



THE TAXABLE RESIDENCE OF COMPANIES AND TREATY PROTECTION

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In this presentation, the tax residency of an individual and interpretation / issues around the same have not been discussed



NEED AND CONCEPT OF RESIDENCY

Relevance of Residency

Residency under IT Act

Residency under Tax Treaty





RELEVANCE OF RESIDENCY

- ▶ Elementary for deciding the basis of charge of income-tax
- ▶ Determining taxable income and tax liability
- ▶ Gateway for accessing Tax Treaties
- ▶ Relevant for allocating taxing rights amongst the countries
- ▶ Identifying the jurisdiction granting foreign tax credit
- ▶ Ascertaining compliance obligations
- ▶ Determining tax withholding obligations of the payer





RELEVANCE UNDER THE IT ACT

- ▶ Section 6 of the Income-tax Act, 1961 ('the IT Act') contains the definition of residence.
- ▶ It provides that a Company is said to be a resident in India in any previous year, if:
 - (i) it is an Indian company; or
 - (ii) its place of effective management, in that year, is in India.
- ▶ In case of other forms of business, treated as resident in India unless their control and management is situated wholly outside India
- ▶ The taxability of income of a resident vis-à-vis non-resident is tabulated hereunder:

Resident	Non resident
<ul style="list-style-type: none">▪ Received/ deemed to be received in India;▪ Accrues/arises/deemed to accrue or arise in India;▪ Accrues or arises outside India.	<ul style="list-style-type: none">▪ Received or deemed to be received in India;▪ Accrues or arises or deemed to accrue or arise in India.



RELEVANCE UNDER TAX TREATY

- ▶ Article 1 grants access to Tax Treaty. It reads as:
This Convention shall apply to persons who are residents of one or both of the Contracting States
- ▶ Concept of residency discussed in Article 4 of Tax Treaties
- ▶ Article 4(1) of UN Model Convention reads -
For the purpose of this Convention, the term 'resident of a Contracting State' means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of incorporation, place of management or any other place criterion of a similar nature, and also includes that State and any political sub-division or local authority thereof. This term, however, does not include any person who is liable to tax in that State in respect of only of income from sources in that State or capital situated therein
The provision of Article 4(1) of OECD Model convention does not contain reference to 'place of incorporation'
- ▶ Article 4(3) provides for tie-breaker rule in case of dual residency of non-individuals
where by reason of the provisions of paragraph 1(a) person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.



TAXABILITY OF VARIOUS STREAMS OF INCOME

Nature of income	IT Act	Treaty*	Basis for taxation
Business/ Profession	Section 9(1)(i)	Articles 5, Article 7 and Article 14	Residence
Salary Income	Section 9(1)(ii)	Article 15	Residence
Dividend Income	Section 9(1)(iv) - At present exempt	Article 10	Source
Interest Income	Sections 9(1)(v), 115A	Article 11	Source
Royalties/ FTS	Sections 9(1)(vi)/(vii), 115A	Article 12	Source
Capital Gains	Sections 9(1)(i), 45	Article 13	Source / Residence
Income from House Property	Section 22	Article 6	Source

* Above is based on UN Model Convention, treaty countries may negotiate differently





PLACE OF EFFECTIVE MANAGEMENT (POEM)

