

The Chamber of Tax Consultants

BEPS MLI - India specific impact areas

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Naresh Ajwani
Chartered Accountant
Rashmin Sanghvi and Associates

BEPS and MLI

- Base Erosion and Profit Shifting (BEPS) measures are being implemented by countries with a view to curb tax avoidance.
- **Inclusive framework** under OECD/G20 permits interested countries to participate. So far 129 countries are a part of inclusive framework.

BEPS and MLI

- Inclusive framework will involve implementation of BEPS package, peer review, develop tool kits for countries with low capabilities, etc.
- **BEPS package** involves DTA amendment, changes in domestic tax rules, exchange of information and preventing harmful tax practices by countries. 15 Action Reports.

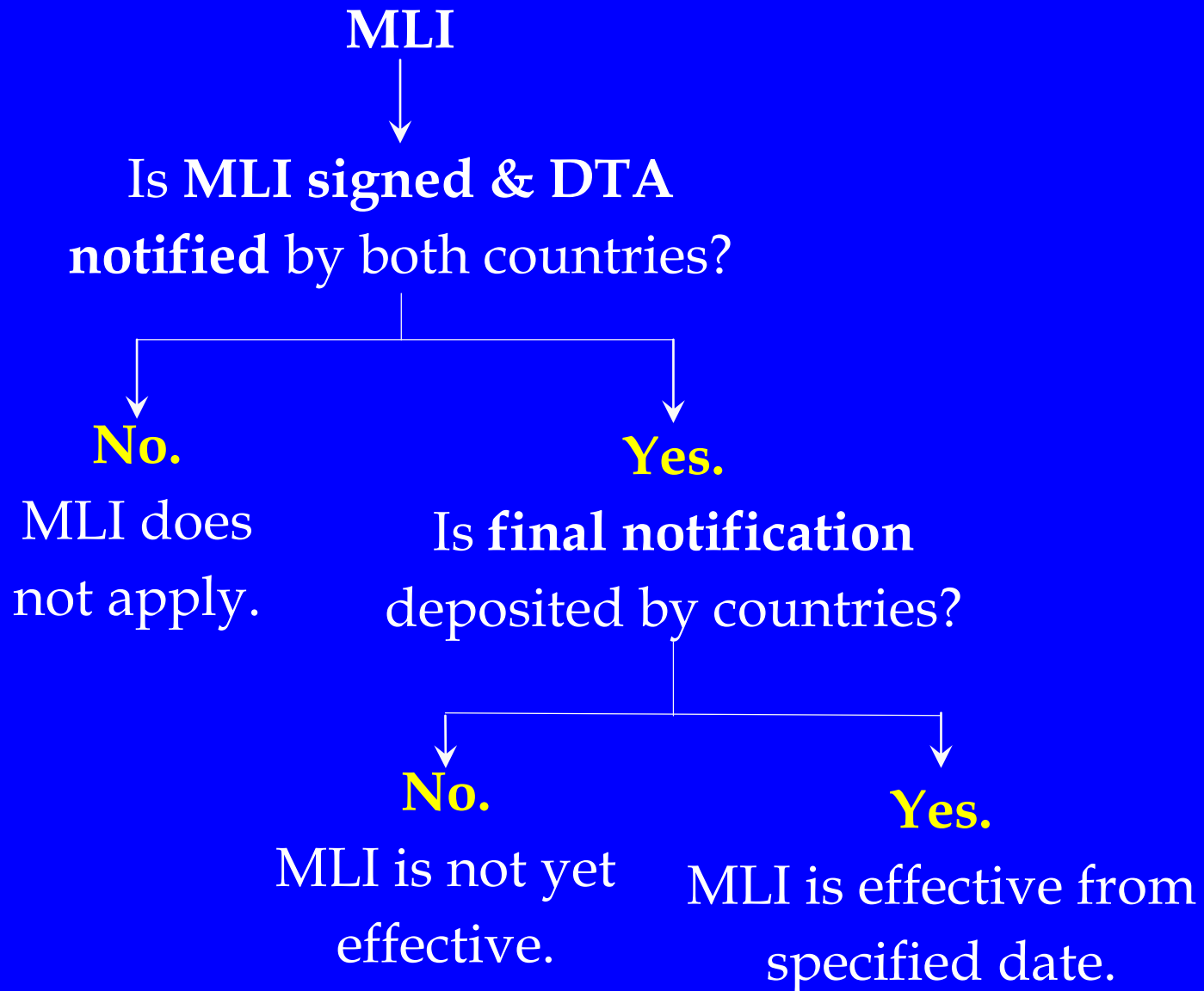
BEPS and MLI

- **Digital economy taxation** (Action Report 1) is the only one pending finalisation.
Consultative document issued in Feb, 2019.
India & others are pushing for Significant Economic Presence concept.

BEPS and MLI

- Multilateral Instrument (MLI) is for amendment of the DTAs. With one instrument, all the DTAs can be amended.
- It is **not renegotiation** of DTAs between Residence & Source countries. (E-commerce tax is an exception.) Only BEPS arrangements are targeted by MLI.

Operation of MLI



Operation of MLI

MLI Provisions



Has country made
any **reservation** for
any MLI provision?

Yes.

That provision
will not apply.

No.

That provision
will apply.

Minimum standards will apply. No reservation for this.

Operation of MLI

MLI Provisions



In case of **optional / alternative provisions**, have both countries selected same option / alternative?

Yes.

That option applies.

No.

Optional/ Alternative MLI provision does not apply.

Operation of MLI

MLI Provisions

Have countries **notified** same provision of DTA which are affected by MLI?

Yes.

