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# TAX FLASH NEWS

16 February 2022

## No separate notification is required to avail the benefit of 'Most Favoured Nation' clause

Recently, the Pune Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of GRI Renewable Industries S.L.[1] (the taxpayer) dealt with the issue of whether a separate notification is required for granting the benefit of the Most Favoured Nation (MFN) clause under the India-Spain tax treaty (tax treaty). The Tribunal observed that once the tax treaty is notified, the Protocol, which is an integral part of the tax treaty, also gets automatically notified along with the tax treaty. Therefore, a separate notification is not required for granting benefit under the MFN clause. The Central Board of Direct Taxes (CBDT) Circular[2] specifying the need for a separate notification for importing the beneficial treatment from another tax treaty, overlooks the plain language of the provisions of Section 90(1) of the Income-tax Act, 1961 (the Act), which treats the MFN clause as an integral part of the tax treaty.

The Tribunal observed that the Circular issued by the CBDT is binding on the Assessing Officer (AO) and not on the taxpayer or the Tribunal or other appellate authorities.

### Facts of the case

The taxpayer is a foreign company (Resident of Spain) and in relation to Financial Year 2015-16 received payment for providing technical support, financial support and advice, legal support, commercial support, etc. It had also received payment for SAP software and implementation of process model. The taxpayer declared the above amounts as 'fees for technical services' (FTS) and 'royalties' respectively, claiming them as covered under Article 13 of the tax treaty. Relying on the Protocol to the tax treaty having MFN clause read with Article 12 of the India-Portuguese tax treaty, the taxpayer claimed that such 'royalties' and FTS were taxable at 10 per cent instead of 20 per cent as provided in the tax treaty.

The AO held that the tax rate of 10 per cent applied by the taxpayer under the India-Portuguese tax treaty could not be applied because Section 90(1) specifically requires the issuance of necessary Notification by the Government of India. In order to import an MFN clause from another tax treaty having lower rate of tax or narrower scope of the definition of certain clause, it is necessary that such importing of the clause must be notified. In the absence of any notification, the AO held that the benefit of the relevant Article of the India-Portuguese tax treaty was not available to the India-Spain tax treaty in terms of the Protocol.

The Dispute Resolution Panel (DRP) upheld the order of the AO. Aggrieved, the taxpayer filed an appeal before the Tribunal.

### Tribunal's decision

India and Spain signed a tax treaty on 8 February 1993, which entered into force on 12 January 1995 and was notified on 21 April 1995. The said tax treaty contains Protocol which provides MFN clause *qua* 'royalties' and FTS. Such Protocol was also signed by both the Governments on the same date. The opening part of the Protocol states that: 'At the moment of signing the India-Spain tax treaty, the undersigned have agreed upon the following provisions which shall be an integral part of the Convention.' It is clear from the opening part of the Protocol, duly signed by the competent authorities of both the countries on the same date on which the tax treaty was signed, that the Protocol has been treated as 'an integral part of the tax treaty'.

The Tribunal observed that once the India-Spain tax treaty was notified on 21 April 1995, the Protocol, which is an integral part of the tax treaty, also got automatically notified along with the tax treaty. In such

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[1] GRI Renewable Industries S.L v. ACIT (ITA No. 202/Pun/2021) – Taxsutra.com
Note – The Tribunal has dealt with several issues in this decision. However, this flash news deals with the issue of MFN clause.

[2] CBDT Circular No. 3/2022, dated 3 February 2022

a scenario, it is difficult to comprehend the need for any separate notification for the import of the MFN clause.

The CBDT issued a Circular[3] laying down four conditions to avail the benefit of the MFN clause in the Protocol to India's tax treaties with certain countries. The Tribunal observed that there was no dispute that the first three conditions[4] were fulfilled in the present case. However, the fourth condition[5] states that a separate notification should be issued by India importing the benefit of the second treaty into the tax treaty with the first state as required under Section 90(1) of the Act.

