with long-standing practices of the tax authorities. The SAT is considering the LOB clause concept and appears to favour a combined PPT and LOB approach. The	Immediate (for existing practices) and subject to implementation of the multilateral instrument

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Permanent establishment status (Action 7)</b>	The SAT considers that its current position regarding PE issues (contained in Circular 75) already reflects the action 7 recommendations.	Immediate (for existing practices) and subject to implementation of the multilateral instrument
<b>Transfer pricing (Actions 8-10)</b>	The recommendations in the Actions 8-10 reports are in line with long-standing practices of the tax authorities. The draft changes to Circular 2 incorporate the recommendations, adapted as appropriate for China.	Revised Circular 2 is expected to be effective retroactively as from 1 January 2016, although this has not been confirmed
<b>Disclosure of aggressive tax planning (Action 12)</b>	The SAT is expected to introduce mandatory disclosure rules into domestic law by revising the Tax Collection and Administration Law and its implementation rules.	Subject to the reform of the relevant law, which is unlikely in 2016
<b>Transfer pricing documentation (Action 13)</b>	The draft changes to Circular 2 incorporate the Action 13 recommendations, adapted for China. Local documentation that may be required by Chinese entities includes a "Chinese" master file, an enhanced local file and a "special issues" file. For qualifying groups, the parent or designated entity will also be required to file a CbC form, which will be required to be filed with the entity's annual EIT return.  On 29 June 2016, the SAT issued a new regulation (SAT Bulletin [2016] No. 42), which replaced the rules in Circular 2 to the extent they relate to transfer pricing compliance (disclosure and documentation).	Revised Circular 2 is expected to be effective retroactively as from 1 January 2016, although this has not been confirmed  Bulletin 42 applies from the 2016 income tax year, which commenced on January 1, 2016.
<b>CbC reporting (Action 13)</b>	The draft changes to Circular 2 incorporate the Action 13 recommendations, including CbC reporting.	Revised Circular 2 is expected to be effective retroactively as from 1

## C. 4. Singapore

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>VAT on business to customers digital services (Action 1)</b>	Not yet known.	Not yet known
<b>Hybrids (Action 2)</b>	Not yet known.	Not yet known
<b>CFCs (Action 3)</b>	Not yet known, but it is unlikely that Singapore will introduce a CFC regime.	Not yet known
<b>Interest deductions (Action 4)</b>	Not yet known.	Not yet known
<b>Harmful tax practices (Action 5)</b>	On 16 June 2016, the government announced that: Singapore's tax incentives are legislated and granted for defined periods of time on qualifying activities. Non-qualifying activities of incentivised companies are taxed at the prevailing corporate tax rate; and The government regularly reviews tax incentives to ensure they remain relevant and competitive. As an outcome of these reviews, some tax incentives have been allowed to lapse and others have been refined.	N/A
<b>Prevent treaty abuse (Action 6)</b>	Singapore is part of a group of countries working with the OECD/G20 to develop a multilateral instrument to counter treaty abuse. Singapore will consider whether to join the instrument after it is finalised and ready for jurisdiction to sign	Not yet known
<b>Permanent establishment status (Action 7)</b>	Not yet known.	Not yet known
<b>Transfer pricing (Actions 8-10)</b>	Not yet known, but the tax authorities may consider whether to adopt updates to the OECD's transfer pricing guidelines into Singapore's existing transfer pricing guidelines on a case-by-case basis.	Not yet known



Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Disclosure of aggressive tax planning (Action 12)</b>	Not yet known.	Not yet known
<b>Transfer pricing documentation (Action 13)</b>	Transfer pricing documentation guidelines were updated in January 2015 to be broadly in line with Action 13 recommendations.	January 2015
<b>CbC reporting (Action 13)</b>	As announced by the government on 16 June 2016, Singapore intends to implement CbC reporting for Singapore-headquartered multinational enterprises for financial years beginning on or after 1 January 2017.	January 2017
<b>Dispute resolution (Action 14)</b>	As announced by the government on 16 June 2016, as a BEPS Associate, Singapore will work closely with other jurisdictions to monitor the implementation of minimum standards on dispute resolution developed under the BEPS project. This will complement the other BEPS minimum standards and ensure that taxpayers have access to effective and expedient dispute resolution mechanisms under bilateral tax treaties.	Not yet known

