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(Re)Navigating Treaties - MLI and PPT

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Foreword

The international tax landscape is undergoing one of the most transformative shifts in decades. As businesses expand across borders at an unprecedented pace, the global community is re-examining long-standing principles that determine how value is taxed and where rights are allocated. Transparency, substance, and fairness have emerged as the cornerstones of this new era—reshaping expectations not only for policymakers, but equally for enterprises operating in an increasingly interconnected world.

India is playing a central and influential role in this evolution. As one of the fastest-growing major economies, and a jurisdiction deeply engaged in global tax dialogue, India stands at the confluence of ambition and responsibility. Our treaty networks are being recalibrated, our domestic anti-avoidance frameworks continue to mature, and our engagement with multilateral initiatives reflects a clear commitment to a stable, equitable, and forward-looking international tax system. These shifts reinforce India's positioning as both a competitive investment destination and a constructive participant in global standard-setting.

Within this dynamic environment, taxpayers and advisors alike are navigating a more nuanced landscape—one where cross-border structuring requires deeper commercial alignment, greater evidencing of purpose, and a more holistic understanding of treaty objectives. The introduction of the Multilateral Instrument (MLI) and the Principal Purpose Test (PPT) marked a watershed moment in this journey. These changes signal a broader shift from form to substance, from box-ticking to intent, from isolated transactions to a holistic appreciation of business rationale.

This publication aims to distill these developments into a practical and insightful guide for businesses, investors, and the broader tax community. The aim is to equip readers with insights that not only clarify technical nuances but also illuminate the broader international tax narrative shaping business and policy choices today.

As India continues to strengthen its position on the global stage, the ability to anticipate and adapt to these shifts will define how enterprises participate in, and contribute to, the next phase of cross-border growth. We hope that this publication serves as a useful companion to that journey.

Warm regards,

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Introduction to International Tax Treaties

In today's globally integrated economy, cross-border investment has become a defining feature of business expansion. Against this backdrop, tax treaties play a foundational role: they shape how jurisdictions share taxing rights, influence capital flows, and provide a measure of predictability to multinational enterprises navigating diverse tax systems.

At their core, tax treaties determine which country has the right to tax various categories of income such as business profits, dividends, interest, royalties, and capital gains. By doing so, they prevent the same income from being taxed twice - once in the country of source and again in the country of residence.

Broadly, tax treaties serve to:

- Eliminate double taxation by clearly defining which country can tax a given income.
- In case of taxation by the source country, provide mechanism for credit of such taxes in the home country.
- Ensure equitable allocation of taxing rights between contracting states.
- Provide certainty and stability to facilitate long-term cross-border trade and investment.

In addition, treaties often reduce withholding taxes on cross-border payments, thereby improving post-tax returns and making international investments more efficient. They also strengthen investor confidence through non-discrimination provisions and dispute resolution mechanisms such as the Mutual Agreement Procedure (MAP), ensuring fairness, predictability, and consistency in tax administration.

While these agreements continue to anchor international tax architecture, their effective operation depends on how well they respond to evolving business models and domestic tax policy objectives. As global commerce becomes increasingly digital and mobile, the interpretation and administration of treaty provisions have taken on renewed importance for both taxpayers and tax authorities.

Challenges with traditional treaty frameworks

International tax treaties were drafted in an era when commerce depended on physical presence and economic activity was relatively easy to trace. Over time, business models have shifted: value is now often derived from intangibles, digital interfaces, and integrated global supply chains. This evolution has strained traditional treaty concepts and triggered divergent views on the scope of key provisions.

The digitalization of business, in particular, has tested long-standing principles for determining nexus and profit attribution. Older treaties, built around the idea of traditional brick-and-mortar business models, do not always address scenarios where significant economic participation occurs without physical presence. This has resulted in increased interpretational disputes, audit challenges, and litigation. Efforts to modernize treaties through tools like the Multilateral Instrument (MLI) reflect the global push to ensure that treaty outcomes remain aligned with value creation. At the same time, these developments have introduced new layers of compliance and subjectivity in assessing treaty eligibility.

A parallel concern has emerged around how treaty networks are accessed. Over the years, investments have sometimes been routed through intermediaries primarily to take advantage of favourable treaty provisions, even when commercial substance in those jurisdictions was limited. Such practices have amplified pressures on tax administration and prompted the international community to recalibrate treaty entitlement rules. This need to safeguard the integrity of treaty benefits has been a central force behind the shift towards stronger anti-abuse standards globally.

Multilateral Instrument (MLI): An Overview

The years following the 2008 global financial crisis marked a turning point in the international tax landscape. As governments confronted shrinking tax bases and rising public scrutiny, it became evident that traditional tax rules were no longer equipped for a world defined by intangible value, digital scale, and globally integrated business models. The ability of multinational groups to structure investments through favourable jurisdictions, shift profits using hybrid arrangements, or exploit gaps between domestic laws and treaty frameworks intensified concerns of base erosion.

Against this backdrop, the G20 mandated OECD to launch the Base Erosion and Profit Shifting (BEPS) Project. The 2015 release of the 15 BEPS Action Plans provided the first globally coordinated blueprint to realign taxing rights with economic substance. Yet, translating these recommendations into practice presented a significant challenge: with more than 3,000 bilateral tax treaties in force globally, implementing treaty-related BEPS measures through conventional renegotiation was neither practical nor timely.

It is in response to this implementation gap that the Multilateral Instrument (MLI) was conceived—an unprecedented mechanism enabling countries to update treaty networks in a synchronized, efficient manner, without reopening every treaty at the negotiating table. The MLI now occupies a central place in modern treaty policy, allowing jurisdictions to strengthen source taxation, curb treaty abuse, and modernize their agreements through a single multilateral framework.

Understanding the MLI – A Modern Treaty Overlay

The MLI does not replace existing bilateral treaties; rather, it operates alongside them by modifying their application in situ. The underlying text of the bilateral treaty remains unchanged, while the provisions of the MLI apply as an overlay, altering how specific articles are to be read and applied where both treaty partners have adopted matching positions. Once both countries notify a treaty as a Covered Tax Agreement (CTA) and align their positions on specific MLI provisions, the treaty is automatically updated to the extent provisions selected by the countries match. This approach preserves the bilateral character of treaties while delivering multilateral outcomes.

The operational design of the MLI balances three objectives:

Since its signing in Paris in 2017, the MLI has achieved broad global acceptance, with about 107 jurisdictions having signed, and 90 countries having brought the instrument into force as of January 2026[1].

1. Document titled "Signatories and Parties to the Multilateral Convention to Implement Tax Treaty related measures to prevent base erosion and profit shifting - Status as of 12 January 2026" published by OECD

Categories of MLI Provisions

Category	Description	Provision
Minimum Standards	Mandatory provisions designed to combat treaty abuse and strengthen dispute resolution. Jurisdictions cannot opt out, except in limited circumstances.	Revised Treaty Preamble, Prevention of Treaty abuse including Principal Purpose Test, Mutual Agreement Procedure ('MAP')
Optional Provisions	Countries may selectively adopt additional measures that expand taxing rights or modernise treaty concepts.	Hybrid Mismatch Rules, Dividends, Capital Gains, Avoidance of PE status, Arbitration, etc.
Reservations	Jurisdictions may opt out of optional provisions, where the MLI framework explicitly permits such reservations.	Article 28 (Reservations) refers to the specific built-in reservation clauses within each optional article allowing full or partial opt-out

How the MLI operates in practice

At a conceptual level, the MLI overlays existing treaty provisions using the principle of lex posterior - the later rule overrides the earlier one, to the extent both countries have agreed to apply it.

A jurisdiction must first ratify the MLI and deposit its instrument with the OECD. After that, the MLI modifies a treaty only when two requirements are met:

1. Both jurisdictions identify the treaty as a CTA, and
2. Both take matching positions on the MLI articles relevant to that treaty.

The result is reflected in a Synthesized Text, a reader-friendly composite that integrates the MLI language with the existing treaty. While helpful as an interpretive aid, the synthesised text is not a standalone legal document—the legal force lies in the original CTA read together with the applicable MLI provisions.

Key terms

- **Covered Tax Agreement (CTA):** A bilateral tax treaty that both contracting jurisdictions have explicitly designated (by notification to the OECD) to be modified under the MLI.
- **MLI position:** The set of choices, reservations, notifications, and options that a jurisdiction declares under the MLI in respect of covered treaties. For each CTA, the MLI will modify treaty provisions only where there is a bilateral "match" - i.e. both jurisdictions accept the relevant MLI provision.
- **Synthesized Text:** A working or composite text that integrates the original CTA provisions and the modifications introduced by the MLI, reflecting how the treaty would operate under the matched MLI provisions. It is not a standalone legal instrument; rather, it is a convenience tool or interpretative aid. For actual legal purposes, one must read the original CTA and the relevant MLI articles (as accepted by both parties) in tandem, considering any reservations, compatibility clauses, or transitional rules

A jurisdiction must first ratify the MLI and deposit its instrument with the OECD.

With these foundational mechanics in place, the internal architecture of the MLI can be better appreciated.

Broad structure of MLI

Once the operational principles of the MLI are understood, its internal architecture becomes clearer. Each article of the MLI follows a consistent and deliberate structure - one that allows it to "plug into" existing treaties without disturbing their core framework. Rather than rewriting treaty text, the MLI introduces modular provisions that apply only where countries have agreed to their inclusion. The predictable layout of each MLI article is therefore essential to understanding how it interacts with bilateral treaties in practice. The broad structure may be viewed as comprising the following elements:

Sr. No.	Structure	Description
1.	Title and Preamble	States the purpose of the treaty within the context of the MLI - *"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),"*.
2.	Scope and Definitions	Defines the specific terms used and outlines the scope
3.	Substantive Provisions	Details the core rules and obligations that the contracting jurisdictions agree to implement. The provisions may address issues such as hybrid mismatches, treaty abuse, etc.
4.	Compatibility Clause	Clarifies how the provisions interact with existing provisions of bilateral treaties (refer section below)
5.	Optional Provisions and Reservations	Jurisdictions can choose optional provisions or make reservations against specific provisions of the MLI
6.	Notification Requirements	Jurisdictions to notify each other of their choices and reservations
7.	Entry into Force and Application	Entry into force and the application of its provisions, specifying when the modifications become effective (refer example below)

Compatibility clauses – The MLI's Integration Engine

A central feature of the MLI is the way each of its articles interacts with existing provisions of a bilateral treaty. Since the MLI does not rewrite entire treaties, but instead modifies them selectively, every MLI article contains a compatibility clause that clarifies how and when the MLI provision will apply to a CTA. These clauses explain whether the MLI replaces a treaty article, supplements it, applies only if a corresponding provision already exists, or applies only where the treaty is silent. Understanding these compatibility formulations is essential to determining the practical impact of each MLI article on a CTA.

Type	When applicable	Impact
"In place of"	There is an existing provision in the CTA	Existing CTA provision is replaced
"applies to" or "modifies"	Applies only when there is an existing provision in the CTA	Application of an existing provision is amended without replacing it
"in absence of"	The provision is absent in the CTA	The provision is added to the CTA
"in place of" or "in absence of"	The provision is present or absent in the CTA	The existing provision is replaced/ superseded or MLI provision is added to CTA (in absence of existing provision)

Entry into Force and Entry into Effect

Entry into force (qua each country): 1st day of the month after expiry of 3 months from the date of deposit of ratified copy. The MLI applies only once both treaty partners have ratified and listed that treaty as a CTA.

