



Concepts and Recent Developments in International Taxation

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Journey of International Taxation

**Interplay between
POEM and PE**

**Beneficial Owner –
Domestic Law vis-a-vis
Tax Treaty**

**Overview of Tax Treaties in
relation to Mauritius and
Singapore**

Question and Answers

POEM – Concept and Guiding Principles



The SAAR of POEM

- **Promulgation:** The Finance Bill 2015 introduced POEM w.e.f. AY 2016-17 - At the enactment Stage, the words 'at any time' were dropped to eliminate any unintended consequences (e.g. single Board meeting of FCo in India = POEM)
- **Draft Guidelines:** The CBDT issued draft POEM Guidelines on 23 Dec 2015
- **Operationalization:** The Finance Act 2016 defers POEM to AY 2017-18 & introduces New Chapter XII-BC (Section 115JH) - modified scheme of taxation of FCo having POEM in India
- **Final Guidelines:** The CBDT issued final POEM Guidelines vide Circular No. 6 dt. 24 Jan 17 + PR of even date with threshold of Rs. 50 Crores for applicability of POEM

- **POEM Threshold:** The CBDT issues Circular No. 8 dt. 23 Feb 2017- POEM not applicable to FCo having turnover or gross receipts of Rs. 50 crores or less in a financial year.
- **POEM clarification:** The CBDT issues Circular No. 25 dt. 23 Oct 2017 – POEM clarification for multinational companies having regional structure
- **POEM Notification:** No. 3039(E) dt. 22 Jun 2018 - Taxation scheme under Section 115JH (*certification that no person is adversely impacted by retrospective effect to this notification*)
- **International developments** - POEM's Tie Breaker cases are treaty abuse and to be resolved through MAP - OECD AP 6 & MLI & Amendments to MC – OECD, UN & US

*For DTAA benefits, POEM needs to be demonstrated in the State of Incorporation & Residence and merely demonstrating POEM outside India not sufficient. **Obligation is distinct and over and above other obligations e.g. LOB, beneficial ownership of income, GAAR and Principle Purpose Test.***

Concept of POEM



POEM means a place where **key management** and **commercial** decisions necessary for conduct of business of an entity, **in substance** are **made**

- Intention to treat shell companies managed from India as resident company
- Intent not to target Indian Multi Nationals which are engaged in business activity outside India or having PE in India
- Focus on substance over form concept
- POEM to be determined annually
- POEM provisions are made effective from AY 2017-18 (i.e. FY 2016-17)
- **POEM shall not apply to companies having a turnover or gross receipt of Rs 50 crores or less in a financial year.**
- **Checks & Balances inbuilt – Tax Officer to take approval of CIT for initiating POEM enquiry AND obtain approval of the Collegium of 3 CITs before concluding on POEM – Opportunity of hearing is s MUST**

Section 115JH of the Income-tax Act

(A) Framework

- FCo treated as NR and taxed at NR rate on income chargeable basis POEM with no impact on income otherwise taxable in India. DDT not applicable.
- Fco subjected to TDS as if it is a NR – S. 195 applicable
- Foreign Tax Credits eligible on same proportion as income offered / assessed to tax
- Exchange Rate – Rule 115
- Transactions with R not altered – TP applicable
- Provisions applicable to Foreign Company and Residents to apply to FCo having POEM in India
- Most complicated provisions
 - Preparation of P&L and B/Sh where accounting year is different from financial year
 - C/f of unabsorbed depreciation and Losses – proportionate computation

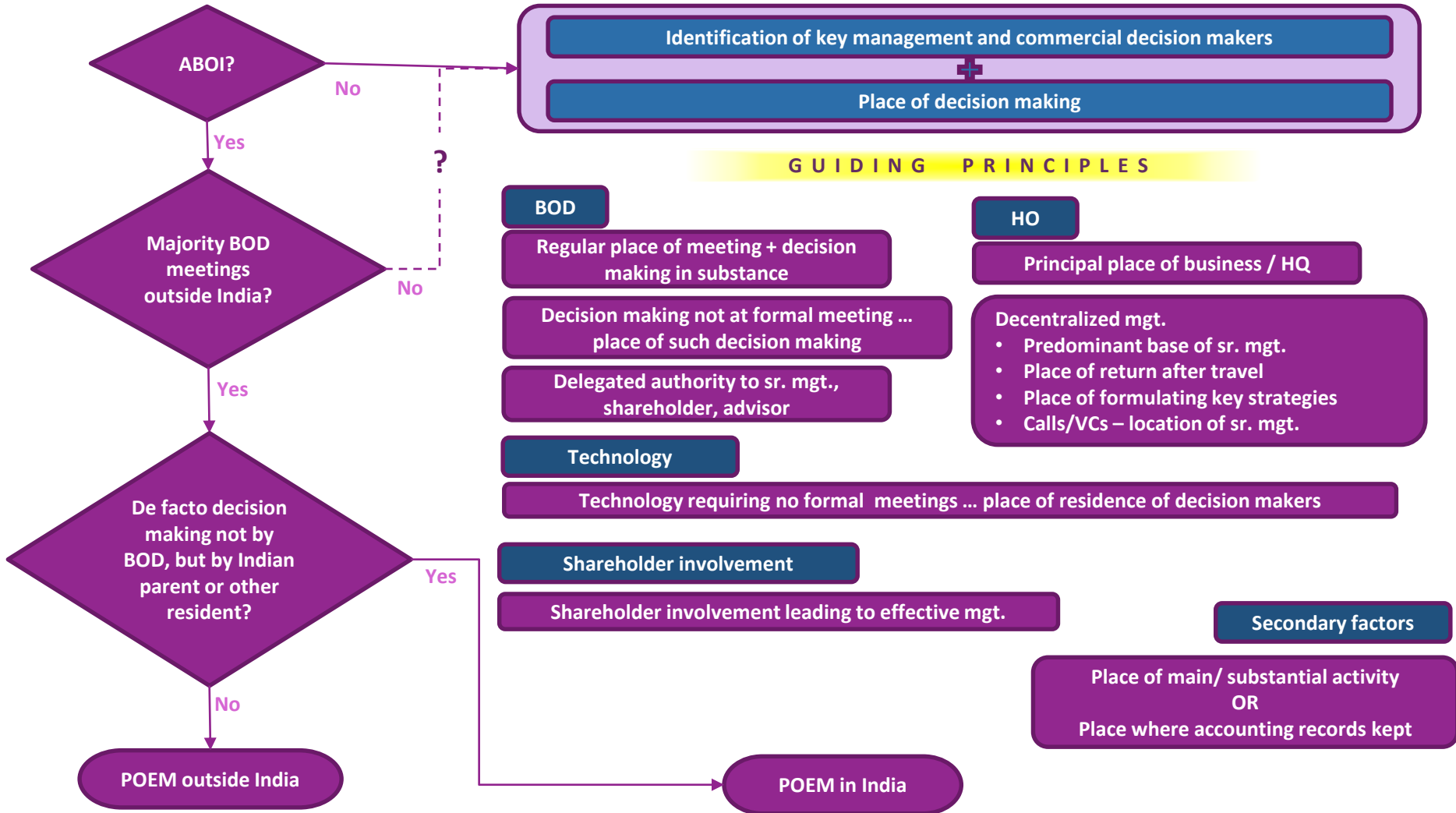
(B) Computation of Depreciation:

- Tax WDV on 1 day of previous year
 - If assessed in Foreign Country - as per Tax records post depreciation allowed / allowable
 - If not assessed to Tax – as per Books

(C) Unabsorbed Depreciation / Losses

- As on 1 day of previous year
 - If assessed to Tax - as per Tax Records of Foreign Country
 - If not assessed to Tax – as per Books
- C/f as per the Act for the remaining years taking the year of incurrence as first year
- They can be set-off only against income taxable of FCo due to becoming Resident
- To be revised in India if revised overseas including due to reassessment

Snapshot



Guidelines

determining POEM

Companies engaged in Active Business Outside India (ABOI)

- Average data of previous 3 years to be considered
- Conditions to be satisfied cumulatively

If conditions satisfied

- POEM outside India if majority BOD Meetings outside India
- However, if de facto decision making authority is not BOD but Indian parent or resident, POEM shall be in India

ABOI Test

- Passive income* > 50% of total income;
- More than or equal to 50% of total assets are situated outside India;
- More than 50% of total number of employees are not situated in India or are not resident of India;
- Payroll expense on such employee more than or equal to 50% of total payroll expenditure

If conditions not satisfied

- Identify person or persons who make key management and commercial decision; and
- Determine the place where decisions are being made- if the same are made in India then POEM shall be in India

Place where decisions are taken would be more important than place where such decisions are implemented

*Passive income would mean income from transactions where both purchase and sale of goods is from / to AEs and would include Royalty, dividend, capital gains, interest or rental income

POEM- Under Treaty

- Concept enshrined in all MC Treaties as well as Indian Tax Treaties
- Incorporated as a “Tie- Breaker Rule” to identify tax residency of the company when the situation of dual tax residency arises – Article 4(3)
- Article 4(1) confers residence based on a variety of criteria, one of which is the ‘place of management’.
- The term ‘POEM’ has not been specifically defined in any of the MCs – There is purpose behind this
- Article 3(2) of the MC – Any term not defined in the Treaty should be understood as per the domestic tax laws
- Different concepts applied by OECD – management & control, place of management, central management & control
- Effective day to day management & control Vs Strategic management and control
- The concept of POEM in the Treaty underwent changes with the changing times – significant changes 1977 till 2017

Internationally accepted standards on POEM

OECD definition of "POEM"	Place where
2005	<ul style="list-style-type: none"> ▪ Key management and commercial decisions necessary for business conduct are made in substance ▪ Most senior person(s) (e.g., BOD) make decisions ▪ Actions to be taken by the entity as a whole are determined
2008	<ul style="list-style-type: none"> ▪ Key management and commercial decisions necessary for business conduct are made in substance
2017	<ul style="list-style-type: none"> ▪ Determining the POEM by the Competent Authorities depending on case to case basis by using different criteria e.g. place of management

Rationale for change in definition

- Eliminate undue priority given to the meeting place of BOD
- Attach real importance to the place where, in substance, key managerial decisions, necessary for an entity to conduct business, are made
- 'The place where the BOD makes its decisions' can only be one of the relevant factors and shall not be treated as a sole determinative factor for determining the POEM

"Place of Management" ('POM')

- Necessary not only to mitigate POEM in India but also to mitigate 'POM' in India – otherwise profit attributable to such 'POM' could be taxable in India as per Article 5(2) of the Tax Treaty

An entity may have more than one place of management, but it can have only one POEM at any one time

OECD Conclusion: All relevant facts and circumstances must be examined

POEM – Model Commentaries and

▪ **OECD MC 2017 – New Article 4(3) pursuant to OECD BEPS AP 6 (2015)**

- Dual Resident Entities (DREs) cases to be examined case by case as could involve tax avoidance.
- Tie Breaker Rule for POEM done away
- DREs – case to be decided by Competing Authorities (CAs) of Contracting State
- Relief / exemption as per agreement between CAs and none in absence thereof
- Factors that are to be considered by CAs – continue to be POEM based (para 24.1)
- Contracting States can agree to retain erstwhile model article – tie breaker rule based on POEM

Note: India's Reservation to OECD MC 2014 were on similar lines – DRE to be resolved through MAP and POEM reference similar to enacted in Section 6(3) by FA 2015

- **UN MC 2017** – Article 4(3) reproduces the OECD MC 2017

▪ **US MC 2016 – Article 4(4)/ (5)**

- Dual Resident Company shall not be resident of either of the contracting state for purpose of relief under the convention
- Dual Resident Person other than an individual or a company, the CAs of the Contracting State to determine the mode of applicability of the Convention

• **Article 4 of MLI**

- Incorporate revised Article 4(3) of OECD MC 2017 to earlier tax treaties which would be CTAs
- Art 4(2) of MLI – “in place of or in absence of” (widest opt-in rule)

OECD reaction to COVID -

Impact on P.O.E.M.

