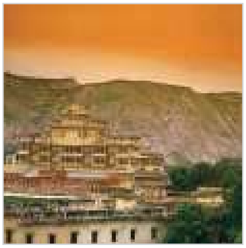
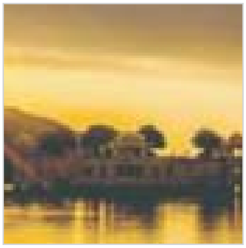
Bombay Chartered Accountants' Society

INTERNATIONAL TAX & FINANCE CONFERENCE 2013

Recent trends in Indian Treaties including Tax Information Exchange Agreements

– Mr. T. P. Ostwal, Chartered Accountant




ITC Rajputana, Jaipur

Mr. T. P. Ostwal, Chartered Accountant

- CA Final Rank holder, Member of The Institute of Chartered Accountants of India since 1978
- Member of the CID TAG (Technical Advisory Group) of OECD, Paris
- Member of the BIAC of OECD, Paris.
- First Vice President of the Executive Committee INTERNATIONAL FISCAL ASSOCIATION-NETHERLANDS
- Ex-Chairman of International Fiscal Association – India Branch.
- Member of Emerging Issues Task Force on Non-Resident Taxation formed by Ministry of Finance, Govt. of India.
- Member of Finance Sub Group of Construction Industry Development Council of Planning Commission of Govt. of India.
- Member of Expert Committee formed by Central Board of Direct Taxes (CBDT), Ministry of Finance, Government of India for framing Transfer Pricing Regulation in India.
- Member of Satawalekar Committee on Real Estate Mutual Fund in India.
- Member - Taxation and international Committee's in various organisations.
- Member of Board of the several companies.
- Regular Contributor on subjects of International Taxation at various forums in India and abroad.
- Professor at the University of Mumbai from 1976 to 1991.
- Visiting Professor at Vienna University Austria for teaching International Tax for LLM studies.
- Co-author of publication "Transfer Pricing Manual" published by The Bombay Chartered Accountants Society & Chamber of Tax Consultants, Mumbai.
- Member of Sub Committee on transfer pricing for developing countries by United Nations, which has released their TP Manual in May 2013.
- Member of committee appointed by CBDT on international tax and transfer pricing in 2012.

Recent Trends In Indian Tax Treaties Including Tax Information Exchange Agreements

Mr. T. P. Ostwal, Chartered Accountant

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PART – II: TAX INFORMATION EXCHANGE AGREEMENTS

PREFACE

Tax treaties are a dynamic area of International taxation. Each jurisdiction views tax treaties by reference to not only international law but also its own tax rules, administrative law & constitutional laws whose variations reflect domestic values of each society. Thus, treaties need to be seen both in their international context and the wider legal systems of contracting states. Further, though the fact is that the world-wide tax treaty network in large part conforms to a model tax treaty, most tax treaties contain deviations. Due to increasing integration of world-wide economies, such deviations gain more and more importance. Therefore, it becomes crucial to understand the significant developments, government actions and trends across the world that interpret and apply tax treaties to business operations. It is a rapidly growing area of tax planning that requires knowledge to be constantly updated.

Proper interpretation and adequate understanding of tax treaties is very important. The tax treaty trends of a particular country can only be identified through in-depth and meticulous study of its tax treaties and policies. However, for this there is no substitute other than a close study of individual treaty provisions using proper interpretative tools.

A humble endeavour has been made to study recent developments on the Tax Treaty policy front due to an opportunity given to me by the Society. Though there are number of issues in each of the points considered, looking at the nature of this paper and the time constraints for debate; I have restricted the posers to the bare minimum though there could be many.

In this paper I have incorporated analysis and comparison of Indian Tax treaty policies. The paper aims at highlighting subtle differences in India's Tax Treaty policies. Further, I have intended to give an insight into the recent trends of Indian tax treaty policies while drawing attention to certain emerging as well as current issues. Also, I have tried to put forward a few instances of interesting tax treaty issues, to which my attention has been drawn.

Further, I am delighted for the opportunity to share my thoughts on the emerging topic of Tax Information Exchange Agreements (TIEA) in light of the fact that it's leading to fundamental change in the tax world we are seeing. We have moved from a world where there was limited Exchange of Information, based simply on comprehensive agreements, to one where – increasingly – information available to one authority is available to all others through regular tax treaties, through TIEAs and through other measures. The general change here took place in the mid-2000s, when the OECD adopted a number of policy shifts in the Article on Exchange of Information in the model tax treaty. The test of information to be exchanged has shifted from information that is "necessary" to information that is "foreseeably relevant" – a deliberately lower standard. Then, two new paragraphs were added to the OECD provision, the first of them saying that States needed to "gather information for the purpose only of exchanging it with other countries, even if the State gathering the information had no domestic interest".

In these changing times, thus it is important to note that TIEAs are here to stay and in very short period of time the world will become a global village with total transparency. Therefore, the tax advisors cannot keep themselves isolated from such global developments and they need to migrate to the new era of developments.

There is a vital link between policy formulation and its implementation. In this context I am reminded of what Dr. B. R. Ambedkar, one of the chief architects of India's Constitution had presciently observed in November 1949:

"However good a Constitution may be, it is sure to turn out bad because those who are called upon to work it happen to be a bad lot. However bad a constitution may be, it may turn out to be good if those who are called to work it happen to be a good lot. The working of a Constitution does not depend wholly upon the nature of the Constitution."

The above observation holds good not only for the Constitution but is also equally applicable in all walks of life.

With this theme in the background let's see……

PART – I: RECENT TRENDS IN TAX TREATY POLICY

1. Introspection of Indian Tax Treaties:

1.1. When one thinks on the topic 'Recent Trends in Indian Tax Treaties', one gets a question in his mind - Are the tax treaties any more reliable? This question gains more importance in light of the recent protocol signed by India amending certain provisions to the India – UK tax treaty. Long time ago, India signed tax treaty with UK. UK authorities with good intent, based on their legal systems provided in their treaty with India, the definition of the term 'person' as follows:

> *Article 3(1)(f)-*
>
> *"The term "person" includes an individual, a company and any other entity which is treated as a taxable unit under the taxation laws in force in the respective Contracting States, but, subject to paragraph 2 of this Article,* ***does not include a partnership****"*
>
> *Para 2 further provides*
>
> *"A partnership which is treated as a taxable unit under the Income-tax Act, 1961 (43 of 1961) of India shall be treated as a person for the purposes of this Convention."*

And now, the protocol signed on 30th October 2012 between India and UK (which is yet to be effective) amends the existing tax treaty that has been in force for nearly 20 years by extending the treaty benefit to UK partnerships by replacing the definition of person as under:

> *"(f) the term "person" includes an individual, a company, a body of persons and any other entity which is treated as a taxable unit under the taxation laws in force in the respective Contracting States;"*

Further Article III of the protocol provides that Para 1 of Article 4 (Fiscal domicile) shall be deleted and replaced by:

> *"1. For the purposes of this Convention, the term "****resident of a Contracting State****" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management, place of incorporation, or any other criterion of a similar nature, provided, however,*
>
> *that:*
>
> *(a) this term does not include any person who is liable to tax in that State in respect only of income from sources in that State; and*
>
> *(b)* ***in the case of income derived or paid by a partnership****, estate, or trust, this term applies only to the extent that the income derived by such partnership, estate, or trust is subject to tax in that State as the income of a resident,* ***either in its hands or in the hands of its partners or beneficiaries****."*

1.2. India's position on OECD model is that - if a partnership firm is denied the benefits of a tax convention, its members will not be entitled to the benefits of the said tax convention entered into by their State of Residence unless expressly provided in the tax treaty. However, it is pertinent to note despite its position on OECD Model, India has now extended the benefit of the above tax treaty to UK partnership firms though India's position on the reservation still remains unaltered.

In light of the above, the question that arises is - *How can one rely on tax treaties? What has changed? Nothing!!!!! Is it a new trend?*

The journey of debate on taxation of partnership in tax treaties does not end here, we will revisit the issue in the latter part of the paper.

1.3. Coming to the introspection of Indian tax treaties, it can be noted that the treaties are normally signed between the two countries to facilitate mutual economic cooperation between the two countries. The treaties also stimulate the flow of investment, technology and services between the two countries. The tax treaties generally are the result of negotiations between the two countries with respect to their taxing rights. Several factors like the GDP growth rate, inflation rate, balance of payments position, global economic and financial situations and political factors like the ruling government and the country's interests influences the tax treaties.

Historically it can be argued that to a large extent the existing treaty rules that determine the source and resident country's taxation rights did not emerge from economic principles but from negotiations emanating based on the circumstances prevailing then.

The Indian Finance Ministry had in 2007 expressed its inclination for reviewing the treaties and stated:

> *"The finance ministry is in favour of reviewing such treaties that India has with over 100 countries, in view of the country's changing economic scenario. The treaties should be such that they are more suitable for Indian investments abroad as much as it is for incoming capital" [Source: Economic Times December 6, 2007]*

1.4. In light of the changing landscape and evolving trends it may not be eccentric to question the reliability and relevance of the tax treaties. For instance, let's consider the most controversial, classic and legendary India – Mauritius tax treaty. Mauritius signed its first tax treaty with India in the year 1982. Perhaps the Indian treaty negotiators at that time thought that India would be a net exporter of capital to Mauritius and hence, quite different from most of the other Indian tax treaties, certain typical features of the OECD Model were incorporated in this tax treaty. The negotiators then did not anticipate that one of these features will come to haunt the Indian tax administration in the future. Under this treaty, the taxation right in respect of capital gains arising from alienation of the shares of a company is given to the country of Residence and Mauritius chooses not to tax capital gains.

1.5. The process of liberalization of the Indian economy started in the year 1991. Many sectors of the economy were opened to foreign investment. Foreign Institutional Investors (FIIs) were also allowed to invest in the Indian stock market. It is not too long thereafter that canny investors spotted the combination of this aspect of the India-Mauritius tax treaty coupled with the domestic law of Mauritius that exempts capital gains from taxation. Almost simultaneously with the opening up of the Indian economy, in the year 1991, the Mauritius government enacted the Mauritius Offshore Business Activity Act (MOBAA) to permit companies registered outside Mauritius to be registered in Mauritius and claim to be residents of Mauritius. These companies could then reap the benefit of the India-Mauritius tax treaty.

1.6. And things merrily progressed along, despite certain misgivings about the 'Mauritius route' and occasional attempts to modify the tax treaty. Similar provisions with respect to taxation of capital gains are prevalent in India's treaty with Cyprus. Besides, treaties with Singapore and Netherland could also provide similar benefit but under certain circumstances. However, recently India's outlook has been to not forgo the right of taxation of capital gains in favour of the country of Residence. Besides, participants would very well recollect the instance of India–UAE tax treaty(1992) wherein the taxability of capital gains on alienation of shares was granted in favour of UAE like Mauritius and the capital gains on such account were taxed in the country of Residence which then became a subject matter for tax litigation. Indian treaty policy was virtually changed to do away with rights given to Residence countries for taxation of capital gains and a new protocol was signed with UAE in 2007 amending the earlier treaty provisions conferring the taxation rights and benefits to Residence country. India initiated to bring out similar changes to its tax treaty with Cyprus, however it didn't materialize as Cyprus backed out of the negotiation to sign the protocol similar to UAE for various reasons around the same time. Furthermore, India's intent can be corroborated from its recent amendment through insertion of section 115QA vide Finance Act 2013 w.e.f. 1.6.2013 that seeks to tax a domestic company (not a listed company) on its distributed income in case of buy back by the company of its own shares i.e. India does not wish to lose on the taxation of capital gains under all circumstances. India's current endeavour has been to avoid extension of treaty benefits in relation to capital gains as contained in the treaties signed by it in the past wherein such benefit was conferred in favour of the other Contracting State. *Currently, it is perceived that these treaty provisions are being abused by foreign investors for investment into India, for which India has decided to take recourse of GAAR and provide for treaty override where GAAR is invoked and hence can these tax treaties be said to be relevant anymore considering that their purpose itself is getting defeated?* Normally, the tax treaties are entered into with certain presumptions that hold good at the relevant point in time. However over a period of time these presumptions loose the significance owing to dynamic changes in the economic, socio and political environment thereby entailing a need to amend or re-negotiate the treaties. Due to similar reasons India is renegotiating tax treaties wherever the treaty partners agree to do so. However, this does not happen so swiftly as can be seen from re-negotiations in case of Indian treaties with Mauritius and Cyprus.

1.7. Before venturing into analysis of the recent tax treaty trends, let's first discuss briefly the historical background, evolution, patterns and past trends of Indian tax treaties and India's tax treaty policy. Discussing about the evolution of Indian tax treaties, it can be observed that tax treaties worldwide are based on OECD and UN Model Conventions - OECD Model guides the tax treaties of developed countries by advocating Residence based taxation system while UN Model guides the tax treaties of developing countries by advocating Source based taxation system. Besides there are other model conventions such as ASEAN for South-east Asian Nations while Andean Community and ILADT for Latin American Nations. The United States has also published its own model treaty to serve as the basis for U.S. treaty negotiations. Further, it is worthwhile to note that countries like Belgium (2010), Russia (2010) and Netherlands (1988) also have their own Income and Capital Model Convention. Surprisingly, European Union neither has a model tax treaty for its member countries nor is planning to develop one. Thus, countries over the world base their treaty negotiations on one of the above models. Even where the treaties of a particular country deviate from the above models on which they are based, such deviations are often relatively consistent. Negotiators tend to incorporate formulations developed in prior negotiations into subsequent treaties. It often occurs, for example that concessions made once to a treaty partner (say a developing or for that matter developed country as well) are demanded subsequently by similarly situated partners and are difficult to deny to them. Thus, each State develops its own standard formulations, and incorporates them, parallel to those of the OECD and UN Models, in its negotiations.

1.8. India negotiates tax treaties with its treaty partners according to its own philosophy. India's tax treaties are based on a combination of the OECD and UN model conventions with a higher emphasis on source country taxation. Analysis of various treaties nonetheless suggests two distinct approaches: a) Treaties negotiated with developing countries following UN model of Source based taxation system and b) Treaties negotiated with developed countries following OECD model of Residence based taxation system. Further analysis of India's tax treaties reveals that: a) With industrialized and developed countries, they cover all sources of income arising out of inflow of technology, industrial equipment and direct investment in India, besides programmes for exchange of teachers, research workers, students and artistes as also provisions relating to avoidance of taxes; b) With the communist bloc countries which do not have a tax system similar to that of European and capitalist countries the agreements cover only international maritime and air traffic; and c) With the developing countries the agreements are structured to encourage the flow of technology, equipment and professional services which India is capable to transfer and offer. Hence, in view of the different approaches adopted, the question arises - Shouldn't India publish its own Model tax treaty?

The Indian Ministry of Finance in early 2007 had stated that

> *"We are working very hard on a model tax treaty as we have realised today that India not only imports capital but also invests abroad. So the very nature of the DTAAs has to change"*

1.9. However, it is surprising to note that till date there has been no iota of development on this front. Thus the question to be asked is: Six years having passed and no signs of any initiation by India to draft its Model tax treaty - Was the Indian Ministry of Finance actually serious about formulating Model tax treaty? Or can we expect to see formulation of India's Model tax treaty in future? If one were to overview the genesis of the Indian tax treaties the following characteristics could be observed.

Under Article 51 of the Constitution of India it is stated that in order to promote international peace and security the State shall endeavour to foster respect for international law and treaty obligations in the dealings of organized peoples with one another.Interestingly, under Article 73 (1)(b) of the Constitution of India, it has been provided that the executive power of the Union shall extend to the exercise of such rights, authority and jurisdiction as are exercisable by the Government of India by virtue of any treaty or agreement. Section 90 of the Income-tax Act, 1961 ('the Act'), empowers the Central Government of India to enter into agreements with foreign countries with the following stated objectives:

a) For granting relief in respect of:
   - income which has been subject to tax in two countries; or
   - income-tax chargeable in two countries to promote mutual economic interests, trade and investment;

b) for the avoidance of double taxation;

c) for exchange of information for the prevention of evasion or avoidance of income-tax in India or the other country; or

d) for recovery of income-tax under the laws of the two countries.

Thus, the dominant objective of Indian tax treaties as can be observed from the above is avoidance of double taxation. Yet India has entered into double taxation avoidance agreements with low tax or no tax countries such as Cyprus, Ireland, Luxembourg, Mauritius, Oman, Saudi Arabia and UAE when there was indeed no incidence of double taxation in certain categories of persons in the other Contracting State.

1.10. Let us look at the title of a tax treaty. The wording says, "Agreement between X country and Y country for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to taxes on income." So the question one should really ask, when you are using a tax treaty - **"Are the taxes of just one country being avoided or, in fact, is double taxation being avoided?"** And the second question is, **"Am I creating something that actually assists with fiscal evasion rather than preventing it?"** There was a case in the United Kingdom which could very well have used this argument – the Smallwood case – but which actually did not. Issue for consideration is whether the tax treaties between India and no tax or low tax countries are void ab initio?

