

Multilateral Instrument Comes into Force in India

October 2019

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1. Introduction

On October 1st, 2019, the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, otherwise referred to as the Multilateral Instrument or MLI, came into force.¹

When it comes into effect², the MLI will amend the bilateral tax treaties of its signatories to ensure that certain minimum international tax standards are met. The implications of this development are significant for international businesses and investors, especially those seeking to avail benefits under India's network of bilateral tax treaties. Importantly, out of 93 CTAs notified by India, 26³ countries have already ratified the MLI as on date and the Double Taxation Avoidance Agreement (DTAA) with these countries will be modified by MLI. For the remaining Covered Tax Agreements ("CTAs"), MLI will take effect as and when these countries ratify the MLI.

While the signatories to the MLI include some of India's strategically important trading partners such as the United Kingdom, Canada, Germany, Japan and France, some countries, like the United States and Brazil, have chosen to not sign the MLI. Other countries, like Mauritius, Iceland, Switzerland and Germany, while signing the MLI have not made it applicable to their tax treaty with India.⁴

Further, in respect of the 26 treaty partners of India who have deposited the Instrument of Ratification on or before 30th June, 2019, entry into effect for India under MLI with respect to the DTAA shall be from financial year 2020-21 onwards, which starts from April 1st, 2020.

It is also important to note that despite being signatories to the MLI, India and Spain have bilaterally inserted a limitation of benefits clause in the India-Spain DTAA recently that is not in line with the MLI LOB, expressly permitting the applicability of domestic GAAR. Therefore till such time Spain submits a ratified instrument the amended India – Spain DTAA shall continue to apply.

Therefore, a thorough understanding of the impact of the MLI is essential, not just for structuring future cross-border operations and investments but also to re-confirm the availability of treaty benefits for existing structures and arrangements.

This summary sets out and analyses the potential impact of the MLI positions adopted by India and some of its key trading and treaty partners, and assesses the impact on India's tax treaties with these jurisdictions.

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1. It was signed by India on June 7, 2017 and ratified on May 27, 2019.
 2. Please refer to section below on entry into effect for further details.
 3. Austria, Australia, Belgium, Canada, Denmark, Finland, France, Georgia, Ireland, Israel, Japan, Lithuania, Luxembourg, Malta, Netherlands, New Zealand, Norway, Poland, Russia, Serbia, Singapore, Slovak Republic, Slovenia, Sweden, United Kingdom and UAE.
 4. While Iceland and Switzerland have submitted its ratified instrument with OECD, Mauritius and Germany are yet to submit their ratified instruments. Therefore, this position may not be final and may be subject to change. Current analysis is based on the interim positions adopted by these countries.

2. How it Works

While the MLI came into force on July 1, 2018 (following its ratification by five countries), for India, the MLI came into force on 1st October, 2019.⁵

Upon coming into effect, the MLI will not replace India's existing bilateral tax treaties entirely. Instead, it will apply alongside India's existing bilateral tax treaties and either supplement, complement, supersede or modify their application to bring them in line with the measures set out in the BEPS Action Reports.

Notification of Covered Tax Agreements.

Once the MLI comes into force, it will not automatically effect all India's tax treaties, but only those tax treaties where both India and her relevant treaty partner have conveyed their intention (by way of a notification) for their tax treaty to be covered by the MLI. Treaties intended to be covered by the MLI are referred to as "Covered Tax Agreements" ("CTAs"). In other words, the MLI will be applicable only to those bilateral tax treaties notified as CTAs by both India and the relevant treaty partner. India has notified 93 of its bilateral tax treaties as CTAs. However, as pointed out above, only 26 other treaty partners have both submitted the ratified instrument and chosen India to be one of their CTAs. Therefore, it is only those treaties that are going to be impacted currently.

Mandatory Minimum Standards under MLI.

Upon qualifying as a CTA, a tax treaty will be required to meet certain prescribed minimum standards i.e., the minimum standard for the prevention of treaty abuse under BEPS Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances) and the minimum standard for the improvement of dispute resolution under BEPS Action 14 (Making Dispute Resolution More Effective). India will have little leeway (almost none) to opt out of adherence to these minimum standards.

Where an MLI provision reflects a BEPS minimum standard, India can opt out of such provision only in limited situations such as where the CTA already meets the minimum standards. India and her treaty partners ("**Treaty Partners**" / "**Contracting Jurisdictions**") 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. Whether a CTA meets the minimum standards will be determined in the course of the review and monitoring process within the inclusive framework on BEPS.

India does however, have the flexibility to opt out (by way of reservations) of provisions that are not regarded as setting a minimum standard (see below).

Reservations with Respect to Non-Mandatory or Optional Provisions.

