



# **CTC MLI Course**

**Prevention of Treaty Abuse – Article 6 (Preamble)  
and Article 7 (PPT) [BEPS Action 6 report]**

**CA Geeta D Jani**

**October 2018**

# Contents

---

- ▶ Background and introduction
- ▶ Purpose of Covered Tax Agreement (CTA)- Article 6 of MLI
- ▶ Prevention of Treaty abuse- Article 7 of MLI
  - ▶ Understanding principle purpose test (PPT)
  - ▶ Examples from Action 6 commentary
  - ▶ Interplay between PPT & Simplified Limitation of Benefit (SLOB)
  - ▶ Interplay between PPT and GAAR
- ▶ Others
  - ▶ PPT impact- all or none approach ?
  - ▶ Effect of multiple treaty benefits
  - ▶ Miscellaneous issues

# Background and Introduction

---

- ▶ The concern of treaty shopping or improper use of treaty conventions was one of key concerns at OECD even prior to BEPS project. In 2003, OECD added the following guiding principle to the commentary on Article 1:

*“A guiding principle is that the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions.”*

- ▶ OECD measure under BEPS Action 6 - *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances* deals with a variety of measures to control treaty abuse

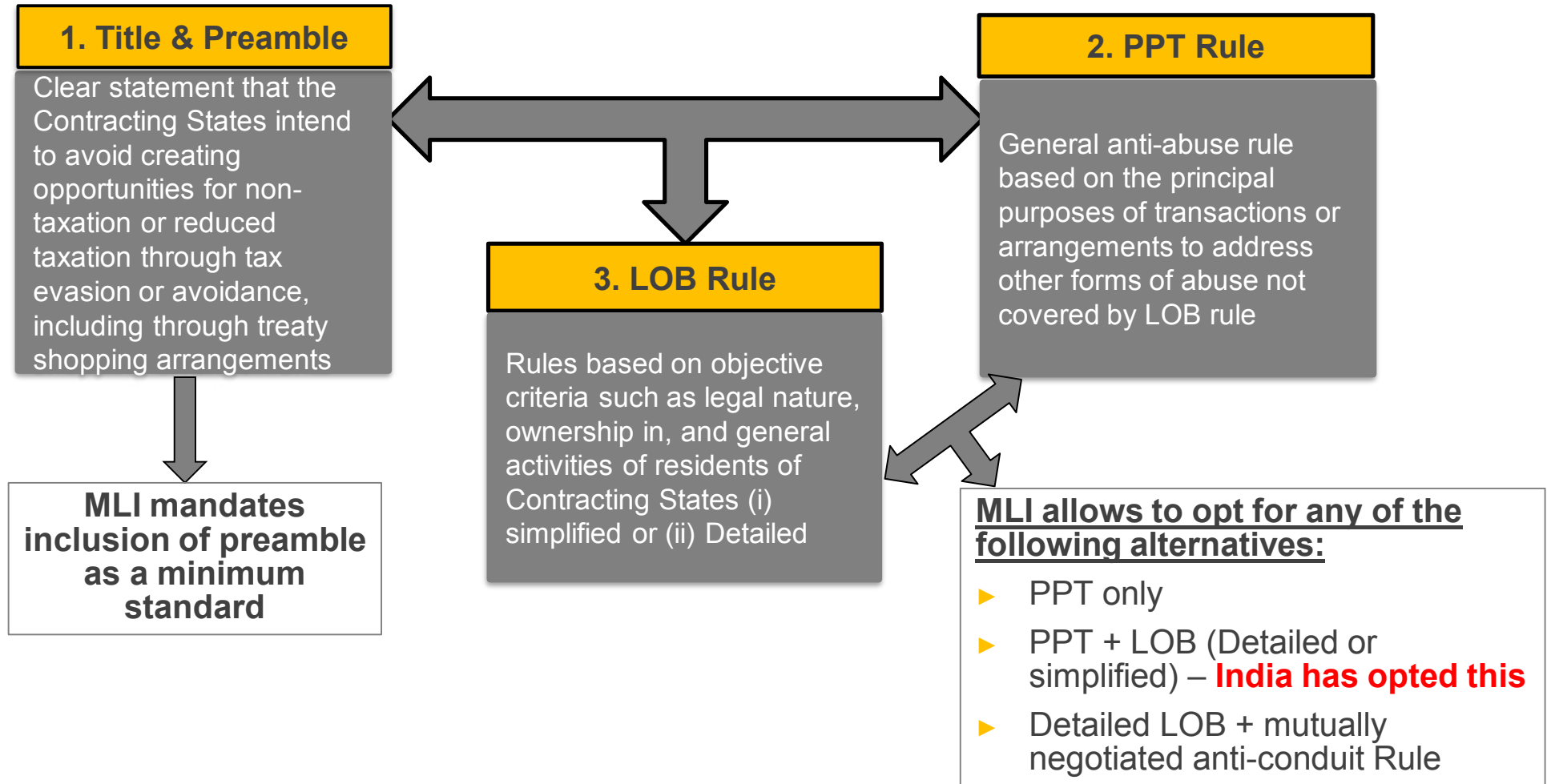
*“Treaty abuse is one of the most important sources of BEPS concerns..... Tight treaty anti-abuse clauses coupled with the exercise of taxing rights under domestic laws will contribute to restore source taxation in a number of cases.”*

- ▶ BEPS Action 6 is one of the minimum standards under OECD BEPS project

# Prevention of treaty abuse

## Minimum standards - Article 6, 7 of MLI

Three-pronged approach to address treaty shopping



# MLI Article and India positions

MLI provisions		Art No.	Minimum standard?	India's positions
<b>Article 6 of MLI</b>	Preamble	6(1)	√	√
	Preamble (additional sentence)	6(3)	X	X
<b>Article 7 of MLI</b>	PPT Rule	7(1)	√	√
	Discretionary relief for PPT	7(4)	X	X
	SLOB Provision	7(8) to 7(13)	X	√

# Purpose of a CTA



# Article 6 of MLI – Purpose of a CTA

---

Following Preamble shall be added to CTA<sup>1</sup> (Covered Tax Agreement)

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

- Being a minimum standard, requires insertion in CTA in absence of or in place of present text. Opt out is highly conditional
- Compatibility clause leads to addition of this text to the existing text

**India has adopted minimum standard text**

---

<sup>1</sup>Para 1 of Article 6 of MLI

# Article 6 of MLI – Purpose of a CTA

---

- ▶ Option provided to countries to include the following text (additional text) in the preamble to CTA (Para 3 of MLI):

*“Desiring to further develop their economic relationship and to enhance their co-operation in tax matters”*

- The additional text is **not** a minimum standard and will modify a CTA only if **both the contracting jurisdictions** agree to adopt and notify their choice to make such modification
- To illustrate, A- B CTA will have the above additional (optional) sentence only when A&B both notify
- If A notifies – but, B does not or vice-versa, A-B CTA will not include the additional text of preamble

- India has not opted for the optional preamble text. India’s treaties does not get modified
- Illustrative list of countries which have opted optional preamble text - Australia, Belgium, Cyprus, France, Japan, Luxembourg, Netherlands, Singapore, South Africa, Switzerland, UK



