



The Institute of Chartered Accountants of India

Western India Regional Council

Direct Tax Refresher Course

- Reading Tax Treaties in the Era of MLI

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Introduction to International Taxation

- ❑ Every nation has a **right to tax** its residents / nationals on their **worldwide income**
- ❑ As a result, the income of a person may get taxed in both the countries i.e. in the **home** country (country of origin) as well as the **host** country (country where it operates) – economic or juridical
- ❑ In **home country** tax is an **obligation**, while in **host country** tax is a **cost**
- ❑ Double Tax Avoidance Agreements ('DTAA') comes into play to mitigate hardships caused by taxing the same income twice
- ❑ DTAA's are also known as Tax Treaty and Double Tax Conventions ('DTC')

International Taxation primarily involves the following provisions of the Income-tax Act, 1961

Section	Provision
Section 4	Charging Section
Section 2(31)	Definition of a Person
Section 5	Scope of Total Income
Section 6	Residence in India
Section 9	Income deemed to accrue or arise in India
Section 90	Agreement with foreign countries or specified territories
Section 90A	Adoption by Central Government of agreement between specified associations for Double Taxation Relief
Section 91	Countries with which no agreement exists
Section 115A to 115BBA & 115C to 115F	Provisions relating to Non - Residents
Section 195	WHT obligation for payment to Non Resident
Section 195A	Income payable 'Net of Tax'

Indian Constitution and Indian Private International Law

- The Parliament has not set out any general policy with regard to transformation of international law instead it allows executive to assume power to enter into treaties.

Article 73: “Subject to the provisions of this Constitution, the executive power of the Union shall extend—

(a) to the matters with respect to which Parliament has power to make laws; and

(b) to the exercise of such rights, authority and jurisdiction as are exercisable by the Government of India by virtue of any treaty or agreement.

- In the absence of legislation, the power to enter into treaties have been devolved to the Central Government. However the implementation of treaties would still require a domestic legislation (parliamentary oversight).

Do State adhere to strict theory of monism and dualism?

Tax treaties under Domestic Law

- Section 90 (1) of the Income-tax Act, 1961 (ITA) gives general transformation powers to the executive as regards Indian tax treaties.
- Section 90(1) implements tax treaties notified by the Government if they are entered in the context of at least one of the following:
 - a) granting relief in respect of (i) Income tax paid in India and corresponding state and (ii) income tax paid in India and corresponding state to promote mutual economic relations, trade and investment.
 - b) Avoidance of double taxation.
 - c) Exchange of information purposes.
 - d) Recovery of income tax and under corresponding law in force in the other country.
 - e) Prevent tax avoidance.

- Section 90(2) provides it to be applicable to the extent they are more beneficial to the taxpayer *vis-à-vis* provisions of a tax treaty.
- Circular 333 dated 2 April 1982 - Where a specific provision is made in a tax treaty, it will prevail over general provisions contained in the domestic tax law.
- Section 90(3): Any term used but not defined in this Act or in the DTAA, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the DTAA, have the same meaning as assigned to it in the notification issued by the Central Government .*

**inserted vide Finance Act 2003 w.e.f. from 1.4.2004*

Amendment to S. 90 vide Finance Act 2020 to align it with Art. 6 of MLI

Section 90(1)(b) amended to provide:

“the Central government may enter into any tax treaty with any other country for the avoidance of double taxation, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of any other country or territory)”.

India’s step to align domestic law with provisions of MLI (Article 6) reaffirms its goal to curb treaty abuse in cases of attempts to circumvent limitations provided by the treaty.

Section 90A:-Adoption by Central Government of agreement between specified associations for double taxation relief.

90A. (1) Any specified association in India may enter into an agreement with any specified association in the specified territory⁸⁵ outside India and the Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for adopting and implementing such agreement—

(a) for the granting of relief in respect of—

(i) income on which have been paid both income-tax under this Act and income-tax in any specified territory outside India; or

(ii) income-tax chargeable under this Act and under the corresponding law in force in that specified territory outside India to promote mutual economic relations, trade and investment, or

(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that specified territory outside India, or

(c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that specified territory outside India, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that specified territory outside India.

Section 91:-Countries with which no agreement exists.

91. (1) If any person who is resident in India in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India), he has paid in any country with which there is no agreement under section 90 for the relief or avoidance of double taxation, income-tax, by deduction or otherwise, under the law in force in that country, he shall be entitled to the deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

Why International Taxation

- Globalization
- Borderless Global Economy - Internet
- Movement of People – Concurrent Earnings
- Growing Opportunities – Cross Border M & A
- To Define Taxing Rights among the States
- To Avoid Double Taxation Conflicts
- Cross boarder exchange of information

Purpose of International Taxation

- Taxing Residents on their World Wide Income
- Taxing Non Residents on their National Income
- There are some exceptions to the above principles

Legislation of International Taxation

- ❑ No separate Codified law – No separate tax – No separate court
- ❑ Provisions of Domestic law to handle Cross Border - Direct & Indirect Taxes
- ❑ Accepted Convention - Can not enforce tax on territory of another country
- ❑ EU Directives / Model Commentaries

Jurisdiction of Taxation

- Source Jurisdiction of Taxation
- Residence Jurisdiction of Taxation

What is a Treaty ?

Vienna Convention on Law of Treaties 1969
defines treaty as –

“An international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument and whatever its particular designation.”



What is a Treaty ?

