www.pwc.in

The Multilateral Convention and BEPS
Investment in and from India

October 2017

pwc

Contents

Glossary

Abbreviation	Terminology
ALP	Arm's Length Price
BEPS	Base Erosion & Profit Shifting
BEPS report	OECD/G20 BEPS project report 2015
CA	Competent authorities
CJ	Contracting jurisdiction
CRE	Closely related enterprises
CTA	Covered Tax Agreement (tax treaty)
DA	Dependent agent
DAPE	Dependent Agent's Permanent Establishment
D-LoB	Detailed Limitation of Benefit
DRE	Dual Resident Entity
FTE	Fiscally Transparent Entity
FE	Foreign enterprise
HMA	Hybrid Mismatch Arrangement
ITL	Indian Income-tax Law
LoB	Limitation of benefit
MAP	Mutual agreement procedures
MLI	Multilateral Convention/Instrument
MNC	Multi-national Company
OECD	Organisation for Economic Cooperation and Development
OECD MC	OECD Model Convention
Parties	Contracting jurisdictions
PE	Permanent Establishment
PoEM	Place of Effective Management
PPT	Principle Purpose Test
P&A	Preparatory & Auxiliary
S-LoB	Simplified Limitation of Benefit
TE	Transparent Entity
UN	United Nations
UN MC	UN Model Convention
WHT	Withholding Tax

Introduction

The report on Action 15 of the BEPS project made it clear that it was not only feasible but also desirable to develop an MLI to amend treaties (of which there are more than 3,000 worldwide) in the least possible time and implement BEPS-related recommendations in treaties. This led to an ad hoc group of around 104 'working group' territories initiating work on the MLI.

On 24 November 2016, the OECD published a 49-page MLI as well as an accompanying 86-page explanatory statement. The MLI has two main aims—first, to transpose a series of tax treaty-related measures from the OECD/G20 BEPS into existing bilateral and multilateral treaties, and second, to set a new standard for mandatory binding arbitration on resolution of disputes pertaining to double taxation.

Several territories have signed up for the MLI since 1 January 2017, but a formal signing ceremony took place only on 7 June 2017. At this ceremony, 68 territories signed the document and another 9 committed themselves to signing up in the future. More are expected to join over time, and according to the OECD, it is likely to organise another official event before the end of 2017.

The MLI covers minimum standards and various other recommendations of Action 6 (on abuse of treaties) and Action 14 (on dispute resolution). It also includes some of the best practices of Action 2 (on hybrids) and Action 7 (on PEs), as well as new optional standard binding arbitration on cross-border treaty-related disputes.

The MLI is expected to enable the signatory parties to make a large number of changes in their existing treaties, whether these changes are based on the OECD or on the UN MC's recommendations, in order to give flexibility to countries. However, some of the territories may take advantage of the flexibility in the MLI and not implement or only partially implement some of the recommendations. While some options were included in the recommendations, a part of the flexibility is designed to enable parties to opt out of particular recommendations altogether or not apply them in individual treaties ('to accommodate specific tax treaty policies', according to the OECD's press release). The parties' provisional notifications of their intention to sign the MLI would better indicate their level of consistency in implementing the measures recommended by BEPS and whether the MLI will effectively achieve its goals.

Matching of counterparty responses, ratification by the concerned parties and the lag before the measures become effective means that taxable periods beginning in 2019 will most likely be the first to be affected by the MLI.

India is among the 68 countries that signed the MLI on 7 June 2017. It has published a provisional list of notifications and reservations, and listed 93 tax treaties, which it intends should be covered by the MLI. Signing of the MLI marks a significant milestone in the international tax scenario. The anti-abuse provisions in the MLI, such as the Principal Purpose Test and the minimum standards, will curtail 'treaty shopping' and abuse of tax treaties.

Signing of the MLI heralds the dawn of a new era with respect to taxation of cross-border transactions. Its implementation will have significant repercussions for Indian businesses, with cross-border operations and foreign investors keen on investing in India, and change the manner in which investments are made in the country and how these are structured. Most importantly, the MLI's minimum standards include denial of treaty benefits if the prime purpose of a transaction is only to avail of the benefits. From the business point of view, the manner of its subjective application is likely to lead to difficulties for businesses. Moreover, in addition to the prospect of these provisions raising the level of uncertainty for businesses structuring their operations, their applicability along with the recently introduced Indian General Anti Avoidance Rules (GAAR) may create further uncertainty.

In this report, we have elaborated on the technical aspects of the MLI, its interpretation, and the impact of India's positions on it from a business perspective as well as on Indian industry in general.

Modalities of the MLI

Construct of the MLI

As mentioned above, the MLI is divided into four main categories. It is further subdivided into various articles as follows:

Hybrid mismatch (optional)

- Transparent entities (Article 3)
- Dual resident entities (Article 4)
- Application of methods for elimination of double taxation (Article 5)

Treaty abuse (minimum standard)

- Purpose of **Covered Tax Agreements** (CTAs) (Article 6)
- Prevention of treaty abuse (Article 7)
- Dividend transfer transactions (Article 8)
- Capital gains from alienation of shares/interests of entities principally deriving value from immovable property (Article 9)
- Anti-abuse rule for PEs situated in third jurisdictions (Article 10)
- Application of tax agreements to restrict a party's right to tax its own residents (Article 11)

Avoidance of PE status (optional)

- Artificial avoidance of PE status through commissionaire arrangements and similar strategies (Article 12)
- Artificial avoidance of PE status through the Specific Activity Exemptions (Article 13)
- Splitting up of contracts (Article 14)
- Definition of a person closely related to an enterprise (Article 15)

Dispute resolution (minimum standard)

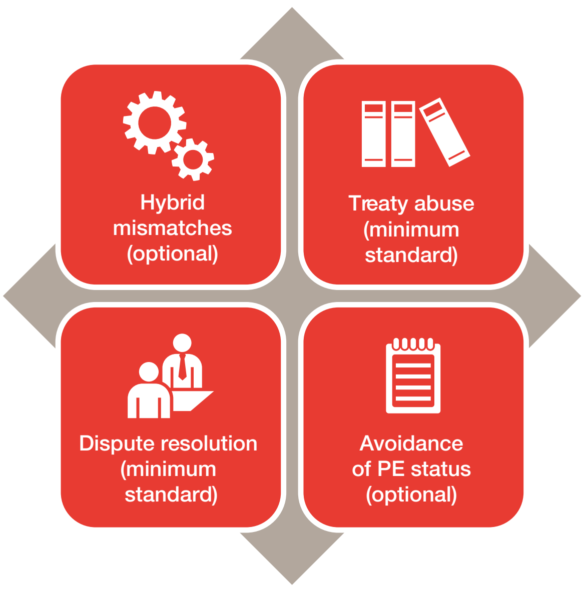
- Mutual agreement procedure (Article 16)
- Corresponding adjustments (Article 17)
- Commitment to mandatory binding MAP arbitration (Article 18 through 26)

Interpretation

Articles 3–17 of the MLI include most of its substantive rules and should be interpreted in accordance with the **normal** principle of interpreting treaties. According to this principle, a treaty is to be interpreted in good faith in accordance with the normal meaning of the terms of a treaty in a certain context and in light of its objective and purpose. (The compatibility clauses in individual articles also seek to explain how the MLI's provisions interact with existing treaty terms).

Framework of the MLI

Broadly, the MLI is structured under four categories—hybrid mismatches, treaty abuse, dispute resolution and avoidance of PE status. Of these, treaty abuse and dispute resolution are minimum standards that need to be complied with.



Covered parties

The MLI will only apply to countries that have signed and ratified it, in accordance with their domestic laws (where such ratification, acceptance or approval is required), and have deposited their instrument of ratification with the OECD's Depository (Depositary). The MLI will come into force from the first day of the month, following expiration of three months from the date on which five instruments of ratification have been deposited with the Depository.

CTAs

The MLI will not apply to all the tax treaties of signatories, but only to those where both the parties to a tax treaty have notified that it is covered. Such treaties are known as CTAs. It is the sole discretion of countries to decide on which bilateral tax treaties will be CTAs.

Notified CTAs and overriding of treaties

The MLI will be applicable to a tax treaty only if both the parties to it notify it as a CTA and if it does not override or substitute existing tax treaties that signatories have in place and now wish to have covered by the MLI. The MLI merely supplements and 'modifies' such treaties with a series of BEPS-related provisions, most of which each signatory can opt for or out, in whole or in part.