### C. 5. United Kingdom

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>VAT on business to customers digital services (Action 1)</b>	The EU VAT directive applies and is already implemented into domestic law.	1 January 2015
<b>Hybrids (Action 2)</b>	Legislation was enacted in September 2016. Imported mismatches and mismatches involving permanent establishments are included.	1 January 2017
<b>CFCs (Action 3)</b>	The UK recently updated its CFC law.	N/A

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Interest deductions (Action 4)</b>	The UK government has confirmed that it intends to introduce rules to restrict interest deductibility. A second public consultation on the detailed design of the rules was published on 12 May 2016 and draft legislation is expected on 5 December 2016.	1 April 2017
<b>Harmful tax practices (Action 5)</b>	Legislation to modify the existing patent box rules to comply with the new international framework and G20/OECD “nexus approach” was enacted in September 2016; the existing regime closed to new entrants from 1 July 2016.	July 2016
<b>Prevent treaty abuse (Action 6)</b>	The UK has PPT clauses in some treaties and is expected to add more through bilateral protocols/treaties and the multilateral instrument. UK has dual resident tiebreaker clauses in some treaties and may add more.	Subject to implementation of the multilateral instrument and bilateral negotiations
<b>Permanent establishment status (Action 7)</b>	Part of the multilateral instrument and will require a domestic law change.	Subject to implementation of the multilateral instrument
<b>Transfer pricing (Actions 8-10)</b>	Immediate adoption in case work. The revisions to the OECD transfer pricing guidelines made by the final report on Actions 8-10 “Aligning Transfer Pricing Outcomes with Value Creation” have been enacted into UK law.	Already adopted in casework
<b>Disclosure of aggressive tax planning (Action 12)</b>	UK already has disclosure rules and these are kept under review.	N/A
<b>Transfer pricing documentation (Action 13)</b>	The UK is not expected to implement specific rules as it already has sufficient powers to require information.	N/A

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>CbC reporting (Action 13)</b>	Regulations to implement country-by-country (CbC) reporting entered into force on 18 March 2016. UK standalone entities and UK sub holding companies are also required to file where the parent company does not. Non- UK headed multinational groups with a UK presence can voluntarily file. Amendments to the regulations will be proposed in Autumn 2016 to include partnerships. The UK is one of the countries that signed a multilateral competent authority agreement for the automatic exchange of CbC reports.	1 January 2016
<b>Dispute resolution (Action 14)</b>	The UK is one of the countries committed to binding arbitration.	Subject to implementation of the multilateral instrument

## D. Implementation of BEPS Action Plans by India

India has actively participated in the OECD - BEPS project. The implementation of BEPS measures would make tax management a challenge in the initial years for multinational enterprises, tax professionals and the Revenue authorities worldwide. Following is the summary of the status of implementation of the Action Plans by Indian government:

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Treatment for digital services (Action Plan 1)</b>	Equalisation levy introduced. Currently the levy is pegged at 6% on the amount of consideration for specified services received by a non-resident not having a PE in India. The term 'specified services' has been defined to mean online advertising or any provision for digital advertising space or any other facility or service for the purpose of online advertisement, or any other service as may be notified by the Central Government.	1 June 2016
<b>Hybrids (Action 2)</b>	Not yet known.	Not yet known
<b>CFCs (Action 3)</b>	Not yet known. India does not currently have CFC regulations.	Not yet known
<b>Interest deductions (Action 4)</b>	Not yet known.	Not yet known
<b>Harmful tax practices (Action 5)</b>	India has introduced a concessional regime for taxation of royalty income from patents @ 10% gross income, in respect of a patent developed and registered in India by a person resident in India.	1 April 2016
<b>Prevent treaty abuse (Action 6)</b>	India has introduced a general anti-avoidance rule as part of domestic tax law.	1 April 2017
<b>Permanent establishment status (Action 7)</b>	Not yet known.	Not yet known

