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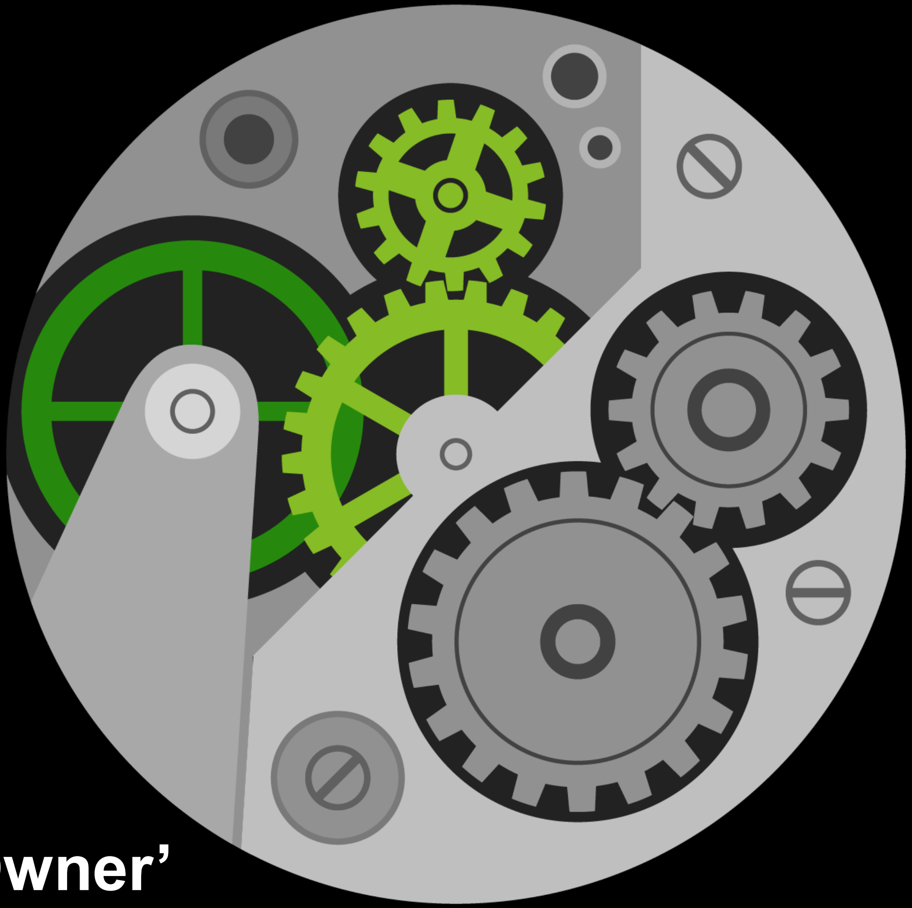


Concept of ‘Beneficial Owner’

Key Highlights

September 2024

CONTENTS

Concept of Beneficial Owner - Article 10/11/12

Concept of Beneficial Owner

- The concept of ‘beneficial owner’ can be found in almost all tax treaties that India has signed with other countries mainly in the allocation of taxing rights of passive income (viz., Dividend, Interest and Royalty and fees for technical services Articles)

- Taxpayers incorporate ‘pass-through’ entities in tax heavens or low tax jurisdictions for avoiding taxes or for availing concessional treaty rates. The concept of ‘beneficial owner’ acts as an anti-abuse provision (or) limitation of benefits clause under the tax treaties

- The term ‘beneficial owner’ is not defined under any tax treaty signed by India.

- Klaus Vogel - “Beneficial owner is a person who is free to decide whether or not the capital or other assets should be used or made available for use by others (i.e., the right over capital), or how the yields from them should be used (i.e., the right over income), or both”

- Legal Owner vs. Beneficial Owner - Beneficial ownership can exist even without legal ownership

Concept of Beneficial Owner

- Use of Beneficial owner as per clauses of 2017 OECD Model Convention:

Article 10 (Dividends)	Article 11 (Interest)	Article 12 (Royalties)
However, dividends paid by a company which is a resident of a Contracting State may also be taxed in that State according to the laws of that State, but <u>if the beneficial owner of the dividends is a resident of the other Contracting State</u>, the tax so charged shall not exceed: *a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company which holds directly at least 25 per cent of the capital of the company paying the dividends throughout a 365 day period that includes the day of the payment of the dividend (for the purpose of computing that period, no account shall be taken of changes of ownership that would directly result from a corporate reorganisation, such as a merger or divisive reorganisation, of the company that holds the shares or that pays the dividend);* *b) 15 per cent of the gross amount of the dividends in all other cases.*	*However, interest arising in a Contracting State may also be taxed in that taxed in that State according to the laws of that State, <u>but if the beneficial owner of the interest is a resident of the other Contracting State</u>, the tax so charged shall not exceed 10 per cent of the gross amount of the interest. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation*	*The provisions of paragraph 1 <u>shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State</u>, carries on business in the other Contracting State in which the royalties arise through a permanent establishment situated therein and the right or property in respect of which the royalties are paid is effectively connect- ed with such permanent establishment. In such case the provisions of Article 7 shall apply.*

Concept of Beneficial Owner - OECD Guidance

Can the provisions w.r.t Capital gains for conduit / shell company be applied here ? Ex: India-Singapore DTAA

OECD Guidance in Commentary to Article 10 (relevant extracts)

Para 12: State of source is <u>not obliged</u> to give up taxing rights over dividend income merely because that income was paid direct to a resident of a State with which the State of source had concluded a convention.

Para 12.2 and 12.3: Where an item of income is paid to a resident of a Contracting State acting <u>in the capacity of agent or nominee or conduit</u> it would be inconsistent with the object and purpose of the Convention for the State of source to grant relief or exemption.

Para 12.4: In these various examples (agent, nominee, conduit company acting as a fiduciary or administrator), the direct recipient of the dividend is not the "beneficial owner" because that <u>recipient's right to use and enjoy the dividend is constrained by a contractual or legal obligation</u> to pass on the payment received to another person. Such an obligation will normally derive from relevant <u>legal documents</u> but may also be found to exist on the basis of <u>facts and circumstances</u> showing that, in substance, the recipient clearly does not have the right to use and enjoy the dividend unconstrained by a contractual or legal obligation to pass on the payment received to another person.

Para 12.5: Concept of BO must not be considered as restricting in any way the application of other approaches (viz., addressing Treaty abuse etc.)

GAAR and PPT to be analysed separately

Para 12.6: Beneficial owner of Income is different from Beneficial owner of shares

Illustration

- XYZ India is an Indian company engaged in development of ERP software. It also has an IT enabled services division.

- XYZ India is held by:
  - XYZ Holdings BV, Netherlands - 70%; and
  - LMN Pvt Ltd - 30%

- XYZ India also availed loan from PQR Pvt Ltd. (INR denominated loan) and XYZ Investment Mauritius (FC denominated loan)
- XYZ India approached you to evaluate the (i) Tax rates applicable and (ii) Criteria to be fulfilled for availing the said rates

