Indirect Transfers 2.0 – Study on Taxability of Gain on Alienation of Shares

- Contributed by Suresh Babu and Sri Harsha

Opening Remarks:

The acquisition of Flipkart by Walmart has attained considerable attention of media. The deal is to the tune US $ 16 Billion, making Flipkart as most valuable e-commerce marketplace in India. Now that the deal is done, the tax considerations/issues surface, one-after the other, the first being the issue of indirect transfers, which recently came up for consideration in the matter of Tiger Global. In this article, we shall deal with the recent judgment of Authority for Advance Rulings (for brevity 'AAR') in the matter of Tiger Global International II Holdings[1]. After setting out the ruling, taking this as a case study, we shall adventure to list out the favourable and adverse tax positions, position after MLI[2] and GAAR[3].

The Facts:

The facts of the subject matter is Tiger Global International II Holdings, Tiger Global International III Holdings and Tiger Global International IV Holdings ('Tiger Global Holdings') are private limited companies incorporated in Mauritius. The companies were set up with a primary objective of undertaking investment activities with the intention of earning long term capital appreciation and investment income. The said companies are regulated by Financial Services Commission in Mauritius and have been granted a Category 1 Global License under the provisions of Financial Services Act, 2007 and are tax residents of Mauritius under the laws of Mauritius and qua the provisions of Double Taxation Avoidance Arrangement (DTAA) between India and Mauritius (Indo-Mauritius DTAA/ I-M DTAA).

Tiger Global Holdings collectively hold shares in Flipkart Private Limited, a private company limited by shares incorporated under the laws of Singapore (Flipkart Singapore). Tiger Global International II Mauritius holds 2,36,70,710 shares, Tiger Global International III Mauritius holds 22,82,825 shares and Tiger Global International IV Mauritius holds 1,05,928 shares in Flipkart Singapore which are acquired at various points in time. Flipkart Singapore holds shares in various Indian entities. The value of Flipkart Singapore is essentially derived from the value of various Indian entities in which it holds shares.

As part of the boarder transaction of Walmart acquiring Flipkart, Tiger Global Holdings have sold the shares in Flipkart Singapore to Fit Holdings S.A.R.L, a company incorporated under the laws of Luxembourg. The gross consideration received by Tiger Global Holdings for the said transfer amounts to US $ 2.08 bn (INR 14,440 Crores).

Tiger Global Holdings had approached the Indian Tax Authorities under Section 197 of the Income Tax Act, 1961 (IT Act) seeking a certification of 'Nil' withholding prior to the consummation of the transfer. The tax authorities had informed that the Tiger Global Holdings were not eligible to avail benefit under I-M DTAA as they are not independent in their decision making and the control over decision making of purchase and sale of shares did not lie with them. The Tax Authorities passed an order under Section

[1] 2020 (6) TMI 159 – Authority for Advance Rulings, New Delhi
[2] Convention on Multilateral Instruments
[3] General Anti-Avoidance Rules

197 prescribe a withholding rate in respect of sale of shares by Tiger Global Holdings to Fit Holdings S.A.R.L.

The Question:

Post such an order under Section 197 by the Tax Authorities, Tiger Global Holdings has approached the AAR on the question, whether, on the facts and in the circumstances of case, gains arising to Tiger Global Holdings, a company incorporated in Mauritius from the sale of shares held in Flipkart Singapore to Fit Holdings S.A.R.L would be chargeable to tax in India under IT Act read with I-M DTAA?

The Ruling:

The Revenue/Tax Authorities has raised objection for the allowing the application before the AAR invoking proviso to Section 245R(2). The proviso states that the AAR shall not allow the application where the question raised in application:

- Is already pending before any Income Tax Authority or Appellate Tribunal or any Court
- Involves determination of fair market value of any property
- Relates to a transaction or issue which is designed *prima facie* for the avoidance of tax

Is already pending before any Income Tax Authority or Appellate Tribunal or any Court:

The Revenue/Tax Authorities have argued that since the matter is pending with Income Tax Authority, the AAR cannot allow the application. The AAR after placing reliance on the decision of Honourable Supreme Court in the matter of Asagarali Nazarali Singaporawalla[4] stated that a legal proceeding is pending as soon as commenced and until it is concluded. Since, the application under Section 197 is disposed, the proceedings shall be taken as concluding and accordingly, the matter is held not pending with the authority as so to fall under the ambit of disqualifications which is provided in Section 245R(2). Accordingly, AAR has stated that there is no matter which is pending to make the application unheard.

Involves determination of fair market value of any property

The Revenue/Tax Authorities have next argued that since the issue involves arriving the fair market value of shares of Flipkart Singapore is involved, the application cannot be allowed for admission. Tiger Global Holdings argued that the question involved in not qua the value on which tax has to be paid but whether tax has to be paid or not, which does not require determination of fair market value of shares and accordingly pleaded that the application can be allowed. The AAR has relied on the judgement of Mumbai AAR in Worldwide Wickets[5] and held that computation of capital gains is embedded in the concept of valuation of shares and merely for this reason the question of capital gains arising in application cannot be barred. Since the question raised by Tiger Global Holdings is on the aspect, whether gain arises in the first place or not and such an exercise does not involve determination of fair market value, the application on this ground cannot be disallowed.

[4] AIR 1957 SC 503
[5] 303 CTR 107 (AAR)

<u>Relates to a transaction or issue which is designed *prima facie* for the avoidance of tax</u>

The major issue before the AAR and for this write-up is whether the application is barred for admission on the ground that the subject transaction is designed prima facie for the avoidance of tax. The Revenue argued mainly on four grounds to demonstrate that the transaction is designed prima facie for avoidance of tax and cannot be allowed. The four board grounds that Revenue took are on the aspects of ***Ownership Structure and Control***, ***Decision Making***, ***Financial Control*** and ***Beneficial Ownership***. Now, let us proceed to examine the key arguments made by Revenue and counter arguments made by Tiger Global Holdings on said aspects.

Issue	Revenue's Submissions	Tiger Global Holding's Submissions
On Ownership Structure and Control	• The Revenue stated that all companies were set up in Mauritius ostensibly for making investment into India and other markets. The said companies were not acting independently but only as conduit for the real beneficial owners based out of USA. • Notes to Financial Statements for year ending 31.12.11 states that the companies were held by Tiger Global Management LLC, USA (TGM USA) based investment that invests in public and private markets across the world through a web of entities based out of low tax jurisdictions in Cayman Islands and Mauritius, which indicated that the real control of the companies does not lie in Mauritius. • The Revenue also stated that on perusal of materials on the record, it prima facie appears that said limited partnership (LP), legally exempted limited partnerships, are default flow through entity for purpose of taxation and all profits directly flow to the partners in the ratio of their capital contribution or as defined in partnership deed. The limited partners, however, are not involved in the day to day business of the LP and it's the General Partner who manages the LP. • The General Partner of TG Private Investment Partners V LP is TG PIP Performance V and its General Partner is TG PIP Management V Ltd which is in turn controlled by Mr Charles P Coleman. Also, management company for TG Private Investment Partners V LP and TG Private Investment Partners VI LP is TGM LLC, USA whose founder member is Mr Charles P Coleman. The Revenue submitted that from the date of inception the companies were part of TGM USA and its affiliates through a web of entities based out of Cayman Islands and Mauritius.	• Tiger Global Holdings argued that the allegation of the Revenue that the transaction was prima facie for avoidance of tax was grossly erroneous, lacked substance and wholly unsubstantiated. • Tiger Global Holdings stated that the transaction involved in the present application was sale of shares simplicitor undertaken between two unrelated independent parties which cannot be considered as being designed for avoidance of tax. • Tiger Global Holdings have placed reliance on the judgment of Honourable Supreme Court in the matter of Vodafone International Holdings BV[6] to emphasize that the onus was on the tax authority to demonstrate how such a design existed in each case. • Reliance on the ruling of the authority in the matter of Star Television Entertainment Limited[7] wherein it was held that a transaction cannot be designed for the prima facie avoidance of tax if there is business rationale surrounding the transaction. • The AAR has also extracted submissions made by Tiger Global Holdings before the Commissioner of Income Tax (CIT). For the allegation of CIT that Tiger Global Holdings had established tax residency in Mauritius only to take advantage of Indo-Mauritius DTAA and that the purpose of such residence was only to avoid paying taxes on returns earned by them, Tiger Global Holdings replied stating that board minutes extracts relied by CIT specifically notes that the Mauritius comprehensive tax treaty network with various countries (and not just India) facilitated efficient asset management and achieved a competitive return for them. The mere fact that they have applied for TRC in order to avail treaty benefits does not mean that a colourable device for tax avoidance was resorted to.
On Decision Making	• The Revenue based on the minutes of the meeting furnished by companies, it is stated that Mr Steven Boyd, non-resident USA director (who was also	

[6] [2012] 347 ITR 001

[7] [2010] 321 ITR 001 (AAR)

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<td>General Counsel of Tiger Global Management LLC) had attended all the Board Meetings in which crucial decisions were taken and the Mauritius Directors were in effect mere spectators or took advice from Mr Steven Boyd.