1.11. The past trends in the Indian tax treaties and policy depict that between 1960's to mid 1970's, a limited right of taxation was granted by Indian tax treaties to country of source and such agreements were mere bi-laterally negotiated documents as there were no model treaties in existence. However, there was a major shift in tax treaty Policy from 1976 as it moved towards more source based taxation of non-residents' income. For example, Finance Act, 1976 introduced clauses (v), (vi) and (vii) in section 9(1) of the Income-tax Act extending the rule of deemed accrual in India to income from interest, royalty and fees for technical services on the basis of source principle. The provisions were made prospective by making them not applicable to agreements made prior to 1977. Sections 44D and 115A were also introduced by the above Finance Act. Several Indian tax treaties started incorporating provision for technical services (which neither existed in either OECD or UN MC) while withholding tax rates on passive income were increased in the Indian tax treaties. The other changes include negotiation of treaties based on UN Model after release of the Model in 1980 and toleration of temporary loss of tax revenues to promote economic development and capital inflows (e.g. providing fiscal incentives and allowing tax sparing method for elimination of double taxation).

1.12. When India entered into its first tax treaty with Malaysia in 1976 effective from 1972, it was in favour of granting taxing right to that country (residence country) like today's principle of residence based taxation considering that Malaysia was a lesser developed country and there did not exist any formal Model. But in 2001, India realized that Malaysia had surpassed it in terms of development, it renegotiated its tax treaty with Malaysia to base the double taxation avoidance provisions on UN Model of Source based taxation. Similar was situation of various Indian tax treaties prior to 1976 when there was no model in existence, these Indian tax treaties were outcome of bilateral negotiations between the two countries. For instance, India's treaties with Germany (1958), Sweden(1958), Norway (1959) and Japan (1960) prior to 1960's and with Austria (1963), Greece (1965), Egypt (1969), France (1969), Japan (revised in 1969) and Belgium (1974) prior to 1976.

2. Tax Sparing:

India was great propagator of 'tax sparing' in UN Model for elimination of the double taxation and accordingly, included such clause in several treaties signed prior to 2006. The recently concluded treaties of India suggest that India is no longer in favour of this method of elimination of double taxation. The last treaty of India having this provision was the one entered into with Serbia and Montenegro, notified in 2006 but negotiated much earlier. It seems it is India's new policy not to negotiate treaties with such tax sparing provisions like USA. However, strangely when one analyses the new protocol of 2012 with UK, it can be seen that there is no amendment to existing tax sparing provision. In fact India was unsuccessful in negotiating a tax sparing clause with USA for almost thirty years (from 1950 till 1989) but now India itself does not favour it. The issue for consideration here is ***- Isn't it strange to find that India which was the biggest votary of the tax sparing system no longer has this provision in its recently concluded treaties? Isn't this indicative of a new trend?***

3. OECD Influence on Indian Treaties

3.1. India is one of the many non-member economies with which the OECD has working relationships in addition to its member countries. In June 2006, India was officially granted the 'observer status' at the OECD Committee of Fiscal Affairs. Further in May 2007, OECD offered enhanced engagement with possible membership to Brazil, China, India, Indonesia and South Africa to strengthen the co-operation with these nations. OECD is nevertheless keen on greater Indian participation in future.

3.2. It is worthwhile to note that India has made as many as 37 reservations and observations on OECD Model Convention and Commentary of 2008 – the third highest by any non-member State of OECD. Despite this fact, courts in India have been referring to the Commentaries in resolving the tax disputes arising in international transactions and have given them due weightage in the past. On the contrary, at times, the judiciaries have been taking a position that reliance cannot be placed on India's position on the OECD Model Commentary as India is not a OECD member country and further acknowledging the fact that the commentaries have only a persuasive value and are thus not binding in nature. Also with India and China's participation in OECD developments of tax work, one could see a big shift in OECD approach and eventually if OECD starts advocating source rule, it would not be surprising for one. Therefore the question for consideration is ***- Whether enhanced observer status has created any impact on India's negotiation of new treaties and interpretation of existing treaties?***

4. India's measures of tax treaty override

It needs to be appreciated that a tax treaty is an inter-nation agreement based on consensus ad idem with a dominant objective of allocation of taxing rights and to eliminate double taxation. However, if amendments to domestic laws are made which defeat the purpose of bilateral tax treaties, a country has entered into with its treaty partners, it amounts to treaty override. A number of countries as a matter of fashion, adopt such practice and hence, I have reiterated this issue at several places in this paper - Are tax treaties anymore reliable? India is not exception to such rule. Few of such amendments to the domestic laws can be seen below:

4.1. Denial of treaty benefit in absence of Tax Residency Certificate ('TRC'):

It was observed, in the past years, that there have been situations whereby taxpayers who are not tax residents of a tax treaty-Contracting State claim benefits anyway under a tax treaty, and even third-State residents claim tax treaty benefits to which they are not entitled. Hence, the tax authorities in India were demanding a TRC as a proof of Residence in the other country from the tax payer and only then considered them eligible to claim the treaty benefits.

In this respect, India's Finance Act, 2012 introduced a new sub-sections 90(4) and 90A(4) in the Act, which state that the non-resident taxpayers to whom a tax treaty is applicable shall not be entitled to claim relief under such tax treaty unless a 'certificate of his being resident' in any country outside India or specified territory outside India, as the case may be, is obtained by him from the government of that country or specified territory. The Finance Act, 2013 further states that the non-resident could be asked to provide 'such other documents and information' as may be prescribed. To this effect, CBDT has issued a Notification No. 57/2013 dated 01-08-2013 which makes an amendment to rule 21AB of the Income Tax Rules, 1962 ('Rules') and provides that a non-resident in addition to the 'certificate of his being resident' needs to furnish following information as prescribed in Form No. 10F - Status (individual, company, firm), Nationality (in case of individual), Assessee's Tax identification number/ unique in the country or specified territory of residence, Period for which residential status is applicable, Address of the assessee in the country or specified territory outside India. The notification further clarifies that the non-resident may not be required to provide the aforesaid information if the same is already contained in TRC submitted in pursuance to section 90(4) and 90A(4) in the Act.

Each country could have different regulations for issue of such TRC. Each country follows its own tax year like calendar year or fiscal year and hence, issues such certificate for that period. At times, experience shows some countries take considerable time to issue such certificate, some countries don't issue unless there exists a transaction and some countries do not know the concept of TRC and hence don't issue

TRC at all. India was also placed in similar position few years ago, where there used to be delay in issue of TRCs by India owing to absence of any formal process, further in certain cases India had also denied to issue TRC. The question for debate thus is - ***How practical these demands are and how far the non- resident would be able to meet them, within reasonable time and costs? At what point of time the TRC would be required to be furnished?***

4.1.1. Terms not defined in tax treaty:

We all know the controversy of the meaning of the term 'may be' taxed in the other Contracting State with reference to the landmark ruling in the case of P.V.A.L. Kulandagan Chettiar, 267 ITR 654 (2004). To overcome the ratio of the said decision,Section 90(3) of the Act empowered the Central Government to give meaning to any undefined term in the treaty, which reads as under:

> *(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.*

Further, Notification No. 91/2008 was issued by CBDT in August, 2008 explaining the term 'may be' used in the tax treaties; which required the residents of India to offer all incomes to tax in India which may or may not have been taxed in the other country due to the application of tax treaty.

As if it was not enough, the Revenue further clarified through Explanation 3 to section 90, inserted vide the Finance Act, 2012, w.r.e.f. 1-10-2009 which reads as under:

> *Explanation 3.—For the removal of doubts, it is hereby declared that where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued thereunder being in force, then, the meaning assigned to such term* ***shall be deemed to have effect from the date on which the said agreement came into force.***

The issue for consideration therefore is - ***Is it not a case of unilateral amendment to domestic law to suit its own convenience which overrides all the tax treaties and that too retrospectively from the date the said agreement comes in to force? Is it tenable in law?***

Further, it is interesting to note that the Protocol to the renegotiated India–Malaysia tax treaty in 2013 contains a specific clause that the term 'may be taxed in the other State' wherever appearing in the agreement should not be construed as preventing the country of Residence from taxing the income. Considering this, the questions for debate are ***- Whether prior to insertion of the said protocol to India–Malaysia tax treaty what would be the meaning of the term 'may be' for residents in India? Do they have to apply section 90(3) or Explanation 3 to section 90 and take a view that such meaning was applicable from 2001 when last Malaysian tax treaty was effective?***

If so, what was the need to amend the provisions of the said treaty through the protocol that is effective from 2013? Is it therefore appropriate to conclude that unless protocols similar to that of Malaysia are signed with each and every treaty country, the provisions of section 90(3) and the explanation 3 to section 90 will have no effect at all?

When there was a specific clause inserted in the Protocol to India-Malaysia tax treaty to clarify the right to taxation of the Contracting States in this respect, why did India give it a miss in its subsequently signed tax treaties? What is the policy India follows? Or is there any policy at all?

Lastly, is 'may be' a term that requires any meaning under the domestic law or it is usage of simple English grammar so to say – it is a phrase and not a term and hence Article 3(2) is not relevant at all?

4.1.2. Difference in rate of tax

India has under its domestic law vide Explanation 1 to section 90 of the Act w.r.e.f. 1962 provided that:

> *"For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company".*

This was done to reverse the decision of Calcutta ITAT in the case of ABN AMRO Bank which was one of the classic case of treaty override. Since it is a matter which has been discussed in the earlier RRC's, I do not propose to deal with in greater detail.

4.1.3. Introduction of GAAR provisions

The famous Vodafone decision led to the introduction of anti-abuse laws i.e. GAAR under the Indian domestic laws. By virtue of Finance Act, 2013 India has provided that the following sub-section (2A) of section 90:

> *"Notwithstanding anything in subsection (2), the provisions of Chapter X-A of the Act (GAAR provisions) shall apply to the assessee even if such provisions are not beneficial to him"*

The current draft of Indian GAAR has not only brought in its ambit transactions which have tax benefit as one of its or incidental objective but has also awarded vast powers in the hands of Indian tax authorities to recharacterise any transaction if obtaining tax benefit was one of its purpose. The anomaly that such provisions could bring to the Indian tax scenario is likely to be widespread. The GAAR provisions although introduced vide Finance Act 2012 its implementation has been deferred till 2016 on recommendations of Shome Committee. Hence, I want to keep the issue alive and pending for the next conferences when these provisions come into force. I am therefore not posing any questions for debate. I am sure another paper on GAAR would be needed if and when these provisions are made effective.

4.1.4. PAN – A mandatory requirement

Most of the tax treaties provide the rate of tax at which passive incomes are subjected to tax in source countries such as dividend, interest, royalties and fees for technical services. However, section 206AA of the Act requires-

"(1) Notwithstanding anything contained in any other provisions of this Act, any person entitled to receive any sum or income or amount, on which tax is deductible under Chapter XVIIB (hereafter referred to as deductee) shall furnish his Permanent Account Number to the person responsible for deducting such tax (hereafter referred to as deductor), failing which tax shall be deducted at the higher of the following rates, namely:—

(i) at the rate specified in the relevant provision of this Act; or

(ii) at the rate or rates in force; or

(iii) at the rate of twenty per cent."

The issues for discussion in this regard, thus are ***- Does it mean that even if the income is not taxable due to the application of treaties, one has to obtain and furnish PAN.?Is it not a case of treaty override? Does it not mean that the treaties now are not of much relevance unless one furnishes his Permanent Account Number and the tax residency certificate to the person responsible for payment of income?***

5. Taxability of Indirect Transfer – A paradigm shift in Fiscal Statute

All of us are aware of the landmark SC ruling in the case of Vodafone, wherein the Apex Court propagated the 'look at' approach for examining a transaction and upheld the legal form of the transaction over its substance. In order to nullify the effect of the above SC ruling, multiple retrospective amendments were made vide the Finance Act, 2012 to bring within its purview, the taxability of indirect transfer of capital asset situated in India. A new explanation 5 has been inserted to Section 9(1)(i) which envisages that any share or interest in a company registered or incorporated outside India shall always be deemed to be situated in India if the economic substance (i.e. underlying assets) are situated in India. The issue to ponder over is ***- Whether the retrospective amendment in sec 9(1)(i) of the ITA made to effectively override the Supreme Court decision on Vodafone will have an impact in cases where tax treaties are involved?***

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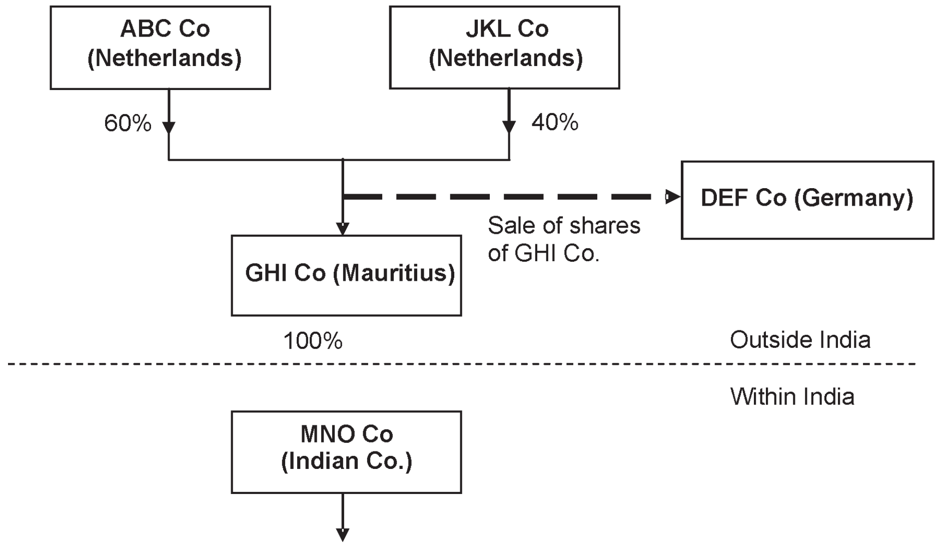
Participants may debate the issue with reference to the following case study:

Case Study 1



Facts:

- ABC Co. and JKL Co. are companies incorporated in Netherlands;
- GHI Co. is a company incorporated in Mauritius;
- MNO Co is a company incorporated in India;
- DEF Co. is a company incorporated in Germany.
- ABC Co. formed a wholly owned Mauritius subsidiary namely, GHI Co. In the same year, ABC Co. entered into a share purchase agreement (SPA) for acquiring majority stake in an Indian company namely, MNO Co. GHI Co. was disclosed as a 'permitted assignee' in the agreement.
- After two years, JKL Co. acquired 40% shareholding of GHI Co. Thus, ABC Co. now had 60% shareholding in GHI Co. GHI Co. subsequently acquired shares of MNO Co. The original capital, including stamp duty, was paid by ABC Co., but later GHI Co. reimbursed ABC Co. in that respect.
- After two more years, both ABC Co. and JKL Co sold their shareholding in MNO Co. to a German Co. namely, DEF Co.

Issues:

- Can the above transaction for sale of shares in GHI Co. be subject to capital gains tax in India under the contention that the investment vehicle used in the deal was a sham entity without commercial substance and what is sold in substance is the interest in MNO Co.? Can the beneficial provisions of India-Netherland tax treaty be invoked?
- Is it a treaty policy of India even to cover indirect alienation of shares under the provisions of Article 13 of tax treaties?

6. Treaty updates

India has a wide network of tax treaties for exchange of information and other administrative assistance for tax purposes from a foreign jurisdiction. Presently, there are approximately ninety (90) tax treaties in force. New tax treaties with twelve other countries are at various stages of negotiations. The tax treaties with countries like Australia, Bangladesh, Norway, Portugal, Poland, UK, etc. have been amended in the recent times and some new tax treaties with countries like Albania, Bhutan, Ethiopia, Nepal, Malaysia, Malta, etc. have been signed. India has also proposed to enter into tax treaties with few other countries such as Chile, Croatia, Fiji, Hong Kong, Iran, Latvia, Senegal, Venezuela, Cuba and Macedonia. Also, India has already signed around 16 Tax Information Exchange Agreements ('TIEAs') out of which 11 TIEAs are in force presently. Further, India proposes to sign TIEAs with several other countries/ jurisdictions in future.

7. Recent Trends in Indian tax treaties

I have attempted to highlight the recent trends in Indian tax treaties choosing selected recent treaties and analysing them thoroughly to bring to surface issues and examine significant trends to accommodate the debate of participants on the topic within the allotted time. I am conscious of the fact that, it is possible to raise many more issues, but considering the length of the paper and the permitted time, I have deliberately not included all of them in the paper but tried to incorporate issues which I felt are important. The significant treaty articles depicting India's recent tax treaty trends are discussed in detail below:

7.1. Partnership Firms and Tax Treaties:

An issue that has plagued partnership taxation with regards to availability of the tax treaty benefits is when a partnership is to be treated as an entity, separate and distinct from its members, and when it is to be treated as an aggregation of its members. The differences in the treatment of partnerships under domestic laws create various difficulties in applying tax treaties to them. Some countries treat partnerships as taxable units (sometimes even as companies) whereas other countries adopt what may be referred to as the fiscally transparent approach, under which the partnership is ignored for tax purposes and the individual partners are taxed on their respective share of the partnership's income. In order to avail of the tax treaty benefits, such entities should be considered as a 'person' and a 'resident' under the tax treaty. Therefore, each tax treaty needs to be carefully examined to find out whether a particular partnership entity would be a 'person' and a 'resident' in order to qualify for the beneficial provisions of the relevant tax treaty. These criteria are even more crucial when it comes to determining treaty eligibility of partnerships in context of fiscally transparent entities. It is interesting to see trends of Indian treaties with respect to conferring treaty benefits to partnerships. While tax treaty with countries like USA explicitly specifies that the term 'person', inter alia, includes a partnership, tax treaty with UK explicitly denies benefit to UK partnerships but as far as Indian partnerships are concerned it points out that partnership which is treated as a taxable unit under the Income Tax Act, 1961 ('Act') of India shall be treated as person. Further, there are few treaties, for instance, treaty with Japan where the term 'person' includes an individual, a company and any other body of persons and the Exchange of Notes, inter alia, clarifies that in the case of India, the term 'person' shall include a partnership and a HUF.

