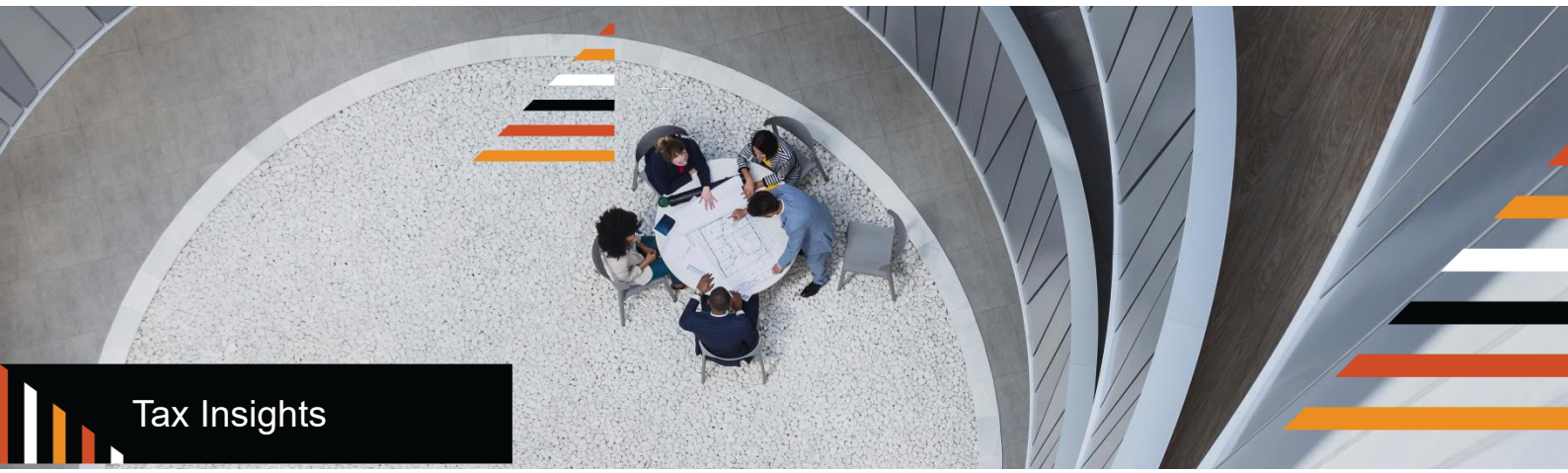

17 February 2022

Protocol is an integral part of DTAA; requirement of a separate notification mandated by a recent CBDT circular to take benefit of MFN clause cannot be applied retrospectively – Pune bench of the Tribunal

In brief

The Pune bench of the Income-tax Appellate Tribunal (Tribunal)[1] held that the protocol is an integral part of the Double Taxation Avoidance Agreement (DTAA), which gets automatically notified with the DTAA. The pre-requisite of a separate notification to be issued by India to import the benefits of the DTAA with the second state to the DTAA with the first state by virtue of the Most Favoured Nation (MFN) clause is a fresh requirement mandated by the Central Board of Direct Taxes (CBDT) circular[2] (CBDT circular), which cannot be applied retrospectively to transactions taking place prior to its date of issuance. The Tribunal observed that the CBDT circular exceeds the boundaries of section 90(1) of the Income-tax Act, 1961 (the Act) and is not binding on the taxpayer or the Tribunal or other appellate authorities.

In detail

Facts

- The taxpayer, a company incorporated in Spain, offered to tax its receipts as royalty and fees for technical services at a lower rate or 10% by taking benefit of the MFN clause under the protocol to the India-Spain DTAA and resorting to the India-Portugal DTAA.
- The Tax Officer (TO) denied the benefit by holding that invoking the MFN clause requires issuance of notification by the Government of India. In the absence of such notification for the India-Portugal DTAA, the TO taxed the receipts at 10% plus surcharge and cess under the Act.

Tribunal's ruling

The Tribunal observed that the CBDT circular lays down pre-requisites for deriving the benefit of the MFN clause in the protocol to India's DTAAs with certain countries, which inter-alia includes a need for separate notification to be issued by India to import the benefit of DTAA with the second state to the DTAA with the first state. In the given case, all pre-requisites, other than the issuance of a separate notification by India, were

1 ITA No. 202/ PUN/ 2021

2 CBDT Circular No. 3/ 2022 dated 3 February 2022. You may refer to our Tax Insights dated 5 February 2022.

fulfilled.

The Tribunal held that the requirement of separate notification for implementing the MFN clause cannot be invoked for the year under consideration, which is much prior to the date of issuance of the CBDT circular. The Tribunal observed as follows:

- The protocol containing the MFN clause, being an integral part of the India-Spain DTAA, got automatically notified when the India-Spain DTAA was notified. There was no need for any separate notification in terms of section 90(1) of the Act.
- The CBDT circular is binding on TO and not on the taxpayer or the Tribunal or other appellate authorities. The given CBDT circular exceeds the boundaries of section 90(1) of the Act and cannot bind the Tribunal.
- The pre-requisite for a separate notification to be issued by India is an additional detrimental requirement mandated by the CBDT circular for taking benefit conferred by the DTAA, which cannot be applied retrospectively.

Based on the above, the Tribunal concluded that the lower authorities were not justified in denying the benefit of the lower tax rate of 10% as per the India-Portugal DTAA.

The takeaways

This is a welcome decision from the Pune bench of the Tribunal, which reaffirms the view that protocol, being an integral part of the DTAA, does not require to be notified separately, in line with the earlier decision of Indian Courts[3]. Although the Tribunal observed that the given CBDT circular exceeds the boundaries of section 90(1) of the Act, it ultimately concluded that the requirement of a separate notification imposed by the CBDT circular cannot be invoked for the period prior to date of issuance of the CBDT circular (i.e. 3 February 2022).

It would be interesting to see how other benches of the Tribunal and Indian Courts deal with this issue, particularly in the context of the requirement of a notification for the transactions post 3 February 2022.

The Tribunal did not discuss the other conditions laid down by the CBDT circular, such as that the second state should be a member of the Organisation for Economic Co-operation and Development at the time of signing the DTAA with India, since the said pre-requisites were satisfied in the given case.

[3] Steria (India) Limited *v.* Commissioner of Income-tax-VI [2016] 386 ITR 390 (Delhi)

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