wts dhruva consultants

INTERNATIONAL RULINGS ON BENEFICIAL OWNERSHIP

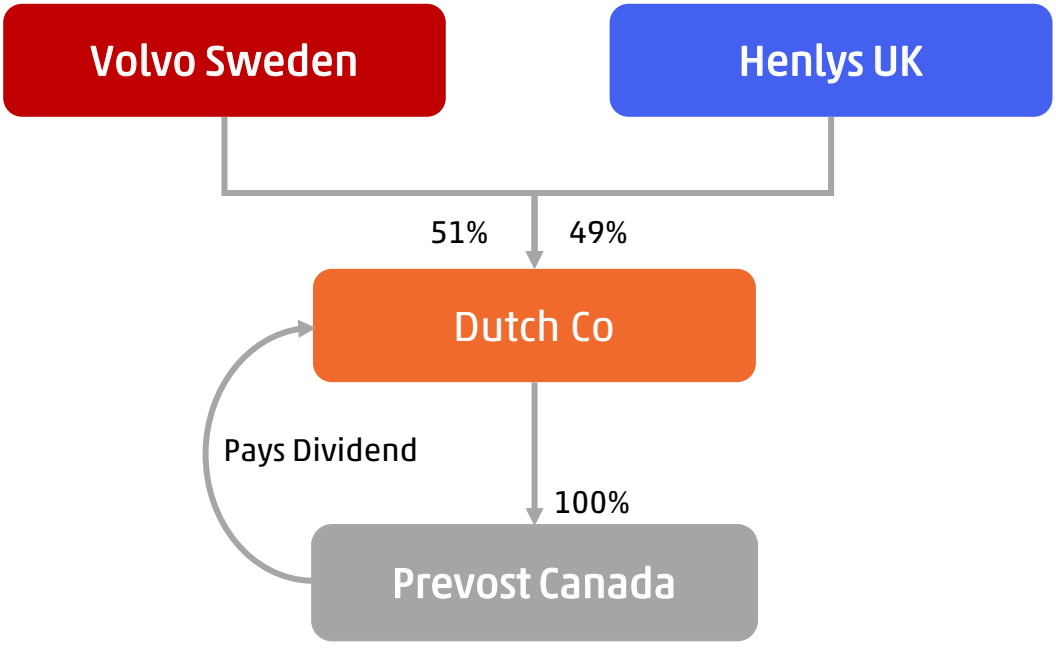
Swipe

CASE 1 – PREVOST CANADA

Volvo Sweden and Henlys UK, entered into an agreement to acquire 51% and 49% stake respectively in a Canadian automobile company, Prevost Canada.

Instead of a direct acquisition, investment in Prevost Canada was made through a Dutch Co (Netherlands company). *Corporate structure depicted in the diagram.*

Volvo Sweden and Henlys UK jointly agreed as shareholders that at least 80% of Prevost Canada **and** Dutch Co's profits were to be distributed as dividends every year. Notably, Dutch Co was **not** a party to this Shareholder agreement.



CASE 1 – WHAT WAS THE ISSUE?

Dividends paid by Prevost Canada to Dutch Co were offered to tax in Canada at 5% by the Dutch Co.

Canadian Revenue Authority argued that **the Dutch Co is not the beneficial owner** of dividend. Instead, Volvo Sweden and Henlys UK are the beneficial owners. Consequently, dividends should be taxed at 15% (as per Canada-Sweden Tax Treaty) and 10% (as per Canada-UK Tax Treaty), not 5%.

Dutch Co on the other hand argued that **tax was a consideration** for its incorporation, but **not an overriding consideration**.

Dutch Co was incorporated because Volvo Sweden and Henlys UK wanted to make the investment from a neutral jurisdiction (i.e., any place other than Sweden and UK).

CASE 1 – WHAT DID THE TAX COURT SAY?

Tax Court held **Dutch Co to be the beneficial owner** for following reasons:

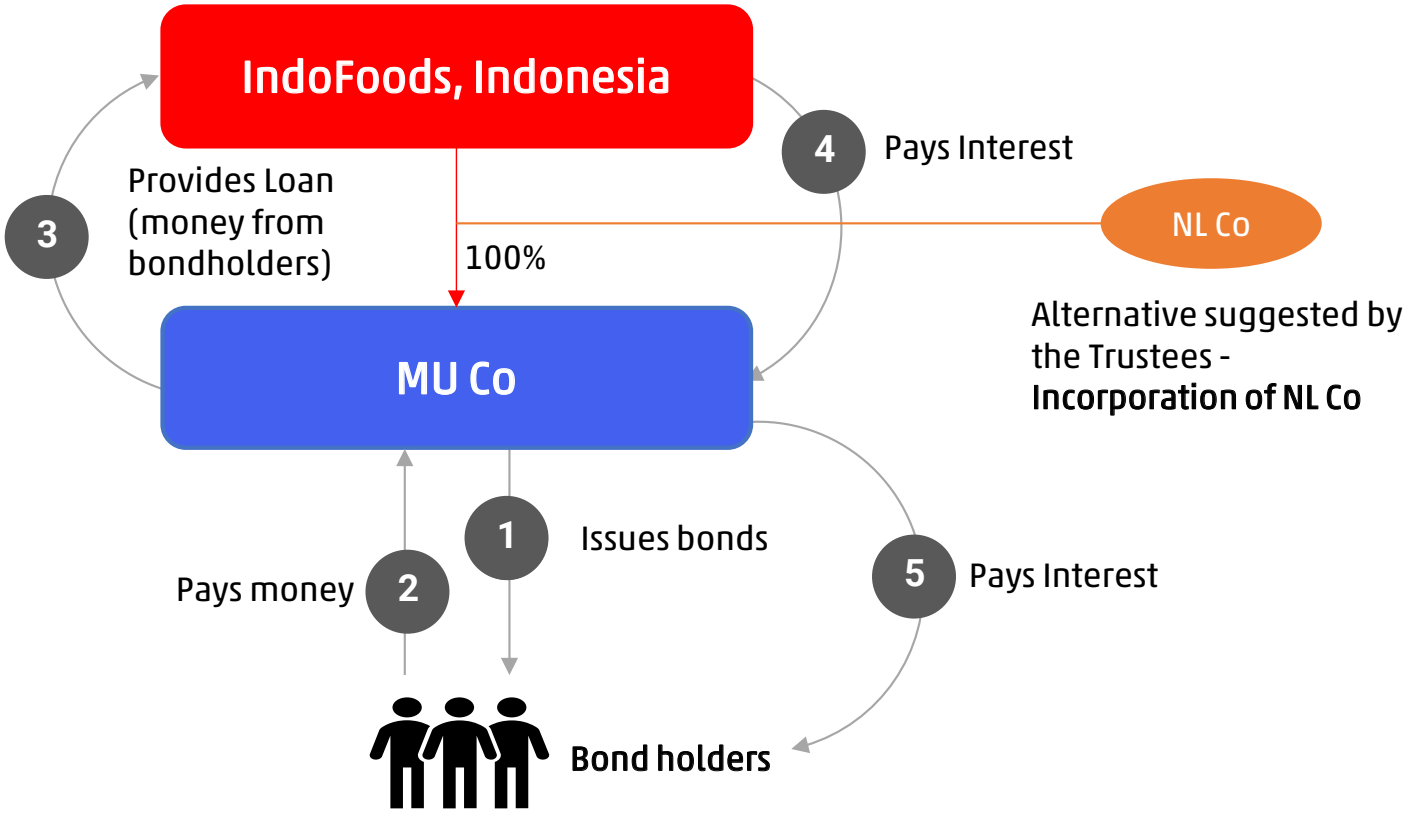
- Dutch Co was an operating company. **Registered ownership** of Prevost shares **cannot be disregarded** unless it is established that Dutch Co is a shell or conduit;
- Dutch Co **enjoyed** the dividends in the **manner it saw best fit**; and
- Dutch Co was **not** a party to the Shareholder Agreement. Hence, it was **not under an obligation to pay the dividends** received by it (from Prevost Canada) to its shareholders.

CASE 2 – INDOFOODS

Indofoods, an Indonesian company, wanted to raise finance from foreign investors by issuing interest bearing bonds. Accordingly, it undertook the following:

- Indofoods incorporated a Mauritius Subsidiary (MU Co) and bonds were issued by MU Co to the foreign investors.
- MU Co in turn lent bond proceeds to Indofoods as 'Loan' on the same terms at which it borrowed funds.
- Interest on loan paid by Indofoods to MU Co was taxed at 10% under Mauritius-Indonesia Tax Treaty.
- Interest paid to foreign bondholders by MU Co was not subject to any tax in Mauritius.

CASE 2 – INDOFOODS



Had Indofoods issued the bonds directly to the foreign investors, interest would have been taxed at 20% under Indonesian domestic law.

CASE 2 – SUBSEQUENT EVENTS

Indonesia terminated its Tax Treaty with Mauritius because of Tax Treaty abuse through conduit / shell companies. Consequently, withholding tax rate on interest payments by Indofoods to MU Co increased to 20%.