Relevant date – Since the participating jurisdictions can differ in the dates on which they deposit the ratification instrument, the relevant date for Entry into Effect will be the latter of the dates when MLI enters into force for both the participating jurisdictions

Entry into effect (qua each CTA):

Type of tax	Entry into effect
Withholding taxes	1st day of the taxable period that begins on or after the "relevant date"
Other taxes	Taxable period that begins on or after expiry of six calendar months from the "relevant date"

Illustration:

India deposited its instrument of ratification on 25 June 2019, and the MLI entered into force for India on 1 October 2019. Singapore deposited its instrument on 21 December 2018, with entry into force on 1 April 2019. The relevant date becomes latter of the two i.e. 1 October 2019

For the India–Singapore treaty, this meant:

India's perspective

- For withholding taxes (like dividends, interest, royalties), the MLI applied from 1 April 2020 (i.e., the first day of the next taxable year).
- For other income taxes (like business profits and capital gains), the MLI applied to taxable periods beginning on or after 1 April 2020 (India's next taxable year, starting six months after the relevant date).

Singapore's perspective

- For withholding taxes: 1 January 2020
- For other income taxes: 1 April 2020

India's Position on MLI

India's MLI position is a blend of broad acceptance and selective reservations

Article No.	Article Name / Description	India's Position
3	Transparent entities	India has exercised a reservation against the application of Article 3
4	Dual Resident Entities	India has adopted the approach under Article 4 of the MLI, pursuant to which cases of dual residence of entities are to be resolved through the Mutual Agreement Procedure (MAP).
5	Application of Methods for Elimination of Double Taxation	India follows the credit method: tax paid in the treaty partner country is allowed as a credit against Indian tax, so the same income is not taxed twice
6	Purpose of a Covered Tax Agreement	Being a minimum standard, the Preamble in accordance with Article 6 would stand modified for all notified Covered Tax Agreements.
7	Prevention of Treaty Abuse	India has opted for the Principal Purpose Test (PPT) and the Simplified Limitation of Benefits (SLOB). PPT being the minimum standard will apply to all its CTAs. India has accepted to apply PPT as an interim measure and intends where possible to adopt LOB provision, in addition or replacement of PPT, through bilateral negotiations.
8	Dividend Transfer Transactions	India has opted to apply such provision. Access to India's reduced treaty withholding tax rate on dividends is subject to a 365-day minimum holding period by the recipient company
9	Capital Gains from Alienation of Shares or Interests of Entities Deriving their Value Principally from Immovable Property	India has opted to apply a 365-day lookback period together with the requirement that shares derive more than 50% of their value from immovable property situated in the source State.
10	Anti-abuse Rule for Permanent Establishments Situated in Third Jurisdictions	India has not expressly notified any reservation and hence the same has been adopted
11	Application of Tax Agreements to Restrict a Party's Right to Tax its Own Residents	India has not expressly notified any reservation and hence the same has been adopted
12	Artificial Avoidance of Permanent Establishment (PE) Status through Commissionaire Arrangements and Similar Strategies	Article 12 expands the PE definition to cover situations where a person habitually concludes contracts or plays a principal role leading to their conclusion on behalf of an enterprise. India has adopted this provision to counter the artificial avoidance of PE status.

Article No.	Article Name / Description	India's Position
13	Artificial Avoidance of Permanent Establishment Status through the Specific Activity Exemptions	India has opted to narrow the PE exclusions, specific-activity exemptions now apply only if the activity is preparatory or auxiliary, thereby expanding PE exposure.
14	Splitting-up of Contracts	India has not expressly notified any reservation and hence the same has been adopted
15	Definition of a Person Closely Related to an Enterprise	India has not expressly notified any reservation and hence the same has been adopted
16	Mutual Agreement Procedure	While India permits access to the Mutual Agreement Procedure (MAP), it has reserved against adopting Mandatory Binding Arbitration (Part VI of the MLI)
17	Corresponding Adjustments	India has opted to apply the provisions except under CTAs where similar provisions already exist
18-26	Arbitration (Part IV)	India has chosen not to apply Mandatory Arbitration and related provisions for dispute resolution and prefers resolving disputes through the MAP
27-34	Other provisions including Entry into Force	For India, the MLI has entered into force on 1 October 2019. India has expressed its reservations for the relevant provisions to apply / not apply / apply with reservations as envisaged under Article 28.
35	Entry into Effect	For India, the MLI has entered into effect on 1 April 2020. Further, India has chosen to substitute "calendar year" with "taxable period".
36	Entry into Effect of Part VI	India has opted out of Part VI (Mandatory Arbitration)

Principal Purpose Test: Design and Key Mechanics

The OECD's Action 6 Report outlines three broad approaches for countering treaty abuse.

PPT Rule

Stand-alone general anti-avoidance rule based on the purpose of an arrangement or transaction

LOB Rule

Rules based on objective criteria such as legal nature, ownership in, and general activities of residents of Contracting States

Can be (i) simplified or (ii) detailed

Through **Article 7**, MLI allows to opt for any of the following alternatives:

- PPT only (default option)
- PPT + LOB (Detailed or simplified)
- Detailed LOB + mutually negotiated anti-conduit Rule

The Principal Purpose Test (PPT) is the central anti-abuse rule introduced through the MLI. It represents a decisive shift in treaty policy: from form-based entitlement toward a purpose-driven assessment of whether treaty benefits are legitimately earned. At its core, the PPT is designed to ensure that treaty relief follows commercial substance — not merely tax-efficient structuring.

Article 7(1) of the MLI on prevention of treaty abuse is reproduced below:

Notwithstanding any provisions of a Covered Tax Agreement, a benefit under the Covered Tax Agreement ***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 Covered Tax Agreement.*

This formulation blends a purpose-based test with an object-and-purpose safeguard, creating a balanced but robust framework

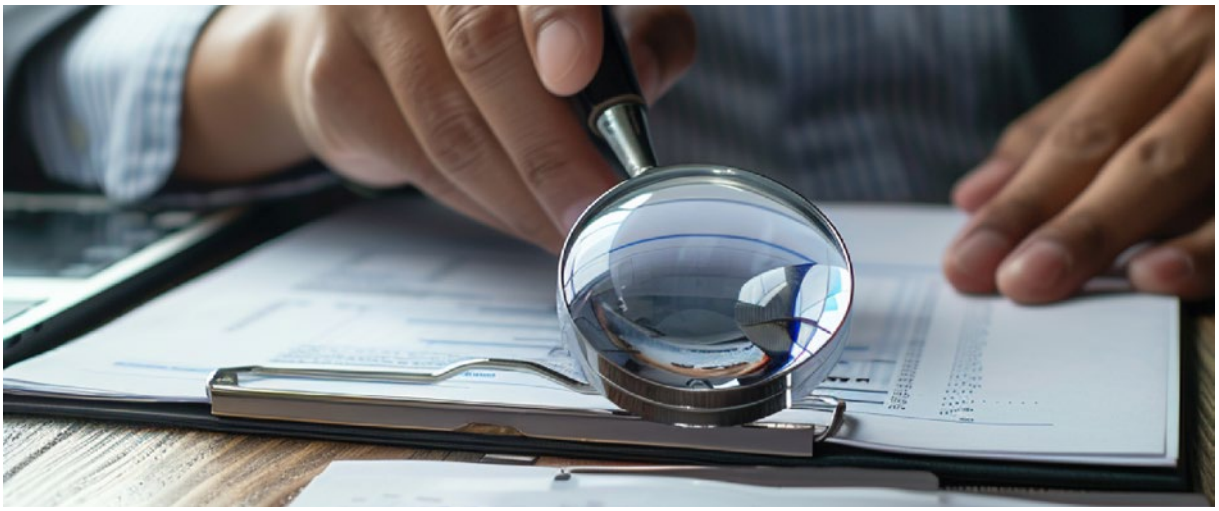
Understanding the PPT: Two Tests Working Together

Test	Description
Reasonable purpose	• A treaty benefit may be denied where, after evaluating all relevant facts and circumstances, it is **reasonable to conclude** that obtaining that benefit was **one of the principal purposes** of the arrangement or transaction • The test is aimed at addressing treaty shopping and other forms of treaty-driven structuring
Object and purpose	• The object and purpose carve out observes that a benefit may still be granted if it is demonstrated that such benefit is in line with the object and purpose of the relevant treaty provision

Evaluating the PPT: A Practical Framework for Taxpayers

The following four-step diagnostic approach offers a business-friendly way to assess PPT exposure:

As treaty abuse rules tighten, a fundamental question arises: How far must a taxpayer go to demonstrate that a transaction has a "reasonable principal purpose" beyond accessing treaty benefits?



The Boundary Question: How Much Substance is Enough?

The PPT looks at specific transactions or income streams and examines whether obtaining a treaty benefit was one of their main purposes. It should not require conclusive proof; a reasonable basis for such a conclusion may be considered sufficient.

This raises a deeper interpretational challenge:

- How should "reasonableness" be judged: what is *fair, sensible*, and *logically supported* by evidence?
- If multiple purposes exist, how does one weigh commercial considerations against tax outcomes?
- Should a transaction be questioned merely because it is incapable of being explained except for the tax benefit, or must the authority objectively evaluate competing explanations?
- Conversely, when does the presence of a treaty benefit become so significant that it overshadows other purposes, even if not the sole or dominant intention?

Where should the line be drawn between a commercially justified arrangement that incidentally enjoys treaty relief, and one where the treaty benefit is so integral that it becomes "one of the principal purposes"?

This remains one of the most nuanced and judgement-laden areas of the PPT, inviting continued debate among practitioners, administrators, and courts alike.

Treaties that already contain a PPT may either include broad-based tests applying to all treaty benefits or narrowly focused provisions applicable only to specified articles, such as capital gains, dividends, interest or royalties. Under Article 7 of the MLI, the reference to denial of "all or part of the benefits" ensures that such limited provisions are substituted with the comprehensive PPT provided in the MLI. Further, where treaties currently employ expressions such as "main purpose" or "primary purpose," these will be replaced by the MLI formulation "one of the principal purposes," lowering the threshold for invoking the test.

Consequently, for the denial of treaty relief under the PPT, it is not necessary to establish that obtaining the benefit was the sole or dominant purpose of the arrangement. It is sufficient if one of the principal purposes of the transaction was to secure such a benefit.

The PPT supplements or replaces existing general anti-abuse clauses in CTAs, ensuring a consistent and treaty-wide minimum standard against inappropriate access to treaty relief.

The above can be understood with the help of the following examples provided by the OECD:

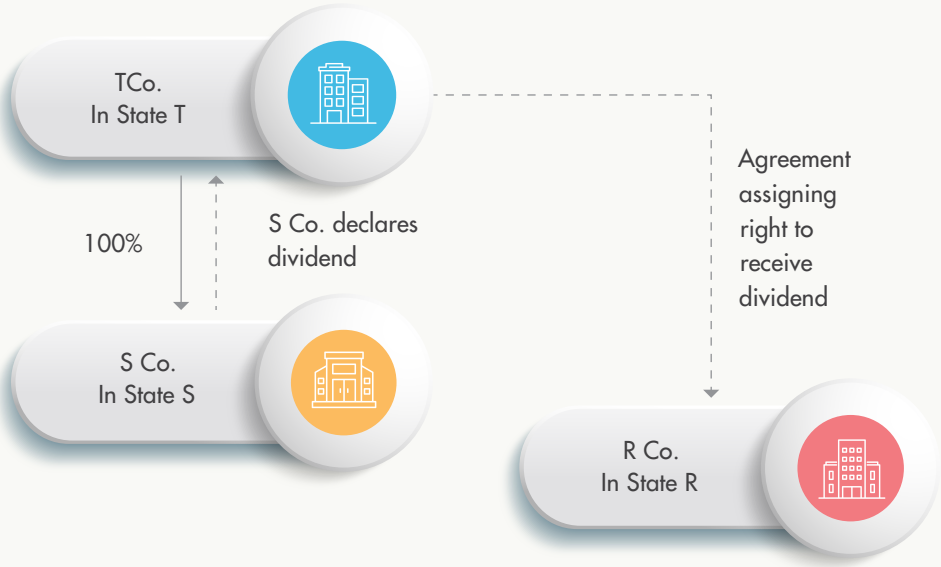
Example 1 – Denial of Treaty Benefit under PPT

Facts

- T Co, resident of State T, holds shares in S Co (State S). In the absence of a T–S treaty, dividends paid by S Co to T Co attract 25% WHT under State S domestic law.
- Under the R–S tax treaty, dividends paid by S Co to a resident of State R are exempt from WHT, provided the dividends are beneficially owned by that resident.
- T Co enters into an agreement with R Co, an independent financial institution in State R, assigning to R Co the right to receive dividends that have already been declared by S Co but are not yet paid.

