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International Tax

India's MFN Controversy

Was India's Supreme Court driven by '*Advaitha*' to apply '*Dvaitha*'?

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October 2023 witnessed a significant event for all international tax enthusiasts as the Hon'ble Supreme Court (SC) of India ruled[1] on the much-debated issue of automatic enforceability of Most Favoured Nation (MFN) Clause under the Double Taxation Avoidance Agreements (DTAAs or Treaty) entered into by India.

The case involved multiple taxpayers and the three DTAAs that were under consideration were India-Netherlands, India-France and India-Switzerland. Two issues came up for consideration before the Supreme Court:

1. Whether MFN Clause could be invoked when the third country with which India has entered into a DTAA was not an OECD member yet at the time of India's entering into the relevant DTAA under consideration?
2. Whether MFN Clause is to be given effect to automatically or it is to only come into effect after a notification is issued?

While the judgment is quite detailed and exhaustive, it raised quite a few eyebrows. While on the first question, the fraternity was divided in its view – some felt that the view that was adopted by the taxpayers was a little far-fetched, others felt that on principle, the benefit should be granted if at the time of invocation of the benefit, the third country was an OECD member; answer to second question caught everyone by *"surprise"* as it was largely accepted, believed and therefore anticipated that the SC would uphold the decisions of the lower Court that had ruled in favour of taxpayer/s, however SC ruled in favour of Revenue and held that a separate notification was mandatory under section 90 for MFN Clause to be available for invocation, in absence of which such a benefit could not be sought.

As was anticipated, the taxpayers have preferred a Review Petition before the SC to review the judgment. The fraternity eagerly awaits the outcome of the Review Petition.

This **kcmSpark** is an attempt to evaluate and understand the possible reasons behind the *"surprise"* and to share some thoughts on what the key arguments / factors could be when the SC considers the Review Petition. As is the objective of any **kcmSpark**, our objective is limited to bringing out a different perspective with a thought-provoking analysis without undermining the importance of the judgment laid down by Hon'ble SC.

The focus in this edition is on SC's answer to the second question because that is where a larger gap appears between what is understood by the fraternity and what the SC has observed and held.

[1] Assessing Officer (International Tax) v. Nestle SA [2023] 458 ITR 756 (SC)

MFN under DTAAs - Basics

MFN treatment is a very popular term in the context of International Trade. In common words, it means providing all members with the most favourable treatment that is provided to any particular member in respect of any particular transaction. What initially started as a bilateral measure, soon found an official place in General Agreement on Tariffs & Trade (GATT) in the context of cross-border transactions of goods.

This, later on, started finding place in DTAAs wherein a country would promise to provide the same favourable tax treatment to the other country in case it (the first country) later on provided a favourable tax treatment to a third country [we will refer to this act of a country entering into a favourable DTAA with a third country later on as a 'future event']. While there is no Law (domestic or international) that mandates insertion of MFN Clause in a DTAA, it would depend upon the countries' political & trade relationship, negotiating powers of a particular country, economic needs of a particular country, etc. One of the instances could be providing similar favourable tax treatments to OECD nations. In terms of coverage, generally, from a DTAA perspective, MFN Clause would provide for favourable tax treatment to residents of a Country in a Source Country in respect of transactions involving interest, dividends, royalties, and fees for technical services, if the Source Country happens to provide a more beneficial treatment on such transactions later on to residents of a third Country pursuant to a DTAA with such third Country. Such favourable tax treatments could typically be either in the form of a reduced rate of tax or a reduced scope for taxability. Because an MFN Clause represents an agreement to act based on an event in the future, it generally finds place in the Protocols (that clarify the understanding between the Parties) that are signed either at the time of signing the DTAA itself or later by way of amending Protocols.

India's DTAAs with twelve countries[2] provide for a MFN Clause whereby India agrees to grant a favourable treatment. As mentioned earlier, the SC judgment dealt with MFN Clauses in DTAAs with the Netherlands, France, and Swiss Confederation.