A signatory to the MLI may reserve the right for provisions of the MLI to not apply:

- a. to its covered tax treaties in their entirety; or
- b. a subset of its covered tax treaties.

Where India or one of its treaty partners reserve the right for provisions of the MLI to not apply to a CTA, the relevant provisions of the MLI will not apply to the CTA irrespective of whether the India or her treaty partner (as the case may be) has made a similar reservation. In case the reservation is made with respect to a sub-set of treaties, the party making the reservation must notify a list of treaties falling within the scope of the reservation. For example, Article 4(2) of the MLI provides Parties the option to reserve the right to not apply Article 4, which deals with "Dual Resident Entities", to its treaties which already provide that the tie-breaker test for residence of dual resident entities shall be decided by the competent authorities of both Treaty Partners through mutual agreement. Parties opting for this reservation would be required to notify their CTAs which already

5. On the first day of the month following the expiration of a period of three calendar months beginning on the date India deposits her instrument of ratification

contain such a provision, in which case, Article 4 would not apply to such CTAs.

Further, most articles of the MLI also provide that in the event a signatory:

- a. neither reserves the applicability of a particular MLI provision, nor
- b. notifies the relevant provisions of a bilateral tax treaty (where such notification is required);

then the respective MLI article will apply to its CTAs and will prevail over the relevant provision of the CTAs to the extent of such provisions are inconsistent.

Optional Provisions. In some instances, the MLI permits a signatory to choose among alternative provisions intended to address the same issue. A signatory is required to notify the Depository of its choice. Unlike in the case of reservations, both Treaty Partners are required to choose the same option in order for such option to apply (except for Article 5 (Application of Methods for Elimination of Double Taxation) and 23(5) (Types of Arbitration Process) of the MLI). In the event that a signatory chooses a particular option, and its treaty partner chooses to apply a different option or no option at all, then none of the options will apply to the relevant CTA. For example, Article 13 of the MLI which deals with “Artificial Avoidance of Permanent Establishment Status through the Specific Activity Exemptions” provides for Parties to opt for either Option A or Option B to modify their CTAs. A particular option will apply to a CTA only when both Treaty Partners have elected that same option.

Notification clauses. Where an MLI provision supersedes or modifies an existing provision of a CTA, the Parties are generally required to make a notification specifying which CTAs contain such provisions and identify

the provisions. While Parties are expected to identify and notify such provisions on a best efforts basis, it is possible that a relevant existing provision is not identified by a signatory. Accordingly, the concept of provisional notifications has been introduced to deal with situations where a signatory to the MLI accidentally omits to notify a provision of a CTA, or Treaty Partners disagree regarding whether a provision is superseded or modified by the MLI, or where both Treaty Partners agree that there is a relevant provision but disagree about which one it is. In such a situation, the exchange of provisional notifications with the other Treaty Partner will afford signatories an opportunity to discuss mismatches in the notifications and correct them prior to finalization of the lists.

The signatories to the MLI (India included) have filed provisional notifications with the Depository as allowed by the MLI at the time of signing of the treaty. The provisional MLI Position of each signatory indicates the tax treaties it intends to cover, the options it has chosen within those provided by the MLI and the reservations it has made. Signatories are normally expected to submit their final notifications at the time of submission of their instruments of ratification with the Depository of the OECD. Further, even after ratification, Parties can choose to opt in with respect to optional provisions or to withdraw reservations.

Compatibility Clauses. The MLI contains compatibility clauses that define the relationship between the MLI and the provisions of a CTA. These are intended to address overlap or conflicts between the provisions of the MLI and the provisions of a CTA. In other words, the compatibility clauses serve to determine whether the provision of the MLI would replace or modify the provisions of the CTA. The MLI contains four types of compatibility clauses as follows:

| Type of compatibility clause | When does it apply | What is the effect on existing provision | Notification Requirement |
|---|--|--|--|
| MLI Provision applies “in place of” existing CTA provision | Only when there is an existing provision in the CTA | MLI provision replaces the existing CTA provision | All Treaty Partners have to notify existing CTA provision |
| MLI Provision “applies to” or “modifies” existing CTA provision | Only when there is an existing provision in the CTA | MLI provision changes the application of an existing provision without replacing it | All Treaty Partners have to notify existing CTA provision |
| MLI Provision applies “in absence of” existing CTA provision | Only when the provision is absent in the CTA | MLI provision is added to the CTA | All Treaty Partners have to notify absence of provision in CTA |
| MLI Provision applies “in place of” or “in absence of” existing CTA provision | Whether existing provision is present in CTA or absent | It replaces or supersedes existing provision, or is added to CTA in absence of existing provision. | <ul style="list-style-type: none"> ▪ Where both parties notify existing provision, the provision gets replaced. ▪ Where one party notifies and other does not, the MLI provision supersedes CTA provision to the extent of incompatibility |

3. Entry into Force & Effect

The timelines for the MLI to come into effect with respect to a CTA differ based on the type of taxation to which the modifications apply.