OECD View

- In the absence of other facts and circumstances showing otherwise, it would be reasonable to conclude that one of the principal purposes for the arrangement under which T Co assigned the right to the payment of dividends to R Co was for R Co to obtain the benefit of the exemption from source taxation of dividends provided for by the State R-State S tax convention and it would be contrary to the object and purpose of the tax convention to grant the benefit of that exemption under this treaty-shopping arrangement.



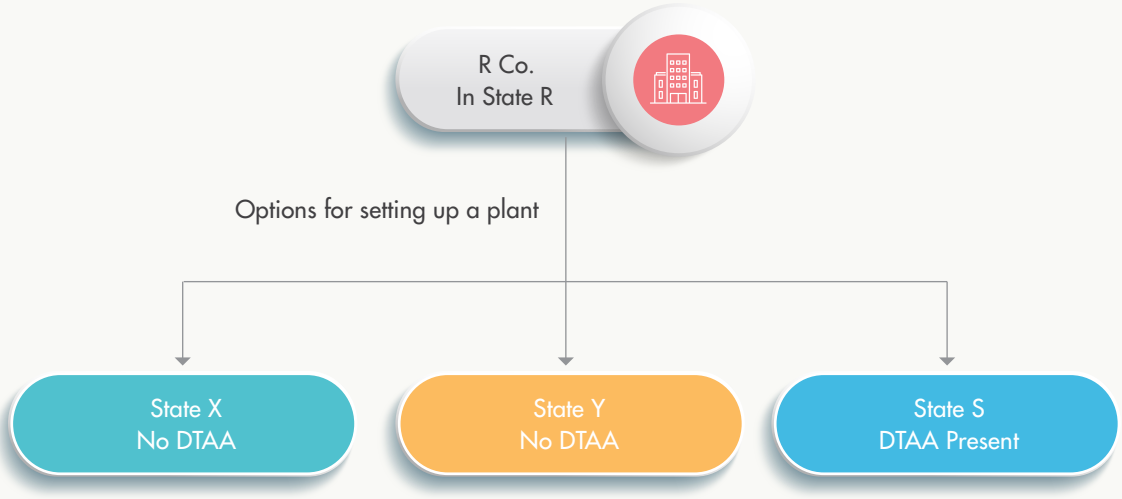
Example 2 – Grant of Treaty Benefit under PPT

Facts

- R Co has three jurisdictions to choose to set up a manufacturing plant in a developing country on account of lower manufacturing costs
- All the three jurisdictions are politically and economically comparable. However, only State S has a tax treaty with State R
- Thus, R Co chooses State S from among the stated options for setting up the plant

OECD View

- 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.



Illustrative Application of the PPT: Ownership Threshold and Dividend Withholding

Facts

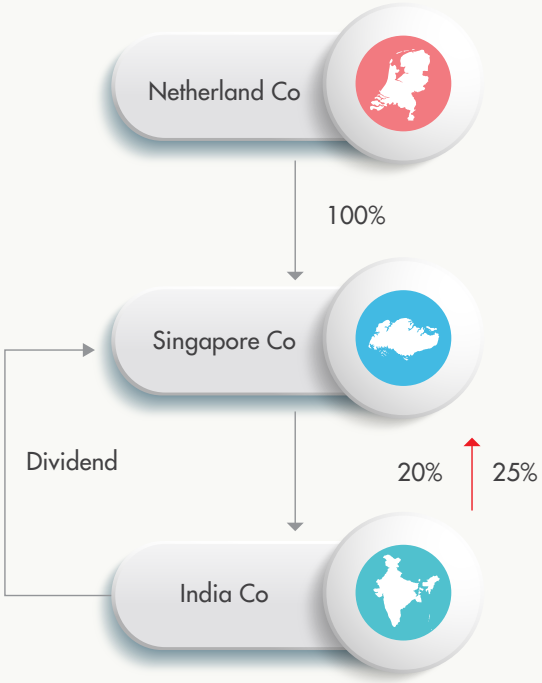
- A Netherlands parent company holds its Indian investment through its Singapore subsidiary
- During the year, the Singapore company increases its shareholding in the Indian company from 20% to 25%.
- Under Article 10 of the India–Singapore DTAA, the dividend withholding tax rate is:
  - 10% where the beneficial owner is a company holding at least 25% of the equity;
  - 15% in all other cases.

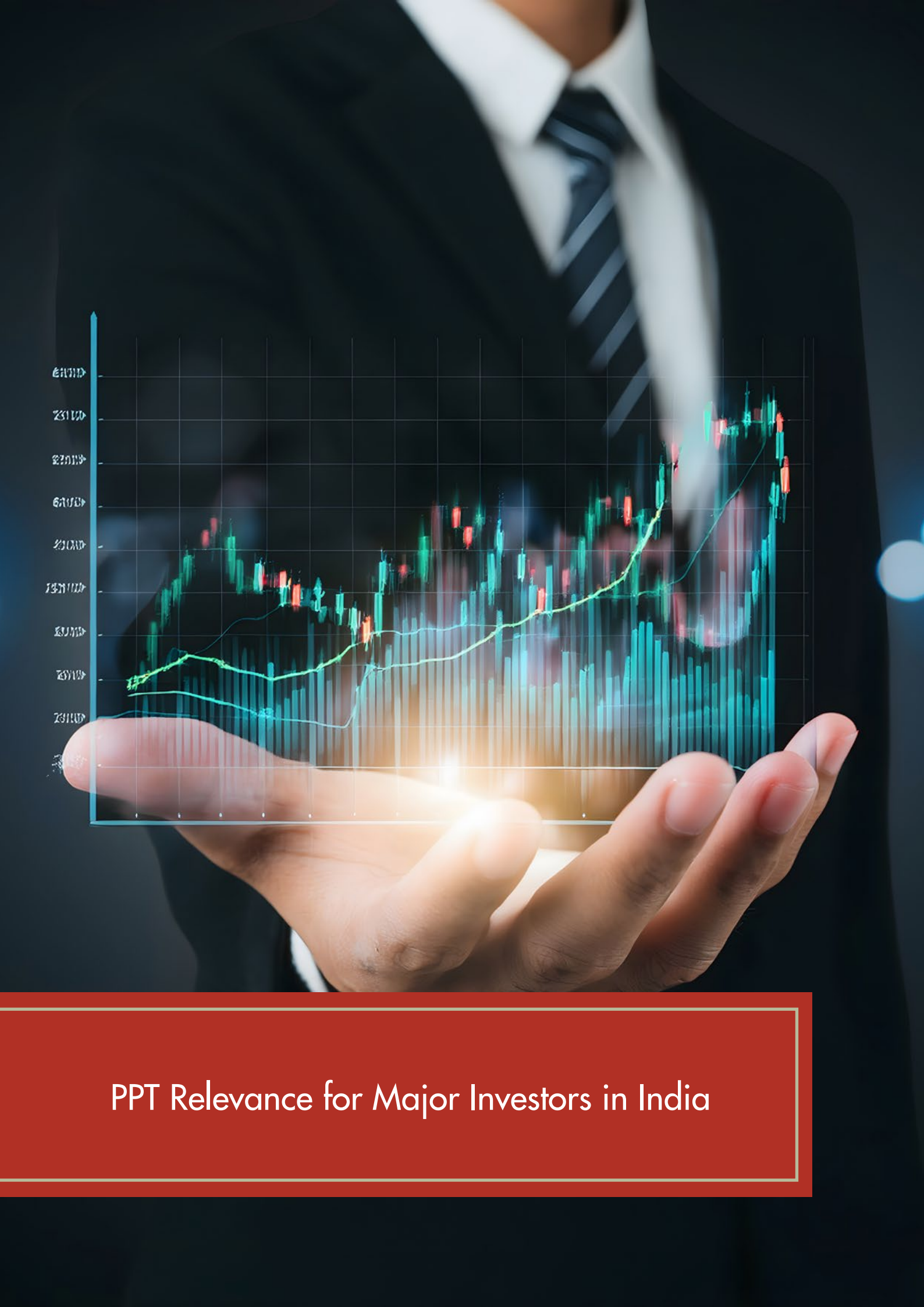
Issues for consideration

- Whether the PPT could be invoked in respect of the additional 5% acquisition?
- Whether the increase in shareholding could be viewed as undertaken solely to access the lower treaty rate?

OECD View

- According to the OECD Commentary (on a comparable example), where a taxpayer genuinely increases its participation in a company in order to meet the ownership threshold prescribed in the treaty, PPT should not be triggered.
- Accordingly, if the increase from 20% to 25% reflects a bona fide commercial decision, the reduced 10% WHT rate under the India–Singapore treaty should remain available.





PPT Relevance for Major Investors in India

India's notifications mean that treaties with countries such as Singapore, the Netherlands, Cyprus, and Luxembourg, traditional investment hubs into India, are now subject to the PPT, requiring substance tests for treaty eligibility.

However, the MLI does not cover noteworthy treaties with the USA, Germany, and China and the same shall be updated bilaterally. A summary of the emerging position is as under:

Treaty Partner	MLI Applicable?	PPT Applicable?	LOB applicable?	Current Position
Mauritius	x	✓	✓	Refer section 4.2 below. LOB applies only to capital gains.
USA	x	x	✓	USA is not a signatory to the MLI – No impact of PPT
Singapore	✓	✓	✓	LOB applies only on capital gains
France	✓	✓	x	Only PPT applies
Netherlands	✓	✓	x	Only PPT applies
Germany	x	x	x	India's treaty is not a CTA
China	x	✓	x	Only PPT applies (Refer Note 1)
Cyprus	✓	✓	x	Only PPT applies
Luxembourg	✓	✓	x	Only PPT applies

Note 1 – The India–China Tax Treaty is not covered by the MLI, as India has not notified it as a CTA. BEPS-aligned changes were instead implemented through a bilateral protocol signed on 26 November 2018, rather than through the MLI framework.

Protocol (2024) to India Mauritius Tax Treaty

For decades, India's treaty with Mauritius has served as a cornerstone of inbound investment, especially for private equity and portfolio flows. Its earlier framework—providing exemption from Indian capital-gains tax—made Mauritius a preferred jurisdiction for investors seeking exposure to India's growth story.

This position began to evolve in 2016, when the two countries agreed that capital gains on shares acquired after 1 April 2017 would be taxable in India, while pre-2017 holdings would remain *grandfathered*. That amendment reflected India's first step toward curbing treaty-shopping of Mauritius treaty and aligning with global anti-avoidance norms.