[2] The Netherlands, the Philippines, France, Belgium, Spain, Switzerland, the U.K., Sweden, Hungary, Saudi Arabia, Finland, and Nepal

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Now that we have understood the basics of MFN under DTAAs, we move on to the relevant observations of SC that resulted in the ruling against the taxpayer/s. For each relevant observation, we shall provide our analysis & comments on why the Review Petition may get considered by SC.

Observation 1 – Treaty or Protocol requires notification under section 90(1) [Para 38 through Para 46 of the judgment]

One of the most fundamental reasons why the issue under consideration arose was because of the requirement of section 90(1) read with the Constitution of India. Section 90(1) of the Act states as under:

90. Agreement with foreign countries or specified territories

(1) The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India-

(a) for the granting of relief in respect of-

(i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or;

(ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or

(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory as the case may be, or;

(c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be,

and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

(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 Acxt shall apply to the extent they are more beneficial to that assessee."

Genesis of section 90

In order to understand the reason behind introduction of section 90, one may refer to the decision of SC in the case of **Azadi Bachao Andolan [2004] 10 SCC 1.** Relevant portion of the said judgment reads as under:

"The power of entering into a treaty is an inherent part of the sovereign power of the State. By article 73, subject to the provisions of the Constitution, the executive power of the Union extends to the matters with respect to which the Parliament has power to make laws. Our Constitution makes no provision making legislation a condition for the entry into an international treaty in time either of war or peace. The executive power of the Union is vested in the President and is exercisable in accordance with the Constitution. The Executive is qua the State competent to represent

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> *the State in all matters international and may by agreement, convention or treaty incur obligations which in international law are binding upon the State. But the obligations arising under the agreement or treaties are not by their own force binding upon Indian nationals. The power to legislate in respect of treaties lies with the Parliament under entries 10 and 14 of List I of the Seventh Schedule.* ***But making of law under that authority is necessary when the treaty or agreement operates to restrict the rights of citizens or others or modifies the law of the State.*** *If the rights of the citizens or others which are justiciable are not affected, no legislative measure is needed to give effect to the agreement or treaty.*
>
> *When it comes to fiscal treaties dealing with double taxation avoidance, different countries have varying procedures. In the United States such a treaty becomes a part of municipal law upon ratification by the Senate. In the United Kingdom such a treaty would have to be endorsed by an order made by the Queen in Council.* ***Since in India such a treaty would have to be translated into an Act of Parliament, a procedure which would be time consuming and cumbersome, a special procedure was evolved by enacting section 90 of the Act.***

SC in that case, goes ahead to explain the rationale behind introduction of section 90, also covering the provisions of the erstwhile Income-tax Act, 1922. It also places reliance on the landmark judgment of SC in the case of **Magan Bhai Patel v. Union of India AIR 1969 SC 783**. Our readers may read through these judgments to get more insight.

The judgments have considered the principle that India follows a Dualist *(Dvaitha)* Model as opposed to a Monist *(Advaitha)* Model and therefore believe that the rule of international law apply within a State only as a result of their adoption by the local law of the State. The principle was laid down by SC in the case of **Jolly George Varghese v. Bank of Cochin AIR 1980 SC 470** and some other judgments. This principle can also be inferred after a complex analysis and evaluation of the interplay of various Articles of the Constitution viz. Articles 51, 53, 73, 245, 246 and 253 read with various Lists. One of the finest judgments to understand all of the above is that of **Madras High Court** in the case of **T. Rajkumar v. Union of India [2016] 68 taxmann.com 182**, it is a tax enthusiast's delight to read!

While there are counters to the said proposition, especially considering the language of section 90, more so the difference between section 90(2) and section 90A(2), it would become a topic in itself deserving a separate kcmSpark and therefore, we will, for now, proceed by assuming that a DTAA needs to be notified under section 90 in order to apply. In the instant case as well, the SC has referred to multiple rulings including few covered above and held that India entering into a DTAA or protocol does not result in its automatic enforceability in courts and tribunals; the provisions of such treaties and protocols do not therefore, confer rights upon parties, till such time, as appropriate notifications are issued, in terms of section 90(1).

Our Analysis

This observation of SC was already well considered by previous rulings. However, these observations do not help conclude that when a Protocol is already notified (and therefore ideally applicable), whether a clause therein requiring a 'future event' for being available for invocation would require a re-notification on happing of such 'future event'. In fact, SC has itself limited the observations to enforceability of DTAA or protocol and not to each line of such already notified DTAA or protocol.

