Analysis: Denmark – India Income and Capital Treaty

See treaty text

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Model on which based: OECD
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This Analysis was updated in June 2013 by **Arne Riis**, Partner, Bech-Bruun, Copenhagen, Denmark and **Ravishankar Raghavan**, Partner, Majmudar & Co, India

Article 1 Personal Scope

See treaty text

Persons who are residents of one or both States.

Article 2 Taxes covered

See treaty text

Taxes on total income or on elements of income or capital;
Taxes on gains from alienation of movable or immovable property;
Taxes on total amounts of wages and salaries;
Capital gains taxes; and
Wealth taxes

As well as application to the taxes existing at the time the Treaty was signed there is a provision applying the Treaty to any identical or substantially similar taxes which are imposed after the date of signing of this Treaty.

Denmark

- Income taxes to the state (statslig indkomstskat (bund-, mellem-, topskat));
- Municipal income tax (kommunal indkomstskat);
- Church Tax (kirkeskat);
- Since 2008: labour market contribution (AM-bidrag)
- Health contribution (sundhedsbidrag)
- Share income tax (aktieindkomstskat)
- CFC tax (CFC-skat);
- Pension yield tax (pensionsafkastskat);
- Hydrocarbon Tax (kulbrinteskat); and

Any identical or substantially similar taxes which are subsequently imposed in addition to, or in place of, the existing taxes.

Since the Convention does not cover wealth taxes, property value tax (ejendomsværdiskat), which is considered a partial wealth tax, is not within the scope of the Convention.

India

In India, a surcharge of 2.5% applies (if the income is more than Rs.10 million) on the income tax. Furthermore, a cess called as Education Cess ("EC") at the rate of 2% along with a separate Secondary and Higher Education Cess ("SHEC") at the rate of 1%, applies on income tax and on the surcharge. Both EC and SHEC are defined as a surcharge, and are therefore included in the definition of surcharge under the Treaty.

Article 3 General Definitions

See treaty text

"Denmark": The Kingdom of Denmark, including any area outside the territorial sea of Denmark within which Denmark may exercise, under its law and in accordance with international law, rights with

respect to the exploration and exploitation of the natural resources of the Continental Shelf; the term include the Faroe Islands but does not include Greenland.
"India": Indian Republic in geographical sense, means its territory, including internal waters, territorial sea and air space over them and includes any area beyond the territorial waters of India which, in accordance with international law and the laws of India concerning the exploration and exploitation of natural resources, may be designated as an area within which the rights of India, with respect to the sea-bed and subsoil and natural resources, may be exercised.
"Person": An individual, company and any other body of persons.
"Company": Any body corporate or any entity which is treated as a body corporate for tax purposes.
All terms not specifically defined take their meaning from domestic tax law.
"National": Any individual possessing the nationality of either State or any legal person, partnership and association or other entity deriving its status as such from the law in force in one of the States
"International traffic": means any transport by a ship or aircraft operated by an enterprise in a Contracting State, except when the ship or aircraft is operated solely between places in the other Contracting
Any terms not defined take their meaning from the law of the State concerned at the time. Meanings specific to tax law take precedence over other meanings.

Domestic Law:

Denmark

"Competent authority" The minister of taxation. In matter relating to international taxation, authority has been delegated to "SKAT", the Danish administrative tax authorities.

India

Under Indian tax law, India is defined to include "the territory of India as referred to in Article 1 of the Constitution, its territorial waters, seabed and subsoil underlying such waters, continental shelf, exclusive economic zone or any other maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976 (80 of 1976), and the air space above its territory and territorial waters". (Section 2(25A) of the Income Tax Act (the "Act").
"Definition of person" Under the Act, a person also includes a "Hindu Undivided Family", a firm (i.e., partnerships including limited liability partnerships ("LLPs"), an association of persons or a body of individuals, a local authority and every other artificial juridical person. (Section 2(31) of the Act.)
"International traffic" means any transport by a ship, or aircraft operated by an enterprise of a Contracting State, except when the ship, or aircraft is operated solely between places in the other Contracting State.
In a case under the India-Singapore DTA, an Indian company hired a ship from a Singapore company to transport petrol from one place in India to another, via a coastal route. The tax authorities contended that the ship operated "solely" within India and therefore, this cannot be termed as "international traffic". The Income Tax Appellate Tribunal (the "ITAT") held that the vessel was traversing in international waters and made a solitary trip between two places in India. On this basis, it cannot be said that it is "solely" operating between two places in India. (Essar Oil v. DCIT, (2006) 102 TTJ (Mum.) 614.)

Article 4 Fiscal Domicile

See treaty text

"Resident": Any person who is liable to tax in one of the Contracting States by reason of his domicile, residence, place of management or any other criterion of a similar nature. Being liable to taxation only because of a source of income or capital in a State does not by itself result in "residency".

Residence: Individuals

In the case of individuals apparently resident in both Contracting States, the usual OECD Model tiebreaker tests apply:

- He will be deemed to be a resident of the State in which he has a permanent home. If he has a permanent home in both States, he will be deemed to be resident in the State with which his personal and economic relations are closer (centre of vital interests).

- If unable to determine the State where the centre of vital interests lies, then he is a resident of the State in which he has a habitual abode.

- If he has a habitual abode in both States, then he is a resident of the State of which he is a national.

- If a national of both States or of neither of them, then the competent authorities must settle the question by mutual agreement.

Domestic Law:
Denmark
According to section 1(1) of the Danish Tax at Source Act (kildeskatteloven), tax liability on its global income applies to (i) persons who are resident in Denmark, (ii) persons without Danish residence who stay on Denmark for at least six months, (ii) Danish nationals employed on vessels which with home port in Denmark, unless it is substantiated that they are tax resident outside of Denmark, and (iv) Danish nationals, who are civil servants deployed for duty abroad. Tax liability under (ii) applies as of the initiation of the stay in Denmark. However, persons visiting Denmark as tourists or students, who remain liable to tax in their home State and are not carrying on business in Denmark will only be considered as tax residents if the stay exceeds 365 days within a 2 year period.
Residence in a foreign State for foreign tax purposes does not preclude residence in the Denmark for Danish tax purposes. Dual residence, often resulting in double taxation of the individual's worldwide income, is generally resolved under the terms of an applicable tax treaty. When a Danish tax resident individual moves out of Denmark, the individual will generally still under Danish domestic law be considered tax resident in Denmark as long as he/she or his/her family still has a house suitable for year-round residence. A house owned by the Danish emigrant will generally be considered as being available unless it is let out on a lease which is not terminable for at least 3 years.
India
The taxpayer's residential status determines the liability to tax under the Act and it is not affected by the nationality or domicile. In India, an individual is regarded as resident in any tax financial year if he or she;
(i) is in India for a period or periods amounting to 182 days or more in the relevant financial year; or
(ii) is in India for an aggregate period of 60 days or more in the relevant financial year and has been in India for an aggregate period of 365 days or more in the four financial years immediately preceding that year.
There are two exceptions to the above rule. In case
(a) an individual who is a citizen of India who leaves India in the relevant financial year as a member of the crew of an Indian ship or for the purpose of employment outside India or
(b) a person of Indian origin who, being outside India, comes on a visit in the relevant financial year, then the period is extended from 60 days to 182 days.
Furthermore, an individual is regarded as “resident but not ordinarily resident” (“RNOR”) in India in any tax year even though qualifying as a resident on one or both of the bases referred to above in (i) and (ii), if he or she: has been a non-resident of India in nine out of the ten tax financial years preceding that tax financial year; or - has during the seven tax years preceding that year, been in India for a period or periods amounting to 729 days or less.
Generally, the day on which a person enters India, as well as the day on which he leaves India, (both days inclusive) are taken into account as stay of the individual in India. (In re Advance Ruling P. No. 7 of 1995, [1997] 90 Taxman 62 (AAR).)
Residents are required to pay tax on their global income, whereas non-residents are not required to pay tax on foreign source income unless such income is deemed to accrue or arise in India, or it is received in India.
Residence: Companies
If a company appears resident in both States, e.g. because one determines residence according to the place of legal incorporation and the other according to place of management then it will be deemed resident of the State in which its place of effective management of its business is situated.
Domestic law
Denmark
All companies taxable under sec. 1 of the Danish Corporate Income Tax Act
(CITA)(selskabsskatteloven) are considered as Danish taxable corporate entities. This list primarily entails, “aktieselskaber” (A/S) and “anpartselskaber” (ApS), which are required to be registered in the Danish Commerce and Companies Agency (Erhvervs- og Selskabsstyrelsen). Further, companies and cooperatives with similar corporate characteristics as the above company types and which have a Danish tax resident management will be considered as taxable in Denmark. Management will normally be considered as resident in Denmark if Denmark is the seat of the daily management. This would generally be the seat of management rather than the board of directors. However, if the board of directors take very active part in the daily management decisions, the venue of the board may depending on the circumstances be considered as the seat of management for tax purposes. In all other cases than aktieselskaber and anpartselskaber, it is recommendable to obtain local advice.

As a noticeable potential exception to the rule that the above entities are considered to be taxable entities, sec. 2A of the CITA provides that if any of the above entities are considered to be tax transparent under foreign tax law to the effect that income in such Danish entity is taken into account in foreign income, then the otherwise taxable corporate entity is for Danish tax purposes considered tax transparent and potentially not protected by the tax treaty. The reclassification rule is an anti-abuse rule aimed at the US check-the-box rules to avoid creating a possibility of double-dip of primarily financing expenses in both Denmark and the US, but it applies equally to other rules with the same effect.

India

Control and management A firm or any other association of persons will be considered as resident in India in any previous year except where (during that year) the control and management of its affairs is situated wholly outside India. Control and management here connotes actual de facto control and not merely the right to control and manage. (CIT v. Nandalal Gandalal, [1960] 40 ITR 1 (SC).)

In one case, the Delhi ITAT was dealing with the case of a Mauritius company that was making portfolio investments in Indian stock markets. It had issued power of attorneys to certain persons in India to finalise investments. The tribunal noted that the investment decisions were taken by the company's board, either in Mauritius, or in the USA. Therefore, it could not be said that the control and management of the Mauritius company was situated wholly in India. (Saraswati Holding Corporation, Inc. v. DDIT, (2007) 111 TTJ (Delhi) 334.)

With respect to the connotation of "place of effective management", various Indian rulings have held that "it relates to the place where the day-to-day affairs of the person are conducted, or the place where the board of directors of the company take their decisions etc. (In re P. No. 9 of 1995, (1996) 220 ITR 337 (AAR); DLJMB Mauritius Investment Co. v. CIT, (1997) 228 ITR 268 (AAR); Integrated Container Feeder Service v. CIT, (2005) 278 ITR 182 (Mum); Saraswati Holding Corporation v. DDIT, (2007) 111 TTJ 334 (Del.); In re P. No. 10 of 1996, (1997) 224 ITR 473 (AAR).) The determination of the place of effective management is extremely fact specific.

Partnerships and fiscally transparent enterprises

There are no definitions given in the Treaty as to which bodies may be treated as transparent. Article 3 merely states that the term "company" designates any body corporate or any entity which is treated as a body corporate for tax purposes.

To the extent that an entity comes under the Treaty definition of "company" its residence is to be determined in the same way as described for companies.

Domestic law

Denmark

Partnerships are not comprised by section 1 of the Danish CITA and therefore generally not recognised as separate taxable entities.

A partnership is either a general partnership (interessentskab (I/S), a limited partnership (kommanditselskab (K/S) or partnerselskab / kommanditaktieselskab (P/S)). The general partnership is the ordinary form of commercial partnership, all partners being jointly and severally liable for the partnerships' debts and obligations. Under current Danish law, a partnership is not a separate legal entity, but is transparent with respect to its (tax) liability. A general partnership is normally not subject to taxation; instead, the individual partners are taxable on their share of the partnership's profits.

With respect to a K/S, separate rules for the tax treatment (transparent or non-transparent) apply. A K/S generally has partners having limited liability (limited partners) and one or more partners having unlimited liability (general partners).

A limited partner (kommanditist or stille deltager) is liable only to the extent of his capital contributions or commitments. Under Danish corporate law, it is a requirement that the general partner (komplementaren) has both administrative and economical rights in the K/S.

A P/S is a limited partnership where all limited shares are divided into actual shares. The affairs of the P/S are, however, governed by the Danish Corporate Act, despite being transparent for tax purposes.

As a noticeable exception to the rule that the above entities are considered to be tax transparent, sec. 2C of the CITA provides that if there are participants in an otherwise tax transparent entity (or a permanent establishment in Denmark) which are resident in a state which considers the entity to be a taxable entity or in a state which does not have a tax treaty or information exchange treaty with Denmark, and such participants hold more that 50 percent of the votes or the capital in the entity/permanent establishment, the entity/permanent establishment will be considered a separate taxable entity for Danish tax purposes. The reclassification rule is an anti-abuse rule aimed at the US check-the-box rules to avoid creating a "reverse hybrid" and thereby the possibility of double non-

taxation in a situation where Denmark would (without this rule) consider income to be earned by the partnership participants, while the jurisdiction where the partners are resident would consider the same income as earned by the partnership.
With respect to foreign entities, whether or not they are treated as taxable or transparent depends on how closely they correspond to the abovementioned Danish partnership forms. If they are significantly different then the general test is that an entity will be considered taxable if none of the participants have unlimited liability for the debts and obligations of the enterprise. In practise another significant criteria has been whether or not the entity has its own corporate bodies (board of directors or management).

India

Partnerships

A Hindu Undivided Family ("HUF") / Firm/Association of Persons / Limited Liability Partnership / Unlimited partnership will be regarded as residents in India unless its control and management is situated wholly outside India. A Hindu Undivided Family may also have "RNOR status if its manager, or "Karta" has been a non-resident for nine out of the previous 10 years or has been in India for a period totally less than 729 days during the seven years preceding the current year.
Partnerships are considered as separate taxable entities. Unless the partnership instrument specifies the profits sharing arrangements, the partnership is taxed according to the tax /slab rates of the individual partners.
In ADIT v Chiron Behring GMBH and Co., ([2009] 118 ITD 324 (Mum.) it was decided that a German limited partnership qualified for treaty benefits under the India Germany DTA (the treaty rate for withholding tax on royalties) on the grounds that it should be treated as a German resident for treaty purposes as it was liable to the German trade tax (Gewerbesteuer) at the entity level. The partnership was classified under Article 3 of the DTA as "any other entity" and treated as a taxable unit, and was therefore entitled to treaty benefits at the entity level.
LLPs in India will be subject to a new Alternate Minimum Tax ("AMT") regime effective April 1, 2012. The concept of AMT has been brought into the Act by the Finance Act, 2011 for the first time and is similar to the Minimum Alternate Tax ("MAT") concept already in place for companies.
Under the new AMT regime, LLPs will be required to calculate the income tax payable under the provisions of the Act (except the AMT provisions) and the AMT payable on the adjusted total income ("ATI"), as per the provisions of Chapter XII-BA of the Act. In case the AMT exceeds the regular income tax payable, then LLPs will be required to pay AMT on the ATI at the rate of 18.5% plus EC, totaling up to approximately 19.05%. Currently, LLPs do not incur a tax liability in the absence of income generated. LLPs will also be required to submit a report issued by a Chartered Accountant regarding their fiscal compliance to the Indian tax authorities. However, LLPs will earn credits equal to the excess of the AMT over the regular income tax payable which they can set-off against the excess of regular income tax over AMT for up to ten (10) assessment years.