Both the countries had not notified the tax treaty as a CTA and had agreed to bilaterally amend the tax treaty. In March 2024, India and Mauritius signed a Protocol to bring the treaty in line with BEPS Action 6 (Prevention of Treaty Abuse) standards as follows:

- **Revised Preamble:** The new language clarifies that the purpose of the treaty is to eliminate double taxation *without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including treaty-shopping arrangements*. This subtle but meaningful change replaces earlier language that referred to "encouragement of mutual trade and investment," shifting the emphasis from incentive to integrity.
- **Introduction of LOB / PPT Clause:** Under this rule, treaty relief can be denied where obtaining that relief was one of the principal purposes of a transaction or arrangement, unless granting it would be consistent with the treaty's object and purpose.

Once the domestic legislative procedures of both countries are met, the Protocol shall be notified and made effective. For investors, there are several practical questions: raised such as when exactly would the new provisions apply, and would they in any way disturb the long-standing grandfathering protection for pre-2017 investments?

Prospective Applicability

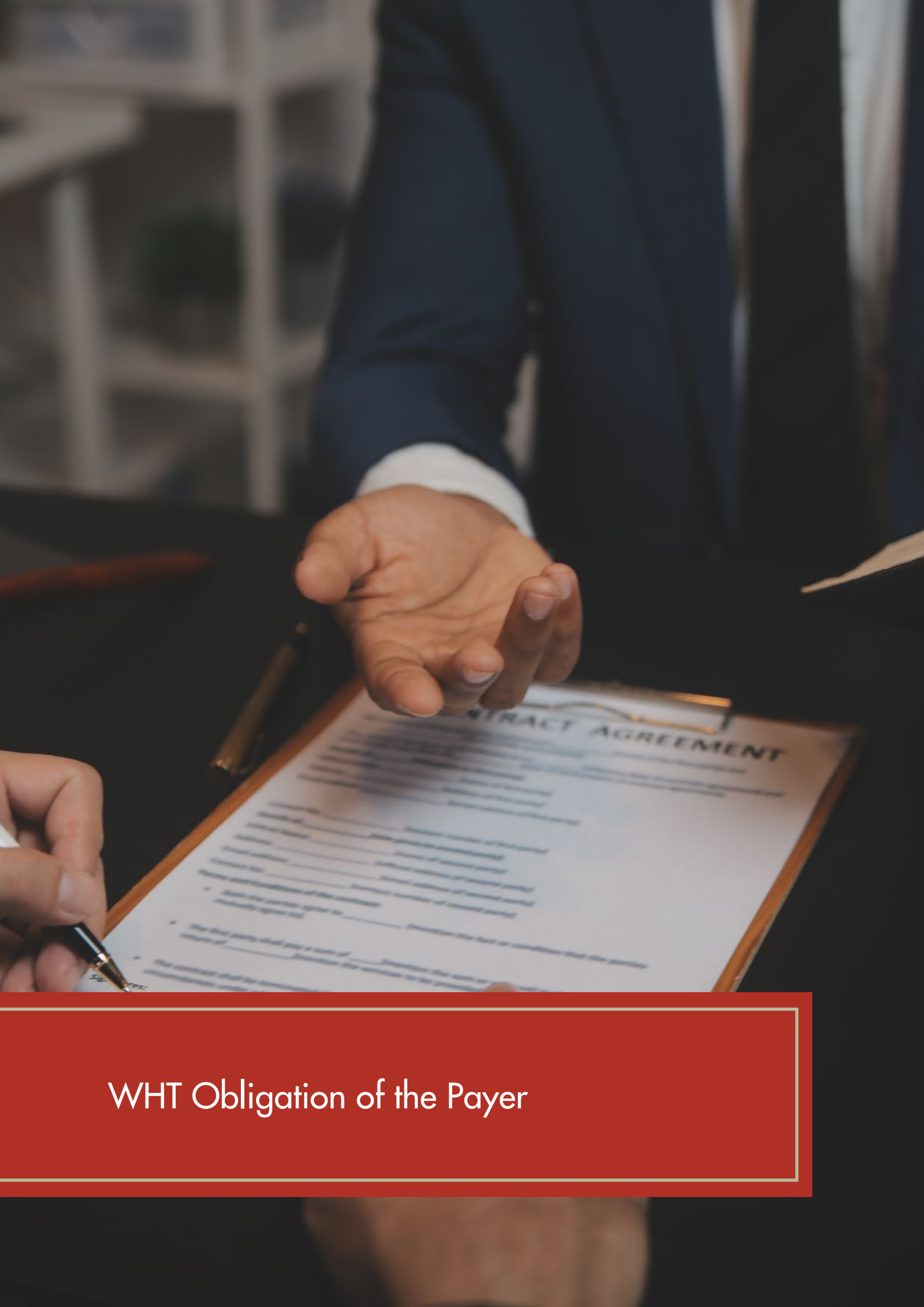
Recognizing these concerns, the Central Board of Direct Taxes (CBDT) issued Circular No. 01/2025 on 21 January 2025 confirming that the PPT provisions would apply prospectively. Broadly, the Circular clarifies that PPT provisions are to be applied prospectively from (i) the date of entry into force of the treaty/amending protocol whereby PPT was introduced pursuant to bilateral negotiations; or (ii) the effective date of provisions introducing PPT into the treaty through Multilateral Instrument (MLI).

However, the critical aspect that arises is whether the anti-abuse standard could affect structures or arrangements put in place before the PPT became operational. Conceptually, once a Covered Tax Agreement (CTA) is modified by the MLI or a bilateral protocol, the PPT applies to all income that accrues after the date on which the modified treaty becomes effective, even if the underlying transaction was executed or structure was created earlier. In this sense, the PPT can influence future tax outcomes of historical arrangements, because it tests the purpose of the arrangement in relation to the income being claimed, not the date on which the arrangement was executed. Unlike General Anti Abuse Rules (GAAR), the PPT does not contain grandfathering provisions.

Thus, the PPT cannot disturb completed assessments or tax positions relating to income that accrued before the PPT became operational. However, once effective, the PPT may still be applied to future income streams arising from pre-existing structures.

Interplay of PPT with Treaty Grandfathering Provisions

Further, the CBDT Circular also clarifies that grandfathering benefit with reference to capital gains arising from transfer of shares of an Indian company by treaty residents of Mauritius, Singapore and Cyprus in respect of shares acquired prior to 1 April 2017 will continue to be grandfathered and will be outside the purview of PPT.



WHT Obligation of the Payer

The introduction of the PPT has sharpened focus on how treaty benefits are applied at the point of withholding. Where reduced treaty rates are claimed on payments such as dividends, interest, or royalties, the PPT is relevant to the determination of treaty eligibility at source, and not merely at a later stage of review or dispute.

At the same time, the PPT presents practical challenges from the payer's perspective. The test requires an assessment of whether securing a treaty benefit was one of the principal purposes of an arrangement: an inherently fact-intensive enquiry that often turns on commercial considerations and motivations lying largely within the non-resident recipient's knowledge. This necessarily constrains the extent to which a payer can meaningfully assess purpose at the time of payment.

In practice, this places the payer's role within defined and pragmatic bounds. While access to a reduced treaty rate remains contingent on the recipient satisfying the PPT, payers are generally expected to apply treaty benefits based on reasonable diligence and contemporaneous information. This typically involves verifying treaty residence, obtaining prescribed documentation (such as a valid Tax Residency Certificate, Form 10F, and beneficial ownership confirmations), and ensuring that the transaction reflects an identifiable commercial rationale.

Where questions arise as to whether a structure or transaction was principally tax-driven, such issues may not be conclusively addressed at the withholding stage. In this regard, the Bombay High Court's decision in *Indostar Capital*[2] observed that determinations made at the stage of withholding do not result in a final resolution of issues relating to tax liability or the character of the underlying transaction. At the same time, the decision does not prevent tax authorities from acting at the withholding stage where there is sufficient *prima facie* material to indicate that a transaction lacks substance.

This leaves an open question for businesses and payers: how far are parties responsible for withholding tax expected to factor in the PPT when applying treaty rates, particularly in situations where they may not be aware of the commercial purpose behind an arrangement or have access to the full facts at the time of payment?

How this question is addressed in practice will have a direct bearing on withholding approaches and risk management, especially in jurisdictions such as India where guidance on the application of the PPT at the withholding stage continues to evolve.

2. *Indostar Capital v. ACIT (Writ Petition No. 3296 of 2018) (Bombay High Court)*

Interplay of PPT with Domestic / Treaty Anti-Abuse Rules

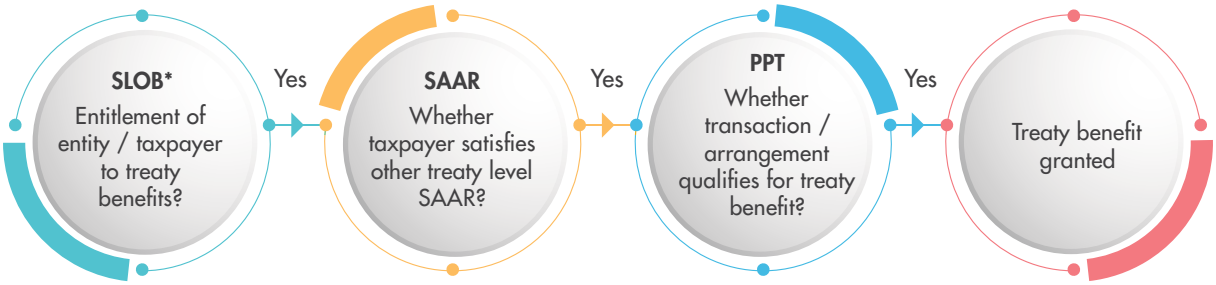
As global tax frameworks continue to evolve, countries are converging on a common principle: tax benefits must be rooted in commercial reality rather than legal form. In India, this principle is reflected in a layered anti-avoidance architecture comprising the Principal Purpose Test (PPT) at the treaty level; the General Anti-Abuse Rule (GAAR) under domestic law and Specific Anti-Abuse Rules (SAARs) under domestic law and tax treaties; as well as targeted treaty-based safeguards, including Limitation of Benefits (LOB) provisions.

The interpretation and application of anti-abuse provisions often depend on the specific facts and circumstances of each arrangement, and the varying scope of such measures further adds to the complexity.

Framework	Operates through	Trigger	What it addresses
PPT	Tax treaties (via MLI)	If *one of the principal purposes* of an arrangement is to obtain a treaty benefit inconsistent with the treaty's object and purpose	Prevents treaty shopping and unintended treaty benefit
GAAR	Domestic tax law (Income-tax Act, 1961)	If the *main purpose* of an arrangement is to obtain a tax benefit and it lacks commercial substance	Prevents aggressive domestic or cross-border avoidance
SAAR	Specific provisions built into tax treaties and domestic law	Pre-defined anti-abuse triggers	Targets specific, recurring forms of tax avoidance
LOB	Individual treaties	Failure to meet defined ownership, expenditure or activity conditions	Provides a mechanical gatekeeper for treaty eligibility

This combination may appear complex, but the underlying philosophy is coherent. Each layer operates at a different point in the tax system - together ensuring that while legitimate cross-border investment enjoys certainty, arrangements lacking substance do not.

A question that may arise as to whether these provisions might overlap or conflict. In practice, however, India's framework has evolved into a hierarchy of application rather than a competition for control:



- If the answer to any of the above is "No", treaty benefits will not be granted
- Domestic SAAR / GAAR may be invoked to re-characterise or re-attribute income upon fulfilment of specified conditions

** The simplified Limitation of Benefits (SLOB) provision acts as an initial screening step, assessing whether the entity is broadly eligible for treaty benefits based on objective criteria, before more detailed anti-abuse tests are applied.*

Interplay between PPT and GAAR

GAAR has been made effective from 1 April 2017 with certain grandfathering provisions.

