



**WESTERN INDIA REGIONAL COUNCIL OF  
THE INSTITUTE OF CHARTERED  
ACCOUNTANTS OF INDIA**

# Impact of Multilateral Instrument ("MLI") on Permanent Establishment

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## A New Report Claims Big Tech Companies Used Legal Loopholes to Avoid Over \$100 Billion in Taxes. What Does That Mean for the Industry's Future?

A new report about [Amazon](#), [Apple](#), Facebook, [Google](#), [Microsoft](#), and Netflix—nicknamed the "Silicon Six" by the non-profit Fair Tax Mark—claims a major gap in the taxes they might be expected to owe and how much they actually pay.

According to the report, between 2010 and 2019, using legal tax avoidance strategies that have become popular among corporations, the taxes paid collectively by the companies across all global territories in which they operate was \$155.3 billion less than what the actual tax rates would have required. When considering not just the cash paid but money put aside for future taxes, the gap was still \$100.2 billion.



## Govts may get more power to tax MNCs like Google, Facebook

*A global push by OECD to bring these digital giants under the ambit of local taxes.*

ET Bureau & Agencies | Last Updated: Oct 10, 2019, 08:23 AM IST



*Companies such as Facebook, Google, Twitter, LinkedIn and Airbnb have reached out to tax experts, seeking an opinion on the OECD proposals and its impact on their India revenues.*

Countries around the world, including India, will get more power to tax big multinationals such as [Google](#), Apple and [Facebook](#) doing business within their borders under a proposed overhaul of decades-old rules. The Organisation for Economic Co-operation and Development (OECD) has proposed to expand government rights to tax multinationals, especially big internet firms, by releasing a methodology for such taxation.

The development is a shot in the arm for India which has proposed its own regulations

## OECD proposal on taxing MNEs to benefit countries like India: Experts

*The proposal is aimed at re-allocating some profits and corresponding taxing rights to countries and jurisdictions where MNEs have their markets.*

PTI | Last Updated: Oct 13, 2019, 01:37 PM IST



*India's draft report on profit attribution gives weightage to sales and users as a factor for profit attribution.*

The OECD's proposal for taxing multinational enterprises (MNEs), including digital companies, based on consumer-facing activities or markets instead of their physical presence would benefit countries like [India](#) in terms of revenue, say experts.

The OECD Secretariat has published a public consultation paper to advance international negotiations to ensure large and highly profitable MNEs pay tax wherever they have significant consumer-facing activities and generate their profits.

**ET** **New vs Old Tax Slab Regime?**  
Know which one benefits you >

# Overview of BEPS AP

*A project by OECD/G20 Members, recommends measures under domestic law & tax treaties to address tax avoidance to realign taxation with economic substance & value creation*

## Coherence

- **Neutralising the effect of Hybrid Mismatch Arrangements (BEPS AP 2)**
- **CFC Rules (BEPS AP 3)**
- **Limit base erosion via Interest Deductions (BEPS AP 4)**
- **Counter Harmful Tax Practices (BEPS AP 5)**

## Substance

- **Preventing Tax Treaty Abuse (BEPS AP 6)**
- **Prevent artificial avoidance of PE Status (BEPS AP 7)**
- **TP Aspects of Intangibles (BEPS AP 8)**
- **TP/Risk and Capital (BEPS AP 9)**
- **TP/High Risk Transactions (BEPS AP 10)**

## Transparency

- **Establish methodologies to collect and analyse BEPS data (BEPS AP 11)**
- **Require taxpayers to disclose their aggressive tax planning arrangements ( BEPS AP 12)**
- **TP Documentation (BEPS AP 13)**
- **Making Dispute Resolution more effective (BEPS AP 14)**

**BEPS AP 1: Address Tax Challenges Arising from Digitalisation**

**BEPS AP 15: MLI developed to amend bilateral treaties to implement treaty related measures of BEPS AP**

# Overview of PE

**Significance of PE** – To determine rights of competing states to tax the business profits of the foreign enterprise and also tax passive income effectively connected with the PE

UN Model Convention	OCED / US Model Convention
Article 5(1) - Basic rule - Fixed Place PE	
Article 5(2) - Illustrative list of PEs - Inclusions to Fixed Place PE	
Article 5(3) - PE in relation to projects - Construction PE & Service PE	
Article 5(4) - List of exclusions - Exclusion from Fixed Base PE	
Article 5(5) - Dependent Agent – Agency PE	
Article 5(6) - Deemed PE for Insurance Business - Insurance Agency PE	No paragraph in OECD / US Model Convention for Insurance Agency PE
Article 5(7) - Independent agent - Agency PE	Article 5(6) - Independent agent - Agency PE
Article 5(8) - Associated enterprise - Subsidiary PE	Article 5(7) - Associated enterprise - Subsidiary PE
Article 5(9) - Meaning of Associated enterprise for the purpose of Article 5	Article 5(8) - Meaning of Associated enterprise for the purpose of Article 5

# Overview of BEPS AP 7

Present concept of PE (Article 5 of MC) revolves around “substantial and physical presence”

- Construction / Supervisory PE
- Presence through dependent agents or Commissionaire Arrangements

## BEPS AP 7: Objective and Recommendations

- Review and changes to the definition of PE - to prevent BEPS taking place through the use of tax avoidance strategies that circumvent the existing PE definition
- BEPS suggested updating definition of PE to avoid the following
  - Use of commissionaire and similar arrangements to avoid Dependent Agency PE
  - Exploitation of exemptions applicable for Preparatory and Auxiliary activities
  - **Fragmentation of activities** by MNEs to qualify for PE exceptions
  - **Splitting** up of contracts

# Adoption of BEPS AP No. 15 - MLI

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- **BEPS AP NO 15 - MLI** – adopted (Nov 2016) and signed (June 2017) by developed and developing economies around the world (including India) to implement tax treaty related measures to prevent BEPS
- **MLI** - Includes following recommendations:
  - BEPS AP 2- Neutralising the Effect of Hybrid Mismatch Arrangements;
  - BEPS AP 6- Prevention of Tax Treaty Abuse;
  - **BEPS AP 7- Preventing the Artificial Avoidance of Permanent Establishment Status;**
  - BEPS AP 14- Making Dispute Resolution Mechanisms more Effective
- **India ratified MLI and deposited ratified copy of MLI** with OECD Depository on 25 June 2019 – MLI effective for 29 Indian Tax Treaties w.e.f. 1 April 2020
- Recommendations under BEPS AP 7 adopted under MLI by way of:
  - **MLI Article 12:** Expanding scope of Agency PE
  - **MLI Article 13:** Restricting Preparatory and Auxiliary exemptions and introduction of Anti-fragmentation rules
  - **MLI Article 14:** Avoiding artificial splitting up of contracts