- ❑ A tax treaty is form of agreement between two or more national jurisdictions concerning taxes where the main purpose of which is to regulate matters concerning taxes.
- ❑ The term ‘treaty’ in the generic sense signifies that the parties intend to create rights and obligation enforceable under international law.
- ❑ May be labelled as Treaties, Agreements, Conventions, pact, charter, statute, act, declaration or otherwise;
- ❑ Includes further protocols, exchange of notes, agreed minutes, memorandum of agreement etc.
- ❑ Latest fashion is multilateral tax treaties

Double Taxation Avoidance Agreements (DTAAs)

- ❑ There are tens of thousand of treaties in existence, the minority of which deals with taxes on income and capital.

India has about

- ❑ 100 Bilateral DTAAs(comprehensive),
- ❑ Limited Agreements 8,
- ❑ SAARC Multilateral 1,
- ❑ Tax Exchange Information Treaties 20,
- ❑ FATCA 1,
- ❑ Multilateral treaty 1
- ❑ **Synthesized Text** of Indian Covered Tax Agreements modified by MLI

Why DTAAs? – Aids in removing certain tax barriers to cross-border trade and investment?

Refer definition of the term ‘Immovable Property’ in Article 6 of DTAA

Therefore, whenever you sit to understand DTAA –

- ❖ Keep your eyes wide open
- ❖ Don't have closed mind
- ❖ Anything is possible
- ❖ Results could be unexpected

Aides to Interpretation of DTAAs

- OECD / UN MODEL CONVENTIONS AND COMMENTARY
- PROTOCOLS
- TECHNICAL MEMORANDUM
- PARALLEL TREATIES
- INTERNATIONAL CASE LAWS

Approach to Interpretation

- ❑ STATIC APPROACH
- ❑ AMBULATORY APPROACH (DYNAMIC APPROACH)
- ❑ OECD/UN RECOMMENDS AMBULATORY APPROACH
- ❑ CANADIAN SC CASE IN R. V. MELFORD DEVELOPMENTS INC.
 - DEFINITION OF THE TERM ‘GUARANTEE FEE’

DTAAs - Types

COMPREHENSIVE AGREEMENTS

This is wider in scope addressing all sources of income.

LIMITED AGREEMENTS

This has limited scope and covers subjects ranging from -

- (1) Income from operation of aircrafts and ships,
- (2) Estates,
- (3) Inheritance
- (4) Gifts

BILATERAL AND MULTILATERAL TREATIES

DTAA Articles

Article 1	Scope
Article 2	Taxes covered
Article 3	General Definition
Article 4	Resident
Article 5	Permanent Establishment
Article 6	Immovable Property
Article 7	Business Profits
Article 8	International Traffic
Article 10	Dividends
Article 11	Interest
Article 12	Royalties & Fees for Technical Services
Article 13	Capital Gains
Article 14	Independent Personal Services
Article 15	Dependent Personal Services
Article 16	Directors

DTAA Articles

Article 17	Artistes & Sportsperson
Article 18	Pensions
Article 19	Government Services
Article 20	Students
Article 21	Other Income
Article 22	Capital;
Article 23	Elimination of Double Taxation
Article 24	Non Discrimination
Article 25	Mutual Agreement Procedure
Article 26	Exchange of Information
Article 27	Assistance in collection of taxes
Article 28	Members of Diplomatic Missions and Counsellor Activities
Article 29	Entry into force
Article 30	Termination
Article 31	Limitation of benefit

