

Combating Tax Treaty Abuse: Tools available under the BEPS Multilateral Instrument

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Abstract

The anxiety of taxpayers, consultants and advisors over the consistent application of Principal Purpose Test (PPT) provisions in tax treaties can now be put to rest as tax authorities are expected to consistently read the PPT provisions in conjunction with the preamble, i.e. the key to application of PPT provisions lies in the preamble of the treaty itself. This follows on taking a leaf out of the Preamble to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion & Profit Shifting (MLI), Vienna Convention, Commentaries on PPT in the respective Organisation for Economic Co-operation and Development (OECD) and United Nations (UN) Model Tax Convention (MTC), 2017 and Australian Taxation Office's (ATO) instructions on PPT which abundantly highlight on conjoint application of the preamble in the course of invocation of PPT provisions. Now, the entire focus of extending treaty benefits has shifted to undertaking bonafide transactions and preventing double taxation as against a tendency of securing tax savings through tax avoidance. Therefore, PPT as read with the preamble can clearly be invoked to combat treaty-shopping arrangements, abusive tax planning and abusive tax avoidance arrangements or transactions. At the same time, tax authorities in any part of the world may not be inclined to invoke PPT as read with the preamble in respect of any arrangement or transaction when taxpayers are able to discharge their onus establishing that (below mentioned conditions to be satisfied in tandem):

- genuine business and commercial reasons for a transaction exist;
- a purpose for the transaction cannot be ascribed to non-taxation or reduced taxation through tax evasion or tax avoidance;
- despite no tax advantages, the transaction would be carried out exactly in the same way; and
- it cannot reasonably be considered that one of the principal purposes of the arrangement or transaction is to obtain treaty benefits and that the object and purpose of the treaty is getting defeated.

Le soulagement domine aujourd'hui chez les contribuables, les consultants et les conseillers qui avaient exprimé des inquiétudes au sujet de l'application cohérente des dispositions relatives à la règle du critère des objets principaux dans les conventions fiscales. Il est aujourd'hui acquis que ces dispositions doivent être interprétées par les autorités fiscales conformément au texte du préambule de la convention en question. Dit autrement, cela signifie que les modalités d'application des dispositions relatives à la règle du critère des objets principaux doivent être définies dans le préambule de la convention elle-même. Ce principe résulte du préambule de la Convention multilatérale pour la mise en œuvre des mesures relatives aux conventions fiscales pour prévenir l'érosion de la base d'imposition et le transfert de bénéfices, de la Convention de Vienne, des commentaires relatifs à la règle du critère des objets principaux élaborés dans le cadre des modèles de convention fiscale de l'Organisation de coopération et de développement économiques (OCDE) et des Nations unies (ONU) de 2017 et des instructions de l'Administration fiscale australienne (ATO) à cet égard, qui indiquent clairement que lorsqu'elles sont invoquées, les dispositions relatives à la règle du critère des objets principaux doivent être interprétées conjointement avec le préambule de la convention concernée. Les avantages accordés dans le cadre d'une convention fiscale visent davantage à encourager les transactions réalisées de bonne foi et à éviter une double imposition, qu'à permettre, comme c'était le cas auparavant, des économies d'impôt via des pratiques d'évasion fiscale. Par conséquent, la règle du critère des objets principaux, selon l'inter-

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prétation qui en est faite dans le préambule, peut clairement être invoquée pour faire échec au chalandage fiscal, aux stratégies fiscales abusives et aux accords ou transactions destinés à l'optimisation fiscale. Dans le même temps, les autorités fiscales, partout dans le monde, peuvent ne pas être disposées à appliquer la règle du critère des objets principaux telle qu'elle figure dans le préambule à l'égard de tout accord ou transaction lorsque les contribuables concernés sont en mesure de faire la preuve que (les conditions mentionnées ci-dessous sont cumulatives) :

- *de véritables raisons professionnelles et commerciales justifient la transaction ;*
- *le but de la transaction n'est pas d'échapper à l'impôt ou de bénéficier d'un avantage fiscal via des pratiques d'évasion ou de fraude fiscale ;*
- *la transaction serait effectuée exactement de la même manière en l'absence d'avantages fiscaux ; et*
- *il ne peut être raisonnablement considéré que l'un des objectifs principaux de l'accord ou de la transaction est de bénéficier des avantages prévus par la convention concernée et de mettre en échec l'objet et le but de cette dernière.*