The PPT under the MLI addresses treaty-level abuse, while GAAR operates at the domestic level, each targeting tax avoidance in its respective domain. The key distinctions are summarized as under:

Particulars	Domestic GAAR	Principal Purpose Test (PPT)
Trigger condition	Applies when the main purpose of an arrangement is to obtain a tax benefit or when any tainted element tests are satisfied.	Applies when one of the principal purposes of an arrangement or transaction is to obtain a treaty benefit, and granting such benefit would be inconsistent with the object and purpose of the treaty.
Scope of consequence	May lead to recharacterization of transactions, reallocation of income, or denial of treaty benefits.	Limited to denial of treaty benefits.
Onus of proof	Primarily on the tax authority.	Primarily on the tax authority, but includes a rebuttal presumption allowing the taxpayer to demonstrate consistency with treaty purpose.
Analytical approach	Involves a counterfactual analysis — assessing how the transaction would have been structured in the absence of a tax motive.	No counterfactual analysis may be required.
Administrative safeguards	Subject to Approving Panel review before invocation.	No standardized mechanism; administration left to each jurisdiction's discretion.
Threshold / De minimis	Includes a de minimis threshold to exclude small cases.	No de minimis threshold.
Grandfathering	Provides grandfathering relief for pre-existing investments.	Grandfathering relief available for existing investments in shares (acquired prior to April 1, 2017)[3], whereas other investments will still be subjected to PPT.

The OECD Commentary (Paragraph 22.1 of Article 1 of the 2003 Commentary and Paragraph 79 of the 2017 Commentary) further clarifies that where domestic anti-avoidance rules lead to a recharacterization of income or a redetermination of the taxpayer, the provisions of the tax treaty shall be applied in light of such recharacterization.

3. Specific Grandfathering provisions under India's tax treaties with Mauritius, Singapore and Cyprus.

The OECD Commentary (2017) on Article 1, Paragraphs 66 and 67, emphasizes that domestic anti-abuse rules continue to play an important role in preventing tax avoidance, reinforcing that the PPT cannot be applied in isolation. In other words, treaty-level anti-abuse measures complement, rather than displace, domestic law. Paragraph 70 of the Commentary further notes that where domestic law and treaty provisions produce conflicting results, treaty provisions are generally intended to prevail.

In the Indian context, section 90(2A) of the Income-tax Act, 1961 provides that *"Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A shall apply to the assessee even if such provisions are not beneficial to him."* Effectively, this provision allows GAAR to override the provisions of a DTAA, even where the treaty might otherwise provide a more favorable outcome.

For instance, Article 24 of the India-USA DTAA incorporates a LOB clause intended to prevent treaty shopping. Under Article 24(1)(a) of the India–USA DTAA, an entity that is a resident of the United States is entitled to treaty benefits if more than 50% of its beneficial interest is, directly or indirectly, owned by one or more individuals who are residents of either the United States or India. Accordingly, such an entity cannot ordinarily be denied the tax benefits available under the India–USA DTAA.

However, notwithstanding the existence of this treaty-based anti-abuse safeguard, the Income Tax Department may still deny such benefits by invoking the provisions of GAAR contained in Chapter X-A of the Act, since section 90(2A) of the Act expressly provides that GAAR shall apply *notwithstanding anything contained in a tax treaty*, including any anti-abuse provisions therein.

Accordingly, this implies that where GAAR applies to a particular arrangement, it may not be necessary to separately evaluate the applicability of the PPT, rendering any distinction between their respective scopes largely academic in such cases. However, such distinction assumes significance where GAAR does not apply - for instance, in situations that are grandfathered or specifically excluded.

Does GAAR grandfathering end the enquiry — or merely redirect it?

A recent development further highlights how this area continues to evolve. In its decision in ***Tiger Global***[4], the Supreme Court adopted a broad approach to the GAAR framework, indicating that grandfathering protection for transfer of investments made prior to April 1, 2017, would not, by itself, preclude scrutiny under anti-avoidance principles if income arises from an arrangement on or after that date. This gave rise to uncertainty regarding the scope of grandfathering protection available to income from legacy investments.

Subsequently, the Central Board of Direct Taxes, amended the GAAR rules (effective March 31, 2026), to clarify that GAAR shall not apply to **income arising from the transfer of investments** made before April 1, 2017. This clarification appears to address the unintended interpretational risk arising out of the Supreme Court's decision, and realign the position with the originally intended scope of grandfathering of capital gains, while continuing to permit GAAR to apply to other cases.

That said, the inapplicability of GAAR in such cases may not place the arrangement beyond scrutiny altogether. Rather, the enquiry may shift to treaty-based anti-abuse provisions, including the PPT, which continue to operate independently and may require separate evaluation. The focus, therefore, remains on whether the structure can withstand a purpose-based and substance-driven review.

Further, in certain situations – such as where even the relevant treaty does not incorporate a PPT - the scope for anti-abuse intervention is correspondingly limited. This does not, however, obviate the need to substantiate treaty entitlement on its own terms. Taxpayers would still be required to demonstrate satisfaction of threshold conditions such as treaty residence, liability to tax, beneficial ownership test and such other applicable treaty requirements.

4. Authority for Advance Rulings (Income-tax) v. Tiger Global International II Holdings (Civil Appeal No. 262-264 of 2026) (Supreme Court)

CBDT Circular 2017 on GAAR

CBDT has issued Circular No. 7 of 2017 to clarify the scope and implementation of GAAR. It provides crucial interpretative guidance on how GAAR interacts with treaty-based anti-abuse provisions such as the Limitation on Benefits (LOB) clause and the Principal Purpose Test (PPT) introduced through the Multilateral Instrument (MLI).

The Circular explicitly recognizes that GAAR and treaty-based anti-abuse provisions are designed to operate in parallel, with their application depending on the facts and circumstances of each case. It draws a clear distinction between situations where the anti-abuse provisions of a tax treaty themselves are sufficient to address avoidance concerns, and that where domestic law intervention may still be warranted.

In particular, the Circular clarifies that where a case of avoidance is "*sufficiently addressed*" by a treaty-based rule (such as an LOB clause) there shall ordinarily be no occasion to invoke GAAR[5]. However, where such treaty provisions do not fully capture the intent or effect of an arrangement, or where the perceived abuse arises from the use of domestic tax incentives rather than treaty relief, GAAR may still be applied. This establishes a functional hierarchy in application - treaty provisions first, GAAR residually.

Further, the Circular also confirms that GAAR and specific anti-avoidance rules (SAAR) can coexist, but the use of GAAR is reserved for cases where SAAR or treaty-level mechanisms are inadequate to address the tax avoidance arrangement[6]. This reinforces the understanding that GAAR is not intended as a first-response tool, but rather as a residual and proportionate measure.

The Circular also provides important context, clarifying that GAAR will not be invoked merely on account of tax-efficient structures or jurisdictional choices that are supported by genuine commercial substance, and that investments made prior to 1 April 2017 enjoy grandfathering protection[7]. These clarifications safeguard business certainty and ensure that legitimate, commercially driven arrangements are not disrupted.

Taken together, these clarifications demonstrate that GAAR is intended to function as a supplementary anti-abuse framework.

Moreover, the Circular underscores the importance of multi-layered administrative safeguards, including approval by the Approving Panel, before GAAR can be invoked, ensuring that it is applied judiciously and with due process.

In Circular No. 1 of 2025, the CBDT emphasized that the PPT is a fact-based test, to be applied on a case-by-case basis, ensuring that bona-fide commercial transactions are not inadvertently penalized. The Press Release also clarifies that Circular does not impact domestic GAAR, SAAR, Judicial Anti-Abuse Rules (JAAR) and other anti-abuse provisions in the treaty which shall continue to apply independently.

Interplay between PPT and SAAR

The Specific Anti-Abuse Rules (SAAR) such as deemed dividends, thin capitalization, transfer pricing regulations or transactions with notified jurisdictions target clearly identified forms of tax avoidance under domestic law,. These provisions operate mechanically once the prescribed statutory conditions are met.

At the treaty level, the PPT serves as a comprehensive safeguard against treaty abuse. Certain provisions of tax treaties can also be identified as SAAR e.g. anti-fragmentation provision, arm's length requirement, beneficial ownership condition etc.

In practice, both rules may apply concurrently but in distinct domains. Where a transaction triggers a domestic anti-abuse provision, SAAR would determine the domestic tax treatment. If the same arrangement also seeks to obtain a treaty benefit (for example, a lower withholding tax rate through a conduit jurisdiction), the treaty SAAR or PPT may further be invoked to examine whether granting such benefit is justified under the treaty.

5. Question 2 of the Circular
6. Question 1 of the Circular
7. Questions 4 and 5 of the Circular

Illustration:

Suppose an Indian company pays interest to an associated enterprise in Country X.

- Under Section 94B (SAAR), interest deduction may be restricted beyond the permitted threshold (domestic law impact).
- Simultaneously, if the group has routed the loan through Country X primarily to avail of a lower treaty withholding rate, the PPT could deny that treaty benefit (treaty-level impact). The beneficial ownership condition in the interest article may also get triggered.

Thus, domestic SAAR, treaty SAAR and PPT together ensure comprehensive coverage — SAAR governs the domestic tax computation, while PPT safeguards against treaty-based abuse.

Interplay of PPT with LOB

The LOB clause and PPT both aim to curb treaty abuse but operate through distinct mechanisms.

The LOB clause is generally a rule-based test that prescribes objective criteria - ownership tests, minimum expenditure, or active business tests - to determine whether a taxpayer is eligible to claim treaty benefits[8]. It focuses on form and substance, granting benefits only to entities meeting the specified conditions (e.g., entities having sufficient local ownership or genuine business operations in the treaty partner country)

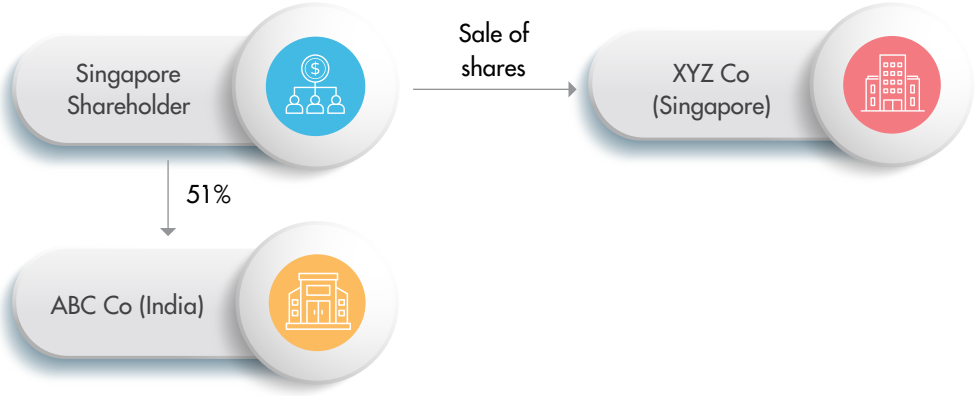
In contrast, the PPT is a purpose-based test, denying treaty benefits if one of the principal purposes of an arrangement is to obtain such benefit in a manner inconsistent with the treaty's object and purpose. It is broader in scope and can apply even where the taxpayer technically satisfies the LOB conditions but lacks genuine commercial intent.

