Issue 5

India Tax Insights

August 2015

Tax and Technology

The changing paradigm for tax payers and Government

Prakash Kumar
Speaks on the 'IT Strategy for GST': its importance and effectiveness

S.Mahalingam
Highlights TARC's recommendation for extensive use of Information and Communication Technology

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Welcome

Sudhir Kapadia

Sudhir Kapadia
National Tax Leader
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This issue marks the fifth edition of our magazine – *India Tax Insights*. It includes insightful articles, interviews and reports that will provide business leaders with the most relevant information to take informed decisions.

Using technology to detect potential tax leakages, calculating the tax provision at the push of a button, or using data analytics to find real-time opportunities for commercially driven tax planning are on the wish list of most tax leaders. Yet, finding a way to effectively access multiple general ledgers, manage the endless spreadsheets that make up the tax provision, and stay on top of endless email-based communication around the identification, status and management of uncertain tax positions (not to mention the status of disputes and litigation), often keeps the lights on until late in the tax department.

In EY's 2014 Tax Risk and Controversy Survey, 56% of the respondents agreed or strongly agreed that a lack of effective technology is a contributor of tax risk within their company. This figure increased to 69% for companies responding from Asia-Pacific. This issue of India Tax Insights focuses on the changing paradigm for taxpayers and governments as a result of technology.

Now more than ever, tax professionals globally are faced with an increasingly complex environment. The need for faster, accurate and increased reporting is putting pressure on the tax departments of global corporations. Difficulties arise in rationing time between compliance and planning. Patrick Trapp, EY's EMEIA Director in Tax Performance and Advisory, and Ajay Kumar from EY India share their views on how technology solutions are playing a crucial role in easing the challenges, improving timeliness and accuracy, and enabling more incisive analytics options.

Failure to address the difficulties many companies face with transfer pricing can lead to significant business risks, such as financial reporting issues, increased tax liabilities, and higher costs of intercompany accounting and tax compliance. To meet these challenges, many companies are adopting a holistic approach to executing transfer pricing. Companies are exploring new ways to improve transfer pricing processes and leverage technology to drive efficiencies and reduce risk. Sveinung Baumann-Larsen, Partner at EY's EMEIA Tax Center, explains how operationalizing transfer pricing can lead to intercompany effectiveness.

In an insightful article, Mr. S. Mahalingam, former CFO and Executive Director at Tata Consultancy Services Ltd., highlights the Tax Administration Reform Commission's recommendation for the extensive use of Information and Communication Technology in the tax system in India.

Mr. Prakash Kumar, CEO of GST Network, a company set up primarily to provide IT infrastructure and services for the GST implementation, shares his thoughts on how technology can be a deterrent for tax evaders in a GST regime.

We also showcase some of EY's tax technology tools such as the GST Navigator, the Quantitative Services tool and the Litigation Management Services tool.

In addition, our regular features – *GlobalNews* and *EconoMeter* – present a snapshot of key global tax developments and economic indicators, respectively.

We hope you find this publication timely and useful, and look forward to your feedback and suggestions.

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In this issue

S.Mahalingam

Prakash Kumar

Rahul Patni

Patrick Trapp

Anthony Davis

Sveinung Baumann-Larsen

Tax and technology

The changing paradigm for tax payers and Government

S.Mahalingam

Former Chief Financial Officer
& Executive Director
Tata Consultancy Services

Tax Administration Reform Commission (TARC), under the chairmanship of Dr. Parthasarathi Shome, has recommended extensive use of Information and Communication Technology (ICT) in the administration and governance of tax system in India. The Commission has emphasized that ICT is a critical enabler for moving to a modern tax administration. The report has highlighted areas where Information Technology can play its part in better interaction with tax payers, in getting improved levels of compliance by tax payers and in its use in revenue forecasting.

TARC has recommended transitioning from two Boards - CBDT and CBEC - to a combined entity called Central Board of Direct and Indirect Taxes over a five-year period… when the structure itself is changed at the top, it will pave way for improved integration below, enabling the efficient functioning of large business service

Central Board of Direct Taxes (CBDT) and Central Board of Excise and Customs (CBEC) have been early adopters of ICT, even among Government Departments. The systems implemented so far have helped tax payers in filing their Income tax (IT) returns and documents for Customs Clearance, TDS information and in payment of taxes and duties. Departments have used the systems as a risk management tool to pick up returns (in the case of IT) and consignments (in the case of Customs) for scrutiny. These systems have been of great assistance to tax payers, as they could file all returns electronically. Recognizing the value of data available in electronic form, both CBDT and CBEC have initiated Data Warehousing and Business Intelligence projects, which would help them to detect patterns and in plugging leakages.

The current systems have been developed as standalone systems, with very limited integration. Efficient organizations run on the basis of extensive digitization of processes leading to streamlined operations, and in having effective checks and controls to improve the quality of data. Beyond streamlining of operations, computerization by data analytics, leading to improved compliance and rigoros forecasting. Technology is rapidly advancing. Concepts such as "Internet of Things" can be effectively utilized by the Customs for real life tracking of movement of goods across the supply chain and facilitate improved clearance at ports. Through systems enhancement, rapid introduction of emerging technology and through better project management techniques, the report of TARC has recommended embedding ICT at the strategic core for harnessing its transformative potential.

There is very little scope for data and information exchange in the current organization structure, where Direct Tax and Indirect Tax departments operate as independent entities. This has resulted in limited utilization of computerization benefits by the departments. The power of integrated system was demonstrated by the GST pilot developed by CBEC. In this pilot, data from the CBEC and CBDT systems were combined with data from Maharashtra VAT System. The Commissioner of Commercial Taxes, Maharashtra reported that he was able to recover INR5 Billion of VAT from traders who had evaded it. Data Exchange across functions and departments will require development of common framework for exchange and common standards and taxonomy. Data exchange will not be restricted to the two departments. There should be capability to access data from different ministries as well as from external sources. The TARC report has gone into details regarding security, privacy, audit and accountability. TARC has recommended transitioning from two Boards – CBDT and CBEC– to a combined entity called Central Board of Direct and Indirect Taxes over a five-year period. Currently, Large Taxpayer Units (LTU) have not exhibited any signs of working in an integrated fashion by the two departments. When the structure itself is changed at the top, it will pave way for improved integration below, enabling the efficient functioning of large business service (LBS). Data and Information Exchange will play a major part in making the new structure work efficiently. TARC report has also recommended the creation of Knowledge, Analysis and Intelligence Centre to provide advanced analytical capabilities so that the data of availability is effectively leveraged. Structure has to facilitate effective ICT usage.

Tax payer segmentation is a critical necessity to ensure that the resources of the tax department are optimally used. The segmentation will lead to four categories – Compliant, Triers, Fence Sitters and Offenders. Systems have to be used to educate tax payers and this will pave the way for Triers and Fence Sitters to move toward the Compliant category, leaving the tax department to deal effectively with Offenders. Predictive Analysis, at the

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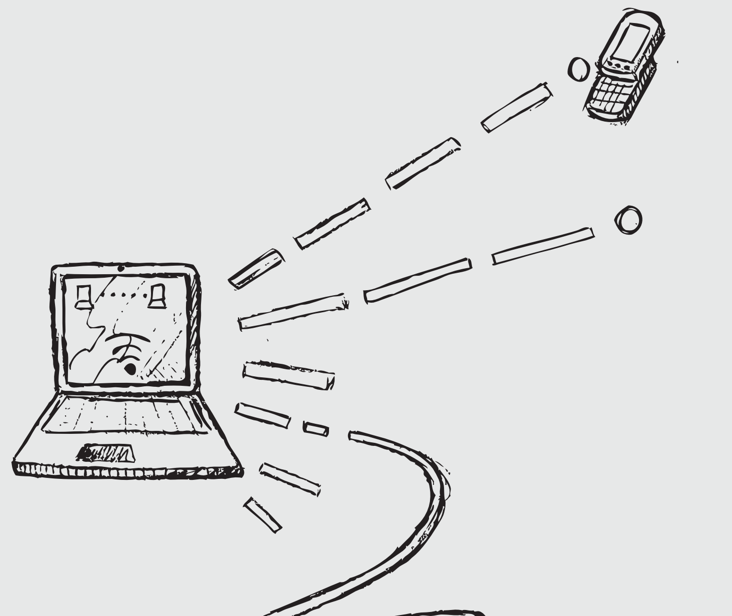

> *The power of integrated system was demonstrated by the GST pilot developed by CBEC. In this pilot, data from the CBEC and CBDT systems were combined with data from Maharashtra VAT System. The Commissioner of Commercial Taxes, Maharashtra reported that he was able to recover INR 5 Billion of VAT from traders who had evaded it.*

time of framing tax laws, by using data mining and other analytical tools, will go a long way in recognizing risks earlier and putting in place an improved tax environment. The report has described approaches that need to be adopted for the tax administration to move from a reactive approach to non compliance, including frauds, to a proactive approach that deters and prevents frauds. Therefore, IT systems will need to go beyond data processing to provide not only these data mining and analytical facilities, but also to provide user-friendly web sites, which provide answers to questions of the tax payer.

Arbitrary revenue targets set by the Ministry and boards lead to irrational assessments, leading to unsupportable, and ultimately unsuccessful, tax demands. Plugging of leakages through better information will lead to increased tax revenue, as was illustrated by the experience in Maharashtra, cited earlier. In addition to these defensive strategies, there is need to use the macroeconomic information gathered in the database to forecast revenue more accurately. The use of advanced analytical techniques using ICT will help in this process. TARC report has covered these forecasting methods and data requirements in detail.

In order to achieve the full benefits of ICT, the departments should adopt a motto "Digital by Default". There are several steps that need to be taken to transition to advanced state of ICT usage, benefitting both the tax payer and the department. Development of plans for a fully digitized environment leading to enunciation of IT architecture principles need to be attempted immediately. This will lead to the creation of plan for procuring and installing an appropriate ICT infrastructure. Project management and maintenance capabilities will have to be of a high order. Taking these into account, TARC report has suggested creation of a special purpose vehicle (SPV), which will enable the department to bring in specialists from outside for a period of time.

ICT needs to be at the core of a transformed tax governance system. Current piecemeal efforts will have to give way to a more rigorous approach.