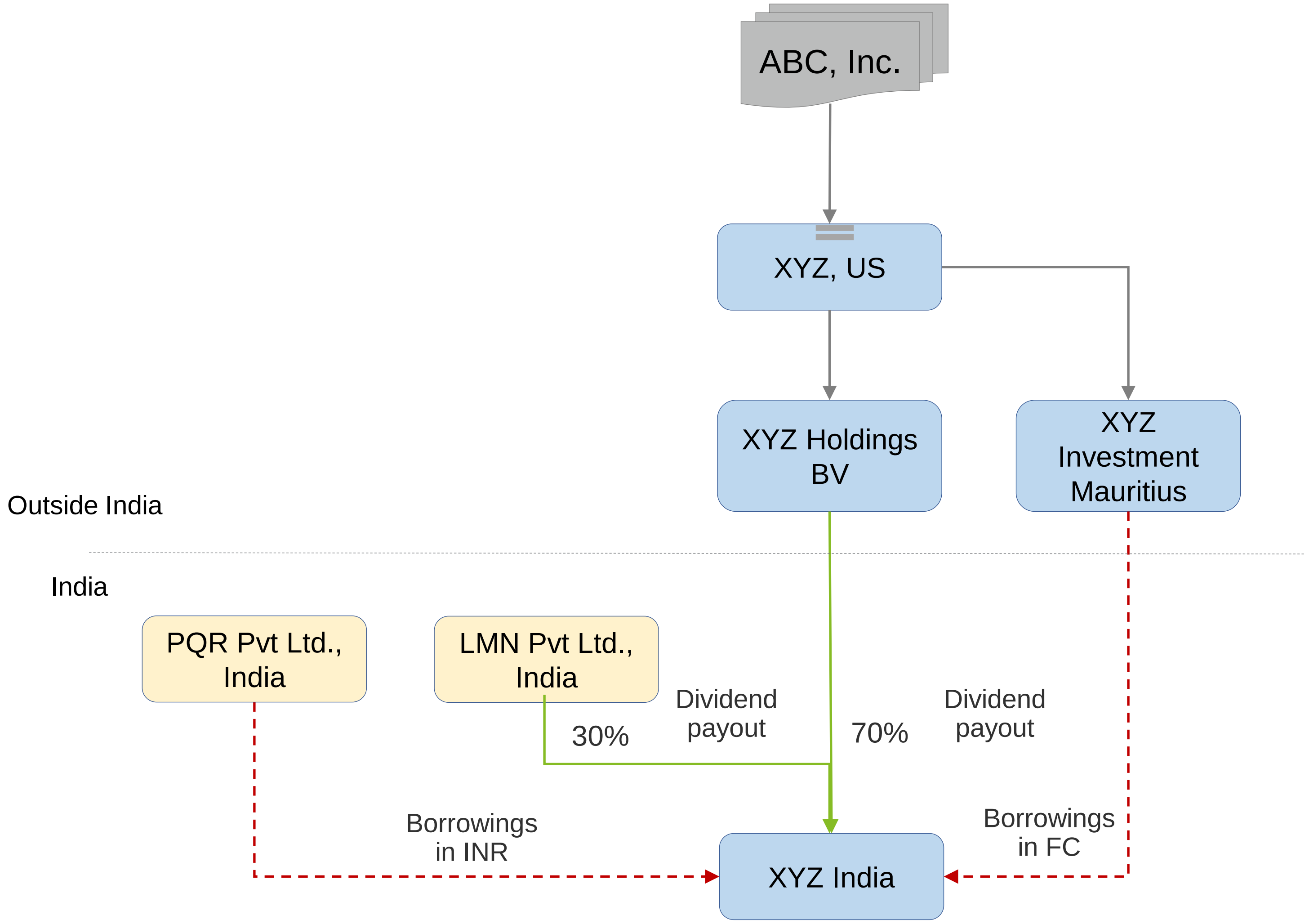


Illustration - Taxability under Act and DTAA (Pre BEPS and MLI)

- **Taxability in the hands of LMN India**:

  XYZ India shall withhold tax @ 10% u/s 194 while remitting Dividend income to LMN India, being a resident company.

- **<u>Taxability in the hands of XYZ BV</u>**:

  Rate of withhold tax u/s 195 r.w.s. 115A(1)(a)(A) of the Act is 20%

  However, Article 10 of India-Netherlands DTAA provides for a concessional rate of 10% subject to satisfaction of certain conditions.

  In addition, the Protocol to the India-Netherlands DTAA provides for MFN clause. Beneficial provisions of India-Slovenia (or) India-Lithuania, 5% rate can be explored (subject to notification by Ministry of Finance)*

- **Taxability in the hands of PQR India**:

  XYZ India shall withhold tax @ 30% u/s 194A while remitting Interest income to PQR India, being a resident company.

- **<u>Taxability in the hands of XYZ Mauritius</u>**:

  Rate of withhold tax u/s 195 r.w.s. 115A(1)(a)(B) of the Act is 20%. It is assumed that the XYZ India obtained a foreign currency loan from XYZ Mauritius in the year 2024. Thus, Sec 194LC would not be applicable.

  However, Article 11 of India-Mauritius DTAA provides for a concessional rate of 7.5% subject to satisfaction of certain conditions.

Particulars	Stream of Income	WHT Rate (Domestic law)	Rate of Tax (DTAA)
Dividend payment to LMN, India	Dividend	10%	NA
Dividend payment to XYZ BV	Dividend	20%	10%
Interest payment to PQR, India	Interest	30%	NA
Interest payment to XYZ Mauritius	Interest	20%	7.5%

* AO *v.* M/s Nestle SA, [Decision dated 19.10.2023 in Civil Appeal No. 1420 of 2023] (SC).

Illustration - Taxability under Act and DTAA (Pre BEPS and MLI)

India - US (Dividend)

- Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.
- However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the laws of that State, <u>but if the beneficial owner of the dividends is a resident of the other Contracting State</u>, the tax so charged shall not exceed 15 per cent of the gross amount of the dividends if the beneficial owner is a company which owns at least 10 per cent of the voting stock of the company paying the dividends

India - NL (Dividend)

- Dividends paid by a company which is a resident of one of the States to a resident of the other State may be taxed in that other State.
- However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, <u>but if the recipient is the beneficial owner of the dividends</u>, the tax so charged shall not exceed 10 per cent of the gross amount of the dividends.

India - Mauritius (Interest)

- Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
- However, subject to provisions of paragraphs 3, 3A and 4 of this Article, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, <u>but if the beneficial owner of the interest is a resident of the other Contracting State</u>, the tax so charged shall not exceed 7.5 per cent of the gross amount of the interest

Significance of TRC

Is TRC not sufficient ?

- Neither the Act nor the DTAAs' define the term 'beneficial owner'. However, the CBDT vide Circular No.789 of 2000 has issued clarifications with respect to taxation of income from dividends and capital gains under the Indian - Mauritius DTAA, which categorically states as under:

  "..It is hereby clarified that wherever a Certificate of Residence is issued by the Mauritian Authorities, such Certificate will constitute sufficient evidence for accepting the status of residence as well as beneficial ownership for applying the DTAC accordingly."

  Circular No. 789, dated 13-4-2000.pdf

- While TRC is a considered as a sufficient evidence to prove beneficial ownership, Courts in several cases have gone beyond TRC. The Apex Court in the case of Vodafone International Holdings [341 ITR 1 (SC)] held that while TRC can be a conclusive evidence for residential status and beneficial ownership, the same can be ignored if treaty is abused for fraudulent purpose of evasion of tax

- Thus, the concept of Beneficial ownership is a fact driven exercise

TRC is Sacrosanct - Judicial precedents

- **ADIT v Universal International Music B.V [2013] 31 taxmann.com 223 (Bombay)**

  - Assessee claimed the benefit of Article 12 of the Double Tax Avoidance Agreement (DTAA) between India and Netherlands and sought to pay tax at concessional rate at 10% in respect of royalty income received from M/s. Universal India Private Limited.

  - The Hon'ble High Court held in favour of the Assessee based on the Certificate issued by the Revenue authorities in Netherlands certifying that the assessee was a beneficial owner of the royalty received. Besides, reliance was placed upon the CBDT Circular No.789 dated 13/4/2000 that certificate from revenue authorities is sufficient evidence of beneficial ownership.

- **HSBC Bank (Mauritius) Ltd. vs DCIT (IT) -2(2)(2) [2018] 96 taxmann.com 544 (Mumbai - Trib.)**

This clause has been deleted from the re-negotiated India-Mauritius DTAA w.e.f 01 April 2017

  - Article 11(3)(c) of the India-Mauritius DTAA prescribes that interest income arising in a contracting state shall be exempt from tax in that state provided it is derived and beneficially owned by any bank carrying on a bona fide banking business which is resident of the other contracting state.

  - The Hon'ble Tribunal held that the CBDT Circular No. 789, dated 13-4-2000 is specifically in the context of incomes by way of dividend and capital gain on sale of shares. It would equally apply even in the present situation where the application of the provisions of the India-Mauritius DTAA is sought to be applied for considering the taxability of interest income as per article 11(3)(c) of the India-Mauritius DTAA. On this aspect itself the plea of the assessee is to be upheld that assessee is the 'beneficial owner' of the impugned interest income on the strength of the TRC issued by the Mauritian authorities.

