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Conflicts under Article 13 of the Model Tax Treaty

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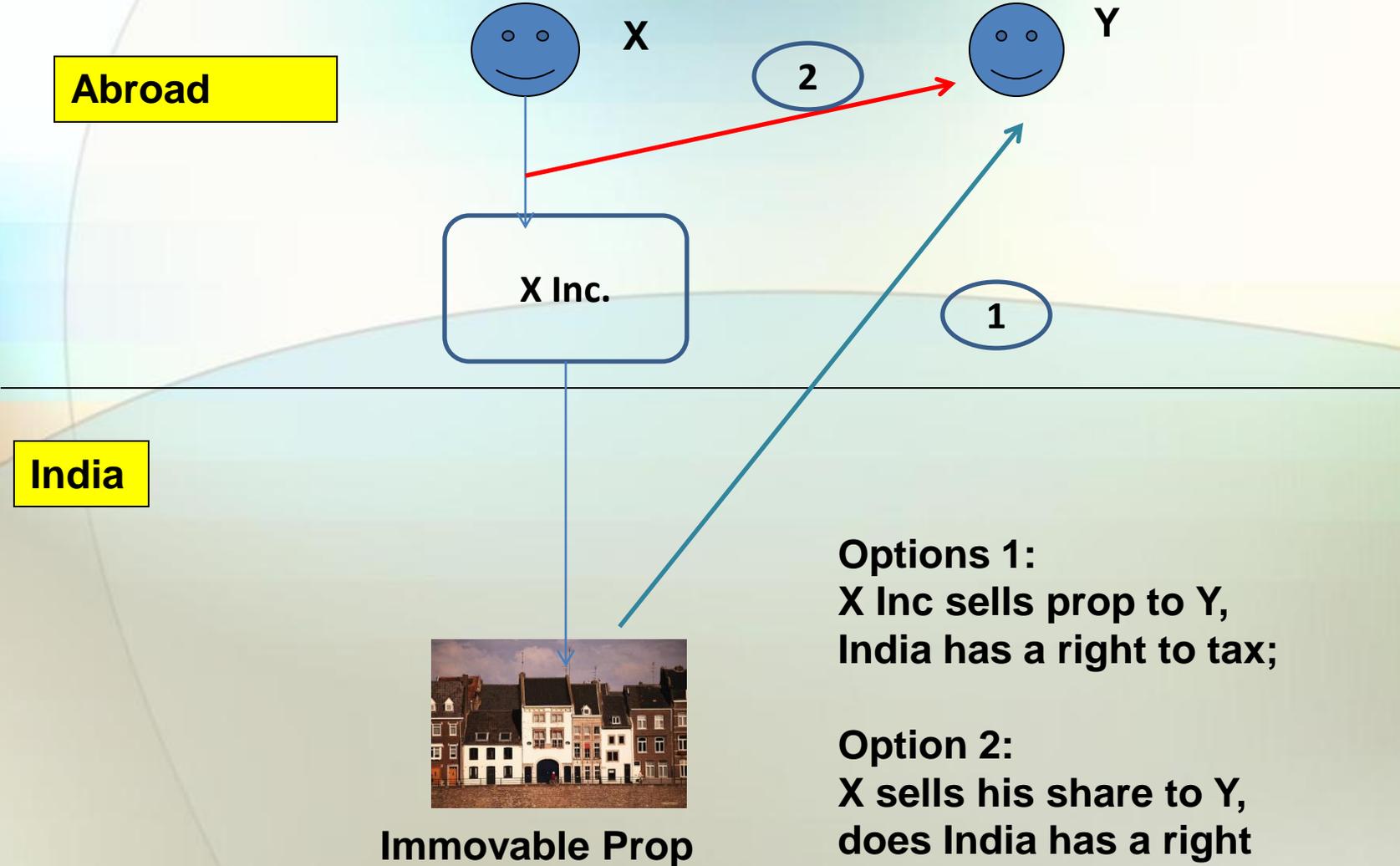
Presentation Structure -

- **Domestic Tax Law**
- **Indirect Transfer**
- **Article 13 of Tax Treaties**
- **Issues under Article 13**

Domestic Tax Law: Source Rules on Transfer - India

- **Income arising from transfer of Capital Assets situated in India is deemed to be taxable in India.**
- **“Transfer” has been clarified to include indirect transfer.**
- **“Property” in context of capital asset has been clarified to include rights of management or control or any rights in or in relation to an Indian company**
- **Any share or interest deriving its value substantially from assets located in India are deemed to be capital asset situated in India.**

Indirect Transfer of Assets



Options 1:
X Inc sells prop to Y,
India has a right to tax;

Option 2:
X sells his share to Y,
does India has a right
to tax?

