

Indian Tax Authorities eye on treaty-shopping – denying benefits where arrangement/transaction lacks commercial substance¹

Whereas Governments of various countries are formulating policies for increasing foreign investments, on the other hand, some countries are moving towards source-based taxation and framing laws to charge tax on income derived or deemed to be derived in source countries. Such action is seen through ratification of Multilateral Instruments² ('MLI') by some of the countries in line with the Base Erosion and Profit Shifting ('BEPS') Action Plan. Statistics³ demonstrate that India has received the maximum foreign direct investments (FDI) in various sectors from countries, like Singapore (US\$ 11.65 billion), Mauritius (US\$ 7.45 billion), Netherlands (US\$ 3.53 billion), Japan (US\$ 2.80 billion) and the USA (US\$ 2.79 billion). Laws in a few of these jurisdictions and even the Double Tax Avoidance Agreements ('DTAA') entered into with these countries, provide a favorable position for the investors. However, simultaneously the tax authorities are closely monitoring the DTAA / treaty benefits availed by the investors, to ensure that the investors are not indulging in treaty shopping.

Though said by various scholars that taxes are never certain, to encourage investments, it is imperative to provide certainty in tax laws, in order to evaluate their return on investments. Tax plays an important role in the investment decisions, as it constitutes a considerable part⁴ of the cost of investments. In this article, the authors have dealt with the capital gains tax benefit regime under some of the DTAA's, requirements for availing the benefit of DTAA, recent judicial decisions, impact of MLI and the care that needs to be taken by the investors in claiming DTAA benefits in the light of the anti-abuse rules.

Capital gains tax benefit under the DTAA

In the past, investments made from certain jurisdictions (such as, Mauritius, Singapore, Cyprus, etc.) enjoyed certain benefits in respect of capital gains taxation on transfer of such investments. Such benefit was reduced / withdrawn by amending the DTAA provisions in the year 2017. For example, capital gains on transfer of Indian shares, which were earlier taxable in the jurisdiction where the transferor is a resident, has been amended to tax such gains in the jurisdiction

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where the company (whose shares are transferred) is a resident. Nevertheless, grandfathering benefit was provided for investments made before April 1, 2017. In case, where the investments were made on or after April 1, 2017 and were sold during the period April 1, 2017 to March 31, 2019, gains on such investments were taxed at a reduced rate. Such amendments were introduced in the DTAA's entered into by India with Mauritius and Singapore.

Requirements of availing the DTAA benefit

Section 90(4) of the Income Tax Act, 1961 ('IT Act') provides that the non-resident taxpayer would not be entitled to DTAA benefit, unless a tax residency certificate ('TRC') from the country in which the taxpayer resides, is furnished. In fact, in the past, there has been a controversy as to whether the TRC is sufficient to claim DTAA benefit and for claiming beneficial ownership. It would be important to note that the Central Board of Direct Taxes⁵ ('CBDT') had issued a clarification⁶ that once a company furnishes a valid and subsisting TRC of Mauritius, the same would suffice to conclude that the company is a tax resident of Mauritius and also holds beneficial ownership. Thereafter, the Supreme Court (being the Apex Court) of India also upheld⁷ the Circular to be valid. The Apex Court gave a finding that DTAA shopping is not considered to be illegal and further the motive of incorporation of

the company in Mauritius is irrelevant. The Court held that it was not permissible for the judiciary to treat the intervening legal steps as non-est, based upon some hypothetical assessment of the 'real motive' of the taxpayer. The said decision was rendered distinguishing the earlier decision in the case of McDowell & Co. Ltd.⁸, which had the occasion of dealing with the concept of tax planning v/s tax avoidance. It was held that a colorable device cannot be a part of tax planning. However, in another landmark case, the Supreme Court⁹ noted that the above circular would not prevent the tax authorities from denying DTAA benefits, if it was substantiated that an entity was interposed solely for the purposes of avoiding capital gains tax.