- OECD reviews concerns regarding a change in a company's tax residency, or the creation of a dual residency, due to emergence of a new "place of effective management" as a result of key executives' inability to relocate or travel due to COVID-19.
- OECD notes that as the circumstances are transitory, the executives should not be considered to meet the standard of "usually" carrying on their activities from the location in which they are stranded.

The application of tie-breaker provisions should resolve conflicts arising from executive activity in a nonresident country, and where such provisions are not determinative, the parties could rely on competent authority procedure. The Competent authorities to deal with the same on case to case basis with Mutual agreement.

Tie breaker rule
post 2017 OECD
Model

- Factors to make their determination:
 - where the meetings of the company's board of directors or equivalent body are usually held
 - where the chief executive officer and other senior executives usually carry on their activities;
 - where the senior day-to-day management of the company is carried on
 - where the person's headquarters are located

Selected Judicial Precedents – India & International

- **AB Mauritius II (2018) (AAR) (not directly on POEM) - Favorable**

- **Relevant** - TRC, Investments in India long term through Banking channels, MD of Holding Company is Director in Mauritius Company and made 11 trips to India / Mauritius, Shares held in Mauritius company name – Legal & Beneficial Owner (No Benami), Mauritius Authorities Certificate on Place of Business in Mauritius, Directors were qualified and Independent, Board meetings took place in Mauritius, etc.
- **Not Relevant** - Persuasive influence of US ultimate Parent, movement of Directors in and out of Mauritius, Participating physically every time is not relevant and participation through electronic / video are valid means. Investment companies do not require huge offices and staff. Outsourcing of secretarial function.

- **AB Holding II (2018) (AAR) – Against - Negative factors:** Board merely reiterated Holding Company decisions, SPA not signed by Directors but Representative of Ultimate US Parent, SPA did impose no obligation on Mauritius Company, consideration paid by Ultimate US Parent, etc.
- **SMR Investment (2010) (Del AT)** - Order for sale and purchase of shares for the Mauritius Company given by Indian Resident Shareholder from Phone then effective place of management is in India
- **Bay Lines (2018) (Mum AT)** - UAE Directors attended BoD only on calls, Mauritius directors were only to satisfy Mauritius Law, BoD transacted no other business except Mauritius Law compliances, even items like letter to AO signed by UAE parent representative – POEM was not in Mauritius

- **Bywater (Australian Full Court)** – Person appointed in AOA and not BoD which controlled the Company and BoD powers were usurped – POEM was where the Person was located and not where BoD meetings held
- **Development Securities (UK Tribunal)** – Jersey Company’s BoD agreed to implement tax planning scheme of UK Parent and all decisions made / supervised by UK Parent even if unlawful / unauthorized and local Directors resigned after the Scheme – POEM in UK and not Jersey (*see also UK HC in Smallwood case which shot down tax planning through Trustees in similar manner*)

Key challenges in applying POEM

Under the Act

- Subjectivity in interpretation of terms - “key management and commercial decisions”, “conduct of business of an entity as a whole”
- Should decisions be “managerial” as well as “commercial” in nature?
- Operating incomes from interest, royalty, rent etc. still treated as passive income?
- No clarity on credit for FTC
- Multiple levels of taxation in case of multi-layered structure – Different countries have different POEM Rules
- No relief for overseas listed companies

Under the Treaty

- Interpretation of the term “POEM” - controversy between Article 3(2) and international concepts & principles
- Different countries have different definition of POEM – different criteria applied from POEM – which country’s domestic definition to be used?
- If POEM in India then other countries like UK, Canada, South Africa treats their domestic companies as “non-residents” for tax purposes – leading to adverse consequences
- BEPS AP 6 – recommended determination of POEM by Competent Authorities

Consequences of

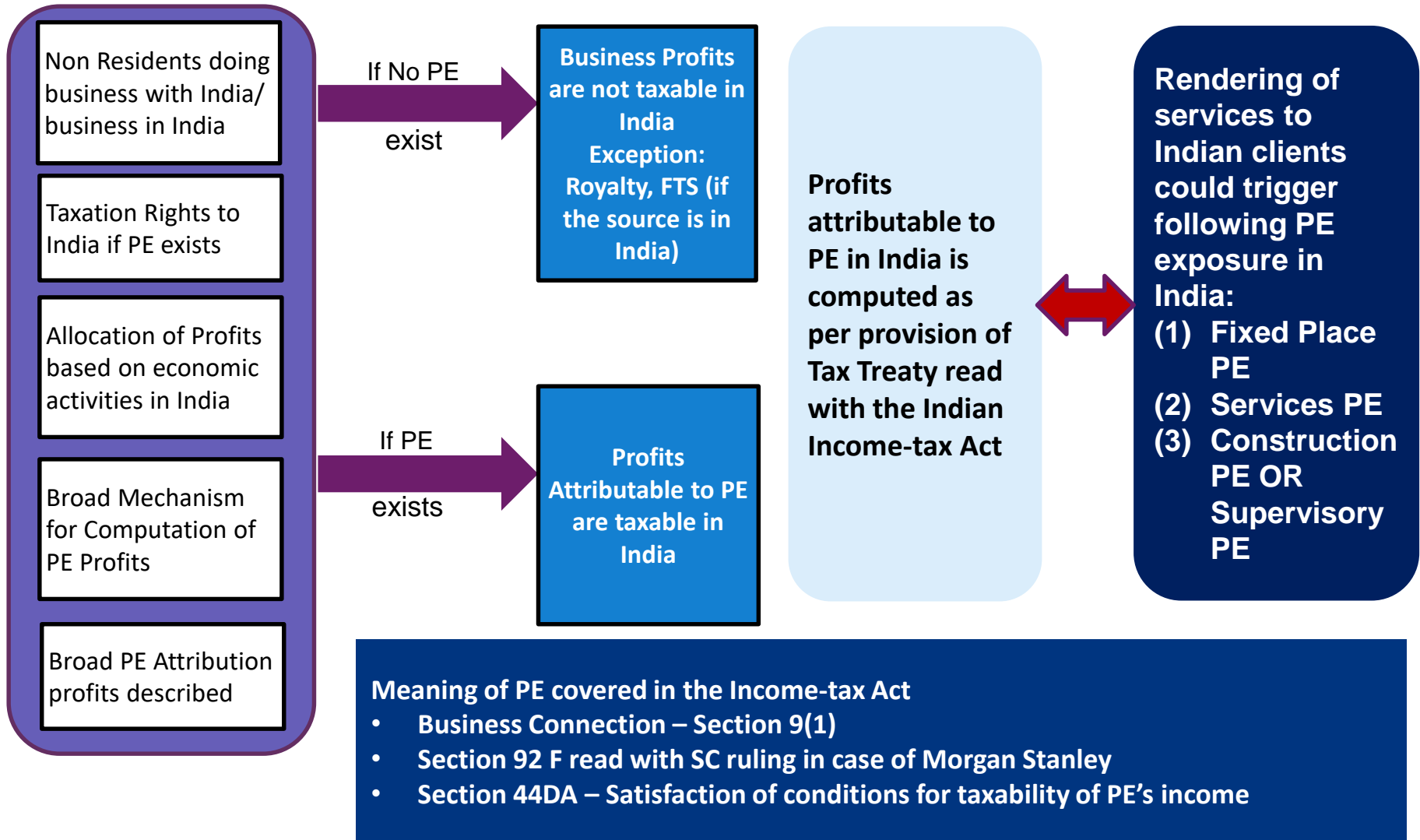
POEM

- Worldwide Income taxable in India @ 40% plus surcharge and cess
- Applicability of TP provisions including reporting of international transaction and maintenance of TP documentation
- Applicability of withholding provisions – unless payment falls within source rule exclusions under domestic law
- Foreign companies will lose the option of adopting presumptive taxation provisions.
- Compliance in form of filing of ROI, TDS return, Equalisation levy, etc.
- Interest and penalty in cases where POEM is determined in India during tax scrutiny
- Payer can also be treated as “Assessee in Default” in case where relief is considered under treaty and subsequently, POEM of payee turns out in India
- Indian Tax Authorities approach – Enquiry moving from PE to POEM

PE – Concept and Guiding Principles



Concept and Relevance of Permanent Establishment (PE)



Article 5 - PE – An Overview – UN Model Commentary

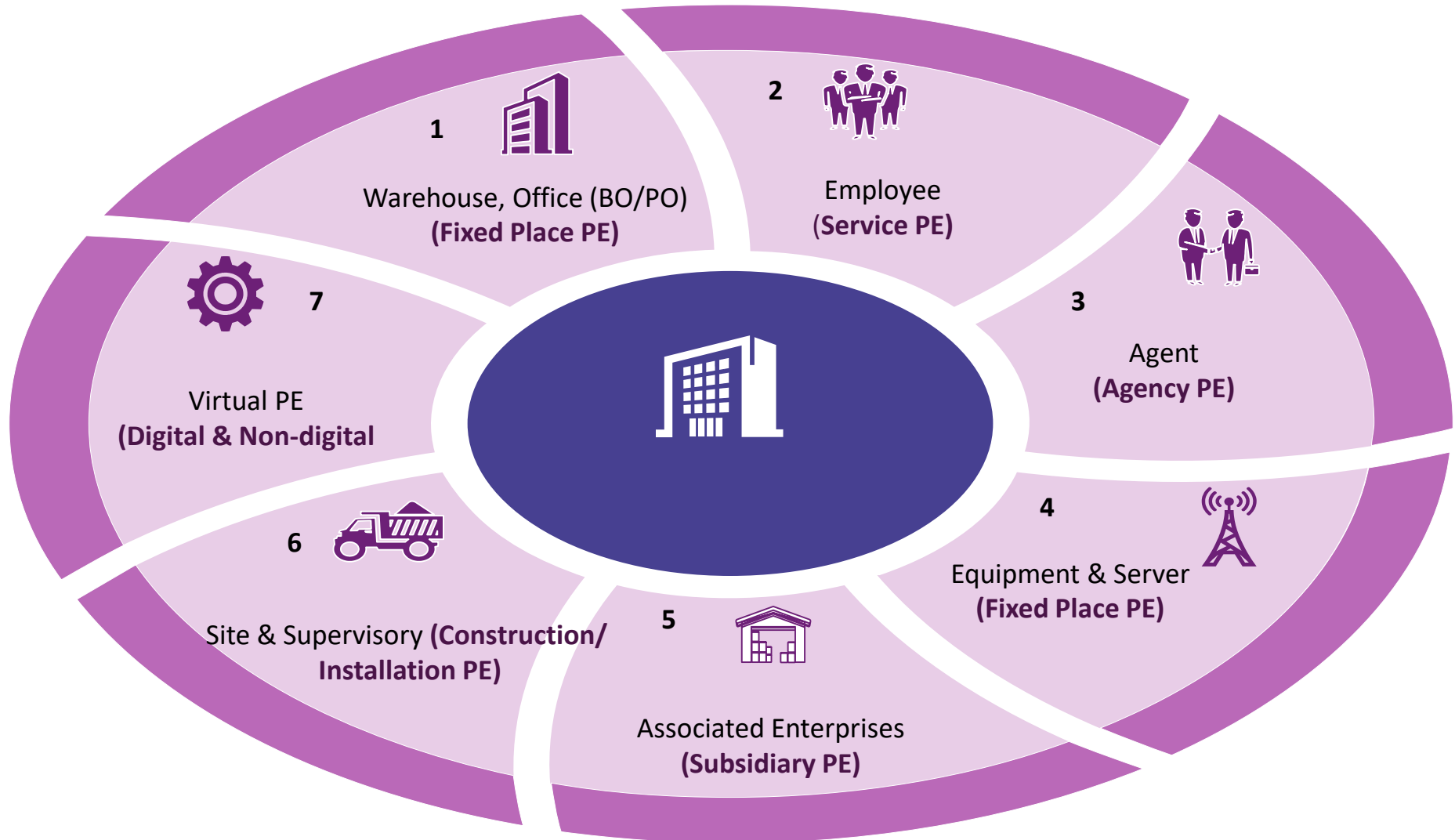
- **Significance of PE** – To determine rights of competing states to tax the business profits of the foreign enterprise

