

The image features a yellow background on the left side, transitioning into a white background with a fine grid pattern on the right. Several large, stylized arrows in shades of blue, red, and grey point from the left towards the right, following a curved path. The arrows vary in size and color, creating a sense of movement and direction.

# **Non-Discrimination under International Tax Law**

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# Non-Discrimination under ITL

## Introduction:

- Prof. Kees Van Raad - An incoherent collection of fairly narrow clauses
- Art. 24 deals only with direct and specific cases of non-discrimination although one may infer that it is very wide in its application due to its overriding nature over the scope of the DTAA
- Contextual application – Art. 24 does not override other articles of the DTAA (eg: Article 7(3) of certain DTAA – subject to limitation of taxation laws of the source state)
- Preferential treatment is not prohibited





# Non-Discrimination under ITL

## Introduction:

- No justification required for establishing discrimination
  - ND provisions have absolute character [M. No. 4 - Klaus Vogel]
  - Differentiation vs. discrimination [Daimler Chrysler India (P.) Ltd. [2009] 29 SOT 202 (PUNE)]. Reliance on Prof. Kees Van Raad book may be misplaced. There should be no need to establish ground for differentiation in treatment that it is unreasonable, arbitrary or irrelevant.
  - Grounds of justification prevalent under EU law: written grounds for justification, overriding reasons in public interest and proportionality test

# Non-Discrimination under ITL

## OECD / UN MC :

24(1)

- Nationality based ND

24(2)

- Stateless persons ND

24(3)

- PE ND

24(4)

- Debtor – Creditor ND

24(5)

- Ownership based ND





# Non-Discrimination under ITL

## Article 24(1) – OECD / UN MC:

**Nationals** of a Contracting State shall not be subjected in the other Contracting State to **any taxation** or **any requirement connected therewith**, which is **other** or **more burdensome** than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.



# Non-Discrimination under ITL

## Article 24(1) – OECD / UN MC:

- Historical background: to strengthen diplomatic protection to nationals wherever resident
- Definition of “national”:
  - Covers individuals and companies (OECD/UN MC Commentary)
  - Some DTAAAs define specifically whereas some do not
  - Companies and corporate bodies cannot be considered as nationals [Credit Lyonnais [2005] 94 ITD 401]; Chohung Bank [[2006] 102 ITD 45 (MUM)]; Advance Ruling Petition No. P-6 of 1995 [[1998] 100 TAXMAN 206 (AAR - N. DELHI)]
- Condition of reciprocity: Only in commentary (Para 5) but not in bare provisions. Equal commitment from both states [Article 60(1) VLCT]





# Non-Discrimination under ITL

## Article 24(1) – OECD / UN MC:

- Meaning of “same circumstances”: Substantially similar circumstances both in law and in fact
- Criteria for same circumstances: Residence and other relevant criteria which is the basis for tax differentiation
- Therefore circumstances should be the same and only nationality should differ in order to test discrimination under Art. 24(1)
- US Model Technical explanation as well as India-US DTAA Technical explanation: Comprehensive taxation not comparable with Limited liability taxation. Therefore US is not obliged to grant same taxing regime to Indian national (being non-US resident) vis-à-vis US national (being non-US resident) for US source income



# Non-Discrimination under ITL

## Article 24(1) – OECD / UN MC:

- “Taxation”: Basis of charge, computation & rate
- “Other requirement connected therewith”: Returns, payment of tax (including advance tax, TDS), prescribed forms, prescribed periods, etc
- “Other”: Taxation as well as other requirements connected therewith cannot deviate from those applicable to nationals even though they may not be burdensome for non-nationals
- “More burdensome”: Must not be more onerous
- Even though Art. 24(1) prohibits taxation or connected requirements which are different than those applicable to nationals, preferential treatment can be granted to non-nationals without violating Art. 24(1) – By virtue of Para 3 and 14 to Art 24 OECD MC Commentary [M. No. 32 Klaus Vogel]



# Non-Discrimination under ITL

## Example of “same circumstances” for individuals

UK  
National

UAE  
Resident

India  
Source of  
Income

v/s



India  
National

UAE  
Resident

India  
Source of  
Income

v/s



India  
National

OMAN  
Resident

India  
Source of  
Income



# Non-Discrimination under ITL

## Example of “same circumstances” for individuals:

- Same residence does not restrict the scope of Art. 24(1). In the above example, resident of UAE can also access UK-India DTAA
- In the comparison, the non-resident of India (viz. in law) has to be a resident of UAE (viz. in fact). Factual similarity required too in order to discourage use of tax havens (Para 8 of Commentary on Art. 24(1))