The following principles / provisions would need consideration when claiming DTAA benefits:

- Test of 'substance over form';
- General Anti-Avoidance Rules ('GAAR') prescribed under the Indian domestic tax laws (IT Act). It would be important to note that investments made before April 1, 2017 are grandfathered from GAAR provisions;
- Conditions specified in the Limitation of Benefit ('LOB') clause provided under some of the DTAA (especially, Singapore);
- Principle Purpose Test ('PPT') introduced through the MLI in the Covered Tax Agreement, from April 1, 2020 by some countries (especially, Singapore).

It appears that the tax authorities are closely monitoring cases where treaty benefits have been claimed (especially, Indo-Mauritius DTAA, where LOB article is not applicable for investments made before April 1, 2017) and they are adopting the test of 'substance over form'. Recently, a number of judicial decisions have been rendered which underscore this and the same are discussed below in order to be well-versed with the interpretations adopted by the Judicial Authorities.

Judicial rulings rendered in the context of Indo- Mauritius DTAA

a) Tiger Global International II Holdings¹⁰

An application was preferred by the Applicants (Tiger Global International II Holdings and its group entities) before

the Authority of Advance Ruling ('AAR') to assess the tax implication of sale of shares of a Singapore based company, which had in-turn invested in the equity shares of an Indian Company. The facts of the case, ruling rendered and the key takeaways are as follows:

Facts

- The Applicants were companies registered in Mauritius ('MCo'), possessing a TRC of Mauritius. They were set up for investment activities, with the intention of earning long-term capital appreciation and investment income.
- A Co. (registered in USA), held shares of the applicant companies (MCo) (registered in Mauritius).
- MCo had invested in the equity shares of a Singapore Company, which derived its value from the shares held in an Indian Company (Flipkart Private Limited).
- In the year 2018, MCo transferred shares of the Singapore Company to a Luxemburg Company and contended that the gains arising on transfer of shares of the Singapore Company were not taxable in India. The Applicant also preferred an application before the Tax Authorities, under section 197 of the IT Act for 'NIL' withholding certificate. However, the same was rejected by the tax authorities on the ground that MCo was not independent in its decision making. MCo preferred an application before the AAR for determining the taxability of gains arising from transfer of shares of the Singapore Company under the Indo- Mauritius DTAA.

AAR Ruling

AAR held that the application was not admissible under section 245R¹¹, as the transaction was *prima facie* designed to avoid tax. While coming to this conclusion, the AAR relied upon, among others, the following:

- Real control and management of MCo was with the US entity's founder and partner of the US entity (i.e. Mr. X). Accordingly, the place of effective management was located outside Mauritius.
- Director (Mr. X) in the MCo was the director of the entire group based in

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US and was a signatory to the Bank accounts of MCo.

- MCo was a see-through entity and the ultimate beneficiary was a US resident. For this, the AAR observed that Mr. X was disclosed as the beneficial owner in the application for 'Global Business License' filed with the Mauritian authorities.
- MCo was not having power to make investments (beyond a prescribed limit), without the approval of the said director.
- Applicant has only made investment in this Singapore Company (deriving value from the shares of the Indian Company) and not in any other entities.
- Grandfathering benefit (i.e. gains on transfer of investments before April 1, 2017) as per revised DTAA entered into between India and Mauritius is applicable only in cases where alienation of shares of an Indian company takes place and it does not cover sale of offshore company shares, the value of which is derived from the assets of the Indian company.

Based on this, the AAR held that the applicants were not entitled to claim the benefit of exemption of capital gains under the Indo- Mauritius DTAA on the sale of shares of the Singapore Company, whose shares derived value from the shares of the Indian company (i.e. indirect transfer of Indian company shares).

