

**National Interest Analysis [2012] ATNIA 4**

**with attachment on consultation**

**Protocol amending the Agreement between the Government of Australia and the  
Government of the Republic of India for the Avoidance of Double Taxation and the  
Prevention of Fiscal Evasion with Respect to Taxes on Income**

**done at New Delhi on 16 December 2011**

**[2011] ATNIF 30**

## NATIONAL INTEREST ANALYSIS: CATEGORY 2 TREATY

### SUMMARY PAGE

#### **Protocol amending the Agreement between the Government of Australia and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income**

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#### **Nature and timing of the proposed treaty action**

1. The proposed treaty action is to bring into force the *Protocol amending the Agreement between the Government of Australia and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* ('the proposed Protocol').
2. The proposed Protocol was signed on 16 December 2011 and amends the *Agreement between the Government of Australia and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income*, done at Canberra on 25 July 1991 ([1991] ATS 49, 'the Agreement'). The proposed Protocol will enter into force, pursuant to its Article 7, on the date of the last notification through the diplomatic channel between the Contracting States confirming each Contracting State has completed its domestic requirements to bring the proposed Protocol into force.
3. The provisions of the proposed Protocol will take effect in Australia in three stages:
  - a) in respect of Australian tax on income, profits or gains of any year beginning on or after 1 July in the calendar year following entry into force;
  - b) in respect of new Article 24A of the Agreement (Non-Discrimination) and the upgraded exchange of information rules in new Article 26, upon entry into force; and
  - c) in respect of new Article 26A (Assistance in Collection of Taxes), on a date agreed in an exchange of diplomatic notes.

#### **Overview and national interest summary**

4. The key objectives of the proposed Protocol are to:
  - a) promote closer economic cooperation between Australia and India by aligning the taxation of business profits and cross-border services with international taxation norms and by including rules to prevent tax discrimination; and
  - b) improve the integrity of the tax system by providing a framework through which the tax administrations of Australia and India can prevent international fiscal evasion.

5. The proposed Protocol updates the current tax treaty arrangements between Australia and India by modernising the rules which determine when an enterprise of one country may be taxed on its activities in the other country. It also provides that an enterprise will only be taxed on the profits attributable to its branch activities in the other country and will not, as is currently the case, also be taxed on activities not carried on through its branch but of a similar nature to the branch activities. (For example, an Australian company may have a branch in India manufacturing goods while a different part of the same company sells similar goods through independent agents located in India. Aggregating the profits on transactions conducted through independent agents with those of the branch can, in certain circumstances, interfere with ordinary commercial activities.) As such, the proposed Protocol should be welcomed by Australian business.

6. Business should also welcome the rules being inserted by the proposed Protocol to protect nationals and businesses of one country from tax discrimination in the other country.

7. The proposed Protocol will amend the exchange of information (EOI) provisions in the Agreement, enhancing the ability of the tax authorities of Australia and India to exchange information on a wider range of taxes (in the case of Australia, all Federal taxes). The new provisions also make clear that neither tax administration can refuse to provide information solely because they do not have a domestic interest in such information, or because a bank or similar institution holds the information. The enhanced EOI provisions also maintain important safeguards to protect the legitimate interests of taxpayers.

8. The integrity of both countries' tax systems will also be enhanced by provisions providing for mutual assistance in the collection of tax debts (AIC).

### **Reasons for Australia to take proposed treaty action**

9. Australia enjoys a positive and constructive relationship with India, with a rapidly expanding bilateral commercial relationship. As a consequence, the proposed Protocol, in modernising the circumstances in which cross-border businesses come under the tax jurisdiction of the other country, will provide for certainty of treatment for businesses establishing themselves in the other country and will better reflect the state of the current trade and investment relationship.

10. The non-discrimination rules will also provide certainty to businesses and individuals investing in the other country, as neither country will discriminate in their treatment of such businesses and individuals in the design of their future laws and processes.

11. The integrity provisions (EOI and AIC) to be inserted into the Agreement by the proposed Protocol will be an important tool in Australia's efforts to combat offshore tax evasion. They will make it harder for taxpayers to evade Australian tax and will discourage taxpayers from participating in abusive tax arrangements by increasing the probability of detection. Accordingly, it will enhance Australia's ability to administer and enforce its domestic tax laws.

12. The proposed Protocol aligns the EOI provisions with the internationally agreed standard on tax information exchange, which was developed by the Organisation for Economic Co-operation and Development (OECD). This standard was endorsed by G20 Finance Ministers at their Berlin meeting in 2004 and by the United Nations Committee of

Experts on International Cooperation in Tax Matters at its October 2008 meeting. It is in Australia's interest to utilise EOI treaty provisions that meet the internationally agreed standard to combat tax avoidance and evasion, and to continue the Australian Government's support of global action on improving information exchange and transparency.

## **Obligations**

13. Article 2 of the proposed Protocol introduces new rules into Article 5 of the Agreement setting out when a business will be taken to have a taxable presence in the other country.

14. Article 3 of the proposed Protocol amends Article 7 of the Agreement and obliges each country to only tax business activities carried out by an enterprise of the other country in its country where those activities are carried out by a branch of the enterprise ('permanent establishment'), as defined in the amended Article 5 of the Agreement.

15. Article 4 of the proposed Protocol inserts a new Article 24A into the Agreement and introduces a general non-discrimination principle, requiring each country to treat nationals of the other country no less favourably than it treats its own nationals regarding taxation and any connected requirements.