La ansiedad de los contribuyentes, consultores y asesores por la aplicación coherente de las disposiciones de la prueba del propósito principal (PPP) en los tratados fiscales puede aplacarse ya, dado que se espera que las autoridades fiscales interpreten coherentemente las disposiciones de la PPP junto con el preámbulo, es decir, que la clave de la aplicación de las disposiciones de la PPP radica en el preámbulo del propio tratado. Además, se sigue el ejemplo del preámbulo de la Convención Multilateral para aplicar las medidas relacionadas con los tratados fiscales para prevenir la erosión de las bases imponibles y el traslado de beneficios (MLI), la Convención de Viena, los comentarios sobre la PPP en la Convención Modelo de las Naciones Unidas (ONU) y el Modelo de Convenio Tributario de la Organización para la Cooperación y el Desarrollo Económicos (OCDE), de 2017, y las instrucciones de la Oficina Tributaria de Australia sobre la PPP, que destacan plenamente la aplicación conjunta del preámbulo en el transcurso de la invocación de las disposiciones de la PPP. Ahora, toda la atención que antes se centraba en ampliar los beneficios de los tratados fiscales se pone en llevar a cabo transacciones de buena fe y evitar la doble imposición en oposición a la tendencia de garantizar el ahorro fiscal a través de la elusión fiscal. Por lo tanto, si la prueba de propósito principal se interpreta junto con el preámbulo, se puede invocar claramente para combatir la búsqueda del acuerdo más favorable y acuerdos o transacciones de planificación fiscal abusiva y elusión fiscal abusiva. A su vez, puede que las autoridades fiscales de ciertas partes del mundo no tengan inclinación por invocar la PPT interpretada junto con el preámbulo respecto de cualquier acuerdo o transacción cuando los contribuyentes sean capaces de descargar su responsabilidad aludiendo (a continuación se mencionan las condiciones que han de satisfacerse en conjunto):

- *verdaderas razones empresariales y comerciales para la existencia de una transacción;*
- *un propósito para que no se pueda atribuir a la transacción una exención o una imposición reducida a través de la evasión o la elusión fiscal;*
- *que pese a la inexistencia de ventajas fiscales, la transacción se llevaría a cabo exactamente de la misma manera; y*
- *que no se pueda considerar razonablemente que uno de los objetos principales del acuerdo o la transacción sea obtener beneficios del tratado, y que el objeto y el propósito del tratado se están viendo frustrados.*

1. Introduction

The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion & Profit Shifting (MLI) is one of the outcomes of the Organisation for Economic Co-operation (OECD)/Group of Twenty (G20) project to tackle Base Erosion and Profit Shifting (BEPS Project) i.e., tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low- or no-tax locations where there is little or no economic activity, resulting in little or no overall corporate tax being paid¹. The MLI entered into force on 1 July, 2018 and it started producing effect from 1 January, 2019. The MLI has the distinction of being the first successfully concluded multilateral tax treaty² and has achieved universal participation, with as much as 95 signatories and 65³ ratifications as of now, out of 139-member⁴ strong Inclusive Framework (IF). There are three signatories of the MLI so far which are non-members of the IF, namely, Cyprus, Fiji and Kuwait. Signing of the MLI by non-members of the IF is

a positive signal conveying importance attached to the MLI and faith reposed in its ability to introduce anti-BEPS measures in a swift manner in tax treaties.

The MLI introduces significant changes in line with BEPS recommendations, out of which, the most discussed is the introduction of the Principal Purpose Test (PPT) as a minimum standard through the BEPS Action 6 Report. PPT has been universally adopted by jurisdictions⁵ that have ratified the MLI. The PPT provisions are set to display an extremely important role in preventing international tax avoidance due to which taxpayers have been expressing their anxiety at various fora over consistent application of PPT provisions and whether PPT would still apply if genuine commercial reason was also one of the principal purposes of the transaction. All this while, the focus of taxpayers, consultants and advisors has been invariably on the PPT provisions. An important aspect which has been deprived of commensurate focus is the conjugal application on the PPT of provisions enshrined in the preamble, particularly with regards to tax avoid-

ance, which is being introduced through paragraph 1 of Article 6 of the MLI.

