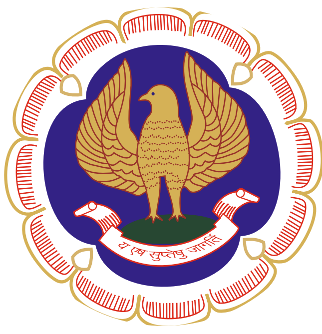

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

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Happy Gudi Padwa

Issue No. 04

NEWSLETTER

April 2023

PUNE BRANCH OF WIRC OF ICAI

(Subscribers copy not for sale)

Chairman's Communique

Dear Members and Students,

CA. Rajesh Agrawal
Chairman
Pune Branch of WIRC of ICAI

I hope this communique finds you in good health and spirits.

Even with the significant increase in regulatory and compliance requirements, we are continuing to navigate through these challenging times, I would like to commend our members and their office team for their unwavering commitment to their profession and their clients. Your dedication to providing quality service to your clients, even in this situation is truly commendable.

I urge all members and students to actively participate in all seminars and conferences to keep their knowledge and skills current.

I am very happy to convey that our both the teams that participated in the Box Cricket Premier League competition organized by the Maharashtra Tax Practitioners Association won with flying colours. I congratulate both the teams of Pune Branch including woman's team for winning.

My best wishes to all the students who are appearing for this May 2023 Exams. We have made available reading room facility for all the students at Prestige Point, Shukrawar Peth, Pune. Please take the benefit of the same.

In March 2023, we have successfully hosted National Conference on Statutory Audit of Bank Branches Organised by Auditing & Assurance Standards Board, ICAI. In the month of March 2023, we have also organized various physical and virtual programs and received excellent response from the members and students including GST Gyansatra 10 days Series, full day program charitable trust etc.

We have declared Saturday Series for members with 60 CPE hours which includes 12 programs of 2 CPE hours and 6 programs of 6 CPE hours and which has received very good response.

In April, we have organized various virtual and physical programs including Virtual Series on International Taxation for 10 days which received very good response from the members of various part of the country and well appreciated by all.

We have also hosted Company Law Refresher Course Organised by Corporate Laws & Corporate Governance Committee, ICAI which is well appreciated by all and attended by more than 200 members.

We have also organized many programs for students including Mock Test Paper Series for Intermediate & Final Course for May 2022 Examination, Marathon Batch which will be very helpful for them to give exams tension free.

We will continue to work tirelessly to update and upgrade our members and students.

In conclusion, I would like to express my gratitude to all members and students for their continued support and cooperation. I wish you all the best in your professional endeavors.

With warm regards,

CA. Rajesh Agrawal,
Chairman
Pune Branch of WIRC of ICAI

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CA. Dhiraj Dandagaval

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National Conference on "Statutory Audit of Bank Branches"

Inauguration

Participants

Panel Discussion (From L TO R) :- Panelists - CA. Anand Joshi, CA. Dhananjay Gokhale, CA. Abhay Mate, Moderator - CA. Ruta Chitale

Shri. Satish Marathe, Director RBI - Chief Guest

CA. Ranjan Kumar Sharma, DIGP, CID, MS, Pune Guest of Honour

CA. Prakash Kulkarni Speaker

CA. Nachiket Deo Speaker

CA. Prashant Tidke Speaker

CA. Sanat Chitale Speaker

CA. Maheshwar Marathe Speaker

CA. Dhananjay Gokhale Speaker

CA. Kiran Kunte Speaker

Evolving Concepts of Permanent Establishment

Contributed by :- CA. Manoj Rathi and CA. Mohit Agrawal
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Evolving Concepts of Permanent Establishment

Permanent Establishment ("PE") as a subject has always remained one of the most involved and debated topics in the international taxation space. One of the basic reasons for the same is the ever-evolving business environment giving rise to newer business models and evolution of digital economy. The laws around PE have also evolved to some extent with changing dimensions of the economy. Accordingly, having a fundamental understanding of the concepts of PE is perhaps more important and relevant than ever.

