3rd Annual Developing Country Forum for Cooperation in International Tax Matters

Presentation on Extractive Industries by

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What type of investment structure is preferred by MNCs in developing countries.

- Is there a risk?
- If Yes, need to spread the risk
- Incorporated vs Unincorporated
- Taxation of AOP/BOI
- For Mineral Oil, section 293A of Indian Income Tax Act and notification no GSR 117E dated 8th March 1996

Design of Fiscal Regime

- **Concession Regime**: Tax and Royalty regime. It is front end loaded regime but regressive as not related to profit of the investor. Normally where there is less risk. Countries can impose higher tax or windfall tax or can have separate regime for extraction industry. Some time Bonus is also provided for which are not attractive to investors. Companies with low TP audit capacity find this attractive
- **Contract Regime (eg PSC):** It has royalty (less than what is in concession regime and also progressive sliding scale) and then production sharing. Common in oil…cost oil and profit oil. Profit Oil is shared on predetermined basis. It is preferred by investors as it is back loaded and is progressive and takes care of their risk. However, countries need to have good TP audit capability. India adopt this.
- **Equity participation by Govt**

Transfer Pricing issues

- Advisory, consultancy, managerial and technical services from related parties…..Transfer Pricing + Withholding tax under relevant DTAA + control by the regulator… India has reporting obligation (15CA), have FTS article in most treaties but "make available" is an issue. These payments are audited…APA experience.
- Hiring of equipment and services in relation to oil and gas are taxed at concessional rate of 4.45% section 44BB…Issue of PE is important
- Padding up of expenses to increase cost. More relevant in PSCs.
- Interposing Offshore marketing companies in low tax jurisdiction ..delineate transactions, look at customers before and after, look at control over risk,
- Use of EOI

Profit shifting through interest deduction

- In accordance with BEPS Action Point 4 India has introduced interest deductibility rule under section 94B.
- Applicable to Indian company or PE of foreign company,
- Paying interest over INR 10 Million (about USD 140000) in respect of debt issued by non resident AE. Also include borrowing from third party borrower guaranteed by an AE.
- Interest in excess of 30% of EBIDTA is disallowed
- Banking and insurance companies excluded
- Disallowed interest expense carried forward for 8 years and allowed to be set off in a year (and to that extent) where interest is less than 30% of EBIDTA

New legal/Administrative innovation in India

- Tax Collection at source section 206C seller of minerals (coal or lignite or iron ore) while selling these minerals collect from the buyer 1% TCS in addition to sale price
- Complete e filing of returns and now e- assessment coupled with faceless assessment
- Infrastructure have been built for 360 degree profiling and e verification.