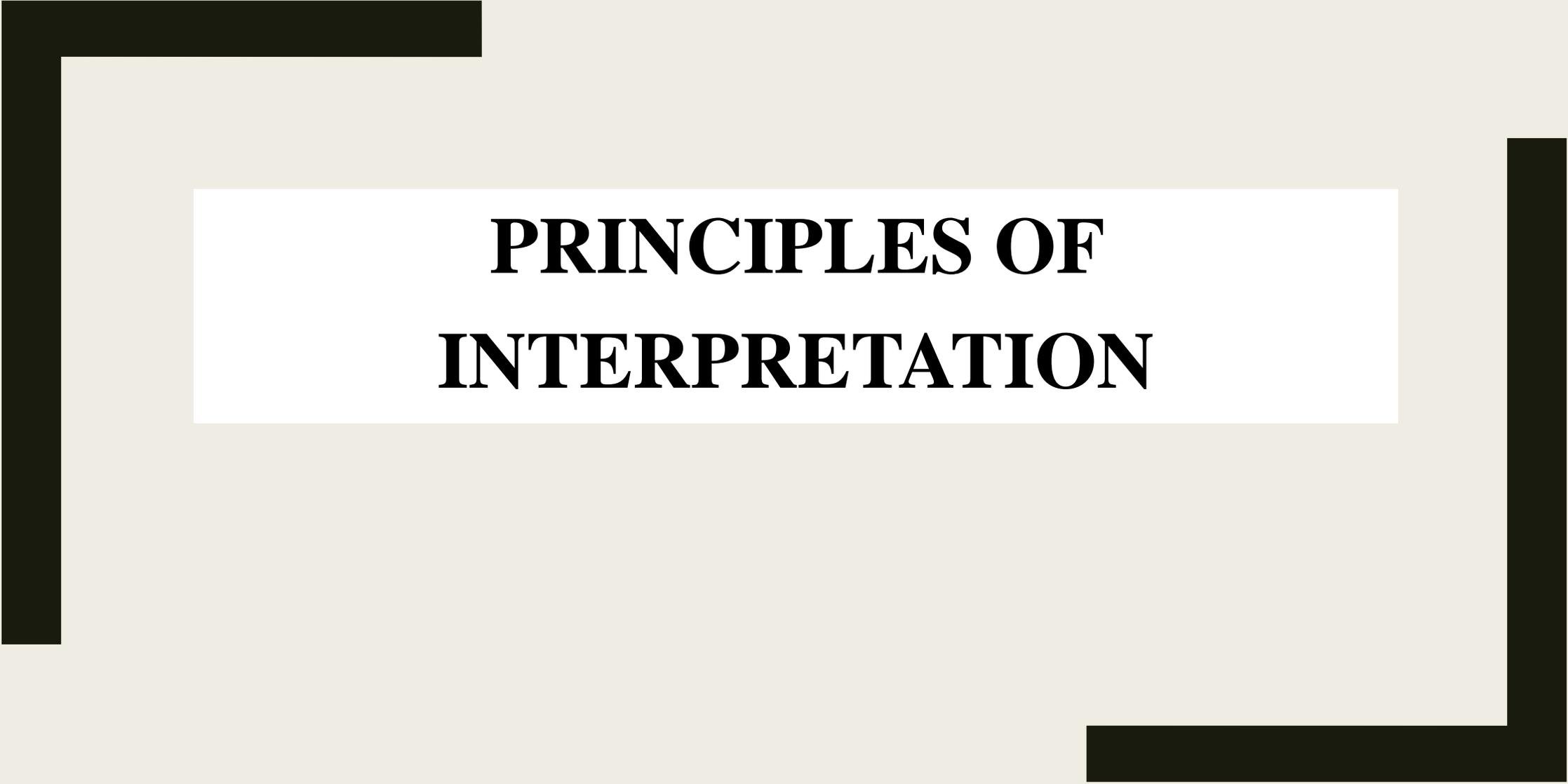


# INTERPRETATIONAL ISSUES IN TAX AND TREATY LAW

*NATIONAL SEMINAR FOR MEMBERS OF THE INCOME TAX APPELLATE  
TRIBUNAL*

