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91st Year

ज्ञानं परमं बलम्

A Monthly Journal of

The Chamber of Tax Consultants

Vol. VI | No. 1 October 2017

THE CHAMBER'S JOURNAL

YOUR MONTHLY COMPANION ON TAX & ALLIED SUBJECTS

Judicial precedents under Income-tax Act on Anti-Avoidance Rules

SAAR versus GAAR Hierarchy

Guidelines and Rules under GAAR

GAAR and DTA

Exemption from GAAR

Corporate restructuring Mergers, Demergers, etc.–GAAR implications

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THE CHAMBER OF TAX CONSULTANTS
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The Chamber's Journal

***READER'S SUGGESTIONS AND VIEWS**: We invite the suggestions and views from readers for improvement of The Chamber's Journal. Kindly send your suggestions on office@ctconline.org.*

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Editorial

Friends, for an optimist like me there are no mistakes, only lessons. Growth is a process of trial and error. Trial and error is a fundamental method of problem solving. This term was devised by C. Lloyd Morgan who was a British ethologist and psychologist. Trial and error is also a heuristic method of problem solving. In field of computer science, the method is called generate and test. There is specific reason why I am referring to 'trial and error' method. When the Hon'ble Prime Minister, while addressing C. S. on the Golden Jubilee celebration of ICSI, stated that GST (as per the Hon'ble PM, good and simple tax) implementation is being reviewed three months into its implementation, is an indication that the policy makers are adopting 'trial & error method' in the implementation of GST. In this age of technology if the Government resorts to such primitive methods of problem solving, then it doesn't reflect positively on the image of this Government.

The GST Council met on 6th Oct., 2017 after its last meeting in the month of July, 2017. In this meeting certain important decisions have been taken. The same are under:

1. Aggregate turnover for composition scheme from ₹ 75 lakhs to ₹ 1 crore (₹ 50 to ₹ 75 lakhs for special categories States for other than Jammu & Kashmir and Uttarakhand).

2. The facility for availing the composition scheme as above is made available to all up to 31st March, 2018.

3. Compulsory registration for Inter-State tax has been mellowed down granting exemption to service provider whose aggregate turnover is less than ₹ 20 lakhs (₹ 10 lakhs in special categories).

4. Enterprise having aggregate turnover less than ₹ 1.5 crore granted relief by allowing them to pay tax and file return on quarterly basis starting from this quarter October to December.

5. The Reverse Charge mechanism has been temporarily suspended till 31st March, 2018.

6. No tax on advance received for enterprise having aggregate turnover of ₹ 1.5 crore.

7. Service provided by GTA to unregistered person is exempt from GST.

8. E-way bill / TDS/TCS provisions are suspended temporarily till 31st August, 2017.

9. Due date for filing return composition by dealer extended to 15th November, 2017.

The Government has declared that the announcement of the above measures is an onset of early celebration of Deepawali. A keen analysis of these announcements shows that this kind of celebrations could have been there had the policy makers considered the representations made by professional bodies. It may not be out of place to point out that the States had been for years adopting the procedure of monthly returns for high turnover dealers, quarterly and six monthly returns for low tax paying small and medium enterprises. Almost all the States had a turnover limit of ₹ 1 crore and above for composition. It was vehemently represented to increase the composition turnover to ₹ 1 crore even before the implementation of the GST. But they, the executives refused to budge. It was also brought to the notice of the authorities that compulsory registration for inter-State taxable supply would be a huge compliance burden on small and medium enterprises but the arrogance of the executives failed to see the reason at that time. Similarly TDS/TCS and E-way bill were accepted to be a compliance burden, a hindrance to smooth flow of business across country and were therefore rightly deferred.

We expect the Hon'ble Prime Minister to take these lapses seriously as the hardships faced by the small and medium size concerns was avoidable and act against the officers who had not acted diligently in allowing the Government to take such policy decisions in spite of the representations made by the professionals.

The general Anti Avoidance Rules have come into force from 1-4-2017. The Journal Committee has decided to dedicate the Special Story of October month to GAAR. I thank all the eminent professionals for contributing to this issue of the Chamber's Journal. I thank my dear friend Vikram Mehta helping with the inputs regarding GST.

K. GOPAL
Editor

From the President

Namaskaar,

Dear Members and Readers, Wish all of you a Happy Deepawali and Happy New Year. This is the time to build a good bond with your family and friends which can keep you motivated to achieve greater personal goals.

The Goods and Services Tax (GST) Council on 6th October, 2017, finalised a slew of relaxation measures bringing significant relief to professionals, small and medium businesses and exporters. It also lowered GST rates for 27 items. The move, which comes nearly 100 days after the indirect tax levy was rolled out on July 1, was in response to representations from all over India Inc due to difficulties faced in filing returns and securing refunds. These measures are understood to have been discussed to boost industry after economic growth hit a three-year low in the first quarter. Hope the Government will henceforth take into consideration the practical difficulties and not thrust a new legislation unless it is well equipped for the same, where people are willing to pay the taxes but the procedural compliance is taking the toll. It would have been better if GST would have come in a phased wise manner allowing regulators, professionals and businessmen to accept it. This transition to new regime should have been gradual and voluntary.

Another historic move to ensure transparency in judicial appointments, the Supreme Court Collegium, led by Hon'ble Chief Justice of India Shri Dipak Misra, have resolved to post on the court's website its recommendations on judicial appointments, transfers and elevations for public consumption. This information posted online will also "indicate" reasons for the recommendation or rejection of a name for judicial appointment, transfer and elevation to High Courts and the Supreme Court, the details of which are now available online under the tag "Collegium Resolutions".

The Supreme Court, again with its progressive decision, has protected the interest of consumers. The recent landmark judgment in the case of *Om Prakash vs. Reliance General Insurance,* (Civil Appeal No 15611/2017 dated 4-10-2017) held that insurance claims cannot be denied merely on the ground of delay in filing the claim, holding that such denial, a technical ground, will result in loss of people's confidence in the insurance industry. The Apex Court emphasised that the Consumer Protection Act was meant to protect the interest of consumers and the law deserved liberal construction.

However, coming back to the financial capital, the recent stampede at the Footover Bridge at Elphinstone Road station at Mumbai is a black hole in the claims of the Government in providing the basic infrastructure to the financial capital. The debate is now on whether India needs a bullet train or better infrastructure for the larger sections of society. I feel Changing India in important but so is managing the change. Accountability is the need of the hour in the public services. We, the citizens need to now shed away the "chalta hai" attitude and be a part of the changing India.

Back to our Chamber, the recent IBC workshop was a unique programme organised jointly by the Allied Laws Committee and Corporate Connect Committee wherein the Hon'ble Member Shri Mukul Shrawat, Judicial Member of NCLT inaugurated the programme. During his talk Hon'ble Member appreciated the structure of this unique programme and also the CTC Journal more particularly the month of September containing Special Story on IBC. The panel discussion was icing on the cake.

Outstation programme jointly with local associations at Jamnagar, Solapur and Kolhapur was also well attended by the local participants.

Our much awaited Direct Tax RRC at Amritsar and GST RRC at Udaipur are announced. Members can take this opportunity of unique events to learn and also enjoy with our friends and colleagues in a relaxed atmosphere.

Lastly but not the least; Making the right decision at the right time leads to a happy successful life. Some tips in brief, that one may follow:

a) Picking an appropriate **social circle** can maximise the chances of reaching happier and fulfilling outcomes.

b) Overcome the **negativity bias**, the worst offender is the negativity bias or the tendency to recall negativity event more easily.

c) Avoid an overload of information. **Information is not knowledge**. Focus on concept and principles. Do not misunderstand intelligence.

d) Inculcate the habit of **charity**.

The Special Story for this month is on "GAAR". I thank all the authors for sparing valuable time and for their contribution to the Chamber's Journal for this month.

Jai Hind.

AJAY R. SINGH
President

Chairman's Communication

Dear Readers,

Yet another monetary policy of Reserve Bank of India was recently announced. As expected the interest rate is unchanged. However one of the significant highlights of the monetary policy is, downsizing economic growth forecast from 7.3 per cent to 6.7 percent. The Government has got a lot of criticism from various quarters of society for slowdown in growth, its failure to arrest the increasing cost of living, failure of demonetisation, hardship faced by business community due to GST etc. But the Government has very strongly refuted the criticism and claimed these to be initial problems to deliver ultimate benefits to the people at large. Nonetheless , the Government has announced some relaxations in GST Law, may be to appease everyone.

The year 2016-17 would be remembered by the professionals for enactments of many new laws viz., RERA, Bankruptcy Code, The Benami Transactions (Prohibition) Amendment Act, 2016 and above all GST. In addition to these new laws, the provisions of GAAR or general anti-avoidance rules have come into effect from April 1. GAAR was first introduced in 2012 by the then Finance Minister Mr. Pranab Mukherjee but its implementation was subsequently deferred. As readers would be aware, GAAR is a set of rules under which the tax department gets the right to scrutinise transactions, if they believe that they are structured for the purpose of avoiding taxes. GAAR is applicable to all investors but is more concerned about foreign portfolio investors, who invest in Indian markets through other countries where tax rates are very low.

Provisions of GAAR, as such, are quite complex and there is not enough material on the subject. Therefore considering the importance of the topic and to educate the members, we have brought out this issue which would give you an insight about the subject. The issue would not have been possible without the efforts of my colleague CA Naresh Ajwani and CA Rakesh Upadhyaya who have very meticulously designed the issue covering all the important aspects. My sincere thanks and appreciation to both of them as well as CA Neeraj Chheda for helping them in co-ordination. My gratitude to all the learned authors for sparing their valuable time and sharing their knowledge.

While all of us are geared up and working hard to finalise the tax audit reports and income tax returns to meet the extended deadline of 31st October, we must spare some time to enjoy the festival of lights, Diwali with our family. Wishing you and your family a very Happy Deepawali and Happy New Year – S.Y.2074 !

VIPUL K. CHOKSI
Chairman – Journal Committee

The Chamber of Tax Consultants

Vision Statement

The Chamber of Tax Consultants (The Chamber) shall be a powerhouse of knowledge in the field of fiscal laws in the global economy.

The Chamber shall contribute to the development of law and the profession through research, analysis and dissemination of knowledge.

The Chamber shall be a voice which is heard and recognised by all Government and Regulatory agencies through effective representations.

The Chamber shall be pre–eminent in laying down and upholding, among the professionals, the tradition of excellence in service, principled conduct and social responsibility.


CA Pinakin D. Desai & CA Vinod Ramachandran

Overview and Background of GAAR

Introduction

Anti-avoidance rules are divided largely into Two main categories — "General Anti-Avoidance Rules (GAAR)" and "Specific Anti Avoidance Rules (SAAR)". Anti-avoidance rules which target specific tax avoidance measures are known as SAAR, or less commonly,Targeted Anti-Avoidance Rules (TAAR). Indian legislation is ripe with a number of SAARs. SAAR in a legislation targets to plug particular mischief by laying down certain tests – often, objective – which need compliance if the stated tax benefit is to be availed. For example, s.64 or s.94B or s.80-IA(3) or transfer pricing provisions may be considered as examples of SAAR.

One of the limitations of SAAR is that a smart taxpayer may so plan his affairs that he complies with the objective conditions of SAAR in letter but not in spirit. Thus, SAAR may not be able to take care of innovative mechanics of tax avoidance exercise adopted by a taxpayer.

GAAR represents a set of rules designed to counteract any known or novel form of tax avoidance. GAAR is a concept within law that provides tax authority a power to deny tax benefits when an arrangement is undertaken without any commercial substance or commercial purpose (i.e., when an arrangement is planned to generate a tax benefit) or when the tax benefit is the primary purpose behind the arrangement. By nature, GAAR is not limited in its application to specified abuse or mischief; it can apply to any tax avoidance exercise which has been primarily designed for seeking tax benefit.

GAAR (Chapter X-A): Successor to judicial GAAR

Much prior to introduction of GAAR *vide* Chapter X-A, the judicial echo in India had drawn a line between permissible and impermissible tax avoidance. It was common ground that tax evasion was always impermissible whereas tax mitigation was always permissible. Between the two, lay the concept of tax avoidance and disputes used to arise whether a tax avoidance exercise on hand belongs to the category of permissible tax avoidance or impermissible tax avoidance.

After reconciling its earlier judgments in *McDowell & Co. Ltd. vs. CTO (1985)(154 ITR 148) (SC)* and *UOI vs. Azadi Bachao Andolan (2003)(263 ITR 706)(SC)*, in case of *Vodafone International Holdings BV vs. UOI (2012)(341 ITR 1)*, the Supreme Court concluded that if the taxpayer has inserted a step having no commercial purpose whatsoever but only with a view to seek tax benefit, the arrangement could be re-characterised and the step could be disregarded.

It was never too easy for the Courts in certain other cases to distinguish between a permissible as opposed to an impermissible tax planning / avoidance exercise.

Why GAAR raises concerns for taxpayers?

It is generally acknowledged that GAAR is never meant to be a revenue raising measure but is a measure of deterrence to impermissible tax avoidance. Its purpose is to keep aggressive taxpayers under a threat that a planning scheme perceived to be driven predominantly by tax benefit (as against a commercial purpose) can be questioned by tax authority. GAAR is meant to relieve tax administration from keeping a close watch on each different mitigation alternative that knowledgeable taxpayers develop by finding loopholes or weaknesses in tax provisions. It is a check against any novel tax planning which a taxpayer may come up with so as to exploit limitations of the framework of statute.

There is, however, justification for concerns from taxpayers. GAAR provisions grant wide powers to tax authority, including, the power to re-characterise a transaction or arrangement. At the same time, the yardstick used for determining acceptability or non-acceptability of a transaction within the GAAR framework is, to a large extent, subjective. The combination of subjectivity and grant of wide powers to tax authority can cut at the root of stability and investor confidence in tax administration, if the implementation is capricious or immature.

It is hence desired that, GAAR should be used as a tool of last resort and necessary safeguards be put in place to prevent misuse of GAAR provisions by the tax authority.

To quote extracts from report of Expert Committee headed by Dr. Parthasarathi Shome:

"GAAR is an extremely advanced instrument of tax administration – one of deterrence, rather than for revenue generation…Every case of tax avoidance should not be considered under GAAR unless it is an abusive, artificial and contrived arrangement…"

Snapshot of international experience on GAAR: A number of countries have adopted statutory GAAR to counter tax avoidance for protecting their tax base.

Following is a list of the countries that have introduced statutory GAAR[1]:

1.	New Zealand	5.	France	9.	Singapore	13.	China
10.	Australia	6.	South Africa	11.	Ireland	14.	UK
12.	Germany	7.	Sweden	13.	Belgium	15.	India
14.	The Netherlands	8.	Canada	15.	Italy		

But, there are also some countries that continue to rely on judicial GAAR (for instance: Russia, USA, Switzerland and Czech Republic).

Evolution of GAAR in India

GAAR has involved an unprecedented history of intense debate and consultation that started with the Government's proposal to introduce GAAR in the Direct Taxes Code Bill, 2009 (DTC 2009). The provisions in DTC 2009 were largely borrowed from South African GAAR.

The introduction of GAAR was considered necessary because, according to the Government, tax avoidance, like tax evasion, was economically undesirable and inequitable; and increasingly sophisticated forms of tax avoidance were being adopted leading to severe erosion of the tax base[2].

However, DTC 2009 could not be enacted due to several representations, and in its place, the Government attempted to introduce

1 The statutory provisions are largely similar but not identical

2 Refer Discussion Paper on DTC 2009

a revised version of the DTC in 2010. On 9 September 2010, the DTC 2010, after being introduced in the Parliament, was referred to a Standing Committee of Parliament for further examination, which, on 9th March 2012, recommended that the GAAR provisions needed an overhaul and should be made more precise, cautioning that lack of certainty could make foreign investors wary of investing in India.

Proposal in Finance Bill, 2012 (FB 2012) to introduce GAAR in the Act

Though the recommendations of the Standing Committee of Parliament were yet to be implemented, quite surprisingly, while presenting the Union Budget of 2012 on 16th March 2012, the Finance Minister fast tracked the implementation of GAAR by proposing to introduce GAAR in the Act w.e.f. 1st April 2013[3]. The FB 2012 largely retained format of the GAAR proposed in DTC 2010, and further widened its scope to include an arrangement where "one of the main purposes" was to obtain a tax benefit. Also, such purpose could be presumed by the tax authority to exist; the taxpayer was saddled with the responsibility to prove otherwise. It was no surprise that the FB 2012 created huge uproar and a sense of nervousness in the tax paying community.

GAAR modified while enacting Finance Bill, 2012

At the stage of enacting FB 2012, the Finance Minister did accept some of the suggestions made by taxpaying community as well as by the Standing Committee of Parliament. Also, GAAR provisions were amended to suggest that the onus of proof to establish the taint of GAAR was on the tax authority. At the same time, application of GAAR was deferred to 1st April 2014 to allow time for further debate and discussion.

Constitution of internal committee by CBDT

On 27th February, 2012, the CBDT constituted an internal committee (comprising officials of the CBDT) to give recommendations on formulating guidelines for proper implementation of GAAR and to suggest safeguards to curb the abuse of GAAR. On 28th June, 2012, this Committee issued draft GAAR guidelines and invited comments/suggestions from stakeholders thereon. Ironically, the draft GAAR guidelines, rather than dispelling concerns of taxpayers, became a cause of heightened uncertainty!!

Constitution of Shome Committee and eventual introduction of GAAR

Sensing the need for far more widespread consultation, the then Prime Minister constituted an Expert Committee on GAAR (hereinafter referred as "Shome Committee") on 17th July 2012, under the chairmanship of Dr. Parthasarathi Shome, to work on a second draft of the GAAR guidelines based on comments from various stakeholders. The Shome Committee submitted its final report to the Government on 1st October 2012.

On 14th January 2013, the Ministry of Finance issued a Press Release to announce that the Government has accepted major recommendations made by Shome Committee, with some modifications. The Government also announced that the implementation of GAAR will be deferred to 1st April 2016 (which was later deferred to 1st April 2018, vide Finance Act, 2015).

Explanations or justifications from Finance Minister and CBDT for introduction of GAAR:

The following rationale for introduction of GAAR was expressed in the Explanatory Memorandum of FB 2012:

3 There is a strong view that the introduction of GAAR as well as some of the amendments in FB 2012 (as compared to earlier draft of GAAR in DTC 2010) is a knee-jerk reaction to Supreme Court's ruling (SC) in case of *Vodafone International Holdings BV vs. UOI (2012)(341 ITR 1).*

> ***"In an environment of moderate rates of tax, it is necessary that the correct tax base be subject to tax in the face of aggressive tax planning and use of opaque low tax jurisdictions for residence as well as for sourcing capital.*** *Most countries have codified the "substance over form" doctrine in the form of General Anti Avoidance Rule (GAAR).*
>
> ***In the above background and keeping in view the aggressive tax planning with the use of sophisticated structures, there is a need for statutory provisions so as to codify the doctrine of "substance over form" where the real intention of the parties and effect of transactions and purpose of an arrangement is taken into account for determining the tax consequences, irrespective of the legal structure that has been superimposed to camouflage the real intent and purpose.*** *Internationally several countries have introduced, and are administering statutory General Anti Avoidance Provisions. It is, therefore, important that Indian taxation law also incorporate a statutory General Anti Avoidance Provisions to deal with aggressive tax planning.* ***The basic criticism of statutory GAAR which is raised worldwide is that it provides a wide discretion and authority to the tax administration which at times is prone to be misused. This vital aspect, therefore, needs to be kept in mind while formulating any GAAR regime.***
>
> *It is accordingly proposed to provide General Anti Avoidance Rule in the Income Tax Act to deal with aggressive tax planning."*

The Finance Minister stated as follows in the Union Budget speech of 2012:

> *"I propose to introduce a General Anti-Avoidance Rule (GAAR)* ***in order to counter aggressive tax avoidance schemes,*** *while ensuring that it is used only in appropriate cases, by enabling a review by a GAAR panel."*

What appears to emerge from the above is that the legislative intent is to capture an arrangement which is aggressive in terms of tax planning and/or which is abusive, artificial or contrived whose object is to avoid or eliminate tax which would have been otherwise payable. The legislative intent, therefore, is not to find out the existence of tax benefit, but, to ascertain whether there is any abusive manner in which tax benefit is sought to be obtained. It is possible that, while interpreting the GAAR provisions, the court may keep in view the above legislative object to protect *bona fide* transactions and/or restrict applicability of GAAR only to clear and egregious cases of tax avoidance.

What are the appropriate safeguards in GAAR against inappropriate invocation of GAAR by tax authority?

Invocation of GAAR requires approval, in the first stage, of the Commissioner, and then, in the second stage, of the approving panel. Foremost, pursuant to suggestions of Shome Committee, the Government has modified constitution of approving panel so as to make it a neutral and independent body. The approving panel comprises three members, headed by a sitting or retired judge of a High Court, one member being from the tax department (not below rank of Chief Commissioner or Principal Chief Commissioner) and one member being an academic scholar having special knowledge of matters such as direct taxes, business accounts and international trade practices.

Assurances from Finance Minister and CBDT that GAAR will be used with restraint

Apart from assurances in FB 2012 reproduced earlier, the following reflect assurances of the Government to ensure that GAAR provisions intend to tackle blatant tax avoidance schemes and are not to be applied indiscriminately:

(i) While proposing amendments to FB 2012 and while answering to parliamentary debate, Finance Minister stated on 7th May 2012:

"To provide greater clarity and certainty in the matters relating to GAAR, a Committee has been constituted under the Chairmanship of the Director General of Income Tax (International Taxation) to give recommendations for formulating the rules and guidelines for implementation of the GAAR provisions and ***to suggest safeguards so that these provisions are not applied indiscriminately."***

(ii) Extracts from article in Economic Times dated 24th August 2017 quoting CBDT Chairman Sushil Chandra[4]:

"Chandra said the GAAR will be used in exceptional circumstances and only to ensure that the country gets its due share of taxes. GAAR will be invoked only if the tax provisions are misused, he said, adding that companies, firms or MNCs should believe in fair taxation."

Safeguards introduced by way of Rules:

Following are the safeguards contained in Rules 10U to 10UC, some of which are introduced pursuant to acceptance of Shome Committee's recommendations:

(i) *De-minimis* threshold is specified so that GAAR is not invoked where tax benefit arising in the relevant assessment year to all the parties to the arrangement does not exceed ₹ 3 Cr.;

(ii) Grandfathering past investments so that GAAR will not apply to income from transfer of investment made before 1st April 2017;

(iii) If part of an arrangement is declared impermissible, the consequences under s.98 shall be determined with reference to such part only;

(iv) Primary onus is cast on Assessing Officer to indicate, by way of show cause notice, the arrangement and reasons why it should be declared impermissible.

Benevolent clarifications introduced by way of Circular

The notable clarifications provided in CBDT Circular No. 7 of 2017 dated 27th January 2017 (the "Circular") are as under:

(i) GAAR shall not interplay with the right of the taxpayer to select or choose method of implementing a transaction.

(ii) GAAR shall not apply if the arrangement is held to be permissible in an advance ruling.

(iii) GAAR shall not apply if the tax benefit obtained by all the parties to the arrangement is less than ₹ 3 Cr. per assessment year.

(iv) GAAR shall not be invoked if tax avoidance is "sufficiently addressed" by limitation-of-benefits clause in the treaty.

(v) As per CBDT, the administrative safeguards provided in law (that invocation of GAAR is to be approved by Commissioner and Approving Panel) will ensure that the consequences of GAAR are determined in a uniform, fair and rational manner.

While the above clarifications are welcome, few critical issues that remain unaddressed are: (a) an unequivocal statement that tax mitigation is different from tax avoidance for the purpose of GAAR; (b) exclusion of intra-group transactions (where overall tax base is unaffected) from scope of GAAR; (c) also, while the Ministry of Finance

4 http://economictimes.indiatimes.com/wealth/tax/central-board-of-direct-taxes-open-to-giving-foreign-companies-a-breather/articleshow/60199647.cms

had clarified in the Press Release dated 14th January 2013 that corresponding adjustment will be permitted across different assessment years if GAAR is invoked for a particular taxpayer, this aspect remains to be codified in the Act or Rules.

Basic concept of GAAR in Indian tax law

Main purpose to obtain tax benefit: As per s.96 of the Act, unless the main purpose of an arrangement is to obtain a tax benefit, the arrangement cannot be declared as an impermissible avoidance arrangement.

An arrangement has been defined widely to include a transaction, operation, scheme, agreement, etc. It need not necessarily be a bilateral arrangement. It could be a unilateral scheme which is conceived by the taxpayer himself. Also, the transaction or agreement, etc. need not be enforceable in order that it can be declared as impermissible.

The onus of establishing that the main purpose is to obtain a tax benefit is on the tax authority. However, since the facts concerning the object or purpose, are within the knowledge of a taxpayer, it is likely that the tax authority will obtain basic evidence from the taxpayer. Therefore, in respect of an arrangement on hand, the taxpayer will need to explain the purposes or objects which he wanted to achieve through the medium of his arrangement and also substantiate such purposes or objects through tangible evidence. Based thereon, an assessment may be necessary as to whether the main purpose was to obtain a tax benefit.

In other words, while the tax consequences were earlier determined by looking at what has been done, with the onset of GAAR, the tax consequences will be determined by examining "why" it has been done.

By way of a crude example, if an individual shifts his physical stay and residence to a tax haven so as to be a non-resident for one year during which he intends to transfer some of his outside India assets, he could be questioned under GAAR – more particularly, if he did not move with the family and was frequently found to be in India. But, if the individual decides to move to a different country along with the family for good, the main purpose cannot be alleged to be obtaining of tax benefit merely because the individual happens to sell some of his outside India assets after some interval.

As stated earlier, if the main purpose of an arrangement is not to obtain a tax benefit, GAAR provisions will not apply. No further inquiry will be needed. Hence, it would be to the advantage of a taxpayer to aggregate and explain various commercial purposes that were pivotal for undertaking the arrangement.

A step in an arrangement vs. the whole arrangement

An arrangement has been defined widely to include a step in an arrangement. In a case where the arrangement is comprised of more than one step, each step may, in itself, be considered to be an arrangement subject to GAAR scrutiny.

Suppose, A Pvt. Ltd. is desirous of selling its asset at a gain but the promoter group is not interested in honouring the capital gains liability. B Pvt. Ltd. owned by same promoter group has huge capital loss. A Pvt. Ltd. makes a gift of asset to B Pvt. Ltd. whereupon the sale is effected through B Pvt. Ltd. The overall arrangement is undertaken with a view to encashing the asset but the intermediate step of gift can be regarded as being introduced to obtain tax benefit. Such a step is an arrangement by itself. Its purpose can be questioned under GAAR as if it is an integrated arrangement.

As per one plausible reading of s.96(2), the whole of the arrangement can be presumed to be for obtaining tax benefit if any step in such whole of the arrangement is engineered with the main purpose of tax benefit. The onus of establishing *prima facie* that the step was inserted with the main purpose of seeking tax benefit is on the tax authority. Once that onus is fulfilled, there is rebuttable presumption against the taxpayer in relation to the overall arrangement (including the identified step). The onus will thus shift to the taxpayer in relation to the other steps as well, but on a rebuttable basis.

This does not however, suggest that GAAR can apply only if the arrangement contains an abusive step. An arrangement can be prone to GAAR inquiry even if it is a one-shot transaction not having steps.

Concept of counterfactual

A counterfactual can be understood as an alternative manner in which a taxpayer could have completed the transaction in a seamless manner without the allegation of obtaining a tax benefit in an impermissible way.

It is possible that the independent panel under GAAR may require the tax authority (who has to discharge his onus) to provide counterfactual which, in the opinion of the tax authority, should have been chosen by the taxpayer to achieve his desired commercial objectives. Any such counterfactual should be relatively simpler and more straightforward and yet it should achieve all the meaningful commercial objects which the taxpayer had in view while implementing the alleged impermissible avoidance arrangement. If the counterfactual compels the taxpayer to sacrifice or compromise his commercial objects, it loses the weight of a valid counterfactual.

Should arrangement necessarily be pre-ordained?

The length of an arrangement may encompass the initial and the destination point of an arrangement if it is pre-ordained or pre-designed. It need not necessarily be a short term arrangement. It can extend over a period or over years. So long as the individual components are pre-conceived or pre-ordained, they can form part of an arrangement. Each of the individual components would qualify as a step in or part of the arrangement.

At times, it may be difficult for tax authority to ascertain, at the threshold, the scope of overall arrangement and the individual components thereof. Evidence can be obtained as the events unfold over a period. The inquiry is likely to begin only in the year when the tax benefit is actually obtained. Intrinsically, GAAR scrutiny is purpose driven. Purpose of any arrangement is in the mind of the progenitor and is best discerned from contemporaneous documents and correspondence including that with the tax advisors. Since a businessman is not expected to have extra sensory perception, his evaluation of commercial factors and purpose will need to be analysed under GAAR based on what may be expected by a reasonable person as the outcome of transaction as of date of implementation. It may not be correct to attribute purpose to a given arrangement on a hindsight basis by putting forth the factors and developments which could not have been within realm of expectations of a reasonable person.

Definition of tax benefit

Tax benefit as defined in s.102(10) of the Act is restricted in its scope to tax liability under the Act. GAAR is not capable of being invoked merely because the object of an arrangement or a step therein is to obtain benefit under some indirect tax law or under stamp duty law or under tax law of any other country.

Improving shareholders value is one of the valid commercial purposes. Tax does dent such value. Thus, while saving tax is a commercial need, it is not to be regarded as a commercial purpose for negating GAAR applicability. Some of the provisions of Chapter X-A make it clear that evaluation of GAAR needs to be done by disregarding the defence of tax benefit being a commercial purpose.

GAAR does not compel taxpayer to pay the maximum tax

It is not the purpose of GAAR that the taxpayer should opt for an alternative mode of completing the transaction which results in maximum payment of tax. Legitimate tax planning within permissible limits continues to be protected even under GAAR. For example, a taxpayer can certainly continue to invest in bonds for the purpose of exemption under s.54EC even if there is evidence that, but for tax exemption, he would have preferred an alternative mode of investment.

Also, as rightly clarified in the Circular, a taxpayer who has legitimate options available to choose from can still lean in favour of an option which results in tax saving. For example, a person can decide to carry on business within the fold of LLP rather than a company; a person can borrow money on interest rather than investing his own money in the business; he can decide to lease or own an asset; investing in debt as compared to equity; rewarding shareholders by buy-back as compared to dividend; etc.

But, the artifice can be questioned if, in reality, the chosen alternative is a gloss for the real transaction. For example, if the person who, in reality, owns an asset wants to raise a façade of a lease so as to claim lease rental as deductible expenditure, the transaction can be questioned under GAAR and can be recharacterised as that of purchase on instalments.

GAAR is wider than transfer pricing and overreaches domestic as also international transactions

GAAR is not restricted in its application to cross border transactions. It can as well capture purely domestic scenarios. Further, while transfer pricing chapter may apply in a case where dealing is between related parties, GAAR can apply in a case where the parties are wholly unrelated and yet are a privy to a GAAR prone arrangement.

The consequences as may follow under GAAR differ materially from those under TP. For example, when GAAR is invoked, the benefit of treaty network can be denied to a recipient of income if it is established that the selection of place of residence of the entity was without any substantial commercial purpose. GAAR can re-characterise the nature of income or transaction, while transfer pricing regulations traditionally can only re-calculate the income. Thus, GAAR is wider in scope than transfer pricing regulations.

Conclusion

While the introduction of GAAR has created a lot of anxiety amongst the taxpaying community, a lot will depend upon the manner in which GAAR is implemented by the tax authorities. If used selectively to shield the tax base, GAAR can prove to be an effective deterrent against abusive tax avoidance. On the other hand, if used as a tool to maximise tax revenue, it can hamper investment climate in India, which the present Government is striving hard to better.

Defending GAAR is not merely a matter of technical argument. "Purpose" of the transaction will be central to the evaluation of GAAR. The taxpayers should ensure that, even while the transaction is being contemplated, commercial purpose is sufficiently documented so as insulate against any possible allegation of GAAR.

To address tax avoidance through abuse of treaty, the Indian Government is committed to the BEPS agenda. The interplay of principal purpose test (enshrined in Article 7 of Multilateral Instrument) and GAAR will pose interesting questions and challenges in dealing with cross-border scenario. These aspects will hopefully be discussed separately in the later chapters.

CA Naresh Ajwani

Applicability of GAAR – Fundamental requirements

Index

1. Preamble

General Anti-Avoidance Rule (GAAR) is effective from 1-4-2017 (Assessment Year 2018-19). It is meant to apply to transactions which are *prima facie* legal, but result in tax reduction. Broadly, tax reduction can be divided into 3 categories. One is tax mitigation which involves legal measures with substance to save taxes (e.g. setting up a new unit in SEZ). This is acceptable even after GAAR has come into force. Second is tax evasion where the transactions are outright sham, or are concealed. This is not covered by GAAR as existing jurisprudence is sufficient to cover tax evasion / sham transactions. The third is tax avoidance with the use of legal steps resulting in tax reduction, which steps would not have been undertaken if there was no tax reduction. This kind of tax avoidance planning are sought to be covered by GAAR.

With GAAR, there is no difference between tax evasion and tax avoidance. All transactions which have implications for avoiding income-tax, can be under the scanner of GAAR. At the same time all tax saving transactions cannot be considered under GAAR. A tax relief provided by the Government cannot be a matter of GAAR scrutiny if the relief has been claimed in a *bona fide* manner and as per rules.

The focus of this article is on fundamental requirements which have to be satisfied for GAAR to apply. There are some exemptions provided from applicability of GAAR. There are issues on applicability of GAAR when SAAR is present or when a DTA is available. Those provisions have been dealt with in separate articles by other authors. Implications if GAAR applies, dispute resolution mechanism and other issues concerning GAAR are also dealt with by other authors in other articles.

Abbreviations used

AO	–	Assessing Officer
GAAR	–	General Anti-Avoidance Rule
IAA	–	Impermissible Avoidance Arrangement
ITA	–	Income-tax Act
R	–	Rule
S/Ss	–	Section/Sections

2. When can GAAR apply?

2.1 Section 95 deals with the basic requirement for applicability. It applies to an <u>arrangement</u> if it is declared as an <u>Impermissible Avoidance Arrangement (IAA)</u>. Arrangement is discussed in paras 2.2.1 to 2.2.3. IAA is discussed in paras 4 to 6.

The section begins with a non-obstante clause – "Notwithstanding anything contained in the Act …". Thus GAAR has an overriding applicability.

There are several non-obstante clauses in the ITA. Some are restrictive and some are exhaustive. For example, S. 94B provides that notwithstanding anything contained in this Act, interest paid to an Associate Enterprise and exceeding 30% of EBITDA will be disallowed under specified circumstances. Will S. 94B override GAAR or will it be the other way? Both provisions continue to apply simultaneously. *Prima facie*, there will be a disallowance of interest u/s. 94B to some extent. This is mandatory. Intention of tax avoidance does not have to be considered. However, if it is determined that the arrangement is IAA, then GAAR can be invoked. If GAAR is invoked, the entire interest may be disallowed (depending on the circumstances). Thus, GAAR can go beyond other sections.

S. 206AA provides that if the recipient of income does not provide PAN to the payer, then higher of the specified TDS rates will be applied – notwithstanding anything contained in the ITA. Here, there is no conflict as such between S. 206AA and GAAR. S. 206AA applies to the payer. GAAR applies to income earner. Hence both the sections can apply simultaneously.

By and large GAAR will have an overarching applicability.

The explanation to section 95 clarifies that the provisions of GAAR chapter may be applied to <u>any step in</u>, or <u>a part of</u>, <u>the arrangement</u> as they are applicable to the arrangement. Thus, scope of applicability is very wide.

2.2.1 **Arrangement** – S. 102(1) defines an "arrangement" to mean:

– any step in, or a part or whole of,

– any transaction, operation, scheme, agreement or understanding,

– whether enforceable or not, and

– includes the alienation of any property in such transaction, operation, scheme, agreement or understanding.

It includes a singular transaction, or multiple transactions which can amount to an operation or a scheme or an agreement or an understanding. It also includes a step in or a part of a transaction.

The arrangement may be enforceable or not. For example, a scheme of illegal betting is not enforceable. However, GAAR can apply.

To avoid any controversy, it has been stated that alienation of any property in an arrangement can also be considered as an arrangement.

2.2.2 A part of the arrangement or a step in it is also considered as an arrangement. There is an issue as to whether GAAR will apply only to that part which is IAA, or the whole. Rule 10UA clarifies that where only a part of arrangement is IAA, GAAR will apply only to that part. There is no clarification in case only a step in the arrangement is considered as IAA. However a step would mean a part of the arrangement. Logically GAAR should apply only to the step in the arrangement which is held as IAA.

Step has been defined in S. 102(9) to include a measure or an action, particularly one of a series taken in order to deal with or achieve a particular thing or object in the arrangement. The emphasis is on a step in a series. Can a single step by itself mean that it is an arrangement? It appears that if it is a part of series of transactions, then it can be considered as a part of arrangement.

2.2.3 Even a single transaction can also be considered as an arrangement. It is difficult to envisage a transaction as an arrangement. For example, if a person gives a gift of his property to a non-resident, by itself it is a transaction. The donor will not earn any income after the gift. This cannot be considered as an arrangement. However in future, the non-resident returns the sum to the donor with the income which he earned outside India (without paying tax in India). Can it be treated as IAA? If it can be established that the transfer of funds abroad was with the pre-determined understanding that the funds will come back to India, it can be considered as an arrangement. Here the arrangement will include all transactions from giving the gift till returning the money. But only one transaction of gift cannot be considered as an arrangement.

However, consider a transaction of a non-resident. Before returning to India, he gifts his funds to an offshore company. The income will be earned by the offshore company. Will this one transaction be considered as an IAA? Perhaps yes. There is another view that GAAR cannot apply to a non-resident. However, in my humble submission, there is no restriction that GAAR cannot apply to arrangements entered into by non-residents if the intention is to avoid Indian tax. R. 10U(2) clarifies that GAAR can apply irrespective of the year in which the arrangement was entered into.

2.3 GAAR will apply in accordance with the guidelines and subject to the conditions as may be prescribed. Rules 10U, 10UA, 10UB and 10UC lay down the guidelines and conditions.

3. Onus on whom?

3.1 Under GAAR the onus is on the revenue to declare an arrangement as IAA. The declaration of an arrangement as an IAA has to be under a specified process u/s. 144BA read with the relevant rules. If the revenue considers that the arrangement is an IAA, the assessee will be given an opportunity to be heard. Based on the response of the assessee further action will be taken.

Thus there is no *suo motu* application of GAAR. It is has to be specifically applied by the revenue by declaring the arrangement as IAA.

Having declared an arrangement as IAA, the onus shifts to the assessee to rebut the declaration or agree with the revenue's view.

This is one of the important differences between GAAR and Specific Anti-Avoidance Rule (SAAR). The SAAR lays down specific rules which have to be complied with in order to obtain the relief/or for tax not to apply. The onus is primarily on the assessee to comply with the rules.

3.2 There is however a presumption regarding the onus on the assessee. If a step in or a part of arrangement is for the main purpose of obtaining tax benefit, then it will be presumed that the entire arrangement is for obtaining tax benefit. This is the presumption even though the main purpose of the whole arrangement was not to obtain tax benefit. [S. 96(2)]. The assessee can then prove that the main purpose of the entire arrangement was not to obtain tax benefit.

This rebuttal by the assessee will be required if the revenue declares the arrangement to be an IAA.

4. Impermissible Avoidance Arrangement (IAA)

The key test for GAAR to apply is IAA. Section 96 defines IAA. Two conditions have to be satisfied together to consider an arrangement as IAA.

A) One is that there is a <u>tax benefit</u>. (This should be the <u>main purpose</u>.)

B) Secondly, any of the four situations occur (or don't occur). (These are also known as <u>tainted element tests</u>.)

   i) creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length.

   ii) results, directly or indirectly, in the misuse, or abuse, of the provisions of this Act.

   iii) lacks commercial substance or is deemed to lack commercial substance under section 97, in whole or in part.

   iv) is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for *bona fide* purposes.

In clause B) above, the tests are not cumulative. These are alternative tests. Each of the above clauses has vast scope. Let us see below the important terms.

4.1 Tax benefit

4.1.1 <u>Tax benefit</u> has been defined in Section 102(10). R. 10U(3)(iv) further clarifies the meaning. It is an inclusive definition and includes:

i) reduction or avoidance or deferral of tax or other amount payable under the ITA – whether due to a DTA or otherwise.

   Tax has been defined u/s. 2(43) to mean income-tax chargeable under the provisions of this Act. (There is a reference to super tax and Fringe Benefit Tax which are currently not relevant.)

   However what will be included in "other amount"? Will it include surcharge, education cess, interest and penalty? In my view interest and penalty cannot be included in the meaning of tax. Interest and penalty are consequences of a delay in payment of tax, or an offence for avoiding tax. However interest, education cess and surcharge will be included in the phrase "other amount" as the character is that of tax.

ii) increase in refund or other amount payable under the ITA – whether due to DTA or otherwise.

iii) reduction in total income or increase in loss.

   Thus benefit due to change in tax or change in income will be considered as tax benefit.

4.1.2 The tax benefit has to be considered in the relevant <u>previous year</u> or <u>any other previous years</u>. The "relevant" previous year is not explained but should mean the year when the arrangement is declared as IAA. However what is the significance of "any other previous years"?

Rule 10U(1)(a) has provided that if the tax benefit is ₹ 3 crores or less, then GAAR will not apply. CBDT has stated in its Circular No. 7 dated 27-1-2017 in answer to Question 14 that benefit has to be seen "assessment year specific". It means that if the benefit during the specific year is ₹ 3 crores or less, GAAR will not apply. Consider an illustration below.

A person enters into an IAA where the tax benefit is ₹ 1 crore per year for 5 years, will

GAAR apply? Section 102(10) provides that the benefit can be in the relevant previous year or any other previous years. Thus it would mean that GAAR will apply as the tax benefit is ₹ 5 crores in the relevant previous year and any other previous years. However CBDT circular states that the benefit has to be seen assessment year specific.

4.1.3 Can one take a view that the limit of ₹ 3 crore has to be considered when the arrangement is declared as IAA? Then the benefit may be in one year or spread over few previous years. In the above example, when the arrangement is declared as IAA, the tax benefit is determined at ₹ 5 cr. It is only spread over a few years. Hence GAAR will apply.

CBDT circular appears to be beneficial. The benefit has to be seen "assessment year specific". In the above case as the benefit is ₹ 1 crore GAAR should not apply.

4.1.4 Should the tax benefit be considered per assessee or spread across all assessees involved in the IAA? Section 96(1) refers to tax benefit in case of an arrangement. Whether one assessee benefits or several assessees benefit, is not relevant. CBDT also has clarified that the tax benefit cannot be restricted to one assessee. (Question 14).

However if an arrangement provides tax benefit to one assessee and excess tax to another assessee, excess tax for one person be reduced from tax benefit to another? The objective is to consider the tax benefit across all assessees. Hence if the net result is a tax benefit of less than ₹ 3 crore GAAR should not apply.

On the same logic, if a person claims a loss in one year due to IAA, but will be paying tax in future years, can GAAR apply (as there is no tax benefit over the years)? Here the GAAR will apply as there is a tax deferment.

4.1.5 How has the tax benefit to be computed? If an assessee has a specific arrangement and has paid tax of say ₹ 100. With what will this tax of ₹ 100 be compared with to arrive at the tax benefit? The revenue will have to "re-arrange" the facts and arrive at reworked facts. These are known as counter-factuals. The tax will be worked out based on reworked facts. The difference between tax on reworked facts and assessee's facts will be tax benefit. The revenue will have to rework the facts and compute the tax benefit before a notice is issued to the assessee.

For example, if instead of dividend, the company makes a buyback of shares. Tax under both arrangements is same or less than ₹ 3 crores, then obviously it will not be an IAA. However see para 11 for more discussion.

4.2 Main purpose

The previous versions of GAAR provided that the tax benefit should be the main purpose or one of the main purposes. The Expert Committee appointed in 2012 recommended removal of reference to "one of the main purposes". Thus tax benefit should be the main purpose of the IAA. If there are other main purposes and tax benefit is one of them, then GAAR will not apply.

The issue is how does one consider whether the tax benefit is the main purpose or only one of the purposes. There is a view which states that there is not much difference "main purpose" and "one of the main purposes". Consider an illustration.

Company A is in the business of manufacturing soaps. Company B is in the business of manufacturing caustic soda (a raw material for soaps). Both are independent companies. For having in-house raw material supplies, it was agreed between the companies that Company B will merge with Company A. This also results in tax savings on account of capital gains; getting access to funds of Company B, etc. Company A could also have bought out the assets of Company B. However merger was agreed upon as there would be no tax.

In this illustration, business reason was one of the main reasons for merger. Tax benefit was also an important reason but not one of the main purposes. In this situation, GAAR cannot apply.

Consider a similar situation but where Company B is a subsidiary of Company A. Here Company A already has access to raw material of Company B (being its subsidiary). If Company B merges with Company A, will tax benefit be considered as the main purpose or one of the main purposes? In this case, the chances of applicability of GAAR are higher.

Consider another illustration where a UK MNC has subsidiaries in a few countries. For investment in India, it can invest from UK, or from a subsidiary in Singapore. While there is an office in Singapore, the staff is limited. Key business decisions are taken in UK. The main purpose of investment from Singapore is to take advantage of India-Singapore DTA which gives relief for Capital Gains tax. The decision for investment is also taken by the UK company. As the main purpose is to obtain tax benefit, GAAR can apply. (Of course GAAR will apply when the company earns income. On just investment, GAAR cannot apply.)

4.3 R. 10U(2) provides that GAAR will apply to any arrangement even if it is entered into prior to 1st April 2017 but the tax benefit is obtained on 1st April 2017 or later.

5. Tainted elements

IAA refers to 4 tainted elements test. Out of these, "lacking commercial substance" test is the most important. Hence that is dealt with first in this article.

5.1 Lacking commercial substance

5.1.1 Lacking commercial substance – Section 96(1)(c) refers to arrangement which:

– lacks commercial substance, or

– is deemed to lack commercial substance,

– in whole or in part.

"Commercial substance" has not been defined anywhere. "Lacking commercial substance" has been defined. Section 97 explains the meaning of "lacking commercial substance". However it actually explains when will the arrangement be considered to be "deemed to lack commercial substance". There is no meaning given specifically to lacking commercial substance.

Does one give importance to difference between "lacking commercial substance" and "deemed to lack commercial substance"? (This distinction is there under sections 5 (accrual of income) and 9 (deemed accrual of income) and has been explained by several courts.) Deemed accrual of income means the income actually may not accrue in India, but is deemed by fiction to accrue in India. Deeming provision has to be construed strictly. However the meaning of lacking commercial substance is so wide, that practically there may be no need to differentiate between the two. Lacking commercial substance and "deemed to lack commercial substance" would in effect mean one and the same thing.

An arrangement shall be considered to be deemed to lack commercial substance if any of the specified conditions are satisfied. I have divided the conditions into two groups as under:

5.1.2 ***Conditions in which form appears more important than substance***

i) Effect of arrangement as a whole is different from individual steps or a part of arrangement.

The Supreme Court decision in *McDowell (154 ITR 148)* has referred to House of Lords decision of Ramsay. Ramsay decision states that there may be a series of steps which individually may be genuine but collectively it gives rise to avoidance of tax. Such an arrangement can be disregarded. The clause refers to such cases.

ii) There is no significant effect on business risks or cash flows of party to an arrangement except for tax benefit.

Illustration – A promoter has two companies undertaking trading business in two different areas – say North India and South India. For some reasons, the company for North India earns profit and the company for South India incurs losses. To reduce taxes, the promoter books more sales for North India in the loss making company. Any shortfall in funds is met with temporary loan from the other company. Can this be considered as an arrangement where there is no effect on business risks or cash flows except for tax benefit? Unless the assessee can establish commercial reasons for the arrangement, GAAR may be applied.

Conditions which include certain actions:

iii) Round trip financing.

If an arrangement involves round tripping of funds, it will satisfy the tainted element test. Round trip finance has been explained in S.97(2). It includes an arrangement in which through a series of transactions:

– funds are transferred amongst parties to an arrangement, and

– transactions do not have any substantial commercial purpose

Normally, Round trip finance is a situation where funds are sent abroad by hawala channel, and these return as official money to India. Funds can come back as export sales, foreign investment, loans, etc. This is largely black money. Under FEMA, RBI has even considered round tripped ownership structure as round tripping. Thus for example, if an Indian company invests in Mauritius company, and the Mauritius company invests in another Indian company, it is round tripping. This is so even if the funds which have been invested abroad, have been used for Mauritius business. These are not invested in India. The profits of Mauritius company are invested in India.

Under GAAR, round trip finance can apply even for tax paid disclosed transactions and not just black money.

Further there is no need for funds to return to the same location from where the same were sent. Nor it is necessary for the funds to return to the person or persons in the group who sent the funds. Simply a series of transactions amongst parties to an arrangement can be considered as round trip financing if the two tests are satisfied. The provision further clarifies that following circumstances are not relevant:

– whether or not the funds involved in the round trip financing can be traced to any funds transferred to, or received by, any party in connection with the arrangement. (The link of funds is not required. Beginning and end in the series is not relevant.)

– the time, or sequence, in which the funds involved in the round trip financing are transferred or received. (A systematic or timely movement of funds is not relevant).

– the means by, or manner in, or mode through, which funds involved in the round trip financing are transferred or received. (How funds move is not relevant.)

This cannot be the objective but that is the language. The correct meaning should be that the funds return to the same place of the same person (or the group of the person is a part of). Then the "round" is complete.

"Series" has not been defined. The dictionary meaning is – a number of similar or related things... In my view, for GAAR, even two transactions will be considered as round tripping. Thus in the example of Mauritian investment, it will be considered as round tripping financing.

The key test is – does the series of transactions have commercial purpose? Commercial purpose has not been defined. One should take a common meaning. Practically it may be equated with commercial substance.

"Fund" has been explained in S. 102(5) to include cash, cash equivalents and right or an obligation to receive or pay cash or cash equivalent. It refers to liquid funds in form of cheques, negotiable instruments, etc. It does not include securities, mutual funds, etc.

Illustration – An Indian company invests abroad by exporting goods to the investee company. The foreign company invests in India by transfer of knowhow. Both these transactions are permitted under FEMA. Funds are not being remitted abroad or remitted to India. Legally this will not be round tripping. However one will be covered by other tainted element test – lack of commercial substance or abuse of law.

iv) Accommodating party

If an arrangement involves an accommodating party, again tainted element test will be satisfied. S. 97(3) explains that an accommodating party will be considered as such if the main purpose of direct or indirect participation of that party in an arrangement (whole or part) is to obtain a tax benefit for the assessee. It is not necessary that the accommodating party is a connected party or not. If there is an accommodating party or a connected person, then such persons can be ignored and the transaction can be considered to have been undertaken by the assessee itself. It may be noted that the implication of GAAR is on the assessee and not on the accommodating party or connected person.

Illustration – A Ltd. exports goods to X Ltd. in Dubai. X Ltd. is owned by a Dubai resident who is not connected to Mr. A. X Ltd. sells goods at a profit. The entire transactions are managed by A. Then after a few years, X Ltd. gives a loan to A Ltd. as an ECB. After 5 years, the loan is written off as A Ltd. is making losses and cannot repay the loan. Thus tax free profits made by A Ltd. and parked with X Ltd., comes back as tax free loan. X Ltd. will be an accommodating party. The accommodating party can be disregarded and A Ltd. can be considered as the assessee for the entire transactions.

"Connected person" is defined in S. 102(4). It is a very wide definition. The first limb itself states that it includes persons who are connected directly or indirectly. But in what manner? On what account? Due to which factor? And the definition states directly or indirectly. Relatives, etc. are included in the definition. The first phrase is simply without any connection to any tests!

Then it further states that connected persons include relatives, director of a company, partner of a firm, entity which has substantial interest by these persons or their relatives, etc. The definition is on the lines of S. 40A(2)(b) which deals with reasonableness of payment of expenditure to related persons.

"Relative" has been defined in S. 102(7) to mean persons defined in S. 56(2)(vi). It is a very broad list of relatives. One may note that it does not refer to the meaning of relative u/s. 2(41) which is a narrower definition.

"Substantial interest" has been defined in S. 102(8) to mean ownership of 20% or more in an entity. It is on the lines of the meaning in S. 40A(2)(b).

"Party" has been explained in S. 102(6) to include a person or a PE which participates or takes part in an arrangement.

v) Elements which have an effect offsetting or cancelling each other.

In an arrangement, where one transaction gives tax benefit, and the other transactions removes the effect of the first transaction, but the tax benefit continues to remain, it will be a tainted transaction.

Illustration – Co. A and Co. B have independent businesses. They decide to join together, merge their businesses, reduce competition and expand. However instead of establishing a new company, or merging, Co. A invests in share capital of Co. B to become 50% shareholder. Company B similarly invests in share capital of Co. A to become 50% shareholder. Both become 50% owners of combined business quickly without any tax implication. Can these two investments in each other be considered as elements cancelling each other?

