



Overview of Double Tax Avoidance Agreements Provisions

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Concept of Double Taxation

Double Taxation can be defined as imposition of taxes in two or more states on the same / different tax payer in respect of the same subject matter in identical periods of time

Juridical Double Taxation

Same person taxed on same income in different jurisdictions

- Worldwide income taxable in more than one state

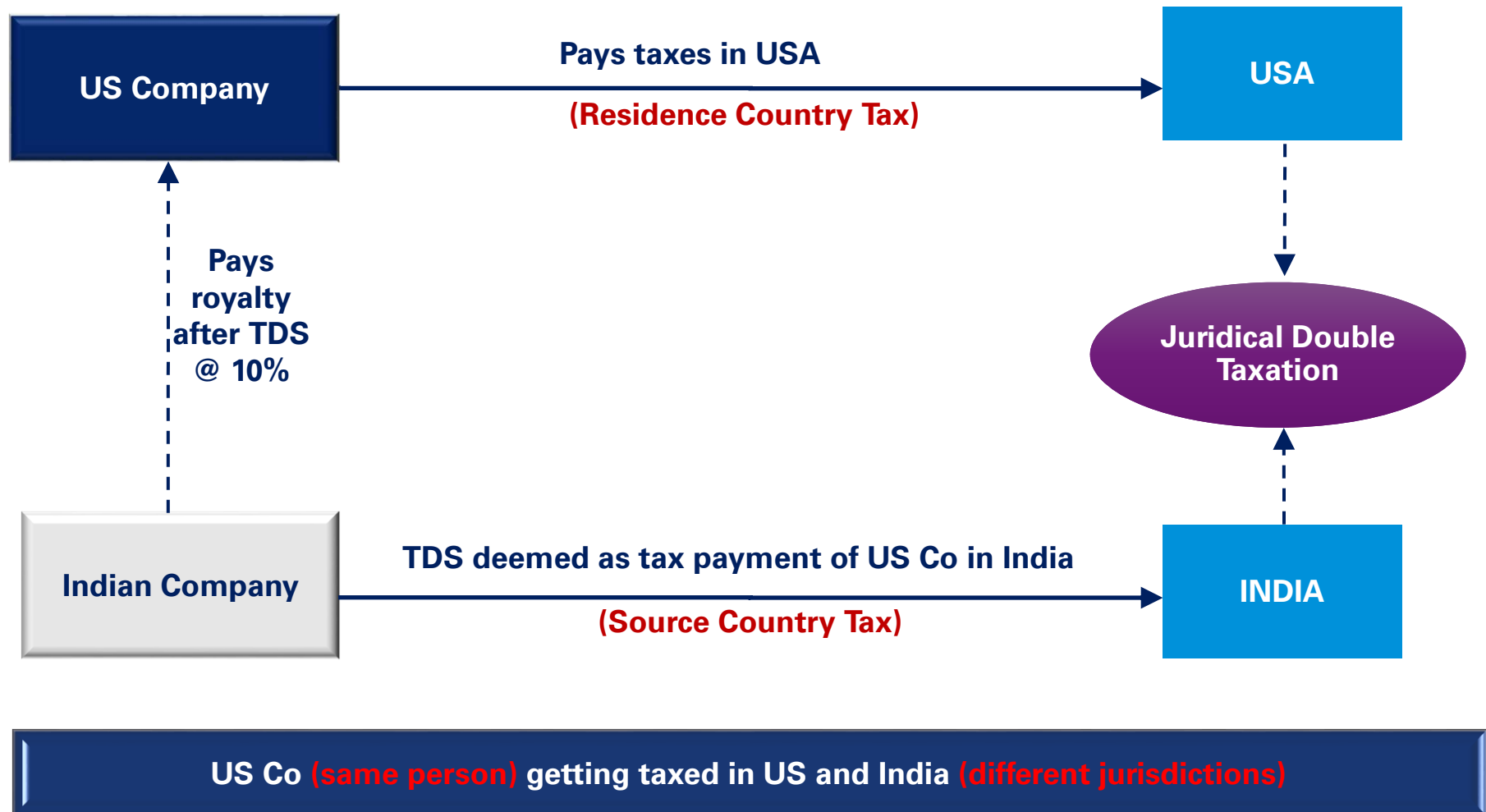


Economic Double Taxation

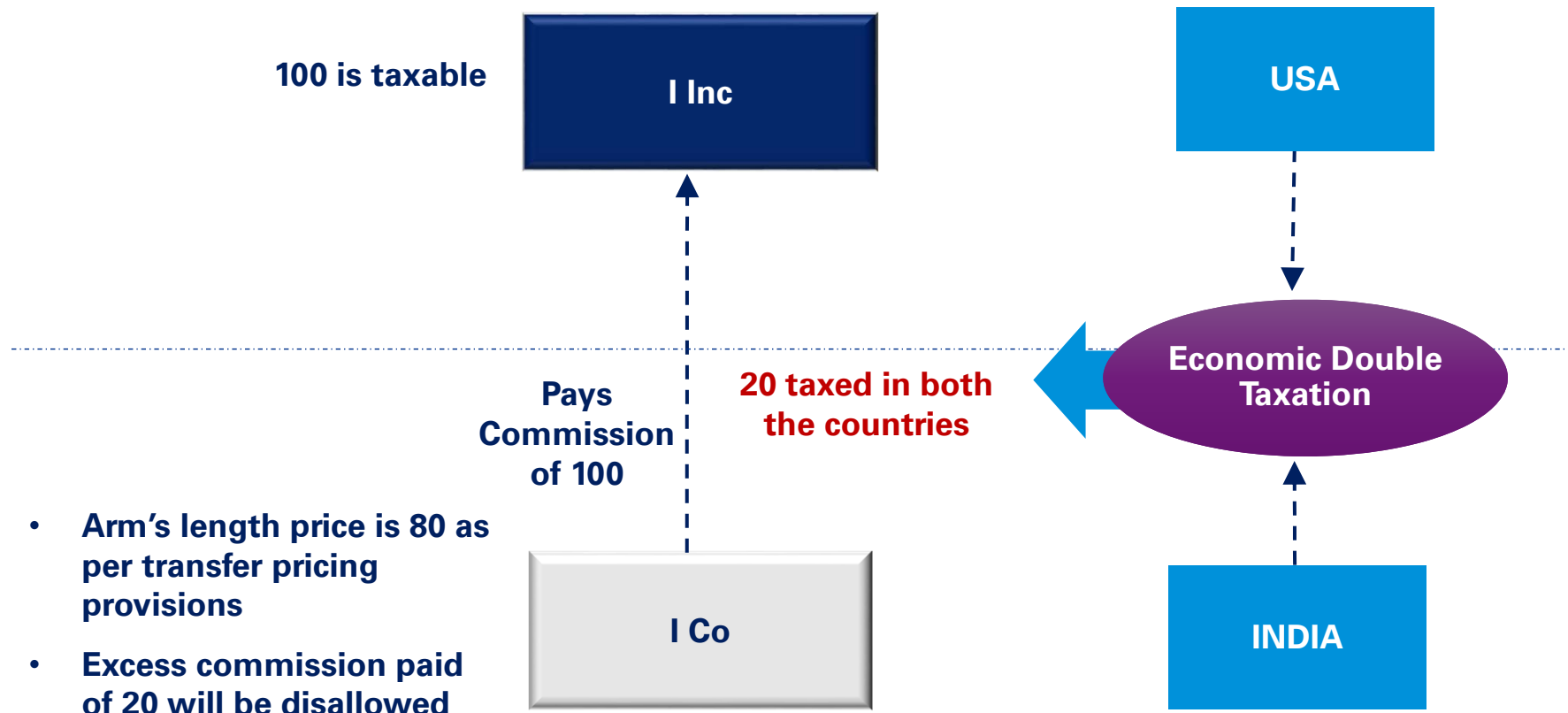
Different persons taxed on same income in different jurisdictions

- Partnership entity as separate taxable entity in COS, Partners of such partnership taxable on pass through principles in COR

Types of Double Taxation - Juridical double taxation



Types of Double Taxation - Economic double taxation



I Co and I Inc (different persons) taxed in US and India (different jurisdictions) for same income



Double Taxation Avoidance Agreements

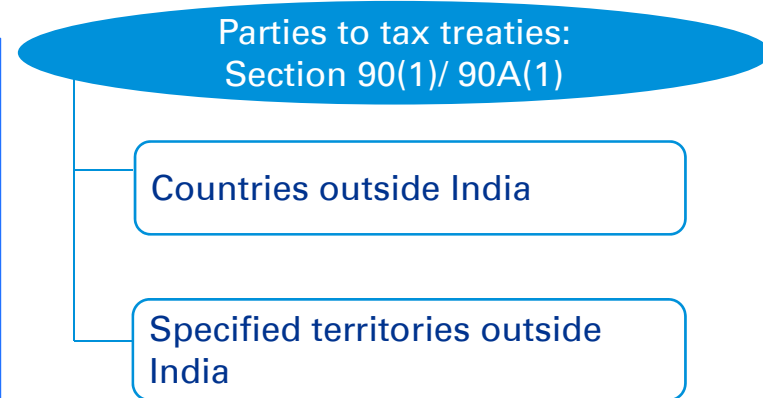
Relief in India from Double Taxation

Indian tax laws

- Section 90 - Empowers Government of India ('GOI') to enter into a Tax Treaty ('DTAA') for avoidance of double taxation
- Section 90A - GOI can adopt agreement entered into between specified association in India and specified association in specified territory outside India

Statutory objective of Section 90(1) and 90A(1)

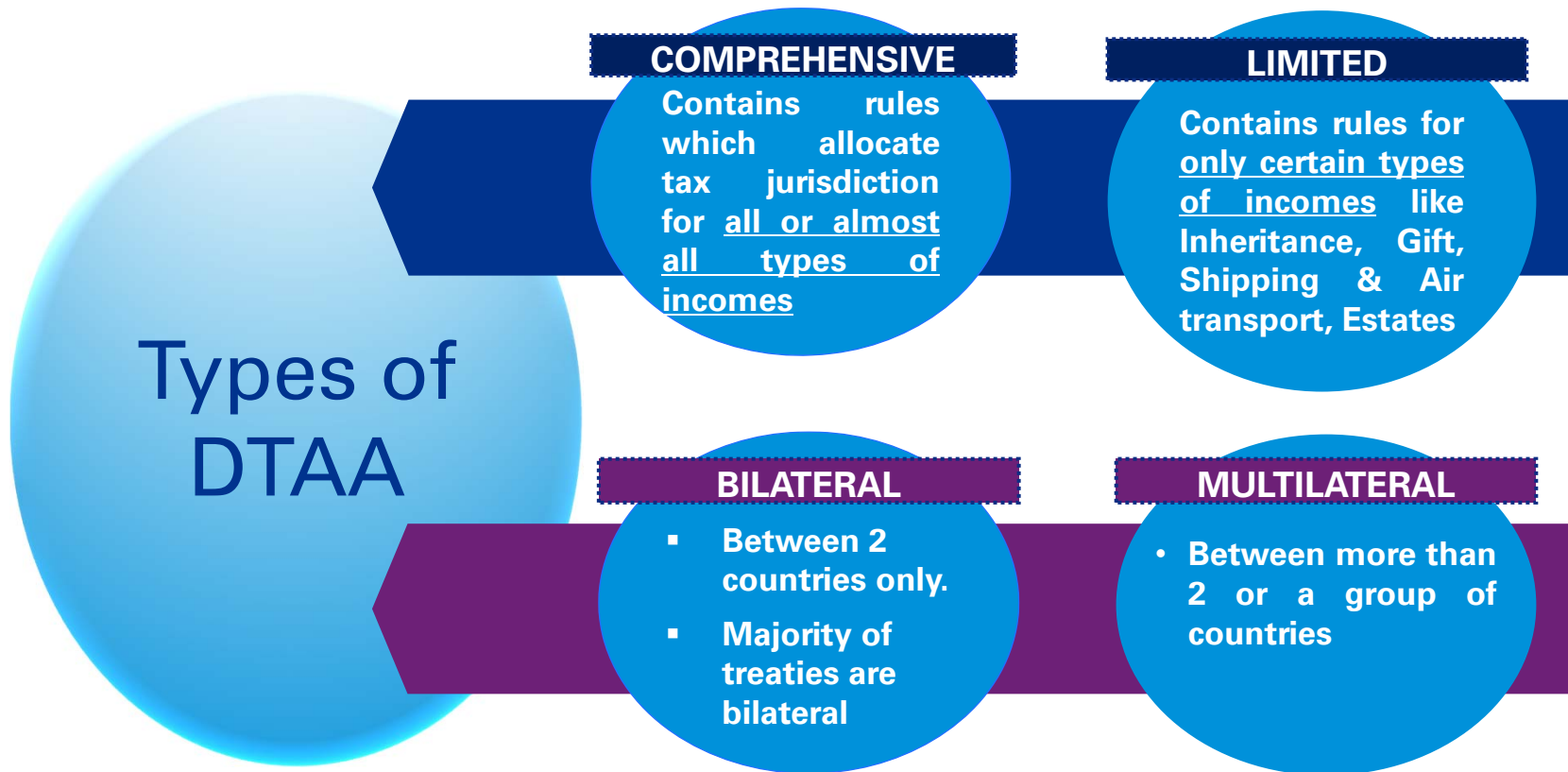
- Avoidance of Double Taxation
- Promotion of mutual economic relations, trade & investment
- Relief on doubly taxed income
- Exchange of information to combat tax avoidance and tax evasion
- Recovery of tax



