



## India meets Luxembourg

September 24 to October 3, 2009

Under the auspices of  
Mr. Jim Penning, Honorary Consul General of India

# Double Taxation Avoidance Treaty between India and Luxembourg

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IBCL

DTA – Luxembourg / India

October 1, 2009



# Agenda/Contents

Business Drivers

DTA Luxembourg / India

Examples of Structures

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Business Drivers

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Examples of Structures

## Objectives:

**Avoidance** of double taxation

**Prevention** of fiscal evasion

– on taxes on income and capital

with a view to **promote** economic co-operation

## Coverage

### **India:**

Income-tax

wealth tax

including any surcharge thereon.

### **Luxembourg:**

Income tax on individuals,

corporation tax, capital tax, and the communal trade tax.

*The treaty does not apply to 1929 holding companies and a few others which get preferential tax treatment.*

## The Journey -

1992	Initiation
1999	State Visit
2002	Embassy in New Delhi
Oct 2005	First round
April 2006	Resumed
April 2007	Second round
Feb 2008	In-principle agreement, Indian cabinet approved on Feb 21, 2008
June 2008	Signed by India and Luxembourg
May 2009	Ratified by Luxembourg Parliament
July 2009	Entered into force.

# Promotion of Economic co-operation under a Tax Convention

**Permanent Establishment** – profits attributable to it.

## **Capital**

Equity - Dividends

Debts – Interest

**Investment** in moveable or Immoveable properties

**Technology** - Royalties

**Skills** – Directors’ fees, Salary, Pensions

**Knowledge** – Professors, Teachers, Research Scholars, Students

**Others** – Shipping and Air Transport, Artists and Sportsperson, Other Income  
Members of Diplomatic missions and consular posts.



## Other Models for Economic Co-operation

Preferential Tariff Agreements

Free Trade Agreements (ASEAN, EU, IBSA)

Free Trade Area (e.g SAFTA, BIMSTEC)

Comprehensive Economic Cooperation Agreement (Singapore, Korea)

# Selection of a Treaty Convention:

**OECD Model**

**UN Model**

**Developments :**

OECD 1977, 2000, July 2005, draft 2008

UN 2001

How they relate to each other?

## Economic Co-operation

Bilateral trade in Goods – € 40 mn

Trade in services – not publicly available.

- 149 Indian companies listed on the Luxembourg stock exchange
- No presence of Indian banks in Luxembourg

## Foreign Direct Investments

Outbound to India : € 60 million

Inbound from India: € 13 million

*(2000 to 2008, Govt. of India)*

# Trade in Goods

## EXPORTS

Machinery	€ 18mn
Base Metal	€ 9mn
Plastics, rubber	€ 0,4mn
Textiles	€ 0,2mn
Articles of Stone	€ 0,2mn
Precision Instruments	€ 0,1mn
 	<hr/>
Total (approx)	€ 27mn
	<hr/>

## IMPORTS

Textiles	€ 5mn
Base Metals	€ 3mn
Machinery	€ 3mn
Chemicals	€ 0,9mn
Plastics, rubber	€ 0,2mn
 	<hr/>
	€ 12mn
	<hr/>

## Fiscal Evasion – an assessment

Globally, offshore evasion estimated at USD 7 trillions.

EU: tax evasion estimated at 2-2.25% of GDP

India: Estimates of tax evasion have varied between USD 600 billion and USD 1400 billion.

No known trade dispute between India and Luxembourg. India Mauritius Treaty - apprehension lingers - Low Tax Country.

Laws in place –

Luxembourg : Directive 2005/60/EC; The law of 12 November 2004.

India: Prevention of Money Laundering Act, 2002 came into effect from 1 July 2005.

# Banking Transparency

“All countries have some form of bank secrecy. What is important is that it can be lifted in well defined circumstances” OECD – Countering Offshore Tax Evasion

## LUXEMBOURG

- 150 banks with traditional obligations
- In mid 2009 proactively aligned with latest OECD standards to come on to “White List” by signing 12th tax information exchange agreement.
- No “fishing” expeditions
- Equivalent to Paragraph 5 of Articles 26 being accepted – in new DTAs – the older ones being updated.