Illustration – A loss making company (say L) sells goods to a dealer, which dealer then sells it to a profitable group company of L, whether one can say purchase and sale transactions offset each other?

vi) Transaction through one or more persons which disguise the value, location, source, ownership or control of funds which is the subject matter of transaction.

Illustration – An investment banker has provided advice from Hong Kong to an Indian resident. There is no DTA between India and Hong Kong. The amount will be taxable in India as FTS. However the documents are arranged by the investment advisor as if it has been rendered from UK. Under the India-UK DTA, the amount is not taxable. This transaction will be considered as tainted.

Illustration – A Discretionary Trust in UK has UK professional trustees. It invests in India and gets relief under the India-UK DTA. The trust is actually controlled by the Hong Kong resident and he is the beneficiary of the trust income. The owner is being disguised. This transaction will be considered as tainted.

vii) It involves the location of an asset or of a transaction or of the place of residence of any party which is without any substantial commercial purpose except obtaining a tax benefit.

Illustration - Mr. A is an Indian resident. He is expecting substantial gain from sale of his foreign assets. He becomes a non-resident, sells the foreign assets, and then returns to India. Here residence of Mr. A is involved. If there is no commercial purpose for Mr. A to become a non-resident, it will be considered as a tainted transaction. See para 5.1.3.

5.1.3 An issue which arises is that whether commercial substance has to be considered for an arrangement or for an entity / person?

For example, if an Indian resident has business in India. He closes the Indian business and starts the business in the foreign company. The foreign company is being operated with proper office, people and resources. It is however controlled from India by Indian owners. The turnover of foreign company does not exceed ₹ 50 crore and hence POEM guidelines do not apply. It is with substance. In this situation, should one see whether the arrangement has substance or the foreign company has substance?

The provision states that the arrangement should have commercial substance. Setting up a foreign company may have substance but the arrangement of transferring business abroad (whereby tax in India has been avoided) should have commercial substance.

This is one of the major differences issues under GAAR. Rearrangement of facts may not be sufficient to avoid GAAR if there is no commercial substance.

5.1.4 S. 97(4) provides that following factors shall be relevant but not sufficient to determine whether the arrangement lacks commercial substance:

- the period for which the arrangement exists.
- whether tax has been paid.
- whether exit route has been provided in the arrangement (exit can be by way of sale of investment, business, operations or activity).

In the previous version of GAAR, it was provided that the above factors were not relevant to consider whether an arrangement lacks commercial substance. As per Shome committee recommendation, the provision has been amended stating that the above factors will be relevant but not sufficient. Now the assessee can consider the above factors along with other factors to establish that there is a commercial substance.

Illustration – An investor from Netherlands had invested in India. He forms a Netherlands company for the purpose of investment. India-Netherlands has a beneficial DTA for capital gain where India cannot tax capital gain earned by a resident of Netherlands. After a few years, the promoter emigrates to UK but continues his investment in India through the Netherlands company.

In such a situation if the Netherlands company sells the shares of Indian company, it should be possible to establish that the investment was in India for many years. While that is not sufficient to establish that it has commercial substance, but the fact that investment was made while the promoter was a resident of Netherlands and he held the investment for several years before he migrated to UK, should be sufficient to establish that there was commercial substance.

5.2 Arm's length dealing

This test provides that if an arrangement creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length, this test will be satisfied [S. 96(1)(a)].

See example in para 5.3 below.

5.3 Misuse or abuse of provisions of this Act

This test provides that if any provisions of this Act (i.e., Income-tax Act) are misused or abused, then this test will be satisfied [S. 96(1)(b)].

For example, an Indian company purchases goods from a third party abroad at a price higher than the normal market price. As the parties are not Associated Enterprises, Transfer Pricing rules primarily do not apply. An SEZ unit of the Indian company sells goods to the third party at a price higher than the market price. Thus excess price paid by the Indian company (which results in excess expenditure), is received back in the SEZ unit (which is tax free income). This will be considered as abuse of law (SEZ unit relief). It can also be considered as creating rights or obligations which are not ordinarily created between persons dealing at arm's length (buying and selling at prices higher that market price).

5.4 *Bona fide* purpose

This test provides that if an arrangement is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for *bona fide* purposes, then the test is satisfied. [S. 96(1)(d)].

Illustration – A foreign company has an Indian subsidiary to which it outsources manufacturing work. All the material, process and knowhow are provided by the foreign company. The holding company pays third parties, charges for marketing expenses, sponsorship payments, etc. The arrangement provides that the subsidiaries will pay a certain share of these expenses to third parties (which the subsidiary does not need to). It will not be considered as an arrangement for *bona fide* purpose.

6. GAAR as additional provisions

S. 100 provides that the GAAR chapter applies in addition to or in lieu of any other basis for determining tax liability. Thus apart from other provisions, GAAR can also apply. GAAR can also apply in lieu (instead of) any other provisions.

This means that even if the person falls within a specific provision (e.g. he has complied with the provisions of Section 10AA, if the AO considers that the income shown is in excess of what would otherwise be, he can invoke GAAR and deny the benefit. In other words he can invoke GAAR, and apply the provisions in lieu of section 10AA.

What does "in addition to" mean? Does it mean that the AO can apply regular provisions and also apply GAAR? This would mean double tax. That cannot be the intention. Without an express provision, no income can be taxed twice. If GAAR is applied, the purported transaction is ignored and the correct transaction as perceived by the revenue is applied (known as counter factual).

Illustration – In an IAA, an Indian resident pays technical service fees to a non-resident and deducts tax @ 10%. Under GAAR, the expense is disallowed. The payer is charged to tax @ 30%. Will the non-resident payee get refund of tax? There is no provision for corresponding adjustment. Here one can say GAAR applies in addition to other provisions. Thus what has been paid as TDS remains. Plus GAAR will apply to the Indian resident and normal tax will be levied. CBDT has clarified in its circular (Question 13) that corresponding adjustment in another person's hands will not be made. GAAR is an anti-avoidance measure and adjustment across different taxpayers will go against the deterrence.

However in case of the same assessee, if the transaction is recharacterised, then tax will be levied as per recharacterised transaction. If any excess tax has been paid by the assessee under IAA, the same will be considered under recharacterised transaction. (GAAR applies to neutralise tax benefit. It is not to levy tax again.)

GAAR will apply in addition to SAAR.

8. Does GAAR seek to tax income where there is no taxable income?

Let us consider a few illustrations:

i) A person acquires shares at a value which is equal to the fair value u/s. 56(2) read with relevant rules (say ₹ 50). The true fair value value is ₹ 75. On purchase of shares at a low price, there is no income. Section 56 has deemed that if the purchase price is less than the specified fair value, the difference will be income. Section 56 is a deeming fiction. Can the AO allege that there is an income of ₹ 25 per share for the buyer? It is assumed that there is no cash dealing over and above the transaction price.

Section 56 is a Special Anti-Avoidance Rule (SAAR). It is true that GAAR can apply even if there is a SAAR. However on purchase, there is no income which can be taxed under the ITA. GAAR cannot presume any income, where there is none.

ii) An MNC has operating subsidiaries in Singapore and Indonesia. The Indonesian company is in the business of mining coal. The main activities happen in Indonesia. The Singapore company does billing for the entire MNC group. After collecting funds, it transfers the same to the operating companies and keeps a small margin for itself. It acts as the central point for the MNC billing. An Indian customer purchases coal from the MNC. The MNC delivers goods from Indonesia to the Indian buyer. The billing is however undertaken from the Singapore subsidiary. As the MNC does not have a PE in India, no income is taxed in India.

The MNC finds that the Indian market is growing and therefore it needs to set up a subsidiary in India. It invests in the Indian subsidiary from the Singapore company.

In this situation, GAAR cannot be applied on sales by the MNC just because the sales are from a company in a low tax jurisdiction. This is because even if it is assumed that Indonesian company is the real person selling the coal, the income would have been exempt in absence of a PE in India.

However when the investment is made from the Singapore company, the company will have to substantiate that the investment has not been made to avoid tax.

iii) Co. A borrows from its parent company abroad. Due to long gestation period of business, there are losses in the Indian company. Consequently, the parent writes off the loan. A write off of loan is a capital receipt and not income. Under GAAR, it is not possible to deem such a write off as receipt of sum without consideration liable to tax u/s. 56(2).

iv) An Indian resident is required to pay compensation to a non-resident who is a UK resident. The non-resident asks the resident to pay compensation to its group company in Netherlands. Compensation is usually not taxable being a capital receipt. However just because the amount is paid in an offshore centre, GAAR cannot be applied as the compensation *per se* is not taxable.

8. GAAR and TDS

Can GAAR apply to a payer for tax deduction at source? *Prima facie* GAAR applies to "tax benefit". Therefore whoever obtains a tax benefit, can be liable under GAAR.

To understand the issue further, one may divide the topic in two categories – i) one where payer has to bear the tax (and therefore gross it up), and ii) where the recipient has to bear the tax.

In the first situation, the payer can be liable under GAAR if he satisfies the test of IAA. Practically in case of third party dealings, it will be difficult for the payer to have an "arrangement" to save taxes. The recipient would not agree for it. Of course if the parties are related, then it may be easy to make an arrangement.

In the second situation, the payer would not like to take the responsibility for default in tax related to the recipient.

However let us consider the following illustrations:

Illustration – An Indian resident purchases shares of an Indian company from a Singapore company. For considering the relief under India-Singapore DTA, the payer will have to see that all the conditions are fulfilled – Singapore company has a TRC, it has incurred expenditure of S$ 2,00,000, etc. If all these conditions are satisfied, tax need not be deducted at source.

Illustration – An Indian company has set up a UAE company and books business in the UAE company. When an Indian resident client approaches this company, he is directed to the UAE subsidiary. The UAE subsidiary has staff, office, etc. However the staff takes instructions from the Indian Head Office. The place of effective management is in India. It may not satisfy the LOB clause of India-UAE DTA. The Indian client does not know this. In such a situation, what is the responsibility of the Indian payer? If the Indian payer takes due care and deals with the UAE staff, he may not be responsible for TDS default. If however he comes to know that the UAE operations are only to avoid taxes, then he should ask the UAE company to obtain a TDS certificate u/s. 197. If he does not deduct tax, then the Indian client can be responsible. This was the case in Vodafone where it was held responsible for non-deduction of tax at source. It was cautioned by the tax department before it paid consideration to Hutch that there could be a tax liability.

Therefore at the time of deduction of tax, payer has to carry out due diligence for the transaction to understand with whom he is dealing with.

9. Payment of foreign tax

An Indian company has set up a Singapore company and books business there. It has POEM in India but does not disclose it to the department. It does not pay tax in India but pays a tax of 10% in Singapore.

Later the department comes to know and applies GAAR. The department wants to levy full tax on the profits. The company claims that it has paid tax in Singapore and therefore the tax benefit in India after considering credit for Singapore tax is lower compared to what the department is alleging. Will it be correct?

Tax benefit has to be considered *qua* the Indian taxes. If the foreign company is an Indian resident, then it is liable to tax on its global income. If it has a proper PE in Singapore, then to that extent it can get credit for tax paid in Singapore. The balance tax payable in India can be considered as tax benefit. However just because tax has been paid in Singapore, it does not mean that it has to be considered as a deduction from the Indian tax.

Thus payment of tax abroad is not relevant by itself to consider the tax benefit in India.

10. CBDT Circular No. 7 dated 27-1-2017

CBDT has issued the above referred circular clarifying a few issues under GAAR. Following questions are relevant to this article.

10.1 Question 3 - Will GAAR interplay with the right of the taxpayer to select or choose method of implementing a transaction?

CBDT states in the answer that GAAR will not interplay with the right of taxpayer to select a method of implementing a transaction.

What does it mean? It means that if there is one or more *bona fide* ways of doing a transaction, then the taxpayer can select the manner he wants. GAAR will not come in between. (CBDT has not said GAAR will not apply. However the meaning should be that GAAR will not apply.) The illustration is of returning funds to the shareholder by way of dividend or buyback of shares. Both are legitimate ways of returning funds to shareholders. However both have different implications. In dividend, only funds are returned. In a buyback, the capital of a company is reduced. If it is a listed company, the liquidity in the market of the shares reduces. Just because a particular manner of returning funds to the shareholder reduces tax, it does not mean GAAR should apply. In essence commercial substance has to be satisfied so that GAAR may not apply.

To take another illustration, if the person has an option of setting up a unit in domestic area and an SEZ, and it chooses the SEZ, it does not mean GAAR can apply. (If the person shifts his existing business to SEZ unit, then GAAR can apply.)

10.2 Question 4 – If an FPI is based in a tax friendly jurisdiction for non-tax commercial reasons, will GAAR apply?

CBDT states that the situation will be examined based on the twin tests of tax benefit and tainted element tests in S. 96. If there are non-tax commercial reasons and tax benefit is not the main purpose, GAAR will not apply.

Thus again, one needs to satisfy the commercial purpose test of any arrangement.

11. Summary

The conditions and tests are very elaborate. Almost any situation which will have the effect of tax reduction, can be covered within GAAR. Therefore one must analyse the tax implication of any transaction very carefully before undertaking the same.

CA Siddarth Banwat

Implications of GAAR applicability

The overall scheme of GAAR provisions consists of two limbs. First limb is to identify the existence of an impermissible avoidance arrangement resulting into tax benefit and second limb empowers the revenue authorities to determine the consequences thereof. The consequence of application of the GAAR is significant as it operates on the doctrine of substance over form. The scope under section 98(1) provides an inclusive list of consequences. Section 98 provides for method of determination of consequences in relation to tax of an arrangement after it is declared to be an impermissible avoidance arrangement. It provides for certain illustrative but not exhaustive methods for determination of tax consequences. However, it also provides that once the arrangement is held to be impermissible, the consequences of the arrangement in relation to tax implication (including denial of benefit under a tax treaty) shall be determined in such manner as is deemed appropriate in the circumstances of the case. Thus, section 98 of the Act empowers the tax authority to evaluate the impermissible arrangement in substance and eliminate that part of an arrangement which is considered to be giving rise the undue tax benefit.

Section 98(1) of the Act provides power to tax authorities to deny tax benefit or a benefit under treaty. The consequences of impressible avoidance arrangement mentioned in section 98(1) of the Act are as under:

a) Disregarding, combining or recharacterising any step in, or a part or whole of, the impermissible avoidance arrangement;

b) Treating the impermissible avoidance arrangement as if it had not been entered into or carried out;

c) Disregarding any accommodating party or treating any accommodating party and any other party as one and the same person;

d) Deeming persons who are connected persons in relation to each other to be one and the same person for the purposes of determining tax treatment of any amount;

e) Reallocating amongst the parties to the arrangement any accrual, or receipt, of a capital or revenue nature; or any expenditure, deduction, relief or rebate;

f) Treating the place of residence of any party to the arrangement; or the situs of an asset or of a transaction, at a place other than the place of residence, location of the asset or location of the transaction as provided under the arrangement; or

g) Considering or looking through any arrangement by disregarding any corporate structure.

Section 98 of the Act provides wide powers to the tax authorities to determine tax consequences in case of impermissible avoidance arrangement. An arrangement may be disregarded in its entirety or the same may even be re-characterised.

Disregarding or re-characterisation of transaction

After identification of a transaction as impermissible avoidance arrangement, while applying provisions of GAAR and determining the implications, there could be two situations. First, where authorities cannot find an alternative transaction to identified impermissible transaction and hence, may disregard the transaction. Second, authorities may re-characterise the whole or even a part of a transaction.

In either of the scenario, a transaction may be real, but its characterisation or legal relation are not acceptable for tax purposes. The main principle in respect of such transactions is that the legal or contractual rights and obligations do not correspond to the characterisation of the transaction given by the taxpayer. The reason for disregarding transaction could be that the legal/contractual law elements of the transaction do not correspond to the essential tax characterisation provided by the taxpayer. For example, an assignment of running contract by profit making entity to loss making entity for no additional consideration may be disregarded as assignment is made only for utilisation of the losses against profits generated from the contract. The objective in transferring the contract under what appears to be a 'assignment' is such that the "loss making entity" has the availability of offset of profits against accumulated losses which would otherwise be lost due to expiry of the limitation period. Another example is the transfer of property to a partnership and later distribution of that property or money by the partnership to that contributor might be treated as disguised sale or exchange of property.

Tax benefit derived as a result of impermissible tax avoidance arrangement may be denied mainly by:

- re-characterisation of transaction;
- disregarding of transaction;
- reallocation of income amongst parties;
- disregarding any corporate structure.

Re-characterisation of transaction

One way to apply doctrine of substance over the form on a transaction is to re-characterise the transaction on account of the real substance according to applicable law. The intent of the parties is of paramount importance and therefore, re-characterisation cannot be done only with the objective to reach a favourable result. Characterisation by a taxpayer cannot disturbed unless the transaction is legally identifiable of other nature. For example, treatment of loan as equity or vice versa; dividend is treated as sale proceeds rather than dividend where dividend represents a recovery of the price paid for the shares and the payment of the dividend is either controlled by the shareholder or is a part of arrangement involving purchase of shares and payment of a dividend; a transaction involving issuance of compulsorily convertible instrument at a fixed conversion ratio; a transaction of sale and lease back. As a matter of fact, for determination of the nature of transaction for tax purposes, the form also matters. Availability of an alternative option may not automatically lead to alteration in characterisation for tax purposes. In other words, a mere subjective intention, is not by itself sufficient to alter the characterisation of transaction for tax purposes.

Thus, re-characterisation is possible on the principle of real substance. It is to be noted that intention of the parties under the contractual law play an important role in characterisation of the transaction. If it is not possible to re-characterise on the basis of real substance, then the re-characterisation/disregarding a transaction would be considered to be driven by the presumption of having a tax avoidance.

Characterisation of a payment requires both wide survey and an exact scrutiny of the taxpayer's activities[1] the label that the entity uses to characterise a payment is not determinative[2]. For example, a licence does not become a lease because the parties chose to call one, if it is in truth a licence[3]. A person does not cease to be an employee and become an independent consultant because the parties use the latter description[4]. An amount does not become interest, if the parties chose to adopt that word, if in law it is not[5].

Unlike the specific anti-avoidance, the GAAR does not expressly re-characterise transactions. Rather, it authorises the authorities to ignore other provisions in the Act or re-characterise the nature of amounts in a manner that denies the tax benefit sought. Therefore, GAAR could result into change in characterisation of a transaction even for the purposes of tax treaties. For example, GAAR could operate to redefine or re-characterise a income under the treaty on the basis of the meaning specifically given in the treaty as a definitional matter. Re-characterisation under the GAAR might include disregarding the existence of an entity or ignoring a particular transaction or provision of the Act. It is provided that GAAR can be applied to deny tax treaty benefits to non-resident taxpayer who would otherwise be entitled to them through improper use of treaty provisions. However, whether such denial of treaty benefit can be done despite having full-fledged measures under the provisions of the Act for obtaining treaty benefit (example: requirement to obtain tax residency certification, prescribed information in Form 10F etc) is a question. Therefore, GAAR could operate to redefine or re-characterise an amount, disregard the existence of an entity or ignore a transaction or the provision of Act.

When there is no specific anti-avoidance provision in law applicable to a transaction constituting an avoidance scheme, the denial of tax avoidance is achieved by denying artificial construction. The revenue authority in that case may re-characterise the transaction according to the true intention of the parties and apply the tax treatment accordingly. Such re-characterisation is based on fact finding and true intention and interpretation of the relevant provision.

However, in principle GAAR is not re-characterisation provision, but an anti-avoidance rule. The revenue authorities cannot re-characterise a transaction in order to determine whether GAAR could be applied, but rather, consequences would follow only once they are satisfied that the main purpose of the arrangement is to obtain a tax benefit. Therefore, re-characterisation is a consequence of GAAR and not a measure to invoke GAAR. Other provisions of the Act may be ignored or the nature of the amount re-characterised in a manner that denies the tax benefits sought. The GAAR could operate to re-define or re-characterise the amount, disregard the existence of an entity or ignore a transaction or the provisions of the Act.

Disregarding of transaction/structure

The GAAR provisions are more expansive than the court based anti-avoidance rules or the specific anti-avoidance provisions. There

1 Western Gold Mines (NL) vs. Commissioner of Taxation (1938) 59 CLR 729, and Spriggs vs. Commissioner of Taxation (2009) 239 CLR1
2 See Commissioner of Taxation vs. Broken Hill Ply Co. Ltd. (2000) 179 ALR 593
3 See Radaich vs. Smith (1959) 101 CLR 209
4 see Hannan & Allen vs. Australian Mutual Provident Society
5 see Noza Holdings Pty ltd. vs. Commissioner of Taxation [2012] 18 taxmann.com 237 (FC-Australia)

are specific provisions under the Income-tax Act. These doctrines together can be referred as doctrine of *"fraus legis"* or "fraud against the tax laws". Meaning thereby, that a business transaction is undertaken in a manner appearing to be lawful, but designed to achieve a result which the law does not intend. The elements entering into a transaction involving fraud against law are: a legal transaction under a lawful form and the intent to cheat the provisions of law. It is avoidance motive and contravention of the purpose and intent of the law. Application of the fraus legis doctrine means that a set of facts is converted with the purpose and intent of the relevant tax legislation becomes possible, which may mean that certain lawful actions are not taken into considerations. It includes ignoring of lawful actions or transactions. Thus, it is pertinent to understand that the applicability of the provisions of GAAR doesn't result into a transaction being declared as illegal. Rather, under GAAR only the nature of the transaction is realigned based on the intent and substance of the applicable law.

If a taxpayer arranges its affairs in such a manner that he remains within the purview of law but still avoids through a transaction which offends or runs contrary to the intention or purpose of the subject provisions, the GAAR provisions would become effective. Where there are specific provisions which give benefits to the taxpayer (like setting up a business unit in SEZ or industrially backward area) and the taxpayer avails of them, there cannot be an avoidance. But where the arrangement does not attract the benefit conferred by the specific provision but is an arrangement which sought to divert income from one taxpayer to another, or where the arrangement is artificial, contrived or out of the ordinary, this might indicate that the arrangement is one to avoid tax with the consequence that applying the provisions of GAAR, such transaction could be disregarded notwithstanding the legal structure.

If the transactions are preordained which lack commercial contents, and are inserted with the sole object of tax avoidance these could be disregarded. The disregard of transactions for fiscal purposes means fiscal nullity. Transactions in a series of transactions are preordained only first of them is entered into, the taxpayer is in a position for all practical purposes to ensure that the second is also entered into. The question is whether an intermediate transaction is, at the time that it is effected - so closely connected with the ultimate disposition that it is properly described as not in itself a real transaction at all, but merely an element in some different and larger whole without independent effect. Secondly a commercial motive appears to be sufficient to protect a scheme from the operation of the new doctrine.

The doctrine of preordained series of transaction was propounded by Lord Brightman in *Furniss vs. Dawson [1984] 1 All ER 530 (HL).* A preordained series of transactions (whether or not they include the achievement of a legitimate commercial end) into which there are inserted steps that have no commercial purpose apart from the avoidance of a liability to tax which in the absence of those particular steps would have been payable seems to be the language expressing with perfect precision the concepts of steps which are formal rather than substantial. In *M. T. Ramsay Ltd. vs. Inland Revenue Commissioners (1981) 1 ALL 65* it was held that the Revenue or the Court must look at a document or a transaction in a context to which it proper belongs. It is the task to ascertain the legal nature of the transaction and while doing so it has to look entire transaction as a whole and not to adopt a dissecting approach. The Revenue cannot start with the question as to whether the impugned transaction is a tax deferment/saving device but that it should apply the look at test to ascertain its true legal nature[6]. In case of *Vodafone International Holdings*

6 See Craven(lnspector of Taxes) vs. White Stephan) (1988) 3 All ER 495

vs. Union of India [2012] 17 taxmann.com 202 (SC), Justice S. H. Kapadia observed:

> *"… Holding Structures are recognized in corporate as well as tax laws. Special Purpose Vehicles (SPVs) and Holding Companies have a place in legal structures in India, be it in company law, takeover code under SEBI or even under the income tax law.*
>
> *When it comes to taxation of a Holding Structure, at the threshold, the burden is on the Revenue to allege and establish abuse, in the sense of tax avoidance in the creation and/ or use of such structure(s). In the application of a judicial anti-avoidance rule, the Revenue may invoke the "substance over form" principle or "piercing the corporate veil" test only after it is able to establish on the basis of the facts and circumstances surrounding the transaction that the impugned transaction is a sham or tax avoidant. To give an example, if a structure is used for circular trading or round tripping or to pay bribes then such transactions, though having a legal form, should be discarded by applying the test of fiscal nullity. Similarly, in a case where the Revenue finds that in a Holding Structure an entity which has no commercial/business substance has been interposed only to avoid tax then in such cases applying the test of fiscal nullity it would be open to the Revenue to discard such inter-positioning of that entity.*

Thus, the courts have been upholding the revenue's right to disregard the consequences of the transactions even in respect of those which are genuinely undertaken if their purpose is to avoid tax that would otherwise be payable. The taxing authority is entitled and is indeed bound to determine the true legal relationship resulting from a transaction[7]. In order to determine whether a transaction of creating the partnership is a sham or illusionary transaction or a device or ruse, the Income-tax Officer is entitled to penetrate the veil covering it and ascertain the truth. This he can also do even where the partnership is genuine[8]. Law permits the courts to lift the corporate veil in ascertain "business realities" and in order to ascertain where the real control and beneficial undertaking lay. The decisions of the Supreme Court in *Juggilal Kamlapat vs. CIT [1969] 73 ITR 702* and *Chandulal Harjiwandas vs. CIT 1967] 63 ITR 627* are the examples where the court has lifted the corporate veil as the as the conception of corporate veil was used for tax evasion or to circumvent the tax obligation. The Supreme Court has upheld the right of the tax authorities to go behind the corporate facade to look at the economic realities of transactions, if the shell of the corporate entity is used for tax evasion or to circumvent tax obligations.[9]

In this context of the powers to disregard a structure or to reallocate the income in the hands of the transacting parties, the importance of the terms accommodating party which included connected persons are important. Section 99 of the Act provides for treatment of connected person and accommodating party. As per section 99 of the Act, in determining whether a tax benefit exists, the parties who are connected persons in relation to each other may be treated as one and the same person. Another consequence of impermissible avoidance arrangement is that income or expenditure may be reallocated among the parties to arrangement.

Connected persons may be regarded as one and the same person. The term 'connected person' has been defined under section 102(4) of the Act to mean any person who is connected directly or indirectly to another person and further provides

7 Workmen of Associated Rubber Industry Ltd. vs. Associated Rubber Industry Ltd. [1986] 157 ITR 77 (SC), CIT v. Durga Prasad More [1971] 82 ITR 540 (SC) and CIT vs. L.N. Dalmia [1994] 207 ITR 89 (Cal.)

8 Sunil Siddharthbhai vs. CIT [1985] 156 ITR 509 (SC) and also CIT vs. Smt. Padma S. Acharya [1996]

9 Juggilal Kamlapat vs. CIT [1969] 73 l TR 702 (SC); CIT vs. Sri Meenakshi Mills Ltd. [1967]63 ITR 609 (SC); Union of India vs. Gosalia Shipping (P) Ltd. [1978] 113 ITR 307 (SC)

an inclusive list of persons who would be regarded as connected persons. The inclusive definition of the term implies a wider scope of the definition not limiting the meaning to what is stated in the definition. The specific categories of persons who would be regarded as connected persons are given in the table below.

Individual	Relative of individual
Company	Director of company or relative of such director
Firm	Partner of firm or relative of such partner
AOP / BOI	Member of firm or relative of such member
HUF	Member of HUF or relative of such member
Any person	Any individual who has a substantial interest in the business of the person or any relative of such individual
Any person	Company / firm / AOP / BOI / HUF having a substantial interest in the business of the person or any director, partner, or member of the Company / firm / AOP / BOI / HUF, or any relative of such director, partner or member
Any person	Company / firm / AOP / BOI / HUF whose director, partner or member has a substantial interest in the business of the person, or family or relative of such director, partner or member
Individual or relative of Individual	Any other person who carries on business if such individual or relative of individual has a substantial interest in the business of that other person
Company/firm/AOP/BOI/ HUF or any director, partner or member of such company/ firm/AOP/BOI / HUF or any relative of such director, partner or member	Any other person who carries on business if such person has a substantial interest in the business of that other person

The term 'relative' has been defined under section 102(7) of the Act to have the same meaning as assigned in the Explanation to clause (vi) of sub-section (2) of section 56 of the Act. As per the said Explanation, relative means –

i. spouse of the individual;

ii. brother or sister of the individual;

iii. brother or sister of the spouse of the individual;

iv. brother or sister of either of the parents of the individual;

v. any lineal ascendant or descendant of the individual;

vi. any lineal ascendant or descendant of the spouse of the individual;

vii. spouse of the person referred to in clauses (ii) to (vi);

The categories of persons to be regarded as 'connected persons' as per section 102 of the Act are similar to the categories specified under section 40A(2)(b).

Re-characterisation of a step or part of a whole of the transaction

Section 98 provides that the GAAR would be usefully applied in to *"any step in, or a part or whole of it (transaction)"* to which the parties have given a "characterisation", that is aimed at tax avoidance. In a tax avoidance arrangement, a transaction is artificially broken into a number of successive acts, conceived from the outset as forming a part of an inseparable chain. Thus, under the provisions of GAAR, the revenue authorities have power alter the transaction on the basis of a legal characterisation that is given to each of the legal acts taken separately, by disregarding, combining, re-characterising or a par or whole of it. It is not necessary the entire arrangement and all the steps are disregarded or re-characterised.

The provision is legal recognition of the step by step doctrine as laid down by the House of Lords in *IRC vs. Ramsay [(1981) STC 174]* and developed in *Furniss vs. Dawson [(1984) STC 153]* and elaborated in *Craven vs. White [(1988) STC 476].* When the intermediate transactions have been inserted for the purpose of tax avoidance, the Commissioner would consider the parties legal situation as it was prior to the first step and the last step and give the transaction as a whole a legal characterisation, without having regard to hat of each step consider individually or in combination. The first question in that case would be whether the series of transaction are pre-ordained; and then the second were the legal characterisation given by the parties aimed at avoiding the tax. Affirmative answer to both the questions, would lead to the third question, can the transaction thus determined be given a legal characterisation that correctly accounts for the legal position of the parties. The taxpayer, at this stage, may, however, avoid the application of GAAR by justifying that obtaining the tax benefit was not the main purpose of the arrangement and the transactions were *bona fide* and with commercial substance.

Characterisation of income

The basis for identifying an impermissible avoidance arrangement is to identify the transaction actually undertaken i.e. its nature and structure. Nature is characterisation, and structure is the form. The characterisation and the form of the transaction actually undertaken by the parties should not be disturbed, except in exceptional circumstances. Income is determined on the basis of transaction as structured by the parties. But in some cases, such structure is not *bona fide*. In other words, independent parties would have not acted in the similar structure. Independent parties would not have agreed to the structure where the economic substance differs from the form and/or where the form and substance being the same, the agreement behind the transaction is different to what could be found at arm's length.

The revenue authority may re-characterise or re-structure the transaction according to the substance. The structured adopted by the taxpayer can be disregarded if the economic substance differs from its form. Party's characterisation is ignored and re-characterised according to its substance. Further, even the place of residence of any party to arrangement or situs of an asset or transaction may be treated at a place different from the place of residence or location as provided in the arrangement.

"Determination" of tax consequences

Section 98(1) provides for the determination of tax consequences after an arrangement having been declared impermissible tax avoidance arrangement. The word "determine" means ending of a controversy by a decision of the authority judicial or authoritative decision. It is not a mere opinion or finding. While determining the tax consequences of impermissible tax avoidance on the basis of the objective fact that the main purpose of the arrangement is to obtain tax benefit and that such tax benefit is inconsistent with the object, spirit or purpose of the provisions relied upon by the taxpayer - there is a requirement for the officer concerned to determine its implication on the tax.

Steps required under the GAAR identifies the objective conditions and then makes a determination of the consequences of the impermissible avoidance arrangement by denying the tax benefit. It relates to denial of tax benefit and not make an assessment of the income. Section 98, therefore, uses the word "determined" for fixing the tax liability. A transaction is assessed, firstly on the basis of its legal substance i.e. whether it constitutes sham. If this test is met, the transaction subjected to the relevant statutory anti-avoidance provisions and, finally, the provisions relied upon by the taxpayer is construed in the light of the scope and intent of the Act in order to determine whether the transaction falls within them. Provided, it does, however, the transactions stands - regardless of whether it was solely or principally tax motivated.

The application of the GAAR involves three steps. It must be determined:

a) whether the main purpose of the arrangement is to obtain tax benefit

b) whether the transaction is an avoidance transaction in the sense of lacking commercial substance or not being a ranged primarily for bona fide purposes other obtain the benefit and

c) whether there was misuse or abuse of the provisions of the Act, in the sense that it cannot be reasonably concluded that a tax benefit would be consistent with the object, spirit or purpose of the provisions relied upon by the taxpayer

The determination of the existence of a tax benefit and an avoidance transaction involves a factual decision. As such, the burden of the same as in any tax proceeding where the taxpayer disputes the revenue's assessment and its underlying assumption of facts. The initial obligation is on the refute or the revenue's factual assumptions by contesting the benefit or by showing *bona fide* non-tax purpose primarily drove the transaction. Presumption alone, without any basis, is not sufficient to establish tax avoidance. If there are no grounds on which tax authority could have presumed tax avoidance or in presuming he has not applied his mind, he could be said to his power in violation of principle of natural justice.

To summarise, the ultimate impact of invoking GAAR provisions is intended to be on the tax benefit arising on account of an impermissible avoidance arrangement and to give effect to eliminate the portion of tax benefit, remedy could be towards the transaction itself (i.e. re-characterisation, disregarding a step or part therein etc.) or denial of tax benefit directly.

"The difference between what we do and what we are capable of doing would suffice to solve most of the world's problem."

— *Mahatma Gandhi*

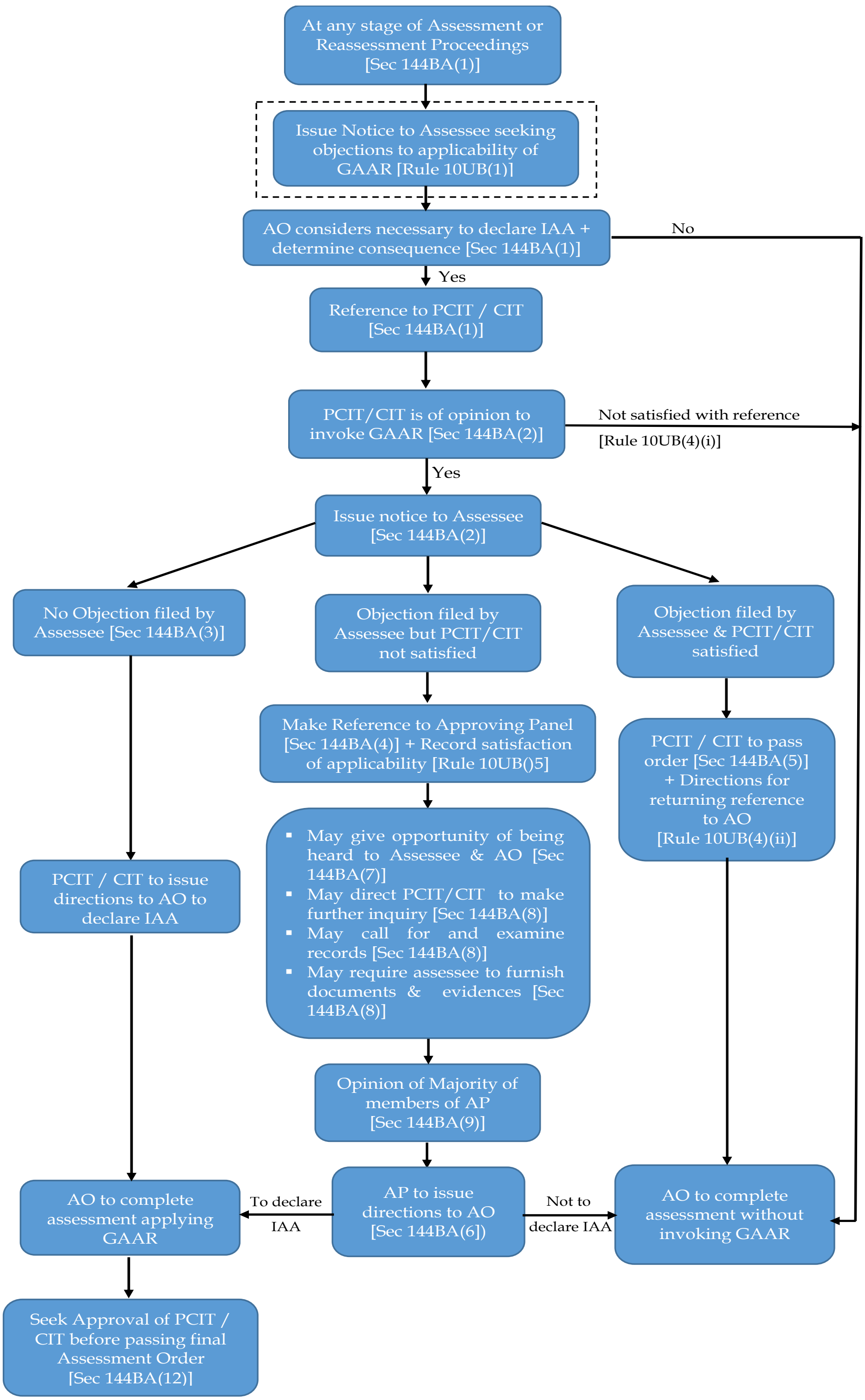
 

CA Harshal Bhuta & CA Tanvi Vora

Guidelines and rules under GAAR

The procedure for invoking Chapter X-A and thereafter determining tax consequences is contained under Section 144BA read with Rule 10UA, Rule 10UB and Rule 10UC. Section 144BA was initially inserted by the Finance Act, 2012 with effect from 1-4-2014 to provide for procedure to invoke provisions of Chapter X-A. Section 144BA was subsequently amended by Finance Act, 2013 and its applicability was also deferred to 1-4-2016 consequent to deferral of applicability of Chapter X-A. The Finance Act, 2013 amended section 144BA on various counts, the important ones dealing with (a) the binding nature of directions issued by the Approving Panel and (b) on strengthening the constitution of Approving Panel.

Section 144BA gives an elaborate procedure for invoking Chapter X-A. Before making an analysis of the various procedural regulations, a simplified snapshot of the procedure is presented below by way of a flowchart. The flowchart depicts the various steps involved in the procedure from making a reference to the Principal Commissioner of Income Tax ('PCIT') or Commissioner of Income Tax ('CIT') by the Assessing Officer ('AO') to passing of final order by him.


At any stage of Assessment or Reassessment Proceedings [Sec 144BA(1)]
Issue Notice to Assessee seeking objections to applicability of GAAR [Rule 10UB(1)]
AO considers necessary to declare IAA + determine consequence [Sec 144BA(1)]
No
Yes
Reference to PCIT / CIT [Sec 144BA(1)]
PCIT/CIT is of opinion to invoke GAAR [Sec 144BA(2)]
Not satisfied with reference
[Rule 10UB(4)(i)]
Yes
Issue notice to Assessee [Sec 144BA(2)]
No Objection filed by Assessee [Sec 144BA(3)]
Objection filed by Assessee but PCIT/CIT not satisfied
Objection filed by Assessee & PCIT/CIT satisfied
Make Reference to Approving Panel [Sec 144BA(4)] + Record satisfaction of applicability [Rule 10UB()5]
PCIT / CIT to pass order [Sec 144BA(5)] + Directions for returning reference to AO [Rule 10UB(4)(ii)]
May give opportunity of being heard to Assessee & AO [Sec 144BA(7)]
May direct PCIT/CIT to make further inquiry [Sec 144BA(8)]
May call for and examine records [Sec 144BA(8)]
May require assessee to furnish documents & evidences [Sec 144BA(8)]
PCIT / CIT to issue directions to AO to declare IAA
Opinion of Majority of members of AP [Sec 144BA(9)]
AO to complete assessment applying GAAR
To declare IAA
AP to issue directions to AO [Sec 144BA(6)]
Not to declare IAA
AO to complete assessment without invoking GAAR
Seek Approval of PCIT / CIT before passing final Assessment Order [Sec 144BA(12)]

The table below presents the time limits involved in the assessment procedure where provisions of Chapter X-A are to be invoked:

Section / Rule	Step	Time limit	Prescribed Form
Applicable to Assessing Officer:			
Sec 144BA(1)	Make reference to PCIT / CIT to invoke	At any stage of assessment or reassessment proceedings	Form 3CEG
Applicable to PCIT / CIT:			
Sec 144BA(2) r.w. Rule 10UB(4)(i)	Issue of directions by the PCIT / CIT to the AO where PCIT / CIT is satisfied that provisions of GAAR are not required to be invoked considering the reference received from the AO	Rule 10UC(1)(iii)(a) → 1 month from the end of the month in which reference is received by the PCIT/ CIT from the AO	Form 3CEH
Sec 144BA(2)	Furnishing of objections by assessee in response to notice of the PCIT / CIT	Sec 144BA(2) → Within time period specified in the notice subject to maximum of 60 days	—
Sec 144BA(3)	Issue of directions by the PCIT / CIT where no objections are received from the assessee in response to the notice issued	Rule 10UC(1)(i) → 1 month from the end of the month in which date of compliance of notice of PCIT / CIT falls	—
Sec 144BA(5) r.w. Rule 10UB(4)(ii)	Issue of directions by the PCIT / CIT to the AO where PCIT / CIT is satisfied that provisions of GAAR are not required to be invoked considering the reply of the assessee	Rule 10UC(1)(iii)(b) → 2 months from the end of the month in which the final submission of the assessee in response to notice issued by the PCIT / CIT is received	Form 3CEH
Sec 144BA(4)	Reference by the PCIT / CIT to the Approving Panel after recording satisfaction of applicability of GAAR provisions	Rule 10UC(1)(ii) → 2 months from the end of the month in which the final submission of the assessee in response to notice issued by the PCIT/ CIT is received	Form 3CEI
Applicable to Approving Panel			
Sec 144BA(6)	Issue of directions by the Approving Panel	Sec 144BA(13) → 6 months from the end of the month in which the reference from PCIT / CIT is received excluding: • Period for getting inquiries conducted through competent authority under Double Taxation Avoidance Agreements or one year, whichever is less	—

Section / Rule	Step	Time limit	Prescribed Form
		• Period during which proceeding of the Approving Panel is stayed by an order or injunction of any court Where the above exclusions leave a time period of less than 60 days for the issue of directions, the remaining period shall be extended to 60 days	—
Applicable to Assessing Officer – For Passing Final order			
Sec 144BA(12)	AO to pass final order pursuant to directions issued by PCIT / CIT or Approving Panel after seeking prior approval of PCIT / CIT u/s. 144BA(12))	Sec 153 → Within over limit as specified in section 153 (<u>which excludes</u> the period commencing from the date of reference received by PCIT / CIT u/s. 144BA(1) and ending on the date of direction under 144BA(3) or 144BA(6) or order 144BA(5) is received by the AO)	—

Analysis of procedural regulations have been made hereunder stage wise:

A. Sec. 144BA(1) – Reference by AO to PCIT/CIT

This sub-section deals with reference that AO can make to the PCIT or CIT as the first step towards invoking Chapter X-A. Since this sub-section provides the threshold that AO needs to cross before making reference to PCIT/CIT, this sub-section has been analysed in greater detail.

There are various important terms that need deliberation under this sub-section. These have been analysed below:

i. <u>"At any stage of assessment or reassessment proceedings"</u>: The expression 'assessment proceedings' or 'reassessment proceeding' has not been defined under the Income Tax Act, 1961. Instead, the word 'assessment' has been defined u/s. 2(8) to simply include 'reassessment'. This definition is of little help in understanding the expressions. It is for this reason that the meaning of 'assessment proceeding' has been disputed repeatedly and been the subject matter of several judicial decisions. Having regard to the provisions regarding procedure for assessment as contained under Chapter XIV of ITA, Supreme Court[1] has explained that the process of assessment involves (i) filing of the return of income under section 139 or under section 142 in response to a notice issued under section 142(1); (ii) inquiry by the AO in accordance with the provisions of sections 142 and 143; (iii) making of the order of assessment by the AO under section 143(3) or section 144; and (iv) issuing of the notice of demand under section 156 on the basis of the order of assessment. Therein, while dealing with the interpretation of time period

1 In Auto & Metal Engineers vs. Union of India [1998] 229 ITR 399 (SC)

allowed for completion of assessment u/s. 153 of ITA, it held that the expression 'assessment proceeding' must be construed to comprehend the entire process of assessment starting from the stage of filing of the return under section 139 or issuance of notice under section 142(1) till the making of the order of assessment under section 143(3) or section 144.

The words 'reassessment proceeding' may be interpreted accordingly. It may be relevant to mention here that the reassessment proceedings may have been initiated based on certain reasons recorded prior to issue of notice u/s. 148(2) which may be different from those compelling the AO to make reference under Chapter X-A. This is expressly sanctioned under Explanation 3 to Section 147.

Further, the phrase 'at any stage of assessment or reassessment proceedings' denotes pendency of the assessment or reassessment proceedings. In other words, the time period for assessment or reassessment proceedings must be open during which the AO can make a reference. It may be noted here that in accordance with Explanation 1(xi) to Section 153, once reference has been made by AO to PCIT/CIT, the period commencing therefrom till receipt of direction from PCIT/CIT or Approving Panel ('AP') is excluded from computing the period of limitation given under Section 153 for completion of assessment / reassessment proceedings.

Although the procedure for assessment is contained under Chapter XIV and Chapter XIV-B of ITA, it may be relevant here to examine whether different proceedings envisaged under ITA could also be covered within the scope of 'assessment / reassessment proceedings'.

a. *Assessment proceeding against representative assessee*: The object of assessing the income of the non-resident in the hands of the representative assessee is on account of the fact that it is quite often difficult to recover the tax from the non-resident. Section 166 of ITA confers powers on the AO to assess either the representative assessee or the principal assessee to whom the income has accrued. If the revenue department is of the opinion that the agent is to be taxed as a representative assessee, then it would call upon the agent to file a return and only thereafter the agent could be taxed as a representative assessee. Once the revenue department chooses to tax such agent as a representative assessee of the non-resident, in accordance with Section 161(1), tax shall be levied upon and recovered from such 'representative assessee' *<u>in like manner and to the same extent</u>* as it would be leviable upon or recoverable from the non-resident. It may be noted here that Section 161 makes a 'representative assessee' liable only as regards the income in respect of which such agent is a representative assessee viz. income of the non-resident. Further, under Section 162(1), every 'representative assessee' has the right to recover the amount of income tax paid on behalf of the non-resident from such non-resident. Alternatively, the representative assessee can retain the amount of income tax from the amount payable to the non-resident. In case of a disagreement between the representative assessee and the principal for the amount to be retained by the representative assessee for discharging the liability of income tax, such representative assessee can obtain a certificate from the AO u/s. 162(2) stating the amount to be retained pending final settlement. Once such certificate is obtained, the AO cannot recover an amount more than the amount specified in the certificate.

From a plain reading of the provisions dealing with the liability of the representative assessee u/s. 161, it seems that Sec. 144BA(1) would cover within its scope the assessment proceeding against the 'representative assessee' too since the representative assessee is considered to have beneficially earned the income which in fact would be accruing to the non-resident. Similarly, within the contours of Section 161(1), assessment is also made in the name of 'representative assessee' though deemed to be in the representative capacity only. However, for want of material and evidence in the possession of such representative assessee, practical considerations may weigh against invoking Chapter X-A during the assessment proceeding against representative assessee. Secondly, the amount to be retained by the representative assessee as certified by the AO may not have taken into account the tax consequences arising out of declaration of an arrangement as an impermissible avoidance arrangement because the AO could not have made reference u/s 144BA(1) for invoking provisions of Chapter X-A at the time of issuance of such certificate for want of pendency of assessment proceeding at the time of application for certificate.

b. *TDS recovery proceedings u/s. 201(1):* Section 201 deals with consequences of failure to deduct tax or pay tax upon deduction. While deciding a case under the provisions of the Income-tax Act 1922, Supreme Court[2] has observed that every order which contemplates computation of income for determination of the amount of tax payable is not an order of assessment within the meaning of the Income Tax Act of 1922 nor does prescribing of procedure for determining and imposing tax liability make it an order of assessment. When the liability to pay tax arises not from the charge created by statute, but from the order of the Income-tax Officer itself, the order so made is not an order of assessment. In other words, if the liability to pay tax arises on account of charging provisions rather than machinery provisions, an order determining the tax liability would be called an order of assessment. A person is liable to pay tax on income earned by him on account of charge of income tax created under the statute on such income. Whereas tax is required to be deducted on payment of such income by another person under the machinery provisions of ITA and if such other person fails to deduct tax on such payment, then tax on such payment can be recovered from the person making the payment yet again under the machinery provisions of ITA rather than provisions creating a charge. Since proceedings under Section 201(1) are merely machinery provisions, an order holding the deductor as an assessee-

2 In M.M. Parikh, Income Tax Officer vs. Navanagar Transport and Industries Ltd. [1967] 63 ITR 663 (SC)

in-default would not amount to an assessment order and accordingly, the proceedings too would not amount to assessment proceedings. Therefore, AO cannot make a reference for invoking provisions of Chapter X-A during pendency of proceedings u/s. 201(1). As a corollary, since no assessment proceedings are pending at the time of determination of liability to deduct tax under Section 195, the question of making a reference by AO for invoking provisions of Chapter X-A while adjudicating under Section 195(2)/195(3)/197 is ruled out[3].

c. *Penalty proceedings:* It is possible for an assessee to lead evidence which is independent of the evidence led in one or the other proceeding, i.e., the assessee is entitled to lead further evidence in penalty proceedings over and above the evidence placed in assessment proceedings. Therefore, one may encounter a situation wherein the assessee would have placed additional material on record during penalty proceedings and the AO may want to make a reference for invoking provisions of Chapter X-A having regard to such material. It may be noted here that Gujarat High Court[4] has categorically held that assessment proceedings and the penalty proceedings are quite distinct and different and that the term assessment cannot encompass penalty proceedings under ITA. Therefore, AO cannot make a reference for invoking provisions of Chapter X-A during the pendency of penalty proceedings.

An arrangement may involve various parties[5] physically located at different places. The jurisdiction of assessment of such parties may also vary[6]. Simultaneously, the tax benefit may differently accrue to different parties and so could be the resultant tax consequences that may be determined respectively for each party. Under such circumstances, it may not be incorrect to assume that individual references should be made by the AO during respective assessment / reassessment proceedings. To put it differently, reference by AO to jurisdictional PCIT/CIT during assessment /reassessment proceeding of one of the parties to the arrangement should not be treated as an automatic valid reference for other parties to the arrangement too. Inevitably, this would also have bearing on the tax consequences, if any, to be determined for each party to the arrangement.

ii. *"Having regard to"*: A simple meaning of the phrase would be 'to take into account or consideration'. However, it could be better appreciated when viewed in light of the change in language of statute under Sec. 92CA(4) *vide* Finance Act 2007. Section 92CA(4) deals with computation of total income of the assessee after receipt of order of TPO. Under Sec. 92CA(4), the words 'having regard to' were replaced by the words 'in conformity with' w.e.f. 1-6-2007. Referring to the decision of

3 This can further be supported by referring to the Supreme Court observation in the case of Vodafone International Holdings B.V. [2012] 341 ITR 1 (SC) that liability to deduct tax is different from assessment under the Act.

4 In CIT vs. Parmanand M. Patel [2005] 278 ITR 3 (Gujarat)

5 As defined u/s. 102(6) of ITA.

6 Although from news reports, it can be gathered that Income Tax Department may launch jurisdiction free e-assessments shortly. Source: http://www.business-standard.com/article/economy-policy/i-t-dept-to-launch-jurisdiction-free-assessment-from-oct-117091401557_1.html.

Supreme Court[7] in the context of Wealth Tax, the Delhi High Court[8] then had interpreted the words 'having regard to' to mean that the AO could take into consideration any other material placed before him by the assessee in addition to and instead of solely relying upon the order of the TPO. In other words, the order of TPO was not binding or conclusive or decisive for the AO and he could take into account other materials before passing the order of assessment. After the change in text of the statute, it emerged that the AO would not have such an option now and that the order of TPO would become binding upon him for computation of total income.

iii. "<u>Considers"</u>: Supreme Court[9] has interpreted the word 'consider' to mean to think over. It connotes that there should be active application of the mind. In other words, the term 'consider' postulates consideration of all the relevant aspects of the matter.

iv. <u>"Necessary"</u>: Again, Supreme Court[10] in the same case has interpreted the word necessary to mean indispensable, requisite; indispensably requisite, useful, incidental or conducive; essential; unavoidable; impossible to be otherwise; not to be avoided; inevitable.

v. <u>"May"</u>: Use of the word 'may' under section 144BA(1) denotes discretion in the hands of the AO.