Fiscally transparent enterprises

Generally, treaties define a "resident" to inter alia mean a "person" liable to tax under the laws of the country, by reason of its domicile, residence, citizenship, place of management, place of incorporation, or any other criteria of a similar nature. The term "person" is defined to inter alia include a partnership, company or any other body of persons, or other taxable entity. Therefore, in order to obtain the benefit of the Treaty, it is crucial that the fiscally transparent entity should be classified as a "person" as well as a "resident".
Regarding a fiscally transparent entity, the Indian tax authorities may argue that a because it is not "liable to tax", it will not fall within the general rule of residence prescribed by the Treaty under Article 4(1). There are judicial precedents that have distinguished between the phrase "liable to tax" and the "actual payment of tax", and have held that the former implies that an entity falls within a country's tax jurisdiction (regardless of whether actual payment of tax liability exists or not).
These issues are debatable and there is no clarity on the subject in India. In addition, India will be introducing a new Direct Tax Code ("DTC") with effect from April 1, 2012. Under this law a person shall not be entitled to claim relief under a treaty unless a certificate of his being a resident in the other country is obtained by him from the tax authority of that country, in such form as may be prescribed. The format has not been prescribed as yet. Therefore, once the DTC becomes effective, the fiscally transparent entities will be required to obtain a certificate of residence from the concerned revenue authorities to claim treaty benefits.
Aside from the above, the OECD Commentary suggests that where a partnership is a pass through entity, the correct treaty to refer will be the treaty of the country/countries where the partners are resident. (Paragraph 8.7 of the Commentary to Article 4 of the OECD Model Convention.) However,

India is not a member of the OECD, and Indian courts and tribunals tend to rely on OECD guidance in a very sporadic manner.

Article 5 Permanent Establishment

See treaty text

This Article defines the term "permanent establishment". The profits of an enterprise of one of the Contracting States can only be taxed on an arising basis in the other Contracting State to the extent that they are attributable to a permanent establishment in that other State.

This Treaty broadly uses the OECD definitions but the treaty also includes items (g)-(k) which is different from the OECD model.

Fixed place of business

A fixed place of business through which the business of the enterprise is wholly or partly carried on will constitute a permanent establishment. The list of types of establishment particularly included involve the following:

- A place of management;
- A branch;
- An office;
- A factory;
- A workshop;
- A mine, an oil or gas well, a quarry or any other place of extraction of natural resources; and

Included in the definition of permanent establishment, different from the OECD, is also:

- A warehouse in relation to a person providing storage facilities for others;
- A farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on;
- A premises used as a sales outlet or for receiving or soliciting orders;
- An installation or structure used for the exploration of natural resources provided that the activities are carried on for a period or periods of 183 days or more in any twelve-month period;
- A building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities (together with other such sites, projects or activities, if any) continue for a period of 183 days or more.

According to the OECD Commentary, a "fixed place of business" means established at a distinct place with a certain degree of permanence, however, it could be a pitch in a market place, or even part of the premises of another enterprise. There is no requirement that the premises be owned. The Commentary offers the example of an employee of Company A who is allowed to use an office at the premises of Company B. This could create a permanent establishment for Company A in the country of Company B if the arrangement persists for long enough and if the employee is carrying out activities which are more than merely "preparatory or auxiliary" (see below).

The OECD considers that to be fixed, a place of business must be at a specific geographic point. However, if the permanent establishment consists of mechanical equipment only, then there is no requirement for mechanical equipment to be fixed to the soil.

As to what constitutes a reasonable period of time to give the necessary degree of permanence, most countries will not consider a presence of less than six months to give rise to a fixed place.

The usual exclusions from the definition of permanent establishment are given so that the following will not constitute a permanent establishment:

(a) The use of facilities solely for the purposes of storage, display or delivery of goods or merchandise belonging to the enterprise;

(b) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display; Note that delivery of stock is not included.

(c) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(d) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or for collecting information, for the enterprise; and

(e) The maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research, or for other activities which have a preparatory or auxiliary character, for the enterprise.

To apply this Article, it is necessary to be able to make a distinction between functions that are core to a business and those that are merely preparatory or auxiliary. What constitutes core functions will vary from one business to the next. However, any fixed place of business from which the business is partly managed will constitute a permanent establishment even if its function otherwise appear to be preparatory or auxiliary. Also, if services are rendered to other companies within the corporate group or to third party customers then this would not be preparatory or auxiliary because activities only count as preparatory or auxiliary if they are carried on "for the enterprise" itself.

Agency permanent establishment

Dependent agents may constitute a permanent establishment. The treaty definition is broader than in art. 5 of the OECD model. Notwithstanding the provisions of paragraphs 1 and 2, where a person - other than an agent of an independent status to whom paragraph 5 applies - is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned State, if:

(a) He has and habitually exercises in that State an authority to conclude contracts on behalf of the enterprise, unless his activities are limited to the purchase of goods or merchandise for the enterprise;

(b) He has no such authority, but habitually maintains in the first- mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise; or

(c) He habitually secures orders in the first-mentioned State, wholly or almost wholly for the enterprise itself or for the enterprise and other enterprises controlling, controlled by, or subject to the same common control, as that enterprise.

An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise itself or on behalf of that enterprise and other enterprises controlling, controlled by, or subject to the same common control as, that enterprise, he will not be considered an agent of an independent status within the meaning of this paragraph.

The fact that a company has a subsidiary in the other Contracting State does not mean that the subsidiary is a permanent establishment of that company, unless it binds the parent company in contract as per the rule for dependent agents. This rule applies generally to groups of companies.

Domestic law

Denmark

The Danish domestic law definition of a permanent establishment is more or less identical to the definition under Article 5 of the OECD Model Tax Convention. A number of decisions have been made by the Danish tax authorities and Danish courts considering the existence of a Danish permanent establishment.

In sec. 2(5) of the CITA and sec. 2(9) of the Danish Source Tax Act (kildeskatteloven), however, a specific provision excluding the existence of a permanent establishment in the event of "distance selling". Hereunder, a permanent establishment in Denmark shall not be deemed to exist for a foreign principal, even if a Danish tax resident representative as such has power of attorney to bind the foreign principal, when carrying out distance selling. Distance selling shall for the purpose of these provisions mean the passive receipt of orders from Danish or foreign customers via telephone, telefax, telex, EDI, internet, mail or similar. However, it is further a condition that (i) the representative is not employed with the principal and that (ii) neither the foreign principal not any of his/her close relatives or a group related entity of the principal carries out business activities which has ties to the activities of the representative.

India

Indian courts often refer to the OECD commentary while deciding judicial cases but India is presently an “observing member” of OECD. All references to the OECD commentary are only indicative and the OECD commentary is not binding in India. Permanent Establishment (“Permanent Establishment”) issues have generated a lot of litigation in Indian courts therefore, while determining whether a Permanent Establishment exists in India, particular care is needed.

Fixed Place Permanent Establishment

For a non resident enterprise to be reckoned as having a Fixed Place Permanent Establishment in India, it should satisfy the following three essential conditions:

(i) the existence of a “place of business”;

(ii) the “right to use” the place of business; and

(iii) the carrying out of the business “through" that place.

From an Indian tax jurisprudence perspective, the Andhra Pradesh High Court, while interpreting a similar clause in the DTA between India and Germany, has held that a Permanent Establishment postulates the existence of a substantial element of an enduring or permanent nature of a foreign enterprise, which can be attributed to a fixed place of business in India. It should be of such a nature that it amounts to a virtual projection of the foreign enterprise in India. Commissioner of Income Tax v. Vishakhapatnam Port Trust, (1983) 144 ITR 146 (AP).

In the case of Motorola, Inc. & Ors. v. DCIT, (2005) 96 TTJ 1 (ITAT). the employees of Motorola, Inc. rendered certain services from the office of Motorola's Indian subsidiary. The salary of these employees was borne by Motorola, Inc. However, the perquisites were borne by the Indian subsidiary. Further, the employees also performed certain services for the Indian subsidiary. The Income Tax Appellate Tribunal (the “Tribunal”) ruled that these employees worked for Motorola, Inc, in India. They used the office of the Indian subsidiary to carry on Motorola, Inc's work, and thus, there was a projection of Motorola in India in the Indian subsidiary's office. It was held that the Indian subsidiary was a fixed place of business of Motorola. However, it was ultimately held that the Indian subsidiary's activities were preparatory or auxiliary in nature, and therefore, Motorola, Inc. did not have a Fixed Place Permanent Establishment in India. In this case, Nokia was also a party, and it had a wholly owned subsidiary in India. Nokia's Indian subsidiary was engaged in supporting Nokia's main activities. The Tribunal held that Nokia had a Permanent Establishment in India as the Indian subsidiary's nature of activities was much more than just preparatory or auxiliary. However, Ericsson, which was the third party in this case, was held not to have a Permanent Establishment in India because, although Ericsson's employees performed certain services using the office of Ericsson's Indian subsidiary, in fact, they had no right to enter the Indian subsidiary's office to carry on Ericsson's activities. Therefore, the Tribunal concluded that Ericsson had no Permanent Establishment in India through its Indian subsidiary.

India's Supreme Court has held that an Indian enterprise performing “back office” functions for an American enterprise, would not be regarded as a Fixed Place Permanent Establishment for the American enterprise in India as “back office” functions were auxiliary and preparatory in nature. DIT v. Morgan Stanley Co. Inc., 292 ITR 406 (2007).

In a recent case eFunds Corporation (“eFunds USA”) had an Indian subsidiary that provided certain “back office" services to eFunds USA. The Indian subsidiary bore limited risks, had little to none assets to perform the services independently, and relied on eFunds USA for performing the services. Here, the Tribunal ruled that the Indian subsidiary was not an independent contactor, but a “partner in business”, and the Indian subsidiary was deemed to be eFund USA's Permanent Establishment in India. The Tribunal observed on the basis of the Form 10K filed by eFunds USA that the activities of eFunds USA in India were not preparatory and auxiliary in nature; rather, they were core income generating activities. It further observed that “it is clear from the above reproduction from the assessee's own statement as given in form 10-K 405, that the operations carried out in India by the Indian entity are integral part of eFund USA's income generating activity. The Indian entity is an independent legal entity to which work has been allocated. However, the Indian entity is not a contractor of the appellants but a partner in business where very limited or almost nil risks of the business of the appellant are borne by the Indian entity.” eFunds Corporation v. ADIT, 2010-TII-165-ITAT-DEL-INTL.

Preparatory or Auxiliary

There has been a fair amount of judicial debate on this point in India. The Supreme Court of India has held that an Indian enterprise performing “back office” functions which support the front office for an American enterprise will not result in a fixed place Permanent Establishment. (DIT v. Morgan Stanley Co. Inc., 292 ITR 406 (2007)). While discussing the term “auxiliary”, the Delhi High Court has held

that this term connotes activities that can be described as "aiding or supporting" or "subsidiary" to the main business. (UAE Exchange Centre v. Union of India, (2009) 223 CTR (Del) 250.)

Agency Permanent Establishment

An agency is said to be established when one entity is expressly or impliedly authorized to act on behalf of another entity. (Syed Abdul Khader v Rami Reddy, AIR 1979 SC 553). On issues dealing with independent agents, the Delhi bench of the ITAT held that if an Indian agent is entirely dependent on a foreign enterprise for its business, then it can be said that the agent is "functionally and financially" dependent on the foreign enterprise. (Amadeus Global Travel Distribution v. DCIT, (2008) 113 TTJ (Delhi) 767)

In one of the rulings, the AAR faced a situation wherein a foreign enterprise had an agent in India, and as per the terms of the agency contract, any contract concluded by the agent required the approval of the foreign enterprise. However, it was found that the agent was routinely concluding contracts on behalf of the principal without any protest or dissent. The AAR held that this would result in an Agency Permanent Establishment (TVM Ltd. v. CIT, (1999)237 ITR230 (AAR)).

Permanent Establishment- Period

There is no specific time period for the determination of a Permanent Establishment in India. It varies from case to case. The Authority for Advance Rulings ("AAR") stressed on the phrase "carried on", stating that the business of the foreign enterprise must be carried on in India. In a ruling by AAR wherein a UAE company which engaged different golf courses in India for conducting tournaments for a period less than a week, the issue arose whether the golf course could be reckoned as the Permanent Establishment of the UAE enterprise. The AAR ruled that the phrase "carried on" is indicative of "continuum, frequency or regularity". Therefore, one isolated golf tournament cannot be held as the business being "carried on". However, on the issue of the golf courses being used for a period of less than a week, the AAR ruled that given the special nature of the business activity, the duration of business operations can be short. (In re Golf in Dubai, LLC, (2008) 219 CTR (AAR) 513.)

Article 6 Income from immovable property

See treaty text

The general rule is that income derived by a resident of a Contracting State from immovable property in the other State may be taxed in that other State. Income from agriculture and forestry is not included. Thus, for instance, if a resident of one State owns a building in the other State and receives rent, that rent may be taxable in the other State.

This treatment also applies to income from immovable property used by an enterprise and to income from immovable property used for the performance of independent personal services.

Immovable property is defined as per the domestic law of the State in which the property is located but it will include livestock and equipment used in agriculture, forestry, general property rights and rights for the working of natural resources.

Domestic Law:

Denmark

Under Danish domestic law, profits from sale of real estate specifically comprises capital gains under the Danish Capital Gains on Property Tax Act (ejendomsavancebeskatningsloven) and recaptured tax depreciation under the Danish Tax Depreciation Act.