Illustration:

Under Article 24A of the India – Singapore Tax Treaty, a minimum expenditure threshold of SGD 200,000 is prescribed for obtaining the benefit of exemption from capital gains on sale of shares in Singapore. This is, in essence, an LOB clause in the context of a specific stream of income, i.e., capital gains.

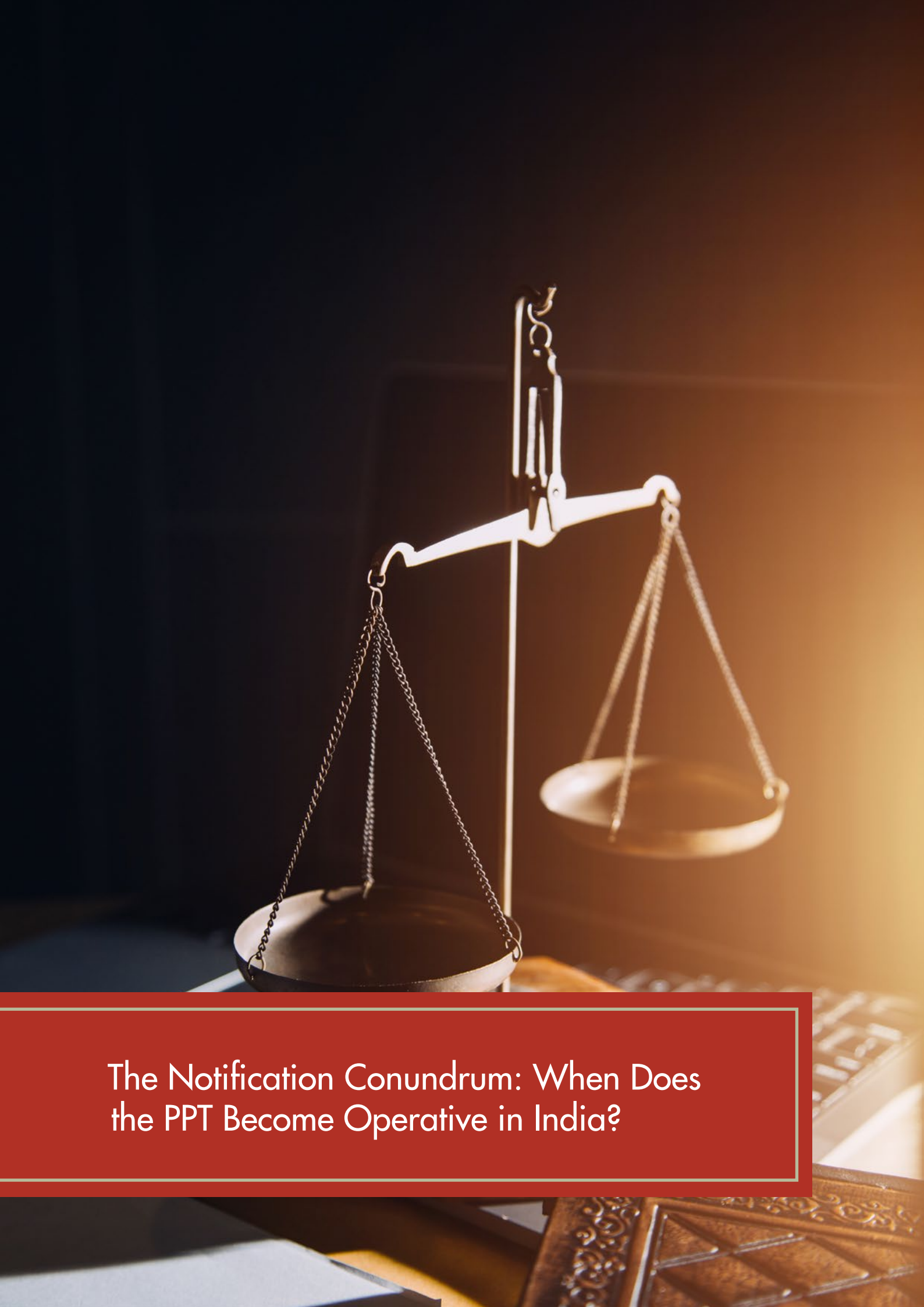
Further, the MLI instruments deposited by India and Singapore postulate that the PPT provisions shall supersede the existing treaty provisions only to the extent that the provisions are inconsistent or incompatible with the PPT under MLI.

Thus, an interesting issue would arise whether the existing LOB clause as above would also stand superseded?



Considering that LOB clause in the India-Singapore DTAA inherently denies treaty benefit if affairs of a taxpayer are arranged with the primary purpose to take advantage of the benefits of the capital gains benefit in the Treaty, one can say that LOB clause is not incompatible with the PPT clause; hence, should be read along with PPT clause.

8. Such LOBs can be found in treaties with Mauritius and Singapore for capital gains income



The Notification Conundrum: When Does the PPT Become Operative in India?

While the conceptual framework underlying the MLI and the PPT is now well established, their application within India's domestic legal system has begun to raise more nuanced questions. In particular, the MLI's design as a multilateral overlay, intended to modify the application of treaties without bilateral renegotiation, has prompted judicial scrutiny on how such modifications take effect within India's constitutional and statutory framework.

Recent Indian jurisprudence has focused squarely on how the MLI and the PPT operate in practice within India's domestic legal framework. Courts and tribunals have begun to articulate the legal and procedural contours within which the PPT may be applied, offering guidance on issues of operability, enforceability, and the limits of administrative discretion, while seeking to preserve treaty certainty. C. These decisions highlight both the judicial guardrails that are emerging, as well as the open questions that continue to shape the practical application of PPT in India.

One of the most consequential questions emerging from India's adoption of the MLI concerns the point at which treaty-level anti-abuse provisions, most notably the PPT, become legally operative under domestic law. While India has signed, ratified, and brought the MLI into force, recent judicial decisions have foregrounded a procedural issue of practical importance: whether the PPT can be applied in the absence of a treaty-specific domestic notification incorporating the relevant MLI provisions into a bilateral tax treaty.

This question goes to the heart of the MLI's architecture. Unlike bilateral protocols that directly amend treaty text, the MLI is designed to operate as a multilateral overlay, modifying the application of Covered Tax Agreements through matching positions, reservations, and notifications. India has given domestic effect to the MLI through Notification No. 57/2019, which records India's adopted positions across its covered treaties and brings the Convention into force. From a policy perspective, this mechanism reflects the efficiency that the MLI seeks to achieve, allowing uniform implementation of BEPS measures without treaty-by-treaty renegotiation.

Recent decisions of the Income Tax Appellate Tribunal, however, have introduced an additional layer of procedural scrutiny. In *Sky High Leasing*[9] and *Kosi Aviation Leasing*[10], the Tribunal held that MLI provisions, including the PPT, cannot be invoked unless the relevant bilateral treaty has been specifically notified under section 90(1) of the Income-tax Act, 1961, incorporating the modified treaty position into domestic law. In the absence of such treaty-specific notifications, the Tribunal concluded that the PPT could not be applied, notwithstanding the fact that both treaty partners were signatories to the MLI and had adopted matching positions.

The Tribunal's approach is anchored in the Supreme Court's decision in *Nestlé SA*[11], which has emerged as the reference point for the notification debate. In *Nestlé SA*, the Supreme Court held that treaty benefits arising from a Most Favoured Nation (MFN) clause are not self-executing and require a specific notification under section 90(1) before they can be applied domestically. The Court underscored that treaty provisions or protocols that alter rights or liabilities under municipal law must be expressly incorporated through a statutory notification, failing which they cannot be given effect by courts or authorities.

At the same time, the context in which *Nestlé SA* was decided is material. The judgment addressed a situation where benefits were sought to be imported into one bilateral treaty by reference to another treaty entered by India with a different country, i.e., a treaty to which the relevant counterparty was not a party. The Supreme Court's concern, therefore, was with the automatic extension of treaty consequences flowing from third-party agreements without explicit domestic incorporation.

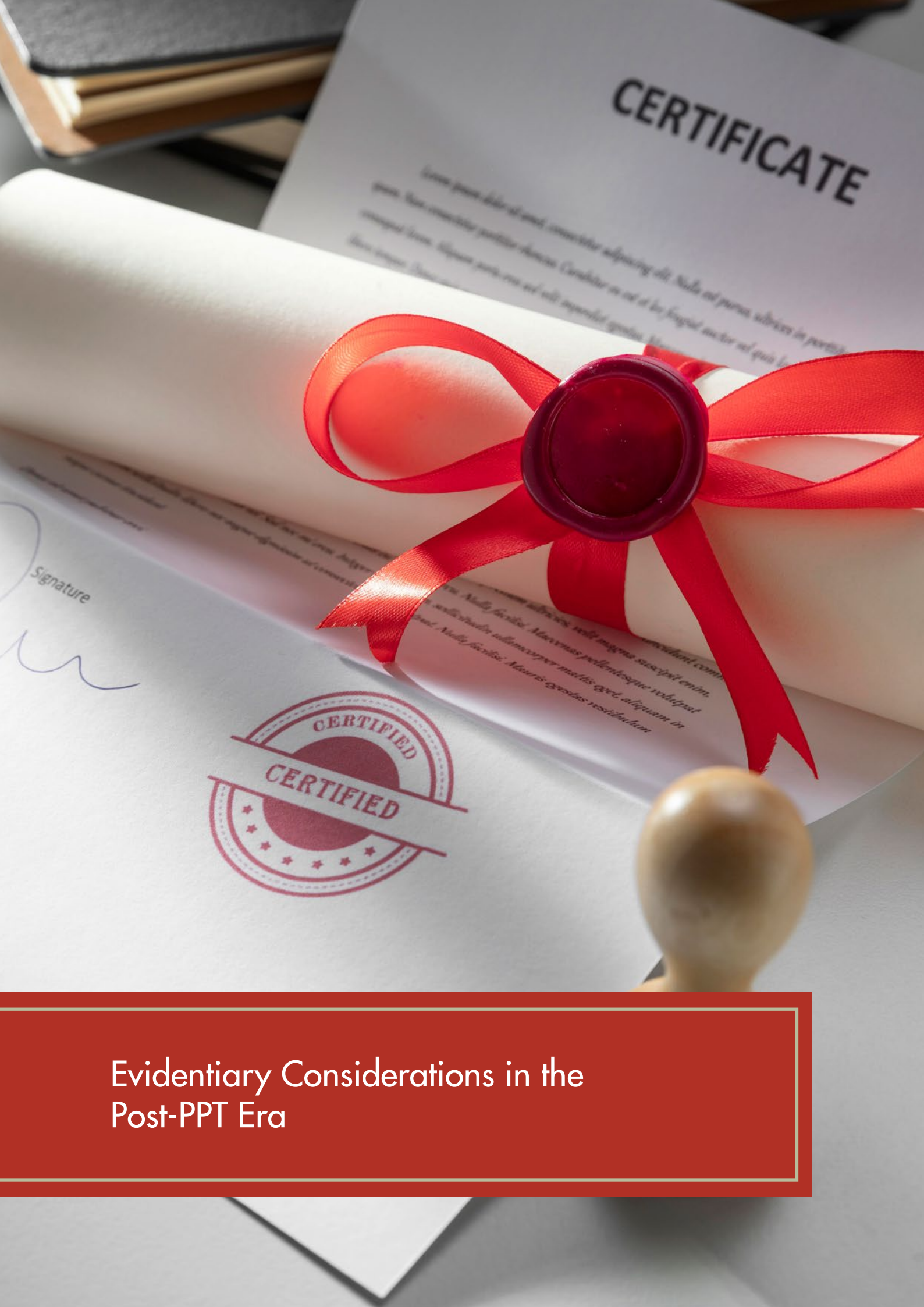
The application of this reasoning to the MLI context represents a significant interpretative extension. Unlike the MFN scenario in *Nestlé SA*, the MLI is a multilateral

9. *Sky High Leasing Company Limited v. ACIT [2025] 177 taxmann.com 579 (Mumbai Tribunal)*
10. *Kosi Aviation Leasing Ltd. v. ACIT* [ITA No. 994 / Del / 2025] (Delhi Tribunal)
11. *Nestle SA* [TS-616-SC-2023]

convention to which both partners to the underlying bilateral treaty are parties, and which is intended to operate alongside existing treaties rather than amend their text through bilateral renegotiation. Nevertheless, relying on the notification principle articulated in *Nestlé SA*, the Tribunal in *Sky High Leasing* and *Kosi Aviation Leasing* concluded that the absence of treaty-specific notifications rendered the PPT unenforceable at the domestic level.