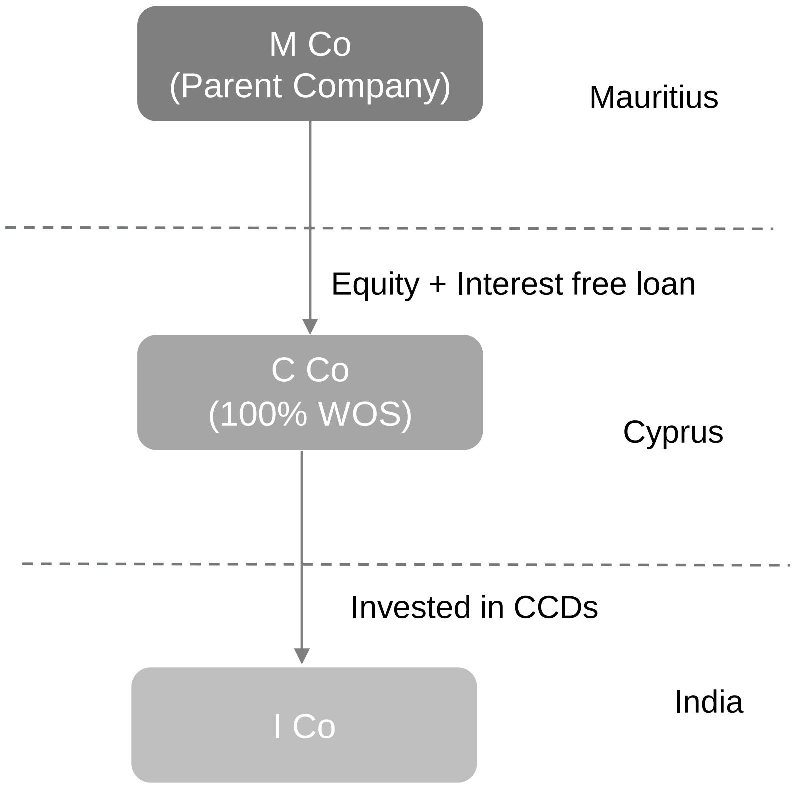
Significance of Factual aspects

Judicial precedents - Others

Golden Bella Holdings Ltd. v. DCIT [2019] 109 taxmann.com 83 (Mum)

Revenue's contentions:

- The investment in CCDs was a mere back-to-back loan transaction. Accordingly, Golden Bella (assessee) was not the 'beneficial owner' of interest income
- The assessee was mere conduit, since it had outsourced its corporate secretariat and management functions to a third party and did not carry any business operations
- It did not exercise dominion and control over the CCDs. Therefore, the interest income is taxable at the applicable rates in force (approx. 42%)
- The DRP confirmed the findings of the AO. It further observed that Circular 789 of 2000 does not apply to Cyprus treaty and, as per judgements, TRC is not conclusive proof of beneficial ownership

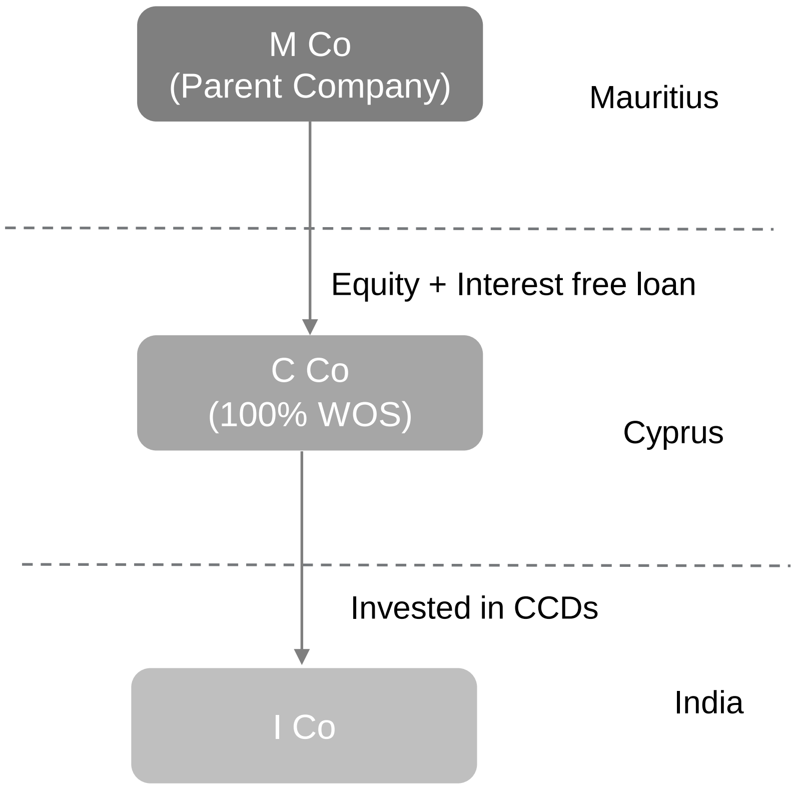


Judicial precedents - Others

Golden Bella Holdings Ltd. v. DCIT [2019] 109 taxmann.com 83 (Mum)

Tribunal's Ruling:

- The assessee invested in CCDs and received interest income thereon for its own exclusive benefit, and not for or on behalf of any other entity.
- Assessee had entire control over funds, assumed forex risk, and the entire interest income was the sole property of the assessee. AO/DRP failed to prove otherwise;
- Mere fact that the investment is funded using a portion of interest-free shareholder loan and share capital does not affect the assessee's status as 'beneficial owner' of interest income
- Tribunal relied on Para 10.2 of the OECD Commentary (2017) on article 11 (Interest) of the OECD Model Tax Convention - " …where the recipient of interest does have the right to use and enjoy the interest unconstrained by a contractual or legal obligation to pass on the payment received to another person, the recipient is the 'beneficial owner' of that interest."



Judicial precedents - Others

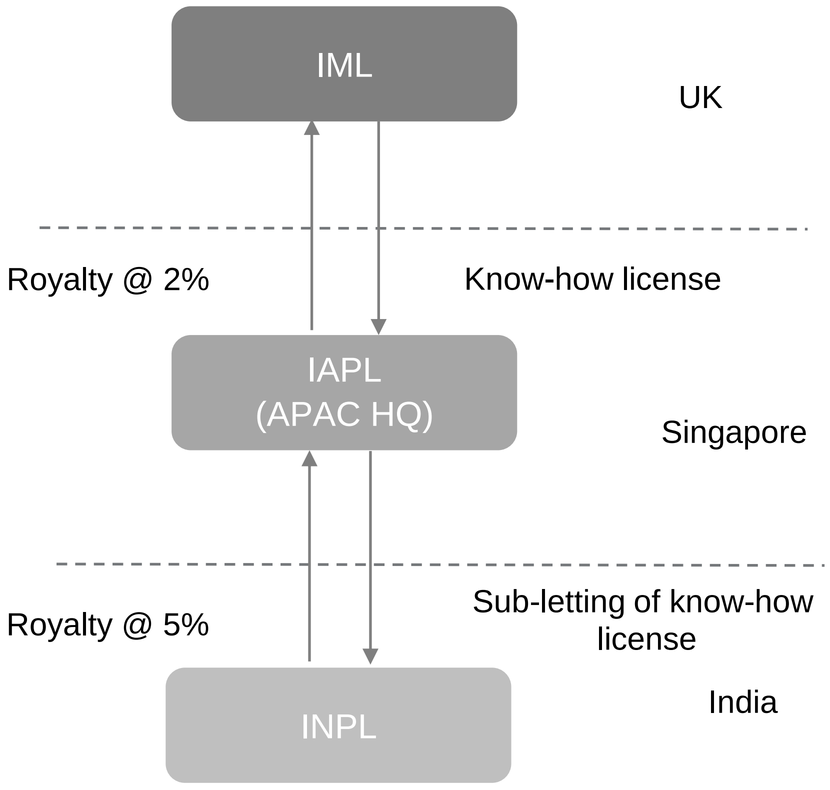
Imerys Asia Pacific (P.) Ltd. v. DDIT [2016] 69 taxmann.com 454 (Pune)

Facts of the case:

- IAPL, a Singapore based company is a 100% subsidiary of IML and has a valid TRC from IRAS;
- IAPL is acting as APAC headquarter, and is an operational entity with sizeable assets, liabilities and turnover. Principal activities include rendering administrative, marketing and sales services to the group and affiliated companies, trading in paper, and other related activities.
- IAPL entered into a Technology License Agreement with INPL against 5% royalty on INPL's net sales. IAPL liable to pay 2% of INPL's net sales as royalties to IML (a UK based group entity and the owner of know-how).