That MLI provision applies.

If MLI provision –

- applies **in place** of existing DTA provision, or
- **applies** to or **modifies** existing DTA provision, or
- applies **in absence** of existing DTA provisions,

MLI provisions will not apply.

No.

If MLI provision –

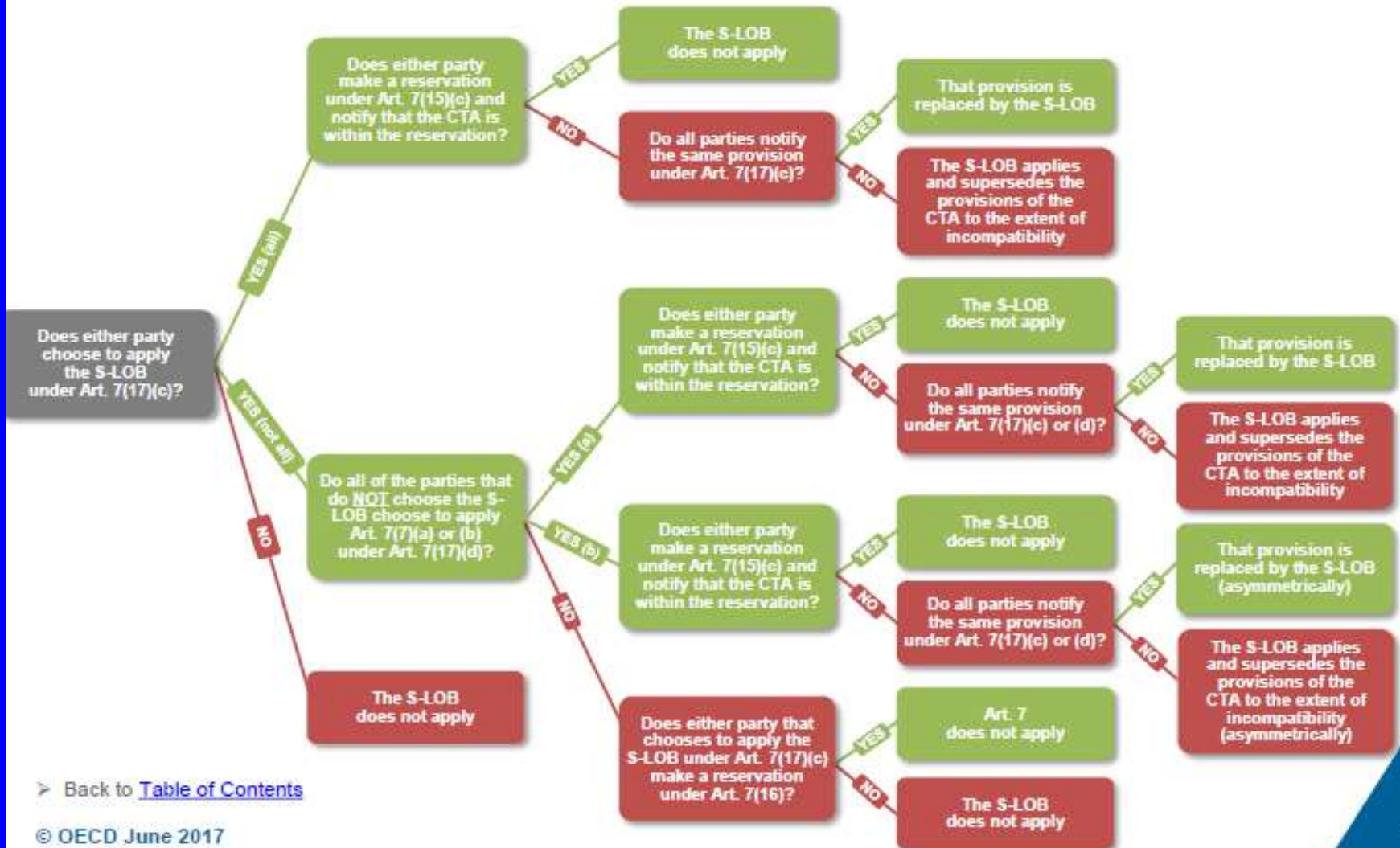
- applies **in place of or in absence of**, existing DTA provisions,

MLI provisions will supersede the existing DTA provision to the extent of incompatibility.



Article 7 – S-LOB

Prevention of Treaty Abuse



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Operation of MLI

- MLI does not replace the DTA but will operate side by side with the DTA.
- USA is one large country which has not signed the MLI. It will enter into bilateral negotiations with countries.

Minimum standards

- **Insertion of Preamble** – DTA is not to create 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).
- MLI preamble also has a similar language.

