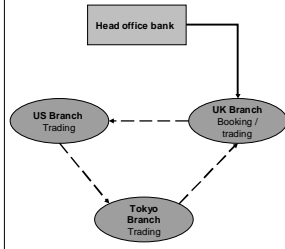


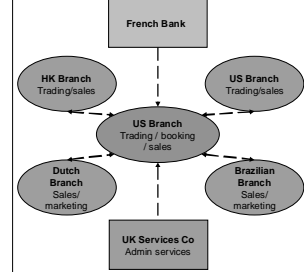
The Integrated Trading model

- > Book passes from one location to another
- > Trading authority may pass but not legal ownership of book
- > Location of book not indicative of where risk taking functions performed



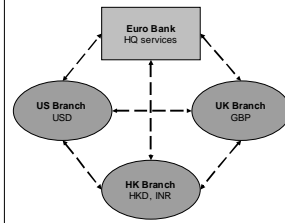
The Centralised Product Management model

- > All market risk centralised and managed in one location
- > Back-to-back transactions – partial risk transfer



The Separate Enterprise Trading model

- > Each location operates as a separate profit centre
- > Risks assumed and managed in one location
- > Overall trading limits set centrally



Principal functions and business processes...

Business Process / Functions/Risks	Pre-sales	Sales	Pricing and Structuring	Execution	Operations and Settlement	Risk management
Sales	→	→	→	→	→	→
Trading	→	→	→	→	→	→
Research	→	→	→	→	→	→
Middle office	→	→	→	→	→	→
Credit risk / Market risk management	→	→	→	→	→	→
Operations	→	→	→	→	→	→
Finance/Legal/Central Management	→	→	→	→	→	→
Systems/Capital	→	→	→	→	→	→

A number of income streams arise based on nature of activities...

- > Interest and dividends
- > Trading gains
- > Income from notional principal contracts & OTC derivatives
- > Fee income from distribution, underwriting & transaction structuring
- > Gains from dealing in liabilities
- > Income from stock lending and repo transactions
- > Broker fees from exchange transactions

Key tax issues

Global trading presents a number of challenges to traditional tax principles...

- Does a Permanent Establishment ('PE') exist:
 - Branch operations
 - Incorporated subsidiary which is an Associated Enterprise ('AE')
- Income attribution to the PE
- Transfer pricing methodologies
- Source of income
- Withholding tax
- Double or under taxation



Have the trading operations created a PE?

- Function of the legal operating structure adopted in each jurisdiction:
 - A branch is already a PE
 - An AE should not of itself ordinarily create a fixed place PE
- Also a function of the activities conducted in the particular jurisdiction; based on facts, activities conducted by AE could result in an Agency PE
- Does AE create a Dependent Agent PE ('DAPE') such that Host country has taxing rights over 2 different legal entities?
- DAPE v the "Hedge Fund" model
 - Morgan Stanley & Co vs DIT - Supreme Court [292 ITR 416]
 - DDIT vs SET Satellite (Singapore) PTE Ltd - ITAT Mumbai [106 ITD 175]



Computation of "profit"

- Profit computation is a function of:
 - Functions to be rewarded
 - Weighting of functions
 - Assessing the contribution of each location
 - Treatment of entities with tax losses
 - Treatment of regulated entities – their role in an Enterprise's overall business
 - Assets used and risks assumed
- Accounting basis – mark-to-market or accrual
- How are treasury revenues to be regarded?
- How are Support functions compensated
- Treatment of enterprise loss
- Implication of 'split hedges'



Profit attribution to the PE

- OECD authorised approach - Working hypothesis of a separate enterprise
- Key entrepreneurial risk taking functions
- Based on FAR analysis:
 - Functions
 - Assets
 - Tangible
 - Intangibles
 - Risks
 - Credit risk
 - Market risk
 - Operational risk
 - Others – legal, solvency
 - Capital
 - Regulatory capital
 - Economic capital
 - "Free" capital



Withholding tax

- Payments exchanged between branches and Head Office
- Characterisation of payments made to other branches for hedging purposes
 - Foreign currency swaps
 - Interest rate swaps
 - Credit derivatives
- Tax deductibility of such payments
 - ABN AMRO vs ADIT – ITAT Kolkata [250 ITR 117]
 - Dresdner Bank AG vs ACIT - ITAT Mumbai [108 ITD 375]



Challenges to introducing APAs / using MAP

- Multilateral rather than bi-lateral
- Pricing of risk models is presently proprietary to each institution
- Accounting for global trading is still evolving