In a globalized economy which has now become more digitised, companies do operate in markets beyond the borders of their home state. They either do this through a subsidiary, resident in another state or may directly operate in the other state through a specific location (e.g., an office or a factory) situated therein or with the assistance of an agent. Regulations around PE therefore come in to determine the taxing rights of the active income of such businesses.

Legislative Backdrop of PE

Globally, there are two types of taxation systems: 1) Residence based taxation and 2) Source based taxation. In the former, taxation of an enterprise happens in respect of its worldwide income by the state of its residence whereas in the latter, taxation of an enterprise happens only on the income from a source inside the country.

India, however, follows a combination of residence based and source based taxation system. The taxation originates from Section 5 of the Income-tax Act,1961 ("the Act") which levies income-tax on the income of foreign companies/ non-residents ("NR"s), but only to the extent of their income sourced from India. Such income may accrue or arise to a NR in India, often through existence of "business connection" which such NR is deemed to have in India as per the provisions of the Act.

The concept of business connection [Section 9(1)(i)] which is the Indian equivalent of PE, essentially establishes an element of continuity or close relationship between the business of the NR outside India and a connected activity carried out in India. Accordingly, the term business connection covers an inclusive and wider scope.

While the above source-based taxation emanates from the Act, in case of a NR the said rule is subject to the provisions of the applicable tax treaty (subject to NRs' treaty eligibility). Generally, a tax treaty provides that business income of an enterprise may be subject to tax in the Source State only if such enterprise has a PE in the source state. In other words, in the context of a tax treaty between a resident state and source state, a PE signifies virtual extension of an enterprise of the resident state, in the source state. Therefore, a PE serves as the basis of economic nexus between a taxpayer and a taxing state.

Types of PE

As aforementioned, PE as a concept gets its origin from tax treaty. Most of the Indian tax treaties are based on the UN Model Tax Conventions and include certain aspects of the Organisation for Economic Co-operation and Development (OECD) Model as well. Generally Indian treaties would cover three types of PEs, i.e., Basic rule/ Fixed place PE, Agency PE and Service PE. In many treaties, one may also find construction PE and installation/ supervisory PE.

Conceptually, various types of PEs can be briefly defined as follows:

- **Basic/ Fixed place PE** – A fixed place of business through which business of NR is wholly or partly carried on; such as factory, office, branch, etc;

· **Agency PE** – When any person (other than agent of an independent status) acting on behalf of an NR, has and habitually exercises an authority to conclude contracts in the contracting state

· **Service PE** – Furnishing of services through employees or other personnel for a period exceeding 6 months within 12 month period

· **Construction / Installation PE** – Includes building site, construction, installation project, construction of roads, bridges, etc where such activities continue for a period mentioned in the particular treaty

Snapshot of Article 5

As compared to the definition of business connection, the scope of PE as per Article 5 has traditionally been limited and exhaustive. Article 5(1) of the UN Model defines PE as follows:

"For the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partially carried on."

Article 5(1) states the "basic rule" for constitution of a PE and expresses the primary meaning of PE. Paraphrasing Article 5(1) as above, a PE exists if the following conditions are satisfied cumulatively:

- There is an "enterprise".
- Such enterprise is carrying on a "business";
- There is a "place of business" in the other contracting state / Source state;
- Such place of business is at the disposal of the enterprise;
- The place of business is "fixed" and
- The business of the enterprise is carried on wholly or partially through this fixed place of business.

A Fixed Place PE does not exist unless all the aforesaid conditions are satisfied. The above conditions are subjective and at times require a very detailed factual exercise. In a generic sense, PE is: (a) a virtual projection of the foreign enterprise in Source state; or, (b) a firm foot in the soil of Source state; and (c) something that does not include casual transactions not involving the presence of the foreign enterprise for a considerable period of time in Source state.

Implications of constitution of PE in India

Where there is a PE trigger in other contracting state (or Source State), such state has a right to tax the income of NR connected with such a PE within the Source State. However, once constituted, a PE of a NR does not become a resident of the source state. It could be possible for an enterprise to have PEs in two or more countries and to have more than one form of presence in the same country, viz., a subsidiary as well as a PE.