Minimum standards

A CTA is required to adhere to the minimum standards for certain core provisions—notably on treaty abuse and dispute resolution (but not binding arbitration that becomes mandatory when states agree to it, and not hybrids or PEs, which are optional inclusions). Parties to a treaty may also choose to opt out of a provision reflecting a minimum standard if they decide to reach a mutually satisfactory solution which is consistent with the minimum standard in some cases. Signatories to the MLI have been given the flexibility to opt out (by way of reservations) of provisions that do not set a minimum standard.

Whether a CTA (or any existing protocol) meets the minimum standard will be determined in the course of the overall review and monitoring process by the Inclusive Framework on BEPS (i.e., the countries that have signed up for the BEPS project and taken into account developing countries participating on an equal footing).

Compatibility-related clauses

The compatibility clause, which includes details of existing provisions that will be superseded, needs to be complied with if there is a conflict between an MLI provision and an existing provision in a tax treaty (that covers the same subject). Every country will need to determine the compatibility of the MLI's provisions with the existing provisions in its tax treaties.

Reservations

A party to the MLI may reserve its right that provisions of the MLI do not apply to its covered tax treaties in their entirety or a subset of its CTAs. Where one of the parties reserves the right that provisions of the MLI do not apply to one of its CTAs, the relevant provisions of the former will not apply to the latter, irrespective of whether the party's treaty partner has made a similar reservation. The MLI also generally provides in most articles that if a treaty partner neither reserves the applicability of a particular MLI article nor notifies the respective provisions, and does not state that the article is reserved in its entirety, this article will then be added to the CTA and will prevail over its relevant provision to the extent of the inconsistency.

Optional provisions

Unlike in the case of reservations, both the treaty partners are required to choose the same option in order for it to apply. In the event one treaty partner chooses a particular option and the other elects to apply a different one or no option at all, then none of the options will apply to the relevant CTA.

Notifications

In the event an MLI provision supersedes or modifies an existing provision of a CTA, the parties will be required to send a notification specifying the CTAs that include such provisions and identify these.

The notifications help to simplify and clarify the modifications needed when existing treaties are examined. However, there will still need to be a process for 'matching' what all parties notify, before one can be sure about application of a modification.

The OECD is responsible for these matters and has already facilitated discussions between the territories. However, we do not expect to see confirmation of the matches on its website for some time.

Note: PwC's MLI tracking tool gives an indication that additional work may still be needed on this and adjustments will need to be made by territories to agree on positions before ratification or the territories will have to accept that some of them have chosen to make modifications and others have not. Consequently, there can be no agreement on modification until a separate protocol is agreed on or a treaty is renegotiated.

Date of applicability

The MLI will only come into force on receipt of the instrument of ratification and its acceptance by or approval from five countries. It will be applicable from the first of the month following completion of three calendar months (beginning from the date of deposit of the fifth instrument). For example, if four signatory countries deposit the instrument before October 2017 and the fifth country does so on 6 October 2017, the MLI will come into force for this country from 1 February 2017. In the case of other signatories that deposit instruments subsequent to the fifth instrument, the MLI will come into force from the first of the month following completion of three calendar months beginning from the date of deposit of the instrument. For example, in the example mentioned above, when the fifth instrument is deposited on 6 October 2017 and the MLI has come into force from 1 February 2018, if a country deposits its instrument on 10 November 2017, the date on which the MLI for the country will come into force will be 1 March 2018.

India has expressed its reservations with regard to the standard language used for entry in the MLI and has chosen to apply the alternative language suggested in it, which makes the date on which it comes into force for the country subject to a procedure that is applicable on a treaty-by-treaty basis. Since India has opted for this rule, it will apply to the MLIs coming into force for all its notified treaties—for India and all its treaty partners.

The effective date of applicability for each of India's notified treaties will be determined as follows:

- **For taxes withheld at source:** The MLI will apply if the event giving rise to such taxes occurs on or after the first day of the 'taxable period' that begins on or after 30 days from the date of the latest notification by each country that it has completed the internal procedures for the entry to the MLI to come into effect for a particular treaty.
- **For other taxes levied by countries:** The MLI will apply with respect to other taxes levied for taxable periods beginning on or after the expiration of six calendar months, 30 days from the date of the latest notification by each country that it has completed the internal procedures for its entry to the MLI to come into effect for the particular treaty.

Impact of signing the MLI on India

Signing of the MLI by India is not 'final', since this is the first step in the process. On completion of domestic procedures, if any, with regard to the MLI, India will have to deposit an instrument ratifying it. Only on depositing this instrument can its entry into the MLI come into force. Currently, India has only provided a provisional list of reservations and notifications. Along with its ratification of the MLI, it will also need to submit a list of its final positions.

The MLI will either change or not change a notified treaty, based on a combination of reservations and notifications submitted by the treaty partners. For each MLI provision, India's position will need to be checked as well as the positions adopted by its treaty partners. The impact of the proposed article on the relevant treaty will be determined based on this. A choice made by a country for a particular provision of the MLI will also be treated as its choice for a CTA and will be applicable to the latter, depending on the choices made by its treaty partner(s).

The MLI will not have an automatic impact on subsequent treaties entered by India, which along with its treaty partners will need to submit a notification to cover subsequent treaties under the MLI. Under the MLI, it is possible to withdraw reservations either entirely or replace them with limited reservations. This can be done by sending a notification to the Depository.

Application of the MLI

The steps detailed in the following table will need to be applied to assess the impact of the MLI:

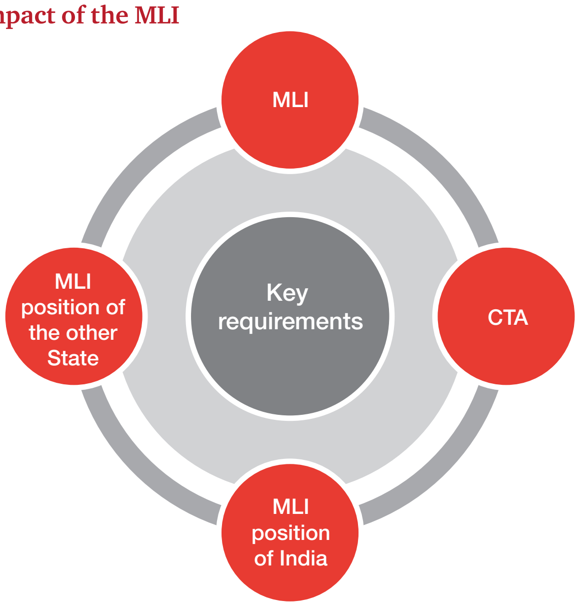
Step-wise process for application of the MLI

Step 1: Check whether the MLI has come into force.	
1. Is the MLI in force?	• If not, the MLI will not apply. • If yes, move to point no. 2 below.
2. Is the MLI in force for both the parties to the CTA?	• If not, the MLI will not apply. • If yes, go to step 2 below.

Step 2: Check whether the treaty is a CTA.	
1. Do both the parties list the tax treaty as an agreement to be covered by the MLI?	• If not, the MLI will not apply to the tax treaty. • If yes, go to point no. 23 below.
2. Is the tax treaty already in force?	• If not, the tax treaty will be a CTA after its entry comes into force. • If yes, the MLI will apply to the CTA – proceed to step 3.

In order to assess the impact of the MLI on different tax treaties, the MLIs will need to be 'read' with the CTAs as well as India's stated positions and reservations, and those of other countries.

Key requirements for assessment of the impact of the MLI



Step 3: Identify specific article of the MLI that applies to the CTA.	
1. Has one of the parties to the CTA made any reservations[1] on the application of an article of the MLI?	• If not, the MLI will not apply. • If yes, move to point no. 2 below.
2. Have both the parties to the CTA chosen to apply an optional[2] provision of the MLI?	• If not, the MLI will not apply. • If yes, go to step 2 below.

Step 2: Check whether the treaty is a CTA.	
1. Do both the parties list the tax treaty as an agreement to be covered by the MLI?	• If not, the MLI will not apply to the tax treaty. • If yes, go to point no. 23 below.
2. Is the tax treaty already in force?	• If not, the tax treaty will be a CTA after its entry comes into force. • If yes, the MLI will apply to the CTA – proceed to step 3.

[1] Any reservations made by a party to the CTA vis-à-vis an article of the MLI generally prevents the application of the such an article, irrespective of the fact that the other party to the CTA has not made any such reservation.

[2] Generally, both the parties are required to choose to apply the same optional provision in order to apply the provision to the CTA.

