



**WIRC OF THE INSTITUTE OF CHARTERED
ACCOUNTANTS OF INDIA**

Interpretation of DTAA post Multilateral Instrument ('MLI')

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MLI - Introduction and Framework

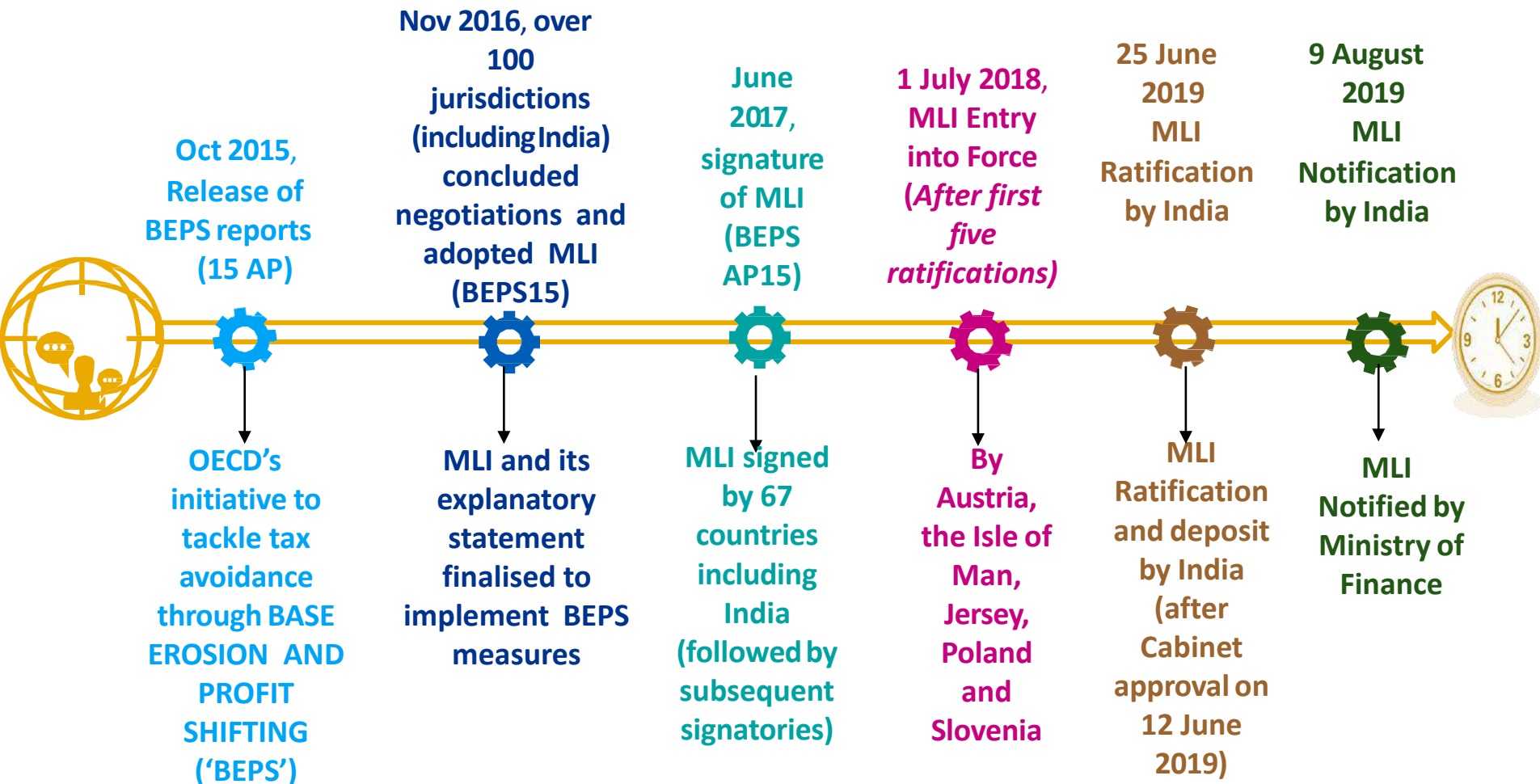
BEPS Action Plan at a Glance

BEPS ACTION PLANS	SCOPE
Action 1	Addressing the tax challenges of digital economy
Action 2	Neutralizing the impact of Hybrid Mismatch Arrangements
Action 3	Designing Effective Controlled Foreign Company Rules
Action 4	Limiting Base Erosion Involving Interest Deductions and Other Financial Payments
Action 5	Countering Harmful Tax Practices more effectively, Taking into account Transparency and Substance
Action 6	Preventing the granting of Treaty benefits in appropriate circumstances
Action 7	Preventing the Artificial Avoidance of Permanent Establishment Status
Action 8-10	Aligning Transfer Pricing Outcomes with Value Creation
Action 11	Measuring and Monitoring BEPS
Action 12	Mandatory Disclosure Rules
Action 13	Guidance on Transfer Pricing Documentation and Country-by-Country Reporting
Action 14	Making Dispute Resolution Mechanisms more effective
Action 15	Developing a Multilateral Instrument to Modify Bilateral Tax Treaties

What is MLI

- **OECD's Base Erosion and Profit Shifting (BEPS) Project** – BEPS refers to tax planning strategies used by MNCs that exploit gaps and mismatches in tax rules to avoid payment of tax by artificially shifting profits to low or no-tax locations where there is little or no economic activity
- **BEPS Action Plans** - a project developed by OECD/G20 Members, recommends measures under domestic law & tax treaties to address tax avoidance to realign taxation with economic substance & value creation
- **Multilateral Instrument (MLI)** - signed by developed and developing economies around the world to implement tax treaty related measures to prevent BEPS
- **MLI** - Includes measures against hybrid mismatch arrangements (Action 2) and treaty abuse (Action 6), strengthened definition of permanent establishment (Action 7) and measures to make mutual agreement procedure (MAP) more effective (Action 14), including provisions on MAP arbitration

MLI - the Journey



Out of 94 Signatories to the MLI as on date, 43 Countries have ratified MLI (including India)

MLI - Certain Basic Concepts

What is MLI

A single instrument that modifies multiple tax treaties to implement certain recommendations under the OECD/G20 BEPS Project.

Applicability

Not automatically applicable – will apply only if a Country is a signatory to the MLI and both the contracting jurisdictions have notified their Tax Treaty as a CTA

What is CTA?

A Tax Treaty on income that is in force between two or more Parties / jurisdictions with respect to which each such Party has notified to the Depository as a listed agreement under the MLI

Impact on existing treaty

Will not replace the existing treaty, but operate alongside it– supplement, compliment, modify its application

Will it freeze the Treaty

No – subsequent modification to the CTA possible

Changes to MLI Position

Subsequent changes / modifications to MLI positions possible– withdrawal from MLI also possible

Basic rule of interpretation

MLI to be interpreted in accordance with ordinary principles of treaty interpretation

