Multilateral Instrument (MLI)

Why in news?

\n\n

India recently became the signatory of the Multilateral Instrument (MLI).

\n\n

What is MLI?

\n\n

\n
- It is an agreement put out by OECD to prevent base erosion and profit shifting (BEPS).
\n
- It will help them crack down on abuse of bilateral tax treaties and treaty shopping.
\n
- India and 68 other jurisdictions became signatories of MLI.
\n
- MLI will preside over 2,300 treaties worldwide.
\n
- It is expected to be transparent and balanced in dispute resolution.
\n
- Under GAAR, the taxman has powers to look into any corporate transactions.
\n
- But MLI has set principal purpose test (PPT) and limit of benefit (LoB) measures, which if fulfilled will shield entities from "harassment".
\n

\n\n

What is GAAR?

\n\n

\n
- India has a similar arrangement called GAAR to prevent the abuse of treaty for gaining undue tax benefit.
\n
- General Anti-Avoidance Rule (GAAR) was part of the 2012-13 Budget speech

to check tax evasion and avoidance.
\n

- It was originally to be implemented from April 1, 2014 but came into effect from April 1, 2017.
\n
- GAAR gives sweeping powers to the taxman.
\n
- It gives tax department the right to scrutinise transactions if they believe that they are structured for the purpose of avoiding taxes.
\n
- It contains provision allowing the government to prospectively tax overseas deals involving local assets.
\n
- There have been fears that the government may use it to target P-Notes.
\n
- To avoid tax altogether under GAAR, an investor may have to prove that P-Notes were not set up specifically to avoid paying taxes.
\n

\n\n

What are the issues?

\n\n

\n

- It is unsure whether GAAR or the MLI will prevail over the other.
\n
- But the spirit of the MLI may be crushed if domestic laws override it in the event of conflicts.
\n
- MLI, Action Plan 6 states that where a conflict does arise, ordinarily MLI provisions will prevail.
\n
- But a government document on GAAR explicitly states that the domestic law overrides every other law in case of disputes.
\n
- Also Mauritius and Singapore, the major contributors of FPI flow into India, are yet to sign the MLI.
\n
- If they keep India as a reserve country, and opt out of a deal with India, it raises the prospects of conflicts.
\n

\n\n

Quick Fact

\n\n

Base erosion and profit shifting (BEPS)

\n\n

\n

- It refers to tax planning strategies used by multinational companies to exploit gaps and mismatches in tax rules.
\n
- They artificially shift profits to low or no-tax locations where there is little or no economic activity.
\n
- In general BEPS strategies are not illegal, rather they take advantage of different tax rules operating in different jurisdictions.
\n

\n\n

\n\n

Source: Business Line

\n