PHD CHAMBER
PROGRESS HARMONY DEVELOPMENT
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***Suggestions on***

## General Anti Avoidance Rules (GAAR)

1. GAAR provisions and Government's GAAR policy is to be seen in context of the stated tax policies of the Government. The Government has clearly stated that it would encourage a non adversarial tax regime along with a clear, stable tax policy to prevent hardships and prevent protracted litigation.

2. For clear stable tax policy to take effect so as to reduce litigation and encourage promotion of India as a business destination or to promote 'Make in India' the tax policy or GAAR policy needs to be objective not subjective and discretion of administrating officers needs to be reasonably curtailed.

3. Dissemination of information and learning amongst all stake holders is material to ensure better understanding of the provisions and so that the provisions are correctly applied. The risk of litigation needs to be reduced. Clarificatory examples & circulars and training of officers will help in better understanding and implementation of the provisions.

4. Some of the GAAR provisions as they stand are subjective discretionary, capable of differences in interpretation which would lead to litigation and hardship. The provisions need to be seen and modified in this respect.

5. Keeping in view the above, a reasonable lead time is required, pursuant to the modification of provisions that may be made, for creating learning amongst all stake holders regarding the provisions. This will promote tax payers compliance and help tax administrators to correctly apply the provisions. As such GAAR provisions need to be postponed for another year before they take effect. GAAR should take effect from Assessment Year 2017-18 rather than Financial Year commencing 1st April, 2015, which would commence shortly.

***Contributed by Mr. Anil K Chopra***
***Dewan P N Chopra & Co.***

6. The tax officers must be accountable. This would help in ensuring proper objective application of the provisions and prevent grievances. It is a settled law that tax officers should not make additions/disallowances based on suspicion, conjectures and surmises. This needs to be ensured in the course of application of GAAR.

7. GAAR provisions must be used fairly in limited number of befitting cases as excessive use would be counterproductive for the nation.

8. There should be no misconception about revenue generation through GAAR. It is not intended to bring an end to tax planning which is within the law. It will not provide a major tax windfall. There is also other anti abuse legislation in place, be it SAAR, Transfer Pricing and other developments such as BEPS. Work would need to be continued with OECD and others to develop anti abuse legislation and processes. GAAR does however serve as a strong deterrent. It must deter abusive tax planning. It however need not deter bona fide businesses and investments. GAAR must be seen as having effect on only limited types of transactions. GAAR must not result in belt and braces approach by which excessive regulatory provisions are laid down. Good governance is always appreciated and the same would be required in application of GAAR provisions.

9. Checks and balances put in place would need to protect both the revenue and tax payer.

10. GAAR should achieve its objective without frequent judicial interpretation.

11. While reviewing the GAAR provisions and implementing the same, the difference between lawful tax mitigation and artificial abusive and contrived arrangement should be appreciated keeping in view the well known judgments and commentary. The views must be based on the totality of the facts and circumstances as a whole and has to be seen from the eyes of a businessman.

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***Dewan P N Chopra & Co.***

12. In 34 ITR 888 (SC) in the case of Jiyajeerao Cotton Mills Ltd. v. CIT, it was observed "Every person is entitled so to arrange his affairs as to avoid taxation but the arrangement must be real and genuine and not a sham or make believe."

13. In Azadi Bachao Andolan, the Hon'ble Apex Court held if the Court finds that notwithstanding a series of legal steps taken by an assessee, the intended legal results have not been achieved, the Court might be justified in overlooking the intermediate steps, but it would not be possible for the Court to treat the intervening steps as non est based on some hypothetical assessment of real motive of the assessee. In our view, the Court must deal with what is tangible in an objective manner and cannot afford to chase a will-o'-the-wisp.

14. The United Nations Commentary on UN Model Double Taxation Convention between Developed and Developing Countries (2012 edn.) states that whether a main purpose for entering into transactions or arrangements is to obtain tax advantages should be based on an objective determination, based on all the relevant facts and circumstances, of whether, without these tax advantages, a reasonable taxpayer would have entered into the same transactions or arrangements.

15. In McDowell & Co. it was held that "Tax planning may be legitimate, provided it is within the framework of law. Colourable devices cannot be part of tax planning. It is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges." The term 'colourable' refers to the lack of bona fides.

16. Substance over form or piercing the corporate veil can only be done after the facts and circumstances of a transaction show that it is sham for tax avoidance.

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***Dewan P N Chopra & Co.***

17. The overall philosophy of administering GAAR should result in making the law fair, non discriminatory and non adversarial. Some important recommendation of Shome Committee which have not currently been brought on the statute need reconsideration, such as

- A clear demarcation should be drawn between business transactions undertaken for tax mitigation (which is to be allowed) versus tax avoidance (where the business case has to be strongly established to avoid the application of GAAR);
- A negative list of transactions where GAAR would not be invoked based on tax mitigation, should be drawn up;
- GAAR should not be applied for intra-group transactions (since this involves only transfer of assets / liabilities between group companies with no net increase in aggregate income / wealth);
- Only abusive, contrived and artificial arrangement should be subjected to GAAR.

