



# Overview of DTAA Provisions

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# Structure of DTAA

<b>Category</b>	<b>Includes</b>
Scope of Convention	Persons and Taxes Covered
Definitions	General Definitions; Definition of Resident and PE
Taxation of Income	Income from Immovable Property; Business Profits; Shipping and Air Transport; AEs; Dividends; Interest; Royalties/FTS; CG; IPS; DPS; Directors Remuneration; Pension; Government Service; Teachers; Students; Other Income
Taxation of Capital	Capital
Methods for Elimination of Double Taxation	Exemption/Credit method
Special Provisions	LOB; Non-discrimination; MAP; EOI; Assistance in Collection of Taxes; Diplomats and Members of Consular Posts
Final Provisions	Entry into Force; Termination
Protocol	Amendments to DTAA

# Title & Preamble of DTAA

## TITLE

- ❑ UN Model DTC 2011
  - Avoidance of Double Taxation
  - Prevention of Fiscal evasion
- ❑ *Comments*
  - Addtl: Promoting Economic cooperation

## PREAMBLE

- ❑ UN Model DTC 2011
  - In accordance with constitutional procedures
- ❑ *Comments*
  - BEPS: Enhancement of co-operation in tax matters; Conclusion of DTAA w/o creating opportunities for non-taxation or reduced taxation through treaty shopping arrangements

# Article 1 - Persons Covered

- UN Model DTC 2011
  - “Persons”
  - “Residents”
  - One or both of the Contracting States
- *Comments*
  - Pass through partnerships?

# Article 2 - Taxes Covered

- UN Model DTC 2011
  - Taxes on Income & Capital. Includes tax on wages / salaries, CG
  - Imposed by Contracting State or Political Subdivision or Local Authority
  - Listing of various types of existing taxes
  - Introduction of / Replacement by identical and substantially similar taxes covered. Competent authorities to notify each other.

# Article 2 – Taxes Covered

## □ *Comments*

- Some Indian DTAA's (e.g. Spain DTAA) contain reference to wealth tax. But abolishment of wealth tax makes it redundant.
- Many Indian DTAA's cover even State taxes [e.g. Germany DTAA(trade tax)] whereas with USA does not cover state taxes; covers even municipal taxes [e.g. Switzerland (communal taxes)]; covers even taxes imposed on elements of income although not income tax [e.g. Finland DTAA (church tax)]
- Equalisation levy?

# Article 3 – General Definitions

## □ UN Model DTC 2011

- Contains important definitions
- For undefined terms, meaning to be taken from domestic law “at that time under law” (firstly tax law failing which general law meaning)

# Article 3 – General Definitions

## □ *Comments*

- India-UK Protocol: Definition of person specifically amended to accommodate UK pass through partnerships
- Sec 90(3) of Income Tax Act: Terms not defined under Act or DTAA, meaning to be assigned to it from CBDT Notification
- Ambulatory approach or Static Approach? – many Indian DTAA's prescribe ambulatory approach (Australia, Finland, Indonesia)

# Article 4 – Resident

## □ UN Model DTC 2011

### ➤ Definition of 'Resident'

- “Liable to tax”
- Deciding factors as referred to in domestic tax law
- Excludes Limited liability to tax

# Article 4 - Resident

## □ UN Model DTC 2011

### ➤ Tie Breaker Test Hierarchy - Individuals

- Permanent Home
- Centre of Vital Interest – Personal and economic relations
- Habitual Abode
- Nationality
- Competent authority mutual agreement

### ➤ Tie Breaker Test Hierarchy – Other than individuals

- POEM
- Competent authority mutual agreement

## □ *Comments*

- Split period residence
- POEM interpretation countrywise
- BEPS Action 6 discards POEM test

# Article 5 - Permanent Establishment

## □ UN Model DTC 2011

### ➤ Fixed Place PE

- Place of business: a facility such as premises or, in certain instances, machinery or equipment
- At disposal requirement
- Fixed: Distinct place; Certain degree of permanence
- Carrying on: Regularity of business

### ➤ Examples of Fixed place PE: Branch, office, factory, workshop

### ➤ Construction PE

- Building site, construction, assembly, installation, connected supervisory activities
- >6 months

### ➤ Service PE

- Furnishing of services
- > 183 days in any 12 month period (not necessarily tax year)