16. Article 5 of the proposed Protocol replaces Article 26 of the Agreement with a new Article 26 which provides obligations for the exchange of information between both countries, including a specific obligation to gather and provide information upon request. The new Article 26(2) imposes a correlative obligation on the country receiving any such information to treat it as secret in the same manner as information obtained under its domestic laws. The new Article 26(3) allows either country to decline to supply information in certain circumstances. Specifically, a request may be denied where: (i) it would require implementation of administrative measures at variance with either country's domestic laws or administrative practice; (ii) the information requested is not obtainable under the laws or in the normal course of administration of either country; or (iii) it would involve disclosure of a trade or business secret or would be contrary to public policy. These circumstances, which act as a safeguard to protect Australia's interests and taxpayers' rights, accord with the *OECD Model Tax Convention on Income and on Capital*.

17. Article 6 of the proposed Protocol inserts a new Article 26A into the Agreement which provides an obligation for the revenue authorities of each country to use their collection mechanisms to collect debts owing in the other country.

## **Implementation**

18. The implementation of the proposed Protocol will require amendment to the *International Tax Agreements Act 1953* to give it the force of law in Australia. The amendment will be effected prior to the proposed Protocol entering into force in Australia.

19. The legislative framework required for Australia to fulfil its obligations under the EOI provisions in the proposed Protocol is contained in section 23 of the *International Tax Agreements Act 1953*.

20. The implementation of the proposed Protocol will not affect the existing roles of the Commonwealth, or the States and Territories, in tax matters.

## **Costs**

21. Treasury has estimated the revenue impact of the proposed Protocol as unquantifiable. However, since the proposed Protocol seeks to expand the scope of taxpayer information available to the Australian Taxation Office (ATO) and provides for assistance in collection of tax debts, the proposed Protocol is expected to increase taxpayer compliance and therefore tax revenue.

22. There would be a small, unquantifiable cost in administering the changes made by the proposed Protocol, including minor implementation costs to the ATO in educating the taxpaying public and ATO staff concerning the new arrangements. There are also 'maintenance' costs to the ATO and the Treasury in terms of dealing with inquiries, rulings and other interpretative decisions and mutual agreement procedures (including advance pricing arrangements, whereby the prices of goods and services transferred between related business entities are agreed by those entities with the tax authorities in the countries in which the related entities operate). However, these costs will continue to be managed within existing agency resources.

## **Regulation Impact Statement**

23. The Office of Best Practice Regulation in the Department of Finance and Deregulation has been consulted and confirms that a Regulation Impact Statement is not required.

## **Future treaty action**

24. The proposed Protocol does not provide for the negotiation of future legally binding instruments. Neither the proposed Protocol nor the Agreement contains formal amendment procedures. Pursuant to customary international law, in the absence of specific procedures, Australia and India may amend the Agreement by mutual consent at any time. It is contemplated that the Agreement will be further revised over the longer term to address issues raised in consultations with business during the negotiation of the proposed Protocol (see the Attachment on Consultation). Any such amendment to the Agreement would constitute a treaty action and would therefore be subject to Australia's domestic treaty-making process.

## **Withdrawal and denunciation**

25. Article 7 of the proposed Protocol provides that it shall form an integral part of the Agreement. Article 29 of the Agreement provides that the Agreement shall continue in effect indefinitely but may be terminated by either Contracting State by providing written notice in accordance with the procedure detailed in that provision.

## **Contact details**

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## ATTACHMENT ON CONSULTATION

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#### Consultation

26. The former Assistant Treasurer's Press Release No. 156 of 15 July 2010 invited submissions from stakeholders and the wider community in relation to issues that might be raised during negotiations on the proposed Protocol. Treasury also sought comments from the business community through the Tax Treaties Advisory Panel, members of which include:

- a) a representative of the Australian airline industry
- b) Australian Financial Markets Association
- c) CPA Australia
- d) Corporate Tax Association
- e) Financial Services Council
- f) Institute of Chartered Accountants Australia
- g) International Fiscal Association
- h) Law Council of Australia
- i) Minerals Council of Australia
- j) Property Council of Australia
- k) Taxation Institute of Australia.

27. Submissions were received from various businesses and from the major accounting firms. These submissions concerned the taxation of services income in India; the taxation of industrial, commercial and scientific equipment under Article 12 of the Agreement dealing with royalty payments; the application of the 'substantial equipment' provisions of the Agreement to leased equipment; bringing the taxation of capital gains in line with international norms; reducing the withholding tax rates on dividends, interest and royalties; the introduction of a threshold number of days' activity before natural resource exploration or exploitation attracts tax in the other country; dealing with India's dividend distribution tax; coverage of the Mineral Resource Rent Tax to ensure that it is a creditable tax in India; the inclusion of rules to deal with fiscally transparent entities; amendments to ensure that transfer pricing adjustments are undertaken in a timely manner and according to OECD transfer pricing guidelines; rules dealing with short-term secondees; expedited processes around

mutual agreement procedures; the prevention of the delivery of goods being treated as a taxable presence where this is not an enterprise's core business activity; the narrowing of rules as to when a dependent agent can constitute a taxable presence in either country; and removal of rules whereby activities of a similar nature to those undertaken by a branch of an enterprise are taxed with the profits of the branch even though the activities are not undertaken through the branch (the so-called 'force of attraction' principle).

28. The extent of the submissions clearly reflects the divergence between Australia's and India's tax treaty practice. The proposed Protocol, accordingly, represents a negotiated position that could be reached in the short term while a full revision can be pursued over the longer term. As such, the proposed Protocol addresses, to some extent, the taxation of services income in India, the taxation of substantial equipment, the taxation of natural resource activities and removes the 'force of attraction' principle.

29. The State and Territory governments have been consulted through the Commonwealth/State Standing Committee on Treaties. Information on the negotiation of the proposed Protocol was included in the schedules of treaty activity provided to State and Territory representatives from March 2010.