# Non-Discrimination under ITL

## Example of “same circumstances” for **companies**:

- Even for companies, discrimination based on nationality (registration/incorporation) is prohibited. (Example 1)
- In many cases, incorporation may be the sole criteria for ascertaining ‘nationality’ as well as ‘residence’ for company under domestic regulations. In such cases, Art. 24(1) may become redundant. (Example 2)

# Non-Discrimination under ITL

## Example 1

➔ Residence Criteria

➔ Company X  
(tie breaker test based on POEM)

State A

Incorporation or  
POEM

POEM  
↓  
(Resident)

State B

Incorporation

Incorporated  
↓  
(National)

State A (Domestic Law)

Company Incorporated in State A  $\xrightarrow{\text{Dividend}}$  Company Incorporated in State A

**Tax exempt for recipient**

Article 24(1) application ✓

Company Incorporated in State A  $\xrightarrow{\text{Dividend}}$  Company X

**Therefore, Tax exempt for Co. X**



# Non-Discrimination under ITL

## Example 2

➔ Residence Criteria

➔ Company X  
(tie breaker test based on incorporation)

State A

Incorporation

--

State B


Incorporation

Incorporated  
➔ (Resident & National)

State A (Domestic Law)

Company Incorporated in State A  $\xrightarrow{\text{Dividend}}$  Company Incorporated in State A

**Tax exempt for recipient**

Article 24(1) application 

Company Incorporated in State A  $\xrightarrow{\text{Dividend}}$  Company X

**Cannot be Tax exempt for Co. X**



# Non-Discrimination under ITL

## Relevant Indian judicial decisions under Article 24(1) – OECD / UN MC:

- Higher tax rate applicable to foreign companies: Chohung Bank [[2006] 102 ITD 45 (MUM)] and host of other decisions. DTAA does not override Finance Act
- ‘Same circumstances’:
  - Chohung Bank [[2006] 102 ITD 45 (MUM)]. Foreign banking company not comparable to Indian banking company. Are all those differentiations relevant for consideration per se under Art. 24(1) since tax rate not dependent upon such differentiations?
  - Same conditions not satisfied by foreign national, hence deduction under Sec. 80M not granted. [BNP Paribas SA [57 SOT 82]]
- Sec. 48 2<sup>nd</sup> Proviso: No discrimination based upon nationality but distinction based on residence. [Transworld Garnet Co. Ltd [2011] 333 ITR 1 (AAR)]





# Non-Discrimination under ITL

## Article 24(2) – OECD / UN MC:

Stateless persons who are residents of a Contracting State shall not be subjected in either Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of the State concerned in the same circumstances, in particular with respect to residence, are or may be subjected.

- Not present in most of the Indian DTAAAs



# Non-Discrimination under ITL

## Article 24(3) – OECD / UN MC:

The **taxation** on a **permanent establishment** which an enterprise of a Contracting State has in the other Contracting State **shall not be less favourably levied** in that other State than the taxation levied on enterprises of that other State **carrying on the same activities**. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.





# Non-Discrimination under ITL

## Article 24(3) – OECD / UN MC:

- “Taxation”: Other requirements not covered.
- “Shall not be less favourably levied”: The result solely counts. If tax levy (in monetary terms) is more burdensome, then covered under Art. 24(3). Otherwise, differential requirements that may be prescribed for PEs may be permitted
- “Same activities”:
  - Same sector of activities.
  - Same type of business (John Avery Jones).
  - Similar legal structure [Mashreqbank PSC [2007] 14 SOT 1 (MUM.)]
  - Regulated vs. unregulated activities