Revenue's contentions:

- The know-how is being provided to INPL by IML, and IAPL (assessee) is acting as mere agent to claim DTAA benefits. Thus, the assessee's claim for lower rate under India-Singapore DTAA is not tenable and the income is taxable at 20% under section 115A of the Act.

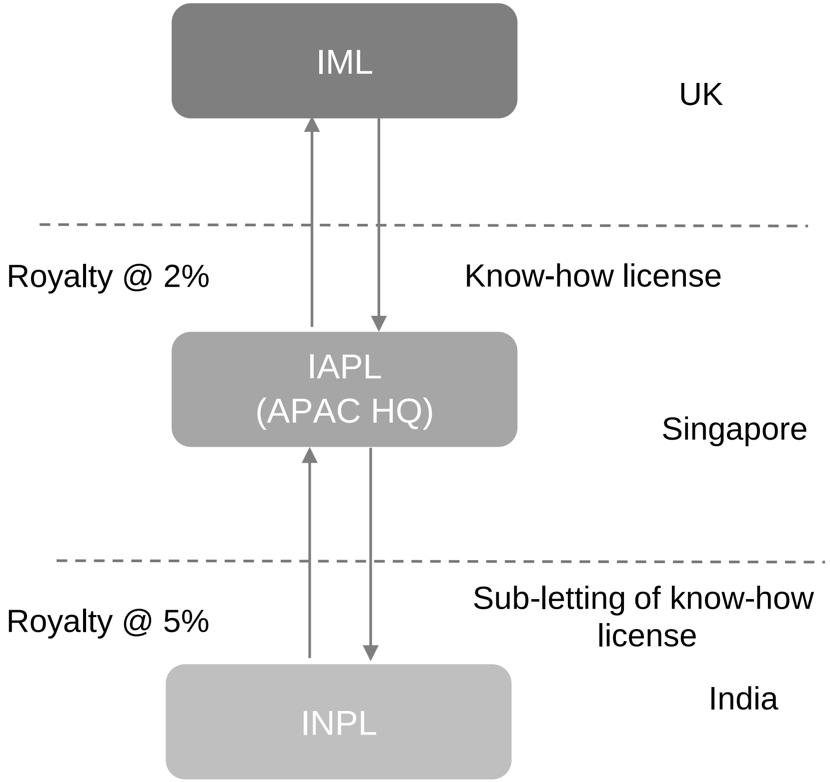


Judicial precedents - Others

Imerys Asia Pacific (P.) Ltd. v. DDIT [2016] 69 taxmann.com 454 (Pune)

Tribunal's Ruling:

- In order to take the benefit of Articles 12 of India-Singapore DTAA, the following conditions need to be satisfied:
- (i) Recipient should be tax resident of Singapore - the assessee has placed a valid TRC on record (ii) Recipient should be the beneficial owner of royalty
- For the second condition above, it is essential that the recipient receives the royalty in its own right. Considering the relevant terms of agreement between INPL and IAPL (along with supporting documents, such as invoices raised, documents submitted with AD Bank for remittance of royalty, extracts of Singapore tax return etc.), the ITAT held that the assessee had entered into an agreement with IML and received the know-how, which in turn was sub-licensed to INPL. Thus, royalty received by the assessee from INPL is on its own right as the beneficial owner.



Impact of BEPS and MLI

Impact of BEPS and MLI

BEPS Action Plan 6 on *'Preventing the granting of treaty benefits in inappropriate circumstances'* was introduced by the OECD/ G20. For implement the Action Plan, the following minimum standards have been proposed for all the signatories to the MLI:

1. **Article 6 (Purpose of CTA)** - an express statement that their common intention is to eliminate double taxation without creating opportunities for non- taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements; and

2. **Article 7 (Prevention of Treaty abuse)** - Having either:
   - Principal Purpose Test ('PPT') alone; or
   - A combination of PPT supplemented by either a simple or detailed Limitation of Benefits clause; and
   - a detailed LOB rule supplemented by a mechanism would deal with conduit financing arrangements not already dealt with in tax treaties.

Impact of BEPS and MLI

- Article 6(1) of MLI provides for modification of the preamble of the CTA (Covered Tax Agreements) as under:

  "A Covered Tax Agreement shall be modified to include the following preamble text: "Intending to eliminate double taxation with respect to the taxes covered by this agreement without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions),"

- Thus, all the transactions will have to be tested through the Preamble

- Article 6(4) of MLI provides that a country can make a reservation on the applicability of Paragraph 1 to any of the treaties if it already contains such a preamble or a broader preamble.

- India has not made any specific reservation on the application of Article 6(1). Thus, the Preamble gets incorporated in all the CTAs.

Impact of BEPS and MLI

- Article 7 of MLI deals with prevention of treaty abuse. It proposes that, as a minimum standard, the signatories, in their treaties should have either:
  - Principal Purpose Test (‘PPT’) alone; or
  - PPT supplemented by either a simple LOB (Limitation of Benefits) or detailed LOB clause; and
  - a detailed LOB rule supplemented by a mechanism would deal with conduit financing arrangements not already dealt with in tax treaties.

India has opted for PPT + SLOB. PPT being minimum standard, it will apply to all its CTAs

- Article 7(1) to 7(5) of MLI lays down the principles of PPT. PPT is a minimum standard and hence mandatory for all CTAs

- Article 7(1) of MLI - a benefit under the CTA shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was ‘one of the principal purposes’ of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the CTA.

- Article 7(4) of MLI - Where the Treaty benefit is denied by invoking PPT, taxpayers can approach the Competent authorities for resolving the issue

- Article 7(6) to 7(14) - Prescribes Simplified LOB rules. Simplified LOB applies only through Symmetrical approach i.e., when both the Contracting jurisdictions notify in their CTAs. Else, the same cannot be read into the treaty.

* Reference can be drawn to OECD 2015 Final Report on BEPS Action Plan 6 - , where the transaction is undertaken for valid commercial reasons but if ‘one of the principal purposes’ is to avail the treaty benefit, the treaty benefit can still be denied. Where the commercial reason and tax benefits are ‘inextricably linked’, and the manner in which the arrangement is implemented is not driven by considerations of obtaining the benefit, the treaty benefit would not be denied

Impact of BEPS and MLI

- **Article 8 (Dividend transfer transactions)** of MLI provides for a minimum holding period of 365 days including the day of declaration of the dividend in order to claim the benefit of concessional rate of tax

- India notified Article 8(1) for several CTAs through Symmetrical approach. India has made a reservation against application of the provisions of this Article in respect of India- Portugal DTAA since India-Portugal DTAA already provides for a higher holding period of 2 years

- **Article 9 (Capital gains from alienation of shares or interest of entities deriving their value principally from immovable property)** of MLI provides for introduction of additional criteria of "365 days minimum holding period" in case of gains arising from alienation of shares or other participation rights if such shares or rights derive more than a specified percentage of their value from immovable property situated in the source jurisdiction Optional provision of inserting a minimum value derivation criterion of 50 percent of their value directly or indirectly from immovable property

- India has opted to apply minimum holding period threshold along with minimum value derivation criterion of 50 percent. The said provision to apply to CTA only if other CTA partner has chosen to apply the said provision

Illustration - Taxability under Act and DTAA (Pre BEPS and MLI)

India - US (Dividend)

- Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.
- However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the laws of that State, <u>but if the beneficial owner of the dividends is a resident of the other Contracting State</u>, the tax so charged shall not exceed 15 per cent of the gross amount of the dividends if the beneficial owner is a company which owns at least 10 per cent of the voting stock of the company paying the dividends

The 365 days condition (Article 8 of MLI) is not applicable since neither India nor Netherlands explicitly opted to amend their CTAs.