MLI - Framework

Minimum Standards

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

Reservations

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

Optional provisions

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

Compatibility clauses

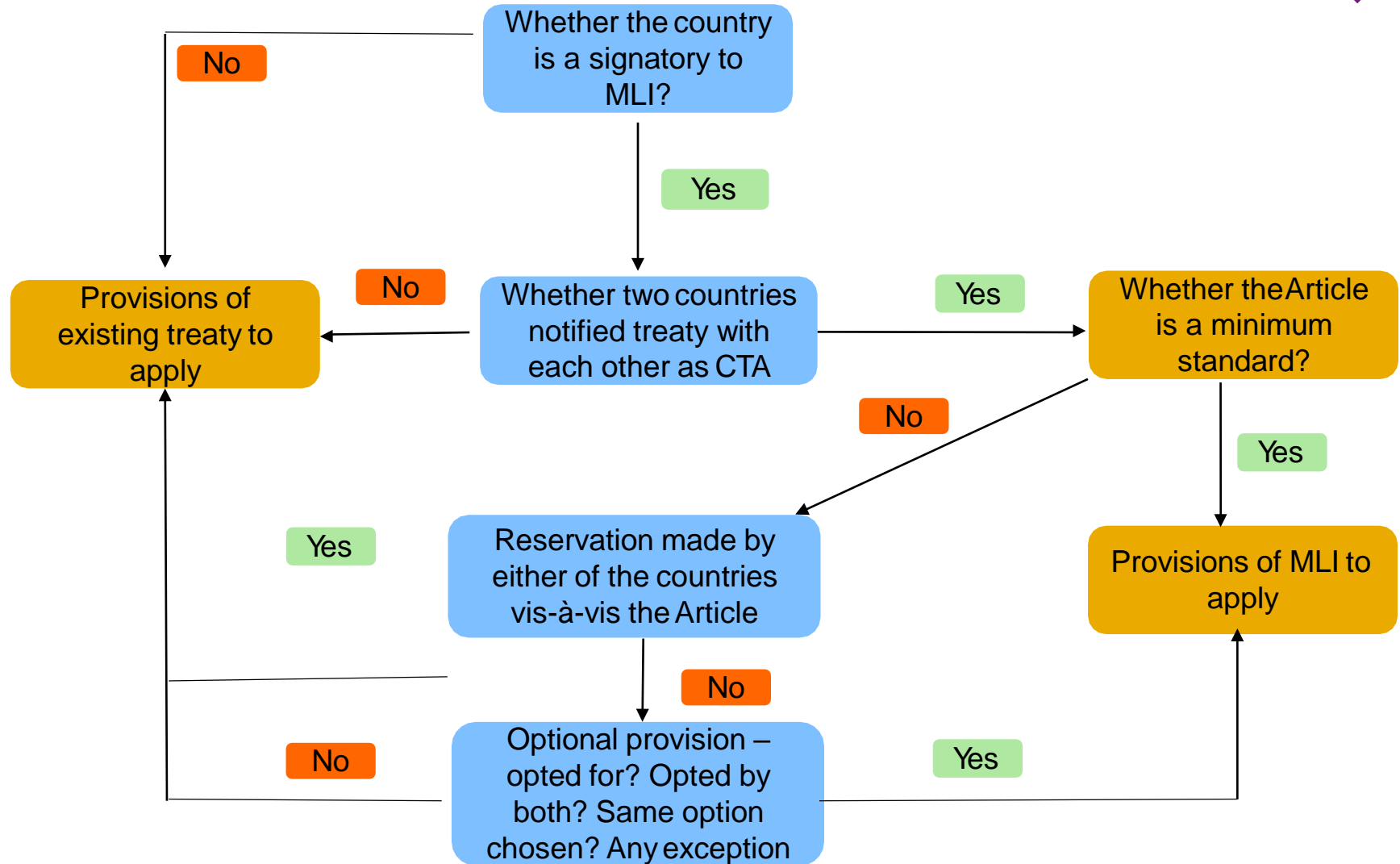
- Defines the relationship / addresses conflict between the MLI and the provisions of a CTA
- MLI provision applies –
 - ‘in place of’
 - ‘applies to’ or ‘modifies’
 - ‘in the absence of’
 - ‘in place of or in the absence of’ – *If notified by both CTA, then gets replaced, else supercedes*

To be notified by both CTA

Notification clauses

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

MLI - Applicability Flowchart



Articles under MLI, Model Convention and BEPS Action Plan



Minimum Standard



India has Opted Out

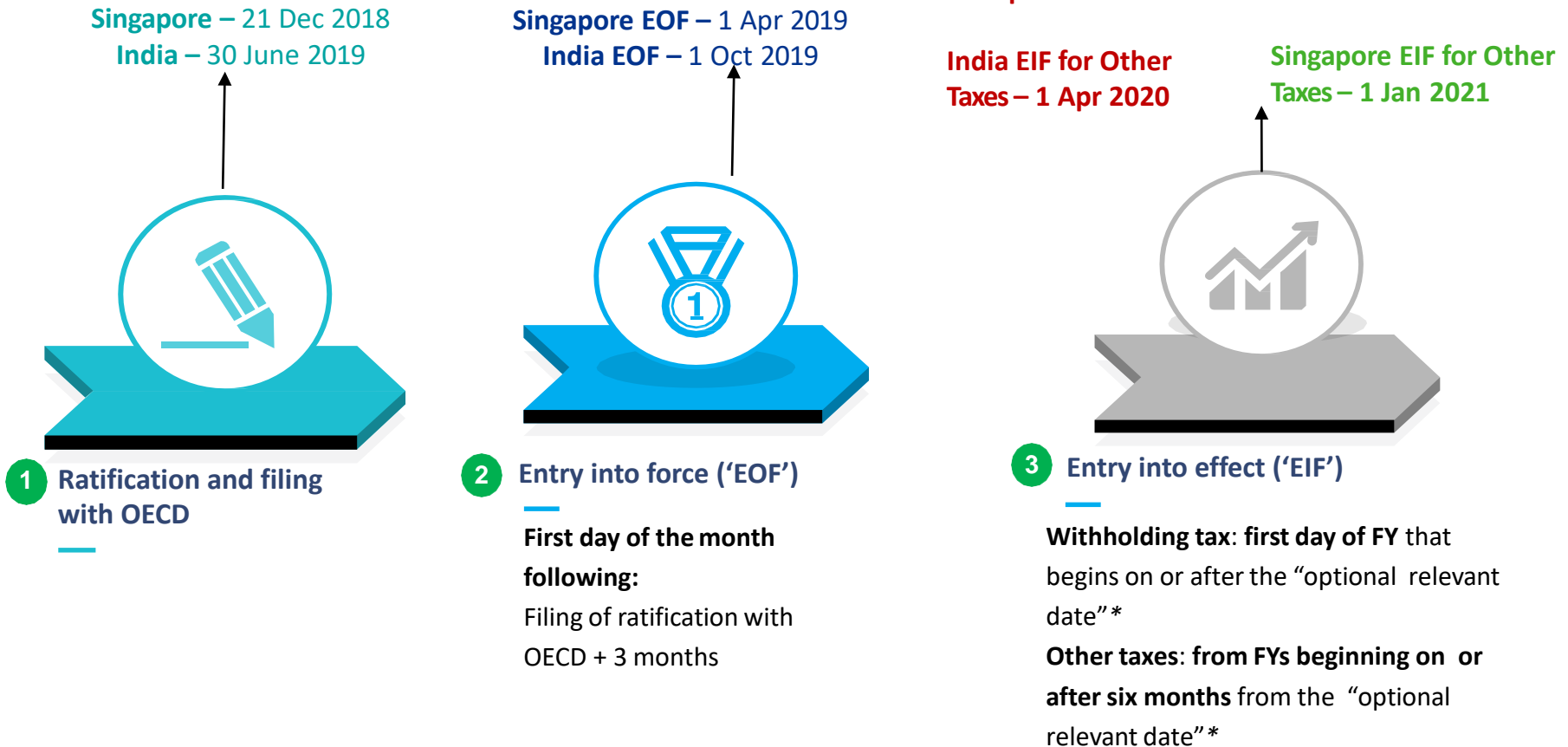
Parts	MLI Articles	OECD / UN MC Articles	BEPS AP
Part I: Scope and Interpretation of Terms		-	
• Scope of MLI	Article 1		
• Interpretation of MLI	Article 2		
Part II: Hybrid Mismatches:			
• Transparent Entities	Article 3	Article 1(2)	BEPS AP 2
• Dual Resident Entities	Article 4	Article 4(3)	BEPS AP 6
• Methods for elimination of double taxation	Article 5	Article 23A & 23B	BEPS AP 2
Part III: Treaty Abuse			
• Purpose of CTA (Preamble)	Article 6	Preamble -Para above Article 1	BEPS AP 6
• Prevention of Treaty Abuse	Article 7	Article 29	
• Dividend transfer transaction	Article 8	Article 10(2)(a)	
• CG from alienation of share/interest deriving value from IP	Article 9	Article 13(4)	BEPS AP 6
• Anti-abuse rule for PE in third state	Article 10	-	
• Taxing rights for own residents	Article 11	Article 1(3)	