In terms of implications, assuming that there is a tax treaty between two contracting states, the profits attributable to the business activities carried out through the PE may be taxable in source country according to its domestic tax laws on a net income basis. The income of the PE may be taxable in the resident country as well under the domestic law. In order to reduce double taxation, normally, the resident country shall grant a tax credit. If there is no tax treaty between contracting states, unless resident country provides for unilateral tax credit to its residents, relief from double taxation of the same income may not be possible, leading to juridical double taxation.

Attribution of profits to PE

While one may find determination of PE as a complex exercise, attribution of profits to a PE adds more layers of complexities. It is given that tax liability to PE would only arise when there are attributable profits to the business operations of the PE.

Captured below is a summary of guidance and approach (from OECD and UN Model) for determining profits attributable to a PE:

1) Relevant business activity approach – Under this approach, quantum of profits which need to be attributed, should not exceed what the whole enterprise could have earned as profits from the relevant business activity of the PE, directly or indirectly. This approach may support the 'Force of Attraction' (FOA) principle which finds its place in a few tax treaties entered into by India.

   Principally, FOA rule specifies that when an enterprise is said to have a PE in another country, it exposes to taxation the entire income that it earns from carrying on activities in that other country, whether or not through that PE. This principle accordingly propagates application of source-based taxation and capital importing countries or developing countries have supported this rule in their tax treaties for a long time since it tries to disincentivise an enterprise from taking undue advantage of a PE by routing transactions directly from their country.

2) Functionally separate entity approach – This approach does not affect determination of the quantum of profits to be attributed to the PE. Instead, it provides that the source state's right to tax does not extend to the profits that the enterprise may derive from that state otherwise than through the PE therein. Imperatively, FOA principle is not supported under the construct or interpretations as per functionally separate entity approach. Also known as, Authorised OECD Approach, it aligns more towards the transfer pricing principles and requires identification of functions performed, assets and capital employed and risks assumed by the PE for ascertaining the amount of attributable profit to the PE. Hence, the profit would be attributed to the PE on the premise that PE and the foreign enterprise of which it is a part are two separate entities.

Profit attribution is a vexed issue in PE's context, since each country may apply its own method for determination of PE's profits. At times, the method for attribution of profits is not consistently used. There is added layer of applicability of transfer pricing provisions to determine the attributable profits.

From India's perspective, considering the uncertainty on account of limited judicial/ administrative guidance, the CBDT released draft profit attribution rules for PE in 2019 where a formulaic approach for calculating profits attributed to operations in India was proposed, giving equal weightage to sales, manpower and assets. Most of the recommendation in this report seem to arise from a concern that India is not getting its fair share of tax from sales in the 'market jurisdiction'. However, these rules are yet to be finalised and with the advanced stage of debate at the global stage on Base Erosion and Profit Shifting (BEPS) 2.0 - Pillar One discussions, probably the Indian administration has adopted wait and watch policy and hence, attribution of profits continues to be debatable area.

Emerging landscape around PE

The traditional definition around PEs revolved around the physical presence for determining the taxing rights. However, with the change is business and advancement in technology and digitization, the businesses have started generating revenue without having need to have a physical presence. Jurisdictions were making several attempts and an emerging debate around taxing such revenues and profits in order to keep pace with the new and evolving business models came up. However, there wasn't any consensus around the mechanism of taxing the same.

This was recognised and addressed in the solution offered by OECD under BEPS Action Plan 1. This Action Plan primarily recommended three interim options to address the tax challenges arising from digital economy till a global consensus is reached to address this issue. These options were:

1) Significant Economic Presence (SEP);
2) Withholding tax on digital transactions; and
3) Equalisation Levy

India, has a large consumer base who has been adopting technology in the past couple of decades and hence was becoming a huge market potential for foreign companies who wanted to enter India and capture the market. Hence, to address and tap the tax on such revenues, India naturally was one of the early movers in the direction to implement OECD's recommendation.

