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By

SBS and Company LLP
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Dear Readers,

Greetings for the season!

In this edition, we bring you, an article on the understanding of the depth of the most litigative entry in the indirect taxation sphere, which is agreeing to the obligation to refrain from an act or tolerate an act or to do an act. Though we understand that we have only touched the tip of iceberg, we have made an honest attempt in understanding the direction in which it would be interpreted. The article comes in two-part series, the one dealing with the position under the European VAT and the next dealing with position under Indian scenario.

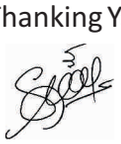
The next article is on the interpretation of 'Most Favoured Nation' clause in the tax treaties. The Courts have shown a direction as to how the same has to be interpreted specifically in the context of interpretation of treaties in light of Vienna Convention of Law of Treaties. However, the Board's Circular has attempted to override the judgments and gave a new interpretation to their favour. Though the said circular is binding only on the revenue and not on the courts or assessee, it would be an unwanted fight of the taxpayer with the revenue. We have covered the exact issue with our remarks.

The next article is on the recent judgment of Honourable Supreme Court in the issue pertaining to the succession by a female child prior to the Hindu Succession Act. The Court answered the question in the favour of female child stating that, as long as the property of the father is self-acquired, the devolution happens by way of succession and not on survivorship.

The finale is on the recent updates in the areas of labour laws. The insights were contributed by our learned senior associate Mr SV Ramachandra Rao.

I hope that you will have good time reading this edition and please do share your feedback. I will also urge clients to mail us topics or issues on which you want us to deliberate in our future editions, so that we can contribute to the same.

Thanking You,



Suresh Babu S
Founder & Chairman

GST

AMBIT OF 'AGREEING TO OBLIGATION TO REFRAIN FROM ACT OR TOLERATE AN ACT OR TO DO AN ACT' - PART I

Contributed by CA Sri Harsha

When the positive list of taxation under service tax laws was done away with the introduction of negative list, a new concept of 'declared services' was introduced with effective from 01 July 12. Declared services are list of activities or transactions, which were specifically covered under the definition of 'service' under the pre-GST[1] laws to clear away the ambiguity, if any, and to drive home the point that such activities or transactions are also services. When the negative list was phased out with the advent of GST laws, majority of the entries of declared services were carried and incorporated into GST laws vide Schedule II of CT Act[2].

In this two part article, we shall deal with one of the entries of declared services/Schedule II (supra) namely 'agreeing to obligation to refrain from act or to tolerate an act or a situation, or to do an act'. This entry created a lot of confusion and infused a cloud of ambiguity. Whenever, a particular transaction or activity is doubtful whether it would fall under the ambit of expression of 'service', this entry was used by tax authorities to bring the same into the tax net. Having no established judicial precedents, clear instructions, boundaries and scope this entry would cover or deal with, helped the revenue to issue notices proposing fat demands on the taxpayers. Since, the said entry also finds place in Schedule II, it would be important to understand the depth of this entry, as the taxpayers would be haunted by similar notices even under the GST laws.

Before proceeding to understand the depth of said entry with the help of judgments, it is important to note that the judgments under pre-GST laws have just touched the tip of the iceberg and in coming days, this entry would create more confusion. The jurisprudence available under the pre-GST laws was already set aside or not considered by the Authority for Advance Ruling or Appellate Authority for Advance Ruling under the GST laws.

There was certain amount of jurisprudence even under the European VAT[3] relating to the current subject. In the matter of Societe thermale d'Eugenie-les-Bains[4], the Court was dealing with a question, whether the payment of deposit, in the context of a contract relating to supply of hotel services, is to be regarded as consideration for supply, especially, when the client exercises the cancellation option, the deposit is retained by the hotel for the loss suffered because of client default. The Court stated that deposit retained by the hotel has no direct connection with the supply of any service for consideration and as such, is not subjected to tax. The Court further stated that payment of deposit by the client, on the one hand, and the obligation of hotelier on the other, not to contract with anyone else in such a way as to prevent it from honouring its undertaking towards the client cannot be classified as reciprocal performance, because the obligation in those circumstances arise directly from the contract for accommodation, not from the payment of deposit.

[1]Goods and Services Tax
[2]Central Goods and Services Tax Act, 2017
[3]Value Added Tax
[4]EUR-Lex - 62005CJ0277 - EN - EUR-Lex (europa.eu)

In another matter, Services de Comunicacoes e Multimedia SA (MEO)[5] , the court while dealing with taxability of charges for pre-termination of contract of telecommunication services, held that such amounts are subjected to tax. MEO concludes the contract with its customers which provide for minimum commitment periods for a lower monthly subscription fee. These contracts stipulate that in case of deactivation of services before the expiry of agreed minimum commitment period at the request of customers for their own reasons, MEO is entitled to compensation corresponding to the amount of agreed monthly subscription fee multiplied by difference between the duration of the minimum commitment period provided for in the contract and number of months during which the service provided. The court held that such amounts received by MEO would be subjected to tax, since the payment that was charged by MEO for breaking of minimum commitment period is equal to that which it would have received if the customer had not terminated the contract prematurely and that does not alter the economic reality of the relationship between MEO and customer. The Court further distinguished the judgment of Societe thermale d'Eugenie-les-Bains (supra) by stating that in that matter, the client has not availed any service by paying the deposit, whereas in the instant matter, MEO has provided service to its customers.

Recently, in the matter of Apcoa Parking Danmark[6] , the court was considering the taxability of penal charges collected by the appellant from its customers for violating the conditions of parking of cars. Apcoa was charging a fixed amount per day from customer who infringe the regulations relating to parking of cars. The question that came up for consideration is, whether such penal amount (which constitutes approx. 35% of total revenues) would be subjected to tax. Apcoa was of the belief that since the amounts were akin to cancellation charges collected by hotelier in Societe thermale d'Eugenie-les-Bains (supra), the same are not subjected to tax. The tax authorities have placed reliance on the judgment of Services de Comunicacoes e Multimedia SA (MEO) (supra) to tax the said amounts. The Court stated that it must be noted that parking in a particular space in of the car parks managed by Apcoa gives rise to a legal relationship between that company and the motorist and accordingly, the condition of reciprocal performance was satisfied. The Court stated that though the motorist pays additional amount as penal charges, the same was for using the parking space and accordingly the said amounts are subjected to tax. The question whether the penal charges are subjected to tax or not is left to the national law and the court opined that the same would not have any difference under the VAT laws.

From the above, it would be evident that if at all there is an identifiable service for which a consideration is received, the same would be subjected to tax. In the Societe thermale d'Eugenie-les-Bains (supra) case, there was no identifiable service provided by hotelier for receipt of deposit and hence it would not be subjected to tax. However, in both the other matters, there was an identifiable service and the amounts received, by whatever name, they are called, would be subjected to tax. Further, the VAT laws therein were not considered with the nature of consideration and left the same to the national laws. With the above background, let us proceed to analyse the judgments delivered in the Indian context in Part II of this article to understand the taxability.