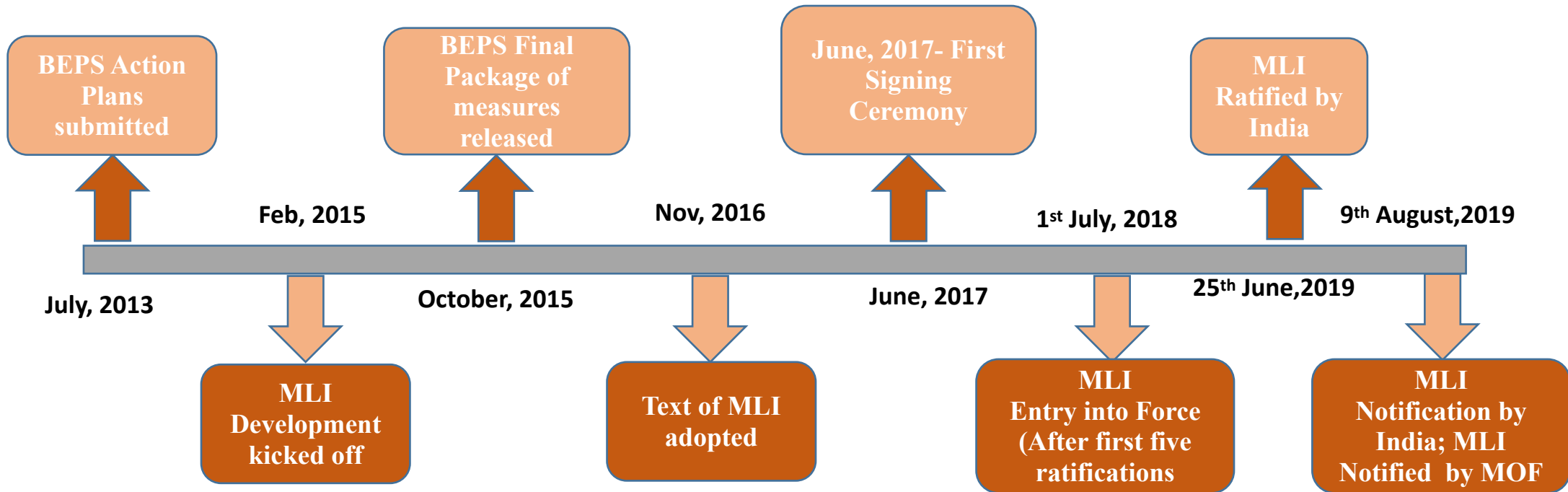
BEPS-History and Progress

- ❖ The OECD/G20 Base Erosion and Profit Shifting (BEPS) Project is about bringing coherence, transparency and substance to the international tax rules, in a vastly different time.
- ❖ OECD and G20 governments came together in 2013 to address the issue of tax avoidance, and agreed a series of actions to tackle it.
- ❖ On 19 July 2013 the OECD released an *Action Plan on Base Erosion and Profit Shifting (BEPS)*.
 - ❖ The purpose of the Action Plan which have been under pressure in recent years from the pace of globalisation and the heightened sophistication of international business transactions and global value chains, as well as the strains that digitalisation has brought to rules developed a century ago an is “to prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from activities that generate it.”
 - ❖ The report indicates that “no or low taxation is not per se a cause for concern, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it.”

BEPS-History and Progress

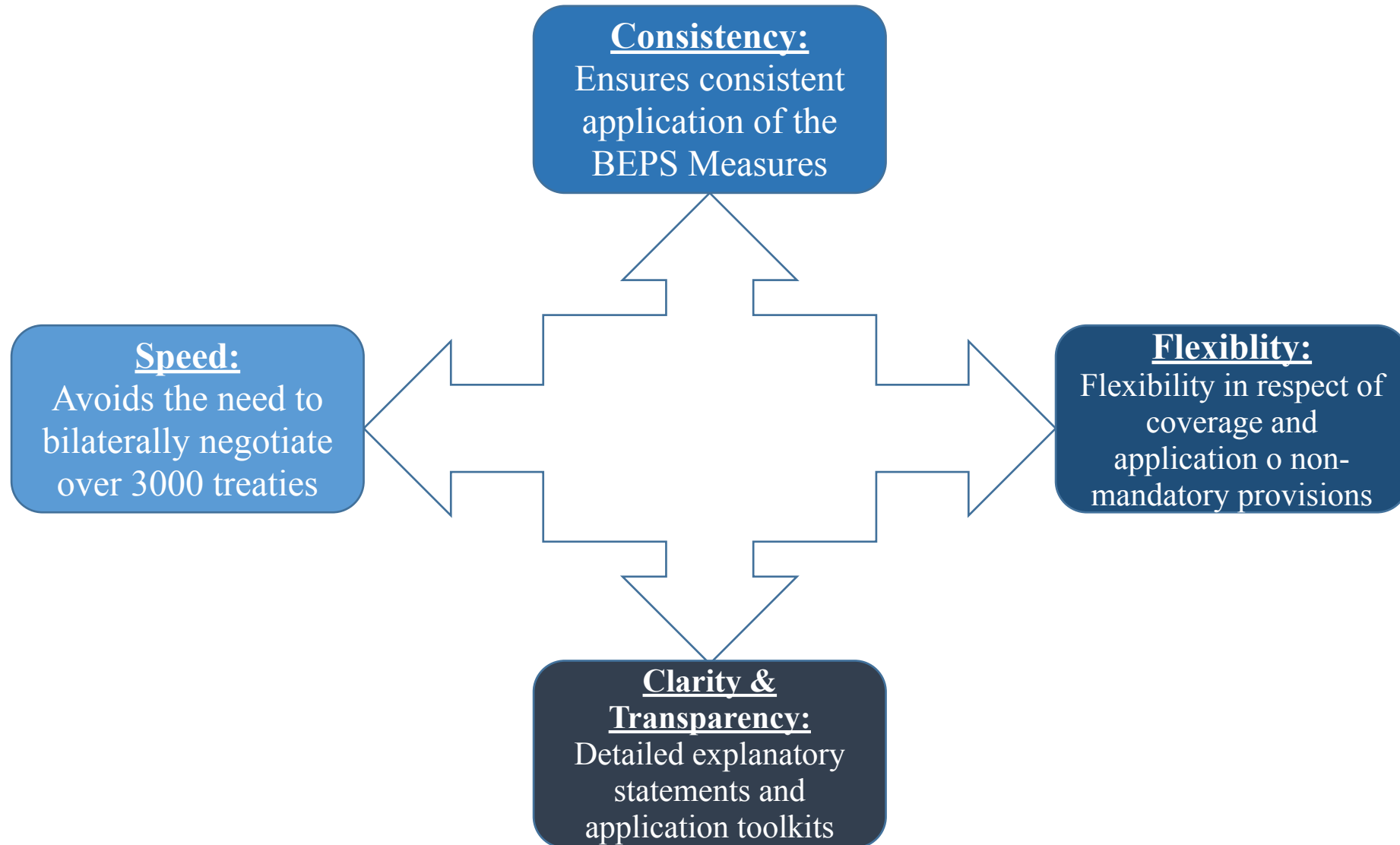
- ❖ The OECD/G20 Inclusive Framework continues to grow from 82 members at the inaugural meeting of the OECD/G20 Inclusive Framework in July 2016 in Kyoto, **it is now composed of 129 members and 14 observers, including over 70% of non-OECD and non-G20 countries and jurisdictions from all geographic regions**. They are working together on an equal footing, and not only to implement the BEPS measures agreed in 2015