Accordingly, the objective of this Policy Brief is the implementation of the PPT provisions by tax jurisdictions across the globe, *inter alia*, highlighting the role of conjoint application of the preamble in the course of invocation of PPT provisions. An important conclusion drawn by the brief is that the anxiety of taxpayers, consultants and advisors over consistent application of PPT provisions shall be put to rest as tax authorities are expected to read the PPT provisions in conjunction with the preamble, i.e., the key to application of PPT provisions lies in the preamble itself.

1.1. Background - BEPS Action 6 Report

BEPS Action 6 Report⁶ titled *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances* identifies treaty abuse, and in particular treaty shopping, as one of the most important sources of BEPS concerns. Jurisdictions have therefore agreed to include anti-abuse provisions in their tax treaties, including a minimum standard to counter treaty shopping. The report includes new treaty anti-abuse rules that provide safeguards against the abuse of treaty provisions and offer a certain degree of flexibility regarding how to do so, *inter alia*, by adopting the following approach:

- A clear statement (Preamble) that the States that enter into a tax treaty intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements will be included in tax treaties.
- A specific anti-abuse rule, the limitation-on-benefits (LOB) rule, which limits the availability of treaty benefits to entities that meet certain conditions, will be included in the OECD Model Tax Convention (MTC).
- In order to address other forms of treaty abuse, including treaty shopping situations that would not be covered by the LOB rule described above, a more general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purpose test or 'PPT' rule) will be included in the OECD MTC. Under that rule, if one of the principal purposes of transactions or arrangements is to obtain treaty benefits, these benefits would be denied unless it is established that granting these benefits would be in accordance with the object and purpose of the provisions of the treaty.

The recommendations of the BEPS Action 6 Report are duly incorporated in the United Nations (UN) MTC 2017 as well. The BEPS Action 6 is a minimum standard with which countries that have committed to the IF must comply with, and is, *inter alia*, being implemented through Articles 6 and 7 of the MLI.

2. Preamble contained in paragraph 1 of Article 6 of the MLI

Paragraph 1 of Article 6 of the MLI states as below:

"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),"

The clear statement of the intention of the signatories to a tax treaty that appears in the preamble is relevant to the interpretation and application of the provisions of that treaty. At the same time, one must not lose sight of the fact that the preamble also expressly provides that States enter into a tax treaty so as to eliminate double taxation which in turn facilitates investment of capital, seamless flow of technology and overall acceleration in the business environment.

2.1. Preamble now clearly addresses tax avoidance in addition to tax evasion

Earlier, provisions of tax treaties were developed with the prime objective of preventing double taxation. This was reflected in the title proposed in both the 1963 Draft Double Taxation Convention on Income and Capital and the 1977 Model Double Taxation Convention on Income and Capital. Subsequently, the Commentary on Article 1 was modified to provide expressly that tax treaties were not intended to encourage tax avoidance or evasion and later, that paragraph was amended to clarify that the prevention of tax avoidance was also a purpose of tax treaties. However, the intention to prevent tax evasion and tax avoidance was still not expressly mentioned in the preamble of the OECD and UN MTC.

In view of the recommendations of the BEPS Action 6 Report, it was decided to state clearly, in the title recommended by the OECD and UN MTC, that the prevention of tax evasion and avoidance is a purpose of tax treaties. It was also decided that the OECD and UN MTC should recommend a preamble that provides expressly that States that enter into a tax treaty intend to eliminate double taxation without creating opportunities for tax evasion and avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States). The clear statement of the intention of the signatories to a tax treaty that appears in the preamble will be relevant to the interpretation and application of the provisions of that treaty.

In order to fully understand the impact being introduced by the new preambular language, it would be expedient at this juncture to briefly discuss the meaning of tax avoidance and tax evasion. Tax avoidance arises in a situation in which a taxpayer reduces its tax liabilities by taking advantage of ambiguities in the legal provisions wherein the latter act is distinctly against the intention of

law. On the other hand, tax evasion is patently illegal involving non-payment of taxes by means of not reporting true taxable income, or by claiming impermissible deductions. Tax evasion entails deliberate misrepresentation, concealment, suppression and fraud due to which treaty benefits may not be granted and since it is unanimously abhorred, it needs no more discussion at this stage for the purposes of this write-up, whereas, tax avoidance merits a history check so as to understand the impact on tax avoidance being brought in by the introduction of paragraph 1 of Article 6 of the MLI.