DTAA vis a vis Domestic Tax Law

- Section 90 of the Income-tax Act, 1961: Domestic tax law will apply to the extent it is more beneficial than the DTAA
- Tax treaties override the domestic tax law

DTAA/ Convention / Charter



Models of Tax Treaties

OECD Model

- Emphasis on residence based taxation
- Developed countries adopted this model in case of treaties with other developed countries
- Started from 1963 draft convention, followed by Regularly updated / amended

UN Model

- Emphasis on source based taxation
- Developed countries adopted this model in case of treaties with developing countries or between two developing nations.
- OECD Model convention has been used as a main reference document

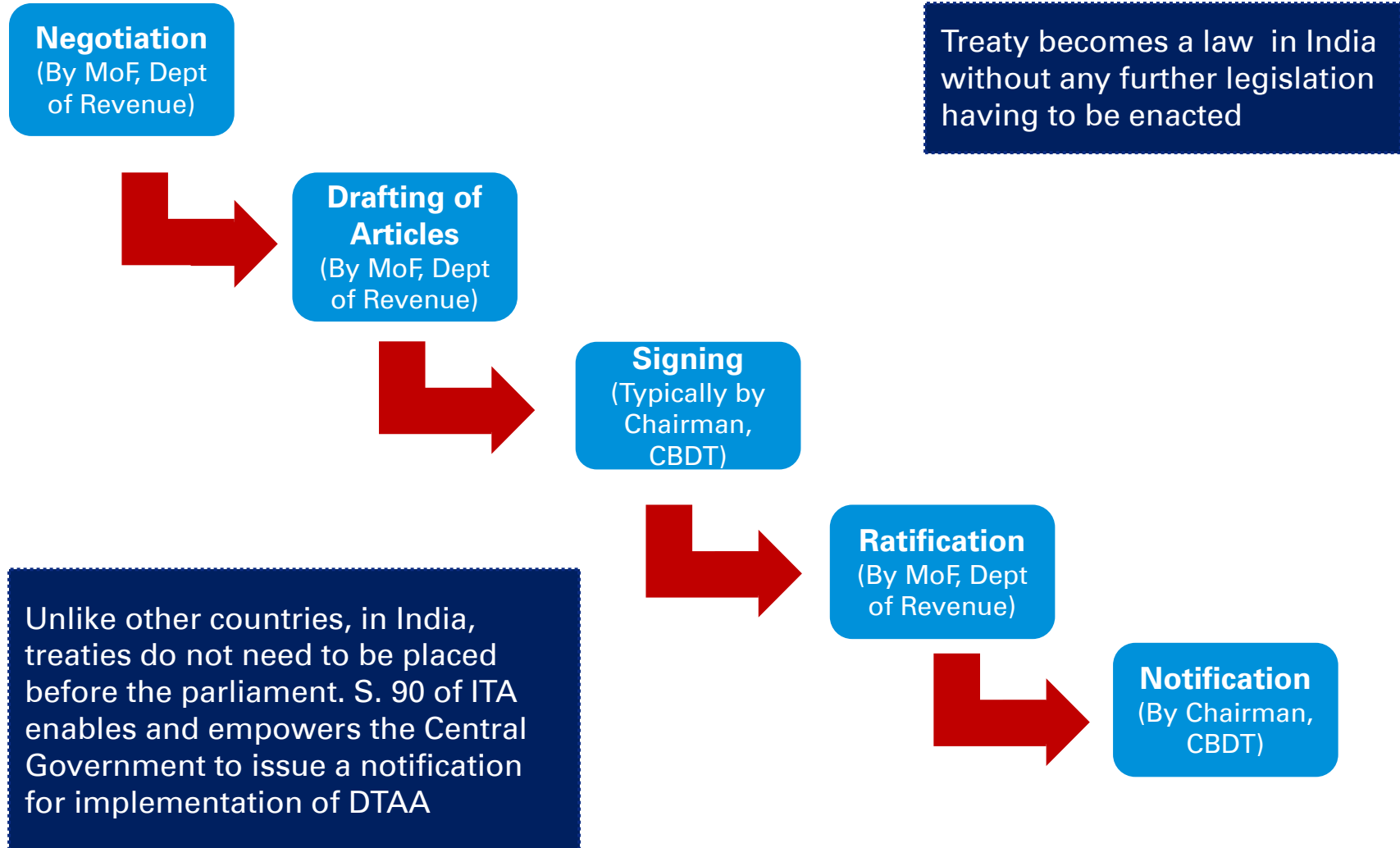
US Model

- Used by USA for all treaty negotiations.
- This model had influence on existing Treaty between India & US
- OECD Model convention has been used as a main reference document

Andean Model

- Adopted by Latin American countries
- Not a very popular model

Steps in effecting a DTAA



Relevant Dates - DTAA

Entry into Force of the Convention (Article 30)

Date of Convention	Date on which Convention is signed
Date of Ratification	Ratification of treaty by legislative/ executive consent in each contracting state in accordance with domestic laws
Date of Exchange of Notes	Notes are exchanged between contracting states confirming ratification of treaty in each state
Date of Entry into Force	Treaty enters into force either upon the date of exchange of notes or a period thereafter as specified in treaty
Effective Date	Treaty provisions become effective in respective contracting states on the dates specified in relevant treaty

Date of Entry into Force and Effective date of application may not be the same dates

Termination of Convention (Article 31)

- Treaty remains in force until terminated
- Some treaties provide for a period during which treaty cannot be terminated (eg India-US Treaty)
- Requires notice through Diplomatic Channels
- Some treaties provide for period of notice and some not

Interpretation of Terms – Relevant Material

Protocol / Exchange of Notes

- Clarifies / elaborates Treaty text
- Binding force – equal to Treaty
- No limit to no. of protocols
- May be entered into even after treaty is concluded

Commentary on Model Convention

- OECD
- UN
- US Technical Explanation

Sources of Interpretation

Public International Law

Vienna Convention on Law of Treaties

- Ordinary meaning of words
- Expressed intention of parties
- Object & Purpose of Treaty

Other Sources

- Mutual Agreement Procedure
- Judicial decisions
- Advance Rulings
- Eminent jurists such as Prof. Klaus Vogel, Philip Baker, Arvid Skaar



Structure and Provisions of a DTAA

Articles of a DTAA (OECD)

SCOPE PROVISIONS

1. Article 1 – Persons Covered
2. Article 2 - Taxes covered
3. Article 31 - Entry into force
4. Article 32 - Termination

DEFINITION PROVISIONS

1. Article 3 - General definitions
2. Article 4 - Resident
3. Article 5 – Permanent Establishment

ELIMINATION OF DOUBLE

1. Article 23 - Elimination of double taxation
2. Article 25 - Mutual Agreement Procedure

ANTI-AVOIDANCE

1. Article 9 - Associated Enterprise
2. Article 26 - Exchange of Information

SUBSTANTIVE PROVISIONS

1. Article 6 – Income from Immovable property
2. Article 7 - Business Profits
3. Article 8 - Shipping, etc
4. Article 10 - Dividends
5. Article 11 - Interest
6. Article 12 - Royalties & FTS
7. Article 13 - Capital gains
8. Article 14 - Independent Personal Services
9. Article 15 - Dependent Personal Services
10. Article 16 – Directors fees
11. Article 17 – Entertainers & Sports persons
12. Article 18 - Pensions
13. Article 19 - Government service
14. Article 20 - Students
15. Article 21 - Other income
16. Article 22 - Capital

MISCELLANEOUS PROVISIONS

1. Article 24 - Non-discrimination
2. Article 27 – Assistance in collection of taxes
3. Article 28 – Diplomats
4. Article 29 – Entitlement to benefits
5. Article 30 - Territorial Extension

Integral part of DTAA

- Exchange of Notes / Protocol
- Memorandum of Understanding ('MoU')

Distributive Rules

Interplay between DTAA and Domestic Law

- Provision of DTAA will operate even when they are inconsistent with provisions of the Act and would override the provisions of the Act
- DTAA provision cannot be thrust upon a taxpayer even if AO perceives that taxpayer may claim DTAA benefit in a subsequent year
- DTAA provision cannot be thrust upon a taxpayer even if the taxpayer has applied the treaty provisions at the assessment stage and raises a claim only at appellate stage that he does not wish to be governed by them
- DTAA cannot create more onerous obligations or liabilities than that provided under the Act
- If the Act exempts certain income, DTAA would be inapplicable since there is no double taxation
- Taxpayer can ask for application of the beneficial provision of the domestic tax law, even when he has opted for being governed by the provisions of the DTAA
- DTAA benefits will generally be available subject to anti-abuse provisions under the domestic law
- Under the Act, every year is an independent unit, and it is for the taxpayer to decide whether to opt for the provisions of the Act or DTAA irrespective of the earlier position adopted



Access to DTAA
- Article 1 to 4

Article 1 – Person Covered

ARTICLE 1

**To whom does
DTAA apply**

- DTAA applies to 'persons who are residents of one or both of the Contracting States'

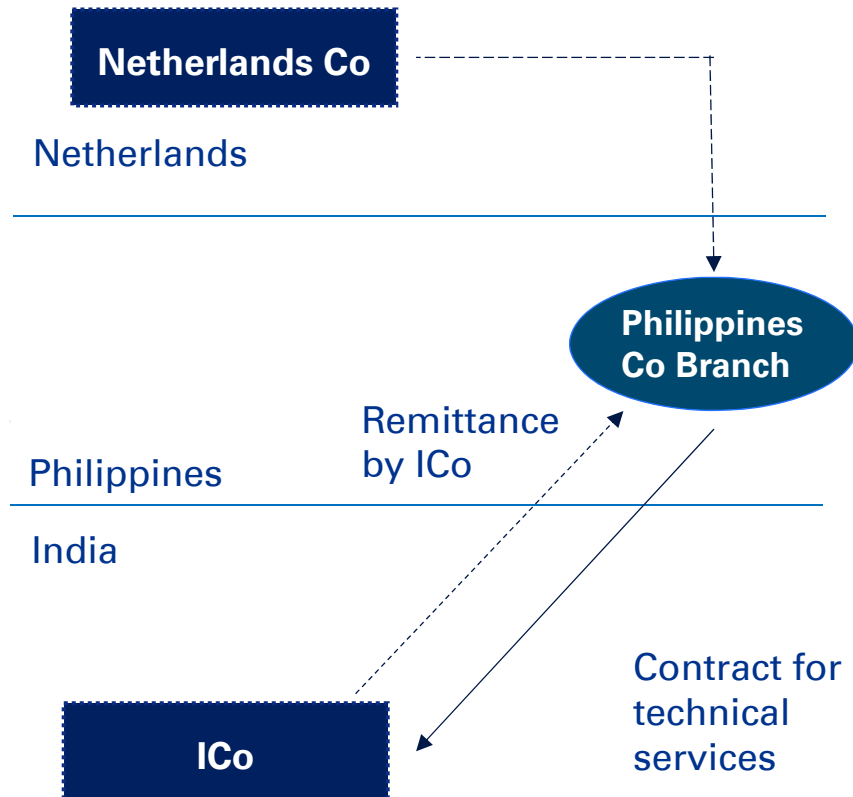
Exceptions

- Article 24(1) (Non-discrimination) - Applies to Residents of third states
- Article 19 (Government service) – Applicable to nationals of third state
- Article 25 (MAP) - Applies to Residents of third states
- Article 1 of OECD MC allows exchange of information in respect of Residents/ nationals of third state

Example of Non-Discrimination

- A citizen of America and a non-resident, exported software from Permanent Establishment ('PE') in India and claimed deduction under section 80-HHE in respect of profits from export of software by invoking non-discrimination clause under India–USA DTAA.
- Sec. 80-HHE is only applicable to domestic companies and residents. However as per India–USA DTAA taxation of a PE of a USA resident shall not be less favorable than taxation of resident enterprise carrying on same activities. Accordingly, deduction u/s 80HHE can be claimed.