The Tribunal observed that the CBDT Circular specifying the need for a separate notification for importing the beneficial treatment from another tax treaty as a corollary of Section 90(1), overlooks the plain language of the section seen in juxtaposition to the language of the Protocol, which treats the MFN clause an integral part of the tax treaty. The language of Section 90(1) indicates that a notification may be made for implementing a tax treaty by the Government with a country outside India for the granting of relief. Reference to the expression 'make such provisions as may be necessary' for the purpose of notification in the Official Gazette, is to adopt the manner of notifying as may be necessary for implementing a tax treaty and not that the notification is to be issued in a piecemeal and in a truncated manner. On notifying the tax treaty, all its integral parts get automatically notified. As such, there remains no need to again notify the individual limbs of the tax treaty to make them operational one by one.

It is trite law that a Circular issued by the CBDT is binding on the AO and not on the taxpayer or the Tribunal or other appellate authorities. The Tribunal relied on various decisions[6] to support its case.

Notwithstanding the above, the Tribunal observed that the requirement contained in the CBDT Circular[7] cannot primarily be applied to the period anterior to the date of its issuance as it is in the nature of an additional detrimental stipulation mandated for taking benefit conferred by the tax treaty. It is a settled legal position that a piece of legislation which imposes a new obligation or attaches a new disability is considered prospective unless the legislative intent is clearly to give it a retrospective effect.

The Tribunal confronted with the CBDT Circular, much less an amendment to the enactment, which attaches a new disability of a separate notification for importing the benefits of the tax treaty with the second state into the treaty with the first state. Obviously, such Circular cannot operate retrospectively to the transactions taking place in any period anterior to its issuance.

Accordingly, the Tribunal observed that the requirement of a separate notification for implementing the MFN clause, as per the recent CBDT Circular[8], cannot be invoked for the year under consideration.

The India-Spain tax treaty, having the Protocol containing the MFN clause as its integral part, was duly notified on 21 April 1995, after having entered into force on 12 January 1995. On such notification of the tax treaty, the Protocol containing the MFN clause triggering the importing of any other tax treaty fulfilling the necessary requirements, including the Portuguese tax treaty, got automatically notified *pro tanto*, in terms of Section 90(1) leaving no room for any separate notification for the importation.

Therefore, the lower authorities were not justified in denying the benefit of the rate of tax at 10 per cent as per the tax treaty read with India-Portuguese tax treaty and also additionally charging surcharge and education cess.

## Our comments

There has been considerable litigation with respect to the availment of the benefit of the MFN clause under the Indian tax treaties. Recently, the CBDT has issued a Circular stating that as per Section 90(1), a separate notification should be issued by India to avail the benefit of the MFN clause under the Indian tax treaties.

In the instant case, the Tribunal, while disregarding this Circular, observed that the Protocol containing the MFN clause is an integral part of the tax treaty which gets notified with the tax treaty. On notification of the India-Spain tax treaty, the Protocol containing the MFN clause triggering the importing of the benefit of any other tax treaty fulfilling the necessary requirements, got automatically notified, in terms of Section 90(1) leaving no room for any separate notification for the importation.

The Delhi High Court in the case of Concentrix Services Netherlands B.V[9] had also held that the MFN clause under the Indian-Netherlands tax treaty has automatic application and there is no requirement of any notification in order to trigger such MFN clause.

This is the first decision after issue of the recent CBDT Circular. The Tribunal has duly considered the Circular and has given its independent finding on the same with a detailed reasoning while ruling in favour of the taxpayer.

Since this is a Tribunal decision, the tax department may file an appeal before the High Court and subsequently, the matter may reach before the Supreme Court. Further, it is important to note that the Delhi High Court in the case of Steria (India) Ltd.[10] had also upheld the above principle as laid down by the Tribunal in the instant case. The SLP filed by the tax department in the case of Steria is currently pending before the Supreme Court. Therefore, one may have to wait for the Supreme Court's decision to finally settle this dispute.