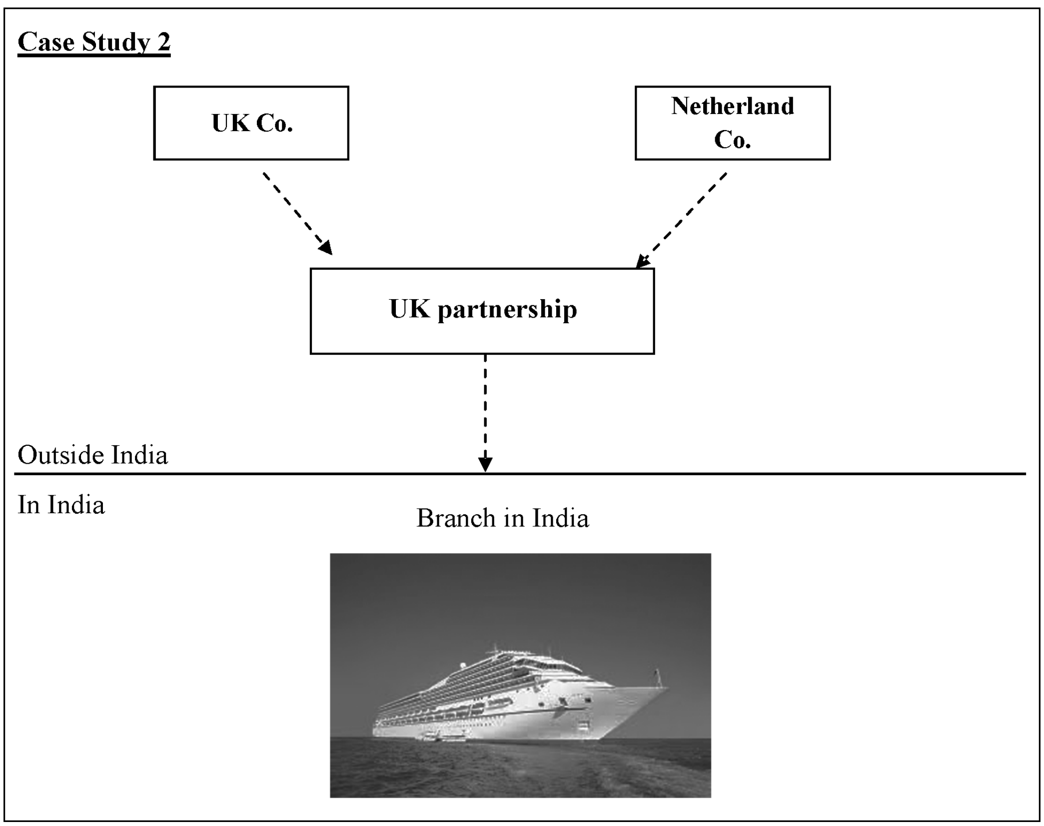
7.1.1 The OECD Commentary on Article 3 treats a partnership as a "person", either because it falls within the definition of 'company' or where this not the case, because they constitute 'other bodies of persons'. One of the preliminary issues that may arise is while a partnership constitutes a 'person', a partnership does not necessarily qualify as a **resident** of a Contracting State under Article 4. Difficulties arise in case where one of the two Contracting states treat them as opaque entity whilst the other one as transparent entity. Whether an entity is transparent or opaque, will be concluded on the basis of the principles of domestic laws of the State where the income accrues or arise, unless the treaty otherwise requires. The OECD Commentary further stipulates that where a fiscally transparent partnership is denied tax treaty benefit, the partners could be eligible to claim the same in respect of their share of income considering that they are the beneficial owners of partnership income and are persons liable to tax on that income.

7.1.2 India has however expressed its position on the above OECD Model Commentary by stating that this result is possible only if the treaty has specific language to this effect. As discussed above, Indian Judiciaries tend to take contrary view with respect to relying on OECD commentaries. Notably, whilst the Indian courts in the past have given due weightage to the OECD Commentary for interpretation of tax treaties in cases where it was convenient and facts specific, the recent rulings have overlooked the OECD's view completely, given India's position on this issue. The binding nature of India's reservations on the OECD Commentary on a Court may, however, be doubtful in terms of international law. Whereas in context of India-UK tax treaty, where the question of treaty eligibility had come up, the Tribunal, taking a fairly liberal view of the matter, ruled that treaty benefits may be granted to the partnership as the partners were taxed on the partnership income. The decision of Hon'ble Mumbai Tribunal in the case of **Linklaters LLP**[1] suggests that tax treaty benefits cannot be denied to the taxpayer, being a partnership firm, since the profits of the partnership firm are taxable, though not in its own hands, but in the hands of the partners. As long as entire income of the partnership firm is taxed in the country of Residence, tax treaty benefits cannot be denied. Accordingly, the ITAT held that since UK partnership was, in fact, liable to tax in the UK, tax treaty benefits could not be denied merely by reason that the profits were taxable not in its hands but in the hands of partners. However, later in the ruling by the Authority for Advance Ruling in case of **Schellenberg Wittmer, *In re***[2], the Authority denied benefits of the India-Swiss tax treaty to a fiscally transparent Swiss partnership on the basis that while the partnership could be said to be domiciled in Switzerland, it was not a 'person' within the meaning of the tax treaty since the partnership was not liable for tax in Switzerland at an entity level and thus not a taxable entity. Furthermore, the benefits of India-Switzerland tax treaty to the partners resident in Switzerland were denied, AAR held that the partners, not being recipients of the income, were not eligible to claim the benefit of the India-Switzerland tax treaty.

1. *Linklaters LLP v. ITO (2011) 9 ITR 217*
2. A.A.R. NO. 1029 OF 2010 (2010) Taxman 319

7.1.3. The discussion on the recent trend with respect to taxation of partnerships would be incomplete without deliberating on the recently signed protocol to India – UK tax treaty on 30th October 2012 that amends the existing tax treaty that has been in force for nearly 20 years. As discussed at the very beginning of this paper, the protocol seeks to extend the treaty benefit to UK partnerships. This amendment is largely on lines of India-US tax treaty enabling partnerships to be eligible for Treaty benefits to the extent income is taxed in UK either at the entity level or at the partner level. The amendments to definition of 'person' have already been deliberated at length above. In addition the protocol further has made requisite modifications to Article 4 by stating that in the case of income derived or paid by a partnership, estate, or trust, the term 'resident of a contracting state' applies only to the extent that the income derived by such partnership, estate, or trust is subject to tax in that State as the income of a resident, either in its hands or in the hands of its partners or beneficiaries. Further, one may ponder that India has opted to extend benefit to UK partnership by virtue of protocol amending the existing provisions on one hand, whereas in case of newer treaties (while negotiating, signing, renegotiating existing treaties or amending them through protocol) like that with Malta, Malaysia, Ethiopia, Bhutan, Nepal, etc. India has not adopted the similar position. Participants may debate the issue with reference to the following case study:

Case Study 2



Facts:

- A partnership firm in UK carrying on shipping business, having following two partners:
  - a) A company from UK
  - b) A company from Netherlands
- The UK partnership firm has a branch in India. All the ships owned and operated by this firm come to India regularly and they claim the benefit of tax treaty UK has with India i.e. they claim the exemption under Article 8 of India – UK tax treaty.

Issues:

- Whether such UK partnership firm is entitled to tax treaty benefit prior to the recent amendment in the UK tax treaty?
- What is the status after the amendment?
- If in this example, the registered office of the UK partnership firm is shifted to Netherlands or the control and management of the partnership firm is situated in Netherlands, what would be the status under India – Netherlands tax treaty for tax purpose

7.2. Persons Covered

All of us know that only a person who is resident of either of the Contracting State is eligible for benefit of the tax treaty. It is interesting to note that the recent trend of Indian tax treaties has been to clarify the persons to whom the benefits of the treaty would not be available.

7.2.1. The meaning of 'Resident' for the purpose of Article 4 of tax treaties with most of the States uses the expression ***"any person who, under the law of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature". In some of the tax treaties, namely: Australia, Singapore, Italy, Romania, the expression used is "if the person is a resident of that Contracting State for the purposes of its tax"***.

Normally, the residents of a State are liable to tax and states/ countries following source rule would also have non-residents who would be liable to tax on the incomes accruing to them in that State. It is worth noting that some countries consider Permanent Establishment as Resident of that country and also issue TRC to such PEs.

7.2.2. As can be seen, the newer trend in India's recent treaties is to clarify who would be regarded as 'Resident' for treaty purpose so as to avail benefit of a particular tax treaty India has with other Contracting State. Further, it is interesting to note that Article 4 of the OECD Model has always stated that the term 'resident of a Contracting State' does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein. Thus, it is enigmatic to observe the specific inclusion of this language in India's recent tax treaties (either renegotiated or amended by virtue of protocol). For instance, whereas Article 4 of the existing treaty does not make any specific distinction, the Protocol to **India – UK** treaty endeavours to clarify that the term resident does not include *any person who is liable to tax in that State in respect only of income from sources in that State,* similar clarification has been provided by protocol to **India – Poland** tax treaty. *Hence* - ***Can a view be taken that non-domiciles of UK are not entitled to invoke India-UK tax treaty? Does it imply that the benefit of the treaties is to be restricted to persons liable to tax on global income and not to those who are liable to tax only in respect of incomes sourced from that State?***

7.2.3. However, the protocol to **India–Malaysia** tax treaty expressly states that the term resident does not exclude residents of countries adopting a territorial principle in their taxation law. This is comprehensible in light of the fact that Malaysia follows territorial principle of taxation and thereby seeks to extend the benefit of its tax treaties to persons that are taxed in Malaysia on the territorial principle. The protocol to India – Malaysia tax treaty further carves specific exclusions for entities that are entitled to tax benefits according to the Labuan Business Activity Tax Act, 1990 to avail the treaty benefits. The companies in offshore zone in Labuan would thus not be eligible to treaty benefits. Though, it further clarifies that the benefit to avail treaty provisions would be available to Labuan companies that have made irrevocable election to be charged to tax under the Malaysian Income Tax Act.

7.2.4. If one looks at treaty practices, South Korea had unilaterally denied the treaty benefit to Labuan companies despite having no exclusion in Korea–Malaysia tax treaty. Similar, is the case of USA not honouring treaty with Netherlands qua Netherland Antilles. However, despite the knowledge, India never ventured into doing so, but now the treaty with Malaysia expressly provides its intention to deny such benefit.

7.2.5. Further, it is worthwhile to note that the protocol to India–Malta tax treaty provides that the provisions of Article 6 to 22 of the tax treaty shall not be applicable to a) any person enjoying a special fiscal treatment under the provisions of the Malta Merchant Shipping Act, 1973 to the extent that it is not subject to tax on the profits derived from the operation of ships in international traffic; or b) any company licensed under the Malta Freeport Act of 1989 to the extent that it is not subject to tax on its profits as a result of such license; or c) any person that enjoys a special fiscal treatment under any law similar to those referred to in a) or b) above, enacted in Malta after the signature of the said tax treaty.

The question for consideration is – ***Does it indicate a new trend in denying treaty to offshore centers and Economic Zones where taxes are not levied by treaty partners?***

7.3. Appropriate adjustments in case of transfer pricing additions

Article 9 on Associated Enterprises deals with adjustments to profits that may be made for tax purposes where transactions have been entered into between associated enterprises on other than arm's length terms. However, in cases where an upward revision/ adjustment is made,the absence of provision granting corresponding adjustments for tax levied on transfer pricing additions effected by the tax authorities of taxing State has led to economic double taxation of same income. To overcome this shortcoming, Article 9(2) was introduced in the OECD Model in 1977 so as to prevent economic double taxation of income and uphold the tax treaties in their true spirit. This is one of the provisions which relieve economic double taxation through the treaties which generally are meant for elimination of juridical double taxation. Article 9(2) provides for a 'corresponding adjustment' of the profit of the associated entity in the other State (i.e. a reduced taxable profit). According to the OECD Model Commentary to Article 9(2), a corresponding adjustment is not mandatory. The obligation for a Contracting State to make a corresponding adjustment is limited to adjustments justified both in principle and as regards the amount.

7.3.1. Paragraph 2 – no such thing as a 'corresponding adjustment'

On the perusal of Article 9 it will appear that the term corresponding adjustment does not appear. It does appear in the OECD Model Commentary to Article 9. What appears in Article 9 is the term 'appropriate adjustment'.

Recently, India has negotiated in its treaties for inclusion of the Article for providing appropriate adjustments and has signed number of new tax treaties & protocols to tax treaties with several countries which contained detailed provisions under Article 9 in an endeavour to correct its lopsided tax perspective and bring parity in international tax laws. The recent Indian tax treaties including Article 9(2) are treaties with Malaysia, Nepal, Ethiopia, Poland which provide for appropriate adjustment. It is interesting to note that few of the Indian tax treaties like that with Germany, France, Greece, Brazil, Belgium, etc. do not have Article 9(2) for 'appropriate adjustment'.

It is worth noting that some countries believe that there is no need to have such express provisions in the treaties, it should work automatically due to existence of Mutual Agreement Procedures provisions in the tax treaties which also has its origin in Model (due to India's contribution). Whereas, there is another school of thought prevalent amongst some countries that no corresponding adjustment is possible in absence of existence of Article 9(2) under the treaty and specific understanding to that effect. India follows the latter principle.

I would like to invite the participant's attention to the view held by UN and OECD Models with respect to anti-abuse provisions according to which despite absence of express provisions within the treaty, anti-abuse provisions as provided under the domestic tax laws of a country can override the treaty provisions. Isn't it a dichotomy then, that corresponding adjustments are not permissible in absence of express provisions whereas anti-abuse provisions can override the treaty though there are no express provisions under the treaty.

7.4. Anti-abuse Provisions

Normally, the domestic tax laws of a State provide for taxing rights of that State for both residents and non-residents in that State; these rights are restricted by the tax treaties. The extent of such limitations imposed may vary depending upon mutual negotiations between treaty countries. As a general rule, the domestic tax law contains provisions for tax treaty to prevail in case of a conflict.

The limitation on taxing rights of a State under a particular tax treaty may tempt the taxpayers to avoid taxes in a particular jurisdiction to exploit the difference in interpretation of tax laws in treaty countries or by 'treaty shopping', which may or may not have been intended by the treaty countries; such attempt may thus, lead to instances of treaty abuse.

The term 'abuse' or 'misuse' of a tax treaty is not defined in the Model Tax Convention (OECD or UN); Paragraph 9.5 of the commentary on Article 1 (OECD Model Convention 2003 update), however, provides guiding principles to determine cases of treaty abuse. Two elements must be present for constituting abuse of tax treaty provisions –

- that the main purpose of entering into the transaction was to secure a more favourable tax position; and
- obtaining that more favourable treatment in given facts would be contrary to the object and purpose of the relevant provisions of the tax treaty.

Treaty shopping is one of the most prevalent forms adopted for tax avoidance though at times it is absolutely legitimate. The concept of treaty shopping can be briefly described as use of a treaty by persons who might not ordinarily come within its scope to avoid taxes. The objective is to reduce source taxation – typically on dividends, interest, royalties and business income not connected to a permanent establishment.

Thus, there are two preliminary questions about treaty shopping ***- Does interposing a conduit in a country to benefit from its treaty network constitute legitimate or abusive tax avoidance?***

If an arrangement or structure is abusive tax avoidance, can it be controlled through domestic anti-avoidance provisions in the country of the taxpayer's Residence or through specific bilateral anti-treaty shopping provisions?

Treaty shopping is generally tackled by countries by adopting provisions in the treaty like introduction of concept of 'Beneficial Ownership' and 'Limitation of Benefit' in the tax treaties. Internationally, tax avoidance has been recognised as an area of concern and several countries have expressed concern over tax evasion and avoidance. Further tax avoidance through treaty shopping is viewed as matter of anxiety. In this respect, countries provide for anti - avoidance rules to mitigate such tax avoidance. These Anti Avoidance Rules are broadly divided into two categories namely 'General' and 'Specific'. Thus, legislation dealing with 'General' rules is termed as 'GAAR', whereas legislation dealing with 'Specific' avoidance is termed as 'SAAR'. Some time legislation intents to target some specific situations and that too from specific jurisdictions, then it is also known as Targeted Anti–Avoidance Regulations (TAAR) such as section 94A of the Act.