Step 4: Identify which of the existing provisions of the CTA have been modified.	
1. The MLI article applies 'in place of' an existing article in the CTA.	• The article in the CTA is replaced with the MLI article if parties to the CTA have notified their existing articles. • The MLI article does not apply if the parties have not notified the same article to the CTA and there is a mismatch.[3]
2. The MLI article "modifies" an existing article in the CTA.	• The MLI article changes application of an existing article of the CTA without replacing it when the parties to the CTA have notified the same existing article. • The MLI article does not apply if parties have not notified the same article to the CTA and that there is a mismatch.
3. The MLI article applies "in the absence of" an existing article in the CTA.	• The MLI article is "added" if both the parties to a CTA have notified the absence of an existing provision in it. • The MLI article does not apply in the event of a mismatch.
4. The MLI article applies "in place of or in the absence of" an existing article in the CTA.	• Existing articles in the CTA are replaced by the MLI article if both the parties to the CTA have notified the same existing article. • The MLI article applies and supersedes the existing articles in the CTA to the extent of their incompatibility in the event of a mismatch. • The MLI article applies and supersedes the existing articles of the CTA to the extent of their incompatibility (i.e., the MLI article will be added) if neither of the parties have notified an existing article in the CTA.

Step 5: Verify whether the MLI articles are effective.	
1. With respect to withholding taxes	• Regarding the latest date on which the MLI comes into force for each of the parties, go to the first day of the next calendar year.
2. With respect to all other taxes	• Regarding the last date on which the MLI comes into force for each of the contracting jurisdictions, the expiration period is six months.

[3] A mismatch would either mean that one of the parties to the CTA has notified an existing article but the other has not, or that the parties to the CTA have made a different notification with respect to existing articles in their MLI positions.

India's perspective on the MLI

Transparent Entities (TEs)

Based on the MLI, an income derived by or through a TE under the domestic tax laws of the parties' territories will be considered the income of a resident of either of the states, but only to the extent that this income is liable to tax in the residence state. This provision is based on OECD's report on TEs and is intended to ensure that benefits are granted in appropriate cases. However, the provision is not a minimum standard and parties can opt out of it.

India has reserved its right on non-applicability of the provisions relating to TE, and accordingly, will not grant treaty benefits to a TE (irrespective of the position taken by its partners). India's tax treaties do not generally include a provision on treatment of TEs (except in the India-US and India-UK tax treaties).

Comments

Generally, a partnership does not need to comply with the 'liable to tax' requirement in order to be eligible for treaty benefits to the extent that the partnership is treated as transparent in its jurisdiction of formation, and income is not taxed in the hands of the partnership. However, treaty benefits should be available to the extent the partners of such a TE are subject to tax (in their residence state) on the same income.

India's position is that neither a TE nor a partner is entitled to a treaty benefit, since the country follows the entity-level approach to taxation. However, treaty benefits are provided to the TE or its partners, but only if a treaty explicitly provides for this, e.g., under the India-US and India-UK tax treaties.

Indian courts have taken varying positions on this subject. For instance, a court has held that since Linklaters LLP[4] and Clifford Chance[5] hold a UK partnership and the partners were subject to tax in the country, they are eligible to claim the benefits of the India-UK treaty. However, in Schellenberg Wittmer,[6] the Authority for Advance Rulings (AAR) took a contrary view and held that a Swiss general partnership was not entitled to treaty benefits since it is a TE.

In light of the above, TEs may continue to face challenges in claiming treaty benefits, and this could result in double taxation, wherein India may subject the payment to a TE to a WHT, while the resident state may not grant a credit.

Dual Resident Entities (DREs)

The CA determines whether a person (other than an individual), i.e., companies, LLPs or other incorporated entities, is to be considered a resident of one or more states. For this purpose, it will need to consider its PoEM, where it is incorporated or has been constituted and any other relevant factors. Where the CA is unable to determine the place of residency, such a person will not be entitled to the treaty benefit.

India has adopted this standard for all its CTAs.

Comments

The tax treaty benefit is available to persons who are 'liable to tax' in a state because of their domicile, residence, place of management or similar criteria. And while it is possible for persons to qualify as residents of one or more states, in order to avoid potential double taxation, most tax treaties mandate their taking the PoEM test as a tie-breaker to determine the state in which they should be a resident.

Hitherto, a foreign company was considered a tax resident in India if control and management of its affairs was wholly carried out in India. However, India has recently introduced PoEM, effective from 1 April 2016, to determine the residence of corporate entities and has explicitly defined it to mean a place where key management and commercial decisions necessary for the conduct of their entire businesses are taken.

While the OECD's Commentary (amended by Action Plan 6) states that countries should take into account (a) where a person's board of directors or equivalent body generally meet, (b) where the CEO and other senior executives usually carry out their activities, (c) where its day-to-day senior management activities are conducted, (d) where its headquarters are located, (e) which countries' laws govern its legal status and (f) where

[4] 132 TTJ 20
[5] 82 ITD 106
[6] 210 Taxman 319

its accounting records are kept, etc.. India's domestic PoEM test prescribes an active and passive income test that is usually only applicable in the context of certain anti-avoidance measures. The country's position on the MLI is likely to have significant ramifications for Indian MNEs with operations outside India, since these are now aligned with domestic tax law-related requirements. However, it seems unlikely that treaty partners will agree to the dual residence of a taxpayer being resolved in favour of India just because it meets the requirements of the PoEM tests in its domestic laws. The manner in which the CA will address this issue remains to be seen.

In this context, provisions under some Indian tax treaties should be noted. For example, the India-Finland tax treaty provides that the state of residence of a person (other than an individual) will be determined by the CA by mutual agreement with regard to the person's place of incorporation, PoEM and any other relevant factors. This is similar to the MLI's provisions.

Many of India's tax treaties, such as the India-UK tax treaty, provide that if a non-individual is a resident of both the states, it will be deemed to be a resident of the state in which its PoEM has been constituted. However, with the POEM rule included in the ITL to determine residency, there could be disputes on how the PoEM rule in a treaty should be interpreted. In such cases, adoption of the MLI may be preferable, since it provides for expanded criteria for the CA to agree on a single jurisdiction of residence. However, there could be significant time expended and costs incurred in accessing a MAP. Furthermore, in such cases, denial of treaty relief in the absence of a mutual agreement could be disadvantageous. The UK and the Netherlands have chosen to apply Article 4 of the MLI to their CTAs and have notified India. In addition, they have applied the new MAP process to resolve dual residency-related disputes.

According to the India-Japan tax treaty, if a person is a resident of both the contracting states, the state of the resident will be determined by the mutual agreement of the CAs of the two states. Japan has notified its treaty with India and has reserved the right to modify the language of Article 4(1)—that no benefits under its CTAs will be granted in the absence of an agreement on a single state of residence.

According to India's tax treaties with South Africa, Ireland, Luxembourg, Norway and other countries, if the resident state of a person (other than an individual) or the state in which its POEM is constituted cannot be determined, the question will be settled by the CA.

France, Sweden, Luxembourg and Singapore have reserved this Article, and accordingly, the existing tie-breaker in India's tax treaties with these countries remains unchanged. Therefore, PoEM will continue to apply in dual residence cases.

In the case of FPI investments, the residential status of collective investment vehicles is adjudged based on that of its investors or stakeholders, and tax implications apply accordingly. This will be a difficult provision to comply with in the event of a change in ownership patterns and may result in denial of treaty benefits to these investment vehicles.

Methods for eliminating double taxation

The MLI provides alternative ways to eliminate double taxation arising from inclusion of the Exemption Method in treaties with respect to income that is not taxed in the source state.

The MLI recommends the following three options a party can choose to apply:

- **Option A: The switchover clause:** An exemption in one country will not apply if the other country applies the treaty to exempt income or reduce the tax rate. Instead, the country should allow a deduction for the tax paid in the other country. However, please note that the deduction will be restricted on the basis of the net income.
- **Option B:** The exemption will not apply to dividends that are tax-deductible in the other country because a deduction is only allowed for tax paid on a net basis.
- **Option C:** This option relates to all types of income that is taxable in the other country. This restricts credit granted on the basis of the net income.

India has not adopted this Article for any of its CTAs, and therefore, this provision will not affect any of its tax treaties. It will continue to grant tax credits in accordance with its existing tax treaties. Credits including underlying tax credit and tax 'sparring' are likely to continue to be available under India's existing tax treaties.

Preamble

Article 6 includes a minimum standard for a treaty to have a suitable 'preamble', excluding its use to reduce taxation through tax evasion or avoidance, or treaty shopping (artificially using conduit entities to structure arrangements in order to obtain treaty benefits). The MLI mandates default wording to be applied as a modification of the existing preamble.

Preamble:

Intending to conclude a convention for the elimination of double taxation with respect to taxes on income and on capital 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 Convention for the indirect benefit of residents of third states) (not optional)

and

Desiring to further develop their economic relationship and to enhance their co-operation in tax matters (optional)

India has not taken any position on this provision. Since Article 6(5) of the MLI stipulates that the language used in the provision will be included in that of the existing preamble, and that even if the language used in existing treaties is not notified to the Depository, the language used in the preamble should be included in all India's treaties.