Triangular case & DTAA applicability



Triangular cases: DTAA applicability

- Netherlands Company has branch in Philippines
- Philippines branch enters into contract for rendering technical services to ICo
- Services are rendered from Philippines

Issue

- Is benefit of India-Netherlands DTAA available?
- AAR in case of Shell Technology India Pvt. Ltd.

Article 2 - Taxes Covered

ARTICLE 2

Taxes Covered

- Taxes on income and capital
- Wealth tax is included in certain DTAA's
- Treaty also includes list of taxes in respect of which treaty applies
 - Indian 'taxes covered' include income-tax and surtax
 - Foreign treaties 'taxes covered' vary from treaty to treaty
- Treaties apply also to any identical or substantially similar taxes which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes

Exceptions

- Indirect taxes, social security charges, monetary fines and penalties, interest for late payment are not regarded as taxes

Examples

- Foreign State and Local levies may vary for each DTAA (India-USA DTAA does not cover State level income taxes)

Article 3 - General Definitions

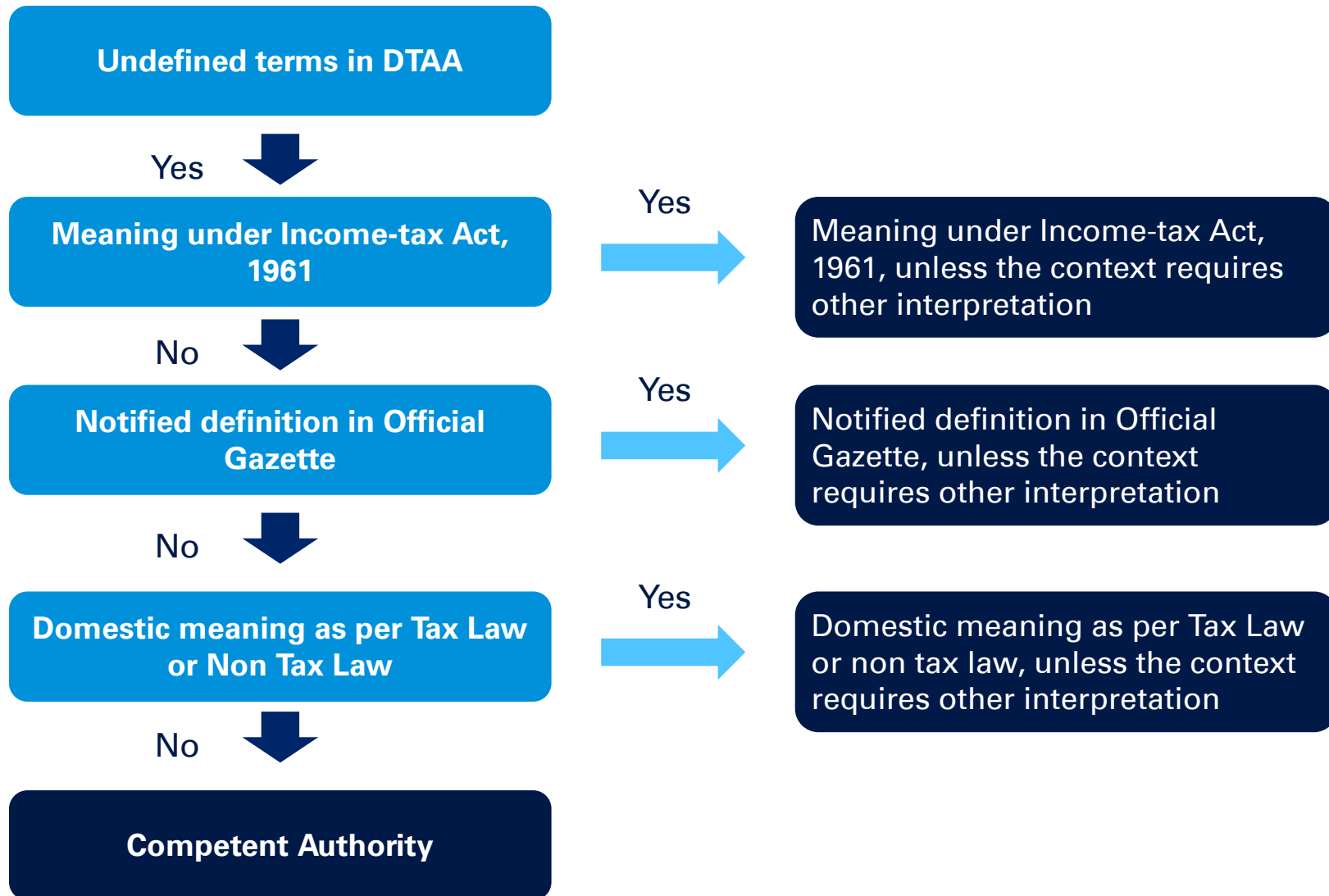
ARTICLE 3 **Definitions**

- Provides general definitions and rules of interpretation applicable throughout the convention

Terms generally defined in DTAA

- Person, Company, Enterprise, Enterprise of a Contracting State and the Enterprise of the other Contracting State, International traffic, Competent Authority, National and Business
 - “Person” includes an individual, a company and any other body of persons
 - “Company” means any body corporate or any entity that is treated as a body corporate for tax purposes
 - Limited Liability Partnership?
 - National – Individual possessing nationality or citizenship – Any legal person, partnership or association deriving its status as such from the laws in force
 - Definition of country very important
 - Northern Ireland is covered in India – UK DTAA and not under India – Ireland DTAA
 - India – China DTAA does not cover Hong Kong

Article 3 - General Definitions



Article 4 - Residence

ARTICLE 4

Residence

- Lays down criteria for determining residence of person
- “Resident of one of the States” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature

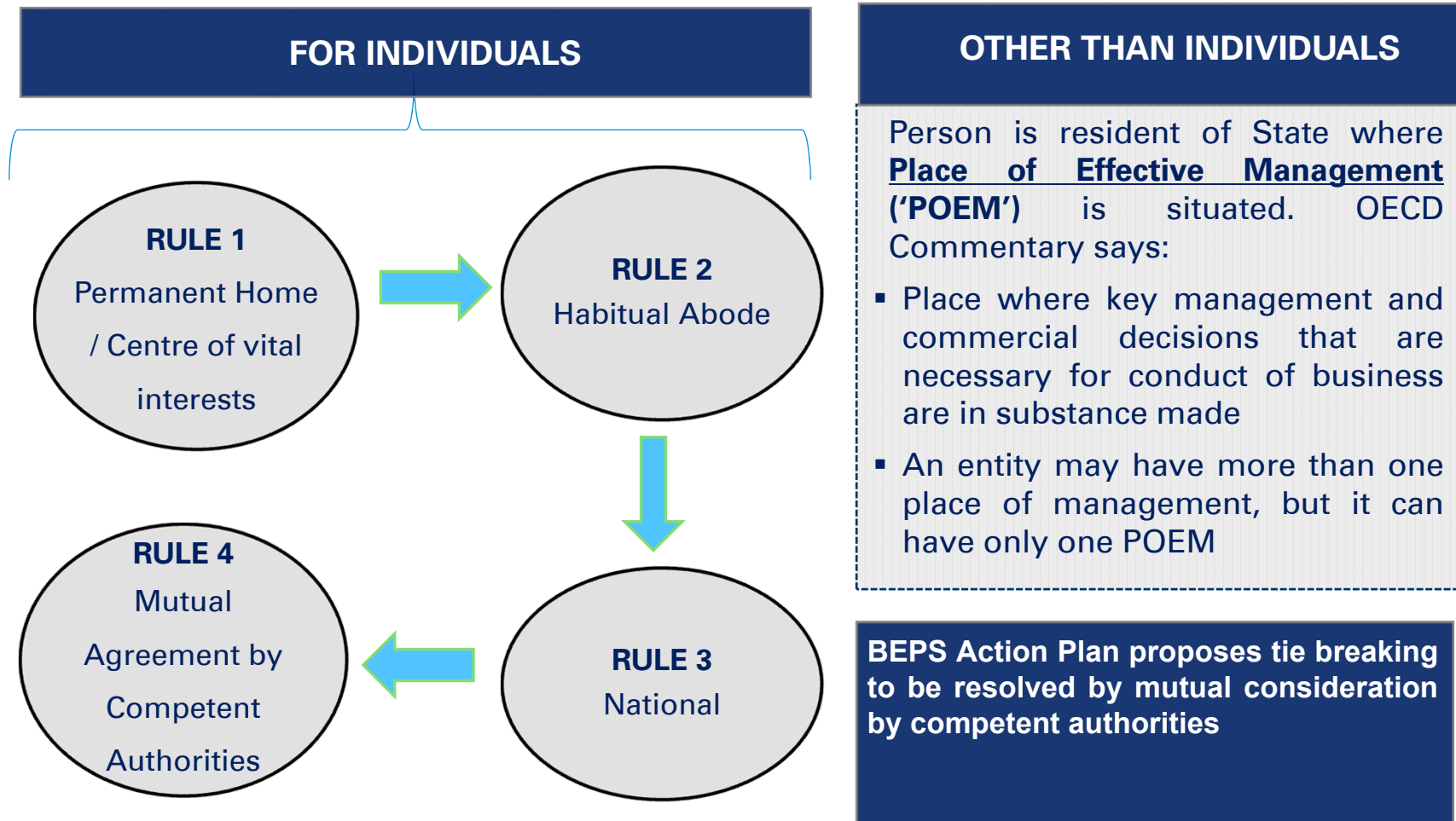
Objective

- The concept of 'resident of a Contracting State' is required
 - in solving cases where double taxation arises in consequence of double residence
 - in solving cases where double taxation arises as a consequence of taxation in the State of residence and in the State of source or situs
- The following articles of a treaty can be brought into operation even if a person is not a resident of either of the contracting states:
 - Article 24: Non-Discrimination: The application of this article is based on nationality rather than residence
 - Article 26: Exchange of Information: The contracting states can exchange information in respect of persons who are not resident of either of the contracting states

Article 4

What if person is a resident in both States ?

Tie-breaker applies if a person is resident in both States under Art. 4(1)



Case Studies

CASE STUDY # 1:



INDIA



U.K.

Facts & Assumptions:

- Mr. X is a citizen of UK. He travels to India on business and spent 200 days in India in 2018
- Resident of both countries under respective domestic tax laws
- He has a home in the UK and lives in a hotel in India.
- How is residency determined under the Treaty?