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In **Magan Bhai Patel's** case and then in **Azadi Bachao Andolan's** case, as highlighted earlier, the SC observed that when the Treaty or Agreement operates to restrict the rights of citizens or others or modifies the law of the State, making of law by Parliament becomes necessary. In simple terms, a DTAA or Protocol that restricts the rights of citizens or others or modifies the law of the State should be notified under section 90. Hence, the moot question is – in the context of MFN clause, when does the Treaty or Agreement (or Protocol) operate to restrict the rights of citizens or others or modify the law of the State?

India's DTAAs generally have the following types of MFN Clauses:

1. MFN Clause that requires negotiations / review after happening of a 'future event', before it can be enforced (Type 1)
2. MFN Clause that requires intimation / notification by India to the other country after happening of a 'future event', before it can be enforced (Type 2)
3. MFN Clause that does not provide for such conditions and therefore, applies 'automatically' on happening of a 'future event' (Type 3)

In this regard, reference can be had to the following MFN Clauses under India's DTAAs (illustrative):

Type 1

Erstwhile India-Switzerland DTAA

"D With reference to Articles 10, 11 and 12

If after the signature of the Protocol of 16th February, 2000 under any Convention, Agreement or Protocol between India and a third State which is a member of the OECD India should limit 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 Agreement on the said items of income, 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 DTAA

"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."*

Type 2

India – Finland DTAA

"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

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*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."*

Type 3

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."*

It is quite evident from the above that the languages used in MFN Clauses under different DTAAs vary significantly. As mentioned earlier, these are conscious decisions depending upon the economic circumstances, trade & political relationships that India shares with each of these countries.

The different types of MFN Clauses can be summarized as follows:

MFN Clause Type	Point of Invocation	Comments
Type 1	Only after negotiations post occurrence of a "future event".	If negotiations fail, there is a possibility that the MFN Clause may not be enforceable. It is important to note that in this type of MFN Clauses, even though enforceability is dependent upon negotiations, there is an **inherent duty / obligation** on the Country to undertake negotiations without delay.
Type 2	Upon intimation / notification to the other Country on occurrence of a "future event".	It is important to note that in this type of MFN Clauses, there is an **inherent duty / obligation** on the Country to intimate / notify without delay.

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MFN Clause Type	Enforceability	Comments
Type 3	On occurrence of a "future event"	No condition. Further, under this type of MFN Clause, Countries agree on the date of signing the DTAA / Protocol itself about the date from which benefits would be granted i.e. the date of occurrence of the 'future event'.

So far as Type 1 MFN Clauses are concerned, till the time the two countries are unable to arrive at an agreement post negotiation, it cannot be said that the MFN Clause has become enforceable. Type 2 MFN Clauses are relatively lenient in that they do not require negotiations but cast an obligation on India to intimate / notify the other country without delay and upon such notification / intimation, the MFN Clause becomes enforceable. Type 3 MFN Clauses are effectively agreements between the DTAA countries on the date of the Protocol / DTAA itself, that provide for automatic application as soon as the "future event" takes place, without requirement of any further negotiation / notification / agreement with the other country.

In light of the above, now we come back to the requirement of section 90 read with the Constitution and the principles laid down by SC in various cases. As discussed earlier, based on the Dualist model followed by India, if the treaty or agreement operates to restrict the rights of citizens or others or modifies the law of the State, it would require a domestic legislation for enforceability.

Therefore, as mentioned earlier, the moot question is what is the point of time when the agreement being, DTAA / Protocol / MFN Clause, operates to modify the law of the State? Once we are able to arrive at an answer to this question, we would be in a position to answer the principal question – *when is a notification under section 90 mandatory?*

Considering that it generally finds a place in a DTAA read with its Protocol, MFN is not, *per se*, a separate agreement between the two countries and hence, it cannot be assumed to be so, unless the provisions of the DTAA or the Protocol that contain the MFN Clause specifically indicate the same. If the DTAA or Protocol does not provide for any condition on fulfilment of which MFN Clause can be considered to be enforceable, the MFN Clause gets subsumed in the main DTAA and Protocol, therefore not a separate agreement. This should remain the case even if the actual invocation of MFN Clause may be 'contingent' (but not conditional) on a future event. On the other hand, if the language of the Protocol indicates that certain conditions need to be fulfilled before MFN Clause can actually be considered as a part of the DTAA or Protocol, it can then be considered that such MFN Clause applies & operates between the two countries only post fulfilment of those conditions and it is only then that such a Clause becomes an "agreement" between the Countries.

