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Tax Flash News

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NITI Aayog recommends presumptive taxation regime for foreign taxpayers to mitigate disputes regarding Permanent Establishment and Profit Attribution

Executive summary

NITI Aayog—the Government of India's public policy think tank—established a Consultative Group on Tax Policy. On 3 October 2025, the Group released a paper titled "*Enhancing Certainty, Transparency, and Uniformity in Permanent Establishment and Profit Attribution for Foreign Investors in India*"[1] (the paper).

The paper highlights that evolving views on Permanent Establishment (PE), challenges in profit attribution, and the impact on past years taxation may deter investment. Accordingly, it has recommended introduction of an optional industry-specific presumptive taxation scheme for foreign taxpayers.

The proposed presumptive taxation scheme allows foreign taxpayers to pay tax on India-sourced gross receipts at prescribed industry-specific profit rates, avoiding disputes over PE status and profit attribution. Alternatively, they can opt out and file returns using audited financials if their actual India-related profits are lower.

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[1] Tax_Policy_Report_WEB.pdf – accessed on 3 October 2025

The paper proposes deemed profit rates for various sectors such as 10 per cent for infrastructure, Engineering Procurement and Construction (EPC) contracts, and engineering and oilfield services, 30 per cent for digital and e-commerce, 20 per cent for consultancy services and 15 per cent for marketing and distribution support.

This Flash News captures some of the significant points from the paper.

Background

The existence of taxable presence in India, such as through a PE or Significant Economic Presence (SEP) can trigger substantial and unforeseen tax liabilities and compliance obligations — such as maintaining books of accounts, filing tax returns, and facing audits — thereby deterring foreign investments. Opportunity cost for prolonged tax disputes is immense as management attention is diverted, strategic decisions are delayed or foregone, and capital is locked up in contingent liabilities.

Foreign investors face significant tax uncertainty and compliance burden due to challenges surrounding PE determination and profit attribution. The profit attribution remains inconsistent, with varied approaches like global profit ratios and the 'separate enterprise' fiction with mixed application of Arm's Length Principle (ALP). India's active participation in global tax reforms (BEPS[2], Pillar One and Pillar Two) aims to curb tax avoidance but also introduces new complexities for foreign investors.

Evolution of PE and profit attribution jurisprudence in India

India's jurisprudence on PE has evolved significantly, mirroring its transition into a capital-importing nation that prioritises source-based taxation. Instead of focusing only on physical presence, India now aims to tax the real economic value created within its borders.

Attribution of profits to India PE has been subject to litigation over the years, primarily due to the absence of specific provisions under the Act, which often led tax officers to resort to rough estimates under Rule 10[3] of the Income-tax Rules, 1962.

[2] Base Erosion and Profit Shifting initiative of OECD

[3] Determination of income in the case of non-residents accruing or arising to any non-resident person through or from any business connection in India

To reduce inconsistency, the CBDT[4] Committee in 2019 proposed amendments to Rule 10 (CBDT draft rules)[5] by introducing a semi-formulaic approach:

- *Three factor apportionment* where profits are attributed based on sales, employees, and assets, equally weighted, ensuring sales (market) received a fixed one-third weight.
- *User-based factor for digital model* to be added, with 10 or 20 per cent weight for 'users' in India.
- *Minimum profit threshold*, where the formula would be applied on 'profits derived from India' defined as at least two per cent of Indian revenue.
- *Compensation for existing transfer pricing adjustments*, crediting profits already taxed via transfer pricing to avoid double taxation.

Though the PE attribution may standardise, perhaps around the 15 to 25 per cent effective range for typical cases, however, uncertainty may still persist because the facts of each case differ, and without a binding rule, both taxpayers and tax officers have leeway to argue their side.

Case for presumptive taxation

Although the OECD traditionally prefers functional analysis, especially for large taxpayers, it acknowledges that safe harbours and simplified approaches can ease compliance burdens, particularly for smaller entities.

India has already implemented presumptive taxation for non-residents operating in specific sectors, reflecting a pragmatic and incremental approach to tax policy.

The paper highlights the key advantages of adopting a presumptive taxation regime such as reducing litigation, promoting predictability, eliminating the need for tax audits and extensive documentation.