Internationally accepted standards on POEM

OECD Commentary

- POEM of an entity shall be determined by competent authorities of two countries by way of mutual agreement
- POEM determination is based on factors such as :
 - where the meetings of BOD are held;
 - where CEO and other senior executives usually carry on their activities;
 - where the company's headquarters are located; and
 - where its accounting records are kept.
- An entity may have more than one place of management, but it can have only one place of effective management at any one point of time

**Tie breaker
clause in
various
DTAAs**

UN Commentary

- The place where the company is actually managed and controlled
- The place where the decision-making at the highest level on the important policies essential for the management of the company takes place
- The place that plays a leading part in the management of a company from an economic and functional point of view
- The place where the most important accounting books are kept

**Definition of
POEM under
the Income-
tax Act, 1961**

Case Studies

CASE STUDY # 2:



Netherlands



India

Facts & Assumptions:

- XYZ is a company incorporated in Netherlands and is a tax resident of the Netherlands
- Its CEO and the Board of Directors meet in India and exercise control over its activities
- How will residence be determined under the India-Netherlands treaty?



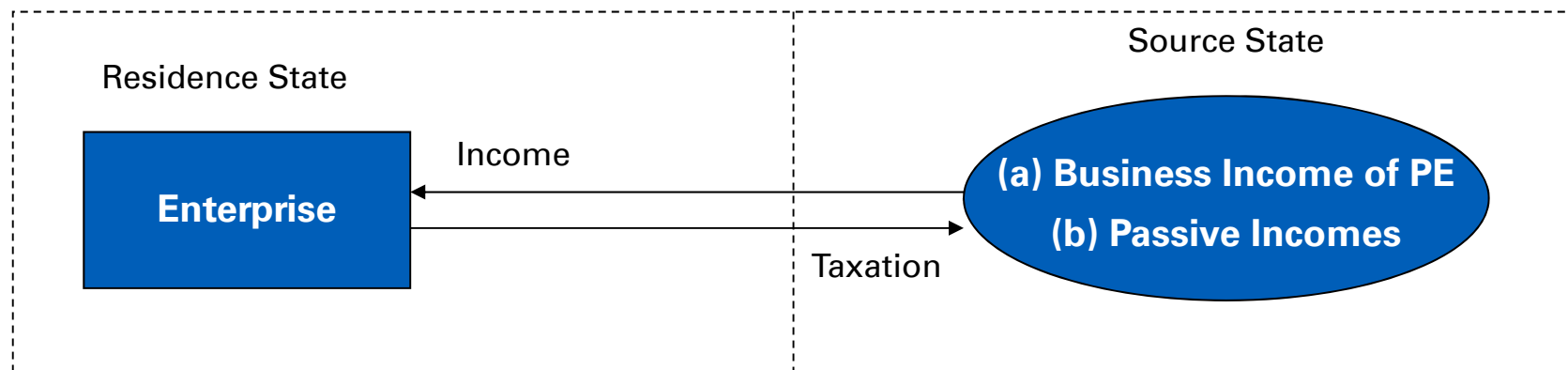
Article 5 - Permanent Establishment

Article 5 - Permanent Establishment

Concept of PE

- Entities increasingly engage in economic activities across several tax jurisdictions
- PE test determines the right of source state to tax business profits
- Defined concept under DTAA

Concept of PE – under Article 5 of the OECD Model Convention (MC)

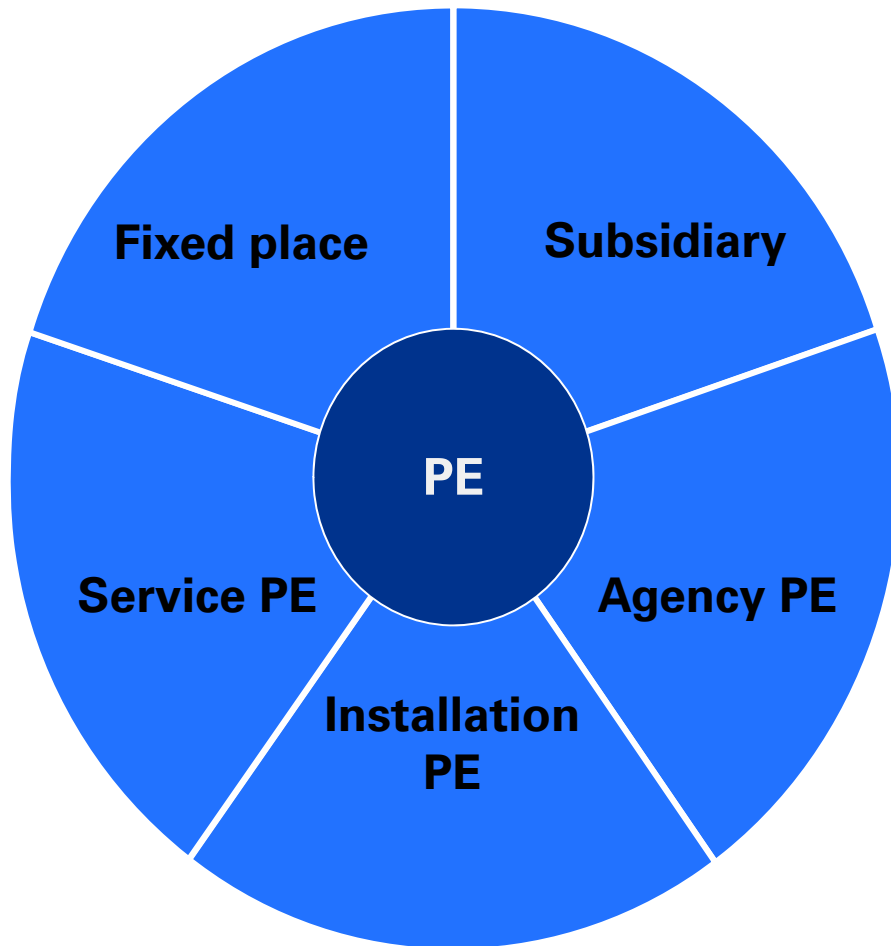


Source Country's right to tax Residents of Other Contracting State under DTAA:

- Taxation of passive income such as dividends, interest, royalties and fees for technical services on gross basis – income not effectively connected to PE
- Taxation of business income (including passive income) attributable to PE on net basis

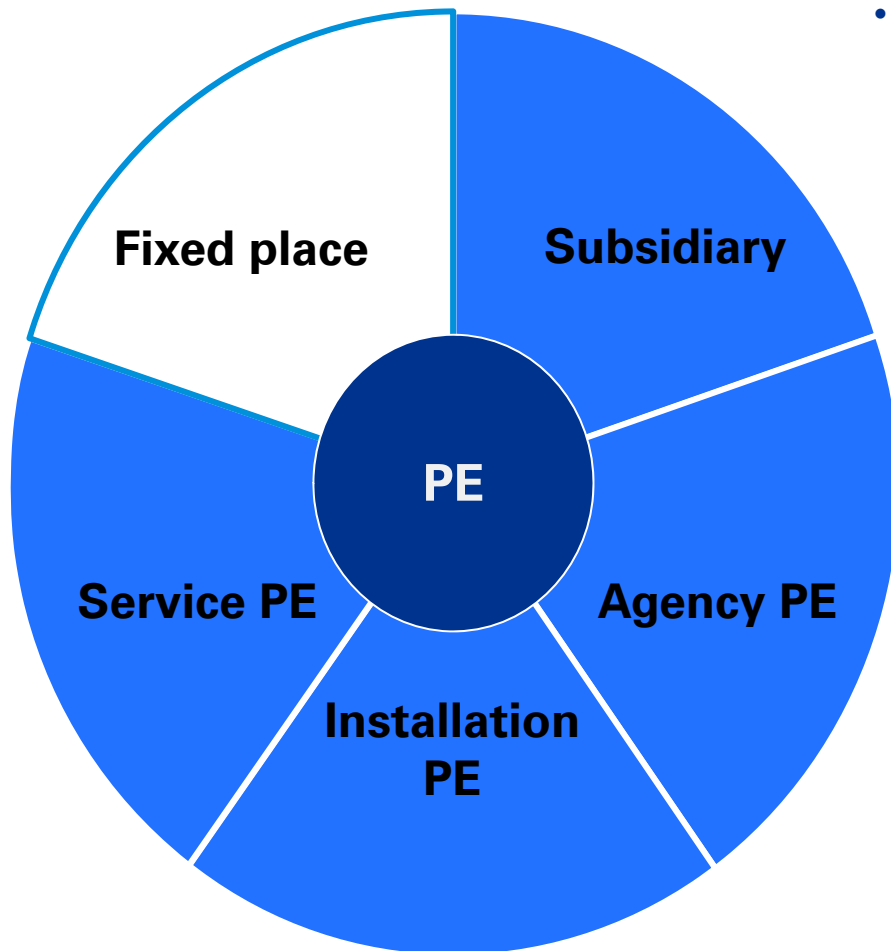
Article 5 - Permanent Establishment

PE definition under tax treaties



Article	Particulars	Type of PE
Article 5(1)	Basic rule	Fixed base PE
Article 5(2)	Illustrative list of PE	Inclusions to fixed base PE
Article 5(3)	PE in relation to projects	Construction / Installation PE
Article 5(4)	List of exclusions	Exclusion from fixed base PE
Article 5(5) & (6)	Dependent / Independent agent	Agency PE
Article 5(7)	Associated enterprise	Subsidiary PE

Article 5 - Fixed Base PE



- **Article 5(1) of the OECD MC governs basic rule for Fixed base PE:**

*“For the purpose of this Convention, the term ‘permanent establishment’ means a **fixed place of business** through which the **business of an enterprise is wholly or partly carried on**”*

Identical definition under UN and US Model

Elements of Fixed base PE:

- Existence of ‘place of business’ and place should be at the disposal of FCo – disposal test
- Place of business must be ‘fixed’ – permanence test
- Business is carried on wholly or partly through fixed place of business – business activity test

Above conditions need to be cumulatively satisfied

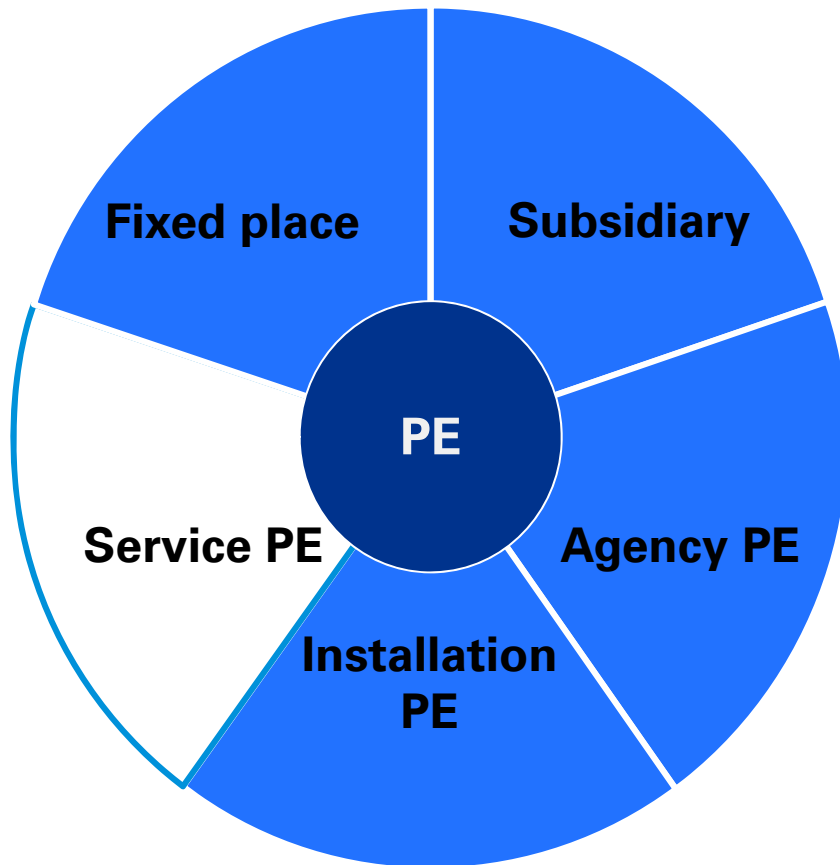
Article 5 - Inclusions to PE

- **Article 5(2) of the OECD MC provides an inclusive definition of PE which reads as under:**
 - a) *“The term ‘permanent establishment’ includes especially:*
 - b) *a place of management;*
 - c) *a branch;*
 - d) *an office;*
 - e) *a factory;*
 - f) *a workshop, and*
 - g) *a mine, an oil or gas well, a quarry or any other place of extraction of natural resources”*
- **The list is indicative and not exhaustive**

Whether Article 5(1) & 5(2) are Independent?