If we evaluate Type 1 and Type 3 MFN Clauses in this context, the following inferences can be drawn:

(a) Under Type 1, the countries have not yet reached an agreement to provide the most favored treatment and may decide to provide the same after negotiations and discussions – accordingly, the enforceability of the MFN Clause is conditional upon negotiations reaching a positive conclusion. Therefore, in such treaties, it becomes important for the two countries to enter into negotiations and then decide if MFN treatment ought

to be given or not. Even in this type, it is of utmost importance that countries start the negotiation process without any delay. Any signs of lack of intent towards negotiations or signs of undue delay could mean disrespecting the DTAA and thereby may constitute a breach of International Law and Constitution.

(b) Under Type 3, the countries have already reached an agreement under the main DTAA / Protocol to provide the most favored treatment without any condition. MFN Clause can be invoked by a taxpayer immediately on happening of a 'future event' without any requirement of negotiations or discussions between the two countries (as was the case in Type 1 MFN Clause). Hence, only the invocation is deferred till happening of the 'future event' (which is even otherwise, the basis / fundamental of any MFN Clause, whether under tax treaties or trade treaties) without any condition attached thereto. The happening of the 'future event' does not result in any new agreement / understanding between the two countries.

In fact, in absence of a provision allowing for negotiations between the two countries, if a country tries to get into negotiations, it would not only result into there being no difference between Type 1 and Type 3 MFN Clauses but it may also be considered as a breach of International Law and Constitution.

To better understand this, an analogy could be drawn, for example, from Article 12 of India-US DTAA (Royalties & Fees for Included Services). Under the said Article, rates are prescribed for first five years and then different rates are prescribed for the subsequent years. Beginning of the sixth year is the trigger event for new rates to apply. However, it is considered as a part of the main DTAA and hence, no separate notification is warranted even though the rate changes. Similarly, even in this type of MFN Clauses, the application of most favored treatment is automatic not warranting a separate notification under section 90.

Based on the above, now coming to the requirement of section 90 (read with Constitution), the trigger event i.e. the point of time when the agreement affects the right of citizens or modifies the law of the State can be arrived based on the point of time when the countries agree unconditionally to provide the most favored treatment. The same can be understood as under:

MFN Clause Type	When do countries agree to provide the most favorable treatment?	When does the agreement operate to modify the law of the State or affect the rights of citizens? (Trigger Event)
Type 1	Only after negotiations post occurrence of a "future event".	Only on successful negotiation
Type 3	Under the main agreement / protocol itself	As soon as the main agreement / protocol (that already contains the MFN Clause) is entered into and the countries have agreed / promised to provide the most favored treatment thereunder

Considering that under **Type 1 MFN Clauses**, the agreement operates to modify the law of the state only after successful conclusion of negotiations even though the 'future event' has already taken place, MFN treatment arising out of such conclusion can be considered as a separate agreement / understanding between the parties that operate to modify the law of the State. In such a case, conclusion of successful negotiations

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becomes the 'trigger event'. This may then warrant a separate notification under section 90 on the principles of *Dualism*.

Under **Type 3 MFN Clauses**, a separate notification is not called for considering that the countries have already agreed to provide the most favoured nation treatment without any conditions. The future 'contingent' event is not a 'condition' for enforceability of MFN (unlike requirement of negotiations) but it is, in fact, the basis for any MFN clause to apply. Accordingly, the domestic law is affected as soon as Governments agree to an unconditional MFN Clause and hence, it is the main DTAA / Protocol wherein the countries have agreed to modify the domestic law of the State. Therefore, the 'trigger event' is the main DTAA / Protocol itself that requires notification and not the 'future event'.