ARTICLE NO.	PARTICULARS	TYPE OF PE
Article 5(1)	Basic rule	Fixed base PE
Article 5(2)	Illustrative list of Pes	Inclusions to Fixed Base 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
Article 5(7)	Independent agent	Agency PE
Article 5(8)	Associated enterprise	Subsidiary PE

Article 5(6) in UN Model contains a special rule for agents of an Insurance Company.

This is absent in OECD and US models

Potential PE Triggers



Place of Management from PE

perspective

- Article 5(2) specifically includes certain establishments within PE and one of them is Place of Management. Place of management exists where ‘control & management’ of an enterprise reside
- “Place of management” is narrower than the term “POEM”
- The place of management, though considered a PE, requires existence of an office or similar facility in order to constitute a PE and the management activities should be conducted through such fixed place. In other words, to constitute a PE, the existence of physical presence is must.

Question	Example
Whether and in which circumstances a company that is a member of a corporate group may constitute a “place of management” of another company of the group so as to constitute a permanent establishment?	<ul style="list-style-type: none">• ACO, a company resident of State S, owns all the shares of BCO, a company resident of State R. Both companies are part of the ACO multinational group.• A part of the administrative functions of the multinational group have been centralized in the headquarters of ACO located in State S. The accounting, legal services, and most of the human resources functions of BCO are provided through ACO employees working at these headquarters.• The tax authorities of State S argue that since the headquarters of ACO constitute a place of management for BCO, BCO has a permanent establishment in State S

Place of Management vs Place of effective management

- Place of management is another residence test adopted by a number of treaty countries to determine residence of non-individuals.
- In Swiss practice, a distinction is drawn between the place of effective management and merely administrative management or decision making by executive bodies (e.g. Where the decisions of a board of directors are limited to control of the company and to basic decisions).
- In describing the meaning of “place of effective management”, Professor Vogel suggests that it is similar to that of “place of management” used under the German domestic law.
- According to the German case law, a place of management is regarded as the place where the management’s important policies are actually made.
- Prof. Kalus Vogel states that “what is decisive is not the place where the management directives take effect, but rather the place where they are given.” It is the centre of top level management, i.e. the place at which the person authorised to represent the company carries on his business managing activities. However, Vogel indicates that a place from which a business is merely supervised would not qualify.
- Prof. Kalus Vogel also states that, under German law, if the place of management cannot be determined by the application of these criteria, the top manager’s place of residence may determine the residence of the company.

Virtual PE – Emerging Concept

- A new emerging concept in the International Tax arena though not provided in Model Conventions.
- More prevalent in developing countries like India, Australia.
- Foreign Enterprise does not have a physical presence in the source country.
- Foreign Enterprise may or may not have an Agent or a Subsidiary in the source country.
- The concept of “Significant Economic Presence” is being applied i.e. presence through Brand, Distribution Arrangement, Digital Presence etc.
- Some Indian court rulings approved the Virtual PE concept
 - CIT Vs Vishakhapatnam Port Trust [1983] 15 Taxman 72 (AP)
 - DHL Ruling of Mumbai ITAT

Exclusions from PE

- Fixed Place PE - Preparatory and auxiliary activities.
 - - 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
- Agency PE - Independent agent.
 - Acting in its ordinary course of business.
 - Group companies are not necessarily dependent agents
- Agency PE - Arms length payment to agent.
 - Dependency test is not met for constitution of PE
- Agency PE - Subsidiary Company
 - Subsidiary Company in the source country need not necessarily be a PE

Key criteria applied for different types of PEs

Place of Business and associated test

Fixed Place PE and Other PEs are mutually exclusive?

Interplay between PE and other specific income articles of Treaty

“Place of Management” often causes challenge

Is subsidiary always regarded as PE of the overseas Parent?

Service PE Vs. Supervisory PE for construction contracts

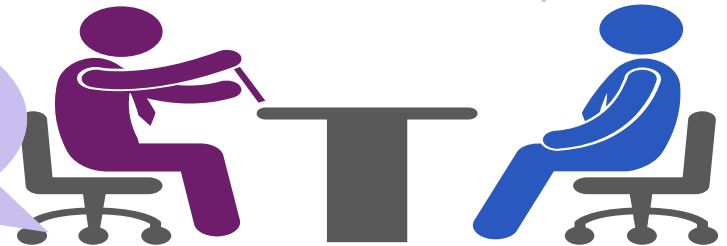
Duration test – still relevant post “Formula One” Ruling ?

Dependent Vs. Independent Agent – Payment of arm’s length remuneration

OECD/UN MC Vs US MC – Agency PE definition

Exclusions from PE – auxiliary and preparatory activities

Recent changes introduced under MLI



Emerging trends in Indian jurisprudence on PE

PROFIT ATTRIBUTION BASED ON EXTENDED FAR
Profit attributed to PE



7

DEPARTING FROM CONVENTIONAL PE THRESHOLDS
Fixed place PE allegations



1

RELYING ON FOREIGN JURISPRUDENCE
Drawing inference from overseas PE decisions



6

EXAMINING ROLE OF AFFILIATES
Agency PE allegations



2

TAXING DIGITAL PRESENCE
Software PE allegations



5

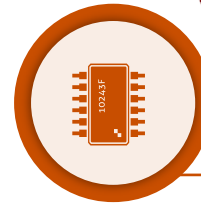
TAXING VIRTUAL PRESENCE
Service PE allegations



3

EMERGING TRENDS IN PE DECISIONS

EXAMINING LOCATION OF BUSINESS APPARATUS
Equipment PE allegations



4

Fast evolving trends in India jurisprudence to identify PE triggers

OECD reaction to COVID situation

Impact on PE

Fixed Place PE (Home Office)

- PE must have **certain degree of permanency and be at the disposal of an enterprise** in order for that place to be considered a fixed place of business
- Home office to be a PE for an enterprise, must be used on continuous basis for carrying on business of an enterprise and the enterprise generally has to require the individual to use that location to carry on the enterprise's business.
- During COVID-19 crisis, individuals who stay at home to work remotely are typically doing so as a result of government directives: it is force majeure not an enterprise's requirement.

It is unlikely that conditions for PE would be met.
OECD does note that its guidance is predicated on the basis that teleworking from home does "...not become the new norm over time."

Agency PE

- The OECD specifically looks at whether the activities of an employee who habitually concludes contracts and is temporarily working from home for a nonresident employer could give rise to a dependent agent PE.
- The OECD analysis focuses on the "habitual" requirement.

Employee presence in the nonresident country is likely to be considered merely transitory and therefore unlikely to be considered habitual if force majeure caused the employee work circumstances.

Construction PE

- The OECD notes that activities on construction sites are temporarily interrupted due to COVID-19.

These temporary interruptions should be included in determining the life of a site and will therefore affect the PE determination.

Consequences of PE in India

- Profits attributable to PE needs to be worked out
- Profits attributable to PE taxable in India on “Net basis” @ 40% plus surcharge and cess subject to satisfaction of conditions in section 44DA of the Act
- Applicability of TP provisions including reporting of international transactions and maintenance of TP documentation
- Applicability of withholding provisions – unless payment falls within source rule exclusions under domestic law
- Applicability of FEMA provisions depending on the nature of the PE
- Applicability of Companies Act provisions depending on the nature of the PE
- Compliance under the Indian Regulations depending on the nature of the PE – PAN, TAN, GST, ROI filing, assessments, Withholding tax, etc.

Interplay between POEM and PE



Interplay Between POEM

PE Both POEM and PE are anti-avoidance measures adopted by the countries to protect their tax base and avoid mi-use of treaty

- It is pertinent to note that having a permanent establishment of a foreign company in India is different from POEM.

Sr.	POEM	PE
1	POEM enables residence based taxation i.e. Global Income will be taxable.	PE allows source based taxation i.e. Only profit attributable to PE will be taxable.
2	Under POEM emphasis shifts from 'place of economic activity' to 'place where strategic decisions are taken'	PE is created when there is strong nexus with a source country i.e. economic activity in the source country reaches certain threshold (i.e. via physical presence or through its employees or dependent agent concluding contracts on its behalf in the source country).
3	POEM is exhaustively defined in the Act	PE is vaguely defined in the Act
4	Actual implementation or execution could be in overseas country	Actual execution and implementation to be in the source country

Interplay Between POEM

Sr.	POEM	PE
5	POEM seeks to tax in the Resident State	PE seeks to tax in the Source State
6	POEM applies “active income” and “passive income” tests	PE applies “active income” test unless “passive income” is attributable to such PE
7	POEM is larger concept	“Place of management” triggering PE is a sub-set of POEM
8	Tax Officer mandatorily need to take approvals from CITs for initiating and concluding on POEM	Tax Officer need not require any approval of the CITs for concluding PE
9	POEM poses challenges in multilayer structure	PE does not get impacted by multi-layer structure
10	POEM could result into economic double taxation	PE generally results into juridical double taxation
11	POEM could result into double taxation due to unclarity on FTC in the residence country	PE generally mitigates against double taxation through FTC in terms of Tax Treaty and domestic FTC Rules
13	POEM defined differently by various countries	PE is an international concept applied universally

Beneficial Ownership



Beneficial Ownership

- “Beneficial ownership” is an anti-avoidance mechanism to protect the tax base of the Source State
- The concept is included in domestic laws of countries as a “Special Anti Avoidance Regulations” (SAAR)
- There is a difference between “Beneficial owner of income” and “Beneficial owner of assets”
- Domestic Tax Laws applies both the concepts depending on the tax avoidance transaction or arrangement – India, US
- Beneficial ownership is applied differently by different countries for domestic tax law purposes
- Concept of “Ultimate Beneficial Ownership” applied in domestic tax laws to combat “Benami arrangements and transactions” as well as “Conduit arrangements”