Danish tax law generally provides for possibility of deducting financing costs on real estate/property under the same circumstances in income and profit thereon as Danish owners of property/real estate. However, in administrative practise it has been determined that for tax purposes it is only possible to allocate financing costs corresponding to debt financing of 80 percent of the value of the real estate to the Danish real estate for Danish tax purposes. Further, foreign currency exchange gains and losses on real estate financing are not deemed to be allocable to the Danish real estate for Danish tax purposes.

When Denmark is the source state, which it is when the immovable property is located in Denmark, there is legal basis in national tax law for taxing operating profits relating to the property in the Danish Tax at Source Act (kildeskatteloven), sect. 1, (1), (5) and in the CITA sect. 2, (1), (b).

Since the Convention does not cover wealth taxes, property value tax (ejendomsværdiskat), which is considered a partial wealth tax, is not within the scope of the Convention.

India

Income from immovable property under the Indian tax law can generally be either classified as income from house property or as capital gains arising from the transfer of a capital asset. Owners of buildings and any land appurtenant thereto (except those land and buildings being used for business or profession) are obligated to pay tax on the annual value of such land and buildings which is either the actual rent received by the owner or the rent that could reasonably be expected to be received if

such property was to be let out. Certain deductions are permitted to be made from this annual value to arrive at the taxable value.
Capital gains accrue on the sale of immovable property if the sale price of such immovable property is more than the acquisition price. Further, costs incurred in connection with the acquisition of immovable property and costs incurred towards improvement are allowed to be deducted from the sale price to arrive at the capital gains. The Act, subject to certain conditions, also permits indexation of the cost of acquisition to off-set the effects of inflation.
Further, Section 50C of the Act embodies a special provision for determining the full value of consideration of immovable property in certain cases. It provides that where the consideration received or accruing as a result of the transfer of land or building or both, is less than the value adopted or assessed or assessable by the stamp valuation authority for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall be deemed to be the full value of the consideration received or accruing as a result of such transfer.

Article 7 Business profits

See treaty text

If an enterprise has both a permanent establishment in a State and also derives other income, say, dividends, royalties or interest unconnected with the permanent establishment, then the dividends or interest may only be taxed in accordance with Articles 10, 11 and 12 of the Treaty and not this Article.
Generally the profits to be attributed to the permanent establishment are the profits that would be expected if the permanent establishment was a distinct and separate enterprise. The starting point for the computation of profits will be the branch accounts, assuming they exist.
The OECD, in 2008, published its final report on the attribution of profits to permanent establishments (July 17, 2008) and updated the Commentary on Article 7 of the Model Treaty. When interpreting a tax treaty, it is generally agreed that the latest version of the OECD's Commentary on the Model Treaty should be used. These notes follow the 2008 version of the Commentary. The “authorised OECD approach” to attributing profits to a permanent establishment now requires that there is a two step process.
Firstly, a functional and factual analysis should be carried out, along the lines set out in the OECD's transfer pricing guidelines, to establish the economically significant activities and responsibilities undertaken by the permanent establishment. This will involve establishing the rights and obligations arising out of transactions between the permanent establishment and third parties, e.g. the sales revenue arising from independent customers generated by the permanent establishment as opposed to by the head office. If the permanent establishment takes the form of a factory, then it would assume the obligation to pay for the raw materials which it uses. The OECD then recommends that “significant people functions” relevant to the attribution of economic ownership of assets are identified to support the attribution of economic ownership of assets of the enterprise to the permanent establishment. Economic ownership is defined as the right to income from an asset or the right to depreciate it. Tangible property should be attributed to the location where it is in use. Economic ownership of intangibles rests with the location in which the risks associated with the intangibles is borne: For instance, if an enterprise owns a patent for a particular drug which is sold by distributor companies in many countries, the economic ownership would rest in that part of the enterprise responsible for commissioning the research to develop the drug and which would bear the losses if medical trials failed. A further set of “significant people functions” are then to be identified: this time, those relevant to the assumption of risks so that an allocation of risks borne by the enterprise can be made to the permanent establishment. For instance, road building equipment may be economically owned by a permanent establishment in Country A but the head office, located in Country B, may have the power to determine on which road building projects the equipment is used and hence the head office bears the risk associated with profits or losses arising from the equipment. The more risks that are managed by the permanent establishment, the higher the share of the profit of the enterprise to be attributed to it. The OECD's 2008 Report looks for the place of active decision taking rather than mere “rubber stamping”. Note that no such distinction between asset management and risk assumption functions are required in the case of enterprises in the financial sector, because it is considered highly likely that these functions would be carried out by the same people.
Secondly, taking into account the picture built up in the functional and factual analysis, the profits of the permanent establishment must be determined. Although this is relatively simple in the case of transactions with third parties, transactions and dealings with other parts of the enterprise must be determined using the rules laid down in the OECD's Transfer Pricing Guidelines. This means that goods and services provided by head office must carry an arm's length mark up. Pricing policies should be properly documented, which in practice may prove troublesome as firms may not take the same care

in documenting the terms of transactions within the firm as they would with third parties. In determining the profits attributable to the permanent establishment, part of the enterprise's interest costs on its borrowings should be allocated to the permanent establishment. The amount of capital needed to support to functions carried out by the permanent establishment on the assumption that it is a separate entity must be calculated. Then, this total theoretical capital must be broken down into debt and equity (or "free capital" in OECD terms). The greater the risks undertaken by the permanent establishment, the higher the proportion of its notional capital that will be regarded as "free capital". Several methods of establishing the split between "free capital" and debt capital are suggested, including the use of thin capitalisation practices in the State in which the permanent establishment is located. Once the amount of notional debt capital has been determined, an allocation of the enterprise's interest liabilities can be made to the permanent establishment. Note that only actual interest liabilities can be allocated. If the enterprise as a whole has paid no interest to external lenders, then there can be no allocation of interest liability to the permanent establishment. The only exception to this rule is where the permanent establishment is involved in treasury dealings with other parts of the enterprise. Whilst this may well be the case in banking enterprises, it would be unusual in other enterprises. Generally, the interest rates used and the terms of the notional loans to the permanent establishment must be such as would be found between parties dealing at arm's length. When deciding what transactions should be recognised between the permanent establishment and other parts of the enterprise, the OECD recommends that the only internal transactions which can be recognised in arriving at the permanent establishment's profits are those which relate to real and identifiable events. These would include the physical transfer of goods, the provision of services, the use of intangibles and the transfer of financial assets. Whilst the internal records (e.g. the branch accounts) are the starting point for identifying these transactions, the true test is whether there has been an internal dealing of economic significance. The OECD's 2008 report suggests the following tests are used when considering whether an internal dealing should have any effect on the profits of a permanent establishment:

- Is the documentation consistent with the economic substance of the internal dealings?

- Are the arrangements such that they are not too different from dealing which one group company might have with a fellow group company? For instance, credit periods should be similar in similar circumstances.

- Are the dealings consistent with the OECD principles for attributing profits to permanent establishments?

Allocations of head office expenses, e.g. for strategic management or centrally managed support functions such as payroll may be set against the profits of the permanent establishment, but the arm's length principle must be observed.

The allocation of profits to dependent agent permanent establishments

A dependent agent is not part of the taxpayer enterprise and will file his tax returns independently. Normally the enterprise will make payments to the agent for his services. The question is: Should the host State merely tax the profits of the agent (the "single taxpayer approach") or should there be an additional charge on the enterprise which is using the services of the agent? The amount of the charge would depend on the excess of the enterprise's profits over the amount paid to the agent which was attributable to the activities of the agent. For instance, a dependent agent may be paid for the sales he procures on a commission bases, but the selling enterprise may make a profit on those sales even after taking into account the (arm's length) commission paid to the agent. The OECD recommends that States should always consider whether the enterprise has made a profit in respect of business transacted via the agent which is in excess of amounts paid to the agent. Hence the host State may tax both the dependent agent and the foreign enterprise.

Alternative method of attribution of profits

This Treaty permits an allocation of the profits of the enterprise to a permanent establishment based on an apportionment of the total profits of the enterprise. This is sometimes known as the unitary, or indirect method of apportionment. It is only acceptable to use this method if it has been customary to do so and in any case, the outcome must be in accordance with the result which would be obtained by using the Authorised OECD Approach (AOA) as set out above.

As is usual no profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise. The same method of attribution is to be used year by year unless there is good and sufficient reason to the contrary.

Domestic law

Denmark

The definition of a Permanent Establishment for Danish domestic law purposes as well as the allocation of profits thereto generally follows that of the OECD Tax Model Convention. A number of decisions consider the existence of a Permanent Establishment and allocation of profits thereto for Danish tax purposes, most of which are based on actual circumstances. Sec. 2 of the Danish Corporate Income Tax Act (selskabsskatteloven) specifically states (i) that permanent establishment building and construction sites which constitute a permanent establishment are considered as established on the first day thereof (ii) that shares can be allocated to a permanent establishment if such shares constitute a part of the core capital of the Permanent Establishment (iii) that profits and losses as well as recaptured depreciation on the sale of goods allocable to the Permanent Establishment is taxable in Denmark. As a significant exception to the main rule that a Permanent Establishment is from a Danish tax perspective considered to be a separate entity, a Danish supreme court ruling from 1993 determined that "interest" payments from a Danish Permanent Establishment to its head office on a "loan" granted to the Permanent Establishment would not be tax deductible for the Permanent Establishment.

Section 8 of the Danish Corporate Income Tax Act lies down a territorial principle for certain corporate activities as it states that if a Danish enterprise has a permanent establishment abroad Denmark will exempt income allocable to such permanent establishment abroad, unless (i) the state in which the Permanent Establishment is located waive its right of taxation under a tax treaty with Denmark or other international agreement, (ii) income in the Permanent Establishment would have been taxable under Danish CFC tax rules if the Permanent Establishment had been a company, or (iii) the income in the Permanent Establishment is income from the operation of ships or aircraft in international traffic.

India

For a non-resident, only that income is subject to tax in India that, inter alia, accrues or arises, or is deemed to accrue or arise in India. (Section 5 of the Act). In this regard, any income accruing or arising, directly or indirectly, through or from a "business connection" in India to a non-resident, is deemed to accrue or arise in India and hence, such income is taxable in India. (Section 9 of the Act.) The term "business connection" is very wide and what constitutes business connection has been the subject matter of judicial scrutiny in a large number of cases. Business connection may take several forms; it may include carrying on a part of the main business, or activity incidental to the main business of the non-resident through an agent, or it may be a relation between the business of the non-resident and the activity in India, which facilitates or assists the carrying on of that business. (CIT v. R. D. Aggarwal & Co., [1965] 56 ITR 20.) However, when the non-resident is entitled to relief under a tax treaty, the provisions of the Act only apply if they are more beneficial to the taxpayer. (Section 90(2) of the Act.)

If a non resident entity is reckoned as having a PE in India, only the following business profits can be subject to tax in India:

(i) the income attributable to the PE;

(ii) the income generated from the sale of goods, etc., of the same or similar kind as those sold through the PE; and

(iii) the income from other business activities carried on by the non resident entity in India of the same or similar kind as those effected through the PE. (Article 7(1) of the Treaty). Further, the income attributable to the PE will be the income which the PE might be expected to generate if it were dealing at an arm's length basis with the non resident. (Article 7(2) of the Treaty.)

India's Supreme Court in the case of Morgan Stanley ((DIT v. Morgan Stanley Co. Inc., 292 ITR 406 (2007), held that no further income will be attributable to a Service PE (occasioned due to the secondment of employees of an American company to its Indian subsidiary) of an American enterprise if the dealings between the American enterprise and its Indian subsidiary are being conducted at arm's length. However, it also held that the situation would be different if the transfer pricing analysis does not adequately reflect the functions performed and the risks assumed by the enterprise. In such a case, there would be a need to attribute profits to the PE for those functions/risks that have not been considered.

Further, in the judicial cases of Galileo (Galileo International v. DCIT, 2007 TIOL-447- ITAT Del.) and Amadeus (Amadeus Global Travel Distribution v. DCIT, (2008) 113 TTJ (Delhi) 767), apart from an Equipment PE (on account of computers provided to agents), the foreign companies were held to have an Agency PE in India on a dependent agency theory. Having said so, they were compensating the Indian agent on an arm's length basis. Accordingly, the Delhi Bench of the ITAT held that no further profits would be attributable to the PE in India. While arriving at this conclusion, the ITAT relied on a

circular issued by the tax authorities that stated that no further profits of a foreign enterprise are to be taxed in India, where the remuneration of the agent fully represented the value of the profits attributable to the service provided by the agent. (Circular Number 23, dated July 23, 1969, issued by the Central Board of Direct Taxes.) They also relied on a similar judgment of the Bombay High Court rendered in the context of the India - Singapore Treaty. (SET Satellite (Singapore) Pte Ltd. v. DDIT, (2008) 110 BOM LR 2726.)

Therefore, based on Morgan Stanley's ruling, if the non resident entity compensates the Indian entity on an arm's length basis adequately reflecting the functions performed and the risks assumed by the Indian entity, it is more likely than not that no income of the non resident entity will be brought to tax in India, if a PE is occasioned. However, this will depend on the fact pattern of each case. Further, Morgan Stanley, as such, related to a Service PE issue. Additionally, the circular relied on by the Tribunal in the above mentioned cases has since been withdrawn.

In a situation, where the tax authorities seek to calculate the taxable income under the Act and the rules made thereunder they can resort to either one of the following three methods:

(a) Presumptive method - tax authorities ascertain a reasonable percentage of the turnover;

(b) Proportionate method - the tax authorities ascertain the profits on the basis of the ratio between global turnover and Indian turnover; and

(c) If none of the above two methods work, the tax authorities may use such other method as they may “deem fit." (Rule 10 of the Income Tax Rules, 1962.)

Article 8 Air transport

See treaty text

This provision relates to income derived from the operation of aircrafts in international traffic. Profits derived by an enterprise of a Contracting State from the operation of aircraft in international traffic shall be taxable only in that State. Interest on funds connected with the operation of aircraft in international traffic shall be regarded as profits derived from the operation of such aircraft, and the provisions of Article 12 shall not apply in relation to such interest.

Denmark

With respect to profits derived by the Danish, Norwegian and Swedish air transport consortium, known as the Scandinavian Airlines System (SAS), the provisions of paragraphs 1 and 3 shall only apply to such part of the profits as corresponds to the shareholding in the consortium held by SAS Denmark A/S, the Danish partner of Scandinavian Airlines System (SAS).