Articles under MLI, Model Convention and BEPS Action

Parts	MLI Articles	OECD / UN MC Articles	BEPS AP
Part IV: Avoidance of PE Status through:			
• Commissionaire Arrangements	Article 12	Article 5	BEPS AP 7
• Specific Activity Exemptions	Article 13		
• Splitting up of Contracts	Article 14		
• Definition of closely related Person	Article 15		
Part V: Improving Dispute Resolution			
Mutual Agreement Procedures	Article 16	Article 25	BEPS AP 14
Corresponding Adjustments	Article 17	Article 9(2)	
Part VI: Arbitration	Article 18-26	Article 25(5)	
Part VII: Final Provisions			
• Signature, Ratification, Acceptance or Approval	Article 27		
• Reservations	Article 28		
• Notifications	Article 29		
• Subsequent Modifications of Covered Tax Agreements	Article 30		
• Entry into Force	Article 34		
• Entry into Effect	Article 35		
• Entry into Effect of Part VI (Arbitration)	Article 36		
• Withdrawal	Article 37		
• Other Provisions	Article 31-33,38 & 39		

Applicability of MLI - how timelines work?

Example: India-Singapore Tax Treaty



*“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

Applicability of MLI - Practical aspects for timelines

Article of the MLI	India's Position	Japan	UAE	Australia	Belgium	Canada	Singapore	Ireland	UK	France
Date of entry into effect- Withholding cases	01st Apr, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020	01st Jan, 2020
Date of entry into effect- Non-Withholding cases	01st Apr, 2020	01st Apr, 2020	01st Apr, 2020	01st Apr, 2020	01st Apr, 2020	01st June, 2020	01st Apr, 2020	01st Apr, 2020	01st Apr, 2020	01st Apr, 2020

Applicability of MLI - Practical aspects for timelines

- **Applicability of MLI - Transitional cases**

Date of Invoice	Date of Booking	Date of payment	MLI Applicability	Possibility of Litigation	Remarks
26 March 2020	31 March 2020	31 March 2020	Not Applicable	No	Withholding liability triggers - At the time of booking (credit) or payment, whichever is earlier (Section 195)
26 March 2020	31 March 2020	1 April 2020	Not Applicable	No	
26 March 2020	1 April 2020	31 March 2020	Not Applicable	Yes	
26 March 2020	1 April 2020	10 April 2020	Applicable	Yes	

- Link for accessing Matching database (For reference purpose only):

<https://www.oecd.org/tax/treaties/mli-matching-database.htm>

- **Applicability of additional notifications or replacement/ withdrawal of Reservations (For both withholding and Non-withholding taxes)**

- On or after 1 January of the year next following the expiration of a period of six calendar months beginning on the date of the communication by the Depository
- i.e.1st day of the following year - Date of Communication + 6 Months

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 USA, Mauritius, Germany

Synthesised Text available for around 19 Indian Tax Treaties – Singapore, UK, Japan, UAE, Australia, Austria, Finland, Ireland, Poland, Lithuania, Slovak Republic, etc.

MLI Impact Areas

Key proposals of MLI

PREVENTING TREATY ABUSE

Preventing treaty shopping (Preamble, PPT and/or LOB)

Dividend stripping

Shares deriving value from immovable property

Third country PEs

AVOIDANCE OF PE STATUS

Expanding scope of Agency PE

Restricting Preparatory and Auxiliary exemptions

Anti-fragmentation rules

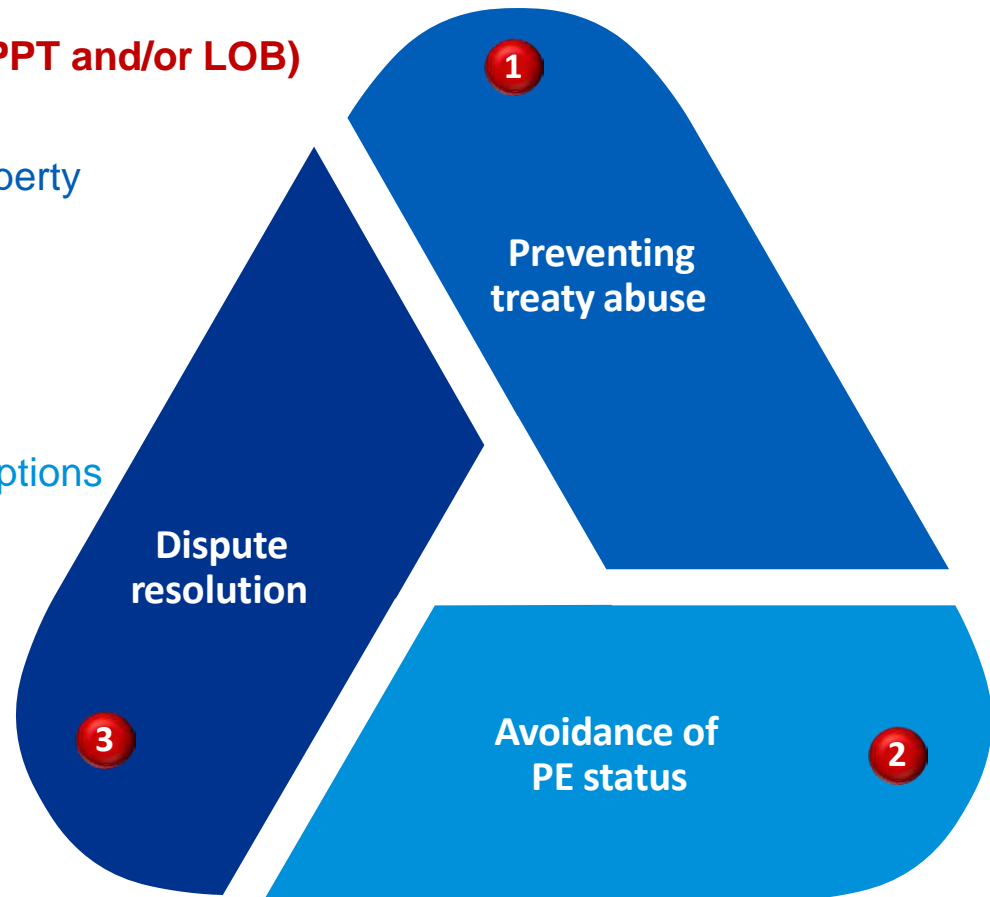
Avoiding artificial contract splitting in case of Construction / Installation PE