18. Disputes should be avoided through provisions and related circulars as to which business transactions constitute tax mitigation and which transactions constitute tax avoidance. For instance, there is difference in this matter between views of CBDT Committee and Shome Committee in aspects such as under which were considered to be tax mitigation by Shome Committee and not so by CBDT Committee:
    - Payment of interest Vs dividend (CBDT Committee regarded as tax avoidance in case of interest to related parties).
    - Distribution of profits through dividend Vs buy back of shares.
    - Non-payment dividend to the Indian holding company.

19. GAAR should not be invoked where SAAR is applicable. This will lead to double taxation and hardship. The rules are silent. Section 100 says that GAAR provisions will apply in addition to any other provisions for determining tax liability of any arrangement. GAAR has potential to serve as hunting ground for SAAR and it may well be used for the same to avoid abuse of the Act.

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***Dewan P N Chopra & Co.***

20. Regarding grand fathering of investments made in a period prior to GAAR i.e. before 30.08.2010, the same should not be only on income from subsequent transfer of investments made before GAAR but the grand fathering should be applicable also on any income from such investments. Rather the grandfathering should be in respect of all income pertaining to structures and arrangements accepted by the Tax Department before 30.08.2010.

21. GAAR provisions should not override Double Tax Treaties. This needs urgent attention in equity and fair play and to avoid the negativity which flows from retrospectivity of provisions. Overriding of the DTAs through GAAR is akin to unilateral modification of treaty provisions and takes away also from certainty and India's competitiveness in the global investment place. If it is believed that a DTA permits abuse of anti avoidance provisions, the Treaty may be revisited, but GAAR should not override the Treaty.

22. The monetary threshold limit of Rs. 3 crores in any assessment year needs to be much increased keeping in view the complexity of GAAR and its scope as also keeping in view the cost of processes related to GAAR. The threshold limit for domestic transfer pricing is Rs. 5 crores. In context of GAAR, the monetary threshold limit should be atleast Rs. 10 crores.

23. Detailed extensive negative list should be specified including such as laid down in Shome Committee's Report. Instances of such negative list as laid down in Shome Committee Report are as under:

    i) Selection of one of the options offered in law. For instance:

        a) Payment of dividend or buy back of shares by a company.

        b) Setting up of branch or subsidiary.

        c) Setting up of a unit in SEZ or any other place

        d) Funding through debt or equity

        e) Purchase of lease of a capital asset.

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***Dewan P N Chopra & Co.***

ii) Timing of transaction, for instance, sale of property in loss while having profit in other transactions.

iii) Amalgamations and demergers (as defined in the Act) as approved by the High Court.

24. Tax Audit Report - Tax Audit Report should be modified to include details of any arrangement which has a tax benefit above threshold limit which the tax auditor feels may be held to be an impermissible avoidance arrangement.
The Tax Audit particulars in Form 3CD under rule 6G, have not been amended till date to capture this requirement.

25. GAAR should not be applied at a preliminary stage in the case of an application u/s 195(2) or 197 if the payer submits an undertaking to pay the tax and interest during the assessment stage if it is found that GAAR provisions are applicable.

26. Presently IAA is triggered if main purpose of any arrangement or step is to get tax benefit. 'Main Purpose' should be replaced by 'Sole Purpose' or predominant purpose of the arrangement for obtaining tax benefit.

27. Definition of IAA to be made more specific. It should have exclusions such as where main purpose is based on commercial substance or where there are bona fide arm's length transactions. It needs to be clarified that lawful tax mitigation is permissible.

28. AAR ruling should be binding on approving panel. This needs to be spelt out. GAAR Rules and clarificatory material should be clearly stated to reduce the need for advance ruling by AAR. Section 245S should specifically include the binding effect of advance ruling u/s 245R on the approving panel.

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***Dewan P N Chopra & Co.***

29. Approving panel must act as a just, fair body and must not become as if it was an administrative approving authority. There are public disappointments voiced regarding dispute resolution panel which has not met its objectives.

30. Some interesting examples where there may be open issues and where GAAR may be invoked unwarrantedly are as under. The Tax Authorities can in such cases allege main purpose to be tax benefit.
    - EPC contracts which are generally split into offshore and onshore
    - Conversion of company into LLP
    - Royalty payments made to an IPR company located in treaty friendly jurisdiction
    - Purchase of assets for availing depreciation claim
    - Lease of assets with option to purchase
    - Would DTA benefits of the parent be available for a transaction if an intermediary is disregarded?
    - How is main purpose to be computed? How does one compute commercial benefit for comparing with tax benefit even in bona fide business transactions?

31. There are some interesting safeguards in South African GAAR which may be considered for Indian GAAR:

    - The South African revenue authorities differentiate between legitimate 'tax planning' at one end of the scale and 'tax evasion' (equated with fraud) at the other.
    - South African GAAR is applicable only where the SOLE or MAIN purpose of an arrangement is to obtain a tax benefit;

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- The word ‘mainly’ to be construed as under in the South African GAAR:
    - A purely quantitative measure of more than 50%
    - As conveying the idea of dominant; or
    - More than anything else, for the most
- New GAAR provisions to apply to only those arrangement which have been entered into post notification the new provisions
- Exclusions from considering a party as accommodating party prescribed
    - Parties subject to comparable foreign income tax
    - Parties engaged in active trading activity
- The South African Revenue Services have also published a draft comprehensive guide to GAAR which provides for guidance on the Revenue Authorities interpretation and application of GAAR.

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***Contributed by Mr. Anil K Chopra***
***Dewan P N Chopra & Co.***