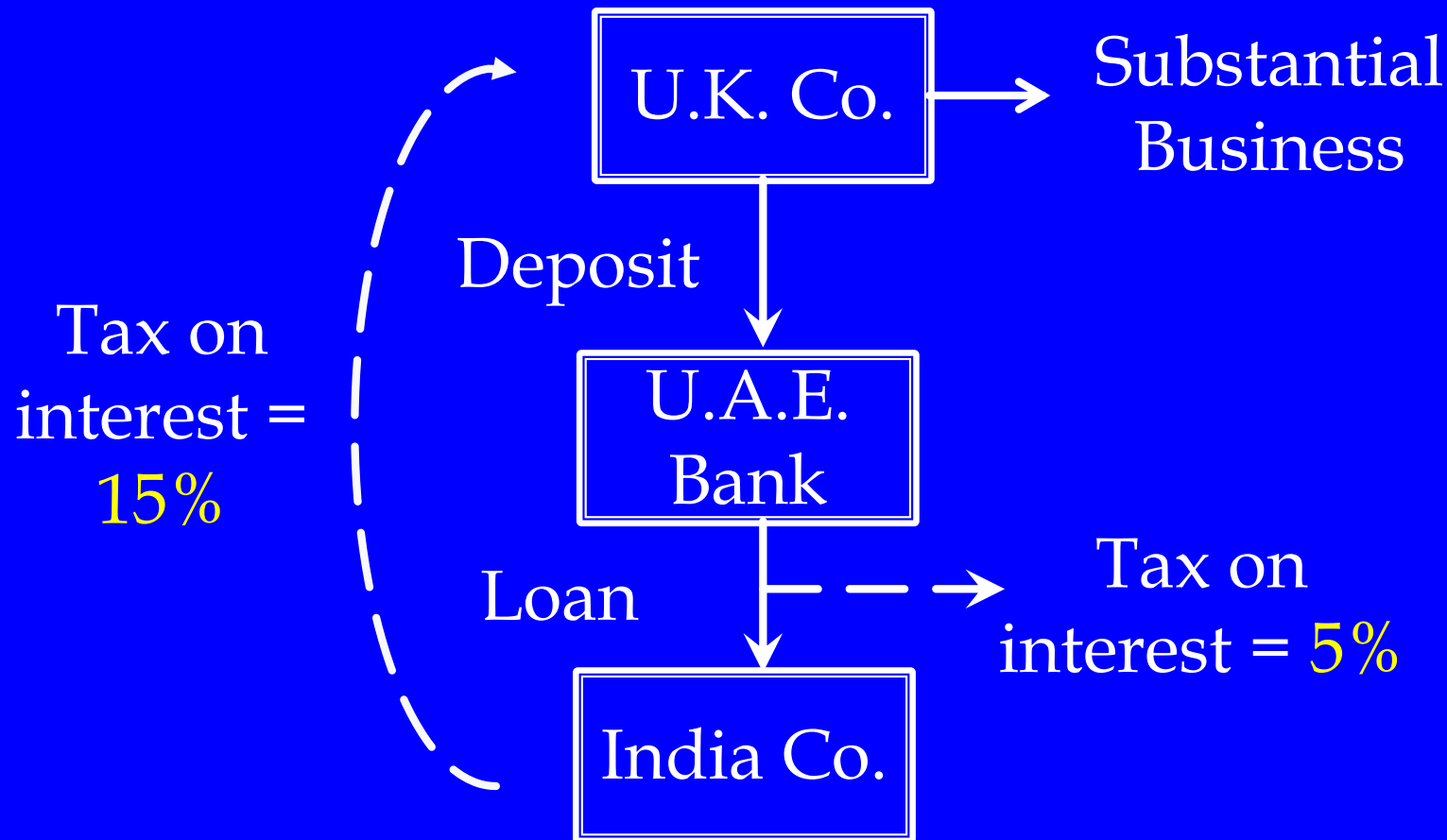
Minimum standards

- Country must adopt the treaty anti-abuse provisions.
- Any of the 3 alternatives can be adopted:
 - PPT, or
 - PPT + SLOB / DLOB, or
 - DLOB + anti-conduit rules.
- Signing MLI is NOT a minimum standard.

Minimum standards

- Country by Country Reporting implementation for Transfer Pricing.
- Review process of harmful tax practices.
- Disputes should be resolved within specified time frames.

Conduit Arrangement



India's tentative position

- India has notified all its 93 comprehensive DTAs in the provisional list.

However some countries like Germany, Mauritius have not notified Indian DTA.

They will enter into **bilateral negotiation** on some of the provisions.

India will notify the recent DTA with Hong Kong in the final list.

India's tentative position

- India has opted to apply strictest BEPS provisions. E.g. SLOB, Anti-Fragmentation rule.
- India has not opted for arbitration provision.

PPT – Article 7

- **Principle Purpose Test (PPT)** – DTA will not apply if **one of the principle purposes** of any arrangement or transaction was to obtain DTA relief.
- A country can reserve the right – not to apply the MLI PPT if it plans to adopt DLOB plus anti-conduit provisions / PPT; or if the DTA already contains a similar PPT.

No country has made any reservation.

PPT

- Countries such as Germany and Mauritius who have not notified the Indian DTA, will enter into bilateral negotiation for PPT.
- India already has such a clause in some DTAs – e.g. UAE, Singapore. MLI PPT as such is not required.

PPT

- Country may grant DTA relief in spite of PPT, if tax payer makes a request.
- This is an optional clause. India has not opted for this clause.
- Only recourse is judicial remedy if India applies PPT and does not grant DTA relief.

SLOB – Article 7

- SLOB lays down objective criteria to determine whether a person is eligible for DTA relief. It is akin to SAAR.