DISPUTE RESOLUTION

Access to MAP process

Corresponding adjustments

Arbitration - Optional

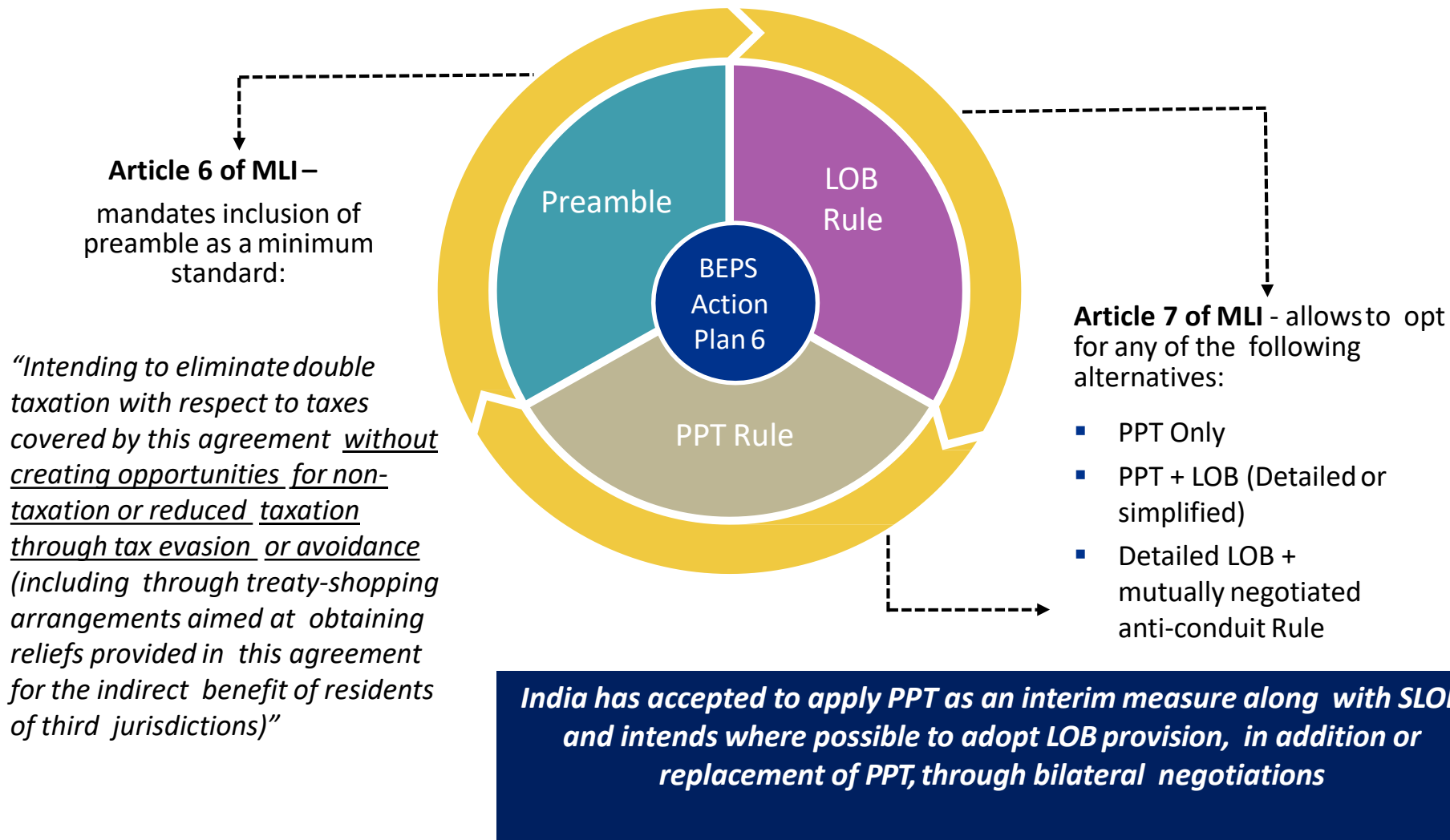


Some of the MLI proposals may have far reaching implications on tax treaties

Prevention of Treaty Abuse

Prevention of Treaty Abuse

Three-pronged approach to address treaty shopping



Article 6 - Purpose of CTA [Preamble]

Impact on Indian Tax Treaties - Few Examples

Country	Existing Preamble	Additional Preamble
Singapore, Netherlands, UK	The Government of, desiring to conclude an Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income..., have agreed as follows	Preamble language to get widened with new preamble which provides for ' <u>without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance</u> ' (including through treaty shopping arrangements.....)
Luxembourg	The Government of, desiring to conclude an Agreement for the avoidance of double taxation and <u>the prevention of fiscal evasion with respect to taxes on income</u> and on capital and with a view to promoting economic co-operation between the two countries, have agreed as follows	Object of economic cooperation is already part of existing treaty, it will continue to remain in the preamble with Luxembourg. The Preamble to get widened to <u>include avoidance of non-taxation / reduced taxation and targeting treaty shopping</u>

Article 7 – Prevention of Treaty Abuse- Para 7(1) – Scope of PPT (1/2)

Para 7(1): Notwithstanding any provisions of a CTA, a benefit under the CTA 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 benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the CTA***

- Benefit’ ***includes*** all limitations on taxation imposed on the State of source. Example - Lower rate of WHT, restricted definition of royalty / FTS, Non- applicability of beneficial Permanent Establishment provisions, Capital gain tax exemption, etc.
- The terms “arrangement or transaction” should be interpreted broadly and include any agreement, understanding, scheme, transaction or series of transactions, whether or not they are legally enforceable. It includes creation, assignment, acquisition or transfer of the income itself or of property or right in respect of which income accrues

Imperative to demonstrate substance and commercial rationale

Article 7 – Prevention of Treaty Abuse- Para 7(1) – Scope of PPT (2/2)

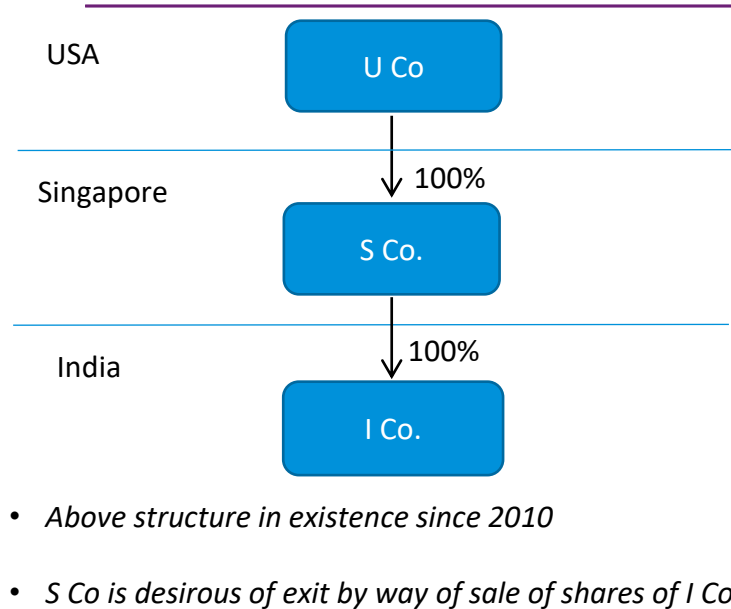
- Second limb of PPT Clause – reads as “**Unless it is established that granting benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the CTA**”
- **Article 31 of Vienna Convention** - A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
- **SC in the case of Azadi Bachao Andolan observed** : similar to deficit financing, treaty shopping, though at first blush might appear to be evil, but is tolerated in a developing economy, in the interest of long term development.

*“.....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.....”*

GAAR and PPT - Interplay

Particulars	GAAR	PPT
Applicability	<ul style="list-style-type: none"> Main purpose is tax benefit; and One of the tainted element tests is present 	<ul style="list-style-type: none"> One of the principal purposes is tax benefit Not in accordance with object and purpose of treaty
Consequences	Re-characterization/disregarding of transaction, re-allocation of income (includes denial of treaty benefit)	Denial of treaty benefit
Onus	Primary onus on tax authority	Primary onus on tax authority and rebuttal assumption for carveout
Administrative Safeguards	Approving Panel	<ul style="list-style-type: none"> To be determined by respective states. OECD and UN Model Commentaries suggest this, but none in India
Grandfathering	Yes	-
De-minimis Threshold	Yes	No

Case Study .1: Inbound Structure - Grandfathering under PPT?