# MLI - Framework

## Minimum Standards

- All countries to meet certain minimum standards (BEPS AP 6 - Treaty Abuse; BEPS AP 14 – Dispute Resolution)
- No leeway to opt out of the minimum standards, except in limited cases

## Reservations

- Flexibility to opt out of a provision if it is not a minimum standard

## Optional provisions

- Option to choose among alternative provisions intended to address the same issue
- Both the countries to choose the same option in order for it to apply
- Possibility of asymmetric application in certain Art

## Compatibility clauses

- Defines the relationship / addresses conflict between the MLI and the provisions of a CTA
- MLI provision applies –
  - 'in place of'
  - 'applies to' or 'modifies'
  - 'in the absence of'
  - 'in place of or in the absence of' – *If notified by both CTA, then gets replaced, else supersedes*

*To be notified by both CTA*

## Notification clauses

- Notify choice of optional provision
- Also, notify the existing provision of CTA to be modified / replaced

# MLI Article 13:

Restricting Preparatory and Auxiliary exemptions and introduction of Anti-fragmentation rules

# MC Article 5(1) and 5(2) - Fixed Place PE

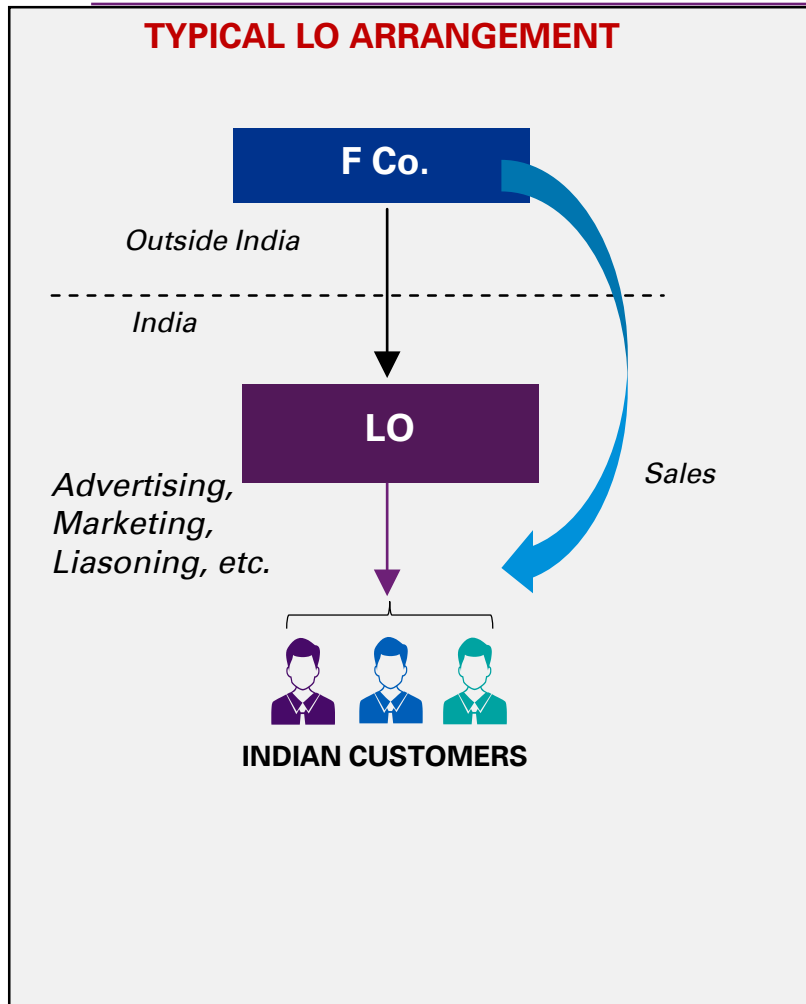
- Article 5(1) of the OECD/ US/ UN MC defines Fixed Place PE- “the term ‘permanent establishment’ means a **fixed place of business through which the business of an enterprise is wholly or partly carried on**”
- Cumulative Conditions in case of Fixed Place PE
  - Existence of ‘ **fixed place of business**’ (Place of Business Test)
  - Place of business is at **disposal** of the enterprise (Disposal Test)
  - Business is **carried on** wholly or partly **through** such fixed place of business (Carrying on Business Test)
- Article 5(2) of the OECD/ US/ UN MC provides illustrative list of Fixed Place PE
  - The term ‘Permanent Establishment’ includes especially:
    - A place of management;
    - A branch;
    - An office;
    - A factory;
    - A workshop, and
    - A mine, an oil or gas well, a quarry or any other place of extraction of natural resources

# MC Article 5(4) - List of Exclusions from Fixed Place PE (Pre BEPS)

UN Model Convention	OECD Model Convention
<b>(a)</b> the use of facilities solely for the purpose of storage or display of goods or merchandise belonging to the enterprise;	<b>(a)</b> the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
<b>(b)</b> the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display;	<b>(b)</b> the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;
<b>(c)</b> the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;	
<b>(d)</b> the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise;	
<b>(e)</b> the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character;	
<b>(f)</b> the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.	

***Preparatory and Auxiliary character not required under clauses (a) to (d) above***

# Typical LO Arrangement



- Permitted activities for a LO in India contained in FEMA regulations
- Ratio laid down in various Court rulings in on whether LO in India constitutes a PE of the foreign enterprise in India
- Permissible activities for LO:
  - Supply of information
  - Acting as a communication channel
  - Doing preliminary and preparatory work
  - Advertising
  - Facilitating meetings, arranging stay and travel arrangements, etc.
- Non permissible activities
  - Negotiating prices
  - Undertaking sales function, etc.