[5]EUR-Lex - 62017CJ0295 - EN - EUR-Lex (europa.eu)
[6]EUR-Lex - 62020CJ0090 - EN - EUR-Lex (europa.eu)

This article is contributed by CA Sri Harsha. The author can be reached at harsha@sbsandco.com

OTHERS

UPDATES IN LABOUR LAWS

Contributed by S V Ramachadra Rao

Jurisdiction in 'Work From Home' Situations:

- InMangala A Gvs. HIL (India) Limited [Kerala HC WP(C) No. 2342/2021 26.11.2021], the question that has arisen for consideration is, what would be the jurisdiction of court in the case of employee who is working from home. The court stated that the question that now boils down to whether mere permission to work from home is sufficient to confer jurisdiction on the court, within whose jurisdiction the employee was working.

- The Court further stated that, if each person who works from home is permitted to raise their objection from his territorial jurisdiction, definitely, it may confer jurisdiction on umpteen number of Courts and may call upon the employer to face litigation in different jurisdictions.

- However, as the situation changes and telecommuting or work from home becomes a permanent feature, unlike the temporary phase that has arisen at present, wherein, as a part of contract of employment, persons who are freshly recruited are permitted to remain in different stations and work from there, with facilities being provided by the employer or where the employer pro-actively encourage the employee to improve the business there and/or provides facilities, in that jurisdiction, the situation may be different. The employer, in such cases will be free to include appropriate clause relating to jurisdiction in the contract of employment.

- ***In the above circumstances, the legal position seems to be very clear that, when a person is permitted to work from home merely as a concession or a convenience, place from where the person so work is not sufficient to confer any jurisdiction.***

ESIC COVID-19 Relief Scheme – Notification dated 01.02.2022:

The scheme was notified on 13.8.2021 for a period of two years with effect from 24.03.2020. Now the eligibility condition of the scheme is as under:

The deceased Insured person must have been in employment on the day of diagnosis of COVID-19 disease and contributions for at least 35 days should have been paid or payable in respect of him/her during a period of maximum one year immediately preceding the diagnosis of COVID-19 disease resulting in death.

ESI Act – Wages- Conveyance Allowance:

- In ESI Corporation Vs. M/s Texmo Industries [2021 LL 799 Supreme Court of India], the question that was taken for consideration is, whether the 'conveyance allowance' paid to employees should be taken as 'wage' for the purposes of determination of ESI Payable.

- The Honourable Supreme Court by referring to the definition of 'wage' as per Section 2(22) of ESI Act has stated that, in light of the specific exclusion in the definition of 'wage', the conveyance allowance should not be included.

- Accordingly, it is observed that, including 'conveyance allowance' in 'wages' on the basis that it is being paid every month to every employee to meet to and from conveyance expenses, is an erroneous construction of section 2(22) of the Act.

Provident Fund Contributions and Income Tax

Employee Contributions:

- The interest earned on provident fund contributions made by the employee towards provident fund and voluntary provident fund above Rupees Two Lakhs Fifty Thousand will be taxable income. However, all contributions made by employees until March 2021, will be treated as non-taxable contributions.

Employer Contributions:

- Contributions made by the employer to Employee Provident Fund more than 12% of salary (salary includes dearness allowance, if the terms of employment provides, but exclude all other allowances and perquisites) will be treated as income from salary.

- Perquisites: Employer's contribution to PF, pension scheme covered under section 80CCD or approved superannuation fund in excess of Rs.7,50,000 is treated as perquisite.

- Interest accrued on the amount exceeding Rs.7,50,000 is treated as perquisite in the hands of employee and such Interest perquisite will be treated as taxable income.

Provident Fund – NEEM [National Employability Enhancement Scheme]:

EPFO File No. Compliance/NEEM Scheme/2021 dated 24.2.2022 – Clarification on NEEM Trainees

- The NEEM trainees are not exempted from the definition of "employee" under section 2(f) of the EPF & MP Act, 1952 and Regulation 15. of the NEEM Regulation 2017 is ultra vires to the provisions of the Act.
- In view of the above all the NEEM trainees should be covered under EPF and ESI.

Maternity Benefit:

- In Dr. Swetha, W/o A V Biradarvs. Union of India and Others [2021 LLR 964 Karnataka HC], the high court has held that a female employee is entitled to the benefits of maternity leave after she has put in 80 days of service in the past 12 months preceding the date of expected delivery, irrespective of her appointment being on regular basis or contract basis. Duration of maternity leave is 26 weeks with pay.

This article is contributed by S V Ramachadra Rao, an associate of SBS and Company LLP, Chartered Accountants. The author can be reached at svrr@resourceinputs.com

OTHERS

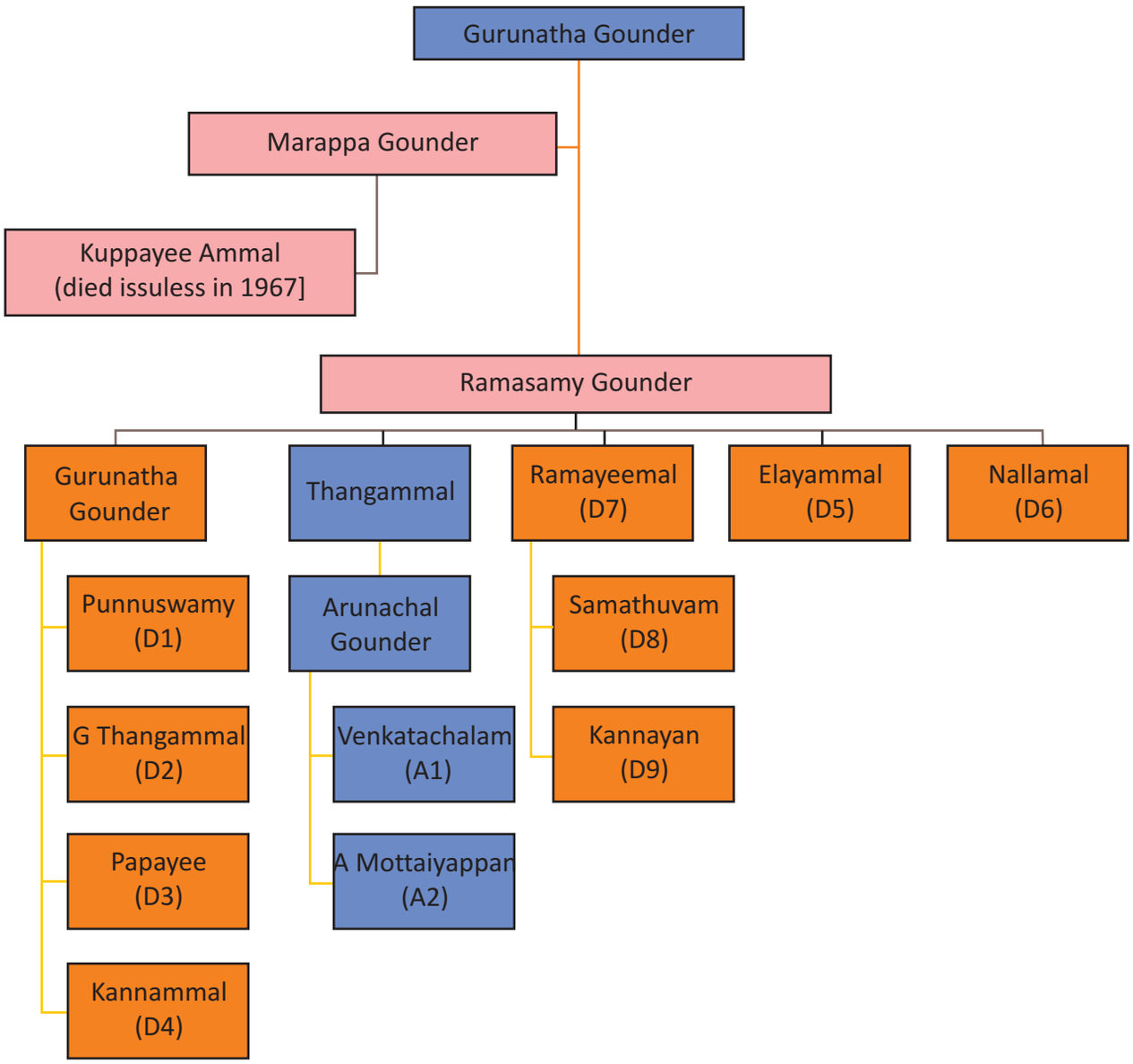
SUCCESSION BY FEMALE – PRIOR TO HINDU SUCCESSION ACT – SC ANSWERS IN AURNACHALA GOUNDER

