Overview

- Under the OECD*/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), more than 125 countries are collaborating to put an end to tax avoidance strategies that exploit gaps and mismatches in tax rules to avoid paying tax
- MLI is an outcome of BEPS Action Plan (AP) 15 of the OECD/G20 Inclusive Framework, which offers solutions for governments to plugs loopholes in international tax treaties by transposing results from the BEPS project into bilateral tax treaties worldwide
- MLI allows governments to modify application of its network of bilateral tax treaties in a synchronised manner without renegotiating each of these treaties bilaterally
- In November 2016, MLI was agreed upon by more than 100 participating jurisdictions**
- MLI came into force on 1 July 2018***
- More than 1,500 tax treaties are expected to be modified
- Till now 89 jurisdictions**** have signed the MLI (30 of these have deposited their instruments of ratification, acceptance or approval [‘ratification instrument’] along with the OECD Secretariat along with its list of reservations and notifications [‘MLI positions’])

** INDIA’s position**

a) 25 June 2019: Ratification instrument deposited with the OECD (with definitive MLI positions)
b) India’s MLI positions – Refer section ‘India’ MLI position (Article-wise)’

Broad Architecture of MLI

**MLI consists of 39 Articles (MLI Articles):**

- Articles 1 and 2 set out the scope of MLI and the interpretation of terms used therein
- Articles 3-17 deal with BEPS tax treaty measures
- Articles 18-26 cover provisions related to mandatory binding arbitration
- Articles 27-39 contain procedural provisions such as provisions relevant to adoption and implementation of the MLI including ratification, entry into force and entry into effect dates, withdrawal, etc

OECD website includes a list of signatories of the MLI, information on the Articles of the MLI that these signatories have chosen to opt, and an MLI Matching Database

Explanatory statement to the MLI amplifies the understanding of MLI Articles

Structure of the MLI

Jurisdictions that sign the MLI are required to adopt MLI provisions forming part of the agreed minimum standards:

• Articles 6 and 7 reflect the minimum standard for prevention of treaty abuse under BEPS AP 6
• Article 16 reflects the minimum standard for improvement of dispute resolution under BEPS AP 14

Opting out of these provisions (forming part of agreed minimum standards) is possible only in limited circumstances

Optional changes to tax treaties in the MLI include:

• Tax treaty benefits eligibility in case of fiscally transparent entities (Article 3)
• Tiebreaker rules for dual resident entities (Article 4)
• Different options for eliminating double tax relief (Article 5)
• Minimum shareholding periods to benefit from the provision related to dividends (Article 8)
• Changes to the definition of a permanent establishment (Article 12), etc

For such MLI provisions, there is generally flexibility to opt out of either all or part of the provision

How the MLI Operates?

• Each party to the MLI must notify tax treaties to which the MLI provisions would apply. MLI provisions would apply to a tax treaty only if both parties to the tax treaty notify it as Covered Tax Agreement [CTA]

• For a specific bilateral tax treaty, MLI would have effect after both parties to a CTA have deposited their ratification instruments with the OECD Secretariat

• MLI would modify application of all CTAs at least to the extent of implementation of following minimum standards viz:
  1) Counter treaty abuse (through Article 6 - purpose of CTA and Article 7 - prevention of treaty abuse)
  2) Improve dispute resolution (through Article 16 – mutual agreement procedure)

• Flexibility to implement BEPS tax treaty measures in various ways:
  – Choices to apply optional and alternative provisions
  – Reservations to opt out of provisions or parts of provisions that are not minimum standards (either for all CTAs, or a select CTAs)
The India Story

24 Nov 2016
Publication of MLI

7 Jun 2017
Signing ceremony: 68 jurisdictions including India signed MLI

1 Jul 2018
MLI entered into force

13 Jun 2019
Indian Government approved ratification of MLI

25 Jun 2019
Deposit of ratification instrument (along with final MLI positions) by India

1 Oct 2019*
MLI enters into force for India

1 Apr 2020
MLI provisions to enter into effect for 23 Indian bilateral tax treaties**

*That is, on the first day of the month following the expiration of three months beginning on the date of deposit of ratification instrument by India with the OECD Secretariat

**That is, Indian tax treaties with jurisdictions that have already deposited their ratification instrument with the OECD Secretariat latest by 30 June 2019 and have notified tax treaty with India as CTA.
**Indian CTAs**

**MLI to enter into effect from 1 April 2020**

<table>
<thead>
<tr>
<th>List of jurisdictions that have notified tax treaty with India as CTA and have deposited their ratification instruments with OECD Secretariat by 30 June 2019</th>
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</thead>
<tbody>
<tr>
<td>Austria</td>
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<td>Finland</td>
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<td>Ireland</td>
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<td>Lithuania</td>
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<td><strong>Netherlands</strong></td>
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<td>Russia</td>
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<td>Slovak Republic</td>
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<td><strong>United Kingdom</strong></td>
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“Entry into effect” with respect to CTA [Article 35]