The meaning of tax avoidance under the English Law was adjudicated upon as far back as in the case of *IRC V. Duke of Westminster (1936) AC 1 (HL)*, wherein, it was held that tax savings by planning for the same cannot be treated as impermissible tax avoidance. Although this ruling was attractive for others seeking to avoid tax legally by creating complex structures, it has since been weakened by subsequent cases where the courts have looked at the overall effect. An example of the courts' later and more restrictive approach can be seen in the case of *W.T. Ramsay Ltd. Vs. IRC (1981) 1 ALL E.R 865 (HL)*, wherein, it was observed that where a transaction had pre-arranged artificial steps that served no commercial purpose other than to save tax, the proper approach was to tax the effect of the transaction as a whole. It was therefore held in the latter case that where a self-cancelling ready-made device, artificial in nature without an independent business purpose was employed, it was treated as impermissible tax avoidance.

In addition to the above, the meaning of tax avoidance can be viewed from the perspective of verdicts of the Hon'ble Supreme Court of India whereby the Hon'ble Apex Court in India has taken contrasting views on tax avoidance by observing as below:

- The Supreme Court of India in *McDowell & Co. Ltd v. CTO (154 ITR 148)* held that substance was more critical than form and that colourable devices⁷ could not be used for legitimate tax planning.
- The Supreme Court of India in the *Azadi Bachao Andolan* case (263 ITR 706) held that legitimate tax planning cannot be challenged merely on the basis of assumed underlying intentions of tax evasion. The Supreme Court, while commenting on the *McDowell & Co. Ltd* decision, opined that the rule laid down in the *McDowell* case cannot be read as laying down that every attempt at tax planning is illegitimate and must be ignored, or that every transaction or arrangement which is perfectly permissible under law, which has the effect of reducing the tax burden of the taxpayer, must be looked upon with disfavour.

It would be pertinent to state here that in a civil law country, like Mexico, the letter of law prevails over judicial interpretation. As a result of this tradition, the

constitutional principles of 'legality' and 'certainty' drive the relationships between taxpayers and the State. According to these principles, the law should be observed and the consequences described in its text should occur.⁸ Accordingly, Mexico has specifically taken steps towards curtailing tax avoidance, including treaty shopping both in its domestic law and under certain treaties.⁹

In order to check aggressive tax planning especially involving transactions or business arrangements which are entered into with the objective of avoiding tax, tax authorities have brought in General Anti-avoidance Rules (GAAR) in domestic laws. The intolerance of policy makers to abusive tax avoidance transactions is now reflected in tax treaties as well with the introduction of paragraph 1 of Article 6 of the MLI, as the preamble now clearly provides that States shall now enter into a tax treaty with an intent to eliminate double taxation without creating opportunities for tax evasion and tax avoidance, thereby implying, an abusive attempt to take advantage of ambiguities in the legal provisions shall meet the same fate as those involving tax evasion through non-payment of taxes by means of under or non-reporting of true taxable income. This is a significant shift in stance of policy makers the world over.

3. PPT contained in paragraph 1 of Article 7 of the MLI

The Action 6 minimum standard includes a commitment to prevent treaty abuse by adopting anti-abuse rules in tax treaties under which jurisdictions should at a minimum include in their tax treaties either:

- a principal purpose test (PPT) only;
- a PPT and either a simplified or detailed limitation-on-benefits (LOB) provision; or
- a detailed LOB provision, supplemented by anti-conduit mechanisms not already dealt with in tax treaties.

Under the MLI, Article 7 prescribes a minimum standard in the shape of a PPT which reads as below:

"Notwithstanding any provisions of the Agreement, a benefit under the Agreement shall not be granted in respect of an item of income 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 Agreement."

In addition, Article 7 of the MLI also provides for the Simplified LOB (S-LOB) provisions. The detailed LOB¹⁰ rule supplemented by a mechanism that would deal with conduit financing arrangements not already dealt with in tax treaties (one of the recommendations of the BEPS Action 6 Report) is not being implemented through the MLI.

Since the PPT rule is the only approach that can satisfy the Action 6 minimum standard on its own, it is presented as the default option in paragraph 1 of Article 7. The PPT is designed to be invoked where the S-LOB rule cannot extend and to address other forms of treaty abuse, including treaty shopping situations that would not be covered by the S-LOB rule.

