

SCV ALERT


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Clarification Regarding MFN Clause

[CBDT Notification dated 19th March 2024]





The Supreme Court of India had recently delivered its judgment in the case of **Nestle SA**¹, wherein the Most Favoured Nation (MFN) and the conditions necessary for availing any benefit by virtue of the same was discussed at length. The Supreme Court had ruled in favour of the tax authorities and had pronounced that without a notification by the Central Board of Direct Taxes (CBDT) under section 90(1) of the Income Tax Act (the Act) 1961, extending the benefit of a lower rate of tax or a restricted scope of taxation by virtue of the MFN clause present in India's Double Taxation Avoidance Agreements (DTAA), no such beneficial treatment could be availed by the tax payer. While the judgment was in the context of India's DTAA with France, Netherlands, and Switzerland, it lays down the law for interpreting and applying MFN clauses in all of India's DTAA's.

The Hon'ble Supreme Court, in its ruling, emphasized that for any Double Taxation Avoidance Agreement (DTAA) or its protocol to effectively alter existing legislative provisions, a fresh notification is obligatory under Section 90(1) of the Income Tax Act, 1961 ('the Act'). Further the court had cited instances where in the past the CBDT had issued such notifications under section 90(1) for extending the benefit under MFN clause of India's DTAA with certain Countries.

In line with the above judgement, The Ministry of Finance, via Notification No. 33/2024 dated March 19th, 2024, has modified the DTAA between India and Spain, particularly Article 13 relating to Royalties and Fees for Technical Services (FTS), by extending the benefit of lower rate of tax of 10% in comparison to the existing rate of tax of 20% in the said Article.

As per the notification the benefit of the lower rate has been extended by virtue of the MFN clause provided in the India Spain DTAA and in light of the DTAA between India and Germany (OECD member) which entered into force on 26th October 1996 i.e. after 1st January 1990 as provided in the Protocol dated 8th February 1993 in the DTAA between India and Spain.

The above modified for taxation of Royalty and FTS as per Article 13 of India Spain DTAA shall be effective from Assessment Year (AY) 2024-25.

¹ [2023] 155 taxmann.com 384 (SC)



SCV's Take Away

Amidst the legal debate on the matter, this announcement through a notification under section 90 of the Act, extending the benefit under MFN clause, has re-iterated the revenue authority's position that a notification to enforce the MFN clause is mandatory. Here it must be noted that while the Protocol to the India Spain DTAA, provides for a rate lower or scope more restricted for Royalty and FTS, the CBDT has chosen to extend the benefit of lower rate of tax only and not the restricted scope. While the position under India Spain DTAA with respect to MFN clause has been clarified and established from a prospective effect, further affirming the tax authority's intent, this leaves the taxpayers at the mercy of the revenue authorities for the past benefits availed.

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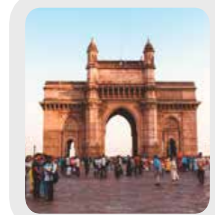
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