Sonia Mathur, Senior Advocate



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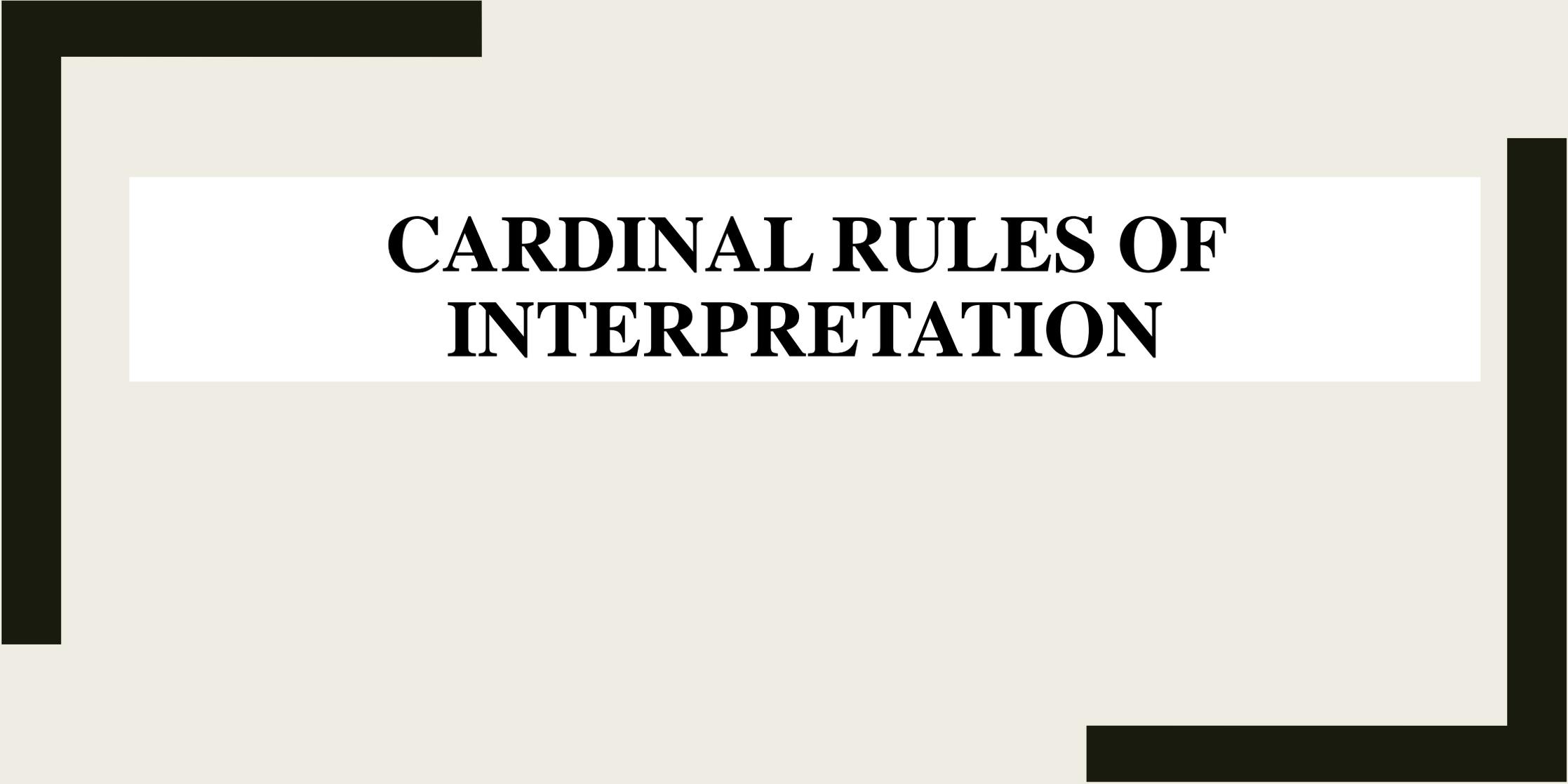
# **PRINCIPLES OF INTERPRETATION**