The PPT consists of two separate prongs: (i) the subjective test, which determines whether one of the principal purposes of the arrangement is to obtain a treaty benefit; and (ii) the objective test, which determines whether the object and purpose of the relevant treaty provisions is to grant that benefit regardless of the principal purpose. The subjective element is the main rule, while the objective element is the exception that safeguards the treaty benefits denied under the main rule.¹¹

The PPT requires the tax authorities to discharge their burden of proof only with regard to the subjective element, i.e. “whether one of the principal purposes of the arrangement is to obtain a treaty benefit” while the burden is shifted onto the taxpayer with regard to the objective element, i.e. “whether the object and purpose of the relevant treaty provisions is to grant that benefit regardless of the principal purpose”. The standard of proof is evidently higher for the taxpayer, who is required to establish that granting the benefit would be in accordance with the object and purpose of the treaty provision. In this situation, ‘onus’ lies on the taxpayers and their representatives to establish the bonafides of a transaction so as to enable tax officers to draw ‘reasonable’ conclusions.

4. PPT to be read along with the preamble enshrined in paragraph 1 of Article 6 of the MLI

4.1. Preamble of the MLI

At the outset, the preamble of the MLI recognises that MLI is an outcome of a mandate by the G20 nations to the OECD which culminated in the OECD/G20 BEPS Project Reports. The preamble of the MLI *inter alia* includes the provisions of paragraph 1 of Article 6 of the MLI also to make it abundantly clear at the very beginning that the Parties to the MLI recognised the need to ensure that existing agreements for the avoidance of double taxation on income are interpreted to eliminate double taxation with respect to the taxes covered by those agreements 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 those agreements for the indirect benefit of residents of third jurisdictions). This statement included in the preamble of the MLI itself is intended to clarify the strong will of the Parties to the MLI to ensure that, henceforth, covered tax agreements (CTAs) must be interpreted in line with their preamble language which is to be modified through the minimum standard contained in paragraph 1 of Article 6 of the MLI.

4.2. Vienna Convention

The clear statement of the intention of the signatories to a tax treaty that *appears* in the preamble will be relevant to the interpretation and application of the provisions of that treaty. According to the basic rule of interpretation of treaties in Article 31(1) of the Vienna Convention, “[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose” [emphasis added]. Article 31(2) of the Vienna Convention confirms that, for the purpose of this basic rule, the context of the treaty includes its preamble.

4.3. OECD and UN Commentaries on the PPT

PPT provisions must be read in the context of the whole treaty, including its preamble. This is particularly important for the purposes of determining the object and purpose of the relevant provisions of the treaty.¹² The PPT provisions establish that a State may deny the benefits of a treaty where it is reasonable to conclude, having considered all the relevant facts and circumstances, that one of the principal purposes of an arrangement or transaction was for a benefit under a tax treaty to be obtained. The provision is intended to ensure that tax conventions apply in accordance with the purpose for which they were entered into, i.e. to provide benefits in respect of bonafide exchanges of goods and services, and movements of capital and persons as opposed to arrangements whose principal objective is to secure a more favourable tax treatment.¹³ The UN MTC 2017 commentary on the PPT provision contains similar opinion (with appropriate modifications to reflect the inclusion of the general anti-abuse rule in para. 9 of Article 29 of the UN Model) as provided in the OECD MTC 2017.¹⁴ Now, the entire focus of extending treaty benefits has been shifted to undertaking bonafide transactions and preventing double taxation as against securing tax savings through tax avoidance.

4.4. Guidance on the PPT issued by the Australian Taxation Office

Tax Administrations across the world have developed several checks and balances from time to time and issued guidance to their officers for a coherent application of tax rules. The guidance on invocation of PPT issued by the Australian Taxation Office (ATO) vide PS LA 2020/2¹⁵ is a step in the right direction to allay the concerns of various stakeholders, as it provides certainty and transparency in the course of invocation of PPT provisions by tax officials. It is expected that more jurisdictions will follow suit and provide similar guidance to their tax officials.

The guidance issued by the ATO in this regard reads as below:

“The preamble to the relevant CTA (as modified by the MLI), in which the Contracting States express their intention not to create ‘... opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements ...), will be important in determining whether it

would be contrary to the object and purpose of the provisions of the CTA to grant a benefit.”

In the course of issuing the said guidance on PPT, the ATO has been mindful of the fact that the preambular provisions have a significant role to play for the taxpayer to satisfy the objective test of the PPT to determine whether the object and purpose of the relevant treaty provisions is to grant that benefit regardless of the principal purpose. The objective test enshrined in the PPT essentially ensures treaty benefits to the taxpayer even though it is reasonable to conclude that one of the principal purposes of the transaction is to obtain a treaty benefit, provided the taxpayer is able to establish that granting such benefits would be in accordance with the object and purpose of the relevant provisions of the treaty.