While these rulings arose in the context of aircraft leasing arrangements, their implications extend more broadly to the manner in which MLI-driven treaty modifications are to be operationalized in India. They raise a practical question of continuing relevance: whether India's existing notification framework is sufficient to give effect to PPT-based modifications, or whether additional treaty-specific notifications may be required to address judicial concerns around domestic enforceability?

From a forward-looking perspective, this issue is likely to remain an area of close attention as India's treaty practice continues to evolve. The MLI represents an innovative mechanism for treaty modification, but its operation, particularly in the absence of treaty-specific domestic notifications, raises complex questions of implementation and enforceability. The above judicial decisions underscore the need for procedural discipline in giving domestic effect to MLI-driven changes, even as India remains committed to BEPS-aligned anti-abuse standards. Whether this phase represents a transitional pause or prompts further legislative, administrative, or notification-based responses will be critical in shaping certainty around the application of the PPT in India.



Evidentiary Considerations in the Post-PPT Era

The introduction of the PPT has intensified the focus on purpose and commercial rationale in treaty claims, prompting renewed scrutiny of traditional proof of treaty entitlement. Until recently, documents such as the Tax Residency Certificate ('TRC') were often regarded as sufficient to establish treaty eligibility — a position settled by the Supreme Court's decision in *Azadi Bachao Andolan*[12].

In the evolving post-BEPS landscape, however, a natural question arises: to what extent do such documents continue to shape treaty entitlement in an environment where intent, purpose, and economic substance increasingly assume central relevance?

The Supreme Court's recent decision in *Tiger Global* provides important guidance in this regard. The Court observed that a TRC, while relevant, is not by itself conclusive to establish treaty entitlement. In doing so, it noted that *Azadi Bachao Andolan* was rendered in a materially different statutory and treaty environment - one that did not incorporate GAAR, judicial anti-avoidance principles (JAAR), or treaty-level anti-abuse standards. Against this backdrop, the Court indicated that the earlier understanding regarding the evidentiary sufficiency of a TRC must be viewed in light of the contemporary anti-abuse framework.

Consequently, the surrounding factual matrix assumes greater significance. Elements such as the commercial rationale underlying the structure, the locus of control and decision-making, and the alignment between legal form and economic substance may be examined to assess whether treaty benefits are being claimed consistently with the object and purpose of the relevant treaty provisions.

In this context, the presence of a TRC or related documentation may not, by itself, preclude further examination where anti-abuse considerations arise. Likewise, factors such as the longevity of a structure or the availability of grandfathering may not automatically insulate an arrangement from scrutiny. These considerations must be evaluated within the overall commercial and factual context, rather than in isolation.

For taxpayers and investors, the implications are clear. Treaty claims increasingly require a coherent commercial narrative supported by contemporaneous material demonstrating the underlying business purpose of the structure across its lifecycle — including entry, operation, and exit. In the post-PPT environment, while documentary discipline remains important, the alignment of legal form with economic substance will often prove decisive in determining treaty outcomes.

12. *Union of India v. Azadi Bachao Andolan [2003] 263 ITR 706 (Supreme Court)*

Impact on Special Purpose Vehicles (SPVs)

Special Purpose Vehicles (SPVs) have historically been used in cross-border investment structures for regulatory, commercial, and financing considerations. With the introduction of the MLI and the Principal Purpose Test (PPT), the sustainability of SPV-based holding arrangements is now subject to a sharper lens. The PPT requires taxpayers to demonstrate that the SPV serves genuine non-tax commercial purposes, and that tax benefits are only incidental to these purposes.

Two-step rationale for SPVs

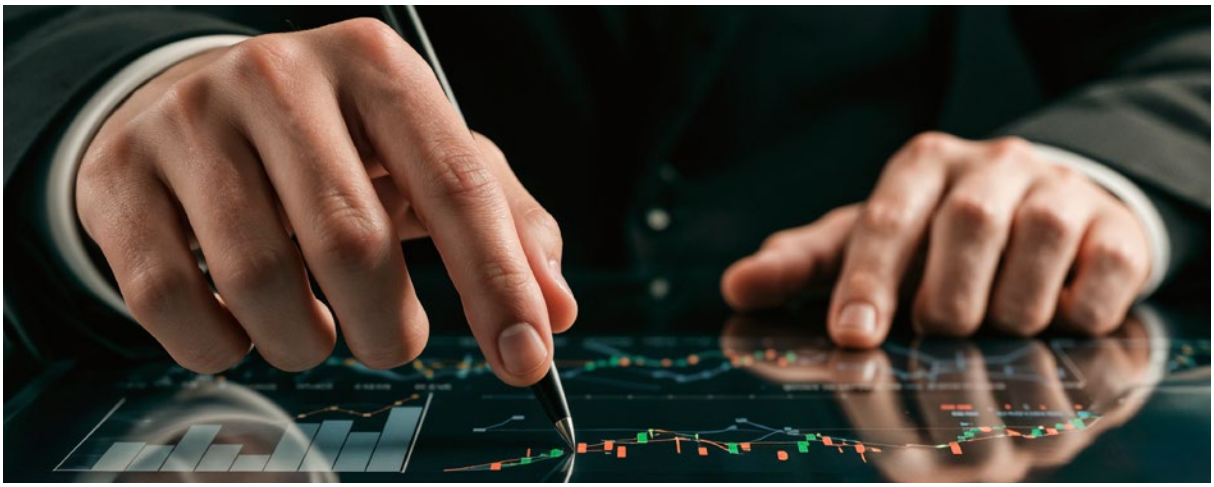
- **Separate entity justification:** Demonstrating legitimate business reasons for housing a specific investment or activity in a separate legal entity, such as risk segregation, governance needs, financing ring-fencing, investor's vehicle, creditor comfort, regulatory considerations, ease of exit, operational efficiency, or management autonomy.
- **Justification for choice of jurisdiction:** Establishing that the choice of SPV jurisdiction is driven by real commercial advantages, such as availability of skilled personnel, infrastructure support, industry ecosystem, regulatory stability, market access, or capital market depth — and not merely the tax treaty network.

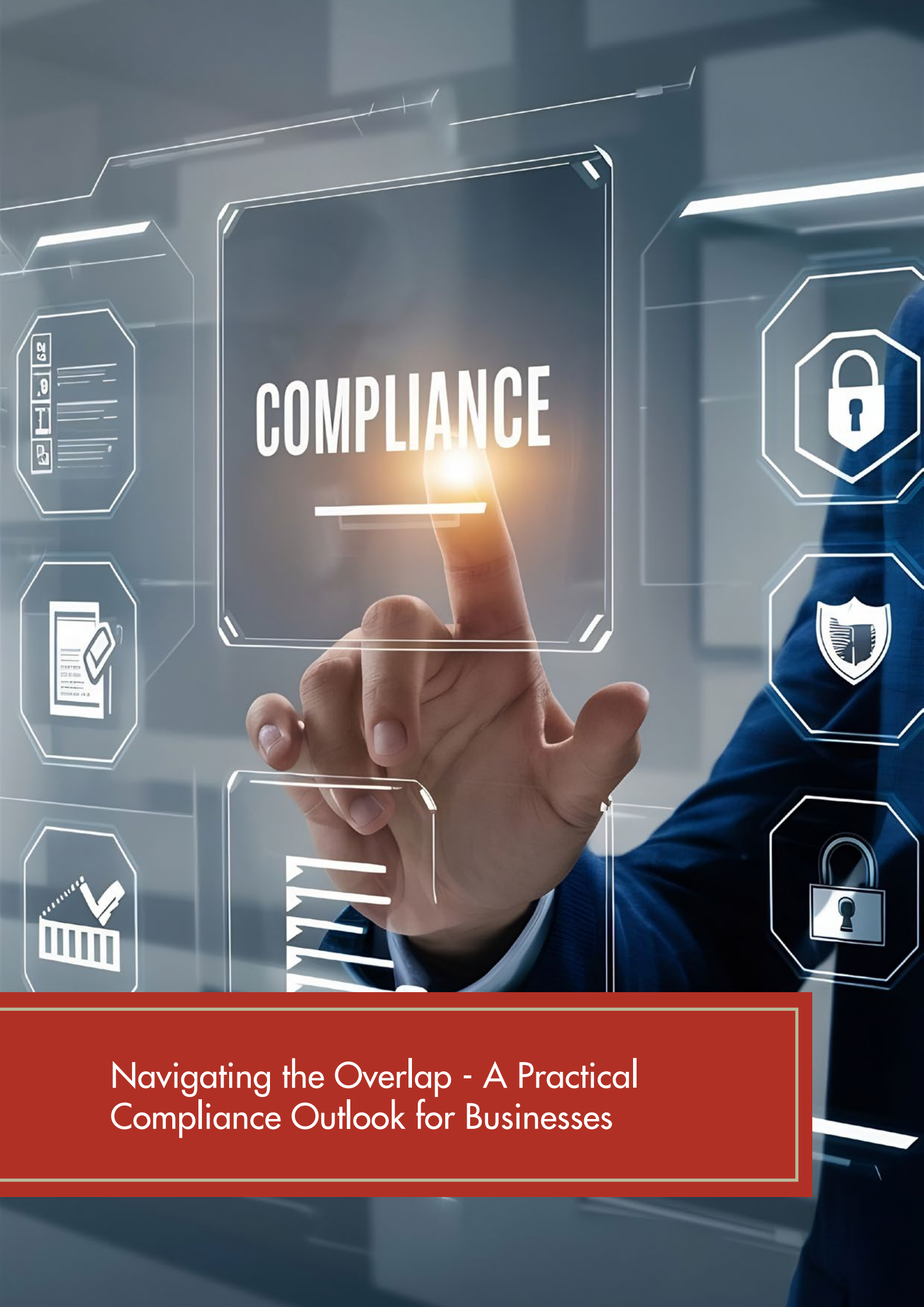
Heightened Scrutiny of 'Location Test' - The more challenging aspect is often explaining *why the SPV is located in that jurisdiction* rather than in the parent company's country. Where the location offers no meaningful commercial advantage beyond a favourable tax treaty, the structure risks being characterized as treaty-driven.

Substance Expectations - Increasingly, tax authorities expect SPVs to exhibit credible operational substance such as local presence, commensurate with the scale of investments, including active decision-making, local directors with industry knowledge, and access to relevant support infrastructure.

SPVs with multi-jurisdiction holding portfolios must show scalability of substance: Where several SPVs exist in the same jurisdiction, the "aggregate substance" and broader commercial context may be relevant rather than an isolated entity-by-entity test.

