

# **Tax Opportunities & Challenges - Post MLI**

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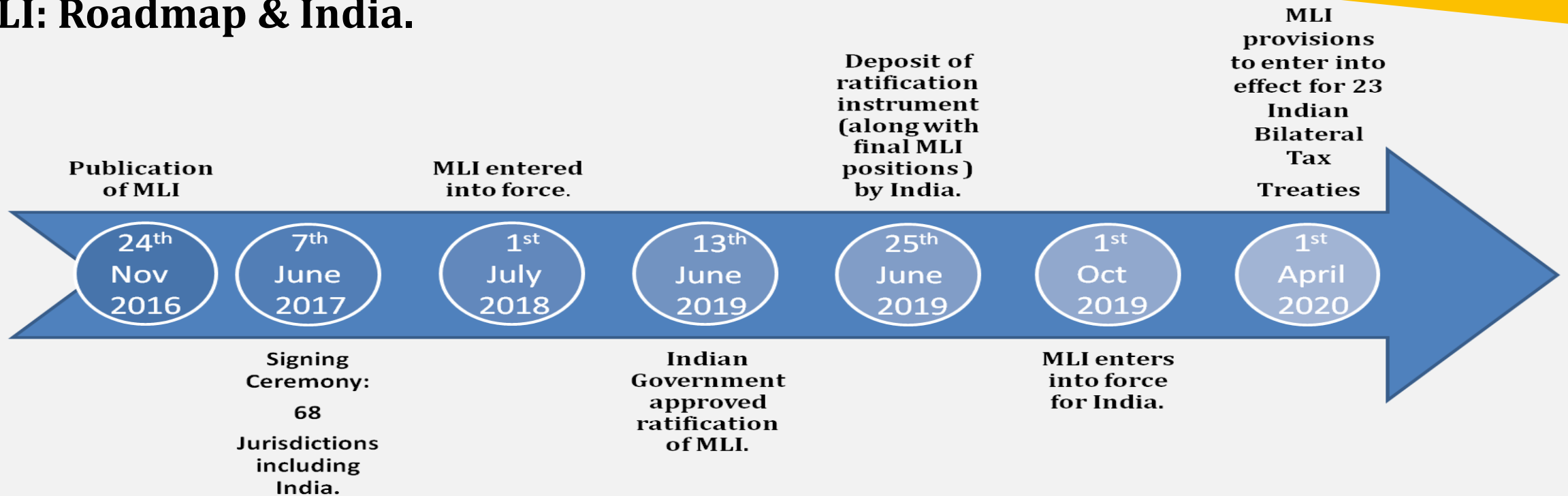
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# MLI: Roadmap & India.



## Backdrop to MLI ratification:

- 126 Agreements (96 - Comprehensive Agreements; 19 - Tax information Exchange Agreement; 8 - Limited agreements; 1 - Limited Multilateral Agreement; 1 - Intergovernmental Agreement to improve International Tax compliance and implement FATCA; 1 - Specified Association Agreement)
- Preamble of Indian treaties & Treaty shopping ?
- “Source” & “Residence”.
- Treaties by and large adopt UN model-source based taxation
- Pre-BEPS LOB article -USA & Singapore
- Beneficial Ownership -Dividend/ Royalty/ FTS.
- Treaty re-negotiation with Mauritius/Singapore/Cyprus/ UAE
- Introduction of GAAR, Equalisation levy, Significance Economic Presence, Limitation on Interest deduction, Income from patents
- Post BEPS new treaties/amendments - Indonesia, China, Belarus, Macedonia, San-Marino, Denmark, Czechoslovakia, Croatia.

# Overview of MLI: Preamble

- ❑ Economic activities & value creation.
- ❑ Swift, co-ordinated & consistent implementation of treaty related BEPS measures.
- ❑ Implement agreed changes in a synchronized & efficient manner to avoid double taxation.