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Transfer pricing (Actions 8-10)</b>	The concept and importance of DEMPE functions has been acknowledged and accepted in practice in certain cases. Given the manner in which low value-add services are currently defined, India is unlikely to adopt the simplified approach in the current form. Adoption of other concepts/actions is not yet known.	Not yet known
<b>Disclosure of aggressive tax planning (Action 12)</b>	Not yet known	Not yet known
<b>Transfer pricing documentation (Action 13)</b>	The Indian Finance Act 2016 has introduced the concept of master file in the Indian TP regulations, though details are to be prescribed later. No additional requirements have been specified in relation to the existing local documentation.	To be notified
<b>CbC reporting (Action 13)</b>	<p>The Indian Finance Act 2016 has introduced the CbC reporting requirement in the Indian TP regulations.</p> <ul style="list-style-type: none"> <li>Core elements of the concept have been proposed in the Bill, details to be prescribed later</li> <li>Requirement to file CbC report effective from Financial Year 2016-17 (April 2016 to March 2017)</li> <li>Proposed threshold to file CbC report in line with OECD mandated threshold of € 750 million</li> <li>Specific threshold in Indian currency to be prescribed – based on exchange rate as on 31 March 2016</li> <li>CbC report to be filed on or before due date of filing return in India (typically 30 November)</li> <li>Stringent penalty norms for non-compliance prescribed</li> </ul>	Effective from Financial Year 2016-17

Action	Notes on local country implementation	Expected timing/ Implemented date
<b>Dispute resolution (Action 14)</b>	Not yet known, however government sources have indicated that mandatory and binding arbitration is unlikely to be acceptable to India.	Not yet known



## E. Snapshot of implementation of BEPS Action plans by select Countries

Following is the summary of the status of implementation of action plans by few countries, where “✓” reflects action taken & “✗” reflects no action taken by the country.

Country Action Plans	India	Australia	Brazil	China	Singapore	United Kingdom
Action 1: Addressing the Tax Challenges of the Digital Economy	✓	✓	✗	✗	✗	✓
Action 2: Neutralising the Effects of Hybrid Mismatch Arrangements	✗	✓	✓	✗	✗	✓
Action 3: Designing Effective Controlled Foreign Company Rules	✗	✗	✓	✓	✗	✗
Action 4: Limiting Base Erosion Involving Interest Deductions and Other Financial Payments	✗	✗	✓	✗	✗	✓
Action 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance	✓	✓	✓	✓	✗	✓
Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances	✓	✓	✗	✓	✗	✓
Action 7: Preventing	✗	✓	✗	✓	✗	✓

Country Action Plans	India	Australia	Brazil	China	Singapore	United Kingdom
the Artificial Avoidance of Permanent Establishment Status						
Actions 8-10: Aligning Transfer Pricing Outcomes with Value Creation	✓	✓	✗	✓	✗	✓
Action 11: Measuring and Monitoring BEPS	✗	✗	✗	✗	✗	✗
Action 12: Mandatory Disclosure Rules	✗	✓	✗	✓	✗	✗
Action 13: Guidance on Transfer Pricing Documentation and Country-by-Country Reporting	✓	✓	✓	✓	✓	✓
Action 14: Making Dispute Resolution Mechanisms More Effective	✓	✓	✓	✗	✗	✓
Action 15: Developing a Multilateral Instrument to Modify Bilateral Tax Treaties	✗	✗	✗	✗	✗	✗

## F. Analysis of impact of BEPS Action Plans to few sectors at India

OECD and G20 countries worked closely to combat BEPS. The project has entailed forging consensus on 15 Actions that combine to create a broad package of tax measures designed for coordinated implementation by participating countries domestically and through treaty provisions, supported by targeted monitoring and strengthened transparency. The goal is to tackle BEPS structures by addressing their root causes, not just the symptoms.

The impact and effect of such measures would be encompassing and far-reaching. The proposed BEPS Action Plans will have impact across every sector. Impact of the same on few select sectors has been summarized in the following paragraphs:

### F. 1. Impact on Consumer Business

MNEs in consumer business sector especially companies engaged in FMCG, retail, ecommerce, travel, hospitality and leisure products are highly driven from client perceptions of their brands and products. They carry a huge reputation risk with regard to tax paid and liabilities arising in a given country which do not correspond to scale of operations in that country. Considering the same, MNEs engaged in consumer businesses need to review their business model viz. their investment holding structures, funding and operating arrangements from BEPS viewpoint.

We have briefly discussed the effects of some of the key action plans which would specifically impact consumer business sector. The steps taken by the respective countries to implement the action plans could have significant impact on the bottom line of a large number of consumer business MNEs by increasing their overall effective corporate income tax rate.