The addition of this provision will make a significant impact on interpretation of the 'object and purpose' of tax treaties. However, the additional content in the optional preamble provided in the MLI on economic relationships and enhancement of cooperation will not be added to India's CTAs.

Comments

In the Cyril Eugene Pereira case[7] in the context of the India-UAE tax treaty, the AAR held that the provisions of the tax treaty do not apply to a case if the same income is not liable to be taxed twice by the existing laws of both the states. Since there is no law in force in the UAE that makes income liable to tax, taxpayers cannot claim relief on account of double taxation unless there is a corresponding tax law in force in the country in respect of their income, which is taxable in India.

In the Azadi Bachao Andolan case,[8] the Supreme Court referred to the preamble to the India-Mauritius tax treaty, which provides for "encouragement of mutual trade and investment" and held that entitlement of treaties is consistent with India's intentions at the time it entered the tax treaty with Mauritius. According to the Supreme Court, there are many principles in fiscal economy, which though at first may appear to be "evil", are tolerated in a developing economy in the interest of its long-term development. (In our view, deficit financing is one and treaty

[7] [1999] 105 Taxman 273 (AAR - New Delhi)
[8] 263 ITR 706

shopping is another). However, despite the sound and fury of the respondents over the so-called 'abuse' of 'treaty shopping', perhaps this may have been intended at the time the Indo-Mauritius tax treaty was finalised. Whether this should continue, and if so, for how long, is a matter that is best left to the executive, since it is dependent on several economic and political considerations. The Supreme Court cannot judge the legality of treaty shopping merely on the ground that a section of people consider it improper. A holistic view needs to be taken to adjudge what is important in contemporary thinking as a necessary evil in a developing economy.

The preamble of the MLI is likely to have a significant impact on interpretation of the position approved by the courts, since it has a specific provision for prevention of tax evasion through treaty shopping.

Treaty abuse

According to the MLI, Article 7 applies to prevention of treaty abuse and relates to the BEPS minimum standard to include (a) a PPT, (b) a D-LOB), an Anti-conduit Rule, and (c) a PPT and an LOB, but this could be an S-LOB.

A territory can opt out of the default option if it wants to comply with the minimum standard another way. (The MLI does not include a D-LOB, which is developed separately.) At the time of signing the MLI, all 68 signature territories chose to apply the PPT. India opted for application of the S-LoB provisions in its CTAs and will follow the PPT approach in addition to the S-LOB.

Comments

India has opted to apply S-LoB as a supplement to the PPT rule. It is important to note that the S-LoB only applies to a CTA when the other party has opted to apply it. If one party applies the S-LoB and the other does not, only the PPT rule (and not the S-LoB) will apply.

The S-LoB applies to the "Qualified Persons" of a state. The term Qualified Persons includes (a) individuals, (b) political sub-divisions and local authorities thereof, an agency or instrument of the state, a political subdivision or local authority, (c) listed companies or other entities and (d) persons other than individuals if on at least 50% of the days of the 12-month period during which the benefits were sought, at least 50% of the shares were owned, directly or indirectly, by Qualified Persons.

A taxpayer involved in active conduct of business will not be required to fulfil the Qualified Person threshold to avail treaty benefits as long as the income it earns from the other state emanates from or is incidental to its business. Furthermore, if such a taxpayer derives income through business activity conducted in the other state, either on its own or through a connected person, this business activity in the residence state should be substantial in relation to the same or complementary business activity it conducts in the other state. The following activities will not be included in the term "active conduct of business" if a taxpayer is (a) operating as a holding company, (b) providing overall supervision or administering a group of companies, (c) providing group companies services including cash pooling or (d) making or managing investments, unless these activities are conducted by a bank, insurance company or registered dealer of securities in the ordinary course of its business.

Under the MLI, the specified wording of the PPT is added by default in the absence of an existing purpose test. It replaces any existing content of a similar nature, whether this only applies in relation to dividends, interest or royalties, or specifies procedural requirements such as notification or consultation between CAs. A territory can opt out of the default if it intends to meet provisions of the minimum standard another way. (The MLI does not include a detailed LOB, which is developed separately). At the time they signed the MLI, all the 68 signature territories chose to apply the PPT. In addition, territories may choose to apply an S-LOB. Including India, 12 territories expect to do this. There is a further provision for taxpayers to make a request for application of benefits, even if they fail to meet the PPT. However, inclusion of its wording and its interpretation are left to the option chosen by individual territories.

Since India is only one among the 12 countries to have opted to apply S-LoB, only a PPT is likely to apply to its CTAs, since it has not chosen a reservation to negotiate a detailed LOB with its treaty partners (who have not chosen S-LoB).

The PPT rule could be broader in its ambit than GAAR under the ITL, since GAAR is only triggered if the main purpose of an arrangement is to obtain a tax benefit. Furthermore, in order for GAAR to be triggered, one of the other 'tainted' elements also needs to be satisfied, i.e., creation of rights or obligations that are not at arm's length, abuse of the ITA and lack of commercial substance or bona fides. Therefore, it is unlikely for GAAR to apply if the PPT rule is met. It is yet to be seen how the interplay between GAAR and the PPT rule will pan out in the treaties.

Countries that have favourable tax treaties with India make substantial investments in the country. To counter tax treaty abuse, BEPS has introduced its minimum standards, which require implementation of the PPT rule, which can have an impact on intermediate holding structures or investment

holdings without adequate substance. Investors will therefore need to review their group structures in order to invest in India.

Dividend transfer transaction

The MLI has inserted an Article that requires a 365-day minimum holding period before entities can benefit from the exemption (e.g., in the case of pension funds) or a preferential rate of Dividend Withholding Tax that depends on the level of shareholding in the paying entity (i.e., the direct holdings rate). The sole purpose of the provision is to introduce a minimum shareholding period without modifying elements such as tax rates, ownership thresholds and form of ownership (directly or indirectly).

India has made a reservation that the provision will not apply to CTAs that already include provisions with a minimum holding period that is longer than a 365-day period. This article will not affect distribution of dividends, since India levies a Dividend Distribution Tax on Indian entities distributing their dividends.

Capital gains – immovable property

Article 13 (4) of the OECD MC provides that capital gains arising from alienation of shares that derive more that 50% of their value from immovable property may be taxed in the country in which such property is located.

Article 9 (4) of the MLI introduces a 365-day period for testing if an entity has been deriving a value of more than 50%, and preventing it from avoiding the typical treaty rule that preserves the right of a jurisdiction to tax capital gains on shares (or comparable interest) deriving value from local immovable property. India has opted to apply Article 9(4).

Comments

Most tax treaties give the source state the right to tax gains derived from alienation of shares valued at over a certain threshold value, directly or indirectly from immovable property in the source state (Article 13(4) of the OECD Model). The relevant threshold value needs to be exceeded on the

date of sale of shares. However, it may happen that shortly before sale of shares, assets are contributed to an entity in such a way that its shares do not derive more than 50% of their value from immovable property. To manage this issue, the MLI provides that the relevant value threshold can be met at any time during the 365 days preceding a sale, thereby enhancing the rights of the source country. Furthermore, in addition to companies, this condition also applies to shares or interest in partnerships or trusts.

Currently, the time limit of a relevant threshold is not mentioned in any of the tax treaties signed by India. Since the Article seeks to cover a country's interest in a partnership or trust, it needs to be seen how this will be applicable for investments in units of REITS or InVITs set up under a trust or an interest under an LLP structure. Article 9(4) only applies to tax treaties where both the parties have notified the Depositary of their choice regarding use of this provision. The existing provision of CTAs will be superseded by Article 9(4) (to the extent of incompatibility), even if the other party to a CTA has chosen to apply Article 9(4), but has not notified the relevant CTA provisions. However, this provision will not apply if the other party has made a reservation.

According to the provisional notification, Article 9(4) has not been adopted by countries including Canada, Cyprus, Luxembourg, Singapore and the UK, while countries such as France, Japan and the Netherlands plan to adopt these provisions.

PE – triangular situation (third state)

The MLI provides that treaty benefits will be denied if an item of income derived by a treaty resident and attributable to a PE in a third jurisdiction is exempt from tax in the resident state, and the tax levied in the PE's jurisdiction is less than 60% of the amount that would have been imposed in its resident state if the PE were located there.

The optional model provision under Action 6 of the BEPS report includes a reference to the tax rate to be determined bilaterally. This relates to the conditions for denial of tax treaty benefits. It provides that these benefits will not apply to any item of income on which the tax rate in the third jurisdiction in which an exempt PE is located is less than "the lower of [rate to be determined bilaterally] and 60% of the tax that will be imposed in" the residence jurisdiction of the enterprise.