Key takeaways

- AAR rejected the application by making a far-reaching observation that the structure was designed to avoid tax. The decision was rendered relying upon the decision in the case of Vodafone International Holdings B.V.¹², and by applying the test of 'substance over form' and lifting the corporate veil.
- Unfortunately, the AAR has not given proper reasonings as to how factors, like, notes to the financial statements, signatory to the bank accounts, etc. are sufficient to establish that the only purpose for making investments through Mauritius was to obtain the DTAA benefits.
- AAR has, in a way, applied Article 27A - Limitation of Benefits (LOB)¹³ (introduced in the Indo- Mauritius DTAA from April 1, 2017) to conclude that the applicant was

a shell/conduit and the beneficial owner was a US Tax Resident. However, what needs to be observed is that fulfilment of the LOB clause is not applicable to Article 13(3A), dealing with capital gains on sale of investments made before April 1, 2017, granting grandfathering benefit. The LOB clause is also not applicable to Article 13(4), dealing with the residual category of alienation of assets (in this case, it was indirect transfer of Indian shares). This itself indicates that the legislature, while framing the LOB clause, intended to grant DTAA benefit for investments made before April 1, 2017 and also to cases where there were indirect transfer of assets, which fall within the residual category, wherein capital gains would be taxable only in the jurisdiction where the alienator is a resident.

- Mauritius has not notified India for the purpose of MLI. Thus, the Indo-Mauritius DTAA cannot be treated as Covered Tax Agreement ('CTA'). Yet, it seems that the AAR attempted to inflict the Principal Purpose Test ('PPT') provision to hold that the arrangement was framed, with the principal purposes to avoid tax.
- Apart from the correctness of the observations made on the factual aspects, the question that remains is whether such assessment of the arrangement undertaken to determine, as to whether there was any treaty shopping or colorable device deployed to avoid tax, is tenable in law? Also, whether such assessment is justified even in case of indirect transfer of shares of an Indian Company.
- AAR held that grandfathering provisions as per revised DTAA entered into between India and Mauritius are not applicable in the case of indirect transfer of shares of an Indian company. However, taxpayers argue that capital gains should be exempted on the basis of the old tax treaty between India and Mauritius, if the structure/arrangement was already in existence before the tax treaty between India and Mauritius was revised and, therefore, decision rendered by Supreme Court in the case of Azadi Bacho Andalon (cited supra) should apply.

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b) Bid Services Division (Mauritius) Ltd.¹⁴

An application was preferred before the AAR to determine taxability of gains arising on transfer of shares of an Indian Company by a Mauritian Entity under the Indo-Mauritius DTAA. The facts of the case, ruling rendered and the key takeaways are as follows:

Facts

- Applicant is a Mauritian Entity ('**BSDM Mauritius**') and a wholly owned subsidiary of a South African parent ('**Bid Africa**'), which in turn is held by a South African listed Company ('**Bidvest**'). The applicant had obtained a valid Mauritius TRC and had its place of effective management in Mauritius.
- Applicant was a part of the consortium to bid for an Indian project (i.e. civil airport project).
- Applicant had subscribed to the 27% shareholding in the Indian Target on various occasions, starting from the year 2006. In 2011, the Applicant sold 13.5% of the shares to the Indian company.
- The Applicant contended that the gains arising on transfer of Indian shares are not taxable under the Indo- Mauritius DTAA and for this, it relied on a number of decisions.¹⁵

AAR Ruling

The AAR applied the 'look through' approach and denied the Indo- Mauritius DTAA benefit. For coming to this conclusion, the AAR observed as follows:

- Applicant company was incorporated only two weeks prior to submission of the final consortium bid, even though substantial correspondence and bidding procedures took place before the said date.
- Name of the applicant was not reflected in any of the documents during the key stages of the bid process.
- Applicant was a shell company, without any tangible assets, employees on its payroll, office space, etc. Unlike, London or New York, Mauritius is not a known financial center or a vibrant business hub from where capital can be sourced at cheaper rate or top-quality professionals/ engineers/ consultants could be employed. Mauritius cannot boast of being a seat of civil aviation experts.

- Applicant was only noting and endorsing the decisions of the parent company in the Board meetings, without any contribution or discussions in the decision-making process. Thus, the Applicant was not in a position to create any value for the Indian venture.
- No commercial justification for setting up a company in Mauritius was provided. In fact, the AAR observed that the company could equally have been formed, either in South Africa or in India.
- The beneficial ownership of the capital gains was with the parent company, located in South Africa (outside Mauritius). Further, the dominant purpose for interposing the Mauritius Company in the structure was to avoid tax.
- Holding of TRC cannot prevent an enquiry, if it can be established that the interposed entity was formed to avoid tax.

