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INTERNATIONAL LAW

MUNICIPAL LAW

Royal Bank of Scotland N.V. v. Commissioner of Income-tax (Calcutta High Court)

Tax rate applicable on PE of "foreign company" in India

29.06.2024

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I N T E R N A T I O N A L T A X A T I O N

Facts

1. Appellant is a branch of ABN Amro Bank NV (Now The Royal Bank of Scotland N.V.) incorporated in the Netherlands with limited liabilities having its original office at Singapore. In India, the appellant is registered as scheduled bank in terms of Schedule-II of the Reserve Bank of India (RBI) Act, 1934. The main activities of the appellant in India are accepting deposits, giving loans, executing forward transaction of foreign currencies for importers/exporters, etc.

2. Article 7 of the DTAA between India and Netherlands provides for taxation in India of a foreign enterprise in respect of profits attributable to its **permanent establishment** (hereinafter referred to as 'PE') in India. Since the **appellant has a PE in India**, therefore, they are liable to tax in respect of income attributable to the PE.

3. ITAT has held that the appellant/ assessee is liable to Income Tax at the rate specified for company "other than domestic company".

4. The ITAT has held that the rate of Income Tax as provided in the Finance Act applicable to a domestic company shall not apply to the appellant/assessee and instead the appellant/assessee is liable to tax at the rate prescribed by the Finance Act for a company other than domestic company. Aggrieved with the order of the ITAT the appellant has filed the present appeal raising the afore-quoted common substantial question of law.

Assessee's Contention

By virtue of **Article 24(2) of the DTAA between India and Netherlands**, it is clear that **if a permanent establishment** of a Netherlands' entity is subjected to a tax treatment, that is **less favorable than an Indian enterprise** that is carrying on similar activities, the **same would than tantamount to prohibited**. The levy discrimination of the Netherlands' entity, an action which is prohibited of tax on the profits of the **Appellant's banking activities** at a **rate higher than the rate applicable to domestic companies** is, thus, **impermissible**.

1. Tribunal erred in Holding that petitioner is chargeable at the **Income tax rate applicable to a foreign company** as against the rate of tax applicable to a domestic company.

2. Assessee contended that in terms of Article 24(2) of DTAA between India and the Netherlands, containing provision of non-discrimination**, the appellant/assessee is liable to Income Tax at the rate applicable to a domestic company.**

Revenue Contention

Section 90(2)

(2) Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

Explanation 1—For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as **less favourable** charge or levy of tax in respect of such foreign company.

- The revenue stated that it is satisfied with the order of Tribunal and is relying on the judgement that the appellant was liable to income tax at the higher rate applicable to a foreign company and not at the rate of tax applicable to a domestic company;
- Further, revenue is of the view charging a higher tax rate on the PE of a foreign company is not less favourable as compared to charging tax to domestic company as both are not the same.

Article 24 (India Netherlands DTAA) Non-Discrimination

1. Nationals of one of the states shall not be subjected the other State to any taxation or any requirement connected therewith, which is other or more burden some than the taxation and connected requirements to which nationals of that other State the same circumstances are or may be subjected. These provisions shall notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the States.

2. **Except where the provisions of paragraph 3 of Article 7 apply, the taxation on a permanent establishment which an enterprise of one of the States has in the other State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities.**

3. The provisions of paragraph 2 shall not be construed as obliging one of the States to grant residents of the other State any personal allowances, reliefs and reductions for taxation purposes account of civil status or family responsibilities which it grants to its own residents.

4. Except where the provisions of paragraph 1 of Article 9 paragraph 9 of Article 11 paragraph 9 of Article 12 apply, interest, royalties and other disbursements paid by an enterprise one of the States to a resident of the other State shall for the purpose of determining the marginal profits of such enterprise, be deductible under the same conditions as if they had been paid to resident of the first mentioned State. Similarly, any debts of an enterprise of one of the States resident of the other State shall, for the purpose of determining the taxable capital of such enterprise, be deductible under the same conditions as if they had been contracted to a resident the first mentioned State.

5. Enterprises of one of the States, the capital of which is wholly or partly owned or controlled directly or indirectly, by one or more residents of the other State shall not be subjected in the first mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprise of the first mentioned State are or may be subjected."

Circular 333 dated 02.04.1982

Specific provisions made in double taxation avoidance agreement - Whether it would prevail over general provisions contained in Income-tax Act

1. It has come to the notice of the Board that sometimes effect to the provisions of double taxation avoidance agreement is not given by the Assessing Officers when they find that the provisions of the agreement are not in conformity with the provisions of the Income-tax Act, 1961.

2. The correct legal position is that where a specific provision is made in the double taxation avoidance agreement, that provision will prevail over the general provisions contained in the Income Tax Act, 1961.

3. Section 90 of the Income-tax Act, 1961, also provide that the laws in force in either country will continue to govern the assessment and taxation of income in the respective country except where provisions to the contrary have been made in the Agreement.

4. Thus, where a Double Taxation Avoidance Agreement provides for a particular mode of computation of income, the same should be followed, irrespective of the provisions in the Income Tax Act. Where there is no specific provision in the agreement, it is the basic law, i.e. the Income Tax Act, that will govern the taxation of income."

Doctrine of Incorporation

The doctrine of incorporation also cognizes the position that the **rules of international law are incorporated into national law are incorporated into national law and considered to be part of the national law, unless they are in conflict with an Act of Parliament.** Comity of nations or no. Municipal Law must prevail in case of conflict. National Courts cannot say "yes" if Parliament has said no to a principle of international law. National Courts will endorse international law but not if it conflicts with national law. National courts being organs of the National State and not organs of international law must perforce apply national law if international law conflicts with it. But the Courts are under an obligation within legitimate limits, to so interpret the Municipal Statute as to avoid confrontation with the comity of Nations or the well established principles of International law. But if conflict is inevitable, the latter must yield."