India

Section 44BBA of the Act contains a special deeming provision for computing the profits and gains accruing to non-residents from the business of operation of aircraft. Five percent of the aggregate of all amounts paid or payable (whether within or out of India) to the non-resident assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India and all amounts received or deemed to be received in India by the non-resident assessee or by any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place outside India are deemed to be the profits and gains of the business of the operation of aircraft chargeable to tax in India.

Article 9 Shipping

See treaty text

This provision relates to income derived from the operation of ships in international traffic. The Treaty provides that such income shall only be taxable in the state in which the seat place of effective management of the enterprise is situated

Notwithstanding such profits may be taxed in the other Contracting State from which they are derived provided that the tax so charged shall not exceed - during the first five fiscal years after the entry into force of this Convention, 50%, and during the subsequent five fiscal years, 25%, of the tax otherwise imposed by the internal law of that State. Subsequently, only the provisions of paragraph 1 (what said above) shall be applicable.

Interest on funds connected with the operation of ships in international traffic shall be regarded as income from the operation of such ships and the provisions of Article 12 shall not apply in relation to such interest; and

Profits from the operation of ships includes profits derived from the use, maintenance or rental of containers (including trailers and related equipment for the transport of containers) in connection with the transport of goods or merchandise in international traffic.

India

The Treaty between India and Denmark relating to operation of ships came up for consideration (with reference to Article 9) by the ITAT in A.P. Moller, Maersk Agency India Pvt. Ltd. v. Dy. CIT ((2004) 89 ITD 563 (Mumbai). The ITAT held that the income derived from the shipping business including slot fees and ancillary charges would attract tax liability in India under Article 9 and such income from shipping business would fall within the scope of section 44B of the Act.
The Calcutta High Court in the case of Universal Cargo Carriers Inc. v. CIT ((1994) 205 ITR 215 (Cal) decided whether shipping business income would be tax exempt in India. In this case the non-resident shipping company incorporated in Panama claimed that it was a resident of Greece and was accordingly entitled to the benefit of tax concession under the Treaty. This plea was rejected by the Indian tax authority based on an agreement under which the affairs of the company in Panama were to be managed by a company in Greece and the Greek company had to render accounts in Panama for which the Greek company was entitled to exemption.
The question arose whether the company in Greece was exercising control and management of the affairs of the Panama company in relation to its business. The court held, on facts, that the Panama company was entitled to claim relief under the provisions of Article 2 (1)(f) of the Treaty between India and Greece and also held that the income from the shipping business of the Panama company must be treated as that of a resident in Greece eligible for 50 per cent concession in respect of the shipping business as per Article 6 of the Treaty. The court also held that the ITAT and the lower authorities in India were not justified in denying the claim for concession to the Panama company in terms of the Treaty because the expression "control and management" used in the Treaty must be taken to mean de facto control and management and not merely the right or power to control and manage the affairs of the company as held in CIT v. Bank of China ((1985) 154 ITR 617 (Cal) and CIT v. Chitra Palayacat ((1985) 156 ITR 730 (Mad).

Article 10 Associated enterprises

See treaty text

This Article contains the usual OECD provisions regarding transfer pricing. Associated enterprises must adopt the arm's length principle in their dealings with each other, and to the extent that they do not, a Contracting State may make an upwards adjustment to taxable profits.
There is no specific provision for the other State to make a corresponding downwards adjustment in taxable profits.
The position regarding "secondary adjustments" is not dealt with. If one State makes an upwards adjustment of taxable profits and the other makes an exactly equal corresponding downwards adjustment, then the tax revenues of the two States might still be different to what they would have been had arm's length pricing been applied in the first place. This is because higher profits in the State where the upwards adjustment took place might well have given rise to higher dividends or interest payments, on which withholding taxes might have been chargeable. So even though the State making the upwards adjustment has retrieved the tax deficit on the enterprise resident there, it has still not retrieved any deficit in withholding taxes. Whether it makes a secondary upwards adjustment to make good this deficit in withholding tax receipts depends on whether this is provided for in domestic law. If it does so, then double taxation will be the result which will not necessarily be relieved by the normal treaty Article on elimination of double taxation and it may be necessary to invoke the mutual agreement procedure.

Domestic law:

Denmark

Under Danish domestic law, transfer pricing rules as well as transfer pricing documentation rules apply which provide that Danish taxable persons and Permanent Establishments in Denmark which carry out business transactions with group related entities are treated for tax purposes as if such transactions are carried out at arm's length. The definition of group related transactions is relatively wide under Danish tax law as it applies to transactions with a party, which controls or is controlled by another party. "Control" means direct or indirect legal ownership of more than 50% of the shares or legal control over more than 50 % of the voting rights. Ownership or control has not been conferred from a pledgor to a pledgee solely as a result of a pledge over shares.
When determining whether a party controls the Danish borrower (or vice versa), votes and shares held by group-related entities are considered. Votes and shares held by non-related shareholders may also be considered if an agreement has been made between a party and non-related shareholders for the purpose of "exercising a common controlling influence" over the Danish borrower. A shareholders agreement may in this context constitute an agreement to "exercise common controlling influence" over the other party.

Not only taxable legal entities are considered as entities for purposes of control; also fiscally transparent entities may be considered if they are "are governed by rules of corporate law, a corporate law agreement or Articles of association".
"Group related" means two or more entities which (i) directly or indirectly are controlled by the same group of shareholders or (ii) which are under common management.
Two parties may be considered to be group related by virtue of common management if they have the same manager or if they have different managers that have entered into an agreement providing for a common management of the lender and the borrower.
In determining an arm's length price the approach taken in the OECD transfer pricing guidelines is generally applied.

India

International transactions between associated enterprises are governed by transfer pricing rules contained in the Act. These rules provide for a very wide definition of the term associated enterprises and are inclusive of direct as well as indirect participation of an enterprise in the management or control or capital of the other enterprise.
Further, two enterprises are "deemed" to be associated enterprises under section 92A of the Act, once certain conditions are fulfilled. These are
(i) direct/indirect shareholding of 26% or more of voting power;
(ii) authority to appoint more than 50% of the board of directors;
(iii) dependency in relation to intellectual property rights;
(iv) dependency relating to loans not less than 51% of total assets; or purchase/sale of goods by an enterprise from/to the other enterprise at prices and conditions influenced by latter, etc.
An accountant's report is also required to be submitted to the Indian tax authorities on an annual basis. This is with regard to the arm's length nature of the international transactions with associated enterprises. The accountant's report certifies the accuracy of the information disclosed and the documentation maintained by the taxpayer and includes details regarding the description of the international transaction entered into, the quantity, value, amount paid/payable, amount received/receivable and the method adopted to test the arm's length criterion, etc.
The Indian transfer pricing regulations require that an arms length price in relation to an international transaction be determined by any of the prescribed methods, being the appropriate method. This practice is generally followed by taxpayers having international transactions.
The prescribed documentation includes information on the parties involved (such as corporate overview, Indian operations, etc.), as well as information relating to the reportable international transactions. More specifically, such documentation is required to incorporate:
(i) the description of the ownership structure of the taxpayer, the profile of the multinational group, including names, addresses, legal status and country of tax, and relationship with all associated enterprises;
(ii) business overview of the taxpayer and of associated enterprises, and the description of industry in which the taxpayer operates;
(iii) description of functions performed, risks assumed and assets utilized by transacting parties;
(iv) nature, terms, volume and value of each international transaction and details of property/service involved, commercial agreements, assumptions and policies with respect to the transactions with associated enterprises and third parties, if any;
(v) record of comparable uncontrolled transactions and economic analysis performed to evaluate their comparability with the relevant international transaction;
(vi) description of methods considered, explanation regarding selection and application for determining the arm's-length price in relation to each international transaction;
(vii) details of comparable data used in applying the most appropriate method and adjustment made to account for differences between controlled and uncontrolled transactions;
(viii) underlying supporting documentation such as copies of invoices, contracts, etc.

Article 11 Dividends

See treaty text

This Treaty provides for rates of withholding tax on dividends below those which may be charged in the absence of any agreement between the two countries.
This Treaty in Paragraph 2, provides that maximum withholding tax rates are to be

- 15% where the recipient owns at least 25% of the paying company's share capital; and
- 25% in other cases.

Paragraph 3 defines the term “dividends” to include income from shares, jouissance shares or jouissance rights, mining shares, founders' shares or other rights to participate in profits. Also included is other income subjected to the same tax treatment as income from shares under the domestic laws of a State. Jouissance shares or rights are financial instruments which grant rights of the types enjoyed by shareholders but which, in some jurisdictions, are viewed as debt rather than equity.
Paragraph 4 provides that where, say, a India company receives a dividend from a Danish company, and that dividend is effectively connected with a permanent establishment which the India company has in Denmark, then the dividend income will be deemed to be part of the income of the permanent establishment and the provisions of Article 7 and Article 14 dealing with the attribution of business profits will apply.
Paragraph 5 contains the usual provision that a State does not have the right to levy any tax on a dividend unless either the dividend is paid by a resident company or received by a resident shareholder. Thus the fact that a dividend paid by, say, a Denmark company may be sourced from profits earned by a permanent establishment which that Denmark company has in India, does not give India any taxing rights over that dividend, unless of course, it is received by Indian shareholders.

Domestic law

Denmark

Individuals

The distribution of dividends from a Danish company to a non-resident individual is generally subject to withholding tax at the rate of 27%. The shareholder may seek a refund from the Danish tax authorities of the tax withheld in excess of 10%. In practise this is done by completing and filing ready print reclaim form 06.003 (available online at www.skat.dk) with the Danish tax authorities (Skattecenter Ballerup), which must contain a statement from the India tax authorities that the beneficial owner of the payment is resident in India.
If the shareholder (in aggregate with shareholders group related to the shareholder) holds less than 10% of the nominal share capital in the Company and the shareholder is tax resident in India, the final tax rate is 15%.
In addition it is possible for the Danish Securities Centre or the dividend distributing company to enter into an arrangement with the Danish tax authorities according to which the obligation to withhold tax is reduced to the tax rate stipulated in the double taxation treaty with the relevant State.

Companies, etc.

Dividends from subsidiary shares (i.e. shares which constitute at least 10% of the share capital in the issuing company) are exempt from Danish withholding tax provided the taxation of dividends is to be waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with the Treaty. Further, dividends from Group Shares (i.e. share in a company in which the shareholder of the company and the issuing company are subject to Danish tax consolidation or fulfill the requirements for international tax consolidation under Danish law) are exempt from Danish withholding tax provided the company investor is a resident of the European Union or the European Economic Area and provided the taxation of dividends should have been waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with a tax treaty with the State in which the company investor is resident had the shares been Subsidiary Shares.
Dividends from Portfolio Shares (i.e. shares which are not Group Shares or Subsidiary Shares) will be subject to taxation irrespective of ownership period.
Dividend payments on Portfolio Shares will be subject to a withholding tax of 27% irrespective of ownership period. The final tax may be reduced pursuant to the Treaty. If the shareholder holds less than 10% of the nominal share capital in the Company and the shareholder is tax resident in India, the final tax rate is 15%, also under Danish domestic law. In practise reclaim of Danish withholding tax is done by completing and filing ready print reclaim form 06.003 (available online at www.skat.dk) with the Danish tax authorities (Skattecenter Ballerup), which must contain statement from the India tax authorities that the beneficial owner of the payment is resident in India. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.

Beneficial ownership

Until recently, the requirement of beneficial ownership (and the content of this term) - although formally existing under the Danish withholding tax rules - has not been subject to real attention from the Danish tax authorities and still no clear guidance on the application thereof by the Danish tax authorities currently exist. However, the Danish Supreme Court has confirmed that specific provisions

of Danish tax treaties should generally be interpreted in accordance with the OECD Commentary (to the extent applicable). The tax authorities have also referred to the OECD Commentary whenever (vaguely) commenting on the concept of beneficial ownership.

Relief under EU law (the EU directives 90/435 and 03/49)

The parent/subsidiary directive does not contain any beneficial ownership provisions. Instead, Article 1 of the parent/subsidiary directive contains a general abuse exception according to which protection under the Dividend Directive may be denied pursuant to domestic or agreement-based (e.g. treaty-based) anti-abuse provisions. We believe that the general anti-abuse exception in Article 1 with almost certainty will be held to reflect the general principle in EU law that abuse of rights is prohibited and that instruments of EU law cannot be extended to cover abusive practices.

Article 1 of the interest and royalty directive sets out a beneficial owner condition. Article 1(4) explains that the receiving company shall be treated as the beneficial owner only if it "receives those interest payments for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person." Beyond this, the interest and royalty directive contains no definition of the concept of beneficial ownership and we have not identified any instruments of EU law which operate with the concept in any way that seems relevant to the interest and royalty directive. It would seem that beneficial ownership is a novel concept in EU law. Thus, the specific meaning of the concept of beneficial ownership in the context of the interest and royalty directive must be held to be uncertain. It will be for the European Court of Justice (ECJ) to determine specifically what it means.

It is conceivable that the ECJ would interpret both the beneficial owner condition and the general anti-abuse exception in light of its extensive case law dealing with abusive practices. Further, it is conceivable, based on the abuse test as it stands after Cadbury Schweppes, that the ECJ would not accept an allegation of abuse under the parent/subsidiary directive or the interest and royalty directive unless it can be established by objective verifiable factors that :

1. The structure has only been established for the purpose of escaping Danish dividend withholding tax; and
2. the establishment of the structure constitutes a "wholly artificial arrangement" which does not reflect a "genuine economic activity" carried out in the residence State of the shareholder.

On 16 March 2010 the Danish Tax Tribunal (Landsskatteretten) published a long awaited ruling on beneficial ownership which found in favour of the tax payer in a structure put in place by certain non-Danish private equity funds which had acquired a Danish company by using a Danish-Luxembourg acquisition structure with a Luxembourg top holding company. On distributing dividends to the Luxembourg no Danish tax was withheld on dividends. The dividends were subsequently reinvested by the Luxembourg company by extending a loan to the dividend distributing company, which was ultimately reinvested into the Danish company acquired. The Tax Tribunal stated that the requirement of beneficial ownership is from a Danish perspective applied as an anti-abuse measure. However, as the dividend payment to the Luxembourg company was in the case At hand not paid on to the shareholders therein, the company could not be considered as a flow-through entity and as such would qualify as the beneficial owner of the dividend. As a result, the dividend distributing company was correct in not withholding tax on the dividend paid to the Luxembourg company.

India

There will be no withholding tax on dividend payments if the resident Indian company distributing the dividends has paid dividend distribution tax ("DDT"). The basic tax rate of DDT is approximately 17% including EC and SHEC.