Most double tax treaties did not contain specific limitations in the past, instead, they rely on the concept of 'beneficial ownership' or domestic anti-abuse legislation to safeguard against hollow conduits. India too has various SAAR provisions under its domestic laws to overcome instances of tax avoidance. In addition to the domestic SAAR, India has also been considering the plugging of loopholes in tax treaties with other nations by introducing anti-abuse rules in the agreements negotiated prior to 2004. Further the tax treaties negotiated since 2004 have anti-abuse rules incorporated in them. Anti-abuse rules are incorporated in the form of imposing limitations on the tax benefit provisions in the tax treaties.

7.4.1. Limitation of Benefits ('LOB'):

A LOB provision is an anti-abuse provision that sets out which residents of the Contracting States are entitled to a tax treaty's benefits. The purpose of an LOB provision is to limit the ability of third country residents to obtain benefits under the said treaty. This type of use of the treaty, where third country residents establish companies in a Contracting State with the principal purpose to obtain the benefits of the treaty between the Contracting States, is commonly referred to as 'treaty shopping'.

There exist variants of the LOB clause in tax treaties which follow OECD /UN model. Some treaties contain concepts like 'subject to tax', 'substance' or 'substantial ownership' tests to restrict applicability of beneficial provisions of a treaty and prevent misuse of the treaty by taxpayer.

India has generally adopted an approach of having greater emphasis on source-country taxation; discouraging treaty shopping was usually not a significant policy goal for India while negotiating tax treaties. Therefore, most of India's earlier tax treaties did not contain anti-treaty shopping provisions. However, India renegotiated the India-Singapore Income Tax Treaty (Singapore Treaty) and the India-UAE Income tax treaty (UAE Treaty) through separate Protocols that added LOB provisions in each, effective in 2005 and 2008, respectively. The India - Singapore tax treaty, as renegotiated in 2005, includes an LOB provision to prevent abuse of the capital gains tax benefit under that treaty.

Post this development, most of India's new or renegotiated tax treaties contain an LOB clause. The introduction of LOB provisions in recent Indian treaties is indicative of a policy to discourage treaty shopping and hence finds place in many Indian tax treaties. The recent LOB clause in Indian treaties provides that the benefits of the treaty would not be available if its affairs were arranged in such a manner as if it was the 'main purpose' or 'one of the main purposes' to take the benefits of the Agreement. The clause further normally provides that the provisions of tax treaty shall in no case prevent a Contracting State from application of the provisions of its domestic law and measures concerning tax avoidance or evasion, whether or not described as such. This is true for the recent Indian tax treaties with UK, Malaysia, Poland, Ethiopia, Malta and Nepal.

Further, in essence, GAAR principles have now been incorporated in the treaty itself. For instance in the India–UK tax treaty, just as GAAR seeks to disregard an impermissible avoidance arrangement even where a step in, or part of the arrangement is presumed to have been undertaken to obtain tax benefit, the LOB clause under India–UK tax treaty seeks to deny benefit to taxpayer or even to a particular transaction entered into by the taxpayer where it is undertaken to obtain benefit under the treaty. However, it may be noted that recent Indian tax treaties have used different languages while embedding LOB clause and there is no consistency unlike USA, where LOB is well carved out in their Model and while negotiating tax treaties of every country, they incorporate comprehensive LOB articles.Can India think on such policy? Can it afford/desire to have such policy keeping in mind the fact that India is still a capital importing country? The question thus arises ***- Is LOB clause in the tax treaties a sweeping GAAR /an indirect GAAR? What does the terms 'main purpose' or 'one of the main purposes' signify?***

In absence of definitions of the aforesaid terms in treaty, which meaning is to be assigned? Whose onus is it to demonstrate 'main purpose' or 'one of the main purposes' to take benefit of the tax treaty?

It is interesting to note that on one hand, the LOB Article contained in India–Ethiopia and India–Nepal tax treaties provide that the provisions of treaty shall not prevent application of domestic tax law concerning tax avoidance and tax evasion whereas on the other hand, the protocol to the treaties specify that if the domestic law provisions are more beneficial than the provisions of this Agreement, then the provisions of the domestic law shall apply to the extent they are more beneficial. The question to be addressed is ***- Isn't it ironical to have such contrary provisions in the treaties given the introduction of GAAR provisions under Indian domestic law which would always be prejudicial to the taxpayer? Isn't it a paradox that GAAR overrides treaty? Is it a written policy to rewrite twice?***

Further the reason for absence of LOB clause in the protocol to India–Australia tax treaty recently concluded in December 2011 (not yet effective) is inexplicable. In light of this, a question for consideration is ***- What is India's tax treaty policy on this subject? Is there any confusion or lack of clarity in the minds of treaty negotiators?***

Considering the domestic anti- abuse provisions which provide for treaty override, questions to ponder are - ***Haven't the treaties become irrelevant? In view of the above, where do the treaties stand with respect to domestic tax avoidance measures passed by countries? Do the relevant domestic rules complement tax treaties? Do they limit the application of treaties? Are they limited by tax treaties? Are they designed to circumvent limitations in treaties? If so then why is there a need for tax treaties at all?***

Also, is the 'abuse of treaty provisions' to be addressed by domestic law principles or by the interpretation of the tax treaty?

Notably, a number of new tax treaties have provisions for application of domestic tax anti-avoidance provisions which are now an integral part of such agreements/ tax treaties. The question for consideration is - ***In absence of such specific provisions in old treaties whether the aforesaid section 90(2A) will automatically apply & if so then why do we need 'Limitation of Benefits (LOB)' clause in the new treaties?***

7.4.2. Beneficial Ownership:

Most tax treaties invariably contain articles that address the taxation of dividends, interest and royalties (commonly collectively known as "passive income"), which flows from a source in one treaty partner to a resident in the other treaty partner. Tax treaties usually operate by partially, or fully, exempting passive income from withholding tax imposed by the source country. Tax treaty partners intend that treaty benefits should be granted to their residents, not to residents of non-contracting states. Moreover, they intend benefits to be granted to persons who enjoy the benefits, not to an artificial entity that is interposed in a stream of income. A question that arises from this framework is whether residents of tax treaty partners who receive passive income qualify for this reduction in withholding tax. Articles 10(2), 11(2), 12(1) of the OECD Model that applies to dividends, interest and royalties, address the question of the qualification for benefits under the treaty. The test that each of these articles applies is "beneficial ownership". Treaties sometimes use terms such as "beneficial owner", "beneficially entitled", "beneficially owned" and "beneficial interest". These terms are all variations of the notion of beneficial ownership. Most Indian treaties have concept of beneficial ownership embedded in them for ensuring that the benefit of the provisions are available only to the beneficial owners of the passive income.

'Beneficial ownership' is, in effect, a specific anti-avoidance concept to prevent treaty shopping through conduit entities. This concept simply implies restriction of availability of treaty benefits to the ultimate beneficial owners of the income. Under the beneficial owner concept, the income is taxed in the hands of the rightful owner and not in the hands of the recipient. The concept has been introduced to prevent treaty shopping involving the use of intermediaries. Countries viewing such practice unfavourably have, as a safety measure, incorporated the concept of 'beneficial owner' in their tax treaties.

The OECD Model does not define the term "beneficial owner". Ever since the introduction of the term in the Model of 1977, its meaning has been a topic of debate. For instance, at the 1998 International Fiscal Association Congress in London, the topic of discussion in one of the seminars was "The Concept of Beneficial Ownership in Tax Treaties". The first question raised in that seminar was, "Should the domestic law of the contracting state be referred to under article 3(2) of the OECD Model to understand beneficial ownership, or does the context of articles 10, 11 and 12 of the OECD Model require that beneficial ownership be interpreted as a concept of international tax language, which is separate from domestic law?". The second issue was, "If the concept of beneficial ownership is not seen as a reference to domestic law, then *how should the concept be interpreted? What then is beneficial ownership?* In absence of the definition of the term – beneficial ownership under the treaty - *What is the meaning that one can assign?*

Beneficial ownership is a common law trust concept that has no equivalent in civil law countries. The concept distinguishes beneficial rights from legal title. A beneficial owner may have the power to vote or dispose of shares depending upon the terms of the trust. The concept of beneficial ownership has different facets depending upon the context in which it appears. In tax law, the concept can be used to provide relief or to challenge transactions. The beneficial ownership concept does not require motive or purpose to apply. Thus, the test devolves on facts and circumstances in each case. With respect to the concept of 'beneficial ownership', the issues for consideration are ***- How does the State of source examine whether the intermediary is really a beneficial owner of the income distributed?***

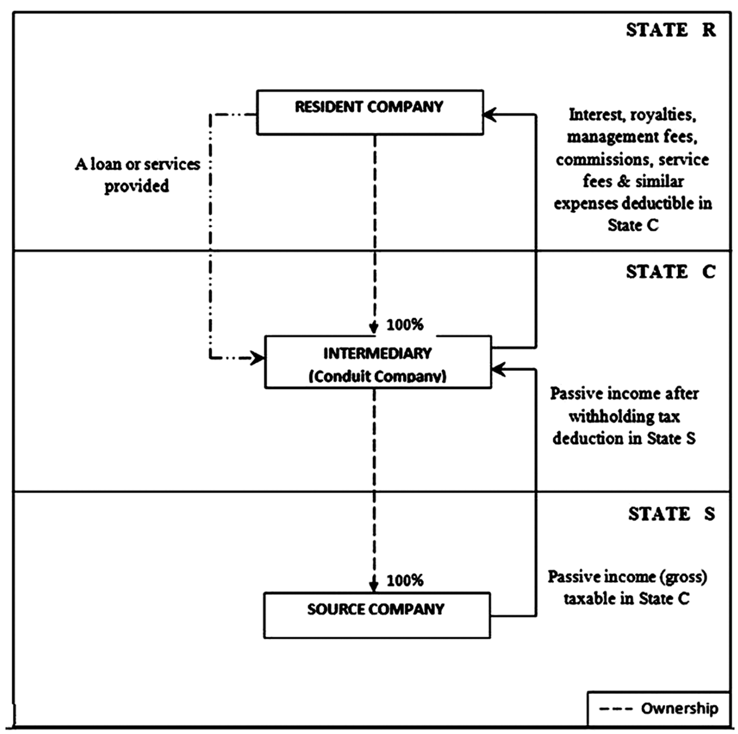
Is beneficial ownership an economic or legal concept?

The concept of beneficial ownership emphasizes the economic reality of the relationship between corporations and shareholder, according to which a corporation is merely a legal fiction that cannot be considered separately from its shareholders. An economic perspective suggests that tax levied on a corporation's income should be integrated with any tax levied on its shareholders. Thus, there is no connection between the concept of beneficial ownership and the notion of companies. This lack of connection is problematic particularly in situation involving interposed companies. In such cases, the approach adopted by the OECD courts corresponds to the conventionally legal point of view, according to which a corporation exists as a legal personality distinct from its shareholders. Applying beneficial ownership test to interposed companies from the legal perspective may result in treaty benefits being passed on to residents of a non-Contracting State. That is, tax treaties tend to operate in a manner that contradicts their own policy, which is to limit tax benefits to residents of Contracting States. In other words, interposed companies distort the general application of the tax treaty policy.

Discussion on Beneficial Ownership also requires an understanding of the concept of Conduit Company Strategies and Stepping Stone Conduits. A conduit company can be described as a company interposed between a company that pays (passive) income from a Source State with which the country of the Residence of the conduit company has a tax treaty and a company (or owner) resident in another State which cannot avail of benefits of the treaty.

Often in conduit company strategies, tax savings do not rely on tax exemptions in the intermediary State alone. Tax savings can be obtained from the combined effect of the withholding tax reduction under a tax treaty and the domestic tax law provisions of the intermediary State. Such strategies are referred as 'Stepping Stone Conduits'.

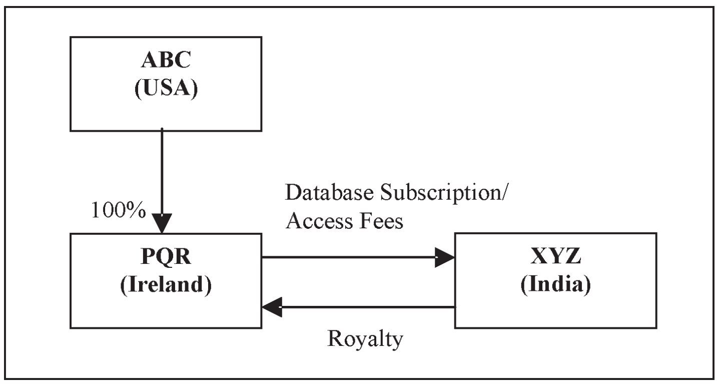
In a stepping stone conduit strategy, State C includes the passive income received by the intermediary from the source company in the intermediary's gross taxable income. Under the general tax provisions of state C the intermediary is then allowed a full deduction for the income that it passes on to the resident company. The income that the intermediary passes on to the resident company may be a (high) interest payment in case of back-to-back loan structure, or in the form of royalties, commissions or management/service fees. In effect, the intermediary does not bear any tax in State C. The concept is diagrammatically represented as under:



In a recent case law issued by The Court of Canada in Velcro Canada Inc. v The Queen on 24th February, 2012 The Tax Court of Canada held that, the recipient of royalties under a sub-licence was the 'beneficial owner' of the royalties, notwithstanding its corresponding obligation to pay royalties to the owner of the underlying intellectual property under a primary licence. As a result, the recipient was entitled to treaty benefits under Canada-Netherland Income Tax Convention. The court found the facts that the recipient of the sub-licence royalties had 'possession', 'use', 'control' and 'risk' in respect of royalties it had received, despite its obligation to pay royalties under the primary licence.

Participants may discuss the following three case studies:

Case Study 3



Facts:

- ABC is a company incorporated in USA.
- It has a wholly owned subsidiary in Ireland, namely PQR.
- An Indian company namely, XYZ pays royalty to PQR as consideration towards database subscription/ access fees.
- The Revenue Department considers that PQR is not a beneficial owner of the royalty payment made to it for various reasons.

Issue:

- If one takes a view that the recipient PQR is not a beneficial owner then can the tax treaty with the ultimate beneficial owner's country be resorted to claim the treaty relief i.e. can India – USA treaty be applied for payments of royalty?

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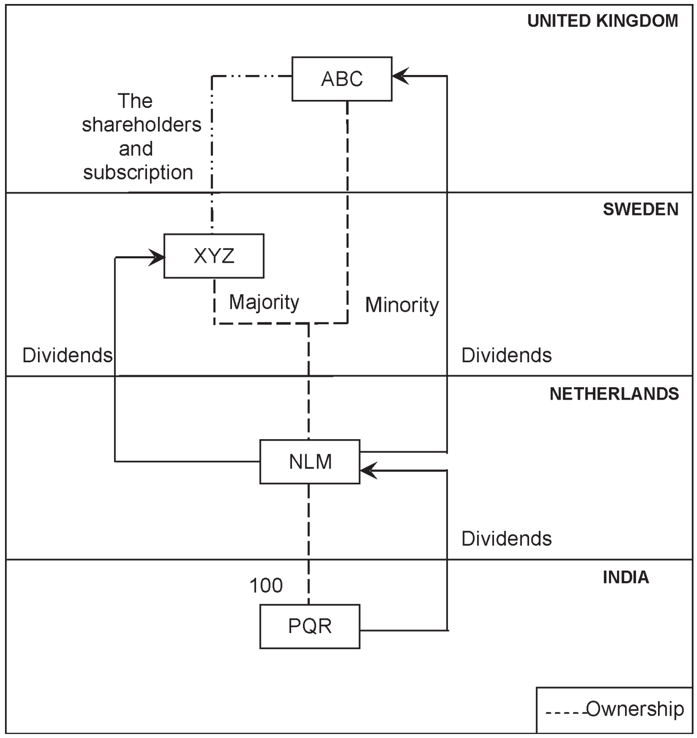
Case Study 4



Facts:

ABC is a company resident in United Kingdom whereas XYZ is a company resident in Sweden.

Both of them entered into a 'shareholders and subscription' agreement under which they incorporated NLM in the Netherlands in order to acquire shares of PQR, an existing Indian company. NLM is not a party to the aforesaid agreement.

As per the agreed terms, XYZ will own the majority of shares in NLM. NLM will have no physical office or employees. It will have the same directors as PQR. NLM executes a power of attorney in favour of a Dutch management company, TIM, to carry out its business transactions and to pay interim dividends on its behalf to XYZ & ABC.

According to the shareholders' and subscription agreement, at least 80% of profits of PQR and NLM are to be distributed to XYZ and ABC. Further, it provides that the board of directors of NLM would take reasonable steps to procure dividends & other payments from PQR to enable NLM to pay dividends to XYZ & ABC.

Issue:

- Who is the beneficial owner of the dividend from PQR and which tax treaty is to be applied?

Case Study 5

Facts:

X Trust, set up in Singapore, is a discretionary Trust, settled by Mr. P, a Non Resident Indian of St. Vincent for the benefit of his 4 brothers who are settled in 3 countries, namely Mr. Q and Mr. R – residents of India, Mr. S – resident of Belgium and Mr. T – resident of Dubai, UAE. Sole trustee of the said trust is a Nominee company situated in BVI, and the Protectors of the Trust are Mr. Q & Mr. T one of whom is a resident of India.