Further with the changes proposed through Multi-Lateral Instrument (MLI), which would broaden the scope of PE in the treaties, there was a perception that the existing provisions of Section 9 were restrictive and hence with emerging business models new nexus based taxing rule should be brought in place.

Accordingly, the CBDT had set up a committee on taxation of e-commerce to evaluate the options available. The committee recommended equalization levy as a viable option for India, since it did not require alternation in the existing tax treaties, which would have been a time-consuming process. Thus, India became one of the first countries to levy equalization levy of 6% on online advertising and related services in 2016. The equalization levy provisions were substantially widened in 2020 by bringing in its ambit the online sale of goods and services as well.

The committee was also of the view that concept of SEP could be introduced within the concept of "business connection". BEPS Action Plan 1 had recommended that a NR would create a taxable presence in a country if it has an SEP in that country on the basis of factors that have a purposeful and sustained interaction with the economy by the aid of technology and other automated tools.

In this backdrop, the SEP provisions were initially introduced in 2018. It was felt that this change in the domestic law will enable India to negotiate for inclusion of this new nexus rule in the tax treaties. These provisions, however, remained inoperative as the thresholds were not prescribed. However, the same got notified in 2021.

Any NR who qualifies the thresholds would be liable for SEP related disclosures, whereas, SEP provisions were introduced in the background of BEPS discussion to tax Digital Economy. However, the broad language of the provisions impacts conventional transactions as well who per se do not have any 'digital' interplay.

With the provisions getting notified from 1 April 2021, a non-resident having an SEP in India shall be deemed to have a business connection in India. Accordingly, income attributable to the transactions or activities referred to in these provisions shall be deemed to accrue or arise in India and hence taxable in India.

SEP of a NR would be established if following thresholds are met:

1) the aggregate of payments arising from transactions in respect of any goods, services or property carried out by a NR with any person in India including provision of download of data or software in India, during the financial year exceeds 20 million (during a financial year); or

2) NR undertakes systematic and continuous soliciting of business activities or engages in interaction with 300,000 or more number of users in India.

It is also pertinent to note that relevant disclosures are now required vide Income tax return where the NRs are expected to report whether the SEP is getting triggered and where the same is in affirmative, the NRs are expected to report the SEP turnover and profit attributable to such revenue.

Interestingly, the concept of SEP has been introduced in the domestic tax law and as far as the tax treaties are concerned, the tax incidence triggers only if the NRs have a PE which would normally get triggered basis some physical presence of an entity. Therefore, NRs who are entitled to claim treaty benefit would prima facie not be impacted by the SEP provisions, considering the narrower scope of PE in tax treaties.

Concluding thoughts

Determining taxing rights would always involve subjectivity and deeper review of factual matrix. With changing businesses, evolving Transfer pricing rules around profit attribution, PE as a concept shall remain dynamic and continue to fetch more disputes and views. Further, with OECD BEPS 2.0 plan, which really revamps the way profits will be reallocated to market jurisdictions perhaps, long lasting PE concepts should be redrawn to address the challenges of Digital Economy.

Unearthing the Unknowns of Beneficial Ownership

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Introduction

The concept of beneficial ownership ('BO') is an important and a complex one when it comes to determining whether a recipient of income qualifies for benefits under the provisions of a Double Taxation Avoidance Agreement (DTAA). Typically, BO is required to be evaluated for a non-resident earning income by way of dividend, interest, fees for technical services ('FTS') and royalties, The same has been a highly piqued and interesting topic in the field of international tax law in recent years. The use of corporate vehicles to hide the real owner behind certain transactions is a practice that has been around for many years. In the last two or three decades, this practice has become more sophisticated with complex structures and chains of corporate vehicles being used to conceal the true ownership behind specific activities. This article discusses the importance of the concept of BO from a tax perspective, in light of the guidance available on the subject, various domestic and international judicial precedents in this regard.