Background and History



Out of 94 signatories to MLI, 47 countries have ratified MLI (including India)

MLI-Rationale



Aids to Interpret MLI

- ❖ BEPS AP 15 – containing the text of MLI;
- ❖ Explanatory Statement to MLI – which reflects the agreed understanding of the negotiators with respect to the MLI;
- ❖ MLI Positions adopted and deposited by various MLI Signatories with OECD - draft MLI positions filed at time of signing MLI and final MLI positions filed at the time of depositing ratified copy of MLI with OECD;
- ❖ **Reports on BEPS AP 2, 6, 7 and 14 - based on which MLI text is developed;**
- ❖ Text of the existing tax treaty along with the protocols (if any) to the existing tax treaty – to which MLI provisions are to be applied / replaced / modified, as the case may be;
- ❖ OECD Model Convention of Tax Treaty and OECD Commentaries - used for interpretation of tax treaty;
- ❖ The Synthesised text of MLI between parties to a CTA
- ❖ MLI matching database available on OECD's Website

MLI Framework

Minimum Standards

- All countries to meet certain minimum standards (Action 6 - Treaty Abuse; Action 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

- 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 supercedes*

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

Timelines for Applicability of MLI

1. Ratification and filing with OECD		2. Entry into Force ('EOF'):		3. Entry into Effect ('EIF'):			
		First day of the month following: Col. 1 + 3 months		i. Withholding taxes:		ii. Other taxes:	
				First day of the calendar year (taxable period for India) on or after the later of the EOF		From taxable periods beginning on or after 6 months from the later of the EOF	
India	Singapore	India	Singapore	India	Singapore	India	Singapore
25 June 2019	21 Dec 2018	1 Oct 2019	1 April 2019	1 Apr 2020	1 Jan 2020	1 Apr 2020	1 Jan 2021

India	Canada	India	Canada	India	Canada	India	Canada
25 June 2019	31 Dec 2019 (assumed)	1 Oct 2019	1 Apr 2020	1 Apr 2020	1 Jan 2021	1 Apr 2021	1 Jan 2021

India	Cyprus	India	Cyprus	India	Cyprus	India	Cyprus
25 June 2019	23 Jan 2020	1 Oct 2019	1 May 2020	1 April 2021	1 Jan 2021	1 April 2021	1 Jan 2021

Impact / Issues of different EIF dates?

Indian tax treaties impacted by MLI w.e.f. 1 April 2020

S. No.	Country	S. No.	Country	S. No.	Country
1	Australia*	11	Israel	21	Russia
2	Austria*	12	Japan*	22	Serbia*
3	Belgium*	13	Latvia*	23	Singapore*
4	Canada	14	Lithuania*	24	Slovak Republic*
5	Denmark	15	Luxembourg*	25	Slovenia
6	Finland*	16	Malta	26	Sweden
7	France	17	Netherlands	27	Ukraine
8	Georgia*	18	New Zealand	28	United Arab Emirates*
9	Iceland	19	Norway	29	United Kingdom*
10	Ireland*	20	Poland*		

No impact on India's treaties with few major partners like U.S., Mauritius, Germany

* Synthesized Text available for 17 Indian Tax Treaties – Singapore, UK, Luxemburg, Japan, UAE, Australia, Austria, Finland, Ireland, Poland, Lithuania, Slovak Republic, Serbia, Belgium, Georgia, Latvia, etc.

Major changes to Indian Tax Treaties through MLI

1. Modification to the Preamble – explicitly mentioned that purpose of treaty is also to prevent treaty abuse and double non-taxation and to prevent extension of benefit of the treaty to persons resident in a third jurisdiction (prevention of treaty shopping)

2. Expansion to the scope of Permanent Establishment
 - Independent Agent scope expanded (i.e. where agent provides services to closely related entities)
 - Dependent Agent PE rule
 - PE exclusion for certain activities to now be restricted only if such activities have a Preparatory or Auxiliary character
 - Anti-fragmentation rule to prevent avoidance of PE through artificial disintegration of cohesive activities
 - Anti-splitting of contracts rule to prevent artificial splitting of contracts between related parties to manipulate time period threshold for PE creation
 - Address the avoidance of PE through Commissionaire Arrangements & similar arrangements

Major changes to Indian Tax Treaties through MLI

3. Resolution of status of Dual Residence of company through MAP
3. Anti-Abuse
 - Principle Purpose Test (minimum standard)
 - Simplified Limitation of Benefits Test to prevent treaty abuse
 - Anti-Abuse Rule for PEs in Third Jurisdictions
5. Corresponding Adjustments in case of related party transactions
6. Lower rate of tax on dividends only if shareholding is maintained for past 365 days, not just on dividend payment date
7. Capital gains from transfer of security whose principal value was derived from immovable property in a country would be taxable not just if such value is derived at the time of transfer but at any time in past 365 days from date of transfer

Synthesized Text of Indian Tax Treaties

- ❑ The “Synthesized Text” represents the shared understanding between the two Governments of the modifications to their DTAA through the MLI and is prepared jointly by the relevant Competent Authorities.
- ❑ The CBDT periodically publishes the “Synthesized Text” of Indian Tax Treaties as and when they are prepared. The treaties whose text has been published till date include the following:

Treaty with	Articles Modified	Articles Added
Australia	Preamble, 1, 4, 5, 13, 25	PPT Clause
Austria	Preamble, 5, 23	Anti-Abuse Rule for PEs in Third Jurisdictions, PPT Clause
Belgium	Preamble, 5,9,13,25	Ant-Abuse Rule for PEs, corresponding adjustment, MAP, PPT Clause
Canada	Preamble,4,10,13,25	Dual resident, Dividend, MAP, PPT Clause
Finland	Preamble	PPT Clause
Georgia	Preamble	PPT Clause
Ireland	Preamble, 4, 5, 13	Anti-Abuse Rule for PEs in Third Jurisdictions, PPT Clause
Japan	Preamble, 4, 5, 9, 13	PPT Clause
Latvia	Preamble	PPT Clause
Lithuania	Preamble, 5, 9, 30	(PPT clause part of Article 30)
Luxembourg	Preamble	PPT Clause

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Treaty with	Articles Modified	Articles Added
Malta	Preamble	PPT Clause
Poland	Preamble, 1, 4, 14, 28A	(PPT clause part of Article 28A)
Serbia	Preamble, 4,5,10,14	Dual Resident, Ant-Abuse Rule for Pes, Dividend, PPT Clause
Singapore	Preamble	PPT Clause
Slovak Republic	Preamble, 1, 4, 5, 9, 10, 13, 23	SLOB, Anti-Abuse Rule for PEs in Third Jurisdictions, PPT
Slovenia	Preamble,4,5,10,13	Dual Resident, Ant-Abuse Rule for Pes, Dividend, PPT Clause
UAE	Preamble	PPT Clause
United Kingdom	Preamble, 1, 4, 5, 27, 28C	(PPT clause part of Article 28C)

[Since the India-Slovak treaty has most of the MLI related amendments, this Treaty is used to show the impact on Indian treaties]

Features of MLI

Features of MLI

- Allowing the countries the option to specify DTAA to which they want MLI to apply
- Matching concept – only if both countries notify their respective DTAA, changes will take place.
- Such DTAAs will be “Covered Tax Agreements” or CTAs. *Other DTAAs to be negotiated bilaterally.*
- Certain minimum standards to apply to if DTAA is CTA
- Possibility to opt out of provisions which do not reflect a BEPS minimum standard with the possibility to opt in later
- Possibility to apply optional provisions and alternative provisions at any time where there are multiple ways to address BEPS
- Notifications of CTAs, reservations, options and affected existing provisions (MLI Positions) to identify modifications. MLI positions provided by each jurisdiction available on the *OECD* website

Covered Tax Agreement (CTA)

The term “Covered Tax Agreement” means an agreement for the avoidance of double taxation with respect to taxes on income (whether or not other taxes are also covered):

i) that is in force between two or more:

A) Parties; and/or

B) jurisdictions or territories which are parties to an agreement described above and for whose international relations a Party is responsible; and

ii) with respect to which each such Party has made a notification to the Depositary listing the agreement as well as any amending or accompanying instruments thereto (identified by title, names of the parties, date of signature, and, if applicable at the time of the notification, date of entry into force) as an agreement which it wishes to be covered by this Convention.

Article 6 - Purpose of a Covered Tax Agreement

Article 6- Purpose of a Covered Tax Agreement

- ❖ Prevention of treaty abuse is a minimum standard covered under Action 6 of the Final BEPS package. Pursuant to such minimum standard under Action 6, requiring express intent in tax treaties to exclude opportunities for treaty abuse, Article 6(1) of the MLI provides for introduction of the following preamble text in a CTA –

*“Intending to eliminate double taxation with respect to the taxes covered by this agreement **without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions)**,”*

- ❖ This preamble text (“MLI Preamble”) is included in place of or in absence of existing preamble language of a CTA which expresses an intent to eliminate double taxation. However, a Party is permitted to make a reservation with respect to those CTAs which already satisfy the minimum standard and contain the requisite preamble language. In case of such reservation by one of the Treaty Partners to a CTA, the preamble of that CTA will remain unchanged.

Article 6- Purpose of a Covered Tax Agreement

Impact & Analysis

- ❖ India has been silent on its position on Article 6. Therefore, in the absence of India notifying any treaty provisions/preamble language, the MLI Preamble will not replace the existing preamble language in India's CTAs but will only be added to the existing preamble text, irrespective of whether or not the other Treaty Partners notify India's treaty for this purpose

India-Mauritius

Please note that Mauritius is not yet a signatory or a party to the MLI. However Mauritius has signalled its intent to sign up to the MLI and this analysis is based on the assumption that Mauritius shall also notify the India-Mauritius DTAA as a CTA.

- ❖ The existing preamble in the Mauritius treaty provides its object as “*the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains and for the encouragement of mutual trade and investment*”.
- ❖ In the landmark judgment of **Union of India v. Azadi Bachao Andolan**, the Supreme Court referred to the text of the preamble of the Mauritius Treaty providing for “encouragement of mutual trade and investment” and legitimized treaty shopping as being consistent with India's intention at the time when the Mauritius Treaty was entered into.