• The Revenue also states that Mr Steven Boyd or one of the representatives of TGM, USA was always present to advise the Board of all the companies which held shares in Flipkart Singapore. The other directors based in Mauritius were mere puppets and not independent. The companies decision making was fully subordinate and placed reliance on the decision of Supreme Court in the matter of Vodafone International Holdings BV[8].</td>
<td rowspan="2">• For the allegation of CIT that based on the facts it can be established beyond doubt that the control of funds lies outside Mauritius in the hands of TGM USA, Tiger Global Holdings replied that the CIT has failed to adduce even a single fact or lead any evidence whatsoever in support of the allegation. The mere fact that the Board of Directors have given a limited authorization to certain persons to operate the bank account does not ipso facto mean that they did not have control over its funds. Tiger Global Holdings further stated that the not a single fact has been adduced by CIT to disprove the submission that the funds invested by them as well as sale proceeds received by them from transaction were legally and beneficially owned by them in sole, independent and exclusive capacity.

• For the allegation that the corporate disclosures state that Mr Charles P Coleman was the beneficial owner. Tiger Global Holdings stated that the mere fact that certain disclosures were made and maintained for Mauritius corporate law purposes does not ipso facto mean that the legal owner does not enjoy benefits of the shares in his independent capacity for income tax purposes, unless clear facts are brought on record to demonstrate otherwise. They have further stated that the logic canvassed by Revenue if applied would result in absurdity leading to a situation whereby no Indian company with foreign shareholders would ever be able to claim treaty benefits in India.

• Finally, Tiger Global Holdings pleaded that the holding structure was of no relevance and the transaction was not prima facie found to be designed for avoidance of tax. They contend that the CIT has deemed the holding structure to be ipso facto determinative of whether the transactions was designed for the avoidance of tax which was not the standard to be applied to invoke clause (iii) of proviso to Section 245R(2). They have contended that <u>it must be proven that the transaction itself and not the structure of the entity undertaking the transaction was designed for avoidance of income-tax in order to invoke the above proviso.</u>

• Tiger Global Holdings stated that it was managed and controlled of its Board of Directors in Mauritius in accordance with its constitution. The decision to invest into and ultimately sell the shares of Flipkart Singapore was taken by Directors of Tiger Global Holdings after proper discussions and deliberations. The shares were held by them and were not accountable to any third party and they were neither sham entity nor a conduit</td>
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<td>On Financial Control</td>
<td>• The Revenue stated that the authority to open bank account for transactions above US $ 2,50,000 lies with Mr Charles P Coleman countersigned by one of the Mauritius Directors and also stated that it has noted that Mr Charles P Coleman is not on the Board of Directors of any of the companies that hold shares in Flipkart Singapore and his presence is not noted in any of the minutes of the meeting where apparently crucial decisions regarding investments were taken.

• The Revenue submits that without being on boards, Mr Charles P Coleman yields maximum authority in controlling the funds of the companies. The other signatories are Mr Steven Boyd, Mr Michael Germino and Mr Anthony Armenia with either of two categories of signatories countersigned by one of the Mauritius based directors. The non-Mauritius based signatories are again senior management personnel of TGM, USA. The Revenue also submitted that Mr Steven Boyd is on Board of Directors of the companies as a non-resident based out of USA.

• Though some of the resident directors were made the authorised signatories for bank account operation, the Revenue contended that Mr Charles P Coleman continued to be authorised signatory along with Mr Anil Castro, both of whom are not on Board of Directors of Tiger Global Holdings and are in fact key personnel of TGM USA. Any transaction above USD 2,50,000 required either 2 signatories from Group A or one each from Group A and Group B. That is to say, the person listed in Group A had the ultimate control over the founds of the Tiger Global Holdings. The Revenue contended that above facts establish beyond doubt that the control of funds lies outside Mauritius in the hands of Tiger Global personnel based out of USA.</td>
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[8] 341 ITR 001

On Beneficial Ownership	• The Revenue stated that on bare perusal of documents submitted by Tiger Global International III Holdings with Mauritius Financial service commission for the purposes of obtaining Category I Global Business License, it is found that the applicants itself has clearly specified the Beneficial Owner of the company as Mr Charles P Coleman.	company and that the treaty benefit being claimed cannot be measured as tax avoidance.

The AAR after hearing both the parties has stated that tax avoidance itself is not illegal per se. In the scheme of tax avoidance, the taxpayer discloses all the relevant facts to tax authorities and claims benefit as provided under the law. The tax avoidance may be considered as legal as the transactions are so planned that relief is obtained even though it was not as per the intent of lawmakers. Then, AAR proceeded to examine as to whether the transaction or the issue raised by Tiger Global Holdings in the present application was designed prima facie for availing the benefit which may appear to be correct but was not intended by lawmakers.

The AAR based on the findings of Honourable Calcutta High Court in the matter of Hela Holdings Private Limited[9] summarised the differences between tax evasion and tax avoidance. The AAR stated that contention of Tiger Global Holdings that the subject sale of shares simplicitor is too simplistic to be accepted. The capital gain is not dependent on mere sale of shares. Since in order to arrive the capital gains, the cost of acquisition has to be reduced from the sale price and therefore, in the mechanism of capital gains computations what is relevant is not only the sale of shares but also purchase of shares. Hence, AAR stated that, it is imperative for them to look at the entire transaction of acquisition as well as sale of shares as a whole and adoption of dissecting approach by examination of sale of shares alone is not appropriate.

The AAR further stated that from the notes to the Financial Statements, it is evident that the principal objective of Tiger Global Holdings was to act as investment holding company for a portfolio investment domiciled outside Mauritius. **The investment in Flipkart Singapore which has an Indian subsidiary, was with a prime objective to obtain benefits under the double taxation treaty between Mauritius and India and between Mauritius and Singapore.** Tiger Global Holdings is part of TGM USA and have been held through its affiliates through web of entities in Cayman Islands and Mauritius. Though holding-subsidiary structure might not be a conclusive proof for tax avoidance, **the purpose for which the subsidiaries were set up does not indicate the real intention behind the structure. The fact that the Tiger Global Holdings were set up for making investment in order to derived benefit under the DTAA between Mauritius is an inescapable conclusion.**

The AAR stated that the next aspect that has to be considered is the control and management of Tiger Global Holdings. Though it was pleaded that the control and management was with the Board of Directors in Mauritius, the AAR stated that what is material is not routine control of the affairs but their overall control, which would mean the head and brain and then proceeded to examine, whether the head and brain of Tiger Global Holdings was in Mauritius. On the powers to Mr Charles P Coleman as signatory of cheques above a particular limit, the AAR stated that it would have made sense if a local person based in Mauritius was appointed to sign the cheques on behalf of the directors. The AAR stated that Tiger Global Holdings have not provided any explanation as to why Mr Charles P Coleman, who was not based in Mauritius was appointed to sign the cheques of Mauritius bank account. The AAR stated that in view of the above facts the appointment of Mr Charles P Coleman as authorised signatory of bank cheques above a limit cannot be considered as mere coincidence. The AAR brushed away the stand taken by Tiger Global Holdings that giving authorisation to operate bank account to a

[9] 263 ITR 124

person does not ipso facto mean that they do not have control over the funds by stating that the authorisation was not given to a certain person but to Mr Charles P Coleman, whose influence over the group is evident. The AAR further stated that from the evidences brought on record, it is evident that the Tiger Global Holdings were ultimately controlled by Mr Charles P Coleman and apparently the decision for investment or sale was taken by Board of Directors but the real control over the decision of any transaction over a limit was exercised by Mr Charles P Coleman and accordingly concluded the head and brains of Tiger Global Holdings was situated not in Mauritius but in USA. The AAR further stated that the holding structure coupled with prima facie management and control of the holding structure, including the management and control of Tiger Global Holdings, would be relevant factors for determining the design for avoidance of tax. The real management and control of the Tiger Global Holdings was not with their respective Board of Directors but with Mr Charles P Coleman, the beneficial owner of the entire group structure and concluded that the Tiger Global Holdings were only a 'see-through entity' to avail the benefits of India-Mauritius DTAA.

