

India increases withholding, reporting and disclosure requirements for transactions involving Cyprus

November 1, 2013

In brief

As an anti-avoidance measure, the Indian government amended its domestic tax law in 2011 with respect to transactions with taxpayers located in certain tax jurisdictions.

The Indian revenue authorities on November 1 issued guidance specifying that it will add Cyprus to the list of jurisdictions covered by these regulations. The regulations prescribe the application of 30% (or higher) withholding tax for payments from India to Cyprus. The regulations also provide that an Indian entity will be subject to tax on any funds received from Cyprus unless the Indian taxpayer can explain the Cypriot person's source of those funds (including beneficial ownership).

This newsalert summarizes the new guidance and the impact on foreign investors doing business with India through an entity located in Cyprus.

In detail

The Indian revenue authorities on November 1 issued a press release indicating that Cyprus will be regarded as a 'notified jurisdiction' with respect to transactions entered into with India.

Under the tax treaty between India and Cyprus for avoidance of double taxation of income and prevention of fiscal evasion, which has been in force since December 21, 1994, both India and Cyprus have an obligation to exchange such information as is necessary for carrying out the provisions of the tax treaty or enforcing the domestic tax laws

of the two jurisdictions, particularly as they relate to the prevention of fraud or evasion of taxes.

The press release states that the Cypriot authorities have not been providing the information requested by India under the tax treaty's exchange of information provisions. Therefore, India has designated Cyprus as a notified jurisdiction for purposes of certain transactions.

The consequences of this designation are that:

- transactions by Indian taxpayers with any person located in Cyprus will be

deemed to be transactions between related parties. As a result, they will be subject to Indian transfer pricing regulations applicable to cross-border related-party transactions, including the maintenance of documentation

- deductions with respect to payments made to any financial institution in Cyprus will be granted only if the Indian taxpayer provides an authorization, in a prescribed form, that permits the Indian revenue authorities to seek certain

information from the Cypriot financial institution. If this information is not provided, the deduction will be denied

- deductions with respect to any other expenditure or allowance arising from transactions with any person located in Cyprus will be allowed only if the Indian taxpayer maintains and provides the Indian revenue authorities with certain prescribed information ¹
- if any sum is received from a person located in Cyprus, the burden of proof will be on the Indian taxpayer to satisfactorily explain the money's source for the Cypriot person or its beneficial owner. If the Indian taxpayer fails to meet this burden, the amount

will be deemed to be income of the Indian taxpayer

- any payment made to a person located in Cyprus will be liable for withholding tax at 30% or the rate prescribed under Indian domestic tax law, whichever is higher.

The takeaway

Foreign investors doing business with India through an entity located in Cyprus could be subject to high tax withholding on payments both from India and sent into India. In addition, foreign investors could face increased reporting and disclosure requirements as a result of the above decision by the Indian revenue authorities. Certain details of the new guidance, such as expense limitation and tax withholding with respect to payments

to Cypriot entities, are likely to add pressure to cross-border transactions as well.

The new guidance also signals that the Indian revenue authorities are focused on information exchange between jurisdictions and also may be looking at more substantive issues regarding parties in various jurisdictions that are engaging in transactions with India.

Taxpayers should wait to see how the Cyprus revenue authorities respond to the new guidance. Taxpayers also should watch for further guidance from the Indian tax authorities relating to other jurisdictions that are commonly used for investing into India.

¹ The documentation requirements, in addition to the documentation required for transfer pricing documentation purposes, are: (a) a description of the ownership structure of the specified person (i.e., the Cypriot person in this case), including name and address of individuals or other entities, whether located in the notified jurisdictional area (i.e., Cyprus) or outside, having directly or indirectly more than 10% shareholding or ownership interests; (b) a profile of the multinational group of which the specified person is a part along with the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom the Indian taxpayer has entered into a transaction, and ownership linkage among them; (c) a broad description of the business of the specified person and the industry in which it operates; (d) any other information, data, or document that may be relevant for the transaction with the specified person .

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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