# Non-Discrimination under ITL

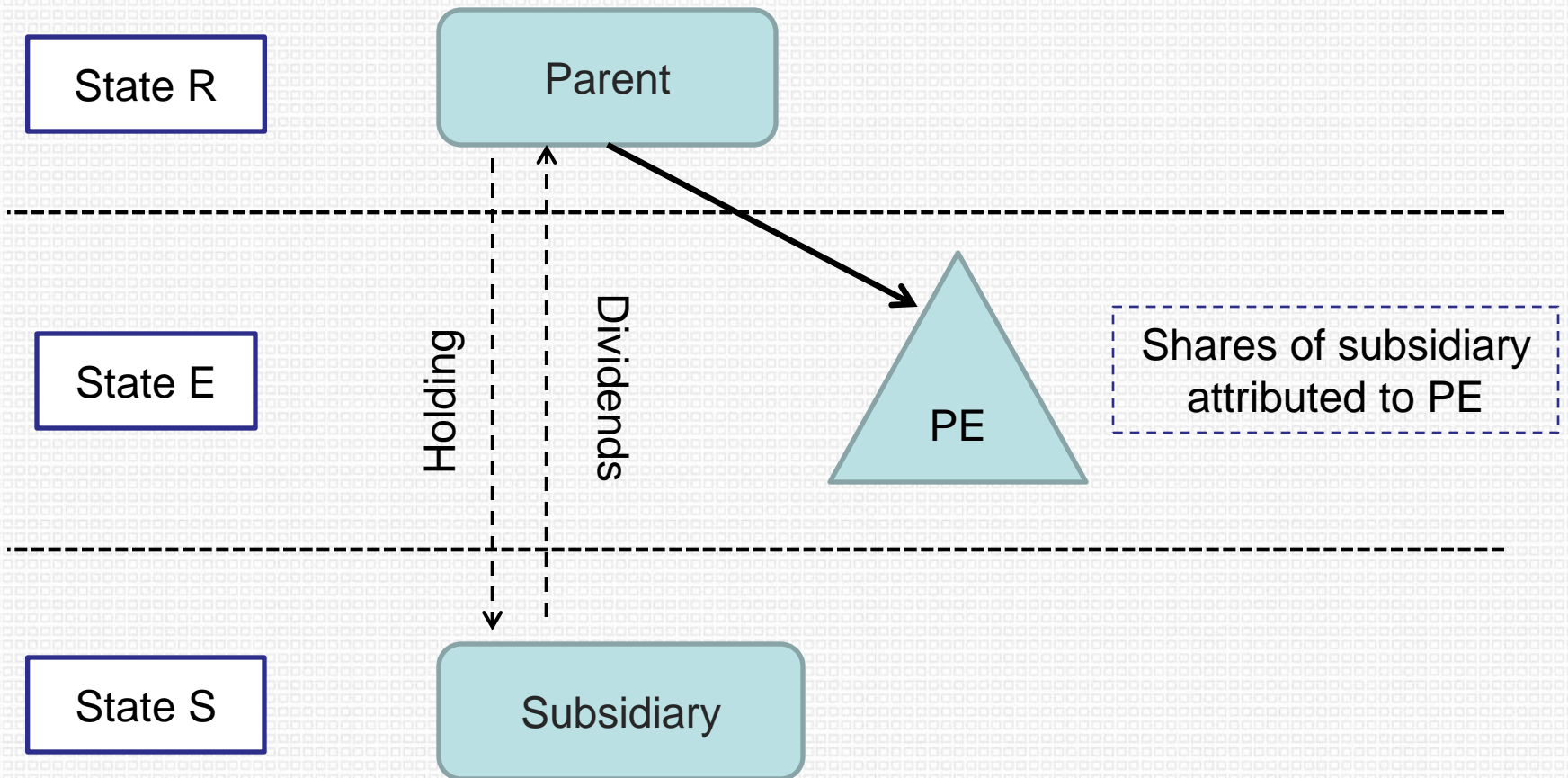
## Article 24(3) – OECD / UN MC:

- Consequence of application of Art. 24(3) - Equal treatment to PE for:
  - Deductions for expenses
  - Depreciation and provision for reserves
  - Loss c/f
  - CG computation
  - Tax incentives (See India position on commentary)
- Group taxation benefit not within scope of Art. 24(3)
- Transfer pricing not in conflict with this provision



# Non-Discrimination under ITL

## Participation exemption for holdings owned by PE





# Non-Discrimination under ITL

## Participation exemption for holdings owned by PE

- Arguments for extension:
  - Once profits are taxed at subsidiary level, they shouldn't be taxed once again
  - State R cannot be expected to exempt PE profits as well as grant underlying tax credit for taxes on profits of subsidiary or vice versa
- Arguments against extension:
  - Avoiding double taxation is responsibility of State R and not that of State E