Once the meaning of the various terms used u/s. 144BA(1) have been appreciated, one could progress to analyse the burden of proof for invoking Chapter X-A. Rephrasing the text of Section 144BA(1) with the meanings as understood above, Section 144BA(1) would signify that the AO should make a reference to PCIT/CIT only if he finds it inevitable to invoke Chapter X-A post his active application of mind by taking into consideration the material and evidence placed before him during assessment or reassessment proceedings. The phrase 'considers that is it necessary' gains importance in light of the meanings ascribed to the words therein raising the threshold for making a reference to PCIT/CIT. It denotes that active application of mind is significant and absolutely essential before making a reference and that such reference cannot be based on conjectures and surmises. This view becomes more evident when one refers to the text of Rule 10UB(1) and 10UB(2) where the AO is mandated to issue a notice to the assessee seeking objections for invoking Chapter X-A[11]. Moreover, such notice has to set out concrete basis and reasons for alleging as to why an arrangement satisfies the pre-requisites of Section 96 and also list the documents and evidences relied upon to make such an allegation. Only if the AO finds it indispensable to make a reference after an opportunity has been given to the assessee for rebuttal, should he make one. This implies that the burden of proof lies initially with the AO and that he has to cross a high threshold before making a reference to PCIT/CIT[12]. It is perplexing at this stage to comprehend use of the word 'may' towards the end of Section 144BA(1) especially when one reaches the conclusion that AO could make a reference only if he finds it indispensable[13]. Once he has made up his mind that it is essential to make a reference, any discretion given to him thereafter would become meaningless.

7 In Juggilal Kamlapat Bankers vs. W.T.O. [1984] 1 SCC 571

8 In Sony India (P.) Ltd. vs. CBDT [2007] 288 ITR 52 (Delhi)

9 In Bhikhubhai Vithalbhai Patel vs. State of Gujarat AIR 2008 SC 1771

10 Ibid

11 The issuance of notice seeking objections of assessee has not been specified u/s. 144BA(1).

12 Contrast with presumption u/s. 96(2) for pre-supposing obtaining tax benefit as the main purpose of an arrangement.

13 Perhaps the word 'may' should be read as 'shall'.

As indicated in the timelines above, reference by AO to PCIT/CIT is required to be made in Form 3CEG. Certain inconsistencies in Form 3CEG are listed below:

Point number	Description	Inconsistency
General	Reference to Commissioner under Rule 11UB and Form 3CEG	References to Commissioner have not been updated yet to include Principal Commissioner post amendment under Income Tax Act *vide* Finance (No. 2) Act, 2014 w.r.e.f. 1-6-2013
5(b)	Assessment years proposed to be covered other than those for which proceedings are pending	Reference u/s. 144BA(1) could be made only where assessment proceedings are pending
6	Factual matrix of the arrangement including details of other parties	The assessee may be in a position to give details only to the best of his knowledge and may not himself have a complete picture of the arrangement
10	Whether notice under Rule 10UB(1) has been served? If yes, date of service of notice	It projects as if issuance of notice to assessee is not mandatory before making a reference to PCIT/CIT
14	Consequences in relation to tax likely to arise if arrangement is declared as impermissible avoidance arrangement	The determination of tax consequences arises after declaration of an arrangement as impermissible avoidance arrangement. Therefore, seeking this information in Form 3CEG may give an impression of impropriety in making the decision of whether provisions of Chapter X-A need to be invoked. However, for seeking such information, benefit of doubt may be accorded to the fact that tax benefit in the first place cannot be estimated if the tax consequences are not perceived beforehand.

B. Sec. 144BA(2) – Formation of opinion by PCIT/CIT:

After the AO has made a reference to PCIT/CIT, the PCIT/CIT has to opine on whether the provisions of Chapter X-A are required to be invoked. If he is of the opinion that the provisions of Chapter X-A are indeed required to be invoked, then he should issue a notice to assessee setting out the reasons and basis of such an affirmative opinion. The purpose of issuing such notice by PCIT/CIT to assessee is to invite objections from assessee and to provide an opportunity of being heard to the assessee.

It is necessary to understand the meaning of the phrase 'he is of the opinion' since it is integral to this sub-section. Supreme Court[14] has equated the use of term 'of the opinion' with 'reason to believe' and held that the reasons for the formation of the belief must have a rational connection with or relevant bearing on the formation of the belief. Rational connection postulates that there must be

14 Supra

a direct nexus or live link between the material before PCIT/CIT (viz. details consolidated and presented in Form 3CEG by AO) and the formation of his opinion that the provisions of Chapter X-A are required to be invoked. This is also evident from the words 'setting out reasons and basis of such opinion in the notice to assessee' used under Section 144BA(2).

Although not clearly spelt out under Section 144BA(2), use of prefix 'if' before the words 'he is of the opinion that the provisions of Chapter X-A are required to be invoked' denotes that PCIT/CIT could also return the reference made to him by AO if he arrives at the conclusion that the reference under Form 3CEG setting out details about the arrangement (and reasons persuading AO to make a reference amongst other information) does not sufficiently lead to the belief that the provisions of Chapter X-A are required to be invoked. This view is fortified if one refers to the text of Rule 10UB(4)(i) where PCIT/CIT is required to issue directions to AO in Form 3CEH for returning the reference made u/s. 144BA(1) when he is satisfied that provisions of Chapter X-A are not required to be invoked.

C. Sec. 144BA(3) to Sec. 144BA(5) – Possible outcomes after sending notice to assessee by PCIT/CIT

Sec. 144BA(3) – No objection is furnished by the assessee: Under such circumstances, PCIT/CIT would issue directions to AO to declare the arrangement as an impermissible avoidance arrangement. It may be noted that there is no prescribed format for issuing directions unlike under section 144BA(2) where Form 3CEH has been prescribed for returning reference to AO. The use of words 'as he deems fit' succeeding the words 'issue such directions' implies grant of liberty to PCIT/CIT in using the format of his choice for issuing directions u/s. 144BA(3).

Sec. 144BA(5) – PCIT/CIT is satisfied by reply of assessee: After receiving objections from the assessee and having heard the assessee, if the PCIT/CIT is satisfied that the provisions of Chapter X-A are not required to be invoked, then he shall communicate the same to the AO by way of an order in writing with a copy to the assessee. Additionally, PCIT/CIT also needs to issue corresponding directions in Form 3CEH for returning the reference to AO in accordance with Rule 10UB(4)(ii).

Sec. 144BA(4) – PCIT/CIT is not satisfied by reply of assessee: Where PCIT/CIT is not satisfied by the explanation given by assessee in response to the notice issued u/s. 144BA(2), then he would make a reference to the Approving Panel under this section in Form 3CEI after recording his satisfaction regarding applicability of provisions of Chapter X-A therein in accordance with Rule 10UB(5).

D. Sec. 144BA(7); Sec. 144BA(8) r.w. Sec. 144BA(19); Sec. 144BA(9) – Proceedings and powers of AP

Sec. 144BA(7) – Opportunity of being heard by AP: Before the Approving Panel gives direction to AO, it has to provide opportunity of hearing to both - the assessee and the AO when such directions may prove prejudicial to respective interests. The provision under this Section is founded on the principles of natural justice and is similar to that contained under Section 144C(11) in case of proceedings conducted by Dispute Panel Resolution ('DRP').

Sec. 144BA(8) r.w. (19) – Powers of AP; Significance of powers equivalent to AAR:

While conducting the proceedings under Chapter X-A, AP has been accorded the following powers u/s. 144BA(8):

i. Directing PCIT/CIT to conduct further inquiry if required; Directing income-tax authority other than PCIT/CIT to conduct an inquiry and present a report containing result of such inquiry to it;

ii. Call for and examine such records relating to the matters it deems fit; and

iii. Require the assessee to furnish such documents and evidence as it may direct.

In addition to the above powers conferred upon AP u/s. 144BA(8), it has also been accorded u/s. 144BA(19) the powers that are vested with Authority for Advance Rulings ('AAR') u/s 245U of ITA. Section 245U in turn makes a mention of the powers vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908) that are specified u/s. 131 of ITA. For the sake of clarity, the powers specified u/s 131(1) are as under:

a) Discovery and inspection;

b) Enforcing the attendance of any person, including any officer of a banking company and examining him on oath.

c) Compelling the production of books of account and other documents; and

d) Issuing commissions.

It is interesting to note that powers similar to those conferred upon AAR u/s. 245U have also been conferred upon the appellate tribunal u/s. 255(6). Further, Commissioner (Appeals) ('CIT(A)') and DRP are also listed as authorities which has been granted powers u/s. 131. Section 131 gives certain powers of a civil court of law to the income-tax authorities, quasi-judicial and judicial authorities created under ITA[15]. Though these authorities do not strictly act as civil courts of law, it is clear from this section that they act in a quasi-judicial capacity and ought to conform to the elementary rules of judicial procedure[16]. Exercising the powers of a civil court, income-tax authorities, quasi-judicial (including Approving Panel) and judicial authorities created under ITA may, under order XIII. R 10, of the Code of Civil Procedure, calls for books and documents seized by a magistrate in other proceedings. In the circumstances of a case the powers under this section may be coupled with a duty, - e.g. a duty to enforce the attendance of a witness whose evidence is material or to call for the assessee's books of account which are in the possession of public authority. The income-tax authorities, quasi-judicial and judicial authorities created under ITA can issue commission for any purpose for which a civil Court may issue a commission: to examine any person, to make a local investigation and examine accounts[17].

However, neither the procedure for conducting proceedings by CIT(A) nor by DRP nor by appellate tribunal under ITA makes reference to the powers specified precisely u/s. 144BA(8) (ii) and (iii) as they are specified for proceedings by AP. On a closer comparison of the powers mentioned u/s. 144BA(8)(ii) and (iii) with those mentioned u/s. 131, it appears that the powers mentioned u/s. 144BA(8)(ii) and (iii) are already included under the powers conferred by Section 131(1)(c) and there is an overlap to that extent.

Sec. 144BA(9) – Opinion of majority of members of AP: If the members of AP (being three in number) differ in opinion on any point, then such point is to be decided according to the opinion of majority of the members.

E. Sec. 144BA(6) – Outcome of proceedings by AP

Sec. 144BA(6) provides that AP shall issue directions as it deems fit for declaring an arrangement to be an impermissible avoidance arrangement. The text of Sec. 144BA(6) tends to suggest that AP can only declare an arrangement as an impermissible avoidance arrangement and cannot conversely hold otherwise. In other words, there is an ambiguity under Section 144BA(6) which suggests that AP cannot give directions to declare an arrangement as not being an impermissible avoidance arrangement. However, Memorandum to Finance Bill 2012 expressly states that the Approving Panel shall either declare an arrangement to be impermissible or declare it not to be so after examining material and getting further inquiry to be made.

15 See Commentary on Sec. 131 by Kanga & Palkhivala on The Law and Practice of Income Tax, 10th Edition.

16 Ibid

17 Ibid

The language deployed under Section 144BA(6) is similar to the language used under Section 144C(5) with respect to proceedings conducted by DRP. In the context of section 144C, it has been held by Delhi High Court[18] that DRP needs to pass a speaking order giving cogent and germane reasons for arriving at the conclusion. The AP could also therefore be expected to pass a speaking order setting out reasons for either declaring or declining to declare an arrangement as impermissible avoidance arrangement while dealing with the objections from the assessee.

F. Sec. 144BA(6) r.w. Sec. 144BA(11) – Applicability of the directions of AP to other previous year(s)

Sec. 144BA(6) states that while declaring an arrangement to be an impermissible avoidance arrangement, AP may specify the previous year or years to which such declaration shall apply[19]. Furthermore, Sec. 144BA(11) stipulates that where the direction issued by AP u/s. 144BA(6) specifies a previous year(s) other than the previous year for which proceedings are pending before the AO, then the AO need not seek fresh directions for such other previous year(s) for completing the assessment / reassessment proceedings of such other previous year(s).

It may be humbly submitted that Sec. 144BA(6) and Sec. 144BA(11) are subservient and restricted in their scope by section 144BA(1) whereby the AO first needs to cross the threshold provided u/s. 144BA(1) viz. making an individual reference for each respective previous year against which assessment / reassessment proceeding is pending. If the assessment / reassessment proceeding is not pending for any preceding or succeeding previous year to the previous year under question, then a reference cannot be made u/s. 144BA(1) for such preceding or succeeding previous year to begin with and consequently, declaration of arrangement as an impermissible avoidance arrangement in either of those years cannot be permitted to be made u/s. 144BA(6). If such direction could not be issued u/s. 144BA(6) on a valid basis, then completion of assessment / reassessment proceeding for such preceding or succeeding previous year could also be challenged to be ultra vires.

This brings one to the question on whether the direction issued by AP u/s. 144BA(6) for a particular previous year can be construed as valid reason for reopening the assessment of other previous year (within the time limit permitted u/s. 149) claiming that facts and circumstances for such other previous year remain the same? It is settled position that in absence of fresh material, a completed assessment cannot be reopened. Therefore, it may prove difficult to reopen an assessment for other previous year on such grounds.

G. Sec. 144BA(10); Sec. 144BA(11) and Sec. 144BA(12) – Completion of assessment / reassessment proceeding and determination of tax consequences:

Unlike the power granted to CIT(A) u/s 251 or to DRP u/s 144C(8) to confirm, enhance or reduce the income of the assessee, equivalent powers have not been granted to AP for determining the tax consequences arising out an arrangement being declared as an impermissible avoidance arrangement. Neither has such power been granted to PCIT/CIT especially when they have been granted the adjudicating powers for determining whether an arrangement can be classified as an impermissible avoidance arrangement. The power to determine tax consequences lies solely with the AO and Sec. 144BA(10) and 144BA(11) simply state that the AO shall complete the proceedings in accordance with the directions received from PCIT/CIT/AP and in consonance with the provisions of Chapter X-A.

Sec. 246A(1)(b) of ITA removes the possibility of appealing against the order of AO before CIT(A).

18 In Vodafone Essar Ltd. vs. DRP [2012] 340 ITR 352 (Delhi)

19 It may be noted that PCIT/CIT has not been granted similar power u/s. 144BA(3) although Form 3CEG seeks information for previous years other than those for which assessment is pending.

Instead, such order can be directly appealed to the appellate tribunal u/s. 253(1)(e). It fails to appeal to a rational mind that an appeal does not lie before CIT(A) against the order of the AO to the extent of challenging the tax consequences especially when AO is the only income tax authority that is competent enough to determine tax consequences of an impermissible avoidance arrangement whereas on the other hand the PCIT/CIT/AP have only the adjudicating power to declare an arrangement to be an impermissible avoidance arrangement.

H. 144BA(12) – Prior approval of PCIT/CIT before passing of order by AO

All the orders of AO pertaining to assessment / reassessment proceedings which include determination of tax consequences need prior approval of PCIT/CIT in accordance with Sec. 144BA(12). A pertinent question that may arise hereunder is whether the PCIT/CIT could vary the tax consequences determined by the AO at the time of granting approval?

In the context of an administrative act under Land Acquisition Act, Supreme Court[20] has held that word 'approval' does not mean anything more than either confirming, ratifying, assenting, sanctioning or consenting. It further held that the power of granting or not granting prior approval cannot be equated with appellate power whereby the findings could be reversed. ITAT Bangalore 'B' Bench[21] has held that the aforesaid decision of Supreme Court would be applicable even to administrative approvals under Income-tax Act, 1961. The prior approval of PCIT/CIT is intended to curb the arbitrary application of Sec. 98 to an arrangement and thus would remain an administrative approval in nature. Therefore, PCIT/CIT may not have the power to review, adjudicate or vary the tax consequences determined by the AO but would be restricted to exercise oversight over the discretion of AO in determining tax consequences in accordance with Sec. 98 of ITA.

I. Sec. 144BA(14): No Appeal under ITA against directions of AP

Sec. 144BA specifies that the directions of AP are binding upon the assessee as well as the PCIT/CIT (including subordinate authorities below them). Further, no appeal shall lie against directions issued by AP u/s 144BA(6). It may be noted however that, in case of gross violation of principles of natural justice, the directions could be challenged by way of writ petition under Article 226 of Constitution.

J. Sec. 144BA(15) to (21)

These provisions deal with the constitution and administrative matters relating to AP.

Conclusion

Although it has been held by the Courts for long that it is not for the revenue authorities to dictate the manner in which an assessee should conduct his business, after the provisions of Chapter X-A having come into effect, once an arrangement is classified as an impermissible avoidance arrangement the revenue authorities may now indeed be in a position to dictate so. On a concluding note, there are sufficient checks and safeguards built-in for invoking the provisions of Chapter X-A. Essentially, the procedural provisions provide for respecting the principles of natural justice at every stage of the procedure defined for invoking the provisions of Chapter X-A. In addition, appointment to the Approving Panel of a member being academic or scholar having special knowledge of matters, such as direct taxes, business accounts and international trade practices would certainly boost confidence for the international community. However, one must remember that the Approving Panel does not have the authority to adjudicate upon the tax consequences and the only safeguard against potential arbitrary determination of tax consequences by AO is the administrative power given to PCIT/CIT to exercise oversight before according approval to the tax consequences so determined by the AO.

20 In Vijayadevi Navalkishore Bhartia vs. Land Acquisition Officer [2003] 5 SCC 83

21 In Toyota Kirloskar Motors (P.) Ltd. [2012] 28 taxmann.com 293 (Bangalore)

CA Sunil Arora & CA Varun Sharma

Exemptions from GAAR

It would be fair to make a statement that General Anti-Avoidance Rules ('GAAR') is a global effort. Countries are either incorporating new anti-avoidance rules in their local tax legislations or strengthening the existing ones. Tax treaties are being re-visited to ensure a fair and 'moral' distribution of profits across jurisdictions. India too has taken an important step in this direction by incorporating GAAR in the Income-tax Act, 1961.

GAAR is a set of anti-abuse provisions which empower the revenue authorities to examine the underlying purpose in each transaction with a view to address the issue of tax avoidance. The Indian GAAR originated from the Direct Tax Code, 2009 and after some turbulence, was formulated in 2012. Given the subjective nature of the 2012 GAAR legislation, an Expert Committee was set up under the Chairmanship of Dr. Parthasarathy Shome to recommend an appropriate implementation strategy in consultation with various stakeholders including the public at large. Subsequently, in 2016, specific rules were notified followed by a circular in 2017 containing FAQs on critical issues.

The GAAR legislation, as it now stands, provides a fairly exhaustive regulatory framework for governing transactions involving tax avoidance. In accordance with the agenda set out for this publication, our paper outlines the nuances relating to exemptions contained under rule 10U of the Income-tax Rules, 1962 ('IT Rules') and addresses some potential issues that may arise in actual practice.

1. The 3 crores tax benefit threshold decoded

Rule 10U(1)(a) provides that the GAAR provisions shall not apply to an arrangement where the aggregate tax benefit arising in a tax year is up to INR 3 crores It is stated that

"(1) The provisions of Chapter X-A shall not apply to —

(a) an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of rupees three crore."

This rule of exemption is apparently based on a recommendation made by the Expert Committee where the intent was to focus only on high value sophisticated structures. Their report explains the rationale of arriving at the said threshold i.e. of the 4,59,270 companies in India, only 6,141 reported a PBT of INR 10 crores At 30%, this resulted into a tax amount of INR 3 crores which was considered material enough to trigger the GAAR provisions in India. This approach and the level of transparency is a laudable effort. Given the math, the threshold may be revised based on improved profit reporting by Indian companies in future years.

That said, the manner in which this provision has been drafted, gave rise to multiple interpretation issues. Some of these were clarified by the CBDT through FAQs in its Circular[1] ('CBDT Circular').

CBDT clarifications

In order that GAAR provisions become applicable, the threshold of tax benefit of INR 3 crores is stated to be

a) arising in the Indian jurisdiction alone as the application of tax law is jurisdiction specific;

b) in relation to a specific assessment year and lastly;

c) not tax payer specific but arrangement specific. In other words, only when the aggregate tax benefit arising in an arrangement meets the threshold, does GAAR apply.

Based on a plain understanding of Rule 10U read with the CBDT Circular, it can be stated that in order for GAAR provisions to apply, the threshold of INR 3 crores is the aggregate tax benefit arising in India in an assessment year where the taxpayers are party to an arrangement.

Other issues examined

Although the CBDT Circular addresses some very pertinent issues, a fine reading of all limbs of Rule 10U indicates specific areas which may require further clarification. These are

a) The period or number of years relevant to threshold of INR 3 crores

As stated earlier, rule 10U(1)(a) requires determination of threshold in respect of a particular assessment year. The CBDT Circular supports this view. However, the definition of expression 'tax benefit' per section 102(10) provides a different view. It is stated that

102(10) "tax benefit" includes,—

(a) a reduction or avoidance or deferral of tax or other amount payable under this Act; or

…………

(f) an increase in loss,

in the relevant previous year or any other previous year;"

The expression 'in relevant previous year or any other previous year' appears to be in contradiction with 'relevant assessment year' quote in rule 10U. Since the quantification of tax benefit is a key criteria for trigger of GAAR provisions a clarification in this respect is deserving.

The CBDT Circular provides that a contrary view will not be taken in a subsequent year if such arrangement has been held to be permissible in earlier year and the facts and circumstances remain unchanged. Now, a fundamental issue which may be pertinent under the 'relevant assessment year' approach is that a different view could arise, based on threshold fulfilment, on the same arrangement in different years. Consider a case where an 'impermissible avoidance arrangement' is considered 'permissible' for want of threshold requirement. Now, would the same arrangement be viewed as 'impermissible' if in the subsequent year, the threshold limit is breached? Well, considering the key essence of GAAR, the answer appears to be 'Yes'. However, this issue would still require clarification, considering the taxpayer, on a plain reading of the Circular, would argue the arrangement to be out of ambit of GAAR.

A related issue here will arise in respect of single transaction, the tax benefit of which is spread

1 Circular No7 dated January 27, 2017

across multiple years. While the cumulative tax impact may be well above the prescribed threshold, one could argue following the 'relevant assessment year' approach that tax benefit arising in one year only will be seen in examining the GAAR applicability in respect of each year. The CBDT Circular supports this position.

b) Gross v. Net Tax Impact

It is clear that the quantum of tax benefit is seen in respect of an arrangement and not a tax payer. In this respect, the CBDT Circular has clarified that the tax benefit is not to be examined with respect to a single taxpayer only and what needs to be examined is the tax benefit arising to all the parties from the arrangement. It is stated that

"Further, GAAR is with respect to an arrangement or part of the arrangement and therefore limit of ₹ 3 crore cannot be read in respect of a single taxpayer only."

Where multiple tax payers are participating in an arrangement, a situation may arise that results into tax benefit to some and tax disadvantage to others. Consider an arrangement which results into tax benefit of INR 4.5 crore to ABC Ltd and a tax loss of INR 2 crore to XYZ Ltd. While the tax benefit to ABC Ltd. is above the prescribed threshold, the net tax benefit in India on such arrangement is below the prescribed threshold. In such a scenario, the revenue may argue that what is to be examined is only the tax benefit to all the parties from an arrangement and not the tax loss and thereby bring the above arrangement under the purview of GAAR.

That said, going by the true intent of the CBDT Circular and the GAAR provisions, tax disadvantage to a party from the same arrangement shall also be considered in computing the prescribed threshold. It would be useful if a clarification is offered on this specific aspect.

c) Determining tax deferral

Per Section 102(10), tax benefit includes any 'deferral of tax'. Such a situation could arise where the benefit available to the taxpayer is by delaying the payment of taxes to future years. The question here is the quantification of tax benefit threshold considering that the benefit would get realised in future years.

Interestingly, these concerns were also raised by some stakeholders after the initial draft guidelines, proposing a monetary threshold, were issued. In response to these concerns, the Expert Committee had recommended that such benefit be computed on the basis of 'discounted present value' considering the rate of interest payable to revenue authorities under section 234B as the inflation factor. This appears plausible and again a clarification would be useful.

d) Whether tax includes other amounts payable under the Act

Section 102(10) states that tax benefit includes 'tax or other amount payable' under the Act. However, Rule 10U restricts the scope of tax benefit to the amount of 'tax' only. There is no mention of 'other amount payable'. This will lead to a conflicting situation wherein the taxpayer would resort to computing the tax benefit threshold without considering other amounts payable under the Act such as (surcharge and cess). This has the potential to impact borderline cases.

It is interesting to note that the Expert Committee in its report had envisaged this situation and had suggested that the scope of tax benefit (for the purpose of computing threshold) be clearly restricted to income tax, dividend distribution tax and profit distribution tax and not other amounts like interest, income, etc. Since this is a known issue, a clarification by way of an inclusive list of taxes covered in computing 'tax benefit' would be useful. Reference is available in UK HMRC regulation which has provided an inclusive list of taxes to which UK GAAR shall apply.

e) Whether tax benefit restricted to Indian jurisdiction?

As mentioned earlier in this note, the CBDT has clarified that in considering the quantum of tax benefit, only the benefit arising in the Indian jurisdiction is seen.

That said, the CBDT Circular does not seem to have envisaged a situation wherein a tax-payer derives incidental tax benefit by virtue of an impermissible arrangement outside India which is also the main purpose in such arrangement. Going by the plain reading of the CBDT Circular, such a scenario may lead to GAAR applicability in India unless the taxpayer can establish that tax benefit in India was not the main purpose of such transaction.

2. Foreign Institutional Investors ('FIIs') – Exempted and to what extent?

Based on the recommendations of the Expert Committee the FIIs which have invested in Indian securities with prior permission of the competent authority have been kept out of the GAAR net. Rules 10U(1)(b) and (c) states that

"(1) The provisions of Chapter X-A shall not apply to —

(b) a Foreign Institutional Investor,—

(i) who is an assessee under the Act;

(ii) who has not taken benefit of an agreement referred to in section 90 or section 90A as the case may be; and

(iii) who has invested in listed securities, or unlisted securities, with the prior permission of the competent authority, in accordance with the Securities and Exchange Board of India (Foreign Institutional Investor) Regulations, 1995 and such other regulations as may be applicable, in relation to such investments;

(c) a person, being a non-resident, in relation to investment made by him by way of offshore derivative instruments or otherwise, directly or indirectly, in a Foreign Institutional Investor."

Accordingly, FIIs who have not availed treaty benefits and a non-resident person in FII, whether such FII has claimed tax treaty benefits or not, have been exempted from applicability of GAAR. The manner in which this provision has been drafted clarifies the intent of the legislator that even in a multi-layer investments structure, only those investments which, directly or indirectly, are made by non-residents in such FIIs by way of offshore derivative instruments qualify for GAAR exemption.

Offshore derivative instrument includes participatory notes, a widely used instrument by non-resident individual investors to invest in the Indian securities markets through registered FIIs. Concerns were raised that participatory notes promote infusion of black money into the Indian system. Surprisingly, these concerns did not find merit with the Expert Committee and they went on to suggest that investment in participatory notes from FIIs should be exempt. However, the legislator took note and addressed this in a different manner - while they accepted the recommendation of the Expert Committee, SEBI tightened the noose on operation of participatory notes by notifying stringent fee requirements through a notification in July 2017. In hindsight, this appears to be a more practical approach which addressed the real concern by use of a simple regulatory yardstick.

CBDT clarifications

The CBDT Circular has offered clarification in respect of two critical issues relating to FIIs. These are

a) A pre-requisite for an FII to remain exempt from GAAR is that such FII should not have claimed any benefit under the tax treaty. Although not in as many words, the CBDT Circular has indicated that claim of such tax treaty benefit may be examined in respect of each year.

b) GAAR shall not be invoked merely on the ground that the entity is located in a tax efficient jurisdiction. It is specifically stated that if the jurisdiction of such FII is based on non-tax commercial considerations and the main purpose of such an arrangement is not to obtain a tax benefit, GAAR will not apply.

Other Issues Examined

Though the exclusion of FIIs and clarifications offered thereafter indicate a conscious decision on the part of the legislature for not invoking GAAR in such cases, there are issues which need to be examined closely prior to making an informed decision. These are

Is there a Blanket Restriction on Availing Treaty Benefits by FIIs?

The rule clearly provides that in order to remain out of the GAAR net, the FII should not have availed treaty benefit. In absence of a specific direction, can it be argued that the restriction imposed under rule 10U operates only in respect of an arrangement tested for GAAR applicability? That said, the intent of the legislature in protecting FII investments from GAAR would ordinarily indicate a blanket restriction and therefore a clarification on this aspect is necessary.

Whether GAAR operates where limitation of benefit ('LOB') clause satisfied?

This is a fundamental issue. The CBDT has clarified in its Circular that if a case of avoidance is sufficiently addressed by LOB clause in the tax treaty, GAAR shall not be invoked. However, rule 10U(1)(b) provides that for an FII to claim exemption under GAAR, it should not have taken benefit under a tax treaty. This creates confusion and room for varied interpretation. Consider a case where an FII, having satisfied the LOB clause in a tax treaty, invites GAAR provisions due to specific provisions under rule 10U(1)(b). This is an issue deserving immediate attention.

3. Grandfathering of Existing Investments – Scope & Coverage

Under GAAR, incomes from transfer of investments made prior to April 1, 2017 ('cut-off date') are grandfathered. It is stated in Rule 10U(1)(d) that

"(1) The provisions of Chapter X-A shall not apply to —

(d) any income accruing or arising to, or deemed to accrue or arise to, or received or deemed to be received by, any person from transfer of investments made before the 1st day of April, 2017 by such person."

The grandfathering provisions were considered imperative in light of benevolent exit provisions in some of the tax treaties that India had agreed, specifically with Mauritius and Singapore which had attracted substantial portfolio or direct investments in India. Accordingly, representations were made to operate GAAR provisions prospectively and thus the legislation was put in place only in respect of incomes arising on or after the cut-off date.

On the issue of whether it is the existing 'arrangement' that should be grandfathered or it is only the 'investment' which should be grandfathered, the Expert Committee recommended that grandfathering of an existing arrangement (instead of existing investments) may result in many future tax avoidance schemes out of examination under GAAR since a tax avoidance structure itself would receive indefinite protection and dilute the effectiveness of GAAR. Accordingly, it was recommended by the Expert Committee that all investments (and not the arrangements) made by a resident or non-resident and existing as on the date of commencement of the GAAR provisions should be grandfathered so that GAAR provisions are not applied at the time of exit resulting into examination or denial of tax benefits.

Clause 2 of Rule 10U further states that

"(2) Without prejudice to the provisions of clause (d) of sub-rule (1), the provisions of Chapter X-A shall apply to any arrangement, irrespective of the date on which it has been entered into, in respect of the tax benefit obtained from the arrangement on or after the 1st day of April, 2017."

Interestingly, a combined reading of clause 1 and 2 seems to suggest that there is no effective grandfathering that is available in respect of investments made up to the cut-off date. While on one hand, clause 1(d) provides grandfathering in respect of income on transfer of investments made up to the cut-off date, clause 2, an overriding provision, denies any benefit in respect of incomes (from any arrangement) arising after the cut-off date. Consider a case where an investment made in January 2014 is sold in September 2017 resulting into tax benefit of INR 5 crore which is exempt under a particular tax treaty. In such a scenario, can it be argued by the tax-payer that the tax benefit after the cut-off date should be grandfathered since it squarely falls under the purview of clause 1(d)? On the other hand, would the revenue authorities also be justified in denying this claim based on the blanket restriction under clause 2?

Investments made pursuant to circular 789 dated April 13, 2000 from Mauritius is a classic example. In a scenario where the investment was made based on TRC produced by the Mauritian Holding Co., can the tax benefit arising to the taxpayer after the cut-off date be denied in accordance with clause 2 of rule 10U?

Given that the true intent of grandfathering is to provide effective shelter to gains arising from legitimate investments that were made up to the cut-off date, a clarification is necessary for the two provisions to operate harmoniously, failing which, the existing 'diluted' grandfathering provisions would operate only in respect of tax benefit recorded up to the cut-off date.

CBDT Clarifications

The clarification offered in respect of grandfathering provisions addresses specific issues put forth by the stakeholders in respect of convertible instruments such as compulsory convertible debentures, convertible preference shares and Global Depository Receipts issued before the cut-off date. The Circular has stated that these convertible instruments will be regarded as Investments made prior to the cut-off date provided the terms of such instruments are finalised at the time of issuance of such convertible instruments.

Similarly, bonuses, share split and consolidation of shares in respect of shares acquired by the same investor (who subsequently receives bonus/ consolidated shares) prior to the cut-off date will also be grandfathered.

It is clearly stated that lease contracts and loan arrangements will not be grandfathered.

Grandfathering Under GAAR and Tax Treaties

It is noteworthy that while GAAR provides relief in respect of an 'investment' made before the cut-off date, the recently modified treaties with both Singapore and Mauritius extends treaty benefits to capital gains earned in respect of any shares 'acquired' before that date. Since the intent under both GAAR and the amended tax treaties is to eventually grandfather investments made by the cut-off date, the use of different expressions, although not deliberate, is likely to cause interpretation issues. A line of clarification will allay concerns.

Another issue that is relevant here is in respect of a potential conflict that may arise on the issue of grandfathering under the amended tax treaties with Mauritius and Singapore when compared with the GAAR provisions under domestic law which have an overriding impact on the tax treaties. Under such scenario, would the tax benefit, accruing after the cut-off date, be denied per rule 10U(2) to a tax payer who has otherwise adequately met the LOB clause per the amended tax treaties? In other words, would the grandfathering apply here in its true sense? Well, the CBDT has addressed this scenario and clarified that if a case of tax avoidance is sufficiently addressed by LOB in the tax treaty, there shall not be an occasion to invoke GAAR. Although this provides some clarity, the expression 'sufficiently addressed' leaves room for ambiguity which the revenue authorities may use to their advantage in invoking GAAR citing misuse of LOB under the tax treaties.

Other Issues Examined

Transactions Under SAAR – Whether Exempt from GAAR?

In light of specific concerns and taking cue from global practices, the Expert Committee had suggested that GAAR should not be applied in situations where Specific Anti-Avoidance Rules ('SAAR') operate under the domestic legislation. However, the CBDT has taken a different position and instead stated that GAAR and SAAR can both co-exist based on the facts and circumstances of each case. This provides room for ambiguity and potential misuse of GAAR even in genuine cases where the taxpayers have met the test of SAAR conditions to the satisfaction of the revenue officer.

Decision by Courts and AAR – Whether Exempt from GAAR?

This issue is squarely covered under the CBDT Circular. It is stated that GAAR will not apply to arrangements that have been held permissible by the Authority of Advance Ruling ('AAR') or other similar authorities (such as judicial courts). This is a welcome step which should typically help the mergers and amalgamations schemes that are examined by the Courts (now National Company Law Tribunal 'NCLT'). However, the actual test of this clarification would be a situation where the Courts / NCLT, approves a scheme without adequately looking into the tax aspects of a business scheme. Will the revenue authorities be justified in invoking GAAR provisions in such a situation?

4. Concluding Remarks

It is evident from this discussion that the existing provisions under the Indian GAAR are generically worded, leaving ample scope for subjective interpretation. Therefore, despite various clarifications and intense public consultations, the taxpayers are getting nervous and wary of the manner in which the GAAR legislation will be implemented. Also if the legislator expects this regulation to operate successfully, the revenue officers would need to be trained on both the technical as well as soft aspects.

The Circular issued by the CBDT has made an honest attempt to clear air on some critical issues but there is enormous scope for exhaustive and more precise clarification. Take for example, the Guidelines on GAAR Exemptions by the UK HMRC where GAAR is carefully constructed to include a number of safeguards that ensure that any reasonable choice of a course of action is kept outside the target area of the GAAR. Specific examples have been provided in the legislation to ensure that the taxpayers right to select a business method is adequately protected from application of GAAR. There are similar instances in the Australian Tax Office's Guidelines on GAAR.

The Indian GAAR has made no such concentrated effort besides issuing clarifications through a Circular in January 2017. This has left much to desire. The legislature ought to have acted wisely in accepting the recommendations of the Expert Committee to introduce a 'negative list' (arrangements not subjected to GAAR) and additionally, prescribe genuine cases where the taxpayer's right to select method of implementing a transaction is safeguarded. These could have acted as an effective ready reckoner for both the tax officers as well as the taxpayers and the selection of cases would then become more of an exception with a higher probability of sailing through the approving panel.

> "The weak can never forgive. Forgiveness is the attribute of strong."
>
> — *Mahatma Gandhi*

Sunil Moti Lala, *Advocate*

Dispute Resolution, Legal Remedies available against GAAR proceedings

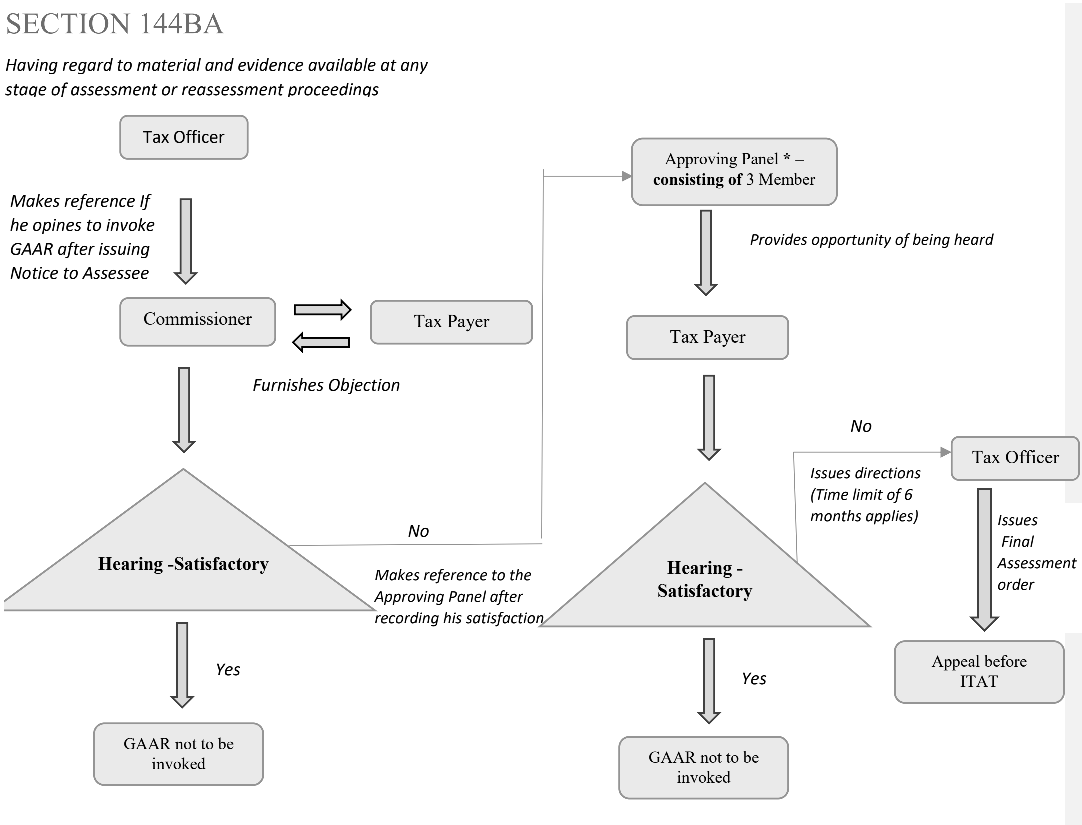
1. Introduction

General Anti Avoidance Rule ("GAAR") provisions contained in Chapter X-A of the Income tax Act, 1961 ("the Act") have come into force from April 1, 2017 i.e. AY 2018-19 onwards. Rules 10U to 10UC have been introduced in the Income-tax Rules, 1962 ("the Rules") in connection with the GAAR proceedings. Extensive deliberations have been made at various platforms / forums in connection with the applicability of the said provisions and the implications thereafter. It is an accepted fact that the said provisions give extremely wide powers and discretion to the Revenue and thus the possibility of arbitrary action being taken by the Assessing Officer cannot be ruled out, in fact the same are already being anticipated. Naturally, an assessee is likely to be aggrieved by such actions and would need to seek suitable redressals. Keeping in view the vast discretionary powers provided to the Revenue, the Legislature has provided a distinctive mechanism under the Act for the aggrieved assessee to seek redressal. However, as the remedies and safeguards provided under the Act may not be adequate at all the stages of the GAAR proceedings, the other possible legal remedies have also been discussed in this article.

2. Relevant provisions of the Act and Rules

The legal remedies available to an assessee at different stages of the GAAR proceedings are being evaluated in this article keeping in mind the provisions of section 144BA of the Act as well as the relevant Rules (i.e. Rule 10U, 10UB and 10UC).

3. The GAAR proceedings emanating from the aforesaid provisions can be summarised through the following chart



** Constitution of Approving Panel 3 Members Retired/ current HC judge, IRS not below PCIT/ CCIT and academic/ scholar. To be constituted for a period of 1-3 years. To have the powers of AAR as specified under Section 245U of the Act.*

4. Legal remedies at different stages of GAAR

The various stages at which the assessee may be required to seek a legal remedy vis-à-vis the GAAR proceedings are enumerated hereunder:

4.1 Legal Remedies – At the stage when the Assessing Officer is making a reference to the Principal Commissioner/ Commissioner:

As per the provisions of Section 144BA(1), having regard to material and evidence available, the Assessing Officer may make a reference to the Principal Commissioner / Commissioner where he considers it necessary to declare an arrangement as an Impermissible Avoidance Agreement ("IAA") and to determine consequences thereof. Prior to making such a reference, the Assessing Officer as per Rule 10UB, has to issue the assessee a notice providing the assessee the basis and reason (along with details of the arrangement, list of documents relied on and the alleged tax benefit arising) as to why he considers it necessary to declare an arrangement as an IAA and seeking objections from the assessee against the reasoning mentioned therein. The assessee, being aggrieved of the action taken by the

Assessing Officer MAY be able to approach the Hon'ble Court in appropriate cases by way of a Writ Petition in the following scenarios / situation:

a. Section 144BA(1) provides that the Assessing Officer having regard to the "material and evidence available" may make a reference to the Principal Commissioner or Commissioner to declare an arrangement to be an IAA. The validity / legality of the reference would have to be judged on the basis of material and evidence in the possession of the Assessing Officer. Therefore, it implies that the Assessing Officer on the basis of mere conjectures and surmises would not be able to invoke GAAR proceedings and make a reference to the Principal. Commissioner. If he does so, in the absence of an alternative legal remedy to directly challenge the validity of the reference, it MAY be possible for the assessee to challenge the same before the Hon'ble Writ Court on the ground that the same is patently illegal or without jurisdiction

b. Rule 10UA (1) (a) to (d) provides certain factual situations in which Chapter X-A itself would not be applicable eg. in case of an FII or where the tax benefit arising to the parties to the arrangement does not exceed Rs. 3 crore etc. However, if the Assessing Officer clutches jurisdiction under Chapter X-A in any of the aforesaid situations in the absence of any alternate legal remedy at that stage, it MAY be possible for the assessee to challenge the action of the Assessing Officer in appropriate cases before the Hon'ble Writ Court on the ground that the same is patently illegal and without jurisdiction. Reference may be made to following case laws wherein the action / notice issued by the Revenue was quashed as the same was patently illegal / without jurisdiction:

- *Vodafone India Service Pvt. Ltd. vs. UOI (359 ITR 133) (Bom HC)*
- *Calcutta Discount Co. Ltd. vs. ITO (41 ITR 191) (SC)*
- *CIT vs. Foramer France (264 ITR 566) (SC)*
- *Ajanta Pharma Ltd. vs. ACIT (267 ITR 200) (Bom HC)*
- *Shubham Fabrics vs. Inspecting ACIT (174 ITR 502) (All HC)*
- *Mercury Travels Ltd. vs. DCIT (258 ITR 533) (Cal HC)*
- *Ajit Jain vs. UOI (242 ITR 302) (Del HC)*
- *Gujarat Gas Co. Ltd. vs. CIT (245 ITR 84) (Guj HC)*

c. Rule 10UB further provides that the Assessing Officer before making a reference to the Principal Commissioner / Commissioner has to issue a notice in writing seeking objections, if any to the application of Chapter XA. The Rule further provides that the said notice must contain details of the arrangement, tax benefit arising from such arrangement, the basis & reasons for considering the arrangement as an IAA and the list of documents relied upon by the Assessing Officer should also be furnished to the assessee. However, if no notice is issued and the Assessing Officer has made a reference to the Principal Commissioner /Commissioner without providing the assessee with the opportunity to file objections, it MAY be possible for the assessee to challenge the said reference before the Hon'ble Writ Court on the ground that the said reference being made in violation of the principles of Natural Justice is bad in law and liable to be quashed [see The State of Uttar Pradesh v Mohammad Nooh - 1958 045 AIR 0086 (SC), JK Synthesis v ITO (1976) 105 ITR 864 (All) and Pancharatna Cement P Ltd v UOI – (2009) 317 ITR 259 (Gau)]. Alternatively, if the notice issued does not comply with the aforesaid requirements it MAY be possible for the assessee to challenge the same before the Hon'ble Writ Court on the ground that the said notice is patently illegal due to non-satisfaction of the preconditional requirements. [Reference may be made to the case laws in Para 4.1(b) above]

4.2 Legal Remedies – At the stage when the Principal Commissioner/Commissioner is making a reference to the Approving Panel ("AP"):

As per the provisions of Section 144BA(2), on receipt of reference from the Assessing Officer, if the Principal Commissioner / Commissioner is of the opinion that GAAR provisions are to be invoked, he shall issue a notice to the assessee setting out reasons for why he is of the opinion that Chapter X-A would be applicable and provide the assessee with an opportunity of being heard and to file objections, if any. If the Principal Commissioner / Commissioner is not satisfied after hearing the assessee's contentions / with the objections filed by the assessee, he shall, after recording satisfaction make further reference to the Approving Panel ("AP") for the purpose of determining whether the arrangement is an IAA. At this stage, in appropriate cases, it may be possible for the assessee to approach the Hon'ble Writ Court requesting it to exercise its extra ordinary jurisdiction in the following situations:

a. Section 144BA(2) provides that pursuant to the reference received from the Assessing Officer, if the Principal. Commissioner / Commissioner is of the opinion that provisions of Chapter X-A are required to be invoked, he shall issue notice to the assessee specifying the reasons and the basis of such opinion for allowing the assessee to file objections, if any and afford an opportunity of being heard. It is imperative that opportunity of being heard must be given and the opinion must be formed objectively with application of mind. However, if without issuing notice / providing opportunity of being heard to the assessee, if the Principal Commissioner / Commissioner makes a reference to the AP, it may be possible to challenge the said reference in a Writ Court on the ground that it is patently illegal / without jurisdiction and made in violation of the principle of Natural Justice. [see *The State of Uttar Pradesh vs. Mohammad Nooh - 1958 045 AIR 0086 (SC), JK Synthesis vs. ITO (1976) 105 ITR 864 (All)* and *Pancharatna Cement P. Ltd.vs. UOI – (2009) 317 ITR 259 (Gau)]*

b. If the Principal Commissioner / Commissioner is not satisfied with the objections filed by the assessee under Section 144BA(2), then he shall make a further reference to the AP under Section 144BA(4) after recording his satisfaction in accordance with the provisions of Rule 10UB(5). It is well settled law that where a satisfaction is to be recorded, it must be a cogent and objective satisfaction justifying the course of action adopted (in this case further reference to the AP). In fact, considering the wide implications / ramifications of an arrangement being declared as an IAA, recording of mere mechanical satisfaction may not tantamount to sufficient compliance of the pre-conditions of Section 144BA(4) and Rule 10UB(5) and it may be possible in appropriate cases to challenge the Reference made by the Principal Commissioner/ Commissioner to the AP. Reference may be made to the following judgments wherein writ was issued as the satisfaction of the Commissioner / Assessing Officer was mechanical and without application of mind:

- *Arjun Singh vs. Asst. DIT (2000) 246 ITR 363 (MP)*
- *Ingram Micro (India) Exports (P.) Ltd. DCIT (2017) 78 taxmann.com 140 (Bom)*
- *Amity Hotels (P.) Ltd. vs. CIT (2005) 272 ITR 75 (Del HC)*

c. Rule 10UC(1)(ii) provides that no reference can be made by the Principal Commissioner / Commissioner to the AP after expiry of two months from the end of the month in which the final submission by the assessee is received. Thus, if the Principal. Commissioner breaches the aforesaid time limit it would vitiate the entire order which may be challenged before the Hon'ble Writ Court with a prayer to quash the same. Reference may be made to the following decisions wherein the notice issued by the Assessing Officer was quashed as it was time barred

- *CIT vs. Foramer France (2003) 264 ITR 566 (SC)*
- *Madhavlal Sindhoo vs. VR Idurkar & Anr – (1956) 30 ITR 332 (Bom)*
- *German Remedies Ltd vs. DCIT – (2006) 287 ITR 494 (Bom)*

4.3 Legal Remedies – Proceedings before the AP

Pursuant to receiving a reference from the Principal Commissioner, the AP can issue such directions as it deems fit including specifying the previous year or years for which the directions would be applicable. Section 144BA(7) provides that no directions shall be issued unless an opportunity of being heard is given to the assessee / Assessing Officer if the directions are prejudicial to their interest. Section 144BA(13) further provides that the aforesaid directions would have to be issued within a period of six months from the end of the month in which the reference was received. Section 144BA(14) provides that notwithstanding anything contained in any other provisions of the Act, no appeal shall lie against the directions of the AP. However, in the absence of a direct alternate and efficacious remedy, it MAY be possible for the assessee in appropriate cases to approach the Hon'ble Writ Court in the following scenarios / situations:

a. As provided in Section 144BA(7), the AP cannot pass any direction without providing opportunity of being heard to the requisite party whose interest would be prejudiced by issuance of such directions. Therefore, if it does so then, the aggrieved party be it Revenue or the assessee may be able to approach the Hon'ble Writ Court on the ground that the principles of natural justice have been violated and pray for quashing of such an order. [see *The State of Uttar Pradesh vs. Mohammad Nooh - 1958 045 AIR 0086 (SC), JK Synthesis vs. ITO (1976) 105 ITR 864 (All)* and *Pancharatna Cement P. Ltd. vs. UOI – (2009) 317 ITR 259 (Gau)*]

b. The mechanism provided under the Act stipulates that once the Assessing Officer incorporates the directions of the AP as well as determines the tax consequence, the Assessing Officer would be able to pass an assessment or reassessment order only after the approval of Principal Commissioner. Though the said order is an appealable order u/s 253(1)(e) of the Act directly before the Hon'ble Tribunal, there is no direct efficacious remedy available against the directions of the AP if the same are patently illegal and / or without jurisdiction eg: the AP over and above declaring an arrangement to be IAA has also calculated the consequences under chapter X-A reference to section 144BA(1). In such a situation, since the AP would have exceeded its jurisdiction, the order would be patently illegal and it may be possible for the assessee in appropriate cases (which may be rare) to approach the Hon'ble Court with a prayer to quash the directions so issued on the ground that they are patently illegal or beyond jurisdiction [Reference may be made to case laws cited in Para 4.1b].

c. Further, if the AP gives direction u/s 144BA(6) after the expiry of the period of six months from the end of the month in which reference was received, it may be possible for the assessee to challenge such direction before the Hon'ble Writ Court with a prayer to quash the said directions being time barred in nature. [See *CIT vs. Foramer France (2003) 264 ITR 566 (SC), Madhavlal Sindhoo vs. VR Idurkar & Anr – (1956) 30 ITR 332 (Bom)* and *German Remedies Ltd vs. DCIT – (2006) 287 ITR 494 (Bom)*]

4.4 Legal Remedies – Against order passed pursuant to the directions of the AP

4.4.1 High Court

As per section 253(1)(e), order of assessment or reassessment passed pursuant to sanction u/s 144BA(12) is directly appealable to the Hon'ble Tribunal. **However**, Section 144BA(12) provides that "**no order** of assessment or reassessment shall be passed by the Assessing Officer **without the prior approval of the Principal Commissioner or Commissioner**, if any tax consequences have been determined in the order under the provisions of Chapter X-A". **Thus**, it would be reasonable to conclude that the Principal Commissioner has to apply his mind to the entire order, which would include not only GAAR consequences but also other additions as well (Transfer Pricing as well as corporate tax), and then provide an approval. It is a settled law that the approval of a quasi-judicial authority cannot be mechanical in nature and the same must postulate application of mind. Thus, in appropriate cases (which may be rare) it may be possible for the assessee to challenge the approval of the Principal Commissioner itself and consequently the order passed in pursuance thereof, if the assessee is able to show that the approval was granted in a casual manner without application of mind. [See Arjun Singh vs. Asst. DIT (2000) 246 ITR 363 (MP), wherein notices issued by the Assessing Officer were quashed in the absence of the requisite approval]

4.4.2 Tribunal

As per section 253(1)(e), order of assessment or reassessment passed pursuant to sanction u/s 144BA(12) is directly appealable to the Hon'ble Tribunal. In such a situation, there would be no adjudication at all particularly on the non-GAAR issues by any of the lower authorities (e.g. CIT(A) / DRP). Therefore, in effect the approval by the Principal Commissioner under Section 144BA would substitute the adjudication by the CIT(A) / DRP. It would be interesting to observe -

i) how the approval by the Principal Commissioner under Section 144BA(12) would operate and whether the Principal Commissioner would issue directions to the Assessing Officer to reverse its proposed findings on non-GAAR issues in case there is a disagreement between the two;

ii) how the Tribunal will adjudicate particularly on non-GAAR issues on which there has been no adjudication by CIT(A) / DRP;

iii) whether the Tribunal would be comfortable to sit in judgment on directions passed by a Retired / Sitting High Court Judge who is part of the AP;

iv) whether (in light of the discussions given hereunder) the Assessing Officer would be able to apply the GAAR provisions in respect of an eligible assessee under Section 144C and if so whether the order would be appealable before the Hon'ble Tribunal.