Article 5 - Service PE

Service PE

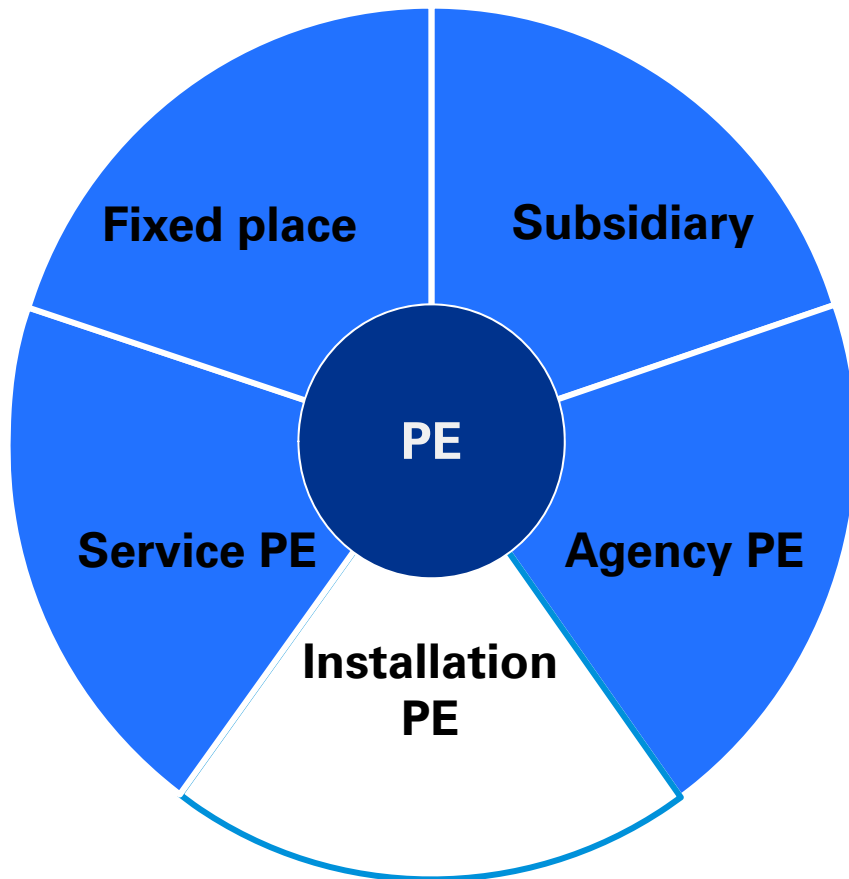


- Furnishing of “services” within India
- Through employees or other personnel
- Residential status of recipient of service is an irrelevant factor
- Activities continue for a period exceeding 90 days (30 days or one day where services are rendered by associated enterprises)
- No service PE clause in some Treaties – Netherlands, Denmark, France & Mauritius
- Services categorized as FTS / Royalty not covered

Secondment of employees

Article 5 - Construction/ Installation PE

Construction / Installation PE



- **Article 5(3) of OECD Model Convention**

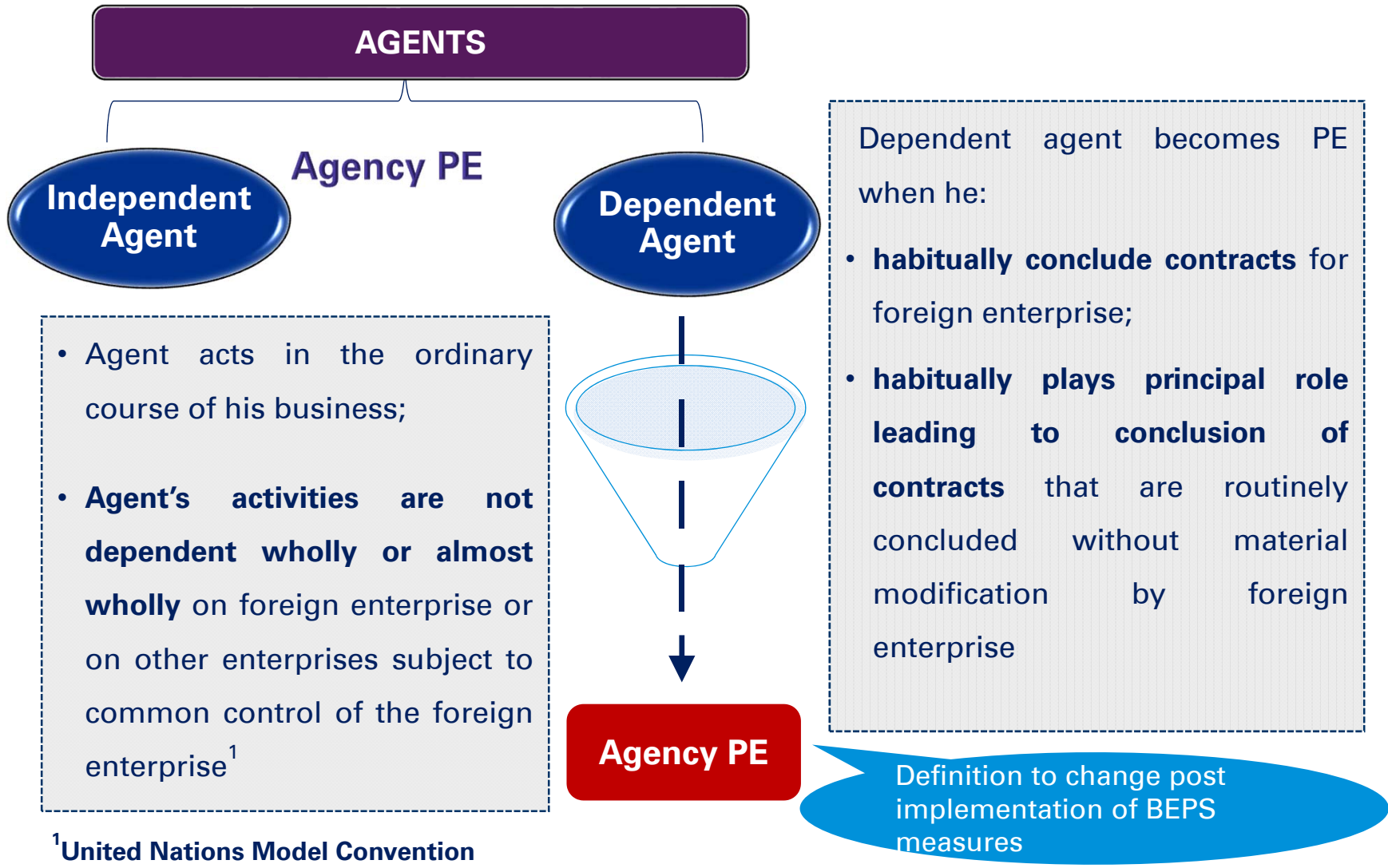
“A building site or construction or installation project constitutes a permanent establishment only if it lasts more than twelve months”

- **Includes:**

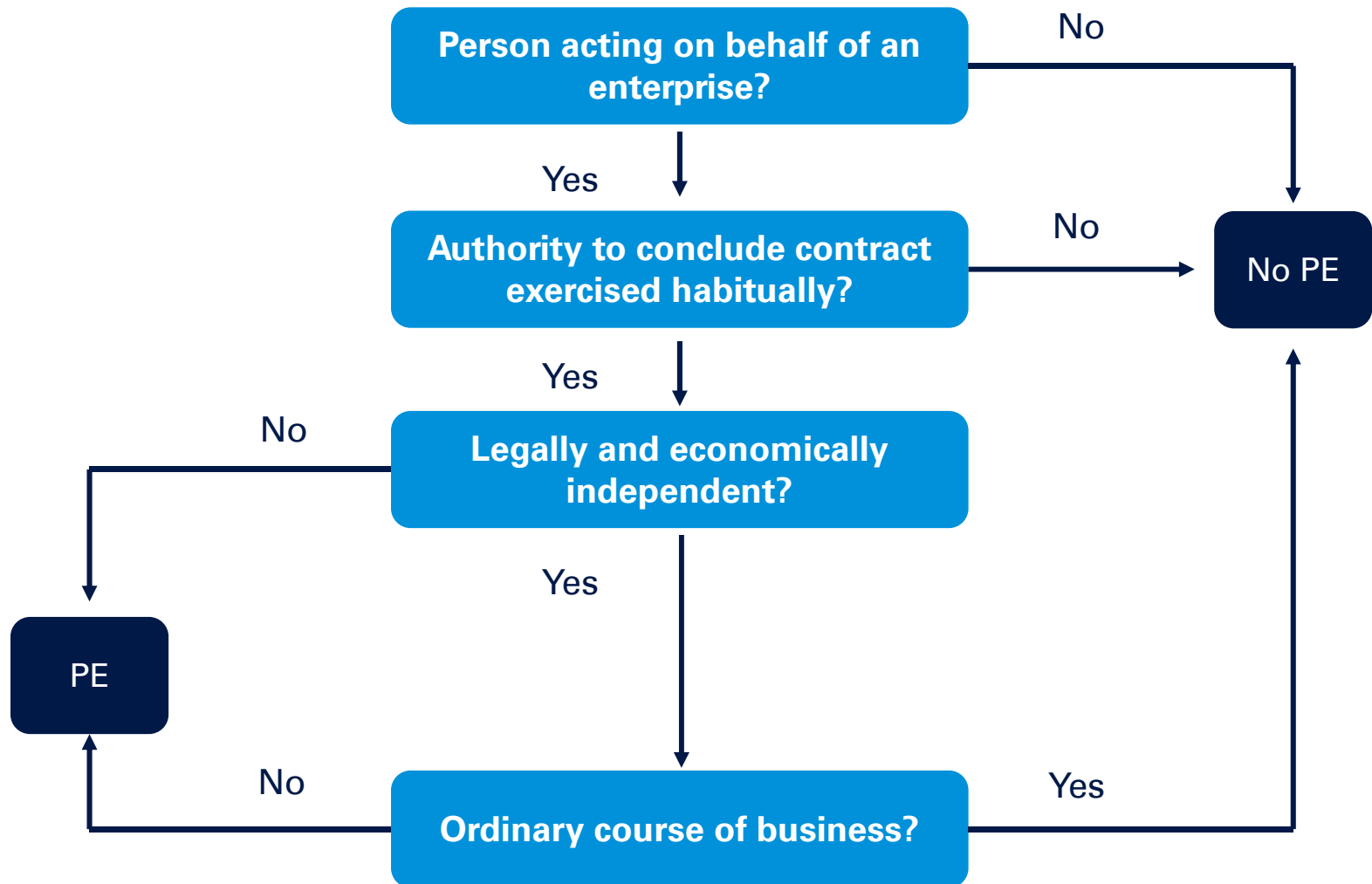
- Construction of roads, bridges, canals, including substantial renovation
- Laying of pipelines, excavating and dredging
- “Installation Project” includes installation of ‘new equipment’ (complex machine)
- Includes assembly and supervisory activities

Some of India’s DTAA prescribe a 9 month period while the DTAA with US prescribes a threshold of 120 days