Patrick Trapp

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Transformation of tax through technology

> *The need for faster, more accurate and reliable information for internal and external stakeholders is a global trend that will continue to put pressure on the tax departments of today and tomorrow. Encompassing technology as a change agent for the tax function is now seen as a necessity*

The ever-changing environment for tax, today and tomorrow

Now more than ever, tax functions and professionals are faced with an increasingly complex and ever-changing environment. The need for faster, more accurate and reliable information for internal and external stakeholders is a global trend that will continue to put pressure on the tax departments of today and tomorrow.

The growing list of challenges thrust upon the tax function is driving a global shift in the way many organizations are evolving their approach to, and focus on, effectively managing tax operations and risks.

Technology enablement as a driver for change

Encompassing technology as a change agent for the tax function is now seen as a necessity. Today, a company can be multinational – even global – from day one of its formation. This brings with it the obligation of meeting the broad requirements of the jurisdictions in which it operates.

As clients look to technology solutions on the market or tools already in use within their organization, we are seeing new and exciting ways of driving operational enablement across the tax function. In working with clients in mature and emerging markets, the trend continues to focus on operational enablement through technology in areas such as:

- Transparency and oversight through **workflow and governance** solutions
- **Integrated controls and validation** technologies embedded within the finance processes, capturing sign-off and hand-off points between resources and systems
- **Tax reporting automation** solutions to support the end-to-end US GAAP/IFRS GAAP to Statutory GAAP to Tax reporting processes
- Enhancing **analytics across all tax processes** to redefine and understand the story behind the data and approach to remediation to proactively manage risks and controls.

Additionally, the increasing focus on the use of outsourced or centralized services (as companies peel off their lower-value, repetitive business operational tasks) brings with it the need to effectively manage the risk and tax considerations as part of the overall transformation.

As a result of these impacts, the key requirements are to develop and strengthen relationships and understanding of the broader finance transformation agenda and enterprise resource planning (ERP) related projects – with an aim to help ensure that changes to systems and processes take current and potential future tax reporting needs into account.

Whether part of a finance transformation exercise or otherwise, now is the time to be forming your tax data and technology roadmap for the future, with IT infrastructure discussions required sooner rather than later. Through our recent work with an **India-headquartered global BPO services provider**, a future state tax technology roadmap was developed. The roadmap has assisted in strategically aligning the tax function's requirements to the existing global finance transformation initiative. This has enabled the Tax function to become a key partner in the overall data/technology and operating model transformation initiative going forward, as opposed to simply being a recipient of the broader decisions and outcomes. It is, therefore, in a position to drive value, efficiency, return on investment and benefits not just for the Tax function, but for the organization as a whole.

Additionally, in the current climate, disclosure and transparency will continue to grow. The use of electronic auditing initiatives, such as the Standard Audit File for Tax (SAF-T), represent the next era of taxpayer-to-tax authority data transfer. Tax administrators are also using

An old adage holds that a database is only ever as accurate as the information input. This is especially true in tax, with broader impacts for the organization, where wrong data can lead to penalties, disputes and reputation risk

technology to intervene earlier in the compliance life cycle. Therefore, going forward, data readiness and controlled accessibility are key to managing the potential risks and responsiveness, considering the ongoing obligations in 2015 and beyond (country-by-country reporting, unrevealed impact of elements of the base erosion and profit shifting (BEPS) project, Common Reporting Standard, etc.)

All this means that tax technology enablement, and tax data readiness and quality, are more important than ever, with the Tax Function being central to addressing these challenges.

Tax authorities leading and following technology trends

Tax authorities are pushing hard to transform their processes to deliver functional improvements, while at the same time reducing operating costs. This, in turn, affects how global tax functions are reacting. Two key global trends that are driving the way tax administrations operate will symbiotically evolve the way taxpayers prepare for the future:

- **Everything must be digital:** Digitization is changing the fundamental ways in which governments and tax administrations work and, therefore, creating a greater emphasis on the accessibility and reliability of tax data at source. This is forcing organizations to think more broadly than the historical need for e-filing to ensure the "end-to-end data environment" is fit for purpose today and in future.
- **Data-driven compliance is growing:** The request for more and higher degrees of granular data is changing the way in which the tax authorities work and operate throughout the tax compliance and tax audit cycle. Their enhanced capabilities to converge, store and analyze huge amounts of data will continue to drive taxpayers' focus on readiness and data quality, as both parties look to drive efficiencies and effectiveness in their respective domains.

The impact of change and staying ahead of the curve

An old adage holds that a database is only ever as accurate as the information input. This is especially true in tax, with broader impacts for the organization, where wrong data can lead to penalties, disputes and reputation risk.

Our view is that successful ERP implementations have become a prerequisite for high-performing companies. They undoubtedly play a mission-critical role in the enterprise-wide business operations of every single multinational company.

However, the reality is that not every company has a consistent, global implementation, even if they have implemented the same package around the world. The result is that tax functions must typically interact with multiple standards and spend valuable time translating them into a common structure or data definition. Even when tax has access to these systems, the data management challenges can be daunting.

As clients look to take advantage of the systems and data environment that impact operations, the tax function can (and must) be involved. One of the **world's largest chemicals companies** was transforming from an environment of multiple and heavily customized ERP systems to a new global ERP single standard. By defining necessary tax data requirements and proactively collaborating into the transformation program, the need for an indirect global tax solution was incorporated. This led to enhanced and streamlined tax processes and controls associated with direct and indirect tax, thereby driving increased levels of automation, integration consistency, accuracy and timeliness. Simultaneously, while delivering overall improved data quality for direct and indirect tax, it also enabled new tax opportunities to be identified that would not have been achievable in the original state.

The importance of tax on the corporate agenda means that now is the right time to be asking for increased investment. The key is ensuring that this investment drives true and sustained value from the operations of the tax function, moving it from the back office to become a true business partner to the organization.

"One of key areas that will help address the changing needs will be a suitable investment in technology by India Inc"

Ajay Kumar
Partner, Tax & Regulatory Services
EY India

Direct and indirect tax collections in India have increased from INR6.23 trillion in 2009-10 to INR11.35 trillion in 2013-14.[1] Over the past few years, the tax environment in India has also witnessed an increase in complexity both in terms of administrative and legislative changes. With both the Center and the States having power to levy taxes, certain transactions are sometimes subjected to dual taxation. Companies are also subject to several state-level compliances. Each of the authorities has independent powers to conduct tax audits. This requires companies to be in an always ready state to deal with audits and inquiries from a number of tax authorities.

The cost of tax adjustments, arising either as a result of non-compliance or due to differences in interpretation of the law between tax payers and tax authorities, can be quite severe. For instance, companies can be exposed to the situations mentioned below:

- Cash flow impact, as typically 50% of the disputed tax is required to be paid upfront
- Payment of interest at high rates
- Penalties and fines
- Risk of prosecution
- Senior management time locked into resolving disputes

In recent years, transfer pricing, withholding tax (TDS) and indirect taxes have been the key areas where corporates have faced significant challenges. Several companies have had to deal with potential prosecution proceedings for non-compliance with TDS provisions.

Simultaneously, Indian business organizations also need to prepare vigorously for comprehensive legislative changes such as the Goods and Services Tax (GST) Act. Income Computation and Disclosure Standards, introduced with effect from the current financial year, will also require companies to track and reconcile differences between statutory accounts and tax accounts over several years. Indian companies with global operations will need to constantly deal with changes that will come into effect due to the Base Erosion and Profit Shifting (BEPS) initiatives.

It will be vital for corporates to ensure that key personnel are updated with the changes from a knowledge standpoint. Tax professionals need to work with Enterprise Resource Planning (ERP) teams to not only ensure that the correct data is captured, but also inform other stakeholders about the changes in the tax landscape and their impact on the company.

One of key areas that will help address the changing needs will be a suitable investment in technology. Different tools need to be developed to meet the shifting paradigms of tax reporting and tax transparency requirements imposed both under the Indian law and the global tax landscape.

1 For 2009-10: http://indiabudget.nic.in/budget2011-2012/ub2011-12/bag/bag2.xls, For 2013-14: http://indiabudget.nic.in/ub2015-16/bag/bag2.xls

In the GST regime, technology can help create a credible deterrence for tax evaders

Prakash Kumar
CEO, Goods and Services Tax Network (GSTN)

India Tax Insights team talks to Prakash Kumar, CEO, Goods and Services Tax Network (GSTN) on how the evolution of technology has helped in the area of tax administration; the importance of GSTN for maximising compliance; addressal of data security concerns and so on.

Q1.

You have been part of the Government and a senior tax administrator in the past. You have also been part of the senior management of leading technology companies. How do you see the evolution of technology in the area of tax administration?

In India, tax departments were among the first ones to adopt technology in the Government. The Income Tax Department, Central Board of Excise and Customs (CBEC), and sales tax departments in states started using technology back in the 1980s and 1990s. This was possible primarily because tax calculation and account keeping was amenable to automation. Introduction of technology helped tax administrations gain quick ROI while it also brought benefit to the taxpayers.

Initially, however, the use of technology was limited to certain pockets within tax administrations; software applications were distributed in nature and worked in silos, and there was no integration between applications/systems. The real change came about when technology allowed disparate systems to be integrated and enabled taxpayers to interact directly with the tax departments. Online filing of returns is one of the most important instances.

Currently, GSTN is working on rolling out a state-of-the-art IT infrastructure that will bring in significant improvement from existing implementations. Core services of registration, return filing and payments will be fully automated; data sharing between GSTN and tax administrations will be near real-time; integration with various external stakeholder systems will be achieved to minimize data entry and for quick validation. All these are expected to bring serious benefits not only to the tax administrations but also to the taxpayers. Some of the unique features of the envisaged system are:

- Real-time, online validation of PAN, Aadhaar, Challan Identification Number (CIN), Director Identification Number (DIN), etc.
- Near real-time sharing of taxpayer uploaded data with tax authorities
- Fully automated return process with multiple modes for upload
- Fully transparent system with comprehensive taxpayer dashboard and ledgers
- GST compliance rating for taxpayers that will be published on GSTN portal

> *The "IT Strategy for GST" envisaged that the process of applying for registration, filing of tax returns and tax payment should be simple and uniform... Also, the compliance process should not place any undue burden on taxpayers and should be an integral part of their business process.*

Q2.