Flow of Events:

- In Nov 2016, over 100 jurisdictions concluded negotiations on MLI (India and Singapore participated)
- In Dec 2016, India and Singapore signed Protocol to India-Singapore Tax Treaty grandfathering investments made before 1 April 2017;
- In June 2017, 67 jurisdictions (including India and Singapore) signed MLI which was principally agreed in Nov 2016;
- India ratified MLI in June 2019

Interpretation of PPT? -

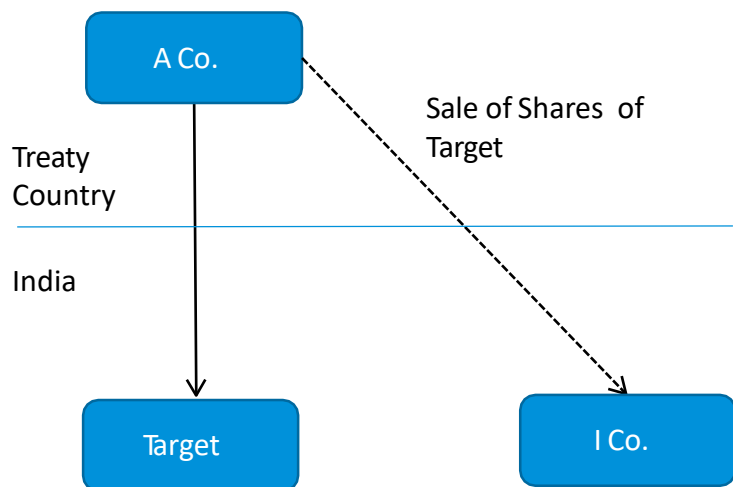
- Treaty Benefits not permitted if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit,
 - **Unless it is established that granting benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the CTA”**

•Which Object and Purpose to be analysed? – Original treaty? Protocol? MLI? Whether investments under India-Singapore Tax Treaty Grandfathered?

•Exits could result into litigation and taxes – imperative to evaluate options for mitigating potential exposure

Indian tax authorities indicate that PPT can be invoked to deny benefits of the India-Singapore Treaty

Case Study 2: Acquisition of shares - Seller in a Treaty Jurisdiction



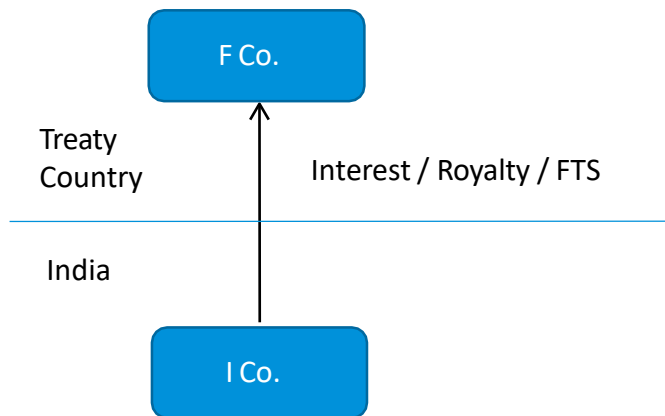
Pre MLI:

- **Circular No. 789, dated 13-4-2000** - Tax residency certificate (TRC) to constitute sufficient evidence for accepting the status of residence, as well as beneficial ownership for applying DTAA provisions
- **SC in Azadi Bachao Andolan** [2003] 132 Taxman 373 upheld the validity of aforesaid Circular No 789
- **TRC** in the prescribed format as per section 90(4) / Form 10F as per section 90(5)

Post MLI:

- Mandatory inclusion of **preamble** as a minimum standard – which states that the object of the treaty is to not create opportunities for treaty shopping
- Treaty Benefits not permitted 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 benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the CTA**”

Case Study 3: Passive Income from India to Foreign Jurisdiction - (Interest / Royalty / FTS)



- *Restrictive definition of Royalty under Treaty- Eg: Computer Software not covered in Treaty;*
- *Restrictive definition of FTS under Treaty- Eg: Make Available benefit, etc.*
- *Interest rate under Treaty (7.5% - 15%)*

Pre MLI:

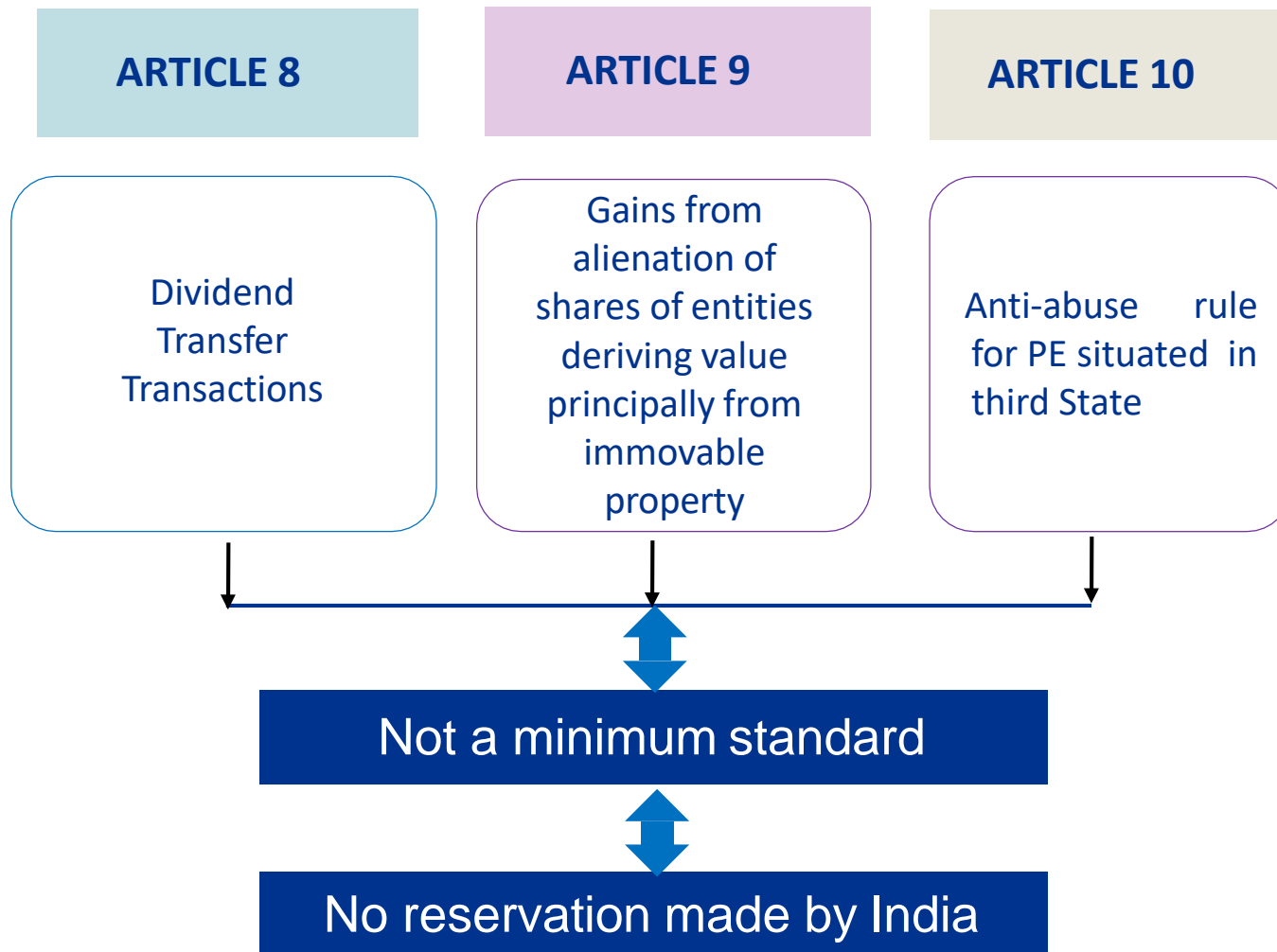
For claiming treaty benefits for lower rate of taxation of Interest / Royalty / FTS—,

