18 April 2019: UPSC Exam PIB Summary & Analysis

Profit Attribution to Permanent Establishment (PE) in India

Context: Recognizing the significance of issues relating to attribution of profits to a permanent establishment as well as the need to bring greater clarity and predictability in the applicable tax regime, a Committee was formed by CBDT to examine the existing scheme of profit attribution to PE under Article 7 of DTAAs and recommend changes in Rule 10 of the Income-tax Rules, 1962. The Committee has submitted its report and it has been decided to seek suggestions/comments of the stakeholders and the general public.

What is a Permanent Establishment?

A Permanent Establishment in India is a fixed place of business, wholly or partly carried out by a foreign enterprise operating in India.

Such fixed place of business can be a branch office, a place of management, a factory, a warehouse, a workshop etc. However the definition of permanent establishment differs in each tax treaty.

(PE) has acquired tremendous importance in recent times as it determines taxability of a foreign company in India. Usually, foreign companies get tax concession under Double Taxation Avoidance Treaties and they pay taxes in their home countries. But if they have PEs in India, they should pay taxes for the income they have created in India. Thus PE makes a foreign companies' Indian income taxable in India.

Tax treatment of PEs

The significance PE lies in the fact that "business profits" of a foreign enterprise can be taxed in India only if it has a PE in India and the profits are attributable to the PE. Even the amount for "royalty" or "fee for technical services" received by foreign enterprises will be taxed in India as business profits if they are attributable to a PE in the country.

Background:

- Taxation of non-residents in India is governed by the provisions of the Income-tax Act, 1961 ("the Act") and the provisions of the Double Taxation Avoidance Agreement(s) [DTAA(s)] concluded or adopted by the Central Government under the powers conferred under Section 90 or 90A of the Act, respectively.
- The business income of a non-resident can be taxed in India if it satisfies the requisite thresholds provided under the Act as well as the threshold provided in the applicable tax treaty, by a concept of Permanent Establishment (PE), which is defined in Article 5 of Model Tax Conventions and tax treaties.
- Under Article 7 in the Indian treaties, profits are to be attributed to the PE as if it were a distinct and separate entity on the basis of the accounts of the PE and where such accounts are not available to enable determination of profits attributable to the PE, the profits attributable to the PE can be determined under the domestic laws.

Suspension of LoC Trade between J&K and PoJK

Context: India suspended Line of Control (LoC) trade between Jammu & Kashmir and Pakistan-occupied Jammu & Kashmir with effect from 19-04-2019 after receiving reports that the cross-LOC trade routes were being misused by Pakistan-based elements for funnelling illegal weapons, narcotics, fake currency, and so on.

Background:

- The LoC trade was meant to facilitate exchange of goods of common use between local populations across the LoC in Jammu & Kashmir.
- The trade is allowed through two Trade Facilitation Centres located at Salamabad, Uri, District Baramulla, and Chakkan-da-Bagh, District Poonch. The trade takes place four days a week. The trade is based on barter system and zero duty basis.
- But unscrupulous and anti-national elements are using the route as a conduit for Hawala money, drugs and weapons, under the garb of this trade.
- According to ongoing investigations of certain cases by the National Investigation Agency (NIA), it has been brought out that a significant number of trading concerns engaged in LoC trade are being operated by persons closely associated with banned terrorist organizations involved in fuelling terrorism and separatism.
- Investigations have further revealed that some individuals, who have crossed over to Pakistan and joined militant organizations have opened trading firms in Pakistan. These trading firms are under the control of militant organizations and are engaged in LoC trade.
- After the Pulwama incident, Government of India has withdrawn the most-favoured nation (MFN) status to Pakistan. Inputs have also been received that in order to evade the consequent higher duty, LoC trade is likely to be misused to a much larger extent.
- So Government of India decided to suspend the LoC trade at Salamabad and Chakkan-da-Bagh in

Jammu and Kashmir with immediate effect.and the issue of reopening of LoC trade will be revisited thereafter.