Contributed by CA Sri Harsha

The recent decision of Honourable Supreme Court in matter of Aurnachala Gounder v. Ponnusamy[1] has reiterated the rights of a female for succeeding to the property in absence of a male issue, though the succession happened prior to the enactment of Hindu Succession Act, 1956. The matter revolves around, who would be the successor to the self-acquired of the father who has only a daughter or brother's son. The trail court and high court have held that the property would devolve by survivorship instead of succession. Since the father does not have any male issue and the daughter has deceased without any issue, the property would devolve by survivorship on the son of deceased brother. The next question that has come up is, if the property is to be devolved by succession to the daughter, how would the succession happen post her demise. The Supreme Court after referring to the various commentaries and judicial precedents has held that the self-acquired property would devolve on the daughter through succession and not to brother's son by survivorship, despite of the fact that the succession happened prior to the enactment of Hindu Succession Act. In this article, we shall analyse the fact, the observations of trail and high court and the ultimate ruling by the Supreme Court.

Before proceeding with the facts of the case, it is necessary to understand the entire family and then the respective claims put forward by them. Marappa Gounder and Ramasamy Gounder were sons of Gurunatha Gounder (for ease of reference, we shall call him Gurunatha Gounder Senior). Marappa Gounder has only a daughter Kupayee Ammal. On the other hand, Ramasamy Gounder has five off-springs, one male and balance were female. The male issue was Gurunatha Gounder (for ease of reference, we shall call him Gurunatha Gounder Junior). The four daughters were named as Thangammal, Ramayeemal, Elayammal, Nallammal. Kupayee Ammal was dead issueless. Gurunatha Gounder Junior had four offsprings namely Ponnuswamy, G Thangammal, Papayee and Kannammal. Thangammal has a daughter Arunachal Gounder and Ramayeemal has two offsprings Samathuvam and Kannayan. The family chart appears like this:

[1] 2022 SCC Online SC 72



Marappa Gounder has purchased the suit property independently in the year 1938, through the process of court auction. The suit for partition is brought by Thangammal, daughter of Ramasamy Gounder claiming 1/5th share in the suit property on the allegation that her father predeceased his brother Marappa Gounder who died in 14.04.1957 leaving behind the sole daughter Kuppayee Ammal who also died issueless in 1967 and after the death of Marappa Gounder, his property was inherited by Kuppayee Ammal and upon her death in 1967, all the five children of Ramasamy Gounder will be entitled for 1/5th share each. After the death of Thangammal, the suit was contested by her daughter Arunachal Gounder, since having died is represented by A1 and A2. The appellant pleaded that the property was purchased by Marappa Gounder using his own funds and accordingly, it becomes his self-acquired property.

However, the respondent's[D1 to D9] contention was that Marappa Gounder died on 11.05.1949 and not on 14.04.1957 as contested by appellant and as per the provisions of the Hindu Law prevailing prior to 1956, Gurunatha Gounder Junior was the sole heir of Marappa Gounder and accordingly, he inherited the suit properties, since according to them, the said property was purchased from family funds and accordingly, it acquires the character of joint family property. Since Marappa Gounder has died prior to enactment of Hindu Succession Act, 1956, the succession opened at the time of his death and the respondent's father, being the sole male heir rightly inherited the property and was in possession and enjoyment of these properties and after his death, the respondents herein, were continuing as lawful owners. The respondent's contention was that by virtue of survivorship, the property would devolve upon Gurunatha Gounder Junior and not on Kuppayee Ammal.

The trail court after considering the evidence bought on record of the case by the parties concluded that Marappa Gounder died on 15.04.1949 and thus, the suit property would delve upon the sole son of deceased Ramasamy Gounder, the deceased brother of Marappa Gounder by survivorship and the appellant has no right to file the suit for partition and accordingly, dismissed the suit. The High Court agreed with the observations of the Trail Court dismissed the appeal preferred by the appellant. The appellant has finally preferred an appeal before the Supreme Court challenging the decision of the High Court.

Arguments of Appellant:

The appellant before the Supreme Court stated that since the property was self-acquired by Marappa Gounder and not a joint property, the said property would devolve onto his daughter, who is close than his brother's son. The appellant pleaded that as per Law of Mitakshara, the right to inheritance depends upon propinquity i.e., proximity of relationship and Kuppayee Ammal was closer to Marappa Gounder than Gurunatha Gounder Junior, the property would devolve on Kuppayee Ammal and not on the respondents. The appellant further pleaded that as per the Hindu Law, the daughter is not disqualified to inherit in separate property of her father and when a male hindu dies without a son leaving only daughter, his separate property would devolve upon the daughter through succession and the property will not devolve upon brother's son through survivorship.

Arguments of Respondents:

The Respondents argued that suit property was purchased by Marappa Gounder in court auction sale out of the family funds and thus, it was joint property, and on his death, since he had no male heir, the defendant as a coparcener succeeded to the estate. Since the trail court decided and the same was upheld by High Court that Marappa Gounder has died in 1949 prior to enactment of Hindu Succession Act, the appellant and her sisters would not be legal heirs and cannot seek for partition of suit property.