Key Takeaways

- AAR in this ruling as well, has not reasoned whether the prevention of abuse provisions as notified in the DTAA and the domestic laws are fulfilled in order to invoke the same and deny the benefits availed. The prevention of abuse provisions was not applicable in the present transaction, since the shares were acquired before April 1, 2017.
- However, the AAR assessed the commercial substance of the arrangement and moped with the practice of treaty shopping. The AAR chose to assess the facts of the case to conclude that the transaction or for that matter, the arrangement of incorporating the company in Mauritius lacked commercial substance and was structured to avoid tax.
- For determining the beneficial ownership test, one can also take into consideration the period of time for which the Indian company shares were held prior to transfer. In this case, the Applicant held the shares for more than 5 years prior to the transfer. Attention is invited to the decision of the Hon'ble Bombay High Court ruling in the case of JSH Mauritius Limited¹⁶, where the key factor on the basis of which DTAA relief was

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allowed, was that the shares were held for 13 years prior to transfer. The AAR has relied upon the decision in the case of Vodafone (cited *supra*), however, it has not considered the principle laid down in this decision, that the period of time for which the shares are held by such holding companies are also relevant. Also, there could be a number of other factors that are required to be considered for choosing the jurisdiction (in this case, Mauritius), like ease of doing business, access to Asian markets, etc.

c) Becton Dickinson (Mauritius) Ltd.¹⁷

The Applicant, Becton Dickinson (Mauritius) Ltd., a tax resident of Mauritius, applied for a ruling on the taxability of gains arising from transfer of shares of an Indian Company to a Singaporean Company. The facts of the case, ruling rendered and the key takeaways are as follows:

Facts

- Applicant held 100% equity shares in an Indian Company. In March 2012, the Group undertook a worldwide group restructuring, wherein the applicant transferred its investment in the Indian Company to a Singaporean Company at Fair Market Value ('**FMV**').
- Consideration was discharged by the Singaporean Company through issue of shares of the Singaporean entity.

AAR Ruling

The AAR allowed the benefit of capital gains tax article on the basis of following key facts:

- Applicant was legal owner of the shares and the sale transaction was backed by a Board resolution.
- Applicant was established for 15 years, carrying on the business and had continued with the business even after the exit. Since the transaction satisfied all the parameters of 'participation of investment', the Court did not need to investigate de facto control v. legal control.
- AAR observed that when the holding company is providing funds to a subsidiary, it is imperative that the holding company will be involved in important decision making, e.g., in areas of deciding the object, its target market, making investments, etc. in

order to ensure that the activities of the subsidiary are in consonance with the overall goal of the holding company.

- Referring to the decision of the Apex Court in the case of Vodafone International Holdings B.V.¹⁸, it was held that merely because the funding for investment was made from a third country, the arrangement cannot be said to be entered into to evade tax.
- Benefit of the CBDT Circular (cited *supra*) can be granted, when the intent and activities of the Applicant are found to be in order. Further, the tax treaty should be honored in good faith.