The Trust is set up by settling the entire share capital of MP Ltd, a company incorporated in BVI by Mr. P. MP Ltd has an operating subsidiary called C Ltd resident in USA which is engaged in the business of manufacturing & assembling parts of automotive industry. During the calendar year 2012, Directors of MP Ltd, in consultation with Protectors Mr. Q & Mr. T, sold the shares of C Ltd which has resulted in huge capital gains of USD 40 millions which was accumulated by the trustee and in June 2013 substantial part of the accumulated capital was distributed to all the four beneficiaries equally.

Mr. Q and Mr. T were taking most of the decisions for the Trust along with the nominee company who simply complied & implemented decisions made by Mr. Q & Mr. T.

Issue:

The beneficiaries want to know the taxability of capital gains and the amounts received by them from the Trust by way of capital distribution.

Coming to the recent trends in Indian tax treaties with respect to beneficial ownership it is interesting to note that the protocol to India–UK tax treaty deletes the existing dividend Article and replaces it with new provisions dealing with dividend. The new dividend Article further contains a specific anti–abuse provision which provides that where the main purpose or one of the main purposes of any person concerned with the creation or assignment of the shares or other rights in respect of which dividend is paid is to take advantage of the Article by means of such creation or assignment. In such case, no relief would be available under the Dividend Article. It is pertinent to note that such an anti- abuse provision has been inserted for the first time may be due to what the discussion draft of OECD is still debating upon i.e. the Royal Bank of Scotland & Velcro's cases and finding way to solve the entangling issue.The point to ponder is - ***What does it signify? Does it mean the person to whom assignment of the shares or other rights in respect of dividend made will not be a beneficial owner even if it is for consideration?***

As per this concept, the treaty benefit of lower withholding tax becomes available to residents of the Contracting States only if they are the beneficial owners of the income from dividends, interest, royalties and fees for technical services. For instance, the recent Indian tax treaties with UK, Poland, Ethiopia, Malaysia, Malta provide for such provision.

The concept of beneficial ownership is also extensively incorporated in the Interest and Royalties Articles under the tax treaties. Anti-abuse provisions embedded in the Royalty Article of the following tax treaties that dwell on subject of assignment of rights is worth noting. For instance, such provisions can be found in Article 12(9) of India–UK tax treaty (the existing Article on Royalties) as well as in Article 12(8) of India – Ukraine treaty.

Further, it is interesting to note that most of the Indian treaties have the concept of 'beneficial ownership', however only the India–Australia tax treaty uses the expression 'beneficial entitlement'. The term 'beneficial entitlement' is somewhat different concept than 'beneficial ownership'. The term 'beneficial entitlement' is concerned with the 'right to use and enjoy' income and not concerned with its ownership.

One can also observe that the trend of India's recent tax treaties has also been to reduce the rate of tax on dividends in the Source State. For instance, Indian treaties with Poland provides for tax at rate of 10%, Ethiopia provides for tax at rate of 7.5%, Malaysia provides for tax at rate of 5%, Nepal provides for tax at rate of 5 %, if the beneficial owner is a company which owns at least 10 % of the shares of the company paying the dividends and 10% in all other cases, Malta provides for tax at rate of 10% if the beneficial owner is a company which owns at least 25% of the shares of the company paying the dividends; and 15% in all other cases.

The Dividend Article in India - Malta treaty further provides, where the dividends are paid by a company which is a resident of Malta to a resident of India who is the beneficial owner thereof, Maltese tax on the gross amount of the dividends shall not exceed that chargeable on the profits out of which the dividends are paid. In terms of Malta domestic tax law, generally no withholding tax is imposed on dividends, interest and royalties. In light of the imputation system adopted in Malta, under most Maltese tax treaties, the maximum tax rates applicable to dividends paid by Maltese companies to persons resident in the other treaty countries do not exceed the tax rate payable by the recipient companies in Malta.

The recent Indian tax treaties with countries such as Bhutan, Albania, Columbia on the same lines, provide for reduced rate of taxation of dividends, interest and royalties in the source State.However, in light of discussion about section 206AA of the Act, earlier in this paper, if the treaty benefits are denied, effective rate of tax now provided u/s 115A is 25%.

Another point for consideration is while the recent trend of Indian tax treaties seems to be to reduce the rate of tax in the Source State, what happens to the rate of dividend distribution tax ('DDT') which is as high as **16.995%** that India levies on distribution of dividend. The issue for debate is - ***Can it be construed that the rate of taxation of source country which in recent treaties is reduced to 5%/7.5% / 10% implies that the rate of DDT can be restricted to such reduced rates?***

7.5. Concept of 'deemed royalty'&'user based royalty' in tax treaties

The genesis of 'international tax' primarily lies in 'source' based taxation. Thus if an income is sourced within a State, then irrespective of the residential status of its recipient, such income may be taxed in such State (where it has been sourced). Source based taxation is justifiable on the ground that the State which provides the opportunity to generate income should have the first right to tax it. Indian income tax law follows hybrid system of taxation.Thus, in India, all residents are subject to tax on their global income whereas income accruing or arising in India is taxable in India irrespective of the residential status of the recipient.Indian domestic law already has Source rule in terms of provisions of section 9(1)(vi) and 9(1)(vii) whereby the royalties and fees for technical services are deemed to accrue or arise in India if the payer is a resident of India. The trend towards source rule and source based taxation of royalties has also been extended to Indian tax treaties. Source rule has normally been given prominence in Indian tax treaties, moreover Secondary Source Rule concept is also prevalent in few of the Indian tax treaties in the past. The recent trend in Indian tax treaties is towards source based taxation of royalties and introduction of concepts of 'deemed royalty' and 'user based royalty'.

7.5.1. Secondary Source Rule – 'user based royalty' under India – US tax treaty:

The India – US treaty contains a secondary source rule under subparagraph 7(b) of Article 12. According to these provisions, a royalty that does not arise in one of the Contracting States under subparagraph (a) and that relates to the use of, or the right to use, a right or property in one of the Contracting States will be deemed to arise in that State. Similarly, a fee for included services that does not arise in one of the Contracting States under subparagraph (a) and that relates to services performed in one of the Contracting States will be deemed to arise in that State. The recent Indian tax treaties have adopted the trend to introduce 'deemed royalty' and 'user based royalty' concepts. The participants may note that the original treaty with Nepal which stands terminated now did contain the 'deemed royalty' clause however it did not incorporate the concept of 'user based royalty' which has now been introduced in the new tax treaty which is effective from 1st April 2013. India – Nepal and India- Ethiopia tax treaty also incorporates the concept of deemed royalty and user based royalty on same lines. However, the India – UK tax treaty does have the 'deemed royalty' clause but however doesn't have the concept of 'user based royalty'. It is enigmatic that whereas the protocol to India – UK tax treaty has sought to amend various clauses, the 'user based royalty' concept has not been introduced in the India – UK tax treaty. Whether the negotiators have done this purposely or simply could not convince the other country's negotiators to incorporate such provisions, is really not known.

Same approach has been followed by the treaty negotiators as far as the India–Poland treaty is concerned. Though original treaty does contain deemed royalty clause the protocol does not introduce concept of 'user based royalty'.

On similar lines the India – Malaysia tax treaty though renegotiated does not have concept of 'user based royalty', nor does the protocol to India – Australia tax treaty introduces such a concept.

7.6. Re- emergence of 'Service PE' concept

In the absence of a fixed place of business or a dependent agent PE, profits from services could remain taxable only in the State where the enterprise is tax resident. The OECD currently takes the position on a service permanent establishment that no change is required to be made to the provisions of the OECD Model and that services should continue to be treated the same way as other types of business activities. Although the 2010 OECD Model does not include a service permanent establishment, the Commentary to Article 5 recognizes that some states may wish to include service permanent establishment in their treaties, particularly where otherwise large amounts of profits would be made in their territory by foreign enterprises providing services there. This is due to elimination of Article 14 in their Model.

The UN Model on the other hand places greater emphasis on the source principle than the OECD Model and Article 5 of the UN Model includes the concept of a service permanent establishment. Like the agency permanent establishment, this is a deemed permanent establishment, because the non-resident does not need to have an actual establishment / premises in the host State. The basic rationale of service PE clause thus is to tax enterprise of the home country for its economic activities in the host country beyond a threshold limit. Since, India predominantly believes in source based taxation, several Indian tax treaties incorporate the concept of creation of service permanent establishment if the services (including consultancy services) are furnished beyond a given threshold limit of number of days by the service provider of one of the Contracting states through its employees or other personnel in the other Contracting State.

The Service PE clause finds place in several Indian tax treaties. Illustrative list being Australia, Canada, China, United States of America, United Kingdom, Switzerland, Singapore, Norway, Indonesia, etc. Even, in the newly negotiated/ renegotiated treaties by India with Malta, Malaysia and Nepal the Service PE clause has been introduced thereby making the concept of 'Service PE' an emerging trend. Accordingly, Service PE clause finds place in 27 of the existing 90 tax treaties. However, post insertion of this new clause, there is a lot of confusion owing to the co-existence of 'Fees for technical services/ Fees for Included Services' and 'Service PE' in these treaties. The treaties are not modelled based on suggested draft by UN Model (2011). In this respect, in creation of Service PE clause, India has contributed substantially.

7.6.1. Fees for technical services

The Model Convention be it OECD Model Convention, UN Model Convention or US Model Convention does not contain any specific Article on Fees for Technical Services. It is interesting and worthwhile to note the changes and trends with respect to taxation of technical fees over the years. The term 'fees for technical services' which was introduced post 1976 in the tax treaties, sought to bring within its ambit the taxation of services of technical, managerial or consultancy nature and hence, during the period from 1980's to 1990's Indian tax treaties normally incorporated the provisions for taxation of technical services. During 1990's to 2000 there was a shift in Indian tax treaties towards concept of taxation of 'fees for included services' and thus the concept of 'fees for included services' and 'make available' replaced the concept of 'fees for technical services' post 1989 which gradually narrowed down the scope of taxability of these services. However, interestingly post 2000 the trend in Indian tax treaties has been to discontinue with the 'make available' concept and shift back to concept of taxation of technical services in order to encompass taxation rights over a wider range of services.

7.6.2. Interplay between Service PE &Fees for Technical Services

While determining the taxation of income from services rendered under tax treaties, it is essential to consider the interplay between 'Service PE' clause and 'Fees for Technical Services' clause. Normally, where there is a co- existence of the service PE clause and FTS in the tax treaty, the treaties specifically carve out exception for FTS for the purpose of determination of existence of Service PE. The text of the Article normally is:

furnishing of services, other than included services as defined in Article 12 (Royalties and Fees for Included Services), within a Contracting State by an enterprise through employees or other personnel, but only if:

……

Though, UN Model doesn't include the exception for FTS, majority of tax treaties signed by India having a service PE clause specifically exclude income covered under Article 12 (Fees for Technical Services). Further, Article 12 also specifically carves out the FTS income which is effectively connected to a PE.

Looking at the recent trend of Indian tax treaties as far as the Service PE clause is concerned, it can be noted that the clause has been incorporated in the Indian tax treaties with Malaysia, Poland, Ethiopia, Nepal, etc. It is however surprising to see that the Service PE clause introduced in the new India–Malaysia tax treaty does not contain exclusion for technical services taxable under Article 13.Again the protocol to India – Poland tax treaty has also introduced the Service PE clause however it has not provided for exclusion for technical services. Same is true in case of the new India–Ethiopia tax treaty i.e. though the service PE clause is present, the exclusion for FTS has not been carved out. The new India–Nepal tax treaty also continues to contain the service PE clause without providing exclusion for FTS but this is comprehensible in view of the fact that there is absence of FTS clause under the India–Nepal tax treaty. In light of the above, the questions for consideration are- ***Where the consultancy services are furnished for more than 90 days but less than 180 days, would it be taxable as 'Fees for Included Services' and taxed accordingly or would it be construed to constitute a 'Service PE' for the profits to be attributed accordingly?***

An observation in connection with 'Service PE' clause that deserves mention is that the threshold limit for creation of 'Service PE' is not uniform. Some older treaties provide the threshold limit as 183 days whereas almost all the newly negotiated/renegotiated treaties generally provide for threshold limit as 90 days for creation of 'Service PE'. The only exception is the India-Australia Protocol signed in 2011, which surprisingly extended the threshold limit for creation of Service PE from the existing time-limit of 90 days to 183 days in 12 months period.

Another interesting observation that emerges from analyzing the treaty trends with respect to Service PE, FTS and FIS is the disparity in characterization and taxability of the technical, managerial or consultancy fees across the treaties. For example, India-France tax treaty and India-Netherlands tax treaty do not incorporate 'Service PE' clause but provide for Most Favoured Nation ('MFN') clause in their respective protocols by virtue of which the concept of 'make available' comes to play and restricts scope of taxation of technical services. On the other hand the India-US tax treaty includes both the 'Service PE' clause and 'make available' clause towards 'fees for included services' in the treaty. Contrastingly, the recently concluded India-Malta tax treaty and India-Malaysia tax treaty incorporate a clause for 'Service PE' but do not provide for 'make available' clause towards 'fees for technical services' in the treaties. Thus, it is very difficult to judge the current trend in negotiating the combination of these clauses as per the new treaties. There doesn't seem to be any fixed policy in the mind of the Indian negotiators. Such varying provisions cause confusion and create conflict regarding applicability of specific Article, i.e. which Article would prevail over the other.

7.8. Automatic Review of treaty provision

It is interesting to note that the Protocol to India-Malaysia tax treaty provides for reviewing the provisions of the tax treaty which is a new way forward of dealing with age old treaties which have longer life than the domestic laws. This would in a way ensure appropriate modifications in the provisions at a point of time since at time of review both the Contracting States would consider the extant regulatory environment in order to decide whether to modify or continue with the existing provisions of the treaty. The issue for discussion is- ***Is it to be viewed as a forthcoming trend in tax treaties which would require both Contracting states to review the provisions of Article beyond a particular / specific time period? Whether any such change will apply prospectively or retrospectively keeping in mind the fact that sometimes treaties are made effective retrospectively as well?***

7.9. Non discrimination

The non-discrimination Article in tax treaties states that nationals of one Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is much more onerous, than it is on the nationals of that other Contracting State in the same circumstances, in particular with respect to residence, are or may be subjected.

Designed to assure equal tax treatment in each treaty country for its own citizens and the citizens of its treaty partner, the non-discrimination clause offers protection for the nationals of both countries from differential tax treatment by supplementing internal laws against discrimination. Modern income tax conventions typically express the non-discrimination principle in three specific provisions each designed to protect a distinct class of treaty partner nationals: individuals, enterprises and permanent establishments of enterprises. However, the protection specifics vary in coverage. Most Indian tax treaties already incorporate non- discrimination Article and the recent trend has been to continue to include the non-discrimination clause in the tax treaties. Recently, non-discrimination clause has been introduced as Article 24A in the India-Australia tax treaty through the new protocol and Article 24 in the new India-Ethiopia treaty. Article 24 is identical in both model treaties.

7.10. Exchange of Information

The Article on 'Exchange of Information' as contained in Indian tax treaties is predominantly based on the UN recommendations which, by the way are mainly in line with the OECD rules. This Article provides that the competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of this Agreement or to the administration or enforcement of the domestic laws concerning taxes of every kind and description, imposed on behalf of the Contracting States. The recently concluded tax treaties as negotiated/renegotiated with Australia, Ethiopia, Malaysia, Malta, Norway, Nepal, Netherlands, Poland and U.K. contain an additional clause to encourage exchange of taxpayer information on a wider range of taxes. It provides that a Contracting State must accept the request of other Contracting State for furnishing the requested information, even though that State may not need such information for its own tax purposes. In no case shall the Contracting State decline to supply information solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person. Earlier, quite a number of Indian tax treaties were silent regarding the application of this Article to the persons not covered by Article 1 i.e. persons who are not residents of either of the Contracting States. However, all the recently concluded tax treaties have a specific clause in its respective Article that the Exchange of Information is not restricted by Articles 1 and 2 of the said treaty which means that the obligation to supply information exists even with respect to non-residents. Moreover, the Protocol to India-Malaysia tax treaty provides that the competent authority of Malaysia will also provide information under Article 27 (Exchange of Information) regarding the persons who are entitled to the benefits of the Labuan Business Activity Tax Act, 1990 notwithstanding the fact that they are not entitled to benefits of the treaty. In light of the above- ***In case of existing treaties which are silent on the applicability of this Article, can a Contracting State seek Exchange of Information from the other Contracting State with respect to persons not covered by Article 1?***

7.11. Assistance in the Collection of Taxes

Of the recent tax treaties that India has negotiated/renegotiated with its treaty partners, the tax treaty with U.K.include an Article for 'Assistance in the Collection of Taxes' whereby the Contracting States would lend each other assistance in the collection of revenue claims in respect of taxes covered by the convention . It is interesting to note that existing Article contained in the Indian tax treaties with Norway and Poland, which hitherto provided for assistance in the collection of revenue claims in respect of taxes covered by the convention has now been amended in the renegotiated treaty/ protocol to provide for assistance in the collection of revenue claims in respect taxes of every kind. Further, the Indian tax treaties with Nepal and Australia which did not earlier contain this Article have now incorporated the same in their renegotiated treaty/ protocol to provide for assistance in the collection of revenue claims in respect taxes of every kind. Also the new India- Ethiopia tax treaty incorporates this Article and provides for assistance in the collection of revenue claims in respect taxes of every kind. When a revenue claim of a Contracting State is enforceable under the laws of that State and is owed by a person who, at that time, cannot, under the laws of that State, prevent its collection, then the competent authority of that State shall make a request to the competent authority of the other Contracting State for the purpose of collection of such revenue claim. That revenue claim shall be collected by that other State in accordance with the provisions of its laws applicable to the enforcement and collection of its own taxes as if the revenue claim were a revenue claim of that other State.