Observations by Honourable Supreme Court:

On Self Acquired vs Joint Family Property:

The Court expressed that it would not involve in determination of the actual date of death of Marappa Gounder, since it was already settled by two fact finding authorities namely trail court and High Court. The Supreme Court than proceeded to examine the question that, whether the property was an absolute property or joint family property. The Court stated that the respondents in their written submissions have agreed that the suit property is absolute property and nowhere shown any evidence to prove the contrary. Accordingly, the Supreme Court based on the written affidavits submitted by respondents have concluded that the suit property was absolute property of Marappa Gounder and not the joint family property as argued by respondents.

On Rights of Sole Daughter vis-à-vis Inheritance:

The Supreme Court then proceeded to frame the important issue, the heart of this article, whether suit property will devolve on to the daughter upon the death of her father intestate by inheritance or shall devolve on to the father's brother's son by survivorship, essentially, Kuppayee Ammal vs. Gurunatha Gounder Junior. The Supreme Court, accordingly, framed three questions:

> *What is the nature of property and what would be the course of succession if it is a separate property as opposed to undivided property?*
>
> *Whether a sole daughter could inherit her father's separate property dying intestate? and*
>
> *If so, what would be the order of succession after the death of such daughter?*

The Supreme Court after tracing the origin of the Hindu Law has stated that the Mitakshara law has always been considered as the main authority for all the schools of law, with the sole exception of that of Bengal, which is mostly covered by another school known as Daya Bhaga. The Court referred to the judgment of Pranjivandas Tulsidas vs. Dev Kuvarbai 1 Bomb. HC B 131, wherein it was held that a Hindu owning separate property died without a male issue, leaving behind a widow, four daughter and a brother and male issues of other deceased brothers and Bombay High Court observed that widow was entitled to a life estate in the property and subject to her interest, the property would devolve to the daughters absolutely in preference to the brother and the issue of deceased brothers. The said judgment was followed in the matter of Tuljaram Morarji vs. Mathuradas, Bhagvandas and Pranjivandas ILR (1881) 5 Bom 662 and Chotay Lall vs. Chunnoo Lall 1874 SCC Online Cal 10. The Court referred to the digest of 'Yajnavalkya [2]' states that 'What has been self-acquired by any one, as an increment, without diminishing the paternal estate, likewise a gift from a friend or a marriage gift, does not belong to co-heirs'. The Court then referring to Standish Grove Grady's book on 'Treatise on Hindoo Law of Inheritance', wherein the judgment in matter of Katama Natchiar vs. The Rajah of Shivagunga was discussed to state that failing male issues, a widow takes the self-acquired property of her husband and no doubt, on the failure of male issue and a widow, the daughter would take. By referring to Mulla's Hindu Law the Supreme Court stated that Mitakshara recognizes two modes of devolution of property, namely survivorship and succession and the rule of survivorship applies only to joint family properties. However, for self-acquired property, the rule of succession applies to property held in absolute severalty by last owner. The Court then concluded that, from the above, it is abundantly clear that a daughter was in fact capable of inheriting the father's separate estate. The Court have arrived at the above conclusion by relying on the below judgments:

[2]The Mitakshara School derives majorly from running commentaries of Smritis written by 'Yajnavalkya'.

S.No	Judgement	Court	Observations by Supreme Court
1	Katama Natchiar vs. Srimut Rajah Mootoo Vijaya Raganadha Bodha Gooroo Swamy Periya Odaya Taver[3]	Privy Council	• The Privy Council noted the arguments of Anga Mootoo Natchiar, where she stated that the Zamindar had been acquired by the sole exertions and merits of her husband and as an issue of law that what is acquired by a man, without employment of his patrimony, shall not be inherited by her brothers and co-heirs, but if he dies without male issue, shall descend to his widows, his daughters and parents, before going to her brothers or remoter collaterals. • The Privy Council after hearing to the above arguments has framed three questions, out of which, the third one, is relevant. The third question is that, if the property is self-acquired and separate, what is the course of succession according to Hindoo Law of such an acquisition, where the family is in other respects an undivided family? • The Privy Council stated that the commentary on Mitakshara affirms in general terms the rights of the widow to inherit on failure of male issue. The said commentary has concluded that a wedded wife, being chaste, takes the whole estate of man, who, being separated from his co-heirs, and not subsequently re-united with them, dies leaving no male issue. The Privy Council however stated that the commentary in the context deals only with cases in which the property in question has been either wholly the common property of a united family, or wholly the separate property of the deceased husband but there was no commentary on the situation in which the property in question may have been in part the common property of a united family, and in part the separate acquisition of the deceased. The Privy Council stated that it cannot be assumed that because widows take the whole estates of their husbands when they have been separated from, and not subsequently reunited with, their co-heirs, and have died leaving no male issue, they cannot, when their husbands have not been separated, take any part of their estates, although it may have been their husband's separate acquisition and accordingly the commentary in the context could not be applied. • The Supreme Court stated that on a complete reading of the judgment of Privy Council, the following legal principals emanate:

[3](1861-64) 9 Moo IA 539

			❖That the general course of descends of separate property according to the Hindu Law is not disputed it is admitted that according to that law such property (separate property) descends to widow in default of male issue. ❖It is upon the Respondent (in the matter before Privy Council) to make out that the property here in question which was separately acquired does not descend according to the general course of law ❖According to the more correct opinion, where there is a undivided residue, it is not subject to ordinary rules of partition of joint property, in other words, if it a general partition any part of the property was left joint, the widow of the deceased brother will not participate, notwithstanding with separation, but such undivided residue will go exclusively to the brother. ❖The law of succession follows the nature of property and of the interest in it. ❖The law of partition shows that as to the separately acquired property of one member of a united family, the other members of the family have neither community of interest nor unity of possession. ❖The foundation therefore of a right to take such property by survivorship fails and there are no grounds for postponing the widow's right any superior right of the co-parceners in the undivided property. ❖The Hindu Law is not only consistence with this principle, but is also most consistent with convenience. • The law therefore is that succession in the case of Hindu male dying intestate is to be governed by inheritance rather than survivorship is affirmed. In the absence of male member, the property devolves upon to the widow and thereafter to the daughter.