The AAR also stated that what was covered under Article 13 of India-Mauritius DTAA is gain arising on alienation of shares of Indian company and not a Singapore company. Hence, for the gain arising on sale of Flipkart Singapore, the Tiger Global Holdings could not seek for the benefit under India-Mauritius DTAA, since shares of Singapore company are not covered in the said treaty and on merits too the case fails. The AAR also brushed away the stand taken that the whole transaction has to be seen for tax avoidance and if it is established that Mauritian company was interposed as a device, it was open to tax department to discard the device and take into consideration the real transaction by stating that the financial statements of Tiger Global Holdings does not reveal any other investments except Flipkart Singapore. Thus, the real intention was to avail the benefits of India-Mauritius Treaty was concluded by AAR. The AAR also brushed away the yardsticks as postulated by Honourable Supreme Court in Vodafone International Holdings BV and relied by Tiger Global Holdings by stating that the foreign direct investment in the subject case has not reached India but to Singapore and accordingly all other yardsticks would not come into play. Finally, the AAR concluded stating that though the shares of Flipkart Singapore substantially derive their value from the assets located in India, the fact remains that the shares sold were belonging to Singapore company and not Indian company and accordingly the benefit of India-Mauritius DTAA would not apply and the issue involved was designed prime facie for avoidance of tax and hence cannot be entertained by them.

<u>Our Comments:</u>

From the above, it is evident that the AAR has rejected to entertain the application on the ground that the transaction is designed prima facie for avoidance of tax. Though the AAR has referred to the judgment of Honourable Supreme Court in the matter of Vodafone International Holdings BV (supra), in our view the rationale was not correctly applied to the Tiger Global Holdings matter. The AAR made reference to the judgment of Vodafone International Holdings (supra) as a matter of routine and to complete the formality but not with an intention to apply the principals enumerated therein.

Now, we wish to examine the aspects which are favourable and against to Tiger Global Holdings tax position. Also, then, we shall take this as a case study and see how this structure would be tested in PPT and GAAR regime.

Positions favourable to Tiger Global Holdings:

Rationale of Honourable Supreme Court in Vodafone International Holdings BV[10]:

On Tax Avoidance - Principals enunciated by Ramsay:

The Honourable Supreme Court stated the test laid down in W.T. Ramsay Ltd[11] is 'look at'. According to the said test, the Revenue is to ascertain the legal nature of transaction and while doing so, it has to look at the entire transaction holistically and should not adopt a dissecting approach. The Court also stated that there is a difference between pre-ordained transaction which is created for tax avoidance purposes, on one hand, and a transaction which evidences investment to participate in India. In order to find out whether a given transaction evidences a pre-ordained transaction in the sense indicated above or investment to participate, one has to take into account the factors namely, duration of time during which the structure existed, the period of business operations in India, generation of taxable revenue in India, the timing of exit, the continuity of business on such exit.

The AAR denied examination of all these aspects only on the sole reason that the investment flowed to Singapore and not India. It is beyond doubt that the funds invested in Singapore have eventually flown into India towards equity or loan in Flipkart India. Further, the plea taken by Tiger Global Holdings to apply the India-Mauritius Treaty is also a factor which establishes that the funds have actually flown to India. The AAR would have examined the issue by taking the said aspect into consideration and in our opinion, that being done, the ruling may be different.

The Honourable Supreme Court stated that HTIL or VIH was not a fly by night operator/short time investor and held that if one applies 'look at' test, without invoking dissecting approach, then the transaction cannot be called as for avoidance of tax and applying the same to the facts of Tiger Global Holdings, the conclusion would be same as the Honourable Supreme Court's in the matter of Vodafone International Holdings BV (supra).

On Tax Avoidance – Taxation of Holding Structure:

Para 68 of the judgment deals with certain international aspects of holding structure, which assumes huge significance for the current context. The AAR has rejected the pleadings of Tiger Global Holdings that the heads and brains of those entities are outside Mauritius and the power of Mr Charles P Coleman can be felt all over those entities. The AAR also stated that the signing of cheques beyond certain a limit resting with Mr Charles P Coleman is not a coincidence and concluded that TGM USA is a beneficial owner of shares.

However, the AAR has not applied the principals enunciated in Para 68 of Vodafone International Holdings BV in true sense. Para 68 states that, it is a common practice in international law, which is the basis of international taxation, for foreign investors to invest in Indian companies through an

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[10] CGP Investment (Holdings) Limited (CGP), company incorporated in Cayman Islands which was holding single share, wherein the value of such share was derived from assets located in Hutchison Essar Limited (HEL), an Indian Company. CGP was holding a total of 52% of HEL through direct and indirect subsidiaries. Further, CGP was an indirect subsidiary of Hutchison Telecommunications International Limited (HTIL), a company incorporated in Cayman Island, listed in Hong Kong. HTIL was the vendor of single share of CGP and Vodafone International Holding BV (VIH), Netherland company was the buyer of such single share. The Revenue argued that inter alia, the interposition of CGP and transfer of share of CGP to VIH was to avoid tax and there is no role other than this for CGP in the entire transaction.

[11] (1981) 1 All E.R 865

interposed foreign holding or operating company, such as Cayman Islands or Mauritius based company both for tax and business purposes. The Court stated that in doing so, the foreign investors are able to avoid lengthy approval and registration process required for a direct transfer of an equity interest in a foreign invested Indian company and recognised such a practice makes taxation of such holding structures complicated and give rise to issues such as double taxation, tax deferrals and tax avoidance. The Court further stated that when it comes to taxation of holding structure, **at the threshold, the burden is on Revenue to allege and establish tax abuse, in the sense of tax avoidance in the creation of such structures and in the application of judicial anti-avoidance rule, the Revenue may invoke the 'substance over form' principle or 'piercing the corporate veil' test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant.**

The Court also stated that, if a structure is used for circular trading or round tripping[12] or to pay bribes, then such transactions, though having a legal form, should be discarded by applying test of fiscal nullity and similarly, in a case, where the Revenue finds that in a holding structure an entity which has no commercial/business substance has been interposed only to avoid tax then in such cases applying the test of fiscal nullity it would be open to the Revenue to discard such inter-positioning of that entity. However, the court stated that it has to be done at the threshold and the task of Revenue/Court to ascertain the legal nature of transaction and while doing so it has to look at the entire transaction as a whole and not dissecting approach. The Court stated that **the Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but that it should apply the 'look at' test to ascertain its true legal nature.** Applying the above tests, the court stated, **every strategic foreign direct investment coming to India, as in investment destination, should be seen in a holistic manner** and concluded **that the corporate business purpose of a transaction is evidence of the fact that the transaction is not undertaken as colourable or artificial device. The stronger the evidence of a device, the stronger the corporate business purpose must exist to overcome the evidence of a device.**

Applying the above, it is imperative for AAR to apply the test of tax avoidance at threshold. The Supreme Court stated that an entity which has no commercial/business substance and has been interposed only to avoid tax, only in such cases, applying the test of fiscal nullity, the Revenue can discard the inter-positioning of that entity. However, the Revenue cannot start with the question as to whether the transaction is a tax deferment/saving device but that it should apply the 'look at' test to ascertain its true legal nature. In other words, the principal is that the courts cannot go beyond a document or transaction and the same has to be taken on face value unless the surrounding circumstances indicate that the transaction is a sham or tax avoidant.

That is, if the surrounding circumstances does not hint that the transaction to be a sham or tax avoidant, then the courts are not bound to discard the interposing entity, that is Tiger Global Holdings. The said entities should only be discarded, if the surrounding facts and circumstances indicate that the transaction is sham or tax avoidant. In the instant case, the money would have flowed from TGM USA to Mauritius entities, from there to Flipkart Singapore and ultimately into Flipkart India. There are no surrounding factors which hint the said transactions or arrangements are sham or tax avoidant. Just because the power to sign cheques vests with Mr Charles P Coleman, it cannot be stated that the funds should have directly going to Flipkart Singapore from TGM USA. If these kinds of tests are applied by AAR, then every foreign direct investment would be seen as sham or tax avoidant. The AAR also

[12] Round Tripping is one of the methods of Treaty Shopping. While other forms of Treaty Shopping are normally allowed and encouraged by source countries, round tripping and abusive restructuring may not be entertained by applying JAAR.

should have taken the matter holistically and apply the said tests instead of arriving at the conclusion that Tiger Global Holdings are 'see-through entities', which in a kind indicate the presumed mindset of AAR.