POEM under the IT Act

Case Study

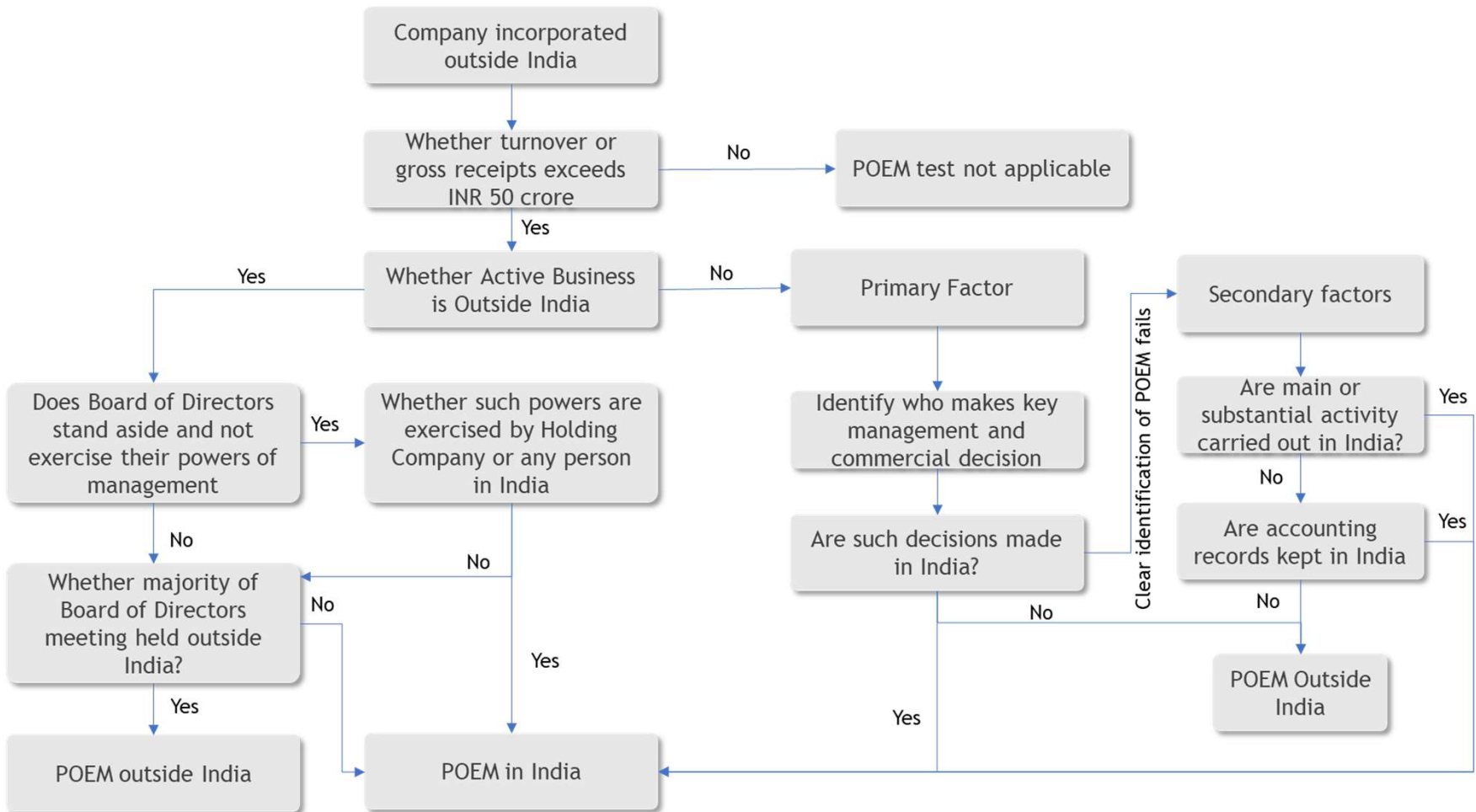
POEM - Treaty vs IT Act

International Jurisprudence

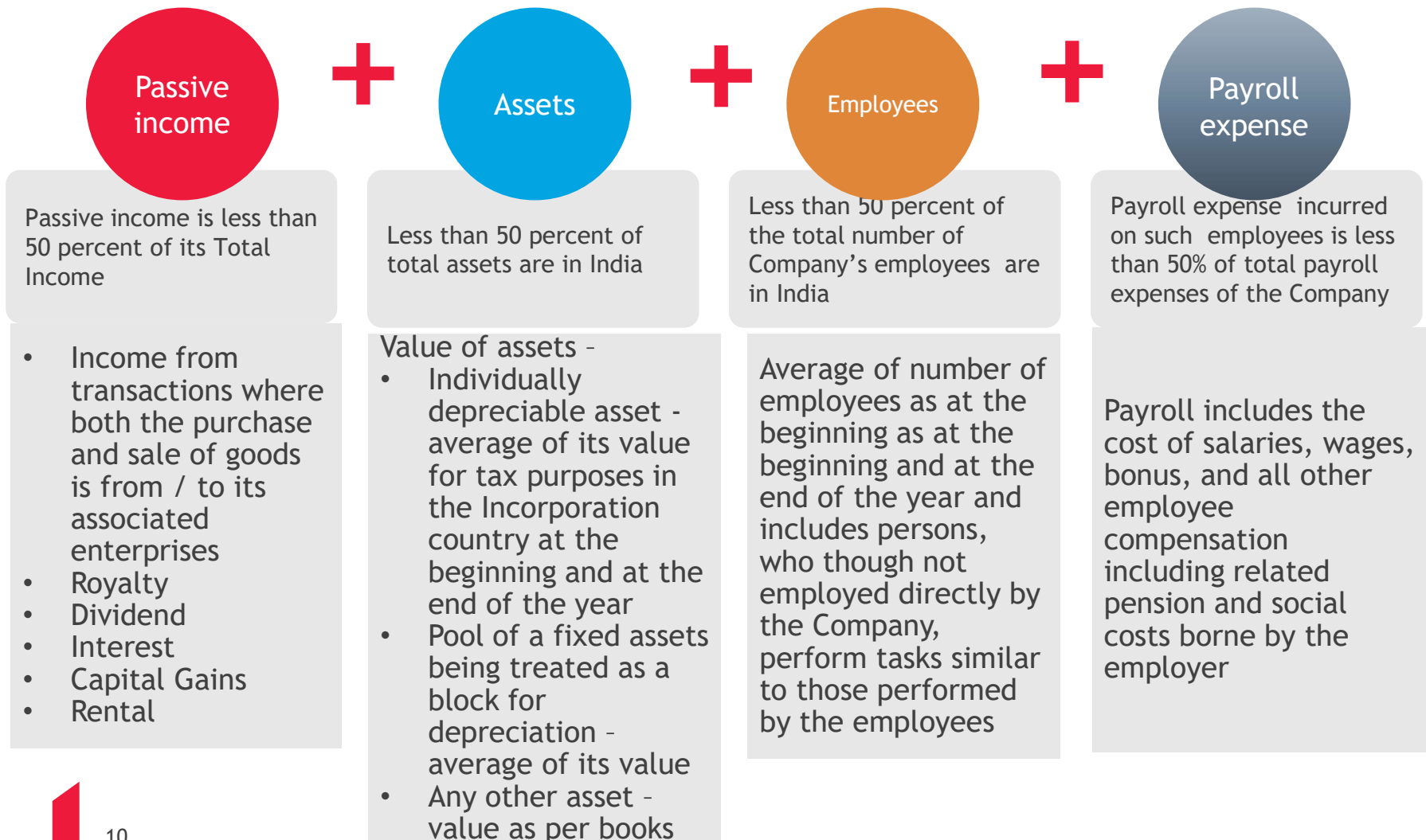


POEM - UNDER THE IT ACT

CBDT guidelines for determination of POEM - circular no. 06/2017



POEM - ACTIVE BUSINESS OUTSIDE INDIA

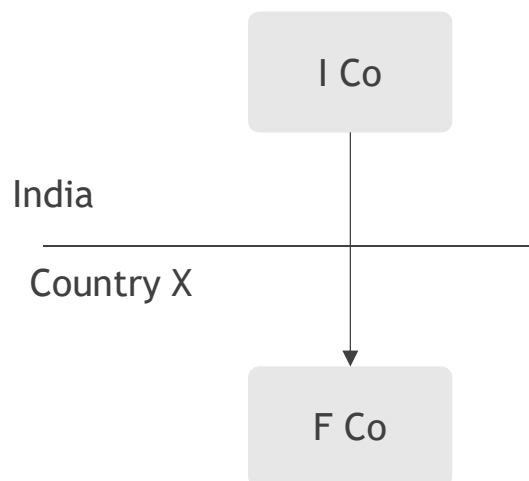




POEM - GUIDING PRINCIPLES

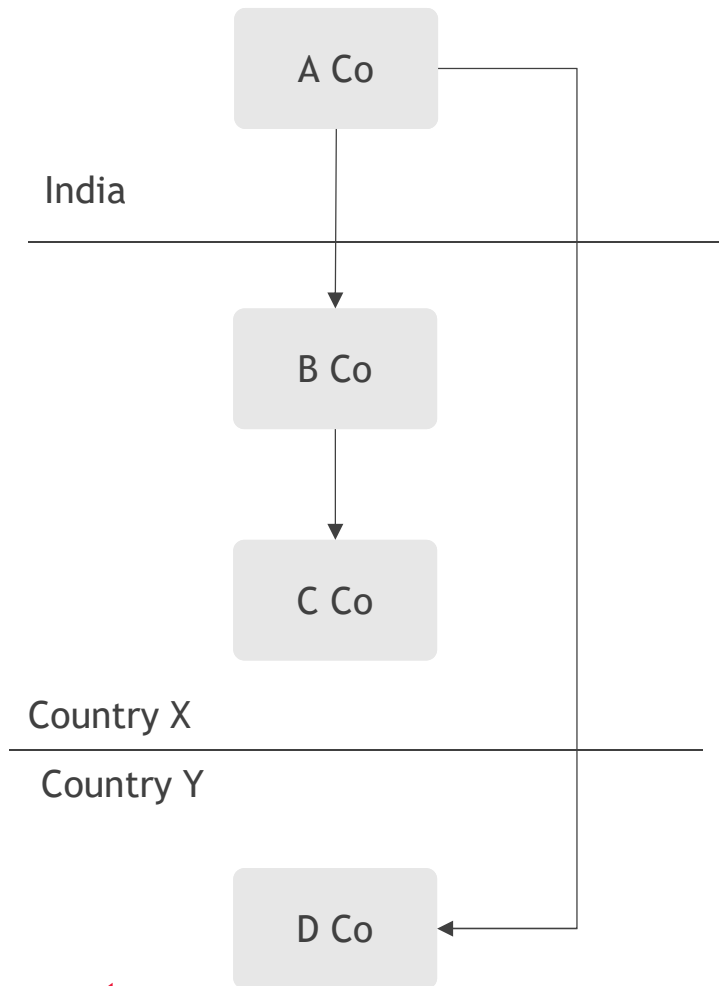
- ▶ Location where the Board regularly meets and make decisions
- ▶ Centralized - location held out to public as Company's principal place of Business
- ▶ Decentralized - location where senior manager -
 - ▶ Primarily and predominantly based
 - ▶ Normally return to following travel to other location
 - ▶ Meet when formulating or deciding key strategies and policies for the Company as a whole