- **Action Plan 1**

Action plan 1 of BEPS aims to address tax challenges of the digital economy. The report observes that the digital economy is increasingly becoming the economy itself and it will be difficult to ring fence the digital economy from the rest of the economy for tax purposes.

‘Equalisation levy’ of 6% has been introduced on consideration being made for ‘specified services’, viz., online advertisement, provision of digital advertising space, or any other facility for the purposes of online advertisement. The Government is empowered to specify any other service on which such levy shall apply.

Every person, being a resident carrying on business or profession in India or a non-resident having permanent establishment in India, shall deposit the levy on the considerations payable to non-resident not having permanent establishment in India. Such levy does not apply where the aggregate amount payable to non-resident does not exceeds INR 100,000 in a year. The corresponding income would be exempt from income-tax in the hands of such non-resident.

With the advent of digital economy, the interlink between the revenue generating activity and geographical location is more obscured as compared to the past wherein a geographical connection with some economic activity entailed taxation in the said jurisdiction. Similar to countries around the world, MNEs in India have been facing tax litigation on account of various e-commerce issues e.g. online advertising, subscription for electronic databases, etc.

- **Action Plan 5**

Action plan 5 of BEPS aims to identify and counter harmful tax practices, taking into account transparency and substance. The Action looks at developing recommendations on the definition of harmful tax practices, and developing a strategy to expand to non-OECD members.

It establishes minimum standards with regard to both determining whether preferential regimes take sufficient account of the need to reward only substantial activities, and ensuring that there is transparency in relation to rulings. It also sets out minimum standards for domestic law provisions in respect of intellectual property [IP] regimes, such as patent box regimes.

**Impact on MNEs in consumer business sector in India:** India has always been an advocator of the substantial activity test and does not have a harmful IP or other regime. India has been a sizeable outsourcing destination for R&D activities. In order to sufficiently capitalize on the vast intellectual resources of our country, and fully reap the attendant economic benefits, it was imperative to develop patents indigenously and provide a conducive framework to encourage this process.

With recent initiatives such as Make in India and Skill India, a concessional taxation regime is introduced in respect of income from patents, which is aimed at encouraging indigenous research and development activities and to make India a global R&D hub.

- **Action Plan 6**

To counter tax treaty abuse, the BEPS project has laid down minimum standards, involving a limitation on benefits [LOB] rule and / or a principal purposes test [PPT] rule.

**Impact on MNEs in consumer business sector in India:** Foreign investors will be required to review their group holding structures and transactions including documentation to consider whether they are sufficiently robust to withstand tests under the LOB / PPT rule and GAAR provisions.

- **Action Plan 7**

Action Plan 7 deals with preventing the artificial avoidance of PE status. The report provides for changes to the definition of PE under the tax treaties, which address strategies used to avoid having a taxable presence or a PE in a country under tax treaties.

**Impact on MNEs in consumer business sector in India:** The proposed expansion of ambit of agency PE and the inability of the Indian subsidiary to be regarded as an 'independent agent' could expose a part of the overseas group entity's profit on sale of products to be taxed in India. MNEs in consumer business sector need to analyse PE risk arising from supply chain model especially activities carried out through marketing and distribution intermediaries and function performed by liaison offices incorporated in India. In case, MNEs create a PE on account of activities undertaken by intermediaries then the same could result in tax cost in/ outside India and impact the overall tax cost of the group.

- **Action Plan 8**

The existing international rules for transfer pricing have been found to be misapplied or considered insufficient to the extent that the allocation of profits is not aligned with the economic activity that results in profits. Action Plan 8 tries to correct the arising imbalance, as it brings out how misallocation of profits generated by valuable intangibles has contributed to BEPS. It proposes revised guidance on transfer pricing rules to ensure that operational profits are allocated to economic activities which generate them.

**Impact on MNEs in consumer business sector in India:** The consumer business sector is highly competitive and branding and technologies are vital factors for the

success of any enterprise in this industry. Considering the significance of “brands” and “market presence” in achieving the sales/market share, the companies have been investing considerably in the marketing campaign in India. Due to significance and magnitude of investment in marketing and sales activities, marketing intangible has been one of the most significant litigious TP issues in India for consumer business sector, with amount under litigation exceeding thousands of crore.

