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THE FULLERTON RULING: HAS THE ITAT TURNED THE LOB TEST INTO A DE FACTO PPT?

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Introduction

India's tax treaties typically contain two types of provisions that limit treaty access in certain situations. These are:

- The Principal Purposes Test ("**PPT**"), which aims to deny treaty benefits where it is reasonable to conclude that "one of the principal purposes" of any arrangement or transaction was to avail such benefits. The PPT has been incorporated into many of India's tax treaties following its adoption of the Multilateral Convention to Implement Tax Treaty Related Provisions to Prevent Base Erosion and Profit Shifting ("**MLI**").

- The Limitation of Benefits ("**LOB**") test, which aims to curb treaty shopping through objective tests based on expenditure or activity thresholds. India's tax treaties with both Singapore ("**Singapore Treaty**") and Mauritius ("**Mauritius Treaty**") contain an LOB clause. The Singapore Treaty also now incorporates a PPT.

Since the introduction of the PPT, courts have faced several interpretational and practical issues relating to its scope and application. Amidst this evolving environment, the Income Tax Appellate Tribunal ("**ITAT**") has in a recent decision blurred the boundaries between the traditionally narrow and objective LOB test and the wider PPT standard.

In *Fullerton Financial Holdings Pte Ltd v. ACIT*,[1] the ITAT suggested that the LOB test in article 24A(1) of the Singapore Treaty must be interpreted and applied similarly to the PPT under article 29A of the Treaty. Article 24A(1) denies claims for Indian tax relief on capital gains arising from the alienation of shares of an Indian company that were acquired prior to April 1, 2017 ("**Grandfathered Shares**") if the claimant's affairs were arranged with the primary purpose of taking advantage of that relief.

While the ITAT ultimately ruled in favour of the taxpayer on the facts, its approach raises critical questions for others claiming relief under the Singapore Treaty in respect of Grandfathered Shares. The ruling may also impact claims under the Mauritius Treaty, which contains similar provisions. This article contextualizes the ITAT's ruling and examines its broader implications.

1 Order dated October 28, 2025 in ITA No. 1137/Mum/2025.

Background

The taxpayer in this case was a wholly-owned Singaporean subsidiary of Temasek, the Singapore Government's investment arm. The taxpayer operated as an investment holding platform for Temasek's financial services portfolio across Asia.

In Financial Year ("**FY**") 2008-09, the taxpayer had invested in Fullerton India Credit Co Ltd ("**Target**"), an Indian non-banking financial company engaged in the SME and micro finance sector, for an ~3.79% stake. In FY 2021-22, the taxpayer sold its entire stake in the Target to the Sumitomo Mitsui Financial Group, Japan and earned long term capital gains of approximately INR 6.81 billion.

In its return of income, the taxpayer claimed this gain to be exempt under article 13(4A) of the Singapore Treaty, which exempts a Singapore resident from Indian tax on capital gains arising from the alienation of Grandfathered Shares.

Importantly, the benefit under article 13(4A) is subject to the satisfaction of the LOB test in article 24A of the Singapore Treaty, which denies that benefit if:

- the affairs of the claimant are arranged with "the primary purpose" to take advantage of such benefit;[2] or
- if the claimant is a "shell or conduit company", with negligible or no business operations or with no real and continuous business activities in Singapore.[3] An entity cannot be labelled a "shell or conduit company" if it is listed on a recognized stock exchange in Singapore, or if its "annual expenditure on operations" in Singapore equals or exceeds SGD 200,000 during each of the two 12-month periods in the period of 24 months before the date on which the gains arose.[4]

To support its exemption claim, the taxpayer submitted two letters from the Inland Revenue Authority of Singapore ("**IRAS**") and KPMG Singapore certifying that its annual operating expenditure in Singapore exceeded SGD 200,000 in each of the two 12-month periods preceding the date on which the gains arose.

The Indian Income Tax Department ("**ITD**") denied treaty relief and made an assessment of capital gains tax against the taxpayer on the basis that:

- most of the taxpayer's expenses were "management fees" recharged to it by FFH (International) Pte Ltd ("**FFHI**"), a group entity incorporated in Singapore from which the taxpayer had availed payroll and other services, which could not be considered "expenditure on operations" for the purposes of article 24A;
- the taxpayer had failed to provide details of the number of hours spent by FFHI employees working for the taxpayer's benefit, the quantum of services consumed by the taxpayer, and documentation showing that the payroll costs incurred by FFHI were truly for the taxpayer's benefit;
- the letters from the IRAS and KPMG did not represent valid evidence, as the Singapore Treaty did not provide for or recognize such letters;

2 Article 24A(1) of the Singapore Treaty. The Explanation to article 24A states that the cases of legal entities not having bona fide business activities shall be covered by article 24A(1).

3 Article 24A(2) of the Singapore Treaty.

4 Article 24A(4) of the Singapore Treaty.

- expenses such as directors' fees were not supported by any benchmarking; and
- insurance premia paid on behalf of directors or officers, without them being formally appointed by the taxpayer, could not constitute operating expenditure.

The taxpayer appealed the assessment to the ITAT.