# Impact of preamble on India's treaties with major investment countries

Country	Assessment of impact
USA	<ul style="list-style-type: none"> <li>▶ Not a signatory to the MLI, hence India's treaty will not be impacted due to MLI changes</li> </ul>
Mauritius	<ul style="list-style-type: none"> <li>▶ Mauritius has not notified India's treaty as a CTA</li> <li>▶ Existing India-Mauritius treaty continues to subsist without any change in preamble</li> </ul>
Singapore, France, UK	<ul style="list-style-type: none"> <li>▶ These countries have notified India as a CTA and hence the preamble language (minimum standard) is likely to change</li> <li>▶ The current preamble of these treaties contain the objective of prevention of double taxation and fiscal evasion</li> <li>▶ The preamble language is likely to get widened with new preamble which provides for <b>'without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance'</b> and <b>anti-treaty shopping objective</b></li> </ul>
Russia	<ul style="list-style-type: none"> <li>▶ Russia has notified India as a CTA and hence the preamble language is likely to be changed</li> <li>▶ Preamble language is likely to be widened to include prevention of fiscal evasion, avoidance of non-taxation / reduced taxation and targeting treaty shopping</li> <li>▶ <b>Object of economic cooperation is already part of existing treaty, it will continue to remain in the preamble with Russia</b></li> </ul>

# Significance of preamble in interpretation of treaties

---

- ▶ **Article 31 of VCLT:** Preamble of a treaty helps in proper interpretation and application of the provisions of a tax treaty
  - ▶ 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.
  - ▶ The context for the purpose of the interpretation of a treaty shall comprise the text, preamble and annexes
- ▶ **Article 32 of VCLT:** Recourse to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:
  - ▶ leaves the meaning ambiguous or obscure; or
  - ▶ leads to a result which is manifestly absurd or unreasonable.

# SC decision in the case of Azadi Bachao Andolan [(263 ITR 706)(SC)] (ABA)

- ▶ SC acknowledged the Taxpayer's arguments to consider Preamble of treaty while interpreting tax treaties:

*".....that the preamble of the Indo-Mauritius DTAC recites that it is for the "encouragement of mutual trade and investment" and this aspect of the matter cannot be lost sight of while interpreting the treaty"*

- ▶ SC noted an academician observation that India has benefited from the "Mauritius Conduit"

*".....Although the Indian economic reforms since 1991 permitted such capital transfers, the amount would have been **much lower without the India-Mauritius tax treaty.**"*

- ▶ SC 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....."*

- Whether ABA conclusion would remain unchanged post MLI?
- Is preamble insertion sufficient to target abuse including of treaty shopping?
- Is preamble sufficient to throw light on object and purpose of a given article ?

# Article 7: Prevention of Treaty Abuse



# Article 7 of MLI – Principal Purpose Test (PPT)

---

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

*Unless*

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

# Key guiding principles on PPT<sup>1</sup>

---

- ▶ “Codification of existing principles dealing with ‘improper use’ of treaty
- ▶ Undertake an objective analysis of aims and objects of all persons involved in putting arrangement/transaction in place
- ▶ Question of fact: Consider all circumstances surrounding the ‘arrangement’
- ▶ “Reasonable to conclude” - conclusive proof of ‘purpose’ not necessary
  - ▶ Alternative views need to be examined objectively
  - ▶ Dictionary meanings of “reasonable”: having sound judgment, fair, sensible
- ▶ Self assertion by taxpayer not sufficient – but, tax benefit not to be assumed lightly

---

<sup>1</sup>Paras 10-13 of BEPS Action 6 report (PPT) and 178-181 of 2017 OECD Commentary on PPT

# Key guiding principles on PPT

---

- ▶ ‘Principal purpose’ (other than treaty benefit) has to justify entering into the arrangement
- ▶ Obtaining treaty benefit not sole or dominant purpose of the arrangement
- ▶ Obtaining benefit is in accordance with the **object and purpose** of the treaty (viz. facilitate cross border movement of goods, services, capital and people)<sup>1</sup>
- ▶ Implicit in a treaty is the object to promote economic development

Is arrangement capable of being explained but for treaty benefit? **OR**,  
Is treaty benefit in itself justifying the transaction?

---

<sup>1</sup>Para 170 of 2017 OECD Commentary

# Meaning of tax benefit

---

- ▶ “Benefit” covers all limitations on taxation imposed on the State of source
  - ▶ Example: tax reduction, exemption, benefit of non-discrimination, UTC, tax sparing
  - ▶ PPT can also be invoked by COR
  - ▶ In Indian context, UTC claimed under India Singapore treaty can be subjected to PPT
- ▶ PPT has no impact on tax concessions admissible in the domestic law ( eg lower withholding rate admissible u/s 194LC/LD )



# Meaning of arrangement

---

- ▶ Action 6 final report provides the interpretation of the term 'arrangement':

*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. These terms also encompass arrangements concerning the **establishment, acquisition or maintenance of a person who derives the income**, including the qualification of that person as a resident of one of the Contracting States, ....*

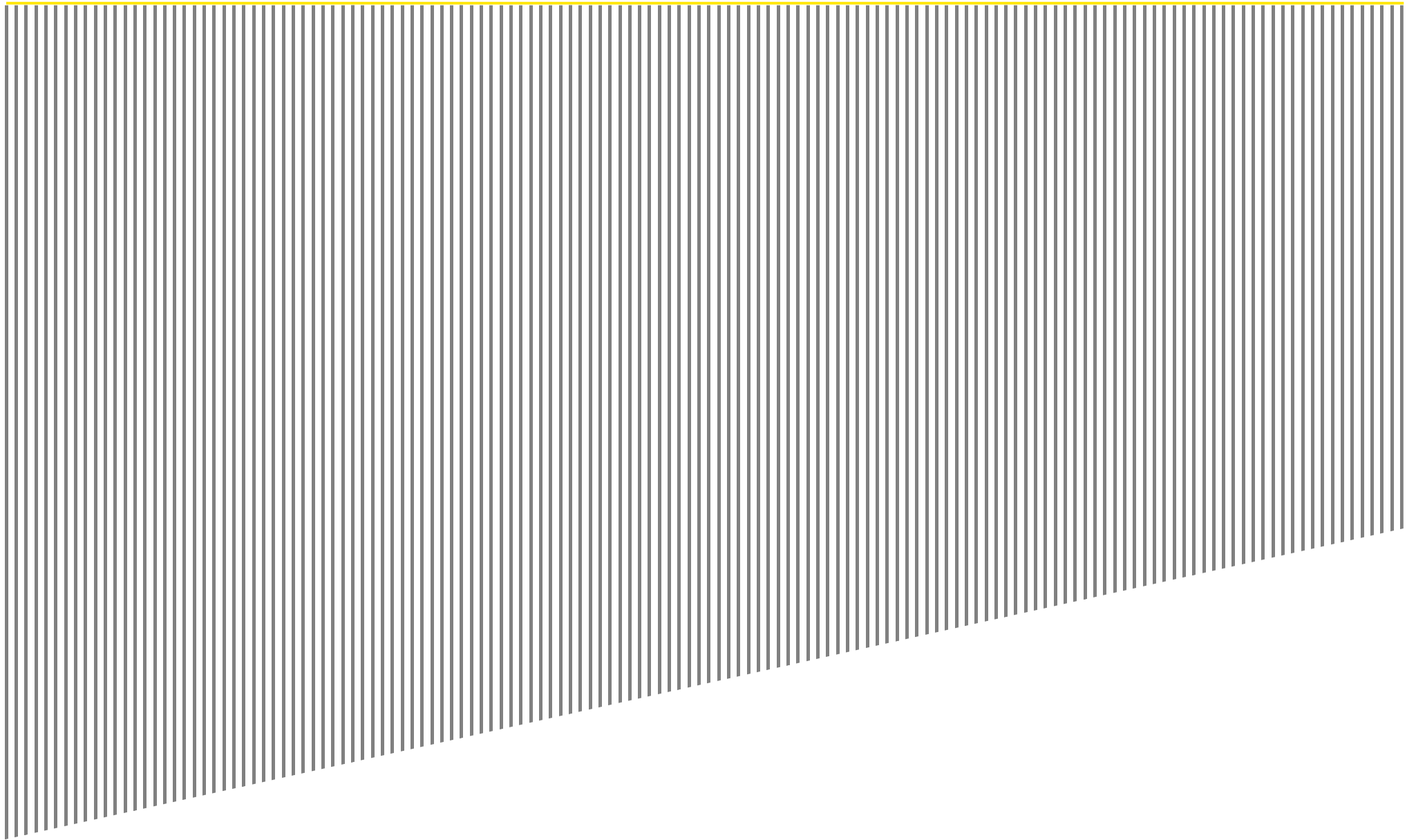
- ▶ PPT applies qua arrangement/transaction though the entity is SLOB compliant or otherwise treaty eligible entity