Article 6- Purpose of a Covered Tax Agreement

Impact & Analysis

- ❖ In the context of treaty shopping in a developing economy, the Supreme Court ruled as follows:
“125. There are many principles in fiscal economy which, though at first blush might appear to be evil, are tolerated in a developing economy, in the interest of long term development. Deficit financing, for example, is one; treaty shopping, in our view, is another. Despite the sound and fury of the respondents over the so called ‘abuse’ of ‘treaty shopping’, perhaps, it may have been intended at the time when Indo-Mauritius DTAC was entered into. Whether it should continue, and, if so, for how long, is a matter which is best left to the discretion of the executive as it is dependent upon several economic and political considerations. This Court cannot judge the legality of treaty shopping merely because one section of thought considers it improper. A holistic view has to be taken to adjudge what is perhaps regarded in contemporary thinking as a necessary evil in a developing economy.”
- ❖ The addition of MLI Preamble to the Mauritius Treaty (if and when signed) is likely to significantly change the position established in **Azadi Bachao Andolan** as the MLI Preamble specifically provides for intent to prevent opportunities for tax avoidance evasion through treaty shopping. **However, where an entity is set up in Mauritius primarily for the purposes of investment into India, the same could be argued to be within the overall object and purpose of the Mauritius Treaty by virtue of the existing preamble language of the treaty, thereby qualifying for treaty benefits.**
- ❖ ***Interestingly US is not a signatory to the MLI***

Article 4 of the MLI- Residency of Dual Resident Entity

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- ❖ No change as far as individuals are concerned
- ❖ Dual Resident Entity (“DRE”) is a person resident in more than one Contracting Jurisdiction.
- ❖ Article 4 of MLI seeks to provide clarity on manner of determination of residential status of non-individual DRE.
- ❖ Presently under DTAA, Place of Effective Management (“POEM”) is the only tie-breaker rule to determine the residential status.
- ❖ It is now proposed that the residential status of a DRE shall be determined by a Mutual Agreement Procedure (“MAP”) between Treaty Partners taking into account place of incorporation or constitution and any other relevant factors in addition to POEM.
- ❖ **This will help to resolve dual residency issues through mutual agreement as POEM rules may differ from country to country resulting in hardship to the tax payer.**

Article 7- Prevention of Treaty Abuse

Article 7- Prevention of Treaty Abuse

- ❖ Article 7 provides safeguard against ‘**Treaty Abuse**’ and in particular ‘**Treaty Shopping**’
- ❖ Three-pronged approach recommended to address treaty shopping arrangements:
 - **Clear statement of intent** in tax treaties to avoid creation of opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements
 - Introduction of specific anti-abuse rule, for instance, the **Limitation-of-Benefits** rule, that limits availability of treaty benefits to entities meeting certain conditions (based on legal nature, ownership in, and general activities of entity to ensure sufficient link between entity and State of residence)
 - Introduction of a more general anti-abuse rule based on the **principal purposes test**

This is a **Minimum Standard** – to include in the tax treaties an express statement that common intention is to eliminate double taxation without creating opportunities for non-taxation, tax evasion or avoidance

In order to implement the minimum standard the treaties should include

- LOB
- PPT
- Simplified LOB supplemented by PPT

Article 7- Simplified LOB (Para 8-13)

- ❖ It is a SAAR aimed at treaty shopping
- ❖ Treaty benefits to be denied to a resident of a Contracting State who is not a ‘Qualified Person’
- ❖ ‘Qualified Person’ to include -
 - An individual;
 - The State, its political subdivision, entities owned by the State;
 - Certain charities and pension funds;
 - Certain public entities and their affiliates;
 - Certain entities that meet certain ownership requirements and/or turnover requirements;
 - Certain collective investment vehicles;
 - Entities permitted by competent authorities.
- ❖ If a person is not a ‘Qualified Person’, the benefit of treaty would be available on satisfaction of certain conditions

Article 7- Principle Purpose Test ('PPT') (Para 1)

*“Notwithstanding any provisions of a Covered Tax Agreement, a benefit under the Covered Tax Agreement shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that **obtaining that benefit was one of the principal purposes*** of any arrangement or transaction that resulted directly or indirectly in that benefit,*

unless

*it is established that granting that benefit in these circumstances would be **in accordance with the object and purpose of the relevant provisions of the Covered Tax Agreement**”*

** this is more stringent than GAAR*

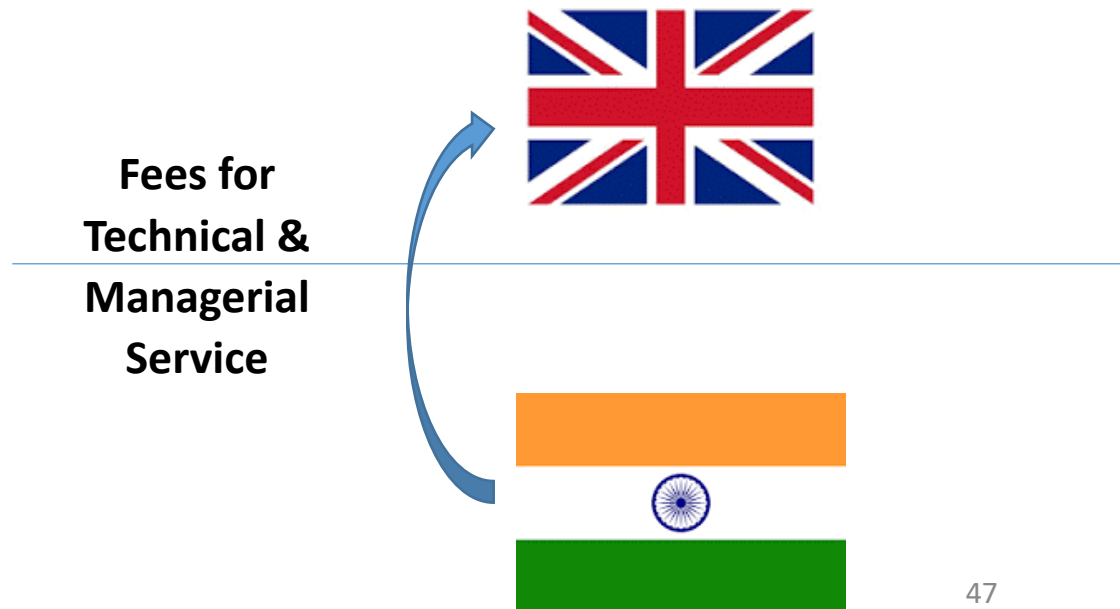
PPT – BURDEN OF PROOF

- ❖ Obtaining tax benefit is one of the principal purposes – Onus on the tax department
- ❖ Arrangement is in accordance with the object and purpose of the treaty – Defence available with the tax payer