To avoid bilateral negotiation of a tax rate in the MLI, the provision solely relies on the 60% test and compares the tax actually paid in the PE jurisdiction with the tax that would have been imposed in the residence jurisdiction if the taxpayer's income had not been exempted.

India has not opted for any notification or reservation on this Article of the MLI. In this scenario, this Article will only apply to treaties where the other state has also not opted for any reservation or notification.

Some of India's treaties that are affected by this rule include those with Fiji, Israel, Japan, Romania, Russia, Spain and Mexico.

PE – commissionaire arrangements

The MLI covers two types of agencies—a dependent agency and an independent agency. The concept of each of these has been elaborated on below:

Dependent agency: A common test for DAPE) is its "authority to conclude contracts" and its "habitual exercise" of this authority. The MLI expands the scope of a DAPE and includes the phrase "if the agent habitually concludes contracts or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise…."

Independent agency: A person acting in an independent capacity in its ordinary course of business is not eligible to be considered a DAPE. However, when such a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, it will not be considered an independent agent.

Closely related enterprises have been defined as a single entity with control of another entity or a common person with control over the entities. If one enterprise owns, directly or indirectly, more than 50% of the beneficial interest in the other enterprise (or in the case of a company, more that 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in it) or a person holds such an interest in both the entities, this should be treated as being closely related.

India has chosen to opt for this option in all its CTAs. However, this provision is only applicable to CTAs if the other party agrees to do the same.

Comments

Most of India's tax treaties use the phrase "authority to conclude a contract." Judicial precedents in the country have interpreted the term as having the "authority to conclude a contract" if a person has the authority to negotiate all the elements or details of a contract, "bind" a foreign enterprise in its business activities and decide the final terms of the contract.

However, it is relevant to note that India's position on the OECD's Commentary has been that if a person has attended or participated in negotiations in a state, such a person can (in certain circumstances) be sufficient by itself to conclude that it has exercised the authority to conclude contracts in the name of the enterprise. Furthermore, a person authorised to negotiate the essential elements of a contract (and not necessarily all its elements and details) on behalf of a foreign enterprise can be said to be exercising its authority to conclude contracts.

Consequently, the phrase "authority to conclude a contract" is widely interpreted by Indian courts in line with the OECD's Commentaries and the position taken by India.

Therefore, irrespective of changes mandated by the MLI, India's existing tax treaties with other countries are interpreted broadly.

The MLI proposes to include the phrase "or habitually plays the principal role leading to conclusion of contracts that are routinely concluded without material modification by the enterprise". Although the term "principal role" has not been defined or explained in the MLI, one can draw a reference from Action 7 of the BEPS report, which includes a commentary to aid its interpretation.

In India's tax treaties, an agent is generally not considered to be independent in the following scenarios:

- The agent works wholly or almost wholly for an enterprise, i.e., the principal, and the conditions are not at arm's length.
- Its activities are only performed for one or more related principals (e.g., the India-Australia or India-Belgium tax treaties).

The arm's length condition is not provided for in the MLI, and therefore, it needs to be evaluated whether its condition is met. This may not help closely related enterprises avoid being accorded a dependent agent status. Therefore, a foreign enterprise, with agents being closely related enterprises that work in India on the arm's length condition, will need to re-evaluate their PE exposure.

Entities that play a leading role in concluding contracts between a foreign enterprise and Indian customers (although without any authority to conclude contracts) and entities engaging distributors (including companies using subsidiaries for marketing functions) also need to revisit their existing models.

[9] The AAR in the case of K.T. Corporation, In re [2009] 224 CTR 234 (AAR)

PE – exemption from specific activities

In this regard, there are two options provided in Article 13 of the MLI:

- Option A explicitly states that activities listed under Article 5(4) of the OECD's MC (or a combination of two of these) need to be preparatory or auxiliary activities on a stand-alone or overall basis to qualify for an exemption to constitute a PE.
- Option B provides that activities included in Article 5(4) of the OECD MC need not be preparatory or auxiliary in nature on a stand-alone basis. And furthermore, any other activity should be preparatory or auxiliary, provided it is conducted at a fixed place of business.

However, the overall activities (combination of such activities) need to be preparatory or auxiliary in nature to be eligible for exception to be granted for specific mandatory activities. Furthermore, the complementary functions of an enterprise or closely related enterprises (that are a part of a cohesive business operation) can be considered together to determine whether such activities can be said to be "preparatory or auxiliary" in nature.

India has opted to apply this provision with Option A for its CTAs, and has thereby created an overall requirement for each exempted activity to be of a preparatory or auxiliary nature. However, this provision is only applicable to CTAs where the other party also chooses this option.

Comments

Activities specified in Article 5(4) of the OECD's MC, such as storage, display, delivery and processing facilities, form a separate and indispensable part of the business activities of a foreign enterprise and are not merely activities of a preparatory and auxiliary nature.

The activities specified in Article 5(4) of the OECD's MC may result in a PE, even if those mentioned in the tax treaties do not specify the condition of their being "preparatory" or "auxiliary for foreign enterprises.

India's Authority for AAR held[9] that if a foreign enterprise, whose primary purpose is collection of information, performs such activities in India, Article 5 (4) (d) of the India-Korea treaty is inapplicable for them because collection of information is not "preparatory" or "auxiliary" in nature in the case of such enterprises.

A foreign eCommerce business with warehouses in India, with a significant number of people or other functions carried out in the country, may not be eligible to claim exclusion from establishing a PE on the basis that its place of business is solely for storage or delivery of goods (since India has adopted Option A above).

PE – fragmentation of activities

The OECD's commentary on Article 5(4) of OECD MC in the case of what has been referred to as "fragmentation of activities" states that an enterprise cannot fragment a cohesive operating business into several small operations to argue that each is merely engaged in a preparatory or auxiliary activity.

Under the MLI, anti-fragmentation means that exception from specific activities will not apply if an enterprise or a related enterprise carries on business activities at the same place or another place, and that place or other place constitutes a PE, or if the overall activities of the two places in combination are not preparatory or auxiliary in nature.

However, these are not mandatory provisions under the MLI and India has not articulated its position on them. Since it has not placed a reservation on this provision, the provision should apply to all its CTAs, except if a treaty partner signatory has placed a reservation.

[10] ADIT vs. Valentine Maritime (Mauritius) Ltd.(2011) 45 SOT 34 (Mumbai)

Comments

Incidences of enterprises avoiding a PE status by fragmenting or splitting up their activities between their different places of business, closely related enterprises or by entities operating cohesive business operations are now being 'plugged' with this Article.

Some of India's tax treaties with countries such as Finland, France, Germany, Korea, Luxembourg, the Netherlands, Switzerland and the UK provide that if a fixed place of business is maintained to conduct a combination of activities, the overall activity resulting from this combination should be of a preparatory or auxiliary nature.

Furthermore, Article 13(4) of the MLI mandates that an enterprise or a group of closely related enterprises cannot fragment a cohesive operation into several small operations while arguing that each is merely engaged in a preparatory or auxiliary activity.

Therefore, in order to evaluate an enterprise's PE exposure, there is a need to check whether business activities conducted by two enterprises at the same place, or by the same enterprise or closely related enterprises at two places, constitute complementary functions that are part of a cohesive business.

PE – splitting up of contracts

Article 14 of the MLI addresses a situation where contracts are divided into multiple parts to avoid application of a time period (the threshold period) in relation to the existence of a PE for specific projects or activities, i.e., building site or construction, installation or other specified project of a particular enterprise (project site).

Article 14 of the MLI includes a new anti-contract splitting rule, which will apply to deemed PE provisions for building sites, construction or installation projects. To assess whether the specified time period to constitute a deemed PE has been exceeded, 'connected activities' that are conducted by closely related persons at the same site or project during different periods of time (that each exceed 30 days) must be added to the aggregate period of time that a foreign enterprise has also conducted activities at the site or project.

This rule does not need to meet a minimum standard, and a country may reserve the right to not apply this rule with respect to its tax treaties.

India has not articulated its position on this provision. And since it has not placed a reservation on it, the provision should apply to all its CTAs, except where a treaty partner signatory has placed a reservation.

Comments

This new rule will require enterprises engaged in or consulting on inbound building construction or installation projects to re-examine the way they determine the PE status of such projects when 'closely related enterprises' are also involved in these.

This provision is particularly relevant for the construction industry and entities involved in EPC activities. Currently, the OECD Commentary (2014 version, paragraph 18) and the UN Commentary (2011 version paragraph ii) provide that domestic anti-avoidance legislative or judicial rules may be applied to prevent schemes that artificially avoid the relevant threshold.