- For taxes which are withheld at source on amounts paid to non-residents, such as royalties, interest, capital gains etc. - MLI will enter into effect where the event giving rise to such withholding tax occurs on or after the first day of the next calendar year that begins on the later of the dates on which the MLI comes into force for each Treaty Partner (“CTA Date”);
- Hence, referring to the above example, for taxes such as tax on business profits attributable to a PE, the MLI shall apply to such taxes levied in India from financial year 2020-21, whereas it will apply for the purpose of such taxes levied in Singapore on or after January 1, 2022.
- In effect, the changes to the CTAs can be expected to be in effect from 1st April, 2020.

This is illustrated by the table below:

| Types of Taxes | Entry into effect | Applicability of MLI by India | |
|--|---|-------------------------------|---------------------------------------|
| Taxes which are required to be withheld on overseas payments | Event giving rise to the withholding tax takes place on or after the 1st day of the next year (calendar year or tax year) that begins on or after the CTA Date. | October 2019 | From April 1, 2020, where applicable. |
| Other Taxes | Levied with respect to taxable periods beginning on or after an expiry of 6 calendar months from the CTA Date. | October 2019 | From April 1, 2020, where applicable. |

- For example, in case of India and Singapore, if the MLI enters into force for India on October 2019 and for Singapore on September 2020, the CTA Date is September 2020 and the MLI will come into effect for all withholding taxes under the India-Singapore tax treaty which relate to an event occurring on or after January 2021;
 - For the purpose of its own application of MLI to withholding taxes, India has chosen to replace “taxable period” for “calendar year”. Accordingly, in the above example, MLI will cover a withholding tax payable in India if the event giving rise to such tax takes place on or after April 1, 2021, while it will cover a withholding tax payable in Singapore if such event takes place on or after January 1, 2021;
 - For all other taxes - MLI will come into effect for taxable periods beginning on or after an expiry of 6 calendar months from the CTA Date.
- Entry into effect for MAP. There is a separate rule provided for entry into effect of Article 16 on Mutual Agreement Procedure (“MAP”). Article 16 shall come into effect with respect to a CTA for a case presented to the competent authority of a Contracting Jurisdiction on or after the CTA Date irrespective of the taxable period to which the case relates. However, an exception is provided for cases that were not eligible to be presented for MAP as of the CTA Date under the treaty prior to its modification by MLI. The exception is intended to ensure that the MLI would not revive earlier cases which had been ineligible for MAP prior to entry into force of the MLI.
- Therefore, it remains to be seen how the entry into effect of MLI for different income streams would practically play out for India vis-à-vis its Treaty Partners. Developments relating to ratification of MLI by different Parties, entry

into force of the MLI and entry into effect of MLI for each CTA should be closely followed and borne in mind while undertaking structuring exercises. We will endeavor to send an updated version of this summary as and when key changes occur.

It should be noted that India has chosen to apply the 30-day rule. Accordingly, the references to CTA Date in the section above should be read as 30 days after the date of receipt by the Depository of the latest notification making a reservation to apply the 30-day rule under Article 35(7).

4. Transparent Entities

Paragraph 1 of Article 3 provides that income derived by or through a transparent entity will only be considered income of a resident of a treaty jurisdiction (and thus eligible for treaty benefits) to the extent that income is treated as income of a resident by that treaty jurisdiction. Paragraph 2 provides that the elimination of

double taxation is not available with respect to income which may be taxed by the treaty partner jurisdictions according to the provisions of a CTA to the extent that those provisions allow such taxation solely because the income is also income derived by a resident of that treaty partner jurisdiction.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|----------------|-----|
| Applies paragraph 1 | 3(1) & 3(2) | X | NA | X | ✓ | X | X | ✓ | ✓ | X | X | ✓ ⁶ | ✓ |
| Reserves the right not to apply paragraph 1 to CTAs that already contain similar provisions | 3(5) (b) | X | NA | X | X | X | X | X | X | X | X | X | ✓ |
| Reserves the right not to apply paragraph 1 to CTAs which already contain provisions which identify in detail the treatment of specific fact patterns and types of entities or arrangements. | 3(5) (d) | X | NA | X | X | X | X | X | X | X | X | ✓ | X |
| Reserves the right not to apply the rule of paragraph 2 | 3(5)(f) | X | NA | X | ✓ | X | X | ✓ | ✓ | X | X | X | ✓ |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | X | X | X | X | X |

Countries in Green are yet to submit ratified instruments to the OECD
Countries in Red have submitted their ratified instruments to the OECD

6. Only where existing treaties do not have a similar clause. India does not have a similar clause. Hence it should apply.