Example- Principle Purpose Test

- ❖ XY a Company registered in UK is looking for expanding its business in Asia. It has identified three different countries with similar economic and political environments. The entity set up by XY will perform its operating in the basis of technical and managerial support provided by XY.
- ❖ It selects India for setting up its business on account of favourable treaty (Make available clause) with India.
- ❖ Will PPT apply?

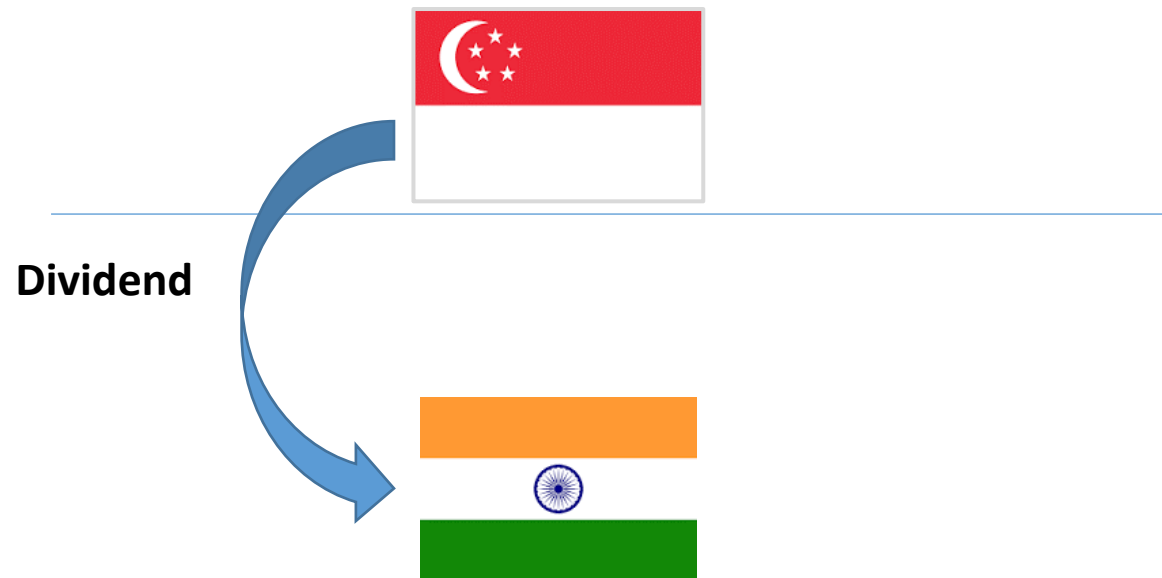
Expansion of business in the principal purpose, but favourable treaty provisions were taken into consideration.



Example- Principle Purpose Test

- ❖ I Co is a collective investment vehicle registered in India managing diversified portfolios of investment globally. It has significant investments in Singapore on account favourable treaty (underlying tax credit) on dividend taxation.
- ❖ Whether PPT applies?

One of the intents of treaties is to provide benefit to encourage cross border investments.



Article 12- Artificial Avoidance of Permanent Establishment Status

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1. Notwithstanding the provisions of a Covered Tax Agreement that define the term “permanent establishment”, but subject to paragraph 2, where a person is acting in a Contracting Jurisdiction to a Covered Tax Agreement on behalf of an enterprise and, in doing so, 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,

Article 13- Artificial Avoidance of Permanent Establishment Status through the Specific Activity Exemptions

Article 13 of MLI – Activity based PE exclusions

Article 13(2) – Activity based PE exclusion under DTAA will now be available only if the overall character of such activity is preparatory and/or auxiliary

Article 13(4) of MLI - NEW ANTI-FRAGMENTATION RULES ('AFR')