Beneficial Ownership under

Sr.	Section	Provisions
1	2(22)	Deemed dividend taxation - when a loan / advance (to the extent of accumulated profits) has been made by a closely held Indian Company to a shareholder, being a person who is the beneficial owner of shares , holding not less than 10% of the voting power in the Company.
2	40A(2)(b)	<p>Transactions with specified persons</p> <p>Explanation to Section 40A (2)(b) of the Act defines the term “substantial interest” in a company to mean “beneficial ownership” of shares carrying not less than twenty percent of the voting power.</p> <p>PE applies “active income” test unless “passive income” is attributable to such PE</p>
3	79	Change in the shareholding of a company beyond 51% of the “voting power”
4	97 read with 102	Transactions that lack commercial substance – Person having substantial interest in the business of the other person
5	92A	Meaning of Associate Enterprises – Person who participates directly or indirectly in the management or control of enterprise of the other person

Beneficial Ownership under

Sr.	Article	Provisions
1	10	Dividend – lower rate applied if the recipient is the beneficial owner of dividend
2	11	Interest – lower rate applied if the recipient is the beneficial owner of interest
3	12	Interest – lower rate applied if the recipient is the beneficial owner of royalty or FTS
4	13	Capital gains – lower or no taxation on capital gains in the Source State if the transferors of assets holds specified percentage of holding or voting powers in the company located in the Source State – India-Netherlands
5	92A	Meaning of Associate Enterprises – Person who participates directly or indirectly in the management or control of enterprise of the other person

Beneficial Ownership

- **Why it is Important to identify Beneficial Ownership?**
- Anonymity enables many illegal activities to take place hidden from law enforcement authorities, such as tax evasion, corruption, money laundering, and financing of terrorism.
- Primarily used to avoid treaty shopping
 - One of the most important anti-abuse provision
 - US has beneficial ownership as concept [beneficial ownership of the income and also beneficial ownership of the entity]
- **A concept widely used but hardly defined**
- To deny treaty benefits to Conduit companies set up as intermediaries for not being the beneficial owner of the income.

Beneficial Ownership

- **Definition of ownership**

Black's Law Dictionary - Eighth Edition

“One who has the right to possess, use, and convey something; a person in whom one or more interests are vested”

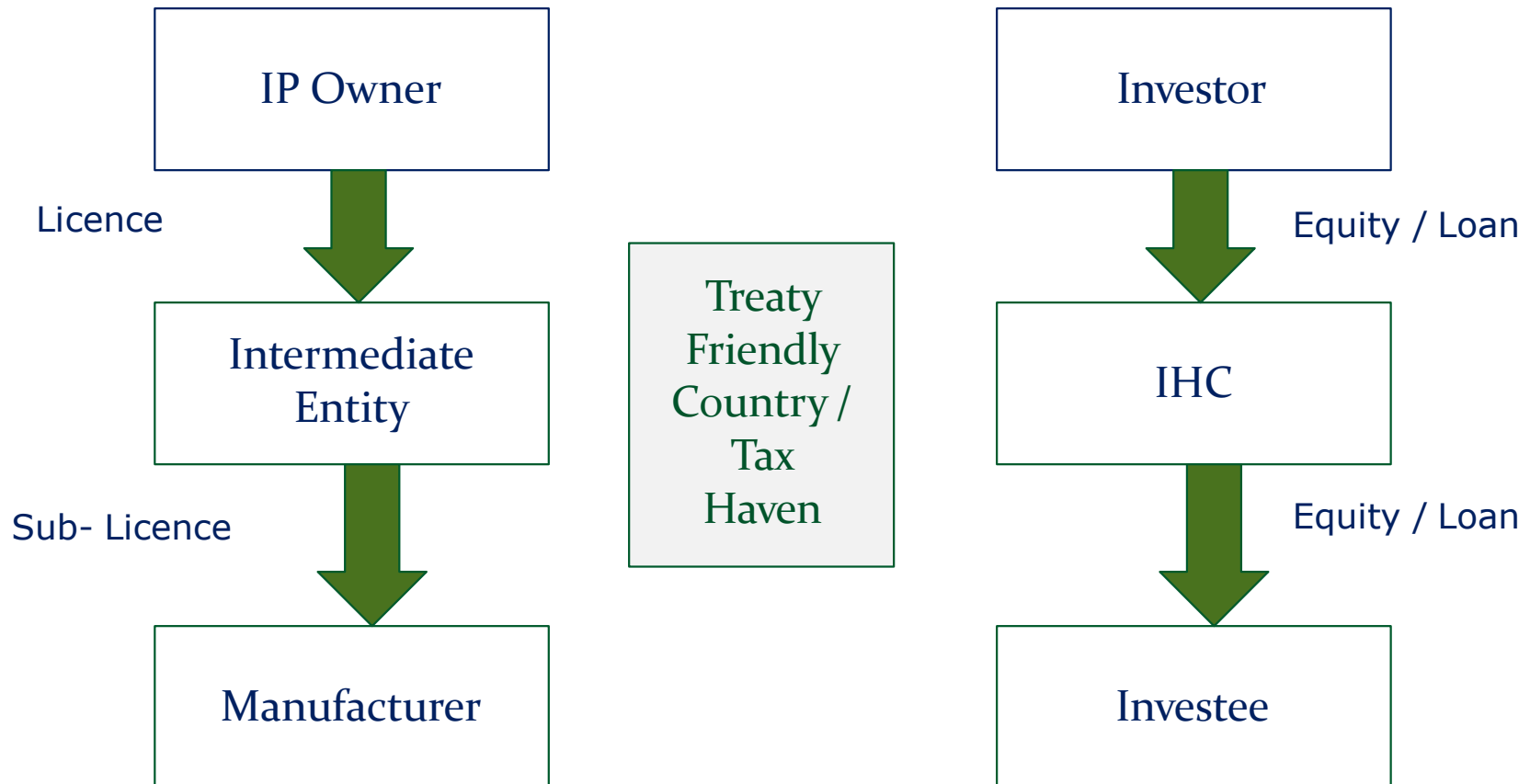
Supreme Court, Swadesh Ranjan Sinha vs Haradeb Banerjee, AIR 1992 SC [1590]

- *“Ownership’ is a bundle of rights attached with a property”*
- OECD – Article 3(2)
 - where the term is not defined in the treaty, it should be interpreted based on source country domestic law, unless the context requires otherwise
- OECD Commentary
 - ‘beneficial ownership’ is not used in a narrow technical sense...”
- English law
 - “beneficial owner”, would exclude a legal owner who is trustee for another

Beneficial Ownership

- In the absence of the precise and clear definition, the term ‘Beneficial ownership’ has always been subject matter of litigation. As per legal dictionaries, the term is defined as under:
- **Black’s Law**
 - “One recognized in equity as the owner of something because use and title belong to that person even though legal title belongs to someone else”
- **Law Lexicon**
 - “One who, though not having apparent legal title, is in equity entitled to enjoy the advantage of ownership”
- **Klaus Vogel**
 - “Beneficial owner is a person who is free to decide whether or not the capital or other assets should be used or made available for use by others (i.e., the right over capital), or how the yields from them should be used (i.e., the right over income), or both”
- **Webster’s**
 - “One who is entitled to receive the income of an estate without its title, custody, or control”

Beneficial Ownership



Beneficial Ownership-

• Concepts OECD

- Concept based on the principle of **substance over form**
- Treaty benefit to the residents of a contracting state only if they are the '**Beneficial owners**' of income in the nature of dividends, interest, royalties and FTS i.e. passive income. Illustrative phraseology [Articles 10, 11 and 12 of the OECD Model Convention of 2010]:

“Such interest may also be taxed in the Source state and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 percent of the gross amount of the interest”

- OECD commentary recognizes the concept of '**Beneficial owner**' as a measure used to counter '**Tax avoidance**'. It provides that the term '**Beneficial owner**' should **not be interpreted in a narrow technical sense**
- '**Beneficial owner**' should be understood in the context and in light of the object and purposes of the tax treaties, including avoiding double taxation and the prevention of fiscal evasion and avoidance.
- Conduit companies set up as intermediaries receiving income on behalf of other persons who in fact receive the benefit of the income concerned, should also be denied tax treaty relief for not being the beneficial owner of the income.

Beneficial Ownership- Tax

High level guidance on interpretation of this term, considering Indian and international jurisprudence, the Commentary on the OECD Model Convention and various international tax commentaries, is given below:

- In general parlance, a 'beneficial owner' is the one who enjoys the ultimate benefits of something which he is entitled to receive. In other words, a beneficial owner is the one who is free to decide how such income yields should be used. Thus, while there could be a legal owner of certain income, however, the beneficial owner thereof could be a different person.
- A person is a beneficial owner if he receives dividends for his own use and enjoyment, and assumes risk, dominion and control over such funds. [The Queen v Prevost Car Inc (2009) (DTC 5053 FCA) and Velcro Canada Inc. v. The Queen, (2012) (TCC 57)]
- Where the recipient of dividend has the right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass on the payment received to another person, the recipient is the 'beneficial owner' of that dividend. (2017 OECD Commentary on the Model Convention)
- A beneficial owner is the person who is the economic owner of the income. (*Klaus Vogel on Double Taxation Conventions, Fourth Edition, Volume 1, page 726*)

Beneficial Ownership- OECD

- OECD focused on use of “agent or nominee or conduit entities” by tax payers to avoid or reduce tax in the Source Country
- OECD highlights following conduit approaches used by tax payers:
 - Direct Conduit Approach – Back to Back Dividend through investments or through other arrangements
 - Stepping Stone Approach – Equity Investment supported by back to back Debt arrangement
- OECD suggested following approaches to combat tax avoidance
 - Look through Approach – whether the target company in the Source State is directly or indirectly controlled by the resident of the other state
 - Subject to tax Approach – benefit available only if the recipient is taxable on such income in the Resident State
 - Channel Approach – Third Country resident control and manages the use of the income for his own benefit or its arrangements/transactions
 - Bonafide Approach – Treaty benefit not to be denied in case of Bonafide transactions or arrangement, listed companies, etc.

Beneficial Ownership – Reference

Materials

- OECD MC and Commentary - 2014 Update
- OECD MC and Commentary 2017 Update
- OECD Conduit Company Report 1986
- OECD Report on Harmful Tax Practices Act, 2018
- OECD Task Force Report 2019
- International Judicial Precedents
- Indian Judicial Precedents – largely on Beneficial Owner of Asset
- US Technical Explanation to US Tax Treaties

The focus of all these rules and regulations is “Substance over Form”

Beneficial Ownership- Tax

- A table summarizing factors that indicate whether the 'beneficial ownership' requirement is satisfied or not is set out below. This is not intended to be exhaustive, and a determination of whether this requirement is satisfied will need to be made on a case by case basis.