# Article 5 - Permanent Establishment

## □ UN Model DTC 2011

- Preparatory and Auxiliary activities: [Non-essential / Non-significant]
  - Use of Facilities for storage or display
  - Maintenance of stock for storage or display / processing by another enterprise
  - Maintenance of place of business for mere purchase
  - Maintenance of place of business for collecting information
  - Maintenance of place of business for other preparatory or auxiliary activities such as advertising, carrying out scientific research, servicing of patent
- Agency PE
  - Habitually exercises authority to conclude contract
  - Habitually maintains stock and regularly delivers from such stock
  - Activities devoted wholly or almost wholly on behalf of the enterprise and dealing at non-ALP

# Article 5 - Permanent Establishment

## □ UN Model DTC 2011

### ➤ Insurance PE

- Foreign reinsurer collects premium in Source State
- Insures risks in Source State

### ➤ Subsidiary as PE

- Either fixed place PE or agency PE

## □ *Comments*

- BEPS Action 1 – Digital economy
- Delivery activity through warehouse may constitute PE under UN Model DTC 2011
- Assembly operations covered under Construction PE vis-à-vis OECD Model DTC
- Article 5(1) vs. Article 5(2)

# Article 6 – Income from Immovable property

## □ UN Model DTC 2011

- Source taxation rights given for income from immovable property
- Meaning of immovable property as per domestic law
- Immovable property includes livestock, right to work mineral deposit, sources and other natural resources
- Excludes ships, boats, aircrafts

# Article 7 – Business profits

## □ UN Model DTC 2011

- Business profits taxable in source state only if there is PE
- Force of attraction rule
- Attribution based on separate entity approach
- Deduction for executive and general administrative expenses wherever incurred (i.e. even head office expenditure).

# Article 7 - Business profits

## □ UN Model DTC 2011

- No deduction / income consideration for internal dealings between PE and head office (or between two PEs of the same head office) otherwise than reimbursement of actual expenses (Exception for banks in case of interest payment/receipt)
- Alternative provision: Attribution based on formulary apportionment
- Consistency in attribution approach
- Priority of special articles over Article 7

## □ *Comments*

- Subject to limitations of tax laws of Source State - Sec 44C, 44DA, etc.
- Attribution is a complex exercise and prone to litigation ;
- Rule 10
- Profit attribution exercise undertaken by each State since Residence State has to grant credit
- UN vs. OECD – Profit attribution

# Article 8 – Shipping, Inland Waterways Transport & Air Transport

## □ UN Model DTC 2011

- Two alternatives:
  - Sole taxing rights to State in which POEM is situated vs.
  - Limited Source State taxing rights arising from more than casual operations
- “International traffic”
- Types of income covered: Transportation income; Directly connected income; Ancillary activity income
- Participation in pool, joint business, international operating agency

## □ *Comments*

- Most Indian DTAAAs do not cover inland waterways.
- Treatment of investment income of shipping/air transport enterprises
- Article 8 prevails over Article 7

# Article 9 – Associated Enterprises

## □ UN Model DTC 2011

- Adjustments to profits for tax purposes only. Not for accounting purposes
- AEs if participation in (and/or common) management, control, capital and non ALP dealings
- Corresponding adjustment by Residence State
- Corresponding adjustment not to be granted in case of fraud or gross negligence or wilful default

## □ *Comments*

- Does not conflict with national legislations
- Corresponding adjustments not automatic. Only if competent authority of Residence State considers the adjustment as proper. Otherwise MAP.
- Thin capitalisation rules not in conflict with Article 9
- Secondary adjustment

# Article 10 – Dividends

## □ UN Model DTC 2011

- Application of Article: Dividends **paid** by resident of Source State to resident of Residence State
- Shared taxing rights but limitation for source state.
- Definition of “Dividend” + Meaning of “Beneficial owner”
- Equal taxation rights to source state (i.e. Article 7 and 14 presides over Article 10) if holding (in respect of which dividends are paid) is effectively connected with PE/Fixed base in Source State
- No force of attraction: Source State cannot tax the dividends distributed (or undistributed profits) by enterprise of residence state even if such dividends are out of profits arising from Source State.