Article 3 does not impact India's treaties since India has reserved against the application of Article 3 in its entirety. India's position, as enunciated in the Schellenberg ruling of the Authority for Advance Rulings, is that where members of a fiscally transparent entity are

subject to tax on the income of the fiscally transparent entity, treaty benefits may be available to such members only where the language of the relevant bilateral treaty expressly provides for it.

5. Dual Resident Entities

determined by mutual agreement between the Treaty Partners. Treaty benefits are in principle withheld from the entity until such agreement is reached.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|----------------|-----|-----|-----|-----|-----|----|----|----------------|-----|-----|-----|-----|
| Applies paragraph 1 | 4(1) | ✓ | NA | X | X | X | X | ✓ | ✓ ⁷ | ✓ | X | ✓ | ✓ |
| Reserves the right not to apply paragraph 1 to treaty provisions that already require resolution of dual residence by mutual agreement. | 4(3)(b) | X | NA | X | X | X | X | X | X | X | X | X | ✓ |
| Reserves the right not to apply the paragraph 1 to treaty provisions that deny treaty benefits in cases of dual residence without requiring the competent authorities to reach mutual agreement | 4(3)(c) | X | NA | X | X | X | X | X | X | X | X | X | X |
| Replaces the last sentence of paragraph 1 with the sentence, "In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by the Covered Tax Agreement." | 4(3)(e) | X | NA | X | X | X | X | X | ✓ | X | X | X | X |
| Reserves the right not to apply the entire article to its CTA with Parties that have made the reservation described in subparagraph e). | 4(3)(f) | X | NA | X | X | X | X | X | X | X | X | X | ✓ |
| Amendment to tax treaty with India? | | | X | X | X | X | X | ✓ | ✓ | X | X | ✓ | ✓ |

7. Japan reserves the right to replace the last sentence of Article 4(1) of the Convention with the following text for the purposes of its Covered Tax Agreements: "In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by the Covered Tax Agreement."

India has chosen to apply Article 4. However, given the reservations of other treaty partners, it will amend only the treaty with the UK, Japan, Canada, Netherlands and Ireland. In practice, as a consequence of the introduction of the POEM test to determine residence under India's domestic tax, there is likely to be a higher incidence of the treaty tie-breaker provision being applied e.g., where a foreign company is rendered resident of India (as a result of POEM), and a resident of its country of establishment (since such country attaches importance to the

place of incorporation of the company). It is unlikely that India will readily concede to the jurisdiction of residence of a dual resident entity being determined in favour of any country other than India. In such a scenario, it is likely that the competent authorities may be unable to reach an agreement on the residence of a dual resident entity, and accordingly, such entity would not be entitled to any benefits under the treaty, except to the extent agreed between India and the respective country.

6. Application of Methods for Elimination of Double Taxation

Article 5 provides three options to countries with respect to elimination of double taxation that may exist where countries follow the exemption method to eliminate double taxation: (a) disallow the exemption method for income that is exempt or subject to a reduced treaty rate in the other jurisdiction, (b) disallow the exemption method for dividends that are deductible in the other jurisdiction and (c) solely apply the credit method.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies Option A (credit method instead of exemption method for any income that is exempt or taxed at a reduced tax rate by other state pursuant to Covered Tax Agreement; cf. art. 23A(4) OECD Model) | 5(2) | X | NA | X | ✓ | X | X | X | X | X | X | ✓ | X |
| Applies Option B (credit method instead of exemption method for dividends that are deductible for payer in other state) | 5(4) | X | NA | X | X | X | X | X | X | X | X | X | X |
| Applies Option C (credit method for all income that may be taxed in other state) | 5(6) | ✓ | NA | X | X | X | X | X | X | X | X | X | X |
| Applies none of the options | 5(1) | X | NA | X | X | X | X | ✓ | ✓ | X | X | X | ✓ |
| Reserves the right not to allow treaty partners to apply Option C with respect to one or more identified or all of its Covered Tax Agreements. | 5(9) | X | NA | X | ✓ | X | X | X | X | X | X | X | X |
| Reserves the right for Article 5 not to apply to its CTAs | 5(8) | X | NA | ✓ | X | ✓ | ✓ | X | X | ✓ | ✓ | X | X |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | X | X | X | X | X |

India has chosen to Apply Option C under Article 5 to its covered tax agreements. This is most likely because India generally does not employ the exemption method of eliminating double taxation in its bilateral tax treaties, preferring to use the credit method (Article 23B of the Model Convention) with some variations on a treaty specific basis. Accordingly, there should be no amendments in cases above where countries have made this article inapplicable in its entirety, for instance Canada, France, Singapore and Sweden. However, in other cases, even if the options chosen are different or if no option is chosen, double taxation shall be eliminated based on the options chosen by the respective countries.