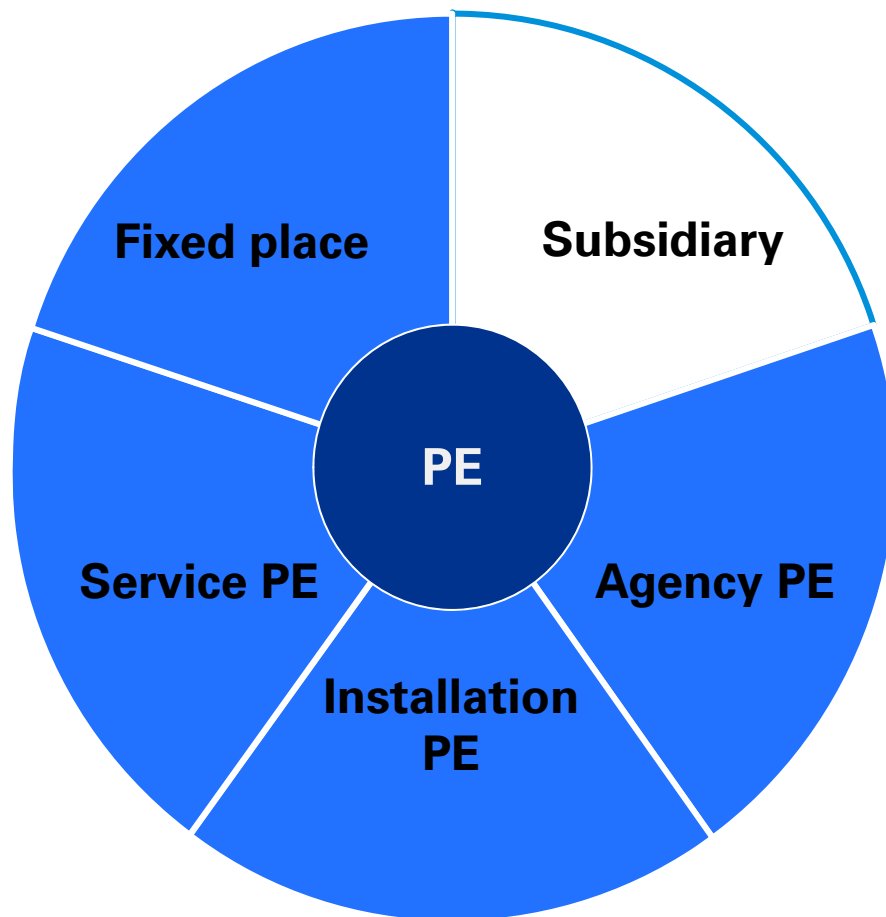
Article 5 - Agency PE



Article 5 - Agency PE



Article 5 - Subsidiaries and PE

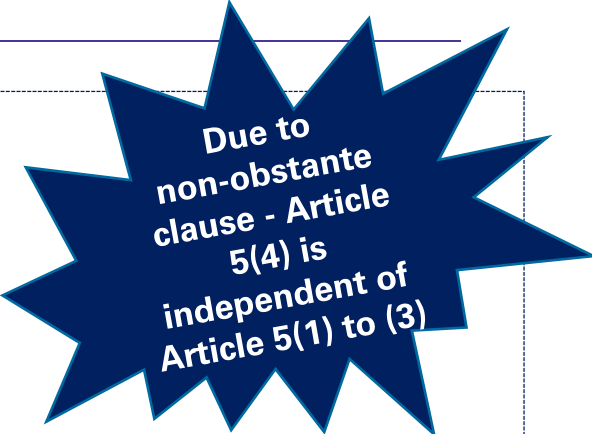


- **Article 5(7) of OECD MC reads as under:**
 - *“The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a PE or otherwise), shall not of itself constitute either company a PE of the other.”*
- **Definition is identical under UN MC and US Model**
- **Existence of a subsidiary by itself does not constitute PE**
 - Legal independence of the subsidiary respected
- **Test of fixed base PE / service PE / agency PE need to be satisfied**

Article 5 - Activities that do not result in PE

Exceptions in Article 5(4)

- *Use of facilities for storage or display of goods*
- *Maintenance of stock of goods for storage or display*
- *Maintenance of stock for processing of goods*
- *Purchasing goods or merchandise or for collecting information for the enterprise*
- *Carrying on, for the enterprise, any other activity of a preparatory or auxiliary character*



Due to non-obstante clause - Article 5(4) is independent of Article 5(1) to (3)

Impact of BEPS on Article 5(4)?

Article 5 - Quiz

Whether an LLP in which a foreign company is a partner be construed as a PE?

Whether Project Office is a PE?

Is duration important for analysis of Installation PE?

Whether a dependent agent securing orders in India constitute a PE?

Whether a Liaison office conducting preparatory activities constitute a PE?

Whether purchasing activity by Liaison office of FCo constitutes PE



Article 7 - Business Profits

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ARTICLE 7

Business Profits

- Existence of PE must for attribution
- Only profits attributable to such PE is taxable in the source country
- PE test for each source of income
- Principle of “force of attraction” present in UN Model

Force of Attraction

- Primarily concerned with taxation of business profits in Source Country
- Prevents tax evasion / avoidance through artificial contracts / business arrangement
- Identification of business transactions – source based taxation

Types of Force of Attraction

- **General** Force of Attraction
- **Restricted** Force of Attraction



Article 9 - Associated Enterprise

Article 9 - Associated Enterprise

Article 9(1)

Applicability:

- (a) Direct or indirect participation by one entity into capital, management or control of other entity; OR
- (b) Same person participates directly or indirectly into capital, management or control of both enterprises



Transactions are not commensurate with a transaction as would have been carried out between independent enterprise (Arms' Length Price ('ALP'))

Impact

Profits which, but for those conditions would have accrued to one of the enterprises, but by reason of those conditions have not so accrued, may be included in the profits of that enterprise and taxed accordingly

Article 9(2)

- Where the transactions between two entities is not at ALP and
- Profits of one entity are re-determined on account of transfer pricing adjustments then
- Enhanced income shall be chargeable to tax in one country and the other country shall provide a tax relief to the extent of enhancement
- Corresponding adjustment available to eliminate economic double taxation



Article 6 - Income from Immovable Property

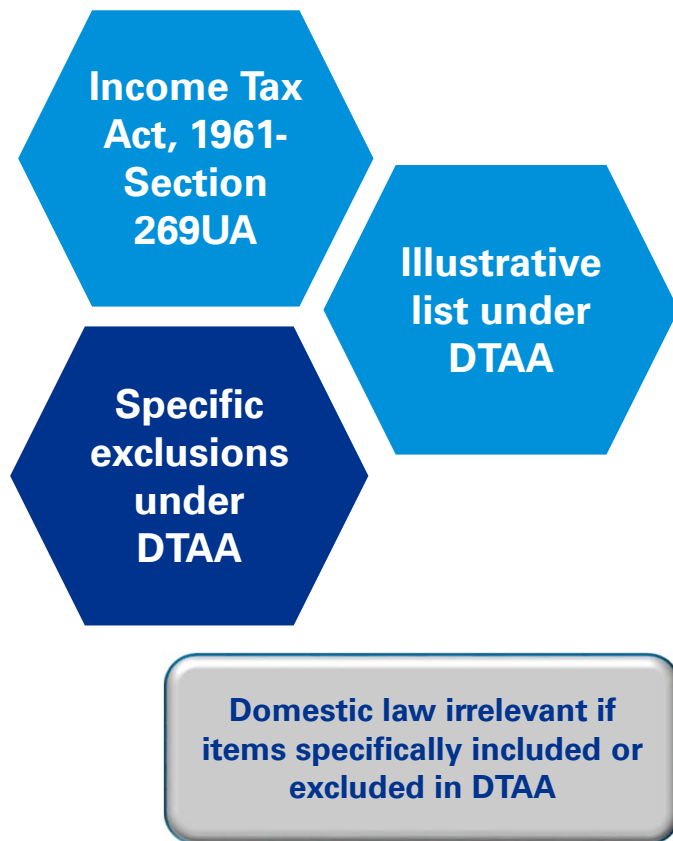
Article 6 - Income from Immovable Property

Para 1 of Article 6 – Applicability – Charging provision

- A resident of Contracting State (State of Residence) derives income;
- Such income is derived from immovable property or agriculture or forestry; and
- Such immovable property is situated in other Contracting State (State of Source)

Article 6 - Income from Immovable Property

Para 2 of Article 6 – Meaning of Immovable property



Para 2 of Article 6 – Inclusions and Exclusions

- **Inclusions as per DTAA**
 - property accessory to immovable property (e.g. Buildings)
 - livestock and equipment used in agriculture and forestry (e.g. Machinery used in Saw mill)
 - rights to which the provisions of general law respecting landed property apply (e.g. Rights covered under Transfer of Property Act)
 - usufruct of immovable property (i.e. income without ownership of the asset)
 - rights to variable or fixed payments as consideration relating to working of, or the right to work, mineral deposits, sources and other natural resources
- **Exclusions as per Treaty**
 - Ships, boats and aircrafts

General Rule – Whatever is affixed or attached to land becomes a part of the land

Article 6 - Income from Immovable Property

Para 3 of Article 6 – Meaning of 'use'

- **Forms of Exploitation**
 - Direct use
 - Letting Out
 - **Use in any other form**

Para 4 of Article 6 – Additional scope

- **Extends scope of situs based taxation**
 - Income earned by an enterprise (PE of non resident in source country) from immovable property
 - E.g. relinquishment of property for use by a third party



Article 8 - Shipping and Air Transport

Article 8 - Shipping And Air Transport

Article 8(1)

Profits from operation of ships or aircraft in international traffic taxable in contracting state in which place of effective management situated

KEY CONDITIONS

- Profits
- Operation of ships or aircraft
- International traffic
- Place of Effective Management (POEM)

Article 8 - Shipping And Air Transport

Article 8(1) - Meaning of 'profits'...

Profits - directly connected with operation

- Enterprise engaged in international traffic that would have some of its passengers or cargo transported internationally by ships or aircraft operated by other enterprises eg. under code-sharing or slot-chartering arrangements or take advantage of an earlier sailing
- Lease of containers by shipping lines or airlines

Profits – ancillary to operation

- Make minor contribution relative to operation of ships
- So closely related that it cannot be regarded as separate business or source of income
- Eg. Advertisement in magazines aboard ships, on board sale of products, etc.

Article 8 - Shipping And Air Transport

'operation of ships or aircraft'...

- Generally, not defined under DTAA
 - Expressions not defined in DTAA - meaning to be ascertained as per domestic laws [Article 3(2)]
- 'Operation of ships' - defined u/s 115VB of IT Act
 - **Company regarded as operating, if it operates any ship (owned or chartered) and includes arrangement such as slot charter (i.e. a slot for a container on a ship)**

Bareboat charter hire

- Payment to owner for hire of bare vessel
- Not considered as 'operation of ship' by lessor - (crew of) lessee operating the ship
- Considered as 'Royalty' for use of equipment
- West Asia Maritime Ltd. v. ITO (109 TTJ 617)(ITAT, Chennai)
- Poompuhar Shipping Corporation Ltd. v. ITO (108 TTJ 970)(ITAT, Chennai)
 - Payment was for 'use and hire of vessel', not for services

Time charter hire

- Payment to owner for hire of vessel with crew and equipment - viz. provision of services
- Considered as 'operation of ship' by lessor - Article 8 benefit available to lessor
- OECD and Klaus Vogel clearly recognise time charter as operation of ships by lessor

Slot Charter

- Payment to owner for hire of slots (space), aboard a container ship
- Considered as 'operation of ship' by lessor - Article 8 benefit available to lessor - **Balaji Shipping (UK) Ltd.**

Article 8 - Shipping And Air Transport

Meaning of 'international traffic'

- Defined under Article 3(1)(e) of DTAA
 - Transport by ship or aircraft operated by enterprise which has its POEM in a contracting state (*prevailing assumption that operations shall be between both contracting states*)
 - Coastal traffic - operation solely between places in other contracting state not covered
 - Illustration

International traffic

- Ships / aircraft plying :
 - Colombo (Sri Lanka) - Chennai (India)
 - Colombo (Sri Lanka) - Chennai (India) - Mumbai (India)
 - Colombo (Sri Lanka) - Chennai (India) - Dubai (UAE)

Not international traffic

- Ships / aircraft plying:
 - Chennai (India) - Colombo(Sri Lanka) (not stopping)- Mumbai (India)
 - Chennai (India) - Mumbai (India)