4.5. Inference of the above discussion

Thus, the application of the PPT provision is not to be done in isolation but it is to be applied in the context of the treaty including its preamble. However, it needs to be borne in mind that the application of the PPT provision becomes all the more potent when applied in the context of the preamble of tax treaties being brought in by paragraph 1 of Article 6 of the MLI, as the latter now expressly provides that States enter into a tax treaty without creating opportunities for non-taxation or reduced taxation through tax evasion or tax avoidance.

PPT can be invoked when obtaining a benefit under a tax convention is not the sole or dominant purpose of a particular arrangement or transaction. It is sufficient that at least one of the principal purposes was to obtain the benefit. On reading PPT with the preamble under paragraph 1 of Article 6, PPT provisions can now be invoked by tax authorities in situations of non-taxation or reduced taxation arising with an abusive ‘tax avoidance intent’, let alone, non-taxation or reduced taxation arising with a ‘tax evasion intent’. Hence, PPT as read with the preamble can now clearly be invoked to combat treaty-shopping arrangements, abusive tax planning and abusive tax avoidance arrangements or transactions. In addition, the term ‘arrangement or transaction’¹⁶ is to be interpreted broadly and includes any agreement, understanding, scheme, transaction or series of transactions, whether or not they are legally enforceable.

It would suffice to state here that a tax expert has posited that while the preamble may assist in interpreting the language of the PPT itself, it is less helpful in interpreting the specific treaty article whose purpose must also be considered in order to decide when there is an abuse of the treaty while applying the PPT, as the exclusion (where granting a specific treaty benefit would be in accordance with the object and purpose of the relevant provisions of the treaty) may not be sufficiently informed by the new preamble.¹⁷ That being said, based on the discussions *supra*, it may be emphasised that if in any arrangement the object and purpose

of the treaty is getting defeated and is creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (which is now specifically forbidden by the preamble), any favourable interpretation (to the taxpayer) of the specific treaty article may not hold good and a tax authority may proceed to hold that there is an abuse of the treaty while applying the PPT. Also, the international tax policy of each country, which may vary from one treaty partner to the other as reflected in the respective bilateral treaties, shall function under the overarching rules now set by the preamble that the treaty shall henceforth not be interpreted in any manner which leads to creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance.

5. Conclusion

PPT provisions must be read in the context of the whole treaty, including its preamble, thereby implying that the PPT provisions are to be read in conjunction with the preamble, i.e., the key to application of PPT provisions lies in the preamble itself. PPT as read with the preamble is designed to override the other provisions of a CTA and shall apply not only to provisions allocating or limiting taxing rights, but also to any general or specific anti-avoidance rules in the CTA.

There is a famous saying in cricket (a sport invented by the British and very popular in the Indian sub-continent, Asia-Pacific, Caribbean, parts of Europe, Africa and the Middle-East) that “fast bowlers hunt in pairs”. Some of the prominent exponents who exemplify this saying are Charlie Griffith-Wes Hall, Dennis Lillee-Jeff Thomson, Andy Roberts-Michael Holding ably supported by Malcolm Marshall-Joel Garner, Wasim Akram-Waqar Younis, Courtney Walsh-Curtly Ambrose, and similar other legendary pairs. One required Gavaskaresque (Sunil Gavaskar - a famed batsman from India) technique of playing with a straight bat to fend off such fearsome bowlers. Likewise, pairing of PPT and the Preamble is a test for multinational enterprises (MNEs) harbouring ambitions of applying abusive tax avoidance arrangements or transactions. It is high time that MNEs start applying the Gavaskaresque technique of playing with a straight bat, failing which, it can be emphatically concluded that deployment of abusive tax avoidance arrangements or transactions by MNEs is henceforth going to be an extremely risky proposition.

That being said, the preamble also provides that States enter into a tax treaty so as to eliminate double taxation which in turn facilitates investment of capital, seamless flow of technology and overall acceleration in the business environment. Hence, tax authorities in any part of the world may not be inclined to invoke PPT as read with the preamble in respect of any arrangement or transaction when taxpayers are able to discharge their onus establishing that (below mentioned conditions to be satisfied in tandem):

- genuine business and commercial reasons for a transaction exist;

- a purpose for the transaction cannot be ascribed to non-taxation or reduced taxation through tax evasion or tax avoidance;
- despite no tax advantages, the transaction would be carried out exactly in the same way; and
- it cannot reasonably be considered that one of the principal purposes of the arrangement or transaction is to obtain treaty benefits and that the object and purpose of the treaty is getting defeated.