7. Purpose of a Covered Tax Agreement

Article 6 is a minimum standard and inserts language in the preamble of tax treaties stating that treaty jurisdictions do not intend to create opportunities for tax evasion or avoidance. As a BEPS minimum standard this provision is mandatory.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|----------------|-----|-----|-----|----------------|----|-----------------|-----------------|-----|-----|-----|-----|
| Applies paragraph 1 | 6(1) | ✓ ⁸ | NA | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Includes a reference in preamble to 'developing economic relationship and enhancing co-operation in tax matters' | 6(3) | X | NA | ✓ | X | ✓ | ✓ | ✓ | ✓ | X | X | X | ✓ |
| Reserves the right not to apply provision to Covered Tax Agreements that already contain preamble language describing that treaty jurisdictions do not intend to create opportunities for tax evasion or avoidance | 6(4) | X | NA | X | ✓ | X ⁹ | X | X ¹⁰ | X ¹¹ | X | X | X | X |
| Amendment to tax treaty with India? | | | X | X | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |

8. India has remained silent on applicability of Article 6. Hence, it shall be applicable as it is minimum standard and other countries have opted for it while choosing India to be a CTA.

9. Only for Bulgaria and Germany

10. Only for Belarus, Ukraine and Uzbekistan

11. Only for Germany

India has been silent on its position on Article 6. Therefore, in the absence of India notifying any treaty provisions/preamble language, the MLI Preamble will not replace the existing preamble language in India's CTAs but will only be added to the existing preamble text, irrespective of whether the other Treaty Partners notify India's treaty for this purpose. However, there will be no change to the treaty with Mauritius and the USA, since Mauritius has not notified its treaty with India as a CTA, and the USA is not a party to the MLI. However, this is based on the positions adopted at the time of entry into force of the MLI in India and such position may change at the time of submission of the ratified instrument by other countries.

This is the most important change along with local General Anti Avoidance Rules which would have an impact on the structuring of cross border transactions. While it was settled law earlier that the treaties were intended to provide relief and therefore had to be interpreted in a taxpayer friendly manner, the addition of the words prevention of double-non taxation, reduced taxation or treaty shopping is likely to result in a significant change.

Nevertheless, the carve out in the MLI allows for treaty benefits to be provided its not an abuse or misuse of the treaty as set out in the analysis of Article 7 below.

8. Prevention of Treaty Abuse

Article 7 is a minimum standard and provides that countries must include one of the following in their tax treaties: (i) a principal purpose test ("PPT"), (ii) a PPT together with a simplified limited limitation on benefits ("LOB") test or (iii) an extensive LOB together with an anti-conduit provision.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|-----------------|-----|-----|-----------------|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies PPT | 7(1) | ✓ | NA | ✓ ¹² | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Applies discretionary relief under PPT | 7(4) | X | NA | ✓ | ✓ | X | ✓ | ✓ | X | X | X | ✓ | ✓ |
| Reserves the right not to apply the PPT to Covered Tax Agreements that already contain a principal purpose test | 7(15)(b) | X | NA | X | ✓ | X | X | X | X | X | X | X | X |
| Opts for Simplified LOB | 7(6) | ✓ | NA | X | X | X | X | X | X | X | X | X | X |
| Chooses to apply the Simplified LOB only in relation to treaty partners that have opted for the Simplified LOB | 7(7)(a) | X | NA | X | X | X | X | X | X | X | X | X | X |
| Allows a treaty partner that has opted for the Simplified LOB to apply the Simplified LOB asymmetrically | 7(7)(b) | X | NA | X | X | X | X | X | X | X | X | X | X |
| Amendment to tax treaty with India (PPT)? | | | X | X | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Amendment to tax treaty with India (Simplified LOB)? | | | X | X | X | X | X | X | X | X | X | X | X |

12. Mauritius has expressed a statement that while Mauritius accepts the application of Article 7(c) alone as an interim measure, it intends where possible to adopt a limitation on benefits provision, in replacement of Article 7(c), through bilateral negotiation.