The situation could be a little tricky when it comes to **Type 2 MFN Clauses**. Unlike Type 1, these MFN Clauses do not require any negotiation. However, unlike Type 3, these MFN Clauses do not have a totally automatic application as well. As highlighted above, these MFN Clauses provide for two requirements on the country agreeing to provide a benefit (say, India), viz. (i) to inform the other country *without any delay* about the 'future event' and (ii) to issue a notification to provide the benefit. The question that arises is whether these two requirements are 'conditions' for MFN Clause to be enforceable or are they mere 'obligations' to be fulfilled by India? On a closer reading of the text, it appears that these are less of conditions and more of India's obligations. Again, when the requirements are read with the phrase *'without any / undue delay'*, it makes things clearer. These appear to be moral procedural obligations and more importantly, binding obligations on India under the DTAA / International Law, non-adherence to which could constitute breach of International Law. In terms of identifying the point of time when the agreement operates to modify the law of the State, one may conclude that it happens only on completion of process, i.e. informing the other country and of issuance of notification, but any delay in the process could be challenged either in Indian courts or as per the principles of International Law. In absence of any such specific requirement of issuance of notification for Type 3 MFN clauses, reading such a requirement therein may constitute breach of Treaty interpretation principles.

SC seems to have apparently missed out on dealing with the above aspects. The only aspects discussed by SC are those relating to the principles of Dualism, section 90 and certain judicial precedents without any discussion as to how these principles apply or don't apply in the context of different types of MFN Clauses. While the principles are well accepted, when we apply the same in the context of MFN Clauses as discussed above, they could give different results. Hence, there is a strong apparent reason why the Review Petition should be considered by SC. In fact, while concluding on the requirement under section 90 (at Para 46), again the SC has only concluded that a Treaty or Protocol does not have automatic application and requires notification under section 90(1) without any mention about specific requirement for MFN Clause.

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Observation 2 – Treaty (Protocol) Practices of India [Para 52 through Para 72 of the judgment]

In this segment of the judgment, the SC has discussed how India's approach has been in respect of various protocols having different types of MFN Clauses. After a very detailed analysis, SC has concluded that irrespective of the language used in different types of MFN Clauses in various Protocols, it has been India's practice to issue a separate notification under section 90, especially in the context of Netherlands, France, and Switzerland, for any MFN Clause to apply.

Our Analysis

As a matter of practice, India has consciously negotiated, discussed, and agreed upon different types of MFN Clauses (discussed at length earlier). The fact that this is a thought through process resulting in difference in languages used, is a clear indication of "India's practice". India's practice has all along remained to have flexibility in its MFN Clauses without insisting upon a particular type in all DTAAs. This coupled with the fact that discussions with DTAA partners would not have allowed India to have MFN Clauses requiring negotiations / notifications for invocation, itself goes to show that India's practice has been to agree to such different types of MFN Clauses.

Looked at from a different angle, the fact that India has not issued notifications in case of all the DTAAs and Protocols involving MFN and that too, for so many years, is also an indication of India's practices in respect of DTAAs. In fact, no further action in case of these DTAAs coupled with a clear language in the MFN Clause providing for 'automatic' application clearly indicates India's practice that is in sync with the language of MFN Clause.

If the requirement of undergoing a procedure of issuing a notification under section 90 is fetched too far so as to mean giving India a right to alter the terms of something already agreed with a DTAA partner (for e.g., initially agreeing to an automatic reduced rate or scope and thereafter unilaterally only notifying a reduced rate), it would not only amount to a breach of the DTAA but also a unilateral act to change the agreement / understanding between the parties.

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Observation 3 – Vienna Convention on Law of Treaties [Para 74 through Para 87 of the judgment]

Under this segment, we would take up various minute observations of the SC with our analysis / comments on each of such observations.

1. Contextual reading of Article 31(3) of Vienna Convention

SC has referred to Article 31(3) of Vienna Convention and considered it to be relevant in India context though India is not a signatory to the Convention. SC stated that the following should be taken into account while interpreting the provisions of a DTAA:

(a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions

(b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding the interpretation of the treaty or the application of its provisions;

(c) Any relevant rules of international law applicable in the relations between the parties

Our Analysis

It is extremely important to understand the exact provision of Article 31.