2	SivagnanaTevar vs. Periasam[4]	Privy Council	• Following the above case, the Privy Council stated that the palaypat was the separate property of the Dhorai Pandian and on death of Dhorai Pandian, his right, if he had any left undisposed of in the property, passed to his widow, notwithstanding the undivided status of the family.
3	Ghurpatari vs. Smt Sampati[5]	Allahabad HighCourt	• The question before the full bench is, whether a custom under which daughters are excluded from inheriting the property of their father, can by implication exclude the daughter's issue both males and females, also such from inheritance. • The Court referring to various commentaries stated that the right of daughter and daughter's son to succeed the property was well recognized in the Mitakshara law and the daughter ranks fifth in the order of succession and the daughter's son ranked sixth.
4	Lal Singh vs. Roor Singh[6]	Punjab & Haryana	• The Court has held that daughters and daughters son have a preferential claim to non-ancestral property as against the collaterals.
5	Gopal Singh vs. Ujagar Singh[7]	Supreme Court	• The Supreme Court stated that the daughter succeeds to the self-acquired property of her father in preference to collaterals.
6	Devidas vs. Vithabai[8]	Bombay HC	• In this case, Arjuna died in 1936 and succession opened and while determining the shares during partition, daughter of one pre-deceased sons of Arjuna namely, Vithabai was held entitled for share. However, the name of Vithabai was removed from revenue records. She filed a suit for declaration for claiming 1/3rd share with other reliefs. When the matter was carried before High Court, the High Court stated as under. • When Zolu died in 1935, he was joint with his father and brothers and his share in coparcenary would devolve by survivorship and not by succession. Since Zolu did not hold any separate property admittedly and therefore, there was no question of property passing over by succession and accordingly Vithabai would not be entitled for share.

[4]ILR (1878) 1 Mad 312
[5]AIR 1976 All 195
[6]PLR 55 P&H 168
[7]AIR 1954 SC 579
[8](2008) 5 Mah LJ 296

The Court stated that, from the decisions and discussions, it is clear that the ancient text as also the smritis, the commentaries have recognized the rights of several female heirs, the wives and the daughter's being the foremost of them. Accordingly, it held that if a property of a male hindu dying intestate is a self-acquired property or obtained in partition of a co-parcenery or a family property, the same would devolve by inheritance and not by survivorship, and a daughter of such male hindu would be entitled to inherit such property in preference to other collaterals. Since, in the instant case, it is concluded that the property is self-acquired by Marappa Gounder, despite the family being in state of jointness, upon his death intestate, his sole surviving daughter Kuppayee Ammal, will inherit the same by inheritance and the property shall not devolve by survivorship.

As far as the question, who would succeed after Kuppayee Ammal, the Supreme Court stated that there are contradictory opinions in respect of order of succession to be followed after the death of such a daughter inheriting the property from his father. One school is of the view that such daughter inherits a limited estate like a widow, and after her death, it would revert to heirs of the deceased male who would be entitled to inherit by survivorship. While the other school of thought is exactly opposite. However, the Court stated that this would not be a challenge in the current set of facts, since, Kuppayee Ammal has deceased in 1967 after the enactment of Hindu Succession Act, 1956 and hence, guided by Section 14 of the said act instead of the situation prior to the said enactment. The Court stated that after the introduction of Section 14, the women acquired absolute interest in the estate and not limited interest as existed earlier, and the succession of those properties would happen in accordance with Section 15. The scheme of Section 15(1) goes to show that the property of Hindu females dying intestate is to devolve on her own heirs, the list is enumerated in clauses (a) to (e) of Section 15(1). Section 15(2) carves out exceptions is confined to the property inherited by a Hindu female either from her father or mother, or from her husband or father-in-law and the exception shall operate only in the event of Hindu female dies without leaving any direct heirs, her son or daughter or children of the pre-deceased son or daughter.

The Court concluded stating that since in the present case, since the succession of suit properties opened in 1967 upon the death of Kuppayee Ammal, the 1956 Act shall apply and thereby Ramasamy Gounder's daughters being Class – I heirs of their father too, shall be heirs and entitled to 1/5th share each in suit properties.

This article is contributed by CA Sri Harsha. The author can be reached at harsha@sbsandco.com

INTERNATIONAL TAXATION

THE STORY OF MOST FAVOURED INTERPRETATION OF MFN CLAUSE IN TREATIES

Contributed by CA Sri Harsha & CA Narendra

Introduction

This article aims at understanding the concept of Most Favored Nation ('MFN') clause in the Double Taxation Avoidance Agreement ('DTAA' or 'Treaty') between India and other countries, issues and controversies therein.

A country enters into treaty with other country for various purposes, the main object of which is for elimination of double taxation by way of sharing/forgiving taxation rights in respect of income earned by assessee.

As there is a requirement to share/forgive taxation rights by two countries, treaty may be concluded on different terms with different countries .In order to protect the interest of the countries for sharing taxation right, some countries may insert MFN clause in the treaty between them.

MFN clause means providing no less favorable treatment to the country than they provide under treaty with other countries. The objective of inserting MFN clause is to safeguard the investment made by the resident of a contracting in another contracting state.

As taxability of income differs from Article to Article in treaty depending upon nature of income, MFN clause may be entered with respect to particular type of Article in such treaty. Hence, MFN clause may differ from country to country. Generally, MFN clause may be inserted with respect to:-

- Taxation based on source and residency (scope of Income).
- Rate of tax in respect of a particular income (specifically with respect to passive income).

India has entered into treaties with majority of countries in the world and has agreed for MFN clause with some of the countries which inter alia includes France, Netherlands, Swiss confederation, Sweden and Spain etc.

India – France DTAA[1]:

'In respect of articles 11 (Dividends), 12 (Interest) and 13 (Royalties, fees for technical services and payments for the use of equipment), if under any Convention, Agreement or Protocol signed after 1-9-1989, between India and a third State which is a member of the OECD, India limits its taxation at source on dividends, interest, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate of scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention, Agreement or Protocol on the said items income shall also apply under this Convention, with effect from the date on which the present Convention or the relevant Indian Convention, Agreement or Protocol enters into force, whichever enters into force later.'

[1]MFN clause with other countries has been reproduced at the end of the Article for understanding

The protocol amending the provisions of treaty between India and France states that if India provides relief (by way of reducing the rate of tax or reducing the scope of income) in respect of dividend, interest or royalty/FTS[2] to any other country which is a member of OECD[3] through any convention or protocol signed on or after 01-01-1989, same relief is applicable for the said income (dividend, interest or Royalty/FTS) in respect of India -France treaty. India has similar MFN clause in treaties with some other counties the details of which are discussed in the Table below:

[2]Fee for Technical Services

[3]Organisation for Economic Co-operation and Development

Treaty between	Scope of MFN	Country to provide relief	Conditions to invoke MFN clause	Effective date of Invocation
India – France	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	• If any agreement/protocol is signed on or after 01.09.1989 by India with any third state which is a member of OECD then, MFN activates automatically.	• Effective from the date on which the protocol with France or the agreement with third state whichever enters into force later.
India – Netherlands	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	• If any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically.	• Effective from the date on which the Convention or Agreement with third state enters into force.
India – Switzerland	• Rate of tax with regard to dividend, interest or royalty/FTS. • Scope of income with regard to royalty or FTS.	India	• In respect of rate of tax, if any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically. • In respect of scope of income, if any agreement/protocol is signed by India with any third state which is a member of OECD then, Switzerland and India shall enter into negotiations without undue delay in order to provide the same treatment to Switzerland as that provided to the third State.	• In respect of rate of tax, MFN activates automatically from the date on which agreement with third state enters into force. • In respect of scope of income, MFN activates from the date on which both the countries agreed to provide relief by way of negotiations.
India – Philippines	• Rate of tax with regard to Article 8 (air transport) and Article 9 (shipping).	Philippines	• If Philippines agrees with any third state for lower or nil tax rate, it shall without any undue delay inform the India and two Govt. will review said Articles for providing similar kind of treatment.	• Protocol states that MFN comes to force from the date on which both the countries agreed to provide such relief.