It is also pertinent to note that though the newly signed India-Malta tax treaty does not provide for 'Assistance in the Collection of Taxes', it contains a MFN clause in its protocol which provides that if after the date of signature of this Agreement, the laws of Malta change to provide assistance in collection of taxes to any country which is not a member of the European Union (the current laws of Malta permit it to lend assistance in collection of taxes on income, profits or gains only to countries that are members of the European Union) or Malta agrees to extend such assistance to any country which is not a member of the European Union, then Malta shall forthwith inform the Indian competent authority and the competent authorities of the Contracting States shall by mutual agreement settle the mode of extending assistance in collection of taxes to each other.

Further, though the renegotiated India-Malaysia tax treaty does not contain an Article towards this clause, it provides that if Malaysia amends its domestic laws for the purpose of 'Assistance in the Collection of Taxes', then, the two Contracting States shall consult each other for the purpose of inserting an Article on this subject in the tax treaty.

7.12. Tax Examinations Abroad

The newly signed Protocol between India–UK tax treaty incorporates a new Article dealing with 'Tax Examinations Abroad' whereby the competent authority of the 'requested state' may allow the competent authorities of the 'requesting state' to enter its territory to interview individuals and examine records of the persons concerned and also be present at the appropriate part of tax examination in the territory of the 'requested state'. Similar provisions are inserted in the new protocols to India-Australia tax treaty and India-Poland tax treaty and in the renegotiated India-Malaysia tax treaty.

Further, though the renegotiated India-Malaysia tax treaty does not contain an Article towards this clause, it provides that if Malaysia amends its domestic laws for the purpose of 'Tax Examinations Abroad', then, the two Contracting States shall consult each other for the purpose of inserting an Article on this subject in the tax treaty. The issue for discussion is - Considering the fact that this Article of 'Tax Examinations Abroad' is present only in a few recent tax treaties, where the treaty partner agreed for inclusion of such Article amounts to a new policy?

Participants may debate the issue with reference to the following case study:

Case Study 6

Facts:

Mr. Smith of UK undertakes business activities in India and returns back to UK. He files his returns in India with respect to his income chargeable to tax in India as he was resident due to his stay in India. The Indian Tax Authorities suspect some concealment in Mr. Smith's transactions with an Indian company namely, R Ltd. In this regard, the Indian Tax Authorities call for information from R Ltd. R Ltd. being unable to submit sufficient information, the Indian Tax Authorities are not satisfied with its explanations. Indian Tax Authorities propose to undertake a search on Mr. Smith by sending its officers to UK. In the process of interrogation, they want to use coercive means and threaten and intimidate Mr. Smith for seeking the required information.

Issue:

Can the Indian Tax Authorities take above coercive actions against Mr. Smith?

PART – II: TAX INFORMATION EXCHANGE AGREEMENTS

8. Tax Information Exchange Agreements

In general, offshore tax evasion takes advantage of a lack of transparency and cooperation among countries to enable high net worth individuals to hide taxable income and asset overseas. While the taxpayers operate globally, the tax administrators remain confined to their respective jurisdictions, and accordingly, they may not get the information available in other jurisdictions since taxation is the sovereign function of the State and manner to collect information is restricted to the State. Thus, to effectively increase the efficiency of the fight against tax evasion and abusive or regressive tax schemes and optimize tax assessments the states are reinforcing international cooperation on tax matters. A key element of such international co-operation in tax matters is done through Exchange of Information mechanism available in DTAA, Tax Information Exchange Agreements ('TIEAs') and Multilateral Agreements for Exchanging Information.

Under the leadership of G20, a major shift from the era of bank secrecy to the era of transparency was marked in 2009 with information exchange upon request being established as the international standard. The OECD Secretary-General Report to the G20 Finance Ministers depicts the restructuring of the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum) and the amendment of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (the Convention). India is part of the Global Forum, which currently has 120 member countries. India is a Vice Chair of its Peer review group and member of its Steering group.

Apart from Tax Information Exchange Agreements (TIEA), new methods of cooperation on an international level such as Joint Audits, Simultaneous Tax Examination, Foreign Account Tax Compliance Act (FATCA) of the U.S.A. have also been seen as recent developments and one cannot afford to overlook the same.

In the light of the U. S. FATCA, it would be interesting to see whether other countries would be obliged to follow such extra-territorial regulations. The Americans having realized these limitations, changed their tricks of trade and started negotiating and concluding Inter-Governmental Agreements (IGA). To what extent is it in India's interest to sign such agreements with USA in order to comply with FATCA Regulations?

These unprecedented developments in the field of International Mutual Assistance through Exchange of Information are quite significant. One doesn't know whether the tax payer is given any attention in the process. After G20 meetings in 2009 in the 'Official Communiqué', the G20 declared: *"We agree to take action against non-cooperative jurisdictions, including tax havens, we stand ready to deploy sanctions to protect our public finances and financial systems. The era of banking secrecy is over".*

With the emergence of black, grey and white list, the world started complying with the new order, which can be compared with 'big bang'. The Universe started expanding rapidly on these matters and exploded with a tremendous expansion of the treaty network.

Many Bilateral Treaties have been renegotiated around the world during the last decade containing standard provisions of the OECD Model Tax Convention (MTC) on Exchange of Information and the present Article-26, para-1, provides that the competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of convention or the administration or enforcement of domestic law concerning taxes of every kind. The Council of Europe of OECD has put forward Multilateral Convention on Mutual Administration Assistance in tax matters, which has been signed by 43 States so far. Switzerland adopted these standards and also signed bilateral agreements. FATCA was enacted by the U.S.A. and is being implemented internationally. India did not lag behind. The Indian Government issued Instruction No.1 of 2013 dated 17th January 2013 in connection with Exchange of Information for tax purposes with foreign jurisdictions – 'Guidance for Inbound and Outbound Requests'. These instructions provide complete details of how India intends to go about in Exchanging Information with tax administrations of other countries with whom India has tax treaties.

The TIEA is an agreement which is based on international standards of transparency and Exchange of Information. Such agreement has a positive impact on the economic cooperation between countries through effective Exchange of Information in tax matters. Some of the salient features of the agreement are as follows:

- Information must be foreseeably relevant to the administration and enforcement of the domestic laws of the Contracting Parties concerning taxes and tax matters covered by the agreement.
- The requesting State has to provide some minimum details about the information requested in order to justify the foreseeably relevance criteria.
- Information is to be treated as secret and can be disclosed to only specified person or authorities, who are tax authorities or the authorities concerned with the determination of tax appeal.
- It also provides for disclosure of information to any other person or entity or authority or any other jurisdiction (including Foreign Governments) with the written consent of the competent authority of the requested Party.
- There is a specific provision that the requested Party shall provide upon request the required information even though that Party may not need such information for its own tax purposes.
- There is a specific provision for providing banking and ownership information.
- There is a specific provision for Tax Examination Abroad where authorities of one State can be present in the tax examination of taxpayer in the other State.
- Upon entry into force, the Agreement allows Exchange of Information forthwith.

The question for deliberation are - ***Whether a State is required to supply information, which would disclose any trade, business, industrial, commercial or professional secrets or trade processes of taxpayer? Does a State have discretion in this regard? If so, where is the tax payer's interest protected?***

8.1 India's need for TIEA and history

In India, "black money" refers to funds earned in the black market, on which income and other taxes had not been paid. The problem of tax evasion and generation of black money is not new. As far back as 1936, the Ayers Committee, while reviewing the income tax administration in India suggested large-scale amendments to secure the interests of the honest taxpayer and effectively deal with fraudulent evasion. An Income-tax Investigation Commission was appointed in 1947 to investigate tax evasion and suggest measures for preventing it in future.

In the past, the government has also resorted to voluntary disclosure schemes providing amnesty to tax evaders if they declared their unaccounted income and paid due taxes on the same. These voluntary schemes have been criticized on the grounds that they provide a premium on dishonesty and are unfair to honest taxpayers, as well as for their failure to achieve the objective of unearthing undisclosed money.

With the liberalisation of restrictions on cross-border flow of goods and services and relaxation of foreign exchange control, new opportunities opened up for misuse of tax havens and misuse of transfer pricing and other sophisticated methods. Globalisation reduced the cost of these sophisticated methods thereby facilitating generation of black money and its transfer across the border. These changes required new strategies to curb black money. The role of tax havens has gradually come under scrutiny globally. With near-zero tax regimes, banking secrecy, and weak financial regulations, these tax havens facilitate hiding of money accumulated through tax evasion and other illegal means in addition to creating risks of terrorist financing and money laundering.

Countries including India have started realising that transparency and cooperation are essential for protecting their tax revenue. Such pressure has increased in recent times in view of the fiscal challenges faced by countries across the world and public resentment against unethical financial practices.

The G20 summit in London in April 2009 proved to be an important milestone when just before the summit, countries like Switzerland, Liechtenstein, Luxembourg, and Monaco announced their preparedness to accept OECD standards of transparency and Exchange of Information. As an equal member of the G20, India played a vital role in sending out a strong message to various countries that if they did not comply with international standards of transparency, they should be ready to face actions from the 20 largest economies.

8.2. India's Role in TIEA

Both the DTAA as well as TIEA are effective tax information exchange mechanisms. Since negotiation of a DTAA takes time, which can delay development of the mechanism for effective exchange, India has taken the plea that a country cannot refuse signing a TIEA if it has been requested by other countries. It was again at India's initiative that this position was accepted and now global consensus has emerged that a country cannot insist on a DTAA and must conclude a TIEA if requested by other countries. After this development, many countries that were earlier insisting on DTAAs, have now agreed to conclude TIEAs with India as well other countries of the world. Hence, India has been a strong proponent of Transparency and Exchange of Information for tax purposes and is playing a major role in international forums to exert pressure on countries that do not conform to international standards of transparency. These global efforts have resulted in many countries/jurisdictions coming on board and they are now willing to co-operate with other jurisdictions for exchanging information as per internationally agreed standards.

On one hand the Indian Government is increasing the number of Income Tax Overseas Units (ITOUs), on the legislative side it is sewing DTAA and TIEA with other countries. India has also signed Multilateral Convention on Mutual Administrative Assistance in Tax Matters on 26th January, 2012, which came into force for India on 1st June, 2012. This convention has been signed by forty-two countries upto 31.10.2012 and has entered into force for 16 countries. The parties to the Convention are obliged to provide administrative assistance to each other with scope wider than DTAAs or TIEAs. Further, the members of South Asian Association for Regional Co-operation (SAARC) have entered into a limited multilateral agreement with wide scope of providing administrative assistance and training. This SAARC Limited Multilateral Agreement has come into force from 1st April, 2011.

8.3. Impact of TIEA in India

Although Exchange of Information provisions existed with some of India's important treaty partners for long, these provisions were not utilized effectively in the past. Even after the recent efforts as outlined above, the investigating officers are not making many requests, primarily because they are not fully aware of the provisions. This is evident from the fact that the total numbers of request received from field authorities were 39, 46, 92 and 386 during the F.Y. 2008-09, 2009-10, 2010-11 and 2011-12 respectively.

In addition to the DTAA, India has a network of TIEAs with eleven low/no tax jurisdictions which are currently in force. Five more TIEAs have been signed and will come into force on completion of internal procedures by the other jurisdictions. Further, India proposes to sign TIEAs with several other countries/jurisdictions in future.

Indian TIEAs with countries which are currently in force include TIEA with Argentina, Bahamas, British Virgin Islands, Cayman Islands, Gibraltar, Guernsey, Isle of Man, Jersey, Liberia, Macau and Monaco. Besides, Indian TIEAs with countries which are signed but not yet effective include TIEA with Bahrain, Bermuda, Liechtenstein, Mauritius and San Marino. Further, amendments have been made with respect to Article that relates to Exchange of Information in numerous existing treaties entered with countries such as Netherlands, Sweden, Georgia, Australia, Poland, UK, Singapore, Malta, Malaysia, Ethiopia, Norway and Nepal.

As stated earlier, the existing Article on information exchange has been amended by virtue of a protocol to the India-UK tax treaty by substituting it with three extensive Articles i.e. Article 28 on Exchange of Information, Article 28A on Tax Examinations Abroad and Article 28B on Assistance in Collection of Taxes. Article 28 on Exchange of Information gives a statutory recognition to the formal process of information exchange between the competent authorities. The information that can be exchanged under this Article is that which enables the carrying out of the provisions of the Treaty or enforcement of domestic law of the Contracting States effectively. Article 28A allows tax authorities from one territory to enter the other territory to conduct interviews, examine records and be present at tax examinations. Article 28B is on assistance in collection of taxes in the treaty territory for smoothing the process of recovery of taxes. Significantly, these provisions can't be invoked in respect of prior matters. However, countries may bilaterally agree to do so.

9. Foreseeable relevance and concept of Fishing Expedition

The term 'foreseeable relevance' is intended to provide for Exchange of Information in tax matters to the widest possible extent. It is to be noted that the Contracting States are not at the liberty to engage in **'fishing expeditions'** or to request information that is unlikely to be relevant to the tax affairs of a given tax payer.

9.1. Foreseeable Relevance

As per TIEA, the Contracting States / Parties are not obliged to exchange information which is not of foreseeable relevance for administration and enforcement of the domestic laws of the requesting State/Party However, if the requesting State provides an explanation as to the foreseeable relevance of the requested information, the requested State may not decline or withhold requested information because of belief that the information lacks relevance to the underlying investigation or examination. The above provisions are similar to the provisions contained in Article on Exchange of Information under the tax treaties which have been discussed earlier.

The OECD instrument of TIEA requires strict confidentiality rules that protect against unauthorized disclosure of exchanged information. Bank secrecy is widely recognized as legitimate tools in protecting confidentiality of the financial affairs of individual and real entities. It derives from the concept that the relationship between bankers and customers obliges the bank to treat all customers affairs as confidential. There are different standards of banking secrecies in the various parts of the world.

9.2. Fishing expeditions

Fishing expeditions refer to requests that have no apparent nexus to an open enquiry. In other words, there should be some link between the requested information and a tax payer who is being investigated. The power to 'fish' for information which is unrelated to any proceedings or which may enable the tax authorities to decide whether to institute proceedings or not is not permitted.

9.3. Group Requests

The possibility of Contracting States to exchange information on the basis of group requests was concretized in the 2012 update of the OECD's Commentary to Article 26. Group request implies a request that not only covers a specific person but a group of tax payers not individually identified that are in a similar situation provoking a similar outcome. Such information should have foreseeable relevance and should not constitute a fishing expedition.

Here therefore the questions that need serious consideration are – ***Can request be made for information relating to a group of persons? Where the request relates to a group of taxpayers not individually identified, how will it be determined whether such a request constitutes a fishing expedition or not?***

9.4. Confidentiality

Effective mutual assistance between competent authorities requires that each competent authority be assured that the other will maintain confidentiality of the information which it obtains in the course of their cooperation. All OECD instruments include strict confidentiality rules against unauthorized disclosure of the exchanged information.

One of the pre-condition under TIEA concluding between the States is that confidentiality of the transferred information is required to be maintained by the requesting State. In this respect, it is interesting to note that some countries use secured computer network or data encryption technologies, whereas set of countries require the requesting States to ensure that the information be subject to the rules of confidentiality of the specific agreement concerned. Further, some States do not guarantee any confidentiality. Some countries go one step further and refuse to disclose any information to another country's tax authority if it is found that the country does not seems to respect the standard of confidentiality. India so far has been maintaining complete secrecy to such an extent that they are not ready to share the information, at times, with the Courts. However, the issue arises for consideration is - ***Whether Indian computer network and the data encryption network technologies are adequate to give this comfort to other countries. Apart from the technology, is any other factor such as human being also relevant in keeping the data secret and what is the level of secrecy in India? Participants may deliberate - Can such information obtained be shared with a third State?***

9.4.1. Lawyers' legal professional privilege

The confidentiality of written communications between lawyers and clients is usually protected. The privilege of confidentiality is based on the concept of the lawyer's role as collaborating in the administration of justice and a lawyer being required to provide, in full independence and in the overriding interests of that cause, such legal assistance as the client needs. Based on this principle, the tax inspector is forbidden from requesting the taxpayer reports and other documents if there was no reason to believe wrongdoing and such search is being carried out as a fishing expedition. The questions for deliberation thus are - Whether confidentiality of written communication between chartered accountants and client is protected?

Whether protection of confidentiality includes advocates and law firm employees who provide or assist advocates in providing legal services and does not include lawyers, who provide their services independently not being members of the Bar?

Whether the lawyer acting as financial intermediary or financial advisor or agent or board member or a director of an entity has his confidentiality protected or not?

9.4.2 Possibility of passing information to third state

The OECD Multilateral Mutual Assistance Convention allows for the information to be passed on to a third state provided that the requested authority has had an opportunity to object or give its permission. However, the general tendency is to refuse the transfer of data to a third state.