The Union Government has put lot of focus on establishing taxpayer-friendly regimes. Recently, the Honorable Finance Minister has exhorted senior tax officials to maximize the use of non-intrusive and innovative methods of investigation. How do you think technology can help achieve these objectives?

Technology has a pivotal role to play in achieving the objective of effective investigation in a non-intrusive manner. The age of data and analytics has already started to fundamentally transform the way indirect tax policy and administration are planned and executed. Collection and collation of data is very central to the business of tax administrations, and because they have access to such large quantities of data, tax administrations are in a better position to adopt analytics than the vast majority of other organizations.

Using analytics to leverage the value of their data and information, tax administrations can make evidence-based decisions, increase organizational knowledge, reduce costs and significantly improve performance on the service and compliance front.

To give you an example, one of the most common instances of the usage of technology in tax administrations in the past has been risk-based selection of taxpayers for audit. The need for risk-based selection was necessitated on account of adoption of self-assessment of tax for return filing. As all taxpayers could not be audited with limited staff, and 80% of the tax revenue came from roughly 20% of the taxpayers, it was prudent to engage the available staff in auditing those cases where ROI is expected to be high. One of the methods used across the world is a "criteria-based selection" system, based on the mathematical theory of "predictive discriminant analysis." The only way to employ such criteria-based selection techniques is to use computers, as only computers can churn large amounts of data and generate reports. Such usage of technology not only helped build an effective tax administration but also significantly reduced the chances of harassment of honest taxpayers.

Today, technology enables us to use advanced analytics techniques, models and frameworks that will be central to maximizing the impact of the information exchange, and will have significant impact in deterring tax evasion and promoting global voluntary compliance. This would mean that tax officials do not go after taxpayers asking them to provide information. Rather, we access such information using technology driven information exchange with various other external systems/databases. These are clear examples of using technology in an unobtrusive and innovative manner to help tax administrators perform their statutory functions.

Q3.

Taxpayers have complained in the past about lack of transparency and misled use of discretion in tax administrations. In your opinion, how much can technology help in addressing those concerns?

Discretion has typically been employed in the absence of clarity on policies and procedures, especially to the taxpayers. In absence of technology-based assessment and enforcement mechanisms, it has been left to the judgment of the tax officials who picked taxpayers for investigations and audit, resulting in grievance among taxpayers.

Technology is instrumental in addressing such concerns. Technology acts as a major catalyst in enhancing transparency through information dissemination. It also helps in creating a mechanism for feedback from taxpayers, escalation mechanism for action on complaints, and intelligent dashboards for senior officers, etc., which help increase objectivity in tax administration.

In the GST regime, apart from the extensive use of advanced technology in tax administration functions, we will also have a rating system mechanism where businesses with higher level of compliance will have higher rating. Thus, they will have a competitive advantage over other businesses with lesser rating. Information on such ratings will be published on the GST portal for the benefit of all taxpayers.

> *Some States do not have matured IT systems for tax, and for them, the back-end system to process registration applications, assessments, appeals, etc., is being developed by GSTN.*

Q4.

Tax officials often have to walk the tightrope balancing facilitation and plugging revenue leakage. How do you see technology helping tax departments develop a balanced approach to risk and value?

"Taxation should not be a painful process for the people. There should be leniency and caution while deciding the tax structure. Ideally, governments should collect taxes like a honeybee, which sucks just the right amount of honey from the flower so that both can survive. Taxes should be collected in small and not in large proportions." – Arthashastra

Technology is the only hope for tax administrators in their endeavor to strike a balance between facilitation and compliance. While self-assessment of tax will continue to stay in the GST regime, technology can help create a credible deterrence for tax evaders. Using technology, we can also encourage taxpayers to indulge in "self-service." The information provided by the taxpayer coupled with information exchange with various other relevant systems can help create 360 degree profiles of taxpayers. A 360 degree profile is an important tool in plugging revenue leakage as has already been proved internationally.

In the GST regime, while all taxpayers will be allowed to file returns on self-assessment basis, input credits availed by the taxpayer will be subsequently verified by the system to ensure that the tax payment for the corresponding supply has been received. In the absence of such confirmation, the credit availed in the earlier tax period will be systematically reversed without any manual intervention. This will tremendously help tax administrations in plugging revenue leakage without any intervention.

Q5.

The GSTN is expected to bring about a sea change (especially in compliance reporting) in the way indirect tax is administered in this country. How do you think this changing paradigm will help both tax administrators and taxpayers in the medium and in the long term?

PK: When the tax authorities automated Delhi sales tax in the 1990s, in every tax office the clerk's job was to maintain 16 odd registers (to track how much tax has been deposited, who all have filed returns, issues of acknowledgement, commodity types and so on). With simple automation, many of these redundant processes were eliminated. These changes were welcomed by the heavily burdened clerks who adopted the changes quickly, which contributed to the success of the new initiative. Now, the officials could focus on the important tax administration functions of assessment and enforcement, and the quality of the assessments went up.

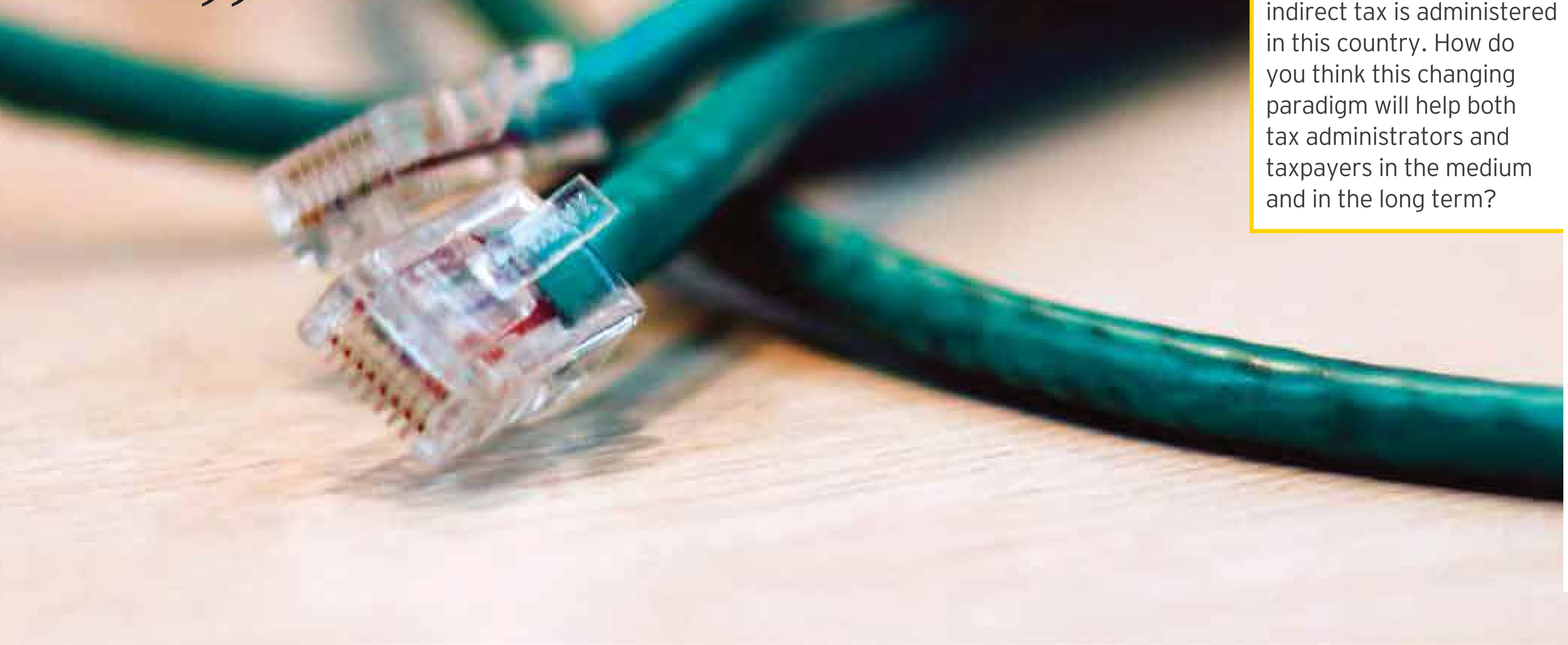
We must remember that tax is only incidental to business, and our goal as the organization responsible to lay IT infrastructure for GST, is to create a platform that will help minimize the time and effort required for tax-related matters. We are working on building an end-to-end automated system that will help tax administrators and taxpayers focus on their core tasks, i.e., performing statutory tax functions and doing business, respectively. The key benefits that the changing paradigm is expected to bring in are:

For taxpayers

- One-stop-shop (GST portal) for all GST-related compliance reporting
- One return under GST replacing returns under VAT, CST, excise, service tax, luxury tax, etc.
- Simplified and uniform formats
- System-assisted return drafting
- Multiple ways to connect to the GST system (portal, third party tablet/mobile-based apps, API-based integration, etc.)
- In more than nearly 95% cases, taxpayers' interaction for GST-related compliance will end at the GST portal

For tax authorities

- End-to-end automation (workflow-based system)
- Quick availability of past data
- Processed inputs
- Standard reports
- Business Intelligence (BI) and analytics aided enforcement



> *In the past few months, GSTN has conducted IT workshops with tax administrations of State and Central Governments, with the objective to integrate their IT systems with the GST system. It is also in discussion with many banks and RBI for smooth integration with the GST system.*

Q6.

GSTN would be the custodian of a huge amount of sensitive financial information. How do you think data security concerns of both tax authorities and taxpayers can be addressed?

PK: We are fully aware of this responsibility and adequate measures are being taken to thwart any security risk to the data. We need to protect data from external as well as internal security breaches.

For the GST system, security architecture has already been designed as part of the solution architecture. Multi-layered security architecture has been conceived to address the issues of data confidentiality and data integrity. Any transmission of information, such as between the GST system and taxpayers, or the GST system and IT systems of State and Central tax authorities, will be in a fully secured and encrypted manner.

We are taking adequate steps to ensure that highest possible security measures are implemented. Access to data will be fully based on credentials and access rights, e.g., tax officials will be able to access taxpayers' data only for their respective jurisdictions and not beyond that. GSTN will also undertake audit trail and other strong measures to ensure data integrity.