Article 31 of Vienna Convention states as under:

"Article 31 General Rule of Interpretation –

1. *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.*
2. *The **context** for the purpose of the interpretation of a treaty **shall comprise**, in addition to **the text, including its preamble and annexes:***
   (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
   (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty."
3. *There shall be taken into account, **together with the context**:*
   (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
   *(b) any **subsequent practice** in the application of the treaty **which establishes the agreement of the parties** regarding the interpretation of the treaty or the application of its provisions;*
   (c) any relevant rules of international law applicable in the relations between the parties."

While SC has focused on the three aids to interpretation in Article 31(3), it is equally or more important to note that those aids are to be seen ***"together with the context"*** which is the starting phrase in Article 31(3). Therefore, while 'interpreting' clause (b) of Article 31(3), one cannot lose sight of the 'context' in which a DTAA or a particular provision thereof has been entered into. As per Article 31(2), 'context' includes text, preamble and annexes. Seen from that perspective, the fact that a particular language has been used for a particular MFN clause in a DTAA cannot be ignored. The difference of language in different types of MFN is in itself an indication of the "context" in which the MFN Clause has been agreed upon. SC has apparently missed out considering the "context" i.e. the language of the MFN Clause while evaluating Article 31(3) of Vienna Convention.

2. Whether Article 31(3) should apply in the first place?

Our Analysis

Considering that SC has given a lot of importance to Article 31(3), for completeness, we started with the relevance of 'contextual' reading of Article 31(3). However, it is important to evaluate whether Article 31(3) should apply in the first place. As mentioned earlier, Article 31 deals with Aids to 'Treaty Interpretation'. At various places in the judgment, SC has observed that the issue under consideration is that of 'Treaty Integration' i.e. assimilation of a DTAA under the domestic law. In fact, SC's act of negating the difference in languages used in different types of MFN Clauses and merely giving an interpretation based on an understanding of section 90 of the Act implies that in the opinion of SC, this is not a matter of interpretation of a treaty or its provision but that of 'Treaty Integration'. Going by that logic, it is a little surprising as to why would one even refer to Article 31 that deals with aids to 'Treaty interpretation'. A perusal of SC's observations at Para 86 of the judgment itself shows that SC considers 'treaty interpretation' and 'treaty integration' as two different terms. In our opinion, it may be possible to contend that Article 31 is relevant for 'treaty interpretation' and not for 'treaty integration'. The SC should consider this as an apparent factor that should make it consider the Review Petition.

3. Article 31(3)(b) – Meaning of 'Subsequent practices'

While emphasizing on the relevance of Article 31(3)(b) of Vienna Convention, SC has referred to the following while explaining the meaning of 'subsequent practices':

(a) International Law Commission ('ILC') Draft Conclusions
(b) International Court of Justice ('ICJ')'s acceptance of various activities of States
(c) Judgments given by ICJ
(d) Papers written by renowned experts

After considering all of the above, SC has held that the practices adopted by India follow a consistent pattern and hence, such practices get covered by 'subsequent practices' as is required under Article 31(3)(b) of Vienna Convention. SC has accordingly held that a notification under section 90 is mandatory to give effect to all types of MFN Clauses, as issuing a notification has remained a consistent practice of India [Para 87].

Our Analysis

There are certain interesting observations / references made by SC which could go in favor of the taxpayer/s:

(a) A 'subsequent practice' is defined as consisting of conduct in the application of a treaty, after its conclusion, ***which establishes the agreement of the parties regarding the interpretation of the treaty***. Such subsequent practice under Article 31 and 32 may consist of any conduct of a party in the application of a treaty, whether in the exercise of its executive, legislative, judicial or other functions and may take several forms. [Para 76]
(b) Put simply, practice covers ***'what states do in their relations with one another'. In a more dynamic sense, it represents the process of continuous interaction between States.*** [Para 76].
(c) A common understanding would be required, regarding the interpretation of a treaty ***which the parties are aware of and accept.*** [Para 78].
(d) The goal of treaty interpretation under VCLT is to determine the meaning of the treaty ***viewed from the perspective of the***

contemporary shared understanding of the parties to the treaties. [Para 80]

