

SATURDAY INTERNATIONAL TAX GYAN !!!

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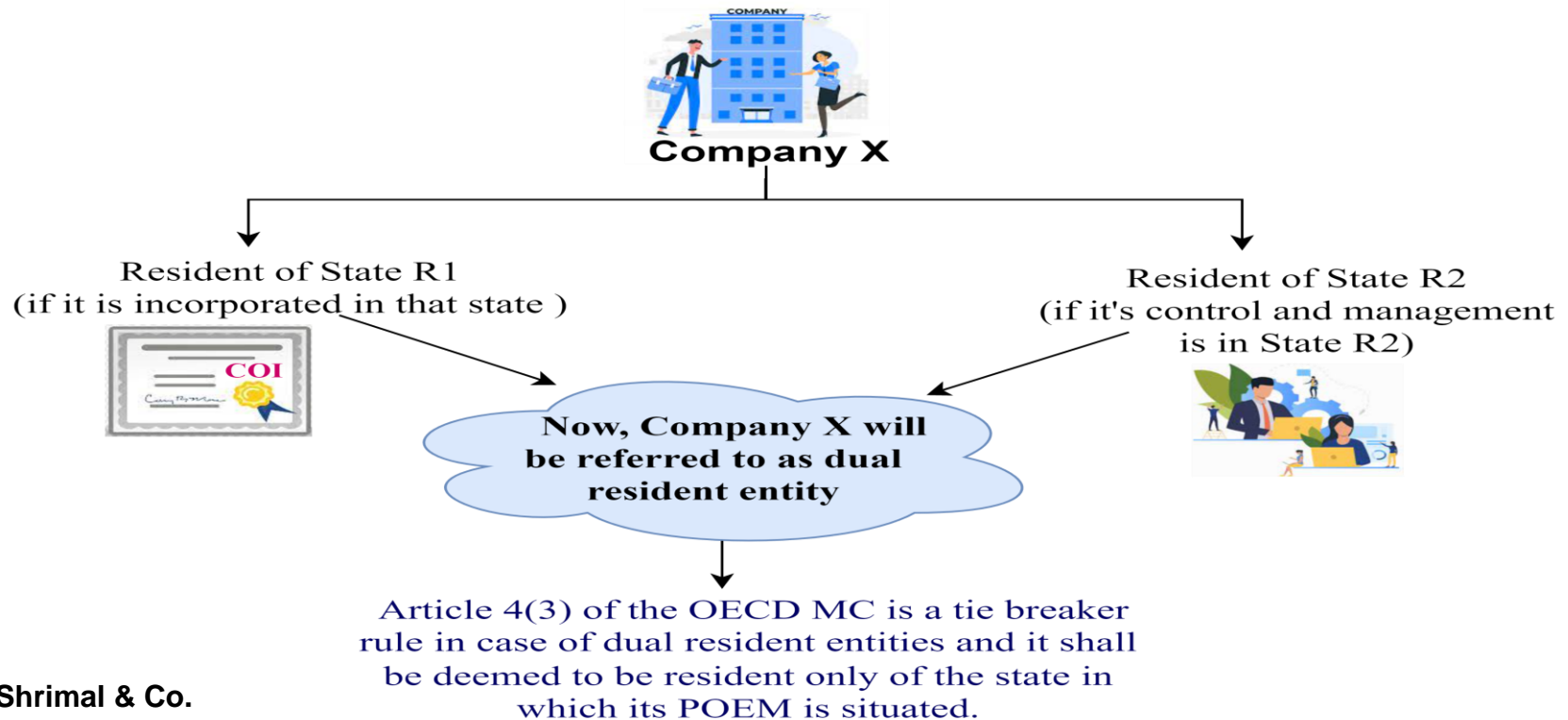
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ARTICLE - 4 DUAL RESIDENCY OF ENTITIES

BACKGROUND

- ❖ As per Article 4(1) of the OECD MC, the treaty residence of a person is dependent on the domestic tax laws of each contracting state.
- ❖ This may result in a person being resident of both states because of residency rules of two countries however **this article is not applicable to individuals.**



POEM as tie-breaker rule before MLI

- ❖ OECD has earlier recommended POEM as a tie-breaker rule for determining residency. An alternative for the same is to let the competent authorities determine the residency of **dual resident entities** by mutual agreement on a case to case basis.



Jethalal!!
Those were the days when tie breaker rule for determining residency of dual resident entities was POEM then why OECD has changed it to mutual agreement of competent authorities?



Sikshak Mahodaya,
there were some inherent limitations of POEM because of which OECD has changed the tie breaker rule.

So let's understand the inherent limitations of POEM as a tie breaker rule...!!

Inherent Limitations of POEM

1. It cannot effectively curb tax avoidance due to entities showing low tax jurisdiction as their Place of Effective Management (POEM).