**A. For Withholding Taxes (WHT):** On or after the first day of the next calendar year following the latest of the dates on which MLI enters into force for each of the party to the CTA. India has chosen to substitute “calendar year” with “taxable period”

**B. For other taxes:** Taxable period beginning on or after the expiry of six calendar months following the latest of the dates on which MLI enters into force for each of the party to the CTA

In relation to Indian tax treaties with jurisdictions tabulated (23), MLI to enter into effect for India from 1 April 2020 (for WHT and other taxes)

**CTAs that get modified next ...**

- Where CTA party deposits ratification instrument latest by 31 December 2019, MLI to come into effect from 1 April 2020 for WHT and 1 April 2021 for other taxes for example Norway, which deposited its instrument of ratification on July 17, 2019
- MLI will not impact a) India-USA tax treaty (since USA has not signed MLI) and b) India tax treaties with China*, Germany, and Mauritius (since Indian tax treaties are not notified by said parties/ India)

*India and China have recently amended its tax treaty through protocol signed on 26 November 2018. Amongst others, protocol incorporates changes required to implement treaty related minimum standards agreed under BEPS project*
Key impact areas vis-a-vis Indian Tax Treaties

For evaluating extent of modification of the Indian tax treaty, India's MLI positions need to be compared with the MLI positions taken by its counterpart. Refer snapshot of these impact areas vis-à-vis select Indian tax treaties

*India and China have recently amended its tax treaty through protocol signed on 26 November 2018. Amongst others, protocol incorporates changes required to implement treaty related minimum standards agreed under BEPS project
Overview of MLI positions of Select CTA parties

Prevention of treaty abuse
- Preamble and PPT to apply to all Indian CTAs
- Opted to apply SLOB: India, Russia, Norway
- Opted to not apply SLOB: France, Netherlands, Singapore, UK, Luxembourg, Australia, New Zealand, Sweden

Broader agency PE rule
- Opted to apply: India, France, New Zealand
- Opted to not apply: Netherlands, Singapore, UK, Luxembourg, Australia, Sweden

PE specific activity exemption
- Opted to apply*: Option A - India, Netherlands, New Zealand, Australia
- Option B – France, Singapore, Luxembourg
- Opted to not apply: Sweden

Splitting-up of contracts
- Opted to apply: India, Netherlands, New Zealand, Australia
- Opted to not apply: France, Singapore, UK, Luxembourg, Sweden

MLI Impact on Select Indian Tax Treaties - Snapshot
MLI provisions to enter into effect for following Indian tax treaties from 1 April 2020 for both WHT and other taxes

India-France tax treaty
- Only PPT to be added since France has not opted for SLOB
- Broader agency PE rule applicable since France has notified India tax treaty
- Avoidance of PE status through specific activity exemptions related provision not applicable since France has not chosen same option
- Splitting up of contracts related provision not applicable since France has made a reservation

India-UK tax treaty
- Only PPT to apply since UK has not opted for SLOB
- Broader agency PE rule not applicable since UK has made a reservation
- Avoidance of PE status through specific activity exemptions related provision not applicable since UK has not chosen any option
- Splitting up of contracts related provision not applicable since UK has made a reservation

India-Netherlands tax treaty
- Only PPT to be added since Netherlands has not opted for SLOB
- Broader agency PE rule not applicable since Netherlands has made a reservation
- Avoidance of PE status through specific activity exemptions related provision applicable since Netherlands has chosen same option
- Splitting up of contracts related provision applicable

India-Singapore tax treaty
- Only PPT to apply since Singapore has not opted for SLOB
- Broader agency PE rule not applicable since Singapore has made a reservation
- Avoidance of PE status through specific activity exemptions related provision not applicable since Singapore has not chosen same option
- Splitting up of contracts related provision not applicable since Singapore has made a reservation

*To apply to particular CTA, if both CTA parties chose to apply same option. Also, whilst option A provides that exemption from PE is available only if all the activities carried on are preparatory and auxiliary in nature, option B broadly provides specific activity exemption as per OECD Model Convention 2014.
MLI’s Challenges and Review Areas

- Interplay of PPT with general anti-avoidance rules (GAAR) under the Indian domestic law
- Impact of PPT rule, in select treaties, on grandfathered income/investments
- Consequences that may arise if the MLI provisions come into effect separately for WHT and other taxes
- Practical challenges in reading MLI provisions that effect CTA given the number of documents, viz. MLI text, MLI positions of CTA partners, etc., to be read together
- Availability of tax treaty benefits to fiscally transparent entities (on account of India’s reservation to Article 3 of MLI)*
- Existing MNEs operating structures in India require review in light of the expanded PE rules