## INDIA

- Banking Secrecy could be lifted under judicial or administrative orders
- Banking Secrecy Act (date not mentioned on RBI website)
- Central Bank - Reserve Bank of India have a close oversight on the entire operations of any bank operating within India.

# Way Forward

Entry into force

Validity – minimum 5 years

## **New developments –**

Social Service Security Agreement

Implication of Direct Tax Code

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## DTA Luxembourg / India

- Signed on 2 June 2008
- In force since 9 July 2009
- Applicable as of 1 January 2010 in Luxembourg
- Applicable as of 1 April 2010 in India

## DTA Article 5 - PE

### Wider PE definition:

- Sales outlets
- Warehouses in relation to a person providing storage facilities for others
- A farm, plantation or other place where agricultural, forestry, plantation or related activities are carried on
- Building site or construction, installation or assembly project or supervisory activities in connection therewith if they last for more than 9 months
- The furnishing of services (incl. consultancy services), if provided for more than 183 days within any 12 months period
- Insurance companies
- Dependent agent definition, including delivery of goods and securing orders

## DTA Article 10 & 11 – Dividends & Interest

- Dividends: only one Withholding Tax rate of 10%
- Interest: 10% of the gross amount of the interests
  - Departure from OECD model: interests paid to a government, a political sub-division or a local authority shall only be taxed in the beneficiary's state

## DTA Article 12 – Royalties and Fees for Technical Services

- Most DTAs concluded by Luxembourg apply a different treatment to technical services remunerations – they usually fall within articles on business profits or on independent personal services.
- In departure from the OECD model convention, the DTA shares taxation rights for royalties and technical services (incl. managerial and consulting services) between source State (10%) and beneficiary State.

## DTA Article 13 - Capital Gains

### Sale of a participation:

- India retains the right to taxation on capital gains realised on the sale of a participation in an Indian subsidiary

## DTA Articles 14 & 15

- Article 14 – Independent personal services
  - Article deleted from OECD MC / present in UN MC
- Article 15 - Dependent personal services
- Both articles provide for taxation in the state where residency exceeds an aggregate of 183 days in any period of 12 months

## DTA Article 24 - Tax Credit / Tax Exemption

- India generally applies the tax credit method
- Luxembourg usually applies the exemption method
  - Tax credits are applicable for dividends, interests and royalties and fees for technical services

## Business Drivers – Tax Rationale

### Why use a holding company?

#### INVESTING FROM INDIA TO LUXEMBOURG

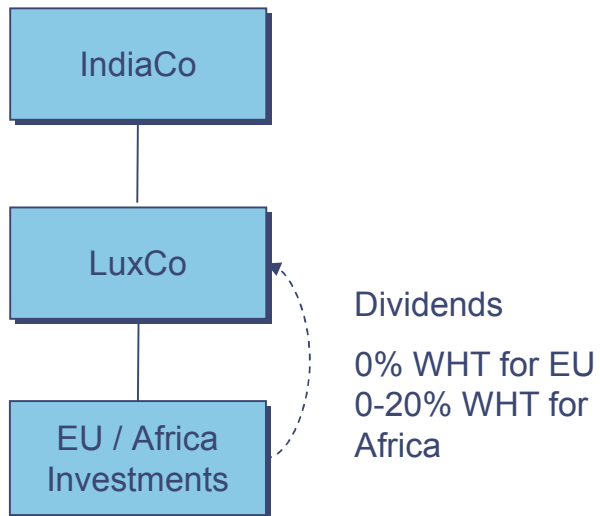
- Dividend income of Indian corporate shareholders from foreign companies taxed in India at high rate: 33.66%
- Long / short term capital gains by Indian shareholders from sales of shares in foreign companies taxed at high rates 22.44% - 33.66%
- High rates make it imperative for Indian entrepreneurs to look for tax efficient jurisdiction to locate holding companies

#### INVESTING FROM LUXEMBOURG TO INDIA

- DTAs entered into by India to be analysed to identify tax efficient jurisdiction
- Beneficial withholding rates