## *Cardinal Rules of Interpretation*

- Principle of Strict/ Literal Interpretation
- Doctrine of Purposive Construction (Golden Rule)
- Rule of Harmonious Construction
- Doctrine of “Reading Down”
- Rule of Beneficial Construction
- Mischief Rule
- Rule of “ejusdem generis”

## *Subsidiary Rules of Interpretation*

- Special Law overrides General Law
- Charging sections (Strict construction) versus Procedural sections (Liberal Construction)
- Statute must be read as a whole
- Conjunction and Disjunction
- Judgments of Foreign Courts –Only persuasive value
- Avoiding Substitution or Addition of words
- Creative Interpretation
- Prospective Applicability



# **CARDINAL RULES OF INTERPRETATION**

# Principle of Strict Construction

- Taxing statute is to be strictly construed.

- Lord Halsbury and Lord Simonds stated :

*"The subject is not to be taxed without clear words for that purpose; and also that every Act of Parliament must be read according to the natural construction of its words."*

*CIT vs. Calcutta Knitweaves (2014) 362 ITR 673 (SC)*

*"The Courts while interpreting the provisions of a fiscal statute, should neither add or subtract a word from the provisions."*

# Strict construction vs. Liberal construction

- The House of Lords observed as under:

*“In a Taxing Act one has to look merely at what is clearly said; there is no room for any intent; One can only look fairly at the language used”.*

*Top Ten Promotions (1969) 3 All E.R 39)*

- Charging Provisions: dealing with “levy” or “charge” to be strictly constructed.

*Gurusahai vs. CIT 48 ITR (SC)1*

- Remedial legislations, generally beneficent or social justice oriented, to be liberally constructed.

- “Exemption” or “relief” to be construed liberally.

- Machinery provisions to be liberally construed.

*CIT vs. Naga Hills 89 ITR 236*

- Statute granting incentives for promoting growth, development should be construed liberally.

- Generally, taxing statutes are to be interpreted strictly, wherever provisions are remedial or beneficent in nature they should receive a liberal construction .
- Penal provisions of the remedial statutes to be construed strictly.

*Balaji Tempo Ltd. 196 ITR (188) SC*

- The House of Lords, while interpreting a remedial statute, observed:

*“Wherever Legislature prescribes a duty and penalty for breach of it, it must be assumed that the duty is prescribed in the interest of the community or some part of it and the penalty is prescribed as a sanction for its performance”*

*London and North Eastern Railway Company vs. Berriman (1946) 1 All E.R 255*

# Doctrine of Purposive Construction (Golden Rule)

- The literal rule would gain precedence over the golden rule.
- The context, scheme of the relevant provision as a whole and its purpose are also relevant.
- The object has to be kept in mind for purposive construction.
- As per this doctrine, the transactions must be considered in the sense in which the Legislature intended it to be done.

- A construction which would defeat the very object of the legislature should be avoided.
- *Vikrant Tyres Ltd. vs. ITO (2001) 247 ITR 821,826(SC)*
- *Kehar Singh vs. State AIR 1988 SC 1883*, Court gave a go by to the golden rule and interpreted according to the grammatical and ordinary sense of the world.

# Rule of Harmonious Construction

- An interpretation which makes the enactment a consistent whole should be the aim of the Courts.
- The Courts should avoid “a head on clash” between the different parts of an enactment and conflict between the various provisions should be sought to be harmonized.

*Union of India vs. B.S. Aggarwal (AIR 1998 S.C. 1537)*

- It is a settled rule that an interpretation which results in hardship, injustice, inconvenience or anomaly should be avoided and that which supports the sense of justice should be adopted.
- The rule explained by the Supreme Court, “when there are, in an enactment two provisions which cannot be reconciled with each other, they should be so interpreted, that if possible, effect should be given to both”.