In its final notification, India has chosen to apply the PPT with the Simplified LOB across all its Notified Treaties. So far as the PPT is concerned, being a default test, it should apply across the board in all of India's treaties irrespective of the other position adopted by the other countries. Since India is only one among 12 countries to have chosen to apply the SLOB, only a PPT is likely to apply to India's CTAs since India has not chosen a reservation to negotiate a detailed LOB with those Treaty Partners who have not chosen the SLOB. Further, most of its other Treaty Partners (including several European countries) have chosen not to allow a one sided symmetric or asymmetric application of the SLOB, thereby resulting in application of only a PPT to those treaties. If the India- Mauritius DTAA does not get covered by the provision of the MLI as stated above, the tests mentioned under this article should not apply. However, in the instances where they do, there appears to be no grandfathering provisions at this point in time and hence may be applicable to future transactions, even though the structure may have been set up prior to the introduction of MLI.

Further, the PPT under the MLI in some cases could potentially be broader in ambit than the General Anti-Avoidance Rule ("**GAAR**") under India's domestic tax laws as the latter gets triggered only if the "main purpose" of the arrangement is to obtain a tax benefit. Further, in order for GAAR to get 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 ITA, lack of commercial substance, or lack of bona fides. Therefore, it may be unlikely for GAAR to get triggered if the PPT is met, except in situations where the PPT is avoided on the ground that the benefit was in accordance with the object and purpose of the treaty provision. GAAR may still get triggered in such situations as it does not provide for such a carve-out.

9. Dividend Transfer Transactions

Article 8 provides that a reduced rate of source state taxation on dividends pursuant to a tax treaty only applies if a minimum ownership threshold required by the tax treaty is met throughout a retrospective 365-day testing period. This provision applies only where both contracting states have notified the relevant provision in their CTA.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|----------------|-----------------|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 8(1) | ✓ ¹³ | NA | X | X | X | X | X | X | ✓ | ✓ | ✓ | ✓ |
| Reserves the right for the paragraph not to apply to its CTAs to the extent that the provisions referred to in paragraph 1 already include a minimum holding period | 8(3(b)) | ✓ ¹⁴ | NA | X | X | X | X | X | X | X | X | X | X |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | X | X | X | X | X |

13. In its list of provisional notifications, of the countries considered, India has only notified USA, Singapore and Canada.

14. India has notified article 10(2) of the treaty with Portugal.

Article 8 is unlikely to have a significant impact on the distribution of dividends. This is because India does not impose a withholding tax on dividend distributions,¹⁵ preferring instead to impose a Dividends Distribution Tax (DDT) on corporate profits out of which dividends are distributed in the hands of the company making such distribution. Hence, any limitation on the availability of treaty benefits with respect to taxes on dividends is unlikely to have an impact on the DDT or the distributions made by Indian companies.

15. Up to an aggregate annual dividend income of INR. 10 lakhs.

10. Capital Gains on Shares in Real Estate Companies

Article 9 introduces a retrospective 365-day testing period with respect to a value threshold in the definition of ‘real estate company’ in a tax treaty and/or includes ‘ownership interests comparable to shares’ in CTAs that already includes provisions to tax capital gains derived from shares in real estate companies, or (optionally) replaces existing Covered Tax Agreement provisions entirely with the new art. 13(4) of the OECD Model as per the final BEPS Action 6 report, or adds this provision to Covered Tax Agreements currently lacking a provision on real estate companies.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|-----------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies the retrospective 365-day testing period to existing provisions on real estate companies | 9(1)(a)/9(6)(d) | ✓ | NA | X | X | X | X | X | ✓ | X | ✓ | ✓ | ✓ |
| Applies the inclusion of interests comparable to shares to existing provisions on real estate companies | 9(1)(b)/9(6)(e) | ✓ | NA | X | X | X | X | X | ✓ | X | ✓ | ✓ | X |
| Chooses to replace or add provision on real estate companies | 9(4) | ✓ | NA | X | X | X | X | X | ✓ | ✓ | ✓ | X | ✓ |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | ✓ | X | ✓ | ✓ | ✓ |

Since India has chosen to apply the Optional Provision under paragraph 4, it would apply only in cases where the other Treaty Partner has also chosen to apply paragraph 4. In all other cases, the provisions notified under paragraph 7 shall be modified in such a manner that paragraph 1 shall apply to the CTAs where the Treaty Partner has not reserved the applicability of this Article. Hence, the applicability of this Article is dependent on the positions adopted by other Treaty Partners.

11. Third-country PE

Article 10 denies treaty benefits for income that the state of residence of the taxpayer attributes to a low-taxed permanent establishment (PE) of the taxpayer in a third country, unless an active trade or business is carried out in that PE.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|---------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 10(1) - 10(3) | ✓ | NA | X | X | X | X | X | ✓ | X | X | ✓ | X |
| Relevant provisions of India treaty amended to the extent not compatible with paragraph 1? | | | X | X | X | X | X | X | ✓ | X | X | ✓ | X |

India has not reserved the applicability of this Article. However, it has also not notified any provisions in the CTA to which this Article should apply to. Therefore, this Article should apply to India's tax treaties, except where the respective Treaty Partner has reserved against the applicability of this Article, or has not notified its treaty with India as a CTA.