On Tax Avoidance – Subsidiaries – Role of CGP:

One of the arguments contended by Revenue in the matter of Vodafone International Holdings BV (supra) is that what was extinguished by HTIL, the vendor is the control in HEL and not a share of CGP and since such control is qua Indian company, the said extinguishment of control results in capital gains in India. Revenue further contended that the subsidiaries were never mentioned in the share purchase agreement entered between VIH and HTIL, which demonstrates that subsidiaries do not have any role to play. The Supreme Court negating the above contention of Revenue stated that it is generally accepted that the group parent company is involved in giving principal guidance to group companies by providing general guidelines to group subsidiaries and the fact that the a parent company exercises shareholder's influence on its subsidiaries does not generally imply that the subsidiaries are to be deemed to be residence of the state in which the parent company resides. The court further stated if a company is a parent company, that company's executive directors should lead the group and the company's shareholder's influence will be generally employed to that end and this obviously implies a restriction on the autonomy of the subsidiary's executive directors and such a restriction, which is the inevitable consequences of any group structure and generally accepted both in corporate and tax laws. The Court further stated that a subsidiary normally complying with the request of parent company may not make the subsidiary puppet. The fact that the parent company exercise shareholder's influence on its subsidiaries cannot obliterate the decision making power or authority of its subsidiary's directors. The Court then formulated a test that the decisive criteria is whether the parent company's management has such steering interference with the subsidiary's core activities that subsidiary can no longer be regarded to perform these activities on the authority of its own executive directors.

Rationale of Honourable Andhra Pradesh High Court in Sanofi Pasteur Holdings SA[13]:

The Honourable Andhra Pradesh Hight Court in the matter of Sanofi Pasteur Holdings SA[14] had an occasion to deal with taxation of indirect transfers vis-à-vis India-France DTAA. The said judgment being judgment post Vodafone International Holdings BV (supra) followed the principals laid down by the Honourable Supreme Court. Apart from those principals which are dealt above, we shall now proceed to understand the principals set out by the Honourable Andhra Pradesh High Court in the said matter.

On Tax Avoidance – Subsidiaries - Role of ShanH:

The Court after analysing the entire transaction, documents, agreements and others has concluded that ShanH (akin to CGP in Vodafone International Holdings BV and Tiger Global Holdings in the current case) incorporated in 2006 was not conceived as a pre-ordained scheme to avoid tax in India and the Revenue has also conceded on the same point. The stand of Revenue asserting that since MA and

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[13] [2013] 354 ITR 316

[14] Sanofi Pasteur Holdings SA ('Sanofi'), France has purchased the entire share capital of ShanH SAS ('ShanH'), France, which was JV of Merieux Alliance ('MA') and Groupe Industriel Marcel Dassault ('GIMD'), France. As on the date of acquisition of ShanH by Sanofi, the former was holding 80% of shares of Shanta Biotech Limited (SBL) an Indian company. The contention of the Revenue inter-alia is, what was transferred is shareholding in SBL and not divestment in ShanH, being sham.

GIMD claim that capital gain is taxable only in France, therefore inferring incorporation of ShanH as part of pre-ordained scheme was struck down by the Court. The Court stated that the contention of Revenue was ambivalent and incoherent for the reason that calling ShanH as part of pre-ordained scheme because MA and GIMD claiming immunity from capital gains taxability transform the entirety of antecedent extortions by ShanH. The Court accordingly concluded that ShanH is a distinct entity of commercial substance, distinct from MA and GIMD incorporated to serve as investment vehicle, this being the commercial substance and business purpose i.e., foreign direct investment in India, by way of participation in SBL.

On Indirect Transfers vis-à-vis India-France DTAA:

The entire contention of the Revenue was that since ShanH is only an interposition entity between SBL and MA & GIMD, the same has to be kept aside and if that being done, then the transfer of shareholding by MA & GIMD in SBL, which is more than 10% to Sanofi, triggers tax liability under Article 14(5) of India-France DTAA. The said para distributes taxing right to source country, where the company in which shares are being sold, is resident, if the alienation is more than 10%. Since, in the instant case, the Revenue contends that what is being transferred is not shares of ShanH, but shares of SBL, the provisions of Article 14(5) gets triggered, once ShanH is kept out picture and Sanofi would have deducted tax while making payments to MA & GIMD. Further, the Revenue contended that the phrase 'alienation' used in Article 14(5) not covers direct transfers but also indirect transfers and accordingly, since ShanH derives value from the assets of SBL, transfer of ShanH indirectly results in transfer of SBL and accordingly said transaction would fall under ambit of Article 14(5).

However, Sanofi argued that, since ShanH is having a commercial substance, the same cannot be discarded and what was transferred is shareholding in ShanH and not SBL, since post transfer also ShanH continued to be the shareholder of SBL. Further, since, the said transaction is not falling under any of the paras of Article 14, it falls under residuary para, that is Article 14(6) and as per which the taxing rights vests with state in which the alienator is resident, that is France in this case. Since, there is no income which is accrued or arising or deemed to accrue or arise in India for MA & GIMD, there is no obligation on them under Section 195 of ITA to withhold tax and treating them as assessee-in-default is erroneous. Further, Sanofi, MA and GIMD argued that the UN Model Convention specifically mentions for incorporation in text of Article 14(5), situations covering indirect transfers and India, France choosing not to do so, nothing can be interpreted in Article 14(5) to cover indirect transfer.

The Honourable High Court has held that the contention of Revenue cannot be accepted to invoke the provisions of Article 14(5) of India-France DTAA and relying on South African Supreme Court of Appeal's judgment in the matter of Tradehold Limited[15] and various other judgments have concluded that the contention as proposed by Revenue is accepted would render the provisions of Article 14(4) otiose. Further, the Court stated that Article 14(5) does not postulate 'see-through' provision on true, fair and good faith interpretation and the phrase 'alienation' cannot be understood from a synonymous expression 'transfer' used in Indian domestic law, since to invoke Article 3(2), the phrase should be identical and not synonymous. The Court concluded that retrospective amendment by insertion of Explanation 5 to Section 9(1)(i) does not change the position under India-France DTAA and accordingly such transaction of sale of ShanH shares by MA and GIMD to Sanofi is not subjected to tax in India.

[15] [2010] ZA SAC.61

Applying the above rationales to Tiger Global Holdings:

Role of Tiger Global Holdings vis-à-vis CGP and ShanH:

The AAR clearly has not applied the above tests. They have not seen whether the TGM USA has a steering interference with Tiger Global Holdings core activities, so that no longer the latter is in position to perform those activities. The AAR simply stated that since strategic meetings were participated by General Counsel of TGM USA who directly reports to Mr Charles P Coleman, stated that the Tiger Global Holdings are nothing but mere puppets and it becomes imperative to see-through such entities. To this extent, it indicates that AAR has mis-applied or not applied the tests in true sense.

The Honourable Supreme Court in Vodafone International Holdings BV (supra), while dealing with the contention of the Revenue that CGP stood inserted at a later stage in the transaction was to bring in a tax-free entity (or to create a transaction to avoid tax) stated that CGP was an investment vehicle. Qua acquisition of CGP, VIH has obtained the same rights or entitlements as HTIL had and this was the motive behind VIH acquiring CGP.

Applying the said rationale, CGP in that transaction was akin to Tiger Global Holdings in the current transaction. Walmart Inc to acquire the same rights and entitlement that Tiger Global Holdings had in Flipkart Singapore, thereby, Flipkart India has purchased the shares of Tiger Global Holdings. Tiger Global Holdings can be said to investment vehicle and there is no necessity for them to hold shares of other companies apart from Flipkart Singapore to prove such point.

The Courts in numerous occasions has stated that revenue is not expected to sit in the armchair of the business man and decide the mode in which business has to be carried. It is prevalent practice that there are subsidiaries created to hold separate investments, so that at later point of time, it would be easy to divest them. Just because a subsidiary does not hold investment in other companies, does not disentitle it from being an investment vehicle.