Circumstances where the requirement of 'beneficial ownership' is met	Circumstances where the requirement of 'beneficial ownership' is not met
<ul style="list-style-type: none">- An intermediate company can still be the beneficial owner if there are business reasons for it to be interposed- There is complete assumption of risk, dominion and control over the funds by the recipient- A distribution of the dividend income without a pre-commitment does not vitiate beneficial ownership	<ul style="list-style-type: none">- Where dividends are received by a person in the capacity of an agent or a nominee. This will include cases where a person holds legal title for the benefit of someone else (e.g. an administrator, a trustee)- Where the recipient acts as a conduit for another person who in fact receives the benefit of the income i.e. where, as a practical matter, the conduit has such narrow powers which render it a mere fiduciary or administrator

Beneficial Ownership- Tax

Treaties

Circumstances where the requirement of 'beneficial ownership' is met

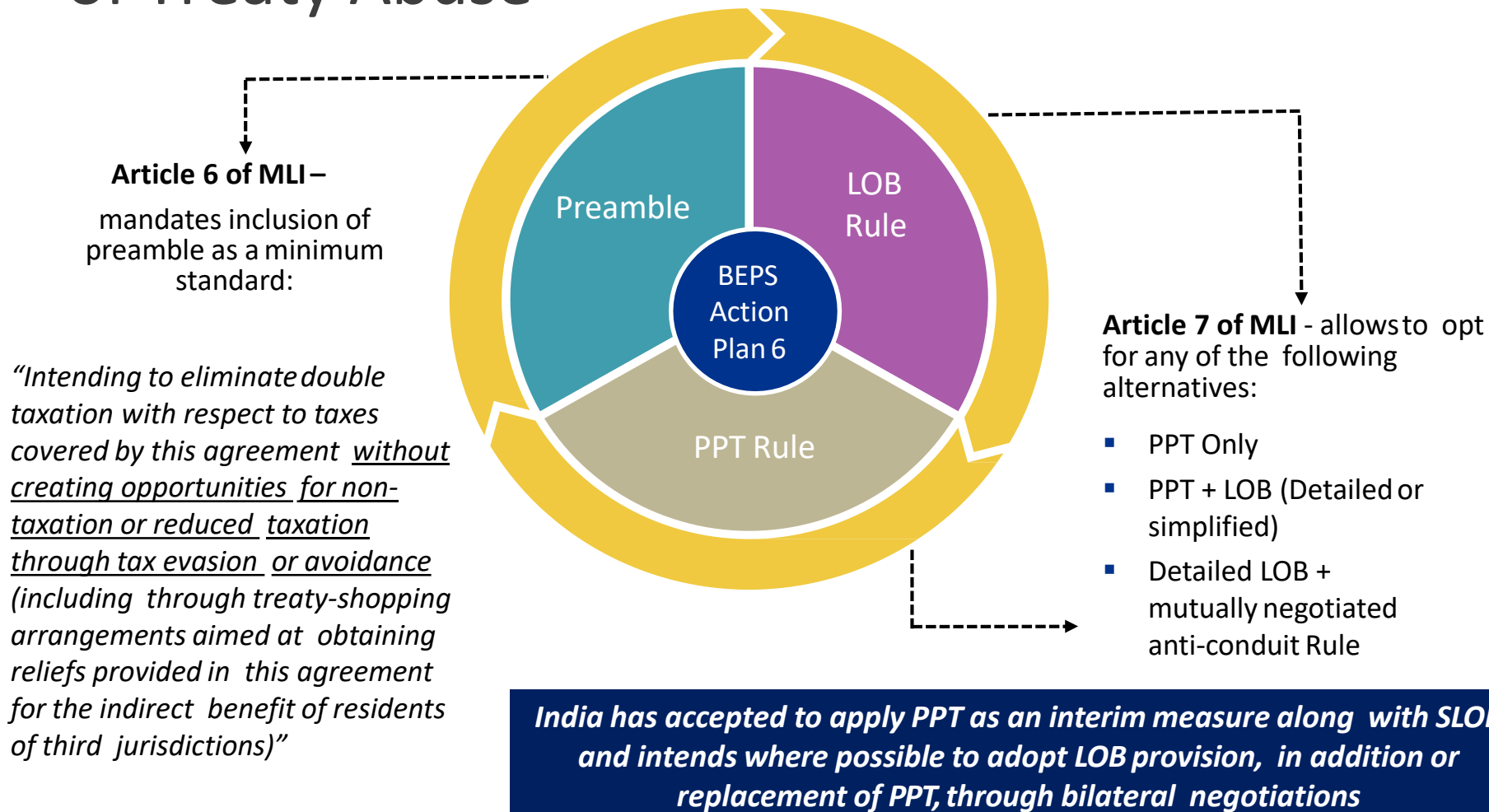
- Location of the bank account in another country does not indicate an absence of beneficial ownership. The relevant factor is control over the bank account and not the location of the bank account

Circumstances where the requirement of 'beneficial ownership' is not met

- Where the recipient's right to use and enjoy the dividend is constrained by a contractual or legal obligation to pass on the payment to another person (such obligations can also be inferred from facts and circumstances that indicate that in substance the recipient has no right to use and enjoy the income)
- If the legal owner of the shares is bereft of all the rights which would normally attach to the shares, he cannot be considered as the beneficial owner
- - Where the facts indicate that the recipient is not in a position to make decisions regarding the utilization of the dividends

India's Position on MLI -

of Treaty Abuse



India's Position on MLI -

Prevention of Treaty Abuse

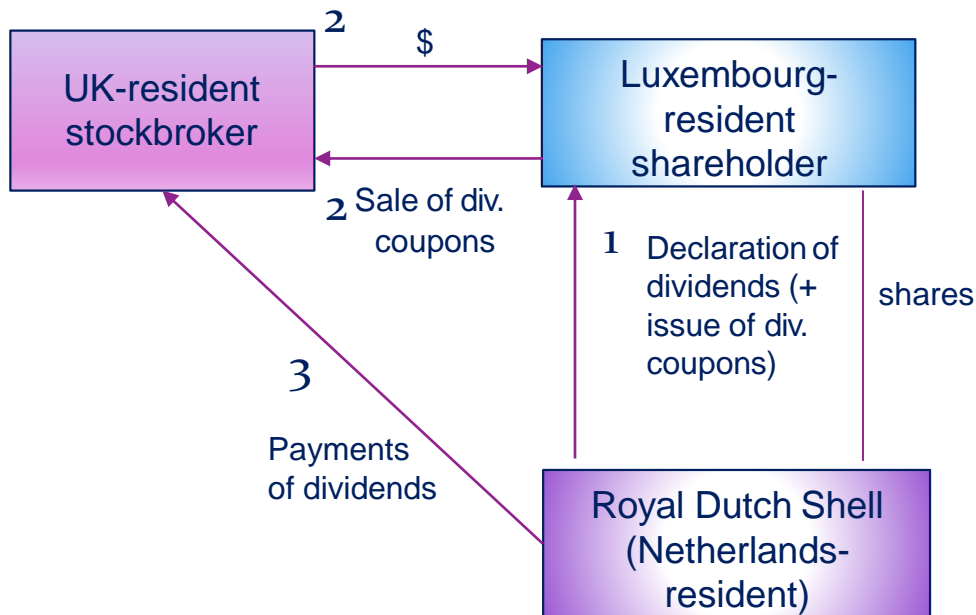
Article	Title/Particulars	Brief Description	India's Position
Treaty Abuse (Action Plan 6)			
6	Preamble (Minimum Standard)	CTA to be modified to include preamble text providing for intention to eliminate double taxation without creating opportunities for double non-taxation (including treaty shopping).	India amended the provisions of section 90 of the Act vide Finance Act, 2020
7(1)	Principal Purpose Test (PPT) (Minimum Standard)	Denial of treaty benefit where it is reasonable to conclude that one of the principal purpose of any arrangement or transaction is to obtain treaty benefit.	India has accepted PPT as an interim measure. Being a minimum standard, it applies to all CTA's, unless other Party makes reservation in entirety of Article 7 not to apply.
7(8 to 13)	Simplified Limitation on Benefit (SLOB)	It is a subjective test to obtain treaty benefit and is based on type of person, ownership, equivalent beneficiary, active conduct of business, etc. It is an optional provisions and supplements PPT.	India has chosen to apply SLOB. SLOB applies only where either other Party has also adopted SLOB, or that Party allows India to apply SLOB symmetrically or asymmetrically

India's Position on MLI -

Treaty Abuse (Action 6) Prevention of Treaty Abuse

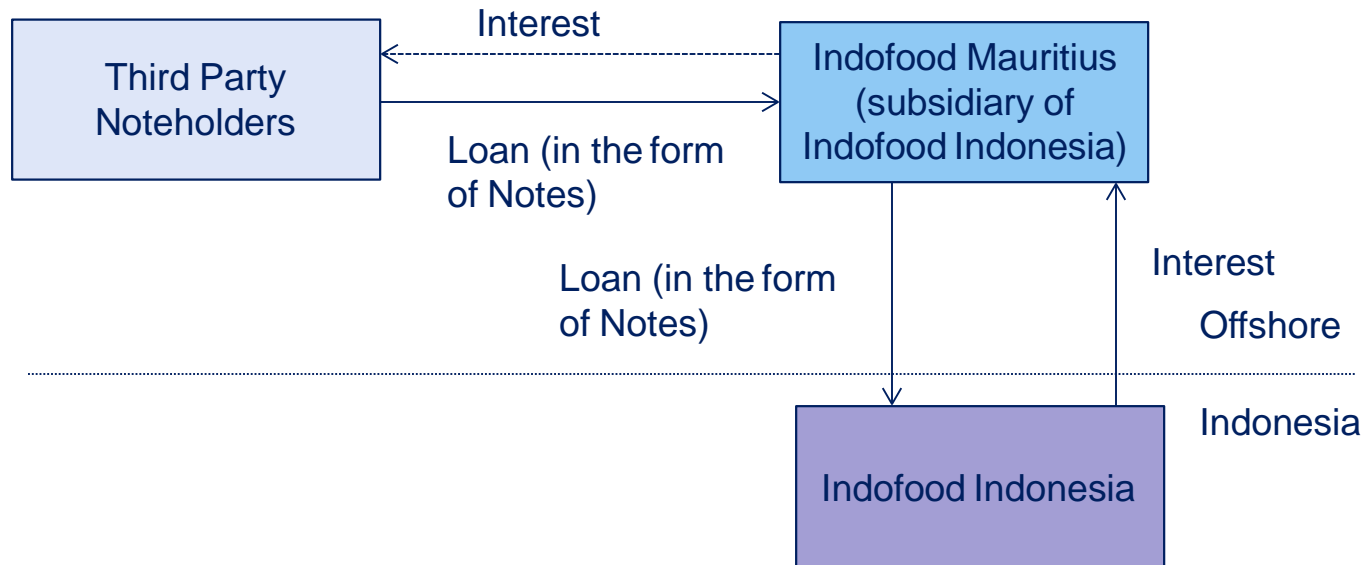
8	Dividend transfer transaction	Additional criteria of “365 days minimum holding period” for the shareholder to avail concessional tax rates under CTA	India has opted to apply the said MLI provision (except in the case of India Portugal treaty, which already contains minimum holding period longer than 2 years). MLI provision to modify CTA provisions except India-Portugal treaty, unless reservation is made by other Party or in case of notification mismatch.
9	Capital Gains on interest in underlying immovable property	Introduces additional criteria of “365 days minimum holding period” in case of capital gains arising from alienation of shares or interests of entities deriving their value principally from immovable property. Optional provision of inserting a minimum value derivation criterion of 50% of their value directly or indirectly from immovable property.	India has opted to apply minimum holding period threshold along with minimum value derivation criterion of 50%. The said provision to apply only if other Party to CTA has chosen to apply the said provision.

Royal Dutch Shell Case



Could the UK-resident stockbroker claim the limitation on Dutch dividend withholding tax, under the UK/Netherlands treaty? In other words, was the UK-resident stockbroker “the beneficial owner” of the dividends?