- ▶ Virtual meeting - telephone / video conferencing - location where highest level of management and their direct support staff are located
 - ▶ Place where the directors or the person taking decisions or majority of them usually reside may also be the relevant factor
- ▶ Circular resolution / round robin voting - place of the person who exercises authority to take decision

CASE STUDY - ABOI, PASSIVE INCOME



- ▶ F Co, a sourcing entity, is a wholly owned subsidiary of I Co
- ▶ The warehouses and stock are the only assets of the F Co and are located in Country X
- ▶ All employees of F Co are in Country X
- ▶ 30% of F Co's income is from transaction where purchases are made from parties which are non-associated enterprises and sold to associated enterprises
- ▶ 30% of F Co's income is from transaction where purchases are made from associated enterprises and sold to associated enterprises
- ▶ 30% of F Co's income is from transaction where purchases are made from associated enterprises and sold to non-associated enterprises
- ▶ 10% of F Co.'s income is by way of interest

POEM - CASE STUDY



- ▶ An Indian multinational group has a local holding company A Co. in India
- ▶ The A Co. also has 100% downstream subsidiaries B Co. and C Co. in country X and D Co. in country Y
- ▶ The A Co. has income only by way of dividend and interest from investments made in its subsidiaries
- ▶ The POEM of B Co. is in India and is exercised by ultimate parent company of the group
- ▶ The subsidiaries C and D are engaged in active business outside India
- ▶ The meetings of Board of Director of C Co. and D Co. are held in country X and Y respectively.