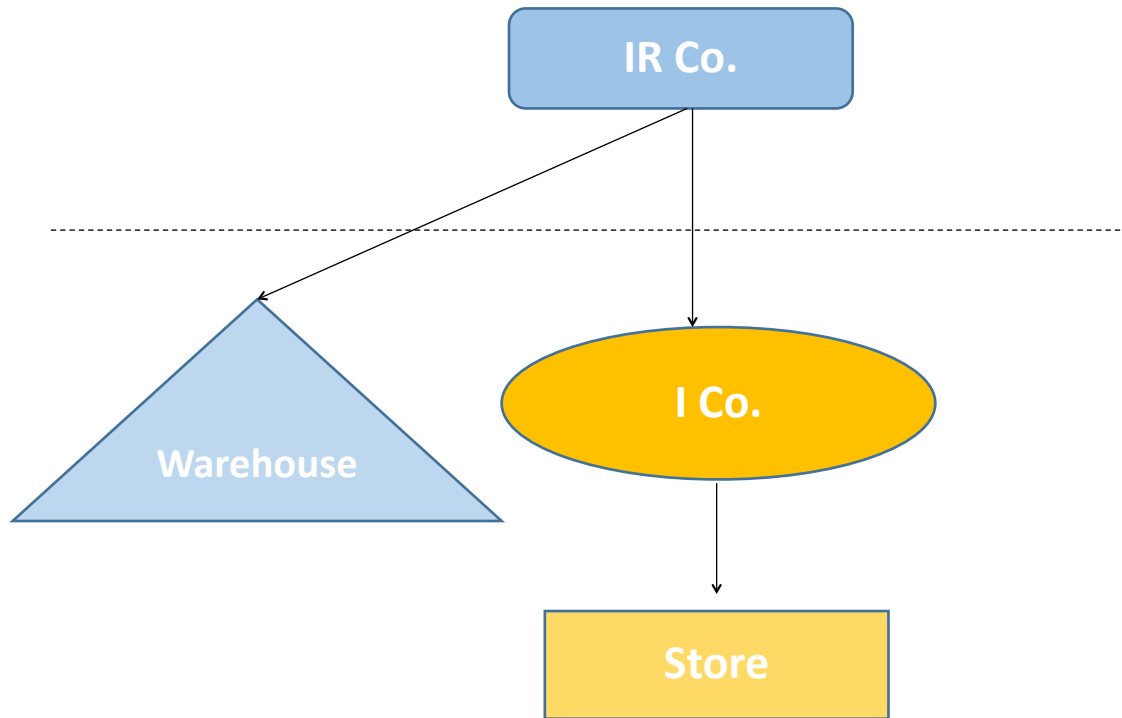
“4.1 Paragraph 4 shall not apply to a fixed place of business that is used or maintained by an enterprise if the same enterprise or a closely related enterprise carries on business activities at the same place or at another place in the same Contracting State and:

a) that place or other place constitutes a permanent establishment for the enterprise or the closely related enterprise under the provisions of this Article, or

b) the overall activity resulting from the combination of the activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, is not of a preparatory or auxiliary character,

provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation.”

Example- Anti Fragmentation



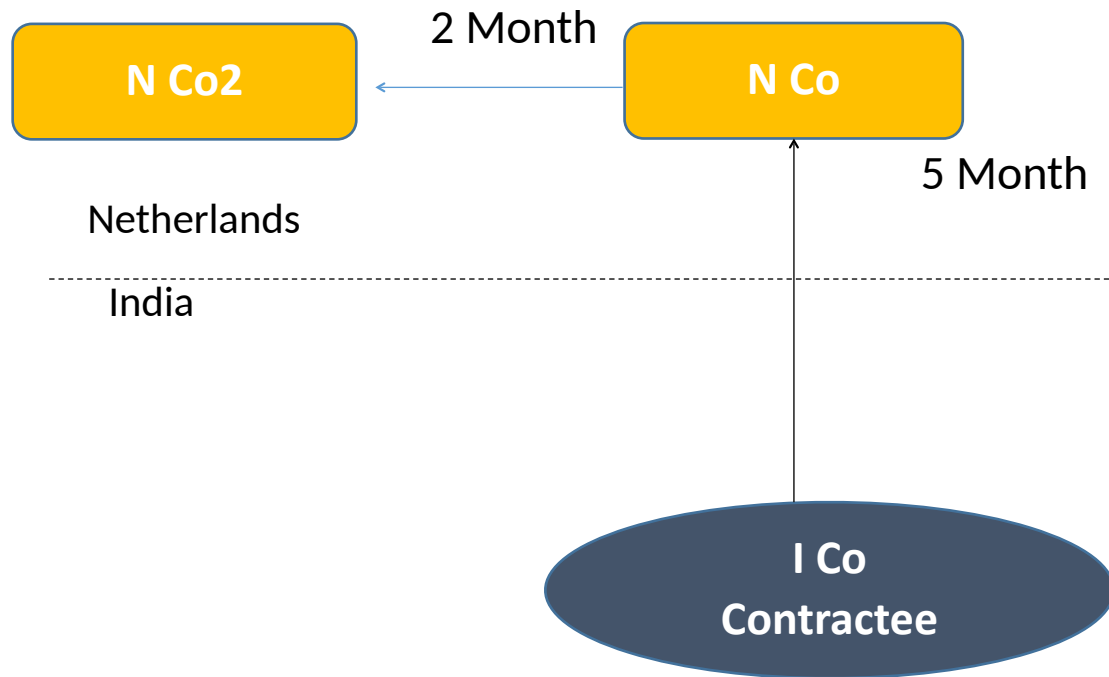
Structure Mechanics:

- ❑ IR Co, a company resident of Ireland, manufactures and sells appliances. I Co, a resident of India that is a wholly owned subsidiary of IR Co, owns a store where it sells appliances that it acquires from IR Co
- ❑ IR Co also owns a warehouse in India where it stores goods displayed in the store owned by I Co
- ❑ Whenever any product is completely sold out from the store, the warehouse supplies such product to the store. It also delivers directly to the customer when a large quantity of any product is ordered

Whether the warehouse would constitute a PE in terms of the new Anti-Fragmentation Rule?

Article 14 – Splitting-up of Contracts

Example- Splitting of Contract



Structure Mechanics:

- ❑ I Co. a company resident in India wishes to establish a mall in India. The project will take 7 months to complete
- ❑ I Co. engages a Netherland Company, N Co. as the main contractor for undertaking the said construction.
- ❑ N Co engages its associated entity N Co 2 to undertake a part of the project which would take 2 months

Whether N Co and N Co2 will be construed as PE in India post- MLI?

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THANK YOU

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