



India signs the third Protocol with Singapore to amend India-Singapore tax treaty

Background

Recently, the Government of India has signed the third Protocol with Singapore amending the India-Singapore tax treaty (tax treaty). This is in line with India's treaty policy to prevent double non-taxation, curb revenue loss and check the menace of black money through automatic exchange of information, as reflected in India's recently revised tax treaties with Mauritius and Cyprus and the joint declaration signed with Switzerland.

On 30 December 2016, the Government of Singapore¹ has issued the text of the Protocol amending the third Protocol to the tax treaty. The key highlights of the Protocol are summarised as follows:

Effective date

India and Singapore shall notify the Protocol after completion of the respective procedure. The Protocol shall enter into force on the date of the later of these notifications. If Protocol does not enter into force as at 31 March 2017 due to either of the aforesaid notifications remaining pending, the Protocol shall enter into force on 1 April 2017.

Capital gains

- Investments in shares made before 1 April 2017 have been grandfathered. Accordingly, gains from alienation of shares acquired before 1 April 2017 shall remain taxable only in the residence state of the alienator.

- Gains from alienation of shares acquired on or after 1 April 2017 in a company which is a resident of a contracting state may be taxed in that state. Further, a two year transition period from 1 April 2017 to 31 March 2019 has been provided during which capital gains on shares will be taxed in source country at 50 per cent of tax rate applicable on such gains in that state.

Limitation of Benefit clause

The earlier Protocol is amended with effect from 1 April 2017 as follows:

- The benefits of capital gain under the tax treaty shall not be available if the affairs were arranged with the primary purpose to take advantage of such benefits².
- A shell or conduit company shall not be entitled to the benefits of the tax treaty. A shell or conduit company is any legal entity falling within the definition of resident with negligible or nil business operations or with no real and continuous business activities carried out in that contracting state.

Where shares acquired before 1 April 2017

- A resident of a state is deemed to be a shell or conduit company if its annual expenditure on operations in that state is less than SGD200000

¹ Protocol to the India-Singapore tax treaty –Taxesutra.com
The Protocol shall form an integral part of the tax treaty and shall remain in force as long as the tax treaty remains in force and shall apply as long as the tax treaty itself is applicable

² This clause remains same under the new Protocol

in Singapore or INR 5,000,000 in India, as the case may be, for each of the 12 month periods in the immediately preceding period of 24 months from the date on which the gains arise.

Where shares acquired after 1 April 2017

- A resident of a state is deemed to be a shell or conduit company if its annual expenditure on operations in that state is less than SGD200000 in Singapore or INR 5,000,000 in India, as the case may be, for the immediately preceding period of 12 months from the date on which the gains arise.
- A resident of a contracting state is deemed not to be a shell or conduit company if:
 - it is listed on a recognised stock exchange of the contracting state; or
 - its annual expenditure on operations in that state is equal to or more than SGD200,000 in Singapore or Indian Rs.5,000,000 in India, as the case may be:
 - (i) in case of shares acquired before 1 April 2017, for each of the 12 month periods in the immediately preceding period of 24 months from the date on which the gains arise;
 - (ii) in the case of shares acquired after 1 April 2017, for the immediately preceding period of 12 months from the date on which the gains arise.
- The meaning of the term recognised stock exchange has been provided as follows:
 - in the case of Singapore, the securities market operated by the Singapore Exchange Limited, Singapore Exchange Securities Trading Limited and The Central Depository (Pte) Limited.
 - in the case of India, a stock exchange recognised by the Securities and Exchange Board of India.

Associated Enterprise

Article 9 on Associated Enterprises has been amended to provide that both countries shall enter into bilateral discussions for elimination of double taxation arising from transfer pricing or pricing of related party transactions. An appropriate adjustment may be made in the profits of Associated Enterprise (AE) in the other contracting state where an adjustment has been made by a country to profits

of a resident, based on arm's length condition and taxes are levied on such profits adjusted. And such profits are also taxed in the hands of AE in the other contracting state.

Overriding provision

The tax treaty shall not prevent a contracting state from applying its domestic law and measures concerning the prevention of tax avoidance or tax evasion. From India perspective, the tax treaty may be subject to the provisions of General Anti Avoidance Rule (GAAR) and other domestic anti avoidance rules.

Our comments

In line with the amended India-Mauritius tax treaty, India and Singapore have amended the tax treaty with effect from 1 April 2017 to provide source based taxation of capital gains arising from transfer of shares in a company as against residence based taxation of capital gains.

The Protocol also grandfathers and continues to retain residence-based taxation in respect of shares acquired prior to 1 April 2017 while providing reduced taxation in transitory period of 1 April 2017 to 31 March 2019. However, both these reliefs are subject to the conditions prescribed under Limitation of Benefit (LOB) article. Source-based taxation in India will be in respect of shares of a company resident in India and will not extend to any other securities. Unlike the earlier Protocol, the modified LOB conditions are not made applicable in respect of capital gains arising from transfer of assets other than shares of a company resident in India. This will provide certainty to investors as well as smooth transition to a new regime.

The amendments also facilitate MAP in Transfer Pricing cases with Singapore, in line with BEPS minimum standards. This amendment is in line with India's commitment made as part of Article 14 on dispute resolution mechanism of OECD's BEPS project and it requires for both the countries to enter into bilateral discussions for elimination of double taxation arising from transfer pricing or pricing of related party transactions.

The Protocol also states that the tax treaty shall not prevent a country from applying its domestic law and measures concerning the prevention of tax avoidance or tax evasion. Accordingly, the tax treaty may be subject to the provisions of GAAR and other anti-avoidance provisions under the Income-tax Act, 1961.

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