For a typical holding structure, the taxpayer needs to explain reasons for having a separate entity and also reasons for establishing the entity in a given jurisdiction. [Need to satisfy separate entity test and location test].

# Impact of PPT on India's treaties with major investment countries

Country	Existing tax treaty has PPT or similar clause	Counterparty posture in MLI	What is the emerging position today?
USA	No	USA has not signed the MLI	<ul style="list-style-type: none"> <li>▶ No impact of MLI on the existing treaty.</li> <li>▶ Existing treaty has a LOB Article, which is similar to the SLOB provision of MLI</li> </ul>
Mauritius	No. LOB is limited to capital gains Article	India has not been notified as CTA by Mauritius.	<ul style="list-style-type: none"> <li>▶ Until bilateral negotiations take place, no change to the existing treaty</li> </ul>
Singapore	No. LOB is limited to capital gains Article	PPT is adopted	<ul style="list-style-type: none"> <li>▶ PPT likely to be applicable to all the articles of the India-Singapore Treaty.</li> <li>▶ In relation to capital gains article, LOB condition of existing treaty applies</li> </ul>
UK	Yes	PPT is adopted	<ul style="list-style-type: none"> <li>▶ PPT as modified by MLI language will form part of CTA in place of existing PPT provision.</li> </ul>
France, Netherlands	No	PPT is adopted	<ul style="list-style-type: none"> <li>▶ As both have notified PPT, MLI PPT will form part of CTA</li> </ul>
Hongkong	Signed in March 2018	PPT is adopted	<ul style="list-style-type: none"> <li>▶ HK not part of India CTA. The recent treaty concluded with HK adopts MLI PPT language</li> </ul>

# Examples from Action 6 Commentary



# PPT limitation applies

---

- ▶ Steps taken to hold BOD meetings to claim changed residency<sup>1</sup>
- ▶ Sell property post changing residence for treaty benefit: Other objects of facilitating sale, reinvestment does not negate PPT applicability
- ▶ Splitting up of 22 month contract to avoid trigger of PE threshold<sup>2</sup>
- ▶ Arrangements resulting in no/low taxation in State S by assigning debt/right to dividend, etc. (without any other objective)<sup>3</sup>

---

<sup>1</sup>Para 9 of proposed commentary on PPT

<sup>2</sup>Example J of para 14 of proposed commentary on PPT

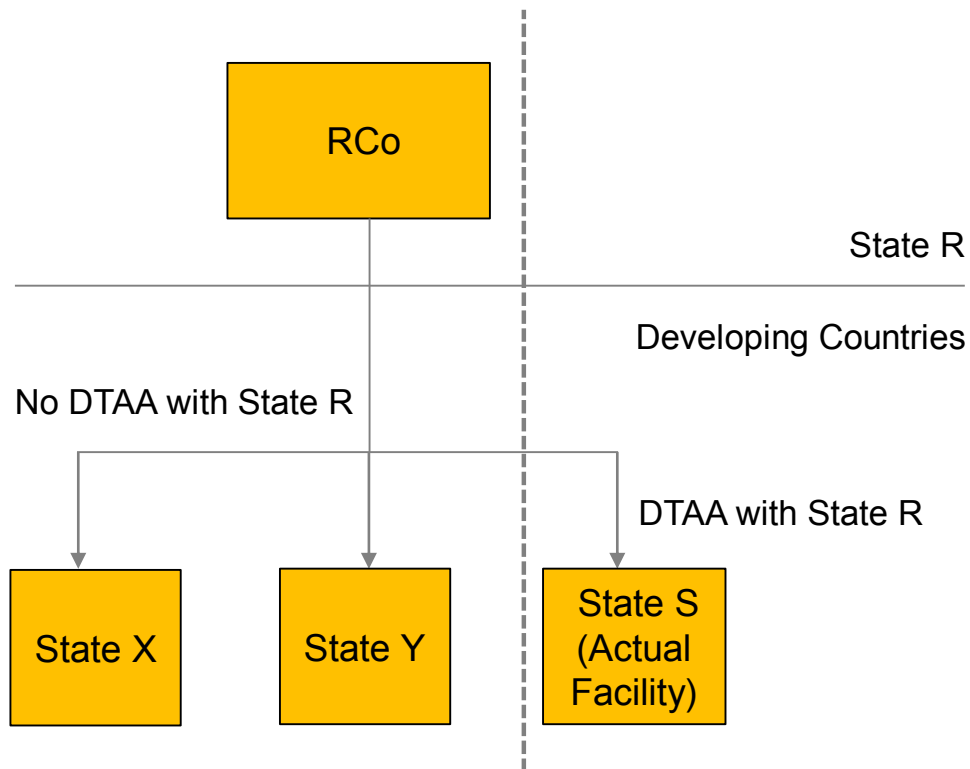
<sup>3</sup>Examples A, B of para 14 of proposed commentary on PPT

# Examples from Action 6 Commentary - PPT limitation not applicable

Ex	Fact pattern complying PPT	Conclusion
C	Setting up manufacturing plant in low cost jurisdiction with favourable treaty.	Meets treaty object of encouraging cross border investment.
D	CIV (with minority shareholders from third country) investing 15% portfolio in jurisdiction which also has favourable treaty.	Context of CIV supports that principal purpose is not treaty benefit.
G	Establishing service company in a jurisdiction with skilled labour force, reliable legal system, business friendly environment, political stability, sophisticated banking system and comprehensive treaty network. The service company conducts real economic functions.	Not reasonable to deny treaty benefits to entity which conducts real business using real assets and assuming real risk
H	Non CIV establishing intermediary in a jurisdiction where experienced local management team reviews, approves and monitors investments.	Investment made in the ordinary course of business of the intermediary.