<u>GAAR vs. DRP?</u>

Section 144C(14A) states that the provisions of Section 144C (applicable to DRP proceedings) shall not apply to any assessment or reassessment order passed by the Assessing Officer with the prior approval of the Principal Commissioner or Commissioner under Section 144BA(12) (applicable to GAAR proceedings). However, as per Section 144C of the Act, it is mandatory for the Assessing Officer to issue a draft assessment order where the assessee is an eligible assessee u/s 144C(15)(b) (i.e. a foreign company or an assessee in whose case a variation in the returned income arises in consequence of the order passed by the Transfer Pricing Officer). Therefore, the issue which arises is whether both proceedings i.e. DRP and GAAR can co-exist in the case of an eligible assessee.

<u>GAAR + DRP → Tribunal?</u>

Alternatively, if one was to read the provisions of Section 144C harmoniously, by ignoring the provisions of Sub-section (14A), taking into consideration the provisions of Section 144C (1) which provides "The Assessing Officer shall, notwithstanding anything contrary contained in the Act…", a possible view may be that both proceedings could co-exist and culminate into one final assessment order incorporating directions of both the AP and DRP, which may be directly appealable before the Tribunal. However, though sub-sections (d) and (e) of Section 253 respectfully provide that (i) an order passed in pursuance of the directions of the DRP and (ii) an order passed in pursuance of the directions of the AP are appealable before the Hon'ble Tribunal, Section 253 does not explicitly provide for filing of appeals against a final assessment order (passed in pursuance of both the directions viz. directions of i) the DRP as well as the ii) the AP.

4.5 Legal remedies – before GAAR proceedings are invoked – Seeking an Advance Ruling

Section 245N of the Act, defining the term "advance ruling" has been amended with effect from 1 4 2015 vide insertion of sub-clause (iv) to clause (a), to include a determination or decision by the Authority on whether an arrangement which is proposed to be undertaken by a resident or non-resident is an IAA as referred to in Chapter X-A of the Act. Therefore, assessees are now also provided with the option of obtaining an advance ruling vis-à-vis applicability of Chapter X-A to its transaction.

Prior to the introduction of sub-clause (iv) to clause (a) to Section 245N, applications containing questions relating to a transaction or issue designed prima facie for the avoidance of tax were not maintainable before the AAR by virtue of the bar laid down in the Proviso to Section 245R(2) of the Act. However, by way of an amendment in clause (iii) of said Proviso, the bar will not apply to applicants falling under Section 245N(b)(iiia) i.e. applicants who have filed applications under Section 245N(a)(iv). However, since Section 245N(b) has been amended by Finance Act, 2017 replacing sub-clause (iiia) with item (V) of sub-clause(A), the Legislature would be required to insert a corresponding amendment in the Proviso to Section 245R(2). [To appreciate this para, simultaneously please refer to the aforesaid provision in the Act].

Obtaining an AAR on the implications of GAAR on a transaction would lend certainty to the applicant as the same would be binding on the Department. This has been clarified by the CBDT in Circular No. 7 of 2017 dated January 27, 2017 which provides that if an AAR holds that an arrangement is permissible, the ruling would be binding on the Principal Commissioner / Commissioner and sub-ordinate income-tax authorities. However, practically, the feasibility of approaching the AAR is still to be evaluated considering the delay experienced in obtaining rulings from the AAR notwithstanding the time limit of 6 months provided in Section 245R(6) for pronouncement of ruling.

5. Conclusion

Writ remedy, being a discretionary power, would be exercised only in exceptional cases and further, the Courts may opine that the Approving Panel itself constitutes an efficacious remedy for the various grievances of the assessee and thereby decline to entertain the Petition. Nevertheless, the assessee in deserving cases would have no option but to approach the Hon'ble Court by way of Writ Petition.

Keeping in mind, the far reaching consequences of the GAAR provisions, it would be imperative for the Principal Commissioner / Commissioner (i) to record his satisfaction (before making further reference to AP) & (ii) to grant approval (to Assessing Officer for passing of the order) with proper application of mind and not merely in a mechanical manner.

Further, as evident from Para 4.4 and 4.5 above there are still some facets of the redressal mechanism which require further clarifications / amendments. Though, the CDBT in its Circular No. 7 / 2017 dated January 27, 2017 has clarified that GAAR provisions will be invoked in a uniform, fair and rational manner and that adequate procedural safeguards have been put in place, but the implementation of the aforesaid clarification would have to be tested in times to come. However, one only hopes and prays that we would not have to sing the famous song from the old Hindi film *Hum Kisi se Kam Nahin – "Kya Hua Tera Vaada".*

CA Anish Thacker

Judicial precedents under Income-tax Act on Anti-Avoidance Rules

Introduction

Chapter X-A of the Income-tax Act, 1961 ('the Act') applies to any income earned on or after 1st April, 2017 from any arrangement, the 'main purpose' of which is to obtain a 'tax benefit'. It is therefore obvious that in the context of Chapter X-A or General Anti Avoidance Rule ('GAAR'), there is no judicial precedent available for a taxpayer to interpret or to understand the provisions of GAAR from seeking guidance from Courts. There are foreign judgments where GAAR in other countries has been interpreted which can serve as guidance but not as interpretational authority. These, I understand, are a subject of a separate article. In this article therefore, what I am attempting to do is highlight the thinking of the Indian Courts on the subject of 'tax avoidance' through legitimate legal means, which GAAR seeks to curb and then throw open a few questions on how the sweeping nature of GAAR may impact commonly used tax planning methods.

The subject of tax avoidance versus tax evasion[1] has always been a subject matter of great interest of both English and Indian Courts. Both countries did not have GAAR till very recently and therefore the Courts looked at tax avoidance keeping in mind that if tax avoidance was a result of legally proper transactions, then even if the result of these was that no tax was payable, the taxpayer was entitled to plan his affairs in a manner that achieved the least tax liability. Therefore, traditionally it has always been the legal form of a transaction that has ordinarily been looked at while deciding the liability of a taxpayer to pay tax. This however, has not always been the case and the Courts have come down heavily on devices that have been described as 'sham' or 'çolourable devices'. There clearly therefore, has been a line, a 'lakshman rekha' that the taxpayer should keep in mind not to cross. This is what has been labelled by some as 'Judicial GAAR'. We will, in the ensuing parts of this article look

1 These expressions are not defined in the Act.

at how Indian Courts have dealt with the issue of tax avoidance. This in my view, is broken up into four distinct periods, the pre-Mc Dowell period[2], the impact of the McDowell decision, the period between McDowell and Azadi Bachao Andolan's case[3], the decision of the Supreme Court in that case and the Vodafone case[4], which has become a must study for every international tax student and expert and became famous the world over.

The Pre-McDowell Era

One of the earliest decisions which came up before the English Courts which dealt with tax avoidance was the Duke of Westminster's case[5] In that case, the Duke of Westminster had made an arrangement that he would pay his gardener an annuity for which he could claim a tax deduction, instead of wages, for which he could not claim a tax deduction. The tax authorities urged that the form of the transaction was not acceptable and that contended that the form of the transaction was not acceptable to it and the Duke was taxed on the substance of the transaction, which was that payment of annuity was treated as a payment of salary or wages. The Crown's claim of invoking of the substance doctrine was, however, rejected by the House of Lords. Lord Tomlin's celebrated words in this regard are quoted below:

"Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax. This so called doctrine of `the substance' seems to me to be nothing more than an attempt to make a man pay notwithstanding that he has so ordered his affairs that the amount of tax sought from him is not legally claimable."

Lord Atkin, however, dissented and stated that *"the substance of the transaction was that what was being paid was remuneration."*

The principles which have emerged from that judgment are as follows:

(1) A legislation is to receive a strict or literal interpretation; (2) An arrangement is to be looked at not in by its economic or commercial substance but by its legal form; and (3) An arrangement is effective for tax purposes even if it has no business purpose and has been entered into to avoid tax.

In India too, the same principles were followed. In the case of A. Raman and Co[6] Justice Shah (as the then was) observed:

"Avoidance of tax liability by so arranging commercial affairs that charge of tax is distributed is not prohibited. A taxpayer may resort to a device to divert the income before it accrues or arises to him. Effectiveness of the device depends not upon considerations of

2 The Decision of the Supreme Court in McDowell and Co. Ltd vs. CTO [1985] 154 ITR 148

3 The decision of the Supreme Court in UOI vs. Azadi Bachao Andolan [2003] 263 ITR 706

4 The decision of the Supreme Court in Vodafone International Holdings B.V. vs. UOI [2012] 341 ITR1 (SC)

5 IRC vs. Duke of Westminster [1935] All ER 259 (HL)

6 CIT vs. A Raman & Co [1967] 67 ITR 11 (SC)

morality, but on the operation of the Income-tax Act. Legislative injunction in taxing statutes may not. except on peril of penalty, be violated, but it may lawfully be circumvented."

It is seen from the above that tax avoidance was not necessarily frowned upon by the Courts so long as the form of the transaction was legal and that more importantly, the principle that a taxpayer was entitled to manage his affairs to achieve the least tax liability, so long as he did not do anything unlawful was clearly set in the minds of the Courts in that period.

The McDowell case and the signs of shift in thought

McDowell was a simple case of whether excise duty paid voluntarily by the buyer to the State Government, would form part of the turnover of the manufacturer for the purpose of levy of sales tax under the Andhra Pradesh Sales Tax Act. The Court had merely to decide whether the manufacturer could legitimately reduce his sales tax lability in this manner. The ratio of the decisions may not be relevant but the observations of the Supreme Court and particularly that of Chinappa Reddy, J, are quite relevant. Reference was made to three decisions of the House of Lords.[7] The House of Lords, during 1980's, began to attach a "purposive interpretation approach" and gradually began to lay higher emphasis on the "economic substance doctrine" as a question of statutory interpretation. In the case of Ramsay (supra), the House of Lords considered this question again. That was a case whereby the taxpayer entered into a circular series of transactions designed to produce a loss for tax purposes, but which together produced no commercial result. If one saw the transaction as a whole, the series of transactions was self-cancelling, the taxpayer was in precisely the same commercial position at the end as at the beginning of the series of transactions. House of Lords ruled that, notwithstanding the rule in Duke of Westminster's case, the series of transactions should be disregarded for tax purposes and the manufactured loss, therefore, was not available to the taxpayer. Lord Wilberforce opined as follows:

"While obliging the court to accept documents or transactions, found to be genuine, as such, it does not compel the court to look at a document or a transaction in blinkers, isolated from any context to which it properly belongs. If it can be seen that a document or transaction was intended to have effect as part of a nexus or series of transactions, or as an ingredient of a wider transaction intended as a whole, there is nothing in the doctrine to prevent it being so regarded; to do so in not to prefer form to substance, or substance to form. It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions intended to operate as such, it is that series or combination which may be regarded."

The House of Lords, therefore, made the following important remarks concerning what action the Court should consider in cases that involve tax avoidance:

7 W.T Ramsay vs. IRC [1982] AC 300, IRC vs. Burmah Oil Co. Ltd [1982] STC 30, Furniss vs. Dawson [1984] 1 All ER 530.

(1) A taxpayer was only to be taxed if the Legislation clearly indicated that this was the case;

(2) A taxpayer was entitled to manage his or her affairs so as to reduce tax;

(3) Even if the purpose or object of a transaction was to avoid tax this did not invalidate a transaction unless an anti- avoidance provision applied; and

(4) If a document or transaction was genuine and not a sham in the traditional sense, the Court had to adhere to the form of the transaction following the Duke Westminster concept.

The House of Lords, had to deal with another tax avoidance scheme in Dawson's case too (supra). The Dawsons, in that case, held shares in two operating companies which agreed in principle in September 1971 to sell their entire shareholding to Wood Bastow Holdings Ltd. Acting on advice, to escape capital gains tax, the Dawsons decided not to sell directly to Wood Bastow, rather arranged to exchange their shares for shares in an investment company to be incorporated in the Isle of Man, Greenjacket Investments Ltd. was then incorporated in the Isle of Man on 16-12-1971 and two arrangements were finalised (i) Greenjacket would purchase Dawsons shares in the operating company for GBP 152,000 to be satisfied by the issue of shares of Greenjacket and (ii) an agreement for Greenjacket to sell the shares in the operating company to Wood Bastow for GBP 152,000.

The High Court and the Court of Appeal ruled that Ramsay principle applied only where steps forming part of the scheme were self-cancelling and they considered that it did not allow share exchange and sale agreements to be distributed as steps in the scheme, because they had an enduring legal effect. The House of Lords, however, held that steps inserted in a preordained series of transactions with no commercial purpose other than tax avoidance should be disregarded for tax purposes, notwithstanding that the inserted step (i.e. the introduction of Greenjacket) had a business effect. Lord Brightman stated that inserted step had no business purpose apart from the deferment of tax, although it had a business effect of tax avoidance,

The House of Lords in Craven's case[8] clarified the position further. In that case, the taxpayers exchanged their shares in a company (Q Ltd.) for shares in an Isle of Man holding company (M Ltd.), in anticipation of a potential sale or merger of the business. Taxpayers, in the meanwhile, had abandoned negotiations with one interested party, and later concluded a sale of Q Ltd's shares with another. M Ltd subsequently loaned the entire sale proceeds to the taxpayers, who appealed against assessments to capital gains tax. The House of Lords held in favour of the taxpayers, dismissing the Crown's appeal by a majority of three to two. The House of Lords noticed that when the share exchange took place, there was no certainty that the shares in Q Ltd would be sold. Lord Oliver, speaking for the majority,

8 Craven vs. White [188] 3 All ER 495

opined that Ramsay, Burmah and Dawson did not produce any legal principle that would nullify any transaction that has no intention besides tax avoidance and opined as follows:

"My Lords, for my part I find myself unable to accept that Dawson either established or can properly be used to support a general proposition that any transaction which is effected for avoiding tax on a contemplated subsequent transaction and is therefore planned, is for that reason, necessarily to be treated as one with that subsequent transaction and as having no independent effect."

It can be seen from the above that though the basic principles did not change and that the legal form of a transaction was still being looked at, the tolerance for arrangements that resulted in tax avoidance had begun to reduce in the 1980's and that the judges in McDowell also saw the arrangement therein as being a colourable device to evade tax and therefore did not accept the claim of the manufacturer in that case. The majority of the judges ruled that tax avoidance, if legitimate was permissible and Justice Chinappa Reddy too concurred. In explaining however, the eloquence with which the English decisions were cited and the principles emanating therefrom were articulated, the message that tolerance for tax avoidance schemes was on the wane, did somewhere appear to have been the target. This however was not the end of the matter as we will see in the next section.

The post economic liberalisation era and Azadi Bachao Andolan's Case[9]

Post the landmark budget of 1985-86, the Indian fiscal landscape changed. The economic liberalisation in 1991, which opened the doors of the Indian economy to foreign investment marked another era in tax jurisprudence. Foreign Institutional Investors ('FIIs') began investing in the shares of Indian companies that were listed on the stock exchange and one saw unprecedented foreign investment coming into the badly starved economy giving it a chance to transform itself. This foreign investment primarily, as statistics tell us, came from pooled funds of foreign investors which were located in tax friendly jurisdictions, that had favourable tax treaties with India, as a result of which India, under the tax treaty or Double Tax Avoidance Agreement (also referred to hereinafter as 'DTAA' or 'treaty') gave up its right to tax capital gains on the transfer of shares of an Indian company, which were derived by a resident of the treaty partner state. These pools of funds were either located in the treaty partner jurisdictions, or, as was noticed by many, a subsidiary was incorporated in the treaty partner jurisdiction, which earned the capital gains mentioned above, and these gains were not subject to tax in India by virtue of the mutually agree treaty provisions. Mauritius, due to various commercial advantages, became the most favoured treaty partner jurisdiction for investment into India. Gains of significant

9 Union of India vs. Azadi Bachao Andolan[2003]263 ITR 706 (SC)

amounts were earned by Mauritius based taxpayers (pools or their subsidiaries as the case may be) and these, due to the liberalised foreign exchange law, (the relatively 'civil' Foreign Exchange Management Act, 1999 ['FEMA'] replacing the 'draconian' Foreign Exchange Regulation Act, 1973 ['FERA']), the gains started being remitted back to Mauritius without suffering tax in India. This, understandably, kindled the curiosity of the Indian income-tax authorities ('ITA') which then started to investigate these 'arrangements' or 'structures'. Notices were issued to several FIIS in the year 2000, which then set the proverbial cat amongst the pigeons and led to widespread publicity in the national and international press, leading to certain executive actions being taken thereafter, which are not the subject matter of this article. What is however noteworthy is that, certain taxpayers sought to achieve tax certainty by approaching the then newly constituted Authority for Advance Rulings ('AAR') to seek certainty on the tax costs of investing in India through the manner described above. The first notable decision of the AAR was in the 'NatWest Case'[10] as it is popularly known. A British Bank incorporated two subsidiaries in Mauritius for investing into an Indian Bank and the contention was that if the British Bank would have directly invested into India (which regulatorily, it could) the position was undisputed that the bank would have been liable to pay tax in India on the capital gains that it would have earned, had it invested directly. The AAR in rejecting the application for a ruling, held that the transaction was *prima facie* entered into to avoid tax and therefore declined to give a ruling. As against that, in another application, popularly known as the 'AIG Ruling',[11] where an American company incorporated several subsidiaries in Mauritius and one of them invested into India and where the prospectus etc. documented several reasons for choosing Mauritius as the investing jurisdiction, tax being one of them, the AAR accepted the fact that when multinationals invest in a country, tax is one of the aspects that they look at when doing so and when tax is one of the many factors in choosing an investing jurisdiction, the arrangement, *prima facie*, is not one for avoidance of tax, and therefore, a ruling was indeed given in the applicant's favour. Sceptics may probably want to contend that the idea of this applicant of 'hiding in plain sight' worked, but the fact remains that the AAR did consider the distinction between tax planning and tax evasion and also did consider whether there was a 'colourable device' to avoid tax. Presented with the facts that tax was not the sole, but one of the many considerations for choosing Mauritius as an investing jurisdiction, the AAR decided that *prima facie,* this was not such a case and therefore ruled in the applicant's favour. In the next couple of years, this aspect was again required to be decided by the Supreme Court in Azadi Bachao Andolan's case where in the wake of McDowell, many Courts in India had as the learned authors of Kanga and Palkhivala's commentary put it, misused the 'McDowell spirit'[12]. Azadi Bachao was a case where by a Public Interest

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10 XYZ in Re [1996] 220 ITR 337 (AAR)

11 XYZ in Re [1997] 224 ITR 473 (AAR)

12 Pun unintended.

Litigation, the validity of Circular 789 issued by the Central Board of Direct Taxes ('CBDT') on 13th April, 2000 was sought to be challenged. The Delhi High Court had ruled in favour of the petitioners and in appeal by the Central Government, the Supreme Court was again required to deal with the subject of tax planning and deal with the reconciliation of the 'Westminster principle' with the 'McDowell Spirit' taking into account the observations of Shah J, in Raman's case (supra). The Hon. Supreme Court, a Bench of two judges, Ruma Pal and B. N. Shrikrishna JJ did that beautifully. They held that the principle laid out in the Duke of Westminister's case (supra) was very much alive both in England, the country of its birth, as well as in India. Tax planning may be legitimate provided it is within the framework of law. Colourable devices cannot be part of tax planning and 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 following passage therefrom, makes this clear:

"In our view the proper way to construe a taxing statute, while considering a device to avoid tax, is not to ask whether a provision should be construed liberally or principally, nor whether the transaction is not unreal and not prohibited by the statute, but whether the transaction is a device to avoid tax, and whether the transaction is such that the judicial process may accord its approval to it."

The Supreme Court went on to trace judicial precedent in England over time, and after noting all the previous jurisprudence on the subject, correctly explained McDowell's case and had set the law in the right perspective in India. It held that not only was tax avoidance legal and permissible but particularly as far as treaty shopping was concerned, the conscious decision to permit the same by developing countries, to facilitate trade and commerce and to consequently generate economic development, could not be lost sight of and indeed, given some degree of primacy as compared to collection of tax. The concept of 'viewing the larger picture' was therefore adopted by the Supreme Court and this decision is regarded by the students of tax as one of the most noteworthy in their study of the law. Tax is only one of the (and no doubt an important one) factors that drive business as well as economic decisions.

The Vodafone Case – The final case in the triology

After the decision in Azadi Bachao's case, the tax authorities had raised an argument in several cases as also the Vodafone case, that that the anti-avoidance principles in McDowell's case should continue to prevail as McDowell was a judgement delivered by five judges and Azadi Bachao was only a two judge decision. This argument fails to appreciate that when a decision of a larger Bench is interpreted by a smaller Bench then, the interpretation of the smaller Bench would bind all lower authorities. Azadi Bachao's decision extensively discusses the principles in McDowell and as such, cannot be termed as delivered per incuriam.

The Supreme Court in Vodafone, examined this issue and the following principles can be summarized in the decision delivered by Kapadia C.J.:

(1) The observations of Chinappa Reddy J, in McDowell's case on the need to depart from the 'Westminster principle' were only in the context of an artificial or colourable device.

(2) All tax planning cannot be treated as illegal/impermissible/illegitimate and even Chinappa Reddy J. made a distinction between schemes and devices and legitimate tax planning

(3) Chinappa Reddy J. had agreed with the majority view that tax planning within the framework of the law was permissible.

(4) There is no conflict between McDowell's case and Azadi Bachao's case.

The concurring decision of Radhakrishnan, J. has considered the difference between tax planning and tax evasion in great detail and thereafter also considered whether the decision in Azadi Bachao's case needs reconsideration. It was correctly held that the view of Reddy J. in McDowell was not the ratio of that decision but merely an opinion. Thus, it may not be correct to say that the ratio in McDowell was contrary to what has been said in Azadi Bachao. The Vodafone decision thus reiterated that every taxpayer can so arrange his affairs so that taxes are as low as possible and he is not bound to choose that pattern which would 'replenish the Government's coffers'.[13]

Conclusion

Does this therefore mean that GAAR changes the position which has been developed after long and interesting judicial debate? Does it mean that a taxpayer no longer can choose the path of 'least tax' and therefore should opt for the 'highest tax' option available? Is paying lower taxes (which is possible without infringement of the law) 'immoral' and therefore punishable? One would, with due consideration to the sweeping language of the provisions in the Chapter on GAAR in the Act, want to argue that that getting a taxpayer to pay tax in all cases where a more efficient alternative is available, was not the intention of enacting GAAR and that GAAR was intended more as a protection for the tax authorities against devices which were legal but have no commercial purpose other than reducing tax liability. It was intended to be more of a stick to be wielded with great discretion and not a 'lethal weapon' in their hands. Time will of course, tell, as it always does, as to how GAAR actually gets implemented, but the fact remains that the debate is far from over. Anew chapter has begun and in the years to come, we will see more jurisprudence and maybe more clarity will hopefully emerge.

The decisions delivered over the years and the principles emerging therefrom, to my mind, are still relevant, and will aid taxpayers in formulating their defence in case GAAR is invoked in their case.

13 13 Kanga & Palkhivala's commentary, 10th edition, page 58

CA Ganesh Rajgopalan

Comparable GAAR rules in USA, UK, South Africa, Australia

The general anti avoidance rules have been introduced in the Indian direct tax landscape recently. It will be some years before the judicial examination of the provisions and their interpretation by the courts are available as guidance to the taxpayers and the administrators. In this scenario, a scan of the legal provisions with countries with codified GAAR may provide some insights. This article attempts to do a comparison of the GAAR of Australia, South Africa and the United Kingdom. Though the comparison is not comprehensive, it aims to touch upon the significant areas and hopefully provide to the reader some straws in the wind about how the provisions will be understood in the future.

Australia

Australian GAAR is contained in the Part IVA of the Income Tax Assessment Act, 1936 (ITAA 36). Part IVA replaced section 260 of the ITAA 36 in 1981. The key elements of the GAAR are existence of a scheme from which the taxpayer must derive a tax benefit and the scheme must have been entered into for the sole or dominant purpose of obtaining a tax benefit. Such a scheme will entitle the Commissioner to make a determination to cancel the tax benefits obtained by the taxpayer and also attract penalties.

Scheme

Under Part IVA provisions, a scheme is defined similar to the definition of the term arrangement in section 102(1) of the ITA and covers all transactions, arrangements and even informal understandings entered into by a taxpayer and includes reference to a unilateral scheme, plan, proposal, action, course of action or course of conduct.[1] Contrastingly, whether or not an arrangement requires more than one party is not explicitly specified in section 102(1) of the ITA though the author believes that the definition under the Indian GAAR covers unilateral acts as well.

As it was felt that Part IVA was ineffective to counter arrangements that have been carried out with a relevant tax avoidance purpose, the provisions were amended to apply to schemes that are entered into, commenced to be carried out, on or after 16th November, 2012. The amendments are prospective and do not apply to pre-existing arrangements on that date. In contrast, the provisions of Chapter X-A apply to any arrangement irrespective of the date it was entered into in respect of a tax benefit obtained on or after 1st April, 2017.[2]

Tax benefit

A scheme must have a related tax benefit to be covered under Part IVA. Tax benefit refers to

1. ITAA 36, section 177A(1).
2. Income-tax Rules, 1962, rule 10U(2).

specified beneficial elements which are relevant to calculate the tax liability like any income not included in assessable income, increase in deduction, a capital loss incurred, a foreign tax credit or reduction of withholding tax.[3] This is similar to the provisions of Section 102(10) of the ITA except that the Indian definition does not cover reduction in withholding tax as a tax benefit.

Under Part IVA, the elements referred to above lead to a tax benefit if (i) they would not have been available or (ii) might reasonably be expected not to have been available to the taxpayer if the scheme had not been carried out. These two limbs represent alternative bases upon which the existence of a tax benefit can be demonstrated. The examination of the first limb ('would not have been available') is required to be made on the basis of an alternative when postulating comprising all the events or circumstances that actually happened or existed other than those forming part of the scheme. In this hypothesis, the scheme must be assumed not to have happened, to have been annihilated, deleted or extinguished. This is also referred to as the 'annihilation approach'. This approach is simple and effective to identify a tax benefit in cases where the scheme in question does not result in material non-tax consequences for the taxpayer.[4]

The annihilation approach may not be successful in identifying any tax benefit in cases where there are commercial, non-tax results of a scheme. In such cases, in order to identify the tax benefit, it may be necessary to speculate on a reasonable alternative that would have been undertaken by the taxpayer if he had not undertaken the scheme. The second limb 'might reasonably be expected to have' in the sub-section 177C paragraphs operate on the basis of postulates that are reasonable alternatives to the scheme. Under this 'reconstruction approach', the transactions are reconstructed based on a reasonable expectation that the commercial results aimed to be achieved by the scheme shall be achieved. In this examination, the taxpayer does not have the defence that he would have done nothing (in place of the scheme) because of the higher potential tax costs which he would have had to bear on the denial of the tax benefit.

A reasonable postulate (alternative) is necessary to reconstruct the scheme so as to determine the tax benefit. However, the criteria contained in s. 177D of the ITAA 36 in respect of the dominant purpose of the scheme (see next paragraph below) is first to be applied to the postulate to ascertain whether or not that postulate is reasonable. The dominant purpose test is the 'fulcrum' or pivot around which the amended Part IVA operates.[5] This requires an inquiry first about whether a person participated in a scheme for the sole or dominant purpose of enabling the taxpayer to obtain a tax benefit based on the criteria specified in section 177D and thereafter going into the presence of any tax benefit.

In the Indian context, there is no such explicit requirement or guidance to first ascertain the main purpose of the arrangement and then determine existence of a tax benefit though arguably, both these determinations are part of a single enquiry: whether the taxpayer participated in an arrangement for the main purpose of obtaining tax benefit?

Purpose

The application of Part IVA requires a dominant purpose of obtaining the relevant tax benefit.[6] Dominant purpose means the 'ruling, prevailing or most influential' purpose.[7] The determination of purpose is an objective exercise based on

3. ITAA 36, section 177C.
4. Explanatory Memorandum to the Tax Laws Amendment (Countering Tax Avoidance and Multinational Profit Shifting) Bill, 2013 ("Explanatory Memorandum"), Paras 1.77 to 1.84.
5. Explanatory Memorandum, Para 1.71.
6. ITAA, 36, section 177A(5).
7. FCT vs. Spotless Services Ltd. [1996] HCA 34; (1996) 186 CLR 404

the eight criteria listed out in Part IVA.[8] These criteria are not exhaustive,[9] and relate to the manner in which the scheme was carried out, its form and substance and its timing. In contrast, the requirement in Indian GAAR is the determination of the main purpose.[10] There are no criteria laid down to assist in the determination of purpose though arguably what is to be examined is the result or effect of the arrangement and not the subjective intention of the parties to the arrangement.

Cancellation of tax benefit

The Commissioner can make a determination under section 177F where it is established that the taxpayer has obtained a tax benefit in relation to a Part IVA scheme. This power of the commissioner includes power of reconstructing the transactions undertaken. The determination by the Commissioner is subject to right of appeal by the taxpayer.

GAAR Panel

In 2000, the Australian Tax Office ("ATO") established a GAAR panel, comprising of senior ATO officers and independent members drawn from the tax profession and academia. The objective of the Panel was to examine cases brought before it by the ATO and approve the use of the GAAR as the basis for assessments. The Panel provides its advice on the basis of the contentions of fact which have been put forward by the ATO and by the taxpayer. The Panel is not a platform for a hearing as part of a judicial or quasi-judicial review. In contrast to the Approving Panel in the Indian GAAR whose directions are binding on both the Tax Department and the taxpayer, the Australian GAAR Panel has no official status nor does it have a statutory basis; its role is purely consultative to the ATO as to whether or not it should proceed with an assessment that is based on the GAAR.

South Africa

Sections 80A-80L were introduced in the South African Income-tax Act, 1962 ("ITA 62") in place of the earlier GAAR contained in Section 103 of that Act. The old GAAR required all the following four requirements to be met for the provision to apply:

- There must be a transaction, operation or scheme;
- Which must result in the avoidance, reduction or postponement of tax (a tax benefit);
- The transaction, etc. must have been entered into or carried out in a manner not normally employed for a transaction of that nature (the abnormality requirement);
- The transaction, etc. must have been entered into solely or mainly for the purpose of obtaining a tax benefit.

The new GAAR is on the same lines as the earlier version though there are certain new elements. There are four requirements that must be met before the GAAR can be applied:

- The existence of an arrangement
- The arrangement results in a tax benefit
- The sole or main purpose of the avoidance arrangement is to obtain a tax benefit
- The avoidance arrangement is characterised by the presence of one or more of four tainted elements for arrangements in the context of business and one or more of three tainted elements for arrangements in the context other than business, which renders it an impermissible avoidance arrangement

Arrangement

An 'arrangement' is defined as 'any transaction, operation, scheme, agreement or understanding

8. ITAA 36, Section 177D.
9. Explanatory Memorandum, para 1.100.
10. ITA, Section 96(1).

(whether enforceable or not) and includes any of the foregoing involving the alienation of property'.[11] The definition in Chapter X-A is similar.[12] An arrangement requires a conscious involvement of two or more participants who arrive at an understanding. It cannot exist in a vacuum and presupposes a meeting of minds, which embodies an expectation as to future conduct between the parties, that is, an expectation by each that the other will act in a particular way.[13] Since the definition now includes the terms operations and scheme, even a unilateral operation or scheme could fall within the definition.

Similar to the Australian Part IVA provisions, the South African GAAR does not apply to pre-existing arrangements on 2nd November, 2006, the date the law became effective.[14] In contrast, the provisions of Chapter X-A apply to any arrangement irrespective of the date it was entered into in respect of a tax benefit obtained on or after 1st April, 2017.[15]

Tax benefit

The term 'tax benefit' is defined to include any avoidance, postponement or reduction of any liability for tax.[16] The tax liability in the definition refers to not an existing liability but an anticipated liability. The ordinary natural meaning of avoiding liability for a tax on income is to get out of the way of, or escape or prevent an anticipated liability.[17] The quantum of tax benefit is irrelevant in determining whether there is a tax benefit.

To ascertain whether there was a tax benefit, one has to determine whether or not "the taxpayer would have suffered tax but for the transaction".[18] For the Commissioner to conclude that a tax benefit has arisen as a result of the arrangement entered into, he has to show what alternative arrangement would otherwise have been entered into to produce the commercial result and the attendant tax consequences. However, the Draft Guidance issued by the South African Revenue (SARS) states that,[19] in preparing its view of the tax liability, the Revenue need not do a comparison to any other hypothetical arrangement and only need to compare the tax liability as computed by the taxpayer with the tax liability determined by the Revenue. This interpretation appears to be an overreach and may not be sustained by the courts.

The onus of establishing a tax benefit and the link between the tax benefit and the arrangement and what the taxpayer's position would have been had he not enter into the arrangement is on the Revenue. While determining existence of a tax benefit, the Revenue has powers to treat connected persons as the same person or disregard any accommodating or tax-indifferent party.[20] This power prevents a party from defeating the GAAR provisions by shifting an existing stream of income to a related person. Similar powers are available under the Indian law as well.[21]

11. ITA 62, section 80L.
12. ITA, section 102(1).
13. FCT vs. Newton [1958] 2 All ER 759 (PC).
14. ITA 62, section 80A preamble.
15. Income-tax Rules, 1962, rule 10U(2).
16. ITA 62, section 80T.
17. CIR v King 1947 (2) SA 196 (A), 14 SATC 184.
18. Income Tax Case No. 1625 (1996) 59 SATC 383.
19. SARS Draft Comprehensive Guidance to GAAR (2011) ("SARS Draft Guidance"), para 3.3.2.
20. ITA 62, section 80F.
21. ITA, section 99.

Sole or main purpose

Under section 103(1) of the ITA 62, the transaction, operation or scheme must have been entered into solely or mainly for the purpose of obtaining a tax benefit, whereby the sole or main purpose of tax avoidance had to be ascertained subjectively based on the intention of the taxpayer. The new provisions refer to the purpose of the arrangement,[22] which means the effect it seeks to achieve, the end accomplished or result attained. The South African provisions recognise that the purpose attributable to a step or part of the arrangement could differ from the purpose attributed to the arrangement as a whole,[23] and that the GAAR can be applied to a step in or a part of an arrangement.[24] There are similar provisions in Chapter X-A.[25]

The South African GAAR provides for a rebuttable presumption that an anti-avoidance arrangement was entered into with the sole or main purpose of obtaining a tax benefit.[26] This presumption places the burden of proof on the taxpayer requiring him to provide objective evidence to satisfy based upon a preponderance of probability that, reasonably considered in light of the relevant facts and circumstances, obtaining a tax benefit was not the sole or main purpose. There is no such presumption of main purpose explicitly provided in the Indian GAAR once the Tax Department proves existence of a tax benefit. However, it would be logical to expect the taxpayer would have to lead evidence regarding the purpose of the arrangement.

Tainted elements

An avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit and it contains the following tainted elements-[27]

(a) in the context of business,

- it was entered into or carried out by means or in a manner which would not normally be employed for *bona fide* business purposes, other than obtaining a tax benefit; or
- it lacks commercial substance, in whole or in part

(b) in a context other than business

- it was entered into or carried out by means or in a manner which would not normally be employed for *bona fide* business purposes, other than obtaining a tax benefit; or

(c) in any context

- it has created rights or obligations that would not normally be created between persons dealing at arm's length; or
- it would result directly or indirectly in the misuse or abuse of the provisions of this Act (including the provisions of this Part).

The Indian provisions also have similar tainted elements to be satisfied for GAAR to be invoked. The means and manner test, abnormality test, the misuse or abuse of the Act test and the commercial substance test all find place in the Indian law with identical words.[28] However, the Indian provisions do not distinguish between a business context and other than business context. Accordingly, we have the lack of commercial substance test, though incongruous, required to be applied even in other than business context. Another difference which can be noticed is that

22. ITA 62, section 80G(1).
23. ITA 62, section 80G(2).
24. ITA 62, section 80H.
25. ITA, section 95, Explanation.
26. ITA 62, section 80G.
27. ITA 62, section 80A.
28. ITA, section 96(1), clauses (a) to (d).

in the means and manner test under the Indian law the *bona fide* purposes do not explicitly exclude the purpose of obtaining a tax benefit.[29]

Consequences

Once an arrangement is held to be impermissible, there are several tax consequences that may be determined by the Revenue. These include disregarding, combining, or re-characterising any steps in or parts of the impermissible arrangement, disregarding any accommodating or tax-indifferent party or treating any accommodating or tax-indifferent party and any other party as one and the same; deeming persons who are connected persons in relation to each other to be one and the same person for purposes of determining the tax treatment of any amount; reallocating or re-characterising any gross income, receipt or accrual of a capital nature or expenditure; or treating the impermissible avoidance arrangement as if it had not been entered into or carried out, or in such manner as in the circumstances of the case the Commissioner deems appropriate for the prevention or diminution of the relevant tax benefit.[30]

Under the Indian law, similar consequences in relation to tax, including denial of a tax benefit or a benefit under a tax treaty, can be determined in respect of an impermissible avoidance arrangement. These consequences may be determined as 'may be deemed appropriate' but there is no explicit limitation that such consequences should be limited to only the 'prevention or diminution of the relevant tax benefit' as is the requirement under the SA GAAR. A connected point is that the SA GAAR is not a charging section.[31] Contrastingly, in answer to a question whether the Indian GAAR will expand the scope of charging provisions of the Act, the CBDT has answered that in case an arrangement is declared to be impermissible, the consequences shall follow. The clarification leaves open the possibility of GAAR being treated as a charging provision with the consequences reversing the tax benefit, and more. The Indian Revenue's position in this respect is, at best, nebulous.

GAAR Panel

There is no provision in the SA GAAR or in practice to have a GAAR Panel. Though there were suggestions when the new GAAR was being formulated to have a centralised committee with a final authority to invoke GAAR for improving certainty for taxpayer, it did not find place in the legislation.

The United Kingdom GAAR

A large body of case law dealing with tax avoidance have emanated from the United Kingdom and have been relied upon by the Indian Courts. The Duke of Westminster principle that a taxpayer can arrange his affairs in such a way that he pays the least amount of tax held the centre-stage in India as well. Whether the Duke and his principle were dead or alive was a matter of intense judicial speculation.[32] In England, judicial indignation to aggressive approach of the taxpayer gave rise to the Ramsay decision and the birth of the 'new approach'. This approach required identifying pre-ordained series of steps to a transaction with no commercial purpose other than avoidance of tax and countering them. However, the subsequent rulings were not consistent in the application of the Ramsay approach and there was substantial dilution of this approach with the taxpayer successfully defending the tax avoidance charge.

This gave rise to a widely-held belief that countering of tax avoidance cannot be only

29. ITA, section 96(1)(d).
30. ITA 62, section 80B(1).
31. SARS Draft Guidance, page 7.
32. Refer Chinappa Reddy J in McDowell & Co. Ltd. v. CTO [1985] 154 ITR 148 (SC) declaring the Duke to be dead followed by Azadi Bachao Andolan [2003] 132 Taxman 373 (SC) wherein the Duke was resurrected.

based on judicial doctrines. The UK Government set up an expert group to study whether the United Kingdom should have a codified GAAR. The Group came out with what is called the Aaronson Report recommending a moderate targeted anti-abuse rule. Subsequently after consultation with business and profession, general anti-abuse rules (GAAR) were introduced in the law in 2013. The UK GAAR is strictly not an anti-avoidance legislation, but has been modelled on the lines of a targeted anti-abuse rule aimed at countering flagrant abuse.

Applicability

The UK GAAR will apply to any arrangement which is entered into on or after 17th July, 2013, the date on which the law was enacted. An arrangement prior to the insertion of the provisions could be referred to, but only if referring to that earlier arrangement would help show that the later arrangement was not abusive.[33] In contrast, the Indian GAAR applies to an arrangement whenever entered into in respect of a tax benefit obtained after GAAR provisions came into effect.[34]

The UK GAAR applies to income tax, capital gains tax, inheritance tax, corporation tax, a CFC charge, the bank levy, the oil supplementary charge and tonnage tax, petroleum revenue tax, diverted profits tax, apprenticeship levy, stamp duty land tax and annual tax on enveloped dwellings.[35] The GAAR also extends to cover National Insurance Contributions ("NICs") by separate legislation.[36] Notably, GAAR applies also to diverted profits tax,[37] which itself is an anti-avoidance rule. In contrast, the Indian GAAR applies only to income-tax. Any priority rule in the UK law shall have effect subject to the GAAR.[38] The position is similar in the Indian legislation.[39]

Arrangements

The term 'arrangements' includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable).[40] This is on the same lines as the definition of arrangement in section 102(1) except that definition of arrangement in Chapter XA includes any step in or any part of an arrangement.[41]

The arrangements can be viewed both narrowly and widely, so that the GAAR can be applied to an arrangement that is part of a wider arrangement or to the wider arrangement as a whole. This is to prevent a tax scheme from being combined with a commercial transaction to avoid being termed as a 'tax arrangement'. While considering a tax arrangement which is part of a wider arrangement, then in determining whether that part is abusive, regard must also be had to the wider arrangement of which it is part.[42] The Indian GAAR does not have such a provision to have regard to such wider arrangement though it can be applied to a step in or a part of an arrangement.[43]

33. FA 2013, section 215
34. IT Rules, rule 10(U)(2)
35. Finance Act, 2013 ("FA 2013"), section 206(3)
36. National Insurance Contributions Act 2014, section 10.
37. DPT (effective from 1st April, 2015) was introduced to prevent multinationals entering into arrangements to divert profits from the UK either by avoid having a UK permanent establishment, or by making payments which lack economic substance
38. FA 2013, section 212(1)
39. ITA, section 95(1)
40. FA 2013, section 214(1)
41. ITA, Section 102(1)
42. FA 2013, section 207(3)
43. ITA, Section 95, Explanation

Abusive tax arrangements

The UK GAAR applies to "tax arrangements" which are "abusive". A 'tax arrangement' is defined as any arrangement if, having regard to all the circumstances, it would be reasonable to conclude that the obtaining of a tax advantage was the main purpose, or one of the main purposes, of the arrangements.[44]

Interestingly, the phrase 'main purpose or one of the main purposes' found in the above definition also found place in the definition of impermissible avoidance arrangement as originally enacted in the Indian legislation. After a lot of public outcry, the definition was amended and the requirement now only includes the term 'main purpose'. These tests contained in the UK GAAR are objective tests and it is not necessary or appropriate to enquire about the taxpayer's intention to derive a tax advantage. In the author's opinion, one can draw the same conclusion in respect of the 'main purpose' test contained in section 96(1) of the ITA.

The 'main purpose' test is explained as where the arrangement would not have been carried out at all were it not for the opportunity to obtain the tax advantage or where any non-tax objective was secondary to the benefit of obtaining the tax advantage. The Indian GAAR also contains this test. The 'one of the main purposes' test examines whether a transaction which would otherwise have occurred has been changed resulting in a lower tax and the desired tax result is itself a substantial objective. This test widens the circumstances where an arrangement becomes a 'tax arrangement'. This test is notably absent in the Indian GAAR. Arguably, in the Indian context, an arrangement which would have occurred irrespective of any tax benefit since it is entered into for commercial or non-tax purposes would not be caught in the examination of the arrangement as an impermissible avoidance arrangement if the tax benefit is the substantial purpose but not the main purpose.

"Tax advantage" is broadly defined to include (a) relief or increased relief from tax, (b) repayment or increased repayment of tax, (c) avoidance or reduction of a charge to tax or an assessment to tax, (d) avoidance of a possible assessment to tax, (e) deferral of a payment of tax or advancement of a repayment of tax, and (f) avoidance of an obligation to deduct or account for tax.[45] This definition is largely similar to the definition of "tax benefit" under the Indian GAAR.

Tax arrangements are defined to be 'abusive' if the entering into or carrying out of such arrangements cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances.[46] This is the 'double reasonableness test' which is unique to the UK GAAR. The Advisory Panel and the courts are not to decide what they believe would have been reasonable but rather they have to decide what could reasonably be regarded as reasonable. This test reinforces the moderate nature of the UK GAAR and offers a significant safeguard for the taxpayer.

The circumstances to be examined while testing whether a tax arrangement is abusive includes:

(a) whether the substantive results of the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions,

(b) whether the means of achieving those results involves one or more contrived or abnormal steps, and

44. Section 207(1).

45. FA 2013, section 208.

46. FA 2013, section 207(2).

(c) whether the arrangements are intended to exploit any shortcomings in those provisions.

The above objective tests for determining whether a tax arrangement is abusive are similar to the testing for the tainted elements, viz., the misuse or abuse of the law test, the abnormality test or the means and manner test contained in section 96(1) of the ITA.

Counteraction

If a tax arrangement is determined to be abusive, the tax advantages arising from the arrangement are to be counteracted by making just and reasonable adjustments in respect of the taxes covered by the GAAR. These adjustments are to be made by way of an assessment or reassessment or by amendment or disallowance of a claim as the case may be. The "just and reasonable" nature of the counteracting adjustment allows for moderation as to the consequences. The guidance is provided that where there are various alternative transactions which could have been carried out by the taxpayer in place of the abusive transaction, the counteracting adjustment need not select the alternative which would result in the highest tax charge.[47] In contrast, under the Indian GAAR, the consequences in relation to tax of an impermissible avoidance arrangement include but are not limited to the denial of tax benefit or a benefit under a tax treaty. The powers of the assessing officer in this regard are extensive. However, such determination of consequences by him should be in a manner as is "deemed to be appropriate". These powers are subject to appeal and judicial review.

Consequential adjustments

Under the UK GAAR, a person can within 12 months of the date when a counteraction becomes final, make a claim for consequential adjustments to be made in respect of any tax to which the GAAR applies.[48] There are no such provisions available in the Indian GAAR.

SAAR and GAAR

The GAAR operates independently of the SAARs and can be applied where an abusive arrangement is used to counteract these SAARS.[49] Where the SAAR is successful in preventing avoidance of tax, there would be no occasion to apply GAAR. However, a taxpayer cannot object to the use of the GAAR simply because all other means available to HMRC to tackle what they consider an abusive arrangement have not been utilised.[50] In the Indian context, the use of this approach is echoed by the CBDT in its Circular wherein it is clarified that the provisions of both GAAR and SAAR can co-exist.[51] Also, the operation of Chapter XA is in addition to or in lieu of any other basis of determining tax liability.[52]

GAAR and the DTAAs

Double tax treaties aim to allocate taxing rights between the treaty States in relation to the income earned by an enterprise. Mere benefit derived by an enterprise from the operation of these rules does not mean that the arrangements are abusive for the GAAR to apply.[53]

However, GAAR can be applied to counteract abusive arrangements where such arrangements exploit a particular treaty provision or exploit

47. HMRC's GAAR Guidance (2013) ("HMRC's Guidance"), para B13.3.
48. FA 2013, section 210.
49. HMRC's Guidance, para B7.
50. HMRC's Guidance, para B6.2.
51. CBDT Circular No. 7 of 2017 [F.No.500/43/2016-FT&TR-IV], dated 27-1-2017, Question No.1.
52. ITA, section 100.
53. HMRC's Guidance, para B5.2.

the way in which such provisions interact with other provisions in the UK domestic tax law. The position under the Indian GAAR is much more specific. In the Indian law, the GAAR can override a treaty provision.[54] Once an arrangement is declared to be impermissible, the assessing officer is empowered to determine the consequences in relation to tax including denying a benefit under a tax treaty.

Advisory Panel

Before the HMRC can take steps for counteraction, the case has to be submitted to an Advisory Panel. The Panel will have three members all of whom will be independent of the HMRC. The Panel is required to give its view if unanimous, or separate views, if different, as to whether the tax arrangement is a reasonable course of action. The HMRC is required to take into account the views of the Advisory Panel though it is free to continue the process to counteract any tax advantage if it has cogent reasons for doing so. The Advisory Panel is not a Tribunal or Court. Its views are not binding though they have to be taken by the Courts or Tribunals while deciding. In contrast, the Indian GAAR has an Approving Panel whose directions are binding on both the taxpayer and the revenue.

Summary

The above brief descriptions of the GAAR legislations of select countries provide a swathe of different approaches to combat tax avoidance. The Australian approach attacks tax avoidance quite vigorously while the UK approach is more benevolent. The South African GAAR has sought to tackle the limitations of the tax avoidance legislations in that country as well as the experience of other countries, notably Canada, while drafting its 2006 GAAR legislation. The Indian GAAR is largely drafted on the lines of the South African GAAR. The administration of Indian GAAR in the form of binding directions of an Approving Panel without recourse to appeal is worrisome. Since the Indian GAAR is largely similar to the South African legislation, the jurisprudence in South Africa on the new GAAR will be watched keenly in our country. Further, how the GAAR will be adopted by the administrator and the Courts in the Indian scenario is to be seen.

54. ITA, section 90(2A).

Keep your thoughts positive because your thoughts become your words. Keep your words positive because your words become your behaviour. Keep your behaviour positive because your behaviour becomes your habits. Keep your habits positive because your habits become your values. Keep your values positive because your values become your destiny.

— *Mahatma Gandhi*

CA Nitin Karve

SAAR versus GAAR – Hierarchy

Background

SAARs and the GAAR

Till fairly recent times, it was an accepted position that to comply with the tax laws it was sufficient to comply with the clear words of the law. Subject to that, taxpayers could so arrange their affairs as to minimise the tax payable by them.

From time to time, cases of tax avoidance were brought to the notice of the legislature, which then brought in provisions to counteract such avoidance where possible. Perhaps the first anti-avoidance provision in Indian income-tax law was introduced in 1918, as section 33(2) of the Indian Income-tax Act, 1918. This provision subsequently became the original section 92 of the Income-tax Act, 1961 ('the Act'). Other examples of anti-avoidance provisions introduced thereafter include sections 60 to 64, 93, 94, the original sections 79 and 104, etc.

Each of these provisions was intended to counteract specific opportunities for tax avoidance. Each such provision is now generally referred to as a Specific Anti-Avoidance Rule ('SAAR'). A SAAR may be contained also in a tax treaty which India has entered into with another country.

The term SAAR distinguishes these provisions from the General Anti-Avoidance Rule ('GAAR') introduced in the Act in 2012 in the form of the new sections 95 to 103 (Chapter X-A). These provisions empower the tax authorities to modify the tax consequences of an impermissible avoidance arrangement. The provisions are not restricted to counteracting any particular avoidance opportunity. They can potentially apply generally to any arrangement by which tax is sought to be avoided – hence the name.

While the GAAR is of general application, a case may arise where a situation is expressly dealt with by a SAAR. The question then arises whether only the SAAR will apply, or both the GAAR and the SAAR will apply. One can rule out a third possibility, that only the GAAR should apply, since it would mean that the GAAR had repealed all the SAARs, and these provisions do not support this view.

The inter-relationship between the GAAR and the various SAARs is discussed below. Before looking into this aspect, it would be worthwhile to examine the old and new approaches to tax avoidance, and to see why opportunities for tax avoidance arise.

The two approaches

The orthodox approach

In the case of *IRC vs. Duke of Westminster*[1], Lord Atkin observed:

> " ... the subject, whether poor and humble or wealthy and noble, has the legal right so to dispose of his capital and income as to attract upon himself the least amount of tax. The only function of a Court of law is to determine the legal result of his dispositions so far as they affect tax."

In the same case, at p. 24, Lord Russell of Killowen observed:

> "The subject is not taxable by inference or by analogy, but only by the plain words of a statute applicable to the facts and circumstances of his case."

The winds of change

In a speech at the Osmania University on March 21, 1980[2], Justice Chinnappa Reddy said:

> "In the case of Taxing statutes again, outmoded view points and principles of interpretation persist. ***The courts appear to view tax avoidance with affection*** and go to the extent of saying that it is perfectly open for persons to evade income-tax if they can do so legally. This attitude has to change. The Judicial smile must freeze into a judicial frown. Tax avoidance is unethical for the simple reason that it transfers the burden of tax liability to the shoulders of the guileless good citizens from those of the 'artful dodgers'. In the matter of interpretation, the judiciary persistently applies the principle that fiscal statutes must be construed strictly. That must change." (emphasis supplied)

In the early 1980s, the judicial approach to tax avoidance in the UK changed. In India, this new approach was commented upon and followed by the Supreme Court in the case of *McDowell & Co. Ltd. vs. CTO*[3], where Justice Reddy said:

> " ... there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is a pretence to say that avoidance of taxation is not unethical and that it stands on no less moral plane than honest payment of taxation."

Judicial affection for tax avoidance

Contrary to what Justice Reddy said in his Osmania speech, it is open to question whether the *Westminster* approach was based on 'affection' for tax avoidance.

As early as 1869, Lord Cairns commented in *Partington vs. AG*[4], as follows:

> "If the person sought to be taxed comes within the letter of the law he must be taxed, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be."