Amendment in India-Netherlands DTAA

1. India-Netherlands DTAA was **amended twice**,

   i. firstly by Notification No. S. O. 693(E) [No. 11050(F. NO. 501/2/83-FTD)] dated August 30, 1999 and secondly by Notification No. 2/2013 [F. No. 501/02/1983-FTD-1/SO 163 (E) dated January 14, 2013. The first amendment was made even after India had negotiated DTAAs with other countries wherein the non excluded from its ambit the rate of tax.

   i. The second amendment was even after discrimination article the insertion of the Explanation but no amendment corresponding to the said Explanation was made to Article 24 of the DTAA.

2. It is submitted that where the **Legislature wanted to enact a provision that would override a treaty provision specific language** to that effect was used. Attention is invited to sub-section (2A) of section 90 of the Act which reads thus:-"(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee even if such provisions not beneficial to him."

3. In the **absence of** a similar **non-obstante clause** in the **Explanation below section 90**, the said Explanation **cannot override the provisions of the DTAA**.
   - ✓ Reliance in this behalf is placed on the following judgment. Sanofi Pasteur Holding SA v. Department of Revenue & Ors. (supra) at Para 105 Pgs. 427-428 of the Reports..

Ruling

- It is admitted case of the appellant that it **is not a "Domestic Company" but "a Company other than a Domestic Company. Therefore, the appellant is liable to tax at the rate specified for a company other than a domestic company.**

- As per ***Explanation 1 of Section 90(2)— "shall not be less favorably levied"*** used in Article 24(2) of the DTAA **simply means that** taxation on a company falling under "any other company.... " under Section 2 (22A) of the Act, 1961 shall not be less favorably levied than an" Indian company" which both fall under one and the same class i.e. Domestic Company under Section 2(22A) of the Act, 1961 read with Section 2(1), Section 2(12)(a) and Paragraph "E‘ of Part I of the First Schedule of the Finance Act, which provisions existed even prior to the DTAA in question and the clarificatory retrospective insertion of the Explanation in Section 90 by the Finance Act, 2001. Thus, there is no conflict between the Explanation to Section 90 of the Act, 1961 and Article 24 (2) of the DTAA.

Ruling

- The **Explanation has merely clarified the existing position of law. Explanation to Section 90 is not in conflict with the provision of DTAA and the Income Tax Act 1961 with regard to non-discrimination.**

- **Effect of circular number 333 dated 02.04.1982** - *provide that the laws in force in either country will continue to govern the assessment and taxation of income in the respective country* ***except where provisions to the contrary have been made in the Agreement.*** Thus, where a Double Taxation Avoidance Agreement provides for a particular mode of computation of income, the same should be followed, irrespective of the provisions in the Income Tax Act.

- Since the expressions used in the aforesaid provisions of the Act 1961 and the Finance Act are clear and capable of **only one construction** as discussed and there is no ambiguity or lack of clarity, therefore, the provision of the Act 1961 and the provision of the Finance Act, as discussed above, are bound to be given full effect. Accordingly it is held that the **appellant is liable to tax at the rate applicable to a company other than a domestic company as provided in the Finance Act.**

OUR COMMENTS

1. Where there is specific provision in DTAA then that provision will prevail over the general provisions contained in the Income Tax Act, 1961 as per circular 333 dated 02.04.1982.

2. While checking about the clause of less favourable as contained in Article 24 we need to compare two foreign companies which have a PE in India and who are on same footing and we should not compare domestic and foreign company.

3. A permanent establishment of a company in India will not be considered as equivalent to domestic company but will be considered as other than domestic company/ foreign company and will needs to be taxed accordingly. Having a permanent establishment in India does not mean it will be domestic company as the company is not registered in India but outside India.

4. In interpreting a taxing statute, **equitable considerations** are entirely out of place. A taxing statute cannot be interpreted on any presumption or assumption. A taxing statute has to be interpreted in the light of what is clearly expressed; it cannot imply anything which is not expressed.

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Section/Article	Article 24 of DTAA and section 90 of Income Tax Act
DTAA/Country	India - Netherlands
Court	High Court of Tribunal
Date of decision	22.05.2024

Note: Case law name in Red- in favour of the revenue, Green-In favour of the Assessee, Orange = Partial

INTERNATIONAL TAXATION

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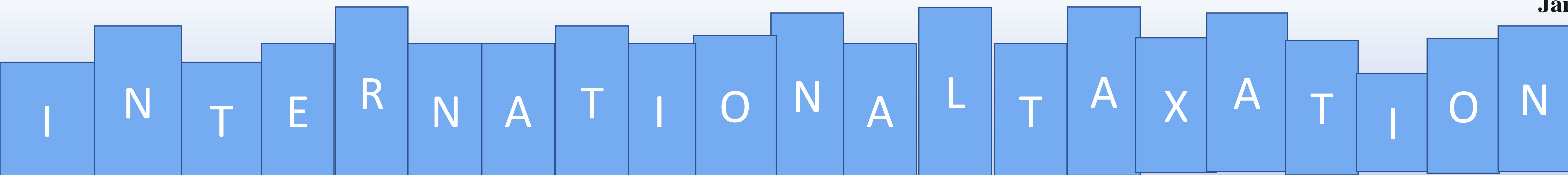

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