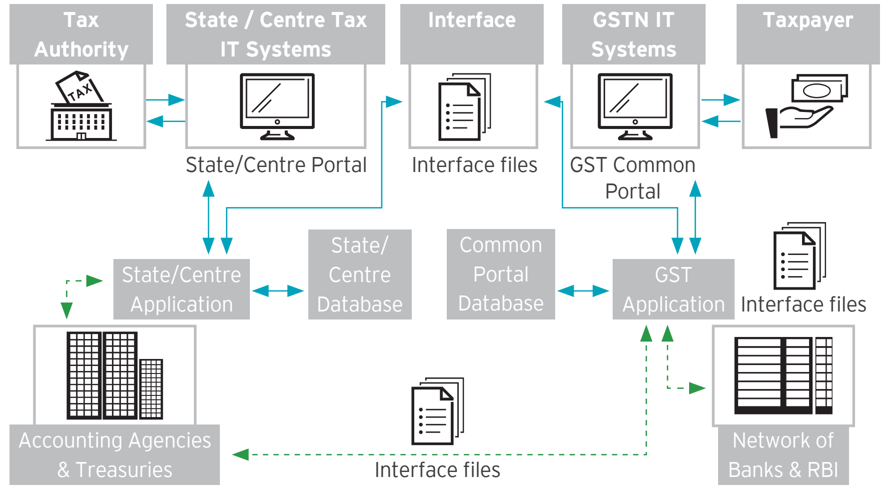
Some of the key features of the security architecture are:

- Security standards: ISO 27001, ISO 22301
- Perimeter security: firewall, Intrusion Prevention System (IPS), APT
- Data security over the network: end-to-end encryption across the network
- Security monitoring: Security Operation Center (SOC)

Q7.

Only GSTN rolling out a state-of-the-art GST system may not suffice. The entire tax ecosystem needs to be ready to reap the full benefit of advanced technology. What are the challenges you foresee and what steps can be taken to get the entire ecosystem ready?

The GST ecosystem consists of the following major players: (detailed diagram in Annexure A)



It is true that to gain the full benefit of advanced technology, all these stakeholders need to be ready to use the new system. GSTN is already working on bringing all important stakeholders on board.

In the past few months, GSTN has conducted IT workshops with tax administrations of State and Central Governments, with the objective to integrate their IT systems with the GST system. It is also in discussion with many banks and the Reserve Bank of India for smooth integration with the GST system. GSTN also plans to conduct workshops for accounting software product companies to help them make their products GST-ready and develop apps that will help their users to upload returns directly.

Some of the key challenges and remedial measures are described below:

Challenges	Steps being taken/planned
IT readiness of states	Some states do not have matured IT systems for tax, and for them, the back-end system to process registration applications, assessments, appeals, etc., is being developed by GSTN. For these states, there will be one common system handling the back-end functions as well.
Readiness of taxpayers to file returns and pay taxes online	Currently, many states do not have online systems of return filing/tax payment. Intensive training is planned through state tax authorities to prepare the taxpayers.
Elimination of the requirement of sending signed physical copy of filed return (in absence of digital signature)	As has been done by Central Board of Direct Taxes CBDT, GSTN is also considering the implementation of e-sign to remove the need for sending the signed physical copy to the designated address. This, however, has to be suitably backed by GST laws.
Readiness of CAs/tax advocates/ Tax Return Preparers (TRPs)	Training

Q8.

We have mentioned about the Government's focus on rolling out a taxpayer-friendly regime. Could you please talk about some key features of the technology solution being envisaged by GSTN that will help taxpayers to comply in an easy and uncomplicated manner?

Simplicity for taxpayers is one of the key desirable features of the GST system to be built by GSTN. The "IT Strategy for GST" envisaged that the process of applying for registration, filing of tax returns and tax payment should be simple and uniform, and should be independent of taxpayers' location and size of business. In addition, the compliance process should not place any undue burden on taxpayers and should be an integral part of their business process.

GSTN is working on achieving these very important objectives of "simplicity" and "standardization" to encourage voluntary compliance.

Some of the key relevant features of the GST system are mentioned below:

Registration

- Common registration form for all applicable GST laws across all states
- Online registration (mandatory): registration data will get shared with both Central and appropriate State tax authorities. Wherever possible, online validation of data will be done to ensure that the applicant does not have to upload scanned copies of supporting documents (e.g., PAN/Aadhaar/CIN/DIN, etc.)
- No physical supporting documents required to be sent to tax authorities
- E-mail and mobile communications to be sent to applicants/registrants on their registered e-mail and mobile number
- Registration Certificate (RC) to be made available online
- No need to appear before the registering authority before registration is granted
- Digital signature certificate and support for Aadhaar-based e-Sign
- Amendment of many fields of the registration to be on self-service basis (without requiring approval) after the registration

Return filing

- One common return form for all different types of taxes; one return per registration per tax period
- Online return filing to be mandatory
- Anytime upload of invoices through multiple modes (direct entry at portal, GSTN provided tool, integration with accounting software, using third party apps, etc.) to be facilitated
- Only sales (supply) invoice data to be uploaded and get reflected automatically in the purchase register of counter-party buyers (recipients of goods/services)
- System to generate draft return, which can be edited by the taxpayer

Tax payment

- Common challan for all different types of taxes; one challan form to capture payment information for all types of taxes
- Online tax payment (mandatory above a certain threshold); for those who want to pay over-the-counter, preparation of challan online at GST system to be mandatory to avoid data entry mistakes
- One-to-one integration with all agency banks (currently all states do not provide the facility to pay in all agency banks)
- Those having accounts in non-agency banks can pay through RTGS/NEFT
- Taxpayers to also receive regular updates regarding their payment through SMS/email-based interaction

Views expressed are personal to the interviewee

Technology in Tax

A catalyst for compliance Risk management and Planning

Rahul Patni

Partner, Tax & Regulatory Services, EY India

In an era where "tax" commands an important role in boardroom discussions, the need of the hour is to ensure that businesses get the right investment into the tax function in order to form a tax technology roadmap.

At a recent EY flagship event "aHead of tax," which was attended by several senior tax and finance professionals in Zurich, a remarkable 50% of respondents to a poll believed that their tax function will change by 25%-50%; 14% of respondents believed that the change will be more than 50%. One of the top five changes in the tax function that were envisaged was "technology and data."

While corporations have embraced and leveraged technology in many functions (e.g., supply chain, finance, logistics, marketing, etc.), it is felt that the involvement of technology in the tax function has been rather limited. Comparing how a tax function in an organization operates now vis-à-vis 10 years ago, it may be said that the pace of adopting technology could have been faster to deal with the ever-transforming dynamics in the external tax environment.

Globally, many tax administrators have been investing heavily in technology and deploying it strategically. International studies show that the use of technology coupled with focused performance management can result in significant improvement in compliance and reduce the tax gap. From an India tax perspective, technology has, over time, moved from data capture to online transaction processing systems, from which both taxpayers and tax authorities have benefitted significantly. The Tax Administration Reform Commission (chaired by Dr. Parthasarathi Shome), in its first report[1] on tax administration reform in India, has recommended forming a Special Purpose Vehicle (SPV). This SPV would establish a state-of-art digital platform for various networking capabilities, including exchange of data among the direct and indirect tax authorities, enabling better taxpayer profiling, and more powerful risk models to support enforcement. The use of electronic auditing initiatives, such as the Standard Audit File for Tax (SAF-T)[2] in several European countries, is also a step in the right direction. The day does not seem far when audit proceedings in India would also be initiated by asking the taxpayer to file a standard pack of information in an electronic form!

There are more than one ways in which technology can help further unlock the potential of the tax function in an organization. EY's recent experience in technology-enabled solutions for

1 http://www.finmin.nic.in/the_ministry/dept_revenue/index_TARC.asp

2 SAF-T (Standard Audit File for Tax) is an international standard for electronic exchange of reliable accounting data from organizations to a national tax authority or external auditors. The standard is now increasingly adopted within European countries as a means to file tax returns electronically

tax in India has been quite exciting and encouraging. Specifically, we have found data analytics to be of immense value in areas such as capex reviews and optimization, indirect tax credit flows, etc. Using the capabilities of data analytics in such projects has helped deliver significant value for clients.

With the evolving international environment (especially around country-by-country reporting) and rising tax activism, there is overwhelming agreement among tax professionals that both litigation and compliance requirements are going to increase substantially in the near future. Filings are increasingly becoming electronic, and digitization is high on the agenda of the tax administrators as well. This should call for a novel and technology-enabled way of managing the tax function. For instance, the response we hear from our clients on the EY litigation management tool[3] has been extremely encouraging; it moves all aspects of litigation to an intelligent digital platform, which does much more than just store documents in a smart digital format. It has an in-built ability to analyze data and provide smart reports to have hands-on information on the litigation status, tax demands, aging analysis, personalized calendar, etc. The solution has been created considering the multifarious requirements of finance heads and tax leads.

As far as withholding tax management is concerned, the Indian tax administration has already moved to a full-fledged online system a few years ago. This system encompasses all aspects such as grant of tax credit, issuance of withholding tax certificates, issuance of refunds, computation of tax liability, calculation of interest, etc. However, on account of different bases of accounting/recognition followed by different taxpayers, there often arises a situation where tax credits are missed or there is a delay in getting a refund, and other resultant mismatches. There is potential to digitize these processes, which will go a long way in the reconciliation of tax data and avoiding unintended litigation.

Enterprise resource planning (ERP) implementations play a very vital role in the business operations of most companies. For example, ERP usage provides complete traceability of transactions, and the values flow seamlessly to various modules that are tightly integrated. If this data is appropriately captured and analyzed from a tax point of view, such ERP systems can be of colossal help in identifying red flags and being better prepared for tax audits. Often, there is resentment among taxpayers about the volume and type of data that is typically requested by tax authorities; at times, it is also difficult to retrieve such information. However, an ERP designed to cater to tax-specific data requests can not only enable an effective audit process but also create efficiency in the tax function.

To conclude, technology still has tremendous potential to help make the tax function agile to the changing tax landscape, raise efficiency and effectiveness to higher levels, and optimize tax costs. In an era where "tax" commands an important role in boardroom discussions, the need of the hour is to ensure that businesses get the right investment into the tax function in order to form a tax-technology roadmap.