*Indian judiciary had evaluated subject issue in the past. In Linklaters LLP vs ITO [2010] 40 SOT 51 (Mumbai) and Clifford Chance vs DOT [2002] 82 ITD 106 (Mumbai), it has been held that UK partnership was eligible to claim tax treaty benefits under the India-UK tax treaty where partners were also subject to tax in the UK. However, there is contrary ruling as well [ref: Schellenberg Wittmer [2012] 24 taxmann.com 299 (AAR - New Delhi)], wherein tax treaty benefits were denied to Swiss-based partnership.
### India’s MLI positions (Article wise)

<table>
<thead>
<tr>
<th>MLI Article</th>
<th>Brief description of the Article</th>
<th>India’s final position</th>
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</thead>
<tbody>
<tr>
<td>Article 2: Interpretation of terms</td>
<td>Notification of tax treaties covered by MLI convention</td>
<td>India has notified 93 tax treaties</td>
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<tr>
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<td>Tax treaties not notified by India: China and Marshall Islands</td>
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<tr>
<td>Article 3: Transparent entities</td>
<td>Tax treaty benefits to be allowed to fiscally transparent entities for the income earned to the extent that such income is taxed in the jurisdiction in which the entity is a resident</td>
<td>India has made a reservation and thus, not to apply to its CTAs</td>
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<tr>
<td>Article 4: Dual resident entities</td>
<td>CAs of both jurisdictions to mutually agree on the manner to determine the residential status of dual resident non-individuals regarding place of effective management, place of incorporation or constitution, and any other relevant factors. In the absence of such agreement, treaty benefits to be denied to such a person (unless otherwise agreed by them)</td>
<td>India has opted for application of such provision; said provision to apply to all its CTAs (unless reservation is made by other CTA partner)</td>
</tr>
<tr>
<td>Article 5: Application of methods to eliminate double taxation</td>
<td>Recommends three options for elimination of double taxation inter-alia including “Option C”, which prescribes application of credit method</td>
<td>India has chosen to apply Option C (i.e., credit method); the said option to apply to all its CTAs for its own residents</td>
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<td>Indian tax treaties generally contains credit method except in select cases (For e.g., tax treaty with Bulgaria, Greece, Egypt, Slovak Republic that contains exemption method). Therefore, exemption method in such select cases to be replaced by “credit method”</td>
</tr>
<tr>
<td>Article 6: Purpose of CTA (minimum standard)</td>
<td>Introduces preamble text in CTA stating that the jurisdictions intend to avoid creation of opportunities for non-taxation or reduced taxation through tax evasion or avoidance, and through treaty shopping</td>
<td>India is silent on its position. Being minimum standard, such MLI provision to apply to all its CTAs</td>
</tr>
<tr>
<td>Article 7: Prevention of treaty abuse (minimum standard)</td>
<td>Envisages following three anti-abuse measures to meet the minimum requirement: A. PPT B. PPT supplemented with either SLOB or detailed LOB clause C. Detailed LOB provision, supplemented by a mutually negotiated mechanism to deal with conduit arrangements not already dealt with in CTA</td>
<td>India has opted for PPT + SLOB. PPT being minimum standard, it will apply to all its CTAs</td>
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<td>India has accepted to apply PPT as an interim measure and intends where possible to adopt LOB provision, in addition or replacement of PPT, through bilateral negotiations</td>
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<td>Not opted for competent authority route under Article 7(4) of MLI and thus, not applicable</td>
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<td></td>
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<td>SLOB to be applicable only where other CTA partner has adopted it or allowed India to apply SLOB asymmetrically</td>
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<tr>
<td>MLI Article</td>
<td>Brief description of the Article</td>
<td>India’s final position</td>
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<tr>
<td>Article 8: Dividend transfer transactions</td>
<td>Introduces additional criteria of “365 days minimum holding period” for the shareholder to avail concessional tax rates under CTA</td>
<td>India has <strong>opted to apply</strong> such provision (except in case of India-Portugal tax treaty, which already contains similar provision) Thus, said MLI provision to apply to all its CTA except India-Portugal treaty (unless reservation is made by other CTA partner)</td>
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<tr>
<td>Article 9: Capital gains from alienation of shares or interest of entities deriving their value principally from immovable property</td>
<td>Introduces additional criteria of “365 days minimum holding period” in case of gains arising from alienation of shares or other participation rights if such shares or rights derive more than a specified percentage of their value from immovable property situated in the source jurisdiction</td>
<td>India has <strong>opted to apply</strong> minimum holding period threshold along with minimum value derivation criterion of 50 percent. The said provision to apply to CTA only if other CTA partner has chosen to apply the said provision</td>