In essence, the MLI requires investors to look beyond treaty mechanics and evaluate whether their SPV structure can clearly withstand scrutiny on purpose, substance and commercial justification—both at the entity and transaction level.

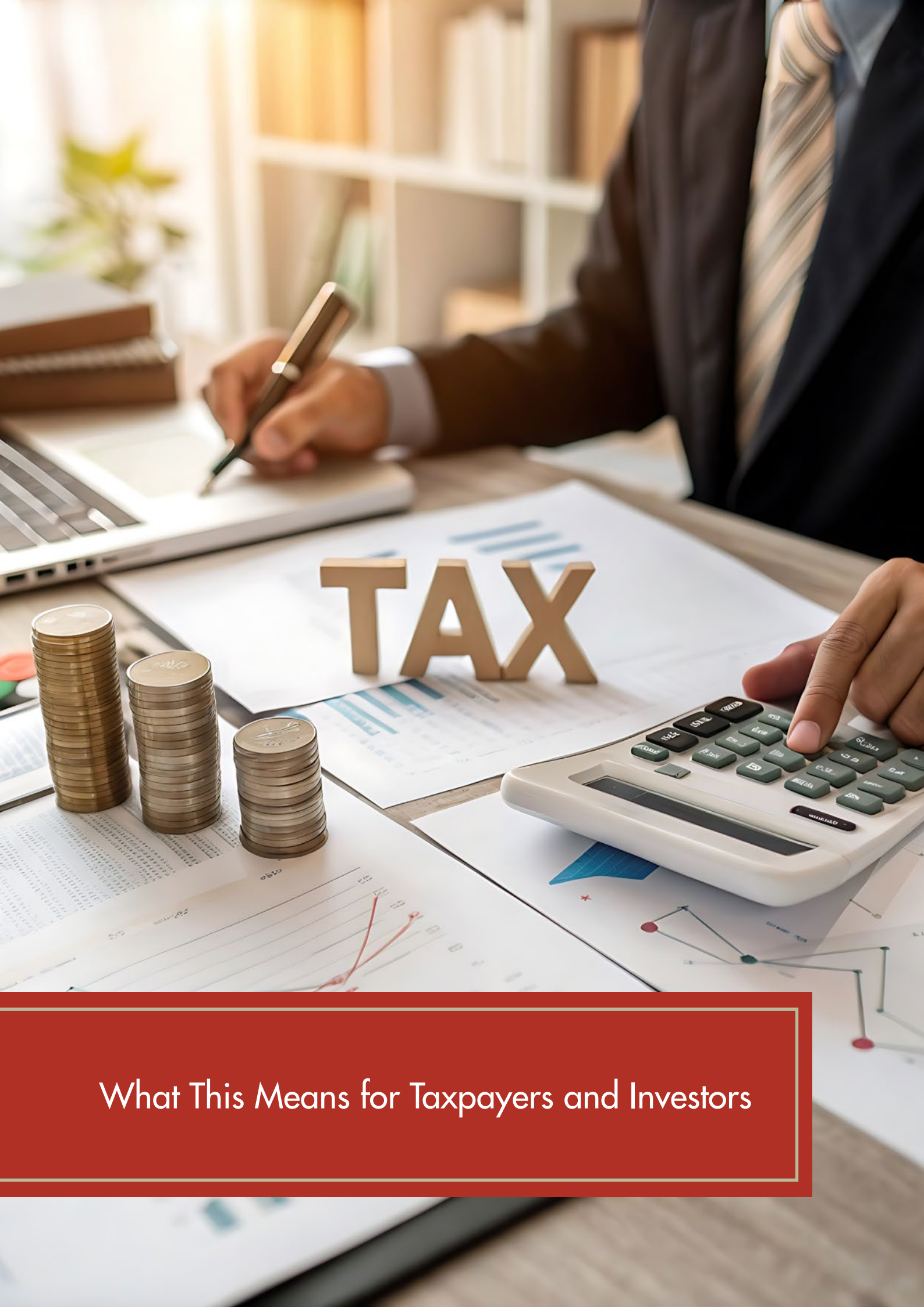




Navigating the Overlap - A Practical Compliance Outlook for Businesses

For global investors, this layered anti-abuse environment demands stronger documentation and governance, but it also offers greater certainty when structures are grounded in commercial reality. The most effective approach is to build a cohesive, substance-driven posture rather than addressing each rule (PPT, GAAR, SAAR, LOB) in isolation.

- **Anchor structures in commercial logic:** Jurisdictional choices should be traceable to genuine business drivers — market access, regulatory efficiency, operational control, investor pooling, or cost optimization — rather than tax outcomes alone.
- **Demonstrate real substance:** Presence of personnel, local expenditure, local directors, decision-making all serve as proof that a holding or investment vehicle is more than a formality.
- **Robust documentation across levels:** Management needs to maintain robust and corroborative documentation in the form of email correspondences, board & shareholder's minutes, management contracts, and inter-company agreements.
- **Avoid over-engineering:** Stacking multiple entities or using hybrid arrangements purely for tax outcomes increases exposure under all four regimes (PPT, GAAR, SAAR, and LOB).
- **Seek certainty where available:** Where ambiguity persists, taxpayers should not hesitate to seek advance rulings or clarifications. Proactive engagement with authorities is often a stronger defense than reactive justification.
- **Stay alert to policy evolution:** India's tax administration is modernising rapidly; guidance and jurisprudence continue to refine the boundaries of these rules. Flexibility and foresight are crucial for staying compliant without eroding efficiency.



What This Means for Taxpayers and Investors

India's evolving treaty landscape reflects a broader recalibration of international tax norms from entitlement-based treaty access toward a framework that places greater emphasis on purpose, alignment, and substance. The adoption of the MLI and PPT signals India's clear commitment to global BEPS standards, while also marking a transition that is still being shaped through domestic law, administrative practice, and judicial interpretation.

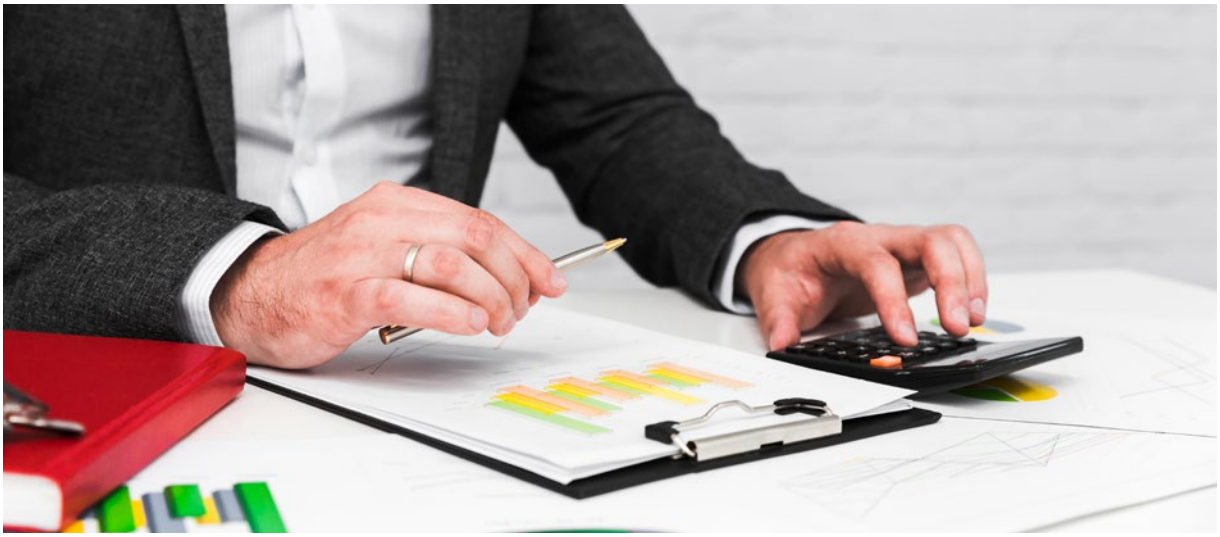
The shift toward purpose-based treaty analysis is directional rather than disruptive. The PPT represents a move away from mechanical reliance on form toward a more contextual assessment of arrangements. At the same time, this evolution has not displaced foundational treaty principles. Treaty benefits are no longer automatic, but neither are they subject to denial by default.

Traditional markers of treaty entitlement continue to matter, even in a post-PPT environment. Instruments such as Tax Residency Certificates, along with demonstrable commercial rationale, governance, and decision-making substance, remain relevant to the evaluation of treaty claims. The emphasis has shifted toward a holistic assessment of facts, rather than mere acceptance of established forms of proof.

The judiciary's role has been central in shaping the contours of this transition. Courts have neither insulated treaty claims from scrutiny nor endorsed an outcomes-driven denial of benefits. Instead, recent decisions particularly the one in the case of Tiger Global point toward a calibrated approach: one that distinguishes between genuine investment structures and arrangements that are principally tax-driven, while resisting presumptions based on structure, jurisdiction, or tax efficiency alone.

Current areas of uncertainty should be viewed as transitional rather than structural. Questions around implementation mechanics and the interaction between treaty provisions and domestic law are part of an adjustment phase as India aligns its treaty network with global standards. Over time, greater clarity—through judicial pronouncement, administrative guidance, or treaty practice—is likely to enhance predictability for taxpayers and investors alike.

Taken together, these developments suggest that while treaty planning in India will require greater attention to purpose, documentation, and alignment, the underlying framework continues to value certainty, proportionality, and principled application. For taxpayers and investors, the focus going forward should be on articulating commercial rationale and maintaining robust contemporaneous records, rather than reacting defensively to the introduction of anti-abuse standards.



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Dhruva Advisors India Pvt. Ltd., a Ryan LLC affiliate, is a leading tax and regulatory advisory firm delivering high-impact solutions across India and key global markets. In a rapidly evolving tax environment, we help clients navigate complexity with clear, practical, and insight-driven guidance.

Founded in 2014, Dhruva has grown into one of India's most respected tax firms, operating from 12 offices across India and international locations in Dubai, Abu Dhabi, Saudi Arabia, and Singapore. Our leadership team includes 28 Partners, 8 Senior Advisors, 17 Associate Partners, and 42 Principals, supported by nearly 500 professionals with deep technical expertise and a strong commitment to client outcomes.

Dhruva Advisors has been consistently recognized by International Tax Review, earning the 'India Tax Firm of the Year' award for five consecutive years (2017–2021) and maintaining a 'Tier 1' ranking through 2026. These accolades reflect our focus on accountability, innovation, and a client-first mindset.

Our expertise spans tax disputes, global structuring, advisory, and regulatory strategy. We support clients across industries including Aerospace & Defense, Agro & Chemicals, Automotive, Conglomerates, Education, Energy & Resources, Financial Services, Healthcare, IT & ITeS, Manufacturing, Pharma & Life Sciences, Private Equity, Real Estate, Transportation, Telecom, and Media.

Wherever tax complexity exists, Dhruva delivers clarity.

Dhruva Advisors has consistently been ranked as 'Tier 1' firm in General Corporate Tax, Indirect Tax, and Transfer Pricing, maintaining top-tier rankings through 2026.

Awarded 'India Tax Firm of the Year' at the ITR Asia Tax Awards for five consecutive years (2017–2021).

Recognized as the 'India Disputes and Litigation Firm of the Year' at the ITR Asia Tax Awards in 2018 and 2020.

Dhruva Consultants achieved ITR World Tax Ranking 2026:

- Tier 1 – Indirect Tax
- Tier 2 – General Corporate Tax, Transfer Pricing, Transactional Tax
- Other Notable: Tax Controversy

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