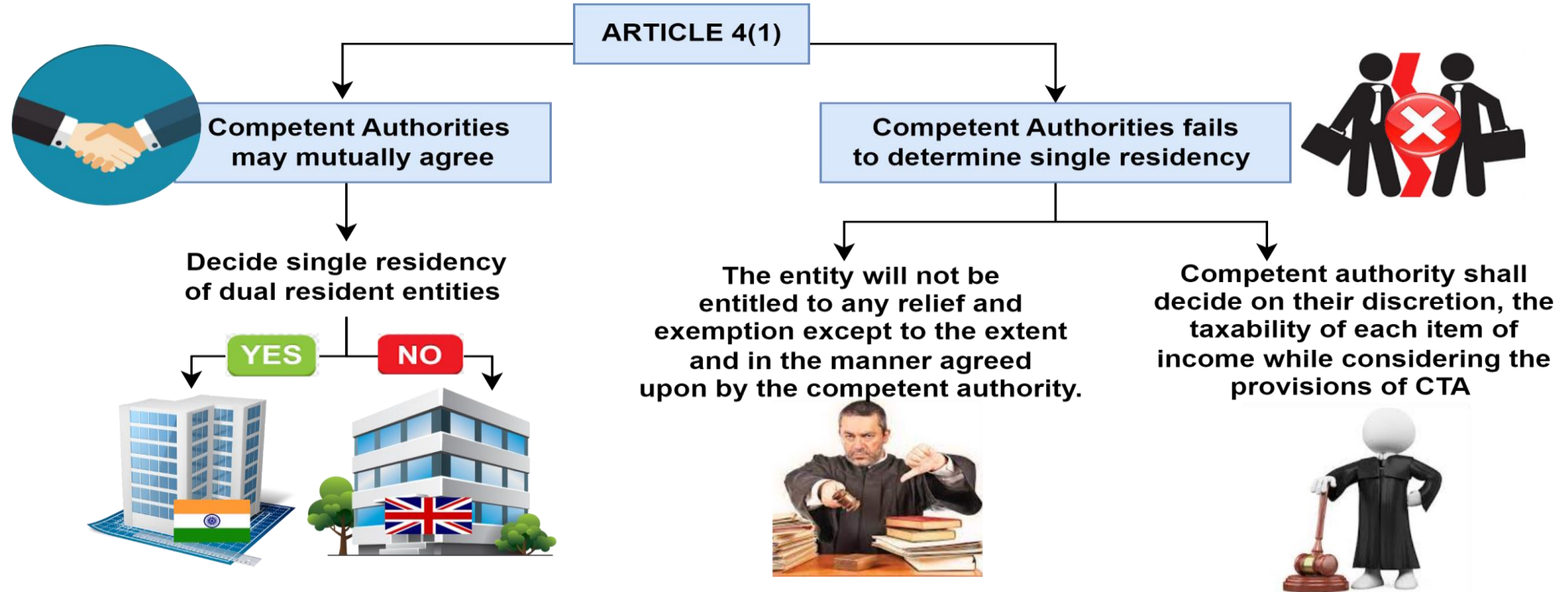
2. However, the term POEM has not been defined in the OECD MC and countries may have different criteria for determining POEM as per their domestic laws. There are few countries which may not have a POEM concept in their domestic laws.

Accordingly, there is **no uniformity or clarity** under the current tie-breaker test for determining the POEM of an entity.

3. There may also be a situation where the POEM of a dual resident entity may be in a third state and accordingly the POEM test as a tie-breaker rule will fail to reserve the dual residency.

Article 4(1)

Main Provision – determining treaty residence of dual residence entities



NOTE: Now POEM will not be the sole criteria for determining the single residency of dual resident entities, this could also be decided by considering other factors as discussed above by mutual agreement of competent authorities.

Article 4 (2), (3) and (4)

Summary

Article 4(2): Paragraph 1 shall apply in place of or in absence of provisions of CTA. The provisions of Article 4 of MLI would replace all tie-breaker rules with respect to residence of person other than individuals.

Article 4(3): Paragraph 3 provides for reservation clause to either opt of this article in entirety or to apply it with certain modifications.
Example : Countries such as Singapore and France has opted out of this article in entirety.

Article 4(4): Para 4 prescribes notification clause to notify the depository about the provisions of its tax treaties where a similar provision in Article 4(1) is already present where the country has not made any reservation. However, this provision is not applicable in case the country has made reservation.

India's Position

- ❖ India, in its notification, has not made any reservation with respect to Article 4 of the MLI
- ❖ Therefore, where India's treaty partner has made a reservation on Article 4, then the same will not apply with respect to the tax treaty between India and such treaty partner.
- ❖ Modifications can be done in reservation clause as shown in below mentioned table:

<p>Countries which have reserved rights in entirety hence, the existing tie-breaker test in India's tax treaties with these countries does not get altered and the POEM test continues to apply. For Example: Singapore, France, Sweden, Germany, Austria, Mauritius, Canada.</p>	<p>UK, Netherlands, Ireland, Slovenia have opted to apply Article 4 to its CTAs and have notified India in their respective CTAs. Accordingly, the tie-breaker rule in these tax treaties will be replaced by the text of paragraph 1 of Article of the MLI</p>	<p>Australia and Japan have reserved their right to modify the language of paragraph 1 of Article 4 in accordance with Article 4(3)(e) i.e., in absence of agreement between the competent authorities with respect to single residency, no benefits under the covered tax agreement will be granted.</p>
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Documents can be referred for Interpretation of MLI

Basic Documents:

- BEPS Action Plan 15
- Explanatory Statement to MLI
- MLI Positions adopted and deposited by Various MLI signatories with OECD
- Report on BEPS Action Plan 2,6,7,14
- Existing tax treaty
- OECD Model Convention of Tax treaty and OECD Commentaries
- Synthesized text of MLI between parties to CTA

Other Documents available on OECD website:

- List of Signatories and parties to MLI
- Frequently Asked Questions (FAQs) on MLI
- Flow chart on matching of reservations and notifications of MLI
- Legal note on functioning on MLI under public international law
- Step by step on applying the MLI
- MLI Matching Database

Link of OECD Website: <https://www.oecd.org/>

Reference of Previous SITG of MLI for beginners Series

S.NO	Particulars	Link
1.	Basic (BEPS)	<u>Click here</u>
2.	Introduction to MLI	<u>Click Here</u>
3.	Structure and Framework of MLI	<u>Click here</u>
4.	India's position on MLI	<u>Click Here</u>

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