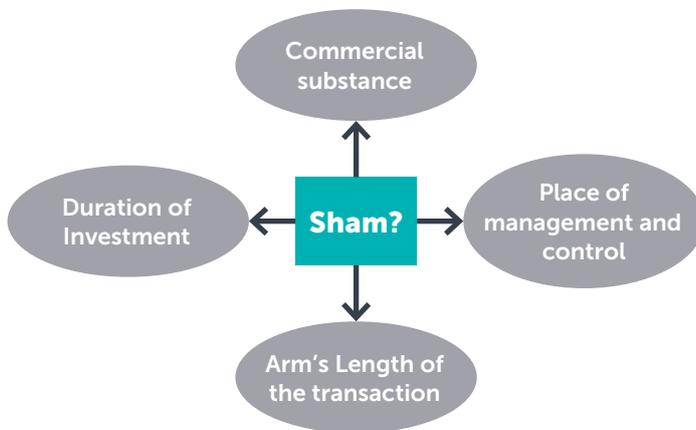
Key takeaways

- AAR rendered this decision for a transaction that had taken place in the year 2012, i.e. before the amendment made in the Indo-Mauritius DTAA. However, the principle remains the same, i.e. whether any benefit accruing as per the DTAA provisions can be denied by applying the test of 'substance over form'.
- The Mauritian company had commercial substance beyond the transaction and was an operational company and not merely an investment company. Further, the tax authorities were unable to prove that the Mauritius company lacked substance. In fact, the company was engaged in genuine business and earned revenue pre and post entering into of the transaction to sell the shares of an Indian Company.
- This ruling recognizes the practicalities of a holding-subsidary relationship and allows room for the parent's role. The ruling also takes into consideration the fact that the investments were made for a considerable length of time.
- Though the benefit of the CBBT circular was granted, the AAR has observed that the intent and activities of the applicant are found to be in order.

From the decisions discussed so far, the principle that emerges is that where the arrangement has commercial substance and is not merely a conduit to avoid tax, the tax authorities have granted the DTAA benefits availed on the basis of TRC.

Summary of recent Judicial AAR rulings¹⁹ in light of MLI provisions

- The judicial rulings given recently indicate that the appellate bodies are now evaluating the facts of the investors and weighing the commercial substance of the transaction, to ensure that the arrangement is not framed as a colorable device to avoid tax, notwithstanding the fact that the investments were made before April 1, 2017 (i.e. before the amendment was made in the Indo-Mauritius DTAA). Some of the parameters that are considered by the Indian tax authorities for determining the commercial substance of the arrangement / transaction are detailed below:



- The vital question that requires consideration is whether such assessment is justifiable in the eyes of law, where the prevention of the anti-abuse provisions framed under the DTAA and the domestic provisions do not intend to cover such transactions. Can a proposition be made that evaluating the commercial substance of the arrangement / transaction and verification of the look-through status of the entity can be done in all arrangements, irrespective of whether the same is expressly provided in Law? Or, whether while analyzing the DTAA provisions, can it be said that when such prevention of anti-abuse provisions does not cover a particular transaction, the legislature had intentionally excluded such arrangements / transactions.

- A reference may be made to Article 7 of the MLI, which provides a minimum standard dealing with the prevention of the treaty abuse provisions. The said Article pronounces a Principal Purpose Test ('PPT'), which denies benefit of the tax treaty, where it is reasonable to conclude, considering all relevant facts and circumstances, that obtaining such benefit was one of the principal purposes for entering into a specific transaction or an arrangement that resulted, directly or indirectly in that benefit, unless where granting that benefit is not contrary to the object and purpose of the relevant provisions of the CTA.

It would be noted that the said Article starts with a "Non-obstante" clause and therefore such Article would override all the other Articles including the Article dealing with the LOB clause. Accordingly, where one of the primary purposes of any arrangement was to obtain tax benefit, PPT clause could get triggered.

Ideally speaking, one could contend that obtaining a tax benefit generally remains one of the primary purposes, while evaluating any business transaction or arrangement. This would include assessing various jurisdictions for setting up the entity etc. Thus, PPT clause may get triggered in such arrangements. In such a situation, the phrase that needs attention is "unless if granting that benefit is not contrary to the object and purpose of the relevant provisions of the Covered Tax Agreement".

Thus, when and under what circumstances can such exception be availed? The moot question revolves around the interpretation of the clause "the object and purpose of the relevant provisions of the Covered Tax Agreement".

- Can it be interpreted that the arrangement should be in line with the object or preamble of the CTA to get covered by the said clause? If this could be the interpretation, as an illustration, reference may be made to the CTA of Singapore. The preamble to the said CTA reads as "desiring to conclude an Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income.

Further, Intending to eliminate double taxation with respect to the taxes covered by this Agreement 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 the Agreement for the indirect benefit of residents of third jurisdictions)”.

