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CBDT

Guidance for application of the Principal Purpose Test (PPT) under India's Double Taxation Avoidance Agreements-re

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CBDT - GUIDANCE FOR APPLICATION OF THE PRINCIPAL PURPOSE TEST (PPT) UNDER INDIA'S DOUBLE TAXATION AVOIDANCE AGREEMENTS-REG

CORPORATE LAWS

Authority

Central Board of Direct Taxes

Circular Date

Jan 21, 2025

Circular Number

01/2025 F. No. 500/05/2020/FT&TR-11

Effective Date

Jan 21, 2025

Applicability:

Applicable to all foreign investors, multinational corporations, Indian companies with overseas transactions, financial institutions, tax professionals, and non-resident individuals claiming treaty benefits.

The Principal Purpose Test (PPT) is a key anti-abuse provision introduced through the Multilateral Instrument (MLI) and bilateral treaty amendments in India's Double Taxation Avoidance Agreements (DTAAs)

- It aims to prevent treaty abuse and revenue loss by denying benefits if one of the principal purposes of a transaction is to obtain a tax advantage.

Scope & Application of PPT

- The PPT applies prospectively to transactions and arrangements.
- For DTAAs amended through bilateral processes (e.g., Chile, Iran, Hong Kong, China), it applies from the date of entry into force of the treaty or amending protocol.
- For DTAAs amended through the MLI, it applies from the date specified under Article 35 of the MLI**,** based on when the MLI enters into force for both jurisdictions.

Interaction with Treaty-Specific Grandfathering Provisions

- Certain DTAAs, such as India-Cyprus, India-Mauritius, and India-Singapore, include grandfathering provisions that are not affected by the PPT.
- These provisions continue to apply as per their respective treaties, ensuring clarity for investors relying on them.

Guidance on PPT Interpretation

The assessment of whether a transaction's principal purpose is tax-driven must be objective and fact-based.

Tax authorities may refer to:

- The BEPS Action Plan 6 Final Report **(**subject to India’s reservations).

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- UN Model Tax Convention (2021) Commentaries on Articles 1 and 29 as supplementary guidance.

Implications for Businesses & Taxpayers

- Increased scrutiny on cross-border structures and tax benefits claimed under India's DTAAs.
- Taxpayers must maintain robust documentation to justify transactions under commercial substance principles.
- Investors relying on treaty benefits should review structures in light of PPT enforcement.

The CBDT's guidance provides much-needed clarity on PPT enforcement in India. Businesses and tax professionals should assess their treaty benefits and align tax structures with commercial realities to ensure compliance.

SOURCE: Click here for more details

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