Evolution of the concept of BO internationally

Reference in	Year	Summary of modifications
Canada-US DTAA	1942	The concept of BO was first introduced in the dividend article of Canada-US DTAA ensuring that the reduced tax rate on the said income was only availed by a bona fide shareholder
OECD Model	1977	Introduction of the concept of BO in the OECD Model. The Commentary only listed a few examples of what is not a beneficial owner, without giving precise guidelines or a positive definition of what a beneficial owner is.
Conduit Company Report	1986	The report discussed the issues regarding ' treaty shopping ' and discussed certain situations of companies acting as conduits/ mere fiduciary or an administrator acting on account of interested parties. Further, the report also highlighted the difficulties in applying the concept.
Commentaries on OECD Model	2003	While the Model itself remained unchanged, the commentaries were amended to clarify the concept and stated that the term BO should be understood as an anti-treaty abuse concept and should not be used in narrow technical sense.
Discussion Drafts	2011 and 2012	Clarifications were issued on the term 'BO' in 2011 and subsequently revised in 2012 based on consultations.
OECD Model	2014	OCED approved the revised proposal of 2012 and commentary to OECD Model on Article 10, 11 and 12 was majorly amended, to provided certain clarifications to avoid further misunderstandings in connection with the term.

Evolution of BO in India

The concept of BO was initially discussed domestically in India in the Circular 789 of 2000, in the context of India-Mauritius tax treaty, wherein it was clarified that wherever a Certificate of Residence is issued by the Mauritian Authorities, such Certificate will constitute sufficient evidence for accepting the status of residence as well as BO for applying the tax treaty accordingly. Subsequently, the SC in the case of Azadi Bachao Andolan held that the said circular does not interfere with Section 90 and Section 119 and is well within the ambit of the Income-tax Act. Thereafter, various courts have accepted the certificate of residency issued by the other country as satisfaction of test of BO. However, in certain cases, it has been held that where the recipient of income is only an intermediary, acting as a conduit for passing income to the real owner in a transparent manner, such recipient may not qualify to be a beneficial owner despite the evidence of status of residence.

Interpretation of the term and issues therein

Beneficial owner is arguably the most well-known undefined term in the OECD and UN model convention and most of the tax treaties and its international tax meaning is a matter that lends itself to much debate. Accordingly, the understanding of the term has been broadened in light of various tax commentaries, judicial precedents and general commercial understanding. We have summarised below a few interpretations of the term:

SN	Reference in	Understanding of the term BO
1	Law Lexicon	One who, though not having apparent legal title, is in equity entitled to enjoy the advantage of ownership.
2	FAFT	The natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes persons who exercise ultimate effective control over legal person or arrangement.
3	Real Madrid FC	An "economic interpretation" can be applied to find the "real owner" of the income whereby the legal ownership of the income could be disregarded. The ownership of the income-generating asset is not relevant; what counts is the link between the recipient and the income."
4	CIT v. Poddar Cements Pvt. Ltd.	Enumerated attributes of ownership as: power of enjoyment of property, power to dictate and determine the use of property, power to destroy it, power to alienate or will it away, right to exclude others, power to charge it as a security etc. The husk of legal title was not regarded as relevant.

Owing to the controversies around the term, various tax experts have questioned the use of the term BO instead of use any other/ clearer word (illustratively – final recipient, associated enterprises, economic owner of income, etc).

BO in context of dividend, interest, FTS and royalties

As discussed in the above table, the 1977 OECD Model first introduced the term BO in its Articles 10 (Dividends), 11 (Interest) and 12 (Royalties) i.e. the said articles stipulate that the treaty benefits viz. exemption/ lower tax rate of withholding tax on the dividend, interest or royalty income shall be available subject to the condition of 'BO'. Prior to the introduction of the term BO in the OECD Model, the same rate of tax was applicable to all recipients of income residing in a contracting state.

The concept was introduced to establish specific conditions for granting tax treaty benefits in the source state when it comes to dividends, interest and royalties, ensuring that the recipient of such income is indeed its beneficial owner. Therefore, in practice, the concept of BO is particularly complex where intermediate companies are holding loan or sub-licensing arrangements, or predominantly holding company of subsidiaries.