It would be noted that the preamble does not refer to any objects such as promoting cross border investments or otherwise. In such cases, claim of benefit under the capital gains Article could be questioned in case of Singapore DTAA, where it is established that one of the primary purposes was to obtain tax benefit. Such a situation would even deny the grandfathering benefit granted towards capital gains.

- Another interpretation which could be adopted is in situations where any benefit is granted under the **“relevant provisions of the Covered Tax Agreement”**, i.e. object of any specific Article needs to be referred to and not the DTAA as a whole (preamble of the DTAA). In case of such an interpretation, benefit of grandfathering may be obtained as one may say that the object of Article 13(4A), i.e. relevant provisions of the CTA, was to grant

such benefit. Additionally, it would support that legislative amendment that the object and purpose of grandfathering provision was to avoid disruptive transition and provide certainty to the investors. Accordingly, PPT ought not to apply or that such transactions would be excluded from such anti-abuse provisions.

The above interpretations could stand clarified once any commentary is released or any judicial authority may invoke the same to that effect.

It would be important to note that Mauritius has not notified India while ratifying the MLI. Thus, the DTAA with Mauritius will not be a CTA and treaty abuse provisions prescribed under the MLI cannot be imposed. Such arrangement would then be required to be dealt in accordance with the provisions of the DTAA and domestic anti-abuse provisions.

- Having analyzed the anti-abuse provisions provided under the MLI, it is vital to consider the interplay between PPT and the domestic GAAR provisions. In the above analyzed decisions, it would be noted that the investments were made before April 1, 2017 and sold before April 1, 2020 and therefore, the PPT and GAAR provisions were not applicable²⁰. However, the interplay between GAAR and PPT (given below), would become crucial, going forward.

GAAR	PPT under MLI
Main purpose is to avoid tax	One of the main purposes is to avoid tax
Additional tainted elements to be satisfied: <ul style="list-style-type: none"> – transaction not at arm's length – Abuse of the provisions of the IT Act – Lacks commercial substance or lack of bona fides 	Following element to be fulfilled – “reasonable to conclude” that obtaining the benefit was one of the principal purposes
Grandfathering of existing investments (i.e. GAAR not applicable to investments made before April 1, 2017)	No grandfathering specifically provided
Excludes transactions / arrangements, where the tax benefit is less than Rs. 3 crores	Excludes cases where benefit under CTA was granted in accordance with the object and purpose of the CTA
If GAAR is invoked, then the transaction can be re-characterized or income can be reallocated or DTAA benefits could be denied, etc.	If PPT is invoked, the DTAA benefits would be denied.
As an administrative safeguard, an approving panel has been appointed under the IT Act	Each of the countries to decide the administrative safeguard

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4. Tax rate varies from 10% to 40% under Indian domestic tax laws
5. Apex Board for Direct Tax Laws in India
6. Circular No. 789 dated April 13, 2000
7. UOI v. Azadi Bachao Andolan (2003) 132 Taxman 373
8. (1985) 154 ITR 148 (SC)
9. Vodafone International Holdings B.V. v. UOI (2012) 341 ITR 1 (SC)
10. (2020) 116 taxmann.com 878 (AAR – New Delhi)- Rendered on March 26, 2020
11. Proviso to Section 245R(2) provides that the AAR shall not allow the application, where it relates to a transaction or issue, which is designed prima facie for the avoidance of income tax.
12. (2012) 341 ITR 1 (SC)
13. Article 27A(1) provides that a resident of a Contracting State shall not be entitled to the benefits of Article 13(3B) (dealing with Capital gains on sale of investments during the period 2017 to 2019) of this Convention if its affairs were arranged with the primary purpose to take advantage of the benefits in Article 13(3B) of this Convention. Further, Article 27A(2) provides that a shell/conduit company that claims it is a resident of a Contracting State shall not be entitled to the benefits of Article 13(3B) of this Convention. A shell/conduit company is any legal entity falling within the definition of resident with negligible or nil business operations or with no real and continuous business activities carried out in that Contracting State.
14. (2020) 114 taxmann.com 434 (AAR – Mumbai) – Rendered on February 27, 2020
15. UOI and Anr. v. Azadi Bachao Andolan (cited supra); E-Trade Mauritius Ltd. (2010) 190 Taxman 232 (AAR – Delhi); D.B. Zwirn Mauritius Trading No. 3 Ltd. (2011) 198 Taxman 295 (AAR); Ardex Investments Mauritius Ltd. (2011) 16 taxmann.com 84 (AAR); Vodafone International Holdings B.V. v. UOI & Anr (2012) 341 ITR 1 (SC). In these decisions, the Indo- Mauritius DTAA benefit has been provided
16. (2017) 84 taxmann.com 37 (Bombay High Court)
17. AAR No. 1306 of 2012 – rendered on September 11, 2019
18. (2012) 341 ITR 1 (SC)
19. Decision of the AAR is legally binding only on the parties involved in a particular case. The ruling may have persuasive value in similar matters before the tax authorities and Courts
20. Rule 10U(1)(d) of the Income Tax Rules, 1962 provides GAAR provisions shall not apply in respect of any income accruing or arising to, or deemed to accrue or arise to, or received or deemed to be received by, any person from transfer of investments made before the April 1, 2017 by such person.