As DDT is not a withholding tax withheld from the payment made to the shareholder, the shareholder generally would find it difficult to claim tax credit for such DDT suffered in its jurisdiction. Further, DDT is not allowed under the Act to be claimed as a deductible expenditure. With effect from June 1, 2011, DDT will be applicable to units operating within Special Economic Zones ("SEZ") which were earlier exempted. Most importantly, DDT must be paid on profits distributed even if no income tax is otherwise payable.

Beneficial ownership

Multinational companies investing in India often use investment structures with holding company, financing or licensing company resulting in flow of dividends, interest or royalties from India to such companies and in this context it becomes imperative that for claiming treaty benefit such companies are not only resident of the relevant country but are also the 'beneficial owner' of income.

Almost all the existing Indian treaties already include an implicit anti-tax avoidance provision in the form of a rule of beneficial ownership. Articles dealing with interest, royalty and dividend income provide that the rate of tax levied in the source country cannot exceed the prescribed concessional rate provided the beneficial owner of such income is the resident in the other state.

The term 'beneficial ownership' is not defined either in the treaties or in the domestic law. There are a few judicial precedents on the rule of beneficial ownership. Hence, when the income in the form of interest, royalty, etc. flowing out of India is received by a company resident in the other country which is in turn a wholly owned subsidiary of company in another country, revenue authorities may be tempted to challenge the satisfaction of beneficial ownership test.
In one of the early advance ruling in case of Natwest, the authority observed that in case of a wholly owned subsidiary, income of the subsidiary could be subject to control and direction of the sole shareholder and hence it could be possible to take a view that subsidiary is not a beneficial owner of the income.
OECD and UN model commentaries point out that the purpose of the beneficial ownership test is to prevent tax avoidance by persons not entitled to protection by a treaty but claiming the same with the help of interposed persons. The commentaries also further mention that a subsidiary can be considered to be a beneficial owner even if its entire capital is held by shareholders resident outside that state.
Beneficial ownership is a key concept in being able to access double tax treaties, yet it is largely an undefined common law concept. There have been few decisions on the interpretation of the term and such decisions have lacked any consistency. The latest view of the term came from the Tax Court of Canada in Pr vost Car Inc. -v- Her Majesty the Queen (2008TCC231).
The case concerned a Dutch holding company, Pr vost Holding (PH) of a joint venture between UK and Swedish shareholders. PH, although incorporated in the Netherlands, had no physical office or employees. PH in turn held all of the shares in a Canadian company, Pr vost Car (PC). During the course of a six-year period, PC paid 12 dividends to PH. The principal issue was whether for the purposes of the Canadian/Dutch treaty, the holding company (PH) was the beneficial owner of dividends it had received and which it subsequently passed on to its own shareholders.
The Canadian Court overturned the decision of the Canadian Revenue Agency and held that PH was in fact the beneficial owner of the dividends. The reason for the decision was that PH had discretion as to the application of the dividends, given it was not bound legally to distribute them to its shareholders following receipt. PH was said to have both received the dividend for its own use and assumed both the risk and control of the dividends received from PC. In order to pierce the corporate veil and regard the shareholders as the beneficial owners of dividends received by a holding company, there would need to be absolutely no discretion resting with that holding company as to the use or application of the dividend received. In the case, legally, it was for the directors of PH to declare the dividend. PH shareholder approval also was required before any dividend could be paid on.
The decision is important because of its potential wide-reaching concern to many multinational business structures and notably to the position of intermediary holding and financing companies.
The authority of this case has yet to be tested and the Crown has appealed the decision. A loss on appeal may provoke the Canadian authorities to amend its tax treaties. Nonetheless, the Pr vost judgment is the first case, albeit at first instance, to consider beneficial ownership "in a completely unfettered way", with a result favourable to the taxpayer. The case can be contrasted with the unusual facts decided upon, using Indonesian tax law principles, the English case of Indofood -v- JP Morgan [2006] EWCA Civ 158. There, the main purpose and arguably the only purpose of suggesting a Netherlands company as an intermediary financing vehicle would be to avoid a higher tax burden. In such circumstances, where the intermediary was, in practical terms, bound to pay on interest it received, the Court decided that the beneficial interest would not rest with the intermediary Dutch company. It was accepted in Pr vost that there were good commercial reasons for choosing the Netherlands as a holding jurisdiction.
Indofoods also concerned beneficial ownership in the context of interest payments. By comparison to dividends, there tend to be fewer, if any, legal formalities required to make interest payments and it may be that this is seen as a distinguishing factor in looking at whether the recipient is merely a conduit.
However, the decision of Pr vost effectively concluded that unless there was a legal obligation on PH to pay dividends received to its shareholders, PH would be the beneficial owner. It would not have been sufficient, as it was in Indofoods for the position to have been judged on the basis of there being no practical likelihood that the dividend was not paid on.

Article 12 Interest

See treaty text

This Article deviates from the OECD Model Convention. The provisions of Article 8 and Article 9, interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. However, such interest may also be taxed in the Contracting State in which

it arises and according to the laws of that State. But the tax so charged on interest payable in respect of a loan given or debt created after the date of entry into force of this Convention, shall not exceed 10% of the gross amount, if such interest is paid on any loan of whatever kind granted by a bank, and 15% of the gross amount in all other cases.
Notwithstanding what said above, interest arising in a Contracting State and derived by the Government of the other Contracting State, a political sub-division or local authority thereof, the Central Bank of that other Contracting State or any agency of that Government, or by any other resident of that other Contracting State with respect to debt-claims of that resident which are financed, guaranteed or insured by the Government of that other Contracting State, a political subdivision or local authority thereof, the Central Bank of that other Contracting State or any agency of that Government, shall be exempt from tax in the first- mentioned Contracting State..
Interest is defined as debt-claims of every kind that are not classed as dividends by virtue of Article 12, whether or not secured by mortgage and whether or not carrying the right to participate in the debtor's profits. The term includes income from government securities, bonds and debentures and premiums and prizes attaching to these securities as well as other bonds and debentures. It includes all items treated as interest under a State's domestic law. Penalties and charges for late payment are not included.
This Article does not deal with the situation where both the recipient and the payer of the interest are resident in the Contracting States but the purpose of the loan was to fund a permanent establishment owned by the player in a third state, and the interest on the loan is borne by that permanent establishment. Because under this Treaty, the bearing of interest by a permanent establishment rather than the payer only applies where the permanent establishment is one of the two Contracting States, the paying enterprise will be subject to withholding tax under this Treaty in the State where it is resident. This leaves open the possibility that under another treaty, the interest might be treated as arising in the state where the permanent establishment is situated and also subject to withholding tax there under the terms of a treaty between the state where the permanent establishment is situated and the recipient's state, or simply under domestic law.
As is usual under the Model Conventions, there is a provision limiting the treaty benefit to an arm's length amount of interest where there is a special relationship between the payer and the beneficial owner.

Domestic law

Denmark

No withholding tax applies to interest paid to individuals whether resident inside or outside EU/EEA.
No Danish withholding tax will apply on interest paid from a Danish corporate entity to a person or entity which does not qualify as a controlling or group related entity foreign lender (subject to definition, cf. below).
Interest paid from a Danish corporate entity to a controlling or group related entity foreign lender will be subject to Danish withholding tax, unless:
(a) the foreign controlling or group related lender has a permanent establishment in Denmark to which such interest income is attributed (in this case the interest is subject to normal corporate tax in Denmark - also at 25 percent) or
(b) the foreign controlling or group related lender is entitled to claim reduction or elimination of Danish withholding tax under the Interest and Royalty Directive (no tax is levied and no withholding tax applies) and the relationship with the Danish borrower is upheld for an minimum period of 1 year, or
(c) the foreign controlling or group related lender is protected under a tax treaty with Denmark (irrespective of treaty rate) and the relationship with the Danish borrower is upheld for an minimum period of 1 year, or
(d) the foreign controlling or group related lender is controlled (as defined under the Danish tax consolidation rules) by a Danish entity, or
(e) the foreign controlling or group related lender is controlled by a party resident in a State that has concluded a tax treaty with Denmark, and further that such State may tax the related foreign lender (specifically defined) on such interest payments pursuant to CFC taxation rules of that State, or
(f) the foreign controlling or group related lender can demonstrate that it has paid foreign income tax on the interest received at a rate of at least 18.75 percent (2013) and further provided that it has not entered into a back-to-back loan with an entity that has paid foreign income tax on the interest received at a rate of less than 18.75 percent (2013).
In order to qualify for reduction or elimination of withholding tax under a tax treaty or the Interest and Royalties Directive, it is a general requirement that the recipient qualifies as beneficial owner of the

interest. Reference is made to the specific comments made on the Danish interpretation of this term under Article 10, above.
For purposes of the Danish interest withholding tax rules, "control" means direct or indirect legal ownership of more than 50% of the shares or legal control over more than 50% of the voting rights. Ownership or control has not been conferred from a pledgor to a pledgee solely as a result of a pledge over shares.
When determining whether the lender controls the Danish borrower (or vice versa), votes and shares held by group-related entities are considered. Votes and shares held by non-related shareholders may also be considered if an agreement has been made between the lender and the non-related shareholders for the purpose of "exercising a common controlling influence" over the Danish borrower. A shareholders agreement may constitute an agreement to "exercise common controlling influence" over the Danish borrower.
Not only taxable legal entities are considered as entities for purposes of control; also fiscally transparent entities may be considered if they are "are governed by rules of corporate law, a corporate law agreement or Articles of association".
"Group related" means two or more entities which (i) directly or indirectly are controlled by the same group of shareholders or (ii) which are under common management.
The lender and the Danish borrower may be considered to be group related by virtue of common management if they have the same manager or if they have different managers that have entered into an agreement providing for a common management of the lender and the borrower.
Not only taxable legal entities are considered as entities for purposes of group relation; also fiscally transparent entities may be considered if they are "are governed by rules of corporate law, a corporate law agreement or Articles of association".
In practise, no filing claims apply to be exempt from withholding tax if the recipient is not group related with the borrower or if the recipient can claim exemption pursuant to (b) or (c), above. In the cases (d)-(f) a 25 percent tax is to be withheld at source and the recipient will need to reclaim the withholding tax by completing reclaim form 06.026 with the tax authorities enclosed with such documentation which substantiates eligibility for exemption under the relevant exception. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.

India

Interest under section 2(28A) of the Act means interest payable in respect of any moneys borrowed or debt incurred including a deposit, claim or other similar right or obligation and includes any services, fee or other charges in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilized. Under the Act, any interest that is paid on capital borrowed for a business purpose is eligible for deduction under section 36(1)(iii) of the Act.
However, any amount of interest paid, in respect of capital borrowed for acquisition of an asset for extension of existing business or profession for any period beginning from the date on which the capital was borrowed and for acquisition of the asset till the date on which such asset was first put to use, is not allowed as deduction.
The Indian judiciary has laid down the broad principles for the eligibility on interest expense deduction under the Act. In a ruling by the Mumbai Bench of ITAT, the bench refused to apply anti avoidance provision against thin-capitalization (a phenomenon where investments are primarily structured as debt instead of equity capital, in order to get favourable treatment under tax laws of a country) to deny the benefits available to a resident of Belgium under India-Belgium Treaty. It was held that because the Act does not provide for any limitations on the benefits in form of any anti thin-capitalization rules, therefore it was not permissible for the tax department to deny such benefits to the taxpayer. Besix Kier Dabhol, S.A. v. DDIT (2010-TII-158-ITAT-MUM-INTL)
Presently, India does not have thin-capitalization rules. It is proposed that the new DTC (which will replace the existing Act) will be implemented from April 1, 2012. The DTC makes an attempt to introduce the concept of thin-capitalisation by providing a benchmark debt-equity ratio.

Article 13 Royalties and fees for technical services

See treaty text

This Article deviates from the OECD Model Convention because the article not only includes royalties, but also concerns fees for technical services.
Royalties are defined as payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematograph films and films or tapes for television or radio broadcasting, any patent, trademark, design or model, plan, secret

formula or process, or for information concerning industrial, commercial or scientific experience. It also includes payments for the use of, or the right to use industrial, commercial or scientific equipment, i.e. leasing payments.
Fees for technical services are defined as payments of any amount to any person other than payments to an employee of the person making payments, in consideration for the services of a managerial, technical or consultancy nature, including the provision of services of technical or other personnel.
Royalties and fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. However, royalties and fees for technical services may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the recipient is the beneficial owner of the royalties or fees for technical services the tax so charged shall not exceed 20% of the gross amount of the royalties or fees for technical services.
There are the usual provisions such that royalties received by a non resident but which relate to a permanent establishment which that non-resident has in the other Contracting State are taxed under Article 7 and thus escape withholding tax.
Where the payer and beneficial owner are connected and the amount of royalties exceeds an arm's length amount, the excess amount paid will not enjoy the treaty benefits and will be liable to tax in the payer's State at the normal domestic rate of withholding tax.

Domestic law

Denmark

Danish withholding tax applies to payments (i) qualifying as royalties for Danish tax purposes, (ii) which are not exempt under the EU interest/royalty directive or a tax treaty. If applicable, royalties paid from a Danish company to a foreign company is subject to 25% withholding tax. The tax is withheld at source by the Danish company and settled with the tax authorities.
In relation to (i), it is noticeable that the term "royalties" according to Danish law is narrower than the definition applied in both Article 12 of the OECD Model Tax Convention and the Interest and Royalties Directive. Indeed, the Danish royalty definition only includes industrial and commercial royalties (i.e. mainly payments for use or right to use patents, trademarks, patterns or models, drawings, secret formulas or production methods information on industrial, commercial or scientific knowhow) and does not include "artistic" royalties. Artistic royalties are described as payments for using or buying the right to use copyrights to literary work, artistic work or scientific work, e.g. author royalties or royalties for the use of music, films, etc.
In relation to (ii) in order to qualify for reduction or elimination of withholding tax under a tax treaty or the Interest and Royalties Directive, it is a general requirement that the recipient qualifies as beneficial owner of the royalty. Reference is made to the specific comments made on the Danish interpretation of this term under Article 10, above.
In practice, if the payment is a royalty, a 25 percent tax is to be withheld at source and the recipient will need to reclaim the withholding tax by completing reclaim form 06.015 with the tax authorities including a statement from the India tax authorities that the beneficial owner of the payment is resident in India. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.