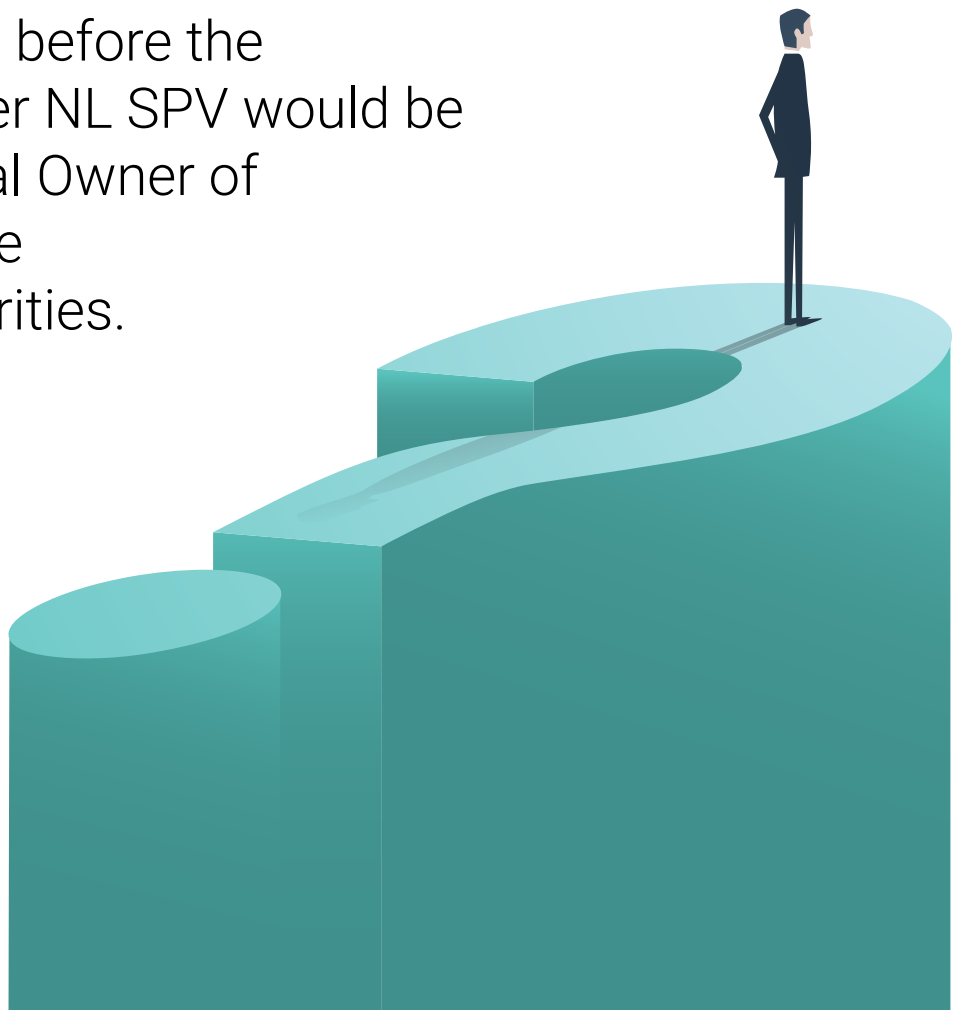
Bond agreement had a '**get out**' clause providing for early redemption in case of tax increase. Indofoods sought to invoke the clause and redeem the bonds.

CASE 2 – WHAT WAS THE ISSUE?

Bond holder's Trustee, being a resident of UK filed a suit in the UK Court against early redemption. It was argued that lower tax rate can be continued by interposing a new SPV in the Netherlands (NL Co) between Indofoods and MU Co.

As per the Indonesia-Netherlands Tax Treaty, withholding tax rate on interest payments by Indofoods to NL Co would be 10%, **if NL Co was the beneficial owner** of interest income.

The primary question before the UK Court was whether NL SPV would be regarded as Beneficial Owner of interest income by the Indonesian tax authorities.



CASE 2 – WHAT DID THE UK COURT SAY?

The Court held that **NL Co was not the beneficial owner** of interest income as it **did not directly benefit** from the interest income. Structure of the loan arrangement was such that NL Co was **legally obliged to pay the interest** income which it received from Indofoods to the foreign bondholders **within a day** of its receipt.

PARTING THOUGHTS

It is clear from the above judgements that there are no uniform rules to examine existence of beneficial ownership.

Generally, if an arrangement / structure is adopted with the **sole purpose of obtaining tax benefit**, it may not satisfy the beneficial ownership test.

On the other hand, if there are **business considerations** in adopting a particular arrangement / structure and **tax considerations do not have an overriding role**, beneficial ownership can be said to exist.

Do you avail Tax Treaty rates for passive incomes from overseas countries? If so, have you evaluated existence of beneficial ownership?

CONTACT US

WTS Dhruva Consultants
207, Emaar Square, Building 4,
PO Box 127165, Dubai, UAE

corporatetax@dhruvaadvisors.com

Website:
https://www.wts-dhruva.com/

OUR TEAM

Nimish Goel

K Venkatachalam

Dinesh Khator

Kapil Bhatnagar

Harpal Chudasama

Jairajesh Nadar

Rachana Bhandari