# Overview of MLI – Minimum Standard

Subject of MLI	Brief description of the Article	India's final position	Impact Analysis
<b>Article 6: Purpose of CTA</b>	Avoid creation of opportunities for non-taxation or reduced taxation through tax evasion or avoidance, and through treaty shopping	India is <b>silent</b> on its position. Being minimum standard, such MLI provision to apply to all its CTAs	MLI Preamble will not replace the existing preamble but will only be added to the existing preamble text.
<b>Article 7: Prevention of treaty abuse</b>	Envisages following three anti-abuse measures to meet the minimum requirement: <ol style="list-style-type: none"> <li>A. PPT</li> <li>B. PPT supplemented with either SLOB or detailed LOB clause.</li> <li>C. Detailed LOB provision, supplemented by a mutually negotiated mechanism to deal with conduit arrangements not already dealt with in CTA</li> </ol>	India has opted for <b>PPT + SLOB</b> . PPT being minimum standard, it will apply to all its CTAs India has accepted to apply PPT as an interim measure and intends where possible to adopt LOB provision, in addition or replacement of PPT, through bilateral negotiations Not opted for competent authority route under Article 7(4) of MLI and thus, not applicable SLOB to be applicable only where other CTA partner has adopted it or allowed India to apply SLOB asymmetrically	<ul style="list-style-type: none"> <li>• MAP in case of dispute –how practical?</li> <li>• GAAR v/s PPT/SLOB</li> <li>• Treaty LOB v/s PPT.</li> </ul>
<b>Article 16: Mutual agreement procedure</b>	Requires MAP request to be made to either state, or implement a bilateral notification or consultation process	India has reserved its right for not adopting the modified MLI provisions on the basis that it will meet the minimum standard by allowing <b>MAP access in the resident state</b> and implementing <b>bilateral notification or consultation process</b>	<ul style="list-style-type: none"> <li>• Modification of all CTA's where there is no reservation</li> <li>• India's treaty with UK, Singapore, Netherlands &amp; France.</li> </ul>

# Overview of MLI - Residency

Subject of MLI	Brief description of the Article	India's final position	Impact Analysis
<p><b>Article 4:</b> <b>Dual resident entities</b></p>	<ul style="list-style-type: none"> <li>• CAs of both jurisdictions to mutually agree on the manner to determine the residential status of dual resident non-individuals regarding place of effective management, place of incorporation or constitution, and any other relevant factors.</li> <li>• In the absence of such agreement, treaty benefits to be denied to such a person (unless otherwise agreed by them)</li> </ul>	<p>India has <b>opted for application</b> of such provision; said provision to apply to all its CTAs (unless reservation is made by other CTA partner)</p>	<ul style="list-style-type: none"> <li>• Consequences for Indian MNC's – PoEM &amp; MLI.</li> <li>• Role of tax payer ?</li> <li>• Treaty with countries having reserved the right for Article 4               <ul style="list-style-type: none"> <li>○ France</li> <li>○ Sweden</li> <li>○ Luxembourg</li> <li>○ Switzerland</li> </ul> </li> </ul>

# Overview of MLI - Permanent Establishment.

Subject of MLI	Brief description of the Article	India's final position	Impact Analysis
<b>Article 12: Artificial avoidance of PE status through commissionaire and similar strategies</b>	Widens the definition of PE given in tax treaties to include cases where a person habitually concludes contracts or plays a principal role in conclusion of contracts of another enterprise	India has <b>opted</b> to apply the said provision; the said provision to apply to a CTA only if any other CTA partner has chosen to apply the said provision	<ul style="list-style-type: none"> <li>• Maintenance of records to prove independent activities at India &amp; modifications of contract undertaken outside of India.</li> <li>• E.g. Treaty with Netherlands &amp; France to be modified.</li> </ul>
<b>Article 13: Artificial avoidance of PE through specific activity exemptions</b>	Provides two options to counter artificial avoidance of PE status through specific activity exemptions. "Option A" states that exemption from PE is available only if the activities carried on are of preparatory and auxiliary nature. Additionally, it provides for anti-fragmentation rule	India has <b>chosen to apply Option A</b> ; the said option to apply to CTA only if other CTA partner has chosen same option. India has chosen to apply anti-fragmentation rule (under Para 4); the said rule to apply to a CTA only if other CTA partner has chosen to apply the said provision	<ul style="list-style-type: none"> <li>• E.g. Treaty with Sweden remain unchanged since Sweden has reserved rights for entire Article 13.</li> <li>• E.g. Treaty with Netherlands is modified to incorporate option A.</li> <li>• Treaty with France &amp; Singapore, only anti-fragmentation rule (under Para 4) to be applicable.</li> </ul>
<b>Article 14: Splitting up of contracts</b>	Addresses avoidance of PE by splitting the contracts between related enterprises to circumvent the threshold of PE creation	India is <b>silent</b> on its position; the said provision to apply to all its CTA (unless reservation is made by any other CTA partner)	<ul style="list-style-type: none"> <li>• Article 14 should be applicable to all of India's tax treaties where it's relevant treaty partner has also not specified a reservation, (e.g. Netherlands &amp; France).</li> <li>• Example of CTA's where reservation is made by other CTA partner               <ul style="list-style-type: none"> <li>○ UK</li> <li>○ Singapore</li> <li>○ Sweden.</li> </ul> </li> </ul>