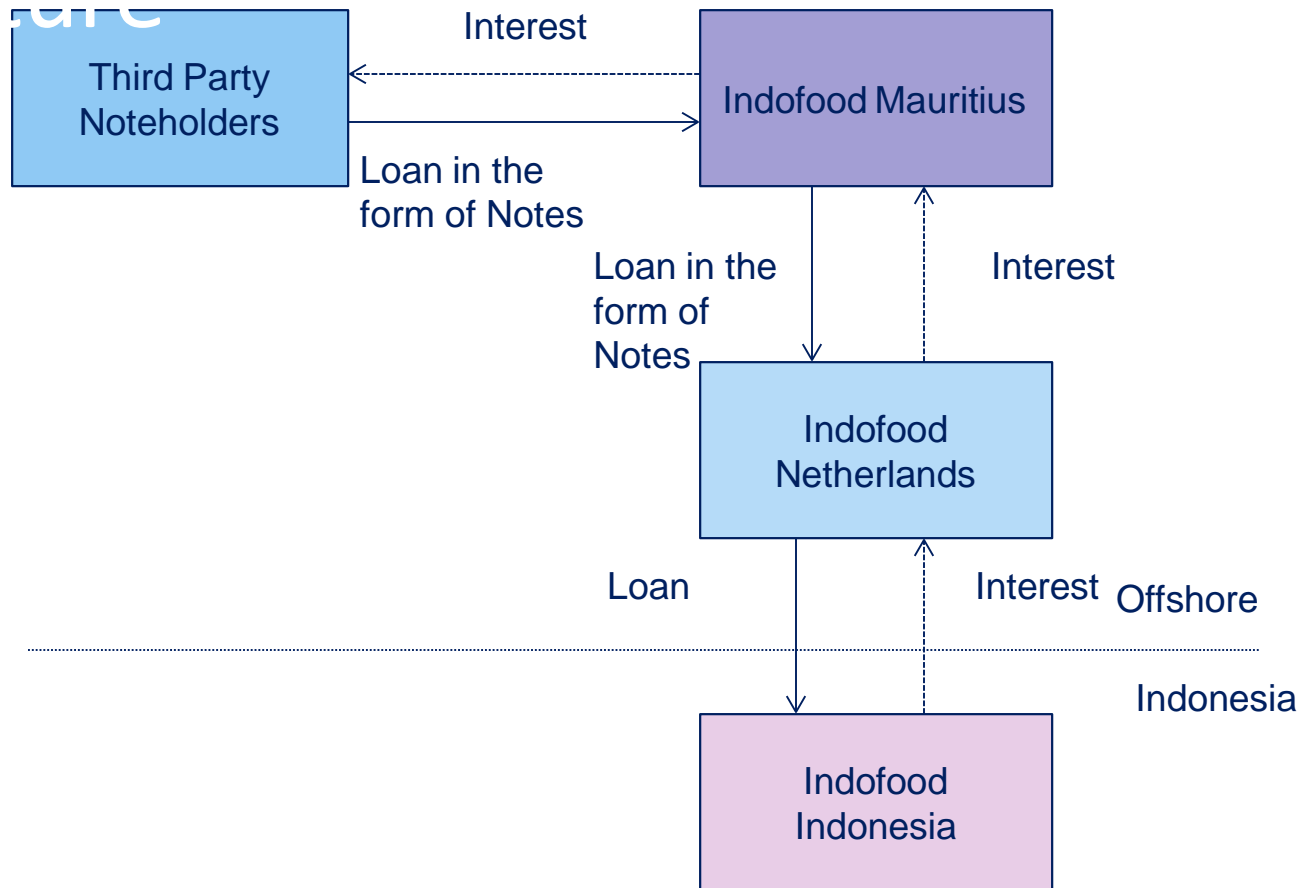
Indofood Case Law



- Indonesia domestic tax law: 20% interest withholding tax
- Indonesia/ Mauritius treaty: 10% (if beneficial owner)
- Indonesia/ Mauritius treaty: terminated in 2005
 - Indofood wanted to redeem the Notes, because of an adverse movement in interest rates and because of the increased “gross up” requirement due to the treaty termination.
 - The treaty termination allowed Indofood to redeem the Notes, unless it could avoid the additional tax by “taking reasonable measures available to it.”

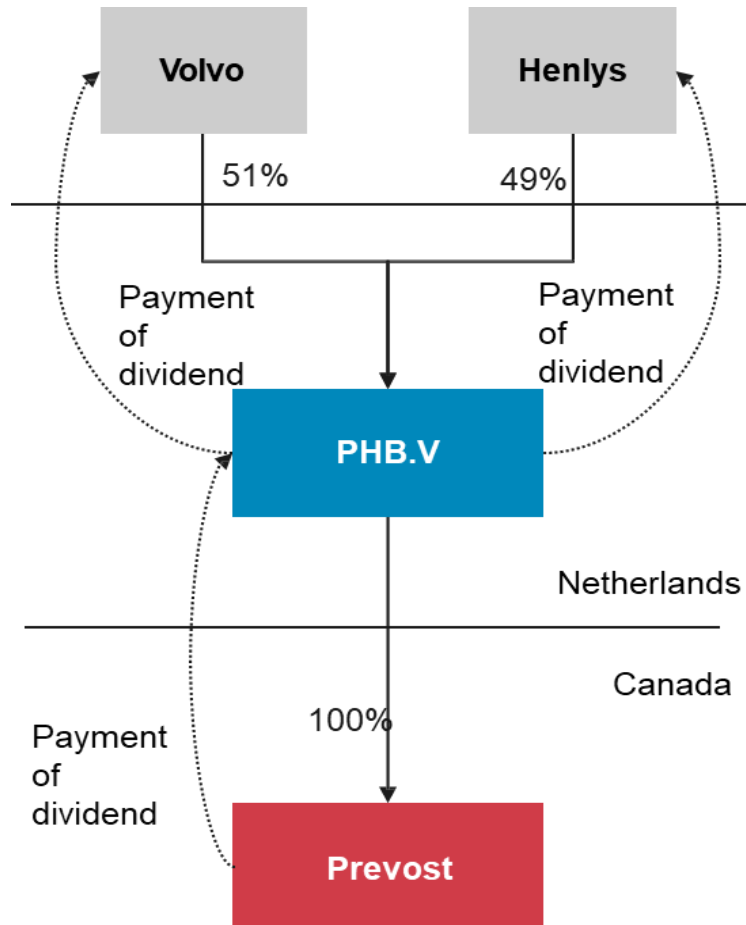
Indofood Case Law- Proposed

Structure Proposed by Trustee



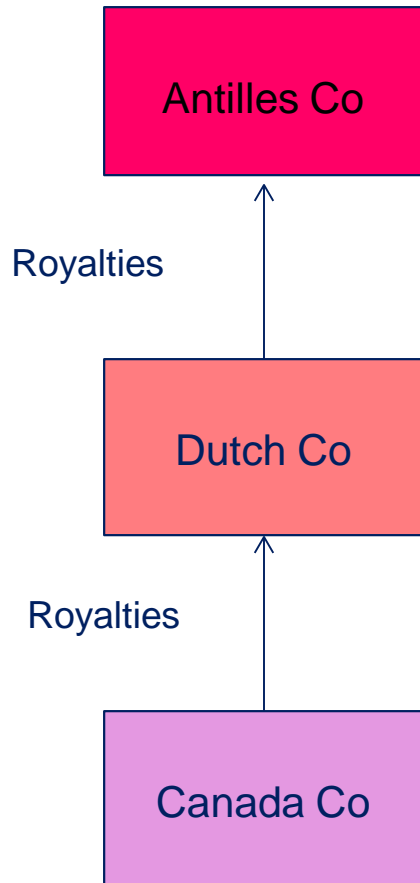
- Indonesia/Netherlands treaty: 0%/10% (if beneficial owner)

Prevost Case Law



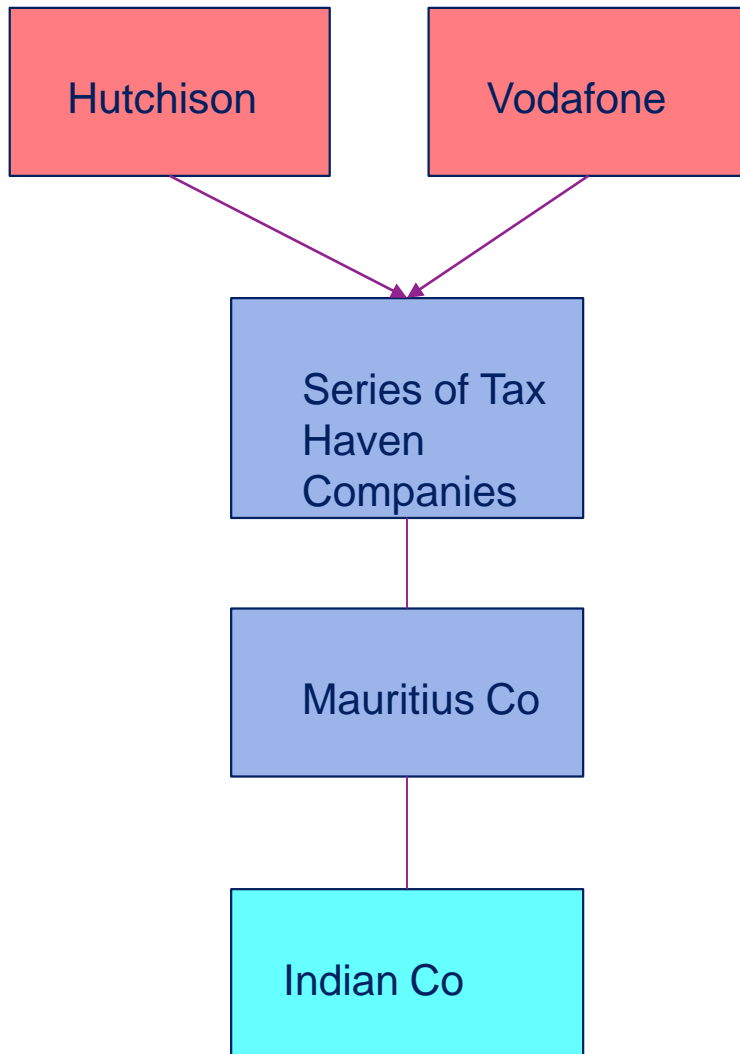
- **Facts of the Case**
- The shareholders of Prevost transferred their shareholding to PHB.V, a Netherlands resident company which was owned by Volvo and Henlys.
- Shareholders agreement provided that at least 80 % profits of Prevost, PHB.V and their subsidiaries to be distributed to Volvo and Henlys.
- Dividends were distributed by PHB.V in accordance with the above agreement
- Prevost applied a beneficial withholding rate of 5 percent under the Canadian Dutch treaty on dividend payments made to PHB.V
- During the year under appeal, PHB.V had no employees in Netherlands nor did it have any investments other than the shares in Prevost
- Further, PHB.V from time to time represented that the beneficial owners of the shares of Prevost were Volvo and Henlys in the KYC documentation provided to its bankers

Velcro Canada Case Law



- Antilles Co is the owner of licensed IP
- Antilles Co assigned right to grant licences of IP rights and to royalty payments to Dutch Co but retains ownership of the IP
- Expenses of Dutch Co reimbursed by shareholders as needed
- Dutch Co has substantial cash, investments in subsidiary and loan receivables
- Arm's length person provides office space, banking, bookkeeping, managing directors to Dutch Co