Article 10 - Dividend
Article 11 - Interest

Article 10 & 11 - Dividend / Interest

ARTICLE 10 **Dividend**

- Source-based taxation
- Dividend – Income from shares, participating in profits rights, other rights not being debt claims, etc.
- Tax Treaty imposes a limitation on the maximum rate to be charged by the source country
- Generally, the condition of “beneficial owner” exists
- Dividends earned if “effectively connected” with PE taxed under Article 7

ARTICLE 11 **Interest**

- Source-based taxation
- Interest – income from debt claims of every kind, income from government securities, income from bonds and debentures
- Tax Treaty imposes a limitation on the maximum rate to be charged by the source country
- Generally, the condition of “beneficial owner” exists
- Interest earned if “effectively connected” with PE taxed under Article 7



Article 12 - Royalty /
Fees for Technical Services

Article 12 - Royalty

OECD MC

ARTICLE 12

Payments of any kind received as a consideration for:

- Use of or right to use:
 - any copyright of literary, artistic or scientific work including cinematograph films;
 - any patent, trademark, design or model, plan, secret formula or process
- information concerning industrial, commercial or scientific experience

UN MC

Apart from the above, notable inclusions are use of or right to use

- films or tapes used for radio or television broadcasting
- Industrial, commercial or scientific equipment

Article 12 - Royalty

Article 12(1)

Royalty of source country may be taxed in other country of which the recipient is a resident

Royalty may also be charged in the source country, but if beneficial owner of royalty is a resident of other country the tax charged shall not exceed specified percent of gross amount of royalties

Article 12(2)

Deals with the meaning of "Royalties"

Article 12(3)

Para (1) to not apply if the

- royalty is effectively connected with PE; or
- the recipient has a fixed Base in the State of Source

Article 12 - Fees for Technical Services

There is no specific article on FTS in either OECD / UN / US MC - it treats it on par with Business Income (Article on FTS at draft stage in UN MC)

Fees for Technical Services

Payments to any person in consideration of managerial, consultancy and technical services including provision of services of technical or other personnel

Managerial Services

Essentially involves controlling, directing or administering the business

Technical Services

Provision of services which require special skills or knowledge related to a technical field

Consulting Services

Provision of advice by someone, such as a professional, who has special qualifications allowing him to do so

Article 12 - Fees for Technical Services

Article 12

Fees for Included Services

- Payments of any kind to any person in consideration for the rendering of any technical or consultancy services if such services:
 - Are ancillary and subsidiary to application and enjoyment of right; or
 - Make available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design

Managerial Services are excluded under the definition of FIS

Excludes services ancillary to sale of property, rental of ships, aircraft, containers or other equipment's, teaching in or by educational institutions, for personal use and to an employee of person making the payment

Article 12

Make Available

- Person acquiring the service is enabled to apply the technology
- Mere requirement of technical input by a person providing services does not necessarily mean that technical knowledge is "made available"



Article 13 - Capital Gains

Article 13 – Capital Gains

Article 13	Type of Capital Asset	OECD Model	UN Model
Para 1	Alienation of immovable property	Taxable in COS	Taxable in COS
Para 2	Movable property forming part of business property of a PE, including gains from alienation of PE itself either alone or along with the entire enterprise	Taxable in COS	Taxable in COS
Para 3	Gains from alienation of ships, aircrafts, or boats or movable property relating to operations in international traffic	Taxable in country of POEM	Taxable in country of POEM
Para 4	Gains from alienation of shares of company resident in source country, deriving their value mainly from immovable property in source country	Taxable in COS	Taxable in COS
Para 5 (Para 6 in UN Model)	Gains from alienation of any other property not included in the Article	Taxable in COR	Taxable in COR
Para 5 in UN Model	Gains from sale of shares of a company resident in source country, other than discussion in para 4 above	Not found in OECD Model, taxable in COR	Found in UN Model, taxable in COS, subject to negotiation



Article 14 - Independent Personal Services

Article 14 - Independent Personal Services

Deals with taxation of income in respect of professional services or other activities of independent character

Taxable in source state if

Regular fixed base available in that state or;

Stay exceeds threshold period mentioned

Amount taxable – only amount attributable to fixed base or activities carried out in source state

Professional services includes especially independent scientific, literary, artistic, educational or teaching activities as well as independent activities of physicians, lawyers, engineers, architects, dentists and accountants

OECD deleted this article w.e.f. the year 2000



Article 15 - Dependent Personal Services

Article 15 - Dependent personal services

Remuneration derived by a resident of a Contracting State in respect of an employment exercised in other Contracting State is taxable in the State of Residence

Taxable in source state if any one of the following conditions satisfied:

Presence in source state for period or periods exceeding specified threshold

Remuneration is paid by or on behalf of resident of source state

Remuneration is borne by PE which the employer has in the source state

Short stay exemption under the Income-tax Act, 1961 Section 10(6)(vi)

- **Employee of foreign enterprise renders service in India**
- **Foreign enterprise is not engaged in any trade/ business in India**
- **Stay in India does not exceed 90 days**
- **Remuneration is not deductible from income of the employer**



Article 16 - Directors' Fees

Article 17 - Entertainers & sportspersons

Article 18 - Pensions

Article 19 - Government Service

Article 20 - Student

Article 16, 17, 18 – Directors' Fees / Entertainers & Sportspersons / Pension

ARTICLE 16

Directors' Fees

- Payments include Director's Fees, payments in cash or kind received in capacity as a Director; severance pay, annuity, etc. in connection with directorship
- Taxable in country of residence of company

ARTICLE 17

Entertainers & Sportspersons

- Overrides Article 7, 14 and 15 of the MC
- Income is taxable in the country in which activities are performed
- Deals with situations where their income accrues to another person (taxable in country in which activities are performed)

ARTICLE 18

Pension

- Applies to individuals only
- Covers private pension and other similar payments (annuity) in consideration of past employment
- Taxable in country of residency

Article 19 & 20 - Government Service / Student

ARTICLE 19

Government Service

- Applies to Individuals only
- Covers salaries, wages and similar remuneration paid by Contracting Country, Political sub division or a local authority
- Pensions from Government
- Primary right to tax is of the Country that makes the payment
- Other contracting state has right to tax if recipient is national or resident of other state

ARTICLE 20

Student

- Period of stay to be in accordance with the education / training
- Payments not to exceed expenses likely to be incurred to ensure student's maintenance, education or training



Article 21 - Other Income

Article 21 - Other Income



Residuary Article



'Element of Income' to be present



Any income not dealt with in earlier articles covered here



Other Income connected with PE will be covered under Article 7 or Article 14 respectively

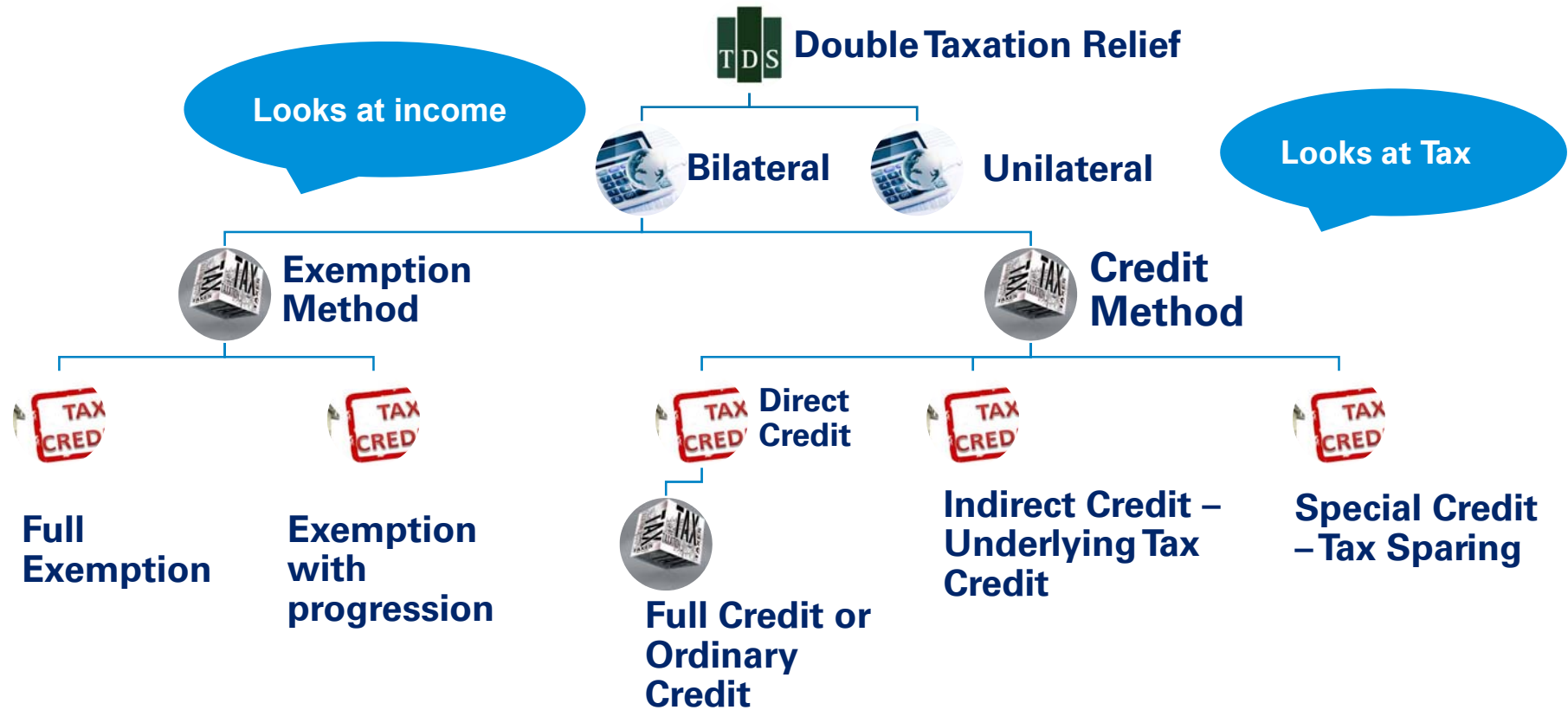


Shared taxation rights between Source Country and Residence Country



Article 23 - Elimination of Double Taxation

Article 23 - Elimination of Double Taxation



Two contracting states in DTAA's can agree to follow different methods for eliminating double taxation

Article 23 - Elimination of Double Taxation

Exemption Method

Full Exemption

- In this method income taxed in source country is totally excluded in resident country for tax purposes.

Exemption with progression method

- Rate of tax is calculated by COR by including income taxed in COS. Then such rate is applied on income excluding income taxed in COS.
- **In the following treaties with India, exemption method has been followed:**
 - By both the states:
 - Bulgaria, Poland and Egypt
 - By the other states (i.e. the other states adopts exemption method and India adopts Tax Credit method):
 - Austria, Belgium, Turkey

Article 23 - Elimination of Double Taxation

Credit Method

Full Credit method

- Under this method COR allows foreign taxes from total tax liability irrespective of different tax rates in COR and COS.

Ordinary Credit method

- COR allows tax credit by restricting it to the rate of tax in COR against income taxed in COS.

Underlying Credit method

- Credit for corporate tax is available when dividends are paid by resident of one state to another. This is in addition to tax paid on dividends

Dividend and Interest always follow tax credit method
Tax credit method – Resident state retains the right to tax

Article 23 - Elimination of Double Taxation

Full credit method

A Ltd, a resident of State R, has earned a total income of Rs 1 Lac. Of its total income, Rs. 20000/- is derived from State S. State R imposes tax of 35%. State S imposes tax of 40%. In this case the credit would be computed as follows

Particulars	Credit Mechanism does not exist	Credit Mechanism exists
Amount of income earned	1,00,000	1,00,000
State R Tax	35,000	35,000
State S Tax	8,000	8,000
Tax credit available	-	8,000
Taxes due in State R	35,000	(35,000-8,000) 27,000
Total tax cost	43,000	35,000

Article 23 - Elimination of Double Taxation

Ordinary credit method

A Ltd, a resident of State R, has earned a total income of Rs 1 Lac. Of its total income, Rs 20,000 is derived from State S. State R imposes tax of 35%. State S imposes tax of 40%. In this case the credit would be computed as follows :

Particulars	Credit Mechanism does not exist	Credit Mechanism exists
Amount of income earned	1,00,000	1,00,000
State R Tax	35,000	35,000
State S Tax	8,000	8,000
Tax credit available	-	(20,000*35%) *7,000
Taxes due in State R	43,000	28,000
Total tax cost	43,000	36,000

**Maximum credit restricted to 7000 (35% which is tax rate in State R on the income earned in State S)*

Article 23 - Elimination of Double Taxation

Underlying Tax Credits (UTC)

Certain DTAA's offer UTC as a method for providing relief to Doubly Taxed Income.