# Some rulings - Preparatory and Auxiliary Services

## **Motorola Inc [2005] 96 TTJ 1 (Delhi SB)**

Activities such as market survey, industry analysis, economy evaluation, furnishing of product information, ensuring distributorship and their warranty obligation, ensuring technical presentations to potential users, development of market opportunities, providing services and support information, procurement of raw materials and accounting and finance services, for one year by employees of a foreign company through an office located at the Indian subsidiary's office qualified as preparatory or auxiliary in nature

## **U.A.E. Exchange Centre Ltd [2009] 183 Taxman 495 (Delhi HC)**

Activity of LO being downloading information contained in main servers located in UAE, drawing cheques based on such information and dispatching such cheques to beneficiaries of NRI remitter in India, held to of preparatory and auxiliary nature as such activities are in 'aid' or 'support' of the main activity

## **Jebon Corporation India [2012] 19 taxmann.com 119 (Karnataka HC)**

Since LO performed functions such as identifying new customers, pursuit and follow-up of customer, price negotiation and finalization, securing orders, processing of orders, payment for material and post sale support, it could be said that liaison office had been carrying on commercial activities and it was PE

## **Rolls Royce Plc [2008] 19 SOT 42 (Delhi Tribunal)**

The core activity of marketing, negotiating, selling of the product and is a virtual projection of its customer facing business unit, who has the responsibility to sell the products belonging to the group and hence cannot be regarded as preparatory or auxiliary nature

## **Brown and Sharpe Inc [2014] ITA No. 219 of 2014 (Allahabad HC)**

the activities of a foreign company's LO in India included preparatory or auxiliary services, the marketing services conducted from the LO could not be treated as preparatory or auxiliary and accordingly a PE was established

# Illustrations of Preparatory / Auxiliary activities

PREPARATORY /AUXILLIARY	NON-PREPARATORY
Market survey / Industry analyses / economy evaluation	Marketing services, negotiation of Contracts, etc.
Furnishing of information including product information to prospective customers	A management office for supervisory and coordinating functions
Ensuring technical presentation to potential users	Supervisory or control of performance of contract
Development of market opportunities	After sales services to customers
Basic operation before commencement of business activities in India	A fixed place of business for the delivery of spare parts to customers

***Enterprise cannot fragment a cohesive operating business into several small operations in order to argue that each part is merely engaged in preparatory or auxiliary activity***

# MLI Article 13: Restricted exemptions-Preparatory/auxiliary activities

**Para 1:** Choice to select between **option A** (para 2) or **option B** (para 3) or neither of the options

**Para 2: Option A** replaces existing treaty provisions to the extent that

- (i) all activities currently included in the treaty (whether or not they are of a P/A nature);
- (ii) any other activity not already mentioned in the treaty; and
- (iii) any combination of activities in (i) and (ii),

shall fall within the specific activity exemptions only if **all such activity (or the overall activity of the fixed place of business from a combination of activities) is of a P/A character**

**Para 3: Option B** provides that all activities (or combinations of activities) not already mentioned in the existing tax treaty must be of a P/A nature to qualify under the specific activity exemption, This option also provides a carve out for any activity already existing in the tax treaty which is not specifically required to be of a P/A nature. Such activity may continue to fall within the specific activity exemptions under Option B.

**Para 4: Anti-fragmentation Rule:** The specific activity exemptions that deem a fixed place of business to not amount to a PE shall not apply where the relevant enterprise, or a closely related enterprise, carries on business activities at the same fixed place or a different place in the same CJ **and** (i) such place constitutes a PE; **or** (ii) the overall activity resulting from the combined business activities of either a) one enterprise or two closely related enterprises operating in two fixed places or b) two enterprises operating in one fixed place, **is not of a P/A character.** ...

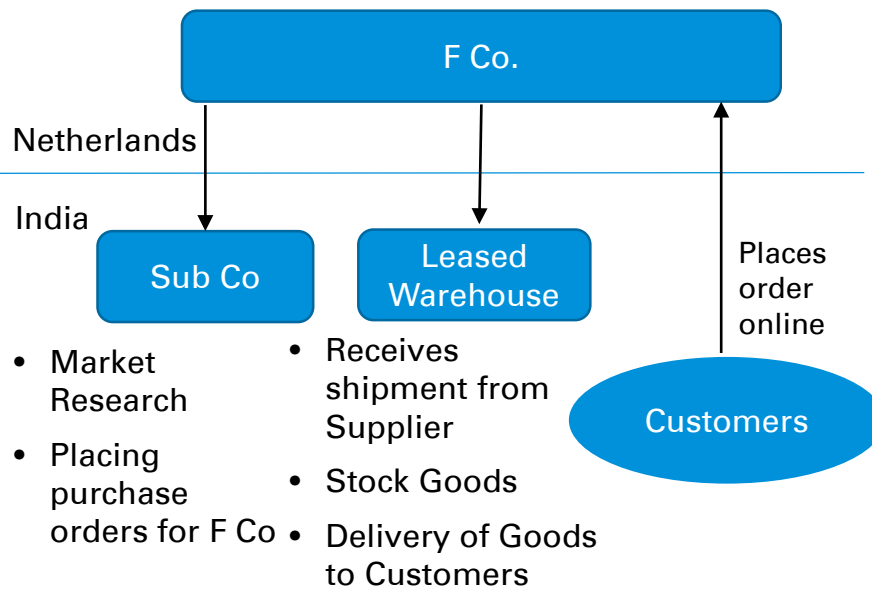
**Para 5:** Para 2 or para 3 to apply 'in place of' .....

**Para 6:** Right to Reservations (**None by India**)

**Para 7 and 8 :** Notifications..... **India adopts Option A**



# Case Study : Restricted exemptions - Preparatory / Auxiliary activities



## Pre MLI:

- Independent activities carried out through Sub Co or Leased Warehouse –was possible to argue no Fixed place PE since covered under specific exemption list or overall activities considered to be of P/A/ Character

## Post MLI:

- **Option A (as selected by India):** Notwithstanding provisions of CTA that define PE, the PE shall be deemed not to include:
  - a) all activities specifically listed in the current treaty (whether or not they are or a P/A nature);
  - b) maintenance of fixed place of business for carrying on any activity not already mentioned in the treaty; and
  - c) maintenance of fixed place of business for any combination of activities mentioned in (a) and (b),**Provided if such activity /in case of subpara (c), overall activity of fixed place of business, is of a P/A character**
- Fragmentation of activities no more permissible
- Both India and Netherlands chose Option A – Each Activity /Overall activities to be checked for P/A character
- F Co likely to constitute Fixed Place PE in India and P/A exemption may not be available