India - NL (Dividend)

- Dividends paid by a company which is a resident of one of the States to a resident of the other State may be taxed in that other State.
- However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, <u>but if the recipient is the beneficial owner of the dividends</u>, the tax so charged shall not exceed 10 per cent of the gross amount of the dividends.

India - Mauritius (Interest)

- Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
- However, subject to provisions of paragraphs 3, 3A and 4 of this Article, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, <u>but if the beneficial owner of the interest is a resident of the other Contracting State</u>, the tax so charged shall not exceed 7.5 per cent of the gross amount of the interest

Mauritius has not chosen India as a CTA. Thus, India-Mauritius DTAA would not undergo any change

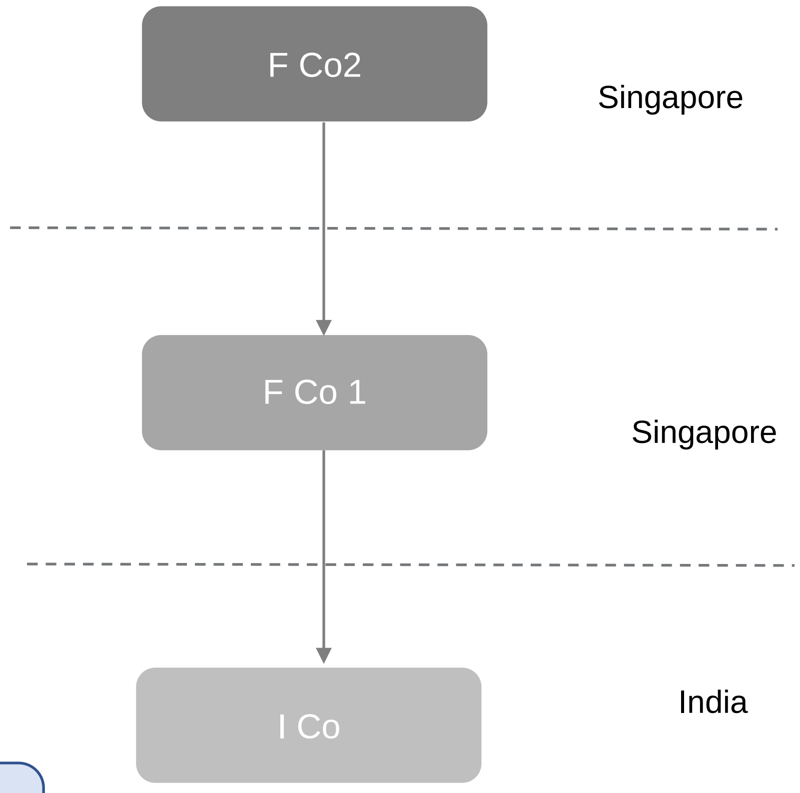
‘What if’ the Beneficial owner concept is not satisfied

Beneficial Owner - Not satisfied

Scenario 1 - Benefit of treaty where the recipient and beneficial owner are distinct entity though resident of same treaty jurisdiction

- Para 2 of Article 12 of India-Singapore DTAA: However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, *but if the beneficial owner of the interest is a resident of the other Contracting State*, the tax so charged shall not exceed:

- Para 2 of Article 11 of India-Mauritius DTAA: However, subject to provisions of paragraphs 3, 3A and 4 of this Article, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 7.5 per cent of the gross amount of the interest

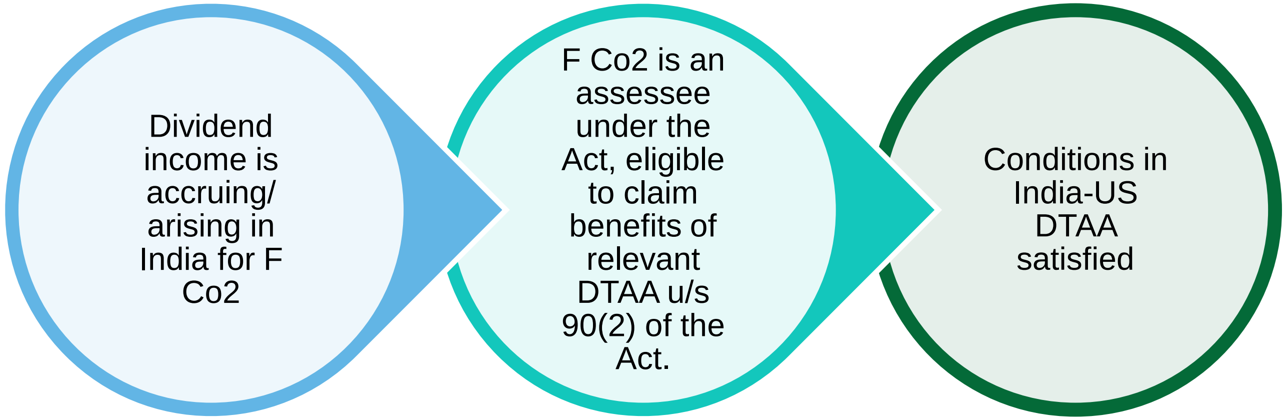


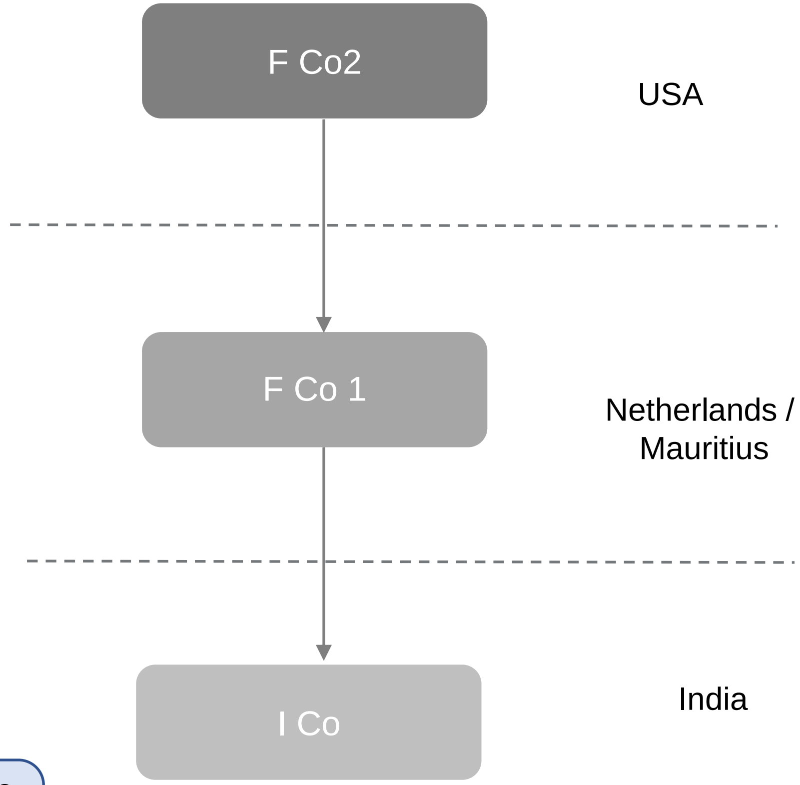
since both the recipient and beneficial owner of interest are resident of Singapore, reduced tax rate of interest under the Singapore DTAA may be availed. Similar wordings present in India- Mauritius DTAA also

Beneficial Owner - Not satisfied

Scenario 2 - Availing benefit of treaty with third state of which the beneficial owner is resident

- Where F Co1 is not considered as beneficial owner of dividend, the tax authorities could seek to apply withholding tax rate as per the Act i.e. 20% (plus applicable surcharge and cess)
- The question that needs to be answered is whether F Co2 can be regarded as the beneficial owner and whether the DTAA between India and USA can be applied?
- In order to apply India-US DTAA, the following conditions need to be satisfied:





Substance should preside over form. This argument is based on interpretation of Article 10 in the OECD commentary and is yet to be tested in India. However, Indian courts have held that corporate veil can be lifted/the beneficial owner can be taxed in India for capital gains.

Concept of Beneficial Ownership in Article 13 (Capital gains) ?

Concept of Beneficial owner in case of Capital Gains

- As such, there is no specific requirement to satisfy the condition of 'beneficial ownership' under Article 13 of Capital Gains.