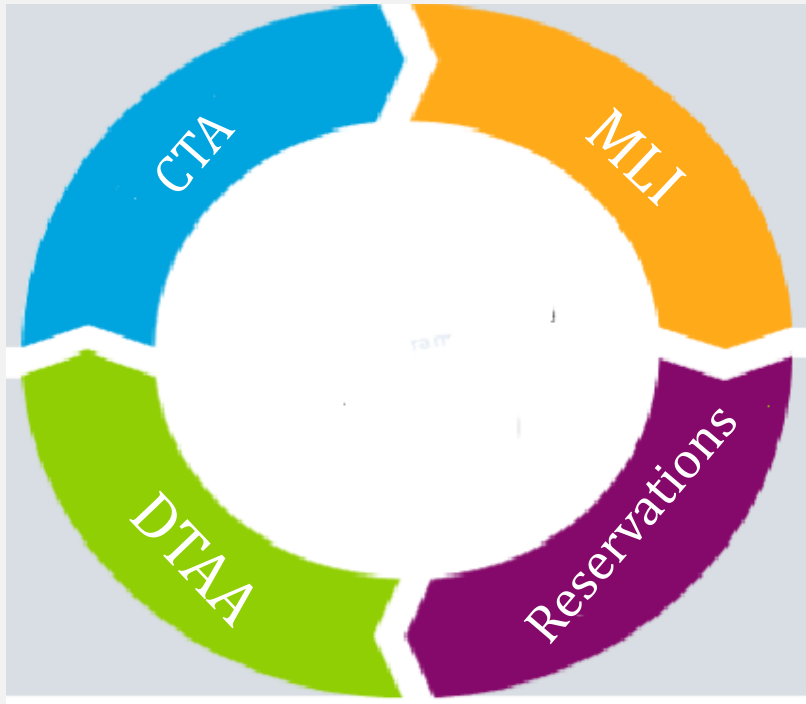
# Overview of MLI - Dispute Resolution (Not a Minimum Standard)

Subject of MLI	Brief description of the Article	India's final position	Impact Analysis
<b>Article 17: Corresponding adjustments</b>	Requires jurisdictions to make appropriate corresponding adjustments in transfer pricing cases	India reserves the right for the entirety of Article 17 not to apply to its Covered Tax Agreements that already contain a provision described in Article 17(2)	<ul style="list-style-type: none"> <li>• Article 17 not to apply to notified agreement for example               <ul style="list-style-type: none"> <li>○ Netherlands</li> <li>○ Ireland</li> <li>○ Switzerland</li> <li>○ UK</li> </ul> </li> <li>• India has not notified its treaties (e.g. Mauritius, France, Sweden) India-Sweden treaty will stand amended &amp; Article 17(1) will apply to India-Sweden tax treaty.</li> </ul>
<b>Article 18-26: Mandatory binding arbitration</b>	Provides mandatory binding arbitration in cases where competent authorities are unable to reach an agreement to resolve a case under MAP	India has <b>not opted</b> for mandatory arbitration	<ul style="list-style-type: none"> <li>• India has opted not to apply Arbitration to any of its CTAs this is ostensibly due to its concern about its sovereignty.</li> <li>• 25 countries has signed up for arbitration provisions in the MLI. Most have opted for option of 'final offer arbitration'.</li> </ul>