In *Cape Brandy Syndicate vs. IRC*[5], Rowlatt J. observed:

> " ... it is often endeavoured to give to that maxim [that 'in a taxing Act clear words are necessary to tax the subject'] a wide and fanciful construction. It does not mean that words are to be unduly restricted against the Crown or that there is to be any discrimination against the Crown in such Acts. It means this, I think; it means that in taxation you have to look simply at what is clearly said. There is no room for any intendment; there is no equity about

1 [1936] AC 1, 8

2 Frontier, Vol. 46, No. 9, September 8 - 14, 2013

3 [1985] 154 ITR 148, 160 (SC)

4 (1869) LR 4 HL 100, 122

5 12 TC 358, 366

> a tax: there is no presumption as to a tax; you read nothing in; you imply nothing, but you look fairly at what is said and at what is said clearly and that is the tax."

While *Cape Brandy Syndicate* is often cited in favour of taxpayers, the case was actually decided in favour of the revenue.

As can be seen, the idea that a taxpayer could arrange his affairs to minimise his taxes was based not upon an indulgent judicial attitude to tax avoidance or any judicial affection for tax avoidance, but upon the principle that a person should be taxed based upon clear words in the statute, whether those words created undue hardship to him or created an unfair advantage in his favour. Even the observations of Lord Russell of Killowen in the Westminster case bear this out.

A double-edged sword

Even the best of policymakers and draftsmen with all the skills and attributes required for their respective jobs cannot imagine every situation in which a law proposed by them can potentially apply or every possible interpretation of the words used in that law.

Hence, as noted by Lord Cairns in *Partington*, sometimes the letter of the law can unfairly cause great hardship to a taxpayer, or equally unfairly provide him a benefit which might not have been intended for him. The argument that fiscal legislation must be interpreted based on the letter of the law is therefore a double-edged sword, with the potential of unfairly hurting the taxpayer or the revenue.

The new approach

In recent years, there have been arguments to the effect that taxes should be paid based not only on the plain words of the statute, but on some underlying sense of morality also. This is what Justice Reddy said, in different words, at Osmania University and in the *McDowell* case.

The GAAR appears to have emerged from some such philosophy based on perceived morality.

The term 'tax morality', though used widely, means different things to different people. Terms like 'tax morality', 'fairness', 'spirit of the law', 'substance', etc. have much in common. All of them seem to be equitable concepts, and raise certain common issues.

It is not intuitively obvious that there is a common underlying theme of morality or fairness in the income-tax law, or that the law is based on 'substance', or that there is an underlying spirit pervading the law. For a law which suffers at least fifty amendments every year from different people with differing philosophies, it would be a struggle to find a common theme of any kind, whether it be of tax morality or of fairness or of some underlying 'spirit', or of some core concept of 'substance'.

A much firmer basis for defining an anti-avoidance policy would be to say that the legislative intention should not be subverted. That can be the only basis for saying that tax avoidance is 'impermissible'. Where a person invests money or locates manufacturing plants based on the signals the legislature provides by way of incentives, the tax benefit is a key element in the choices made and is consistent with the legislative intent. Certainly, such choices should not be 'impermissible'.

One fundamental flaw of the new approach and the GAAR is that it has sought to focus on only one edge of the double-edged sword. The possibility that the letter of the law can unfairly cause great hardship to a taxpayer contrary to the legislative intention, and that such outcomes should also be addressed in the application of the law has not been considered at all.

This background is important while addressing the issue of how the GAAR should interact with a SAAR.

GAAR v. SAAR

Difference between a SAAR and the GAAR

As observed earlier, a SAAR is a provision brought in to counteract the possibility of tax avoidance relating to a specific situation. Where such a possibility is brought to the notice of the legislature, the legislature applies its mind to the relevant situation, identifies the tax benefit, and defines what constitutes impermissible avoidance. Based on that, the precise remedy for that avoidance is also identified and defined by legislature. A SAAR is generally a binding legal rule. In many cases, SAARs ignore the taxpayer's motives altogether.

The GAAR, on the other hand, is a very non-specific provision, based largely on the taxpayer's motives. An important point to note is that it is not an inherently binding legal rule. It is merely an enabling power granting discretion to tax officers to identify what is impermissible tax avoidance and to counter it, within defined limits.

Does the GAAR override a SAAR?

As mentioned earlier, while the GAAR is of general application, a case may arise where a situation is expressly dealt with by a SAAR, and the question arises as to which should apply.

The Revenue view

It is the view of the Central Board of Direct Taxes ('CBDT'), set out in a Circular, that the provisions of the GAAR can coexist with SAARs and can apply, as may be necessary, depending on the facts and circumstances of each case.[6] As regards tax treaties, if a case of avoidance 'is sufficiently addressed by' the Limitation on Benefits clause of the treaty, there is no occasion to invoke the GAAR, but anti-abuse rules in a treaty 'may not be sufficient to address all tax avoidance strategies', and hence the GAAR can be invoked.[7]

It should be noted that the views of the Revenue are not binding on taxpayers or on appellate authorities, but are indicative of the basis on which tax officers will invoke the GAAR.

'Non obstante' clause

Section 95, the key GAAR provision, begins with the words: "Notwithstanding anything contained in the Act … ".

As against this, section 40 begins with: 'Notwithstanding anything contained in sections 30 to 38 … ', and section 40A(1) begins with: 'The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other provision of the Act relating to the computation of income under the head "Profits and gains of business and profession" … '.

Sections 60 to 64 and 92 to 94 do not have a non obstante clause.

Because the various SAARs either have no non obstante clause, or have a limited clause, prima facie, no SAAR will override the GAAR.

However, a non *obstante* clause only deals with a situation where there is a direct conflict between two provisions.

One still has to evaluate whether any of the GAAR provisions are in conflict with the SAARs.

Also, given that the GAAR does not lay down any binding legal rule, but merely grants discretion to tax officers, one has to evaluate the limits of that discretion.

The relevant provision

Section 100 of the Act reads as follows:

100. Application of this Chapter.– The provisions of this Chapter shall apply in addition to, or in lieu of, any other basis for determination of tax liability.

These words are seemingly wide, but it is open to question whether 'any other basis' covers a SAAR, and the legislative material seems to suggest that this section was not intended to cover any SAAR.

It should be noted that the GAAR provisions introduced in 2012 were replaced in 2013. Section 100 as introduced in 2012 was in the same terms as above.

6 CBDT Circular No. 7 of 2017, dated 27th January, 2017, Question No. 1, [2017] 391 ITR 234 (St.), at p. 235

7 Question No. 2, ibid.

The legislative intent

For understanding the legislative intent, assistance can be taken from the Finance Minister's Budget speech, and the Explanatory Memorandum to the Finance Bill.

In the Budget speech for 2013-14, on the subject of the GAAR, the Finance Minister stated as follows:

"150. Hon'ble Members are aware that the Finance Act, 2012 introduced the General Anti Avoidance Rules, for short, GAAR. A number of representations were received against the new provisions. An Expert Committee was constituted to consult stakeholders and finalise the GAAR guidelines. After careful consideration of the report, Government announced certain decisions on 14-1-2013 which were widely welcomed. I propose to incorporate those decisions in the Income-tax Act."[8]

The Report of the Expert Committee (also known as the Shome Committee) contained the following comments, on the subject of the role of SAARs:

"In view of the above, the Committee recommends that where SAAR is applicable to a particular aspect/element, then GAAR shall not be invoked to look into that aspect/element. Similarly, where anti-avoidance rules are provided in a tax treaty in the form of limitation of benefit (as in the Singapore treaty) etc., the GAAR provisions shall not apply overriding the treaty. If there is evidence of violations of anti-avoidance provisions in the treaty, the treaty should be revisited, but GAAR should not override the treaty."[9] (emphasis in the original)

As stated in the Finance Minister's speech, the Government's response to the Shome Committee Report was announced by the Finance Minister on 14th January, 2013, in a press conference. The decisions announced were published by the Press Information Bureau. On the subject of the role of SAARs, the statement read:

"(xiii) Where GAAR and SAAR are both in force, **only one of them will apply to a given case,** and guidelines will be made regarding the applicability of one or the other." (emphasis in the original)

The Explanatory Memorandum to the Finance Bill[10] referred to the Shome Committee Report and to the fact that the major recommendations were accepted by the Government, with some modifications. However, it did not refer to the issue of SAAR versus the GAAR. Even the Notes on the Clauses in the Bill[11] do not refer to this issue.

From the above, it appears that nothing was expressly decided by Parliament on this issue, but the references in the Parliamentary material to the Shome Committee Report and to the Press Conference of 14th January, 2013, could amount to a representation to Parliament as to how the discretionary powers granted under the GAAR provisions were to be utilised by the tax authorities.

Also, the fact that it was not considered necessary to change section 100 might suggest that that provision does not include SAARs within its scope.

General versus special provisions

It is a settled principle that a general rule will not apply where a specific rule is available. Based on this rule, generally, where a SAAR exists covering a particular situation, the GAAR should not apply to that situation.

This rule applies to situations where there are specific and general rules in a statute covering the same ground. It should apply with greater force when a specific statutory rule is confronted by a general rule granting discretion to tax authorities, as in the case of the GAAR.

8 see 351 ITR, on p. 39 (St.), para 150

9 see 348 ITR, on page 38 (St.), conclusion in para 3.19

10 see 351 ITR, on page 186 (St.)

11 see 351 ITR, on page 138 (St.)

As mentioned earlier, in the case of a SAAR, the legislature applies its mind to the relevant provision, identifies the tax benefit, and defines what constitutes impermissible avoidance. Based on that, the precise remedy for that avoidance is also identified and defined by legislature.

Under the GAAR, the tax officer has discretion to identify the tax benefit, define what constitutes impermissible avoidance, and also identify the precise remedy for that avoidance.

It would not be reasonable for a discretionary power to be used to second-guess the legislature on these aspects.

The difference between the use of a discretionary power and a considered legislative response was brought out clearly in the case of *CIT vs. Walfort Share and Stock Brokers P. Ltd. [2010] 326 ITR 1 (SC),* where the taxpayer subscribed to mutual fund units on a cum-dividend basis, received the dividends, and immediately redeemed the units at a loss. The dividend earned was treated as exempt income, and the loss incurred as an allowable loss. The tax officer unsuccessfully sought to deny the allowance of the loss, by seeking to treat the transaction as a sham. He placed reliance on *McDowell and Co. vs. CTO [1985] 154 ITR 148 (SC)* and other cases. He also sought to deny the allowance of the loss under section 14A. The case related to the period prior to the introduction of sub-section (7) in section 94,

Subsequently, a SAAR was introduced in the form of section 94(7), dealing with dividend-stripping. Had this provision applied in the assessment year relevant to the case, the allowance of loss would have been denied only to the extent of the amount of the dividend. As against this, the tax officer had sought to deny the entire loss. This provision does not invoke section 14A at all. Nor does it treat the entire transaction as a sham.

The legislature applied its mind to a situation and created a SAAR which was much less onerous than what the tax officer sought to do.

This shows that a SAAR based on defined outcomes is generally fairer than a GAAR solution based on discretion.

Proportionate response

SAARs normally provide only for the nullification of the benefit derived from tax avoidance.

For instance, where an international transaction is entered into at a price other than an arm's length price, only the difference between the two prices is sought to be taxed. The transfer pricing provisions do not seek to declare the transaction to be a sham or to place a greater burden upon the taxpayer than the benefit derived by him from the non-arm's length transaction.

Similarly, the provisions of sections 40 and 40A are tailored to the 'mischief' sought to be attacked.

If the GAAR were to apply over and above the SAAR in such cases, the burden on the taxpayer would go beyond the benefit derived from the 'mischief'.

This is why the Shome Committee observed:

"For instance, transfer pricing regulation in respect of transactions between associated enterprises ensures determination of taxable income based on arm's length price of such transactions. Here, GAAR cannot be applied if such transactions between associated enterprises are not at arm's length even though one of the tainted elements of GAAR refers to dealings not at arm's length."

What is 'impermissible'?

Even where tax avoidance is found to exist, the question of what constitutes 'impermissible' remains.

In the Walfort case, the revenue found the sequence of events to give rise to a colourable device. It was not in dispute[12] that had the transaction of redemption happened at a later date instead of happening immediately after the distribution of the dividend, the transaction would not have been a colourable device. In other words, a subjective, and possibly arbitrary, dividing line was drawn between what constituted a colourable device and what did not.

On the other hand, section 94(7) lays down a clear dividing line as to the number of days for which securities must be held to avoid the application of the SAAR.

This shows that in the case of a SAAR, generally, there are objective tests to determine what is 'impermissible'.

Assuming that the GAAR can override a SAAR, it might be open to a tax officer to accuse a taxpayer of impermissible tax avoidance even in a case which complies with the mandatory holding period under section 94(7) and squarely falls outside that provision. This would be contrary to the express legislative intent that once an asset has been held for a defined period of time, the dividend-stripping provision should not apply.

Two edges of the sword

As discussed above, a fundamental flaw of the GAAR is that it has sought to focus on only one edge of a double-edged sword. That makes the GAAR inherently unfair.

If a taxpayer has the law against him, but tax morality in his favour, there is no redress available. The Courts will tell him:

"It may be that the construction we are adopting … may operate harshly against [the taxpayer] … . These indeed are serious considerations but the Courts have to construe the statute according to the plain language and tenor thereof and ***if any untoward consequences result therefrom it is for authority other than this Court to rectify or prevent the same.***" (emphasis supplied)

per *Das J., in Turner Morrison & Co. Ltd. vs. CIT [1953] 23 ITR 152 (SC)*

Under section 94(7), a buyer who buys securities cum-dividend can lose the benefit of the tax exemption available for dividends, but the seller who effectively earns the dividend through a higher selling price ends up paying tax on his entire income without any exemption. In effect, neither the buyer nor the seller gets the benefit of the dividend exemption. A balanced SAAR provision could have transferred the dividend exemption to the seller of cum-dividend securities and denied it to the buyer.

This aspect of anti-avoidance policy is an important reason to limit the scope of GAAR to cases where it is really needed. Where a SAAR is available, invoking the GAAR can make the entire tax system look unreasonable, with the dice loaded against the taxpayer.

Summary

To conclude,

1. The GAAR overrides other provisions which are in conflict with the GAAR provisions;
2. It is open to question whether section 100 overrides the SAARs in the Act;
3. The rule of interpretation that special provisions override general provisions supports the view that the GAAR should not apply where a SAAR applies; and
4. There are good policy reasons for holding that general discretion granted under a non-specific provision should not override or add to a specific solution to a specific problem enacted as a binding statutory rule.

12 See CIT vs. Walfort Share and Stock Brokers P. Ltd. [2009] 310 ITR 421 (Bom.), at p. 437, para 40

CA Bhaumik Goda

GAAR and DTA

Background

It is commonly understood that taxpayer can arrange their affairs in a way that will give him tax benefits, which are through genuine and legitimate actions. However, with passing time, changing outlook of Government and people – line of distinction between legitimate and illegitimate tax planning is getting blur. When it comes to non-residents, provisions of Income-tax Act, 1961 (Act) provides option to the Taxpayer to opt for provisions of domestic law or tax treaty whichever is beneficial. Supremacy of tax treaty has time and again upheld by Courts on various occasions be it - capital gains under India-Mauritius treaty, exclusion of aircraft rent under India-Ireland treaty, treaty rate *vis-à-vis* section 206AA rate in absence of PAN, narrowed definition of make available under various treaties etc etc. Interplay between General Anti Avoidance Rule (GAAR) and tax treaty is relevant to determine whether aforesaid positions holds good in GAAR era.

This article examines inter-play of tax treaties with GAAR rules which are effective from 1 April, 2017. Inter-play becomes more dynamic as one evaluates interaction of GAAR with proposed Base Erosion and Profit Shifting (BEPS) action plans. Issue of treaty override – i.e. GAAR overriding provisions of tax treaty is relevant as grandfathering provisions under the Act are restrictive and provisions doesn't grandfather all types of income earned by Taxpayer even though contract/structure is established prior to 1st April 2017. This makes it imperative for Taxpayers to examine their existing arrangements to evaluate if they may fall within the boundary of being considered as impermissible avoidance arrangements and thereby hit by the consequences provided in the GAAR provisions which can be quite onerous. This exercise may also help them take corrective actions to mitigate the said exposure.

International experience

OECD Commentary on Article 1 of the Model Tax Convention clarifies that GAAR provisions in domestic law in the nature of 'substance over form rule' or 'economic substance rule' is not in conflict with treaty. As a guiding principle OECD Commentary states that that the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions.

Internationally, GAAR provisions finds place in tax legislature of multiple countries like Australia, South Africa, China, Brazil, Norway, Canada etc. In most countries, domestic law specifically provides that provisions of GAAR shall override tax treaty.

Treaty override under Act

India's position on application of GAAR *vis-à-vis* tax treaty is clear. Section 90(2) provides option to the taxpayer to apply provisions of Act or treaty whichever is beneficial by stating that provisions of Act shall apply to the extent it is beneficial to taxpayer. However, as regards GAAR, section 90(2A) states that provisions of Act shall apply even if such provisions are not beneficial to taxpayer. Relevant provisions are extracted hereunder:

"(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee even if such provisions are not beneficial to him."

Thus, it may not be open for taxpayer to rely on beneficial treaty provisions if GAAR is invoked by tax authorities. Accordingly, once transaction is held to be impermissible avoidance agreement (IAA), consequences in relation to tax arising therefrom shall be determined in accordance with provisions of Chapter X-A. It may be noted that section 90(2A) merely provides that provisions of Chapter X-A shall apply even if it is not beneficial to taxpayer. It does not disentitle Taxpayer to tax treaty once provisions of Chapter X-A are invoked. Contrast this language of section 90(2A) with section 90(4) which reads as under:

"An assessee, not being a resident, to whom an agreement referred to in sub-section (1) applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory."

Aforesaid proposition is further supported by section 98 which provides for consequences of IAA. Section 98(1) reads:

"If an arrangement is declared to be an impermissible avoidance arrangement, then, the consequences, in relation to tax, of the arrangement, including denial of tax benefit or a <u>benefit under a tax treaty</u>, shall be determined, in such manner as is deemed appropriate, in the circumstances of the case, including by way of but not limited to the following, namely…."

Amongst other consequences, section 98(1) empowers tax authorities to deny benefit under tax treaty – it does not provide for denial of tax treaty itself. This usage of language is significant as GAAR not only applies to arrangement but also applies to step in, or part of arrangement [proviso to section 95]. Thus, taxpayer may avail treaty benefit for other steps or part of arrangement which is not tainted by GAAR. Illustratively, a NCD infused by Mauritius company may be treated as IAA to avail benefit of lower tax rate of 7.5% under amended India-Mauritius tax treaty and benefit of lower tax rate may be denied. However, benefit of capital gains exemption under tax treaty (assuming NCD is sold in same year in which GAAR is invoked) *ipso facto* cannot be denied (unless GAAR is invoked to this specific limb separately) as amended India-Mauritius treaty grants taxing right to India in respect of 'shares' of company and not in respect of any other instrument.

On parity of reasoning it can be contended that an IAA post application of consequences of section 98 should still be subject to tax treaty. Illustratively, say an German Company enters a transaction of transfer of IRP. Tax authorities invokes GAAR and recharacterizes the transaction as use of IPR. In such a case, it may be contended that arrangement post recharacterisation still continues to be that of royalty and benefit of lower treaty rate of 10% should be granted to taxpayer on recharacterised transaction.

Continuity of treaty benefit is significant. It may be explored if taxpayer against whom GAAR is invoked can apply to its competent authority to invoke Mutual Agreement Procedure (MAP) if taxpayer considers that GAAR will give rise to taxation which is not in accordance with tax treaty. This may be relevant as it may provide additional safeguard other than provided under domestic law as also potentially address the issue of availment of tax credit in resident state if GAAR is invoked.

Further, provisions are restrictive to deny benefit available under tax treaty. GAAR cannot be invoked to enlarge scope of tax treaty. Illustratively, location of Singapore Company engaged in business of distribution of shrink wrapped software is challenged under GAAR. Singapore Company does not have PE in India. Singapore Company is in turn owned by US Company. In this case, even though residence of Singapore Company is challenged, GAAR provisions still cannot work prejudicial to taxpayer by expanding the scope of tax treaty and considering shrink wrapped software to be royalty which is not unless tax treaties specifically provide. In this context, Courts has unanimously held that Explanation 3 to section 9(1)(vi) cannot be imported into tax treaty.

Interesting situation arises in recent bilateral tax treaties that India has entered into (e.g. India's tax treaties with Luxembourg and Malaysia) as well as in recent amendments to treaties such as with Singapore where treaty override provision has been specifically included. Illustratively, refer Article 28 – Limitation of Benefits Clause in India-Malaysia tax treaty which reads as under:

"1. *The provisions of this Agreement shall in no case prevent a Contracting State from the application of the provisions of its domestic law and measures concerning tax avoidance or evasion, whether or not described as such.*

2. *A resident of a Contracting State shall not be entitled to the benefits of this Agreement if its affairs were arranged in such a manner as if it was the main purpose or one of the main purposes to take the benefits of this Agreement."*

As can be seen, Article 28(2) disentitles taxpayer to treaty benefit if affairs were arranged to take benefits of tax treaty. It needs to be explored whether taxpayer can take fall back on section 90(2A) and opt to be governed by GAAR by relying on section 90(2) as treaty benefit is not denied in totality under GAAR.

Specific Anti-abuse provisions under Treaty

India's tax treaties contain specific anti-avoidance rules (SAARs), such as restricted force of attraction rule under Article 7(1), article 9 dealing with associated enterprises, beneficial ownership requirement under Article 10,11 and 12 dealing with dividends, interest and royalties, special relationship rule with respect to interest and royalties in articles 11 and 12, alienation of shares of real estate entities in article 13 (4), Limitation of Benefit (LOB), Limitation of Relief in India-Singapore tax treaty.

As can be seen from above, there are numerous anti-abuse provisions already forming part of tax treaty to check particular tax avoidance mechanism. Thus, issue arises on interplay of GAAR and SAAR which are already forming part of tax treaty. Question arises whether GAAR will have an overriding impact negating the existence of SAAR or GAAR cannot be invoked if particular abusive mechanism is checked by SAAR. At fundamental level, it needs to be recognised that SAAR forming part of tax treaty represents acceptance of two contracting states and common ground to tackle abusive practice whereas GAAR represents unilateral law formed by a Contracting State. On this issue CBDT via Circular No 7/2017 opined that GAAR and SAAR may co-exist and are applicable, as may be necessary in facts and circumstances of the case. On the issue of application of GAAR in context of tax treaties which contain LOB provisions, CBDT opined that anti-abuse rules in tax treaties may not be sufficient to address all tax avoidance strategies, and the same are required to be tackled through GAAR. If a case of avoidance is sufficiently addressed by the LOB, GAAR shall not be invoked. Issue of interplay between GAAR and SAAR is dealt with in details in other chapters of this Journal.

Interplay between GAAR and BEPS

Concerns regarding base erosion and profit shifting is a global phenomenon. Members of OECD and G20 nations adopted a 15-point action plan to address problem of BEPS (BEPS Action Plan). The BEPS Action Plan seek to eradicate double non-taxation, end treaty abuse and ensure that profits are taxed at the place of value creation. To this end, the BEPS Action Plan contain a number of tax treaty related measures, requiring the implementation of wholesale changes to the existing international tax treaty network. Carrying out such large-scale changes on a treaty-by-treaty basis would have been time consuming and may have led to inconsistencies across treaties due to the politics and vagaries of bilateral negotiations. Therefore, Action 15 of the BEPS Action Plan recognized the MLI, a multilateral treaty, as an innovative mechanism that would allow a more coordinated approach with immediate effect, while retaining the flexibility required to implement these changes in a broadly consensual framework to tackle base erosion. While the MLI attempts to retain flexibility by providing the countries a template of limited choices to choose from, it also mandates compliance with certain 'minimum standards'. MLI applies to tax treaties where both Parties to such tax treaty have conveyed their intention (by way of a notification) for such treaty to be covered by the MLI - such treaties being referred to in the MLI as "Covered Tax Agreements" ("CTA"). Once notified, tax treaties will be required to meet certain prescribed minimum standards which amongst other includes prevention of treaty abuse under BEPS Action 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances). Signatories to MLI have limited flexibility to opt out of adherence to minimum standards.

As a minimum standard, the Action 6 Report requires countries to implement at least one of the following anti-abuse measures in their treaties –

(i) a principal purpose test ("PPT") only, which is a general anti-abuse rule based on the principal purpose of transactions or arrangements

(ii) a PPT supplemented with either a simplified or a detailed limitation on benefits ("LOB") provision, or

(iii) a detailed LOB provision, supplemented by a mutually negotiated mechanism to deal with conduit arrangements not already dealt with in tax treaties.

In its provisional notification, India has chosen to apply the PPT with the SLOB across all its Notified Treaties. So far as the PPT is concerned, being a default test, it should apply across the board in all of India's treaties irrespective of the other position adopted by the other countries. Since India is only one among 12[1] countries to have chosen to apply the SLOB, only a PPT is likely to apply to India's CTAs.

PPT has been introduced as a default test which provides that no benefit under the CTA shall be granted if it is reasonable to conclude that obtaining that benefit was <u>one of the principal purposes</u> of any arrangement or transaction that resulted <u>directly or indirectly in that benefit</u>. However, most importantly, there is a carve out for granting such treaty benefits if availing such benefits was is in accordance with the object and purpose of the relevant provisions of the CTA. The PPT supersedes existing general anti-abuse provisions of the CTA, or is added to the CTA in the absence of such provisions.

Once PPT comes into force in tax treaties, interplay between PPT and GAAR will be interesting. Intention of both provisions is to tackle tax avoidance. However, PPT forms part of tax treaty which represents consensus of two

1. *Other countries being Argentina, Armenia, Bulgaria, Chile, Colombia, Indonesia, Mexico, Russia, Senegal, the Slovak Republic and Uruguay*

contracting states and GAAR is a unilateral legislature. Further, there are differences between GAAR and PPT which requires consideration:

Particular	PPT	GAAR
Scope	• Possible to invoke even if 'one of the principle purpose' is to avail tax benefit • Can be invoked even if tax benefit is directly or indirectly	• Can be invoked only if 'main purpose' is to obtain tax benefit • Arguably tax benefit should be direct in absence of qualification
Additional test	• No additional conditions to be satisfied apart from purpose test	• One of the other tainted elements also needs to be satisfied, i.e., creation of rights or obligations that are not at arm's length, abuse of ITA, lack of commercial substance, or lack of bona fides.
Safeguards	• No safeguards are in place and hence Assessing Office can deny treaty benefit on the ground that PPT test is not met	• Procedural safeguard in the form of approval panel which is chaired by High Court Judge, revenue member and research scholar
Exclusions	• No exclusions	• Monetary limit of INR 3 crs each financial year • Foreign Institutional Investor (FII) if prescribed conditions are satisfied • Investment by NRI in financial derivatives issued by FII
Grandfathering provisions	• No grandfather. Hence structures already in existence are also impacted	• Income arising from transfer of investment made prior to 1 April 2017 grandfathered

As can be seen from above, scope of domestic GAAR is more restrictive vis-à-vis PPT. Thus, issue arises whether principle of choice is available for Taxpayer to opt to be governed by GAAR visa-a-vis PPT to determine tax avoidance motive under section 90(2). In other words, if Taxpayer is able to establish that GAAR provisions are not satisfied or it is covered by exclusions even though PPT test under treaty is not satisfied, can Taxpayer avail treaty benefit. Prima facie, such argument appears attractive, issue requires detailed research and deliberation.

Carve out of PPT test allows treaty benefit to a transaction if granting the benefit is in accordance with the object and purpose of the relevant provisions of the tax treaty. Relying on carve out it can be argued that PPT test should not be involved in case of lower withholding tax rate in case of royalty, fees for technical service (FTS), interest or narrowed scope of royalty definition say – India-Netherland treaty which excludes equipment royalty, India-Ireland treaty which excludes aircraft royalty, make available requirement in FTS article, capital gain exemption under India-Netherland etc.

Rule 10U(d) specifically grandfathers any income accruing or arising to, or deemed to accrue or arise to, or received or deemed to be received by, any person from transfer of investments made before the 1 April 2017 from applicability of GAAR. Amended India-Singapore treaty provides for taxation of capital gains only in the residence state if the shares were acquired before April 1, 2017 subject to satisfaction of LOB test under treaty. On co-joint reading provisions, it can be concluded that GAAR should not be applicable and gains derived on transfer of shares by Singaporean Company acquired prior to 1 April 2017 would be taxable in Singapore. However, under MLI, India and Singapore has provisionally notified its respective treaty to be covered by MLI and consequently PPT test. Thus, whilst GAAR should not be applicable, PPT test will still be applicable to Singaporean entity. In other words, Singapore Company will have to establish that one of the primary purpose of establishing company in Singapore is not to avail treaty benefit. This is likely to have severe implications on investors who have invested from Singapore in past.

All in all, there is a need for further clarity on aforesaid issue otherwise it will give rise to uncertainty and protracted litigation.

Impact on payer

Under the provisions of Act, payer is required to withhold tax if income of NR is chargeable to tax. Onerous consequences follow in terms of interest and penalty if tax is not withheld appropriately. It may be difficult for payer to determine whether a transaction is impacted by GAAR. Law does not provide any explicit exemption from application of onerous provisions to payer if GAAR is invoked in hands of recipient. Payer will have to establish its bonafide to defend levy of penalty. However, levy of interest is automatic. Illustratively, Taxpayer does not withheld tax on being satisfied that recipient is entitled to treaty benefit. Subsequently, if tax authorities invoke GAAR in hands of recipient and considers transaction as chargeable, payer will be liable to pay interest under section 201(1A). In case the contract is 'net of tax' contract, payer needs to undertake sufficient due diligence to safeguard against applicability of GAAR in hands of recipient.

Law also empowers tax authorities to treat payer of income as representative assesse of NR under section 163. In such a case, if tax authorities invoke GAAR in hands of payer, it will give rise to substantial difficulty as GAAR is intent based provisions which needs to be supported by facts to prove that main purpose of transaction is not to avail tax benefit or that Taxpayer does not satisfy tainted element test. Payer may not be in possession to provide counter factual or requisite information as generally intent is best known to recipient of income. In such situation payer may be subject to severe tax consequences which may not have been envisaged at the time of entering into contract. Further, in case of continuing contract post 1 April 2017 grandfathering provisions may not be applicable (as provisions merely grandfather income arising from transfer of investment) and transaction may be subject to GAAR. In case of net of tax contract, commercial disputes are likely to arise. Typically, in case of net of tax contract, liability shift on payee if it is in consequence to 'change of law'. It will be a matter of debate whether GAAR or PPT pursuant to BEPS Actions Plans can be construed as 'change of law'.

Concluding Remarks

GAAR by its nature should be lender of last resorts. From tax treaty perspective, GAAR provisions will pave way to a new chapter of tax litigation. Government has time and again assured that procedural safeguards will address investors' concerns - one hopes that such assurance are followed in spirit. Coupled with GAAR, concerns continue to hover around PPT test which will form part of most treaties. Both provisions though similar in purpose but different in language are likely to create uncertainty for investors, taxpayers and consultants alike.

 

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Corporate Restructuring – Mergers, Demergers, etc. – GAAR implications

Corporate restructuring – Perspective and tax scenario in India

Corporate restructuring signifies reorganisation or rearrangement transactions undertaken by business entities to achieve various objectives. Typically, there is at least one dominant objective which drives the restructuring exercise towards enhancement of value to stakeholders, viz., achievement of inorganic growth, business diversification and synergies, coping with regulatory and culture aspects, wading through domestic and global competitive forces, reduction of operating costs, etc. With globalisation, the opportunities and challenges to businesses are enormous and continuously evolving. This is likely to increase further as disruptive technologies will drastically alter the life cycle of businesses and companies. As businesses are forced to become nimble, the spurt of corporate restructurings will only increase and can never lose relevance in this dynamic business world.

Corporate restructuring or reorganisations may represent various strategies or forms viz. mergers, acquisitions, demergers, joint ventures, alliances etc., and depending on the objectives in some cases reflect combination of these forms.

The importance of tax in corporate reorganisations cannot be undermined since tax is one of the major transaction costs. Identification of and addressing key issues during the early stages of these transactions are crucial to the success of these transactions in the long run. Careful deliberation of possible tax issues and extant Government policies impacting transactions at conceptualisation stage itself, is pertinent for minimising future tax uncertainty and litigation and associated costs.

The Indian Income-tax Act 1961 (the Act) has provided for various tax concessions / exemptions in relation to taxability of capital gains, carry forward of losses, claim of exemptions or deductions etc., subject to conditions. Certain tax treaties with India may also provide for tax neutrality in the context of capital gains on sale of shares of companies. The focus of this article is not to evaluate the tax neutrality norms or forms of tax neutral reorganisations from the perspectives of tax planning or tax avoidance, but to present a perspective about the implications of anti-tax avoidance safeguards through the General Anti Avoidance Rules (GAAR) under the Indian income tax law on corporate restructuring arrangements.

GAAR in India – Interplay with other provisions of Indian Income-tax law

In India GAAR fundamentally stems from judge made law which had sought to prevent tax avoidance through colourable devices. However there was no general provision in the law which sought to strike down tax avoidance. The principles of GAAR were first proposed as part of Direct Tax Code Bill which was tabled before the Parliament on 30th August 2010. Though the DTC never saw light of the day, the provisions of GAAR were introduced by the Finance Act 2012 under Chapter X-A to be effective from 1st April 2012 onwards. GAAR has become finally effective from financial year 1st April 2017 through provisions contained under sections 95 to 102 of the Act.

Fundamentally the Act provides that if any step in or part of an arrangement is designed or deemed to create non arm's-length rights or obligations between transacting parties or which lacks commercial substance or carried on in a manner not ordinarily employed for *bona fide* purposes, leading to the main purpose of obtaining tax benefit, then such arrangement may be regarded as an impermissible avoidance arrangement liable to tax consequences in India. The far reaching tax consequences of declaration of impermissible avoidance arrangement which is inclusively provided for under the Act, *inter alia* includes denial of tax treaty benefits, disregarding or recharacterisation or ignoring of any step or part of or whole of such arrangement, reallocation of expenses and income and even disregarding any corporate structure. The onus is on the taxpayer to prove that GAAR is not applicable in its case.

The phrase tax benefit has been inclusively defined to include various scenarios of lowering tax effects. It encompasses scenarios of reduction or deferral of income, enhancement of tax refunds, tax losses, use of tax treaties toward off tax incidence.

In summary, General Anti-Avoidance Rules (GAAR) are aimed at empowering revenue authorities with the right to scrutinise tax transactions which are structured solely to avoid taxes. The main objective of introduction of GAAR was to deal with the aggressive tax planning leading to loss of tax revenue, which in turn resulted in a need to view such transactions from a perspective of substance over form. The procedures for application of GAAR provisions and the conditions under which such provisions will not apply are prescribed under Rules 10U to 10UC of the Income Tax Rules 1962 (the Rules).

GAAR applies through non-obstante provisions, which indicate that notwithstanding the application of other provisions of the Act, the GAAR provisions would have effect. Hence, it may be imperative to test whether use of beneficial provisions under the Act, viz., exemption provisions, deduction provisions, treaty relief entitlement provisions, certain withholding tax provisions, could attract attention of tax authorities for invoking GAAR. When there is a conflict between two or more statutes or two or more parts of a statute, then the rule of harmonious interpretation needs to be adopted. The doctrine of harmonious interpretation is the thumb rule to interpretation of any statute. An interpretation which makes the enactment a consistent whole, should be the aim of the Courts and a construction which avoids inconsistency or repugnancy between the various sections or parts of the statute should be adopted. The Supreme Court in case of *CIT vs. Hindustan Bulk Carriers*[1], very aptly laid down that the Courts must avoid a "head on clash" of seemingly contradicting provisions and they must construe the contradictory provisions so as to harmonise them. Further, it held that the provision of one section cannot be used to defeat the provision contained in another unless the Court, despite all its effort, is unable to find a way to reconcile their differences. When it is impossible to completely reconcile the differences in contradictory provisions, the Courts must interpret them in such as way so that effect is given to both the provisions as much as possible. The Supreme Court in this

1 259ITR449 (SC)(2003)

case also laid down that Courts must keep in mind that interpretation that reduces one provision to a useless number or dead is not harmonious construction.

From the above, it may be inferred that the tax neutrality or tax relief provisions in relation to corporate reorganisations are aimed at the legislature's intent to facilitate such transactions. In comparison, the GAAR provisions essentially seek to curb any attempts to solitarily avoid or dodge tax by engaging into transactions without commercial basis. Therefore, apparently provisions under the Act governing the scheme of tax neutrality in case of transactions like amalgamation, demerger etc., ought not be impacted by the GAAR provisions if it can be demonstrated through conduct, associated documents and interactions with authorities that the principal purpose of such transactions is not to obtain tax benefit. Typically Court approved schemes of arrangements or intra group arrangements resulting into a tax benefit to one entity without altering the overall revenue of the group ought not be impacted by GAAR. Even usage of tax treaty provisions to claim reliefs or credits in relation to cross-border transactions need to be fundamentally backed through *bona fide* commercial rationale, to avoid GAAR implications.

Moreover, alongside GAAR, the repercussion of implications under Specific Anti-avoidance Rules (SAAR) viz., Transfer Pricing regulations, specific disallowance provisions etc. had been a specific point for consideration among taxpayers and have been clarified by the CBDT through Circular 7 of 2017. **It sums up that both SAAR and GAAR constitute separate provisions under the Act and hence can separately co-exist. GAAR shall apply only to such situations which are not addressed by SAAR.** The said CBDT Circular also clarifies that likewise, if the Limitation of Benefit clause in a tax treaty does not entirely address all tax avoidance strategies, GAAR can be invoked in such situations as well.

Shome Committee Report on GAAR – Impact on corporate restructuring outcomes in India

When GAAR provisions were first introduced in the Act by the Finance Act 2012, through Chapter XA of the Act, it was provided in the Act that GAAR provisions would be applied in accordance with certain guidelines and subject to such conditions and the manner as may be prescribed. A number of representations were received against the provisions contained in Chapter XA and the draft guidelines issued by the CBDT during June 2012. Hence, on July 13, 2012, the then Prime Minister approved the constitution of an Expert Committee on GAAR chaired by Dr. Parthasarathi Shome to examine the concerns expressed by the stakeholders, finalise the guidelines for GAAR and suggest the roadmap for implementation of GAAR. The Shome Committee submitted its final report on September 30, 2012, recommending amendments in the Act, Income Tax Rules and issuance of clarifications and guidance by the CBDT.

It is important to note that the Shome Committee endorsed the viewpoint of the Committee, that GAAR provisions should not be invoked in case of tax mitigation but should be applied in case of legal structures or transactions designed solely to avoid tax.

Some of the noteworthy recommendations in the Shome Committee report as accepted by the Governments since then are

a) deferral of GAAR,

b) prescription of a minimum threshold for invoking GAAR at INR 3 crores,

c) obtaining tax benefit be the main purpose instead of one of the main purposes of any step or part of any arrangement,

d) grandfathering of investments (though not arrangements) from application of GAAR as reflecting on the date when GAAR provisions become effective,

e) limiting application of GAAR provisions only to the part of the arrangement which is treated to be for impermissible avoidance

f) framework of the Approving Panel and allied procedures for invoking GAAR provisions, etc.

Amongst many other recommendations, certain illustrations on business reorganisations transactions captured in the Shome Committee report explain the applicability of GAAR provisions on certain corporate restructuring arrangements. For instance, round tripping cases, cases of interposition of entities in low tax jurisdictions for obtaining tax treaty benefits, selective buybacks in low tax jurisdictions, booking of capital losses on sale of shares acquired at artificially inflated costs, disguised financing arrangements whereby a company purchases unlisted securities with a condition to sell back at a future date factoring a specific rate of return and records long term capital gains instead of interest income, etc., are cited as cases of tax avoidance, subject to application of GAAR. On the other hand, the merger of a profit making company into a loss making company or *vice versa* may result in offsetting losses against the profits thereby reducing the tax liability. If this scheme of merger has been sanctioned by a High Court after due consideration of all aspects including taxes, such arrangement ought not attract GAAR as per the Shome Committee.

It is important to note that while the Governments thus far have amended the Indian tax law as per most of the recommendations of the Shome Committee report on GAAR provisions, some of the recommendations in the report are yet to be considered. Due to the subjectivity associated with the extant draft of the GAAR provisions, some of these unaddressed recommendations assume importance. The Act lays down conditions to deem an arrangement to lack commercial substance but stops short of defining the term "commercial substance" as was recommended by Dr. Shome. As mentioned earlier the Shome Committee endorsed the view that tax mitigation strategies should not fall within the ambit of GAAR applicability, by distinguishing them from tax avoidance strategies.

The Committee also recommended that unless a tax avoidance arrangement is abusive or artificial or contrived, GAAR provisions should not apply. Thus the Committee recommended that an illustrative negative list of transactions viz., setting up of units in SEZs, amalgamations and demergers through court approved scheme, purchase or lease of capital assets, intra group transactions not resulting in altering consolidated group revenue, etc. may facilitate greater understanding and certainty about the applicability of GAAR provisions. Such a negative list is yet to feature in the extant Indian income tax law.. Non-adoption of the above recommendations on GAAR provisions leaves enough scope for debate or litigations about the applicability of GAAR in these arrangements. Hence, till the Government clarifies its stand in this regard, it may be incumbent upon Courts to decide on principles about the applicability of GAAR provisions in these cases. However the views of the Shome Committee on the various situations of corporate restructuring should certainly have a persuasive value as it represents views of an empowered committee comprising of different stakeholders. Some of the situations of corporate restructuring as covered by some of the illustrations in the Shome Committee report, highlighted below may be worthy of recall as they may provide the thinking on application of GAAR provisions. The logic may hold good even in similar other situations which are not expressly frowned on.

In case of an outbound investment scenario with an intermediate holding company outside India, if foreign step down subsidiaries distribute dividends to such intermediate holding company, GAAR provisions should not be invoked on the premise that no dividends were onward distributed in India. This is so because the declaration of dividend is a business choice of a company and India does not have an anti-deferral provision in the law yet. On an extended illustration of a merger of such intermediate holding company with its Indian parent company thereby saving on tax on distribution of dividend, the Shome Committee opined such restructuring and non-declaration of dividend prior to such transaction is a business choice left to the company and such merger of intermediate foreign holding company with its Indian parent company is exempt for the purpose of capital gains taxation under section 47 of the Act, hence GAAR cannot apply in such case, as well.

As far as amalgamation of companies is concerned, there are specific provisions of the Act covering such situations subject to the various conditions under the Act and hence ought not be subject to GAAR provisions.

In an organisation structure, where the shares of an asset owning Indian company (say ICO1) is held by another Indian company (say ICO2) the shares of which are in turn held by foreign companies in a tax favourable jurisdiction. If ICO2 is voluntarily liquidated and subsequently the shares of ICO1 (vesting with the foreign company) are transferred for consideration without any capital gains impact in India, such a transaction ought not be subject to GAAR provisions since the taxpayer selects a tax efficient manner of disposal of shares.

It is this context that CBDT circular of January 2017 clarifying implementation of GAAR provisions assumes significant importance.

Key takeaways from the CBDT Circular 7 of January 2017 with respect to restructuring transactions.

The CBDT *vide* its aforesaid Circular sought to provide answers to certain specific questions concerning the implementation GAAR provisions. The following points may be pertinent in this regard.

1. GAAR provisions will not interfere with the right of the taxpayer to choose a particular method of transaction.

2. SAAR and GAAR can co-exist and apply to a transaction – To the extent SAAR does not address an issue in a transaction, GAAR can apply.

3. The above interplay also holds good *vis-à-vis* Limitation of Benefits (LOB) clause in tax treaties – To the extent the LOB clause does not address a tax avoidance scheme, GAAR provisions shall apply.

4. Denial of tax treaty benefits to a Special Purpose Vehicle (SPV) in a tax friendly jurisdiction on the grounds of no employees of business premises may happen pursuant to GAAR provisions if the main purpose of such entity set up is tax avoidance.

5. Grandfathering benefit under Rule 10U (1)(d) shall be available to investments made before 1 April, 2017. If bonus shares are issued with respect to original investments made up to 31st March 2017 or any consolidation or split up happens with respect to grandfathered shareholding, Rule 10U(1)(d) benefit shall be applicable to such bonus shares / split up / consolidated shares. If shares are issued upon conversion of convertible instruments like CCDs CCPS, issued up to 31st March 2017, the benefit of grandfathering shall apply if the terms of issuance and conversions were finalized at the time of issuance of such convertible instruments on or before 31st March 2017.

6. GAAR will not apply in cases where the SAAR has held a transaction to be a

permissible arrangement or which has been sanctioned by the Courts or National Company Law Tribunals

7. Lease contracts or loan arrangements not being investments *per se*, will not be entitled to grandfathering relief under GAAR provisons.

GAAR & BEPS

Base Erosion and Profit Shifting (BEPS) is a project embarked upon by the OECD under the mandate of the G20 nations to counter tax evasion or tax arbitrage between sovereign nations by multinational enterprises based on the tax policies of these nations. Essentially, as per Action Plan 15 of the BEPS measures, nations through a multilateral instrument seek to amend their various tax treaties swiftly, the fundamental objective being protection of the tax revenue base. GAAR provisions are also enacted with this objective. While GAAR may be invoked if the main purpose of an arrangement is to obtain tax benefit through avoidance, as per the principle purpose test enshrined in the multilateral instrument, treaty benefits may be denied if one of the main purposes of an arrangement or transaction is to obtain tax benefits directly or indirectly. From the above, it is apparent that even if the GAAR provisions fail on application in some cases, as far as cross-border transactions are concerned, the MLI principle purpose test may apply to deny treaty benefits in such cases.. It would be interesting to observe how the interplay between the provisions of GAAR and those prompted by the BEPS agenda will play out. The Revenue is unlikely to treat the changes mandated by BEPS at the same pedestal as provisions of SAAR thereby retaining the right to invoke GAAR at their discretion in cross-border situations. These may be pertinent considerations for cross-border deals in the years to come.

Conclusion

The prolonged debate around the subjectivity of the GAAR provisions and application thereof by tax authorities has led to amendments of certain provisions under the Act and Rules including issuance of guidance by the CBDT, in order to allay certain concerns of taxpayers, before these provisions finally become effective. Some of the most significant clarifications and amendments with respect to the GAAR provisions were essentially based on the recommendations of the Shome Committee. These include provisions such as tax avoidance being the dominant purpose of an arrangement and grandfathering of transactions till 31st March 2017 from application of GAAR provisions, stringent procedure for invoking GAAR. However, the wide ambit of certain definitions under GAAR viz. fund, step, tax benefit, connected person are still prone to multiple arrays of interpretation and lack clarity on courts. It will therefore be interesting to see how best the litigations around the subject is controlled.by taxpayers and tax authorities. Moreover, it would certainly help if the Government accepts the recommendations of the Shome Committee entirely so as to provide complete clarity in advance to proposed transactions.

To conclude, in order to fulfil the intent of the Government to continue to attract foreign investment and ease of doing business in India, it would be essential for the Government to take a more careful approach on the application of GAAR to ensure that it is limited only to contrived transactions and colourable devices This is all the more necessary as the wheel has turned a complete circle for the Revenue from having little or no ammunition against tax avoidance to having a complete arsenal comprising of GAAR, BEPS and associated power of the MLI. They would be well advised to heed to the preaching of Lord Buddha and follow the middle path.

CA Siddharth Parekh

LOB clauses under Indian DTAAs

1. Introduction

Limitation on Benefits Provision[1] (hereinafter referred to as "LOB Clause" or "LOB Provision") has been explained in the Organisation for Economic Co-operation and Development's[2] (the "OECD") glossary on tax terms as *"Tax treaty provisions designed to restrict treaty-shopping opportunities by limiting treaty benefits to persons who meet one of several enumerated tests, which may require minimum level qualifications, e.g., local ownership."*.

The above definition raises some fundamental questions as to what is the meaning and context in which the term "treaty-shopping" has been used here and more fundamentally what indeed is the role of a tax treaty and its interaction with the domestic tax laws of a country. This article analyses these question before proceeding to analyse some of the common examples of LOB Clauses found in Indian Double Taxation Avoidance Agreements ("DTAAs") and concludes with some thoughts on recent developments.

1.1. Meaning and role of tax treaties

Tax treaties are (usually)[3] bilateral agreements between two sovereign countries for the avoidance of double taxation. Historically, the main purpose of tax treaties happened to be the avoidance of (juridical) international double taxation. This was with the objective of promoting the cross-border exchange of goods and services and the movement of capital and persons. However increasingly it has been a stated objective of tax treaties to prevent tax avoidance and evasion of taxes.

The provisions of a DTAA normally apply to persons who are "residents"[4] of either one

1 Also referred to as Limitation of Benefits Provision in tax literature and some tax treaties

2 The OECD is an inter governmental economic organisation with 35 member countries, founded in 1960 to stimulate economic progress and world trade. While India is not a member of the OECD, India is one of the many non-member economies with which the OECD has working relationships in addition to its member countries. India has been co-operating with OECD since 1995 and also participating in various OECD led projects, notably the 2013 Base Erosion and Profit Shifting Project ("BEPS") and also providing its observations and reservations on the OECD Income and Capital Model Convention and Commentary

3 There have been instances of multilateral treaties in force for e.g., the Nordic Convention (1996) is a multilateral tax convention for the avoidance of double taxation between Denmark, Faroe Islands, Finland, Iceland, Norway and Sweden

4 This term is defined in Article 4 of the OECD Model Tax Convention on Income and Capital, 2014 (hereinafter, "OECD Model, 2014")

or both of the countries who are party to the DTAA. The way tax treaties operate is by defining which of the two countries constitutes as "residence state" of the taxpayer and the other country being referred to as the "source state". The DTAA then proceeds to distribute the taxing rights between the residence state and the source state by limiting the application of domestic tax law and/ or imposing an obligation on each of the two countries.

A common example of such limitations could be where the distributive provisions envisage tax sharing for a class of income e.g. interest income[5] where there is a cap (usually set at 10% of the gross amount of interest earned) beyond which the source state cannot exercise the taxing right under its domestic tax law. Such a tax sharing provision is coupled with the obligation on the residence state to provide double tax relief[6] either by way of credit for foreign taxes paid or by way of exemption. Alternatively, for certain provisions, complete exemption of taxation in the source state is agreed e.g. pension income is usually taxed only in the state of residence of the taxpayer[7] or till very recently capital gains accruing to a resident of Mauritius on disposal of shares in an Indian company were exempt in India and only taxable in Mauritius.[8] This capital gains exemption under the India-Mauritius DTAA has been one of the biggest drivers for Mauritius being the top country for making FDI investments into India. A recently released statistics report by the RBI confirms this with Mauritius and Singapore accounting for 50% of the total FDI which has been received by India between April 2000 to March 2017.[9] It is important to realise that treaties do not operate depending on whether the residence state ultimately taxes the income. They apply irrespective of whether a tax liability arises under the domestic laws of the residence state and seek to restrict the taxing right of the source state. Given this feature of treaties in conjunction with favourable domestic tax treatment for taxation of capital gains in Mauritius meant that effectively a very low level of taxation was suffered where investments were made through a holding company established in Mauritius. Ordinarily this would not be an issue given that countries who sign tax treaties are expected to be aware of the domestic tax system of the counterparty to the treaty. However, this situation presents an issue where tax residents of third countries – which may not have an equally favourable treaty with India – seek to benefit from the provisions of the India-Mauritius DTAA.

Take for example the case of an MNC headquartered in the United States ("US") which wishes to invest in India. The India-US treaty provides for source state taxation of the capital gains earned on disposal of shares of a company. To circumvent these seemingly unfavourable provisions, the US MNC has the alternative to invest in India by setting up a subsidiary in Mauritius which keeping aside other considerations would be considered to be a tax resident in Mauritius and entitled to benefit from the India-Mauritius DTAA. This situation is commonly referred to as "treaty shopping".

1.2 Meaning of "treaty shopping", is it legal and how do countries counter this?

Treaty shopping may thus be described as structuring a cross-border transaction solely with the purpose of taking advantage of a favourable DTAA which otherwise would not have been available because the person claiming benefits

5 Article 11 OECD Model, 2014

6 Article 23A/23B OECD Model, 2014

7 Article 18 OECD Model, 2014

8 Article 13 of the India-Mauritius DTAA has been amended to provide that capital gains on sale of shares of a company resident in India and acquired on or after 1 April 2017 may also be taxed in India

9 Refer RBI Fact Sheet on FDI From April, 2000 to March, 2007 which can also be accessed at: http://dipp.nic.in/sites/default/files/FDI_FactSheet_January_March2017.pdf

is not a tax resident of one of the countries to the treaty.

To counter such abusive practices, countries have introduced various anti-avoidance rules like the beneficial ownership requirement, LOB Clause and the principal purpose test at the treaty level and the general anti-avoidance rule ("GAAR") into the domestic law. It is important to note that all such anti-abuse rules are complementary in nature and their role is to be applicable in specific situations.

A company being an artificial person can only be expected to comply with the law and not be required to pay what constitutes a "fair" share of taxes. Given this, it is important to clarify if treaty shopping is *per se* illegal in India. This question has been adjudicated by the Supreme Court in the landmark case of *Union of India vs. Azadi Bachao Andolan*[10].