3 EY has introduced application-based Litigation Management Services ("LMS"), to manage myriad litigation data. The application comes with an inbuilt ability to analyze data and provide smart reports to have hands-on information on the group's litigation status and help in decision making with regard to tax litigation. The solution has been created keeping in mind the multifarious requirements of finance heads and tax leads of the companies.

> *Enterprise resource planning (ERP) implementations play a very vital role in the business operations of most companies... enables an effective audit process and creates efficiency in the tax function.*

Our experience

"We were approached by one of the largest private sector conglomerates in India to review and comment on the tax depreciation claim. This company was making consistent, large capex spends, and felt that its current processes may not be supporting an appropriate tax classification of fixed assets and depreciation claim thereof.

We were tasked to review the fixed asset register and underlying data, which ran into approximately 80,000 line items. With the help of data analytics, we could shortlist a smaller population of assets in a matter of days, which, under a traditional approach, could have taken weeks to complete. With the use of technology, we were successful in shortlisting assets of a sizeable quantum which have the potential for reclassification (into a higher depreciation class for tax purposes) and identifying areas for further review in subsequent phases."

Saurabh Shah, Senior Tax Professional, EY contributed to the article

EY Management Tools

Litigation

Digital Enablement

Functionality of the tool

- Provides real-time status of various tax cases
- Tracks all open tax cases along with associated demands, interest payment and penalty
- Tracks how issues have traveled through various levels of judicial hierarchy
- Provides risk-wise analysis of all issues faced by the group for all kinds of taxes and for all years
- Provides visibility on total tax amount locked in disputes, demands and refunds outstanding
- Tracks team members and consultants associated with any tax litigation
- Stores and retrieves back-up data for each return filed with tax authorities
- Provides reminders and escalations for upcoming or overdue events
- Generates smart reports around pending and closed tax cases
- Stores and retrieves all documents relation to tax litigation cases

Benefits to the user

- Mitigates risk of loss of crucial documents of tax cases such as challans/refunds received, submissions filed, orders received, appeals filed, etc.
- Improves decision-making around tax litigation
- Significantly reduces time spent on monitoring and reporting tax cases
- Provides control and transparency of all open cases
- Mitigates loss of reputation and prosecution risks by reducing the risk of submission of wrong data
- Helps management focus on high-risk cases
- Helps management focus on collection of outstanding tax refunds stuck in disputes
- Significantly reduces risk of missing reporting deadlines
- Generates automated reports and status updates

Profiles of companies that should adopt it

- Given the complex tax litigation environment in India and the various benefits provided by this tool, almost all companies operating in the country would benefit from adopting this application. However, it provides significant benefit for those companies that are currently facing major litigations in both direct as well as indirect taxes and have difficulties in tracking or managing them.

Intercompany effectiveness

Managing the practical challenges of transfer pricing

Sveinung Baumann-Larsen
Partner, EMEIA Tax Center
EMEIA Intercompany Effectiveness Leader, EY

Globalization is significantly increasing the proportion of intercompany trade within multinationals. While businesses think and operate internationally, tax authorities focus minutely on the tax bases in their jurisdictions, and multinationals face ever-increasing complexity around their international tax affairs and in particular transfer pricing. In addition to existing widespread transfer-pricing documentation rules, new transparency requirements are required now driven by BEPS importance. This leads to more focus on the operational transfer pricing management.

This point of view looks at current drivers for operational transfer pricing management and frequent practical challenges we observe. We will provide an overview on elements of a holistic framework for operational transfer pricing management.

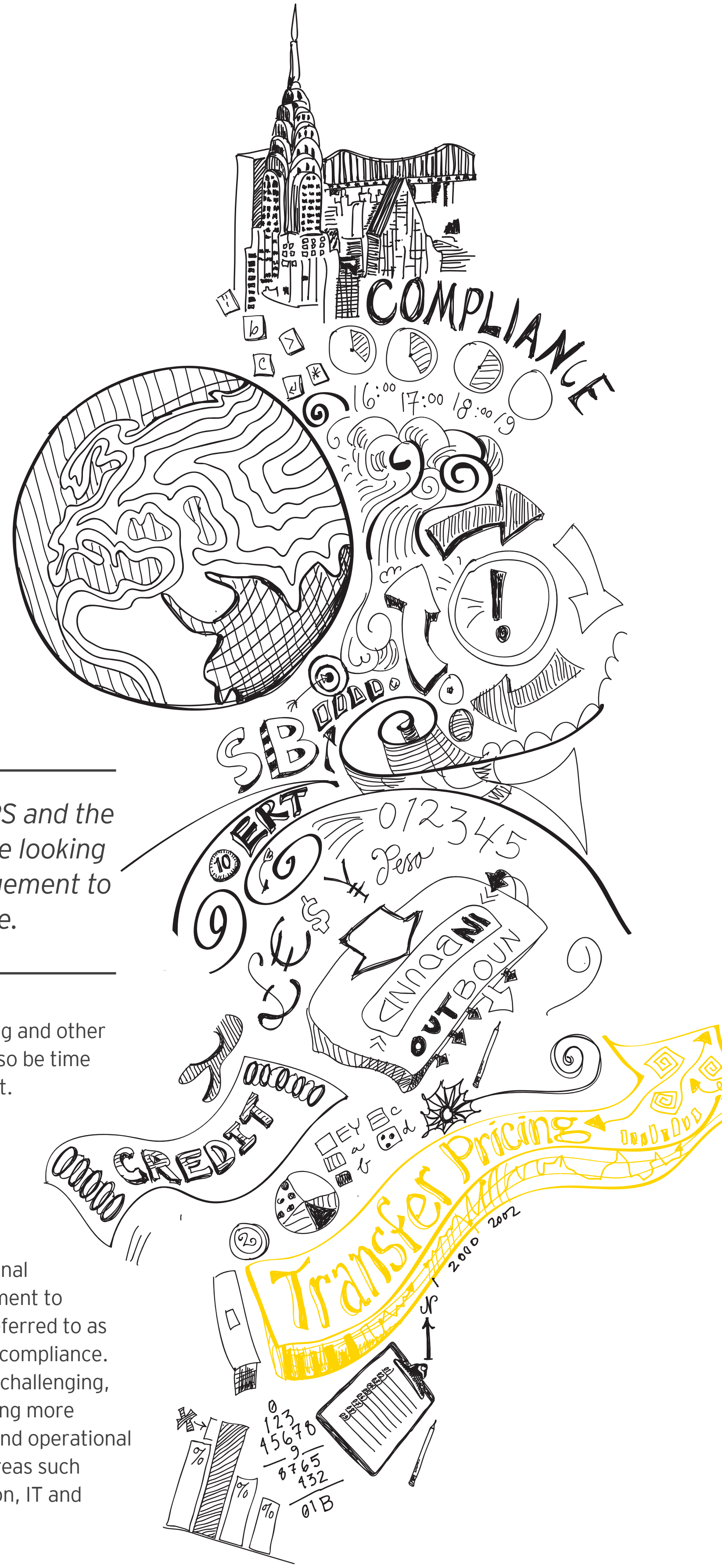
With new transparency requirements driven by BEPS and the increasing audit focus anticipated, many groups are looking to improve their operational transfer pricing management to achieve material transfer pricing compliance.

Context

Stringent transfer pricing documentation rules are now widespread and extend far beyond the original OECD countries driving this trend. This has led to significant focus on documentation and to achieve what may be referred to as formal compliance.

Conversely, operational transfer pricing has typically received less focus within multinationals. Many organizations struggle to deliver the pricing and profitability required to align with their policies or maybe get there in the end through cumbersome and retrospective year-end processes. Either way, this can result in significant transfer pricing and other tax exposures and can also be time consuming and inefficient.

With new transparency requirements driven by BEPS and the increasing audit focus anticipated, many groups are looking to improve their operational transfer pricing management to achieve what might be referred to as material transfer pricing compliance. Many tax teams find this challenging, since it involves integrating more effectively with finance and operational teams across different areas such as processes, organization, IT and reporting.



Typical issues and experiences with operational transfer pricing management

It can be helpful to think of transfer pricing as end-to-end life cycle. This starts with transfer pricing strategy setting, planning and policy development, which receive considerable focus from most groups as they prepare their transfer pricing files and reports. At the other end of the cycle most groups will engage in some form of testing and compliance as part of their annual documentation process. This is often a struggle and it can be interesting to analyze a little deeper why this is so.

Recurring Process

1. Planning & Policies
2. Price Setting & Contracts
3. Transactions & Journal Entries
4. Monitoring & Adjusting
5. Testing & Compliance
6. Controversy & Litigation

Multinationals operate in a complex and fast-changing world. As part of developing and delivering their financial strategies, most groups place significant attention on budgeting and forecasting, which are typically formalized finance processes. Many companies leverage this information at the beginning of the financial year for re-setting transfer prices.

The operational challenge is that a budget is just one scenario and circumstances can quickly change. A product launch may be delayed, a new manufacturing line may have technical problems, a major tender may be won against the odds. All these events and more can mean that budgets can quickly become outdated and as a result the transfer pricing built around them may be out of date too.

It requires strong monitoring and adjustment processes to manage transfer pricing in such an environment. Many tax teams we work with understand this, but find how to go about it to be challenging. Financial and management reporting are not generally driven by tax requirements and therefore, the transfer pricing team does not typically receive the sort of information it needs to monitor and adjust.

For example, finance do not generally segment results by transfer pricing function and in many cases information may be focused on product groups or clusters rather than at a formal legal entity level. This has driven the emergence of parallel transfer pricing reporting typically on spreadsheets that can be cumbersome, inefficient and in some cases unreliable.

Some leading practice trends in this area are clearly emerging. Companies we see take a much more integrated approach with finance and operations and integrated their transfer pricing setting, transaction execution, and monitoring and adjustment activities within key business processes they leverage from, including Record to Report, Plan Budget & Forecast, Order to Cash and Procure to Pay.