## Doctrine of “Reading Down”

Lord Reid in *Federal Steam Navigation Co. vs. Department of Trade and Industry* [1974] 2 All E.R. 97 at p.100, has stated thus:

*“ the judge may read in words he considers to be necessarily implied by words which are already in the statute and he has limited power to add to, alter or ignore statutory words in order to prevent a provision from being unintelligible, absurd or totally unreasonable, unworkable, or totally irreconcilable with the rest of the statute. ”*

The meaning and scope of the word 'reading down' and 'severance' dealt with in Australian Federal Constitutional Law by Colin Howard reads as follows:

*“ The High Court presumes the validity of the legislation to the extent that it will not of its own motion raise questions of constitutionality. Legislation is treated as valid unless the parties to litigation challenge it on constitutional grounds. The techniques of construction known as reading down and severance are corollaries to this presumption. Reading down puts into operation the principle that so far as its reasonably possible to do so, legislation should be construed as being within power.”*

# Rule of Beneficial Construction

- If interpretation of a fiscal statute is open to doubt and two views are reasonably possible:
  - a. *Most beneficial or favorable to the assessee should be adopted.*
  - b. *Even if it results in his obtaining a “double advantage”.*
  
- A beneficial legislation should receive liberal interpretation which would advance the purpose and object of the enactment.
  
- *CIT vs. Kullu Valley Transport Co. Ltd. (1970) 77 ITR 518 (SC)*
  
- *CIT vs. Behpur Sugar and Allied Industries (1983) 141 ITR 404 (Bom)*

*Oil and Natural Gas Corporation Ltd. vs. Sawpipes Ltd. (AIR 2003 S.C. 2629),*

- The phrase “Public Policy of India” in Section 34 of the Arbitration and Conciliation Act in issue, it was held that a wider meaning should be given to that expression to ensure that some of the provisions of the Act do not become nugatory. This is particularly so, since the expression connotes matters which concern public good and public interest.

*New India Assurance Co. Ltd. vs. C. Padma [(2003) 7 SCC 713]*

- In a case arising under the Motor Vehicles Act, the Court held that a beneficial legislation should be liberally construed so as to provide effective relief, untrammelled by technicalities .