# MLI Article 13: Impact on Few Indian Tax Treaties

Few Example of Countries Notified by India	Positions of the Other Contracting Jurisdictions	Impact on India's CTA with the Country
Singapore	Selected Opt B – Reservation on Para 4	No Impact
Netherlands	Selected Opt A	Opt A to apply
UK	Not Selected any Option – No Reservation on Para 4	Para 4 to apply
Japan	Selected Opt A	Opt A to apply
Canada	Opt out	No Impact

# MLI Article 14:

Avoiding artificial splitting  
up of contracts

# MC Article 5(3) - Construction / Installation PE - Pre BEPS

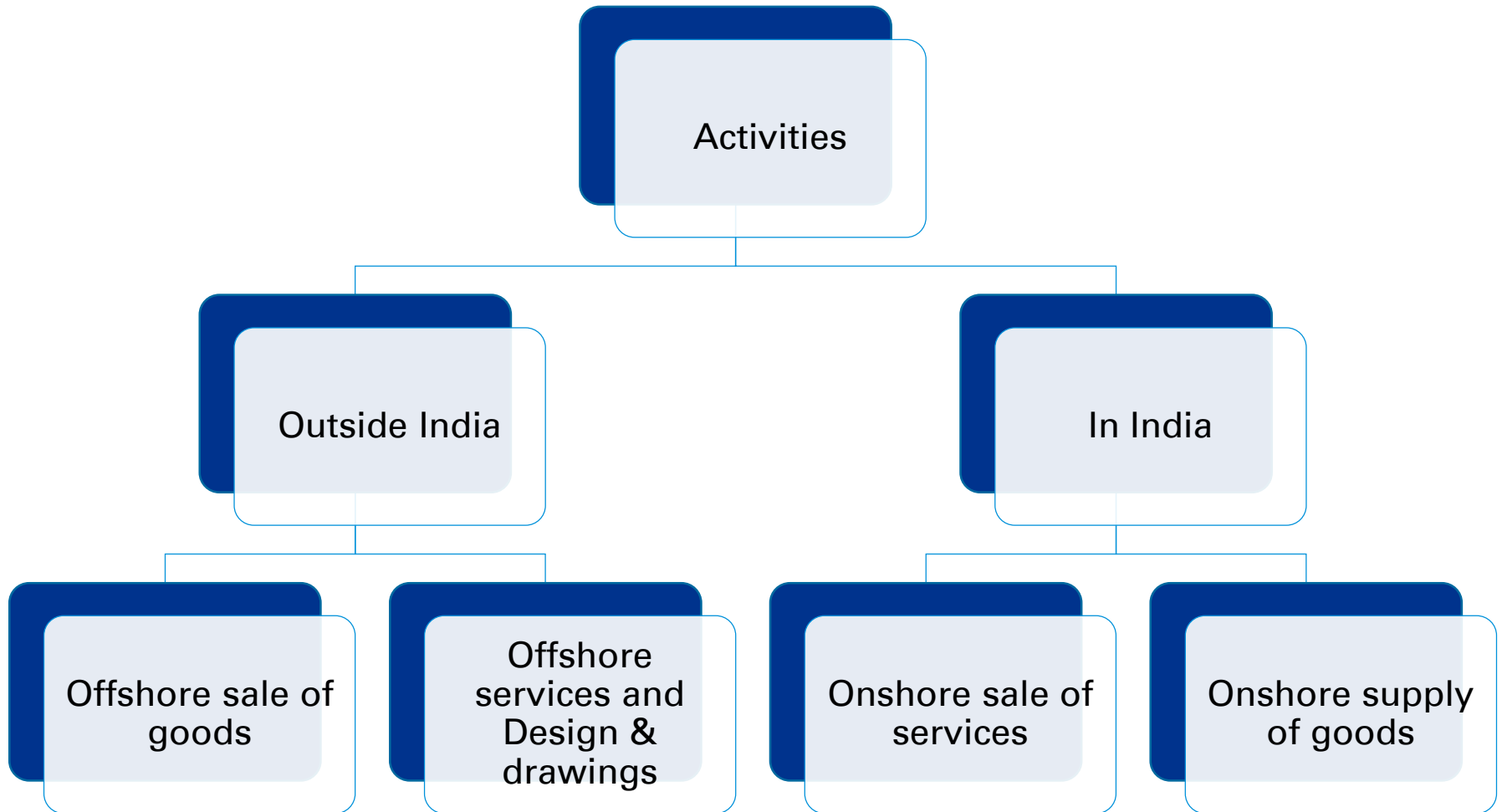
UN Model Convention	OECD Model Convention
<p>The term “permanent establishment” also encompasses:</p> <p>(a) A building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only if such site, project or activities <b><u>last more than six months</u></b>;</p>	<p>A building site or construction or installation project constitutes a permanent establishment <b><u>only if it lasts more than twelve months</u></b>.</p>

## **Building site or construction or installation project includes:**

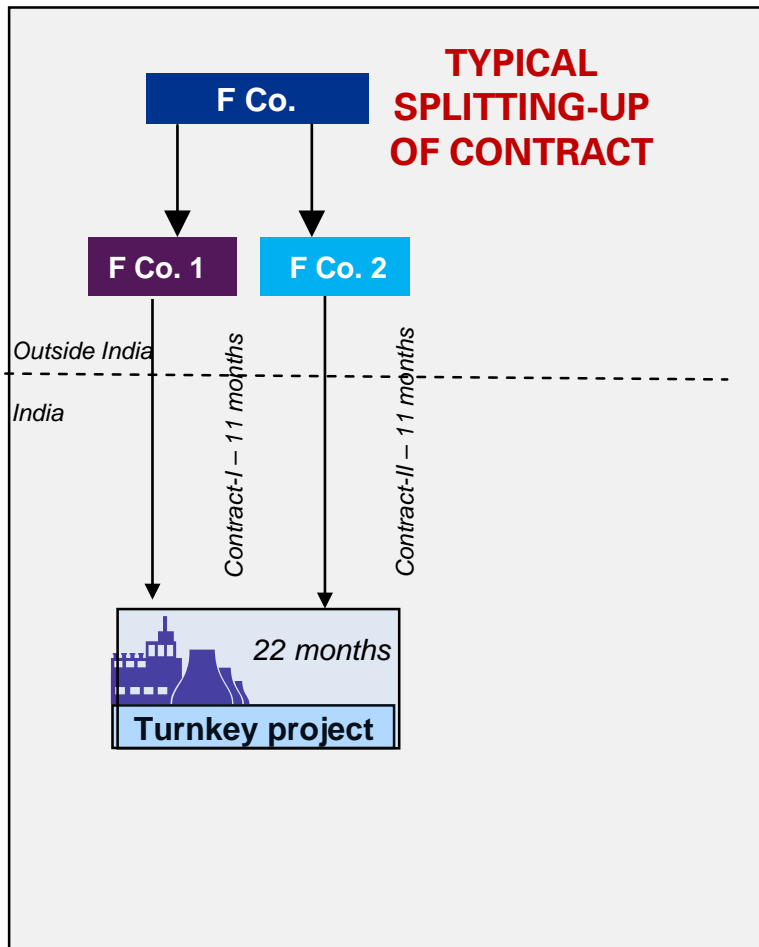
- construction of roads, bridges or canals
- renovation (involving more than mere maintenance or redecoration) of buildings, roads, bridges or canals
- Laying of pipelines
- excavating and dredging
- installation of new equipment in an existing building or outdoors
- onsite planning and supervision of the construction of a building