# Examples from Action 6 Commentary

## “one of the principal purposes”



### Example C of OECD Commentary on PPT

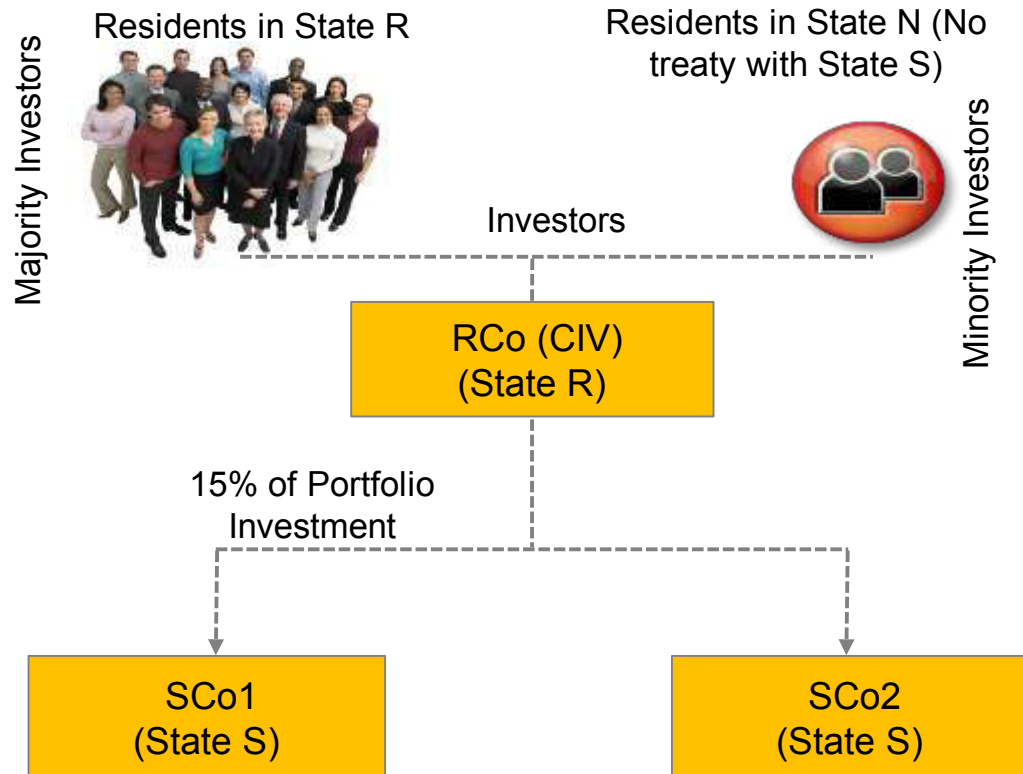
- ▶ Setting up a manufacturing facility in State S which was one of the three shortlisted locations for establishing manufacturing facility.
- ▶ Though all three locations were comparable economically and politically, presence of treaty with State S tilted the choice.
- ▶ Though tax is one of the principal factors in decision making, treaty benefit is to be granted.
- ▶ Encouraging cross border investment and availing treaty benefit for actual plant set up in State S meets with object and purpose of the treaty.

### GAAR parallel

- ▶ Example 1 of Shome Committee report provides GAAR may be not invoked where actual new unit is set up in SEZ in order to obtain tax incentive

# Examples from Action 6 Commentary

## “one of the principal purposes”



### Example D of OECD Commentary on PPT

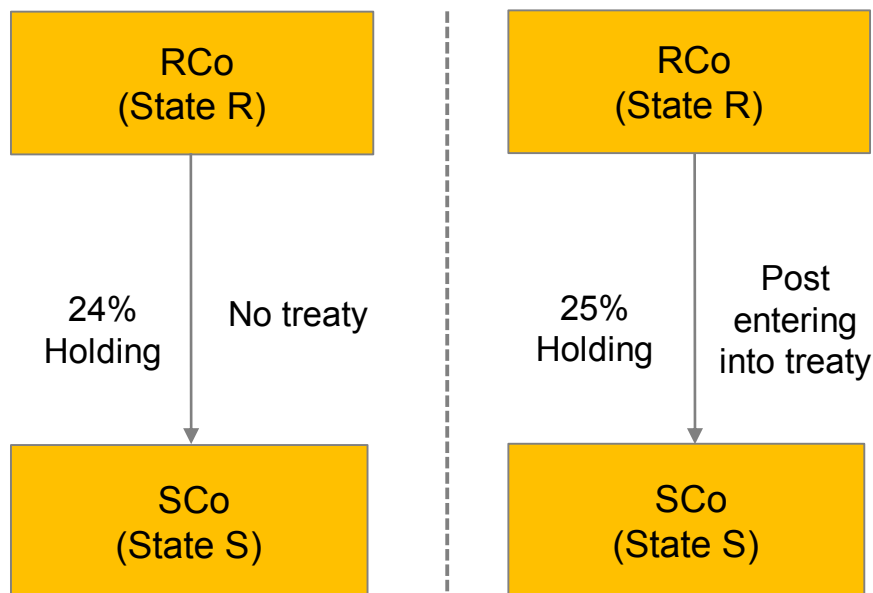
- ▶ Investment by a CIV, resident of State R, in shares of companies in state S.
- ▶ CIV, receives dividend from its investment in companies in State S, after withholding tax at 10% under the State R – State S treaty.
- ▶ Majority investors of CIV are residents of State R and minority investors are residents of State N (no treaty between State S and State N).
- ▶ Investors’ decisions to invest in CIV and CIV’s investment strategy is independent.
- ▶ Though CIV has considered the existence of a benefit under the State R-State S treaty with respect to dividends, this alone would not be sufficient to deny treaty benefits.
- ▶ Encouraging cross border investment meets the object and purpose of the treaty.

### GAAR impact:

- ▶ Q. No. 4 of GAAR Guidelines (Circular 7 of 2017)  
*“GAAR shall not be invoked merely on the ground that the entity is located in a tax efficient jurisdiction”*

# Examples from Action 6 Commentary

## “one of the principal purposes”



### Example E of OECD Commentary on PPT

- ▶ Increasing ownership stake to 25% (from 24% stake) in order to avail concessional WHT rate of 5% on dividends.
- ▶ The facts suggest one of the principal purposes is clearly to obtain the benefit of the lower WHT rate provided by Article 10(2)(a) of a treaty.
- ▶ However, granting benefit under this Article is permitted to a taxpayer who genuinely increases its participation in a company in order to satisfy the arbitrary threshold of 25%.

### GAAR impact

- ▶ Example 15 of Shome Committee report
  - ▶ GAAR may be invoked if the main purpose of increasing shareholding % was to obtain tax benefit and if there is no commercial justification for increase in the shareholding %.