India

Royalties

Taxation of royalty has been a much debated subject in India. If an Indian company imports concept designs and drawings from a company incorporated in another country, many questions about the taxation of the payment for such designs and drawings would arise. Whether such a payment in the nature of a royalty payment, thereby subjecting it to withholding tax, or is it a payment for an outright purchase of the designs and drawings? The answer to these questions depends on the scope of the term "royalty."
The Act defines "royalty" to mean any consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital Gains") for -
(i) the transfer of all or any rights (including the granting of a license) in respect of a patent, invention, model, design, secret formula, process, trademark or similar property;
(ii) the imparting of any information concerning the working of, or the use of a patent, invention, model, design, secret formula, process, trade mark or similar property;
(iii) the use of a patent, invention, model, design, secret formula, process, trade mark or similar property;

(iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
(v) the use or right to use any industrial, commercial or scientific equipment, not including the amounts referred to in section 44BB;
(vi) the transfer of all or any rights (including the granting of a license) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, not including consideration for the sale, distribution or exhibition of cinematographic films; or
(vii) the rendering of any services in connection with the activities referred to in sub-clauses (i) to (iv), (iva) and (v). (Explanation 2 to Section 9(1)(vi) of the Act)
Income from royalty is taxable in India under the Act. However, when designs are imported by an Indian company from a foreign company, it becomes pertinent to ascertain the definition of royalty given in the Treaty, if any, that India may have with that foreign country. For example, in the India-Denmark Treaty, a royalty payment is a payment of any kind for the use of, or the right to use:
(a) any patent, trademark, design or model, plan, secret formula or process;
(b) industrial, commercial or scientific equipment, or information concerning industrial, commercial or scientific experience;
(c) any copyright of literary, artistic or scientific work including cinematographic films, and films or tapes for radio or television broadcasting. (Article 13(3) of the India-Denmark Treaty)
The Treaty between India and Denmark came up for consideration before the Delhi Bench of the ITAT in DCM Ltd. v. ITO ((1988) 31 TTJ 171 (Del.)) and the ITAT held, after examining the terms of the collaboration agreement, that the royalty payable to the foreign collaborator could be considered as commercial profits and as such would not be taxable in India because the foreign company did not have a PE in India.
The Delhi High Court has issued an important ruling in the case of Asia Satellite Telecommunications Limited (Asia Satellite Telecommunications Co. Ltd. v. DCIT, 85 ITD 478 (Del.)) ("Asia Sat") on the issue of taxability of lease of transponders. The Court ruled that lease rentals paid to foreign satellite service providers does not constitute 'royalty' under the provisions of the Act and accordingly, not taxable under the Act.
The characterization of the payment for lease of transponder space has been a subject matter of extensive debate owing to conflicting judicial decisions at the appellate level. India does not agree with the interpretation in paragraph 9.1 of the OECD commentary on Article 12 according to which a payment for transponder leasing will not constitute royalty. The Indian position is that income from transponder leasing constitutes an equipment royalty.
Under the proposed DTC, the definition of royalties includes payments made for 'the use of or right to use of transmission by satellite, cable, optic fiber or similar technology.' Considering this wide definition, transponder lease payments would be taxable as royalties under the DTC.

Fees for technical services

There has been a lot of controversy over taxation of fees for technical services in India.
In the case of Ishikawajima-Harima Heavy Industries Ltd. v. DIT ((2007) 288 ITR 408) ("Ishikawajima") the Supreme Court had held that under Section 9(1)(vii) of the Act, fees for technical services applies only when services by a non-resident are rendered and utilized in India. This decision appeared inconsistent with the plain reading of the text of the provisions of the Act.
This issue once again came up before the Mumbai Bench of the ITAT, in Ashapura Minechem v. ADIT ((2010) (40 DTR 42) (Tri)). In this case, Ashapura Minechem had entered into an agreement with a Chinese company ? China Aluminum International Engineering Corp Ltd ("CAIEL") whereby it had agreed to pay a fee of $1 million in consideration for bauxite testing services performed by CAIEL. Ashapura Minechem contended that it was not liable to deduct tax at source under section 195 of the Act, because the principal sum of $1 million was not exigible to tax under section 9(1)(vii) of the Act. Ashapura relied principally on the decisions in Ishikawajima and Clifford Chance (Clifford Chance v. DCIT, [2009] 318 ITR 237 (Bom).). Ashapura also argued, in the alternative, that the sum did not qualify for taxation under Art. 12 of the India-China Treaty.
The ITAT rejected the submission that Ishikawajima continues to be good law. It held, that after the retrospective amendment inserted by the 2010 Finance Act, the law in India is that fees for technical services paid to a non-resident are taxable when those services are utilized in India, regardless of where they are rendered. The ITAT held that this is not inconsistent with the principle of "territorial nexus" and observed that, observing that most countries follow a combination of source and residence taxation, and the ensuing conflict is sought to be resolved internationally by a network of bilateral agreements. In the absence of such a treaty, there is nothing to prevent both countries from taxing

the same transaction, and no legal principle is available to a taxpayer to challenge such a levy. The ITAT noted that it is fallacious to proceed on the basis that territorial nexus to a tax jurisdiction being sine qua non to taxability in a jurisdiction is a normal international practice in all systems.. The second contention that Ashapura Minechem raised was as to whether the India-China Treaty treated fees for technical services differently. Art. 12(4) of the India-China Treaty defines "fees for technical services" as "any payment for the provision of services of managerial, technical or consultancy nature by a resident of a Contracting State in the other Contracting State?" Art. 12(6), the deeming provision, provides that "royalties or fees for technical services shall be deemed to arise in a Contracting State when the payer is ? a resident of that Contracting State."
Ashapura Minechem argued that Art. 12(4) is a peculiar provision that applies only when services are both rendered and utilized in India, and based this submission on the expression "provision of services? in the other Contracting State". It contrasted this with other double tax conventions that omit a deeming provision for fees for technical services. The ITAT rejected this submission by noting that such transactions are in any case taxable under Art. 12(6) and noted that Ashapura Minechem's view of Art. 12(4) would render Art. 12(6) meaningless, for every transaction to which it could conceivably apply would be covered by Art. 12(4). This, in sum, appears to have put the controversy over taxation of non-residents for fees for technical services to rest.

Article 14 Capital Gains

See treaty text

The usual rule that gains derived by a resident of a Contracting State from the disposal (alienation) of immovable property as defined in Article 6 and situated in the other Contracting State may be taxed by that State applies under this Treaty. In other words, the Contracting State where the property is situated may tax the capital gain. The term "alienation" is used in connection with events giving rise to capital gains. This will include normal disposals of assets and also events such as exchange of assets, expropriation, gifts and the passing of assets to another on death. Not all States levy tax in all these situations, but the meaning of the term "alienation" is sufficiently wide to give them the right to do so if their domestic law provides for a charge to tax in a particular situation.
As with all treaty provisions, this Article does not impose a requirement upon either State to tax a capital gain; it merely allocates taxing rights so that the relevant State can tax a gain if it chooses. Also applicable is the usual rule that gains on alienation of movable property forming part of the assets of a permanent establishment may be taxed by the Contracting State where the permanent establishment is situated, including gains from the alienation of the permanent establishment, whether or not as part of the alienation of the whole enterprise. Thus, for example, the sale of a wholly owned company resident in State A and owned by a resident of State A could give rise to a tax charge in State B if that company has a permanent establishment in State B. This does not include gains on ships and aircraft operated in international traffic nor to other movable property used in such a trade. All other gains are taxable only in the State where the person making the disposal is tax resident.

Domestic law

Denmark

Under Danish law, only alienation of real estate as well as assets or liabilities attributable to a permanent establishment in Denmark are subject to Danish taxation if the alienator is not a Danish tax resident person.
Shares, receivables and intellectual property rights are generally exempted from Danish capital gains tax under Danish domestic law when not attributable to a permanent establishment in Denmark (as Denmark would normally also be prevented from taxing such income under its tax treaties). However, as a very narrow definition of interest applies under Danish domestic law, a specific provision applies according to which any capital gains on receivables in the form of a difference between the nominal amount of the receivable and the amount actually borrowed which is agreed in advance between the debtor and the borrower will be subject to tax in the hands of a non-Danish creditor, if such payment would also be taxable in Denmark to the creditor if it had been an interest.

India

Under the Act, any profits or gains that arise from the transfer of a capital asset will be chargeable to income tax under the head "Capital Gains." (Section 45 of the Act). Such capital gains will be deemed to be the income of the previous year (1 April to 31 March) in which the transfer of the capital asset takes place.
In this regard, if the shares of an Indian company are held for a period of twelve (12) months or less, then they are regarded as "short term capital assets" and any gains arising from the transfer of such shares will be regarded as "short term capital gains". (Sections 2(42A) and 2(42B) of the Act.)

If the shares are held for more than twelve (12) months, then they are regarded as “long term capital assets" and any gains arising from the transfer of such shares will be regarded as “long term capital gains”. (Sections 2(42A), 2(29A) and 2(29B) of the Act.)
Long term capital gains arising from the transfer of shares of an unlisted company will be chargeable to tax at the rate of 21.115% (including surcharge at the rate of 2.5% and education cess at the rate of 3%).
Short term capital gains arising from the transfer of shares of an unlisted company will be chargeable to tax at the rate of 32.672% (including surcharge at the rate of 2.5% and education cess at the rate of 3%).
If the total income of a taxpayer is less than Rupees 10,000,000, then long term capital gains will be subject to tax at the rate of 20.6% (without additional surcharge). (Sections 112 and 115AD of the Act.)
If the total income of a taxpayer is less than Rupees 10,000,000, then short term capital gains will be subject to tax at the rate of 30.9% (without additional surcharge). (Sections 112 and 115AD of the Act.)
The mode of computing capital gains will typically be as under:
Step 1: Determine the full value of sale consideration;
Step 2: Deduct the indexed cost of acquisition and only if applicable:
(i) Expenditure incurred wholly and exclusively in connection with the transfer,
(ii) Cost of improvement;
Step 3: From the above, deduct exemptions, if any;
Step 4: The resultant amount will be either long term or short term capital gain.
If the Treaty provides for a reduced rate of tax, or a restricted scope of taxation, then the taxpayer's liability will be limited accordingly.
Generally, capital gains from the transfer of assets located in India are deemed to arise in India and are taxable in India. There is a requirement for vendors to withhold tax (20% or 30% depending on whether the gain is short term or long term). This is especially significant because the Indian tax authorities are attempting to “look through” the sale by offshore holding companies whose underlying assets consist of shares in Indian companies.
In the well known Vodafone controversy (Vodafone International Holdings B.V. Vs. Union of India and Anr., 2010(112)BomLR 3792). Vodafone International Holdings B.V (“Vodafone”) an entity based in the Netherlands acquired 100 percent shares of CGP (Holdings) Limited (“CGP”), which is an entity based in Cayman Islands, from Hutchinson Telecommunications International Limited (“HTIL”), i.e., another Cayman Islands based entity. CGP had controlling stake in Hutchison Essar Limited (“HEL”), an Indian entity. HEL was a joint venture between the Hutchinson group and the Essar group. The acquisition resulted in Vodafone acquiring control over CGP and its subsidiaries, including HEL. The Indian tax authorities issued a show cause notice to Vodafone to explain why tax was not withheld on payments made to HTIL in relation to the above transaction.
Vodafone filed a writ petition in the Bombay High Court challenging the jurisdiction of the tax authorities in the matter. In the judgment of the Court, the issue was whether the tax authorities had the jurisdiction under the Act to tax the gains arising from the transfer of shares of a foreign holding company. The Court held that the transaction must be viewed from a commercial perspective, and it was crucial to determine the place or the source from which the profits had been generated. The Court observed that the price paid for the acquisition included controlling rights and other entitlements of the Indian business. Moreover, the divestment of the seller's interests comprised of many components and, therefore, the tax authorities had the jurisdiction to tax the transaction. Further, given the multiplicity of arrangements involved in the transaction, the Court also held that there should be an apportionment of the income between the part which has a nexus with India and the part which does not.
The principle being asserted by India is that if the property being sold is ultimately Indian situs property, then Indian tax on the capital gain arises. As in this case, the seller, HTIL was a Cayman Islands based entity and the Cayman Islands does not have a treaty with India currently. Therefore, the taxability of the capital gains was to be determined as per the provision of the Act.

Article 15 Independent personal services

See treaty text

Article 14 was taken out of the OECD model in its 2000 revision as a separate provision as it was generally deemed not to be different in substance from Article 7. However, this Treaty still has separate Articles governing the taxation of income from permanent establishments (see Articles 5 and 7) and income from professional services. This Article provides that where a resident of one of the

States has a "fixed base" in the other State, income in respect of professional services attributable to that fixed base may be taxed in the country in which it is situated. Thus an Indian accountant with an office in Denmark will be taxable in Denmark on profits attributable to the Danish office. The attribution of profits is dealt with in the same way as for other business profits under the provisions of Article 7. If the resident stays in the other Contracting State is for a period or periods amounting to or exceeding in the aggregate 183 days in the fiscal year of that other State, only so much of the income as is derived from his activities performed in that other State may be taxed in that other State.
The term "professional services" is defined to include especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

Domestic law:

Denmark

Reference is generally made to Article 7, above.

India

The Indian position on independent personal services can be explained by the Bombay High Court decision in Clifford Chance vs. The Deputy Commissioner of Income Tax ([2009] 318ITR237(Bom)). In this case, the assessee, a UK based law firm, had provided legal services in connection with power projects in India which were operated by a joint venture involving certain Indian and foreign companies. The fees receivable by the assessee was determined on a time spent basis i.e. after considering the time spent by each partner / associate of the firm who had worked on the matter and their respective chargeability rates. In the course of providing the professional services, the partners of the assessee firm had an aggregate presence in India in excess of 90 days. Therefore, in view of Article 15 of the India-UK Tax Treaty, the income tax department argued that the services were utilized in India and is consequently deemed to have accrued in India. The Bombay High Court was however, disinclined to accept such an unfettered construction of the taxability of income earned by non-residents. Reiterating the ratio of the Supreme Court of India in Ishikawajima, the High Court asserted that unless there is sufficient nexus between the earning of income and the territory of India, there is no justification for subjecting such income to tax. Since the services, though utilized in India, were not entirely rendered in India, the assessee was held to be taxable only to the extent of the income which is attributable to the legal services provided by the partners while in India. However, after the Finance Bill 2010, the position laid down by Ishikawajima has been superseded by the Explanation to section 9(1) which mentions that for the purposes of this section, income of a non-resident shall be deemed to accrue or arise in India, whether or not the non-resident has rendered services in India.