Relying on various judicial precedents, the following factors may be relevant for evaluating BO:

Type of Income	Indicative factors for evaluation of BO
Dividend	• Economic control & command • No contractual or legal obligation to pass on the income received • Power to dispose of investment • Ability to take decision in relation to asset/ income
Interest	• Existence of financing profile, bears underlying risks, etc • Not a mere conduit, nominee or agent • Right to use income to pay off creditors
Royalty	• Power of enjoyment of intellectual property ('IP') substantiated by DEMPE, power to dictate & determine use of the IP, existence of similar arrangements with others, right to exclude others, power to charge it as security, etc
FTS	• Existence of underlying skillsets & infrastructure, existence of similar arrangements with others, right to terminate, etc

The ECJ Danish cases

Recently, the European Court of Justice (ECJ) provided an interesting take on the concept of BO by handing down the rulings in six Danish cases regarding cross-border dividends and interest, which have popularly been dubbed "the Danish BO cases". These rulings have shed new light on what is considered abusive behaviour in EU direct tax law, and due to the fundamentally economic nature of the abuse assessment composed by the ECJ, they have provided new tools for disentangling abusive behaviour from valid business activity. The ECJ did provide its interpretation of BO in EU law, but apart from this, the Court almost entirely shifted the focus away from BO as a concept, as enquired into by the referring courts, to a focus on the notion of abuse in EU law.

To illuminate the topic, we have discussed the basic principles on which advice was premised in the two cases set forth by ECJ out of the six it addressed. In first case, Danish Co had distributed dividend to Luxembourg parent company that was indirectly owned by private equity funds through another Luxembourg company. In second case, US Co had provided loan to Danish Co through intermediaries situated in Bermuda and Cyprus. The income received by Danish Co was up streamed to US Co through such intermediaries in form of dividend income. While analysing availability of benefit under EU Parent-Subsidiary Directive, the ECJ laid down the principles on anti-abuse and BO for the Danish Court to adjudicate on the matter further. In context of "BO", ECJ stated that for the purpose of Article 10, the i) recipient is not regarded as BO if all or almost all dividend is passed on to another entity; ii) the conduit earns insignificant taxable profit and is solely engaged in the activity of transmission of dividend to another parties; iii) a person is not regarded as BO if it does not have right to use or enjoy dividend not only due to contractual or legal obligation but also in substance.

Applicability of BO to 'Capital Gains'

Owing to the above discussion, a question arises as to whether the concept of BO also applies to the income from capital gains, despite the fact that no such condition has been explicitly specified for claiming treaty benefit in the UK or OECD MC. Also, wherever required, various countries internationally have specifically included the test of BO in the CG article (eg. India-Israel tax treaty). Further, as per the guidance provided by Article 31(1) of the Vienna Convention, tax treaty terms should be interpreted good faith in line with its object and therefore, may be interpreted to mean that unless something is specifically stated, one cannot read words into treaty provisions. However, various judicial precedents (both Indian and international) have applied the concept of BO while determining taxability of Cgs.

Even though the tax treaties do not specifically require evaluation of BO test for claiming treaty benefits from CGs, one may still be required to demonstrate substance/ BO over its assets in light of the approach followed by various judicial precedents.

Interplay with Indian Company Law

Section 90 of the Companies Act, 2013 along with the corresponding rules, requires Companies (regardless of status and size) to identify natural persons who are regarded as significant beneficial owner (SBO) for the purpose of effectively implementing a transparency structure in the corporate laws of India. The term SBO has been defined under the Companies Act and requires identification of a natural person (individuals) who can be regarded as significant owners of the reporting entity where the parameters/ stipulations are in lines of certain percentage shareholding, "control over the reporting entity or 'significant influence' over the reporting entity. Such reporting casts an onus on the Companies to share information regarding BO.
A question therefore arises as to whether the said concept under domestic law would impact interpretation of the term BO under the tax treaty. In this regard, it is important to note that the concept of SBO has been brought in from the perspective of identifying the ultimate controllers of a corporate entity being an artificial person under the law. However, BO needs to be interpreted broadly through the lens of its meaning as is understood worldwide to counter treaty shopping and tax avoidance.

