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Sharp Insights

[1]Karnataka High Court holds protocol an integral part of DTAA, no separate notification required to make applicability effective for MFN clause

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[1] Apollo Tyres Limited v/s. Commissioner of Income-tax (International Taxation) [WP Nos 31737 & 31738 of 2016 & 32300 & 32301 of 2016]

Background/Facts

- Apollo Tyres Limited (the Company) had made certain payments to non-residents without deducting taxes relying on the Most Favoured Nation (MFN) clause in the protocol to the India-Netherlands Double Taxable Avoidance Agreement (DTAA) read with India-Finland DTAA.
- The tax officer denied the aforesaid benefit stating that no separate notification existed allowing applicability of MFN clause in the protocol to the India-Netherlands DTAA, read with India-Finland DTAA. In the absence of the same, the tax officer held that taxes were required to be withheld under section 195 of the Income-tax Act, 1961 (the Act).
- Aggrieved by the order of the tax officer, the Company preferred an application for revision under section 264 of the Act.
- The Commissioner of Income-tax (International Taxation) (CIT) after placing reliance on the decision of the Authority for Advanced Rulings (AAR) in the case of Steria (India) Limited [(2014) 45 Taxman 281 (AAR New Delhi)] upheld the order of the tax officer.
- Aggrieved by the aforesaid decision of the CIT, the Company filed the petition(s) before the Karnataka High Court (Karnataka HC).
- The Company specifically relied on the following and argued that no separate notification is required to make the MFN clause of the DTAA applicable:
  - Divisional Bench of the Delhi High Court (Delhi HC) in the case of Steria (India) Limited [(2016) 386 ITR 390(Delhi)] had set aside the order of the AAR in the case of Steria (India) Limited (supra);
  - The Delhi HC had concluded that the text of the protocol to the India-Netherlands DTAA makes it self-operational and that protocol forms an integral part of the DTAA;
  - Language of Article 12 of the India-Netherlands DTAA along with the protocol makes it clear that no separate notification is required to make the protocol effective;
  - Accordingly, the payment was not taxable considering the beneficial Fees for Technical Services (FTS) clause of the India-Finland DTAA.

Issues for consideration

In view of the aforesaid facts, the Karnataka HC was called upon to adjudicate as to whether a separate notification was required to make the protocol to the India-Netherlands DTAA, read with India-Finland DTAA, effective.

Ruling of the Karnataka High Court

The Karnataka HC after considering the arguments of the tax department and the Company decided in favour of the Company, holding that the protocol was an integral part of the DTAA and no separate notification was required to make its applicability effective. While doing so, the Karnataka HC has *inter-alia* observed as under:

- The protocol itself provides for automatic application of subsequent DTAA, to the India-Netherlands DTAA and therefore, no separate notification was envisaged to be issued for enforcing such subsequent DTAA with another OECD country, i.e., Finland (in the present case), to be made applicable.
- The decision of the AAR in the case of Steria (India) Limited (supra) cited by the Revenue authorities, cannot be relied upon in light of the decision of the Delhi HC in the case of Steria (India) Limited (supra).

Conclusion

The Karnataka HC has held that protocol is an integral part of the DTAA and no separate notification is required to make the MFN clause of the protocol effective.

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