12. Savings Clause

Article 11 allows a state to tax its own residents notwithstanding the provisions of a tax treaty.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 11(1) | ✓ | NA | X | X | X | X | ✓ | X | X | X | X | X |
| Relevant provisions of India treaty amended to the extent not compatible with paragraph 1? | | | X | X | X | X | X | ✓ | X | X | X | X | X |

India has not expressly reserved the applicability of Article 11 in its provisional notification. However, in the absence of an express reservation, the provisions of Article 11 will apply to India's CTAs, except where a reservation has been made by one of India's treaty partners.

13. Artificial Avoidance of PE Status – Commissionaire Arrangements

Article 12 lowers the threshold for the existence of a dependent agent PE to include foreign persons acting on behalf of a taxpayer that habitually play a principal role in the conclusion of contracts on behalf or by the taxpayer.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|-------------------------------------|-------------------------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 12(1) and 12(2) ¹⁶ | ✓ | NA | X | X | X | X | X | ✓ | X | ✓ | X | X |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | ✓ | X | ✓ | X | X |

¹⁶. These provisions apply only where both parties to a treaty have notified the treaty with respect to this provision.

Keeping in mind that several of India's treaties already provide for some of the recommended provisions under Article 12 (or a similar version), it is no surprise that India has not chosen to exercise its right of reservation and has accordingly notified all its treaties with respect to both paragraphs 1 and 2 of Article 12. By making this choice India has effectively sought to bring all its treaties in line with the MLI. However, it should be noted that these provisions will only apply to a particular tax treaty to the extent that India's relevant treaty partner has similarly not exercised its right of reservation, and notified India with respect to Article 12. Therefore, where both Treaty Partners have notified Article 12 as being applicable, instances where commissionaire arrangements exist would now constitute a PE, such as in the case of the Japan. There have been several cases in the recent past where the courts have agreed to an expanded view on the agency PE and the implementation of these standards is likely to increase the chances of a tax exposure. Hence, current arrangements should be reviewed to ensure that any tax exposure is anticipated in advance and mitigated.

14. Artificial Avoidance of PE Status – Specific Activity Exemption

Article 13 stipulates that: (a) the specific activity exemption in the treaty definitions of a PE applies only to activities of an auxiliary or preparatory character or (b) the specific activity exemption in the treaty definitions of a PE applies irrespective of whether an activity is of an auxiliary or preparatory character. The anti-fragmentation rule aggregates activities carried on by closely related enterprises for purposes of determining the existence of a PE.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies Option A (specific activity exemption applies only to activities of auxiliary or preparatory character) | 13(2) | ✓ | NA | X | X | X | X | X | ✓ | X | X | ✓ | X |
| Applies Option B (specific activity exemption applies irrespective of whether activity is of auxiliary or preparatory character) | 13(3) | X | NA | X | ✓ | X | ✓ | X | X | X | ✓ | X | ✓ |
| Applies anti-fragmentation rule | 13(4) | ✓ | NA | X | X | X | X | ✓ | ✓ | X | ✓ | ✓ | ✓ |
| Amendment to tax treaty with India? | | | X | X | X | X | X | ✓ | ✓ | X | X | ✓ | X |
| Anti-fragmentation rule applicable to tax treaty with India | | | X | X | X | X | X | ✓ | ✓ | X | X | ✓ | ✓ |

While Parties to the MLI have been given the right to reserve the applicability of Article 13 in its entirety, or reserve against only paragraph 2 or paragraph 4, India has chosen to notify Option A and not exercise its right to reservation with respect to paragraph 4. This essentially means that India's tax treaties will be modified to replace existing provisions with respect to specific activity exemptions with the language of Option A, but only to the extent that India's treaty partner has also notified Option A. In the event that a treaty partner reserves Article 13 or chooses to notify Option B, the tax treaty between India and such country will remain unchanged. Further, by not actively exercising its right to reserve the applicability of paragraph 4, India has agreed to apply the provision to its treaties. However, the change will only take place between India and its treaty partners if such treaty partner also refrains from exercising its right to reserve and has notified its treaty with India for this purpose.