# Mischief Rule of Interpretation (Heyden's Rule)

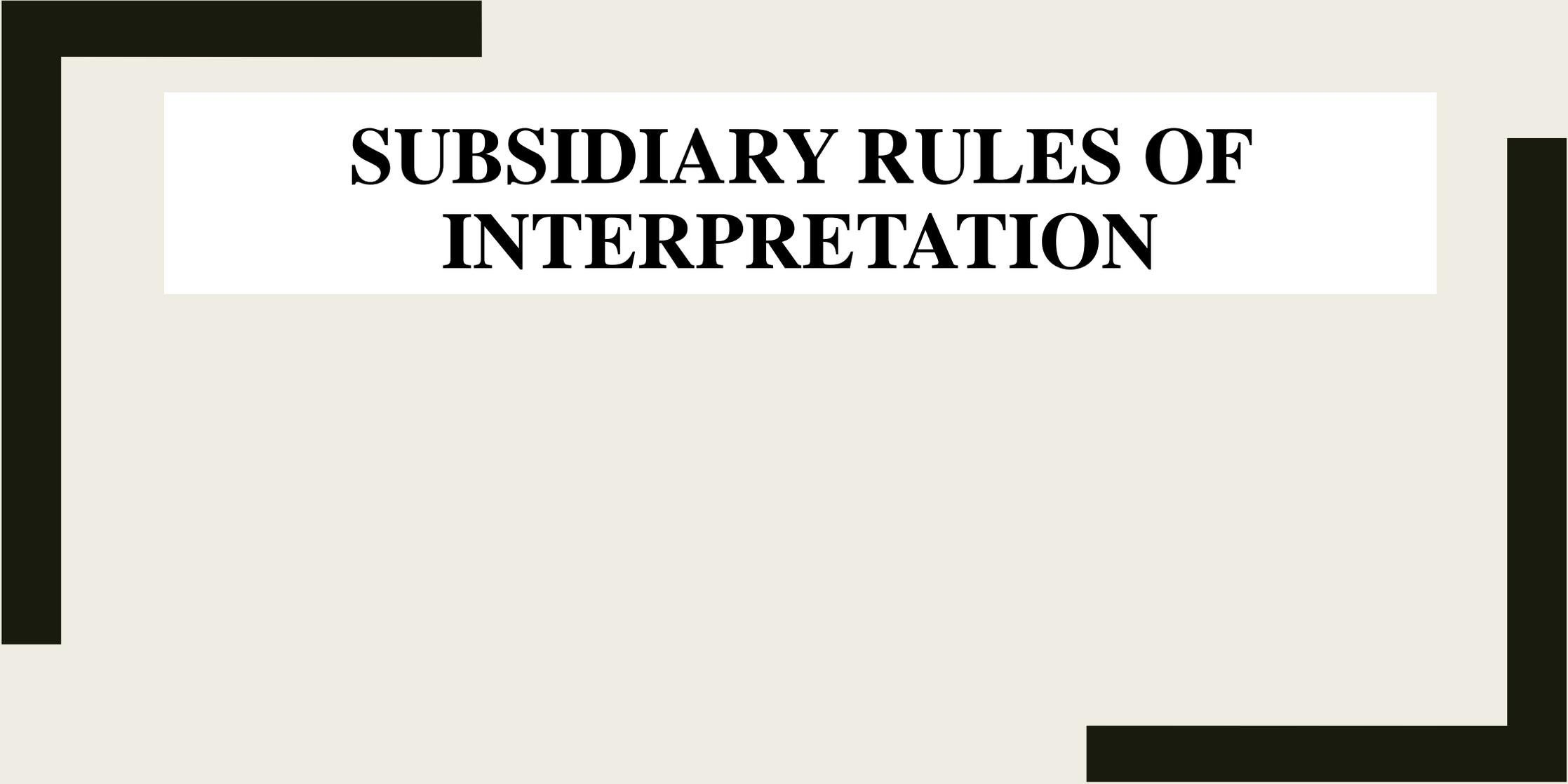
- A statute is to be construed so as to suppress the mischief in the law and advance the remedy.

*Heydon's case (1584) 3 Co. Rep. 7a* it was set out as under:

*“ Under this rule the judge will look at the Act to see what was its purpose and what mischief in common law it was designed to prevent ”*

- a. *What was the law prior to the enactment of the statute in question;*
- b. *What was the defect or mischief for which the earlier law did not provide;*
- c. *What remedy had the legislature intended to remedy the defect;*
- d. *The true legislative intent behind the remedy.*

**Reckitt Colman of India Ltd. vs. ACIT (2001) 252 ITR 550 (Cal)**



# **SUBSIDIARY RULES OF INTERPRETATION**

# Special law overrides General Law

- The literal meaning of the expression '*Generalia Specialibus Non Derogant*' is that general words or things do not derogate from the special.
- When there is a conflict between a general and special provision, the latter shall prevail.

*CIT v. Shahzada Nand and Sons 60 ITR 392 (SC)*

*UOI v. Indian Fisheries (P.) Ltd. AIR 1966 SC 35*

# Charging Provision and Machinery Provision

## ■ Charging Provision:( *Strict Construction*)

- Before taxing any person, it must be shown that he falls within the ambit of the charging section by clear words used in the section.
- No one can be taxed by implication.

*CWT vs. Ellis Bridge Gymkhana & Ors. (1998) 229 ITR 1*

## ■ Machinery Provision: ( *Liberal Construction*)

- Must be so construed as would effectuate the object and purpose of the statute and not defeat the same.