POEM - TREATY VS IT ACT

IT Act	UN MODEL COMMENTARY	OECD MODEL COMMENTARY
<ul style="list-style-type: none"> Place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made Set of guiding principles for determination of POEM have been issued for the benefit of the taxpayers as well as for tax administration 	<ul style="list-style-type: none"> Place where key management and commercial decisions that are necessary for the conduct of the entity's business as a whole are in substance made All relevant facts and circumstances must be examined to determine the place of effective management An entity may have more than one place of management, but it can have only one place of effective management at any one time 	<ul style="list-style-type: none"> Place where the company is actually managed and controlled where the decision-making at the highest level on the important policies essential for the management of the company takes place that plays a leading part in the management of a company from an economic and functional point of view where the most important accounting books are kept



INTERNATIONAL JURISPRUDENCE

- ▶ POEM is the place where -
 - key decisions are taken¹ ; or
 - the most important business decisions are made²
- ▶ POEM is the economic and effective centre of a Company³
- ▶ The expression ‘effective’ implies realistic / positive management and ‘place of effective management’ is the place where the shots were called⁴
- ▶ POEM refers to a place where all of the management functions are exercised⁵
- ▶ The decisive factor for determining the POEM is the management of daily business activities within the Company’s purpose rather than the top-level management activities and purely administrative activities, or the board meetings and general assembly meetings³



ACCESS TO TREATY

Relevance under the Tax treaty

Tax Residency Certificate





RELEVANCE UNDER THE TAX TREATY

- ▶ The purpose of the Convention is to eliminate double taxation and hence the Convention takes into account only persons who are liable to tax in the Contracting State
- ▶ To be **liable to tax**, the person must be subject to tax laws of that jurisdiction. However, while being subject to the laws makes a person liable to tax, it does not necessarily make him **subject to tax** (i.e. actually liable to pay tax)
- ▶ Whether 'liable to tax'
 - Loss making entities
 - Where the entity is exempt from tax in Country of Residence
 - Where an exemption is provided to the entity in the Country of Residence for certain period of time
 - Where the source of income is not taxable in the Country of Residence
 - Certain type of entities are not taxed as per the tax laws of Country of Residence
 - Where there are no tax laws in the Country of Residence
 - Where there is no tax liability due to deemed tax credit
 - Entity liable for other taxes but not income tax



TAX RESIDENCY CERTIFICATE

- ▶ As per Section 90(4) of the IT Act, a non-resident will not be entitled to claim benefits under the Tax Treaty unless he obtains a TRC from the Government of his residence country
- ▶ Furnishing TRC mandatory requirement
- ▶ Notification 57/2013 dated 1 August 2013 issued by CBDT, which mandates submission of following information in Form 10F:
 - Status (individual, company, etc) of the assessee
 - Nationality or country or specified territory of incorporation or registration
 - Assessee's tax identification number in the country and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government
 - Period for which the residential status is applicable; and
 - Address of the assessee in the country
 - Declaration not required, if TRC contains above particulars