In Indian context, MNEs have incorporated R&D centers in India to take advantage of the availability of abundant and economical talent pool. Further increased focus on brand positioning for augmenting the business/ market share is also a key objective for their Indian presence. In this regard, exercising important functions by the foreign principal and control over service providers are important factors for determination of ownership and entitlement to intangible related return.

- **Action Plan 13**

The G20/OECD have agreed on very significant changes to the compliance and reporting of global information, for risk assessment and transfer pricing purposes. As an active member in the BEPS initiative, for implementing the international consensus on Action 13 of the BEPS project, India has introduced the Country by Country (CbC) reporting requirement and the concept of master file in the Indian Income Tax Act, 1961 (through the Finance Act 2016). The OECD has adopted a three-tiered approach to documentation, which includes:

- a **master file** containing standardized information relevant for all multinational enterprises (MNE) group members;
- a **local file** referring specifically to material transactions of the local taxpayer; and
- a **Country-by-Country (Cubic) report** containing certain information relating to the global allocation of the MNE's income and taxes paid together with certain indicators of the location of economic activity within the MNE group.

Considering the consumer centric business model of consumer business sector entities, MNEs in this sector need to align their tax models in line with the OECD BEPS Actions. From both inbound and outbound investment perspective, the MNEs in consumer business need to track tax policy changes as regards management of intangibles particularly brands, remodel their supply chain models, review the group holding structure along with inter-company

transactions, evaluate the tax aspect of digital transactions in order to meet the level of compliance requirements and undertake risk assessment of the transfer pricing policy and documentation along with the reporting requirements. All in all the MNEs in consumer business need to align their business models with regards to the actual 'value generation' to 'economic activity' in countries which they operate.

## **F. 2. Impact on Manufacturing**

This part of sectoral analysis seeks to capture some of the key potential impact of BEPS Actions for Indian MNEs in the manufacturing sector having global operations as well as to MNEs operating in India. Following are the few important points for manufacturing concerns:

- **Action plan 1**

India introduced equalisation levy of 6% on specified services which include online advertisement, provision of digital advertising space and other facilities/ services for the purpose of online advertisement, which impacts manufacturing sector too.

- **Action Plan 2**

A large number of foreign companies invest in India by subscribing to Compulsory Convertible Debentures [CCDs] issued by their Indian subsidiaries. Till the time of conversion to equity, India would generally regard the CCDs as debt and grant a tax deduction for interest on such CCDs. With the proposed linking rules in relation to hybrid instruments contemplated under BEPS, if the home country of the CCD-holder regards the instrument as equity and does not tax the dividend, India may deny a deduction for such interest.

- **Action Plan 7**

One of the recommendations in Action 7 dealing with preventing the artificial avoidance of PE status is that the PE exceptions will be modified to ensure that all activities that qualify for exemption are purely in the nature of preparatory and auxiliary activities. In the light of the recommendations under action plan 7, exceptions from creating a PE for specific activities (such as maintenance of stocks of goods for storage, display, delivery or processing, purchasing or collection of information) will only apply where the activity in question is of preparatory or auxiliary character. This is to reflect modern ways of doing business, where such



activities may represent a key part of the value chain of a business (particularly relevant for supply chain involving digital sales).

- **Action Plan 8**

India has always been an advocator of the substantial activity test and does not have a harmful IP or other regime. Action Plan 8 of the BEPS report emphasizes that the group companies performing important functions, controlling economically significant risks and contributing assets in development, enhancement, maintenance, protection and exploitation (DEMPE) of the intangible, as determined through the accurate delineation of the actual transaction, shall also be entitled to an appropriate return reflecting the value of their contributions.

- **Other Impacts:**

- **Interest deduction** India is typically regarded as a high tax jurisdiction from the corporate tax perspective. The BEPS proposal to limit interest deductions by following a fixed ratio rule may impact the interest deductibility of manufacturing MNEs in India.
- Many multinational enterprises operate in India through a subsidiary to marketing support. Typically the Indian subsidiary receives a fee or commission that is taxable in India, whereas the overseas group entity is not taxable in India on the profit of the sales, in the absence of a PE in India. The proposed expansion of the definition of agency PE in the context of conclusion of contracts discussed above and the inability of the Indian subsidiary to be regarded as an '**independent agent**' could expose a part of the overseas group entity's profit on sale of products to be taxed in India, depending on the facts of the case.