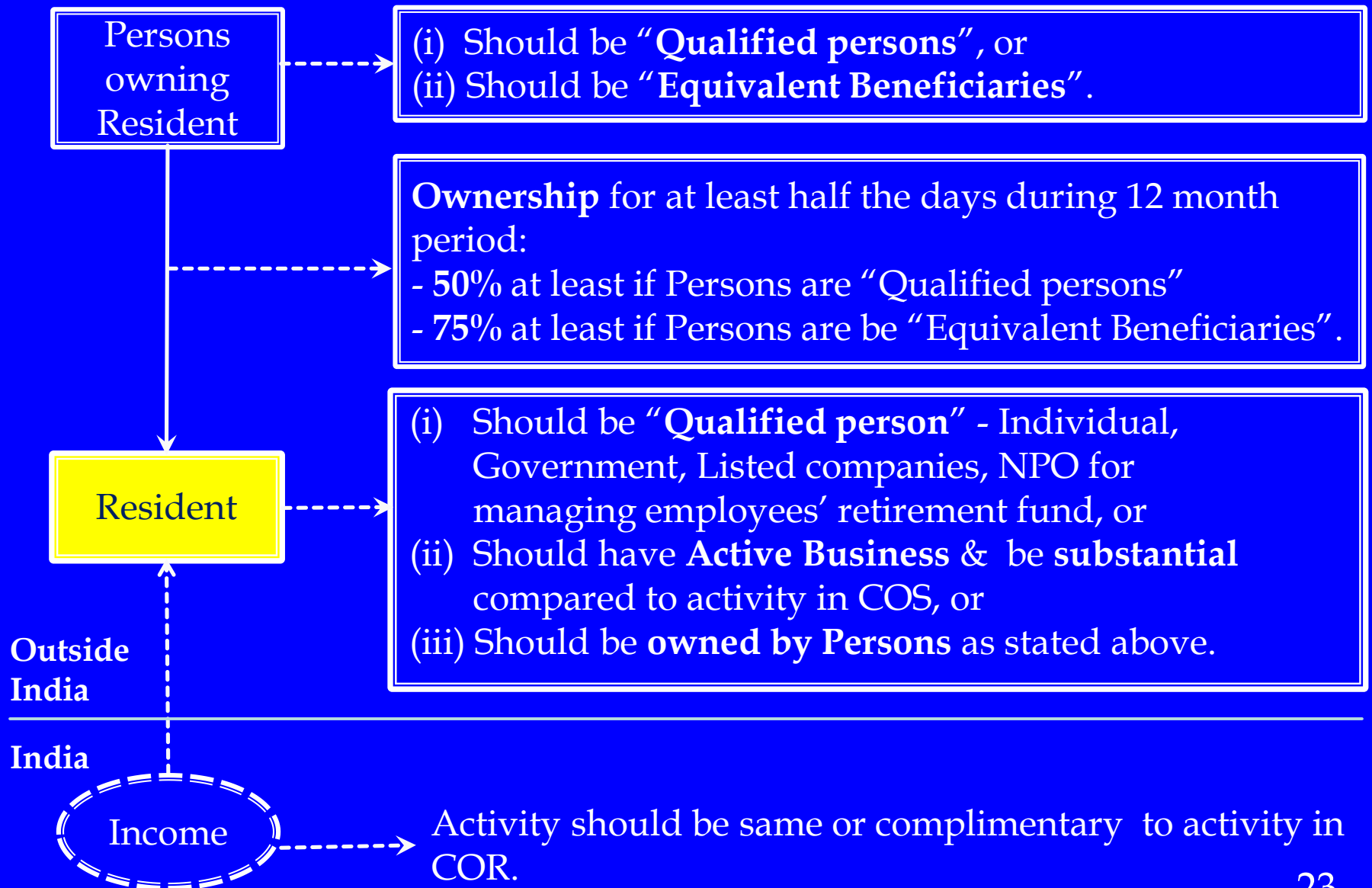
It is **anti-treaty shopping measure**.

- A person should be “**qualified person**” or should be owned by “**equivalent beneficiary**”. India’s view is that “**equivalent beneficiary**” should directly own shares of COR company.

SLOB

- Or person should be engaged in “**active business**” in COR; business should be substantial compared to business in COS; & activity in COS should be same or complimentary to activity in COR.
- Country may grant DTA relief even if a person does not satisfy SLOB clause if the person demonstrates that there was no purpose to obtain DTA relief.

SLOB - in nutshell



SLOB

- India has adopted SLOB.

SLOB will not apply where countries have not notified Indian DTA (e.g. Mauritius, Germany).

SLOB will not apply where country has not opted to apply SLOB (e.g. Singapore, UK). Few countries have opted for SLOB.

- It will apply in case of Indonesia.