15. Splitting-up of Contracts

Article 14 provides that for the determination if a building site, or construction or installation project constitutes a PE, (i) activities carried on during one or more periods of time that, in the aggregate, exceed 30 days and (ii) connected activities carried on by closely related enterprises, are aggregated.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 14(1) | ✓ | NA | X | X | X | X | X | X | X | X | ✓ | ✓ |
| Reserves the right not to apply provision with respect to existing treaty provisions relating to the exploration for or exploitation of natural resources | 14(3)(b) | X | NA | X | X | X | X | X | X | X | X | ✓ | ✓ |
| Amendment to tax treaty with India? | | | X | X | X | X | X | X | X | X | X | ✓ | ✓ |

As India has neither stated its reservation with respect to Article 14, nor do any of its treaties have existing language with respect to the splitting up on contracts, Article 14 should be applicable to all of India's tax treaties where its relevant treaty partner has also not specified a reservation. This is likely to have an impact on works contracts and the formation of service PEs in India

16. Definition of ‘Closely Related Persons’

Article 15 provides that persons are closely related if one has control of the other or both are under the control of the same person. A close relationship is deemed to exist in case a threshold of 50% of vote and value in a company is met.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|---|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 15(1) | ✓ | NA | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Reserves the right for the entirety of Article 15 not to apply to the Covered Tax Agreement to which the reservations described in Article 12(4), Article 13(6) (a) or (c), and Article 14(3)(a) apply. | 15(2) | X | NA | ✓ | ✓ | ✓ | ✓ | X | X | ✓ | X | X | X |
| Amendment to tax treaty with India? | | | X | X | X | X | X | ✓ | ✓ | X | ✓ | ✓ | ✓ |

India has not exercised its right of reservation with respect to Article 15, and all its treaties stand modified to include this provision to the extent that its relevant treaty partner has also not made such reservation.

17. Mutual Agreement Procedure

Article 16 implements the BEPS minimum standard for mutual agreement procedures which is intended to ensure an effective and timely resolution of treaty-related disputes. The BEPS minimum standard is complemented by optional best practices.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|---------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 16(1) - 16(3) | ✓ | NA | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Reserves the right not to apply the first sentence of 16(1): "Where a person considers that the actions of one or both of the Contracting Jurisdictions result or will result for that person in taxation not in accordance with the provisions of the Covered Tax Agreement, that person may, irrespective of the remedies provided by the domestic law of those Contracting Jurisdictions, present the case to the competent authority of either Contracting Jurisdiction." | 16(5)(a) | ✓ | NA | X | X | X | ✓ | X | X | ✓ | X | X | X |
| Reserves the right not to apply the second sentence of 16(2): "Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting Jurisdictions." | 16(5)(c) | X | NA | X | X | X | X | X | X | ✓ | X | X | X |
| First sentence of para 1 applicable to India treaty? | | | | X | X | X | X | X | X | X | X | X | X |
| Amendment to tax treaty with India? | | | X | X | | | | | | | | | ✓ |

¹⁷. Except the second sentence of 16(2).

India has made a specific reservation against the first sentence of Article 16(1) on the basis that it intends to meet the minimum standard required under the BEPS Action Plan 14. India has not made any additional reservations, and has notified the relevant CTAs with respect to the remaining provisions under Article 16. Keeping in mind that India does not have a reservation against the second sentence of Article 16(1) and that the provision is applicable in the in place of or in the absence of the relevant provision, all of India's CTA should be modified to the extent that the relevant treaty party has not made a reservation with respect to the same.

18. Corresponding Adjustments

Article 17 requires jurisdictions to make an adjustment to the profits of a taxpayer in its jurisdiction if the other contracting jurisdiction makes an at arm's length pricing adjustment to the profits of a taxpayer in that other contracting jurisdiction. Any increase or decrease in that other jurisdiction would be mirrored by a corresponding adjustment to the profits of the taxpayer in the first jurisdiction.

| Options & Reservations | MLI Article | IND | USA | MAU | LUX | SWE | SG | UK | JAP | CAN | FRA | NED | IRE |
|--|-------------|-----|-----|-----|-----|-----|----|----|-----|-----|-----|-----|-----|
| Applies article? | 17(1) | ✓ | NA | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Reserve applicability against treaties which already contain similar provision | 17(3)(a) | ✓ | NA | ✗ | ✗ | ✓ | ✗ | ✗ | ✗ | ✓ | ✗ | ✗ | ✓ |
| Change to India treaty? | | | ✗ | ✗ | ✗ | | ✗ | ✗ | ✗ | ✗ | ✓ | ✗ | ✗ |

India has reserved the right for the entirety of Article 17 not to apply to its Covered Tax Agreements that already contain a provision described in paragraph 2 of Article 17 of the MLI.

For a more detailed analysis of India's MLI position, please refer to the research paper by Nishith Desai Associates available at the following address:

http://www.nishithdesai.com/fileadmin/user_upload/pdfs/Research_Papers/India_s_MLI_Positions.pdf

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