</tr>
<tr>
<td>Article 10: Anti-abuse rule for PE in third jurisdiction</td>
<td>Addresses abuse of CTAs in a triangular situation</td>
<td>India is <strong>silent</strong> on its position; the said provision to apply to all its CTA (unless reservation is made by any other CTA partner)</td>
</tr>
<tr>
<td>Article 11: Application of tax agreement to restrict a party’s right to tax its own residents</td>
<td>Preserves the right of jurisdiction to tax its own residents</td>
<td>India is <strong>silent</strong> on its position; the said provision to apply to all its CTA (unless reservation is made by any other CTA partner)</td>
</tr>
<tr>
<td>Article 12: Artificial avoidance of PE status through commissioner and similar strategies</td>
<td>Widens the definition of PE given in tax treaties to include cases where a person habitually concludes contracts or plays a principal role in conclusion of contracts of another enterprise</td>
<td>India has <strong>opted</strong> to apply the said provision; the said provision to apply to a CTA only if any other CTA partner has chosen to apply the said provision</td>
</tr>
<tr>
<td>Article 13: Artificial avoidance of PE through specific activity exemptions</td>
<td>Provides two options to counter artificial avoidance of PE status through specific activity exemptions. “Option A” states that exemption from PE is available only if the activities carried on are of preparatory and auxiliary nature Additionally, it provides for anti-fragmentation rule</td>
<td>India has <strong>chosen to apply Option A</strong>, the said option to apply to CTA only if other CTA partner has chosen same option</td>
</tr>
<tr>
<td>Article 14: Splitting up of contracts</td>
<td>Addresses avoidance of PE by splitting the contracts between related enterprises to circumvent the threshold of PE creation</td>
<td>India has <strong>chosen to apply anti-fragmentation rule</strong>, the said rule to apply to a CTA only if other CTA partner has chosen to apply the said provision</td>
</tr>
<tr>
<td>Article 15: Definition of a person “closely related to an enterprise”</td>
<td>Defines the term “person closely related”, in the context of Articles 12, 13, and 14 of the MLI</td>
<td>India is <strong>silent</strong> on its position; the said provision to apply to all its CTA (unless reservation is made by any other CTA partner)</td>
</tr>
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<tr>
<td>Article 16: Mutual agreement procedure [Minimum standard]</td>
<td>Requires MAP request to be made to either state, or implement a bilateral notification or consultation process</td>
<td>India has reserved its right for not adopting the modified MLI provisions on the basis that it will meet the minimum standard by allowing MAP access in the resident state and implementing bilateral notification or consultation process</td>
</tr>
<tr>
<td>Article 17: Corresponding adjustments</td>
<td>Requires jurisdictions to make appropriate corresponding adjustments in transfer pricing cases</td>
<td>India has chosen to apply the said provision except for CTAs where the provisions already exist</td>
</tr>
<tr>
<td>Bilateral APA and MAP allowed even in absence of Article 9(2) – clarified by CBDT vide press release dated 27 November 2017</td>
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<tr>
<td>Article 18-26: Mandatory binding arbitration</td>
<td>Provides mandatory binding arbitration in cases where competent authorities are unable to reach an agreement to resolve a case under MAP</td>
<td>India has not opted for mandatory arbitration</td>
</tr>
<tr>
<td>Article 35: Entry into effect</td>
<td>Effect of provisions of the MLI</td>
<td>India has chosen to substitute “calendar year” with “taxable period”</td>
</tr>
<tr>
<td>If other CTA partner opts for calendar year, date of applicability of MLI provision for such other CTA partner will differ via-a-vis as for India</td>
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</tbody>
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India’s Final MLI Positions viz-a-viz Provisional MLI Positions

<table>
<thead>
<tr>
<th>Provisional List*</th>
<th>Final List**</th>
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</thead>
<tbody>
<tr>
<td>• India notified China as a CTA</td>
<td>• India excluded tax treaty with China as CTA; added Hong Kong to the list of CTAs</td>
</tr>
<tr>
<td>• India had made reservation against application of Article 5 of MLI suggesting options for double taxation elimination</td>
<td>• India opted for Option C; Option C is broadly in line with the tax credit method</td>
</tr>
<tr>
<td>• India accepted PPT, being the minimum standard; in addition, chose to apply SLOB subject to CTA party’s position</td>
<td>• India has additionally noted its intent stating that whilst it accepts PPT as an interim measure, it intends to adopt LOB provision in addition to or in place of PPT vide bilateral negotiations</td>
</tr>
<tr>
<td>• For “entry into effect”, India had made a reservation to consider reference date as 30 days after the date when the depositary receives latest notification to the effect that such country has chosen this reservation and completed its internal procedures for entry into effect of MLI provision</td>
<td>• Deleted</td>
</tr>
</tbody>
</table>

*Submitted by India at the time of signing the MLI
**Submitted by India at the time of depositing the ratification instrument
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