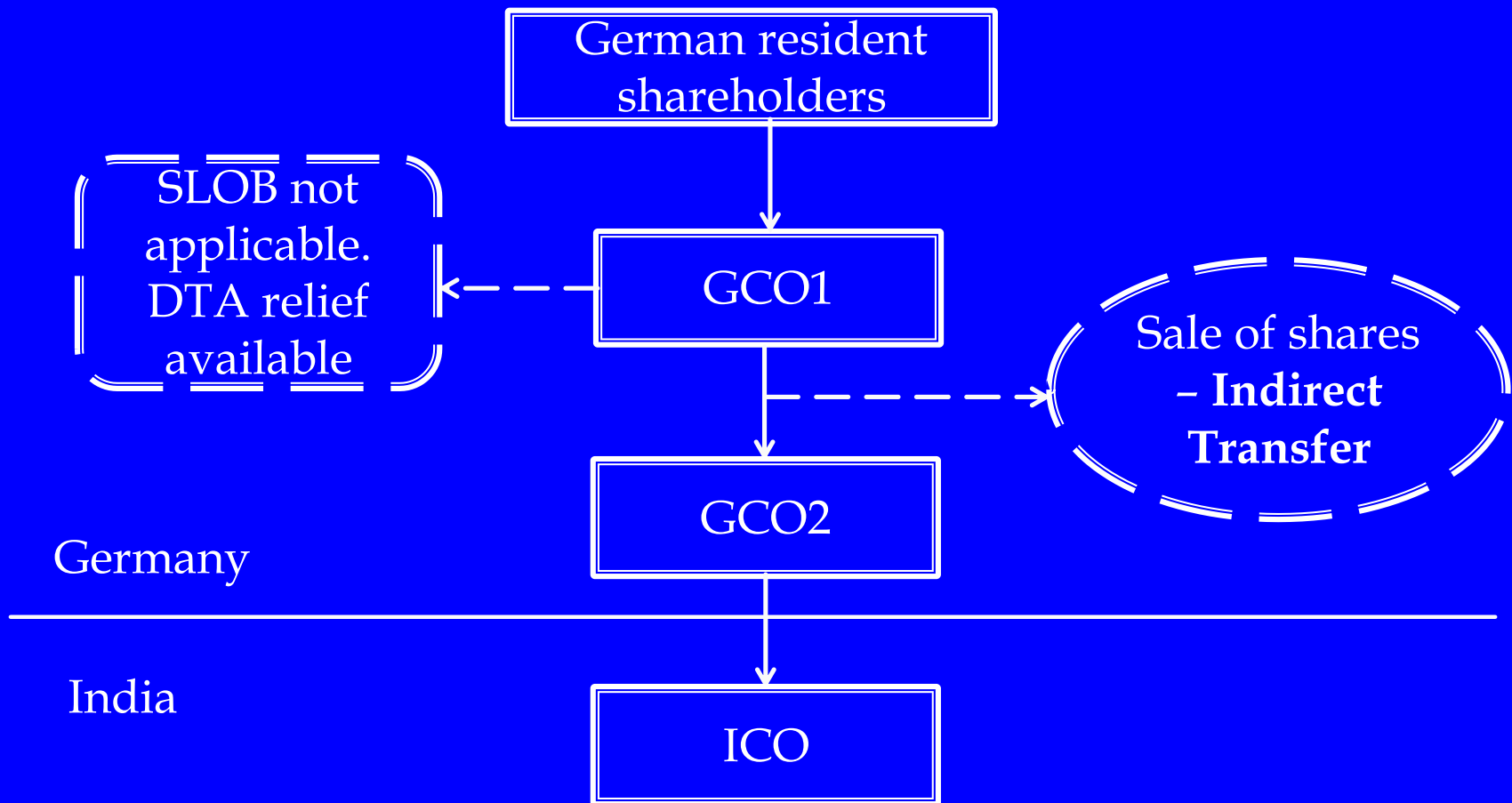
PPT and SLOB

- PPT and SLOB, both can apply.
- SLOB – Assessee has to apply; objective; but may not catch all conduit arrangements.
- PPT – AO has to allege treaty abuse; far more facts are required to establish that person does not satisfy PPT; subjective.
Even if there is no treaty shopping, PPT can apply if there is treaty abuse.

PPT and GAAR

- PPT and GAAR, both can apply.
- PPT is for preventing treaty abuse. GAAR is for preventing domestic law abuse (including treaty).
- No grandfathering in PPT. Limited grandfathering in GAAR.
- GAAR has Indian guidelines – e.g. Rs. 3 cr. of tax avoidance, panel, etc. PPT does not have specific guidelines.