- F Co to be beneficial owner of Interest / Royalty / FTS;
- F Co to have TRC / Form 10F;

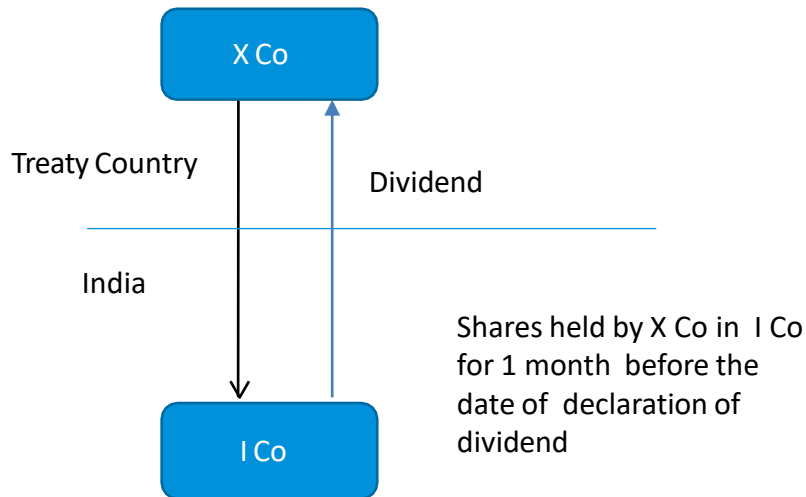
Post MLI:

- In addition to the requirements under the Pre MLI scenario,
 - **Preamble** to be considered;
 - **PPT Test** – availing tax benefit should not be one of the principal purposes of the arrangement / transaction.

Other Treaty Abuse - Dividend, Capital Gains, PE in Third State



Case Study 4: Payment of Dividend by Indian Co. to Foreign Co.



Pre MLI:

For claiming treaty benefits of lower rate for withholding on Dividend based on shareholding threshold:

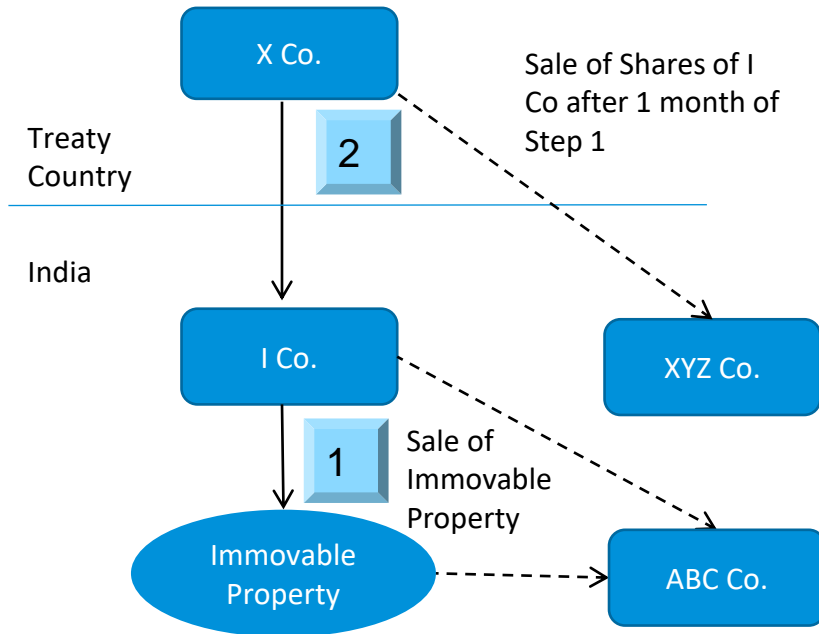
- X Co required to meet the threshold as shareholder only on the date of payment of dividend

Post MLI:

For claiming the above referred treaty benefits of lower rate for withholding on Dividend Income –

- X Co required to be shareholder of I Co **throughout a 365 day period that includes the day of the payment of the dividends;**

Case Study 5: Capital Gains from alienation of shares deriving value from Immovable Property



Pre MLI:

For claiming treaty benefits for capital gain taxation on sale of shares of I Co at step 2:

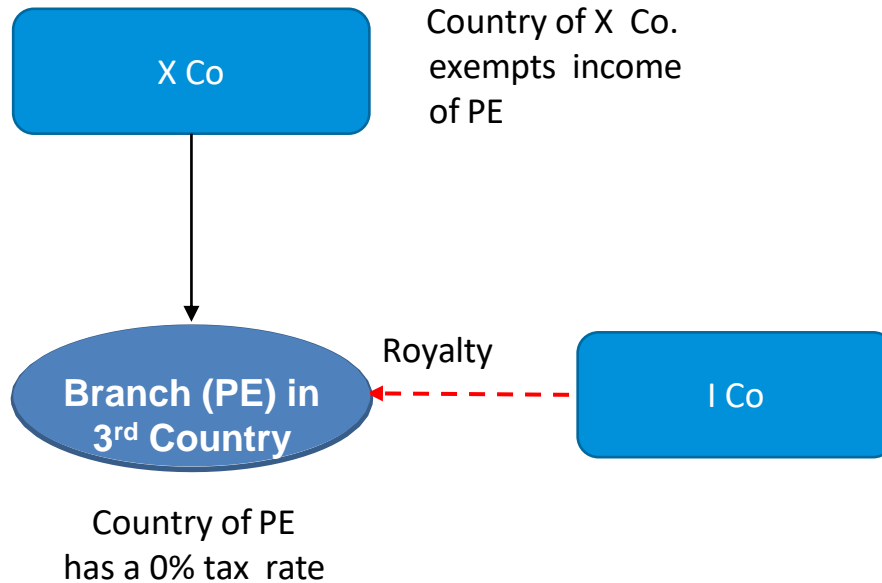
- the shares should not derive value from Immovable Property on the date of sale of shares

Post MLI:

For claiming treaty benefits for capital gain taxation on sale of shares of I Co at step 2:

- Such shares should not have derived value from Immovable Property situated in Source Country throughout a **365 day period preceding the alienation**;

Case Study 6: Payment from India to Foreign Co's Branch in Third State



Pre MLI:

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

Post MLI:

Following questions need to be verified:

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

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

Simplified LOB

- Tax Treaty benefits available only to '**qualified person**' which covers:
 - Individual
 - Contracting jurisdiction / political subdivision/ local authority
 - Listed entity
 - NGO / regulated retirement benefit entity
 - Entity in which atleast 50% shares held by above persons who are residents of the State, on atleast half of the days in 12 month period
- Tax Treaty benefits to be available to **non-qualified persons** engaged in '**active conduct of business**' if income derived from other State emanates from / is incidental to that business
- Activities not falling under 'active conduct of business'
 - Operating as Holding Company
 - Supervision / administration of group companies
 - Group financing
 - Making / managing investments (except banks / insurance companies / registered security dealer)
- Possible to apply Simplified LOB symmetrically or asymmetrically

Simplified LOB

Countries that have chosen to apply Simplified LOB

- Argentina
- Armenia
- **Bulgaria (India's CTA)**
- Chile
- **Colombia (India's CTA)**
- **Indonesia (India's CTA)**
- **India**
- **Mexico (India's CTA)**
- **Russia (India's CTA)**
- Senegal
- **The Slovak Republic (India's CTA)** and
- Uruguay

Countries where Simplified LOB may become applicable

- Bulgaria
- Colombia
- Indonesia
- Mexico
- Russia and
- The Slovak Republic

Countries that already have Simplified LOB in Tax Treaty with India

- Albania
- Armenia
- Iceland
- Mexico
- Sri Lanka
- Tajikistan
- Tanzania
- Uruguay and
- USA

Artificial Avoidance of PE Status

Artificial avoidance of PE

KEY IMPACT AREAS

1

ARTICLE 12 (Agency PE)

Marketing support arrangements by F Co. in India

Agency arrangements in India

2

ARTICLE 13 (Preparatory/auxiliary activities)

Restricted exemptions for preparatory and auxiliary activities

Storage operations, activities of liaison offices, etc.