# MLI – Addition to Income Tax Statute

## Updated Tax Treaty Formulator



Lock



Key



Key hole



Article 4

Article 6(1)

Article 7(8)

Article 3(1)

Article 3(2)

Article 7(1)

Article 7(9)

Article 7(10)

Article 7(11)

Article 7(12)

Article 7(4)

Residence

Associated  
Enterprises

Non -  
Discrimination

# MLI – Addition to Income Tax Statute Cont'd

- ❑ Interplay with Income Tax Act
  - 90(2) – 90(2A)
  - Act vis-a-vis treaty read with MLI
  
- ❑ Treaty Entitlement / Qualification.
  - Pre – MLI
    - Resident
    - BO
    - Look at approach
    - TRC
  
  - Post – MLI
    - At Entity Level
    - At Income Stream Level
      - SLOB
      - PPT
  
- ❑ No tax rate under MLI.
  
- ❑ GAAR- Treaty LOB- PPT/ SLOB /DLOB
  
- ❑ Different Benefit - Article 7(4)
  - Benefit of other tax treaty covered in the structure (WHT rate & or scope)
  - Benefit of other jurisdiction's tax law covered in the structure?

## Preamble to MLI

# Inbound Investment Structures

- ❑ Compliance under Companies Act, FEMA, SEBI.
- ❑ Applicability of GAAR
  - “Main purpose of obtaining tax benefit”
  - 4 Tainted elements
  - Threshold -Rs 3 crores
  - FAQ
  - Grandfathering only with respect to income arising from investments before 31<sup>st</sup> March 2017.
  - Recharacterization of transactions /arrangements.
- ❑ Treaty specific benefits /concessions (Mauritius/Singapore/UAE) vis-a-vis MLI
- ❑ Treaty qualification at entity level.
- ❑ Hybrid Entity & Instruments
- ❑ ALP

# Inbound Investment Structures Cont'd

Dividend Income	Interest Income	Royalty Income	Business Income
<ul style="list-style-type: none"> <li>• No WHT under Income Tax Act - No impact of MLI.</li> <li>• DDT               <ul style="list-style-type: none"> <li>○ 115 BBDA vis-à-vis 10 (34)</li> <li>○ No advantage of tax treaty – No Impact of MLI</li> <li>○ Restricting DDT to rate of tax under relevant tax treaty                   <ul style="list-style-type: none"> <li>- Views?</li> <li>- Applicability of MLI</li> </ul> </li> <li>○ Credit of DDT to Non Resident Shareholders ?</li> <li>○ MLI?</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Taxation as per Income Tax Act - No impact of MLI.</li> <li>• Concession of Treaty availed – MLI applicable</li> <li>• Credit of Taxes by Non Resident – MLI?</li> </ul>	<ul style="list-style-type: none"> <li>• Rate of tax Income Tax Act v/s Treaty               <ul style="list-style-type: none"> <li>○ Identical</li> <li>○ or Treaty rate not considered</li> </ul> </li> <li>• Credit of taxes by Non Resident – MLI?</li> </ul>	<ul style="list-style-type: none"> <li>• No business connection in India or no operations in India- No treaty benefits – MLI ?</li> <li>• Business connection in India but no PE at India               <ul style="list-style-type: none"> <li>○ Taxed under IT Act , treaty benefit to eliminate double tax- MLI significant</li> <li>○ Tax benefit under treaty availed , MLI applicable</li> </ul> </li> <li>• PE in India               <ul style="list-style-type: none"> <li>○ Computation as per Act 7(1) -7(3) of the treaty ?</li> <li>○ MLI applied – Treaty benefits denied</li> </ul> </li> </ul>

# Inbound Investment Structures Cont'd

## Capital Gains on Sale of Shares

### To obtain treaty benefits

- Is Article 7(1) applicable?
  - Obtaining benefit was one of the principal purposes of transactions?
  - Check 6 (1) & 6 (3) – object & purpose of relevant treaty
    - Example India – France v/s India – UK Treaty.
  - Check 7(4)?
  