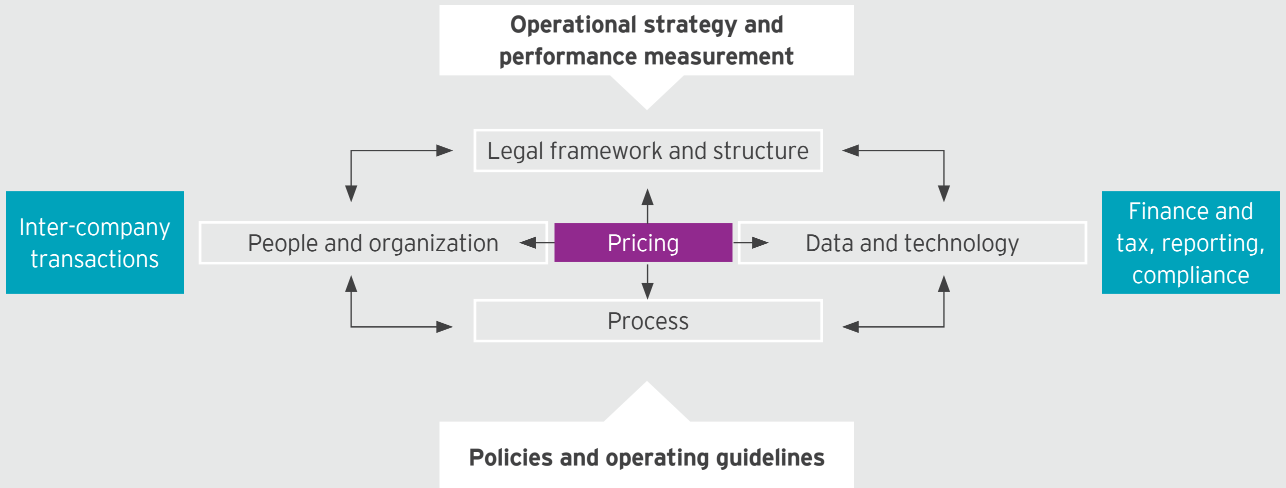
This integration requires strong definition and articulation of roles and responsibilities around transfer pricing across the organization. Moreover, reporting and technology may need to be enhanced to provide the information and functionality the transfer pricing team needs. This may require some realignment with performance measurement systems as sometimes there can be competing objectives that are steering the business away from transfer pricing compliance.

To summarize, there are several different elements to consider in building a practical, efficient and integrated operational transfer pricing system.

EY point of view

Intercompany effectiveness framework for holistic operational transfer pricing management

The ICE framework is a holistic framework to help align interrelated elements, which are organization, processes, pricing, technology and governance structures across the transfer pricing life cycle. This takes place under consideration of the group strategy and performance measurement as well as related policies.



The question now is, how could all these elements be tied together to resolve practical issues. In the following section we would like to share our point of view for a practical challenge.

Margin management as a success factor for material compliance

Currently, multiple MNEs face difficulties in achieving the target margins of their various transactional segments. In practice the "outcome-testing" approach is popular, but leads regularly to substantial year-end adjustments. These could cause several tax and operational issues. Looking for alternative ways, the "price-setting" approach is straight forward, which promises to arrive in an uncertain world closer at the target corridor. However, typically, an integrated approach is required to make that happen.

Typical framework elements that have to be integrated are:

a. **People and organization.** Ensure cross functional integration and define roles and responsibilities for setting, monitoring, reporting and adjustment of transfer prices.

b. **Processes and controls.** Establish cross-functional setting, monitoring, reporting and adjustment processes.

c. **Data and technology.** Implement a technology solution enabling, monitoring, reporting and adjusting of transfer prices. The backbone is typically a segmented profit and loss statement that displays revenue and cost structure of transactional segments.

d. **Policies and guidelines.** Establish a practical operating manual, harmonized across functions.

Conclusion

Due to latest developments, operational aspects of transfer pricing becomes more and more important. In our point of view, there are multiple elements to be considered to build an effective and efficient transfer pricing management. We want to encourage MNEs to prepare for post-BEPS and to assess if the own operational transfer pricing management meets future requirements.

EY Management Tools

GST *Navigator*

A technology solution for impact assessment

Functionality of the tool

- GST will usher in significant changes that will need to be understood, measured and acted upon to capitalize on opportunities, deal with risks, and manage transition.
- Complex supply chain structures, with multiple transactions connecting each one of them, augur the need for a systematic and clinical approach to study the impact of GST.
- EY's proprietary tool, "GST *Navigator*," has been built on a state-of-the-art technology platform to assess and simulate tax impact.
- GST *Navigator* can present tax analytics for the current and simulated GST regime to understand the impact through various scenarios including:
  - Multiple bases and points of levy
  - Possible rates of tax and characterization of transactions
  - Alternate place of supply rules
  - Framework for allowing input credits
  - Changes in supply chain network
  - Cash flow related aspects

Benefits to the user

- Early assessment of tax impact of the change, with ease of future refresh as the regulations evolve
- Reports offer multiple drill downs, providing high quality analytics.
- Clients are using the output of the GST Navigator for:
  - Advocacy - Determine what is adversely impacting at a policy level that can be then represented to the Government; companies are able to identify, validate and back up their claims of impact
  - Pricing (Profit & Loss and cash flow impact) - Understand the internal impact of GST from a product pricing stand point, credit flows, lost credits, higher/lower taxes, impact on distribution supply chain, and on secondary sales (distributors and retailers)
  - Strategic - Understand opportunities or threats likely to be posed by GST, the potential impact on supply chain, the potential impact on vendors, and change in impact on alternate supply chain scenarios to optimize the impact of GST

Profiles of companies that should adopt it

- Manufacturers with supply chains in multiple states
- Large scale importers and traders
- Service providers with presence or client base across multiple states
- Mixed supply providers (developers/project owners and works contractors)

01 South African administration issues draft guidance on POEM

The South African Revenue Service recently published a draft interpretation note 6 (IN 6) on the concept of Place of Effective Management (POEM) for public comments.[1]

While the term POEM is not defined in the domestic tax law of South Africa, the IN 6 discusses the principles and guidelines to be applied to determine residency of companies under the domestic law of South Africa. The discussion covered in the IN 6 may not be relevant for unique business vehicles such as hybrid entities as well as new types of trusts.

The IN 6 acknowledges that the principles and guidelines are consistent with POEM used as a residency tie-breaker rule in Article 4(3) of tax treaties along the lines of OECD Model Commentary. Highlights of the draft IN 6 include:

- A company's POEM is the place where key management and commercial decisions that are necessary to conduct its business as a whole are made in substance. It is not the place where day-to-day management is undertaken.
- The POEM test is one of substance over form. It, therefore, requires the identification of those persons in a company who actually "call the shots" and exercise "realistic positive management."
- Key factors relevant for the determination of POEM include, illustratively: the location of the company's head office, where senior management takes key decisions, or place of board meeting; place of de facto (actual) authority, not de jure (legal) authority; change in telecommunications, information technology, global travel and modern business practices, etc.
- Factors such as location of support functions (e.g., data management, HR, customer support, accounting, etc.), legal factors (such as registration or incorporation of a company) and economic nexus may not be generally relevant in the determination of POEM. These factors may be given weight only where other factors are inconclusive.

1 South African Revenue Service website, www.sars.gov.za

Global news

02 Developments relating to "Digital Economy"

While the OECD works on its final report on Digital Economy (BEPS Action 1), countries around the world are attempting to reform their tax rules to be able to tax part of the profits made by digital companies. After the enactment of the UK's new Diverted Profits Tax (DPT), and a French report on the taxation of the Digital Economy, the following countries have taken steps to tackle the challenges:

- On 2 April 2015, the Tax Authority of Israel published a draft circular regarding services provided by foreign corporations to Israeli clients via the internet, addressing related income tax and value added tax implications.[2] The circular, inter alia, states that:
  - Corporations that have a "significant digital presence" in Israel may be subject to tax in Israel.
  - In cases where a foreign corporation's core activity is conducted through the internet, and some or all of certain terms (such as the internet site's connection with the Israeli market) are found to exist, the corporation's activity should constitute a permanent establishment (PE) in Israel.
  - Regarding foreign companies providing services in Israel through the internet, the circular lays down certain conditions (e.g., high usage of website by Israeli users, substantial marketing/support functions undertaken in Israel, etc.) based on which a PE can be deemed to exist in Israel.
  - The circular also lays down guidance in relation to dependent agent PE and attribution of profits to a PE.
- Based on news published in the Italian press on 24 April 2015, the Government of **Italy**[3] is considering the introduction of a 25% withholding tax (WHT) on certain virtual transactions. It covers the virtual presence of foreign MNCs selling into the Italian market without a physical structure falling within the traditional definition of PE. The WHT would be applied on the assumption of the presence of a virtual PE based on "significant digital presence." It would be triggered when the "presence" exceeds, in terms of payments, a certain threshold, which in terms of the proposed rule is €1 million within a period of six months. The WHT will be levied by banks and financial intermediaries on payments to foreign MNCs in connection with transactions with Italian customers. The proposed tax, to be introduced as part of a major tax reform in Italy, is yet to be implemented.
- After the introduction of the DPT in the UK, **Australia** had announced its intention to pursue a similar measure. In May 2015, as part of its annual budget, Australia released a multinational anti-avoidance law, intended to tackle perceived tax avoidance by MNCs. The law has measures clearly directed at US technology companies, but will inevitably sweep up many other foreign enterprises operating in the Australian market.[4] Notably, the change does not create a new tax similar to the UK's DPT. Where the rule applies, Australian income tax may be assessed as though the non-resident did have a PE in Australia, together with harsh penalties (including 100% of the unpaid tax plus interest), and will also override Australia's treaty obligations. Further, the Australian budget extends the levying of the Goods and Services Tax to sale of digital products and services in Australia by offshore suppliers.

2 "Israeli Tax Authorities publish draft circular regarding internet activity of foreign companies in Israel", EY Global Tax Alert, dated 16 April 2015; www.taxanalyst.com

3 "Italy considers introduction of tax on digital activities", EY Global Alert dated 27 April 2015

4 www.ibfd.org

03 Proposed revisions to the US Model Income Tax Convention[5]

On 20 May, the US Treasury Department released proposed revisions to the US Model Income Tax Convention (US MC). These are intended to address changes in the global international tax environment in recent decades that have eroded the US tax base. The US MC is the US Government's baseline document used in treaty negotiations.