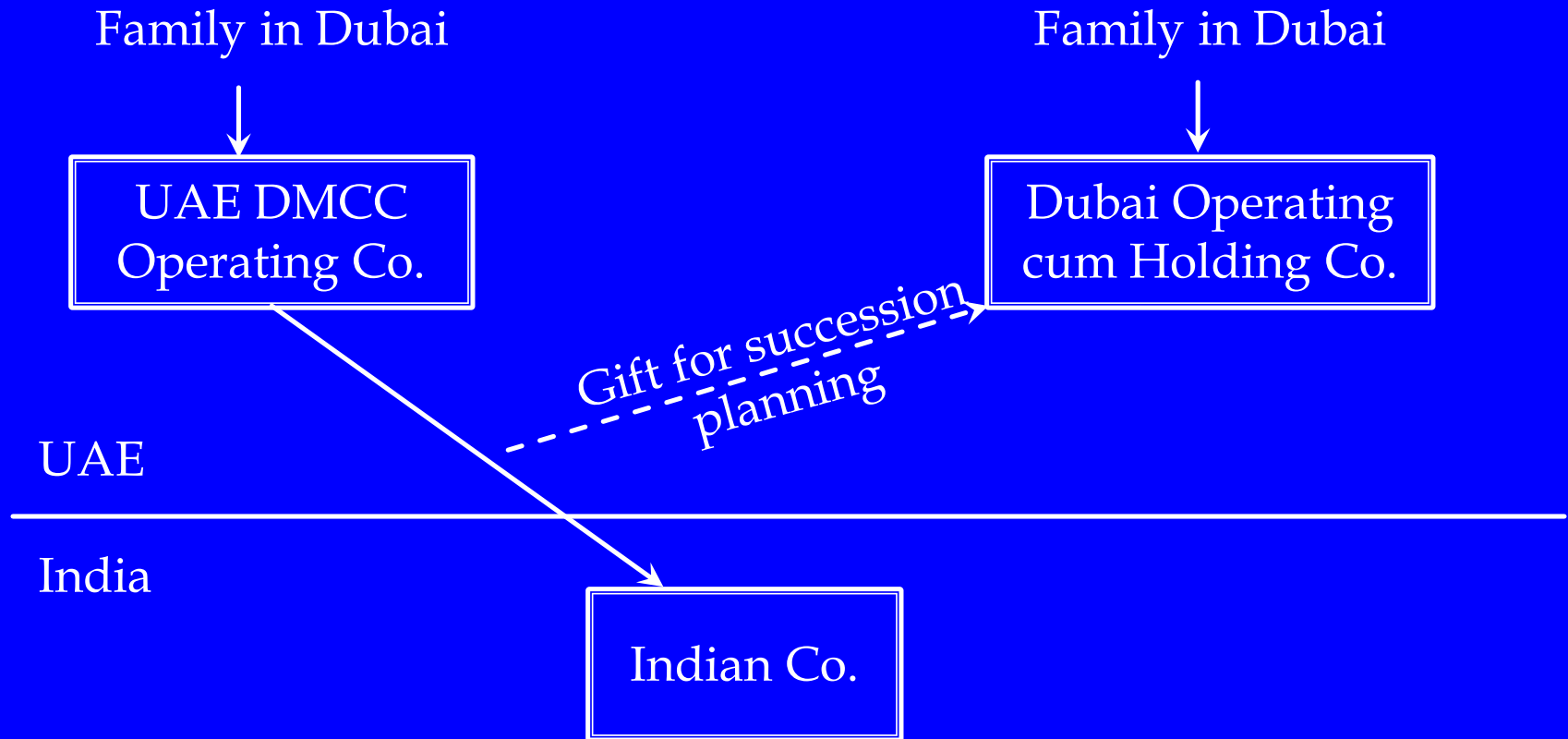
PPT and GAAR



To be considered –

- Article 13(4) and 13(5) of India-Germany DTA.
- PPT and GAAR.

PPT and GAAR



-Examine:

- S.56 (2)(x)
- UAE-India DTA - other income article
 - LOB clause
- GAAR/PPT

Dependent Agent PE – Article 12

- Commissionaire agency and similar strategies are plugged by MLI article.
- If the dependent agent concludes contract or plays a principal role leading to conclusion of contract that are routinely concluded by the principal, it will be a PE.
- India has not made any reservation. Hence MLI article will apply.

Dependent Agent PE

- If a country has made a reservation, MLI article will not apply. (E.g. U.K.)
- However India-U.K. DTA has a clause to consider dependent agent as PE if he has the authority to negotiate and conclude contracts. Protocol also states that it will be considered whether PE negotiated, concluded or fulfilled contract – it will be indirect attribution of profit.

Dependent Agent PE

- India's view on OECD commentary – participation in a negotiation or attending a negotiation can amount to a PE.
- **Independent agent** will not be a PE. However if the agent acts exclusively or almost exclusively for group companies, he will not be independent agent.
- Most DTAs have such a clause. MLI may not make much difference.

PE exemption – Article 13

- Preparatory and Auxiliary (P&A) activities are not considered as PE.
- MLI provides for two options:
 - Option A – Each listed activity should be P&A to be exempt. (E.g. In case of trading, purchase activity cannot be P&A).
 - Option B – A listed activity is exempt – whether it is P&A or not.
- India has opted for Option A – Each activity should be P&A.

PE exemption

- U.K. has not selected any option.
Hence MLI provision will not apply. DTA provision continues to apply, i.e., each listed activity is exempt from PE.
- Australia has selected option A. Hence MLI provision will apply.