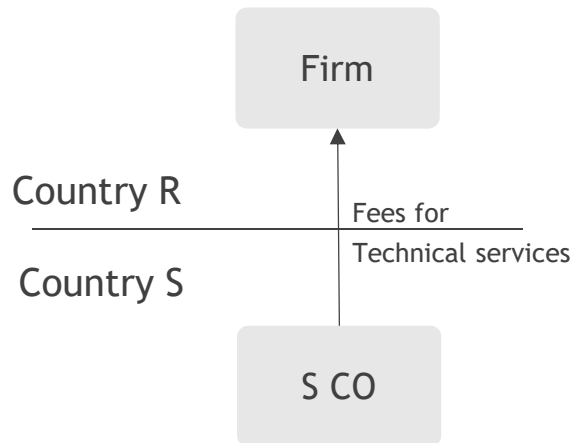


INTERPRETATIONS AND ISSUES - CASE STUDIES



CASE STUDIES

Fiscally Transparent entity - partners in same country



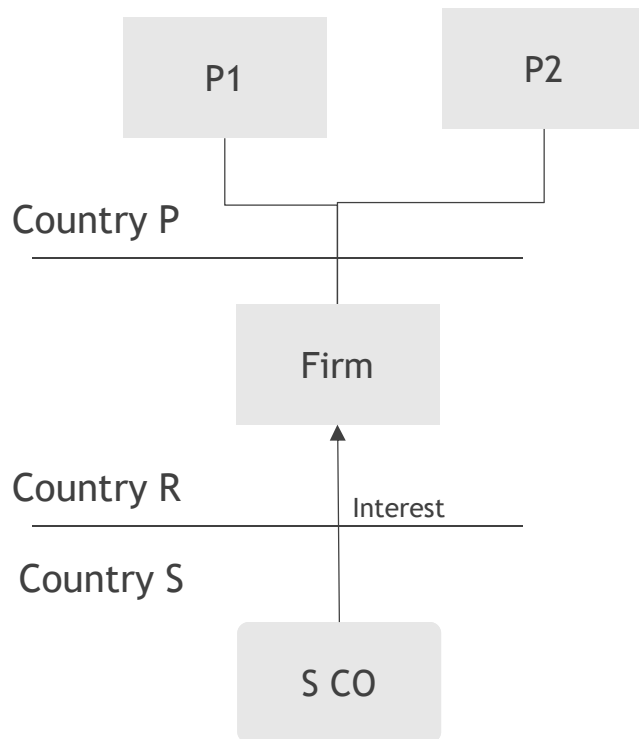
- ▶ S Co pays Fees for Technical Services to the Partnership Firm located in Country R
- ▶ As per the laws of Country R, the Firm is a fiscally transparent entity
- ▶ All the partners of the Firm are tax resident of Country R
- ▶ As per laws of Country S, the Firm is opaque i.e. a taxable entity
- ▶ As per the tax treaty between Country R and Country S, the payment is not taxable in Country S. However, as per the domestic tax laws of Country S, the payment is taxable

Points for consideration

- ▶ Whether the Firm can access the Tax Treaty benefit?
- ▶ What if Country R does not issue TRC to the Firm?

CASE STUDIES

Fiscally Transparent entity - partners in different country



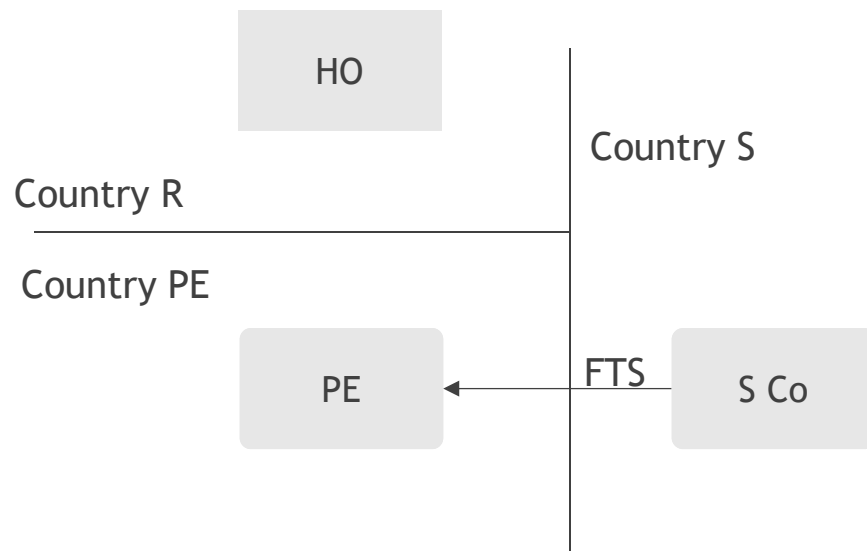
- ▶ S Co pays interest to the Partnership Firm located in Country R
- ▶ As per the laws of Country R, the Firm is a fiscally transparent entity
- ▶ The partners of the Firm are tax residents of Country P
- ▶ As per laws of Country S, the Firm is opaque i.e. a taxable entity and the payment is subject to tax in Country S
- ▶ As per the tax treaty between Country R and Country S, the payment is not taxable in Country S.
- ▶ As per the tax treaty between Country P and Country R, the payment is taxable in Country P
- ▶ As per domestic laws of Country P, foreign sourced income is not taxable

Points for consideration

- ▶ Which Tax Treaty will be applicable - P-S or R-S or R-P?
- ▶ What if the Firm is an opaque entity as per Country R and the Firm distributes profits to P1 and P2?