It would be observed from the above, that PPT in some cases could potentially be broader in ambit than GAAR. Therefore, if the PPT is met, it may be unlikely for GAAR to get triggered, except in situations where the PPT is avoided on the ground that the benefit was in accordance with the object and purpose of the DTAA

Of course, there is an ongoing battle, as to whether GAAR provisions can override the provisions of the DTAA (including PPT under MLI). Reference may be made to the CBDT clarification issued on January 27, 2017, which reads *“It has also been clarified that adoption of anti-abuse rules in tax treaties may not be sufficient to address all tax avoidance strategies and the same are required to be tackled through domestic anti-avoidance rules. However, if a case of avoidance is sufficiently addressed by Limitation of Benefits (LoB) provisions in the tax treaty, there shall not be an occasion to invoke GAAR.”* Thus, it appears that the CBDT intends to invoke GAAR, where in case any arrangement does not get triggered by the PPT clause in the DTAA. Of course, one would also need to consider the DTAA provisions, for example, Article 28A of the Indo- Singapore DTAA which provides that the Contracting State shall not be prevented from applying its domestic law concerning the prevention of tax avoidance or tax evasion.

Care to be taken by Investors (including, Private Equity Investors)

Aforementioned tax developments to the extent permitted by commercial considerations, investors should pay attention to the following points:

- a. Payers making the payment should investigate the PPT read with the GAAR provisions, before considering the DTAA benefits.
- b. Where there is any doubt about entitlement of DTAA, it is advisable to obtain a certificate from the tax authorities for lower / NIL withholding of taxes.
- c. In cases, where there is a challenge in obtaining the certificate from the tax authorities, it would be advisable to withhold appropriate taxes and the payees can claim refund from the tax authorities by filing tax returns.

- d. Parties can also approach the AAR to obtain clarity on the tax implications on such transactions. However, this is a time-consuming approach.
- e. Appropriate indemnities / representations/ warranties may be obtained from the payees. Alternatively, monies equivalent to the tax amount (may be, including interest and penalty) can be deposited in an escrow account, until the tax authorities accept the DTAA position taken by the payee.

Conclusion

It would be noted that the anti-abuse measures are being applied by the tax authorities to deny the tax benefit accruing pursuant to the DTAA, basis factual evidences indicating lack of commercial substance in the arrangement or the transaction. It appears that the Courts are increasingly lifting the corporate veil to test the ‘substance over form’ principle and deny the benefit, ignoring even the grand fathering provisions provided under the DTAA. Hence, it would be advisable for investors to bear in mind the substance over form requirements and also maintain contemporaneous documentation to substantiate the factual position before the tax authorities. Anti-abuse provisions, by their very nature, are bound to be strictly enforced, at times overzealously. Aggressive tax planning may no longer be overlooked, internationally. In such a situation the only hope is consistency in judicial decisions.