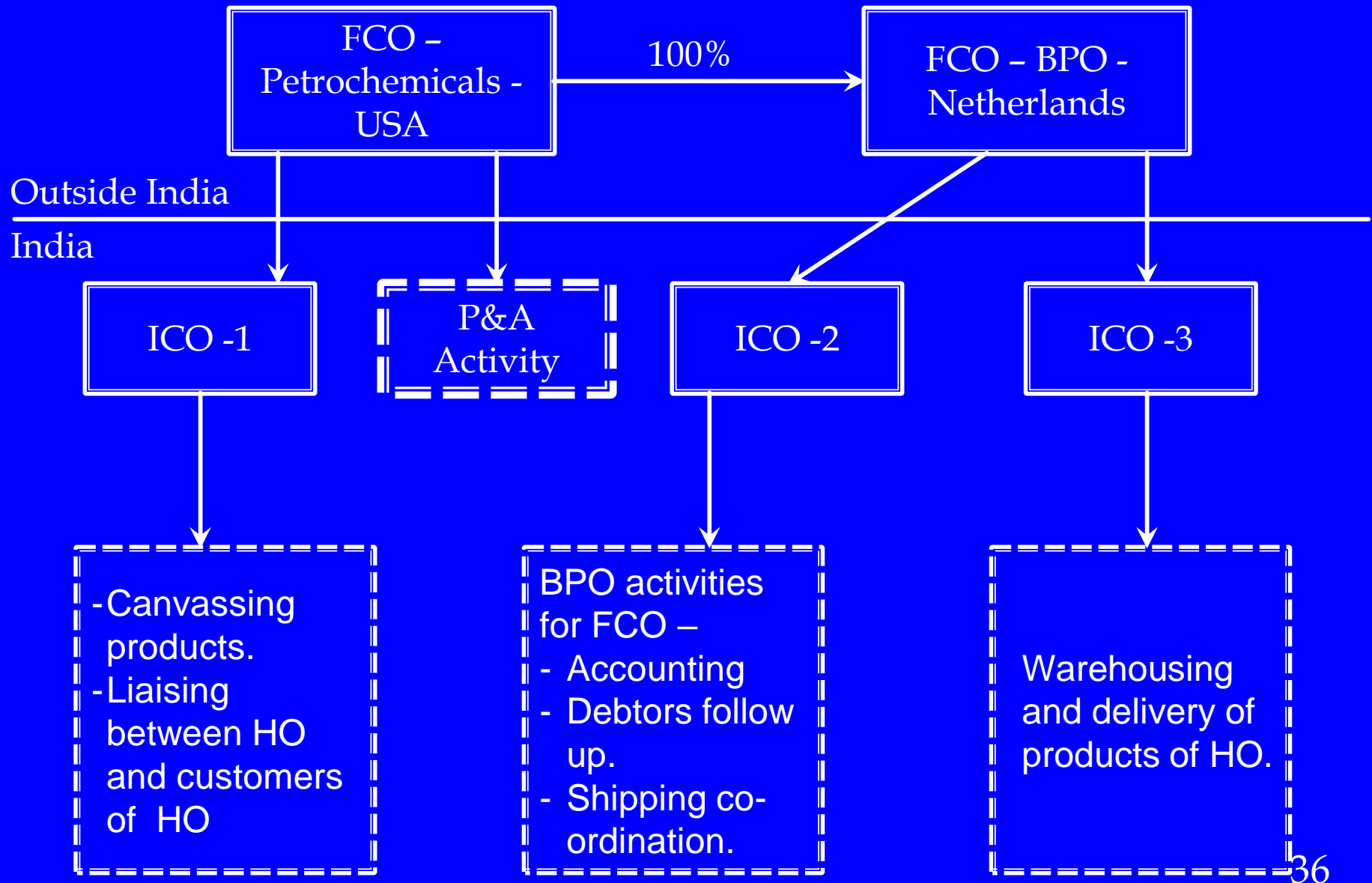
Anti-fragmentation rule – Article 13

- MLI prevents a person to fragment activities between many places or entities & claim that activity in each place/ entity in P&A.
- If **activity is split** between various places or group entities, it will be a PE if overall activities of the places or group are substantial (these are not P&A).
- Activities should be complementary functions that are a part of cohesive business operations.

Anti-fragmentation rule

- India has not made any reservation. Even without this rule, India's view is entity cannot fragment its activities (OECD 2017).
- The rule will not apply to countries which have made a reservation (e.g. Singapore); or made a reservation for entire article 13 of MLI (e.g. Canada).
- It will apply to other countries (e.g. U.K.)

Anti-fragmentation rule



Splitting of Contracts – Article 14

- Construction PE – applies when it crosses the days specified in the DTA.
- MLI provides that **if contracts are split** between group entities so that each entity operates for fewer days than that specified in the DTA, then **all the days of all entities will be added** to determine whether number of days has crossed the DTA threshold. This is the sole purpose of MLI article.

Splitting of Contracts

- This clause applies to Construction PE and not to other anti-splitting rule for other PEs if any.

Splitting of Contracts

- India has not made any reservation.
- This article will apply to those countries which have not made any reservation (e.g. Australia).
- It will not apply to countries which have made reservation (e.g. UK).

However, India-UK DTA is sufficient to take care of this situation.

Dual Resident entities – Article 4

- If a person (other than an individual) is resident in both countries, competent authorities will determine residence as per MAP.
- If countries cannot come to an understanding, **DTA relief will not apply to such a person.**

Dual Resident entities

- India has not made any reservations. MLI provision will apply depending on the other country. E.g. It will apply to UK DTA. It will not apply to Australia DTA.
- A firm, AOP can be resident of two countries easily. They may not get DTA relief. (e.g. UK LLP).
- A foreign company with POEM in India can be resident of two countries. It may not get DTA relief.

Gain on sale of entity with immovable property – Article 9

- In some DTAs it is provided that if shares of a company are sold and the value is mainly derived from **immovable property** in COS, then gain is taxable in COS.
- MLI provides that the value criteria can be met at any time during 365 days preceding the transfer.

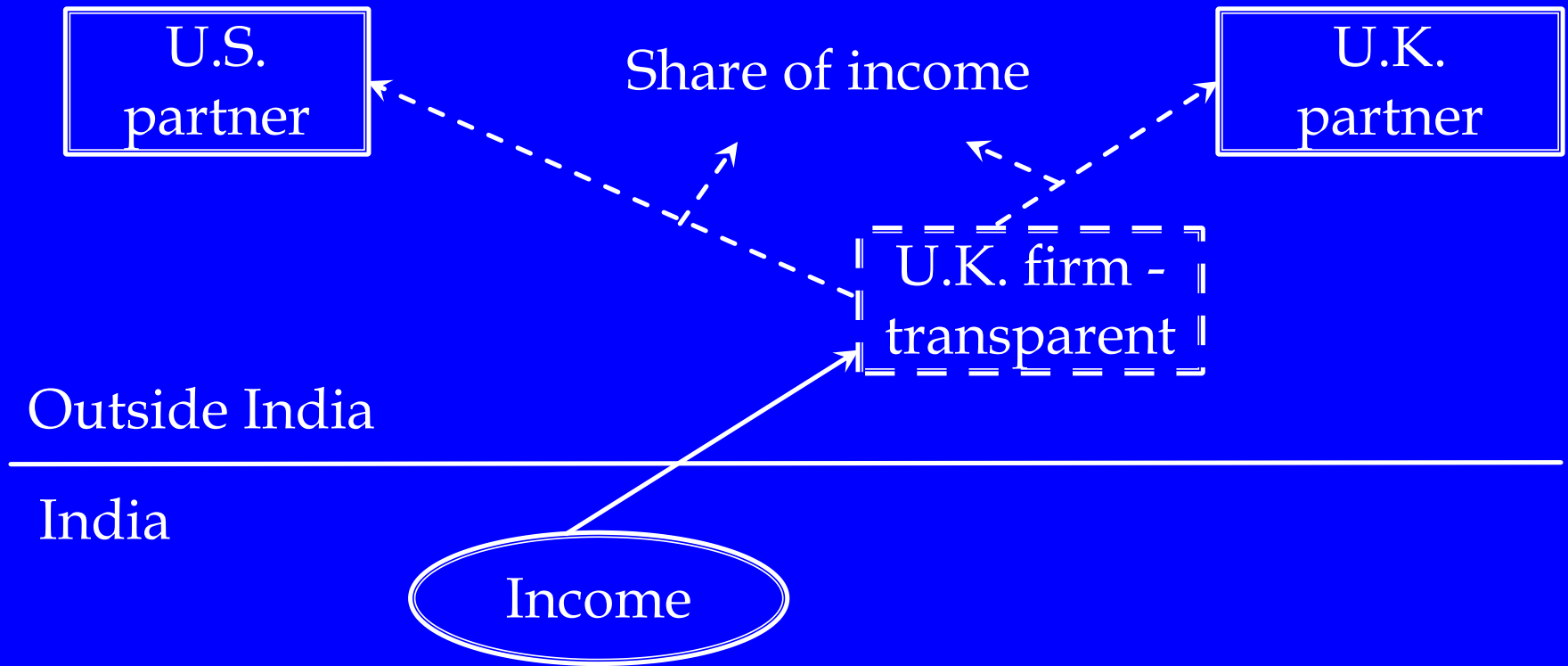
Gain on sale of entity with immovable property