(e) ***Subsequent practice denotes the decisive consent of the parties***, and acts as a cogent, peremptory means of treaty interpretation [Para 80]

(f) The way in which a treaty is actually applied by the parties is usually a good indication of what they understand it to mean, ***provided the practice is consistent, and is common to, or accepted by, all the parties.*** [Para 81]

(g) ICJ's judgment in Case Concerning the Land, Island and Maritime Frontier Dispute (El Salvador v Honduras) has dealt with a case ***where all three parties to the Treaty acted in the same manner at multiple occasions.*** It was in that backdrop that ICJ considered and explained how practice of parties assumes significance in treaty interpretation. [Para 83]

As can be seen from the above, consistently, at multiple instances, the SC has highlighted the importance of *practices by multiple parties* to an agreement for them to be considered as relevant aid to treaty interpretation. However, it is very evident that in the case under consideration, none of the practices adopted by India are also the ones adopted by the other country to the DTAA. It is surprising that on one hand, SC has given importance to subsequent practices *accepted by all parties* (see point 'f' above), on the other hand, it has gone ahead to consider India's practice in isolation (based on constitutional differences) as right means for treaty interpretation (see Para 87 of the judgment)!

4. Silence on the part of one country amounts to acceptance of subsequent practice

At Para 77 & 78 of the judgment, the SC has considered silence or inactivity of one state as acceptance of the subsequent practice by the other state in order to hold that the notifications issued by India and not countered by the other countries amount to acceptance by the other countries.

Our Analysis

This may turn out to be an aspect that actually benefits the taxpayer/s on two counts:

(a) A similar argument (of silence amounting to acceptance) should equally apply from the perspective of the other countries. For instance, the Netherlands has already issued a Decree way back in 2012. However, there was no opposition by India on applicability of MFN Clause pursuant to the said Decree. In fact, as per CBDT Circular No. 3 of 2022, it appears that India has communicated its position to The Netherlands, France, and Switzerland against their respective Decrees. However, as is mentioned in the Circular, this difference of position is on the limited point of third state being a member of OECD at the time of signing of the treaty and not as to when the MFN clause is enforceable. Accordingly, one may argue that India has remained silent as regards the date from which the MFN is enforceable. Issue of Circular in 2022, i.e. years after occurrence of the 'future event' may show that India never acted upon the same earlier.

(b) On one hand, SC states that the practices of the Netherlands, France and Switzerland cannot be considered for evaluating the case, as treaty practice of these countries is dictated by conditions peculiar to their constitutional and legal regimes. On the other hand, SC tries to consider

SC Ruling - Main Observations & Our Analysis

Article 31(3)(b) to state that treaty practice of India (actually driven by its constitutional and legal regime) should be considered as 'subsequent practices' having been accepted by both the countries, that too on the assumption that other countries are silent and further, such silence amounts to acceptance! In our opinion, there could be two possibilities:

- SC should consider the practices of the three countries as their 'subsequent practices' to permit apple to apple comparison. If this is permitted, it would not result in acceptance of India's position as there is no consistency between the two countries.
- If the above is not acceptable, reference to Article 31(3)(b) could be considered as misplaced because these country-specific positions are governed by the Constitution of each of the countries and hence, rendering the comparison impossible.

Apparent reasons for review by SC – A Summary

Coverage

On perusal of the judgment, it appears that in concluding, SC has taken recourse to multiple factors, most of which may have possible counters as in, taxpayers may call the following as possible points that SC has apparently missed out to consider and which may have changed outcome of the judgment:

Sr. No.	Observation	Apparent reasons for review	Relevance of the reasons
1	A separate notification under section 90 is required for all types of MFN clauses	SC has not evaluated as to how an MFN Clause in isolation would require a separate notification	Extremely High
		Such an observation would render usage of different languages in different DTAAs useless	Extremely High
		A separate notification is not required for Type 3 (and possibly Type 2) MFN Clauses as the main agreement / protocol (already notified) itself affect the domestic law	Extremely High
		Requiring / delaying notification in case of Type 3 MFN Clauses could constitute breach of DTAA and International Law	Extremely High
		Entering into negotiations / communications (like Type 1 MFN Clauses) in Type 3 MFN Clauses could constitute breach of DTAA and International Law	Extremely High
2	India's Treaty Practices	India agreeing to different types of MFN Clause with different types of countries in itself throws light on 'India's practices'	High
		Not all of India's MFN are notified. This would also be in sync with the fact that Type 3 MFN Clauses are 'automatic' in nature	Medium
3	Vienna Convention on Law of Treaties	SC has not emphasized on the fact that Article 31(3) is to be read together with the context (i.e. text of the DTAA)	Extremely High
		Applicability of Article 31(3) is itself a question – Treaty Interpretation vs. Treaty Integration	High
		Subsequent Practices – SC has itself considered multiple situations that warrant actual practices by both the countries involved	Extremely High
		Silence amounts to subsequent practice – This observation can be relooked at on multiple counts viz. actual conduct (decrees) of the other countries or impossibility of comparison on account of different Constitutional procedures	Extremely High

Conclusion

Coverage

While delivering the judgment, SC has considered multiple theories / possibilities as enumerated below and that too on a cumulative basis, which a taxpayer may argue to be a little far-fetched:

1. Only an implied and subtle conclusion that, Section 90, not only deals with DTAA / Protocol but also with MFN Clause contained therein.
2. All types of MFN Clauses require a notification without differentiating between the nature and without properly applying the principle of Dualism.
3. Ignoring 'treaty practice' of other countries on the pretext of constitutional differences but still considering India's 'treaty practice' (wrongly concluded as driven by constitution) as relevant for Vienna Convention.
4. Assuming that other countries have remained silent – though the Netherlands follows Monism (as per Klaus Vogel – also considered by SC at Page 49 (Para 73) of the judgment) and therefore, its Decree cannot be considered as a practice driven by constitution, warranting importance in the context.
5. Not considering the fact that India never issued any Circular to the contrary even after 10 years and hence, India has remained silent in that sense.

From the above discussion, we believe that there is a good possibility of SC reviewing the judgment after considering that the current judgment has been rendered on the basis of quite a few aspects may require re-consideration, inter alia, the following:

1. With all due respect, considering 'future event' as the trigger event i.e. a new agreement / understanding warranting a notification under section 90, seems to be an apparent error. SC did not specifically deal with the aspect of 'point of time' when an MFN Clause alters the rights of citizens or modifies the law of the State, thereby mandating a notification under section 90.
2. Whether entering into discussions / negotiations with the other country for applying Type 3 MFN even when only Type 1 MFN allows for the same, would result in breach of International Law and disrespect of the DTAA? In our opinion, if the Government tried to enter into negotiations / discussions with the Netherlands, France or Switzerland, it could be a breach of International Law because DTAAs with these countries never require negotiations / discussions unlike erstwhile DTAA with Switzerland.
3. Understanding of the phrase "subsequent practices" could have been misplaced – practices governed by Constitution cannot be compared and if the same are to be compared, equal importance should be given to practices followed by other countries.

Conclusion

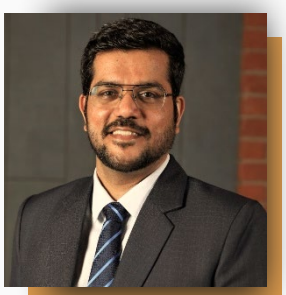
Coverage

Food for thought

Some of the Protocols to India's DTAAs contain provisions that allow India a possible additional taxing right (of course, subject to domestic tax law) on happening of a 'future event'. It would be interesting to see if the Revenue would restrict itself from invoking the said provisions pending a separate notification under section 90, if the SC decides not to overturn this decision!

Ironically, it appears that SC is largely driven by *'Advaitha'* (only India's perspective) to interpret and apply *'Dvaitha'*! Only time would tell if SC would review its decision but whatever be the result, the judgment has already changed the way tax enthusiasts interpret DTAA and understand the *'Dualism'* theory!

Should you need more information, kindly reach out to



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