

China-India Protocol enters into force

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Executive summary

The Chinese Government announced on 9 July 2019 that the protocol amending the current China-India Income Tax Treaty (the Protocol) entered into force on 5 June 2019. The Protocol becomes effective on 1 January 2020 for China and 1 April 2020 for India.

Significant provisions in the Protocol include:

- ▶ Introduction of a fiscally transparent entity/arrangement concept (Article 1)
- ▶ Tie-breaker rule for a treaty residency determination for non-individual dual resident persons (Article 4)
- ▶ Clarifying the determination of permanent establishment (PE) (Article 5)
- ▶ Narrowing the scope of business profits (Article 7)
- ▶ Principal purpose test for the entitlement to benefits (Article 27A)

This Alert summarizes the key provisions of the Protocol.

Detailed discussion

Fiscally transparent entity/arrangement concept

Paragraph 2 of Article 1 is revised to provide that income derived by or through an entity or arrangement that is established in either Contracting State and that is treated as fiscally transparent under the tax law of either Contracting State will be considered to be income of a resident of a Contracting State only to the extent that the income is treated, for the purposes of taxation by that State, as the income of a resident of that State.

Tie-breaker rule for non-individual dual resident persons

Paragraph 3 of Article 4 provides that, in cases where a person other than an individual is a dual resident, the competent authorities of the two Contracting States will seek a determination by mutual agreement of the country of residence based on the place of effective management, the place of incorporation or otherwise constituted and any other relevant factors. In the absence of such agreement, the person will not be entitled to any treaty relief unless the competent authorities of the Contracting States agree on such relief.

Permanent establishment

Prior to the amendment by the Protocol, a Construction PE relating to a building site or construction, installation or assembly project or supervisory activities was determined in aggregate with other similar sites, projects or activities. The Protocol removes this aggregation rule. In addition, when

computing the 183-day threshold, the aggregation of the time spent on connected activities on the same project by one or more closely related enterprises is required, if each connected activity exceeds 30 days.

The Protocol also clarifies that a Service PE will exist if services continue for at least 183 days in any 12-month period. Further, the services for the same or connected projects are required to be aggregated.

With respect to a Dependent Agency PE, the Protocol extends the provision to include persons who:

- ▶ Habitually play the principal role leading to the conclusion of contracts that are routinely concluded without material modifications by the enterprise; or
- ▶ Habitually maintain a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise.

The Protocol also introduces the concept of “closely related enterprises” in denying independent agent status.

Business profits

The Protocol amends Paragraph 1 of Article 7 in which business profits of an enterprise are taxed only to the extent that the profits are attributable to the PE.

Entitlement to benefits

A new Article 27A is inserted, which provides that a benefit will be denied if obtaining the benefit under the treaty is one of the principle purposes of any arrangement or transaction that would result directly or indirectly in that benefit.

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EYG no. 003795-19Gbl

1508-1600216 NY
ED None

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