The ITAT's Ruling

The ITAT allowed the appeal. It held that the taxpayer had satisfied the "PPT" under article 24A(1) of the Singapore Treaty since obtaining the benefit of article 13(4A) was not the "primary purpose" of the impugned transaction, for the following reasons:

- ***Sufficient Economic Substance:*** The taxpayer was not a "conduit company"; it was independently managed, had economic substance, and exercised operational control over its income and investments. The taxpayer's governance and management was carried out by an experienced board of directors. All key investment decisions were made at regular board meetings.
- ***Justified Motives:*** The taxpayer was incorporated in Singapore for sound commercial reasons, and its overall conduct indicated that its affairs were not arranged with the "primary purpose" of taking advantage of article 13(4A) of the Singapore Treaty. The taxpayer had made a long-term strategic investment that aligned with its regional objectives, which was not a tax-motivated arrangement. The sale of that investment represented a genuine commercial realization.
- ***Bona fide Expenses:*** Management fees and employee remuneration (including director fees) paid by the taxpayer represented consideration for services received in the ordinary course of business. These expenses were reimbursed by the taxpayer to FFHI on arm's length terms, in accordance with Singaporean transfer pricing regulations. Insurance premia were paid to protect directors and officers against liabilities arising in the discharge of their official duties. Hence, all expenses constituted bona fide operating expenditure.
- ***Evidence of Expenditure:*** The letters issued by the IRAS and KPMG, supported by invoices, contracts, and schedules of significant expenditures, established that the taxpayer had satisfied the minimum operating expenditure test prescribed under article 24A of the Singapore Treaty.
- ***Sovereign Ownership:*** The taxpayer was a subsidiary of Temasek, which was wholly owned by the Singapore Government. From a beneficial ownership standpoint, the taxpayer's income was really the income of the Singapore Government, which, in any event, could not be subjected to Indian tax by virtue of the principle of sovereign immunity.

Analysis

Although the ITAT's reaffirmation of the Singapore route for genuine investments is welcome, its reasoning creates additional challenges for taxpayers claiming Singapore Treaty benefits on Grandfathered Shares. Some of the key considerations arising from the order are discussed below:

- ***Source of Law:*** The ruling appears to stem from a fundamental confusion on the

source of the PPT rather than deliberate judicial evolution. In its order, the ITAT states that "*The Principal Purpose Test (PPT) was introduced under Article 24A of the India-Singapore DTAA by way of the Third Protocol (…)*". This is factually incorrect. The Third Protocol to the Singapore Treaty (2016) amended the *LOB provisions* in article 24A. The PPT on the other hand is a product of the MLI (2018) and only took effect from October 1, 2019. This conceptual error perhaps explains why the ITAT proceeded to apply the "primary purpose" test in article 24A as if it were the subjective "principal purposes" test of the MLI.

- ***Conflating LOB and PPT:*** The PPT is a broad test that looks at whether *one of* the principal purposes of any *arrangement* is to obtain a tax benefit. By contrast, the "primary purpose" test in article 24A(1) operates within a narrower scope, applying only where the *affairs* of a claimant are arranged with *the* primary purpose of taking advantage of the capital gains relief on Grandfathered Shares available under article 13 of the Singapore Treaty. By treating "the primary purpose" limb of article 24A(1) as analogous to the PPT, the ITAT effectively reads the PPT test into the LOB test, superimposing a PPT style broader inquiry into article 24A(1). If this interpretation gains wider acceptance, it could reshape how the ITD applies article 24A(1) of the Singapore Treaty. It poses an even greater risk for claims under the Mauritius Treaty, which contains a similar LOB provision (article 27A), but *does not incorporate* the PPT, as it is outside the MLI's coverage.

- ***Satisfying the "primary" purpose:*** The ITAT initially held that the *subjective* criteria of the PPT must be met to pass the LOB test under article 24A(1) of the Singapore Treaty and claim relief on Grandfathered Shares. Yet, it paradoxically relied on the taxpayer's compliance with the *objective* SGD 200,000 expenditure threshold in article 24A(4) to conclude that this subjective test was satisfied. By using an objective metric to satisfy a subjective test, the ruling creates significant uncertainty on how these tests should be applied to secure treaty benefits.

- ***Administrative Conflict:*** The Central Board of Direct Taxes ("**CBDT**") had issued a circular on January 21, 2025 clarifying that the PPT only applies prospectively i.e., from the date from which the MLI took effect with respect to a tax treaty.[5] However, by effectively reading the PPT into the LOB test in article 24A(1) of the Singapore Treaty, the ITAT has potentially created a pathway for the ITD to rely on PPT-based arguments even in cases that are otherwise not subject to the PPT.[6]

Conclusion

The ITAT's ruling comes as a mixed bag. On the one hand, the ITAT has held in favor of the taxpayer and upheld entitlement to capital gains tax relief on Grandfathered Shares under the Singapore Treaty. On the other hand, its approach in the application of the "primary purpose" test has resulted in more confusion and potential new challenges for taxpayers seeking treaty relief.

What makes the ruling particularly striking is that the ITAT had a far simpler – and more logical – resolution readily available. When the Singapore Treaty was first notified in 1994, it did not provide a specific exemption from source-state taxation of capital gains arising from the alienation of shares. That benefit was introduced only in 2005 by way of

5 Circular No. 01/2025 dated January 21, 2025, F. No. 500/05/2020/FT&TR-II.

6 Especially since coordinate benches of the ITAT have recently ruled that the PPT cannot be invoked unless it is specifically incorporated into a tax treaty via a treaty-specific notification. ***See*** *Sky High Appeal XLIII Leasing Company Ltd v. ACIT*, order dated August 13, 2025 in ITA No. 1122/Mum/2025; and *Kosi Aviation Leasing Ltd v. ACIT*, order dated September 30, 2025 in ITA No. 994/Del/2025. The Indian Government has not issued any such notifications as yet.

an amending protocol. The taxpayer was incorporated in 2003, *two years before* that benefit was even introduced. In these circumstances, the argument that the taxpayer was a conduit or that it was structured with the "primary purpose" of securing that benefit was inherently absurd. The ITAT could have disposed of the matter on this finding alone. Instead, it chose a path that raises more questions than answers on treaty access for foreign taxpayers.