Further, applying the decision of Honourable Andhra Pradesh High Court in Sanofi Pasteur Holdings SA (supra), where in, it was held that incorporation of ShanH as an investment vehicle for making foreign direct investment into India has a commercial substance and hence cannot be called as sham to Tiger Global Holdings, would render the same conclusion. Tiger Global Holdings which was also incorporated as investment vehicle, cannot be stated to be sham or non-existent or call for application of 'see-through'. Tiger Global Holdings can be stated to have a commercial substance and business purposes, investing into Flipkart Singapore and finally into Flipkart India.

From the above, it can be clearly argued that the interposition of Tiger Global Holdings had actually a business sense when seen it holistically and applying the principals laid down by Honourable Supreme Court and Honourable Andhra Pradesh High Court and the transaction cannot on a prima facie basis be said for avoidance of tax.

Indirect Transfers – Article 13(4) of I-M DTAA[16] vis-à-vis Article 14(6) of I-F DTAA[17]:

Before applying the rationale of Sanofi Pasteur Holdings SA (supra), let us examine, what made Tiger Global Holdings invoke the provisions of India-Mauritius DTAA.

As stated in facts, Tiger Global Holdings sold shares of Flipkart Singapore to Fit Holdings S.A.R.L but claimed the benefit under India-Mauritius DTAA. Ideally, the DTAA which has to be referred is the Mauritius-Singapore DTAA, since the Tiger Global Holdings is resident of Mauritius and the shares belong to Singapore company, that making the source country, Singapore. Hence, the treaty which shall be applicable is Mauritius – Singapore DTAA and this may be one of the reasons that the AAR has stated that Tiger Global Holdings cannot invoke the benefit enshrined under India-Mauritius DTAA. Let us proceed to examine the same.

The reason why Tiger Global Holdings invoked India-Mauritius DTAA is Explanation 5 to Section 9(1)(i) of ITA[18]. Vide Explanation 5, it is clarified that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India **shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.**

Normally, the situs of the share is where the company is incorporated and accordingly the situs of share of Flipkart Singapore would be Singapore but for the Explanation 5. Because of the said explanation, the deeming fiction gets triggered and the situs of shares of Flipkart Singapore travels from Singapore to India. It may be the said reason as to why Tiger Global Holdings have invoked the provisions of India-Mauritius DTAA, because the source jurisdiction has been shifted from Singapore to India.

Article 13 of India-Mauritius DTAA deals with Capital Gains. Article 13A and 13B have been inserted by amending the protocol to said DTAA. Vide such amended articles, the gains on alienation of shares acquired post 1st April 17 in a company shall be taxed in the state where the said company is resident and the tax rate shall not exceed 50% of the tax applicable on such gains in the resident state of company whose shares are being alienated. However, as evident that the above paras would apply only for the shares which are acquired prior to 1st April 17. In cases, where the shares were acquired prior to 1st April 17, the earlier position would continue, which was guided by Para 4. The unamended Para 4 used to state that gains from the alienation of property other than referred in Para 1 to Para 3, shall be taxable only in the contracting state of which alienator is a resident.

Since, in the instant case, Tiger Global Holdings have acquired the shares prior to 1st April 17, the gains would be taxable only in the state where the alienator is resident, that is Mauritius and not in India. Further, Article 13(4) being residuary in nature, would cover the indirect transfers like in the instant case, the shares of Flipkart Singapore and accordingly, the gains would be taxable only in Mauritius[19]. In fact this was the proposition laid down by Honourable Andhra Pradesh High Court in Sanofi Pasteur Holdings SA (supra), wherein they have stated that transfer of ShanH would trigger the residuary

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[16] India – Mauritius DTAA

[17] India – France DTAA

[18] Income Tax Act, 1961

[19] The Honourable Supreme Court in the matter of Azadi Bachao Andolan reported in [2003] 263 ITR 706 has an occasion to deal with 'liability to tax' appearing in Article 4 of India-Mauritius DTAA and held that liable to tax and payment of tax are different aspects and non-payment of tax in Mauritius would not make any person not a resident of that state. Further, after referring to various foreign judgments namely Federal Court of Canada in Late John N Gladden and High Court of Australia in Lamesa Holdings BV has held that there is no necessity for the income to doubly taxed to claim the benefit under DTAA.

category and not Article 14(5) as contended by Revenue, as Article 14(5) does not support see-through. It is worth noting that there is no similar article to Article 14(5) of India-France DTAA in Article 13 of India-Mauritius DTAA.

The AAR without going through the said aspects like situs of Flipkart Singapore by virtue of Explanation 5 to Section 9(1)(i) and Article 13(4) of India-Mauritius DTAA has ruled that Tiger Global Holdings could not invoke the India-Mauritius DTAA since what is being dealt is not share of Indian Company, which in our view is grave injustice.

Now, we shall proceed to determine, whether there are any setbacks or adverse provisions against Tiger Global Holdings tax position.

<u>Positions adverse to Tiger Global Holdings:</u>

<u>Tax Neutral situation in Vodafone International Holdings BV vis-à-vis Tiger Global Holdings:</u>

One of the main reasons for Honourable Supreme Court to rule in the matter of Vodafone International Holdings BV (supra) that there is no tax avoidance could be the no tax position even if sale is done at level of Mauritian holding companies which were holding shares of HEL instead of sale of CGP, a Cayman Island company which was holding shares in all the Mauritian holding companies. The Hutchison structure was that CGP was holding shares in Array Holdings Limited, which in turn hold shares in five companies incorporated in Mauritius with downstream investment into HEL, India. In other words, had if VIH purchased shares in Mauritius subsidiaries instead of purchasing shares in CGP, there would not be any tax liability in the hands of Mauritius subsidiaries in light of India-Mauritius DTAA. Since, there was no tax liability either in the sale of shares at Mauritius subsidiaries level or at the level of CGP, the Honourable Supreme Court might have come to a conclusion that on a holistic basis, the role of CGP is not for tax avoidance or sham.

However, in the facts of Tiger Global Holdings, if they are treated as sham or puppets and by applying the test of fiscal nullity, the residence gets shifted from Mauritius to USA and by applying the provisions of India-USA DTAA, Article 13 states that each contracting state may tax capital gains in accordance with the provisions of its domestic laws, which would definitely trigger a tax liability in India as compared to no tax position as per India-Mauritius DTAA. Even though there is a remote possibility for the courts to arrive at this conclusion, the above proposition cannot be ruled out. If this being applied, it becomes an adverse position for Tiger Global Holdings.

<u>Reliance on Federal Court of Appeal's judgment in Prevost Car Inc[20] in Sanofi Pasteur Holdings SA:</u>

The Honourable High Court of Andhra Pradesh in Sanofi Pasteur Holdings SA (supra) in arriving to the conclusion on the aspect of 'beneficial ownership[21]' has placed reliance in the Federal Court of Appeal's judgment in Prevost Car Inc.

The facts in Prevost Car Inc is that, Prevost Car Inc (for brevity 'Prevost Inc'), a Canadian resident corporation has paid dividend to its shareholders, Prevost Holding BV (for brevity 'Prevost BV'), a corporation resident in Netherlands. Subsequent to such receipt of dividend by Prevost BV, substantially the same amounts were remitted to its corporate shareholders, Volvo, swedish resident company and to Henlys, a UK resident company, in terms of shareholder agreement between Volvo

[20] 2009 FCA 57

[21] The aspect whether the test of 'beneficial ownership' has to be applied only for incomes at Article 10, Article 11 and Article 12A of I-M Treaty or will also be applicable for incomes under Article 13 is not being discussed herein and proceeded with an assumption that they will apply to Article 13 since AAR was dealing with 'beneficial ownership'.

and Henlys. If Prevost Holding were to be treated as beneficial owner of the dividends, the rate of withholding under Canadian Income Tax Act was 5% and if Volvo and Henlys were treated as beneficial owners of dividends, then the rate of withholding is greater than 5%. The Tax Court of the Canada found that the beneficial owner of dividends was Prevost BV and not Volvo and Henlys against which the Canadian Revenue has appealed. The Federal Court of Appeal rejected the Canadian Revenue's contention that the expression 'beneficial ownership' has to be read as 'ultimate beneficial ownership' and agreed with the Tax Court's judgement wherein it was held that the beneficial owner of dividends is a person who receives the dividends for his/her own use and enjoyment and assumes the risk and control of the dividend received, is the person who enjoys and assumes all the attributes of ownership, the dividend is for the owners own benefit and this person is not accountable to anyone for how he deals with dividend income. The Federal Court of Appeal also endorse the view of Tax Court that Prevost BV cannot be said to be conduit in absence of any evidence to such an extent despite that Prevost BV did not have no physical office or employees in Netherlands or elsewhere nor was the evidence that dividends from Prevost Inc were ab initio destined for Volvo and Henlys with Prevost BV a mere funnel for flowing of dividends.