*Whitney vs. Commissioner of Inland Revenue (1926) AC 37,*

## Tax Statute to be read as a whole

Courts should adopt the interpretation which makes the statute workable, and reject a view which would render it unworkable and a futility

In *R.S. Raghunath vs. State of Karnataka AIR 1992 S.C.81*, Court quoted its earlier observations:

- *“The Court must ascertain the intention of the legislature by directing its attention not merely to the clauses to be construed but to the entire statute; it must compare the clause with the other parts of the law and the setting in which the clause to be interpreted occurs.”*

- Justice Holmes, said “*it is not an adequate discharge of duty for Courts to say, we see what you are driving at, but you have not said it, therefore we shall go on as before*”.
- *ITO vs. Damodarbhat (1969) 71 ITR 806 (SC)* where the Court rejected the contention which sought to nullify the provisions of section 297(2)(g) of the I.T. Act, 1961.

# Conjunction and Disjunction

- The word “or” is generally used disjunctively while “and” is used conjunctively.
- In certain situations however, these words may be interchanged.
- The Supreme Court considered this issue in the leading case of *Chamarbaugwala AIR 1957 S.C. 699*, with a view to give effect to the clear intention of the Legislature as evidenced from the statute as a whole.

# Doctrine of binding precedents

- A precedent is a judicial decision which contains in itself a principle. English Law is based on a doctrine called binding precedent.
- The fundamental principle on which the doctrine of precedent is based is known as stare decisis – let the decision stand

## *Expressio unius est exclusio alterius*

- The expression of the thing implies the exclusion of another.
- It conveys an important rule of interpretation to signify the circumstance where the express mention of one person or things in totality the exclusion of another.
- This maxim is valuable but it is definitely a dangerous master in the construction of statutes and documents.
- Collary to this maxim is *expressum facit cessare facitum* which states that when there is express mention of certain things, then anything not mentioned is excluded.

# Doctrine of Parimateria

*“ Statutes in parimateria are to be taken as one system to suppress the mischief. The two laws are only parts of the same provision.”*

- 1. Acts which have been given a collective title- Parliamentary recognition*
- 2. Acts which are required to be constructed as one- Parliamentary recognition*
- 3. Acts having short titles that are identical (apart from the calendar year)*
- 4. Other Acts which deal with the same subject matter on the same lines.*

# Avoiding Addition or Subtraction of words

*CIT vs. Calcutta Knitweaves (2014) 362 ITR 673 (SC)*

The Apex Court stated as under:

*“ The Courts, while interpreting the provisions of a fiscal legislation, should neither add nor subtract a word from the provisions.”*

# Casus Omissus

- Court only interprets the law and cannot legislate.
- A casus omissus should not be readily inferred and for the purpose all the parts of the statute or section must be construed together and every clause of a section should be construed with reference to the context and other clauses thereof so that the construction to be put on a particular provision makes a consistent enactment of the whole statute.
- It is not open to court to add something or read something in statute.  
*ACIT v. Velliappa Textiles Ltd. (2003) 263 ITR 550 (SC)*  
The duty of the Court is to decide what the law is and apply it, not to make.

