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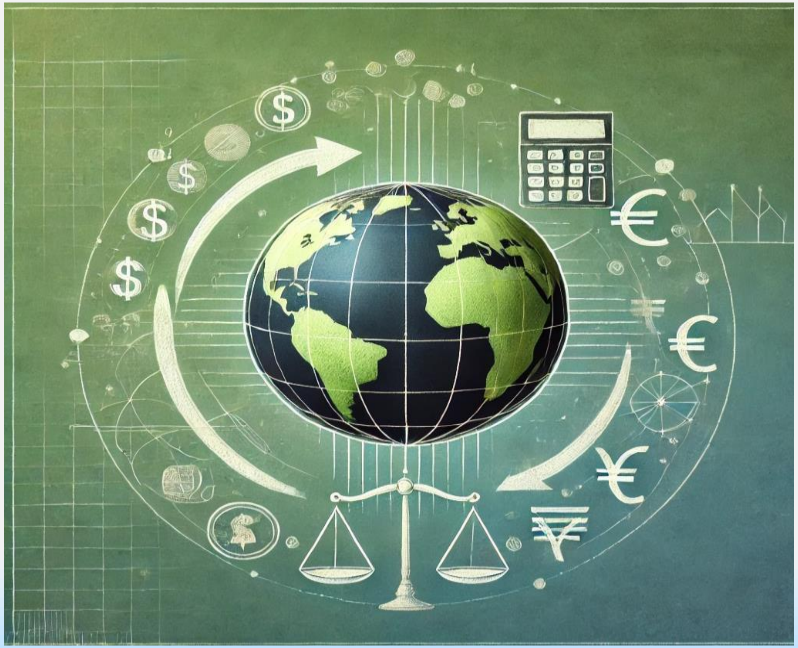
SITG

Back to Basic Principles



SITG No. 245

Retrospective amendment in the act cannot be read into DTAA

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Introduction

- In the realm of international taxation, Double Taxation Avoidance Agreements (DTAAs) play a crucial role in determining tax liabilities across different jurisdictions.
- These treaties, negotiated between sovereign states, establish clear guidelines on how certain types of income should be taxed, ensuring that taxpayers are not subjected to double taxation.
- However, conflicts often arise when one country **unilaterally amends its domestic tax laws**, particularly with **retrospective amendments**, to widen the scope of taxation on certain types of income and to redefine key terms like "royalty," "fees for technical services," or "permanent establishment.“
- The **key question** that arises in such situations is whether such unilateral amendments can override the provisions of an existing DTAA. Therefore, this topic explores the implications of retrospective amendments in tax laws, their potential conflict with DTAAs, and how courts have interpreted the interplay between domestic tax amendments and international treaty obligations.

Landmark Case 1

Case: DIT vs New Skies Satellite BV [2016] 68 taxmann.com 8 (Delhi) [08-02-2016]

- The issue in this case revolves around whether the income earned by the assessee (a Thailand-based company) from providing digital broadcasting services through its satellite is taxable as "royalty" under Section 9(1)(vi) of the Income Tax Act, 1961, and Article 12 of the Double Taxation Avoidance Agreement (DTAA) between India and Thailand after the retrospective amendment in the Finance Act, 2012 where the services were provided prior to 2012.

- The Revenue argued that post **Finance Act, 2012**, Explanation 6 to **Section 9(1)(vi)** clarified that **royalty includes payments for satellite transmission services**, therefore it should be taxed accordingly.

- Further, since the DTAA's definition of royalty was similar to the Act's definition before the amendment, the **amended Section 9(1)(vi) should also apply to DTAA cases**.

Landmark Case 1

- The case went to the **Delhi High Court**, which ruled that **Finance Act, 2012**, which expanded the domestic definition of royalty, **could not automatically modify the definition under the DTAA**.
- The **treaty definition** remains binding unless both countries **mutually amend** the DTAA. So, the new definition of "royalty" under Indian law **does not apply to treaty cases**.
- Hence, the court ruled **in favour of the assessee**, holding that the income was **not taxable as royalty** under the DTAA.

Analysis of the Case Law

- The judgment highlights the **primacy of Double Taxation Avoidance Agreements (DTAAs)** over domestic law amendments when a conflict arises.
- It reaffirms that **amendments to domestic tax law (Finance Act, 2012) cannot unilaterally override the definitions in a DTAA** unless the treaty is amended bilaterally.
- A **taxpayer must be able to arrange their affairs based on existing laws** without fear of retrospective taxation.
- **The legislature cannot use retrospective amendments to nullify judicial rulings** (e.g., Asia Satellite case).
- Therefore, the **Finance Act, 2012 amendments could not retrospectively tax payments that were previously held non-taxable under existing law**.

Landmark Case 2

Vodafone-Hutchison Tax Case (India)

- In 2007, Vodafone acquired a **67% stake in Hutchison Essar Limited** (an Indian telecom company) for **$11 billion** through an offshore transaction between Vodafone's Dutch subsidiary and Hutchison's Cayman Islands subsidiary.

- The Indian government claimed **capital gains tax** on the transaction, arguing that the deal indirectly transferred Indian assets.

- The case went to the **Indian Supreme Court**, which ruled in **2012** that Vodafone was **not liable to pay tax** because the transaction occurred outside India.

Landmark Case 2

- India, on March 2012, amended its tax laws **retrospectively**, giving itself the power to tax similar offshore transactions. This led to a **₹22,100** on Vodafone. **crore ($3 billion) tax demand**

- Vodafone challenged the retrospective tax in **The Hague-based Permanent Court of Arbitration (PCA)**. In **2020**, the PCA ruled in Vodafone's favour, stating that India's demand violated **bilateral investment treaties**.

- In **2021**, India scrapped the retrospective tax law and agreed to refund Vodafone's tax payments.

Various case laws

This principle which essentially implies that retrospective amendments could not automatically modify the definition under the DTAA was extended to various cases like **–**

- Dy. CIT V. Boston Consulting Group Pte Ltd. [2005] 94 ITD 31 (Mumbai- Tribunal)
- Dy. CIT V. Gupta Overseas [2014] 42 taxmann.com 42/ [2015] 153 ITD 357 (Agra – Tribunal)
- Intec Billing Ireland V. Asstt. DIT(IT) [2018] 90 taxmann.com 94 (Mumbai - Trib.)

Our Comments

- As per our understanding, any amendment in the act can restrict or expand the scope of any definition or redefine key terms like "royalty," "fees for technical services," or "permanent establishment“. But it cannot **override the definitions in a DTAA** unless the treaty is amended bilaterally. Hence, a unilateral amendment cannot affect DTAA.

- Assessee is allowed to choose beneficial provision for him and retrospective amendment in the act cannot override this rule.

- Even, a change in DTAA cannot be implemented unilaterally until issuing a notification under Income tax act and implementing such change. Similar view were taken in various judgements of Hon’ble Supreme court such as Nestle SA etc.

Reference of Previous SITG of Back to Basic Principles Series

S.No	Particulars	Link
1.	Right to Choose Between DTAA and IT Act	Click here
2.	If two views possible, view which is favourable to taxpayer should be adopted	Click Here
3.	Taxpayer can adopt taxability either under Act or under DTAA, whichever is beneficial for each stream of income	Click Here
4.	Treaty to be read as a whole and not in isolation	Click Here

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