# Turnkey Contracts

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# Artificial splitting-up of contracts - Typical Structure



- Turnkey / EPC contracts are typically divided amongst group entities in overseas jurisdiction - such that presence of none of the foreign entity in India exceeds the prescribed threshold for determination of Construction / Installation PE
- One of the Foreign entity is contractually liable for entire contract with ICO

# Some rulings - Artificial splitting-up of contracts

## **Valentine Maritime (Gulf) LLC [2011] 45 SOT 359 (Mumbai Tribunal)**

The ITAT held that aggregation of time spent on different projects can only arise where inter-connected activities are provided. Connection would not arise only because contracts are carried out at nearby geographical location or for same person, but there has to be something in nature of work that must be connected

## **J. Ray McDermott Eastern Hemisphere Ltd [2012] 27 taxmann.com 101 (Mum Tribunal)**

In absence of any finding that contracts were inextricably interconnected, interdependent, duration of different contracts entered into by the assessee cannot be aggregated for determination of PE in India

## **Hyundai Heavy Industries Co. Ltd. [2007] 161 Taxman 191 (SC)**

Where fabrication work was done overseas and delivered overseas, PE cannot be constituted vis-à-vis such fabrication work and only for the activities carried out in India, the installation PE was constituted and the profits were attributed

## **Sumitomo Corporation [2014] 43 taxmann.com 2 (Delhi - Tribunal)**

Where a Japanese company was rendering supervisory services in India, relating to import and installation of equipment through its three project offices, since such supervisory services were for different sites and different Purchase Orders, all contracts put together did not form a coherent whole, commercially or geographically and therefore period of services so rendered could not be aggregated by different offices in order to determine assessee's construction / installation PE in India.

# MLI Article 14: Artificial splitting-up of contracts

**Para 1:** To determine whether the period (or periods) referred to in a provision of a CTA that stipulates a period (or periods) of time after which specific projects or activities shall constitute a PE has been exceeded:

a) where an enterprise of a CJ carries on activities in the other CJ at a place that constitutes a building site, construction project, installation project or other specific project or carries on supervisory or consultancy activities in connection with such a place, and these activities are carried on **during one or more periods of time that, in the aggregate, exceed 30 days without exceeding the period or periods referred to in the relevant provision of the CTA;** and

b) where **connected activities** are carried on in other CJ at (or, where the relevant provision of the CTA applies to supervisory or consultancy activities, in connection with) the same building site, construction or installation project, or other place identified in the relevant provision of the CTA **during different periods of time, each exceeding 30 days, by one or more enterprises closely related to the first-mentioned enterprise;**

**these different periods of time shall be added to the aggregate period of time** during which the first-mentioned enterprise has carried on activities at that building site, construction or installation project, or other place identified in the relevant provision of the CTA

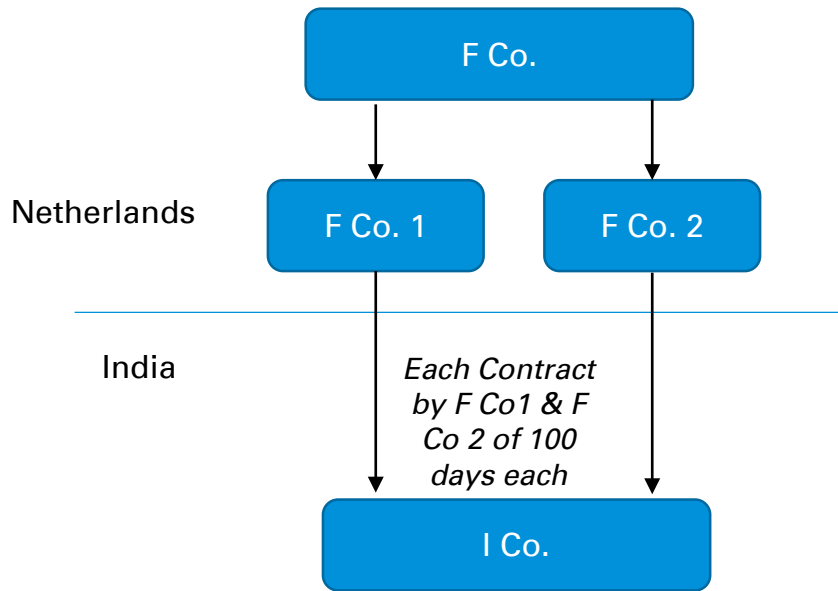
**Para 2:** Para 1 to apply 'in place of or in absence of' .....

**Para 3:** Right to Reservations **(None by India)**

**Para 4:** Notifications..... **(None by India)**



# Case Study : Payment to a NR for Construction / Installation Contracts



## Pre MLI:

- Since Netherlands Treaty threshold is that each construction / installation project should continue for a period of more than 183 days:
  - Independent contracts between F Co 1 & I Co, and F Co 2 & I Co, do not constitute construction / installation PE in India
- Practice of issuing no PE declaration by F Co's to I Co for payment without WHT

## Post MLI:

- Following different period of time to be added to determine threshold for constitution of construction / installation PE:
  - activities carried on in source state during one /more periods of time which in aggregate, **exceed 30 days** without exceeding the threshold prescribed in the CTA; **AND**
  - connected activities are carried on same project site during different periods of time, **each exceeding 30 days, by CRE**
- PE to be formed by **disregarding splitting-up** of **contracts** between F Co1 and F Co 2
- I Co required to withheld tax@40%(plus surcharge & cess) on net income of F Co1 & F Co 2

