

# Dispute Resolution Hotline

February 13, 2010

## DOMESTIC HANGOVER: STATE GOVERNMENTS NEED NOT COMPLY WITH INTERNATIONAL TREATIES

In a land mark judgment, the Bombay High Court ("**Court**") has held that state governments are not required to comply with the understanding between nations under international treaties ("**Treaty/ Treaties**") -- unless the legislature enacts a law to reflect the principals agreed under such treaties.

This and such interesting interplay between international law and the domestic state legislature have been discussed in the present case of Karan Dileep Nevatia ("**Petitioner**") vs. The Union of India ("**UOI**") through the Commerce Secretary, Ministry of Commerce and Industry, The State of Maharashtra ("**GoM**") through Secretary, Home Department, The Commissioner of State Excise and The Collector of Mumbai (City) ("**Karan Dileep Case**")<sup>1</sup> discussed below.

**Facts:** The Petitioner is engaged in the import of foreign liquor/wines and distribution of the same in the GoM under FL-I Licence No. 113 granted to the Petitioner by the Collector of Mumbai city under the provisions of the Bombay Prohibition Act, 1949 ("**Act**"). The respondents are various government authorities in the GoM who, by way of various notifications ("**Notifications**")<sup>2</sup>, have either imposed heavy taxes in the form of 'Special Fees', 'Authorization Fees', 'Label Registration Fees' etc. ("**Duties**"), on foreign liquor in the GoM or have remitted the whole of excise duty leviable under the Act in respect of wine manufactured from the grapes produced within the GoM and thus offered favoured treatment in comparison with imported wines sold in Maharashtra.

**Dispute:** The Petitioner challenged the constitutional validity of the Notifications, which was alleged to have made a hostile discrimination between locally produced wines and imported wines. Domestic wine makers are not subject to the said Duties imposed by the impugned Notifications, and the Petitioner contended that such imposition of the Duties was arbitrary and unconstitutional.

The Petitioner drew reference to India being party to and ratifying various agreements under General Agreement on Tariffs and Trade ("**GATT Agreements**"). In the lights of the principles promoted by the GATT Agreements, in particular the principles of 'Most Favored Nation' and 'National Treatment' the Petitioner contended that the Notifications are *ultra vires* and unreasonable. Briefly, Most Favored Nation essentially means non-discrimination, where nations may not discriminate against the other members of the Treaty in the matters of applying the provisions of the Treaty. National Treatment implies that when a state provides certain privileges to its citizens, it also should provide similar rights and privileges to foreigners from the treaty countries, which also implies that the domestic duties, taxes and fees have to be levied at the same rates on the like products of both domestic as well as imported (from other countries) origin.

Before discussing the mail contentions, the Court, referring to Maganbhai Patel's case<sup>3</sup>, held that the Central Government was well within its powers to enter into treaties with foreign countries in respect of matters included in the State List.

**Contention 1:** Whether the impugned Notifications are in contravention of the GATT Agreements.

The Petitioner challenged the supremacy of the UOI and the GoM for issuing the Notifications which are in direct contravention to treaties entered into by the UOI. For this contention, the Court relied on the discussions in the Maganbhai Patel's case, where the Constitution Bench held that Treaties that affect private rights of the people must receive parliamentary assent through an enabling act of the Parliament. Consequently, to the extent that the provisions of the Treaties are not incorporated as the law of the land by the legislature, the agreements contained therein do not form part of the law of the land. In discussing this concept further, the Court held that the force of a Treaty, in principle, binds only the contracting nations and not their subjects. However, if Treaties contain provisions with regard to rights and duties of the subjects, courts, officials etc., of the contracting nations, these nations must take steps as are necessary according to their domestic municipal law, to make these provisions binding upon their citizens. In referring to a subsequent judgment<sup>4</sup>, the Court agreed with the contention that while the Parliament has a constitutional control over the executive, the creation of the obligations under the treaties is the function of the executive alone. Once the treaties are created, while they bind the nation as against the other contracting nations, the Parliament may refuse to bind the subjects of the nation by passing a law. The Court in the present case observed that the discussions above are valid even in the context of the Indian Constitutional set up.

Reference to Azadi Bachao Andholan<sup>5</sup>: The Petitioner sought to draw reference to the judgment of the Supreme Court in Azadi Bachao Andholan where the provisions of an international tax treaty are being adhered to by the various states within India. The Court in response, drew a comparison between the differences between the facts in Azadi Bachao Andholan and in the present case. In Azadi Bachao Andholan the Parliament itself enacted Section 90 of the Income Tax Act, 1961 ("**Section 90**"). Under the Section 90, the Central Government was empowered to enter

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into Treaties with foreign countries and to implement them by a Notification in the official gazette. Therefore, this case would in fact act an antithesis of the present case where express law is made by the Parliament under Article 253 of the Constitution of India ("Article 253")<sup>6</sup> to give effect to understanding under international treaties.