# Retrospective, Prospective and Retroactive

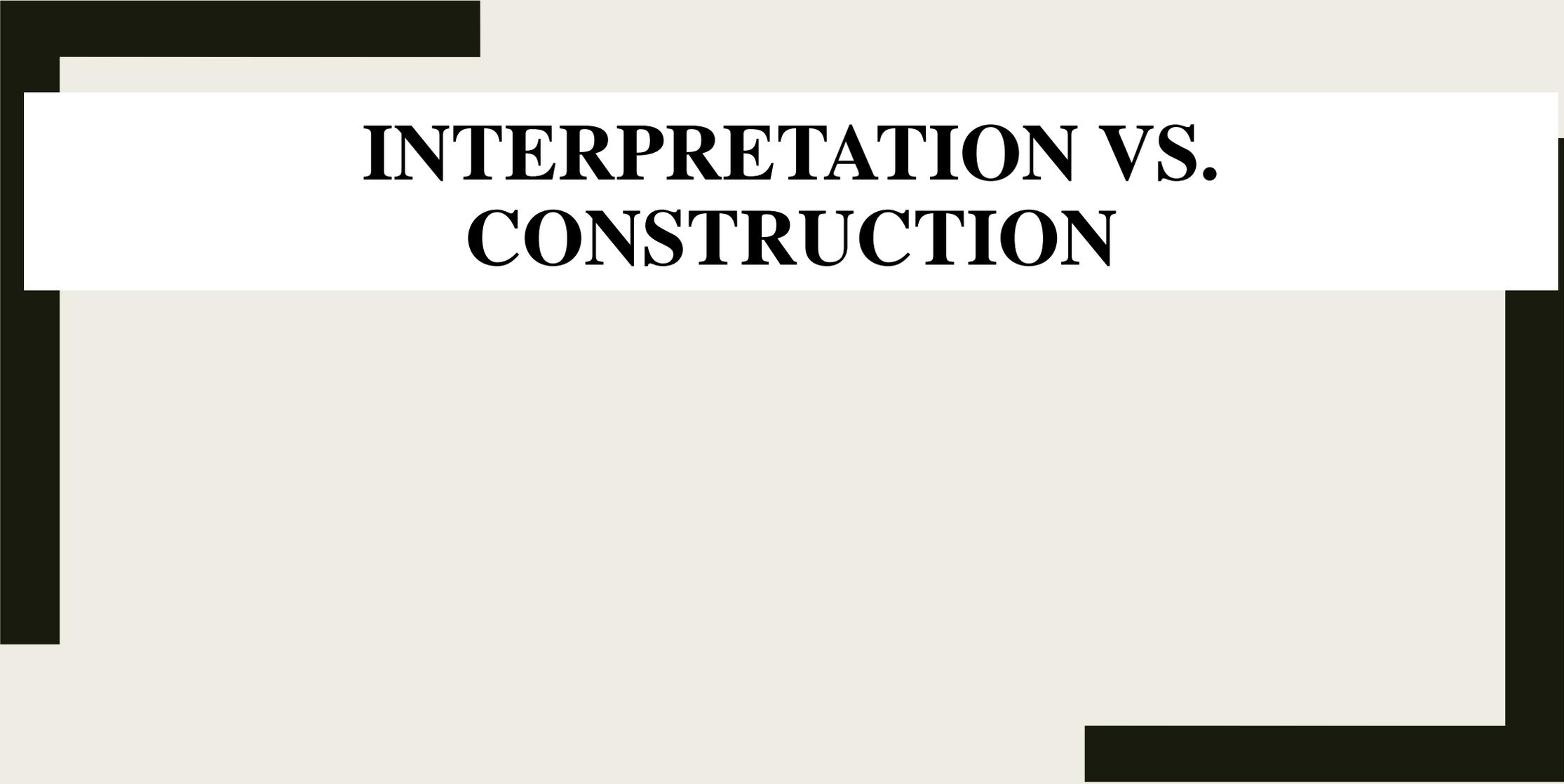
- The general rule:-
- “ *All statutes other than those which are merely declaratory or which relate only to matters of procedure or of evidence are prima facie prospective* ” and retrospective operation should not be given to a statute so as to effect, alter or destroy an existing right or create a new liability or obligation unless that effect cannot be avoided without doing violence to the language of the enactment.

*Hitendra Vishnu Thakur vs. State of Maharashtra AIR 1994 S.C. 2632,*  
Court held:

- i. A statute which affects substantive rights is presumed to be prospective in operation, unless made retrospective, either expressly or by necessary intendment, whereas a statute which merely affects procedure, unless such a construction is textually impossible is presumed to be retrospective in its application.*
- ii. Law relating to forum and limitation is procedural in nature, whereas law relating to right of action and right of appeal, even though remedial, is substantive in nature;*
- iii. Every litigant has a vested right in substantive law, but no such right exists in procedural law.*

- iv. *A procedural statute should not generally speaking be applied retrospectively, where the result would be to create new disabilities or obligations, or to impose new duties in respect of transactions already accomplished.*
- v. *A statute which not only changes the procedure but also creates new rights and liabilities shall be construed to be prospective in operation, unless otherwise provided, either expressly or by necessary implication.”*

■ This principle stands approved by the Constitution Bench in the case of *Shyam Sunder vs. Ram Kumar AIR 2001 S.C. 2472*

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# **INTERPRETATION VS. CONSTRUCTION**

- “Interpretation” is the art of finding out the true sense of any form or words, the sense which they are intended to convey.
- “Construction” is the drawing of the conclusions, respecting objects that lie beyond the direct expression of the text.  
“Construction” constitutes the conclusions which are in the spirit though not within the letter of the law.