- UN Model convention acknowledges the absence of BO condition in Capital gains article but also states that its impact is not materially different as capital gains is earned by alienator of the capital asset and such alienator needs to be the owner in his own right before the income can be assessed in his hands.

- Article 13(5) of Israel-Singapore DTAA specifically includes the test of beneficial owner in Capital gains article

  "5. Gains derived by a resident of a Contracting State from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4, shall be taxable only in the Contracting State of which the alienator is a resident, <u>if that resident is the beneficial owner of the property from which the capital gains are derived</u>."

Judicial precedents

#	Case law/ Citation	Court	Summary
1	Sanofi Pasteur Holding SA	Hon’ble Andhra Pradesh High Court	The tax department failed to establish that the genesis and continuance of ShanH establishes as an entity of no commercial substance and/or that ShanH was interposed only as a tax avoidant device. Thus, no case was made out for piercing or lifting the corporate veil of ShanH.
2	Vodafone International Holdings B.V.	Hon’ble Supreme Court of India	Thus, whether a transaction is used principally as a colourable device for the distribution of earnings, profits and gains, is determined by a review of all the facts and circumstances surrounding the transaction. It is in the above cases that the principle of lifting the corporate veil or the doctrine of substance over form or the concept of beneficial ownership or the concept of alter ego arises.
3	Bid Services Division (Mauritius) Ltd.	Hon’ble Bombay High Court	Upheld the capital gains exemption for investments made before 01 April 2017 and held that LOB conditions cannot be applied for such investments.
4	Tiger Global	Hon’ble Delhi High Court	Upheld the capital gains exemption for investments made before 01 April 2017 and held that LOB conditions cannot be applied for such investments. a TRC should be considered conclusive proof of an entity’s bona fide status and that piercing the corporate veil is justified only in cases of tax fraud or sham transactions.

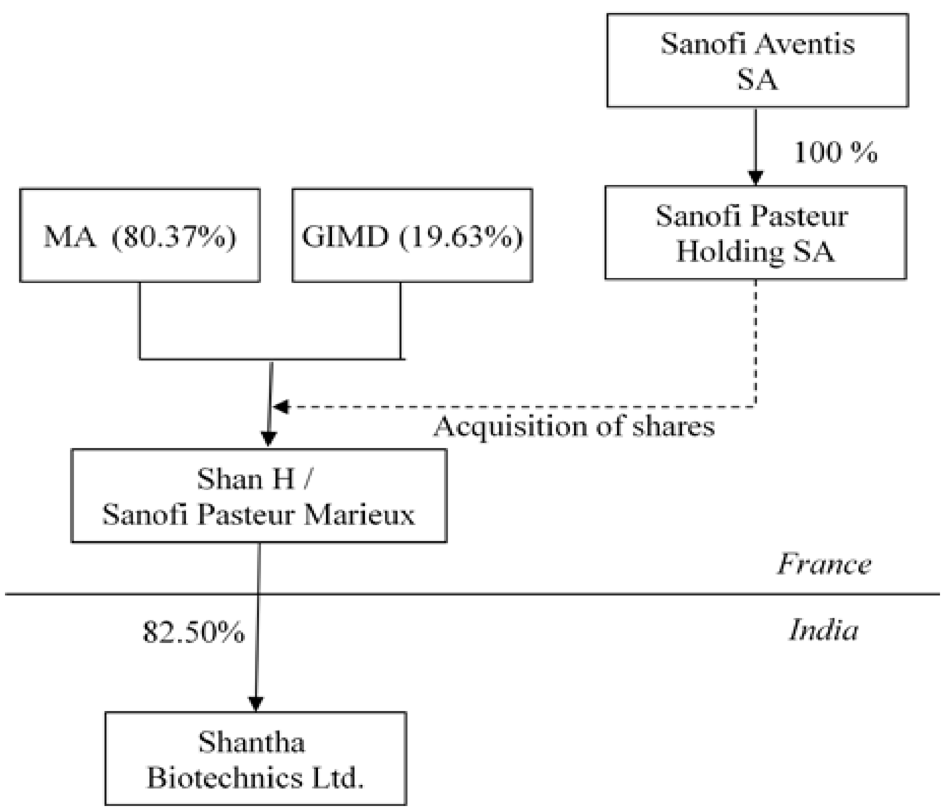
Beneficial Ownership - Capital gains

Sanofi Pasteur Holding SA vs. Dept of Revenue [2013] 30 taxmann.com 222 (AP)

Facts of the Case:

- During the year 2009, Sanofi France purchased 80.37% of ShanH from Merieux Alliance (MA), a French company, and balance 19.63% from Groupe Industriel Marcel Dassault (GIMD), another French company.
- ShanH held 82.5% of the share capital of SBL.
- The tax department passed an order on Sanofi dated 25 May 2010 under Section 201(1)/(1A) of the Act holding Sanofi as an 'assessee-in-default' for not withholding taxes on payments made to MA and GIMD on acquisition of shares of ShanH
- MA and GIMD made an application to the Authority for Advance Ruling (the AAR) on the taxability of the transaction. The AAR in November 2011 ruled that the capital gain arising from the sale of shares of ShanH by MA and GIMD was taxable in India in terms of Article 14(5) of the tax treaty.
- Subsequently, both the parties i.e. the Buyer (Sanofi) and Sellers (MA and GIMD) filed writ petitions before the Andhra Pradesh High Court (High Court).

Transaction flow



Beneficial Ownership - Capital gains

Sanofi Pasteur Holding SA vs. Dept of Revenue [2013] 30 taxmann.com 222 (AP)

Contentions of Revenue:

- ShanH is not a company with an independent status and is only an alter ego of MA and GIMD. ShanH had no control over SBL management nor enjoyed any rights and privileges in SBL as a shareholder.
- For a proper and purposeful construction of tax treaty provisions, the expression 'alienation of shares' in tax treaty must be understood as direct as well as indirect alienation. Thus, no conflict between the provisions of the Act pursuant to the retrospective amendments carried out by the Finance Act, 2012 and Article 14(5).
- The retrospective amendments to Section 2(47) of the Act (By the Finance Act, 2012) clarifies that 'transfer' would mean and would deem to have always meant the disposal of an asset whether directly or indirectly or voluntarily or involuntarily.

Ruling of High Court:

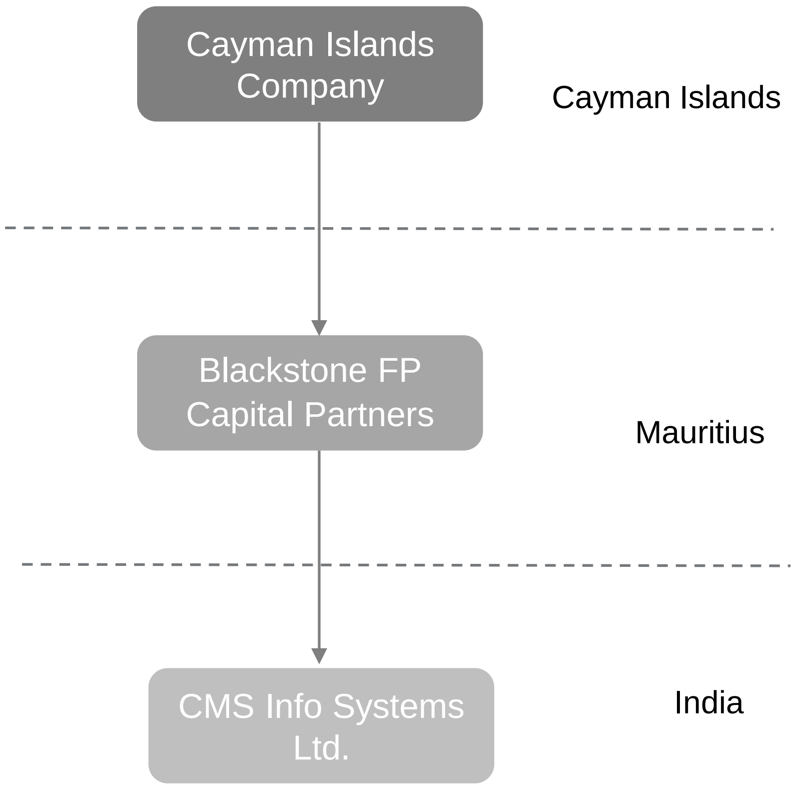
- Since the tax department failed to establish that the genesis and continuance of ShanH establishes as an entity of no commercial substance and/or that ShanH was interposed only as a tax avoidant device, no case was made out for piercing or lifting the corporate veil of ShanH.
- De hors the conclusion that there was no case piercing the corporate veil of ShanH, the transaction in issue was clearly one of transfer by MA and GIMD of their shareholding in ShanH to Sanofi and it was not a case of transfer of shareholding in SBL, which continues with ShanH.
- The transaction was for alienation of shares of ShanH held by MA and GIMD in favour of Sanofi and falls within Article 14(5) of the tax treaty. The transaction neither constitutes the transfer nor deemed transfer of shares or of the control/management or underlying assets of SBL.
- The retrospective amendments do not alter the provisions of the tax treaty and given the text of Section 90(2) of the Act, these amendments do not alter the taxability of the present transaction.