3

ARTICLE 14 (Installation/Construction PE)

Artificial split-up of contracts

Splitting-up of contracts amongst multiple entities

Live instances of PE allegations in India aligned with ML

proposal

HOW INDIAN TAX AUTHORITIES ALLEGE PE?

1

AGENCY PE

(Demonstrating principal role of agent / employee)

- **Digital communication** – email exchanged b/w I Co. and F Co., tone of emails, etc.
- **Employee social media and job profile** – linked in profiles, job designations / descriptions, appraisal letters, etc.
- **Conduct of top management** – presence of common directors, demarcation of role for F Co. and I Co. operations

2

PREP AND AUX

(Re-characterising P&A activity)

- **Collecting market information** – as customer identification
- **Providing clarifications and information sharing** – as proposal development
- **Participation in meetings** – as contract negotiation
- **Communicating approval** - as finalization of contract

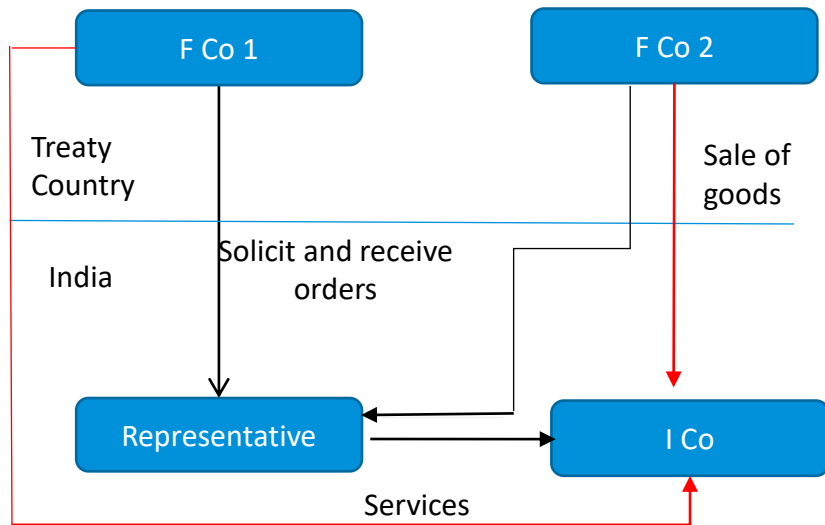
3

INSTALLATION / SERVICE PE (aggregating tenure of related contracts)

Contracts alleged to be 'related' or 'connected' based on:

- **Common purpose**
- **Common nature of work**
- **Common person**
- **Common location**

Case Study 7: Purchase of Goods from NR having Representative in India - Expansion of Agency PE



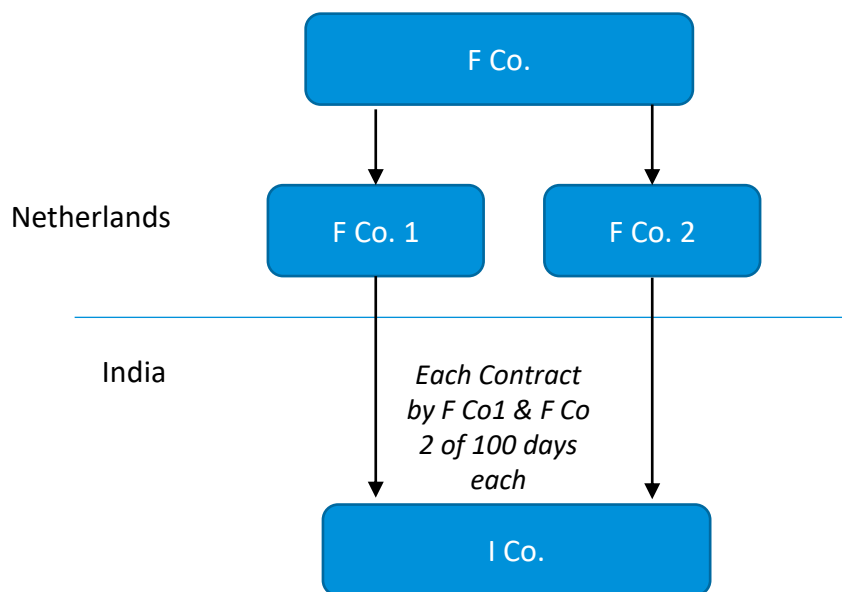
Pre MLI:

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

Post MLI:

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

Case Study 8: Payment to a NR for Construction / Installation Contracts



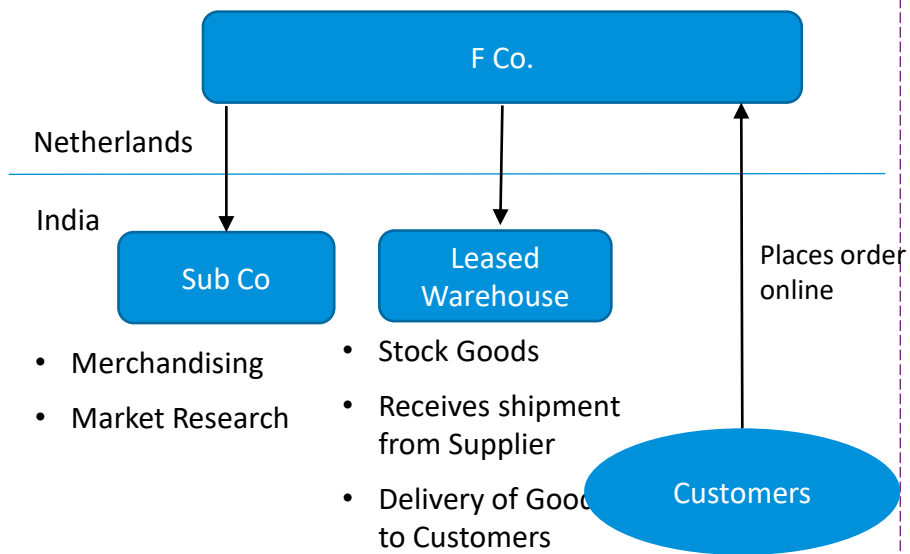
Pre MLI:

- Since Netherlands Treaty threshold is that each construction / installation project continues for a period of more than 6 months:
 - Independent contracts between F Co 1 & I Co, and F Co 2 & I Co, do not constitute construction / installation PE in India
- Practice of issuing no PE declaration by F Co's to I Co for payment without WHT

Post MLI:

- PE to be formed by **disregarding splitting-up** of **contracts** between F Co1 and F Co 2 since:
 - Installation activities are performed by **closely related enterprises i.e. F Co1 and F Co 2**; and
 - **Duration** of each such activity (i.e. of F Co1 and F Co 2) exceeds **30 days**
- I Co required to withheld tax @ 40% (plus surcharge and cess) on net income of F Co1 & F Co 2