Relevance of BO post introduction of PPT

As discussed above, the concept of BO is a specific anti avoidance rule whereas the Principal Purpose Test is a General Anti-Avoidance Rules ('GAAR'). Therefore, a question arises as to whether or not lex specialis derogat legi generali holds good, post introduction of PPT is an interesting question to be analysed.

India introduced domestic GAAR with effect from 1 April 2017 wherein wide powers were granted to the tax authorities to disregard/ look through/ recharacterize the arrangement and deny tax benefit to taxpayers, subject to satisfaction of specific conditions. A reference may be invited to the OECD BEPS Action 6 Final Report 2015 dealing with "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances" which suggests certain minimum standards to be incorporated in tax treaties to counter situations of treaty shopping:

· Simplified LOB ("SLOB test) - it generally provides objective parameters on basis of which a taxpayer may be construed as "qualified person" for the purpose of availing treaty benefits, e.g. listing on stock exchange test, active business test, etc. Refer SLOB clause as incorporated in India-USA Tax Treaty.

· Principal Purpose Test ("PPT"') - Complementing the above SLOB test, the PPT clause applies to deny the treaty benefits if, having regard to all the relevant facts and circumstances, it is reasonable to conclude that obtaining the treaty benefit was either the principal purpose or one of the principal purposes of an arrangement or a transaction. It is a very subjective test and requires case to case analysis.

LOB/ PPT clause may be construed as a general anti-abuse provision under the tax treaties as it seeks to deny the treaty benefits to certain entities which fail to meet the respective tests or the result of the subjective test yields that the entities were incorporated/ transaction was undertaken with the principal purpose to claim treaty benefits.

However, the concept of BO may be perceived to be a specific anti-abuse rule incorporated to target specific instances of treaty shopping involving the use of agents/ nominees/ conduit i.e. entities which act as mere administrators or fiduciaries of income.

To understand the interplay between the three concepts, reference may be made to the India-Iceland tax treaty which embodies all the three anti-abuse concepts. Suppose Ind Co (an Indian company) pays royalty income to Ice Co (Iceland company), which is a wholly owned subsidiary of S Co (Singapore Company). The royalty income of Ice Co would be taxed as:

a. SLOB Test – As per Article 24 of the India-Iceland treaty, Ice Co may be entitled to claim benefits under the treaty only if it qualifies as a 'qualified person' as provide under the said clause;

b. PPT and BO Test – Assuming Ice Co qualifies for treaty benefits as per Article 24, next, it would be required to be evaluated if the Company qualifies for the treaty benefit in light of the PPT in view of MLI and BO Test as per Article 12 of the treaty.

c. Only if Ice Co satisfies all the above conditions, it may be eligible to claim the benefits under the India-Iceland DTAA.

The above example may be suggestive of the fact that, practically, there may be a holistic application required of all the aspects in an interlinked manner for the purpose of ascertaining whether a particular entity can be said to be entitled to treaty benefits.

Conclusion

As emphasized in the previous paragraphs, the BO concept aims to be an efficient anti-abuse rule for tax treaties. The evaluation of beneficial ownership is a very fact-specific exercise with far-reaching implications. Despite decades of discussion on the subject in various judicial precedents and by eminent tax experts, the meaning of the term BO remains unclear and highly debatable. BO will maintain its great importance in the international arena for years to come in the post-BEPS era, and we hope that the Government/ tax authorities would finally clarify the correct use of the term to end this age-old argument.

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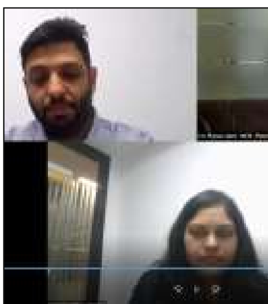
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