A judicial precedent in the context of Article 5(3) of the India-Mauritius tax treaty provides that a series of contracts entered by a contractor that are interdependent, both commercially and geographically, should be treated as a single unit for application of the threshold test.

Some of India's tax treaties, such as those with Australia, China, Denmark, Italy and the US, specifically provide that the time spent on other sites or projects should also be considered while determining the time threshold for a PE. Such clauses in these tax treaties may not be adversely affected by the MLI provision.

MAP

According to Article 16 (1) of the MLI, if a person considers that the actions of one or both contracting jurisdictions will result in taxation for a person that does not comply with the provisions of the relevant tax treaty, the person may present the case to the CA of either jurisdiction, irrespective of the remedies provided by domestic law. However, the case must be presented within three years to the CA. If the contracting states are able to arrive at a satisfactory solution, they can resort to a Mutual Agreement arrangement. They may also consult with each other for resolution of cases not provided for in the tax treaty.

According to Article 16(1) of the MLI, a case must be presented to the CA within three years of the first notification of the action alleged to have resulted in taxation that is not in compliance with the tax treaty. This provision will apply in place of an existing provision, which provides for a period of less of than three years, or where such a provision does not exist.

India has made reservation to CTAs on the applicability of the first sentence of Article 16(1). The country has opted not to modify its tax treaty provision to allow access to 'either CA,' but to implement the minimum standard through a bilateral notification or consultation process under the MLI.

It should be noted that currently none of India's treaties provide that a case should be presented to the CA of a contracting jurisdiction and that adoption of the MLI could be advantageous in cases where taxpayers want to approach other CAs.

Comments

India has opted for the option where cases can be presented by taxpayers, but only in the countries of their residence. With regard to the time limit for presenting a case to MAP, India has agreed to a time limit of three years (although there is a shorter time limit for certain countries such as Canada).

Most Indian tax treaties provide for a time limit of three years. The exceptions include the following:

- Currently, India's tax treaties with Belgium, Canada, Italy and the UAE have a two-year time limit. And while the UAE has not signed the MLI, in the case of Belgium, Canada and Italy, the time limit for the tax treaties will be increased to three years.
- Currently, India's tax treaties with Brazil and Turkey have a five-year time limit. Brazil has not signed the MLI and Turkey has not opted for a three-year time limit. Therefore, the five-year limit will continue for these treaties.
- Currently, India's tax treaty with the UK does not have a time limit. However, the three-year limit will apply due to implementation of the MLI.

Corresponding adjustments

Article 17 of the MLI is supposed to apply in the absence of provisions in covered tax agreements that require a corresponding adjustment if the other treaty party makes a transfer pricing adjustment.

Paragraph 1 of Article 17, which is in line with the existing Article 9(2) of the OECD Model, is reproduced below:

"Where a Contracting Jurisdiction includes in the profits of an enterprise of that Contracting Jurisdiction — and taxes accordingly — profits on which an enterprise of the other Contracting Jurisdiction has been charged to tax in that other Contracting Jurisdiction and the profits so included are profits which would have accrued to the enterprise of the first-mentioned Contracting Jurisdiction if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other Contracting Jurisdiction shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjustment, due regard shall be had to the other provisions of the Covered Tax Agreement and the CAs of the Contracting Jurisdictions shall if necessary consult each other."

Furthermore, reservations on the applicability of Article 17 to CTAs can be made if:

- The country making the reservation needs to make a corresponding adjustment.
- The Competent Authority of the country making a reservation wants to resolve Transfer Pricing cases under MAP.
- Countries want to make reservations if alternative treaty provisions that limit the time during which they can make an adjournment to transfer prices or income is allocated to a PE in their CTAs.

India has chosen to apply this provision, except where similar provisions already exist, i.e., this provision will be added to its treaties with signatories to the MLI that do not have such a provision. India's treaties with similar existing provisions have been specifically excluded by reservation. The country has notified its treaties with the Netherlands, Ireland, Japan, Luxembourg, the US and Singapore.

Comments

This will open up access to bilateral Advance Pricing Agreements (APAs) and Transfer Pricing-related disputes in MAP for several treaties. India has refused access to disputes pertaining to Transfer Pricing under MAP or bilateral APAs till date in the absence of Article 9(2) in its tax treaties – especially with European countries.

Adoption of Article 9(2) in India's tax treaties would facilitate settlement of Transfer Pricing-related disputes through MAP and bilateral APA negotiations with countries such as Russia, Sweden, the Slovak Republic and Greece, with which it has no Article 9 (2) in its existing tax treaties.

The UK, Singapore, Sweden, the Netherlands and France have not made reservations with respect to the second sentence of Article 16(1), i.e., cases should be presented to the CAs within three years and the CTAs between these countries and India should be modified to include the language under the second sentence of Article 16(1).

Furthermore, with respect to the first and second sentences of Article 16(2) (need to approach other Competent Authority) and 16(3) (need for both contracting states coming together to resolve the matter), India's CTAs are already largely in compliance with the provisions of the MLI.

The number of CTAs notified for not having in place the relevant provisions is limited. Only such notified CTAs should be modified.

India's CTAs with Singapore, Sweden, the Netherlands and France already include such provisions. No modifications should be made with

respect to the first sentences of Articles 16(2) and 16(3) in its CTAs with the UK, Singapore, Sweden, the Netherlands and France, since these treaties already include the relevant language.

Although Article 19 of the MLI provides for mandatory binding arbitration in the event that CAs are unable to reach a decision under MAP within two years, India has not accepted such a provision, taking the position that such a binding arbitration would adversely affect its sovereignty.

Therefore, in the absence of a timeline, CAs may take a lot of time to resolve MAP-related disputes. Coupled with this is the fact that since India's CTAs will not include an arbitration clause, this will place a burden on taxpayers and also lead to a huge amount of litigation in the domestic courts.

Arbitration

The MLI enables countries to include mandatory binding treaty arbitration (Arbitration) in their tax treaties. However, arbitration is only applicable between countries that expressly opt to apply it to their CTAs.

Countries may reserve the right to apply the Arbitration provision of the MLI to some or all their DTAAs that already include an Arbitration provision.

Arbitration rules, once adopted, will provide taxpayers with the much-needed certainty that a case once submitted to MAP will be resolved.

Arbitration rules allow a person to request arbitration if a Competent Authority has not been able to reach an agreement under MAP within two years. CAs may agree on a shorter or longer period to resolve a particular case through MAP, provided they notify the affected people before expiration of the mandatory two-year period. However, countries that have subscribed to the Arbitration rules can make a reservation and substitute the two-year period with a three-year period in all their DTAAs.

Unless a country makes a specific reservation with respect to the scope of its cases that are eligible for arbitration, all treaty-related disputes that are not resolved through MAP could be subject to arbitration.

India has opted not to apply Arbitration to any of its CTAs.

Comments

That India has chosen not to apply Arbitration is ostensibly due to its concerns about its 'sovereignty'. Although this could be a hindrance to improvement of its tax treaty dispute resolution framework, and its concerns about its sovereignty may not have much of a standing from a legal perspective, India's policy concerns as regards even-handedness, amongst others, is understandable, and there is little content in the MLI to address such apprehensions.

Many more territories are in favour of adopting arbitration, but some are keen to first see how it is applied in practice. Some other territories are arguing strongly against using this option. India's experience with international arbitration in the context of investment-protection treaties is perhaps the reason for its decision to not opt for the Arbitration clause. In fact, most developing countries feel that their domestic mechanisms serve them better than arbitration. Moreover, since arbitration proceedings are not mandatorily binding on taxpayers, their decisions on long arbitration are not likely to be finalised soon.

While India has opted out of the Arbitration clause, 25 countries among the total number of signatories have signed up for the arbitration provisions in the MLI. Most have opted for the option of 'final offer arbitration'. Since the carve-outs are fairly broad under the MLI and not very clearly drafted, it is yet to be seen how many disputes will be covered in their scope.