CASE STUDIES

PE Triangular Case



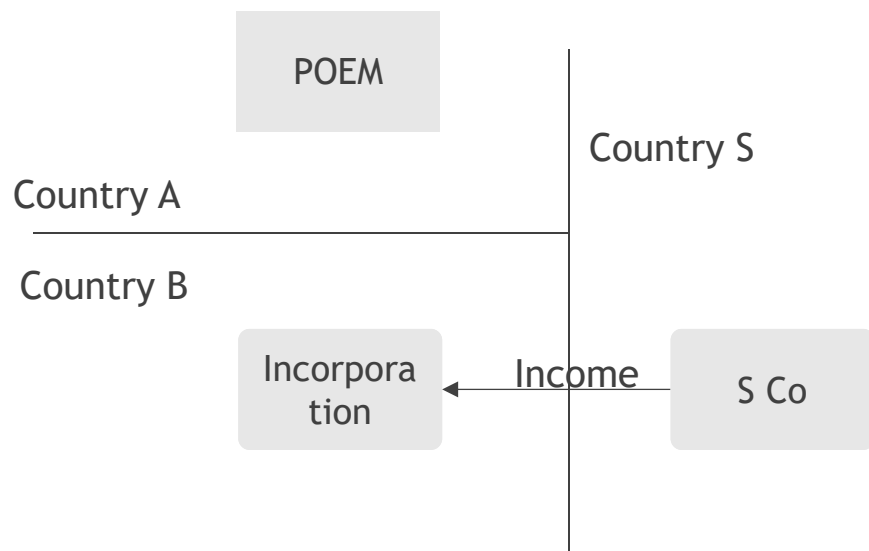
- ▶ HO is tax resident of Country R
- ▶ HO has set up a Branch in Country PE
- ▶ S Co, a tax resident of Country S, has taken certain services from PE.
- ▶ PE is receiving payment towards rendering of services to S Co

Points for consideration

- ▶ Which Treaty will be applicable - PE-S or S-R?

CASE STUDIES

Dual Residency



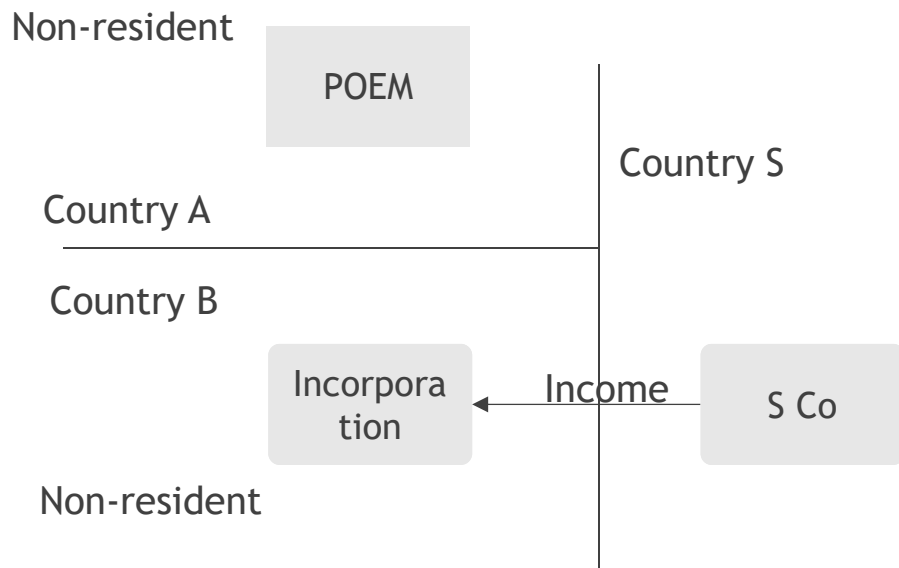
- ▶ A company is resident in Country A due to its place of incorporation
- ▶ The same company is resident of Country B on the basis of its place of management
- ▶ As per the DTAA between Country S and Country B the income is taxable in Country B
- ▶ As per DTAA between Country S and Country A, the income is taxable in Country S
- ▶ As per DTAA between Country A and B, Company is a resident of Country A using the tie-breaker test

Points for consideration

- ▶ In order to determine the withholding obligation in Country S whether you would refer to DTAA between S-B or S-A?