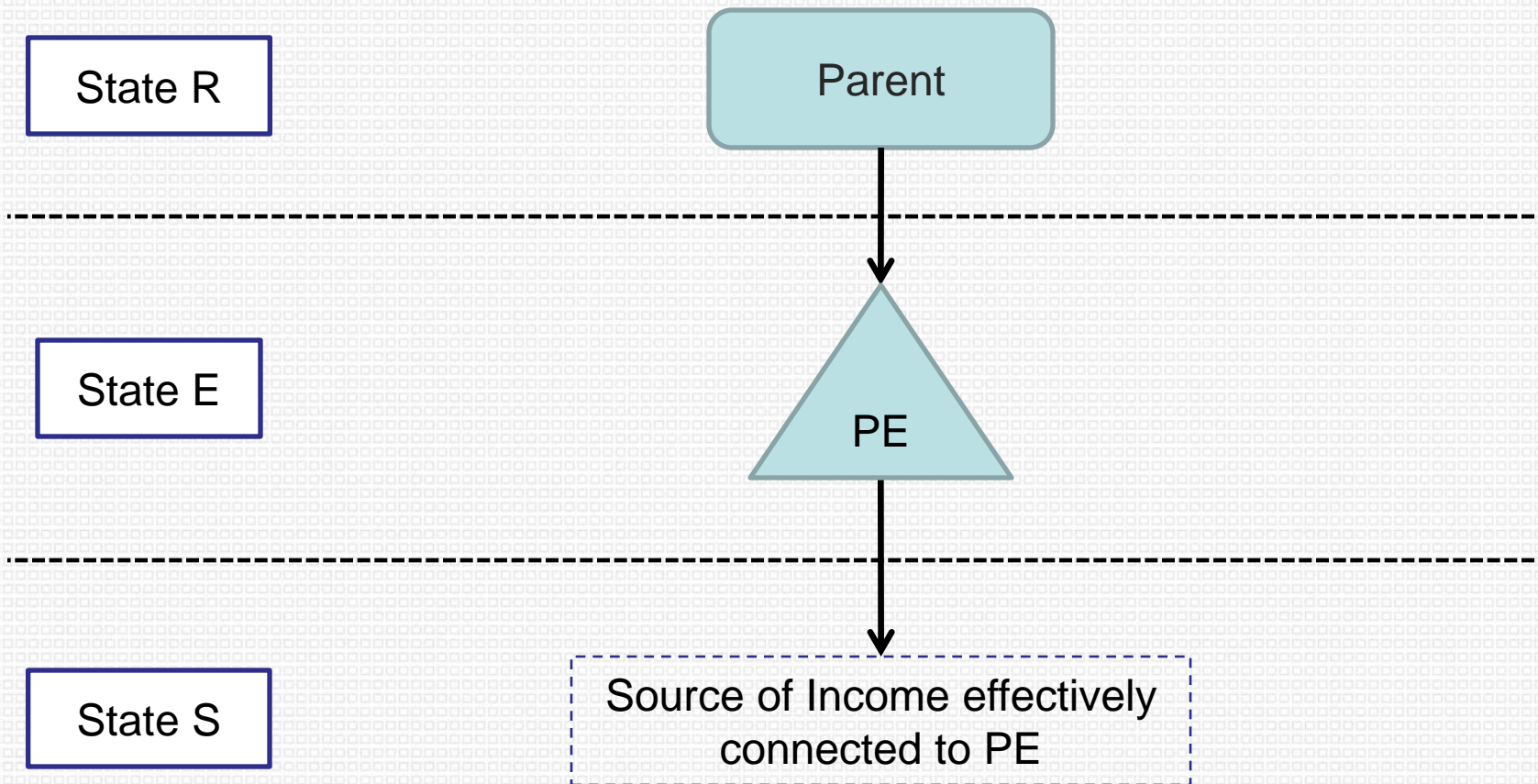
# Non-Discrimination under ITL

## Article 24(3) – OECD / UN MC:

- Progressive taxation
  - Profits of the whole company to be considered for determining slab rate applicable to PE profits
  - Losses to be ignored
  - Principle of equity?
- Compatibility of Branch Profits tax and Branch level interest tax
- WHT in case of payment by State E payer to PE located in State E: No discrimination if WHT applicable to payments to residents too (Para 64-65 to Art. 24(3) OECD MC Commentary). But is WHT a final tax?