Beneficial Ownership - Capital gains

Blackstone FP Capital Partners Mauritius V Ltd. vs. DCIT [ITA Nos. 981 and 1725/Mum/2021 (Mumbai ITAT)]

Facts of the Case:

- The assessee held a global business licence (GBL) with a valid TRC, and is also registered as a foreign venture capital investor (FVCI) with SEBI.
- During the relevant previous year, the assessee sold 8.32 crore equity shares of CMS Info Systems Ltd. and earned Rs. 904.98 crores which was in the nature of long-term capital gains.
- Dispute arose with respect to treaty protection, in terms of Indo Mauritius tax treaty, in respect of the said long-term capital gains.
- The AO concluded that the assessee company has no independent existence, and that its entire activity was controlled and directed as per the directions of its affiliates. The entire scheme of purchase and sale of shares was designed for the benefit of the entities in Cayman Islands and that it was a fit case to lift the corporate veil.
- It was thus held that the beneficial owner of the shares is not the assessee, and the benefit of article 13(4) of Indo Mauritius tax treaty will not be admissible.



Beneficial Ownership - Capital gains

Blackstone FP Capital Partners Mauritius V Ltd. vs. DCIT [ITA Nos. 981 and 1725/Mum/2021 (Mumbai ITAT)]

Tribunal Ruling:

- The Hon'ble Tribunal passed an interim order to hold that the AO incorrectly proceeded on the assumption that the principle of beneficial ownership can be read into the Indo-Mauritius DTAA, when the treaty does not provide for the same explicitly. The Tribunal further that reading the principle of 'beneficial ownership' into Article 13 would amount to re-writing the tax treaty itself.

- However, instead of concluding the matter, the Hon'ble Tribunal remitted the matter back to the AO, directing him to find out whether the beneficial ownership test can be applied to the Indo-Mauritius DTAA.

- The Taxpayer filed a miscellaneous application seeking rectification of the Hon'ble Tribunal order on the ground that the Tribunal cannot remand the matter back to lower authorities on a question of law, when all the facts and evidences pertaining to the matter have already been provided.

- The Hon'ble ITAT while adjudicating the miscellaneous application acknowledged that there was indeed a 'mistake apparent on record', which was remitting the matter back to the AO on a question of law and accordingly allowed the miscellaneous application and posted the case to be heard afresh on the issue of Beneficial owner before a regular bench.

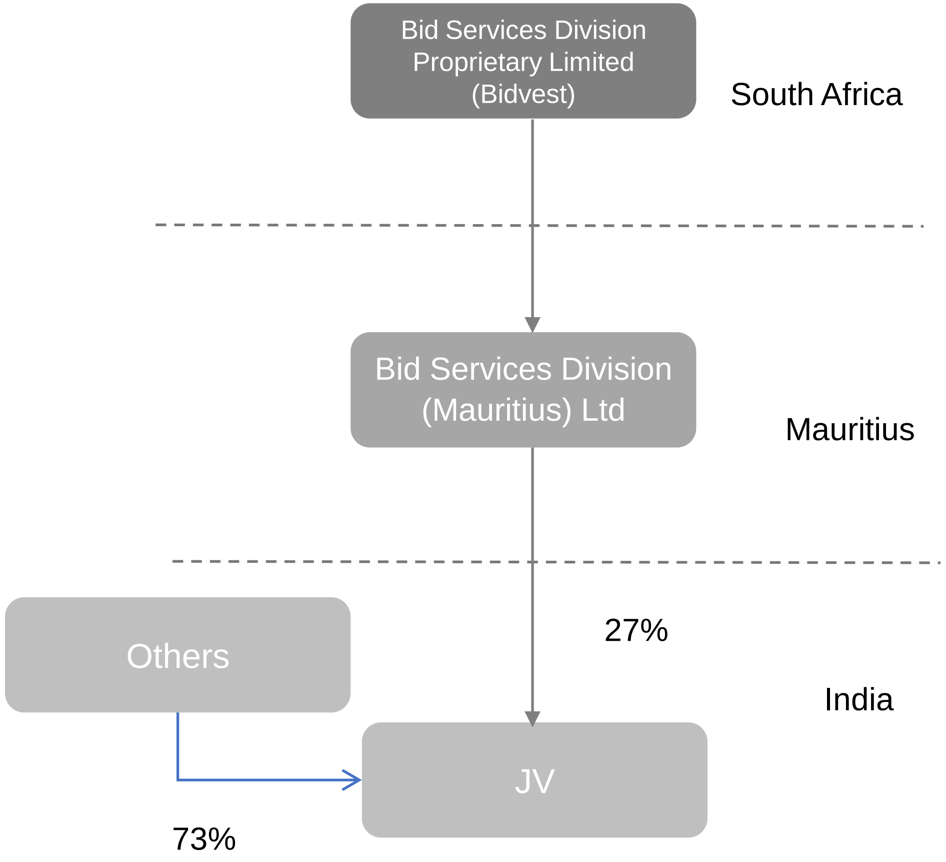
Blackstone - MA Order

Beneficial Ownership - Capital gains

Bid Services Division (Mauritius) Ltd. [148 taxmann.com 215 (Bombay HC)]

Facts of the Case:

- The Assessee was a non-resident company incorporated under the laws of Republic of Mauritius having a valid TRC issued by the Mauritian Authorities. The ultimate parent entity of the Assessee was Bid Services Division Proprietary Limited (Bidvest) incorporated in South Africa.
- The Assessee, having a valid TRC from the Mauritius authorities, was a part of consortium that filed the expression of interest and successfully obtained the bid for operation, management and development of the Mumbai airport.
- The Assessee which held a 27% share in the JV established to carry out the project sold 13.5% shares to other party of the consortium in FY 2011-12. The Assessee received a Nil withholding certificate from the Indian tax authorities u/s 197 of the Act.
- Post the transaction, the Assessee filed an application before the AAR for ascertaining certainty on the taxability of capital gains under India-Mauritius DTAA.



Beneficial Ownership - Capital gains

Bid Services Division (Mauritius) Ltd. [148 taxmann.com 215 (Bombay HC)]

Facts of the Case:

- AAR passed an adverse order holding that the purpose of interposing the Assessee in the JV was to avoid taxes and the Assessee was only a shell company not having any tangible assets, employees, office space, etc. and was incorporated only two weeks before the bidding process, thereby lifted the corporate veil.

- The Assessee filed a writ petition before the Hon'ble Bombay High Court and relied upon the following:
  - Circular No.789 dated 13th April 2000 issued by the CBDT.
  - The investments made before 01 April 2017 were grandfathered, and the provisions of Article 27A of the DTAA which deals with LOB were inserted w.e.f 1st July 2017 whereas the sale transaction pertains to the FY 2011-12.