Article 16 Dependent personal services

See treaty text

This equates to the "Income from Employment" (Article 15) of the OECD Model and follows the OECD provisions. Salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of employment are taxable only in that State unless the employment is exercised in the other State. If so, remuneration derived from the other State is taxable in the other State. However, the other State (the source State) will not tax provided:

- The recipient is present in the other State for no more than 183 days, including normal interruptions of work in aggregate in the income year; and

- The remuneration is paid by, or on behalf of, an employer not resident in the other State; and

- The remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other State.

The purpose of this Article is to ensure symmetry in taxation. If the employer is not taxable in a State, because it is neither resident there nor has a permanent establishment there then it will not receive any tax deduction in that State for wages and salaries paid. Wages and salaries paid by the employer in respect of short term employment postings of employees to that State are correspondingly exempted from tax in that State in the hands of the employees.
There are special provisions for employees in the international transport industry.

Treatment of stock options

The treatment of employee stock options is not expressly dealt with and can be difficult as entitlement to the benefit taxable as a result of the option may have accrued partly whilst the employee was working temporarily in one of the States but there may be no taxable event, such as exercise of the

option until the employee returns to the other State. A State is permitted to tax that part of the taxable benefit that can be related to the portion of the entitlement period spent working in that State.
Determining the extent to which an employee stock option benefit is derived from employment exercised in a particular State has to be done on a case by case basis, taking into account all relevant facts and circumstances. Whether a period of employment would be considered in allocating taxing rights between two States would depend on whether the entitlement to exercise the stock option was contingent upon continuing employment during that period. If an option was granted with a right to exercise, say, in three years' time, regardless of continuing employment then time elapsing between grant and exercise would not count towards an apportionment of the taxing rights over the benefit in the absence of any other factors.
Periods of employment before the option was granted may be considered in the apportionment of taxing rights if the grant of the option was contingent upon a minimum period of employment or attainment of performance objectives.
Once the option is exercised, any further benefit to the employee, normally in the form of a capital gain on a disposal of the shares at a profit, will be dealt with under Article 13 and so probably only taxable in the State where he is resident.
If the shares do not vest irrevocably on exercise of the option (e.g. because they are liable to forfeiture upon certain conditions) then the increase in value of the shares until they do vest irrevocably will also be dealt with as employment income and subject to the same considerations as the benefit arising between grant and exercise.
The method of apportioning stock option benefits recommended by the OECD is by reference to the proportion of the number of days during which the employment was exercised in one State to the total number of days of employment from which the entitlement to the stock option benefits were derived. Thus if an employee was required to work for an employer for 520 days in total during a particular time period to qualify for the benefits of the stock option and was sent to work in the other State for 260 days out of that period, then half of the stock option benefits would be taxable in each State.

Domestic law

Denmark

Under Danish domestic rules, Denmark can tax non-resident employees on income from employment when work is carried out in Denmark. The Danish domestic rules apply to all forms of payment and irrespective of when payment is made. The provision specifically includes severance payments and payment during a termination period when such payments attributable to employment in Denmark. Further, the Danish domestic law provides for a 30 percent tax on hiring out of labour when work is carried out in Denmark.
In a ruling from 2006 by the Danish Tax Council (Skatterådet) the Danish tax authorities confirms that it considers stock options granted as remuneration for employment was comprised by Article 15 of this Treaty.
When taxable in Denmark, a person will generally be taxable pursuant to the same rules as a Danish tax resident employee. When only working in Denmark for part of the income year (normally the calendar year for individuals), specific calculation rules apply to ensure that the progressive Danish tax system applies to the income from Denmark. In very general terms, the marginal tax rate, including labour market contributions (AM-bidrag) of 8 percent, applicable to personal income (such as salaries, etc.), is approx. 56 percent. This rate applies to annual income in excess of DKK 421,000 (about. EUR 56,440) per income year. Salary income lower than this amount is taxable between 0-44 percent. Specific rules on aggregate taxation of income apply to married couples.
Denmark offers a special tax regime to highly paid inbound expatriates and researchers recruited from abroad (subject to criteria). Employees may elect to be taxed at a rate of 26 % in up to 60 months. All other income, including benefits-in-kind other than company car and free telephone, are taxed at the ordinary rates. Such income includes any private income received by the expatriate from outside Denmark.
In addition to the 26 % tax, AM-contribution of 8 % must be paid.
Outbound expatriates are generally not taxed by Denmark on the salary, when the expatriation extends to more than six months.

India

Article 16 i.e. income from dependent personal services gets activated only when there is an employer-employee relationship under which the individual provides services and the employer pays him remuneration in a country other than the one where the individual is tax resident. The scope of “salaries, wages and any other similar remuneration” is very wide and will be construed as per the

Act. As a result, it brings within its sweep all forms of remuneration connected with the employment irrespective of whether such remuneration is received in cash or in kind and includes perquisites such as stock options, club memberships, accommodation, etc as well.
Once the income earned qualifies as "remuneration" under the Treaty, its taxability will depend whether such income fulfils the physical presence test or under the principles of presumptive taxation. Under the physical presence test, the period of employment in the other country and the extent of remuneration attributable to such employment as carried on in the other country determines the taxability. Currently, a physical presence exceeding one hundred and eighty three (183) days during any twelve (12) month period beginning or ending in a fiscal year is enough to allow the other country to tax the income from such employment. Presumptive taxation can happen once there is a PE in the other country. Once there is a PE and the remuneration has been borne the PE then such remuneration is taxable irrespective of the duration of actual physical presence in the other country. This is based on economic principles as the remuneration borne by the PE is allowed as a deduction from the taxable income of the PE and therefore taxed separately.
Presumptive taxation is a system whereby the income of the PE is computed on the basis of a certain presumptions wherein a deduction is permitted on an implied basis for all expenses which can be reasonably presumed to be expended in course of earning of the income by the PE. The AAR has held that remuneration is said to be "borne" by the PE when the financial obligation of paying such remuneration lies with the PE. (Stanley Keith Kinnett v. CIT (238 ITR 155))
The Delhi ITAT, in Ensco Maritime Ltd. vs. DCIT (91 ITD 459) has acknowledged this view of presumptive taxation of PEs under section 44BB of the Act. However, the ITAT allowed the remuneration paid to employees as a deduction from the taxable income of a company that had a PE in India by virtue of offshore drillings that it operated.
However, the Delhi ITAT, in the subsequent decision in Pride Foramer S.A. v. ACIT (15 SOT 562) observed that merely finalizing an assessment under Section 44BB of the Act is not conclusive evidence that remuneration paid had actually been deducted while computing the income of the PE. It further opined that the words 'deducted' and 'deductible' are not inter changeable and cannot be, ipso facto, interpreted as deemed to be deducted or borne by the PE.
Notwithstanding the above, India reserves the right to tax incomes earned by Indian residents abroad. In this regard, in British Gas India Pvt. Ltd. (287 ITR 462), the AAR has held that once the requirements of Article 16 are fulfilled, it is irrelevant where the remuneration paid to the employee is actually received. In this case, two employees were sent on a long-term assignment to the work for the UK company whilst continuing to be on the rolls of the Indian company and received salaries in India which were reimbursed by the UK company. As the employees paid tax in the UK on the salaries earned, the receipt of salaries in India was held to be inconsequential as the employees had become residents of the UK under the India ? UK Treaty.
However, in a subsequent ruling by the AAR in S. Mohan (294 ITR 177) short term deputations were held to not confer residential status and consequently such remuneration was held to be exigible to tax in India. Therefore, for Indian residents rendering services in Denmark under a contract of employment, evidence of payment of tax in Denmark and the duration of employment will determine taxability of such remuneration in India.
Section 10(6)(vi) of the Act also confers a short-stay exemption on non-Indian employees of foreign companies rendering services in India if their stay is less than ninety (90) days.
There are special provisions for dealing with the remuneration earned by employees of airlines and shipping companies and the key point in this regard being that these special conditions are attracted only if the employment is actually aboard a ship or an aircraft and not if they work on the ground.

Article 17 Directors' fees

See treaty text

These fees may be taxable in the country in which the company is resident as well as that in which the director is resident.
This treatment extends not only to directors' fees but also to similar payments deriving from duties as an administrator, manager, liquidator or other duties which are considered analogous by the paying State.

Domestic Law:

Denmark

Under Danish domestic rules, Denmark can tax fees paid for membership a board of directors, a commission, a committee, a council or similar when payment is made from a Danish company or entity.
The payment is taxable as personal income, cf. in further detail Article 15, above.

India
Under Indian Law, director's fees is taxable as his personal income, based on rules of residency as under Section 6 of the Act (Refer to description under Article 4 above).

Article 18 Artists and Athletes

See treaty text

Income derived by a resident of one State as an entertainer, such as a theatre, motion picture, radio or television artist, or a musician, or as an athlete, from their personal activities as such exercised in the other State may be taxed in the other State. This also applies where the income accrues not to the entertainer or athlete himself, but to another person, e.g. a management company or a troupe, team or orchestra forming a legal entity or to an artist company. Notwithstanding, income derived by an entertainer or an athlete who is a resident of a Contracting State from his personal activities as such exercised in the other Contracting State, shall be taxable only in the first-mentioned Contracting State, if the activities in the other Contracting State are supported wholly or substantially from the public funds of the first-mentioned Contracting State, including any of its political subdivisions or local authorities. The last part, starting from "notwithstanding" is different from the OECD-model.
If the performance in question is supported to a significant extent out of public funds or if it is carried out within the framework of a programme of cultural exchange between the two States, then the income will be taxable only where the performer is resident.Notwithstanding, where income in respect of personal activities exercised by an entertainer or an athlete in his capacity as such in a Contracting State accrues not to the entertainer or athlete himself but to another person, that income shall be taxable only in the other Contracting State, if that other person is supported wholly or substantially from the public funds of that other State, including any of its political subdivisions or local authorities. The last part, starting from "notwithstanding" is different from the OECD-model.

Domestic Law:

Denmark
Denmark has - in practice - limited access to tax such income as Danish domestic tax law does not have specific provisions on this type of income and therefore only allows taxation when the nature of the payment is payment from employment in Denmark, cf. also Article 15, above.

India
The Act does not lay out any specific provisions for taxation of non resident artistes. Accordingly, a non resident artiste will be subject to tax based on the provisions outlined in Section 5 read with Section 9 of the Act. Further, the remuneration received by a non resident artiste who is taxable under the Act will be subject to withholding taxes under Section 195 of the Act.
However, there are specific provisions in the Act regarding the taxability of non resident sportsmen or sports association. Section 115BBA of the Act provides that a sportsman who is a non resident and not an Indian citizen will be taxable at the rate of 10% on the gross income received or receivable for the following
(a) participation in India in any games or sport,
(b) Advertisement and
(c) contribution of any article in a newspaper, magazine or journal relating to any game or sport in India.
There are certain provisions such as section 194E and 195 in the Act which relate to withholding taxes on payments made to non resident sportsman or sports association under the Act.

Article 19 Pensions and Government Payments

See treaty text

The main rule in article 19 is that any pension (other than a pension, paid by a Contracting State or a political subdivision or a local authority) or annuity paid to a resident of a Contracting State shall be taxable only in that State.
Pensions and other allowances, periodic or non-periodic, paid under the social security legislation of a Contracting State or under a public scheme organised by a Contracting State in order to supplement the benefits of that legislation shall be taxable only in that State.

Domestic Law:

Denmark
Under Danish domestic law, Denmark is entitled to tax payments from Danish pension schemes to non-resident persons. The Danish pension tax system is relatively complex and a detailed description thereof is not made herein. Generally, tax deductibility for pension contributions is allowed irrespective of whether the pension scheme is established in Denmark or elsewhere in the EU when certain criteria are met. The deductible annual amount depends on the type of pension scheme. During the life of the

pension scheme, an annual mark-to-market pension yield tax of 15 percent applies. When the pension is ultimately paid to the pensioner (or beneficiaries) such payments are taxable as personal income (cf. Article 14, above). However, payments from a capital pension scheme are taxable at a flat rate of 40 percent.
In 1998, the Danish ministry of taxation issued a statement regarding the application of the Danish tax treaties to payments under the Danish social legislation, which contains guidance on how to apply the Danish tax treaty to various types of payments under the Danish social legislation.
India
The place of taxability of pension assumes significance for a retired person who is a resident of one contracting state and receives pension from the other contracting state. The same can be said for Government employees, members of Diplomatic Missions and Consular Posts who are in active employment and are posted abroad. Generally, it is the State of residence of the recipient of such pension which has the primary right to tax such income. Thus, in case of an Indian resident, under Indian tax law, pensions will be taxable under the head income from salaries. The residential status of the pension recipient will determine whether income from pension will be taxed in India or in the other contracting State. Please incorporate by reference to our discussions under Article 4 relating to residence.

Article 20 Students

See treaty text

Payments which a student, or business apprentice who is, or was immediately before visiting a Contracting State, a resident of the other Contracting State and who is present in the visited State solely for the purpose of his education or training, receives for the purpose of his maintenance, education or training shall not be taxed in the visited State, provided the payments arise from sources outside that State.
Remuneration from employment in that other State not exceeding DKK 20,000 or its equivalent in Indian currency during any fiscal year of that other State provided that such employment is directly related to his studies or is necessary for the purpose of his maintenance shall also be exempt from tax in that other State.
The student allowance, which is the amount deemed by the tax authorities to be necessary for the maintenance and education of the foreign student, is fixed at DKK 42,000 in 2013.