# Non-Discrimination under ITL

## Triangular Situation







# Non-Discrimination under ITL

## Triangular situation:

- Three scenarios:
  - Domestic tax law of State E provides for credit to be granted to residents as well as PE of a non-resident: No need for application of ND provision
  - Domestic tax law of State E provides for credit to be granted to residents but not to PE of a non-resident: Application of ND provision and therefore credit granted to PE by State E
  - Credit is allowed to residents only under DTAA entered by State E: Can benefit of Art. 25 of E-S DTAA be applied to PE by virtue of ND provision under R-E DTAA? Only if such specific provision is contained under R-E DTAA to grant credit to PE of State S taxes for lower of taxes deducted as per R-S DTAA or E-S DTAA



# Non-Discrimination under ITL

## Relevant Indian judicial decisions under Article 24(3) – OECD / UN MC:

- 80HHC:
  - Allowed since carrying on same activities [Bhagwan Shivlani (53 SOT 233)].
  - 80HHC considered as personal deduction on account of civil status and therefore denied [Mustaq Ahmed (126 TTJ 523)]
- 80HHE: Allowed [Rajeev Gajwani (129 ITD 145)(Ahd SB)]
- 44C: Art. 24(3) takes precedence over Art. 7(3) and therefore 44C not applicable [Metchem Canada Inc. vs DCIT (2006) 99 TTJ 702 (ITAT Mumbai)]. Some treaties have exception for Art. 7(3) cases under Art. 24(3) provision itself but in any case, Art. 24(3) has to be read in context of Art. 7(3) and most Indian DTAAAs have wording under Art. 7(3) that subject it to limitations under domestic tax law for deductions (eg. 44C)





# Non-Discrimination under ITL

## Article 24(4) – OECD / UN MC:

Except where the provisions of paragraph 1 of Article 9, paragraph 6 of Article 11, or paragraph 4 of Article 12, apply, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of such enterprise, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State.

- This provision does not apply to mispricing
- In general, it applies even to trade payments



# Non-Discrimination under ITL

## Relevant Indian judicial decisions under Article 24(4) – OECD / UN MC:

- 40(a)(i): Herbalife [101 ITD 450] and host of other decisions restricting application of Sec. 40(a)(i) pre amendment by Finance Act 2003. Many decisions have indeed referred to provisions under DTAA corresponding to Art. 24(1) instead of Art. 24(4)
- 40(a)(ia) 2<sup>nd</sup> Proviso: Same conditions as mentioned in Proviso to Sec. 201(1) if satisfied by Non-resident, then 2<sup>nd</sup> Proviso to Sec. 40(a)(ia) to be read into Sec. 40(a)(i)
- 40(a)(ia): Can limit of non-deduction to 30% for payments to resident be considered as discriminatory?





# Non-Discrimination under ITL

## Article 24(5) – OECD / UN MC:

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

- Group taxation outside the scope since this provision is aimed at payer related ND and not beyond that
- Stringent TP documentation is permissible (Para 80 to Art 24(5) OECD MC Commentary). More burdensome requirement prohibited under Art. 24(5)?



# Non-Discrimination under ITL

## Relevant Indian judicial decisions under Article 24(5) – OECD / UN MC:

- Sec. 79: [Daimler Chrysler India (P.) Ltd. [2009] 29 SOT 202 (PUNE)]
  - Unless a company in which public is substantially interested, any change in shareholding beyond 51% would disentitle the company to carry forward and set-off the accumulated losses
  - Benefit granted when an Indian subsidiary has an Indian parent company whose shares are listed on any recognized stock exchange of its domicile country, i.e., India, but not granted when an Indian Subsidiary has a German parent company whose shares were listed in any stock exchange in its domiciled country, i.e., Germany
  - No rational basis for this differentiation in treatment
  - Therefore, Art. 24(5) overrides Sec. 79 in this case





# Non-Discrimination under ITL

## Article 24(6) – OECD / UN MC:

The provisions of this Article shall, notwithstanding the provisions of Article 2, apply to taxes of every kind and description.

- Therefore, ND provisions apply to all kinds of taxes such as indirect taxes as well as state level or municipal level taxes
- But many Indian DTAAs restrict the scope of taxation to taxes covered within Art. 2 of the convention



# Thank you



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