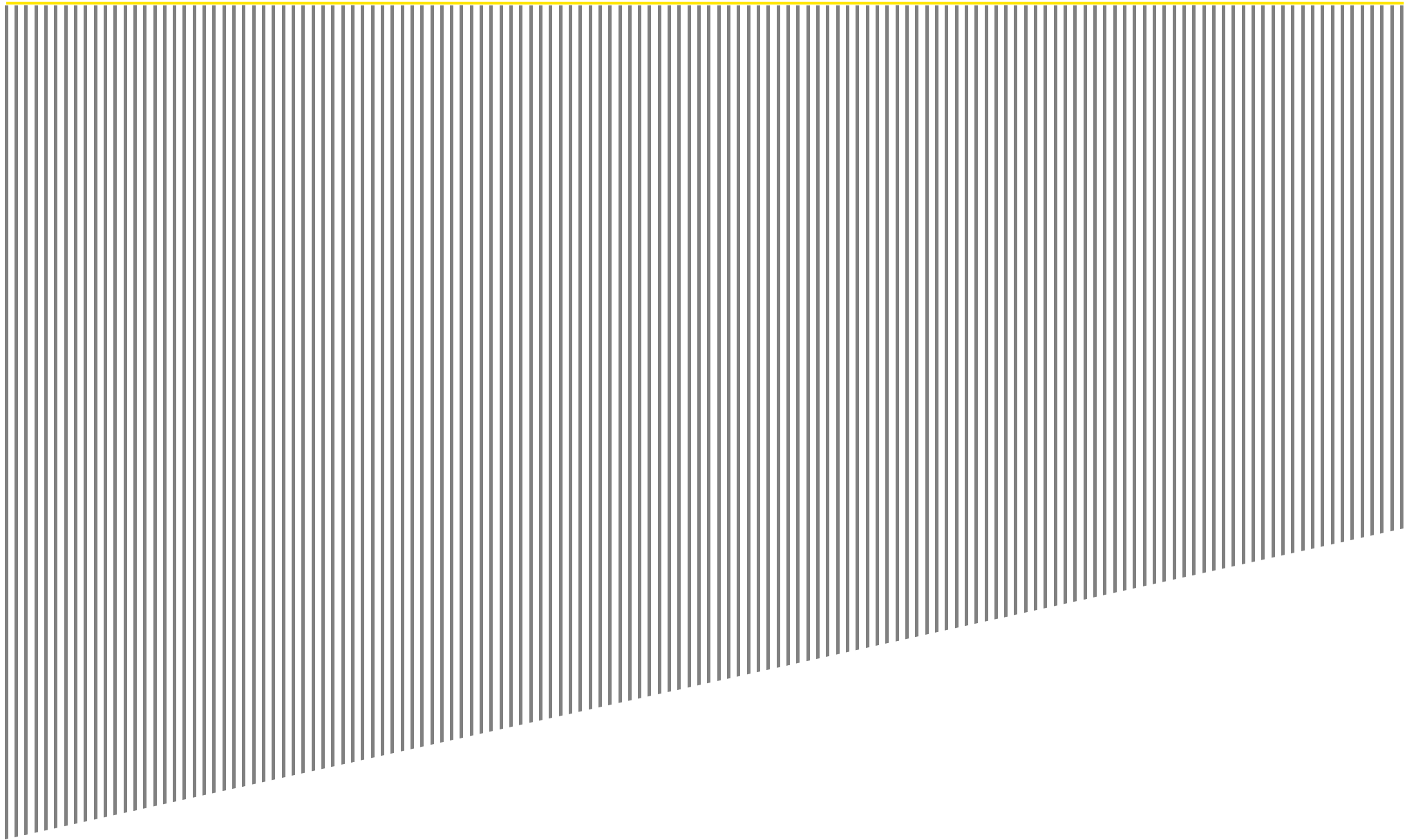
# PPT– Discretionary relief rule

---

- ▶ Discretionary relief (Competent Authority (CA) Rule)
  - ▶ Where treaty benefits are denied to a person under the PPT Rule, CA may grant the intended benefit or any other benefit in respect of an item of income or capital:
    - ▶ Based on an application by the taxpayer;
    - ▶ After consideration of relevant facts and circumstances,
    - ▶ CA determines that the benefits would have been otherwise granted in the absence of the transaction/arrangement
  - ▶ Rejection of request can be only after consulting the CA of the other Contracting State
  - ▶ CA rule is an **optional** provision and will apply only in addition to PPT rule if opted for
    - ▶ CA rule will apply to CTAs only if **both** the respective contracting countries to CTA notify their intention to apply this in conjunction to PPT rule