## □ *Comments*

- Effectively connected: PE is economic owner
- Dividends “paid”
- Branch profit tax

# Article 11 - Interest

## □ UN Model DTC 2011

- Application of Article: Interest **arising** in Source State and paid to resident of Residence State
- Shared taxing rights but limitation for source state.
- Definition of “Interest” + Meaning of “Beneficial owner”
- Equal taxation rights to source state (i.e. Article 7 and 14 presides over Article 10) if debt-claim (in respect of which interest is paid) is effectively connected with PE/Fixed base in Source State
- “Arising”: Deemed in the Source State if payer is resident of Source State *or* if PE/fixed base of payer located in Source State (and interest borne by PE/fixed base)
- Article applies only to ALP amounts. Excess amount could be recharacterized under domestic law

## □ *Comments*

- Exemption for government(-run) banks; Islamic finance instruments
- Risk of double taxation in case of back to back arrangements



# Article 12 - Royalties

## □ UN Model DTC 2011

- Application of Article: Royalties **arising** in Source State and paid to resident of Residence State
- Shared taxing rights but limitation for source state.
- Definition of “Royalties” + Meaning of “Beneficial owner”
- Equal taxation rights to source state (i.e. Article 7 and 14 presides over Article 10) if right or property (in respect of which royalty is paid) is effectively connected with PE/Fixed base in Source State
- “Arising”: Deemed in the Source State if payer is resident of Source State *or* if PE/fixed base of payer located in Source State (and royalty borne by PE/fixed base)
- Article applies only to ALP amounts. Excess amount could be recharacterized under domestic law

# Article 12 - Royalties

## □ *Comments*

- FTS Article to be introduced in revised UN Model; present in most Indian DTAAAs
- Concept of FIS – Make available
- Exemption of payment for personal use under FTS
- Exemption of payment for teaching activities under FTS
- Characterization issues for Royalty:
  - ICS equipment
  - ICS experience
  - Computer Software
  - E-commerce payments (e.g. cloud computing, download of digital products)
  - Transponder leasing
- Secondary source rule: India-USA DTAA (Payment by non-resident payer to US payee for right to use ICS equipment in India)

# Article 13 - Capital Gains

## □ UN Model DTC 2011

- Alienation of Immovable property: Shared taxation rights between Residence State and Source State
- Alienation of Movable property of PE/fixed base: Shared taxation rights between Residence State and Source State
- Alienation of PE/Fixed Base itself: Shared taxation rights between Residence State and Source State
- Alienation of Ships and aircraft by operator: Sole taxation rights to state in which POEM is situated
- Source Rule - Alienation of shares in company / interest in partnership, trust, estate where such shares / interest derives > 50% value from immovable property in Source State: Shared taxation rights between Residence State and Source State
- Alienation of shares of Source State resident company held for more than 12 months: Shared taxation rights between Residence State and Source State

# Article 13 - Capital Gains

## □ UN Model DTC 2011

- Alienation of any other property: Sole taxation rights given to Residence State

## □ *Comments*

- Computation mechanism: As given in respective domestic laws (e.g. indexation, forex conversion rate, cost of acquisition, etc)
- Taxation of other securities such as bonds, debentures solely in Residence State
- Meaning of alienation?: Under domestic laws since not defined under DTAA. Sale, exchange, transfer, conversion, gift, inheritance?

# Article 14 - Independent Personal Services

## □ UN Model DTC 2011

- Primary right of taxation given to Residence State
- Secondary right given to Source State if:
  - There is fixed base in Source State and activities are performed in Source State through that fixed base or
  - Residents stay in Source state for > 183 days in any 12 month period
- Illustration of professional services

## □ *Comments*

- Inclusive meaning and not exhaustive.
- Same principles for determination of and attribution to PE to be applied for determining existence of as well as attribution to fixed base
- No force of attraction principle under this Article unlike Article 7
- Hierarchy between IPS and FTS

# Article 15 - Dependent Personal Services

## □ UN Model DTC 2011

- Primary right of taxation given to Residence State
- Secondary right given to Source State if:
  - Employee is present in Source state for > 183 days in any 12 month period **and**
  - Remuneration is paid by employer of Residence State **and**
  - Remuneration is not borne by PE/fixed base of employer in Source State
- Remuneration for employment exercised aboard ship/aircraft operated in international traffic: Secondary taxation rights given to state in which POEM of employer is situated
- Subject to Article on Directors Fees, Pension & Government Service

## □ *Comments*

- Meaning of “borne” by PE
- Concept of economic employer for 2<sup>nd</sup> condition
- ESOPs

# Article 16 – Directors’ Fees & Remuneration of Top-Level Managerial Officials

## □ UN Model DTC 2011

- Shared taxation rights between Residence State and Source State

# Article 17 – Artistes and Sportspersons

## □ UN Model DTC 2011

- Shared taxation rights between Residence State and Source State
- “Entertainer” and “sportsperson”
- Artiste companies clause

## □ *Comments*

- Entertainment character should be present
- Public performance criteria
- Streams of income covered?: Royalties, advertising income, sponsorship income

# Article 18 – Pensions and Social Security Payments

## □ UN Model DTC 2011

- Subject to Article on Government Service
- Two alternatives: Sole taxation right with Residence State vs. Shared taxation rights between Residence State and Source State
- But if pension and annuity paid under social security scheme of a Contracting State, then taxable solely under that State.