The Supreme Court had to decide if "treaty shopping" by which the resident of a third country takes advantage of the provisions of the DTAA, is illegal and thus forbidden. The Supreme Court held that many developed countries tolerate and even encourage treaty shopping possibly for non-tax reasons. Developing countries allow such treaty shopping to encourage capital and technology inflows and the loss of tax revenues needs to be viewed in light of other non-tax benefits to the economy. The Court refused to rule that treaty shopping is illegal but rather put the onus on the Government to evaluate the policy considerations behind permitting or banning it. The Court in part drew this inference by noting that the absence of an LOB Clause in the India-Mauritius treaty – in comparison to the India-US DTAA – as evidence that if the test of residence was satisfied there was no bar on third country residents taking advantage of the treaty. In the Court's view where the loss of tax revenue outweighs the non-tax benefits the Government should renegotiate the treaty with Mauritius.

The US is a prime example of a country which has a clear policy that it does not support treaty shopping and insists on including a LOB Clause in all of its tax treaties including its treaty with India. The technical explanation to the US 1996 Model Treaty contains helpful guidance on the role and purpose of the LOB clause. The explanatory notes begin by confirming that the US views a tax treaty as a vehicle for providing treaty benefits to residents of the two Contracting States and it is very important to determine which persons should qualify as "resident" for the purpose of granting treaty benefits. In their view, "treaty shopping" means the use, by residents of third states, of legal entities established in a Contracting State with a principal purpose to obtain the benefits of a DTAA between the US and the other Contracting State. It is however clarified that such a definition of treaty shopping does not cover all the cases in which a third-country resident sets up an entity in the country of a treaty partner and in which this third-country resident itself would not be entitled to treaty benefits. Where the third country resident has valid business reasons for setting up the entity in this manner and the structure is not setup merely to obtain treaty benefits, it should not be hit by the LOB provision. The above interpretation of the role of an LOB clause makes it necessary to examine the taxpayer's intent in each case. Recognising the administrative impossibility of this, the LOB Provision (as set out in US Model) sets out a series of objective tests. The assumption is that a taxpayer who meets the requirement of at least one of the tests has a valid business purpose for the structure or has a sufficiently strong nexus to the other Contracting State for claiming treaty benefits.

The above explanation clarifies the role and purpose of the LOB Provision at least for US treaties and serves as a helpful starting point for negotiating LOB Provisions in actual treaties.

10 263 ITR 706

2. Examples of LOB Clauses in Indian DTAAs

If we analyse treaties signed by India, we notice that early examples of LOB style clause are found in India's treaties with the US, United Arab Emirates ("UAE") and Singapore. India very recently amended the LOB clause in its treaty with Singapore and also incorporated such a provision in its treaty with Mauritius. In addition, there are many other recent treaties where India has included a LOB clause which have also been listed for completeness.

2.1 LOB Clause under the India-US DTAA (1989)

The India-US DTAA (1989) has a LOB provision included in Article 24 which seeks to limit treaty benefits to residents of third countries the provisions of which have been analysed below.

Paragraph 1 – Two-part ownership and base erosion test

Paragraph 1 provides that a person other than an individual will only be entitled to benefit from the treaty on satisfaction of the two-part test broken down into a) ownership test and b) base erosion test. The reason for excluding individuals from the scope of the LOB Clause is that there is limited risk of individuals indulging in treaty shopping by changing their country of residence.

The ownership test is met where more than 50% of the beneficial interest in the person claiming treaty benefits is owned directly or indirectly by individuals who are either resident in or subject to tax on their worldwide income in either of the two countries. By making a reference to both direct and indirect ownership, where an MNE group has a chain of companies which are ultimately held by resident individuals of the Contracting States, this test is met. The base erosion test is met where the person's "income" is not used in a "substantial" part, directly or indirectly, to meet liabilities (including interest or royalties) in the form of tax deductible payments to persons who are not residents of either of the contracting states. The technical explanation clarifies that generally payments which do not exceed 50% of the "income" (explained to mean gross income/receipts less cost of goods/services) would not be interpreted as "substantial".

Where a taxpayer fails to meet this two-part test one should check if any of the exceptions contained in paragraphs 2 or 3 are met.

Paragraph 2 – Exemption for active trade or business

There is an exemption from the limitation provided in paragraph 1 if the taxpayer meets the active trade or business exemption. This paragraph provides an exemption from the LOB requirement where the taxpayer has an active trade or business and the income received is in connection with or incidental to the active trade or business. This exemption, however, does not apply where the business consists of making or managing investments except in the case of a banking company or insurance company engaged in banking or insurance activities. Taxpayers should note that this is not an entity level test and rather needs to be tested for each type of income.

Paragraph 3 – Exemption for listed entities

There is an exemption from the limitation provided in paragraph 1 if the entity is listed on a recognised stock exchange in either of the two countries and there is substantial and regular trading in the entity's principal class of shares on such a recognised stock exchange. The term "recognised stock exchange" has been defined in the treaty to mean in the case of US, the NASDAQ System and any stock exchange which is registered as a national securities exchange with the Securities and Exchange Commission, US and in the case of India any stock exchange which is recognised by the Central Government under the Securities Contracts Regulation Act, 1956.

Paragraph 4 – Reference to Competent Authorities
This is the residual clause where treaty benefits may still be granted at the discretion of the competent authority even if the taxpayer does not satisfy any of the tests laid out in the preceding paragraphs. This ensures that the competent authority is able to take into account all the relevant facts and circumstances into consideration including the business structure and the nature of trade/ business in determining the eligibility for availing treaty benefits which may have been harshly denied given the mechanical nature of the tests.

2.2 LOB Clause under the India-UAE DTAA (1992)

Another example of an old Indian treaty which has a LOB Clause is the India-UAE treaty which was entered in 1992. Article 29 of the DTAA contains the LOB provision and provides that an entity shall not be entitled to the benefits of the DTAA if the main purpose or one of the main purposes of the creation of such entity is to obtain the benefits of the DTAA.

A plain reading of this provision makes it clear that it is worded very differently from the India-US DTAA and does not rely on objective tests to deny benefits of treaty shopping. It rather lays down a subjective test which evaluates the main purpose for choosing the particular structure or interposing the entity which seeks to avail the treaty benefits.

What is concerning for the taxpayer however is how the above provision will be administered in practice. A corporate structure is usually chosen for a variety of commercial and business reasons including the level of tax burden suffered. Given this it will be prudent for taxpayers to document the various business and commercial considerations when opting for a particular structure. Also, while Article 29 in the India-UAE DTAA has been given the heading "Limitation of Benefits" – the actual text is more similar to the principal or main purpose test which is found in domestic GAAR rules (or akin to the principal purpose test under BEPS Action 6) rather than a traditional LOB Clause which lays down a series of mechanical tests.

2.3 LOB Clause under the India-Singapore DTAA (1994) and the India-Mauritius DTAA (1982)

2.3.1 India-Singapore DTAA (1994)

We have seen two variants of the LOB provision in Indian tax treaties. The third type of variant is found in India's treaties with Singapore (which was recently renegotiated by signing of the third protocol amending the treaty in line with the revisions to the India-Mauritius DTAA). This provision only aims to prevent the abuse of the capital gains benefit in the treaty and does not seek to restrict other benefits available under the treaty.

The substantive revision introduced by the protocol provides India the right to tax capital gains arising on sale of shares of an Indian company which have been acquired on or after 1st April 2017 by a Singapore resident.[11] However where such gains arise between 1st April 2017 and 31 March 2019, there is transitory relief which caps the rate of tax to 50% of the prevailing tax rate.[12] Capital gains on shares acquired on or before 31st March 2017 have been grandfathered and continue to be exempt in the source state but are now subject to the revised LOB provision.[13] Further, the treaty has been amended to explicitly clarify that treaty provisions will be overridden by domestic anti-avoidance measures such as the GAAR, which came into effect in India from 1 April 2017.[14]

The revised capital gains provision described above (Article 13) is however subject to the

11 Article 13.4B India-Singapore DTAA

12 Article 13.4C India-Singapore DTAA

13 Article 13.4A India-Singapore DTAA

14 Article 28A India-Singapore DTAA

revised LOB Clause included in the treaty and found at Article 24A. The main provisions of this revised LOB Clause have been analysed below.

Paragraph 1 – Motive Test

Paragraph 1 denies the grandfather benefits[15] and the transitory relief[16] to a person if its affairs are arranged with the primary purpose of availing the benefits of these exemptions and reliefs. This provision ensures that erstwhile structures which were setup with the primary purpose of availing the capital gains exemption in the treaty before the recent amendments are denied such benefits.

Paragraph 2 – Shell or conduit companies / bona-fide business test

Paragraph 2 provides an additional limitation which prohibits the claiming of transitory benefits[17] by shell or conduit entities which have been defined to mean any legal entity with negligible or nil business operations or with no real and continuous business activities carried out in the country. This provision thus tries to target entities which are not carrying out any genuine or *bona-fide* business activities from claiming treaty benefits.

Paragraph 3 – Expenditure test

An entity is deemed to be a shell or conduit company if its annual expenditure is less than SGD 200,000 in Singapore or less than INR 5,000,000 in India, during each of the 12 month periods in the immediately preceding 24 months from the date on which the capital gains arise. Where this test is not met, the grandfathering benefits will be denied. In respect of availing the benefit of the reduced tax rate during the transitory period, the expenditure test will need to be met but only for the immediately preceding period of 12 months from the date on which the capital gain arises.

Paragraph 4 – Exemption for listed entities or where the expenditure test is met

An entity is not deemed to be a shell/conduit company if it is listed on recognised stock exchange of a country or if it meets the Expenditure test laid out in paragraph 3.

The above LOB Clause is supplemented by the introduction of Article 28A which provides that treaty provisions shall be overridden by the application of a country's domestic anti-avoidance rules. This provision makes it clear that it is the intention of the legislature to enforce GAAR even in situations where there are specific anti-avoidance provisions in a DTAA and hence investors will have to meet a higher threshold when claiming treaty benefits. Interestingly however there is no equivalent provision which has been introduced in the India-Mauritius DTAA as analysed in the next section.

2.3.2 *LOB Clause under the India-Mauritius DTAA (1982)*

India renegotiated its treaty with Mauritius with the signing of the protocol in 2016. This amendment led to the revision of the capital gains provision (Article 13) and the introduction of a LOB Clause (Article 27A) in the treaty. Significantly for India, the treaty was amended to provide for the phased elimination for the source exemption on capital gains arising on sale of shares of a company if the shares have been acquired on or after 1st April 2017.[18] However where such gains arise between 1st April 2017 and 31st March 2019, there is transitory relief which caps the rate of tax at 50% of the prevailing tax rate in the source state.[19] Capital gains on shares acquired on or before 31 March 2017 have been grandfathered and continue to be exempt in the source state.

15 Article 13.4A India-Singapore DTAA

16 Article 13.4C India-Singapore DTAA

17 Article 13.4C India-Singapore DTAA

18 Article 13.3A of India-Mauritius DTAA

19 Article 13.3B of India-Mauritius DTAA

The transitory relief described above is however subject to the new LOB Clause included in the treaty and found at Article 27A. The main provisions of this revised LOB Clause (which is similar in structure to the LOB Clause in the India-Singapore DTAA) have been analysed below:

Paragraph 1 denies the transitory relief to a person if its affairs are arranged with the primary purpose of availing the benefits of this relief. Paragraph 2 provides an additional limitation which prohibits the claiming of transitory benefits by shell or conduit entities which have been defined to mean any legal entity with negligible or nil business operations or with no real and continuous business activities carried out in the country. This provision thus tries to target entities which are not carrying out any genuine or *bona-fide* business activities from claiming treaty benefits. Paragraph 3 lays out the expenditure test which provides that an entity is deemed to be a shell or conduit company if its annual expenditure is less than Mauritian ₹ 1,500,000 in Mauritius or less than ₹ 2,700,000 in India, in the immediately preceding period of 12 months from the date on which the capital gains arises. Paragraph 4 provides an exemption from the LOB provision if the entity is listed on recognised stock exchange of a country or if it meets the Expenditure test laid out in paragraph 3.

When one compares the LOB provisions found in the India-Singapore and India-Mauritius DTAA, the LOB Clause in the India-Mauritius DTAA (Article 27A) has a narrower scope with the latter only applying to instances where transitional relief in respect of capital gains (Article 13.3B) is claimed under the India-Mauritius DTAA (the former in addition to the transitional provisions also applies to the erstwhile exemption for capital gains earned before 1st April 2017). In addition, there is no reference to the domestic anti-abuse or GAAR provisions in the India-Mauritius DTAA (as compared to the provision found in Article 28A of the India-Singapore DTAA).

This raises a question as to what is the interaction between a LOB Clause in a DTAA and a country's domestic anti-abuse rules. Can an inference be made that to the extent the LOB Provision in the India-Mauritius DTAA is satisfied there should be limited possibility for invoking GAAR? One will have to carefully weigh the arguments in support of the overriding nature of treaties given their status as international agreements and their role of relieving double taxation against the inherent purpose of domestic general anti-avoidance rules which is to counteract tax avoidance situations which are not adequately caught by LOB style specific anti-abuse rules.

While the revised capital gains provisions and introduction / revision in the LOB Clause aims to bring certainty to the application of the India-Singapore and India-Mauritius DTAAs, it remains to be seen how the above provisions (especially given the differences in the scope and wording in the two treaties) will be administered in practice. The LOB Clause in both the treaties adopts a mix of objective criteria e.g., the Expenditure test and Listing requirement combined with subjective criteria of evaluating the primary purpose of the structure for denying treaty benefits. Given this, taxpayers will have to adequately document the business and commercial reasons including for existing structures where investments are made through Mauritius or Singapore resident entities to ensure they do not fall foul of the LOB Clause.

3. Concluding Remarks

The last couple of years have indeed been very interesting for international tax advisors as the economic slowdown and reduction in tax revenues have pushed tax administrations to improvise the tools at their disposal for tackling tax avoidance and evasion. India has been an active participant both globally – as a part of the global BEPS Agenda led by the OECD and domestically – with the introduction of domestic GAAR and revision of Indian DTAAs to counter tax avoidance by inclusion of an LOB Clause. Given these developments it is worth highlighting how policy action in these areas is interacting with the existing framework of LOB Clause found in India DTAAs.

3.1 Uniformity in India's approach to inclusion of LOB Clauses in DTAAs

There are many other Indian tax treaties which include the LOB Provision in their text. While it is not possible to list and analyse all of them, in general the trend has been towards inclusion of a subjective motive test under the LOB Clause. For instance, Article 29 of the India-Norway DTAA (2011) has a LOB Provision which denies treaty benefits if the main purpose or one of the main purposes of the transaction or the formation of the entity (i.e. residence) is to avail treaty benefits. Similar wording has also been included in Article 28C of the India-United Kingdom DTAA (1993) and Article 28A of India-Poland DTAA (1989).

The above examples make it clear that there is no standardised approach which has been adopted by India in negotiating its tax treaties with a mix of objective criteria and subjective criteria being use in the LOB Clauses found in India's tax treaties. From an investor's perspective, different wording in each treaty increases the complexity in the interpretation of the tax treaties and consequently the compliance burden and overall tax risk in respect of their investments into India.

3.2 CBDT's views on interaction of domestic GAAR and treaty LOB Clause

The introduction of the domestic GAAR[20] with came into effect from 1st April, 2017 will provide an insight into the practical administration of this domestic anti-abuse provision and its interaction with various specific anti-abuse rules including those at a treaty level e.g. LOB clauses. The stated objective behind the introduction of the domestic GAAR is to tackle tax avoidance including in respect of those transactions where improper benefits are availed under a DTAA. Given this the preliminary question to answer is if benefits under a DTAA subject to the application of challenge under the GAAR provisions. While one can debate the constitutional validity of such a provision and if it constitutes treaty override, the amendments made to sections 90(2A) and 90A(2A) of the Income-tax Act, 1961 make it clear that the intention of the legislature is that treaty benefits can only be enjoyed subject to GAAR. This will be the case even where the provisions of GAAR are not beneficial to the assessee.

Following from this, the next question then is to understand if the tax administration will seek to invoke GAAR even in instances where the DTAA contains adequate anti-abuse safeguards and more specifically its interaction with LOB Clauses. The CBDT in a Circular[21] issued in the beginning of 2017 has tried to clarify aspects on the implementation of the GAAR. The circular clarifies that CBDT believes that both GAAR and specific anti-avoidance rules (e.g., Beneficial Ownership requirement, LOB Clause) can co-exist given that the specific rules may not be able to address all types of tax avoidance. Specifically, in respect of the interaction of GAAR and LOB clause under the treaty, CBDT considers that the decision on whether or not to invoke GAAR would depend on the sufficiency and nature of the LOB in addressing the mischief. Where the tax avoidance is sufficiently addressed by the LOB Clause, CBDT does not believe that there would be a requirement to invoke GAAR.

20 Chapter X-A of Income-tax Act, 1961

21 Circular No. 7 of 2017

3.3 BEPS Action item 6 recommendations and its interaction with Indian DTAAs on signing of the Multilateral Instrument ("MLI")

BEPS Action item 6 deals with treaty abuse situations and OECD was given the mandate to develop *"model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances."*[22] OECD's work in this area recommended that countries adopt the following three key changes in its tax treaties to tackle treaty abuse:

1. Clarify the purpose of a DTAA - A clear statement of intention in the preamble to the treaty that the Contracting States, when entering into a treaty, wish to prevent tax avoidance and, in particular, intend to avoid creation of opportunities for treaty shopping

2. LOB Rule - Introduction of a simplified LOB rule in tax treaties with the objective of addressing a large number of treaty shopping situations based on the legal nature, ownership in, and general activities of, residents of a Contracting State

3. The Principal Purpose Test – Introduction of a general anti-abuse rule based on the principal purpose of the transaction or arrangement to deal with other forms of treaty abuse including treaty shopping situations which are not addressed by the LOB rule

The above mentioned dual-approach by OECD of tackling abuse of residence by third country residents by introduction of simplified LOB Clause combined with a principal purpose test for transactions or arrangements is different compared to the approach adopted by India in many of its existing tax treaties for e.g., Norway, United Kingdom, Poland where the principal purpose test has been used to check abuse of both the residence conditions and transactions.[23] With 70 countries including India signing the MLI on 7th June, it will be interesting to analyse the corresponding choices made by India's treaty partners and how this conflict in approach is resolved where changes to the DTAA are implemented by the signing of the MLI.

22 OECD BEPS Action 6: Final Report, 2015 – Preventing the Granting of Treaty Benefits in inappropriate circumstances

23 Mukesh Butani, The Multilateral Instrument Era – Measuring the Impact on India, Asia-Pacific Tax Bulletin, 2017 (Volume 23), No. 2

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Case Studies – International Tax considering GAAR

1. Introduction

In the Indian tax law, till date, general anti-avoidance has been dealt with through judicial decisions. In dealing with general anti-avoidance, while some courts have shown courage to look at the substance of the transaction, there have been decisions which have strictly looked at the form and pronounced the judgment.

Memorandum to Finance Bill, 2013 mentioned that most countries have codified the substance over form doctrine in the form of General Anti-Avoidance Rules ('GAAR'). It was further stated that keeping in view the aggressive tax planning with the use of sophisticated structures, there is a need for India to codify the said doctrine of substance over form where the real intention of the parties and effect of the transaction and the purpose of an arrangement is taken into account while determining the tax consequences.

Tax avoidance is an international issue and the same has been recognized by the OECD in its Base Erosion and Profit Shifting reports as well. While the recently signed Multilateral Instrument ('MLI') seeks to address a lot of anti-avoidance concerns, it may not be able to cover all tax avoidance schemes. Further, there are countries which have not yet signed the MLI or have not opted for some of the articles of MLI or not notified India in their list of countries with which the MLI applies. Accordingly, lot of anti-avoidance schemes can still be addressed by the GAAR provisions.

2. Applicability of GAAR provisions and some concepts

Although tax authorities have been granted unfettered powers under the GAAR provisions, GAAR can be invoked only when it is proved that the assessee has employed an **arrangement** which is entered into for the **main purpose** of obtaining a **"tax benefit"** and it satisfies either of the following tainted elements:

- creates unusual rights and obligations which are not created between persons dealing at arm's length;
- results in misuse or abuse of the provisions of the Income-tax Act, 1961 (the Act);
- lacks commercial substance; or
- is carried out in a manner not ordinarily employed for *bona fide* purposes.

While certain terms have been explicitly defined under provisions, certain important terms such as "main purpose" and "bonafide purpose" have not been specifically defined. Further, terms like "arrangement" and "tax benefit" have been very widely defined which would cover almost all tax avoidance. Consequently, it becomes very important to analyse each transaction / arrangement that one enters into from GAAR perspective.

Over the years, it is observed many tax payers structure / organise / re-structure their internal businesses, entities and agreements for tax planning purposes within the judicial frame work. Going forward, under the GAAR regime, these arrangements / re-arrangement of affairs will have to pass through the test of the above referred four tainted elements if it is entered into for the main purpose of obtaining a tax benefit. In this article, we shall look at some examples in the form of case studies and analyse them from GAAR perspective.

3. Case Studies

3.1 Investment abroad and shifting operations abroad

In a trading business, at times it is easy to shift the base for operations from one country to another. In such a situation, it might be possible to structure the trading operations in a manner to obtain some tax benefits. The below case study discusses one such structure and analyses the applicability of GAAR on the structure.

The facts of the case are as under:

<u>Year 1</u>

(a) India Co. is a private limited company incorporated in India and tax resident of India.

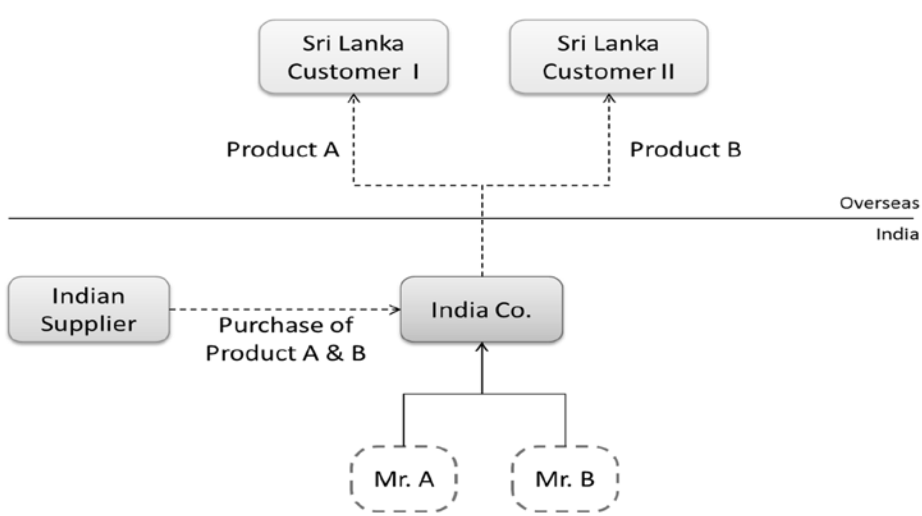
(b) Mr. A and Mr. B (both Indian residents) are the shareholders of the company.

(c) India Co. is in the business of wholesale trading in FMCG products and deals in only two products, Product A and Product B.

(d) During year 1, India Co. procures both the products from an Indian Supplier and sells Product A to Sri Lanka Customer I and Product B to Sri Lanka Customer II.

(e) The net profit margin earned by India Co. on product A (being a luxury product) is 50% and that on Product B is 15%.

<u>Year 1</u>



Year 2

(a) In year 2, the consultant of India Co. advises it to set-up a free zone company in UAE which will be held 95% by India Co., 2.5% by Mr. A and 2.5% by Mr. B.

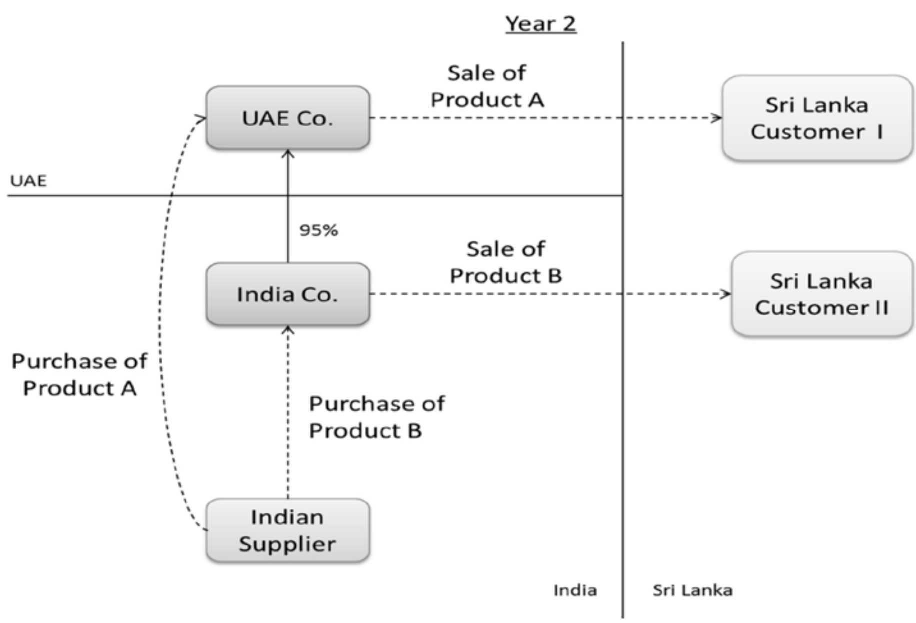
(b) The UAE company is set-up with a trading licence and with an intention to start trading operations of Product A through UAE Co. Consequently, the trading operations of Product A will be discontinued in India Co. Please note that there is no business transfer agreement entered into between India Co. and UAE Co.

(c) UAE Co. operates through a physical office in free zone in UAE.

(d) For taking care of day-to-day operations, it has appointed one key person (UAE resident) who has the requisite skills for handling the trading operations. Apart from the key person, the UAE office is staffed with 4 more employees (UAE residents) who have requisite skills and experience in trading business and 2 employees for maintenance of daily books of account.

(e) Mr. A, Mr. B and the key person are the board members of the UAE Co. Mr. A and Mr. B periodically visit UAE and conduct a board meeting for making strategic decisions. Mr. A and Mr. B are not involved in any business activity of UAE Co. when they are in India.

(f) Under the new structure, in year 2, UAE Co. will acquire Product A from Indian supplier and sell it to Sri Lanka Customer I and India Co. will continue to sell Product B to Sri Lanka Customer II.



Issue

Given the facts of the case, let us analyse the applicability of GAAR provisions.

Comments and analysis

Before we go into analysis of GAAR provisions, it is important to note that shift of operations which is a business restructuring may be subject to applicability of provisions of Chapter X (Transfer Pricing provisions) of the Act and an analysis with respect to the said provisions would be required. However, the said provisions would only take care of the issue as to whether there should have been a consideration (and consequent taxability) flowing from UAE Co. to India Co. on shift of operations. Chapter X would not be enough to address the issue of taxability of future trading profits of the UAE Co. in India. Accordingly, one needs to analyse GAAR provisions. Further, it would also be important to note that if income tax officer applies GAAR, as a consequence, the shift of operations can be disregarded. If the shift of operations is disregarded, there is a possibility to argue that the transfer pricing provisions should not apply. Accordingly, given the facts of the case, GAAR and Transfer Pricing provisions should not co-exist. Transfer Pricing provisions and GAAR should both be applied only to the facts of the case where consequence of applicability of GAAR permits application of TP provisions as well.

In order to analyse the applicability of the GAAR provisions to any transaction, it is first important to check whether the act of the assessee (shift of operations in the present case) would fall within the definition of "arrangement" as per section 102(1) of the Act. The definition of "arrangement" as per section 102(1) includes any step in, a part or whole of any transaction, operation, scheme, agreement or understanding. In the instant case, trading in Products A and B should qualify as an 'operation' carried on by the group and selling product A through UAE Co. should qualify as a "part" of the whole trading operations and accordingly, should be covered under the definition of "arrangement".

Next, it is important to check if there is a tax benefit arising to the assessee by virtue of shifting of operations. The computation of income and tax in year 1 and year 2 is given in the table below:

<u>Year 1</u>

Sr. No.	Particulars	Amount (₹ in Crs.)	Amount (₹ in Crs.)
		Product A	Product B
	<u>India</u>		
1	Sales	100.00	100.00
2	Cost	-50.00	-85.00
3	Net profit	50.00	15.00
4	**Corporate Tax @ 34.608%**	-17.30	-5.19
5	Net Income available to Indian Co.	32.70	9.81
6	**Less: DDT u/s. 115-O @ 20.358%**	-6.66	-2.00
7	Dividend paid to shareholders	26.04	7.81
8	**Less: Dividend Tax @ 11.845% u/s. 115BBDA**	-3.08	-0.93
9	Net Income of shareholders (Post Tax)	23.32	6.88
10	Total Income of Shareholders	30.20	
11	**Total tax paid by India Co. (4 + 6)**	31.15	
12	**Total tax paid by Shareholders (8)**	4.01	

Year 2

Sr. No.	Particulars	Amount (₹ in Crs.)	Amount (₹ in Crs.)
		Product A	Product B
A	**UAE**		
1	Sales	100.00	
2	Cost	-50.00	
3	Net profit	50.00	
4	Corporate Tax @ 0%	0.00	
5	Net Income available to Dubai Co.	50.00	
6	Dividend payable to shareholders	50.00	
B	**India**		
7	Dividend income for India Co. /Net Profit from Product B	50.00	15[1]
8	**Less: Tax on Dividend u/s. 115BBD @ 17.304%**	**-8.65**	–
9	**Less: Corporate Tax @ 34.608%**	–	5.19
10	Net Income of India Co.	41.35	9.81
11	**Dividend Distribution Tax @ 20.358%**	–[2]	2.00[3]
12	Net Income to Shareholders	41.35	7.81
13	**Less: Dividend Tax @ 11.845% u/s. 115BBDA**	**-4.90**	**-0.93**
14	Net Income of shareholders (Post Tax)	36.45	6.88
15	Total Income of Shareholders	43.33	
16	**Total tax paid by India Co. (8 + 9 + 11)**	**15.84**	
17	**Total tax paid by Shareholders (13)**	**5.83**	

As can be seen, in year 1, the total tax outflow to the India Co. (Corporate tax + DDT) is ₹ 31.15 Crs. And total tax paid by the shareholders is ₹ 4.01 Crs., **total combined tax outflow being ₹ 35.16 Crs.**

However, in year 2, only because of shift of operation to UAE Co., the amount of tax paid by UAE Co. is Zero, tax outflow of India Co. reduces to ₹ 15.84 Crs. (as compared to ₹ 31.15 Crs.) and that for the shareholders increases to ₹ 5.83 Crs. (as compared to ₹ 4.01 Crs.). Consequently, the **total combined tax out flow for Year 2 reduces to ₹ 21.67 Crs.** resulting in an **overall tax benefit of ₹ 13.49 Crs.** It is important to note here that there is a possibility that the income-tax officer might want to claim that declaration of dividends from UAE Co. to India Co is only a consequence and therefore, would want to compare corporate tax paid on Product A i.e. ₹ 17.30 Crs. in year 1

1 Refer Sr. No. 3 under calculations for year 1

2 DDT payable u/s. 115-O will be set off due to tax paid u/s. 115BBD. Hence, no tax is payable by the Indian company on payment of dividend (refer Sr. No. 11 for product A).

3 Technical reading of section 115-O permits reduction of entire ₹ 50Crs. of dividends received from the UAE Co. from total dividend distributed by India Co. of ₹ 51.16 Crs. (41.35 +9.81), in which case the DDT at sr. no. 11 above would be ₹ 0.24 Crs. However, we have adopted a conservative approach and claimed a reduction of ₹ 41.35 Crs. (i.e. net dividends).

vis-à-vis zero in year 2. A better view would be to compare the tax assuming cash flow at India Co level.

As can be seen from the above, there is a reduction of tax and consequently a tax benefit as per section 102(10).

As per section 97(1)(c), an arrangement shall be deemed to lack commercial substance, if it involves transfer of an asset or transaction which is without any substantial commercial purpose other than obtaining tax benefit. In the facts of the present case, the shift of business operations from the India Co. to UAE Co. and sale of Product A from UAE is without any substantial commercial purpose. Therefore, the arrangement of sale of Product A from UAE should be deemed to lack commercial substance. Further, since there is no other substantial commercial purpose of shift of operations, obtaining tax benefit should be regarded as the main purpose of the arrangement.

Consequently, as per section 96(1) since the arrangement is the one main purpose of which is to obtain tax benefit and is also deemed to lack commercial substance, the same should be regarded as an impermissible avoidance arrangement. In terms of section 96(1), the said arrangement should also fairly get covered under section 96(1)(d) which mentions about an arrangement which is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for *bona fide* purposes.

Here, it is very important to note that the commercial substance of the entity in UAE (which can be proved from the facts) would be irrelevant for the purposes of analyzing the applicability of GAAR provisions and what is relevant is the commercial substance and bona fides of the arrangement. In a case where the shift of operations is backed by substantial commercial purpose, like business partner residing abroad, investor requiring presence in overseas jurisdiction, convenience of physical presence due to customer base in the overseas country, regulatory benefits, etc., there could be a possible argument available with the assessee to justify the bona fides of shifting operations and consequently to defend applicability of GAAR provisions.

Once the arrangement is declared as an impermissible avoidance arrangement, the consequences with respect to disregarding the arrangement in parts or as a whole would follow. A careful reading of the above analysis shows that the real tax benefit is in the hands of the India Co. (assessee). Whereas, the shareholders (although getting a higher net income) are liable to pay more tax in year 2 (₹ 5.83 Crs.) as compared to year 1 (₹ 4.01 Crs.). In such a situation, a question remains to be answered as to whether while computing the revised tax liability of India Co. (assessee), the net tax benefit (after considering the additional tax paid by shareholders) will be considered or whether it will be calculated on standalone basis. Given that section 99 requires looking through a corporate structure and treating parties who are connected purposes as one and the same[4], it should be possible to argue that the additional tax paid by the shareholders should be considered while calculating the revised tax liability.

3.2 Investment in India through offshore jurisdiction – Debt

Having seen the shift of operations overseas by an Indian resident (outbound structure) in the first case study, let us pick up a case study on inbound structure.

The facts of the case are as under:

a) USA Co. is a company incorporated in USA and a tax resident of USA.

4 Also refer Question 14 of Circular No. 7 of 2017 dated 27-1-2017 which states that tax benefit should be considered after taking into account impact to all the parties to the arrangement i.e. on a net basis.

b) India Co. is a company incorporated in India and a tax resident of India.

c) USA Co. has entered into a term sheet with India Co. to subscribe to Compulsorily Convertible Debentures ('CCDs') for ₹ 200 crores to be issued by India Co. carrying interest @ 9% per annum.

d) The consultant of USA Co. advised it to set-up a wholly-owned subsidiary ('WOS') in Mauritius and let the Mauritius WOS subscribe to the CCDs of India Co.

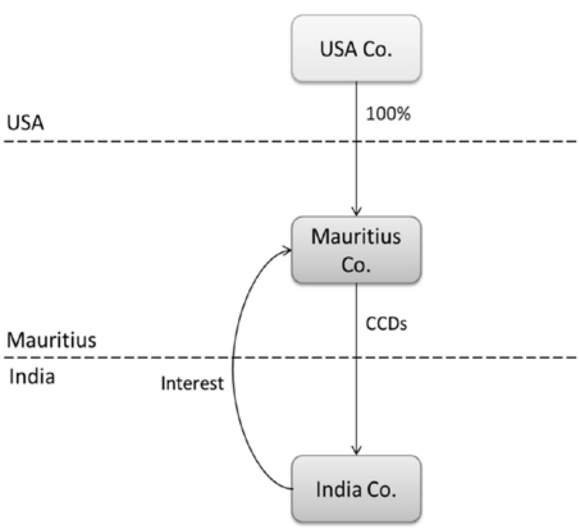
e) Based on the advice, USA Co. sets-up Mauritius Co. as a WOS in Mauritius.

f) Mauritius Co. is a company incorporated in Mauritius and a tax resident of Mauritius.

g) Mauritius Co. subscribes to CCDs issued by India Co.

h) India Co. pays interest of ₹ 18 crores (₹ 200 Crs x 9%) to Mauritius Co. at the end of year 1

Given below is the diagrammatic representation of the structure:



Issue
Given the facts of the case, let us analyse the applicability of GAAR provisions.

Comments and analysis
Setting-up of WOS in Mauritius and Investment in CCDs of an Indian company would both, individually as well as put together, qualify as a 'transaction' and therefore would fit within the definition of 'arrangement' as per section 102(1).

As per section 97(1)(c), as can be seen from the facts, the above referred arrangement should be deemed to involve location of the Mauritius WOS which is without any substantial commercial purpose.

Is there a tax benefit as per section 102(10)? Based on the facts of the case, the Mauritius Co. should be liable to pay tax on the interest earned from CCDs @ 40% as per provisions of the Act. However, Mauritius Co., being a tax resident of Mauritius and holding a valid tax residency certificate, should be eligible to a reduced rate of tax of 7.5% as per Article 11 of the DTAA between India and Mauritius. In case the investment was not made through Mauritius Co., the benefits of DTAA between India and Mauritius would not have been available. Accordingly, the tax benefit that can be quantified would be approx. (₹ 5.85 crores. [differential tax rate of 32.5% (40-7.5) being applied to interest of (₹ 18 crores].

However, there could be a possible argument on the part of the assessee that in case the investment was not made through Mauritius Co., the investment would have been made directly by USA Co. and therefore the benefits under Article 11 of the DTAA between India and USA should be taken into account while determining the tax benefit. As per Article 11 of the DTAA between India and USA, interest is taxable in India at the rate of 15%. Accordingly, the tax benefit should be calculated as (₹ 1.35 crores approx. [differential tax rate of 7.5% (15-7.5) being applied to interest of (₹ 18 crores]. If such a view is adopted, as per Rule 10U(1)(a), since the tax benefit in the relevant assessment year is less than (₹ 3 crores, the provisions of Chapter X-A should not apply to the facts of the case. As per Section 90(2A), GAAR provisions shall apply to the assesse even if such provisions are not beneficial. Could this mean that once GAAR provisions are applied, the benefits of any DTAA should not be available? The answer should be no. Section 90(2A) seeks to deny the benefits of the DTAA which is the part of the tainted arrangement (i.e. India – Mauritius DTAA in the present case) and not to deny the benefits of India – USA DTAA discussed above. Accordingly, a better view would be to consider the India – USA DTAA benefit while calculating the tax benefit.

However, in case the income-tax officer considers the tax benefit as (₹ 5.85 crores (by denying the benefit under India-USA DTAA), he would treat the arrangement of setting up of Mauritius Co. and subscribing to CCDs of India Co. as an impermissible avoidance arrangement as arrangement is deemed to lack commercial substance and is entered into for the main purpose of obtaining tax benefit as discussed above. And the consequences as per section 98 shall follow. Consequently, the law of the land laid down by the Hon. Supreme Court in Union of India vs. Azadi Bachao Andolan[5] on availability of treaty benefits based on a Tax Residency Certificate would now be re-tested with the applicability of the GAAR provisions. It would be interesting to see how the courts look at this issue on transactions post 1 April 2017.

3.3 Sales in India through an agent

Facts of the case

(1) SimSmart Limited is a company incorporated in UK and a tax resident of UK. It is in the business of manufacturing and selling 'Sim Card manufacturing machines' to telecom service providers.

(2) Ramesh, a person resident in India, is an agent of SimSmart for its India sales. Ramesh's activities are devoted almost wholly for SimSmart.

(3) In the course of his services under an agreement, Ramesh performs the following activities in India:

  (a) Sends e-mails, makes telephone calls to, or visits large organisations in order to convince them to buy products of SimSmart.

  (b) Uses his relationship building skills to convince the prospective customers;

  (c) Ramesh has the authority to negotiate price with the customers; and

  (d) Habitually plays the principal role leading to finalisation of the terms of contracts.

(4) The final drafted contracts, as agreed between Ramesh and Indian customers, are then sent to SimSmart for execution and the same are executed by Simsmart without any material modifications or changes outside India.

(5) Ramesh does not have authority to conclude contracts with the Indian customers on behalf of SimSmart.

(6) The premises of Ramesh are not available at the disposal of SimSmart.

Issue

Given the facts of the case, please analyse the applicability of GAAR provisions?

Comments and analysis

As per Article 7 of the Double Tax Avoidance agreement ('DTAA') between India and UK, 'Business Profits' from sale of machines / equipment by SimSmart would be liable to tax in India only if SimSmart has a permanent

5. Citation: 263 ITR 706 [2003] (SC)

establishment ('PE') in India through which the business of the SimSmart is carried on. Given the facts of the case, as per Article 5(4) of India-UK DTAA, SimSmart should not be regarded as having an agency PE in India through Ramesh as Ramesh does not have an authority to conclude contract and is factually also not concluding contracts in India on behalf of SimSmart. Accordingly, based on the facts of the case, SimSmart should not be liable to tax in India on its business profits as per Article 7 of India-UK DTAA read with section 90 of the Act.

However, it seems important to analyse the GAAR provisions under Chapter X of the Act with respect to the agreement between SimSmart and Ramesh. The detailed analysis of the GAAR provisions is as under.

Arrangement as per section 102(1) includes an agreement and therefore the agreement between Ramesh and SimSmart would qualify as an "arrangement" as per Section 102(1) of the Act.

As per the agreement, Ramesh does not have an authority to conclude contracts on behalf SimSmart and therefore, although the agreements are negotiated and finalised by Ramesh, the conclusion and signing is performed by SimSmart outside India. Accordingly, although in substance, Ramesh is concluding contracts on behalf of SimSmart, in form, he is not. Therefore, as per Section 97(1)(a), the agreement between Ramesh and SimSmart would be an arrangement that shall be deemed to lack commercial substance as the substance and effect of the arrangement as a whole, is inconsistent with and significantly differs from its form.

In case SimSmart had a PE in India, it would have been liable to tax in India on the profits attributable to the activities carried out in India by Ramesh. Accordingly, there is a tax benefit as per section 102(10). Here, it is important to note that section 102(10) speaks about reduction of tax payable under the Act, i.e. reduction of tax payable in India. Accordingly, a higher tax liability on these profits in the country of residence would not change the fact that there is a tax benefit as per section 102(10).

Accordingly, without any other commercial justification, the agreement with Ramesh could be considered as having been entered into by SimSmart for the main purpose of avoiding tax presence in India. Consequently, as per Section 96(1), the agreement between Ramesh and SimSmart should be regarded as an impermissible avoidance arrangement as it is entered into for the main purposes of obtaining a tax benefit and it is deemed to lack commercial substance.

There could be a possible argument as to whether GAAR provisions can override the treaty, i.e. whether the treaty benefits can be denied by invoking the GAAR provisions. This issue has been discussed at length in another chapter. However, in the facts of the present case, whether the Income Tax Officer will really deny the benefits of the DTAA as a consequence of GAAR being applied? The answer would be no[6]. If GAAR is applied, the consequence would be that the Income Tax Officer would deem Ramesh to be having an authority to conclude contracts on behalf of SimSmart and that he is habitually exercising the said authority. The Income Tax Officer would not deny the benefits of the DTAA but once the Income Tax Officer has re-arranged the facts as above, he would apply the provisions of the India – UK DTAA and conclude that SimSmart has a PE in India based on the re-arranged facts referred above.

3.4 Shift of residence

Viscount Sumner *[Levene vs. IRC 13 TC 486, 501 (HL)]* has remarked: "It is trite law that His Majesty's subjects are free, if they can, to make their own arrangements so that their cases fall outside the scope of the taxing Act." This thought has to undergo a change now with the GAAR provisions in place. The below

6. Please note that the applicability of principle purpose test under the DTAA has not be discussed here.

case study covers a situation where an Indian resident individual would physically move himself outside India to dispose of his India and Overseas Assets.

The facts of the case are as under:

a) Rahul is a citizen of India and is resident of India for tax purposes since many years.

b) Rahul is holding investment in shares of a foreign company which he had invested when the foreign company was a start-up (5 years back). Rahul also holds shares in Indian unlisted companies which have gained value over the years. Rahul had made the investments in these companies 4 years back.

c) Rahul does not have any business presence outside India.

d) On 1st April, 2017, Rahul travels outside India and stays abroad for the whole year. Consequently, Rahul would be a non-resident of India for tax purposes for FY 2017-18.

e) During FY 2017-18, Rahul sells the shares of the foreign company and a couple of unlisted companies and earns a capital gain of ` 30 crores (` 15 crores from transfer of shares of foreign company and balance ` 15 crores from transfer of shares of unlisted Indian companies).

Issue

Given the facts of the case, please analyse the applicability of GAAR provisions?

Comments and analysis

A careful reading of the facts suggest that Rahul performed the following two actions:

- He physically moved himself outside India and stayed outside India for the whole year; and
- Sold shares of foreign company and unlisted Indian companies in FY 2017-18.

Accordingly, it will be important to check if either or both of the above actions would be an "arrangement". As discussed earlier, the definition of "arrangement" as per section 102(1) includes any step in, a part or whole of any transaction, operation, scheme, agreement or understanding. A view could be that physically staying outside India, by itself, does not get covered under either 'transaction', 'an operation', 'scheme', 'agreement' or 'understanding'. Accordingly, shift of residence should not be regarded as an arrangement. However, sale of shares is definitely a "transaction" and therefore would qualify as an "arrangement".

As per section 97(1)(c), since the arrangement (being sale of shares), involves location of Rahul outside India which is without substantial commercial purpose, the arrangement would be deemed to lack commercial substance.

Rahul, being a non-resident during FY 2017-18, would not be required to pay tax on sale of shares of foreign company as per section 5 of the Act. Further, he would get the benefit of section 112(1)(c) and consequently pay tax on gains on sale of shares of unlisted Indian companies @ 10%. Had he sold these shares as a tax resident of India, he would have paid tax @ 20% under section 112(1)(a). Accordingly, it can be concluded that there is a reduction of tax and therefore, a tax benefit as per section 102(10).

However, as discussed, there are two actions performed by Rahul, i.e. shift of residence and sale of shares. The tax benefit that has been derived by Rahul as discussed above is on account of 'shift of residence' which is not an arrangement as concluded above. On the other hand, 'sale of shares' which qualifies as an arrangement, by itself, does not derive any tax benefit. Accordingly, for the purposes of section 96(1), it could possibly be argued that 'shift of residence' is not an arrangement. And 'sale of shares' which is an arrangement, is not entered into for the purposes of obtaining tax benefit. Accordingly, the said two actions performed by Rahul should not be regarded as an impermissible avoidance arrangement and consequently GAAR provisions should not apply.

A question therefore would arise as to whether the two actions (shift of residence and sale of shares) together would qualify as an arrangement. The Income Tax Officer would want to take a view that both the actions together would qualify as a "scheme of selling shares as non-resident". If such a view is taken by the Income Tax Officer, the consequent applicability of Section 97(1)(c) and the fact that the main purpose of shift of residence and sale of shares is to obtain tax benefit would lead to Rahul's separate actions being regarded together as an impermissible avoidance arrangement and the consequences of non-allowability of tax benefits would follow.

Please note that the above conclusion is based on the assumption that Rahul has travelled abroad for the main purpose of obtaining tax benefit explained above. The purpose of travel abroad would be a very important factor to determine the applicability of GAAR provisions in such cases. Consider a case where Rahul has a business abroad and moves outside India to participate and look after the overseas business; or say Rahul takes up employment abroad and therefore moves outside India and post that disposes India and overseas investments to buy a house to stay in the country in which he has taken up business / employment. With such facts, there could be very good chances that Rahul will be able to rebut the applicability of GAAR provisions as the test of 'main purpose' and 'arrangement lacking commercial substance' should not be regarded as have been satisfied.

5. Conclusion[7]

As can be seen from the comments and discussion on the case studies above, it is very important to analyse the applicability of GAAR provisions on each and every transaction that we advise on, as the way the provisions read, some of the tax planning even though performed within the four corners of the law, may be hit by GAAR. From a cross border transaction perspective, it is important to note that an overseas structure which leads to tax benefit can be hit by GAAR provisions if there is no commercial substance for creating an overseas structure, even if the overseas entities which are part of the structure have fully operating offices with employees. In other words, the rationale and commercial substance of the arrangement is to be looked at and not commercial substance of the entities. Further, GAAR being a new codification, with practically nothing in terms of jurisprudence, it would be interesting to see how strictly or liberally courts interpret these provisions.

7. Please note that the intent of this Chapter is to provide an overview of practical aspects of GAAR applicability and understand the same through some selected case studies. Apart from the cases referred above, there will be lot of other arrangements which will be tested under GAAR and each arrangement needs to be examined basis the principles referred above.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Case Studies – Domestic Tax considering GAAR

The provisions of General Anti-Avoidance Rules ('GAAR') dealt with in Chapter X-A of the Income-tax Act, 1961 ('Act') have been introduced with effect from financial year 2017-18. While judicial decisions based on GAAR has a long history in India, formally codified legislation in this regard and its applicability to various situations and interplay with various provisions of the Act is inscrutable. Some of such situations are discussed here.

Setting up SEZ unit and downsizing domestic unit

Units established in Special Economic Zones ('SEZ') have been granted tax holiday by way of exemption under Section 10AA of the Act. As per the provisions of Section 10AA, 100% of profits and gains derived by SEZ units from export of article or things manufactured or services provided by the unit, are exempt from tax for first 5 years and only 50% of such profits are taxable in subsequent 5 or 10 years subject to the conditions specified therein. Accordingly, while business units set up in Domestic Tariff Area ('DTA') are subject to normal corporate tax rate of 25 to 30% (plus applicable surcharge and cess), business units set up in SEZ enjoy tax holiday and are only subject to minimum alternate tax at the rate of 18.5% (plus applicable surcharge & cess). Further, in cases where SEZ units are set-up in the same company in which domestic unit is in existence, the effective additional tax on such SEZ unit profits could be 'Nil' or substantially lower than even MAT. A question therefore arises whether provisions of GAAR can be applied for setting up units in SEZ instead of domestic area or to cases where domestic units see reduction in the level of activities along-side setting up SEZ units.

General Anti-Avoidance Rules or GAAR are anti-abuse provisions introduced as a measure to curb tax avoidance or misuse or abuse of tax provisions. To fall within the ambit of GAAR provisions, the assessee should have entered into 'an arrangement' and such arrangement entered into by the assessee should fall within the definition of an 'impermissible avoidance arrangement'.

'Arrangement' has been defined in Section 102 to mean any step in, or a part or whole of, any transaction, operation, scheme, agreement or understanding, whether enforceable or not, and includes the alienation of any property in such transaction, operation, scheme, agreement or understanding. While the term has been defined in an exhaustive manner, the definition has a wide scope and would cover operations such as establishing an SEZ unit.

Section 96 requires that for any arrangement to be considered as an impermissible avoidance arrangement, it is essential that the main purpose of entering into the arrangement should have been to obtain a tax benefit. In addition to this main or principal purpose test, at least one of the tainted element tests (arm's length test, misuse or abuse test, commercial substance test or *bona fide* purpose test) as laid down in Section 96 should be fulfilled for an arrangement to be considered as an impermissible avoidance arrangement.

Coming to our example, even if decision of setting up of a SEZ unit may be driven by the tax benefits or tax incentives available to SEZ units, availing benefits legally accorded by law should not be considered as abuse of the provisions. Exemption under Section 10AA has been granted with an intention to develop and promote SEZ units and hence setting up of SEZ unit and availing tax benefit would be in accordance with the object and purpose of the provisions of the law and would therefore not meet the main purpose test and tainted element tests laid down in Section 96.

The report of OECD on Action plan 6 of the Base Erosion and Profit Shifting Project in context of preventing grant of tax treaty benefits in inappropriate circumstances refers to the GAAR and principal purpose test as follows – 'general anti-abuse rule based on the principal purposes of transactions or arrangements (the principal purposes test or 'PPT' rule) will be included in the OECD Model Tax Convention. Under that rule, if one of the principal purposes of transactions or arrangements is to obtain treaty benefits, these benefits would be denied unless it is established that granting these benefits would be in accordance with the object and purpose of the provisions of the treaty.' Accordingly, where a tax benefit is in accordance with the object and purpose of provisions of the law, the same should not be considered as abuse of the provisions of the law.

The Shome Committee report also recommended inclusion of an illustrative negative list of arrangements to which GAAR should not be applied, which included setting up of unit in SEZ *vis-à-vis* any other place. Press Release issued by CBDT on draft guidelines regarding implementation of General Anti-Avoidance Rules in June 2012 also concurred this view that GAAR should not be applied in case of tax benefits arising on setting up of unit in SEZ as the same is not in the nature of tax avoidance.

CBDT *vide* its Circular No. 7 of 2017 dated January 27, 2017 has further clarified that GAAR will not interplay with the right of the taxpayer to select or chose method of implementing a transaction. Accordingly, where a taxpayer has options legally available to him and he choses one of the options, such as in case of setting up of unit in SEZ *vis-à-vis* DTA, GAAR should not apply.