# MLI Article 14: Impact on Few Indian Tax Treaties

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Few Example of Countries Notified by India	Positions of the Other Contracting Jurisdictions	Impact on India's CTA with the Country
Singapore	Opt out	No Impact
Netherlands	Reservation only for exploration and natural resource	Para 1 of MLI Article 14 to supersede
UK	Opt out	No Impact
Japan	Opt out	No Impact
Canada	Opt out	No Impact

MLI Article 12:

Expanding scope of  
Agency PE

# MC Article 5(5) & 5(6/7)-Dependent Agency PE (DAPE)-Pre BEPS

UN Model Convention	OECD Model Convention
<p>Article 5(5): Person other than an agent of an independent status acting in a CS on behalf of a foreign enterprise, shall constitute DAPE if he:</p> <ul style="list-style-type: none"> <li>(a) Has and habitually exercises in that CS an authority to conclude contracts in the name of the foreign enterprise,.....; or</li> <li>(b) Has no such authority, but habitually maintains in the first-mentioned CS a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise.</li> </ul> <p>Article 5(7): Activities carried out by broker, general commission agent or any other agent of an independent status shall not constitute DAPE</p> <p>If activities of such an agent are devoted wholly or almost wholly on behalf of foreign enterprise ....., he will not be considered an agent of an independent status within the meaning of this paragraph</p>	<p>Article 5(5): Person other than an agent of an independent status acting in a CS on behalf of a foreign enterprise, shall constitute DAPE if he:</p> <ul style="list-style-type: none"> <li>(a) Has and habitually exercises in that CS an authority to conclude contracts in the name of the foreign enterprise,.....;</li> </ul> <p>Article 5(6): Activities carried out by broker, general commission agent or any other agent of an independent status shall not constitute DAPE</p>

# Potential PE risk in marketing support / agency arrangement

F Co.

Outside India  
-----  
India

Market Support Provider/  
Indian agent

- Briefing customers
- Product demonstrations
- Explaining utility
- Communicating price/price range
- Resolving complaints



INDIAN CUSTOMERS

- F Co. sells **products** in India through its Indian agent
- Indian agent interfaces with customers, **makes calls**, sends **e-mails**, **visits premises** to convince them to buy product
- Indian agent also indicates **price of product** and explains **standard terms of contract** with F Co.
- **Contracts** with customers **concluded remotely by F Co.** for **quantity** agreed and **price** discussed with Indian agent
- Indian agent does not have **authority to vary standard terms of contract**, including prices fixed by F Co.
- F Co. **remunerates the Indian agent** for its services at **cost plus mark-up** (*as may be agreed*)

# Some rulings - Dependent Agency PE

## **Varian India (P) Ltd [2013] 33 taxmann.com 249 (Mumbai Tribunal)**

The assessee has no authority to accept orders on behalf of any of the Varian Group Companies ('VGCs'). Also, the assessee does not deal with one entity of Varian Group, but also for other VGCs. Hence, the condition that the person habitually secures orders wholly or almost wholly for the enterprise is not met.

## **Nokia Networks OY [2018] 194 TTJ 137 (Delhi Tribunal) (SB)**

Held that where installation activities were carried out by Indian Sub co (NIPL), since NIPL has not negotiated or concluded any contract of supply of equipment on behalf of Nokia which binds Nokia. Marketing agreement is an independent agreement bearing no relation with supply of equipment by Nokia and for which NIPL is remunerated at arm's length

## **Daikin Industries [2012] 19 taxmann.com 119 (Karnataka HC)**

It was observed that entire activity starting from identifying and approaching customers, negotiating prices and finalisation of products were done by Indian group co of Daikin i.e. DIAPL in India and not only for the products sold directly by DIAPL as a distributor, but also for which Daikin Japan claimed to have made direct sales. The mere fact that the Daikin Japan was formally signing the contracts of sale does not, in any manner, alter the position that DAIPL was habitually exercising authority in India to conclude contracts on behalf of Daikin Japan.

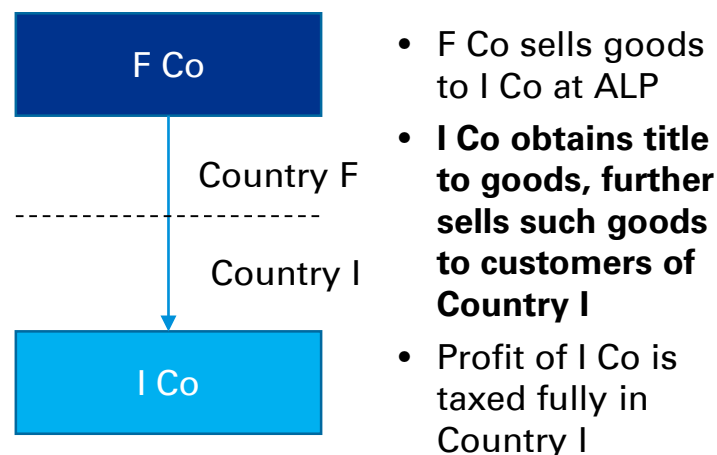
## **GE Energy Parts Inc [2017] 78 taxmann.com 2 (Delhi Tribunal) [as affirmed by Delhi High Court in [019] 411 ITR (Delhi HC)]**

Where Agent carries out activities in COS for more than one group company, such agent shall not be regarded as an agent of an Independent status

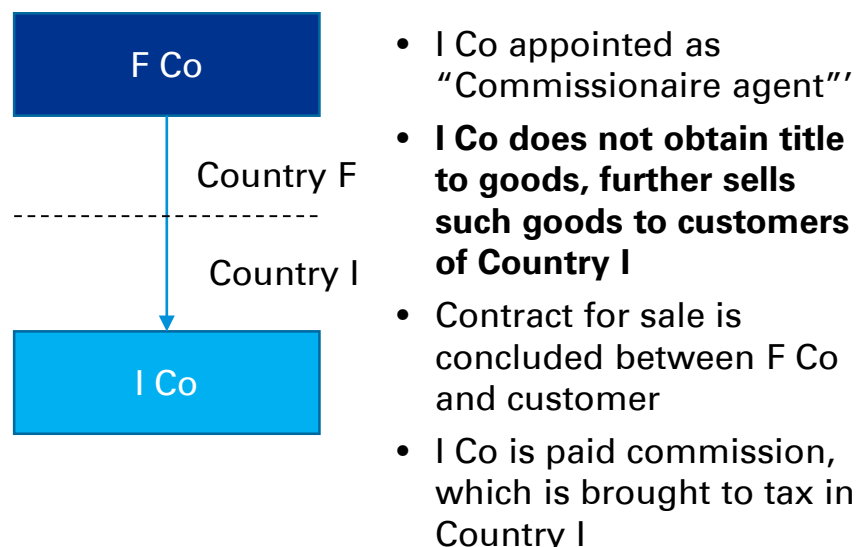
# Meaning of Commissionaire arrangement

## Commissionaire arrangement

### Normal arrangement



### Commissionaire arrangement



1 Commissionaire arrangement may be loosely defined as an arrangement through which a **person sells products in a given state in its own name but on behalf of a foreign enterprise** that is the owner of these products. Commissionaire generally does not legally binds the principal