# Article 19 – Government Service

## □ UN Model DTC 2011

- Employment income paid by a Contracting State is taxable solely under that State unless it is paid to a national of the other state who did not become a resident solely for rendering the service.
- Pension and annuity paid by a Contracting State for services rendered to it is taxable solely under that State unless it is paid to a national cum resident of the other State.
- If business motive present, then this Article not applicable



# Article 20 – Students

## ☐ UN Model DTC 2011

- Remittances from abroad to a student / business trainee / apprentice studying in the Other Contracting State shall not be taxed in that State.

## ☐ *Comments*

- Time limitation in many DTAA's
- Article on similar lines for Teachers / Professors / Research Scholars dealing with remuneration earned by them in Source State

# Article 22 – Capital

## ☐ UN Model DTC 2011

- Similar on lines of Article 13 – Capital Gains

## ☐ *Comments*

- Redundant in Indian context since wealth tax has been abolished

# Article 21 - Other Income

## □ UN Model DTC 2011

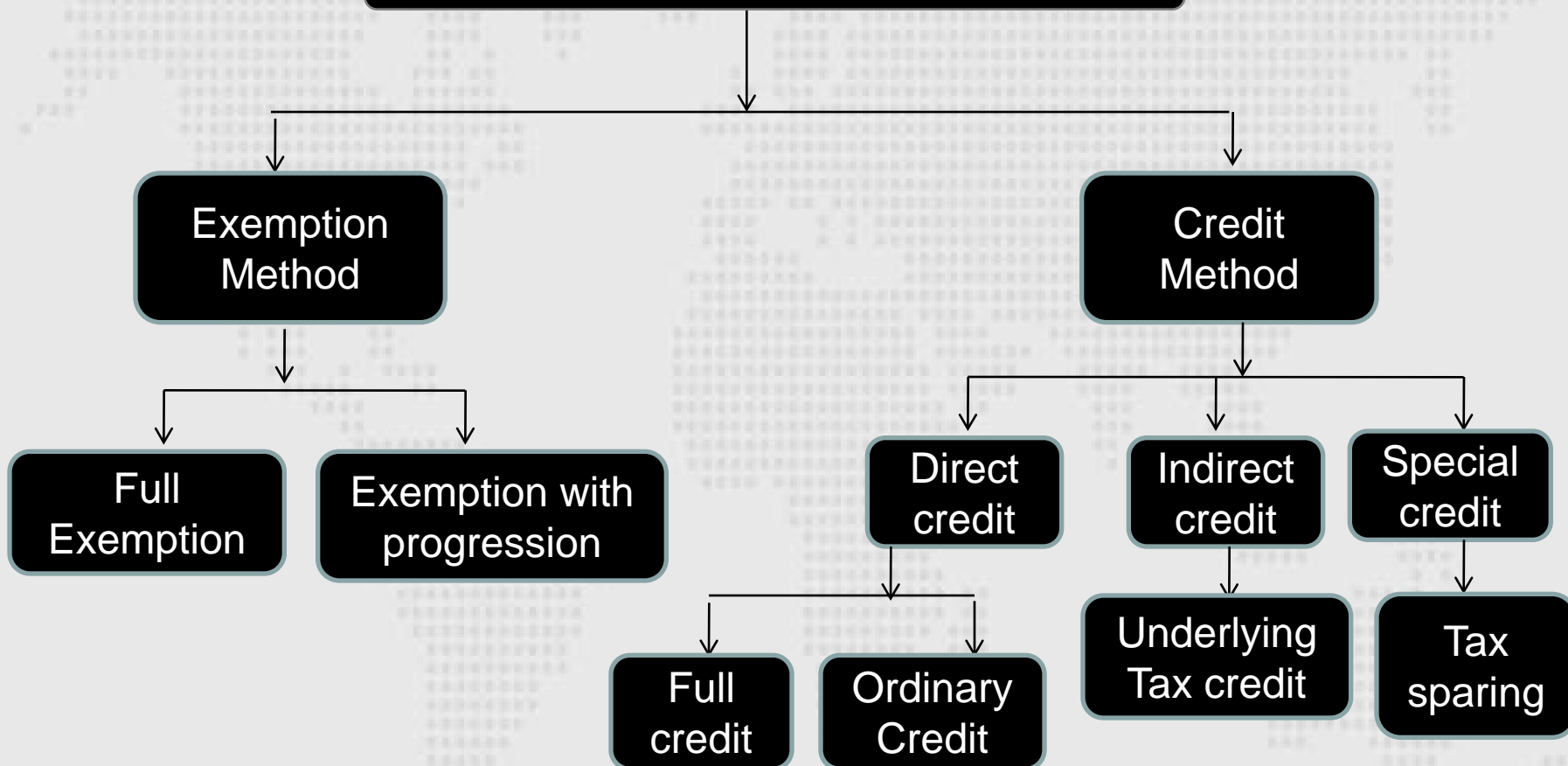
- Application of Article: For items of income not dealt with in any other Article of DTAA
- Shared taxation rights between Residence State and Source State
- Other income effectively connected to PE / Fixed base in Source State will be governed under Article 7 or 14 respectively