Company in State S	Amount
PBT	300,000
Tax @ 30%	90,000
PAT	210,000
Dividend Distribution	210,000

- Company in State R holds 80% stake in Company in State S and receives dividend of 1,68,000 (210,000 @ 80%) from Company in State S
- TDS by State S – 33,600 (168,000 @ 20%); Net dividend received by Company in State R – 134,400
- Tax rate in State R – 35%
- *Assumption:* Dividend Income is the only income of Company in State R and it has no deductible expenses

Article 23 - Elimination of Double Taxation

Underlying Tax Credits (UTC)	
Particulars	Amount
Net Dividend Income received in State R	134,400
Add: Taxes Withheld	33,600
Gross Dividend Income	168,000
Underlying tax credit = Gross Dividend / Distributable profits x Actual tax paid on those profits (1,68,000 / 2,10,000 * 90,000)	72,000

Article 23 - Elimination of Double Taxation

Tax Sparing

Need

- Source State may provide tax incentives on certain income
- State of Residence may tax that income
- Result – Country of residence may collect taxes foregone by Source Country

What does Tax Sparing mean?

State of residence –

- grants credit for deemed tax paid on income otherwise exempt in Source State
- considers tax payable; not tax paid

Article 23 – Unilateral Tax relief illustration

Section 91 of the Income-tax Act, 1961:

- Applicable to cases where there is no DTAA with foreign country in which tax is paid / liability incurred
- Quantum of Relief - Proportionate method *i.e.* lower of 'Indian Tax Rate' or ' Foreign Tax Rate' (Ordinary Credit method and not full method)

Particulars		Case I	Case II
Income in India		150,000	150,000
Income in foreign country		100,000	100,000
Total income		250,000	250,000
Tax rate in India		30%	30%
Tax rate in foreign state		25%	35%
Workings			
Income tax on total income	(A)	75,000	75,000
Indian tax on foreign income	(B)	30,000	30,000
Foreign tax on foreign income	(C)	25,000	35,000
Unilateral tax relief as per the Act – Lower of (B) or (C)	(D)	25,000	30,000
Tax payable in India (A) – (D)	(E)	50,000	45,000
Total tax outflow (B) + (E)		75,000	80,000
Effective tax rate		30%	32%



Article 24 - Non-discrimination

Article 24 – Non-discrimination

- Prevention of discrimination under tax laws of the host country on account of the following four criteria:
 - Nationality of the taxpayer [Art 24(1)] and [Art 24(2)] – tax deductions?
 - PE in the host country [Art 24(3)]
 - Deduction - Payment of interest, royalties, other consideration, etc. to a recipient abroad [Art 24(4)]
 - Holding of shares in a resident enterprise by non-residents [Art 24(5)] – section 79?
- Other provisions:
 - Stateless Persons [Art 24(2)]
 - Inclusion of other taxes [Art 24(6)]



Article 25 - Mutual Agreement Procedures ('MAP')

Article 25 - MAP

- MAP is an alternative available to taxpayers for resolving disputes giving rise to double taxation – juridical or economic
- Taxpayer of the country having to bear the incidence of double taxation can apply for assistance of competent authorities ('CA') under MAP to resolve the issue of such double taxation
- Agreement of CAs of both the states
- No obligation of CAs to reach mutual agreement
- Notwithstanding remedy under domestic tax law of source state
- Time limit for filing of MAP – generally 2 / 3 years from the date of original assessment giving rise to double taxation
- Generally in case of:
 - Specific Provisions where taxation is not in accordance with the DTAA
 - General Interpretation issues such as those under Article 4 – Resident
 - Issues not covered under DTAA such as economic double taxation, including TP adjustments of their resident countries



Steps for applying tax treaties

Steps for applying tax treaties

Step 1 – What is the nature of the income?

Step 2 – Does the treaty apply?

Step 3 – Determine which article applies?

Step 4 – How are taxing rights assigned?

Step 5 – How is the income calculated?



Limitation of Benefits

Limitation of Benefits (LOB)

- Intention is to prevent misuse of tax treaties by third countries
- Generally, a LOB clause in a DTAA is designed to test the substance of a claimant to the DTAA
- Condition is satisfied where certain objective criteria's are met – residential status of shareholders, listing, active trade / business activity, minimum expenditure, etc.
- LOB articles in treaties vary between each treaty in terms of conditions and complexity
- India – US DTAA is India's first DTAA with LOB clause
- BEPS Action Plan 6 – Treaty abuse recommends LOB article to be included in DTAA, objective rule plus subjective Principal Purpose Test

Limitation of Benefits (LOB)

Form of LOB

- Place of Effective Management
- Beneficial owner
- Subject-to-tax or liable-to-tax approach
- Specific article on LOB

Examples of Indian treaties with LOB

Clause:

- India USA DTAA
- India Singapore DTAA
- India Kuwait DTAA

- In the India – US DTAA (Article 24) is as follows:
 - Beneficial ownership test i.e. who are actual owners holding more than 50% of the company's shares
 - Base erosion test i.e. income is not used directly or indirectly to meet liabilities outside the contracting states of a DTAA
- Protocol to India-Singapore DTAA
 - Shell or conduit company set-up or where the affairs are arranged with a primary purpose to take the benefit of favorable capital gains clause



Beneficial Owner

Beneficial Owner

- Critical condition for availing benefit of DTAA in case of interest, dividend, royalty and FTS income
- BO not defined in tax treaties
- Conduit companies are classic case of non-beneficial ownership
- OECD recognized that in many situations person to whom income was paid might be the bare legal owner (e.g. a nominee – such as custodians use – or an agent) with no rights to the income
- 2010 OECD Commentary indicates that term “beneficial owner” should not be used in a narrow technical sense but should be in its context and light of the objectives of OECD MC - avoiding double taxation and preventing fiscal evasion and avoidance
- As per 2017 OECD update, recipient of said income is BO when:
 - He has right to use and enjoy such income;
 - Unconstrained by a contractual / legal obligation to pass on the income to another person
- CBDT Circular No. 789 dated 13 Apr 2000 states that Tax Residency Certificate issued by the Mauritian authorities is sufficient evidence of BO (followed by SC – Azadi Bachao)



Most Favored Nation Clause

Most Favored Nation Clause (MFN Clause)

- MFN clause usually found in Protocols and Exchange of notes
- Benefit generally restricted to specific group countries like OECD countries or developing countries
- Benefit could be either lower rate or narrowing of scope
- Attempts to avoid discrimination between residents of different countries
- Ensures equal treatment between a subset of countries
- Extends similar benefits to one country as extended to certain other countries

MFN Clause - Sample

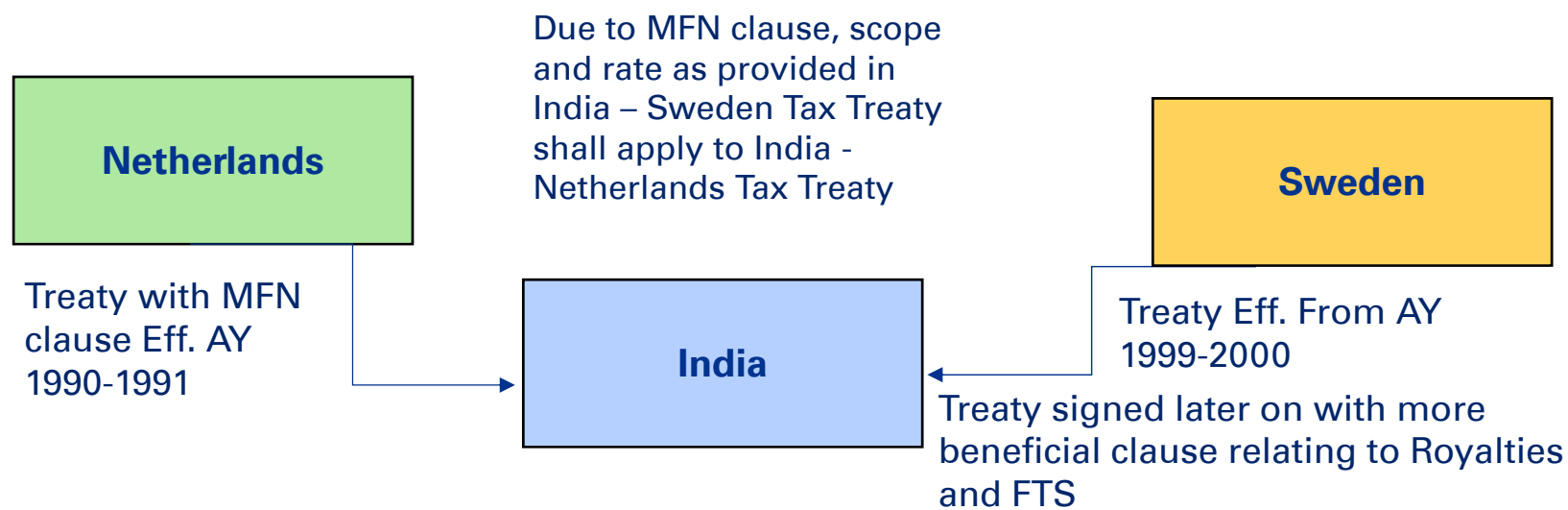
- MFN CLAUSE IN THE PROTOCOL:

“In respect of Dividends, Interest, Royalties, FTS and payment for use of equipment, if under any Convention, Agreement or Protocol signed after 1st Sept 1989, between India and a third State which is a member of the OECD, India limits its taxation at source on dividends, interest, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention, Agreement or Protocol on the said items of income shall also apply under this Convention ...”

MFN Clause

- Applying the MFN Clause

Example: In a MFN situation, generally, one of the contracting states (say India) to the DTAA grants the residents of the other contracting state (say Netherlands), the same beneficial treatment made available by it (that is, by India) to the resident of a third country (say Sweden) with whom it has entered into a Tax Treaty





BEPS

Key causes of BEPS

- MNEs use wide range of cross border tax planning techniques that results in little or no tax liability – such results are referred to as “base erosion and profit shifting”
- OECD and G20 jointly established BEPS project to address global concerns
- This effort is supported by the G7 and G20 countries, the European Union (EU) has been working in parallel, and developing countries are involved as well
- In October 2013, the UN Committee of Experts on International Co-operation of tax matters established a sub-committee on BEPS issues for developing countries
- The sub-committee is mandated to work with relevant bodies and OECD with a view to highlight issues on BEPS with officials in developing countries.
- On 5 October 2015, the OECD issued its ‘final’ reports on the 15 Action points identified in its Action Plan on BEPS. The reports have been the subject of consultation and the content of the reports is largely in line with expectations.



Key Take Aways

Key Take Aways

- Significant increase in Cross border transactions – not restricted only to big cos. but even SMEs - this leads to increase in International Tax Issues
- Need to look at arrangement holistically
- Need for corporates to respond proactively to evolving PE-related concepts
- Indian law also incorporating amendments in laws to align with tax treaties
- Importance of International Tax is gaining with every day
- As of 2019, the BEPS treaty changes could be included in many of the existing 3000 bilateral treaties.
- Review tax treaty positions. Potential impact for dividend, interest and royalty transactions and for capital gains.
- Monitor implementation of the MLI per jurisdiction, including implementation of the minimum standards.
- Interpretation of tax treaties is expected to change. New title and Preamble are minimum standards.
- Access to Treaty benefits would be more difficult as a result of the Introduction of a PPT/LOB or a mixture of the two.

Questions & Answers



Questions



Answers



Thank You!