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[3] CBDT Circular No. 3/2022, dated 3 February 2022
[4] Conditions [under points (i) to (iii)] mentioned under CBDT Circular No. 3/2022, dated 3 February 2022
[5] Under point (iv)
[6] CIT v. Hero Cycles Pvt. Ltd. [1997] 228 ITR 463 (SC), CCE v. Ratan Melting and Wire Industries [2008] 220 CTR 98 (SC)
[7] CBDT Circular No. 03/2022, dated 3 February 2022
[8] CBDT Circular No.03/2022, dated 3 February 2022
[9] Concentrix Services Netherlands B.V. v. ITO and Optum Global Solutions International B.V. v. DCIT [2021] 434 ITR 516 (Del)
[10] Steria (India) Ltd. v. CIT [2016] 386 ITR 390 (Del)

# KPMG in India addresses:


**Ahmedabad**
Commerce House V, 9th Floor,
902, Near Vodafone House, Corporate Road,
Prahlad Nagar,
Ahmedabad – 380 051.
Tel: +91 79 4040 2200

**Bengaluru**
Embassy Golf Links Business Park,
Pebble Beach, 'B' Block,
1st & 2nd Floor,
Off Intermediate Ring Road, Bengaluru – 560071
Tel: +91 80 6833 5000

**Chandigarh**
SCO 22-23 (1st Floor),
Sector 8C, Madhya Marg,
Chandigarh – 160 009.
Tel: +91 172 664 4000

**Chennai**
KRM Towers, Ground Floor,
1, 2 & 3 Floor, Harrington Road,
Chetpet, Chennai – 600 031.
Tel: +91 44 3914 5000

**Gurugram**
Building No.10, 8th Floor,
DLF Cyber City, Phase II,
Gurugram, Haryana – 122 002.
Tel: +91 124 307 4000

**Hyderabad**
Salarpuria Knowledge City,
6th Floor, Unit 3, Phase III,
Sy No. 83/1, Plot No 2, Serilingampally Mandal,
Ranga Reddy District,
Hyderabad – 500 081.
Tel: +91 40 6111 6000

**Jaipur**
Regus Radiant Centre Pvt Ltd.,
Level 6, Jaipur Centre Mall,
B2 By pass Tonk Road,
Jaipur – 302 018.
Tel: +91 141 - 7103224

**Kochi**
Syama Business Centre,
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682 019.
Tel: +91 484 302 5600

**Kolkata**
Unit No. 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata – 700 091.
Tel: +91 33 4403 4000

**Mumbai**
2nd Floor, Block T2 (B Wing),
Lodha Excellus, Apollo Mills Compound, N M Joshi Marg,
Mahalaxmi, Mumbai- 400011
Tel: +91 22 3989 6000

**Noida**
Unit No. 501, 5th Floor,
Advant Navis Business Park,
Tower-A, Plot# 7, Sector 142,
Expressway Noida,
Gautam Budh Nagar,
Noida – 201 305.
Tel: +91 0120 386 8000

**Pune**
9th floor, Business Plaza,
Westin Hotel Campus, 36/3-B,
Koregaon Park Annex,
Mundhwa Road, Ghorpadi,
Pune – 411 001.
Tel: +91 20 6747 7000

**Vadodara**
Ocean Building, 303, 3rd Floor,
Beside Center Square Mall,
Opp. Vadodara Central Mall,
Dr. Vikram Sarabhai Marg,
Vadodara – 390 023.
Tel: +91 265 619 4200

**Vijayawada**
Door No. 54-15-18E,
Sai Odyssey,
Gurunanak Nagar Road, NH 5,
Opp. Executive Club, Vijayawada,
Krishna District,
Andhra Pradesh – 520 008.
Tel: +91 0866 669 1000


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