Snapshot of India's position on the MLI

BEPS measures	MLI article
Hybrid mismatches	Article 2: Interpretation of terms
	Article 3: TE
	Article 4: Dual resident entities
	Article 5: Application of methods for elimination of double taxation
Treaty abuse	Article 6: Purpose of a CTA
	A clear statement is needed that the contracting parties that enter a tax treaty intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, as well as through treaty shopping.
	Article 7: Prevention of treaty abuse
	PPT
	A LOB article combined with a PPT
	A more complex LOB along with either an anti-conduit rule or a PPT
	Article 8: Dividend transfer transactions
	India has adopted this article except in its treaty with Portugal, which has a longer holding period.
	Article 9: Capital gains from alienation of shares or interests of entities deriving their value principally from immovable property
	Article 10: Anti-abuse rule for PE situated in third jurisdictions
	Article 11: Application of tax agreements to restrict a party's right to tax its own residents
PE	Article 12: Artificial avoidance of PE status through commissionaire arrangements and similar strategies
	Article 13: Artificial avoidance of PE status by exemption of specific activity
	Article 14: Splitting up of contracts
	Article 15: Definition of a person "closely related" to an enterprise
Improving dispute resolution	Article 16: MAP
	Article 17 : Corresponding adjustments
	Articles 18–26: Arbitration

Content	India’s provisional position
This includes details of the treaties covered by the MLI.	India has compiled a provisional list of its 93 comprehensive tax treaties.
Income derived by or through a TE or arrangement will be considered to be the income of a resident of the contracting state.	Not adopted
If an agreement is silent about dual resident entities, the CAs must agree on their residence with regard to their place of effective management and incorporation, and any other relevant factors.	Adopted
Three options are provided in the Convention, which will only apply where the contracting party has chosen to apply and has made a notification.	Not adopted
No position expressed	
Contracting parties should include one of the options below in their tax treaties:	
India has chosen to apply the PPT test along with S-LOB.	
The MLI has added a 365-day minimum holding period before entities can benefit from tax exemption on dividends.	
There is a 365-day prior period requirement for exempting gains from alienation of shares that principally derive their value from immovable property.	Adopted
This is an anti-abuse rule for income allocable to a PE in a third jurisdiction where low tax is levied.	No position expressed
This article allows contracting parties to tax their residents under their jurisdiction’s domestic laws.	No position expressed
This includes strict rules on determination of a PE, e.g., in an adopted commissionaire arrangement in terms of the provision on agents and contracts.	Adopted
This article includes modification of specific exemptions from activity with the introduction of the anti-fragmentation test.	Option A chosen by India
This includes anti-splitting rules to prevent avoidance of crossing the 12-month threshold for construction projects by splitting up of contracts between associated enterprises.	No position expressed
This article provides a definition of a “closely related” person for Articles 12, 13, and 14.	Not adopted
This article details procedural and substantive requirements for full implementation of MAP.	Adopted the minimum standards
CAs should provide for appropriate corresponding adjustment in cases where they find that such an adjustment is justified.	Chosen to apply this provision except where similar provisions already exist
These include provisions on setting up a new standard for mandatory binding arbitration in the MAP process.	Not adopted

Impact of India's position on its key treaties

Whereas India has entered around 134 tax treaties, there are countries that have opted to sign the MLI, and others have chosen not to sign it. A list of treaties with India that have not signed for the MLI is provided below for your reference:

List of countries						
Bangladesh	Hashemite Kingdom of Jordan	Mongolia	Nepal	Sudan	Turkmenistan	Uzbekistan
Beralus	Kazakhstan	Montenegro	Oman	Syrian Arab Republic	United Arab Emirates	Vietnam
Botswana	Kenya	Morocco	Philippines	Tajikistan	Uganda	Zambia
Brazil	Kyrgyz Republic	Mozambique	Qatar	Tanzania	Ukraine	
Estonia	Libya	Myanmar	Saudi Arabia	Thailand	United Mexican States	
Ethiopia	Malaysia	Namibia	Sri Lanka	Trinidad and Tobago	United States of America	

A list of countries that have excluded India from applying for the MLI:

List of countries			
Andorra	France	Jersey	Pakistan
Argentine Republic	Gabon	Liechtenstein	San Marino
Burkina Faso	Germany	Luxembourg	Senegal
Chile	Guernsey	Mauritius	Seychelles
China	Hong Kong	Republic of Monaco	Switzerland
Costa Rica	Isle of Man		

A snapshot of the impact of the MLI on key Indian tax treaties:

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Transparent entities	Not adopted	No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Dual resident entities	Adopted	No impact	CAS to determine	CAs to determine	CAs to determine	No impact	CAS to determine	No impact	CAS to determine
Methods for elimination of double taxation	Not adopted	No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Purpose of CTA: Preamble of the treaty to include that the common intention is to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax avoidance or evasion, including through treaty shopping arrangements	No position expressed	Existing preamble to be updated	Existing preamble to be updated	Existing preamble to be updated	Existing preamble to be updated	Existing preamble to be updated	Existing preamble to be updated	Existing preamble will be updated	Existing preamble will be updated
Prevention of treaty abuse: Treaty benefit not to be granted where obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted in that benefit, unless granting of such benefit is in accordance with object and purpose of relevant treaty provisions	Chosen to apply PPT along with the S-LOB provision	PPT rule to apply	PPT rule to apply	PPT rule to apply	PPT rule to apply	PPT rule to apply	PPT rule to apply	PPT rule to apply	PPT rule to apply

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 7: Prevention of treaty abuse – Article 7(4) – where the benefit of a treaty is denied to a person applying PPT, where the CTA of the CJ that would have otherwise granted such benefit will treat the person as eligible for the benefit if such a CA on the person's request (based on facts and circumstances) determines that benefit would have been granted to the person in the absence of the transaction or arrangement (before rejecting the person's request, the CA needs to consult the CA of the other jurisdiction.)		No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Article 7 – Prevention of treaty abuse – Article 7(8) to (13) – SLOB provisions		No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact

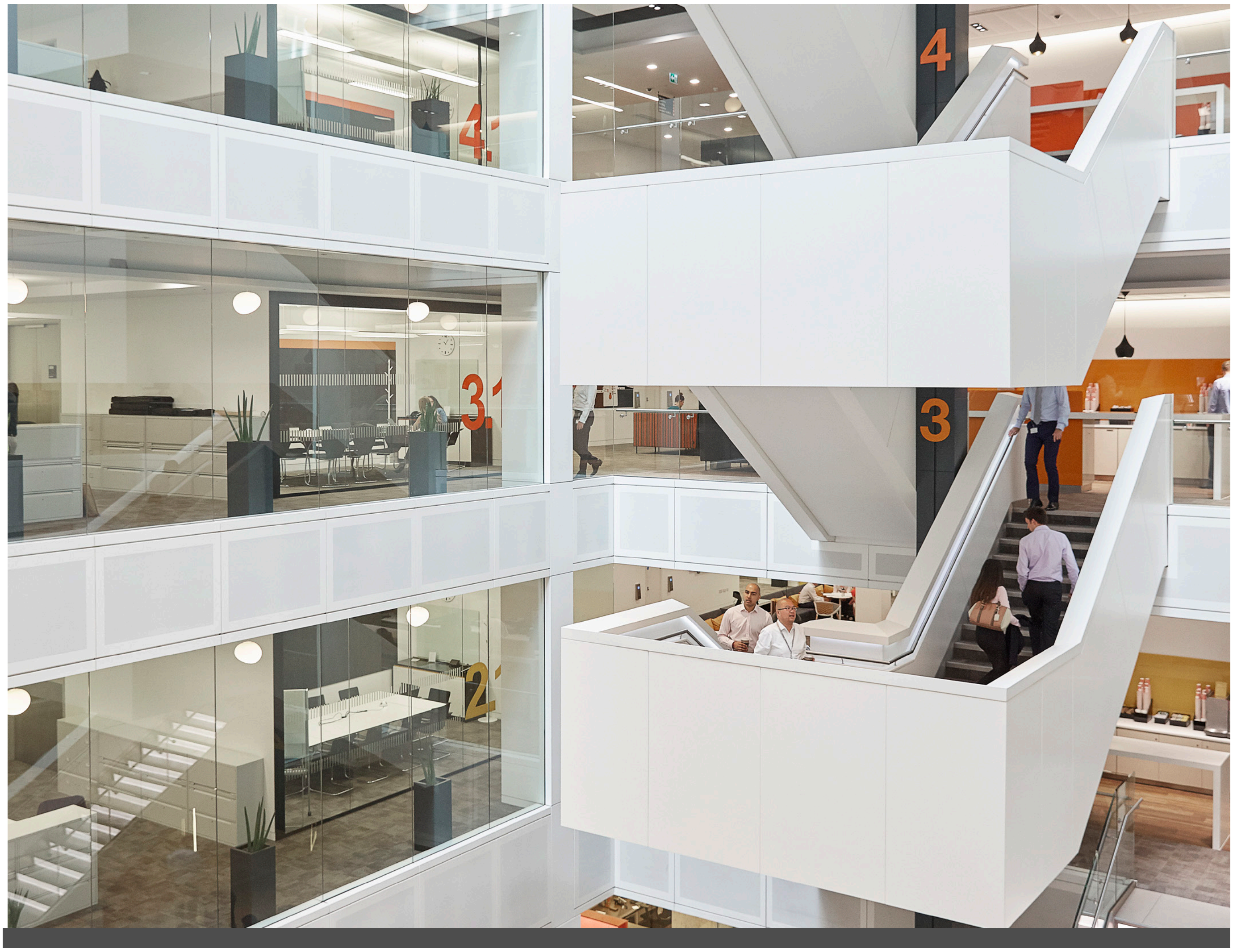
MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 8 – Dividend transfer transaction – treaty provisions that exempt dividends or that limit the tax rate on such dividend, subject to the minimum shareholding requirement, which will only apply if the ownership-related conditions are met through the 365-day period	Adopted except in its treaty with Portugal in which a longer holding period was already prescribed	No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Article 9 – Capital gains from alienation of shares or interests of entities deriving their value principally from immovable property – Article 9(1) – treaty provisions giving taxing rights to the other CJ, in respect of gains derived from alienation of shares or other rights of participation in an entity, where the share or interest derived more than a certain part of their value from immovable property in the other CJ, which will apply if the value threshold is met at any time during the 365- day preceding the alienation and will also apply to shares or comparables	Adopted	No impact	Article 9(1) to apply	Article 9(1) to apply	No impact	No impact	No impact	No impact	No impact
Article 9 – Capital gains from alienation of shares or interests of entities deriving their value principally from immovable property—Article 9(4) – gains derived from alienation of shares or comparable interests, which may be taxed in the other CJ if at any time during the 365 days preceding the alienation, the shares or comparable interests derived more than 50% of their value from immovable property situated in the other CJ	Adopted	No impact	No impact	No impact	No impact	No impact	Article 9(4) to apply	Article 9(4) to apply	Article 9(4) to apply