India – Sweden	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS. • Taxation of PE in India of Swedish Companies.	India	• If any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically.	• Protocol does not provide specific effective date for MFN clause. Hence, effective date of protocol/DTAA is applicable for invoking the MFN clause i.e., 25.12.1997.
India – Israel	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	MFN clause has been omitted through a protocol with effective from 14.02.2017.	
India - Belgium	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	• If any agreement/protocol between India with any third state which is a member of OECD comes into force after 01.01.1990 then, MFN activates automatically.	• Effective from the date from which the protocol or the Convention or Agreement with third state is effective, whichever date is later.
India – Finland	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	• If any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically. However, India shall inform the Finland for issuing the notification in this regard.	• Protocol states that MFN comes to force from the date on which notification in this regard is issued by both the countries.
India – Spain	• Rate of tax or scope of income with regard to royalty/FTS.	India	• If any agreement/protocol between India with any third state which is a member of OECD comes into force after 01.01.1990 then, MFN activates automatically.	• Effective from the date on which the protocol comes into force or the relevant Indian Convention or Agreement with third state, whichever enters into force later.
India – Hungary	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India	• If any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically.	• Protocol does not provide specific effective date for MFN clause. Hence, effective date of protocol/DTAA is applicable for invoking the MFN clause i.e., 04.03.2005.
India – Kazakhstan	• Rate of tax or scope of income with regard to dividend, interest or royalty/FTS.	India and Kazakhstan	• If any agreement/protocol is signed by India with any third state which is a member of OECD then, MFN activates automatically.	

Issues in interpretation of MFN Clause:

On plain reading of the treaty, MFN clause seems to be unambiguous. However, it has created a buzz in direct tax litigations in India in recent times.

The majority of treaties with India which contains MFN clause states that if India enters into any agreement with any third state (which is a member of OECD) after the agreement with first mentioned state, MFN clause would be applicable.

The protocol amending the provisions of treaty between India – Netherlands/France states that in order to invoke FMN clause, following conditions are to be satisfied:

i. India has to enter into a treaty with any third state on after signing of treaty with Netherlands/France.

ii. Such third state shall be a member of OECD.

iii. India provides relief in respect of rate of tax or scope in respect of passive income i.e., interest, dividend, royalty/FTS.

India has entered into treaty with Slovenia, Lithuania and Colombia with lower rate of tax on dividend income (5 percent)after the agreement with Netherlands or France. However, such counties were not the members of OECD at the time of entering the treaty with India and have become members of OECD in recent times.

As these countries i.e., Slovenia, Lithuania and Colombia have become members of OECD after the signing of treaty with India, the question that arose is, whether MFN clause triggers in the case of Netherlands, France etc?

In this regard, Netherlands has issued a decree dated 28.02.2012[4] to clarify that beneficial provisions of DTAA between India and Slovenia are applicable for India – Netherlands DTAA as Slovenia has become member of OECD from 21.07.2010.Similar decree/Bulletin has been issued by France and Swiss Confederation.

Interpretation of MFN Clause by the Indian Income Tax Department:

Indian income tax department has taken different stand and states that as those countries are not the members of OECD on the date of signing of treaty with India, which is the precondition for invoking the MFN clause, the beneficial provisions contained in India – Slovenia are not applicable in respect of Netherlands.

The department has stated that the protocol appended to India – Netherlands treaty is like a contingent contract and such MFN clause can be invoked only if following conditions are satisfied:

- The third country should be a member of OECD on the date of signing of treaty with India and also on the date of invoking the MFN clause.

- The beneficial provisions are extended to residents of third state post execution of treaty with India.

Further, tax department has argued before the High Court in certain matters, that MFN clause is effective only when India issues a notification in the Official Gazette in this regard.

[4]No. IFZ 2012/54M, Tax Treaties, India

Interpretation of MFN Clause by Indian Judicial Fora:

The Hon'ble Delhi High Court[5] has analysed protocol appended to treaty between India – Netherlands in detail and given the judgement.

With regard to issue of separate of notification for invoking the MFN clause, the Court has relied on Divisional Bench judgement[6] in the context of India – France treaty, wherein the High Court has held that once the DTAA has itself been notified, and contains the Protocol including para 7 thereof, there is no need for the Protocol itself to be separately notified or for the beneficial provisions in some other Convention between India and another OECD country to be separately notified to form part of the Indo-France DTAA.

With regard to Slovenia becoming the OECD member after the signing of treaty with India, the Court has held as follows:

- MFN clause in India – Netherlands can be applied only if third state with whom India entered into treaty is a member of OECD and India agrees to provide relaxations in respect of specified incomes.
- The best way to interpret the protocol to the treaty is how the other state has interpreted the protocol.
- The principles of common interpretation should be applied while interpreting the international treaties.
- While interpreting the international treaties including tax treaties, the rules of interpretation that apply to domestic or municipal law need not be applied. The treaties are negotiated by diplomats and not necessarily by men instructed in the law.

Accordingly, the High Court has held that beneficial provisions contained India – Slovenia are applicable for India – Netherlands treaty with effective from Slovenia becomes the member of OECD.

CBDT Circular on interpretation of MFN Clause:

Subsequent to the High Court Judgment, the Central Board of Direct Taxes ('CBDT') in India has issued a Circular[7] dated 03.02.2022 for interpretation of MFN Clause. CBDT has issue the circular as follows:

- The uniliteral decree or bulletin passed by Netherlands or France donot represent the shared understanding of India in respect of interpretation of MFN clause.
- On plain reading of MFN clause with Netherlands, France or Swiss Confederation, it is clear that there is a requirement that the third state is to be a member of OECD both at the time of conclusion of treaty with India as well as at the time of invoking the MFN Clause.
- The protocol to the treaties states that MFN clause is effective from the date of entry into force of treaty between India and third state. Thus, decree or bulletin issued by respective countries to make MFN applicable from the date of such third state becoming the member of OECD is not in accordance with the provisions of MFN clause.
- It is requirement in India under section 90 that treaty or protocol to treaty are implemented after the Notification in the Official Gazette. Hence, in order to invoke provisions of MFN clause, such MFN clause has to be notified by the Government of India in the Official Gazette.

[5]Concentrix Services Netherlands B.V. and Optum Global Solutions International BV[TS-286-HC-2021(DEL)]

[6]Steria (India) Ltd[TS-5588-HC-2016(Delhi) O].

