

SATURDAY INTERNATIONAL TAX GYAN !!!

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Australia-India Economic Cooperation & Trade Agreement (AI ECTA)

Relief provided in relation to tax on services provided by IT companies in Australia being taxed as royalty till now

Background:

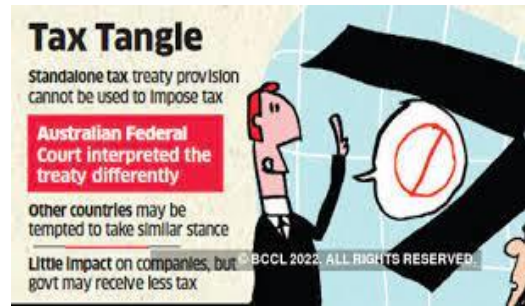
- ❖ Before this trade agreement between India and Australia, Australia considering DTAA has been taxing income generated from offshore IT services by Indian firms as **royalty**.
- ❖ **Australia has been taxing this income based on DTAA** between the countries entered in 1991 which is worded in such a way that Federal Court of Australia in a verdict against **Tech Mahindra in October 2018**, ruled that the payments received by an Indian company from its clients in Australia **will be taxed in Australia as 'royalty'**.
- ❖ **In the Judgement this income is considered as royalty as per Article 12(3)(g) of DTAA between India and Australia. Relevant extract is as below:**

3. The term "royalties" in this Article means payments or credits, whether periodical or not, and however described or computed, to the extent to which they are made as consideration for:

(g)	<p><i>the rendering of any services (including those of technical or other personnel), which make available technical knowledge, experience, skill, know-how or processes or consist of the development and transfer of a technical plan or design;</i></p> <p><i>but that term does not include payments or credits relating to services mentioned in sub-paragraphs (d) and (g) that are made;</i></p>
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In the Tech Mahindra's case law, the court have bifurcated clause (g) in two limbs one is related to "**Make available**" and other related to "**development and transfer**" and have considered the services provided by Tech Mahindra under the limb of Development and transfer of a technical plan or design and thus taxable as Royalty even if the knowledge is not made available to the client.

- ❖ Based on the judgement the Indian companies, especially in the IT services, were grappling with the consequences of this ruling for the past few years i.e., litigation, taxes in Australia, adverse impact on their businesses for rendering services and cash blocked in Australia.



- ❖ Therefore, to provide relief to companies **Australia-India Economic Cooperation and Trade Agreement is signed. It is a Free Trade Agreement (FTA) signed between both the countries.** FTA refers to arrangement made between two or more countries or trading confederations to reduce or eliminate custom tariffs or non-tariff barriers which hinders the trade between the countries.

Notification:

- ❖ On 02.04.2022, India and Australia signed Australia-India Economic Cooperation & Trade Agreement (AI ECTA) in which:
 1. Australia has agreed to amend Australian domestic law to stop the taxation of offshore income of Indian firms providing technical services to Australia.
 2. Australia will implement the amendments to its taxation legislation in a similar time period as the agreement.

Implications:

- ❖ Agreement will provide relief from royalty withholding tax on offshore IT services for Indian IT companies providing such services to Australian clients.

Our Comments:

- ❖ It has not been clarified whether the amendment is retrospective or prospective.
- ❖ The amendment/ clarification has been made in domestic law of Australia and hence no amendment is required to be made in the DTAA between India and Australia.

Minister for Trade, Tourism and Investment

Parliament House
CANBERRA ACT 2600

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2 April 2022

Shri Piyush Goyal
Honourable Minister of Commerce & Industry,
Consumer Affairs, Food & Public Distribution and Textiles
Government of India
Ministry of Commerce and Industry
Udyog Bhawan, New Delhi
110011, INDIA

Dear Minister Goyal



In connection with the signing of the Australia-India Economic Cooperation and Trade Agreement ("the Agreement"), I have the honour to confirm the following understandings reached between the Government of Australia and the Government of the Republic of India ("the Parties"):

1. The Government of Australia has agreed to amend Australian domestic taxation law to stop the taxation of offshore income of Indian firms providing technical services to Australia. This would resolve the issue that the Indian Government has raised about the Double Taxation Avoidance Agreement between the Government of the Republic of India and the Government of Australia for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, done at Canberra on 25 July 1991.
2. Australia will implement the amendments to its taxation legislation referred to in paragraph 1 in a similar time period as the Agreement.

I have the honour to propose that this letter and your letter in reply confirming that your Government shares these understandings, which will come into effect on the date on which the Agreement enters into force, shall constitute an integral part of the Agreement.

Your sincerely



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Stay Healthy! Stay Safe!
Thank you