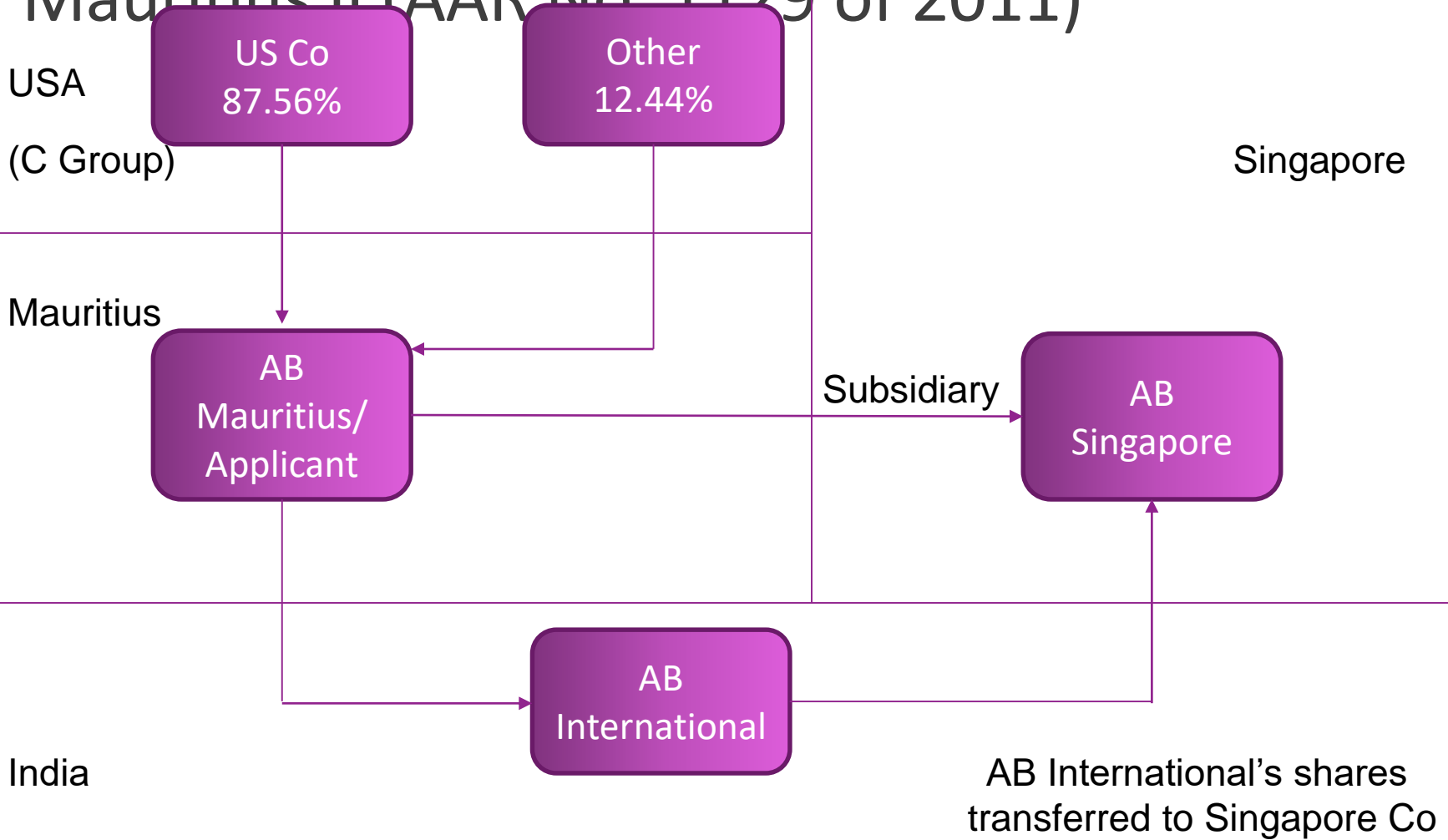
Vodafone Ruling



- Vodafone Ruling while did not really focus on beneficially ownership of share, it did refer to as a concept in relation to alternate arguments put forth by the tax department.
- In this case also, the Supreme Court laid the law that you have to respect the structure.
- Simply having layer of companies with very little business objective does not automatically calls for rejection of structure.
- Each company has authority to decide their activities and unless and until these rights are surrendered or compromised, it cannot be treated as not being the beneficial owner.

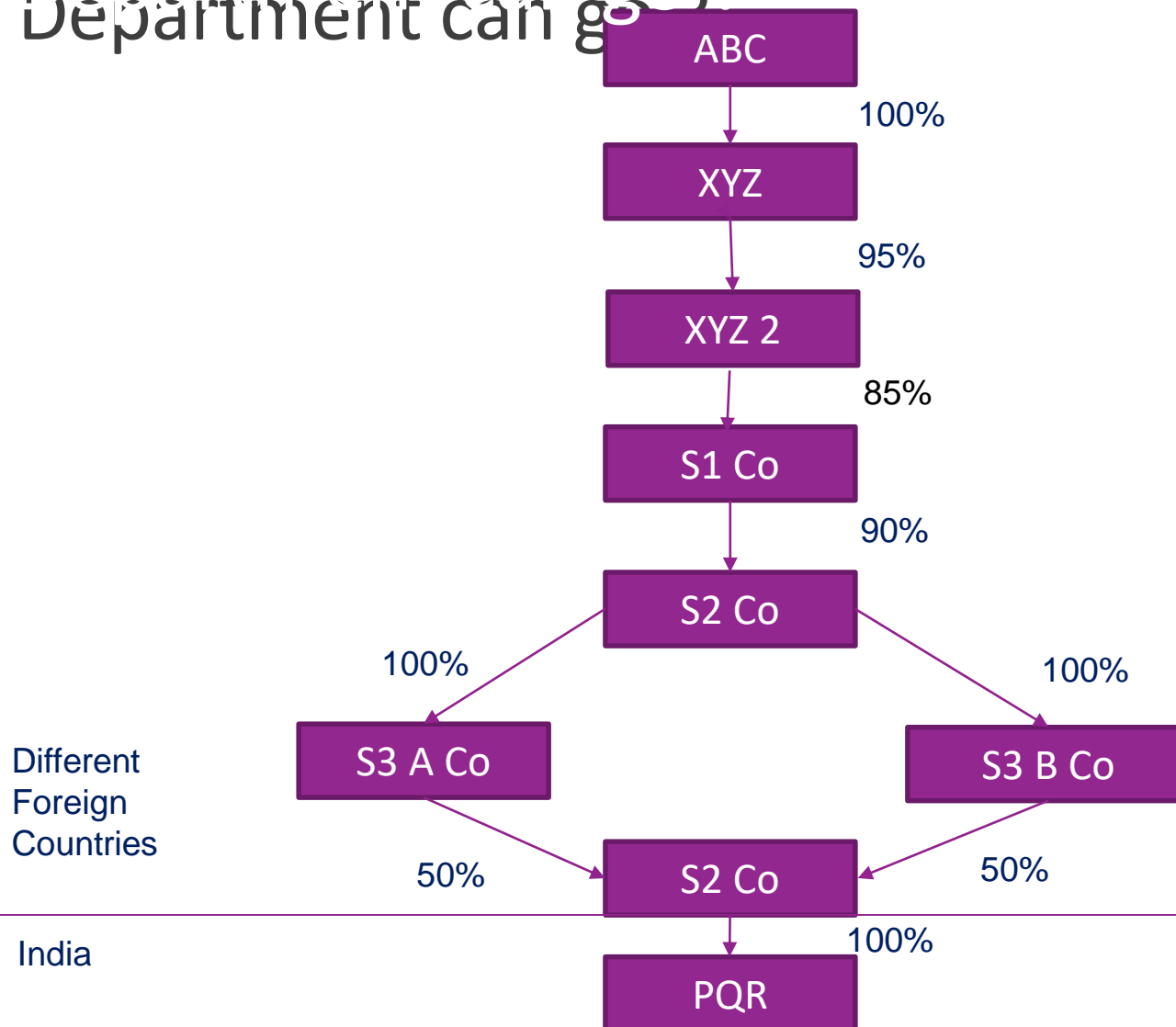
Beneficial Ownership – AB Holdings

Mauritius II (AAR No. 1179 of 2011)
Mauritius II (AAR No. 1179 of 2011)



Ultimate beneficial Owner - How far the

Department can go?



Indian Tax Treaties – Special Reference to Mauritius and Singapore



Structure of a Tax Treaty

ARTICLE

- Article 1 and 2
- Article 3, 4 & 5
- Article 6 to 22 (except Article 9)
- Article 9
- Article 23
- Article 24 to 28
- Article 29 and 30

Scope

- Scope of persons, Taxes covered
- General definitions, Permanent Establishment
- Distribution of taxing rights for incomes like business profits, immovable property, dividend, royalty/FTS, salary, other income
- Associated enterprise
- Method of elimination of double taxation
- Non discrimination, MAP, Exchange of information, assistance in collection of taxes, diplomats
- Entry into force and termination