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# TREATY LAW

# ADJUDICATING FORUMS

- High Court/Supreme Court
- Tribunal
- Mutual Agreement Procedure
- Advance Pricing Agreement
- Authority for Advance Ruling
- Settlement Commission
- Union Cabinet

# BASIC TREATY PRINCIPLES

- Treaty obligations to be fulfilled by the parties in good faith
- Provisions of its domestic law cannot be invoked as justification for its failure to meet treaty obligations.
- Interpretation of treaties in view of ordinary meaning of its terms, context and its object and purpose

# INTERPRETATION OF TREATIES VS. DOMESTIC LAW

*“Principles adopted in interpretation of Treaties are not the same as those in interpretation of Statutory Legislation ....Treaties are negotiated and entered into at a political level and have several considerations as their bases ....”*

- *Section 90 of the Income Tax Act*
- *Treaty interpretation should be holistic*
- *Indian Supreme Court Decision – Union of India vs. Azadi Bachao Andolan (2003)*

# VIENNA CONVENTION

- Rules embodied in Articles 31, 32 and 33 of the Convention are often referred to in interpretation of tax treaties.
- Some aspects of those Articles are good faith; objects and purpose and intent to enter into the treaty.
- Basic principles need to be kept in mind while construing DTAA.

# 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;*

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 its interpretation; ...”*

4) *“A special meaning shall be given to a term if it is established that the parties so intended”*

# ARTICLE 32

## ■ SUPPLEMENTARY MEANS OF INTERPRETATION

- Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:
  - A. leaves the meaning ambiguous or obscure; or
  - B. leads to a result which is manifestly absurd or unreasonable

# India

- **Courts** in India rely on foreign case laws from the Commonwealth countries and the United States and OECD Commentary
- Azadi Bachao Aandolan 263 ITR 706(SC)
- Vienna Convention - Article 31
- **C.I.T. vs. P.V.A.L. Lulandagan Chettiar (2004) 267- ITR-657 (SC) :**  
*“In the case of a conflict between the provisions of this Act and an Agreement for Avoidance of Double Taxation between the Government and a foreign State, the provisions of the Agreement would prevail over those of the Act.*

# Australia

- Holistic application of the general rules of interpretation under Article 31 of Vienna Convention
- Starting point is the text which receives priority in the interpretation process
- Context, object and purpose of treaty provision to be construed liberal manner
- Treaties often fail to exhibit precision of domestic legislation

# Germany

## ■ In re Partnership 10 ITLR 628

*A right to tax the interest in Germany could not be derived either from the terms of the protocol concluded at the time of conclusion of the double taxation convention, or by reference to the technical explanation to the convention issued by the US Treasury, or from the practice of the two revenue authorities in handling similar issues. The practice of the contracting states could not be employed as an aid to treaty interpretation in these circumstances under Article 31(3) of the Vienna Convention on the Law of Treaties*

## ■ United States of America

### ■ **Jamieson vs. Commissioner of Internal Revenue; 11 ITLR 40**

“Last in time” rule applies in US and where there is a later conflicting domestic law it would override the Tax Treaty

# Canada

- **Crown Forest Industries Ltd – Supreme Court (1995) 2SCR 802**

Paramount goal is to find meaning of the word in question looking to the language used and intention of parties

- **Her Majesty the Queen v. Melford Developments Inc., 1982 2 SCR 504**

There cannot be an implied override of a tax treaty

**THANK YOU!!!**