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 10 – Anti-abuse rule for permanent establishments situated in third jurisdictions – subject to the exception in Article 10 (2) of the MLI, benefit of the treaty not to apply to any item of income on which the tax rate in the third jurisdiction in which an exempt PE is located is less than 60% of the tax that will be imposed in "residence jurisdiction of the enterprise ('Exempt PE' refers to a situation where profits attributable to the PE are exempt from tax in the residence jurisdiction of the enterprise. The CA of the other CJ may however grant the treaty benefit denied under Article 10(1) of the MLI.)	No position expressed	No impact	Article 10(1) to 10(3) not to apply	No impact	No impact	No impact	Article 10(1) to 10(3) to apply	No impact	No impact
Article 11 – Application of tax agreements to restrict a party's rights to tax its own residents (A CTA will not affect taxation by a CJ of its residents, except with respect to the benefits granted under provisions of the CTA.)	No position expressed	No impact	No impact	Article 11(1) not to apply	Article 11(1) to apply	No impact	No impact	No impact	No impact
Article 12 – Artificial avoidance of PE status through commissionaire arrangements and similar strategies Article 12(1) – Activities of an enterprise to constitute a PE if the agent habitually concludes contracts or plays the principal role, leading to conclusion of contracts routinely, without material modification by the enterprise, unless its activities are conducted at a fixed place of business, which does not constitute a fixed place PE under the CTA	Adopted	No impact	Article 12(1) to apply	No impact	No impact	No impact	Article 12(1) to apply	No impact	No impact

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 12 – Artificial avoidance of PE status through commissionaire arrangements and similar strategies Article 12(2) – Article 12(1) not to apply where the agent acting in a CJ on behalf of an enterprise conducts business in the CJ as an independent agent and acts for the enterprise in the ordinary course of this business (The agent is not to be considered an independent agent if he or she acts exclusively or almost exclusively on behalf of one or more enterprises to which the individual is closely related.)	Adopted	No impact	Article 12(2) will apply	No impact	No impact	No impact	Article 12(2) to apply	No impact	No impact
Article 13 – Artificial avoidance of PE status through specific activity exemptions Article 13(1) – Provisions reducing the scope of the exceptions to a definition of a PE	Chosen to apply this provision with Option A to all its notified tax treaties since they include a PE exemption provision	No impact	Article 13(2) – Option A to apply	Article 13(2) – Option A to apply	No impact	No impact	Article 13(2) – Option A to apply	Article 13(2) – Option A to apply	No impact
Article 13 – Artificial avoidance of PE status through specific activity exemptions Article 13(4) – Provisions addressing fragmentation of activities between closely related enterprises		No impact	Article 13(4) to apply to Article 5(4)	Article 13(4) to apply to Article 5(4)	Article 13(4) to apply	No impact	Article 13(4) to apply	Article 13(4) to apply	Article 13(4) to apply
Article 14 – Splitting up contracts – provisions to avoid such a situation where splitting up of contracts is used as a potential strategy for artificial avoidance of a PE status through abuse of PE exceptions	No position expressed	No impact	Article 14(1) will apply	Article 14(1) to apply	No impact	No impact	No impact	No impact	Article 14(1) to apply
Article 15 – Definition of person closely related to an enterprise		No impact	Article 15 to apply	Article 15 to apply	Article 15 to apply	No impact	Article 15 to apply	Article 15 to apply	Article 15 to apply

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 16 – Mutual Agreement Procedure Article 16(1) – approaching CA where taxed not as per the treaty	Chosen not to modify its tax treaty provision to allow access to "either competent authority" but has chosen to implement the minimum standard through a bilateral notification or consultation process under the MLI	No impact	No impact	No impact	Case to be presented within three years	Case to be presented within three years	No impact	Case to be presented within three years	Case to be presented within three years
Article 16 – Mutual Agreement Procedure: Article 16(2) – First sentence (CA to resolve case by MAP)		No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Article 16 – Mutual Agreement Procedure Article 16(2) – Second sentence (There is no time limit for implementation of mutual agreement.)		No impact	No impact	No impact	Article 16(2) – second sentence to apply	No impact	No impact	No impact	No impact
Article 16 – Mutual Agreement Procedure Article 16(3) – First sentence – CA to resolve interpretation/ application of treaty by MAP		No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Article 16 – Mutual Agreement Procedure									
Article 16(3) – Second sentence – elimination of double taxation possible even if not provided in treaty		No impact	No impact	Article 16(3) – second sentence to apply	Article 16(3) – second sentence to apply	No impact	No impact	No impact	No impact

MLI provision	India's position	Impact of the MLI on India's select tax treaties							
		Cyprus	Netherlands	Australia	UK	Canada	Japan	Italy	Ireland
Article 17 – Corresponding adjustment	Adopted, except where similar provisions exist	No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact
Article 18 to Article 26 – Part VI of the MLI on Arbitration	Not adopted	No impact	No impact	No impact	No impact	No impact	No impact	No impact	No impact



Closing comments

Various tax-related factors have an impact on decisions on inbound and outbound investments, structuring of transactions, financing and other cross-broader transactions. Due to the changes made in Indian tax treaties because of the MLI, businesses will need to evaluate the consequences to their fact patterns, consider re-arranging these and apply appropriate safeguards in transactions.

Interpreting the MLI is a complex process due to the need for multiple cross-referencing. The sheer number of tax treaties that will be amended only exacerbates this complexity, since these will have to be read with corresponding domestic tax laws.

Aspects such as the introduction of new anti-avoidance rules, changes made in allocation of taxing rights and expansion of the scope of a taxable presence mean that there will be increased uncertainty and subjectivity involved in interpretation of tax treaties, at least for a while.

The OECD has already created and uploaded a software tool on its website to match the reservations made by various countries under the MLI. And although we can expect many more such technological initiatives that are aimed at simplifying the process of interpretation and application of the MLI, it will become a necessity for businesses to reach out for informed and specialised advice to help them evaluate the impact of the MLI on their existing and future arrangements. It is therefore imperative that every development in this domain is closely monitored.

Notes

Notes

About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 158 countries with more than 236,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com

In India, PwC has offices in these cities: Ahmedabad, Bangalore, Chennai, Delhi NCR, Hyderabad, Kolkata, Mumbai and Pune. For more information about PwC India's service offerings, visit www.pwc.com/in

Contacts

Abhishek Goenka

PwC | Partner – Tax & Regulatory Services
Email: abhishek.goenka@in.pwc.com
PricewaterhouseCoopers Private Limited
6th Floor, Tower 'D', The Millennia, 1 & 2 Murphy Road
Ulsoor, Bengaluru - 560 008, India.
Direct: +91 (80) 4079 6279 | Mobile: +91 9886 553377

Dwaraknath E N

PwC | Partner – Tax & Regulatory Services
Email: dwaraknath.e.n@in.pwc.com
PricewaterhouseCoopers Private Limited
6th Floor, Tower 'D', The Millennia, 1 & 2 Murphy Road
Ulsoor, Bengaluru - 560 008, India.
Direct: +91 (80) 4079 6003 | Mobile: +91 9945046060