Article 13: OECD Model

- **Para (1), if**
 - a resident of contracting State
 - derives gains
 - From the alienation
 - of such immovable property within meaning of Art. 6 as is situated in the other contracting State,

such gains may be taxed in the State of situs of immovable property.

Article 13: OECD Model

- **Para (2), if**
 - a resident of a contracting State.
 - derives gains from the alienation of movable property.
 - forming part of the business property of a permanent establishment which an enterprise of a contracting state has in the other contracting state
 - Including gains derived from the alienation of such a permanent establishment (alone or with whole enterprise)

Such gains may be taxed in the State of PE.

Article 13: OECD Model

- **Para (3), if**
 - **a resident of a contracting State.**
 - **derives gains from the alienation of**
 - **ships or aircraft operated in international traffic**
 - **or boats engaged in inland waterways transport**
 - **or moveable property pertaining to the operation of such ships, aircraft or boats,**

Such gains can be taxed only in the State of the enterprise's place of effective management.

Article 13: OECD Model

- **Para (4), if**
 - **a resident of a contracting State.**
 - **derives gains from the alienation of shares**
 - **deriving more than 50% of their value**
 - **directly or indirectly from**
 - **immovable property situated in the other**
 - **contracting State.**

Such gains may be taxed in the State of situs of immovable property.

Article 13: OECD Model

- **Para (5), if**
 - **gains are from alienation of any property other than referred to in Para (1), (2), (3) & (4) then**

Such gains shall be taxed only in the State of which the alienator is a resident.

Article 13: UN Model

- **Difference – Para (4) and new Para (5) –**
- **Para (4), if**
 - **a resident of contracting State**
 - **derives gains from the alienation of**
 - (i) shares of the Capital Stock of a company**
 - or**
 - (ii) an interest in a partnership, trust or estate**
 - **the property of which consists**
 - **directly or indirectly principally of immovable property situated in a contracting state.**

Such gains may be taxed in the State of situs of immovable property.

Article 13: UN Model

Para (4) contd....

Exception for land used in business unless it is in the business of managing land.

The term principally is defined to mean value of immovable property exceeds 50% of the aggregate value of all assets.

Article 13: UN Model

- **Para (5), if**
 - resident of a contracting State.
 - derives gains (other than to which Para 4 applies) from
 - alienation of Shares of a company and
 - the alienator has at any time during the twelve month preceeding the date of alienation held directly or indirectly at least _____% of capital of that company.

Such gains may be taxed in the State of residence of the Company.

Article 13: Indian Tax Treaty

- **There is no specific Indian Model.**
- **Indian DTAA with different countries is a mix of both UN Model and OECD Model.**
- **In certain DTAA's like with Mauritius, Singapore etc., the taxation right on gains from alienation of shares of companies resident in India has been granted to State of residence of the alienator.**

Article 13: Issues

- **Meaning of “alienation”**
 - The term “alienation” has not been defined.
 - OECD Commentary as well as UN indicate that “Alienation” is broad enough to include “the sale or exchange of property and also from a partial alienation, the expropriation, the transfer to a company in exchange for stock, the sale of a right, the gift and even the passing of property on death”.
 - Article 3(2) – meaning – contextual interpretation.
 - Whether definition of “transfer” in domestic law applies
 - “deemed transfer” whether covered.

Article 13: Issues

- **Meaning of “share”**
- **Meaning of “directly or indirectly”**
- **Date of valuation**
- **Effect of liabilities**
- **Basis for taxation**
- **Fluctuation in rates of Exchange**
- **“See through” approach its scope and applicability**
- **Whole of the gains no proportion.**
- **Transfer of small holdings**

Thanks