## □ *Comments*

- Meaning of “not dealt with”
- E.g. Alimony payment; lottery income; gift income
- Wherever arising: Rent paid by a resident of a Contracting State for the use of immovable property situated in a third State

# Article 23 – Exemption / Credit Method

## Methods of Elimination of double taxation



# Article 23 – Exemption / Credit Method

## □ *Comments*

- Most Indian DTAA's contain credit method as far as credit by India is concerned
- Under a particular DTAA, each Contracting State could also select different methods (e.g. India-Swiss DTAA)
- Exemption method generally excludes income streams under Article 10,11,12
- Qualification conflicts
- Timing mismatch
- Subject-to-tax clause
- Relief from taxes subject to domestic tax law provisions (viz. FTC rules)
- Recent draft FTC rules prescribe source by source as well as country by country limitation

# Article 24 - Non-Discrimination

## □ UN Model DTC 2011

- 24(1): Nationality based Non-Discrimination
- 24(2): Stateless persons Non-Discrimination
- 24(3): PE Non-Discrimination
- 24(4): Debtor-Creditor Non-Discrimination
- 24(5): Ownership based Non-Discrimination
- 24(6): Non-Discrimination not restricted by taxes listed u/a 2

## □ *Comments*

- Most Indian DTAAAs do not contain provision similar to Art. 24(2) & 24(6)
- “Same circumstances”; “carrying on same activities”; “same conditions”
- Triangular situations

# Article 25 – Mutual Agreement Procedure

## □ UN Model DTC 2011

- Actions of one or both Contracting States result or will result in taxation in variance with provisions of DTAA
- Irrespective of remedies under domestic law
- Case to be presented within 3 years of first notification of such action
- MAP agreement to be implemented notwithstanding domestic law time limits
- Alternative provision: Arbitration proceedings if MAP Agreement not reachable within three years of presentation.
- Exception to Arbitration: If court has given a ruling already

## □ *Comments*

- Interaction between MAP agreement and domestic court ruling

# Article 26 – Exchange of Information

## □ UN Model DTC 2011

- Exchange of information which is “foreseeable relevant”
- Not restricted by Article 1 and 2 of DTAA
- Information exchanged to be treated as secret and permitted to be shared/disclosed only under specific circumstances
- No exchange of information which contains professional and trade secret /process and/or sensitive for public policy purpose
- Information held by a Bank/FI also liable to be obtained and exchanged

## □ *Comments*

- Many DTAAs also contain Article on “Assistance in Tax Collection”

## □ *Recent Developments*

- Cbc Multilateral Competent Authority Agreement
- Multilateral Convention on Mutual Administrative Assistance in Tax Matters

# Article 28 – Entry into force

## □ UN Model DTC 2011

- Ratification of DTAA as per domestic law of each State
- Exchange of Instruments of Ratification by each State
- Effective Date: May be different for each State

## □ *Comments*

- Could be retrospective too especially for protocol introducing Article on EOI

# Article 28 – Termination

## □ UN Model DTC 2011

- Time period given for sending Notice of Termination
- Effective Date



# Limitation of Benefit

## □ *Comments*

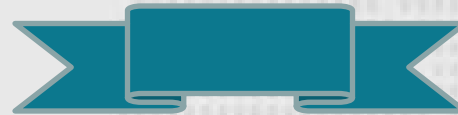
- US DTAA Model
- BEPS Action 6
- Many Indian DTAAs amended to include LOB clause
- Application of Domestic GAAR vs. LOB clause under DTAA
- “Main purpose test”
- Exclusions

## Protocol

## □ *Comments*

- Post negotiation / signing of DTAA
- MFN clause

**Thank you**



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