2 Concept found in civil law countries

3 India, being a common law country, may not be much impacted by commissionaire arrangements as such structures are not permissible under the provisions of Indian Contract Act

# MLI Article 12: Commissionaire/Market support arrangements

**Para 1:** Notwithstanding the provisions of CTA, Where a person acting in a CJ on behalf of an enterprise, habitually concludes contracts, or **habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification** by the enterprise, and these contracts are:

- a) in the name of the enterprise; or
- b) for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use; or
- c) for the provision of services by that enterprise,

that enterprise shall be deemed to have a PE in that CJ in respect of any activities which that person undertakes for the enterprise unless these activities, if they were exercised by the enterprise through a fixed place of business of that enterprise situated in that Contracting Jurisdiction, would not cause that fixed place of business to be deemed to constitute a PE

**Para 2:** Para 1 not to apply where the person acting in a CJ on behalf of an enterprise of the other CJ carries on business as **an independent agent and acts for the enterprise in the ordinary course of that business**. Where, however, a person acts exclusively or almost exclusively on behalf of **one or more enterprises to which it is closely related**, that person shall **not be considered to be an independent agent** within the meaning of this para...

**Para 3:** Para 1 and para 2 to apply 'in place of'.....

**Para 4:** Right to Reservations (**None by India**)

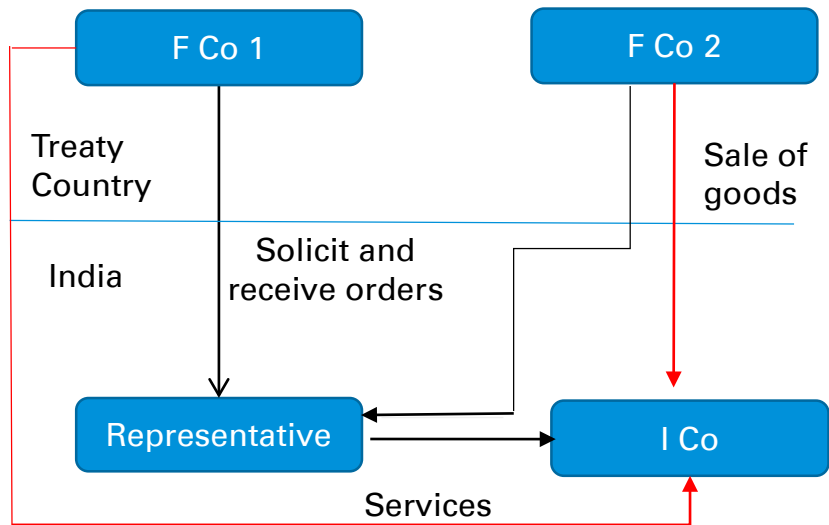
**Para 5 and 6 :** Notifications..... Para 1 and 2 to apply in place of existing provision **only where both the countries have notified the same**



# Comparative review of amendment in domestic law and Treaty

	Existing language as per various Tax Treaties	India domestic tax law – position prior to Budget 2018 amendment	Changes in PE Status in line with update under Indian Budget 2018 & BEPS Action Plan – 7 / MLI Article 12
<p>Agency PE is also constituted when a 'dependent agent'</p>	<p>Habitually <b>concludes contracts</b> on behalf of non-resident entity</p>	<p>Habitually <b>concludes contracts</b> on behalf of non-resident entity</p>	<p>Habitually concludes contracts or <i>habitually plays principal role leading to conclusion of contracts*</i> [that are routinely concluded without material modification by non-resident entity]</p> <p>* OECD 2017 November update in light of BEPS AP-7 is already effective but it is expressly not made ambulatory and amended definition is not intended to impact existing treaties</p>
	<p>Habitually secures orders for non-resident entity including group entities</p>	<p>Habitually secures orders for non-resident entity including group entities</p>	<p>Habitually secures orders for non-resident entity including group entities</p>

# Case Study : Purchase of Goods from NR having Representative in India - Expansion of Agency PE



## Pre MLI:

- No agency PE of F Co in India if its Representative does not have authority to conclude contracts
- Even if agent works for multiple entities of same group – still considered as “Independent Agent” and hence not covered under Agency PE Article
- Practice of issuing no PE declaration by F Co group to I Co for payment without WHT

## Post MLI:

- Agent acting **exclusively** or **almost exclusively** on behalf of **one or more closely related enterprises** **not to be considered independent**
- **Scope** of PE expanded to include agent **playing principal role**, leading to routine conclusion of contracts, **without material modification**
- Crucial to understand the activities performed by Representative in India
- If such Representative constitutes Agency PE of F Co in India, payment by I Co to attract higher rate of WHT being 40% (plus applicable surcharge and education cess) on net income

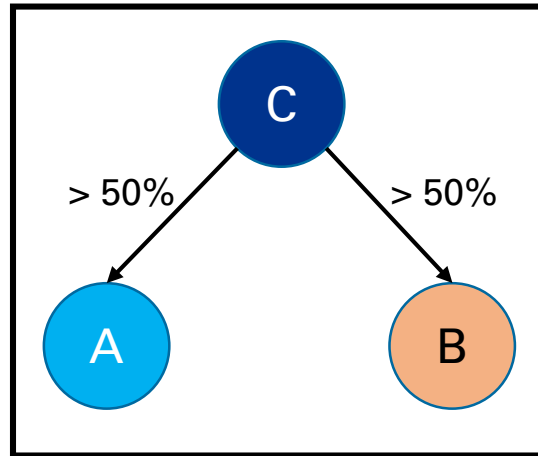
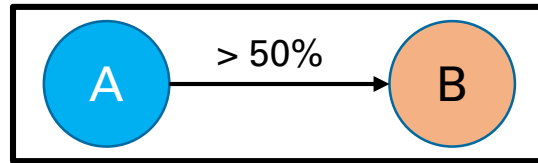
# MLI Article 12: Impact on Few Indian Tax Treaties