HC Ruling:

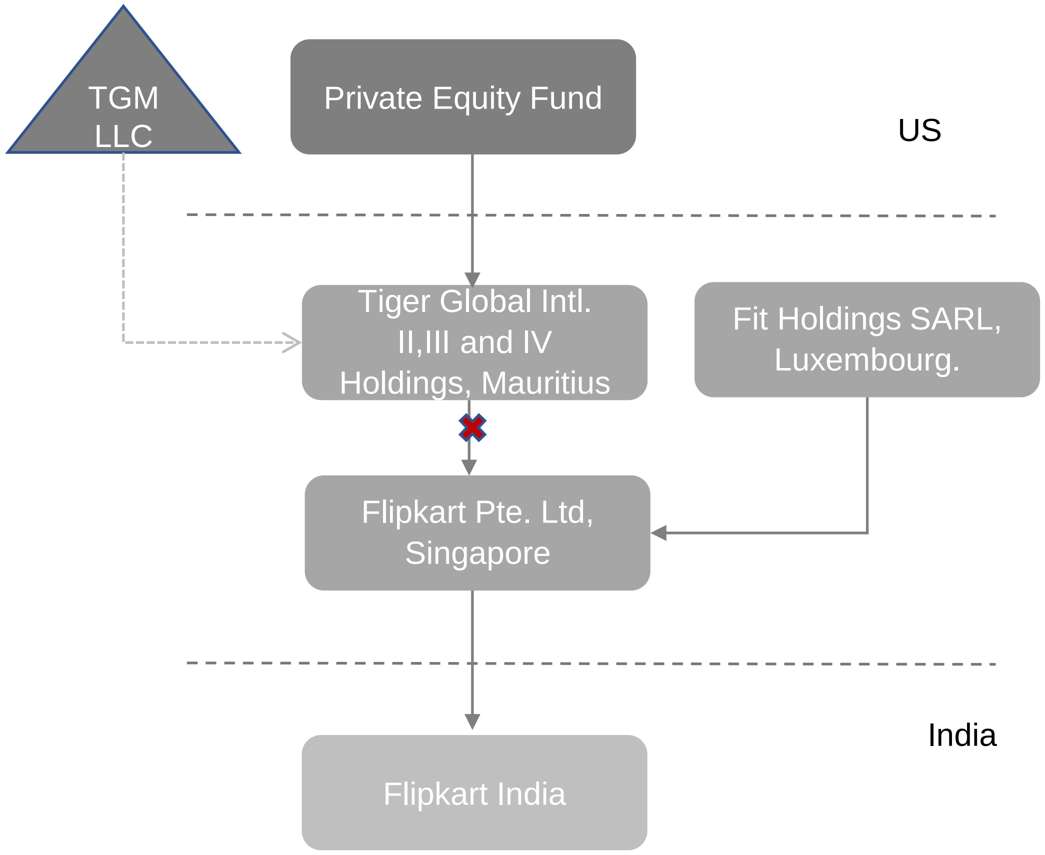
- The Assessee holds a valid TRC which is sufficient proof of its residence in Mauritius and cannot be enquired into, unless there is a fraud or illegal activity, which in this case, has neither been alleged nor demonstrated. Reliance was placed on the Apex Court rulings in the case of Vodafone International Holding B.V. & Azadi Bachao Andolan. Also, upheld that LOB is applicable only for investments from 01 April 2017 and accordingly remanded the matter back for fresh consideration.

Beneficial Ownership - Capital gains

Tiger Global International Holdings II [Hon'ble Delhi HC]

Facts of the Case:

- The assessee was a company incorporated in, and fiscally domiciled in, the Republic of Mauritius It holds a category 1 global business licence (GBL) issued by the Financial Services Commission, Mauritius.
- Assessee was established primarily for investment activities to be conducted on behalf of Tiger Global Management LLC ('TGM LLC'), a company based in Delaware, United States. TGM LLC is the Assessee's investment manager.
- The Assessee is owned by a private equity fund that has approximately 500 investors across 30 sovereign jurisdictions.
- The Assessee acquired the shares of Flipkart Singapore between 2011 to 2015 and subsequently transferred shares to Fit Holdings SARL, a Luxembourg entity.



Beneficial Ownership - Capital gains

Tiger Global International Holdings II [Hon’ble Delhi HC]

Rulings of AAR:

- Upon approaching the AAR and relied upon Article 13(3A) and Circular 789. Also, contended that LOB conditions would not apply for investments made prior to 01 April 2017.
- The AAR ruled that the organizational structure of the Tiger Global Group demonstrated that the Assessee is a mere intermediary in a tax-avoidance scheme. It held that the actual control and management of the Assesse are with TGM LLC, which was situated in the United States and not in Mauritius.

High Court Ruling:

- Assessee submitted that it was independently managed by a board of directors based in Mauritius. It submitted that TGM LLC is merely an entity engaged by the Assessee to provide investment related services and it had no right to bind the Assessee or take any decisions on behalf of Assessee, without the approval of its own board of directors.
- Assessee relied upon Azadi Bachao Andolan to substantiate that DTAA benefits must be granted based on treaty terms, irrespective of the motives behind Mauritius-based entities. Department relied upon Vodafone case to state that the corporate veil could be pierced when the holding structure of an entity has no commercial or business substance and has only been interposed to avoid tax.
- The Delhi HC held that TGM LLC served only as an investment manager and could not be considered the parent or holding company. It also observed that the Assessee, a Mauritius entity was a fairly significant entity with considerable economic activity, having been set up as pooling vehicles for investments. The Assessees’ board of directors, despite the presence of board members connected with the Tiger Global Group, exercised genuine decision-making authority, and made decisions collectively.

Beneficial Ownership - Capital gains

Tiger Global International Holdings II [Hon’ble Delhi HC]

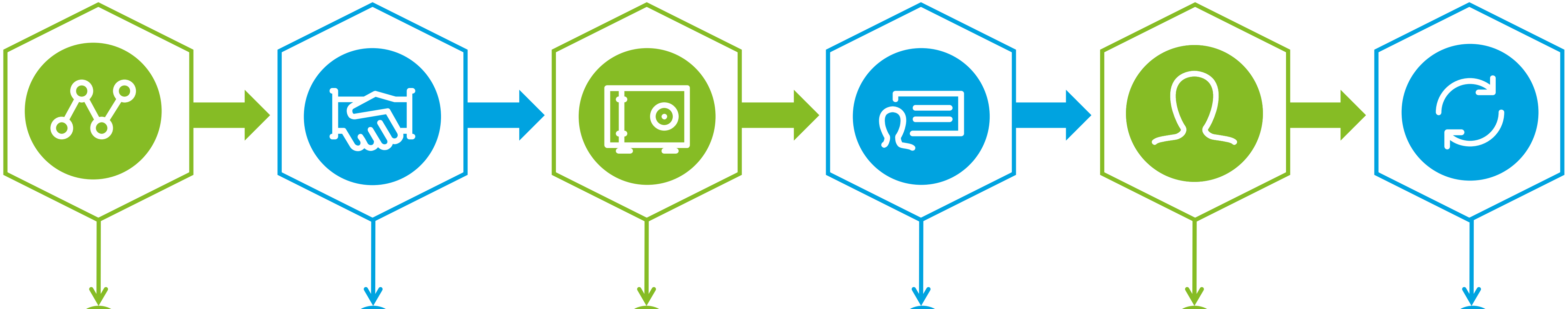
High Court Ruling:

- Regarding beneficial ownership, the Court relied on its factual finding that TGM LLC was not the Assessee’s parent company and no evidence suggested that the Assessee was obligated to transfer the revenue to TGM LLC or that the transactions were carried out at their behest.
- The Court further held that the issuance of a TRC should be considered conclusive proof of an entity’s bona fide status and that piercing the corporate veil is justified only in cases of tax fraud or sham transactions. However, these must be supported by compelling evidence, and it is the onus of the revenue authorities to establish the same.

Refer Para 26, 27 and 28 of the OECD Model Commentary to Article 1 for a better understanding of when a Collective Investment Vehicle (CIV) can be construed as a ‘Resident’ and a ‘Beneficial owner’ of Income

Way forward

Beneficial Owner - Checklist (Illustrative)



1. Provide TRC and information in Form 10F.
2. Prove commercial and business expediency (If incorporated in tax favorable jurisdiction)
3. Recipient enjoys the fruits of the ownership and has the ability to dispose of it for his own benefit (i.e., not as a mere agent or nominee working on behalf of the parent company under parent company’s instruction)
4. Recipient should have discretion to use the income (exclusive possession and control over the income received)
5. The risk associated with such income must be borne by the company.
6. No contractual obligation to pass on the income to the third party.

Q&A

Thank You

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