[7]F.No.S03/1/2021-FT&TR-1

- Selective interpretation of MFN clause is not acceptable. Treaty between India – Slovenia provides separate rate of taxes for dividends i.e., 5% subject to satisfaction of shareholding condition and 15% in other cases. Invoking MFN clause with respect to 5% when such shareholding conditions are met and not switching to 15% of tax in other cases is not acceptable.

Accordingly, CBDT has given the following clarification to invoke MFN clause in treaty:

- ❖ Treaty with the third state is entered after the signing of treaty with the country with whom India agreed for MFN clause.
- ❖ The treaty is entered into between India and a third state which is a member of the OECD at the time of signing the treaty with it.
- ❖ India limits its taxing rights in the second treaty in relation to rate or scope of taxation in respect of the relevant items of income.
- ❖ A separate notification has been issued by India, importing the benefits of the second treaty into the treaty with the first State, as required by the provisions of sub-section (1) of Section 90.

If all the conditions enumerated in above Paragraph are satisfied, then the lower rate or restricted scope in the treaty with the third State is imported into the treaty with an OECD State having MFN clause from the date as per the provisions of the MFN clause in the DTAA, after following the due procedure under the Indian tax law.

Interpretation of CBDT Circular by Indian Judicial fora:

The Tribunal[8] has opined that it is not required to issue fresh notification by the Government in official Gazette for invoking the MFN clause. The Tribunal has held that Circular issued by the CBDT is binding only the revenue as held by the Supreme Court[9] and not on the assessee, Tribunal or other appellate authorities. The Tribunal has further held that such Circular is effective from the date of issuance and cannot be operative retrospectively.

Authors' Remarks:

The crux of the litigation is whether such OECD membership is required at the time of signing of treaty with India in order to invoke MFN clause. Vienna Convention on the Law of Treaties states that a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

In order to interpret the MFN clause, attention may be drawn to the intention of the parties incorporating the MFN clause in treaty between them.

If the intention of the state to negotiate MFN clause with India is to have parity with OECD members so that such country may have equal trade and investment options along with other OECD members, then interpretation advanced by the Hon'ble Delhi High Court in the case of Concentrix Services Netherlands B.V may be inline with the intention of MFN clause. In this regard, the other states have already expressed their intention by way of decree or bulletin which may not be considered as unilateral measures. In such a situation, it is required to test the condition of OECD membership at the time of invoking the MFN clause.

[8]GRI Renewable Industries S.L [TS-79-ITAT-2022(PUN)].
[9]Hero Cycles Pvt. Ltd. (1997) 228 ITR 463 (SC)

CBDT circular has stated that on plain reading of MFN clause, such third state is to be the member of OECD both at the time of entering into treaty with India and invoking provisions of MFN.

However, when it comes to paragraph 5 of Circular specifying the conditions for invoking MFN clause, it is stated that '*The second treaty is entered into between India and a State which is a member of the OECD at the time of signing the treaty with it.'*

It is not clear as to whether it is to be considered as deliberate omission of condition regarding membership at the time of invoking the MFN clause?

If yes, whether MFN clause can be invoked even if such third state ceases to be a member of OECD at the time of invoking MFN clause. If no, whether it means such conditions is to be tested both at the time of signing the treaty with India as well as at time of invoking MFN clause?

However, treaty between India Netherlands/France does not have such type of wording in MFN clause which mandates to check such condition both at the time of signing the treaty with India as well as at time of invoking MFN clause.

Further, upon reading of the above Circular, it appears that CBDT tried to impose new set of conditions for invoking the MFN clause in the treaty some of which are against the settled law in interpretation of treaties.

It is well established law that once the treaty or protocol has been notified the Government in Official Gazette, entire treaty or protocol is applicable from the date of such notification and no other notification is required for piece of treaty or protocol unless there is a change in such treaty.

Further, treaties containing MFN clause with India provides different methods for making the MFN clause effective. The treaty between India – Finland states that '*The competent authority of India shall inform the competent authority of Finland without delay that the conditions for the application of this paragraph have been met and issue a notification to this effect for application of such exemption or lower rate.'*

The above-mentioned condition is not found in treaties with other counties viz. Netherlands, France or Swiss Confederation. If there is any requirement to issue notification for MFN clause, same might have incorporated in the protocol with such treaties.

Taking a different stand in respect of issue of separate notification which is already settled by various judicial fora may create unnecessary litigation.

MFN *clause states that 'India limits its taxation at source on dividends, interest, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate of scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention, Agreement or Protocol on the said items income shall also apply under this Convention'*

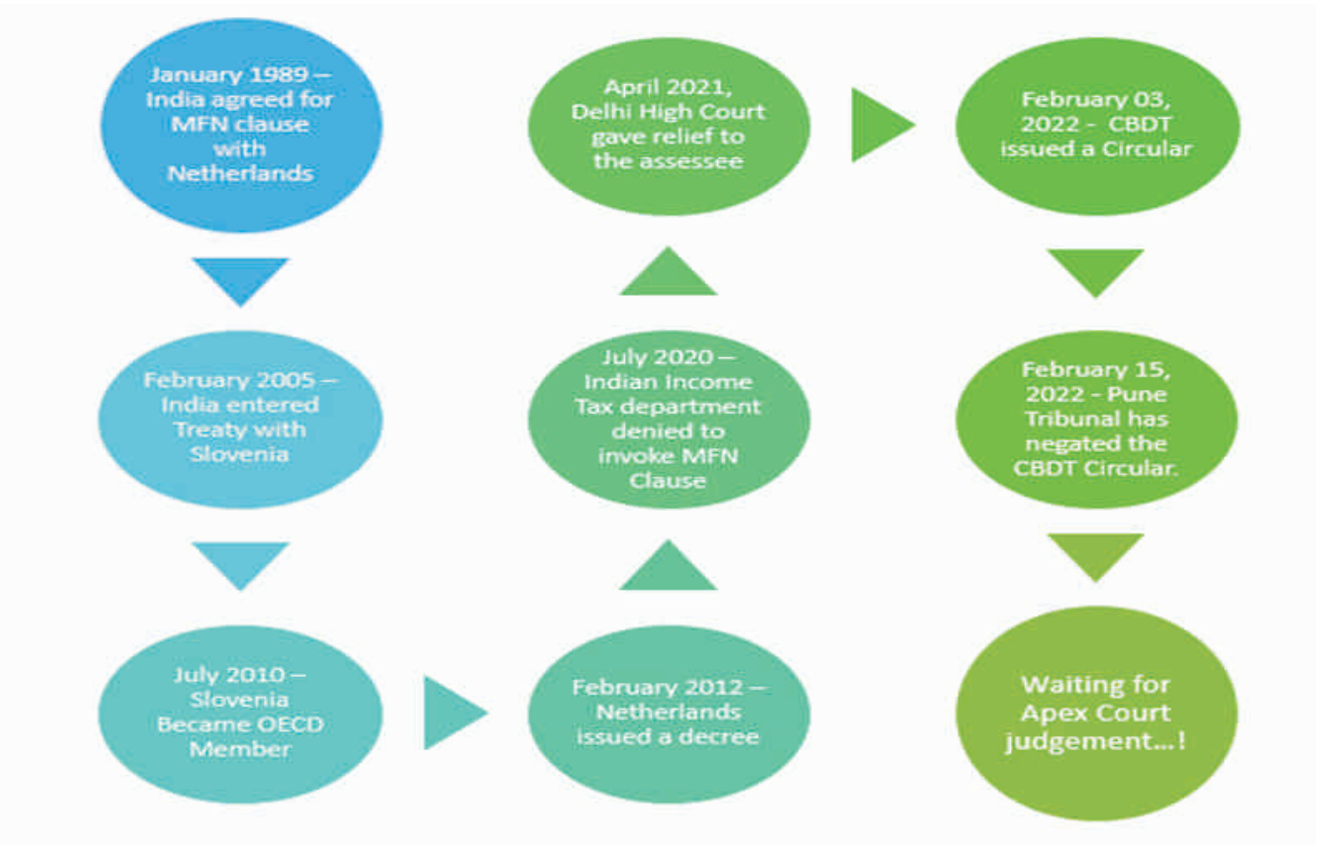
In this regard, CBDT has gone one step further and denied invoking MFN Clause with respect of beneficial rate of tax i.e., 5% rate of tax. However, the stand taken by the CBDT may be against the object and purpose of entering into MFN clause.

