

NovioTax **Delhi High Court confirms 5% dividend WHT rate under India-Netherlands DTAA**

June 2021

This article is an update to our previous article, titled: *“Reduction of Dividend WHT (to 5%) under India-Netherlands DTAA as India abolishes DDT (from 1 April 2020)”*. With the abolition of the Indian Dividend Distribution Tax (“DDT”) and a return to the “shareholder based taxation system” for dividends paid by Indian companies with effect of 1 April 2020, the withholding tax (“WHT”) rates prescribed in respect of dividends in the Indian Double Taxation Avoidance Agreements (“DTAAs”) have become a popular topic for discussion.

With regard to the dividend WHT rate under the India-Netherlands DTAA, the Dutch perspective is clear because of a decree clarifying that the rate is 5% with effect from 21 July 2010 (i.e. the date on which Slovenia became a member country of the OECD, owing to the interplay of the “most favoured nation” (“MFN”) clause in the India-Netherlands DTAA and the India-Slovenia DTAA of 2005). However, there has been some ambiguity from the Indian perspective. Therefore, the recent Delhi High Court ruling confirming that the dividend WHT rate under India-Netherlands DTAA is 5% with effect from 21 July 2010, is of particular importance. This confirmation is relevant for dividends distributed after the abolition of the Indian DDT (i.e. on or after 1 April 2020).

Dividend WHT rate under the India-Netherlands DTAA

The text of the India-Netherlands DTAA prescribes that either country may levy 15% WHT on the gross amount of dividends flowing to the other country. However, in Protocol IV no. 2 of the DTAA, it has been agreed that, “if, after the signing 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 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”. (Such provisions in tax treaties are commonly referred to as “MFN clauses”).

Effect of the MFN clause in the India-Netherlands DTAA

Due to the aforementioned MFN clause in the India-Netherlands DTAA, lower dividend WHT rates (i.e. lower than 15%) prescribed under Indian DTAAs signed after the India-Netherlands DTAA, can be relied upon in order to reduce the dividend WHT rate applicable between India and the Netherlands.

Art. 10(2) of the India-Germany DTAA stipulates that India is (in principle) allowed to levy 10% of the gross amount of the dividends distributed to a German company. This rate is further reduced to 5% under Art. 10(2)(a) of the India-Slovenia DTAA of 2005 for companies that directly own at least 10% of the Indian company paying the dividends. It should however be noted that the reduction to 5% only applies as from 21 July 2010, when Slovenia signed an Accession Agreement with the OECD. It should also be noted that the interplay with the MLI (signed by both, India and Slovenia) may require Dutch holding companies to satisfy a minimum holding period of one year in order to avail the favourable dividend WHT rate provided under the India-Slovenia DTAA.

Delhi High Court ruling of 22 April 2021

The Delhi High Court (“HC”) ruling in the case of Concentrix Services Netherlands B.V. and Optum Global Solutions International B.V. (collectively referred to as “taxpayers”) sets aside the WHT certificates issued by the Indian tax authorities to the taxpayers in respect of dividend payments from their respective Indian subsidiaries prescribing a WHT rate of 10% and directs the Indian tax authorities to issue fresh WHT certificates prescribing a lower WHT rate of 5%.

Facts of the case: The taxpayers, which are Dutch parent companies of Indian subsidiaries, applied for lower withholding certificates seeking a 5% WHT rate on dividends payable by their respective Indian subsidiaries. In their applications, the taxpayers relied on the MFN clause in the India-Netherlands DTAA (in combination with the DTAAs entered into by India with

Slovenia (and also, Lithuania and Columbia)). These DTAA's provide for a beneficial withholding rate of 5% on dividend payments. The Indian tax authorities issued withholding certificates at the rate of 10% based on the WHT rate on dividends in other Indian treaties reasoning that, since Slovenia, Lithuania and Columbia were not OECD member countries when the India-Netherlands DTAA was signed, these DTAA's could not be relied upon to lower the dividend WHT rate in the India-Netherlands DTAA.

Reasoning of the HC: The HC observed that the MFN clause in the India-Netherlands DTAA, which is part of the protocol thereto, is an integral part of the DTAA and therefore, no separate notification is required to apply the MFN provisions. Further, the HC noted that the use of the word "is" in the sentence: "which is a member of the OECD", as stated in the MFN clause. The HC observed that it requires countries to be OECD members when the source taxation is triggered in India and not at the time when the India-Netherlands DTAA was signed. The HC also referred to the Dutch decree clarifying that the dividend WHT rate under the India-Netherlands DTAA is 5% with effect from 21 July 2010. In this context, the HC stated that, "the best interpretative tool that can be employed to glean the intent of the Contracting States in framing Protocol IV no.2 would be as to how the other contracting State (i.e., the Netherlands) has interpreted the provision". Accordingly, "for efficient and fair application of the India-Netherlands DTAA", the HC held that, "a common interpretation should be applied to ensure consistency and equal allocation of tax claims between the Contracting States". Lastly, the HC emphasized that, while interpreting international treaties including tax treaties, "the rules of interpretation that apply to domestic or municipal law need not be applied, for the reason that international treaties, conventions and tax treaties are negotiated by diplomats and not necessarily by men instructed in the law".

Key Takeaways

- With effect as from 1 April 2020, there has been some discussion in India in relation to the dividend provision and the MFN clause in the India-Netherlands DTAA. Recently, however, a Delhi High Court ruling confirmed that the dividend WHT rate under the India-Netherlands DTAA is 5% with effect from 21 July 2010. This confirmation is relevant for dividends distributed after the abolition of the Indian DDT (i.e. on or after 1 April 2020).
- Availing the lower WHT rate on dividends in accordance with the India-Netherlands DTAA is subject to the provision of the requisite documentation: TRC, Form 10F and a declaration of beneficial ownership. If the requisite documentation is not provided in time by the Dutch company, the Indian company distributing the dividend is obliged to withhold (effectively) 21-22% of the dividend paid out, in accordance with the domestic WHT rate on dividends.
- In such case, or if dividends have already been distributed after 1 April 2020 with a WHT deduction of anything in excess of 5%,¹ the Dutch shareholder could claim a refund within a period of three years after the expiration of the calendar year in which the tax has been levied.² The refund process may, however, take some time and is not guaranteed to yield the desired result.

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¹ For most Dutch companies, the dividends received (as well as capital gains realized) from Indian companies should be exempt from Corporate Income Tax in the Netherlands by virtue of the Participation Exemption (subject to satisfying the provisions thereof). In this respect, no credit is available for the 5% dividend WHT paid in India.

² It should, however, be noted that there is an Indian domestic tax-law limitation of one year from the end of the financial year for filing of the refund claim.