<b>Few Example of Countries Notified by India</b>	<b>Positions of the Other Contracting Jurisdictions</b>	<b>Impact on India's CTA with the Country</b>
Singapore	Opt out	No Impact
Netherlands	Opt out	No Impact
UK	Opt out	No Impact
Japan	Opt in and Notified India	MLI Article 12 to be replaced
Canada	Opt out	No Impact

# MLI Article 15: Closely Related Enterprises

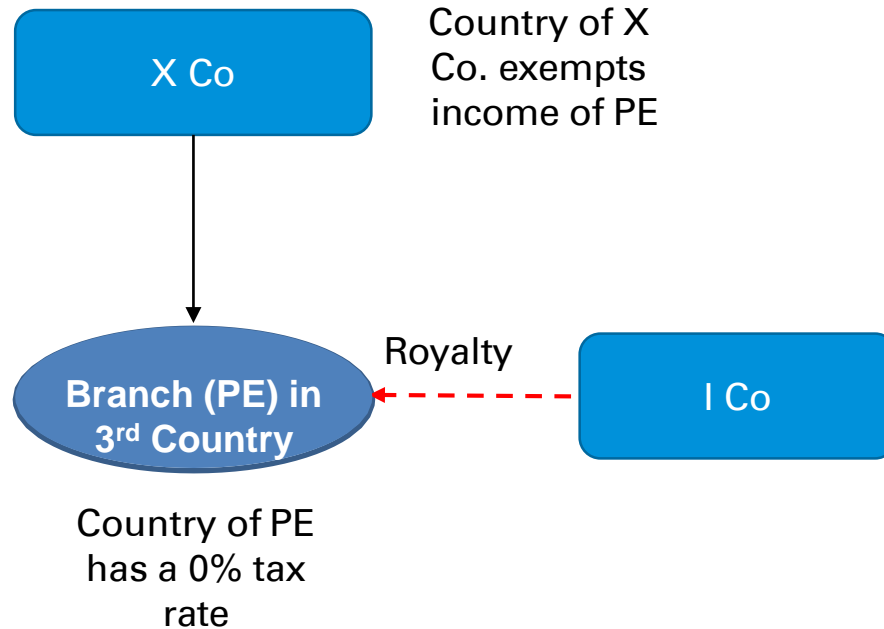
A person is closely related to an enterprise if, based on all the relevant facts and circumstances, one has **control** of the other or both are under the **control** of the same persons or enterprises.

In any case,



- ❑ In case of a Company, > 50% of the aggregate vote and value of the Company's share or beneficial equity interest in the Company
- ❑ In case of others, > 50% of beneficial interest of others

# Case Study on MLI Article 10 : Payment from India to Foreign Co's Branch in Third State



## **Pre MLI:**

- Typically in case of Branch, Invoice is raised by Parent Co, for royalty payable to Branch
- For availing treaty benefits w.r.t payment from India to any of the Branch of F Co:
  - Payer required to analyse availability of Treaty benefits between India and Country of X Co

## **Post MLI:**

Following questions need to be verified:

- 1) Whether income from Branch in 3<sup>rd</sup> Country is exempt in hands of Parent, X Co in Country X; and
- 2) Whether tax payable by Branch of F Co in 3<sup>rd</sup> Country is less than 60 percent of taxes that would have been paid in Country X, if Country X wouldn't have exempted income from such PE,

If answer to both the above questions is in affirmative, benefits of treaty between India and Country X – Not available

# Way Forward

# Consequences of PE

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- Even a part of business carried on through a PE is sufficient for taxation
- Business income is taxable at 40% on net profits
- Company Law; FEMA; TDS Compliances
- Books of accounts and audit may be required
- Transfer Pricing implications for transactions with AE's
- Interest, Royalty and FTS may be taxed as business income
- TDS obligation on payers

# What has changed?

## Before MLI

- **Tax Residency Certificate** [as per Section 90(4)]
- **Form 10F** to be submitted [Section 90(5)]
- **Other conditions:**
  - Whether Resident of treaty country
  - Taxes Covered?
  - Whether “No PE Declaration” is available
  - Whether “No POEM Declaration” is available
  - Whether recipient is a Beneficial Owner in case of passive income like Dividend, Interest, Royalty, FTS
  - Whether “Make Available” clause satisfied
  - Whether “LOB” clause satisfied
  - Whether benefit under “MFN” clause is available



## Additional Questions to be considered in the Post MLI Era

- What is the principal purpose for undertaking a transaction from a particular treaty country
- What are the activities of the payee’s representatives in India
- Is payee hit by the expanded definition of PE
- Are payments being made to multiple group entities under split contracts

***Multiple Checks before applying a tax treaty provision***



# Way Forward

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- List the foreign payments where treaty rates are applied
- List Payees in countries where MLI is effective
- Analyse nature of payment & whether relevant Article under Treaty is modified
- Check Whether Payment is to be made to related party or third party
- Evaluate if the declaration from Payee (like no PE, satisfaction of PPT etc.) needs to be broadened
- If Payer aware of Split contracts- Whether no PE Declaration be accepted?
- Whether changes in Reps and Warranties are required?
- Whether revised Indemnities are required?

# Glossary

Terms	Abbreviations	Terms	Abbreviations
Base Erosion and Profit Shifting Action Plan	BEPS AP	Multilateral Instrument	MLI
Competent Authorities	CAs	Mutual Agreement Procedure	MAP
Contracting jurisdiction	CJ	Organisation for Economic Co-operation and Development	OECD
Contracting State	CS		
Covered Tax Agreement	CTA	Permanent Establishment	PE
Double Taxation Avoidance Agreement	DTAA	Place of Effective Management	POEM
Entry into Force	EOF	Principle Purpose Test	PPT
Entry Into Effect	EIF	Preparatory or Auxillary	P/A
Functions, Assets & Risks Analysis	FAR	Qualified Person	QP
Fees for Technical Services	FTS	Supreme Court	SC
Intellectual Property	IP	Simplified LOB	SLOB
Limitation of Benefit	LOB	Withholding Tax	WHT
Model Convention	MC	United Nations	UN

Thank You