As far as implementation of PPT by tax authorities is concerned, the UN MTC 2017 Commentary on PPT has provided very insightful guidance.¹⁸ In addition, the guidance on invocation of PPT issued by ATO vide PS LA 2020/2 is a step in the right direction to allay the concerns of various stakeholders, as it provides certainty and transparency in the course of invocation of PPT provisions by tax officials. It is expected that more jurisdictions will follow suit and provide similar guidance to their tax officials.

Endnotes:

¹ Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion & Profit Shifting (MLI), para. 1.

² Though the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MCMAA) precedes the MLI, the former is primarily confined to facilitating the exchange of information between the signatory jurisdictions, whereas, the latter's impact over tax treaties is much wider and far-reaching as it is one of the outcomes of the OECD/G20 Project to tackle BEPS.

³ Signatories and Parties to the MLI - status as of 29 June 2021.

⁴ Composition of the Inclusive Framework as of 29 July 2021.

⁵ The Organisation for Economic Co-operation and Development (OECD), *OECD/G20 Inclusive Framework on BEPS Progress report July 2019 – July 2020* (Paris, 2020) (Box 1 on page 21). Available from <https://www.oecd.org/tax/beps/oecd-g20-inclusive-framework-on-beps-progress-report-july-2019-july-2020.pdf>.

⁶ OECD, *OECD/G20 Base Erosion and Profit Shifting Project, 2015 Final Reports, Action 6* (Paris, 2015). Available from <http://www.oecd.org/tax/beps-2015-final-reports.htm>.

⁷ Colourable devices mean resorting to dubious methods and subterfuges as part of tax planning.

⁸ Daniel Fuentes Hernández and César Alejandro Ruiz Jiménez, "Mexico", in *GAARs – A Key Element of Tax Systems in the Post-BEPS Tax World*, Michael Lang et al., eds. (Amsterdam, IBFD, 2016). Available from https://research.ibfd.org/#/doc?url=/linkresolver/static/gaar_c20&refresh=1629280075656%23gaar_c20.

⁹ International Fiscal Association, "Reconstructing the treaty network", *Cahiers de Droit Fiscal Internationale*, Volume 105A (2020). Available from

https://research.ibfd.org/#/doc?url=/linkresolver/static/ifacahier_2020_volume1_mexico.

¹⁰ Explanatory Statement to the MLI. para. 90.

¹¹ Ameya Mithe, "Critical Analysis of the Principal Purpose Test and the Limitation on Benefits Rule: A World Divided but It Takes Two to Tango" *World Tax Journal*, vol. 12, no. 1 (2020). Available from https://research.ibfd.org/#/doc?url=/collections/wtj/html/wtj_2020_01_in_1.html.

¹² OECD Model Tax Convention (MTC) 2017 – para. 173 of the Commentary on Article 29.

¹³ *Ibid.*, para. 174.

¹⁴ United Nations (UN) Model Tax Convention (MTC) 2017 – para. 37 of the Commentary on para. 9 of Article 29.

¹⁵ Australia, Australian Taxation Office's PS LA 2020/2. Available from [https://www.ato.gov.au/law/view/view.htm?docid="PSR%2FPS20202%2FNAT%2FATO%2F00001"](https://www.ato.gov.au/law/view/view.htm?docid=).

¹⁶ OECD, *BEPS 2015 Final Report*.

¹⁷ Jonathan Schwarz, "The Impact of the New Preamble on the Interpretation of Old and New Treaties and on the Policy of Abuse Prevention". Available from https://research.ibfd.org/#/doc?url=/collections/bit/html/bit_2020_04_o2_1.html.

¹⁸ UN MTC 2017 – para. 40 of the Commentary on paragraph 9 of Article 29.

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Efforts to reform international cooperation in tax matters are exhibiting a distinct acceleration. The direction of change must recognize and incorporate innovations in developing country policies and approaches, otherwise the outcomes will obstruct practical paths to development.

The policy brief series is intended as a tool to assist in further dialogue on needed reforms.

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