In the present case, the Court decided that the executive is competent to represent the state in all international matters. But, the obligations arising under the agreement or Treaties are not by their own force binding upon Indian nationals, and should expressly be made into the law of the land for the citizens to follow the same. If the rights of the citizens are not affected, no legislative measures are needed to give effect to the Treaty.

**Contention 2:** On the conflict between Treaty and domestic law.

The petitioner contended, relying on Kesoram's case<sup>7</sup>, that a court is required to interpret domestic laws in conformity with the provisions of international treaties. It was also held in the same case that international conventions and norms may also be applied under the Indian law "in the absence of enacted domestic law occupying the field".

The court placed reliance in ratio of the case of Tractoroexport Moscow<sup>8</sup> and other similar judgments<sup>9</sup>, where it was decided that if statutory acts are clear in meaning, they must be treated as the primary source of law and construed according to their meaning even though they are contrary to the understanding between nations. Therefore in light of the precedents, the court held that Notifications should prevail over the states obligations under the Treaties.

**Contention 3:** Whether the imposition of the Duties under the impugned Notifications is arbitrary and is not based on any valid classification between the domestic and imported wines.

In response to the above contention, the respondents stated that the classification of foreign wines as a distinct class for the purpose of taxation is not discriminatory as the state has a wide discretion in that behalf.

The Court relied various judgments presented by the respondents<sup>10</sup>. In particular, the Court drew reference to the Sony India<sup>11</sup> case where the Madras High Court was concerned with the question whether fixing of a higher rate of taxes on imported goods is violative of Article 14 of the Constitution of India ("Article 14")<sup>12</sup>. The Madras High Court in this case sought to differentiate between the concepts of class legislation (which has the effect of singling out certain persons within the same category for special benefits or burdens) and classification. While Article 14 of the Constitution forbids class legislation, it does not forbid reasonable classification.

Similar to the present case, it was argued before the Madras High Court that there cannot be differential classification with respect to imported and indigenous goods in the light of the agreements signed under GATT, the Madras High Court observed that the GATT does not curtail the Government's power to identify the imported goods as separate class and to levy higher rate of tax. Agreeing with the aforesaid judgment, the Court held that the judiciary is not expected to interfere with the discretion of the state unless a very strong case of hostile discrimination is made out and unless the taxing statute operates unequally within the range of its selection.

**- Yamini Dwarkanath & Shafaq Uraizee -Sapre**

1 MANU/MH/0001/2010

2 Notification (1) No. BWR.1105/CR-9/EXC-3 dated 31/3/2006 (2) No. MIS. 1107/CR-33(2)/EXC-3 dated 10/7/2007, (3) No. MIS. 1107/CR.33(1)/EXC-3 dated 12/11/2007, (4) No. MIS. 1107/CR-40/II/EXC-3 dated 28/8/2008, (5) No. BWR, 0509/IMP/CR-143/EXC-3 dated 22/7/2009 amending the Bombay Foreign Liquor and Rectified Spirit (Transport) Fee Rules, 1954 and (6) No. BWR.0509/IMP/CR-143/EXC-3 dated 22/7/2009 amending the Maharashtra Potable Liquor (Fixation of Maximum Retail Prices) Rules, 2009.

3 Maganbhai Ishwarbhai Patel v. Union of India and Anr. AIR 1969 SC 783

4 MANU/PR/0031/1937 : AIR 1937 PC 82

5 Azadi Bachao Andolan and Anr. AIR 2004 SC 1107

6 Article 253: Legislation for giving effect to international agreements: Under this Article the Parliament has power to make any law in India for implementing any international treaty or agreement.

7 State of West Bengal v. Kesoram Industries Limited and Ors., MANU/SC/0038/2004

8 V/O. Tractoroexport Moscow v. Tarapore & Co., Madras and Anr. MANU/SC/0003/1969 : AIR 1971 SC 1

9 Gramophone Company of India Limited v. Birendra Bahadur Pandey and Ors. MANU/SC/0187/1984; Kuldip Nayar v. Union of India and Ors. MANU/SC/3865/2006

10 Avinder Singh v. State of Punjab and Anr. MANU/SC/0299/1978 : AIR 1979 SC 321; A. Venugopal and Ors. v. State of Tamil Nadu and Ors. AIR 1999 Mad 431; Soni India Limited v. The Commercial Tax Officer, The State of Tamil Nadu MANU/TN/9256/2007 : (2007) 5 MLJ 881.

11 Soni India Limited v. The Commercial Tax Officer, The State of Tamil Nadu MANU/TN/9256/2007

12 Article 14 speaks about Equality before law.- The State shall not deny to any person equality before the law or the equal protection of the laws within the territory of India.

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