The questions for deliberation on this aspect are:

Can the Contracting State refuse to provide the information if the disclosure is contrary to the Public Policy? Whether illegally obtained data used for inspection against the taxpayer is against the Public Policy to promote theft? Does it amount to information laundering, which could not be the intent of TIEA?

Can the courts declare the tax assessment based on documents illegally acquired as void?

Can the tax payer object after the information has been supplied? What are the procedural rights of the tax payer?

9.5 Jurisprudence

The effort to develop a global consensus towards co-operation in Exchange of Information between tax administrations has increased tremendously. In effect, the tax administrations have taken an aggressive approach for obtaining tax information. Under the current standards regarding Exchange of Information, the requested authority can refuse cooperation if the tax administration of the requesting country fails to demonstrate that the information sought is relevant for the administration or enforcement of its domestic laws.

In most cases, several inevitable questions arise regarding whether the information request is valid under both the relevant tax treaty and domestic law. In response, taxpayers have moved to block such information requests, especially when the nature of the request appears to be more of a 'fishing expedition' having no nexus with the taxability of the transaction.

Recently, the U.S. District Court of Illinois ('Court') in *Bikramjit Singh Kalra v. United States*[3] of America quashed summons that were issued by the U.S. Internal Revenue Service ('IRS') pursuant to a request made by the Indian tax authorities concerning the tax liability of (the taxpayer, on grounds of lack of statutory procedure and purpose.

Likewise, the Singapore High Court in the decision of *Comptroller of Income Tax v AZP*[4] dismissed the comptroller's application for an order requiring the bank to produce the Indian company's bank records and held that information cannot be disclosed under Article 28 of tax treaty in absence of strong connection between requested information & India's tax laws and such information is not foreseeably relevant for Singapore's domestic laws.

Thus the issue for consideration is - In view of the above decisions, could the Indian tax authorities make spurious or frivolous requests for information to other countries without strong evidence to simply conduct a fishing expedition? Whether a mere request not based on strong evidence would really suffice? What kind of evidence would be considered? Also, what is exactly meant by foreseeable relevance?

3. Case no 12-CV-3154. Date of the decision April 23, 2013.
4. [2012] SGHC 112

10. Salient features of section 94A of the Act

Central Government is authorised to notify any country or jurisdiction outside India as notified jurisdiction area ('NJA') having regard to fact that such country or jurisdiction does not have an effective Exchange of Information relating to taxation matters with India [Section 94A(1) of the Act]

Applicability of Transfer Pricing Provisions – If the taxpayer enters into transaction, where one of the party to transaction is a person located in NJA then in such a case all the parties will be deemed to associated enterprise of the taxpayer within the meaning of section 92A of the Act and the transaction as defined under section 94A(2)(ii) of the Act will be deemed to be international transaction within the meaning of section 92B of the Act. Further, all the provisions of transfer pricing except second proviso to section 92C(2) of the Act will be applicable. [Section 94A(2) of the Act].

The finance ministry had inserted this section to notify countries that were not cooperating in information exchange. The government is now considering blacklisting foreign jurisdictions not sharing information on money parked by Indians in their country, despite a tax information exchange agreement with India. Blacklisted countries would find it difficult to do business with Indian citizens. Besides a higher tax burden, Indian taxpayers dealing with such jurisdictions would be disallowed deductions in respect of expenditure, allowance or payment made to a financial institution in that country unless assessee maintains adequate documents and furnishes such information as may be prescribed.

11. CBDT's Manual on Exchange of Information:

CBDT's Foreign Tax and Tax Research Division has released a 88-page Manual on Exchange of Information ('MOE') on 17 January 2013. The MOE is intended to provide guidance to CBDT officers on how to effectively use the Exchange of Information ('EOI') provisions seeking information from foreign tax authorities as well as on how to deal with requests for information from foreign tax authorities. The manual outlines communication formats, protocols and guidelines for different types of Exchange of Information requests. While the number of requests from Indian IT department increased from 39 in FY 2008-09 to 386 in 2011-12, it was still felt as substantially low. Hence, such a manual was sought to primarily make the CBDT officers aware of the provisions of Exchange of Information as per the treaty.

The MOE notes that simultaneously and along with the global efforts, effective steps have been taken in the last three years for creating an appropriate legislative framework for receiving and effectively utilizing the information received from foreign jurisdictions. These steps include renegotiating the existing DTAAs, entering into new DTAAs with provisions on Exchange of Information as per internationally agreed standards and entering into TIEAs with no tax or low tax jurisdictions, signing of Multilateral Convention for Administrative Assistance, SAARC Limited Multilateral Agreement, etc. Further, a number of legislative changes have also been made including extension of time limit for completing of assessments, extending time limit for reopening cases to sixteen years etc. Administrative measures such as strengthening of the Foreign Tax and Tax Research Division in the CBDT and creation of a dedicated Exchange of Information Cell have also been taken.

The MOE highlights India's efforts to amend Article 26 (EOI) of various DTAAs in order to bring it in line with the OECD Model Tax Convention. Paragraphs 4 and 5 of Article 26 in OECD Convention provides for obligation to exchange information without domestic effect as well as exchange of banking information. The MOE states that even in the absence of paragraph 4 and 5 in a DTAA the Exchange of Information is possible. Therefore, such absence should not deter the officers from seeking banking information. ***The question here is, whether the other country would be willing to share the information in the absence of these paragraphs?***

MOE provides guidelines on how to make a request for Exchange of Information. It has provided a proforma for making an information request and states that the information request should be made through Competent Authority. The Competent Authorities for different regions have also been specified. The MOE notes that the AO is authorized to obtain information from foreign tax authorities in view of the provisions of Sec 142(2).

MOE says that while making a request, information like background note, summary of case, factual analysis should be given. It further specifies that all the means available in India for obtaining information should be exhausted before seeking information from foreign authorities. MOE states that when tax officers come across a situation where the data is available on servers / computers located in another country, then a request can be made to tax authorities of treaty partner country for requisite information from the person in control of such computer/server.

EOI is possible when such information is 'foreseeably relevant' for administration and enforcement of domestic law. MOE elaborates on the meaning of the term 'foreseeably relevant' and states that it should be demonstrated in the request made. It gives illustrations on the types of information that can be exchanged and clarifies that information which is available with tax department and other authorities such as government organisation, banks and FIIs etc could be exchanged.

MOE states that EOI can provide great assistance in the case of transfer pricing audits. The information exchange could also be useful to determine beneficial ownership, treaty exemption or tax residency. MOE provides guidelines on handling requests from foreign tax authorities, for making a request to foreign tax authorities for collection of taxes and handling of similar request from foreign tax authorities. It also elaborates on the other forms of administrative assistance like Automatic Exchange of Information, Spontaneous Exchange of Information, Tax Examination Abroad, Simultaneous Examination and Joint Audits.

MOE highlights the importance of giving feedback on information utilization which should be timely and comprehensive. It details the confidentiality provision with respect to the information collected through the use of EOI provisions. It further states that under the EOI provisions, any information received by a Contracting State must be treated as secret in the same manner as information obtained under the domestic laws of that Contracting State.

12. Automatic Information Exchange

Automatic Exchange of Information comprises periodic transmission of bulk tax payers information by one country to another country concerning various categories of income e.g. fees for technical services, dividends, interests, royalties, salaries, etc For example in India, the taxpayers are required to submit the information to Income Tax Department related to remittances made to the foreign tax payers as per the provisions of the Act and this information is submitted by the remitters online to the Income Tax Department. This data may be exchanged on automatic basis with the other countries so that the recipient country may ensure that the tax payers in their country have discharged their liability towards the payment of taxes. Automatic exchange can also be used to transmit other useful types of information such as change of residence, the purchase or disposition of immovable property, etc. In addition, information concerning the acquisition of significant assets may be used to evaluate the net worth of an individual, to see if the reported income reasonably supports the transaction. Different countries exchange different types of information under the Automatic Exchange of Information programme. Automatic Exchange of Information is most common with respect to interest and dividend income. Besides, it is also relevant with respect to income from dependent personal services, other income, and royalty income derived from the activities of artists, pensions, director's fees, income from independent personal services, income from immovable properties, business profits, income from government services capital gains and payments to students etc.

Automatic Exchange of Information is one of the most effective ways to improve voluntary tax compliance and decreases the incidence of tax evasion. Although many countries have started exchanging information automatically, at present it is not mandatory as per the provisions of the DTAAs/TIEAs and is not considered as a part of international standards on Transparency and Exchange of Information for tax purposes. However, this item is on the agenda for action in Base Erosion & Profit Shifting report of OECD.

12.1 India's Role and Scenario

India has taken a lead in making the Automatic Exchange of Information as standard of Exchange of Information so that all countries start exchanging the information available with them regarding taxpayers of other countries voluntarily and on automatic basis. India's Commitment to the exchanging information periodically was demonstrated by the speech of the Hon'ble Prime Minister during the Cannes Summit in November, 2011, where he stated the following:

> *"G-20 countries should take the lead in agreeing to automatic exchange of tax related information with each other, irrespective of artificial distinctions such as present or past, tax evasion or tax fraud in the spirit of our London Summit that the era of bank secrecy is over"*

The above statement was quoted by the Hon'ble Finance Minister while replying to the debate on adjournment motion on black money on 14th December, 2011. Further, during the G20 meeting in Los Cabos, Mexico on 18-19 June, 2012, mainly due to India's insistence, the following line was included in the official communiqué:

"We welcome the OECD report on the practice of automatic information exchange where we will continue to lead by example in implementing this practice. We call on countries to join this growing practice as appropriate and strongly encourage all jurisdictions to sign the Multilateral Convention on Mutual Administrative Assistance"

India has been receiving information from some countries on automatic basis in the past although the numbers were small as seen below:

Information received during	Pieces of Information
2008-10(disseminated in January, 2011)	7,704
January to June,2011	480
July to December,2011	1,006
January to June, 2012	4,614

(Source: Instruction No. 01 of 2013 dated 17th January 2013 issued by CBDT)

The information which is exchanged automatically is normally collected in the source country on a routine basis, generally through reporting of the payments by the payer (financial institution, employer, etc).

13. OECD report on 'A Step Change in Tax Transparency':

The OECD report on 'A Step Change in Tax Transparency' has been prepared in response to the G8 Presidency request, to analyse how jurisdictions could build on the recent developments to implement automatic exchange in multilateral context. It sets out key success factors for an effective model for automatic exchange, outlines four concrete steps needed to put such a model into practice. The steps include (i) enacting broad framework legislation to facilitate the expansion of a country's network of partner jurisdictions, (ii) selecting (or entering into) a legal basis for the Exchange of Information, (iii) adapting the scope of reporting and due diligence requirements and coordinating guidance, and (iv) developing common or compatible IT standards. Also, the timeframes for each of the action items are provided.

Further, the report recognises that offshore tax evasion being a global issue requires global solutions – otherwise the issue is simply relocated rather than being resolved. It states that a global solution also means a global standard to minimise costs for businesses and governments, while at the same time enhancing effectiveness, maintaining confidence in open markets and best serving society at large. A propagation of inconsistent models would be in nobody's interest.

It has been pointed out in the report that globalisation has enabled the taxpayers to keep vast amounts of money offshore and the same go untaxed to such an extent that taxpayers fail to comply with tax obligation in their home jurisdictions. Cooperation between tax administrations is critically required to tackle this problem and Exchange of Information is a key aspect of such cooperation.

The report recognises that for an effective automatic exchange of financial information, it must be specifically designed with residence jurisdictions' tax compliance and also it needs to be standardised so as to benefit the maximum number of residence jurisdictions and financial institutions while recognising that certain issues remain to be decided by local implementation. The advantage of standardization would be process simplification, higher effectiveness and lower costs for all stakeholders concerned.

The 2012 OECD report titled 'Automatic Exchange of Information: What it is, How it works and benefits, What remains to be done' recognizes (i) a common agreement on the scope of reporting and exchange and related due diligence procedures; (ii) a legal basis for the domestic reporting and international exchange of information; and (iii) common technical solutions as the main success factors for effective automatic exchange. The Report also lists four steps that could be taken to implement a standardised multilateral model of automatic exchange: (i) Enact broad framework legislation; (ii) Select a legal basis for the exchange of information; (iii) Adapt the scope of the reporting and due diligence requirements and coordinate guidance to ensure consistency and reduce cost; and (iv) Develop common or compatible IT standards.

The participants may discuss the following case studies resembling real life facts if time permits:

Case Study 7

Facts:

Mr. B, an Indian citizen and resident, is the promoter of a large consumer goods manufacturing group in India. He incorporated a company in British Virgin Islands (BVI) namely BVI Ltd in the year 2004-05. BVI Ltd was wound up in the year 2010-11. From the date of incorporation till winding up –

a) Mr. B was the sole shareholder of B Ltd, holding one ordinary share of US $ 1. Mr. B actually did not contribute US $ 1 but it has been recorded as share capital contribution in the books of BVI Ltd.

b) Throughout 2000-01 till date, Mr. B has been resident of India for income tax as well as FEMA purposes, though he has been travelling out of India frequently in each of these years ranging from 150 days to 170 days in each year. Mr. B is and has been holding directorship positions in many overseas subsidiaries of the group.

c) BVI Ltd was administered by a licensed professional administration company in BVI who provided two corporate directors, registered agent, registered office and a company secretary to BVI Ltd.

d) Initial incorporation cost was paid by a friend of Mr. B resident in United Kingdom (UK). Thereafter, annual professional fees and other expenses of BVI Ltd were met by BVI Ltd out of its revenues and borrowings.

e) BVI Ltd opened a bank account with the Singapore branch of a Swiss Bank. Mr. B has been sole signatory to bank account. Instructions to bank were given through fax. For opening the bank account, KYC documents of BVI Ltd and Mr. B were furnished.

For co-ordination of banking operations, bank provided a Relationship Manager based in UK branch of said Swiss Bank with whom Mr. B used to interact for all matters including the fax instructions.

f) During the period, BVI Ltd executed certain transactions both with the group companies of Mr. B (Indian and overseas) as well as with foreign third parties. Payments and receipts arising out of these transactions were routed through the Singapore bank account of BVI Ltd, with the fax instructions of Mr. B.

g) Maintenance of books of accounts and audit not being mandatory in BVI, it is not possible now to trace the transactional documents. However, Mr. B is able to recollect the transaction entries appearing in the bank statements, except some entries of receipts and payments amounting to US $ 1 million.

h) As mentioned above, Indian group companies availed certain services from BVI Ltd for which these Indian companies made payments and claimed tax deduction for these expenses.

Mr. B, being a young man, has a very good friend Ms. A, who is an Indian citizen but has been residing in France until March 2010 and has now moved & settled in USA. The winding up proceeds of BVI Ltd (substantial amount) were transferred to French bank account of Ms. A. Mr. B has not disclosed this overseas structure and bank account to the authorities in India. It is understood that BVI Ltd has earned and accumulated substantial income during its existence from its transactions with third parties and group companies.

In the year 2012-13, the information about Mr. B's aforesaid overseas structure has been disclosed on the website of ICIJ (www.icij.org), which reflects details pertaining to shareholding, directorships, bankers, etc. The website does not disclose the financial information pertaining to BVI Ltd.

Based on information available on the said website, Indian income tax authorities desire to investigate into this case and has issued the letters to Mr. B seeking further details of said overseas structure and bank account and has also asked Mr. B to sign a 'consent waiver form' whereby the bank is authorised to furnish relevant records of said bank account to Indian Income tax authorities. Mr. B has also been threatened of appropriate penal consequences if he fails to do so.

Mr. B proposes to deny having any such overseas structure and bank account as the BVI Ltd has already been wound up.

The Revenue Department of India seeks the following waiver letter from Mr. B

Privileged and Confidential:

For the attention of:	Copied to:
Mr. ABC General Counsel- Switzerland XYZ Private Bank SA XXX Street Geneva Switzerland	Mr. DEF General Counsel-Global Private Bank XYZ Private Bank SA XXX Street Zurich Switzerland

Account No(s). _______________ Master No(s). _______________

Instructions to provide Account Records

____

Name(s) of the Accountholder(s)

Name(s) of the Beneficial owner(s)/Settlor(s)/Beneficiaries (As appropriate)

____

Address of the beneficial Owner(s)/Settlor(s)/Beneficiaries

____

____

Date of Birth of Beneficial owner(s) / Settlor(s) / Beneficiaries

Contact Number/ Fax Number

I/We, _______________, am/are the ______of one or more accounts at XYZ Private Bank SA.

I/We hereby declare and confirm that I am/we are cooperating with the Income Tax Department, Government of India. In connection with our cooperation, I/we are providing a copy of this waiver to the Income Tax Department, Government of India.

I/We hereby instruct and authorize XYZ Private Bank SA to provide to me any and all Account Records in XYZ Private Bank SA's possession relating to the Account(s). With this instruction, I/we hereby waive all protections provided under the data protection, privacy, and/or bank secrecy laws of Switzerland.

I/We understand that 'Account Records' encompass all documents that a customer is entitled to, i.e.:

a) documents identifying the account holder, the beneficial owner and/or authorized persons;
b) documents pertaining to foreign entities established or operated on behalf of the Indian taxpayer;
c) account opening documents;
d) correspondence between the bank and the customer and/or Beneficial Owner and/or third parties in relation to the Account; and,
e) account statements and statements of assets.