From the above, it is evident that the term 'beneficial ownership' has been legally interpreted as against the substance-over-form approach which is normally adopted by the courts all over the world. Even in the judgment of Sanofi (supra), the High Court has stated that what was being done in Prevost is a treaty shopping activity but continued to bless it and apply it to the facts of Sanofi, to hold that ShanH is not a sham entity and beneficial owner of shares of SBL.

However, the current trend across the globe is to apply substance over form approach when it comes to understanding of 'beneficial ownership' as against legal interpretation adopted in Prevost Car Inc[22]. Hence, if the substance over form is applied, the result in Sanofi (supra) may be different and the Courts while examining the issue with respect to Tiger Global Holdings may look at principals Sanofi (supra) with the above changed position.

Deeming Fiction under the Domestic Legislation vis-à-vis Treaty Application:

Ambulatory vs Static:

As stated earlier, the invocation of provisions of India-Mauritius DTAA by Tiger Global Holdings was for the sole reason that the situs of shares by fiction carved by Explanation 5 to Section 9(1)(i) was deemed to be in India. The question that arises now, is, whether the benefit arising as a consequence to the said deeming fiction can be granted to Tiger Global Holdings. In other words, the entire reason for insertion of Explanation 5 with a retrospective effect is to tax the transfer of shares which are located outside India but substantially deriving their value from the assets located in India and looked in that hue, whether it can be said that India gave up its taxing right to Mauritius vide the residuary Article 13(4)? Can it be stated that this was a conscious decision made by India and Mauritius at the time of signing of the DTAA? It is important to note that while dealing with coverage of indirect transfers under the residuary article in India-France DTAA in Sanofi (supra) matter, the India and France have chosen not to include the transactions which are in kind of indirect transfers under Article 14(5) and did such discussion happen between India and Mauritius?

Further, the Article 13(5) of India-Mauritius DTAA states that for the purposes of the said article, the term alienation means the sale, exchange, transfer, or relinquishment of the property or the

[22] The Beneficial Ownership Limitation in Article 10, 11 and 12 OECD Model and Conduit Companies in Pre and Post BEPS Tax Treaty Policy: Do We (Still) Need It? By Robert J Danon

extinguishment of any rights therein or the compulsory acquisition thereof under any law in force in the respective contracting states. The term ‘transfer’ has not been defined in the Article 3(1) of India-Mauritius DTAA. However, Article 3(2) states that in the application of provisions of this convention by a contracting state, any term not defined therein shall, unless the context otherwise requires, have the same meaning which it has under the laws in force of that contracting state relating to the areas which are subject of the convention.

Applying the provisions of Article 3(2), the phrase ‘transfer’ as defined in Section 2(47) of ITA can be accessed. The said phrase vide Explanation 2 states that for the removal of doubts, it is clarified that ‘transfer’ includes and shall be deemed to have always included disposing of or parting with an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or indirectly, absolutely or conditionally, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterised as being effected or dependent upon or flowing from the transfer of share or shares of a company registered or incorporated outside India.

The above explanation essentially covers the indirect transfers. However, the said explanation was inserted with retrospective effect from 1st April 1962 by Finance Act, 2012. In other words, when the India-Mauritius DTAA was being negotiated, the said explanation was not on the statute book and now can it be said that the explanation which was not there at the time of negotiation but later got included by way of a retrospective amendment, should be read into the Article 13(5) of India-Mauritius DTAA? If this cannot be so, then the benefit under Article 13(5) cannot be invoked by Tiger Global Holdings, making the transaction subjected to tax in India. We shall proceed to examine the same.

First, as per Article 3(2), any term which has used in the convention but not defined has to be understood in accordance with the meaning laid down under the domestic legislation. Before, we proceed to examine, whether the term ‘transfer’ has to be understood in terms of ITA, first, we have to examine, whether the expression ‘transfer’ falls in the ambit of ‘term’ used in Article 3(2) to access the meaning under domestic legislation. The Honourable Mumbai ITAT[23] had an occasion to examine the said issue in the matter of Reliance Jio Infocomm Limited[24], wherein the ITAT was interpreting the issue, whether the expression ‘process’ used in the definition of ‘royalty’ in DTAA, is a ‘term’, which calls for invocation of Article 3(2) and accordingly understand the said expression ‘process’ in terms of ITA. The ITAT has held that the ‘term’ is defined to mean a word or phrase used to describe a thing or to express a concept, especially in a particular kind of language or branch of study, in addition to being a word, it connotes some kind of a point of reference, whereas a word is only a constituent of language. Accordingly, held that Article 3(2) will come into play only in respect of undefined treaty terms, which are in the nature of reference points and which have some peculiar significance as term employed in the treaty, and not all the undefined words and expressions used in treaty.

Applying the said rationale, can it be said the expression ‘transfer’ used in Article 13(5) falls under the ambit of ‘term’, to invoke the definition as per Section 2(47)? There are two views possible. One, since the expression ‘transfer’ expresses a concept and connotes some kind of reference, it is possible to say that the said expression would fit as ‘term’ to invoke Article 3(2). The other possible view is that since ‘transfer’ is used to explain the definition of ‘alienation’ used in Article 13, it becomes a word and not ‘term’ to invoke Article 3(2). However, for the purposes of this article, we assume that first view has higher possibility to succeed in court of law and accordingly proceed to understand the expression ‘transfer’ as ‘term’. Now, this being done, the next important question, that would need

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[23] Income Tax Appellate Tribunal

[24] [2020] 77 ITR (Trib) 578W (ITAT[Mum])

to be answered is, what approach should be applied to understand the term 'transfer', ambulatory or static. If ambulatory approach is adopted, then the 'transfer' has to be understood as it exists in ITA as on the date when treaty is being applied. On the other hand, if static approach is to be applied, the expression 'transfer' should be understood without making reference to the retrospective amendment to the said definition under ITA. While this is not an easy exercise, especially, courts in India are divided on this and factoring the interplay of definition under domestic legislation vis-à-vis, defined and undefined treaty terms makes it more complicated, let us proceed to examine.

The Honourable Bombay High Court in the matter of Siemens Aktiongesellschaft[25] had an occasion to analyse the said issue. In the matter of Siemens Aktiongesellschaft (supra), the court was seized with a question as to whether the phrase 'royalty' which is not defined in the India-German DTAA has to be understood in terms of domestic legislation which define the said phrase. The assessee's argument was that since the phrase 'royalty' has not been defined either under the said DTAA or ITA at the time of entering of the agreement between India and Germany, the definition under the ITA cannot be referred to. In other words, the assessee contends that the treaty is static. However, the court without not getting into detail, finding force from the aspect that the said treaty does not cover only taxes which are in force at the time of signing of the agreement but would also include any other tax as taxes of substantially similar character subsequent to the date of agreement, has not accepted the contention of the assessee that the law would be applicable or as defined when the DTAA was entered into. In a way, the court has endorsed the ambulatory approach as against static approach.

However, post Siemens Aktiongesellschaft (supra), there were numerous occasions when the courts were seized with the same question, as to treat, the DTAA as static or ambulatory. However, majorly, in all other occasions, the courts endorsed the static approach especially, when the terms under domestic law are amended with an intention to override the tax position that existed pre-amendment[26]. In short, it can be argued by the tax payer, the term in domestic legislation should be made applicable by adopting ambulatory approach, when it is beneficial to him. However, the tax authorities may not be accepting such proposition by quoting Article 31 of VCLT[27] which states the treaty has to be interpreted in good faith in accordance with the ordinary meaning to be given to the terms in their context and in light of its object and purpose.

If the courts take the view that since at the time of signing of India-Mauritius DTAA, the term 'transfer' cannot be understood to cover indirect transfers, then it may be ruled that Tiger Global Holdings would not be eligible to claim the benefit of Article 13(4) of India-Mauritius DTAA. This view also gains support from the following paras.