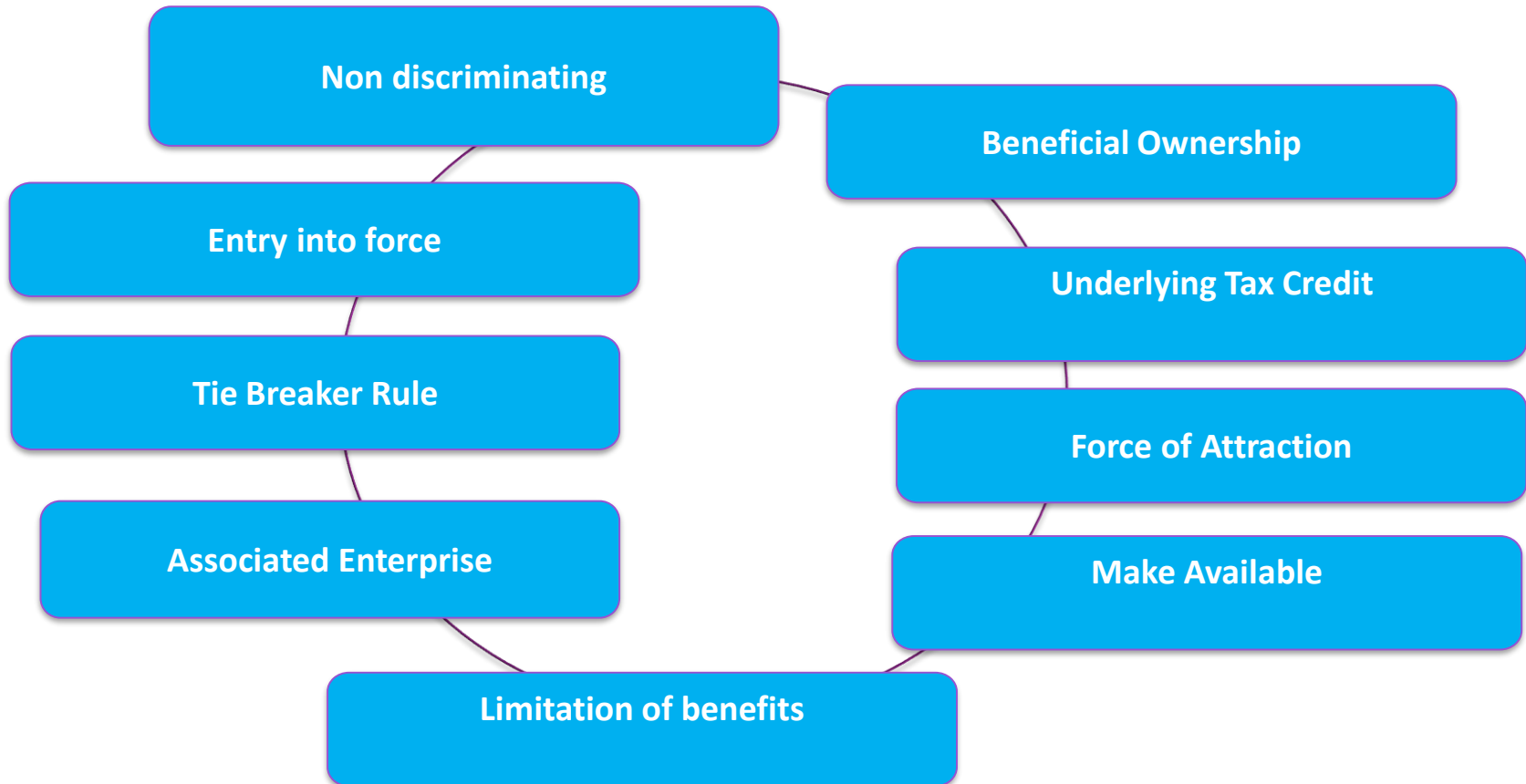
Fundamental Aspects of Tax

Treaty

Persons Covered	Taxability in the Country of Residence	Taxes Covered
<p>Individuals</p> <p>Company</p> <p>Partnership Firm</p> <p>Body of Individuals</p> <p>LLP?</p> <p>Trust?</p> <p>S Corporations?</p> <p>Fiscally transparent entities?</p>	<p>Economic Taxation vs Fiscal Taxation</p> <ul style="list-style-type: none">- Particular source of income not taxable- Person is exempt in state R- Person is not covered by tax law in state R- Person is not required to pay tax in state R- Person is taxable in state R only on source income	<p>Federal and State Tax</p> <p>Corporate Income Tax</p> <p>Dividend Distribution tax</p> <p>Property / wealth tax</p> <p>Surcharge</p> <p>Municipal and Country Tax?</p> <p>Equalization levy?</p> <p>Branch Profit tax</p> <p>Digital Tax?</p> <p>Buyback Tax?</p>

Important Concepts in the Indian

~~Tax Treaties~~ Tax Treaties



Overview of India's Tax Treaties

Article	India- Mauritius	India- Singapore
Business Profits	The profits of an enterprise are taxable only in the state where the business operations are carried out. If a Mauritius-based business has a permanent establishment in India, the profits attributable to the permanent establishment will be taxed only in India.	The profits of an enterprise are taxable only in the state where the business operations are carried out. If a Singapore-based business has a permanent establishment in India, the profits attributable to the permanent establishment will be taxed only in India.
Dividend**	<ul style="list-style-type: none"> a) 5% of the gross amount of dividends if the BO is a company which holds directly at least 10% of the capital of the company paying the dividends; b) 15% of the gross amount of dividend in all other cases. 	<ul style="list-style-type: none"> a) 10% of the gross amount of dividends if the BO is a company which owns at least 25% of the shares of the paying the dividends; b) 15% of the gross amount of dividend in all other cases.

*** From 1 April 2020, India has abolished the DDT and the dividends will be taxed in the recipient's hands. Instead, India has introduced a dividend withholding tax. The rate will be 20% if paid to foreign investors or rate as per treaty whichever is beneficial*

The Introduction of the new dividend tax regime by India creates an outstanding opportunity for substantial tax savings by making a foreign company a shareholder of an Indian company. This can be very beneficial to both foreign and Indian shareholders.

Overview of India's Tax Treaties

Article	India- Mauritius	India- Singapore
Interest	7.5% of the gross amount of interest if the BO is a resident of the other Contracting State.	a) 10% of the gross amount of the interest if such interest is paid on a loan granted by a bank carrying on a <i>bona fide</i> banking business or by a similar financial institution (including an insurance company); b) 15% of gross amount of interest in all other cases; if the BO is a resident of other contracting state.
Royalty & Fees for Technical Services ('FTS')	Article 12 – Royalties Article 12A – FTS Royalties- 15% of the gross amount of royalties. FTS- 10% of the gross amount of FTS if the BO is a resident of the other Contracting State.	Article 12- Royalties & FTS 10% if the recipient is the beneficial owner of the royalties & FTS
Make Available Clause	Not available	Available
Independent Personal Services	Clause not available	Clause available

Overview of India's Tax Treaties

Article	India- Mauritius	India- Singapore
Shipping & Air Transport	Profits from the operation of ships or aircraft in international traffic shall be taxable only in the Contracting State in which <i>the place of effective management of the enterprise is situated.</i>	Profits derived by an enterprise of a Contracting State from the operation of ships or aircraft in international traffic shall be taxable <i>only in that State.</i>
Limitation of Benefit/ Relief	Available (Article 27A) – State the nature of the LoB	Available (Article 24) – State the nature of the LOB
Shell/Conduit Company	if its expenditure on operations in that Contracting State is less than Mauritian Rs.1,500,000 or Indian Rs. 2,700,000 in the immediately preceding period of 12 months from the date the gains arise.	if its annual expenditure on operations in that Contracting State is less than S\$ 200,000 in Singapore or Indian Rs. 5,000,000 in India, as the case may be: (a) in case of gains from alienation of shares acquired before 1 April 2017, for each of the 12 month periods in the immediately preceding period of 24 months from the date on which the gains arise; (b) in case of gains from alienation of shares acquired on or after 1 April 2017 but disposed off before 31 March 2019, for the immediately preceding period of 12 months from the date on which the gains arise.

Overview of India's Tax Treaties

Article	India- Mauritius	India- Singapore
Capital Gains	Shares Acquired	Capital Gain Tax on Sale of Shares
	Before 1 April 2017	Such shares will continue to benefit from the current capital gains exemption in Article 13(4) of the India-Mauritius treaty
	Acquired on or after 1 April 2017 –but disposed of before 31 March 2019	Limited transitional provisions will be applicable. Disposal of such shares will be subject to a reduced tax rate of 50% of the domestic rate in India. The application of the reduced rate is however subject to a Limitation of Benefits (LOB) clause.
	After 31 March 2019	Disposal of such shares will now be subject to tax in India.
Foreign Tax Credit	<ul style="list-style-type: none"> Dividend Income – Underlying Tax Credit ('UTC') Other Income – Ordinary Credit To promote Economic Development- (Eg: SEZ)- Tax Sparing Credit 	<ul style="list-style-type: none"> Dividend Income- UTC Other Income- Full Credit To promote Economic Development- (Eg: SEZ)- Tax Sparing Credit

Indian Tax Treaties impacted by

with effect from 1 April 2009

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 USA, Mauritius, Germany

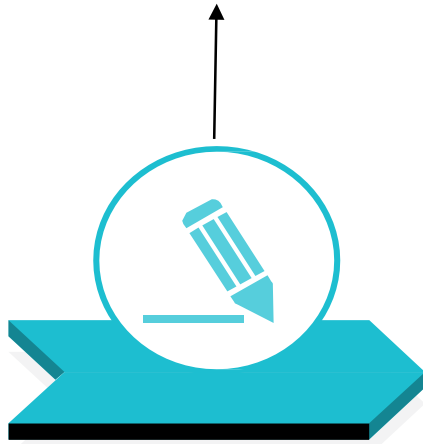
Australia, Austria, Finland, Ireland, Poland, Lithuania, Slovak Republic, etc.

Applicability of MLI – how

timelines work?

Example: India-Singapore Tax treaty

Singapore – 21 Dec 2018
India – 30 June 2019



- 1 Ratification and filing with OECD

Singapore EOF – 1 Apr 2019
India EOF – 1 Oct 2019



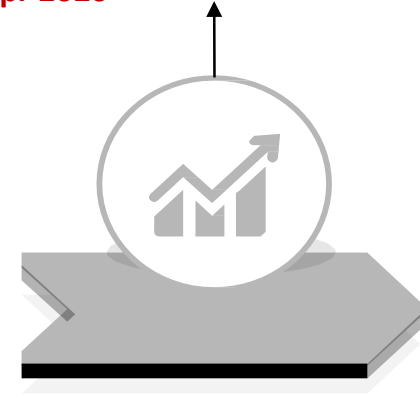
- 2 Entry into force ('EOF')
First day of the month following:
Filing of ratification with OECD + 3 months

India EIF for WHT
– 1 Apr 2020

India EIF for Other Taxes – 1 Apr 2020

Singapore EIF for WHT
– 1 Jan 2020

Singapore EIF for Other Taxes – 1 Jan 2021



- 3 Entry into effect ('EIF')
Withholding tax: first day of FY that begins on or after the "optional relevant date"*
Other taxes: from FYs beginning on or after six months from the "optional relevant date"*

*"Optional Relevant Date" shall be determined from "30 days from latter of the dates on which OECD receives notification from India and its treaty partner about completion of its respective internal procedures"

For countries that have deposited the MLI instrument with OECD : EIF with India is FY 20-21 For countries that have not yet deposited the MLI instrument with OECD : EIF to be analyzed

Summing Up



Summing Up

- Each Source Country is protecting its “tax base” – conflict between “Global Village” and “Own Village”
- Digital advancements is changing business models so as the taxation principles – new challenges are being thrown open
- Significant Thrust on “Substance over Form” – Treaty Shopping and Conduits are under constant scanner
- International commentaries / judiciaries are now beholding at “look through approach” instead of “look at approach”
- BEPS Action Plans, PPT, MLI, GAAR ad other anti-avoidance regulations will play an important role in structuring cross border transactions and investments
- Stringent KYC norms/ disclosure norms, sharing & exchange of information, GAAR, PPT, SLOB clause will not permit conduit transactions and treaty shopping
- Imperative for taxpayers to examine agreements and arrangements from international perspective
- International taxation is evolving all the time and new set of challenges emerges resulting in new set of litigations and controversies

Q & A



Questions



Answers

THANK YOU ALL FOR YOUR ATTENTION !

CA JAYESH KARIYA

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Significant Beneficial Owner as per Companies Act

- As per Section 90(1) of the Companies Act, 2013 read with SBO Rules '18, SBO is
 - Every Individual, who, acting alone or together, or
 - through one or more persons or trust:
 - Including a trust and persons resident outside India **holds**
 - Ultimate beneficial interest of **at least 10%** in shares of a Company or
 - the right to exercise, or the actual exercising of significant influence or control as defined in clause (27) of section 2 over the company **but**
 - whose name is not entered in the register of members of a company as the holder of such shares.
 - *Note: Instruments in the form of global depository receipts, compulsorily convertible preference shares or compulsorily convertible debentures shall be treated as shares for the purpose of determining significant beneficial owner.*
 - As per section 89(10) of the Act, Beneficial Interest in a share includes, directly or indirectly, through any contact, arrangement or otherwise, the right or entitlement of a person alone or together with any other person to –
 - ✓ Exercise or cause to be exercised any or all of the rights attached to such share; or
 - ✓ Receive or participate in any dividend or other distribution in respect of such share.