### **F. 3. Impact on infrastructure funding structures**

Like many sectors, even infrastructure industry is anticipating millions or billions of additional tax due to BEPS action items. While most of the BEPS Action Plan is likely to impact infrastructure sector. Some of the BEPS recommendations discussed below, if implemented, could have significant impact on these infrastructure projects.

- **Action Plan 2**

The hybrid nature of some instruments result into tax deductions in India and no tax outflow on dividend income in recipient's jurisdiction due to specific tax

exemption. BEPS Action Plan 2 has suggested rules to deny the interest deduction or, alternatively, tax interest income in recipient's jurisdiction in order to neutralize undue advantage availed by the taxpayer.

- **Action Plan 4**

The Action Plan 4 recommends an approach based on a fixed ratio rule (limiting interest to fixed percentage of EBITDA), with a potential range of ratios (between 10% to 30%) to take into account that not all countries are in equivalent position. The fixed ratio approach can be supplemented by a worldwide group rule ratio.

The above recommendations will adversely impact the funding structures of highly leveraged infrastructure sector and the infrastructure companies will have to reevaluate their global financing / income arrangements and the desired quantum of interest break in line with BEPS recommendations.

- **Other key BEPS recommendations relevant for infrastructure sector:**

Apart from above, some of the other relevant BEPS recommendations are summarized below which will have impact on business models of infrastructure companies:

- The Finance Act, 2016 has already introduced the country by country ('CbC') reporting and master file requirement. The CbC reporting requirement is introduced with effect from Assessment Year 2017-18 (financial year 2016-17), requiring Indian headquartered Multi-national Enterprises ("MNEs") and certain other Indian entities of global MNEs to file the CbC report with the prescribed Indian Authority.  
Aforesaid reporting is intended to increase transparency across jurisdictions to identify whether companies have engaged in unfair practices that have the effect of artificially shifting substantial amounts of income into tax-advantaged environments;
- Development of multilateral treaty provisions under BEPS Action Plan 15 was proposed as a most effective measure to implement treaty related recommendations. In November 2016, more than 100 jurisdictions have concluded negotiations on a multilateral instrument (MLI) that will swiftly implement a series of tax treaty measures to update international tax rules and lessen the opportunity for tax avoidance by multinational enterprises. Some of the aspects covered under MLI are hybrid entities, countering tax treaty abuse, artificial avoidance of PE status, improving dispute resolution,

etc. If signed by India in coming year, MLI would save bilateral negotiations to implement the tax treaty changes in the BEPSProject and facilitate quicker implementation of standards to counter treaty abuse.

#### **F. 4. Impact on Technology, Media and Telecommunication**

- **Action Plan 1**

The digital economy is based on conventional production of goods and services such as software development, IT services, telecommunications, advertising, or content creation. The global companies serving millions of users are changing the rules of the game and bringing far-reaching changes in various sectors of the economy through - intense reliance on digital technologies and innovative business models. India is on the brink of internet revolution with the latest figures indicating that India has more internet users than the population of the US and has become the country with the second largest population of internet users after China.

- **Impact of other BEPS action on TMT Companies**

India is the first country to introduce equalization levy under its domestic tax legislation based on the recommendations of the committee formed by the apex tax body. The move is targeted at foreign internet companies who earn substantial revenues from digital advertisement. The following are the key players who are impacted because of equalization levy:

- Foreign Internet companies like social media companies, internet search engines, media websites, e-commerce companies, apps and games developers who do not have any presence in India
- Foreign broadcasting network companies who derive revenue from Indian companies for advertisement in television and radio.

[Sources: <https://www2.deloitte.com> & <http://www.pwc.in>]

## **G. Concluding remarks**

BEPS Action Plans lay down minimum standards and threshold which should be incorporated by all participating countries into their domestic law & treaty policy. Coupled with such implementation by the government across the globe, the tax payers will have to relook at their business models & contractual terms to eliminate issues concerning BEPS and achieve desired tax efficiency. While BEPS Action plans are committed for both elimination of double taxation and elimination of non taxation, it would be in the interest of all that implementation of BEPS do not hamper the global trade and cross border transactions. Unilateral action by few countries will also pose certain challenges on harmonized implementation of BEPS action plans. It is in the interest of all stakeholders that ambitious BEPS project achieves its desired objective and all the stakeholders find it successful. 2017 will witness tremendous interest and activity across the globe for further implementation & monetary process of BEPS Action Plans.