Indirect Transfers vis-à-vis Residuary Para:

The plea that the Honourable Andhra Pradesh High Court in the matter of Sanofi Pasteur Holdings SA (supra) already held that indirect transfers are covered under Article 14(6) of India-France DTAA may not be taken on face value, because the court therein was deciding whether the indirect transfer falls under Article 14(5) or Article 14(6) and held that since Article 14(6) is residuary, it would also cover indirect transfers. However, in case of India-Mauritius DTAA, there is no article like Article 14(5) and it has only the residuary which is similar to Article 14(6). Hence, in absence of a similar fight as existed

[25] [2009] 310 ITR 320 (Bom)

[26] New Skies Satellite BV – [2016] 382 ITR 114, Reliance Jio Infocomm Limited [2020] 77 ITR (Trib) 578W (ITAT[Mum]).

[27] Vienna Convention on Law of Treaties

in Sanofi Pasteur Holdings SA (supra) in Tiger Global Holdings, whether it can be interpreted that Article 13(4) includes indirect transfers is doubtful.

Indirect Transfer vis-à-vis Article 31 of VCLT – John N Gladden's case:

In the matter of John N Gladden[28], the Federal Court of Canada was seized with a question on taxability of capital gains arising on deemed disposition of shares. The facts in that matter are that Mr John N Gladden was a resident of USA and at time of his death, he holds shares in two privately held companies in Canada. The estate has filed returns in Canada by reporting capital gains as per the deemed disposition provision pursuant to Canadian Income Tax Act. However, the estate has claimed refund by invoking the provisions of USA-Canada DTAA, by stating that the treaty vide Article VIII, covers only sale or exchange and does not include deemed disposition. The deemed disposition was a subsequent amendment to the Canadian Income Tax Act, which was not in existence at the time of entering treaty. The Canada Revenue pressed for tax demand that deemed disposition is also covered under the treaty. The Federal Court of Canada stated that on application of interpretation suggested by Article 31 of VCLT, the sale or exchange cannot be said to be including the deemed disposition especially, when such tax was not on statute book in Canada at the time of entering the treaty.

Applying the same to the facts of Tiger Global Holdings, it would be tough for them to argue that the expression 'transfer' would include indirect transfers, since the same was not on statute book as on the date of entering India-Mauritius DTAA and ascribing the ordinary meaning of 'transfer', the indirect transfer would not fall under provisions of Article 13. Further, since the said income is not in the nature of fee for technical services or royalty, it may not be argued that the gain on alienation of shares would fall under the ambit of business profits to seek taxation only when there is permanent establishment in India. The income from alienation may be argued by tax authorities to fall under the Article 22 'Other Income' and by virtue of provisions of para 3, the income of a resident of a contracting state not dealt with in the foregoing articles and arising in the other contracting state may also be taxed in other state, that would be India.

Deeming Fiction in Domestic Law vis-à-vis Treaty – Mr Fowler's case:

Finally, the recent judgement of Honourable Supreme Court in the matter of Mr Fowler[29] had also an occasion to deal the applicability of deeming fiction in domestic legislation vis-à-vis treaty. Mr Fowler, a resident of South Africa (SA) has engaged in certain diving assignments in continental shelf of United Kingdom (UK). Mr Fowler pleaded that the diving income which he has earned to be treated as trade income (Article 7 of UK-SA DTAA), because the UK domestic legislations treat so. The HMRC[30] on the other hand pleaded that such income is in the nature of income arising from employment and treatment of divers income as trade income is only restricted to domestic legislation and cannot be applied to treaty. If the court found the contention of Mr Fowler to be correct, then there is no income arising for Mr Fowler in UK, since he does not have permanent establishment in UK. If the court found the contention of HMRC to correct, then Mr Fowler's income is taxable in UK, since as per the provisions of (Article 14 of UK-SA DTAA), the salaries would be taxable in the state where they arise, that is UK, in the instant case. The Supreme Court after examining the treaty provisions, the domestic law provisions and the decisions reached by lower courts, has confirmed that the deeming fiction erected under the domestic legislation cannot be applied to treaty provisions to characterise the income earned. The court stated that the deeming fiction created is plainly not for the purpose of

[28] 85 DTC 5188
[29] [2020] UKSC 22
[30] Her Majesty's Revenue and Customs

rendering a qualifying diver immune from tax in UK, nor adjudicating between the UK and SA as the potential recipient of tax and for the purpose of adjusting the basis of a continuing UK income tax liability which arises from receipt of employment income and accordingly held that applying deeming provision in domestic legislation so as to alter the meaning of terms in the treaty with the result of rendering a qualified diver immune from UK taxation would be contrary to its purpose and would produce an anomalous result. The Court further held that Article 3(2) of UK-SA DTAA should not be construed so as to bring qualifying diver within Article 7 rather than Article 14 would contrary to the purposes of treaty.

Applying the same to the facts in Tiger Global Holdings, the tax authorities can argue that reading of expression 'transfer' in Article 13(4) of India-Mauritius DTAA, so that Tiger Global Holdings immune from tax liability under the treaty would not be the objective of the treaty or the domestic legislation and accordingly demand the tax liability in India.

Conclusion on Taxability:

Having discussed the favourable and adverse positions to Tiger Global Holdings, we understand that the final taxability which would be decided by Courts, is not an easy task. From an academic view point, we have examined the different positions that are applicable to Tiger Global Holdings and they may be incomplete and not exhaustive. We are sure that this issue when settled by Honourable Supreme Court will be a significant step in taxation of 'Indirect Transfers'.

Now, we shall proceed to examine, the taxability of this structure in PPT and GAAR regime.

Position post MLI:

As part of BEPS[31] project, the convention on MLI has been ratified and notified by many countries. On becoming the signatory of MLI and notifying a jurisdiction and a simultaneous notification by the other jurisdiction, would trigger the MLI. The role of MLI is to amend the provisions of DTAA as per the options and reservations chosen by each party to the DTAA. India has notified Mauritius for the purposes of MLI. However, as on date, Mauritius has not notified India. Hence, the provisions of DTAA would not get effected by MLI. For the purposes of this article, let us assume that Mauritius has also notified DTAA with India to the Depository. On such an assumption, let us examine, the position of structure as evident in facts on the touchstone of Article 6 and Article 7 of MLI.

Article 6 of MLI vis-à-vis Preamble of I-M DTAA:

Article 6 of MLI springs out from Action 6 of BEPS Package. Article 6 of BEPS Package identifies treaty abuse, and in particular treaty shopping, as one of the most important sources of BEPS concerns. Treaty shopping and other tax treaty abuse strategies would lead to loss of tax revenues to countries which extend benefits to residents of other jurisdiction, where residents of other jurisdictions are not otherwise eligible to access such treaty benefits, because of the reason that they are not seriously resident of such jurisdictions.

In order to prevent treaty abuse, it is agreed by all the countries that the preamble of the DTAA should be amended to make a clear statement that the tax treaty intends to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements. This being a minimum standard, each contracting jurisdiction has to adopt the same.

[31] Base Erosion and Profit Shifting

It is evident that the amended preamble[32] makes it clear that the object and purpose of the treaty intends to eliminate double taxation and without creating opportunities for non-taxation through tax evasion or avoidance including treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions. However, the current preamble[33] does not make any reference to creation of opportunities for non-taxation.

The above distinction is important because, Article 31 of VCLT requires interpretation of treaty in good faith in accordance with the ordinary meaning to be given to the terms in their context and in light of its object and purpose. Article 32 of VCLT which deals with supplementary means of interpretation states that recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of Article 31 or to determine the meaning when the interpretation according to Article 31. Hence, on a combined reading of Article 32 and Article 31, the preamble to DTAA shall definitely be a supplementary means of interpretation.

Seen from such an angle, the terms of treaty has to be interpreted in light of the object and purpose of the treaty, which specifically shouts now that treaty shopping is kind of illegal[34] and not allowed. Hence, now it calls for scrutiny of the structure in terms of the new preamble which specifically does not allow treaty shopping. Hence, there are high chances, post implementation of MLI, qua the amended preamble, these kinds of structures [similar to CGP in Vodafone International Holdings BV (supra) and ShanH in Sanofi Pasteur Holdings SA (supra)] may have to pass strong business test to rule them out from conduit structures.