Tax benefit to SEZ units have been granted to incentivise setting up new units in SEZ to boost further manufacturing and also exports. However, where setting up of SEZ unit is coupled with reduction in the level of activities in domestic unit, the moot question could be whether the same can be said to have met the objective of introducing the said incentive provision. The Apex Court in the case of Bajaj Tempo Ltd.[1], in relation to granting benefits under Section

1 [1992] 62 Taxman 480 (SC)

15C of the erstwhile Income tax Act, 1922 dealing with exemption available to newly established industrial undertaking observed that a provision in a taxing statute granting incentives to taxpayer should be construed liberally. However, the same should apply when the benefits availed by the assessee is in accordance with the objective of the incentive provisions. If the beneficial provisions of law are frustrated by arranging the transactions in an artificial manner, the rules of liberal interpretation of beneficial provisions laid down in the judicial decisions may not come to rescue of the taxpayer.

It may be relevant to note that Section 10AA itself includes specific Anti-Avoidance Rules or 'SAAR' to ensure that taxpayers do not misuse the said provisions and only newly set up units in SEZ, engaged in manufacturing or provision of services avail exemption benefits. Section 10AA(4) provides that the exemption under Section 10AA shall not apply if –

(i) the SEZ unit is formed by the splitting up, or the reconstruction, of a business already in existence or

(ii) the unit is formed by the transfer to a new business, of machinery or plant previously used for any purpose, exception being imported machines which was never used in India prior to installation at the SEZ unit. However, it also provides quantitative thresholds that where old or previously used plant or machinery is transferred to the new SEZ unit and such old plant or machinery comprises less than twenty per cent of the total plant and machinery used in the business of SEZ unit in value terms, the same is excluded from the SAAR provisions.

Non-obstante clause in Section 95 indicates that GAAR provisions will apply notwithstanding other provisions of the Act. Considering that provisions of Section 10AA(4) as well as Chapter-XA are in the nature of anti-avoidance rules, there is no conflict amongst them and the same can co-exist. In relation to interplay of SAAR and GAAR, CBDT *vide* its Circular No. 7 of 2017 dated January 27, 2017, has also clarified that general anti-abuse provisions are needed because specific anti-avoidance provisions may not address all situations of abuse and hence provisions of GAAR and SAAR can co-exist and are applicable based on the facts and circumstances of the case.

In fact, the provisions of GAAR would supplement SAAR provisions. The restrictions in Section 10AA(4) would continue to apply even after introduction of GAAR (and the threshold of tax benefits exceeding ₹ 3 crores would not be available in such case). At the same time, where the assessee has arranged the transaction in a manner just to meet the quantitative threshold of Section 10AA(4), GAAR may still be invoked if conditions of Section 96 are fulfilled.

To put it differently, there could be three scenarios – (i) the case is not covered by a SAAR provision, (ii) SAAR provision with quantitative tests is applicable or (iii) SAAR provision with qualitative tests is applicable to the facts and circumstances of a particular case. We believe there appears to be no dispute that cases which are out of coverage of SAAR provisions can be subjected to tests of GAAR. In case where special anti-abuse provision prescribes quantitative thresholds (similar to 20% old machinery criterion mentioned above), there is possibility to argue that GAAR may not be applied in so far as such requirement is concerned. However, where the threshold are met by arranging the transactions artificially, the same could be regarded as abuse of provision of law and therefore GAAR provision should be capable of being invoked in such circumstances. As regards the third set of cases where SAAR provisions are applicable and arrangements are subjected to qualitative tests under SAAR, the provisions of GAAR should generally not be applicable in such circumstances. This is because the qualitative tests under SAAR and the tests under GAAR are both based on the fundamental principle of substance over form and in fact, GAAR and SAAR co-exist in a way that while applying qualitative tests under SAAR, GAAR provisions may provide guiding principles and *vice versa*. Accordingly, where qualitative tests are applied under specific anti-abuse provisions such as transfer pricing provisions and where it is concluded that the transactions have been entered into in accordance with arm's length principles, GAAR provisions should not be reapplied to such cases.

Coming back to the issue on hand, the terms 'split up' as well as 'reconstruction' used in Section 10AA(4) are in the nature of qualitative SAAR tests. These terms are not defined in the Act and the same would be capable of subjective interpretation depending upon circumstances of each case. In case of *Textile Machinery Corporation Ltd.*,[2] while dealing with provisions of Section 15C the Indian Income-tax Act, 1922 corresponding to Section 80J of the Act, the Apex Court held that reconstruction of business involves the idea of substantially the same persons carrying on substantially the same business and where the business activities of the industrial undertaking set up by the assessee was not the same as before, exemption under Section 15C was allowed to the assessee. In the said case, the Apex Court laid down fact based guiding principles that can be applied to identify whether or not the new industrial undertaking has been formed by reconstruction or split up of old business, such as (i) investment of substantial fresh capital in the industrial undertaking set up, (ii) employment of requisite labour therein, (iii) manufacture or production of articles in the said undertaking, (iv) earning of profits clearly attributable to the said new undertaking, and (v) a separate and distinct identity of the industrial unit set up. It may also be important to note that in the case of *Chenab Information Technologies (P.) Ltd.*[3], since the existing business of the assessee as well as business of the new unit was the same and where the new STPI business unit was set up by the assessee with a minimal investment in leased premises and with existing employees, it was held that the new unit was formed by splitting up of the existing business. Exemption under Section 10A was thus denied even though the STPI unit served new customers. These decisions clearly indicate that 'split up' or 'reconstruction' is a fact-based examination and quantitative thresholds cannot be prescribed for the same.

At this juncture, it may be relevant to note that decline in operations of domestic unit could be a consequence of several contributory factors and it need not necessarily be a corollary to tax benefits arising to the SEZ unit. Therefore, it would be crucial to establish a nexus between setting up of SEZ unit and downsizing of domestic unit, before the same is subjected to rigours of GAAR. For application of GAAR provisions, it would be essential that the arrangement meets main purpose test and tainted element test to be considered as an impermissible avoidance arrangement. For instance, whether or not the customers of domestic unit are served by the SEZ unit, whether there is a shift in customer contracts, a shift in resources such as employees, etc. from domestic unit

2 [1977] 107 ITR 195 (SC)

3 [2008] 25 SOT 432 (Mumbai)

to SEZ unit or not, etc. and many more corroborative facts and circumstances. Tax authorities would be required to establish that there is misuse or abuse of provisions of Section 10AA and that the SEZ unit has been established by downsizing of the domestic unit and shift of assets and resources therefrom before invoking GAAR in such circumstances.

Dividend and bonus stripping

Specific anti-avoidance provisions to curb dividend and bonus stripping are incorporated in Section 94 of the Act to disallow capital loss or business loss arising on account of such transactions. However, it may be relevant to note that the specific provisions of Section 94(7) and Section 94(8) provide for quantitative thresholds and do not lay down qualitative tests to prevent tax avoidance.

Question arises with respect to cases of dividend and / or bonus stripping not falling within the specific provisions of Section 94. For instance, assessee could have entered into dividend stripping, however, the shares could have been acquired 95 days prior to record date i.e. just before the three months' timeline. In this case, it can be said that there does exist a SAAR to cover such transactions the provisions of GAAR should apply only if the threshold limits have been artificially met to frustrate the provisions of Section 94(7).

Further, while Section 94(7) covers cases of dividend stripping in relation to shares as well as units of mutual funds, Section 94(8) only provides for anti-avoidance rules in relation to bonus stripping from mutual fund units. Section 94(8), thus, does not lay down anti-avoidance provisions in cases of bonus stripping in relation to shares of companies.

Here it may be relevant to note the decision of Bangalore ITAT in the case of **B. G. Mahesh**[4], which held that the provisions of Section 94(8) were clearly applicable only to mutual fund units and not to shares and other securities. The ITAT in that case also observed that Section 94(7) in relation to dividend stripping was introduced by Finance Act 2001 and covered both securities and units, whereas Section 94(8) which was introduced subsequently by Finance Act 2004 was applicable only to transactions of bonus stripping in case of mutual fund units. It was thus inferred that the intention of legislature was to exclude the shares of companies from the ambit of the provisions of section 94(8) of the Act and the ITAT held that there was no legislative authority to deny the loss even if it is intentionally created by the assessee as the case of bonus stripping in case of shares was specifically outside the purview of provisions of Section 94(8) of the Act. Considering that GAAR provisions were introduced to cover tax avoidance cases which were not covered by SAAR, GAAR should be applicable in such cases which are not covered by SAAR. Chapter XA now provides that authority of law referred by the Hon'ble ITAT in the said decision and therefore the decision of ITAT may be different under post-GAAR scenario.

Here, it may be relevant to note the decision of Supreme Court in the case of *Walfort Share & Stock Brokers (P.) Ltd.*[5] where in context of dividend stripping prior to introduction of Section 94(7) it was held that receipt of dividend which is exempt under Section 10(33) being in accordance with the provisions of the law, cannot be considered as 'abuse of law'. Further, subsequent to introduction of Section 94(7), the Court observed that Section 94(7) restricts allowance of losses only to the extent of

4 [2014] 43 taxmann.com 158 (Bangalore - Trib.)

5 [2010] 326 ITR 1 (SC)

amount of tax exempt dividend earned by the assessee and losses over and above the amount of the dividend received would still be allowed, based upon which the Court held that the Parliament has not treated the dividend stripping transaction as sham or bogus, it has not treated the entire loss as fictitious or only a fiscal loss. Taking a cue from the Supreme Court decision, a question may arise as to whether the abuse test or substance tests for qualifying the tainted element tests would be fulfilled in case of dividend or bonus stripping transaction. It may therefore be essential to have detailed scrutiny of the facts and circumstances of the case in detail to identify if the transaction so undertaken meet bona fide test or other tainted element test laid down under Section 96 of the Act, for application of GAAR provisions.

Delaying transfer by long-term lease arrangements

In case of lease arrangements, lessor is taxed on lease rentals received from the lessee under the head profits and gains from business or profession and lessee is entitled to claim deduction with respect to lease rentals so paid. Further, under the current provisions of the Act, lessor gets deduction on account of depreciation on the assets provided on lease irrespective of the type of lease. The same has been upheld by various judicial decisions such as in the case of I.C.D.S. Ltd.[6], wherein the Supreme Court held that lessor being the owner of the asset would be eligible to claim depreciation under Section 32 and not the lessee. CBDT *vide* its Circular No. 2 of 2001 dated February 9, 2001 also clarified the same.

On the other hand, in case of transfer of assets, gains arising on transfer of assets would be chargeable to tax in the year of transfer and right to claim depreciation also gets transferred to the transferee. In light of the above, a taxpayer may be benefitted on providing assets by way of long term lease instead of transferring the assets in certain cases.

With respect to applicability of GAAR, it may be noted that leasing of assets is not prohibited under any law. Accordingly, when an enterprise provides an asset on lease instead of transferring the same, but at the same time retains the legal and economic rights over the asset, the same should not be considered as an abuse or misuse of the provisions of the law as tax benefit is availed in accordance with the provisions of the law.

Also, in view of CBDT Circular 7 of 2017 which clarifies that GAAR will not interplay with the right of the taxpayer to select or chose method of implementing a transaction, assessee's decision of providing assets on lease instead of selling the same should not *per se* be subject to GAAR.

However, where the assets provided on lease are in substance transferred to the lessee, GAAR may however be applied in such case subject to fulfilment of conditions of Section 96. Say for example a land is proposed to be transferred, however, considering that the same was held for less than 24 months, immediate transfer would attract higher tax on short term capital gains. In order to avail benefits in relation to long term capital gains, the parties agree that transferor shall provide the asset to the transferee on lease for two years and will transfer the asset to the transferee at the end of the lease period. Say the sales consideration is fixed in the lease agreement itself and the interest portion on the deferred consideration is agreed to be paid as lease rentals. In such case, the lease rental is paid towards the lease for the term of two years and not towards part performance of the sale contract referred to in Section 53A of Transfer of Property Act,

6 TS-8-SC-2013

1882. Thus, despite the fact that the person has already parted with the possession of the property and has also received certain portion of the money, section 2(47)(v) may still not be invoked and thus would not be regarded as 'transfer' when the lease is granted. Thus, the tax on transfer is deferred by two years and the tax rate would reduce from 30% to 20% (plus applicable surcharge and cess) and could be further reduced if benefit of exemption u/ss. 54 to 54F is claimed. In ordinary circumstances, lease may not generally be questioned on the basis of GAAR, however, where the circumstances and other actions surrounding the said transactions have been undertaken with the main objective of tax benefit (and in substance the property has been effectively already conveyed), the tax authorities may be keen to test the provisions of GAAR.

Conversion of Company to LLP

Another instance could be conversion of company into Limited Liability Partnership ('LLP'). From a tax perspective, one of the distinguishing factors between the two forms of entities is that LLPs are not subject to dividend distribution tax and profits distributed. In other words, LLPs are subject to one-tier taxation whereas companies are subject to two tier taxation in India.

From a legal perspective, both Company and LLP are forms of incorporated entities, legally permitted under the statutes. Further, conversion of company into LLP is also permitted under the provisions of law. LLPs are generally subject to less amount of compliance requirements and are subject to less stringent regulations as compared to companies. Accordingly, conversion of company to LLP may also be driven by commercial reasons such as ease of operations and not just tax benefits.

In fact, the Act itself recognises conversion of company into LLP and considers it as a tax neutral transaction under Section 47(xiiib) subject to conditions therein. While considering tax benefit for the purpose of GAAR, should it include unconditional tax benefits only or it should also include tax benefits under defined circumstances (e.g., declaration of dividend). It may be relevant to note that corporate tax rate for small companies has been reduced from 30% to 25% whereas LLPs are continued to be taxed at 30%. Therefore, if a company, which has not declared any dividends in past years, say for past ten years or say since its inception, can conversion of such a company into LLP be considered as an impermissible avoidance arrangement (on the ground that LLP would in fact shell out more tax than it would have paid had it remained a company not declaring dividend)? Considering that Section 47(xiiib) also imposes restriction on distribution of profits by LLPs for three years subsequent to its conversion from company to LLP, can conversion of company to LLP be considered as a transaction entered into with the purpose of availing tax benefit? If the arrangement can be argued to meet the tests of section 96, the computation of 'tax benefit' for applying threshold of Rs. 3 crore would also require consideration from various aspects.

Where taxpayer choses or opts a legal form of entity over another, where both these forms are available to him under the statutory provisions, there may be good arguments to support the position that conversion of company into LLP may not be regarded as an impermissible avoidance arrangement unless the same is coupled with other transactions. In other words, rigours of GAAR cannot be applied where tax neutrality is accorded by the provisions of the statute. However, where the quantitative thresholds in section 47(xiiib) granting tax neutrality are met by artificial steps, possibility of applicability of GAAR can be considered.

CA Rashmin Sanghvi

Disruptions in Income Taxation

Let us consider in this article the Disruption in Taxation. There is an attack on tax evasion (black money) as well as tax planning. And the attack is within India as well as globally. There is tremendous progress & innovation in technology causing disruption in business. Same technology is causing disruption in taxation also. Compliance by Tax-payers, Practice by Consultants and Administration by Tax Department – all are disrupted. The attack on black money covers Demonetisation and GST. However, in this article, we focus on Income-tax only.

A brief understanding of – Threats to Income Taxation and the Causes for the Threats – is presented below.

The attack on tax planning is through several amendments in Income-tax Act and through BEPS. Attack on tax evasion is through sharing of information by banks & Governments. This sharing of information has become practical because of technology.

1. Threats to Income tax

We have received several "Wake-up calls". Now the wake-up calls are over and harsh provisions have already been passed into several laws. All these provisions together will give tremendous presumptive powers in the hands of tax administration.

1.1 Legal Amendments

The tax laws have been amended and are in the process of further amendments. Transfer pricing with considerable presumptive provisions, is already a serious difficulty. Now GAAR has been passed, POEM has become a law. We already have more than 30 SAARs. Black Money law has serious provisions. BEPS (Base Erosion & Profit Shifting) is making huge provisions amending Double Tax Avoidance Agreements and making it difficult to do tax planning. It will be difficult for tax commissioners as well as tax consultants to understand and apply these provisions.

1.2 Collapse of Banking Secrecy

Swiss banks and banks in several tax havens provided secrecy to people holding money with those banks. Now with the pressure of OECD & G20, all secrecy has collapsed. All banks, financial institutions and financial intermediaries have to share information about – the beneficial owner and his investments – with the country of tax residence of the investor. All the information about any person's funds available in any bank etc. almost anywhere in the world are available to the Governments where they are liable to pay tax. This is not future. Information sharing has already started.

There were some instruments through which people with black/criminal money could hide their identity. For example – numbered accounts; accounts in the name of companies with bearer shares; discretionary trusts where the trustees could change the names of beneficiaries and so on. All these instruments have collapsed. Banks & financial institutions have to maintain full identity (KYC including copy of passport) of the ultimate beneficial owner. And this information is being shared with the Country of Residence (COR) of the beneficial owner.

1.3 Restrictions on Tax Havens

Tax haven Governments were actively promoting incorporation of companies and other entities in tax havens specifically to avoid the taxes and other regulations of the Countries of Residence. With the pressures of OECD & G20 and amendment of treaties through Multilateral Instrument (MLI under BEPS programme), these different tax avoidance plans have become next to impossible. All tax havens may lose significant amount of their business.

1.4 FEMA to FERA

Harassment by Enforcement Directors under FERA had become legendary. Their courage in harassing people crossed limits and some officers even harassed members of Parliament. This is when the outcry against Enforcement Department reached top Government authorities. In the year 2000 FERA was replaced by FEMA. Enforcement Directorate powers were clipped and people heaved a sigh of relief.

By Finance Act, 2015, Sections 13(1A) to 13(1D) & 37A have been added to FEMA. Section 37–A in short provides that:

"If the Enforcement Director suspects that any person has any foreign assets, in violation of section 4 of FEMA, he (ED) – can seize Indian assets of that person equivalent in value to the foreign assets".

Now consider this provision.

(i) The ED may merely have a "suspicion". The law does not require that he should have evidence of violation of S. 4 of FEMA.

(ii) And the law does not require that ED should serve a notice, should provide opportunity to explain, etc. – before seizing the Indian assets.

The Government may, by internal rules provide for certain safeguards. However, to make such a law giving wide open powers to the regulator and then hoping that there will be internal rules and regulations; amounts to Police Raj. I sincerely hope that if these provisions are challenged before a Court of law, the Court will strike down these provisions as unconstitutional. However, very few assessees have resources adequate to go to a High Court and Supreme Court fighting against law. Until someone successfully fights again FEMA, rest of the people will suffer under such absurd law.

When a tax consultant advises his client to have assets outside India in furtherance of the tax planning, he must ensure that it does not amount to violation of FEMA. This needs emphasis because I already hear tax planning products that amount to FEMA violations. Those tax-payers who get tempted into such tax planning products, are exposed to serious consequences.

Now FEMA has become more draconian than erstwhile FERA. One can imagine the consequences of giving such wide powers in the hands of ED.

1.5 Technology

Computers, internet and communication systems (mobile telephones and other telecommunication systems) have all made considerable technological progress. And all these technologies have converged. All our communications are easily available to Governments. In case, some reader may not know: all internet service providers (ISP) like VSNL, SIFY etc., are required by law to maintain 100% records of all the communications through their system. Thus, telephone calls from mobile phones, e-mails, sms etc. ALL are stored with ISP for many years. Whenever, Government wants, this information can be accessed by Government.

1.6 Automatic Exchange of Information

As a part of BEPS programme about 100 countries have agreed to share tax & finance information. Earlier, there have been Court decisions that Indian Income-tax department cannot make "Fishing Enquiries". It is possible that some people may have black money abroad. Indian Government has no information about such money. Then they cannot even make enquiry. Now, under BEPS, all the Governments including the tax haven Governments are expected to send information about all Indian residents' income and wealth in those countries. It will not be necessary to make enquiry. They will send the information automatically. Several tax havens already officially shared information with Government of India.

Whether the income/wealth is held in the personal name of the assessee or through any entity (discretionary trust or company etc.) and any number of entities in a series; still the information applicable to the ultimate beneficial owner will reach Government of India.

1.7 Departmental Expertise

There was a time when tax professionals were ahead of the Income-tax department. Some professionals knew a lot more than the Income-tax Commissioners. Now there are several Income-tax Commissioners who have studied abroad, travelled abroad and worked with OECD/ IBFD. They have tremendous amount of knowledge of income-tax & international taxation. Commissioners with expert knowledge are now armed with wide deeming provisions under the law.

1.8 Judiciary

There was a time when, a taxpayer and the tax consultant considered the judiciary to be on the side of the assessee. Today things are changing. Some of the Tribunal and Court decisions are rejecting the tax planning. Judiciary is demanding substance.

This cannot be said to be an all India trend. Some decisions even now ignore the substance of facts and intention of legislation; and go by the form of paper work.

There is no clear trend in judicial decisions. Still, overall, today one can expect more judgments to be in favour of the department than could be expected five years before.

1.9 Benami

Consider the Benami Transactions (Prohibition) Act (BTPA). It was suggested in 1973 and passed as a law in 1988. However, it was not implemented till 2016. It is only now after 28 years that the law has become effective in the year 2016. This is a part of the concerted attack on black money. In the past, there was no political will to implement the law. Present Government has made it a mission to attack black money & tax avoidance.

1.10 Army of laws

Within Income-tax Act, we have – more than 30 SAARs, GAAR, Transfer Pricing, POEM etc., attacking black money & tax planning. The attack on black money is not just through Income-tax Act. A list of other laws is: FEMA, Prevention of Money Laundering Act, Benami Transactions (Prohibition) Act, Automatic Information Sharing Agreement – all together attack black money. BEPS which affects Double Tax Avoidance Agreements, attacks tax planning.

This army of legal provisions has been arranged against the taxpayer trying to avoid tax. The army includes several deeming provisions. These can be used to terrorise even an honest taxpayer.

1.11 Convergence of Several Forces

Thus, there is a convergence of law, technology, departmental expertise and judiciary. All together are against tax evasion as well as tax planning.

While people will keep trying to find out ways of tax planning, it will be tremendously difficult. It will disrupt the practices of some tax consultants, banks & tax havens.

There have been many cases where people thought it normal to set up discretionary trusts and SPVs in tax havens and to hold black money through such tax havens. Now these people may find themselves being prosecuted.

2. Cause of this situation

A submission: For many harsh anti-avoidance provisions, the cause lies in the fact that: Some taxpayers avoided taxes by resorting to aggressive tax planning and the appellate Courts upheld the tax avoidance. In India, cases like Vodafone & Azadi Bachao Andolan are illustrations. In Europe, tax avoidance by Google, Apple, Starbucks etc., are illustrations. Parliament had no option but to bring in anti-avoidance provision.

Let us see illustrations to see whether the above submission is correct. These illustrations may also help in getting a perspective of SAAR, GAAR, BEPS, etc.

2.1 Consider the simplest of the Specific Anti-Avoidance Rule (SAAR) – clubbing provision under Section 64. In the olden days, a husband would reduce his tax liability by diverting his wealth to his wife and children. If all the income were to be taxed in the hands of husband only, it would attract tax at a higher rate. By gifting away his wealth – source of income – income is diverted at the source itself. Wife & minor children who may have no/lower income; get the benefits of lower taxes. By making deeming provision u/s. 64 this planning is curbed. Simple tax provision has become a bit complicated.

2.2 From the simple SAAR, let us see a complex SAAR: Section 9(1)(i) Explanation 5. (Vodafone provisions.) Vodafone did a tax planning and avoided massive tax payment. These facts are too well-known. These are briefly stated below. Hutchison, a Hong Kong company held two third shares in Hutchison SR, an Indian company providing mobile telephone services. Hutchison held the shares through a Cayman Island company. Hutchison sold its share to Vodafone, a British Company. Instead of selling the shares of the Indian company, Hutchison sold one share of $ 1 in the Cayman Island company to Vodafone and then claimed that the shares of the Indian company were never sold. Only the share of Cayman Island company was sold. Hence there was no liability to pay tax in India. I have written articles on this subject saying that this transfer of shares was liable to tax in India even under the law before amendments. Supreme Court of India in the decision on Vodafone held that Hutchison was not liable to pay tax and hence Vodafone was not liable to deduct tax at source. Government of India amended Section 9 and introduced Explanations 5, 6 & 7 to Section 9(1)(i).

Consider the provisions of Explanation 5. In simple words, it provides that if the share or any interest – in a foreign company or any foreign entity derives – directly or indirectly – its value substantially from assets located in India; then such share or interest shall be held to be situated in India. The consequence of this amendment would be that on a transfer of such foreign share etc., capital gains would be payable in India.

This Explanation created several controversies. What is meant by "Substantially"? A foreign mutual fund may be holding share in several Indian companies. When the units in the foreign mutual fund are transferred, would they become liable to tax in India? Foreign unit holders may or may not have any idea about the investments made by the mutual fund. How will they pay capital gains tax? All these controversies arose because Hutchison and Vodafone made a tax planning which was contrary to logic and common sense. In trying to cover such tax avoidance within the tax net, Indian Income-tax Act has become complex.

2.3 Transfer Pricing

The Transfer Pricing provisions in the Indian Income-tax Act had terrorised many taxpayers. The provisions require the tax payers to artificially decide a market price (Arm's Length Price). When any commercial transaction happens amongst associated parties, each and every transaction has to be compared with the Arm's Length Price (ALP). In reality, we know that there is no standard market price. Even for branded products like toothpastes and readymade garments, individual buyers negotiate the price and get a negotiated price. In several products like diamonds and personal consultancy services, there is no way to determine a market price. In all these situations, tax consultants prepare thousand page reports justifying their assumed ALP. The Tax Commissioners reject entire reports and assume different ALP. In the process, the taxpayers suffer huge tax, interest and penalty.

This entire difficulty has happened because many famous MNCs actually resorted to underinvoicing or overinvoicing of their products sold amongst associated enterprises. When MNCs resorted to aggressive tax avoidance and called it legal, Governments had no option but to amend the legal provisions and prevent such tax avoidance.

2.4 Tug of war

When gifts to wife and minor children were covered under Section 64, taxpayers came out with the new tax planning of discretionary trust. These trusts were also used for holding assets outside India. One can get into details of such tax avoidance games. However, Indian Government introduced Section 164 under the Indian Income-tax Act and taxed discretionary trusts at the maximum marginal rate.

So, taxpayers came out with oral trusts. Again, the law was amended & S. 164A was introduced.

Then the taxpayers came out with oral AOP. Multiple HUF was again another idea for tax avoidance. Each and every such planning attracted specific anti-avoidance rules by different sections.

In this tug-of-war between tax-payers and Government of India, Indian Income-tax Act went on becoming longer, more complex and far removed from reality.

Under the Indian Partnership Act, when a partner contributes his assets to the partnership firm, or withdraws his assets, retires or dissolves the firm – in all the situations, there is no transfer. The reason is that under the Partnership Act, partnership is not a separate entity. It is a relationship amongst the partners. Partners and their firm are not separate.

When the Indian Income-tax Act has been amended, theses fundamental principles of Partnership Law have been thrown out. Why Section 45 had to be amended and complex provisions had to be brought in? Because, in Kartikey Sarabhai Case, Mr. Sarabhai formed a partnership firm on day one. Introduced capital asset to the firm on day two. The firm was dissolved on day three and the asset was taken away by another partner. Mr. Sarabhai got cash which was introduced by the other partner. In short, the capital asset was sold by Mr. Sarabhai to a third party through the means of partnership firm and capital gains tax was avoided.

This tax planning was upheld by the Hon'ble Supreme Court.

Government had no option but to amend Section 45 and bring in deeming provisions in the form of sub-sections (3) & (4).

This is how the Income-tax Act has become complex.

3. BEPS

Tax avoidance through complex planning is not the monopoly of Indian taxpayers. In fact, MNCs do massive tax planning through very complex structuring etc.

3.1 American Multinational Companies like Apple, Google, Starbucks etc. avoided the taxes of European countries like Britain, France & Germany. This caused beginning of a process to control Base Erosion & Profit Shifting (in simple terms – Tax Avoidance). G20 & OECD together have prepared fifteen Action Reports and finalised Multi-Lateral Instrument (MLI).

This MLI will sit on top of about 3,000 Double Tax Avoidance Agreements signed by several countries around the world. Interpretations of existing DTAs will change due to MLI.

This is expected to prevent a lot of Income-tax avoidance that MNCs were indulging in. Even the existing tax avoidance arrangements will be hit when MLI becomes effective.

Now we have ITA which stands modified by DTA.

Then DTA stands modified by MLI.

And MLI is subject to individual country reservations. Interpretation of law itself will be very difficult.

3.2 MLI brings in several provisions like:

3.2.1 MNCs and their subsidiaries have to submit – Country by Country reports.

3.2.2 Transfer Pricing provisions have been made tougher.

3.2.3 Treaty shopping will be very difficult. Even regular foreign investors will have to prove that no treaty shopping, etc. is involved.

Similarly, there are other measures to control tax avoidance.

4. Conclusion so far

Tax provisions have become extremely complex to understand, difficult and costly to comply with. Responsibility for this fact lies squarely with MNCs and other tax payers, their tax consultants and the tax judgments which upheld such artificial tax avoidance.

While the tax consultants and taxpayers both have abused the law, we are all aware of the corruption within the tax department. Corrupt officers have harassed taxpayers even under the old Income-tax law. The new law will give machine guns in the hands of Income-tax officers and Enforcement Directors.

5. Way out

Till the year 1973, we had Income-tax @ 97.25% for incomes above ₹ 1,00,000. Wealth-tax was @ 8%. Hence most of the wealthy people had to sell their wealth to pay Income-tax and Wealth Tax or hold their wealth and income as black money. Estate Duty was @ 85% for estate in excess of ₹ 20 lakhs. No sensible person would be able to avoid temptation of black money.

From this high level of taxation, Government of India has come a long way. Estate duty, wealth tax and gift tax have been abolished. Income-tax rates have been brought down under 35%.

Have we responded to Government's positive action by honest payment of taxes? If we do not respond to Government's positive moves, we attract harsh provisions.

The only way out is to actually pay taxes honestly in substance & in spirit. Drop all the tax planning products. Acquire the confidence of Indian Government as well as international associations of Governments and then pray for better laws.

6. Possible future

Look at the whole tug-of-war as a global drama unfolding.

6.1 In the past, there have been Governments – in India & abroad, who have passed laws that –

(i) Curb tax avoidance; and also –

(ii) Permit specific kinds of tax avoidance.

6.2 When the present Government came in power in the year 2014, there was a move to ban Participatory Notes (PNs). When lobbyists complained, the Finance Minister made the famous public statement. "India is not a Tax Haven. Such tax avoidance instruments have to go." In a few months, FM forgot his statement. PNs continued. In the year 2017, SEBI has been successful in bringing some restrictions on PNs.

6.3 Place of Effective Management (POEM) provisions in Section 6(3) of ITA were a big blow on tax planning through tax haven companies. Someone lobbied. And now all foreign companies with turnover of less than ₹ 50 crore are exempted from POEM provisions. The companies with turnover of more than ₹ 50 crores will most likely have their POEM outside India. New Section 6(3) is far better for tax avoidance than the old Section 6(3). Lobbying has been successful under present Government in frustrating an anti-avoidance measure.

6.4 Tax consultants used to selling tax planning products have already started marketing some products – which they believe; will take care of SAAR, GAAR & BEPS; and help the tax avoidance. These products already look hollow & are likely to crash.

And the tug-of-war goes on.

> Relationships are based on four principles: respect, understanding, acceptance and appreciation.
>
> — *Mahatma Gandhi*

Index of Case Laws

B. V. Jhaveri, *Advocate*

DIRECT TAXES
Supreme Court

S.45(5) : Enhanced compensation and interest thereon under an interim order passed by the High Court in pending appeals relating to land acquisition matter are liable to be assessed for income tax in the year in which it has been received

CIT vs. Chet Ram (HUF) [Civil Appeal No.13053/2017, (@ SLP (C) No.751/2009) dated 12th September, 2017]

(i) The scheme of Section 45(5) of the I.T. Act, 1961, was inserted w.e.f. 1-4-1988 as an overriding provision. As stated above, compensation under the LA Act, 1894, arises and is payable in multiple stages which does not happen in cases of transfers by sale, etc. Hence, the legislature had to step in and say that as and when the assessee claimant is in receipt of enhanced compensation it shall be treated as "deemed income" and taxed on receipt basis. Our above understanding is supported by insertion of clause (c) in Section 45(5) w.e.f. 1-4-2004 and Section 155(16) which refers to a situation of a subsequent reduction by the Court, Tribunal or other authority and recomputation / amendment of the assessment order.

(ii) Section 45(5) read as a whole [including clause (c)] not only deals with reworking as urged on behalf of the assessee but also with the change in the full value of the consideration (computation) and since the enhanced compensation/consideration (including interest under Section 28 of the 1894 Act) becomes payable/paid under the 1894 Act at different stages, the receipt of such enhanced compensation/consideration is to be taxed in the year of receipt subject to adjustment, if any, under Section 155(16) of the 1961 Act, later on. Hence, the year in which enhanced compensation is received is the year of taxability. Consequently, even in cases where pending appeal, the Court/ Tribunal/Authority before which appeal is pending, permits the claimant to withdraw against security or otherwise the enhanced compensation (which is in dispute) the same is liable to be taxed under Section 45(5) of the 1961 Act. This is the scheme of Section 45(5) and Section 155(16) of the 1961 Act. We may clarify that even before the insertion of Section 45(5)(c) and Section 155(16) w.e.f. 1-4-2004, the receipt of enhanced compensation under Section 45(5) (b) was taxable in the year of receipt which is only reinforced by insertion of clause (c) because the right to receive payment under the 1894 Act is not in doubt.

(iii) It is important to note that compensation, including enhanced compensation/consideration under the 1894 Act, is based on the full value of property as on the date of notification under Section 4 of that Act. When the Court/Tribunal directs payment of enhanced compensation under Section 23 (I-A), or Section 23(2) or under Section 28 of the 1894 Act it is on the basis that award of the Collector or the Court, under reference, has not compensated the owner for the full value of the property as on date of notification.

[Commissioner of Income Tax, Faridabad vs. Ghanshyam (HUF) (2009) 315 ITR 1 (SC) followed.]

IT: Where High Court proceeded to decide revenue's appeal without formulating substantial question of law, order passed by it was to be set aside

[2017] 85 taxmann.com 262 (SC) Supreme Court of India Maharaja Amrinder Singh vs. Commissioner of Wealth Tax

The question, which arose for consideration was whether the High Court was justified in allowing the appeal filed by the revenue and setting aside the orders passed by the Tribunal without formulating substantial question of law.

Allowing the appeal and setting aside the order and remanding the case to the High Court for deciding the appeal afresh, the Supreme Court held as under:

(a) A three Judge Bench of the Court in *Santosh Hazari vs. Purushottam Tiwari [2001] 3 SCC 179* had examined the scope of section 100 of the Code of the Civil Procedure, 1908.

(b) The Court succinctly explained the meaning of the words "substantial question of law" and "question of law" and held that in order to admit the second appeal, what is required to be made out by the appellant being *sine qua non* for exercise of power under section 100 of the Code, is existence of "substantial question of law" arising in the case so as to empower the High Court to admit the appeal for final hearing by formulating such question. In the absence of any substantial question of law arising in appeal, the same merits dismissal *in limine* on the ground that the appeal does not involve any substantial question of law within the meaning of section 100 of the Code.

(c) Now coming to the facts of the case, it is found that the High Court proceeded to decide the appeals without formulating the substantial question(s) of law. Indeed, the High Court did not make any effort to find out as to whether the appeal involved any substantial question(s) of law and, if so, which is/are that question(s) and nor it formulated such question(s), if in its opinion, really arose in the appeals. The High Court failed to see that it had jurisdiction to decide the appeals only on the question(s) so formulated and not beyond it.

(d) In the light of foregoing discussion and keeping in view the law laid down in the case of Santosh Hazari (supra), it is held that the impugned order is not legally sustainable and thus liable to be set aside.

S.119 : The CBDT has no jurisdiction to issue a Circular to amend the legislative provisions set out in the Act. Such action is *ultra vires* and liable to be quashed

CIT vs. S. V. Gopala Rao & Ors. [Civil Appeal No(s). 4901/2010, dated 13th July, 2017]

Rule 68B(1) of the Second Schedule to the Income-tax Act, 1961 reads as under:

"68B (1): No sale of immovable property shall be made under this Part after the expiry of three years from the end of the financial year in which the order giving rise to a demand of any tax, interest, fine, penalty or any other sum, for the recovery of which the immovable property has been attached, has become conclusive under the provisions of section 245-I or, as the case may be, final in terms of the provisions of Chapter XX:

Provided that where the immovable property is required to be resold due to the amount of highest bid being less than the reserve price or under the circumstances mentioned in Rule 57 or Rule 58 or where the sale is set aside under Rule 61, the aforesaid period of limitation for the sale of the immovable property shall stand extended by one year."

The assessment of the petitioner was completed before June 1, 1992. The Department tried to auction the property but auction was cancelled because the price procured in such auction was not acceptable to the Department. Therefore, the Department claimed one year's further time in accordance with the proviso to sub-rule (1) of Rule 68B of the Second Schedule to the Act. The High Court stayed the sale proclamation and the stay continued for a period of five years. On a writ petition challenging the sale as beyond time, it was contended by the Department that Rule 68B was inserted by an Act of Parliament in 1992 and the Central Board of Direct Taxes made an amendment to Rule 68B, by Notification No. S. O. 164(E), dated March 1, 1996 , by inserting a proviso to Rule 68B(1) by which the time limit of three years for sale of attached immovable property under Schedule II, Rule 68B had been extended to four years. The petitioner contended that the benefit of the amendment could not be given effect to, as it was *ultra vires* the Act.

The Andhra Pradesh High Court allowed the writ petition and held that no power had been given u/s. 119 of the Act to issue such notification. Therefore, the time limit of three years in Rule 68B(1) would alone continue and the amendment by way of notification had no effect at all. Hence, the sale was carried out beyond the time and as such set aside.

Dismissing the appeal of the Department, their Lordships of the Supreme Court held that the CBDT issued a Circular under Section 119 of the Income-tax Act, 1961, whereby it amended the provisions contained in Rule 68B of the Second Schedule to the Income-tax Act, 1961, which has a statutory force. Such legislative provisions cannot be amended by CBDT in exercise of its power under Section 119 of the Act. The High Court has, therefore, rightly held the circular *ultra vires* and quashed the same.

S.260A : Right of appeal is not a matter of procedure. It is a substantive right. This right gets vested in the litigants at the commencement of the *lis* and such a vested right cannot be taken away or cannot be impaired or imperilled or made more stringent or onerous by any subsequent legislation unless the subsequent legislation said so either expressly or by necessary intendment. An intention to interfere with or impair or imperil a vested right cannot be presumed unless such intention be clearly manifested by express words or by necessary implication

K. Raveendranathan Nair vs. Commissioner of Income Tax & Anr. [Civil Appeal No. 3131 of 2006 dated 10th August, 2017]

The Supreme Court held as under:

In the present case, as noted above, when Section 260A of the IT Act was introduced by way of amendment with effect from October 1, 1998, it contained provision in the form of clause (2) of sub-section (2) thereof relating to payment of Court fee as well. As per that provision, fixed Court fee of ₹ 2,000/- was provided. This provision was, however, omitted with effect from June 1, 1999. The Court fee became payable as per Section 52 of the 1959 Act. The amendment in question in the 1959 Act, i.e., Section 52A, was made effective from March 6, 2003. This provision has not been made retrospective.

We, therefore, are not able to subscribe to the aforesaid view of the High Court and set aside the same. In fine, we hold as under:

(i) Wherever assessee is in appeal in the High Court which is filed under Section 260A of the IT Act, if the date of assessment is prior to March 6, 2003, Section 52A of the 1959 Act shall not apply and the Court fee payable shall be the one which was payable on the date of such assessment order.

(ii) In those cases where the Department files appeal in the High Court under Section 260A of the IT Act, the date on which the appellate authority set aside the judgment of the Assessing Officer would be the relevant date for payment of Court fee. If that happens to be before March 6, 2003, then the Court fee shall not be payable as per Section 260A of the IT Act on such appeals.

IT : In view of amendment made in Section 132A by Finance Act of 2017, 'reason to believe' shall not be disclosed to any person or any authority or Appellate Tribunal as recorded by Income-tax Authority under section 132 or section 132A

[2017] 85 taxmann.com 361 (SC)

Supreme Court of India N. K. Jewellers vs. Commissioner of Income-tax, New Delhi

(a) In a search by Railway Police (GRP), the employee of the appellant, who was returning from Amritsar was found in possession of ₹ 30 lakhs cash. The said employee sold gold biscuits and in return received the cost of 40 gold biscuits and previous balance totalling in all to ₹ 30 lakhs.

(b) The said information was received by the Investigation Unit, Jalandhar from SHO, GRP Station Jalandhar on 29-5-2000. Warrant of authorisation u/s. 132A of the Income-tax Act, 1961, (hereinafter referred to as the Act), was obtained from the Director of Income Tax, Ludhiana and the cash of ₹ 30 lakhs was requisitioned on 3-6-2000 and seized. Proceeding for assessment for the block period from 1-4-1991 to 3-6-2000 under Section 158BD of the Act was initiated.

(c) The explanation of the appellant before the Assessing Authority was that his employee had gone to Amritsar to make some purchases of gold but the transaction did not materialise. The Assessing Officer was of the view that the amount represented sales of gold made by the appellant on earlier occasions and the sale proceeds were being carried back to Delhi. After considering the statements of various persons and other material on record, the authorities came to the conclusion that it was concealed income and accordingly the appellant was assessed to tax.

(d) Before the Supreme Court the learned counsel for the appellant submitted that the proceedings initiated under Section 132 of the Act were invalid for the reason that it cannot be based on a search conducted on a train by the police authorities and, therefore, the proceedings initiated for block assessment period 1st April, 1991 to 3rd June, 2000 are without jurisdiction.

(e) Dismissing the aforesaid plea and accordingly dismissing the appeal, the Supreme Court held as under:

"7. This plea was not raised by the appellant before any of the authorities.

Further, we find that in view of the amendment made in Section 132A of the Income-tax Act, 1961 by Finance Act of 2017, the 'reason to believe' or 'reason to suspect', as the case may be, shall not be disclosed to any person or any authority or the Appellate Tribunal as recorded by Income Tax Authority under Section 132 or Section 132A. We, therefore, cannot go into that question at all. Even otherwise, we find that the explanation given by the appellant regarding the amount of cash of ₹ 30 lakhs found by the GRP and seized by the authorities has been disbelieved and has been treated as income not recorded in the books of account maintained by it.

"8. In view of the above, we do not find infirmity in the order passed by the High Court."

S.115-O : Dividend Distribution Tax: Entire law on the Constitutional validity of Dividend Distribution Tax (DDT) under Article 246 of the Constitution read with Entry 82 of List I and Entry 46 of List II in the Seventh Schedule and whether tea companies are liable for the tax on only 40% of the dividend income explained

Union of India & Ors. vs. Tata Tea Co. Ltd. & Anr. [CA No. 9178 of 2012, dated 20th September, 2017]

Their Lordships of the Supreme Court held as under:

"24. As noted above Entry 82 of List I embraces entire field of "tax on income". What is excluded is only tax on agricultural income which is contained in Entry 46 of List II. Income as defined in Section 2(24) of the 1961, Act is the inclusive definition including specifically "dividend". Dividend is statutorily regulated and under the article of association of companies are required to be paid as per the Rules of the companies to the shareholders. Section 115-O pertains to declaration, distribution or payment of dividend by domestic company and imposition of additional tax on dividend is thus clearly covered by subject as embraced by Entry 82. The provisions of Section 115-O cannot be said to be directly included in the field of tax on agricultural income. Even if for the sake of argument it is considered that the provision trenches the field covered by Entry 46 of List II, the effect is only incidental and the legislation cannot be annulled on the ground of such incidental trenching in the field of the State legislature. Looking to the nature of the provision of Section 115-O and its consequences, the pith and substance of the legislation is clearly covered by Entry 82 of List I.

"25. We, thus, repel the argument of the learned counsel for the writ petitioners that provision of Section 115-O is beyond the legislative competence of the Parliament."

"34. The provisions of Section 115-O are well within the competence of Parliament. To put any limitation in the said provision as held by the Calcutta High Court that additional tax can be levied only on the 40% of the dividend income shall be altering the provision of Section 115-O for which there is no warrant. The Calcutta High Court having upheld the *vires* of Section 115-O no further order was necessary in that writ petition."

Paras S. Savla, Jitendra Singh, Nishit Gandhi
Advocates

DIRECT TAXES
High Court

1. Issuance of notice under section 148(1) of the Income-tax Act, 1961 – Second notice under section 148 was issued on the identical reasons that of first notice which has been quashed – Second notice invalid. A.Ys. 1997-98 & 1998-99

Gay Travels (P.) Ltd vs. DCIT [2017] 85 taxmann.com 131 (Madras)

Assessee had entered into an agreement for sale dated 4-7-1996 with M/s. Shorelines Pvt. Ltd. to sell their agricultural lands located in Muttukadu Village, for a total sale consideration of ₹ 3,50,00,000/- and received a sum of ₹ 1,60,00,000/- in assessment year 1997-98 and a sum of ₹ 1,90,00,000/- in assessment year 1998-99. The returns filed by the assessee were accepted by the department concluding that no capital gains are attracted on the sale transaction entered into by the assessee. While finalising the assessment for the year 1998-99, the assessment for A.Y. 1997-98 was reopened to consider the question of assessing the capital gains arising on the sale of agricultural lands, as the assessee had entered into the agreement for sale in AY 1997-98. The said consideration was not considered for taxability in the assessment year 1998-99. The A.O. issued notice under Section 148 of the Act dated 25-1-2001 for assessment year 1997-98, which was served on 1-2-2001 and the last date for passing the reassessment order was 31-3-2002. The assessee appeared on 19-3-2001 and produced books of account and the case was part-heard. On the next date i.e. 21-3-2001 the assessee filed further details and the case was taken as heard. The officer thereafter dropped the reopening proceeding on technical grounds stating that necessary approval will be obtained to issue Section 148 notice afresh and treated as technically dismissed. AO issued new notice u/s. 148 on 16-8-2002. The assessee sought for reasons for reopening and the same were furnished by the officer, which was priming on the ground that the lands sold were not agricultural lands. The assessee filed its replies *vide* letter dated 3-9-2002 and 9-9-2002 and submitted that in the light of the first notice issued and the proceedings have been failed to be pursued as contemplated under Section 153(2) of the Act, in the absence of any further materials at the hands of the A.O., the second notice issued is without jurisdiction. Since no further action was initiated on the representations filed by the assessee, the assessee approached the Hon'ble Madras High Court by way of writ petition. Hon'ble court was pleased to allow the writ petition and quashed the reassessment proceedings by observing that on a careful perusal of the original file including the note file, it is evidently clear that there is no factual difference for reopening the assessment as proposed in the first notice and as presently proposed in the impugned notices. The only difference being the language, as the officers are different. The same documents which formed the basis for reasons for reopening and issuance of notice dated 25-1-2001 is identical to that of the reasons, which are set out for the issuance of the impugned notice.

2. Special audit – Section 142(2A) – Additional ground can be raised before Appellate Tribunal challenging the reference made for special audit and consequently the assessment order passed is bad in law. A.Y. 2008-09

Consulting Engineering Services (India) Private Limited vs. ITAT & Anr. W.P. (C) 7734/2017 order dated 1-9-2017

The assessee during the course of hearing before the Appellate Tribunal raised an additional ground challenging the validity of assessment order passed being illegal and without jurisdiction as the reference and order under section 142(2A) of the Act is bad in law. The Appellate Tribunal passed an order dated 8-8-2017 rejecting the additional ground raised by the assessee relying on the decision of Hon'ble Apex Court in the case of *Sahara India (Firm) vs. CIT (2008) 169 Taxman 328 (SC),* wherein it has been held that it is impermissible to permit the ITAT to examine the validity of order passed under Section 142(2A) of the Act in order to hold that the assessment has been barred by limitation. On further appeal, the High Court allowed the writ petition filed by the assessee and quashed the order passed by the Appellate Tribunal, observing that the ITAT ought to have permitted the assessee to raise the aforementioned additional ground and ought to have decided the said additional ground on its merits in accordance with law. Hon'ble court while deciding the writ petition relied on the decision of Hon'ble Delhi High Court in the case of *PCIT vs. Nilkanth Concast (P.) Ltd. [2016] 387 ITR 568 (Delhi).*

3. Reopening u/s. 148 – Earlier writ withdrawn without seeking any liberty to file fresh writ petition – Second writ seeking same prayers on same facts not maintainable

Kamal Galani vs. ACIT, Writ Petition Nos. 1033, 1258 to 1261 of 2017, Bombay High Court, order dated 14-8-2017

In this case the Assessee had originally filed a Writ Petition challenging notice u/s. 148 and Order disposing the objections of the Assessee and also the notice seeking imposition of penalty u/s. 271(1)(b) for non-appearance. The said Petition was withdrawn without seeking any liberty to file a fresh petition after it was pointed out that there were certain incorrect statements in the Writ. The Petitioner again filed a fresh Writ Petition challenging the above referred notices and order after making certain amendments as compared to those in the Writ Petition originally filed and also deleting certain irrelevant / incorrect paragraphs which were present in the earlier Writ. The Hon'ble Bombay High Court relying on the Judgment of the Hon'ble Supreme Court in the case of *Sarguja Transport Service vs. State Transport Appellate Tribunal AIR 1987 SC 88* dismissed the second writ petition based on the same facts challenging the same notices. The Court, going through earlier petition and the order thereof, observed that the petitioner has also indulged in Bench hunting tactics, and hence applied Sarguja Transport's principle to the present facts and circumstances. The Court clearly noted the observations of this Court and which point towards an abuse of this Court's jurisdiction. The Court was persuaded to go on with the matter despite the objection raised by the respondents about the status of the petitioner. The petitioner despite noticing this position insisted on arguing the writ petition and argued it. After a preliminary hearing, on finding that it was not possible to get over the objection raised and the allegation of suppression of a material fact, the petitioner withdrew the writ petition, but without seeking any liberty to file a fresh petition on the same cause of action. The Court held that it would be acting contrary to judicial discipline, if it entertained second writ petition on the same cause of action but with a marginal improvement. The Court further observed that it is not a case where substantial justice demands that it overlooks the point of maintainability. It observed that this is a clear case where knowing the state of law and being aware of the legal position, a decision was taken to withdraw the writ petition without seeking any liberty, as above. In the circumstances, the bar, as enacted by the Hon'ble Supreme Court and which is founded on public policy, is clearly attracted.

4. Appellate Tribunals power to rectify mistakes – Section 254(2)

CIT vs. Income Tax Appellate Tribunal – [(2017) 85 taxmann.com 42 (Mumbai)]

The assessee applicants (Reliance Communications Limited, Reliance Communications Infrastructure Limited, one by Reliance BPO Limited and four by Reliance Telecom Limited) filed Miscellaneous Applications against an order passed by the Tribunal citing therein certain inadvertent mistakes apparent from record which need to be modified/rectified u/s. 254 (2) of the Act. The mistakes sought to be rectified were, (i) a particular "Agreement and General Terms and Conditions of Purchase" was not considered in arriving at the final conclusion; (ii) that the ratio of the Delhi High Court's decision in the case of *Director of Income Tax vs. Ericsson A.B. [2011] 16 taxmann.com 371/[2012] 343 ITR 470/204 Taxman 192* was not correctly read; (iii) that certain decisions of the Co-ordinate bench brought to the Notice of the Tribunal were ignored and a larger Bench was not constituted in case of a different view. On such an application being filed the Revenue raised an objection to the maintainability thereof. However, the Tribunal, in considering this and the other objections arrived at a conclusion that the initial order indeed suffered from mistakes apparent on the record and the ingredients of sub-section (2) of section 254 of the Income-tax Act, 1961 were satisfied. Proceeding thus, it allowed the Miscellaneous Applications by the impugned order and resultantly it restored all appeals which were decided by the earlier order in order to be re-heard and re-decided. The revenue challenged the said order by way of filing a writ petition under Article 226 of the Constitution of India challenging the order dated 18th November, 2016 restoring the appeals for a fresh hearing on the ground that Tribunal has no jurisdiction u/s. 254(2), by restoring the appeals for a fresh hearing, to revisit the merits of the case having once decided the appeals on merits. The Hon'ble High Court dismissed the said petition observing that the view taken by the Tribunal that its initial order contained some mistakes and which need to be rectified does not require interference in writ jurisdiction. If the objections of the Revenue are taken as they are, they are not going to the root of the case, namely, the maintainability of the proceedings, styled as Rectification Applications and the alleged limited jurisdiction of the Tribunal. At no stage it was the contention of the Revenue that the Tribunal has become functus officio after it delivered its order dated 6th September, 2013. If it had to re-look or re-visit that order it must be for a limited purpose and permitted by section 254(2) of the Income-tax Act, 1961. It could not have then touched the files and the cases or the original records so as to allow the assessee to take up all pleas on merits. The merits may have been decided erroneously, but the Tribunal has that jurisdiction and within its powers it may pass an erroneous order. The only remedy to question its order is to appeal to a higher court. This is not the nature of the objections raised before the Tribunal. Rather, a perusal of the submissions as summarised by the Tribunal in the impugned order from paragraph 5 onwards would reveal that the Revenue also entered into the merits of the case by justifying and supporting the findings and conclusions of the Tribunal in the initial order. Those are clearly on the merits of the controversy. In such circumstances when the parameters as they are and known to all, extremely limited, allegedly not adhered to is not the sole complaint. The complaint is that the Tribunal should not have re-visited and recalled its conclusions in the initial order also on merits. Thus, the view taken by the Tribunal is a mixed one. By perusing the order under challenge, we find that it could be termed as a plausible view of the proceedings. In the larger interest of justice the Tribunal felt that it must allow the assessee to contest the appeals of the Revenue which were decided by the initial order of 6th September, 2013, fully and properly on merits. A fair, just and complete opportunity ought to be granted and the assessee deserves the same. That is the conclusion of the Tribunal in the impugned order. Such a conclusion is not vitiated by any error of law apparent on the face of the record or perversity warranting our interference in writ jurisdiction.