It is settled law that treaties have to be construed in a way in which they have been drafted. The MFN clause clearly provides that if India provides any relief to third state, same relief is to be provided to first state and it may not be the objective of the MFN to replace the specific Article in treaty first state with Article in treaty with third state.

However, as CBDT Circular is binding on the revenue, officer who has assessment powers, may not provide relief to the assessee. Further, the judgment given by the Delhi High Court in the case of Steria (India) Ltd is pending at Supreme Court.

Hence, the beneficial provisions contained in MFN cluse are not readily available to the assessee in current times as long as the issue is not settled by Apex Court in India.

Flow of Activities in India:



MFN Clauses in Different treaties:

India – Netherlands DTAA:

'If after the signature of this convention under any Convention or Agreement between India and a third State which is a member of the OECD India should limit its taxation at source on dividends, interests, royalties, fees for technical services or payments for the use of equipment to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, then as from the date on which the relevant Indian Convention or Agreement enters into force the same rate or scope as provided for in that Convention or Agreement on the said items of income shall also apply under this Convention.'

India – Switzerland DTAA:

'In respect of Articles 10 (Dividends), 11 (Interest) and 12 (Royalties and fees for technical services), if under any Convention, Agreement or Protocol between India and a third State which is a member of the OECD signed after the signature of this Amending Protocol, India limits its taxation at source on dividends, interest, royalties or fees for technical services to a rate lower than the rate provided for in this Agreement on the said items of income, the same rate as provided for in that Convention, Agreement or Protocol on the said items of income shall also apply between both Contracting States under this Agreement as from the date on which such Convention, Agreement or Protocol enters into force.

If after the date of signature this Amending Protocol, India under any Convention, Agreement or Protocol with a third State which is a member of the OECD, restricts the scope in respect of royalties or fees for technical services than the scope for these items of income provided for in Article 12 of this Agreement, then Switzerland and India shall enter into negotiations without undue delay in order to provide the same treatment to Switzerland as that provided to the third State.'

India – Philippines:

'With reference to Articles 8 and 9 if at any time after the date of signature of the Convention the Philippines agrees to a lower or nil rate of tax with a third State the Government of the Republic of the Philippines shall without undue delay inform the Government of India through diplomatic channels and the two Governments will undertake to review these Articles with a view to providing such lower or nil rate to profits of the same kind derived under similar circumstances by enterprises of both Contracting States.'

India – Sweden:

'In respect of Articles 10 (Dividends), 11 (Interest) and 12 (Royalties and fees for technical services) if under any Convention. Agreement or Protocol between India and a third State which is a member of the OECD, India limits its taxation at source on dividends, interest, royalties, or fees for technical services to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention, Agreement or Protocol on the said items of income shall also apply under this Convention.

With reference to Article 25:

The taxation in India of permanent establishments of Swedish companies, shall in no case differ more from the taxation of similar Indian companies than is provided by the Indian law on the date of signature of this Convention.'

India – Belgium:

'If under any Convention or Agreement between India and a third State being a member of the OECD which enters into force after 1st January, 1990, India limits its taxation on royalties or fees for technical services to a rate lower or a scope more restricted than the rate or scope provided for in the present Agreement on the said items of income, the same rate or scope as provided for in that Convention or Agreement on the said items of income shall also apply under the present Agreement with effect from the date from which the present Agreement or the said Convention or Agreement is effective, whichever date is later.'

India – Finland:

'It is agreed that if after coming into force of this Agreement, any agreement or convention between India and a Member State of the Organisation for Economic Cooperation and Development provides that India shall exempt from tax dividends, interest, royalties or fees for technical services (either generally or in respect of specific categories of dividends, interest, royalties or fees for technical services) arising in India, or limit the tax charged in India on such dividends, interest, royalties or fees for technical services (either generally or in respect of specific categories of dividends, interest, royalties or fees for technical services) to a rate lower than that provided for in paragraph 2 of Article 10 or paragraph 2 of Article 11 or paragraph 2 of Article 12 of the Agreement, such exemption or lower rate shall be made applicable to the dividends, interest, royalties or fees for technical services (either generally or in respect of those specific categories of dividends, interest, royalties or fees for technical services) arising in India and beneficially owned by a resident of Finland and dividend, interest, royalties or fees for technical services arising in Finland and beneficially owned by a resident of India under the same conditions as if such exemption or lower rate had been specified in those paragraphs. The competent authority of India shall inform the competent authority of Finland without delay that the conditions for the application of this paragraph have been met and issue a notification to this effect for application of such exemption or lower rate.'

India – Spain:

'If under any Convention or Agreement between India and a third State which is a Member of the OECD, which enters into force after 1-1-1990, India limits its taxation at source on royalties or fees for technical services to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of incomes, the same rate or scope as provided for in that Convention or Agreement on the said items of income shall also apply under this Convention with effect from the date on which the present Convention comes into force or the relevant Indian Convention or Agreement, whichever enters into force later.'

India – Hungary:

'In respect of Articles 10 (Dividends), 11 (Interest) and 12 (Royalties and fees for technical services), if under any Convention, Agreement or Protocol between India and a third State which is a member of the OECD, India limits its taxation at source on dividends, interest, royalties or fees for technical services to a rate lower or a scope more restricted than the rate or scope provided for in this Convention on the said items of income, the same rate or scope as provided for in that Convention. Agreement or Protocol on the said items of income shall also apply under this Convention.'

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