Article 6 of MLI also gives contracting jurisdictions an option to add to the preamble that the intending countries desire to develop their economic relationship and to enhance their co-operation in tax matters. Assuming the same is adopted for I-M Treaty, the structures may state that the treaty has to be interpreted by keeping the expression ‘develop their economic relationship’ and investing in India may be one of the objects and purposes of the treaty and benefit should be given. However, considering the circumstances post MLI, it would be an aggressive position. Further, the same has to be interpreted keeping in sight the amended Article 13 and new Article 27A of I-M Treaty.

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[32] intending to eliminate double taxation with respect to 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)’

[33] The Government of the Republic of India and the Government of Mauritius, desiring to conclude a Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains and for the encouragement of mutual trade and investment.

[34] The Honourable Supreme Court in Azadi Bachao Andolan [2003] 263 ITR 706 has held that in developing countries treaty shopping is often regarded as a tax incentive to attract scarce foreign capital or technology. The countries are able to grant tax concessions exclusively to foreign investors over and above the domestic law provisions. In this respect, it does not differ much from other similar tax incentives such as tax holidays, grants etc.

Article 7 of MLI:

This article can be referred as core article of MLI because it starts with non-obstinate clause. In other words, what other provisions of CTA[35] may state, if the provision of Article 7 when translated into respective articles of CTA, then the benefit of a CTA shall be available only on satisfaction of the provisions contained in respective articles of CTA qua Article 7.

Article 7(1) deals with principal purpose test (PPT). It states that **notwithstanding any provisions of CTA, a benefit under CTA shall not be granted in respect of an item of income or capital 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 relevant provisions of CTA.**

As everyone is aware that India has opted for PPT and simplified limitation of benefits (SLOB) as an interim measure against implementation of detailed limitation of benefits (DLOB) by negotiating with each country. For the purposes of this article, we shall only deal with the test of PPT. The question now, is whether the structures, namely the investment vehicles would pass the test of PPT, especially, when a see-through test is applied would result in tax liability. Now, let us proceed to examine the same.

In other words, assuming that the 'transfer' in Article 13(4) of India-Mauritius DTAA would also cover the indirect transfer and accordingly, the taxing rights vests with Mauritius and such income would not be taxable in India. Such a benefit shall be extended to Tiger Global Holdings only if it can prove that obtaining such a benefit was not one of the principal purposes of any arrangement or transaction. The phrase 'principal purpose' is not defined in MLI. It has to be understood from an example from Action 6 Report:

R Co , a company resident of State R, is in the business of producing electronic devices and its business is expanding rapidly. It is now considering establishing a manufacturing plant in a developing country in order to benefit from lower manufacturing costs. After a preliminary review, possible locations in three different countries are identified. All three countries provide similar economic and political environments. After considering the fact that State S is the only one of these countries with which State R has a tax convention, the decision is made to build the plant in that state.

In this example, whilst the decision to invest in State S is taken in the light of the benefits provided by the State R-State S tax convention, it is clear that the principal purposes for making that investment and building the plant are related to the expansion of R Co's business and the lower manufacturing costs of that country. ***In this example, it cannot reasonably be considered that one of the principal purposes for building the plant is to obtain treaty benefits.*** *In addition, given that a general objective of tax conventions is to encourage cross-border investment, obtaining the benefits of the State R-State S convention for the investment in the plant built in State S is in accordance with the object and purpose of the provisions of that convention.*

[35] Covered Tax Agreement – when both the contracting jurisdictions notify their DTAA under MLI Convention, the same would be referred as CTA.

From the above example, it can be understood how subjective the PPT is going to be. It should not be lost out of sight, that the said example deals with set-up of manufacturing facility, wherein, in cases of set-up of investment vehicles, there will not be much of reasons to justify incorporation in another country for purpose of investing. Hence, there will be definitely tougher times for investment vehicles to justify their incorporation in a third country and 'better treaty network' may not be enough and the courts may rule that in case of investment vehicles, one of the principal purposes is undoubtedly the treaty benefits, especially in case of liabilities if 'see-through' is applied.

PPT vis-à-vis Columbia Court's decision in Starr International Company Inc:

The United States District Court of Columbia in Starr International Company Inc (for brevity 'Starr') had an occasion to deal with 'primary purpose' test while granting treaty benefits to Starr. Even though the said judgment deals with interpretation of LOB and not PPT provisions, nonetheless, we can understand how the tax department may see the principal purpose test.

The facts of the matter of Starr were that Starr was one of the largest shareholders of insurance giant AIG Inc. Starr was domiciled in Switzerland and when the AIG Inc has declared dividends, they have withheld tax on such pay-outs to Starr and followed up by Starr writing to competent authority to grant treaty benefit under discretionary relief. The competent authority rejected such a discretionary relief to Starr. Against such an order, Starr approached the Court. After examining, the detail history of Starr, right from its incorporation to recent movement to Switzerland has stated that Starr is not eligible for the discretionary relief. The Court noted that Starr has listed four jurisdictions for relocation and put a table for finalisation of the jurisdiction to which Starr intends to relocate. One of the criterions for arriving the decision is 'tax'. Hence, looking at such a table and 'tax' being taken into consideration, the Court stated that one of the primary purposes for Starr to relocate to Switzerland is tax and hence it should not be eligible for discretionary relief. Further, the court stated that the primary question should be not as to why Starr has chosen Switzerland over Ireland, but why Starr chose Switzerland over any other jurisdiction where it might have moved.

Hence, applying the above rationale, the tax authorities may ask, why Mauritius or Cayman Islands or any other tax heaven instead of any other jurisdiction and the investment vehicles should have a better reasons and justifications to substantiate the choice of jurisdiction.

Now, the investment vehicles may alternatively plead that the benefit of CTA may be granted in circumstances that granting such a benefit is in accordance with the object and purpose of relevant provisions of CTA. However, as detailed earlier, this would also be harder.

Position under GAAR:

Assuming that the investment structure gets through the PPT, it has to clear one more hurdle, which is in the form of GAAR before it can claim any benefit. Section 90 of ITA deals with powers of Central Government to enter into an agreement with Government of any country outside India for granting the relief from double taxation.

Section 90(2) states that where Central Government has entered into an agreement with Government of any country outside India for granting the relief or avoidance of double taxation, then, in relation to assessee to whom such an agreement applies, the provisions of ITA shall apply to the extent they are beneficial to him. In other words, a resident of contracting state can choose the provisions of domestic tax law or tax treaty whichever is beneficial to him.

Further, detailing, the investment vehicle can choose the PPT or GAAR[36] whichever is beneficial to him in light of Section 90(2) of ITA. This would have been the possibility if there is no Section 90(2A). Section 90(2A) has been inserted with effective from 1st April 2016 stating that notwithstanding anything contained in Section 90(2), the provisions of GAAR shall apply to the assessee even if such provisions are not beneficial to him.

In light of the specific restriction envisaged vide Section 90(2A), it becomes not possible for the investment structures to only satisfy PPT and leave GAAR. Hence, such resident has to satisfy both PPT and GAAR. The next question would be, whether GAAR is wider than PPT? Let us proceed to examine the same.

GAAR under the ITA states that notwithstanding to anything contained in the ITA, an arrangement entered by assesse may be declared to be an impermissible avoidance arrangement and the consequence in relation to tax arising therefrom may be determined accordingly. An impermissible avoidance arrangement[37] means an arrangement, the main purpose of which is to obtain tax benefit and it contains one of the four tainted elements.

When GAAR is juxtaposed with PPT, it is evident that whilst GAAR deals with 'main purpose' of an arrangement is to obtain benefit, PPT deals with 'one of the principal purposes'. Hence, the fight is between 'main purpose' vis-à-vis 'one of the principal purposes'. Hence, it would be evident that PPT is much wider than GAAR and an arrangement or transaction which normally gets through PPT should also normally go through GAAR except the tax authorities in India tend to see it differently. However, the burden of clearing both the tests is necessary.

Concluding Remarks:

The decision of courts on taxability in the hands of Tiger Global Holdings would be an interesting watch. It has to be waited and seen, whether the courts would follow the principals laid down in Vodafone International Holdings BV (supra) and Sanofi Pasteur Holdings SA (supra) or take a stock of recent developments across the globe (particularly the taxation in conduit arrangements) and deliver a different ruling. Whatever the courts may finally deliver, it definitely would be a learning exercise for all of us. Fingers Crossed!

[36] Because GAAR is forming part of domestic tax law
[37] Section 96 of ITA