**India has not opted for the CA rule**

# PPT & SLOB

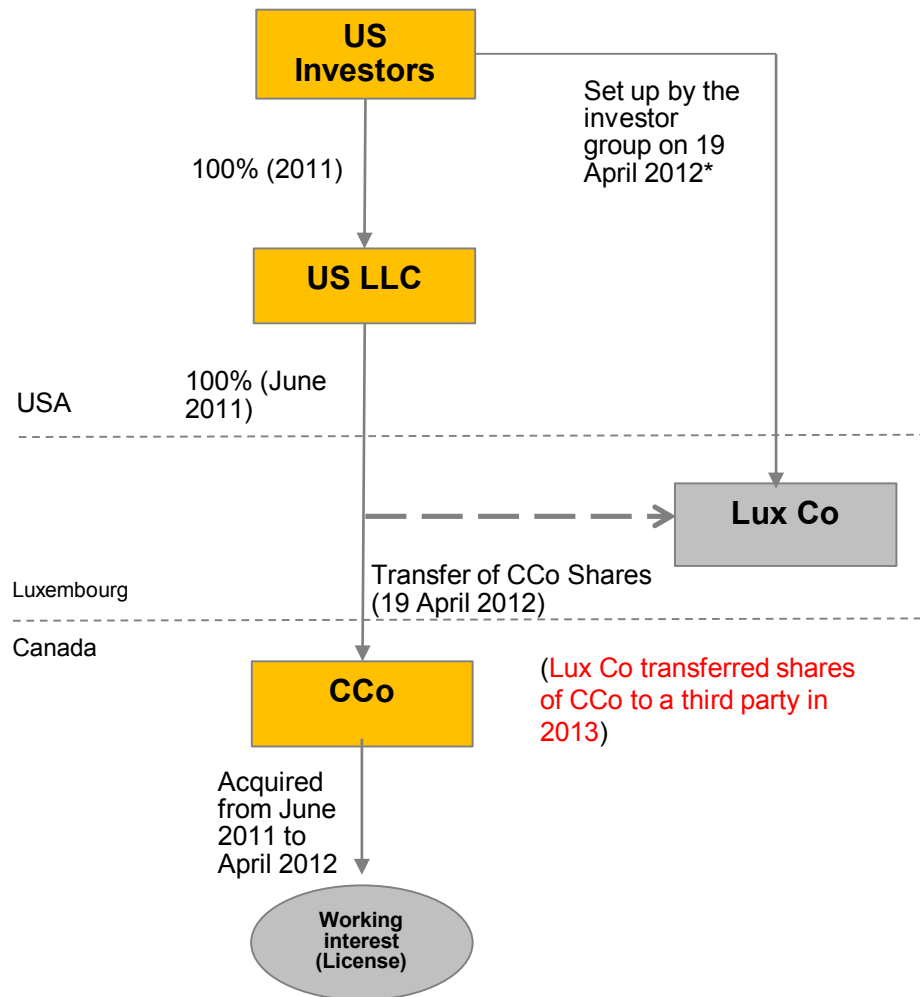


# Interplay of PPT with LOB/SLOB

---

- ▶ Taxpayer needs to fulfil all objective conditions of treaty entitlement such as being a resident, beneficial owner, expense test, ALP payment, etc
- ▶ PPT rule is a “notwithstanding” over-arching Rule
- ▶ Should PPT test fail, treaty benefit can be denied
- ▶ PPT test may fail qua transaction / arrangement though the entity:
  - ▶ Is treaty resident and fulfils SLOB test to be a qualified person
  - ▶ Is a beneficial owner of income
    - ▶ Receives income at ALP and such income is not “excessive”
  - ▶ LOR or other substance based LOB test is fulfilled

# Recent Canadian decision on GAAR/treaty shopping – Alta Energy Ruling



- ▶ Black stone (US) a private equity fund was interested in partnering with Alta group (US) which was engaged in oil and gas exploration
- ▶ Both parties (US investors) set up a JV, US LLC
- ▶ JV was set up in USA as the intent was to explore O&G reserves in North America
- ▶ US investors however, decided to exploit reserves in Canada and set up CCo in Canada in 2011
- ▶ Having regard to possible trigger of CFC taxation (as investment was in Canada), holding co was sought to be located outside USA
- ▶ Lux Co was set up in April 2012
- ▶ Same day US LLC transferred CCO shares to Lux Co
- ▶ In August 2013, Lux Co transferred CCO shares and claimed exemption under Article 13(5) of Lux-Canada treaty
- ▶ Lux Co upstreamed dividend to investors

\* Lux Co was a WOS of Canadian partnership firm. It is not clear what was the shareholding structure of the investor group in the Canadian partnership firm.

# Recent Canadian decision on GAAR/treaty shopping – Alta Energy Ruling

---

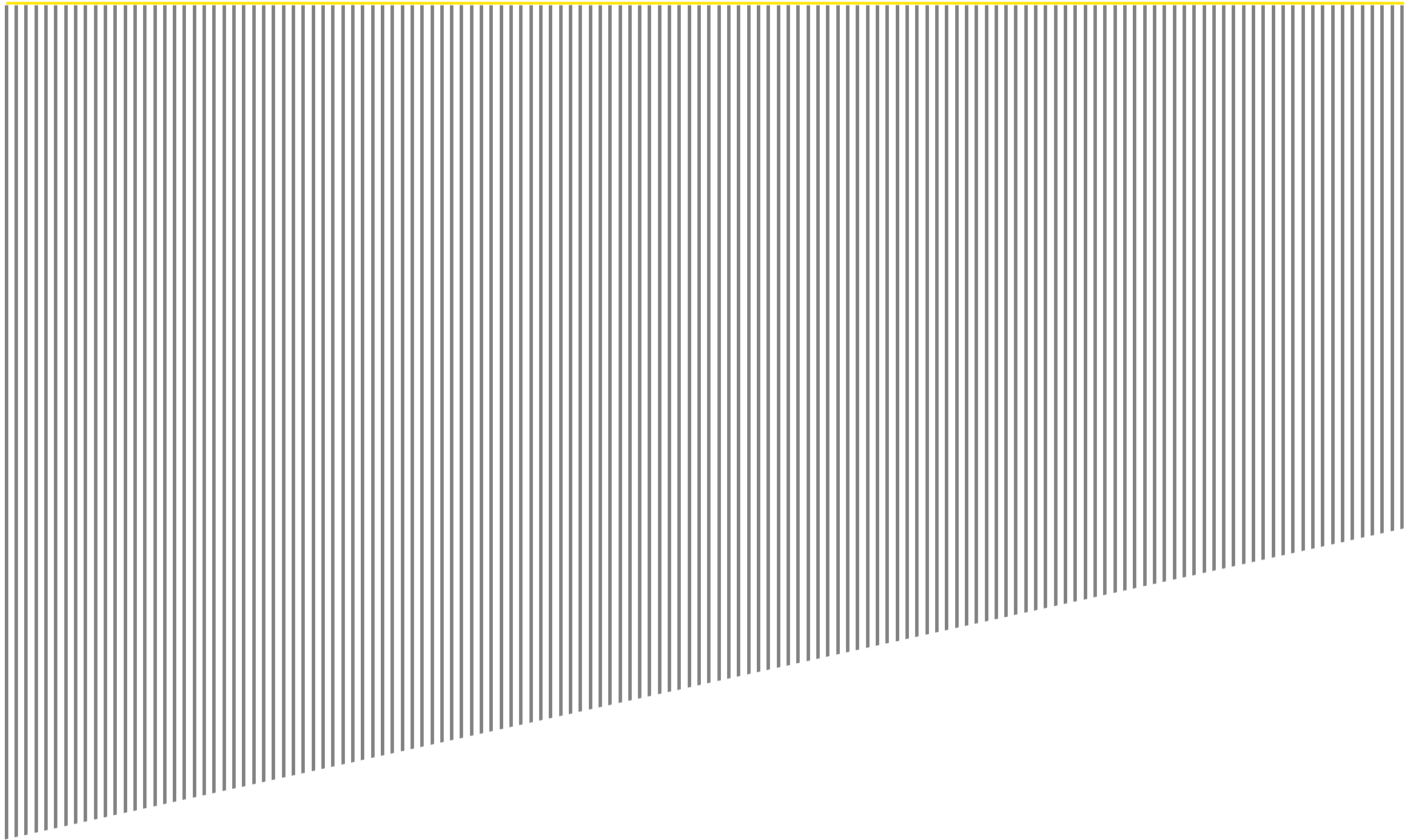
- ▶ Acceptance by tax authority that gains arises to Lux Co indicates acceptance that Lux Co is beneficial owner
  - ▶ Only a nominee/agent does not qualify as a BO
- ▶ Double non-taxation (gains not taxed in Luxembourg) is not fatal to treaty benefit which is not made “subject to tax condition”.
- ▶ Lux Co being held by third country residents is of no relevance in absence of LOB
  - ▶ Canada Lux treaty did not include LOB unlike other treaties of Canada

# Recent Canadian decision on GAAR/treaty shopping – Alta Energy Ruling

---

- ▶ Canadian laws required satisfaction of 3 cumulative conditions for invoking GAAR
  - i. Tax benefit
  - ii. Tax avoidance transaction
  - iii. Tax avoidance transaction resulting in misuse or abuse of law
- ▶ It was accepted that conditions (i) and (ii) are satisfied – though, applicability of (iii) was resisted
- ▶ Misuse or abuse to be seen in light of intent of specific treaty article and not in light of preamble of the treaty which provides general object of treaty
- ▶ Treaty exemption was envisaged for shares deriving principal value from immovable property in which business is carried on. There is use of treaty provision and not abuse/misuse
- ▶ A specific provision to regard treaty shopping to be abuse introduced later under Canadian domestic law was not applicable for the current transaction