- Is Article 7(8) applicable ?
  - Check Article 7(9), 7(10), 7(11)
  - Check Article 7 (12)
  
- Computation of gain/ period of holding – Act v/s Treaty Grandfathering
  
- Treaty Grandfathering.
  - PPT under MLI applicable ?

### No treaty benefits availed

- No impact of MLI.

## Capital Gains on Sale of other Assets

- Assets situate in India
- Section 9 of Income Tax Act vis-a-vis MLI.

# Outbound Investment Structures

## Background

- ❑ Indian Company permitted to set up Foreign Company or through Subsidiary Company.
- ❑ Effect of POEM
- ❑ Compliance with the statutory requirements of FEMA, SEBI & Companies Act 2013.
- ❑ Overarching provisions of GAAR plus JAAR
- ❑ Grandfathering of structures upto 1<sup>st</sup> April 2017
- ❑ Treaty Residency & MLI.

# Outbound Investment Structures Cont'd

## Capital Gains

- ❑ No impact of MLI.
  
- ❑ Non Resident exempt from Capital Gain – Applicable for direct holding. (Subject to fulfillment of conditions) e.g. UK
  
- ❑ No Capital Gain under domestic law (e.g. Mauritius, Netherland, UAE, Singapore) – applicable for direct holding through subsidiary.
  
- ❑ At India - LTCG or STCG
  - 15% / 20% / 22%

# Outbound Investment Structures Cont'd

## Dividend & Underline Tax Credit (UTC)

- ❑ Exempt from Tax under Domestic Law of Foreign Company

	Direct Holding	Holding through Subsidiary Co
<b>With Holding Tax</b>	No	No
<b>UTC</b>	Yes*	Yes*^
<b>Tax at India</b>	15% 115BBD	

- ❑ Note:-

1. No impact of MLI for WHT
2. Tax u/s 115-0 vis-a-vis tax payable u/s 115BBD
3. Tax sparing clause – effect of MLI

\* Subject to domestic law provision ,CTA?, LOB clause restricting UTC ? (e.g. Mauritius , Singapore, UK)

^ Double Dip of UTC? (e.g. UK-Mauritius-India)



# Outbound Investment Structures Cont'd

## Dividend & Underline Tax Credit (UTC) Cont'd

- Taxable under Domestic Law of Foreign Company

	Direct Holding	Holding through Subsidiary Co
With Holding Tax	Yes	Yes
UTC	Yes*	Yes*^
Tax at India	15% 115BBD	

- Participation Exemption

- ATAD

- Consequences – holding Foreign Company through SPV (Indirect transfer of foreign company? MLI?)

*\*Check if no / reduced WHT under domestic law and relevant treaty. (e.g. Singapore, UAE, India – Netherland)*

*^Subject to CTA, LOB clause restricting UTC*

# Outbound Investment Structures Cont'd

## Interest Deduction.

- ❑ Income Tax Provisions
  - 36(1)(iii), 115BBD (Without Dividend Income ?)
  - 14A
  - Thin Capitalization
  - Transfer Pricing Provisions for declaration of dividend ?
  
- ❑ Impact of BEPS AP 4
  
- ❑ WHT by Foreign Company for payment to Indian Co.
  - Generally taxable under Domestic Tax Law
  - WHT rate prescribed under Indian Treaty
  - No impact of MLI (Subject to PPT, LOB)
  
- ❑ WHT by Foreign Company for payment to Subsidiary Company
  - Exemption under EU directives, Participation Exemption.
  - Group Taxation –Structuring Opportunities
  - No MLI (Subject to PPT, LOB)

# Outbound Investment Structures Cont'd

## Royalty and Management Fees.

- ❑ No impact of MLI – 'FIS'
- ❑ PPT rule under MLI
  - Income arising to Indian Parent ?
  - Income arising to SPV /Sub Co ?
- ❑ 115BBF- Tax @ 10% for Indian Resident
  - POEM rule consequences for SPV Co.
- ❑ No tax under domestic law (e.g. UAE)-Structuring Possibilities
- ❑ WHT- Treaty network subject to LOB/SLOB

# THANK YOU

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