Overview of the proposed presumptive taxation scheme

- *Industry-specific rates*: Presumptive profit rates (i.e., a deemed profit percentage on gross receipts earned in India) should be set for specific sectors, based on historical data and industry trends and a margin of safety to protect revenue. The CBDT

[4] Central Board of Direct Taxes
[5] CBDT Proposal for Amendment of Rules For Profit Attribution To Permanent Establishment (dated 18 April 2019)

may be empowered to prescribe rates and conditions *via* notification to ensure flexibility and responsiveness to evolving business models. The scheme should be periodically reviewed (say, every 5 to 10 years) to ensure alignment with economic reality and international tax reforms.

- *No separate PE determination needed (Safe Harbour):* If a foreign company opts for presumptive taxation, the Indian tax authorities should not litigate PE existence for that activity.
- *Rebuttable framework*: The scheme should allow opt-out for foreign companies with genuinely lower margins. Optional nature of the scheme should help mitigate treaty non-discrimination issues. India may also consider negotiating with major treaty partners to include clauses or protocols acknowledging the presumptive taxation regime.
- *Administrative simplicity*: For those opting-in, compliance should be straightforward, with exemptions from detailed account maintenance for those activities. For those opting-out and claiming lower profits should be required to maintain and get audited India-related books of account. At the same time, its abuse should be prevented by including a multi-year lock-in provisions, thereby restricting frequent switching between opting in and out.
- *Exclusive tax scope*: Income taxed under the presumptive regime should not be subject to any other provisions of the Act that could yield a higher tax.
- *Scope of activities and nexus*: The scheme should clearly enumerate activities and income types covered by each presumptive rate, aligning with common dispute scenarios such as construction/ EPC projects, provision of services, royalty/ technology-intensive sectors, and digital/e-commerce streams.

Illustrative presumptive profit rates for select industries

Industry/ Sector	Proposed Presumptive Profit Rate (on gross receipts)	Rationale
Infrastructure Construction/ EPC	10 per cent	Aligned with existing rate under the Act for power project construction
Engineering Services/ Oilfield Services	10 per cent	Aligned with existing rate under the Act for oil/ gas service providers.

Industry/ Sector	Proposed Presumptive Profit Rate (on gross receipts)	Rationale
Telecom/Technology Equipment Supply with Installation	5 per cent (supply portion) 20 per cent (services portion)	Recognises lower profit margins on offshore equipment supply and higher margins for onshore services/ installation to avoid litigation over contract splitting.
Digital / E-commerce (Online platforms, Streaming, etc.)	30 per cent of gross revenue from Indian users	Reflects generally high profit ratios in digital businesses.
General Services (Consultancy, Management, Software)	20 per cent of gross fees	Aligned with existing rate under the Act for specific electronics services
Marketing and Distribution Support	15 per cent of gross revenue from India	A moderate rate between extremes, acknowledging the critical role of Indian marketing operations.

These are provisional rates and aim to initiate discussion. These rates need to be reviewed and revised periodically by an expert panel appointed by CBDT to align them with economic realities.

Other proposals

- *Safe harbour for PE attribution*: Scope of existing safe harbour provisions[6] should be expanded to include transaction and remuneration approaches, along with arm's length rates for PE attribution.
- *Advanced Pricing Agreement (APA) for PE attribution:* Bilateral APA negotiations for PE attribution should be promoted, especially for foreign enterprises with branches or project offices in India. Clarity on access and procedure for multilateral Mutual Acceptance Procedure (MAP) or APA in triangular structures, involving more than two jurisdictions, is also crucial to reduce double taxation and enhance certainty for multinational groups with integrated operations.
- *Treaty eligibility for US LLCs:* Treaty eligibility under the India-USA tax treaty should be explicitly extended to fiscally transparent US LLCs that meet Limitation of Benefits criteria under the tax treaty, facilitating dispute resolution access to APA and MAP mechanisms for such entities.

[6] Section 92CB

Next steps

The paper recommends that the Ministry of Finance evaluate these proposals and consider establishing a dedicated working group to draft the necessary legal provisions. This process should include consultation with relevant stakeholders, such as industry bodies, tax professionals, and treaty partners. Given the existing framework—including presumptive taxation measures for certain sectors and CBDT draft rules on profit attribution—the current environment is well-suited for the introduction of a comprehensive presumptive taxation regime.

Our comments

The involvement of government policy think-tank such as NITI Aayog in addressing tax matters related to non-resident taxpayers is a positive development. This engagement is expected to encourage further policy-level dialogue on taxation issues. Attention will now turn to the Finance Ministry's response to these recommendations and the potential establishment of a working group for broader stakeholder consultation.

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