## Holding structures (outbound)



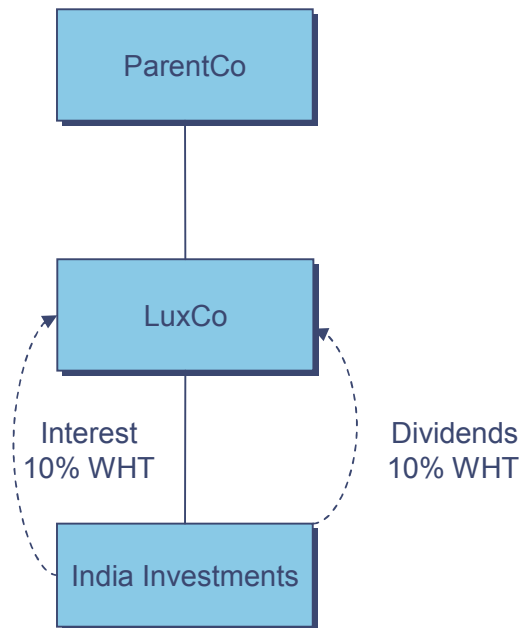
### Objective

- Tax optimization and investment through Luxembourg

### Tax benefits

- No WHT on dividends paid from EU to Lux. Dividends from EU / African entities / capital gains on the disposal on EU / African entities should be tax exempt in Luxembourg provided that the conditions of Luxembourg participation exemption regime are met
- Dividends will be retained in LuxCo

# Holding structures (inbound)



## Objectives

- Tax optimization for financing

## Tax benefits

- Loan is provided by LuxCo to India
- 10% WHT on interest from India to Luxembourg
- Low effective tax rate on interest in Luxembourg achievable (and tax credit)
- Max. 10% WHT on dividends paid from India to Luxembourg
- Dividends received by LuxCo should be tax exempt. India WHT tax not creditable in Luxembourg.

## Consideration

- Capital gains on disposal of India investments are also taxable in India based on DTT

## DTA Article 29 – Limitation of Benefits

- Exclude companies from the benefit of the DTA if the main reason for the creation for the company was to take advantage of the DTA
- Article is subjective

## DTA – Summary

Dividend distributed (art 10)	<ul style="list-style-type: none"> <li>• WHT of 10% based on DTT but no WHT applied in Luxembourg and India (based on internal law)</li> </ul>
Interest (art 11)	<ul style="list-style-type: none"> <li>• Interest taxable in the state of residency of the beneficiary</li> <li>• WHT of 10%; in principle, no WHT on interest in Luxembourg based on internal law</li> <li>• Exempt if the beneficiary is government, political divisions and certain banks and institutions</li> </ul>
Royalties (art 12)	<ul style="list-style-type: none"> <li>• Royalties taxable in the State of residency of the beneficiary;</li> <li>• 10% WHT according to treaty; in principle, no WHT on royalties in Luxembourg based on internal law</li> </ul>
Capital gains (art 13)	<ul style="list-style-type: none"> <li>• Capital gains from the disposal of shares of a company can be taxed in the state of residency of the company;</li> </ul>
Wealth (art 23)	<ul style="list-style-type: none"> <li>• Taxed in the State where the wealth is located;</li> </ul>
Elimination of double taxation (art 24)	<ul style="list-style-type: none"> <li>• In the case of India:             <ul style="list-style-type: none"> <li>➢ Deduction from the India tax of the amount of tax paid in Luxembourg is allowable</li> </ul> </li> <li>• In the case of Luxembourg:             <ul style="list-style-type: none"> <li>➢ For the income in accordance with article 10, 11, 12 and 17 (dividends, interests, royalties), deduction from the Luxembourg tax of the amount of tax paid in India is allowable (but see above for dividends);</li> <li>➢ For any other income, if it has been taxed in India, tax exemption is allowable in Luxembourg.</li> </ul> </li> </ul>
Limitation of Benefits (art 29 & 30)	<ul style="list-style-type: none"> <li>• Legal entities that do not have « bona fide business activities » should be excluded from this DTT</li> <li>• H29 companies are excluded from this DTT</li> </ul>

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