The proposed revisions to the US MC broadly include:

- **Subsequent changes in law:** Potential denial of treaty benefits upon subsequent changes in a country's tax law that result in: rates below 15% with respect to substantially all the income of resident companies; or provide an exemption from taxation to resident companies for substantially all foreign source income
- **Special tax regime:** Denial of treaty benefits to certain income items benefiting from a "special tax regime" (which provides a preferential effective tax rate) in the beneficial owner's country of residence, to generate stateless income or double non-taxation
- **Limitations-on-benefits (LOB):** Making certain modifications to the LOB article, including adding a "derivative benefits test;" the derivative benefits rule is based on a broader concept of ownership, generally applying to determine whether a holding company or financing entity qualifies for treaty benefits
- **Expatriated entities:** Denial of treaty benefits to US companies that change tax residence in a corporate inversion or expatriation transaction, and imposition of full US withholding taxes on dividends, interest, royalties and other income paid by US companies that are "expatriated entities"
- **Exempted PE:** Tightening of the "triangular provision" that would deny treaty benefits when certain income is attributable to a PE outside the beneficial owner's country of residence; the rules are intended to reduce BEPS by preventing residents of third countries from inappropriately obtaining the benefits of a bilateral tax treaty

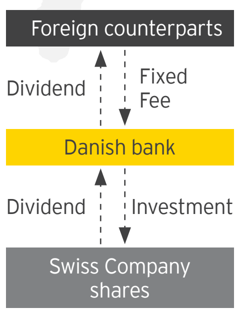
5 *"Recent US international tax developments", EY Global Tax Alert dated 21 May 2015*

Global news

04 Swiss Supreme Court (SC) rules on "beneficial ownership" in a derivative contract[6]

On 5 May 2015, the Swiss SC delivered its long-awaited judgments[7] in two cases concerning the application of the tax treaty concept of beneficial ownership to derivatives contracts over Swiss shares entered into by a Danish resident bank.

In 2007, a Danish resident bank concluded derivative contracts involving Swiss company shares. Under the arrangement, the Danish bank was, in particular, to pay to its foreign counterparts an amount corresponding to the dividends received in respect of the Swiss shares. The foreign banks invested in the underlying Swiss shares in order to hedge their positions and charged/retained a fixed fee in respect of services rendered.



The dividends received by the Danish bank on the Swiss shares were subjected to WHT in Switzerland at 35% under domestic laws. The Danish bank filed claims for a full refund of the WHT under the Denmark-Switzerland tax treaty (the Treaty), according to which the WHT rate was NIL.

Though the dividend article of the Treaty did not contain beneficial ownership requirement or any specific anti-abuse rule, the Swiss Federal Tax Administration (SFTA) denied beneficial ownership of the Danish bank. The SFTA considered that dividends received were substantially passed on by the bank to its counterparts, all of which were residents of third states that would not have obtained full refund of WHT.

The Swiss SC upheld the SFTA's view, confirming the rejection of the WHT refund due to lack of beneficial ownership of the Danish bank. It observed that:

- There also is an implicit beneficial ownership requirement in treaties that do not explicitly mention beneficial ownership.
- Beneficial ownership requires that the recipient of a dividend has an unconstrained right to use, enjoy and dispose of the dividend received. If the recipient has a legal or factual obligation to pass on the dividend received to a third party, beneficial ownership is denied.
- Furthermore, the beneficial owner must bear the economic risk of whether a dividend is distributed or not. Where such risk is passed on to a third party in a derivative contract, beneficial ownership is denied.
- The derivatives contracts entered into by the Danish bank were accurately matching their investment in the underlying shares, both in volume and timing. The Danish bank had an obligation to pass on the dividend received by it to foreign counterparts, so that both the risks and rewards of the investment in Swiss shares were substantially with the foreign counterparts and not with the Danish bank, which made only a small profit from these transactions. Accordingly, the Danish bank was not a beneficial owner of such dividend under the treaty.

6 *Source: www.taxanalyst.com; "Swiss Supreme Court issues long-awaited decisions in the "Denmark" derivatives cases", EY Global Tax Alert dated 7 May 2015*

7 *SC judgments 2C_364/2012, 2C_377/2012, and 2C_895/2012 of 5 May 2015*

EY Management Tools
Depreciation

Functionality of the tool

- Depreciation optimization is a holistic approach to optimize the claim of tax depreciation.
- It involves analyzing large capex data sets for appropriate classification of assets and applicability of appropriate depreciation rates for tax purposes, inter-alia, with the help of data analytics. The primary areas for potential tax savings include:
  - Identification of special category assets eligible for higher rate of depreciation being classified as generic plant and machinery
  - Identification of peripheral assets forming part of special category assets being classified as generic plant and machinery
  - Classification of assets based on their functional use to identify potential correct classification
  - Identification of Repairs & Maintenance expenditure which are being capitalized

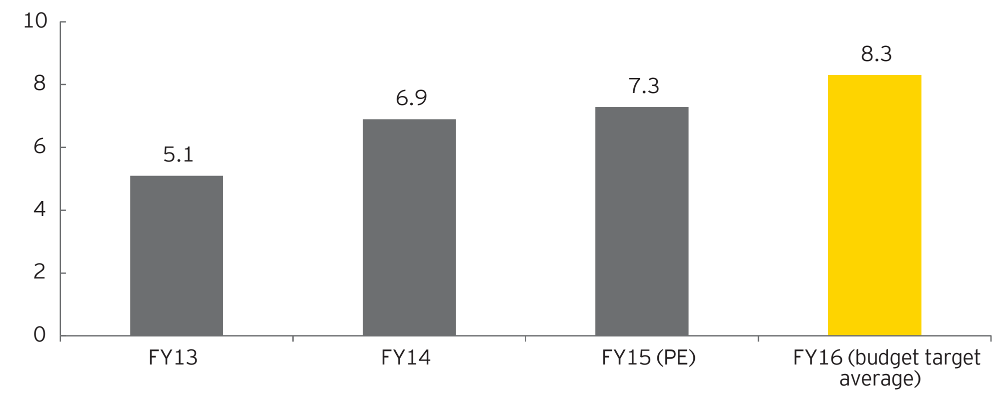
Benefits to the user

- Identification and appropriate categorization of assets that qualify for accelerated allowances, thereby generating cash tax savings; these benefits could be up to 100% of the value of eligible assets
- Provides insight for improving internal processes in tax function for appropriate categorization of project expenditure
- Combines tax technical knowledge, data analytics and technical/engineering teams to ensure a sharper output, which makes the tool unique
- Helps in creation of robust audit trail that accurately traces source data to tax depreciation claims on a line-by-line capital expense basis

Profiles of companies that should adopt it

- Companies that have incurred a capital expenditure or those that have a capital expenditure planned should look at adopting this tool.

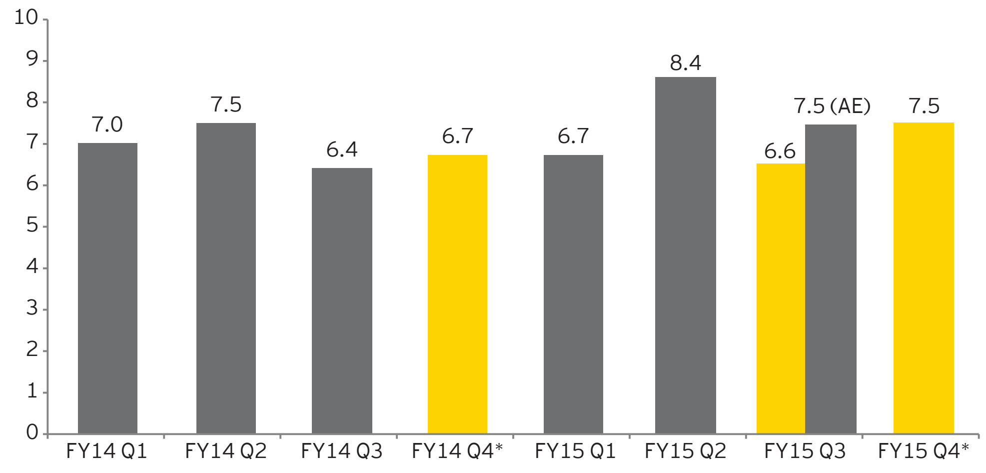
Chart 1: Economic growth (Gross Domestic Product at Market Prices (GDPMP), 2011-12 prices



Source: CSO, Ministry of Statistics and Plan Implementation, Government of India and Union Budget FY16 PE - Provisional Estimates

The Indian economy grew at 7.3% (2011-12 prices) in FY15, compared with 6.9% in FY14, as both domestic and external demand remained weak. Real GDP growth for FY15 has been revised downwards from 7.5% [based on Advance Estimates (AE)] to 7.3% [Provisional Estimates (PE)].

Chart 2: Quarterly economic growth (GDPMP, 2011-12 base)



Source: CSO, Ministry of Statistics and Plan Implementation, Government of India

GDP growth for 3QFY15 was revised downwards from 7.5% (AE) to 6.6% (PE), leading to a downward revision of overall GDP for FY15.

Table 1: Growth in components of aggregate demand (2011-12 base, % y-o-y)

	Private final consumption expenditure	Government final consumption expenditure	Gross capital formation	Exports	Imports	GDP at market prices
FY13	5.5	1.7	-0.3	6.7	6.0	5.1
FY14	6.2	8.2	3.0	7.3	-8.4	6.9
FY15	**6.3**	**6.6**	**4.6**	**-0.8**	**-2.1**	**7.3**
FY141Q	7.7	27.3	2.3	2.6	-3.5	7.0
FY142Q	5.6	5.3	6.3	-1.6	-8.4	7.5
FY143Q	4.6	11.0	5.3	15.7	-14.2	6.4
FY144Q	7.0	-7.2	-1.4	14.1	-7.0	6.7
FY151Q	6.2	1.6	8.7	9.1	-3.6	6.7
FY152Q	7.1	8.9	3.8	-2.0	1.1	8.4
FY153Q	**4.2**	**27.6**	**2.4**	**-0.3**	**2.8**	**6.6**
FY154Q	**7.9**	**-7.9**	**4.1**	**-8.2**	**-8.7**	**7.5**

Source: CSO, Ministry of Statistics and Plan Implementation, Government of India | Data for 4QFY14 is derived based on the AE published by the CSO.