Case Study 9: Restricted exemptions - Preparatory / Auxiliary activities



Pre MLI:

- Independent activities carried out through Sub Co or Leased Warehouse – looked upon and was possible to argue no Fixed place PE since independent activities are of P/A/ Character

Post MLI:

- Both India and Netherlands chose Option A – Overall activities / combination of activities to be checked for P/A character
- Fragmentation of activities no more permissible
- F Co likely to constitute Fixed Place PE in India and P/A exemption may not be available

Impact on Few Indian Tax Treaties

Few Example of Countries Notified by India	Positions of the Other Contracting Jurisdictions	Impact on India's CTA with the Country
Singapore	Opt out	No Impact
Netherlands	Opt out	No Impact
UK	Opt out	No Impact
Japan	No specific reservation Notification for Para 1 and Para 2	Article 12(1) and Article 12(2) would apply
Canada	Opt out	No Impact

Dispute Resolution

Article 16 and 17: Dispute Resolution

KEY CHANGES PROPOSED BY MLI AND INDIA'S POSITION TO KEY CLAUSES

- **Presentation of case to competent authority (CA) under MAP:**
 - India expresses reservation on presentation of case to either of the CAs
 - To be presented by the taxpayer only in the country of its residence
 - In case such CA does not find merit in the taxpayer's objections; bilateral notification / consultation process with CA of other state to be implemented
- **Time limit for presenting the case for MAP:**
 - Agrees with the model time limit of three years
 - Extends time limit under Tax Treaties with shorter time limit e.g. Canada
- **Adoption of Article 9(2) of OECD model convention:**
 - Agrees to adopt Article 9(2) through MLI

India has given reservation on Arbitration

Impact on Tax Deduction u/s 195

Rate of TDS

- Section 195 of the Act- Rates in Force
- Sec 2(37A)(iii)- For the purpose of TDS u/s 195, rates in force mean the rate specified in **Part II of First Schedule to the Finance Act** of the relevant year **or the rates specified under DTAA**, as may be **beneficial** u/s 90(2) of the Act.

Consequences of PE

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

Obligations on Indian Payer while making Foreign Remittances

- Indian Payer responsible for deduction of tax under sec 195 – if sum chargeable to tax in the hands of Payee
- Indian Payer also liable to be assessed as Representative Assessee under sec 161 r.w. sec 163, in respect of the payment made, to the extent of income of Non-Resident
- Indian Payer can approach Tax Department under sec 195(2) to determine the sum chargeable to tax on which WHT is required
- Failure of deduct WHT to result in disallowance of expenditure under sec 40(a)(i) and can also result in various penal consequences in the hands of Payer

Liability of Indian Payer is absolute

What has changed?

Before MLI

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



Additional Questions to be considered in the Post MLI Era

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

Multiple Checks before applying a tax treaty provision

Declaration from the Payee post MLI- What has changed?

Compliance with Article 7 of MLI- Prevention of Treaty abuse:

- Obtaining benefit of treaty is not a principle purpose.
- Beneficial owner.
- Non resident payee is not a shell or conduit company.
- All necessary facts for purpose of WHT in India as per provisions of the Act and treaty have been disclosed with the payer.



Microsoft Word
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Issuance of Form 15CB- Key Considerations going forward

- **Article 4 of MLI (Dual Resident entities)**

- In case of dual resident entities, in place of POEM tie-breaker rule, competent authorities would determine the residential status having regard to incorporation, POEM, etc
- Till such determination, DTAA benefits shall not apply

- **Article 7 of MLI (Principal Purpose test)**

- No benefit of DTAA if one of the main purpose of transaction is to obtain DTAA benefit

- **Article 12 of MLI (Commissionaire arrangements)**

- Agent shall constitute PE if he plays a principal role in conclusion of contract
- Agent is not independent if his activities are wholly or almost wholly on behalf of enterprise or CRE (Closely Related Ent.)

Issuance of Form 15CB- Key Considerations going forward

- **Article 13 of MLI (Specific Activity exemption)**
 - Preparatory and auxiliary benefit for PE is not available if all the activities are not P&A
 - Activities of CRE (Closely related to such enterprise) in State to be considered.
- **Article 14 of MLI (Splitting up of Contracts for Construction PE)**
 - Activities of CRE (Closely related to such enterprise) to be considered in determining number of days

Way Forward

Summary Chart- MLI Applicability for Key Indian Tax Treaties

MLI Provisions	India-Singapore	India-Netherlands	India-UK	India-Japan	India-Canada	
Article 4 – Dual Resident Entities	NA (Opt Out)	Applicable				
Article 5- Methods for Elimination of Double Taxation	NA (These Countries Not Notified by India)					
Article 6 – Purpose of Covered Tax Agreement (Preamble)	Minimum Standard - MLI Preamble to supecede existing preamble					
Article 7 - Prevention of Treaty Abuse – PPT / SLOB	Minimum Standard. However only PPT to apply. SLOB not opted for by these Countries					
Article 8 - Dividend transfer transaction	NA (Opt Out by Singapore, UK, Japan and Canada; & India is not notified by Netherlands)					
Article 9 - CG from alienation of share/interest deriving value from IP	NA (Opt Out)	Applicable	NA (Opt Out)	NA (not notified by each other)	NA (Opt Out)	
Article 10 - Anti-abuse rule for PE in third state				Applicable		
Article 11 - Taxing rights for own residents	NA (Opt Out)		Applicable	NA (Opt Out)		
Article 12 – Expansion of Agency PE	NA (Opt Out by all these Countries)			Applicable		
Article 13 - Preparatory/ Auxiliary activities – Restricted Exemptions	NA (Diff Option selected)	Option A of MLI Article 13 to Apply	Anti Fragmentation Rule to Apply	Option A of MLI Article 13 to Apply		
Article 14 - Artificial splitting-up of contracts	NA (Opt Out)	Applicable	NA (Opt Out)			
Article 16 & 17 – Dispute Resolution	Applicable					

Way Forward



- List the foreign payments where treaty rates are applied



- List Payees in countries where MLI is effective



- Analyse nature of payment & whether relevant Article under Treaty is modified



- Check Whether Payment is to be made to related party or third party



- Evaluate if the declaration from Payee (like no PE, satisfaction of PPT etc.) needs to be broadened



- If Payer aware of Split contracts- Whether no PE Declaration be accepted?



- Whether changes in Reps and Warranties are required?



- Whether revised Indemnities are required?

Risk Mitigation Strategies

6 CONTRACTUAL INDEMNITIES (For I Co.)

Contractual safeguards and documents (like No PE certificate) essential to ring-fence PE risks



1 ADVANCE RULINGS

Speedier mechanism to attain tax certainty on PE related issues



2 NIL / LOWER WITHHOLDING TAX ORDERS

Attain certainty on withholding tax due to highly subjective nature in PE situations

5 ALTERNATE BUSINESS MODELS

Explore alternate business models (like buy-sell model) to mitigate PE risks



RISK MITIGATION STRATEGIES

4

WRIT PETITIONS

Legal remedy to approach High Court in certain situations



3

MUTUAL AGREEMENT PROCEDURE ('MAP')

Seek assistance of Competent Authorities to resolve double taxation from PE related issues



Essential to adopt a combination of risk mitigation strategies

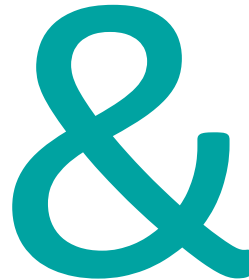
Glossary

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

Questions & Answers



Questions



Answers



Thank You

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