# Interplay between PPT and GAAR



# Interplay between PPT and GAAR

Particulars	GAAR	PPT
Applicability	<ul style="list-style-type: none"> <li>Main purpose is tax benefit and</li> <li>One of the tainted element tests is present</li> </ul>	<ul style="list-style-type: none"> <li>One of the principal purposes is tax benefit</li> <li>Not in accordance with object and purpose of treaty</li> </ul>
Consequences	Re-characterization of transaction, re-allocation of income (includes denial of treaty benefit)	Denial of treaty benefit (subject to relaxation as per discretionary power of Competent Authority, if adopted)
Onus	Primary onus on tax authority	Primary onus on tax authority and rebuttal assumption for carve out
Methodology	Involves analysis of 'counter factual'	Focus only on actual transaction?
Administrative safeguards	Approving Panel	To be determined by respective states. UN Model Commentary explicit on this
Grandfathering	Yes	No
De-minimis threshold	Yes	No

Encompass 'arrangements' concerning establishment, acquisition, or maintenance of a person that derives income including its qualification as resident



# Interplay between GAAR and PPT

---

- ▶ Qua treaty benefit, PPT fulfilment essential
- ▶ If arrangement/transaction is PPT tainted, treaty benefit is denied:
  - ▶ GAAR invocation may not be necessary for denying treaty benefit
  - ▶ GAAR may still re-characterise the transaction
- ▶ If arrangement passes PPT test, GAAR test most likely gets fulfilled
  - ▶ Main purpose test of GAAR is, if at all, stricter
  - ▶ S.97(1)(c) test likely to be passed as location/residence is likely to be for substantial commercial purposes

## **OECD 2017 Commentary observes:**

*“To the extent that the application of the (**domestic**) rules results in a re-characterization of income or in a redetermination of the taxpayer who is considered to derive such income, the provisions of the Convention will be applied taking into account these changes.....”*

*(Para 22.1 of OECD MC)*

# Threshold under GAAR and PPT : Is PPT wider?

---

- ▶ **“One of the principal purposes” v “main purpose test”**: Threshold is practically same (View 1)
  - ▶ ‘Main’ and ‘principal’ are synonym as per dictionary
  - ▶ Explanatory Statement to BEPS MLI (para 95) alludes that “principal purpose” covers “main purpose” or “primary purpose”
  - ▶ 2017 Commentary on PPT (Para 181) - the object and purpose of the PPT is primarily to target treaty shopping arrangements in cases, where obtaining treaty benefit is considered to be a “principal consideration” of entering into a transaction or an arrangement
  - ▶ PPT rule is codification of existing principles which deal with improper use of treaty.
    - ▶ Para 61 of the 2017 OECD Commentary on Article 1 - it is provided that PPT merely confirms otherwise applicable principle that treaty benefit is not available where “main purpose” is to secure treaty benefit.

# Threshold under GAAR and PPT : Is PPT wider?

---

- ▶ **“One of the principal purposes” v “main purpose test”**: Threshold is not same, PPT has lower threshold (View 2)
  - ▶ Expert committee on GAAR recommended to change threshold of applicability of GAAR from ‘one of the main purposes’ to ‘main purpose’
  - ▶ Literal interpretation indicates differential threshold
  - ▶ 2011 UN Commentary on Article 1 (para 36)
    - ▶ The term ‘main purpose’ may impose an unrealistically high threshold for tax authorities to deny treaty benefits for abusive transactions, which would render the provision ineffective.
    - ▶ Lower threshold of ‘one of the principal purposes’ to trigger PPT, as against the ‘sole purpose’, the ‘essential purpose’ or ‘predominant purpose’, makes it relatively easy for the tax authorities to establish that the subjective test is met.
  - ▶ UK HMRC guidance on GAAR and UN Handbook titled ‘GAAR in protecting tax base’ indicates differential threshold

# Threshold under GAAR and PPT : Is PPT wider?

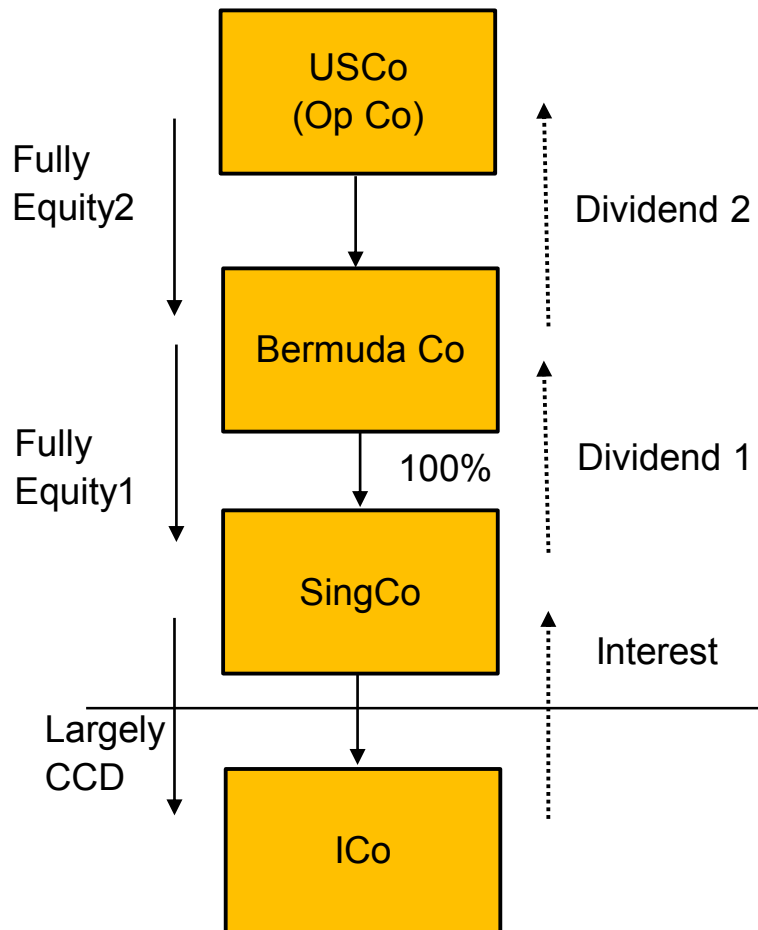
---

- ▶ **“One of the principal purposes” v “main purpose test” : similarities and differences**
  - ▶ GAAR in India, as also PPT of a treaty do factor the object and purpose of an arrangement.
  - ▶ Both the tests require objective of quantitative analysis of all relevant facts and circumstances, but the conclusion needs to be drawn on ‘qualitative’ or ‘overall impression’ basis
  - ▶ PPT may likely have a threshold which is lower compared to ‘main purpose’ test
  - ▶ However, the significance of word ‘main’ as part of the requirement of ‘one of the main purposes’ should not be understated. The tax purpose should be of a threshold which is meaningful and not insignificant/ trivial/ secondary