The CSO has lowered its estimates of private consumption expenditure growth for FY15 from 7.9% to 6.3% in its PE (6.2% in FY14), while exports of goods and services have fallen from 0.9% (AE) to 0.8% in PE (robust growth of 7.3% in FY14). External demand continues to remain subdued.

Table 2: Sectoral output growth at 2011-12 prices (% y-o-y)

	FY13	FY14	FY15 (AE)	FY15 Q1	FY15 Q2	FY15 Q3	FY15 Q4
Agriculture & allied activities	**1.2**	**3.7**	**0.2**	*2.6*	*2.1*	*-1.1*	*-1.4*
Industry	**2.3**	**4.5**	**6.1**	*7.7*	*7.6*	*3.6*	*5.6*
Mining and quarrying	-0.2	5.4	**2.4**	*4.3*	*1.4*	*1.5*	*2.3*
Manufacturing	6.2	5.3	**7.1**	*8.4*	*7.9*	*3.6*	*8.4*
Electricity, gas and water supply*	4.0	4.8	**7.9**	*10.1*	*8.7*	*8.7*	*4.2*
Construction	-4.3	2.5	**4.8**	*6.5*	*8.7*	*3.1*	*1.4*
Services	**8.0**	**9.1**	**10.2**	*8.7*	*10.4*	*12.5*	*9.2*
Trade, Transport and communications**	9.6	11.1	**10.7**	*12.1*	*8.9*	*7.4*	*14.1*
Finance, insurance, real estate and professional services	8.8	7.9	**11.5**	*9.3*	*13.5*	*13.3*	*10.2*
Pub. Admin., and defence	4.7	7.9	**7.2**	*2.8*	*7.1*	*19.7*	*0.1*
Total GVA at basic prices	**4.9**	**6.6**	**7.2**	*7.4*	*8.4*	*6.8*	*6.1*

Source: CSO, MOSPI, Economic Survey 2014-15 | *Includes other utility services | ** Includes repair, hotels and restaurants, and storage services

On the supply side, real GVA at basic prices grew by 7.2% in FY15, up from 6.6% in FY14, led by higher growth in services and industrial sector output. The growth in agricultural and allied activities (GVA) plummeted to 0.2% in FY15 compared with 3.7% growth in FY15.

Table 3: Inflation based on Consumer Price Index (new series): combined index for rural and urban areas (month over corresponding month of previous year: % change)

	General	Food, beverage	Pan, tobacco and intoxicants	Fuel and Lighting	Housing	Clothing, bedding and footwear	Miscellaneous
FY13	10.3	11.7	11.1	11.1	11.0	8.5	7.6
FY14	10.0	11.4	9.5	9.6	11.6	7.3	7.3
FY15	5.9	6.5	8.1	7.3	6.9	4.2	4.6
May 2014	8.3	8.9	7.6	8.4	13.7	4.7	6.7
Jun 2014	6.8	7.3	7.6	8.2	6.8	4.5	6.1
Jul 2014	7.4	8.7	7.7	8.3	6.6	4.3	6.0
Aug 2014	7.0	8.6	7.8	8.0	6.1	3.9	5.4
Sep 2014	5.6	6.3	7.9	7.3	5.8	3.4	4.3
Oct 2014	4.6	4.3	7.6	7.3	5.6	3.4	4.3
Nov 2014	3.3	2.0	8.0	6.9	5.4	3.5	3.7
Dec 2014	4.3	4.4	7.9	6.3	5.2	3.4	3.5
Jan 2015	5.2	6.3	8.3	6.2	5.1	3.8	3.1
Feb 2015	5.4	6.8	9.2	6.4	5.0	4.7	2.9
Mar 2015	5.2	6.2	9.2	6.3	4.8	5.1	3.0
Apr 2015	4.9	5.4	9.4	6.1	4.7	5.5	3.2
May 2015	5.0	5.1	9.5	6.1	4.6	6.0	3.8
Jun 2015	5.4	5.7	9.8	6.3	4.5	5.9	4.2

Source: Ministry of Statistics and Plan Implementation, Government of India

Consumer Price Index (CPI)-based inflation increased to 5.4% y-o-y in June 2015 after having remained sticky around 5% y-o-y during the last two months. Below average rainfall continues to pose upside risk to inflation. Benign global food and fuel inflation may act as a cushion if the Indian Government anticipates and imports well in advance to cope with likely shortages of specific food items.

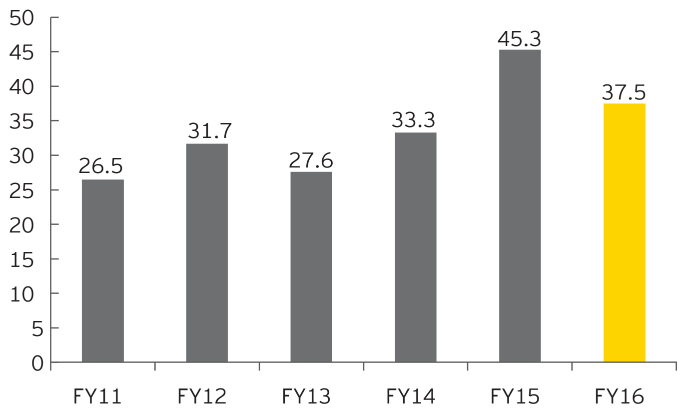
Table 4: Growth in Index of Industrial Production (major industries) (month over corresponding month of previous year: % change)

	General Index	Mining	Manufacturing	Electricity
FY12	2.9	-2.0	3.0	8.2
FY13	1.1	-2.3	1.3	4.0
FY14	-0.1	-0.6	-0.8	6.1
FY15	2.8	1.4	2.3	8.4
May 2014	5.6	2.5	5.9	6.7
Jun 2014	4.3	4.8	2.9	15.7
Jul 2014	0.9	0.1	-0.3	11.7
Aug 2014	0.5	1.2	-1.1	12.9
Sep 2014	2.6	0.1	2.7	3.9
Oct 2014	-2.7	4.5	-5.6	13.7
Nov 2014	5.2	4.0	4.7	10.0
Dec2014	3.6	-1.7	4.1	4.8
Jan 2015	2.8	-1.8	3.4	3.3
Feb 2015	4.8	1.6	5.1	5.9
Mar2015	2.5	1.1	2.8	2.0
Apr 2015	3.4	0.2	4.2	-0.5
May 2015	**2.7**	**2.8**	**2.2**	**6.0**

Source: Office of Economic Advisor, Government of India

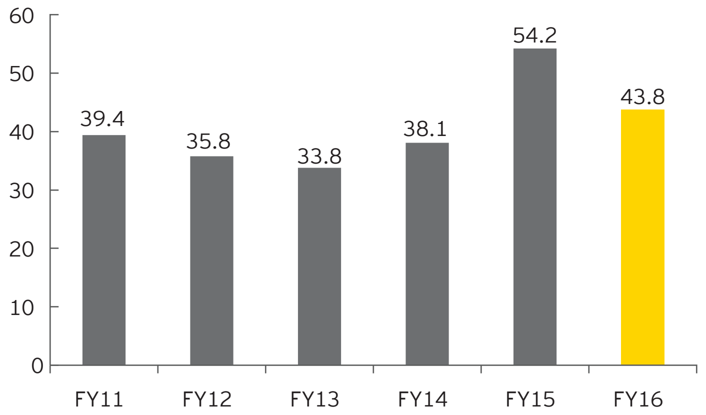
Industrial sector growth fell in May 2015 both in terms of the overall Index of Industrial Production (IIP) and that of the manufacturing sector. This shows that industrial recovery in India is still not robust.

Chart 4: Cumulated fiscal deficit Apr-May 2015 (as % of annual budgeted target for FY16)



Source: Controller General of Accounts, Government of India

Chart 5: Cumulated revenue deficit in Apr-May 2015 (as % of annual budgeted target for FY16)



Source: Controller General of Accounts, Government of India

Although the Central Government's cumulated fiscal as well as revenue deficit in the first two months of the current fiscal year continues to remain elevated, it is still an improvement over FY 15 levels during the corresponding period.

Table 5: Major heads of Central Government revenue (INR billion)

Revenue heads	FY14 actual	FY15 (PE)	FY16 (BE)	% change in FY15 PE over FY14 actual	% change in FY16 BE over FY15 PE
Gross revenue receipts	13,376	14,420	16,712	7.8	15.9
Tax revenue (including States' share)	11,387	12,450	14,495	9.3	16.4
Corporation tax	3,947	4,289	4,706	8.7	9.7
Taxes on income	2,429	2,584	3,274	6.4	26.7
Customs	1,721	1,880	2,083	9.3	10.8
Union excise duties	1,702	1,891	2,298	11.1	21.5
Service tax	1,548	1,680	2,098	8.5	24.9
Non-tax revenue	13,376	14,420	16,712	-1.0	12.6

Source: Union Budget, Controller General of Accounts | PE - Provisional Estimates, BE - Budget estimates

Central taxes are budgeted to grow at a much higher rate in FY16 compared with the growth in FY15.

Table 6: Major heads of Central Government expenditure (INR billion)

Expenditure Heads	FY14	FY15 (PE)	FY14 (BE)	% change in FY15 PE over FY14 actual	% change in FY16 BE over FY15 PR
Total expenditure	**15,594**	**16,448**	**17,775**	**5.5**	**8.1**
Non-plan	11,061	11,911	13,122	7.7	10.2
Plan	4,533	4,536	4,653	0.1	2.6
Revenue	13,718	14,577	15,360	6.3	5.4
Capital	1,877	1,870	2,414	-0.4	29.1

Source: Union Budget documents

The total Central Government expenditure budgeted at 12.6% of GDP for FY16 is at a historical low because of resource crunch. In its attempt to revive investment demand in the economy, the Government has budgeted to increase capital spending by 29.1% in FY16 relative to spending growth of just 5.4% in FY15.

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Thoughts

If your business is not on the Internet, then your business will be out of business

Bill Gates

Technology is nothing. What's important is that you have a faith in people, that they're basically good and smart, and if you give them tools, they'll do wonderful things with them

Steve Jobs

We cannot solve problems with the same thinking we used when we created them

Albert Einstein

Technology is anything that was not around when you were born

Alan Kay

Any sufficiently advanced technology is indistinguishable from magic

Arthur C. Clarke

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