- It further provides that the MLI provision will apply to other interests in an entity such as a firm or trust.
- India has opted for this provision.

Transparent entities – Article 3

- In case of transparent entities (where entity is not taxed but members are taxed), COS will apply the DTA relief only to that much income which is taxable in the hands of member of COR.
- **India has made a reservation.** This article will not apply. India's view is that DTA cannot apply to entities of 3rd country. OECD view is that this can apply to entities of 3rd country.

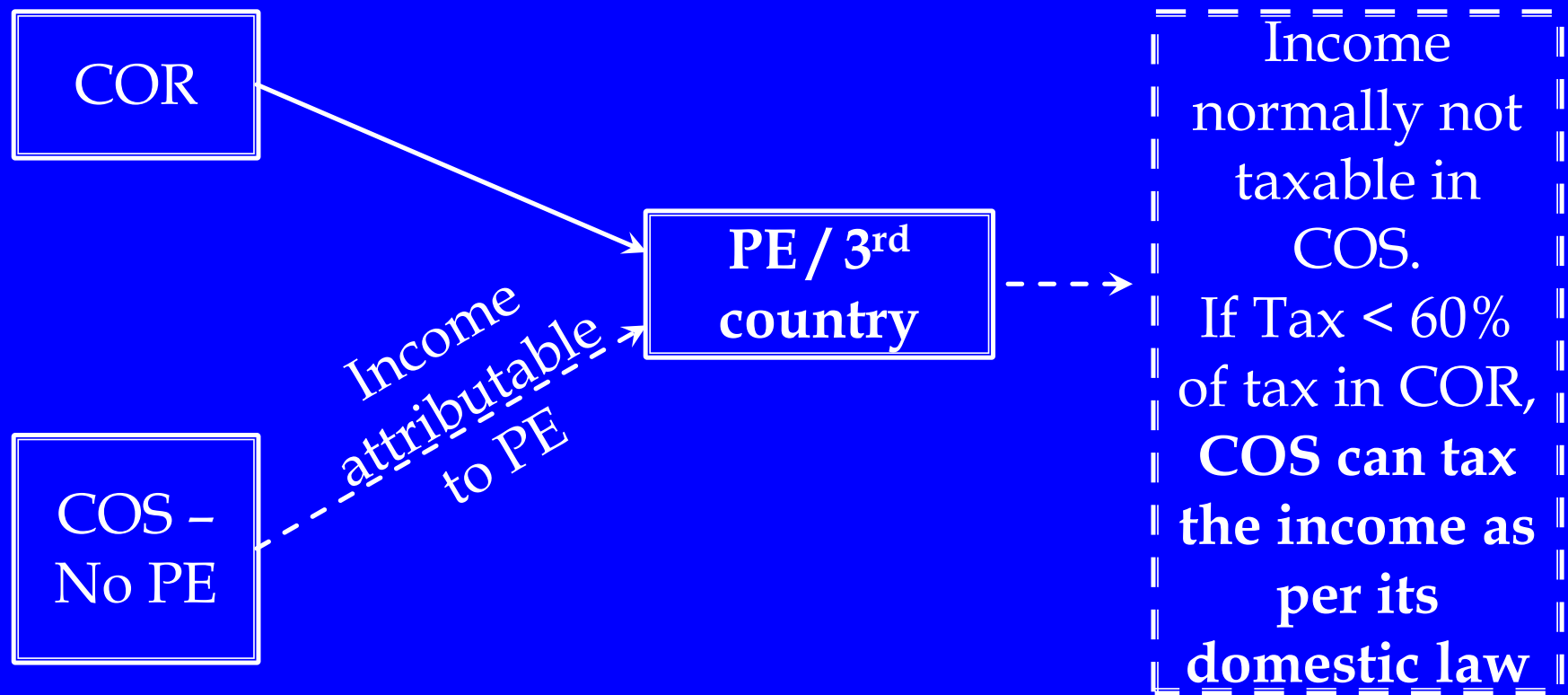
Transparent entity



India will not apply India – US DTA to income derived by US partner from U.K. firm.

It will apply India – U.K. DTA to income derived by U.K. partner.

PE in 3rd country – Article 10



However COS cannot tax income if income in COS is in connection with or incidental to active conduct of business through PE.

PE in 3rd country

- India has not made any reservation or notification.
- If other country has made a reservation, this article will not apply (e.g. UK).
- In case of other countries, this will apply (e.g. Austria).

Questions and comments welcome

Naresh Ajwani
naresh@rashminsanghvi.com