I/We further instruct XYZ Private Bank SA to follow these instructions until revoked by me/us expressly and in writing. I/We confirm that I am/we are aware of the consequences that these instructions could have.

Privileged and Confidential:

I/We further instruct documentation be provided in both paper and electronic form to the above mentioned address. You are further authorized to inform XYZ Private Bank SA when documentation is released pursuant to this instruction and provide them with a copy of this instruction. I expressly waive the protection offered by the Swiss banking secrecy and data protection in rules accordingly.

For Accounts held through an entity (e.g. trust, corporation or foundation): I/We understand that only a person with legal authority can request the Account Records for a trust, corporation or foundation, such as an authorized signatory, power of attorney or trustee. We confirm:

- I am/ We are authorized to act on behalf of the entity holding the Account(s).
- The entity is no longer in existence and, accordingly, I am/We are the only remaining party/parties with an interest in the disclosure of the Account Records.
- I/We will promptly take appropriate steps to have the authorised signatory/power of attorney/trustee of the entity sign this instruction form and provide it to XYZ Private Bank SA.

Please send a copy of all Account Records to the following recipient:

Name　　　　Company/ Firm

Contact Number/ Fax Number

Signature(s) of the account holder(s)/beneficial owner(s)/authorised signatory/trustee (please indicate):

Place/Date　　　　Signature/Print Name

Place/Date　　　　Signature/Print Name

Please have your signature notarized

Issues:

- Can the Indian tax authorities approach tax authorities of the other country to seek the necessary information? If yes, tax authorities of which country– Singapore, BVI, UK or Switzerland? Can tax authorities of the other country deny the information sought on the basis of lack of foreseeable relevance?
- If the tax authorities of the relevant country express their inability to provide the information - Can the Indian tax authorities approach the Tax Courts of that country to compel the bank to give the information?
- What could be the tax and penal consequences in India under Income Tax Act, 1961-
  - If Mr. B admits having the overseas structure and the bank account
  - If Mr. B denies having any such overseas structure and bank account
- Whether any other Indian authorities such as authorities under Foreign Exchange Management Act or Prevention of Money Laundering Act, etc. can seek these information from foreign states?

Case Study 8:

Facts:

Mr. X is an employee of a XYZ bank of Switzerland. Mr. X in some manner succeeds to get unauthorised access to the database and collects confidential information about all HNI's accounts with the bank. Mr. X analyses this information and realises that several Indian film stars, celebrities, politicians and German HNIs have hefty sums lying in the Swiss bank. Mr. X thinks of making fortune out of this opportunity and approaches the Indian and German Governments to provide such information for a handsome price. The Governments of one of the countries acquire the stolen information from Mr. X and discloses the same to the Government of the other country. On this basis, the Revenue Department of the latter country launched investigation and interrogation against its resident taxpayers with respect to their foreign accounts.

In this process, Indian Income tax authorities issued a letter u/s 133 of the Income-tax Act to Mr. Y, a resident of India, alleging that based on information available in their possession, they are aware that Mr. Y is having a bank account with XYZ bank, Switzerland. The letter also mentions the bank account number and the name of the bank. Vide this letter, Income tax authorities also sought following -

i. Details and documents of all foreign bank accounts of Mr. Y and all of his family members held in last 10 years.

ii. Details and documents of all foreign entities (company, trust etc) in which Mr. Y and/ or any of his family members held shares or directorship or any other interest in last 10 years.

Mr. Y appeared in the proceeding and filed an affidavit denying having any foreign bank account as alleged by the Indian Income tax authorities.

Indian Income tax authorities issued him another letter u/s 133. In this second letter, the Indian Income-tax authorities took note of Mr. Y's denial of having any foreign bank account. However, vide this second letter, Indian Income tax authorities called upon Mr. Y to sign and execute a 'consent waiver form' in the prescribed form annexed with the said letter authorizing XYZ bank to furnish the records of the alleged bank account to Indian Income tax authorities and to waive all the privileges available under the banking secrecy laws of Switzerland. Consent Waiver Form also states that his waiver shall be in force until revoked by the executor expressly and in writing.

Having received this letter, Mr. Y now seeks collective advice of BCA ITF Conference-2013 participants on the following issues as Mr. Y is now getting very nervous on this issue and is afraid of any unnecessary prosecution.

Issues:

- Can the tax authorities / Governments acquire such stolen information?
- Based on such stolen information can proceedings be initiated on tax payers?
- Should he sign and execute the 'consent waiver form'?
- Having executed 'consent waiver form' and delivering the same to Indian Income-tax authorities, can he revoke this consent by directly filing a revocation letter with XYZ bank?

Conclusion

With an increasing integration of the world economies, the need for Exchange of Information by the tax administrations cannot be overstated. Substantial work has recently been done in this area and still much more needs to be done. It has been duly realized that merely having an article in a tax treaty is no guarantee that there will be effective Exchange of Information. And thus TIEA are gaining significance and relevance as well. Tax Information Exchange Agreements (TIEA) with known tax havens in order to ferret out information is the order of the day. India also reportedly wants to enter into such agreements. However, negotiating bilateral TIEAs with about 70 known havens is both time and resource-intensive. Despite this, it is overwhelming to note that all major countries recognize the importance of Exchange of Information in today´s borderless world not just to counter tax evasion but also to counter terrorism.

In the Indian context, effective Exchange of Information would require an attitudinal shift on administrations' part and the need for calibrated policy endeavours. Recent amendments to the Income Tax law, empowering signing of Agreements with non sovereign states and move to rush signing of TIEA is suggestive of the pace of development. However, hurdles to implementation of such bilateral agreements are being witnessed.

In conclusion, the so-called "big bang" of 2009 has led to an unprecedented network of tax treaties, TIEAs, multilateral treaties, directives and informal agreements on Exchange of Information. Fundamentally, it seems that there are three main challenges: (a) to coordinate all these legal rules; (b) to ensure that an effective Exchange of Information takes place, namely that states can effectively obtain the relevant information domestically through different manners such as KYC questionnaires and determination of beneficial ownership; and (c) protection of the taxpayer. On this third point, what about an international standard of protection rules for the taxpayer? After all, the universe is expanding at all points.

A thought came to my mind – This paper ought to have been written by a policy maker. But I have endeavoured to provide the participants, a birds-eye view of the recent trends in Indian tax treaties including TIEAs. Nevertheless, the participants would appreciate that each topic taken for discussion is a topic in itself and there would be a desire to have in depth and detailed discussion on the same. Also it is possible to write a book on each of the above topics. I am sure some young scholar in future will do that for BCA RRC. I am an old man and do not have the appetite to write so much in detail anymore.

Appendix

References to Recent Indian Tax Treaties:

1) India – Malta Tax Treaty (2013) – Not yet effective
(Substitution to the 1994 Tax Treaty)
2) India – Poland Protocol to the 1989 Tax Treaty (2013) – Not yet effective
3) India – Malaysia Tax Treaty (2012) – Effective from April 1, 2013
4) India – United Kingdom Protocol to the 1993 Tax Treaty (2012) – Not yet effective
5) India – Nepal Tax Treaty (2011) – Effective from July 16,2013
(Substitution to the 1986 Tax Treaty)
6) India – Ethiopia Tax Treaty (2011) – Effective from April 1, 2013 (New Tax Treaty)
7) India – Norway Tax Treaty (2011) – Effective from April 1, 2012
(Substitution to the 1986 Tax Treaty)
8) India - Australia Protocol to the 1991 Tax Treaty (2011) - Not yet effective
(Substitution to the 2001 Tax Treaty)

Summaries of Foreign Case Laws:

1) **Smallwood v. Commissioners for H M Revenue and Customs- [2010] EWCA Civ 778 -** In this case, Mr Smallwood, who was resident and domiciled in the UK, created the Trevor Smallwood Settlement (“the Settlement”) in 1989 for the benefit of himself and his family. The trustee of the Settlement was a Jersey company and the Settlement’s assets comprised primarily shares in two quoted companies, the value of which had increased considerably.. Mr Smallwood and the trustee had been advised to dispose of the shares.

Section 86 of the Taxation of Chargeable Gains Act 1992 (“TCGA”) contains special provisions in relation to chargeable gains arising to non-resident trustees where there is a UK resident settlor who retains an interest in the trust. If the relevant conditions are met, the gains arising to the trustees are treated as arising to the settlor directly. The Settlement met all of the conditions under section 86 TCGA and, therefore, had the Jersey company remained the trustee of the Settlement throughout the year of assessment, Mr Smallwood, as the settlor, would have been liable to capital gains tax (“CGT”) on the chargeable gain arising on the disposal of the shares.

In order to mitigate the CGT payable on this gain, Mr Smallwood was going to make the most of a so-called “round the world” scheme. The scheme involved appointing a Mauritian company as trustee of the Settlement in place of the Jersey company prior to the trustees selling the shares. At the time in question, Mauritius did not tax capital gains and had a double tax agreement (“DTA”) with the UK under which chargeable gains on the shares were only taxable in the state in which the trustees were resident. In the same tax year, the Mauritian company retired and Mr and Mrs Smallwood were appointed as trustees of the Settlement. The purpose of this was in order to migrate the Settlement back to the UK so that the trustees were not non-UK resident for the complete tax year in question. The trustees' UK return for the Settlement claimed double tax relief in respect of the gains accrued on the sale of the shares, which was disallowed by HMRC. Mr Smallwood's personal tax return was also amended to include the chargeable gain.

The Special Commissioners had found that the trustees were dual-resident for the purposes of Article 4(1) of the DTA. This required them to consider the tiebreaker test at Article 4(3). The tie-breaker is based on the Settlement's place of effective management ("POEM"). The Special Commissioners interpreted POEM to mean the place in which key management and commercial decisions were made and this was found to be in the UK as there was a scheme of management which went above and beyond the day-to-day management by the trustees, the control of which was in the UK. This meant that, although the disposal took place when the Settlement had offshore trustees, the highest level decisions had been made in the UK. The trust was, therefore, UK resident and Article 13(4) of the DTA did not provide protection from UK tax. The chargeable gain was, therefore, taxable in the UK. The taxpayers appealed the decision.

Upholding their appeal, the High Court held that a "snapshot" approach should be used when interpreting Article 13(4) of the DTA, i.e. it was only necessary to consider the residence of the trust at the date of the disposal of the shares. On the basis that the trust was clearly resident in Mauritius at the date of disposal, the capital gain arising was only taxable there, and there was no need to consider the tie-breaker test based on the POEM of the trust. HMRC appealed. The Court of Appeal rejected the argument that the residency of the trustees at the date of disposal, i.e. the "snapshot" approach, was the only method of determining the issue of residency, and that the subsequent actions following the disposal must also be considered in order to determine all of the possible tax consequences. It was held that the trust was resident in both the UK and Mauritius in the year in question and it was, therefore, necessary to consider the tie-breaker test. Hence, the trust was subject to UK tax in respect of the gain on the sale of the shares.

2) **Royal Bank of Scotland (2006) 9 ITLR 683 -**

The facts of the case: the US parent company sold to a UK company (Royal Bank of Scotland-RBS), usufruct of shares of its fully owned French subsidiary. According to the terms of the contract, consideration paid by RBS to acquire usufruct would be recovered by RBS in form of a pre-determined dividend paid by the French subsidiary. The US parent company guaranteed RBS compensation, in case of failure of the French subsidiary to pay the dividend. The US parent had also agreed to buy back shares of the French subsidiary if the dividend did not reach RBS in a pre-determined manner. French tax authorities did not consider RBS a beneficial owner. The Court of Appeal in Paris decided in favour of the taxpayer. However, Counseil de Etat ruled that RBS was not a beneficial owner. The Court held that this arrangement was done to hide the real transaction of the loan, which would be repaid in the form of dividends from the French subsidiary. The Court observed that the main purpose of the arrangement was to access the France-UK tax treaty to obtain refund of tax credit on taxes paid on dividend income received by RBS.(Avoir Fiscal)

3) Velcro Canada v. The Queen [2012] 20 12TCC57 -

The facts of the case are: Velcro Canada - a company resident in Canada - paid a royalty to Velcro Holdings BV, a company resident of Netherlands. The intellectual property for the use of which royalty was paid was owned by another group company - Velcro Industries BV - which was resident in the Netherlands Antilles. The Netherlands Antilles company (Velcro Industries BV), being owner of IPs assigned the same to the Netherlands holding company (Velcro Holding BV) for the consideration of an amount calculated as a percentage of net sales of the licensed products within 30 days of receiving royalty payments from the Canadian company. The percentage was ultimately determined to be equal to 90 percent of the royalties received on approval from the Dutch authorities. Tax authorities held that the Netherlands holding company (Velcro Holding BV) was not a beneficial owner. However, the Court held that it was a beneficial owner because royalty payments were intermingled with the holding company's other accounts. The funds were not segregated and paid directly to the Netherlands Antilles company (Velcro Industries BV). The funds were exposed to creditors of the Netherlands holding company. After elaborate discussion, it held that the holding company in the Netherlands had the "possession, use, risk and control" of the funds. In addition, the holding company (Velcro Holdings BV, Netherlands) was neither an agent nor a nominee nor it could be regarded as a conduit company. It did not have the power to legally bind the Netherlands Antilles Company(Velcro Industries) and was acting on its own behalf at all times. Applying Prévost, it was held that a conduit has absolutely no discretion with respect to funds received, which was not the case here.

4) Comptroller of Income Tax v AZP [2012] SGHC 112 -

AZP is about the Exchange of Information clause within the Singapore-India tax treaty. The current Organisation for Economic Co-operation and Development model treaty language envisages the sharing of information that is "foreseeably relevant" to the administration and enforcement of a country's tax laws. "Fishing expeditions", i.e. speculative requests for information that have no apparent link to an investigation, are not allowed. Where the information requested is protected by Singapore bank confidentiality rules, the Comptroller has to apply to the courts for access. In this case, the Comptroller made an application under section 105J of the Income Tax Act for an order requiring AZP, a bank in Singapore, to produce records and information relating to two bank accounts, from 1 January 2008 to date, held with AZP. Account 1 was held in the name of Company X and Account 2 was held in the name of Company Y. The Indian tax authorities had seized documents from an Indian national and believed that those documents indicated the existence of undeclared income and bank accounts overseas. It was alleged that the two accounts held with AZP were associated with the Indian national and the Indian tax authorities had therefore requested the Comptroller to facilitate the release of certain information under the Singapore-India tax treaty. The Comptroller's application was dismissed by the High Court. Choo Han Teck J was not satisfied that the information requested was "foreseeably relevant" for carrying out the provisions of the Singapore-India tax treaty because of inadequate supporting documentation provided by the Indian tax authorities. Companies X and Y were not Indian-incorporated entities. Nor were they under any investigation by the Indian tax authorities. The Indian tax authorities were not able to provide evidence of any transaction between the Indian national and either of the companies on or after 1 January 2008 (which is the effective date of the Exchange of Information clause). All that was provided was certain unsigned transfer instructions issued before 2008. 5Ever since the incorporation of an Exchange of Information clause within many of Singapore's tax treaties, there have been concerns as to how stringent or liberal the courts would be in allowing access to information held by banks, trustees, or the like. After all, Singapore prides itself on the security and integrity of its banking information. While Singapore is obliged to meet its treaty obligations, the courts need to safeguard the privacy of taxpayers. A delicate balancing exercise, no doubt, but if AZP is any guide, it seems clear that the courts will ensure that only specific and concrete requests are entertained.

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INDIA – TAXATION SYSTEM

"Ideally, governments should collect taxes like a honeybee, which sucks just the right amount of honey from the flower so that both can survive." - Chanakya's Arthashastra (350 BC)

India has had a mature tax system for a period of over 10,000 years. Rishi Manu laid down some clear rules of taxation:

- ❖ Taxes should be related to the income and expenditure of the subject.
- ❖ There should not be extremes, neither complete absence nor exorbitant taxation.
- ❖ The king should arrange to collect the taxes in a manner such that the subjects wouldn't feel the pinch of paying them.
- ❖ Traders and artisans should pay 1/5th of their profits in silver and gold whilst agriculturists 1/6th, 1/8th or 1/10th of their produce, depending on their circumstances.

Some of these have evolved over time and still exist in the present-day taxation system.

DAD	Manu's taxation system
1970	11 tax slabs with highest tax rate being 97.75% including surcharges.
1860	The British officially introduced a systematic code of income tax
1873	Tax system abolished
1886	Tax system re-introduced
1950-80	Income tax levels in India were extremely high at
1991-92	Gross direct tax collections of the Central Government: ₹ 15,352 crore
1992-93	Tax rates were reduced later on, by maximum tax rates were reduced to 40%.
2012-12	Gross direct tax collections of the Central Government: ₹ 548,845 crore

(*Source: http://incometaxindia.gov.in/HISTORY/PRE-1922.ASP)*

INTERNATIONAL TAX & FINANCE CONFERENCE 2013

Bombay Chartered Accountants' Society
7, Jolly Bhavan 2, Ground Floor, New Marine Lines, Mumbai - 400020
Website : www.bcasonline.org | Email: bca@bcasonline.org
BCASWebTV: www.bcasonline.tv | Tel: +912261377600 | Fax: +91 2261377666