# Other issues



# Issue: PPT impact – all or none approach?



- ▶ Sing Co has subscribed to CCDs of Rs. 500 Cr. with a coupon rate of 10% issued by I Co in 2010
- ▶ Sing Co holds valid TRC
- ▶ I Co has paid interest to Sing Co by withholding tax @15% as per I-S treaty
- ▶ Sing Co and Bermuda Co are financed fully by equity
- ▶ Interest received by Sing Co is up-streamed up to USCo by way of Dividend
- ▶ Absent treaty benefit, tax liability in respect of CCD interest is @40% + surcharge as per domestic law
- ▶ India and Singapore have signed MLI on 7 June 2017

Withholding on interest	Rate
Domestic law of India	40% + sc
India-Singapore DTAA	15%
India-USA DTAA	15%

# Effect of PPT: Tax Authority's contentions

---

- ▶ Sing Co has been established to obtain lower WHT rate
- ▶ PPT works on 'either or not' principle; it does not look beyond I-S Treaty except under discretionary relief mechanism
  - ▶ PPT Article is CTA centric; does not permit 'look through' beyond that
- ▶ India has not opted for discretionary relief provision
- ▶ In any case, immediate holding entity to be seen which is not equivalent beneficiary
- ▶ Even for SLOB Article, India has made reservation and required equivalent beneficiary at an immediate / direct level

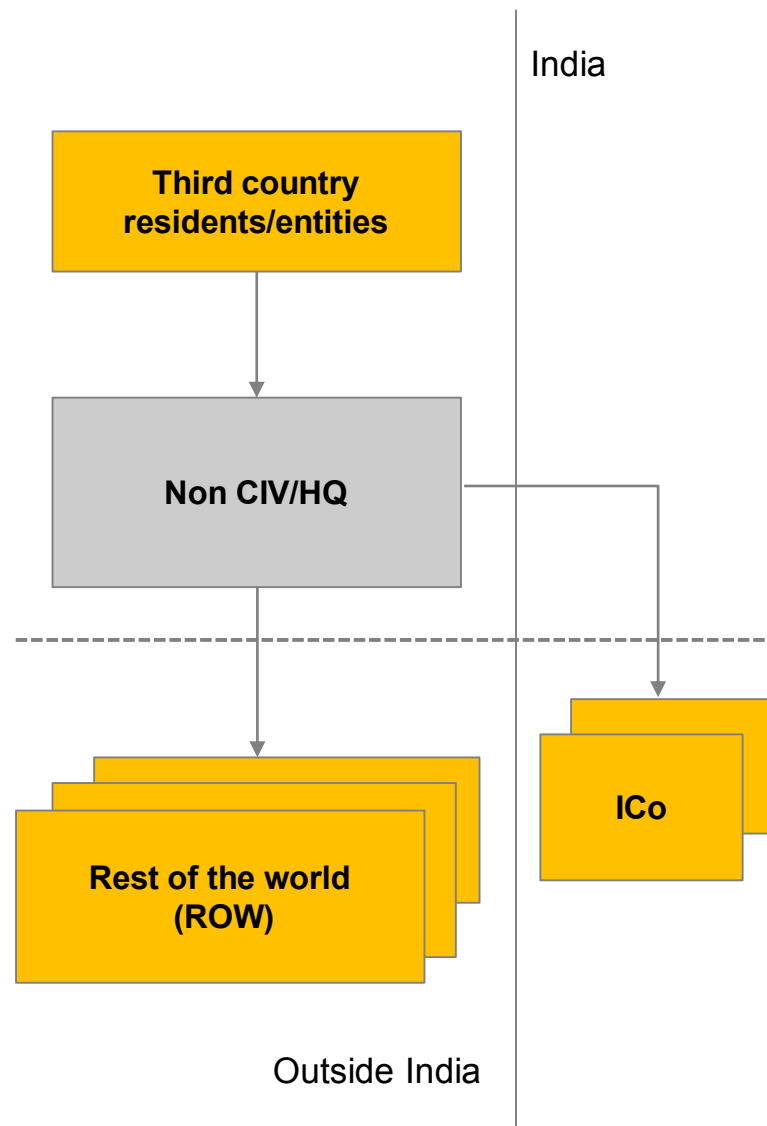
# Effect of PPT: Taxpayer's contentions

---

- ▶ PPT is codification of principles of OECD commentary dealing with improper treaty use, particularly, treaty shopping
- ▶ PPT leads to denial of 'benefit'
  - ▶ Dictionary meaning of the term 'benefit' suggests some improvement in condition
  - ▶ No improvement as US or Singapore would have the same result
- ▶ Identification of benefit by comparison with 'counterfactual'; consequences based on realistic counterfactual
- ▶ Clear text of PPT requires denial of the benefit from the tainted arrangement and does not contemplate harsher consequences
- ▶ Fair consequences of PPT are not limited by presence of discretionary relief provision
  - ▶ Discretionary relief is an inbuilt good practice not controlled by explicit assertion
- ▶ India having opted for SLOB, cannot selectively reserve notion of indirect equivalence



# Issue: Effect of multiple treaties benefit



- ▶ HQ holds multiple investment across globe/regions
- ▶ HQ investment in Indian entities is miniscule compared to Rest of the World (ROW)
- ▶ HQ is not able to explain commercial reasons for its presence in HQ jurisdiction
- ▶ HQ to take benefit of treaty network of country of its incorporation
- ▶ HQ's claim: India cannot invoke PPT as tax benefit in India is not "one of the principal purposes" of its existence in HQ jurisdiction
- ▶ OECD's take on impact of benefit arising from multiple treaties

*".....If the facts and circumstances reveal that the arrangement has been entered into for the principal purpose of obtaining the benefits of these (multiple) tax treaties, it should **not** be considered that obtaining a benefit under one specific treaty was not one of the principal purposes for that arrangement."*

# Miscellaneous issues

---

- ▶ Relevance of commentaries; examples prepared as part of BEPS agenda
- ▶ Impact on tax withholding obligation & PPT
- ▶ Is evaluation of PPT to be done at the stage of entering into transaction/ arrangement or can be done at a later stage?
- ▶ Substance determination exercise: Do POEM, GAAR, PPT and even TP converging towards evaluation of substance and of “realistically available commercial options?”

# PPT- time to gear up for uphill ride?

---

*“There is every reason to fear that, once the MLI is in force and a large number of countries (including ones with tax authorities that do not have a reputation for predictable interpretation of tax treaties) begin to apply the PPT, this will undermine the whole system of tax treaty benefits. Put simply, no taxpayer who has given any consideration to the impact of a tax treaty on its transactions or arrangements will be able to rely with any certainty on obtaining the benefits of the tax treaty” – Mr. Philip Baker*

# Questions?

---



# Thank You!

This Presentation is intended to provide certain general information existing as at the time of production. This Presentation does not purport to identify all the issues or developments. This presentation should neither be regarded as comprehensive nor sufficient for the purposes of decision-making. The presenter does not take any responsibility for accuracy of contents. The presenter does not undertake any legal liability for any of the contents in this presentation. The information provided is not, nor is it intended to be an advice on any matter and should not be relied on as such. Professional advice should be sought before taking action on any of the information contained in it. Without prior permission of the presenter, this document may not be quoted in whole or in part or otherwise.