Article 21 Other Income

See treaty text

Any income not dealt with in the preceding Articles is taxable only in the State of residence, provided that the income is subject to tax in that state (subject-to-tax-test). There is an express provision that income in respect of rights or property which is connected to a permanent establishment is taxed under Article 7 as the income of that permanent establishment or Article 14 (fixed base for independent personal services).
Notwithstanding what said above, items of income of a resident of a Contracting State not dealt with in the foregoing Articles of this Convention, and arising in the other Contracting State may be taxed in that other State.
Domestic Law:
Denmark
The provision is deemed to have only very little practical impact. Taxation hereunder requires - similar as the other provisions of the Treaty - that Danish domestic law contains a right to tax income hereunder. This would only exceptionally be the case.
India
At the outset, it should be noted that “Other Income” as per Article 21 is not the same as “Income from other sources" as per Section 56 of the Act. Certain types of income such as dividend and interest, although taxed as ‘income from other sources’ under the Act, will be governed by a separate Article under the tax treaty and not by the ‘other income’ Article. A few types of income which will typically be included under this Article are Winnings from lottery; Prize money; Gambling income; Punitive damages; Non compete payments; Guarantee fees by a group company, - if giving guarantee is not its regular business; Income from non traditional financial instruments; Social security payments; Interest rate swaps; Payments to students or ex employees who are not covered by the respective Articles.
In the case of DLJMB Mauritius Investment Company v. Director of Income Tax (228 ITR 268) (“DLJ”), the applicant was a limited liability company based in Mauritius which conducted its business through various subsidiaries. DLJ had a number of subsidiary companies which invested a certain portion of

their committed capital on a side by side basis with DLJ in DLJ's Merchant Banking Investments. The applicant expected that with all these funds pouring into it from various affiliated entities, it would be able to make investments in Indian shares, debentures and other debt instruments to the tune of 100 million U.S. dollars. Since the applicant was a resident of Mauritius and there is a Treaty in force between India and Mauritiu and the applicant expected to be entitled to benefits under Articles 10, 11, 13 and 22 of the said Treaty. One of the issues before the AAR was whether any other income earned by the applicant, not being in the nature of dividends, interest or capital gains and not any other head under the treaty, will be taxed in Mauritius only and not in India. The AAR answered the question in positive and held that if the income is not included in the above articles, then it will not be taxable in India.

Article 22 Capital

See treaty text

Wealth taxes may be imposed on:

- Immovable property according to the State where the property is located; and

- Movable property used by a permanent establishment may be subject to wealth tax in the State where the permanent establishment is located.

Ships and aircraft operated in international traffic and by boats engaged in inland waterways transport, and by movable property pertaining to the operation of such ships, aircraft and boats, shall be taxable only in the Contracting State in which the enterprise is a resident.

Domestic Law:

Denmark

Denmark does not levy general wealth taxes. However, a partial wealth tax applies in the form of property value tax which is levied at the value of real estate which is the domicile of the owner and/or his family or the summer residence of the owner and/or his family. The tax rates are 1 per cent up to a value of DKK 3,040,000 (2011) and 3 per cent of values in excess thereof. The value is generally determined as the so called publicly assessed value, but certain modifications may apply. For Danish tax resident individuals the domestic tax rules apply both to real estate situated in Denmark and abroad. For non-resident individuals, the tax applies to real estate situated in Denmark (in practise primarily Danish summer houses or apartments).

India

Indian wealth tax is payable at a rate of 1% if the taxable value of net wealth exceeds Rupees 1.5 million. Assets that are subject to tax generally include residential houses, cars, yachts, boats, aircrafts, urban land, jewellery, bullion, precious metals, cash in excess of a prescribed limit, any amount not recorded in the books of account and commercial property not used as business, office or factory premises.

However, a residential house and houses owned by an employer and provided to employees earning less than a prescribed limit are exempt from tax. A deduction is also allowed for debts owned that are incurred in relation to taxable assets. The tax is levied on net wealth as of March 31 preceding the year of assessment.

Article 23 Methods for the Elimination of Double Taxation

See treaty text

India

India will use the exemption method apart from dividend income. The method is exemption with progression so that the amount of exempt income will be taken into accounting determining the tax rates to be applied to income remaining in charge to tax in the State of residence. However, for dividend and interest income the credit method will be used. No credit is given for corporation tax underlying a dividend.

Denmark

Denmark generally applies the tax credit method under its domestic rules, unless another method follows from a tax treaty or is specifically provided for under domestic law. However, the exemption method applies on income included by Article 18 (new rule). Matching credit is given: at the rate of 10% in the case of dividends, to which the provisions of paragraph 2 of Article 10 apply; and at the rate of 10% in the case of interest to which the provisions of paragraph 2 of Article 11 apply; and at the rate of 20% in the case of royalties to which the provisions of paragraph 2 of Article 12 apply. The credit is the lesser of either (a) the foreign tax actually paid on the income, and (b) the proportionate amount of the overall Danish tax payable which can be allocated to the foreign income. However, according to the Danish Tax Assessment Act (ligningsloven), a net income calculation

principle applies in internal Danish law when determining the amount of tax credit available. Under this principle any expenses directly relating to foreign source income initially eligible for a tax credit ("related expenses") should be deducted from such income when computing the Danish tax credit. Further, when calculating the Danish tax credit any expenses which are not immediately allocable either to the taxpayer's foreign source income or Danish source income (unallocated expenses) should be allocated proportionally (pro rata) to the foreign and Danish source income (i.e. in proportion to the foreign and Danish gross income). To which extent an expense is a related expense or a general expense must be determined on a case by case basis.

As regards participants in partnerships, Denmark allows Danish partners therein a tax credit, also for tax levied on the partnership as such when the partnership is considered tax transparent in Denmark.

An exemption method applies pursuant to sec. 33A of the Danish Tax Assessment Act to income from employment abroad when the employment exceeds 6 months and the employee only has limited stays in Denmark during the foreign employment period as further specified therein.

Further, Sec. 8 of the Danish Corporate Income Tax Act lies down a territorial principle for certain corporate activities as it states that if a Danish enterprise has a permanent establishment abroad Denmark will exempt income allocable to such permanent establishment abroad, unless (i) the state in which the Permanent Establishment is located waive its right of taxation under a tax treaty with Denmark or other international agreement, (ii) income in the Permanent Establishment would have been taxable under Danish CFC tax rules if the Permanent Establishment had been a company, or (iii) the income in the Permanent Establishment is income from the operation of ships or aircraft in international traffic.

Domestic law

Denmark

Denmark's participation exemption can reduce tax payable where a resident company or permanent establishment of a foreign company receives dividends, currency gains and capital gains on shares. These are exempt from Danish taxation if they arise from a minimum shareholding of 10% in a directly owner subsidiary located within another EU Member State or a state with which Denmark has a tax treaty, provided the tax treaty between Denmark and that state provides for a reduction in the rate of withholding tax. Thus dividends received by a Danish company from an India subsidiary in which there was a minimum shareholding of 10% would be exempt from Danish taxation, although if not covered by the Parent-Subsidiary Directive, they may have suffered India withholding tax.

India

In India, section 91 of the Act provides that while working out the tax on a doubly taxed income, the assesee shall be entitled to the deduction from the Indian income tax payable by him at the Indian rate of tax or the rate of tax of the other country, whichever is the lower, or at the Indian rate of tax if both the rates are equal. Similar tax treatment is done to assessee's share in the income of a registered firm assessed as resident in India in any previous year and such share includes any income accruing or arising outside India during that previous year (which is not deemed to accrue or arise in India).

In the case of CIT v. Bombay Burmah Trading Corpn. Ltd ((2003) 259 ITR 423 Bom), the assessee had its business in India, Tanzania and Thailand. During the relevant year the assessee suffered loss from Thailand branch and earned income from Tanzania.

For computing relief under section 91(1), the assessee claimed that the relief should be allowed in respect of the income from Tanzania without adjusting the loss from Thailand branch. The Assessing Officer allowed the relief only on the net income after adjusting the loss.

The Tribunal allowed the assessee's claim. The Bombay High Court held that under section 91(1), the expression 'such doubly taxed income' indicates that the phrase has reference to the tax which the foreign income bears when it is again subjected to tax by its inclusion in the computation of income under the Act.

Further section 91(1) of the Act shows that the relief under section 91(1) is by way of reduction of tax by deducting the tax paid abroad on such doubly taxed income from tax payable in India. If incomes from foreign countries were to be aggregated, it would be impossible to compare the rate of tax of the foreign country with the rate under the Act. The relief can be worked out only if it is implemented country wise.

In DCIT v. Tata Unisys Ltd. (2002 82 ITD 695 Mum) the assessee earned certain income outside India. The assessee company was resident in India and its foreign income was liable to assessment in India as well. Such foreign income was included in the gross total income of the assessee. However, before computation of total income, the assessee was given deduction at the rate of 50 per cent on the foreign income in accordance with the provisions of section 80-O of the Act. As the same income had

also been subjected to tax outside India, the assessee claimed double taxation relief in respect of the entire taxes paid overseas. The Assessing Officer held that the relief under section 91 claimed by the assessee was required to be restricted to 50 per cent because by virtue of provisions of section 80-O of the Act only 50 per cent of such income was subjected to tax in India. On assessee's appeal, the Commissioner (Appeals) directed that the assessee may be allowed full double taxation relief as claimed. However, the High court reversed the impugned order and restored the order of the Assessing Officer.

Article 24 Non-discrimination

See treaty text

Nationals of one of the States shall not be subjected in the other State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of the other State in the same circumstances are or may be subjected.

Each State will grant to nationals of the other the same exemptions and personal allowances as it grants to its own nationals. The non-discrimination principle applies to all taxes, not just those covered by this Treaty.

Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned Contracting State to any taxation, or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of that first-mentioned State are or may be subjected.

Domestic Law:

Most double tax conventions between India and various foreign countries contain an express article for non-discrimination to secure ensure that the non-resident and/or the resident would not be subjected to a greater burden of tax or placed at a more onerous situation than what would have been if the income is taxed in the respective foreign country in accordance with the tax laws in force in that country at the relevant time.

The non-discrimination clause would generally come to the aid of a non-resident as well as the Indian counterpart in the matter of determining the tax liability in India, on the one hand and discharge of such tax liability in India, wherever attracted, in such a manner as not to be subjected to more onerous burden in financial and non-financial terms.

An illustration of how the non-discrimination clause should be given effect to in matters of taxation of non-residents in India is provided by the decision in Standard Chartered Bank v. IAC ((1991) 39 ITD 57) wherein the Tribunal in Mumbai Bench of the ITAT has explained the non-discrimination clause and granted relief to the non-resident to avoid any discrimination by virtue of being taxed in India, in comparison to the burden of tax which may be imposed in the foreign country under the law prevailing in that country. Although this decision was rendered in the context of the non-discrimination clause in Article 23 of Treaty between India and U.K., the principles laid down would govern equally the interpretation and application of other similar clauses in other double tax conventions to secure non-discrimination. Readers should therefore, refer to and be guided by this decision in matters of non-discrimination.

Article 25 Mutual agreement

See treaty text

The usual provision found in the OECD Model is used.

Where a person considers that the actions of one or both of the States will lead to taxation in conflict with the provisions of this Treaty, the person may present his case to the competent authority of the State of which the person is resident. This is so irrespective of the remedies provided by domestic law. The time limit for presenting the case is restricted to the usual three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Treaty.

The tax authorities of the two States will try to resolve the case by mutual agreement. They will also try to agree on definitions of terms not specifically defined in the treaty and on general matters of interpretation of the Treaty.

Thus, this Article removes the need for the tax authorities in each State to go through diplomatic channels, they may simply contact each other directly. The mutual agreement procedure is commonly used to decide matters concerning income and expense allocations and transfer pricing.

Domestic law

Denmark

The competent authority in Denmark on matters of tax treaties is SKAT (Legal Center), which is resident on Østbanegade 123, DK-2100 Copenhagen. On issues on relation to transfer pricing and the EU Arbitration Convention, the competent authority is SKAT (Store selskaber), which is resident on the same address.

India

Mutual Agreement Procedure ("MAP") is a dispute resolution mechanism provided for under the Treaty which is outside the purview of the domestic tax law. MAP can be invoked by resident of a contracting state if tax is charged in another State, not in accordance with the Treaty. The time period allowed for presenting the case under this Treaty is three (3) years. By initiating action under the MAP provisions, the taxpayer typically does not forego the existing legal remedies viz. appeal, revision etc. available as per the domestic law of India. The taxpayer can opt for MAP while simultaneously applying for relief within the domestic law. This is so especially if the competent authorities are unable to resolve the issue or where the agreement reached by them is not to the satisfaction of the taxpayer. Thus, it can be said that under MAP, the taxpayer has an "additional remedy" available to ensure that his grievance is duly addressed. In the Vodafone case (currently pending before Supreme Court), the Netherlands asked the Indian government in November 2010 to consider using an MAP to finally reach a resolution. However, India did not accede to this proposal.

Article 26 Exchange of information

See treaty text

This Article is almost identical to Article 26 of the OECD Model Convention.

The scope of this Article is limited in that it only provides for exchange of such information as is "foreseeably for carrying out the provisions of this Convention and of the domestic laws of the States concerning taxes covered by the Convention insofar as the taxation thereunder is in accordance with the Convention." Exchange of information is not limited only to residents of the two States.

The article includes the usual provisos relieving the States from any obligation to:

- Carry out administrative measures at variance with the laws or administrative practices of either State;

- Supply information which is not obtainable under the laws or in the normal course of the administration of either State; and

- Supply information which would disclose any trade, business, industrial commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

Domestic Law:

Under section 90(1) (c) of Act, the Indian government may enter into an agreement (e.g. double tax conventions and Tax Information Exchange Agreement (TIEA)) with the government of any country outside India for exchange of information for the prevention of evasion or avoidance of income tax. The purpose of TIEAs is to promote international co-operation in tax matters through exchange of information. double tax conventions also sometimes help in collection of taxes from assets located abroad. Twenty-seven (27) out of eighty (80) double tax conventions contain such a provision for assistance in collection of taxes. In last two years, India has negotiated sixteen (16) TIEAs, eighteen (18) new double tax conventions and has also renegotiated twenty-one (21) existing double tax conventions. Recently, a TIEA with the Bahamas has been signed and has also entered into force.

Article 27 Assistance in collection

See treaty text

This Article does not exist in the OECD Model Tax Convention. It contains quite wide ranging mutual assistance in the collection of each other's taxes.

Article 28 Diplomatic Agents and Consular Officials

See treaty text

This Article follows Article 28 of the OECD Model Convention. Nothing in this Convention shall affect the fiscal privileges of diplomatic or consular officials under the general rules of international law or under the provisions of special agreements.

Article 29 Territorial expansion

See treaty text

The article provides that this Treaty may be extended either in its entirety or with any necessary modifications to any part of the territory of Denmark which is not included in the scope of the Treaty

and which imposes taxes substantially similar in character to those to which the Treaty applies. Any such extension shall take effect from such date and subject to such modifications and conditions - including conditions as to termination - as may be specified and agreed between the Contracting States in notes to be exchanged through diplomatic channels or in any other manner in accordance with their constitutional procedure.

Domestic law:

For Denmark, this would only be relevant if it were decided to include Greenland and/or the Faroe Islands hereunder.

Article 30 Entry into Force

See treaty text

The Treaty entered into force as per the income year 1990.

Article 31 Termination

See treaty text

This provision relates to the termination of this treaty. The Treaty can be terminated with a notice of 6 months before the end of a income year. In case of such termination, the Treaty will cease to have effect from the following income year.