CASE STUDIES

Dual non-residency



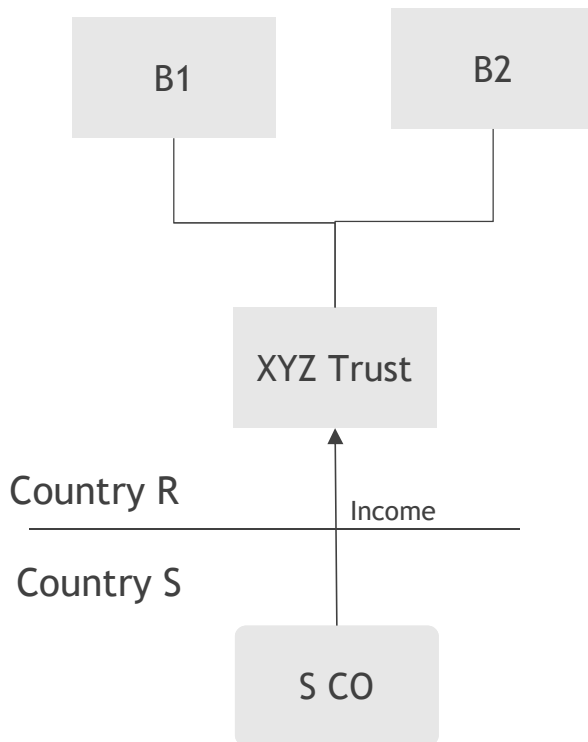
- ▶ As per laws of Country A, a Company is resident only if it is incorporated in Country A
- ▶ As per laws of Country B, a Company is resident if it has POEM in Country B
- ▶ As per the DTAA between Country S and Country B the income is taxable in Country B
- ▶ As per DTAA between Country S and Country A, the income is taxable in Country S
- ▶ As per DTAA between Country A and B, Company is a resident of Country A using the tie-breaker test

Points for consideration

- ▶ In order to determine the withholding obligation in Country S whether you would refer to DTAA between S-B or S-A?

CASE STUDIES

Trust



- ▶ XYZ Trust is a pension trust exempt from taxes in Country R
- ▶ Income earned by the trust is by investing in Country A as a foreign institutional investor
- ▶ XYZ Trust is a transparent entity in Country R.
- ▶ As per the Tax Treaty, XYZ can be regarded as a resident of Country R only if its beneficiaries were taxed in Country R on income earned by XYZ Trust.

Point for consideration:

What if the Trust is unable to determine residency or furnish any evidence that the income earned by the beneficiaries from the trust would be taxed in the hands of beneficiaries



CONCLUDING THOUGHTS





RESIDENCY - IN THE NEW BUSINESS ENVIRONMENT

Relevance of concept of residency in light of

- ▶ Equalisation Levy
- ▶ General Anti-Avoidance Rule
- ▶ Multilateral instruments
- ▶ Digital Economy and New Taxing Rights





THANK YOU





INTERNATIONAL JURISPRUDENCE - CITATION

1. Indofood International Finance Ltd vs JP Morgan Chase Bank NA, London Branch (2006) IBFD Case No A3/2005/2497 (English and Wales Court of Appeal (Civil Division))
2. IBFD Case No AWB 10/00157 (Supreme Court of Netherlands)
3. Wensleydale's Settlement Trustees vs IRC (1996) Simon's Tax Cases (Special Commissioners' Decisions) p 241
4. IBFD Case No RA 2008 ref 30 (6639-06) (Supreme Administrative Court of Sweden)
5. IBFD Case No 2C-1086/2012, 2C-1087/2012 (Federal Supreme Court of Switzerland)