5. Deduction u/s. 35(2AB) – Scientific expenditure – Revision u/s. 263

CIT vs. Sun Pharmaceutical Industries Ltd. Reported in (2017) 85 taxmann.com 80 (Gujarat)

The assessee was allowed a claim of deduction u/s. 35(2AB) of the Act in respect of in-house scientific research expenditure while framing the assessment order u/s. 143(3) of the Act. The said order was revised by the Commissioner u/s. 263 of the Act directing the AO to consider correct amount of disallowable expenditure after considering the financial documents and other relevant details/submissions filed by the assessee and as available on record with a view to ensure that there is no discrepancy in the facts and figures on record. According to the Commissioner since the prescribed authority had not sent the intimation in Form 3CL to the Revenue, the claim of the assessee could not have been accepted. The assessee challenged the said order u/s. 263 before the Tribunal. The Tribunal held that, the prescribed authority shall submit its report in relation to the approval of the in-house research and development in Form 3CL to the Director General of Income Tax (Exemption) within 60 days of its granting approval. However, the same was merely in form of intimation to be sent by the prescribed authority to the department. In case of the assessee, the research and development activity having already been approved in Form 3CM, the assessee thereafter, had no further role to play in the inter-departmental correspondence. The Tribunal therefore, held that the assessee was entitled to deduction on the capital and revenue expenses incurred on in-house research and development amounting to ₹ 237,77,05,310/-. The Department challenged the said order of the Tribunal. The Hon'ble High Court held that undisputedly, the research and development facility set up by the assessee was approved by the prescribed authority and necessary approval was granted in the prescribed format. The communication in Form 3CM was thereafter, between the prescribed authority and the department. If the same was not so, surely, the assessee cannot be made to suffer. To this extent, the Tribunal was perfectly correct and the Commissioner was not, in observing that in absence of such certification, claim of deduction under section 35(2AB) was not allowable. However, neither the prescribed authority nor the Assessing Officer has applied the mind as to the expenditure, be it revenue or capital in nature, actually incurred in developing the in-house research and development facility. To the limited extent, the Commissioner desired the Assessing Officer to verify such figures, the Court allowed the Assessing Officer to do so. In other words, in principle, the Court accepted Tribunal's reasons and conclusions. Merely because the prescribed authority failed to send intimation in Form 3CL, would not be reason enough to deprive the assessee's claim of deduction under section 35(2AB) of the Act.




Neelam Jadhav, Keerthiga Sharma &
Neha Paranjpe, *Advocates*

DIGEST OF CASE LAWS
Tribunal

Reported Decisions

Section 9 r.w. Article 12 – Payment received by non-resident outside India for services rendered outside India, and which did not make available any technical knowledge was not taxable in India as per Article 12 of the India-Netherlands DTAA

APM Terminals Management BV vs. DCIT (Intl. Tax) (ITA No. 3621/Mum/2015) (TS-386-ITAT-2017(Mum) (Assessment Year: 2007-08)

Facts

The non-resident assessee was engaged in the business of providing technical and support services to various companies, which were in the business of port and container terminal operations. It had entered into a contract with Shanghai Zhenhua Port Machinery Company Ltd., China ('ZPMC'), as per which all group entities of the assessee would purchase cranes from only ZPMC and in return, ZPMC would pay a consultancy fee to the assessee for every crane sold by it through its group company. Pursuant to this agreement, an Indian affiliate of Assessee purchased cranes from ZPMC and ZPMC paid a consultancy fee to the Assessee. The Assessing Officer ('AO') alleged that the amount received by the Assessee from ZPMC was taxable as fees for technical services as per the provisions of India-Netherlands Double Taxation Avoidance Agreement since the design of the crane was decided by the Assessee and the Indian affiliate did not have any say in it and that the income was from a source in India. The order of the AO was upheld by the Commissioner of Income-tax (Appeals) ['CIT(A)'].

Held

On appeal filed by the Assessee, the Income Tax Appellate Tribunal ('Tribunal'/'ITAT') held that the said consultancy fee was not received by the Assessee during the year, since the Revenue had itself held that the Indian affiliate was an assessee-in-default in the proceedings under section 201 of the Income-tax Act, 1961 ('Act') for AY 2008-09. Consequently, the non-resident Assessee could not be taxed in AY 2007-08, when it had received any income. Further, the Tribunal held that the consultancy fees received by the non-resident Assessee was not taxable since the services were rendered and utilised in manufacturing cranes outside India and could not deem to accrue or arise in India. Further, the consultancy fee did not make available any technical knowledge, experience, skill to Indian company and hence was not taxable as fees for technical services as per the provisions of Article 12 of the India-Netherlands DTAA.

Reopening – Section 147 r.w.s. 143(3) of the Act – Assessment proceeding initiated under section 142(1) of the Act – No

notice under section 148 of the Act can be issued before completion of assessment proceeding

Medapati Venkayamma vs. ITO [ITA 252/VIZG/2013], [2017] 85 taxmann.com 51 (Visakhapatnam) (Assessment Year: 2008-09)

Facts

The Assessee is an individual, had not filed return of income for the year under consideration. The AO issued a notice dated 29-1-2010 under section 142(1) of the Act. No return of income was filed in response to the said notice before due date mentioned in the notice. Thereafter, the AO issued a notice under section 148 of the Act. The Assessee filed a return of income in response to the said notice declaring income of Nil. The AO, further, issued the notice under section 143(2) and completed assessment under section 143(3) of the Act determining income at higher amount. On appeal, the CIT(A) confirmed the action of the AO. The Assessee being aggrieved by the appellate order preferred an appeal before the Appellate Tribunal.

Held

The Tribunal held that the AO had issued a notice under section 142(1) of the Act within time limit allowed for filing return of income under section 139 of the Act. Since the Assessee failed to respond to the notice under section 142(1) of the Act, the AO should have invoked the provisions of section 144 of the Act on or before 31-3-2011. Since the assessment was already initiated, during the pendency of assessment proceedings, there was no case for invoking the provisions of reassessment under section 148 of the Act. Once the AO Initiated assessment proceedings, he could not resort to reassessment unless the assessment proceedings were concluded. In the impugned case the assessment proceedings under sections 143(3)/144 of the Act should have been completed within period of limitation allowed to AO i.e. 31-3-2011. However, the AO passed the assessment order under section 143(3) of the Act on 29-12-2011. Thus, the assessment order passed under section 143(3) of the Act on 29-12-2011 was barred by limitation and the same was annulled. Further, the AO issued a notice under section 148 of the Act for reassessment, during the pendency of assessment proceedings which was bad in law and could not be sustained. Accordingly, the notice issued under section 148 was quashed.

Income from business and profession – Section 28(iv) of the Act – Assessee received a villa as gift from Dubai based company – No addition under section 28(iv) is warranted merely because Assessee attended annual day celebrations of the company

ACIT vs. Shahrukh Khan [ITA 8555/Mum/2011 & 80/ Mum/2012]), [2017]84 taxmann.com 209 (Mumbai) (Assessment Year: 2008-09

Facts

The Assessee was a film actor by profession. During the relevant year, the Assessee received a gift of signature villa from Dubai based company namely Nakheel PJSC. The said flat was gifted by Nakheel PJSC on account of natural love and affection of the friend of the Assessee, who is executive director of the said company. The AO observed that Nakheel PJSC was using Assessee's brand image for endorsing its project since 2004 on its official website and other electronic media. The AO, therefore, assessed the said gift as professional receipts under section 28(iv) of the Act. On appeal, the CIT(A) confirmed the action of the A.O. The Assessee being aggrieved by the appellate order preferred an appeal before the Appellate Tribunal.

Held

The Appellate Tribunal observed that the material relied by the revenue was news items concerning Assessee and few photographs at donors annual day in year 2007, which was placed on website of the company, to reach a conclusion that the Assessee undertook brand endorsement for the donor in exchange of gift. However, the photographs in the assessment order revealed that Assessee figures in event gallery. The same did not suggest stage performance by the Assessee in any manner. The Assessee merely addressed the employees of the company at the said gathering. The said conclusion was supported by the fact that the gift was offered to the Assessee in 2004, whereas the annual day took place in the year 2007. So far as the taxability of gift in kind was concerned, the gift of immovable property on or after 1-10-2009 was brought to tax by the Finance Act, 2009 *vide* amendment to section 56(2)(vii)(b) of the Act. Since the case pertained to A.Y. 2008-09, the said amendment did not apply to the case of the Assessee. In view of the above facts, the Tribunal held that the villa was received in gift by the Assessee and not out of exercise of profession and therefore, the same was not taxable in Assessee's hands.

Unreported Decisions

Section 9 r.w.s. 40(a)(i) – Payment made for use of licence software was not royalty and hence no tax had to be deducted

DCIT vs. Societe Generale [ITA Nos. 4542 & 1671/Mum/2015] dated 11th September, 2017 (Assessment Years: 2009-10 & 2010-11)

Facts

The Assessee, having a permanent establishment in India, purchased AML licence software from a Switzerland entity. The AO alleged that the payment was in the nature of royalty and since tax was not deducted at the time of making the payment to the overseas party, the expense was disallowed under section 40(a)(i) of the Act. The CIT(A) deleted the disallowance, and the Revenue preferred an appeal before the Tribunal.

The Assessee had also reimbursed to its Head Office and Singapore Branch the cost of data communication charges, Annual Miscrosoft Enterprise Software product billing and true up charges incurred etc. for the India Branch. The AO alleged that the payments were to be taxed royalty or fees for technical services as per the provisions of sections 9(1)(vi)(c) and 9(1)(vii)(c) and Article 13 of the India-France DTAA. The CIT(A) had deleted the addition since it was a mere reimbursement and appeal was preferred against the same.

Held

Following the decision of the Delhi High Court in the case of *DIT vs. Infrasoft Ltd. (2014) 220 Taxman 273 (Delhi)*, and the Mumbai Tribunal in the case of *DDIT vs. Solidworks Corporation (2013) 152 TTJ 0570 (Mum)* and *ACIT vs. Sonata Information Technology Ltd. (2013) 152 TTJ 590 (Mum)*, it was held that the payment made to the Switzerland entity was a right to use the copyrighted material and not a right to use the copyright itself and hence, the payment was not royalty.

With regard to the reimbursement of costs to the Head Office and other branches, the Tribunal held that the payment was a mere reimbursement, and hence was not taxable in India. Reliance was placed on *M/s. Societe Generale vs. DCIT (IT), Mumbai (ITA No. 1854/Mum/2015), dated 19-4-2017.*

On another ground of appeal, following the order of the Tribunal for the earlier years, the Tribunal in the impugned year also upheld the contention of the Assessee that guarantee commission earned by it was accounted for in its books of account over the period of guarantee and offered to tax accordingly.

Capital Gains – Section 45 of the Act – An agreement to sell was entered into and cancelled subsequently without acting upon – The capital gains from subsequent transfer cannot be treated as Short Term Capital Gain in view of the earlier agreement

Naresh Kukreja vs. ITO [ITA 4044/Mum/2014] dated 13th September, 2017 (Assessment Year: 2009-10)

Facts

The Assessee, an individual, entered into an Agreement to sell dated 19-7-2004 for selling one half of the Shop No. 6A, situated at Khan Market, New Delhi for total consideration of ₹ 5 lakhs. The said agreement was cancelled *vide* agreement dated 3-12-2008 as the title of the property was not clear. The Assessee also returned all the cheques received by the vendee without encashing them. Further, the Assessee entered into an agreement dated 28-12-2008 to sell the Shop No. 6A for total consideration of ₹ 75 lakhs. The Assessee filed the return of income for the impugned assessment year claiming Long Term Capital loss of ₹ 16,37,400 taking cost of acquisition as on 1-4-1981. The AO referring to a clause in the agreement dated 28-12-2008 observed that one half of the property sold by the Assessee to Mrs. Meenu Chawla and Meenakshi Chawla on 19-7-2004 and the same was repurchased on 3-12-2008. Thus, the said property was held by the Assessee for less than 36 months. The AO, therefore, treated the capital gains of one half of the property as short term capital gains. Accordingly he adopted the sale consideration of the same at ₹ 37.50 lakhs out of total consideration of ₹ 75 lakhs. The AO after considering the cost of acquisition of ₹ 5.32 lakhs assessed short term capital gain of ₹ 32.18 lakhs. On appeal, the CIT(A) confirmed the action of the AO. The assessee being aggrieved by the order of the CIT(A) preferred an appeal before the Tribunal.

Held

The Tribunal held that the issue here was whether the transaction was completed or not in view of the agreement dated 19-7-2014 entered with Mrs. Minu Chawla and Mrs. Meenakshi Chawla for sale of half share in the shop for ₹ 5 lakhs and subsequent agreement dated 3-12-2008 cancelling the agreement dated 19-7-2004. The said property was inherited by the Assessee from his mother through probate. Prior to this, probate proceedings were going on in district court. Thus, the Assessee decided to sell the one half of the property to meet the cost of litigation due to financial problems. Accordingly, the Assessee entered into agreement dated 19-7-2004 to sell one half property by receiving ₹ 40,000 in cash and 4,50,000 through cheques. The said agreement was subsequently cancelled *vide* agreement dated 3-12-2008. The Assessee returned back all the cheques to the purchaser without encashing them. The parties to this agreement agreed that the Assessee will have right, title and interest in the property forever. The Assessee's claim was forfeited by the fact that the same cheques were returned and no new cheques were given to the purchaser. Thus, the Tribunal held that for all intent and purposes, the agreement to sell dated 19-7-2004 was called subsequently on 3-12-2008 and the parties never acted upon it and sale was never completed. Accordingly, the capital gains on subsequent transfer effected by the Assessee *vide* agreement dated 3-12-2008 for sum of ₹ 75 lakhs was to be treated as Long-Term Capital Gain.

Business Income – Section 28 of the Act – Loan amounts deposited in bank and earned interest – Loan was inextricably linked with the commissioning of the power project – Interest earned from the same is business income. [r.w.s. 56(1) and 57(iii)]

Urjankur Shree Tatasaheb Kore Warana Power Company Limited vs. ITO [ITA No. 1817/Mum/2017] dated 23rd August, 2017

Facts

Assessee is engaged in the business of manufacturing of electricity from bagasse coal and other fuels. During the Assessment, the AO found that Bank of Baroda had credited interest on term deposits to the Assessee, which was not offered the same for taxation. Therefore, AO had reduced the same from its capital work-in-progress and further held that interest income on fixed deposits from banks fall under the head Income from other sources as per the provisions of s. 56(1) of the Act. The CIT(A) held that the Assessee had not commenced its business during the year under consideration, it had borrowed funds for purpose of setting up its business and while it was in process of implementation of 44 MW Bagasse based power project, the unutilised surplus funds were kept in fixed deposits on which interest income was earned. The Assessee had simply parked its unutilised idle surplus funds in fixed deposits and earned interest thereon. He confirmed the addition as interest income.

Held

The ITAT observed that the loan taken by the Assessee for development, construction and operation of a 44MW power generation project from a consortium of banks. As per the loan agreement Trust and Retention Account ('TRA') had to be opened by the Assessee with a scheduled bank designated and acceptable to the TRA agent. The receivables and other revenues of the project had to be credited or debited in the TRA account and Bank of Baroda was designated as TRA bank. The Assessee deposited the loan amounts received from the consortium with Bank of Baroda, and it earned interest income on the money parked with the bank. The issue was whether the activity which was taken up for setting up of the business and the funds which were garnered were inextricably connected to the setting up of the business or not. The ITAT held that the loan was inextricably linked with the commissioning of the power project, as evidenced from the agreement. Consequently, it was held that the income earned by the Assessee could not be taxed under the head Income from other sources and that it had to be set off against the WIP.

Business Income – Section 28 – Penalty amount received from Members, Transfer to "Investors Protection Funds" – Does not constitute business income of the Assessee

DCIT vs. M/s. National Commodity & Derivatives Exchange Ltd. [ITA No. 1423/Mum/2011] dated 9th August, 2017 (Assessment Year: 2007-08)

Facts

During the year, the Assessee had collected penalty amount from its members as per the direction given by the "Forward Market Commission" ('FMC'). As per the guidelines issued by FMC, penalty collected was required to be transferred to a separate fund "Investors Protection Fund" after deducting 10% towards administrative expenditure. The Assessee credited the said amount in the profit and loss account under the head "Other income". However, it transferred it to Investors Protection Fund account and shown the same as its liability in the balance-sheet. AO took the view that the said penalty constitutes income and accordingly he added the same to the total income of the Assessee.

Held

The ITAT held that, the penalty amount cannot be considered as income of the Assessee as it had been diverted to the Investor's Protection Fund by overriding title, as per the guidelines issued by the Forward Market Commission. However, the Assessee had kept in a separate account in the books of account and was shown as liability. The ITAT held that the said collection of penalty by the Assessee could be business income of the Assessee.

Condonation of Delay – S. 253(5) – Delay was due to seeking opinion for further appeal – No sufficient cause – Rejected application for condonation

M/s. Sara Research and Development Centre Pvt. Ltd. vs. DCIT [ITA No.3529/Mum/2015] dated 13th September, 2017

Facts

The Assessee filed an application before Tribunal for condoning the delay which is accompanied by an affidavit of the Director of the company. The Director stated that the company was in the process of seeking an informed opinion to prefer an appeal before the Tribunal that there was delay in filing the appeal and that the delay was not *mala fide* or intentional.

Held

The company was a corporate entity and it was helped by professionals. It was represented before lower authority by a Chartered Accountant. The appeal filed before the lower authority was within the prescribed time limit and it clearly showed that the Assessee was well aware of the time limit of filing the appeal. The Tribunal held that Assessee had not given any sufficient reasons or cause for the delay in filing the appeal within the stipulated time and accordingly it rejected application for condonation of delay.

CA Tarunkumar Singhal & Sunil Moti Lala, *Advocate*

INTERNATIONAL TAXATION
Case Law Update

A. HIGH COURT

1. The Court confirmed Tribunal's Order holding that the commission payments made to Indian agent of non-resident in India was taxable in India and non-deduction of tax on such payment would lead to disallowance of expenditure u/s. 40(a)(i)

Smt. Fathima Harris [TS-390-HC-2017 (Mad.)]

Facts

i) The assessee engaged in the export of garments, made payment of commission on exports to an agent of Hong Kong company situated in India and claimed deduction of the expenditure without deducting TDS contending that as the services were rendered outside India by the non-resident, the same was not taxable in India.

ii) The AO disallowed the expenditure u/s. 40(a)(i) on the ground that the assessee ought to have deducted tax on the commission payment since the payment was made in India.

iii) The CIT(A) observing that the assessee's export sales had been effected through the Indian concern and the commission payment was made in India, confirmed the disallowance made by the AO u/s. 40(a)(i).

iv) The Tribunal upheld the order of the AO.

v) Aggrieved, the assessee appealed before the High Court.

Judgment

i) The Court observing that the commission payment was actually received in India, confirmed the disallowance u/s. 40(a)(i) and held that the commission payments received by the Indian agent of non-resident in India were taxable in India.

ii) It rejected assessee's reliance on CBDT Circular No. 786 dated 7-2-2000 (which provided that no tax was deductible u/s. 195 on export commission and other related charges payable to a non resident for services rendered outside India) by holding that the same was applicable only for foreign agents of Indian exporters while in the present case commission was received in India by an agent of the foreign entity.

2. The Court confirmed Tribunal's order deleting penalty u/s. 271(1)(c) in absence of deliberate concealment attempt in the case of an international transaction

GAP International Sourcing India Ltd. [TS-677-HC-2017(Del.)-TP]

Facts

i) The assessee, incorporated in India as a wholly owned subsidiary of GAP International Sourcing Inc, USA, operated as a procurement support service company whereby it facilitated sourcing of apparel merchandise from India for its AE. The assessee was remunerated at total operating costs plus a 15% mark-up thereon. The goods were sourced by the AE directly from the third party vendors in India and were not routed through the financial accounts of the assessee. The assessee, a low-risk service provider benchmarked its transactions with AEs by adopting TNMM as the most appropriate method.

ii) The TPO accepted TNMM as the most appropriate method, however, recharacterised the assessee as a 'significant risk bearing' entity having intangibles as opposed to a low risk service provider. Accordingly, it determined ALP of assessee's transactions by determining commission at 5.22% (arithmetic mean of the comparables) on the value of goods procured by the foreign AE directly from third party vendors from India and made TP adjustment.

iii) The addition made by the AO was confirmed by the DRP.

iv) In the quantum proceedings, the Tribunal noting that it was entitled to a cost plus mark-up on total operating cost of GAP International Sourcing India Ltd. (and not the value of goods sourced by GAP US), rejected the assessee's recharacterisation as a significant risk bearing service provider and accepted the assessee's classification i.e. low risk service provider. However, the Tribunal did not accept assessee's mark-up of 15% and instead relying on the Delhi Tribunal's decision in the case of *Li & Fung's [TS-583-ITAT-2011(Del.)-TP]* substituted the mark-up of 32% (i.e., the maximum operating margin adopted in Li & Fung decision). The assessee conceded by accepting the mark-up of 32% consequent to the decision of the Tribunal whereby the final adjustment was restricted to only ₹ 6.92 crore as against addition of ₹ 255.97 crore made by the AO.

v) Thereafter, the AO levied penalty under Explanation 7 of Section 271(1)(c), contending that since the assessee had accepted the mark-up of 32% as against 15%, the computation of price charged was not done in good faith and with due diligence.

vi) The CIT(A) confirmed the order of the AO.

vii) During the appeal arising out of the penalty proceedings, the Tribunal followed the decision of the Co-ordinate Bench in the assessee's own case for the earlier AY wherein similar penalty had been deleted on the ground that penalty could not be imposed merely because the addition was accepted by assessee. The Tribunal held that the assessee had made a choice to accept 2% of the addition (i.e., ₹ 6.92 crore vis-a-viz adjustment of ₹ 255.97 crore made by the TPO) made by AO and exercise of such choice in order to achieve peace of mind in the absence of *mala fide* intention, could not attract penalty u/s. 271(1)(c) for concealment or filing of inaccurate particulars. It further observed that the TPO accepted TNMM as the most appropriate method and accepted PLI and comparables selected by the assessee. Further, the Tribunal in the quantum proceedings accepted assessee's claim that it was a limited risk bearing support service provider. Accordingly, it held that the TP study carried out by the assessee was in good faith and with due diligence adhering to the requirements of Section 92C.

viii) Aggrieved, Revenue preferred appeal before the jurisdictional HC.

Judgment

i) The Court upheld the Tribunal Order deleting concealment penalty levied u/s. 271(1)(c) with respect to TP adjustment confirmed in quantum proceedings holding that penalty cannot be imposed merely because the addition was accepted by the assessee. It observed that the Court in the earlier year involving the same issue, had dismissed the Revenue's appeal against the Tribunal's order deleting the penalty u/s. 271(1)(c).

ii) Accordingly, it dismissed the appeal in absence of substantial question of law.

3. The Court upheld the Tribunal's Order excluding comparables which were functionally different from the assessee (ITeS service provider)

New River Software Services Pvt. Ltd. [TS-672-HC-2017(Del.)-TP]

Facts

i) The assessee was engaged in the business of processing information and data through electronic and information technology enabled infrastructure. The assessee benchmarked its transactions under TNMM and selecting 17 comparables with an average margin of 8.45% as against its own operating margin of 10.33% contended that its transaction were at ALP.

ii) The TPO rejected the comparables of the assessee and adopted 5 new comparables which inter alia included:

a. Coral Hub Ltd.

b. Infosys BPO Ltd.

c. Wipro Ltd.

The TPO also rejected the assessee's working capital adjustment since the assessee had not demonstrated that there was difference in the levels of working capital employed *vis-a-vis* the comparables.

iii) The DRP upheld the TPO's order.

iv) The Tribunal excluded these 3 comparables observing that:

a. Coral Hub Ltd.: This company was functionally different since its business model was based on outsourcing of service

b. Infosys BPO Ltd.: This company was functionally different due to huge turnover, extraordinary events taking place, existence of brand.

c. Wipro Ltd. This company was functionally different due to huge turnover, extraordinary events taking place.

With respect to working capital adjustment, the Tribunal remanded the matter to the TPO directing him to allow working capital adjustment while determining the profit margins of comparables.

v) Aggrieved, the Revenue appealed before the High Court.

Judgment

i) Since there was delay in filing appeal, the Court refused to condone the delay since there was no satisfactory explanation offered by the Revenue.

ii) However, on merits, it observed that

a. Coral Hub Ltd.: the Co-ordinate Bench in the case of *Rampgreen Solutions (P) Ltd. [TS-387-HC-2015(Del.)-TP]* had excluded Coral Hub Ltd. observing that a business model where services were rendered by employing one's own employees and using one's own infrastructure would have a different cost structure as compared to a business model where services were outsourced.

b. Infosys Ltd.: Exclusion of the comparable was upheld by the Court in case of *Pentair Water India (P) Ltd. [TS-566-HC-2015(Bom)-TP]* and *Agnity India Technologies Pvt. Ltd. [TS-189-HC-2013(Del.)-TP].*

c. Wipro Ltd.: 'Wipro BPO' was more or less on the same footing as Infosys BPO as far as the size and scale were concerned and thus rightly excluded.

iii) Accordingly, it upheld the order of the Tribunal.

4. The Court held that even in the case of remand proceedings, the AO ought to have passed the draft assessment order u/s. 144C before passing final assessment order

JCB India Ltd [TS-706-HC-2017(Del.)-TP]

Facts

i) The Petitioner was engaged in the business of manufacture of earth-moving/construction equipments.

ii) The AO had passed final assessment order u/s. 143(3) r.w. Section 144C which the Tribunal had set aside to the file of the AO for fresh adjudication with the direction that both the assessee as well as the revenue were at liberty to file fresh T. P. Study and fresh comparables so as to arrive at the Arm's Length Price in accordance with law. Thereafter, the AO asked the TPO to quantify the TP adjustment in pursuance to the remand made by the Tribunal for fresh adjudication. The AO then incorporating the TPO's order passed the final assessment order without passing the draft assessment order.

iii) Aggrieved, the petitioner filed Writ Petition before the High Court contending that after the remand proceedings, the AO could not have passed the final assessment order without issuing a draft assessment order.

Judgment

i) Relying on the decision of Co-ordinate Bench in the case of *Turner International India Pvt. Ltd. [TS-400-HC-2017(Del)-TP]*, wherein it was held that it was mandatory for the AO to pass the draft assessment order u/s. 144C prior to issuing final assessment order, the Court held that even where the Tribunal had remanded the matter, the AO ought to have passed the draft assessment order u/s. 144C.

ii) It further held that Section 292B of the Act could not save an order passed in contradiction to the provisions of the Act since it was an incurable illegality.

iii) Accordingly, it held that the final assessment order passed by the AO was without any jurisdiction on account of the failure by the AO to first pass a draft assessment order before passing the final assessment order. Accordingly, it quashed the order of the AO as well as the order of the TPO passed pursuant to the remand by the Tribunal.

5. The Court quashed Tribunal's Order remanding the AMP issue to the TPO and directed the Tribunal to decide itself whether in the first place there existed international transaction involving the assessee and its AE

Haier Appliances (India) P. Ltd. [TS-684-HC-2017(Del.)-TP]

Facts

i) The assessee, manufacturer of consumer products had entered into an agreement with its AE viz., Haier Electrical Appliances Corp. Ltd., China, whereby the assessee had used and promoted the trademark and brand name owned by Haier China and had incurred advertisement, marketing and promotional (AMP) expenditure.

ii) The TPO noting that AMP/sales ratio of the assessee was 16.04% as compared to 3.87% of the comparables, held that the advertisement expenses over and above the normal AMP expenses incurred by the comparables was towards brand building and accordingly, he made TP adjustment.

iii) The DRP confirmed the action of TPO.

iv) Relying on the decision of Delhi High Court in the case of *Sony Ericsson Mobile Communications vs. CIT (2015) 374 ITR 118 (Del.)*, the Tribunal remanded the matter to the AO/TPO with the direction to examine all the functions carried out by comparables as per the guidelines laid down by the High Court.

v) Aggrieved, the assessee appealed before the High Court contending that at the time the Tribunal passed the order, it did not have the benefit of order subsequently passed by Delhi High Court in the case of *Sony Ericsson Mobile Communications vs. CIT (order dated 28th January 2016 in ITA 638 of 2015)* and *Daikin Airconditioning India Pvt Ltd. (order dated 27th July 2016 in ITA 269/2016)* wherein it was held that prior to commencing TP exercise, the existence of an international transaction involving the assessee and its AE had to be first established and the Court had accordingly remanded the matter to the Tribunal.

Judgment

i) The Court observed that since the Tribunal had not examined whether there existed international transaction involving the assessee and its AE in the first place the matter was to be restored to the file of the Tribunal in the light of its subsequent decision in Sony Ericsson (supra).

B) Tribunal Decisions

6. Taxation of an Indian Working Overseas – Overseas taxes and Medicare would not constitute taxable salary in India – Held in favour of the assessee

Sunil Shinde vs. ACIT [TS-377-ITAT-2017(Bang.)]
Assessment Year: 2011-12

Facts of the case

i) The taxpayer was an employee of Fidelity Business Services India Pvt. Ltd. who was transferred to Fidelity Investments Systems Inc, USA from 7th October, 2010 to 21st June, 2012. The taxpayer derived income from salary during the Financial Year (FY) 2010-11.

ii) The taxpayer was an ordinary resident (ROR) in India during the said FY. Further, in the United States (U.S.) he was a non-resident during the year 2010 and a resident in 2011.

iii) The taxpayer had offered the actual salary income received in U.S. as taxable in his India tax return and claimed Foreign Tax Credit (FTC)2 in respect of the Federal Tax withheld from his overseas salary.

iv) The Assessing Officer (AO) in his order added the Federal Tax claimed as FTC to the income of the taxpayer.

v) The Commissioner of Income-tax (Appeals) [CIT(A)] upheld the order passed by the Assessing Officer (AO) and enhanced the amount of Federal Tax so added to income. Furthermore, the CIT(A) added Medicare paid in the U.S. and State Tax withheld in the U.S. to be part of the total income of the taxpayer, considering the same as benefit in his hands

vi) Aggrieved by the order passed by the CIT(A), the taxpayer had filed an appeal with the Tribunal.

vii) The assessee contended as under:

A) The taxpayer argued that the Federal Tax and State Tax do not constitute taxable income based on the following judicial precedents for the following reasons:

- *CIT vs. Yawar Rashid [1996] 218 ITR 699 (MP)*
- *CIT vs. Y.N.S. Hobbs [1979] 116 ITR 20 (Ker.)*
- *CIT vs. Shaw Wallace and Co. Ltd. [1983] 143 ITR 207 (Cal.)*
- *CIT vs. Blundell Spence & Co. Ltd [1952] 21 ITR 28 (Bom.)*
- *CIT vs. Oriental Co. Ltd. [1982] 137 ITR 777 (Cal.)*
- *CIT vs. Ambalal Kilachand [1994] 210 ITR 844 (Bom.)*

(a) Tax Deducted at Source (TDS) is a diversion of income by overriding title. As the tax deducted would be paid to the Government, only the net income received by the taxpayer should be subject to tax in India

(b) Taking a cue from Section 198 of the Act, TDS under the provisions of the Act is only deemed to be income received. However, Section 198 does not refer to TDS outside India

(c) Section 5(1)(c) of the Act does not provide for taxation of amounts deemed to accrue/ arise/ be received outside India. Unlike other parts of the said section, deeming fiction does not form basis of taxation in respect of income earned/ received outside India.

(d) Given the above, the taxpayer contended that the Federal Tax and State Tax are to be considered as income deemed to be received outside India or deemed to accrue/ arise outside India and are therefore not taxable in his hands in India.

B) In respect of Medicare, the taxpayer claimed that the same is not a taxable perquisite in his hands. The taxpayer has placed reliance on various judicial precedents : *CIT vs. Lala Sridhar [1972] 84 ITR 192 (Del), Yoshio Kubo vs. CIT [2013] 36 taxmann.com 1 (Del), CIT vs. L. W. Russel [1964] 53 ITR 91 (SC)* where in case the benefit accruing is purely contingent in nature or the employee does not get a vested right at the time of contribution, then the amount so contributed should not be considered as taxable perquisite.

C) The taxpayer contended that if State Tax paid in the U.S. is considered as income in India, he should be allowed to claim FTC of such State Tax in India.

Decision

The Tribunal held as follows:

i) It has been observed that as per Section 5(1)(c) of the Act, the Federal Tax and State Tax withheld in the U.S. would not constitute income that accrues or arises outside India as the same is not actually received by the taxpayer.

ii) Accordingly, the Tribunal has accepted the claim of the taxpayer by relying on *CIT vs. Yawar Rashid [1996] 218 ITR 699 (MP)* referred by the taxpayer, drawing reference to Section 5(1)(c) of the Act, which enables taxability of actual income that is received by the taxpayer outside India.

iii) Therefore, Federal Tax and State Tax were not considered taxable in the hands of the taxpayer and the net income after giving effect to deduction of taxes was considered taxable in India.

iv) The claim of FTC was remanded to the AO to determine the quantum of FTC as per Article 25 of the DTAA. The FTC claim shall, however, be restricted to the tax payable on the total income before giving effect to FTC.

v) With respect to Medicare paid outside India by the employer, the Tribunal agreed with the taxpayer's contention having regard to the case of *CIT vs. Lala Sridhar [1972] 84 ITR 192 (Del.)* referred by him. Accordingly, the same was not considered as a taxable perquisite.

7. Delay in deduction of tax from payment for professional charges and corporate management charges – Whether disallowed u/s. 40(a)(i) applying Non Discrimination Article – Held : No. Whether Payment for Server Maintenance Charges and Testing & Development Charges to the

Parent Company in Germany taxable as "Fees for Technical Services: Held: No – Whether payment for Testing and Development Charges paid to Italian Company taxable as "Fees for Technical Services:– Held: No – In favour of the assessee

Cooper Standard Automotive India Pvt. Ltd. vs. ACIT [TS-311-ITAT-2017(CHNY)] Assessment Year: 2003-04

Facts of the case

i) **Payment for professional charges and corporate management charges**

During the AY 2003-04, the taxpayer has made payment for professional charges and corporate management charges after deducting TDS under Section 195 of the Act. However, payment for TDS was remitted to the Government of India beyond the due date specified under Section 200(1) of the Act. The Assessing Officer (AO) made the disallowance under 40(a)(i) of the Act. The Commissioner of Income-tax (Appeals) [CIT(A)] confirmed the disallowance made by the AO.

ii) **Payment for server maintenance charges and testing and development charges**

- The taxpayer had made the payment for server maintenance charges for the usage access of the server belonging to the parent company based at Germany. All the activities of the parent company as well as subsidiary companies based around the world are routed through the server. According to the taxpayer, the server maintenance charges are in the nature of reimbursement charges paid to parent company using software related issues, and hence TDS is not applicable.
- The AO made addition holding that services rendered outside India is taxable, even though there is no Permanent Establishment (PE) in India. By virtue of an amendment to the Explanation of Section 9(2) of the Act, the FTS payable outside India would be deemed to accrue or arise in India and hence TDS is deductible.
- Similarly, the taxpayer also paid testing and development charges to Hutchinson Italy for the services rendered in the vendor location in Italy. However, no tax was deducted on such payment under Section 195 of the Act. Therefore, the AO made the addition under Section 40(a)(i) of the Act. Subsequently, the CIT(A) confirmed the addition made by the AO.
- The auto components of power steering system consisting of three hoses 'suction line, pressure line, and return line' are tested for various parts. The taxpayer manufactures the said parts according to drawing and specifications and designs of the company and subsequently sent to vendor location in Italy for testing on their efficiency and strength.
- The taxpayer contended that the testing was largely done on machines with very little of human judgment or skill. The only skill required was knowledge to operate the machine and to take readings. The only task of non-resident was to give a report on the performance of component by giving actual values based on readings and design specifications.

Decision:
The Tribunal held as under:

A) Payment for professional charges and corporate management charges – Amendment made by the Finance Act, 2003 in Section 40(a)(i) of the Act

- The provisions of Section 40(a)(i) of the Act as stood prior to amendment by the Finance Act, 2003 prescribe the disallowance for non-deduction or non-payment. The Proviso to the said Section provides that where the tax has been deducted but paid in any subsequent year, the same will be allowed as deduction in the year in which tax has been paid or deducted. The Circular No. 7, dated 5 July 2003 referred by the taxpayer also states the same. Therefore, for allowing the deduction of the expenditure, not only deduction of tax at source but also remittance to the government account is a mandatory requirement. The Proviso to Section 40(a)(i) of the Act makes it very clear that expenditure is allowed in the year in which the tax has been remitted to the government account. Thus, the taxpayer is entitled to claiming the expenditure in the year in which it was paid.

- In the taxpayer's case, though the tax was deducted but remitted to the government account in the subsequent year. Therefore, the AO has rightly applied the disallowance under Section 40(a)(i) of the Act.

B) Payment for professional charges and corporate management charges – Applicability of non- discrimination clause

In the case of *Millennium Infocom Technologies Ltd. vs. ACIT [2009] 117 ITD 114 (Del)*, the Delhi Tribunal has held that similar payments in the case of residents do not attract the disallowance in the event of non-deduction of tax at source. Thus, taxing the amount under Section 40(a)(i) for non- deduction of tax at source on similar amounts tantamount to discrimination. Therefore, the tax treaty and the decision relied on by the taxpayer for non-discrimination clause squarely applicable in the taxpayer's case. Accordingly, it has been held that the disallowance under Section 40(a)(i) of the Act would not be applicable in the case of the taxpayer.

C) Server maintenance charges

- The server maintenance charges are paid for usage of the intranet, the internet, mail data backup, etc., located at Germany. The server is administered by the parent company, and the activities support the periodical data backup, software upgradation, and renewal, inter-office communication like messenger and communicator, etc.

- On perusal of various decisions: *Siemens Ltd. vs. CIT [2013] 142 ITD 1 (Mum), CIT vs. Bharti Cellular Ltd. [2009] 319 ITR 139(Del.)*, the FTS involve human element and consideration is for rendering the managerial, technical and consultancy services. Therefore, applying the rule of *noscitur a sociis* the word 'technical' as appearing in Explanation 2 to Section 9(1)(vii) of the Act would also have to be construed as involving a human element.

- However, the facility provided by the parent company in the case of server maintenance charges was the usage of various activities, and no human interface is involved. The only actual costs are recovered by the parent company from group constituents, and there was no profit element.

- From the facts of the present case, it is observed that the taxpayer is merely using the technology provided by the parent company and no managerial, consultancy and technical services are provided by the parent company. Therefore, it has been held that the payment made is not for FTS and the decisions relied upon by the taxpayer are squarely applicable in the taxpayer's case. Therefore, it has been held that the payment was for reimbursement of expenses and hence no tax is deductible under Section 195 of the Act as held by the Tribunal in the case of *Cairn Energy Pvt. Ltd. vs. ACIT [2010] 2 ITR 38 (Chennai).*

D) Testing and development charges

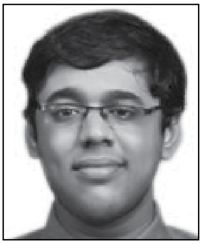
- The activity of testing, operating of the machine and noting of actual reading, whether it suits to the design specifications or not is a specialised activity only a technical person can do but not the machines alone. The machine cannot discharge such functions, and human expert knowledge only can decide whether the parts are acceptable or not. The mere machine operator cannot decide whether the auto parts are as per the specifications and drawings or not. Therefore, the payment is made for technical services.

- The taxpayer contended that the services are rendered outside India and to tax the income under Section 9(1)(vii) of the Act the services should have been rendered in India and utilised in India. The Explanation to Section 9(2) of the Act was introduced in 2007 with effect from 1976 and the AY under consideration is 2003-04, the taxpayer cannot predict the amendment and deduct the TDS which is an impossible task.

- The payment was made for FTS, and it is taxable under the Act and the tax treaty. However, the services are rendered outside India and utilised in India. As per the decision of Supreme Court in the case of *Ishikawajima-Harima Heavy Industries Ltd vs. DIT [2007] 288 ITR 408 (SC),* it is clarified that despite the deeming fiction in Section 9, for any such income to be taxable in India, there must be sufficient territorial nexus between such income and the territory of India. It further held that for establishing such territorial nexus, the services have to be rendered in India as well as utilised in India.

- The Explanation to Section 9(2) of the Act was introduced by the Finance Act, 2007 with effect from 1976 and as on the date of assessment there was no provision to tax the FTS rendered outside India and hence it has been held that no tax is deductible under Section 195 and consequent disallowance is not called for. This view is supported by the Mumbai Tribunal in the case of *Channel Guide India Ltd. vs. ACIT [2012] 25 taxmann.com 25 (Mum).*

- Therefore, it has been held that the payment made by the taxpayer for FTS for the services rendered outside India are not taxable under Section 9(1)(vii) of the Act and the disallowance was to be deleted.



Ishaan V. Patkar, *Advocate*

GST on charitable institutions and non-profit sector

General taxability

GST is a tax on supply of goods and services. A supply can take place anywhere and everywhere in all kinds of contexts. Commercial transactions will of course contain supplies. However, even non-commercial transactions will contain supplies if the general meaning of "supply" is looked at. A charitable organisation "supplies" food to orphan children if rules of ordinary language are followed.

That being so, GST is a tax which is statutorily confined to a transactions which take place in course or furtherance of "business". At first glance, no reasonable person will conclude that charitable activities constitute "business", for there is a commercial ring to the way the term "business" is understood. A business is understood generally as an organised and repetitive activity undertaken with a view to earn profit.

But the CGST Act defines "business" in Section 2(17) in such manner as to make profit-motive completely irrelevant. Furthermore, a single transaction may also constitute "business". This modified definition thus strikes a body blow to any claims by the non-profit sector to remain outside GST.

An activity or transaction which is ancillary or in connection with or incidental to the main business activity is also "business" under Section 2(17)(b). However, profit motive has not been ousted in this sub-clause (b). Similarly, if the main activity is not "business", then the ancillary or incidental activity will automatically fall outside the definition of "business". Thus, where the main activity of the trust is to spread the message of Sai Baba, it was held that the same is not "business" and hence the ancillary activity of selling books and literature was also not "business" *[Commissioner vs. Sai Publication Fund]*

Exemptions

Now even though supplies by Charitable organisations are taxable generally, there are some exemptions which need to be noticed:

"Services by way of charitable activities" are exempt from tax under Entry 1 of the Notification No. 12/2017 – Central Tax (Rate). However, this exemption is available only to such entities which are registered under Section 12AA of the Income-tax Act. The policy is clearly to disallow any other entity from coverage of this exemption. This condition to restrict the exemption to a certain class of charitable entities is thus a substantive condition which bodes complete compliance. It is not a procedural condition or a technicality. The term "charitable activities" itself has been extensively defined. This is also a substantive condition.

But exemptions are not pigeon-holes. A charitable entity may avail of exemption under other entries if it falls within that entry even though it cannot avail of the exemption under Entry No. 1 of the Notification No. 12/2017 – Central Tax (Rate). Thus, a Dharmashala whose declared tariff of a unit of accommodation is below ₹ 1,000 per day may very well avail of the exemption to residential and lodging services under Entry 14 of the Notification.

Similarly, entities not registered under Section 12AA of the Income-tax Act, 1961 or not coming within the "charitable activities" definition may avail exemptions under the following entries of Notification No. 12/2017 – Central Tax (Rate) if the other conditions of those respective entries are fulfilled:

(1) Services provided by or to educational institutions under Entry 66;

(2) A veterinary clinic providing health care services in respect of animals or birds under Entry 46;

(3) Library services are exempted under Entry 50 of that Notification;

(4) Admission to museum, national park, wildlife sanctuary, tiger reserve or zoo is covered by Entry 78;

(5) Services by way of public conveniences such as provision of facilities of bathroom, washrooms, lavatories, urinal or toilets under Entry 76;

(6) Services provided by clinical establishments, ambulance services and bio-medical waste treatment for such clinical establishments which are covered by Entries 74 and 75;

(7) Cord blood bank services under Entry 73;

(8) Vocational and other training services under Entries 71 and 72;

(9) Empanelled bodies undertaking skill development services under Entry 70;

(10) Rice handling, storage and other services under Entry 24 and fruit and vegetables related services specified under Entry 57.

Entries 13, 77 and 80 also deal with charitable activities which have been discussed in subsequent parts of this article.

Now what are "charitable activities"? The definition is contained in Para 2(r) of the Notification:

"(r) "charitable activities" means activities relating to –

(i) public health by way of,-

  (A) care or counseling of

    (I) terminally ill persons or persons with severe physical or mental disability;

    (II) persons afflicted with HIV or AIDS;

    (III) persons addicted to a dependence-forming substance such as narcotics drugs or alcohol; or

  (B) public awareness of preventive health, family planning or prevention of HIV infection;

(ii) advancement of religion, spirituality or yoga;

(iii) advancement of educational programmes or skill development relating to,-

  (A) abandoned, orphaned or homeless children;

  (B) physically or mentally abused and traumatised persons;

  (C) prisoners; or

  (D) persons over the age of 65 years residing in a rural area;

(iv) preservation of environment including watershed, forests and wildlife"

The ordinary meaning of "charitable activities" is contained in the four-fold classification by Lord Macnaghten in *Special Commissioners vs. Macnaghten [(1891) AC 531]* which is a judgment under the UK Income Tax law:

(i) Relief of poverty,

(ii) Advancement of education,

(iii) Advancement of religion,

(iv) Other activities beneficial to the community.

This classification has inspired a similar definition in the Indian Income Tax law. See *Lok Shikshana Trust vs. CIT [(1975) 101 ITR 234 (SC)].*

Of these four categories, Entry 1 of the Notification deals with category (iii), that is "advancement of religion" and even extends it to "yoga". Entry 13 deals with conducting religious ceremonies etc.

The first category enunciated by Lord Macnaghten, that is, "relief of poverty" is not covered expressly, though some activities like skill development etc. may benefit the poor. "Advancement of education" is dealt with in a rag-tag manner. Entry 1 covers a very limited area of educational activities. Entry 66 is wider and is not limited to non-profit institutions.

Animal welfare, care and counselling etc. come within category 4 or what is known in the Indian Income Tax law as "any other object of general public utility". However, the definition of "charitable activities" in Clause 2(r) of the Notification is not open-ended. It is a restrictive clause in which all objects of general public utility are not covered. If an activity is not specifically mentioned in the definition, it cannot be exempted under Entry 1.

Next, there is Entry 13 of the Notification. As aforesaid, Entry 13 deals with conducting religious ceremonies. It also covers renting services provided by a religious place.

The following conditions are applicable for exemption to renting services:

(1) Premises should belong to a religious place meant for general public;

(2) Premises should be owned or managed by:

a. Entity registered as charitable or religious trust under Section 12AA of the Income-tax Act, 1961;

b. Trust or institution registered under Section 10(23C)(v) of the Income-tax Act, 1961; or

c. Body or authority covered under Section 10(23BBA) of the Incom-tax Act, 1961.

(3) But exemption is not available to:

a. Renting of rooms where charges are ₹ 1,000 or more per day;

b. Renting of premises, community halls, kalyan mandapam or open area and the like where charges are ₹ 10,000 or more per day;

c. Renting of shops or other spaces for business or commerce where charges are ₹ 10,000 or more per month

The conditions as to registration under Section 12AA of Income-tax Act, 1961 applies solely to renting services and not to conducting of religious ceremonies. Thus, any non-individual person engaging in conducting of religious ceremonies will also be exempted under Entry 13.

Entry No. 77 is an extremely shabbily drafted. This entry deals with non-profit clubs and associations where members contribute towards the expenses of an unincorporated body or a non-profit entity registered under any law for the time being in force:

(i) Services provided by a trade union to members are completely exempt,

(ii) Where reimbursement or contribution relates to services which are otherwise exempt from GST, then the reimbursement or contribution is also exempt,

(iii) Reimbursement or contribution up to ₹ 5,000 per member is exempt if it relates to sourcing of goods or services from a third person for the common use of members in a housing society or residential complex.

Thus, clubs and associations cannot avail of the exemption under Entry No. 77 unless the reimbursements or contributions relate to services which are otherwise exempt from GST.

Under Entry 80 of the Notification, an entity providing services in relation of training or coaching or recreational activities are exempt if:

(i) Services of training or coaching in recreational activities,

(ii) Such services must relate to arts and culture or sports,

(iii) Such services must by provided by an entity registered under Section 12AA of the Income-tax Act, 1961.

It is true that all these exemptions relate to supply of "Services". However, most supplies of goods should be covered by these services if the rules for composite and mixed supply are kept in mind.

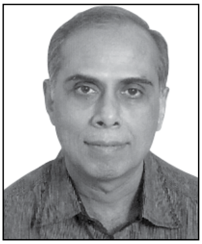
Registration

If the "aggregate turnover" of the charitable organisation as defined in Section 2(6) is above ₹ 20 lakhs, the organisation will need to get registered and undertake the uncharitable processes of return filing etc. However, it is pertinent to note that donations received by a charitable organisation will not come with the "aggregate turnover" definition. That definition only covers aggregate value of "taxable supplies" and a donation entails no supply.

Where the activities of a charitable organisation are completely exempt from GST, there is no liability for registration under Section 23 of the CGST Act. However, if the aggregate turnover of a charitable organisation is above ₹ 20 lakhs and even if all its activities are exempt, the organisation will have to register if any notified reverse charge supply is received by such an organisation [See Section 24(iii) of the CGST Act]. Most charitable organisations receive legal services at some point or other. Legal services provided to a "business entity" whose turnover is above ₹ 20 lakhs is taxable on reverse charge basis. "Business entity" is defined in the Notification No. 12/2017 – Central Tax (Rate) as any person carrying out "business". Thus the liability for reverse charge will arise in the hands of charitable organisations and this is something all such organisations must look out for even though their activities are otherwise exempted.

But does the liability to registration over-ride the exemption granted to a charitable organisation? The answer is in the negative. An organisation may be liable to register due to reverse charge supplies, but there is no tax liability if the activities of that organisation are exempted. It must file NIL returns. This is a sorry state of affairs and may need to be looked into by the Government at the earliest.

> Forgive and forget, but never forget to forgive. You may find a happier heart is the key to a happier life.
>
> — *Mahatma Gandhi*



CA Rajkamal Shah & CA Bharat Vasani

INDIRECT TAXES
GST – Legal Update

NOTIFICATIONS

CGST Act

28/2017 – Central Tax, dt. 1-9-2017 (Late fees for filing of GSTR 3B for the month of July waived)
Late filing fees waived for all registered persons who failed to furnish the return in Form GSTR 3B for the month of July 2017 by the due date.

29/2017 – Central Tax, dt. 5-9-2017 (Due dates for furnishing of details/returns for the month of July and August extended)
Due dates for GSTR 1, GSTR 2, GSTR 3for July were extended up to 10th, 25th and 30th September respectively and that for August up to 5th, 10th and 15th October respectively. However, again the dates are further extended as per Notification No. 30 given below.

30/2017 – Central Tax, dt. 11-9-2017 (Time limit for filing of GSTR 1, GSTR 2 and GSTR 3 further extended)

Return	Class of taxable / registered persons	Time period for furnishing of details / return
GSTR 1	Having turnover of more than ₹ 100 crores	Up to 3-10-2017
	Having turnover of up to ₹ 100 crores	Up to 10-10-2017
GSTR 2	All	Up to 31-10-2017
GSTR 3	All	Up to 10-11-2017

Due dates of return filing for the month of August will be notified later.

31/2017– Central Tax, dt. 11-9-2017 (Time limit for filing of GSTR 6 extended)
Time limit for filing of return by an Input Service Distributor for the month of July is extended up to 13-10-2017. Due date for the month of August will be notified later.

32/2017 – Central Tax, dt. 15-9-2017 (Exemption granted to casual taxable person making taxable supplies of handicraft goods from the requirement of registration)
Casual taxable person making taxable supplies of handicraft goods are exempted from obtaining registration provided aggregate value of such supplies, on all India basis, does not exceed ₹ 20 lakhs (₹ 10 lakhs in case of Special Category States, other than Jammu & Kashmir).

Such person shall obtain PAN and generate an e-Way Bill in accordance with provisions of Rule 138 of CGST Rules, 2017.

List of items and corresponding HSN codes covered under "handicraft goods" are given in the said notification.

Similar Notification is issued under IGST (Notification No. 08/2017-Integrated Tax, dt. 14-9-2017)

33/2017-Central Tax, dt. 15-9-2017 (Provisions of TDS under CGST Act, 2017 notified)

Appoints 18th Sept 2017 as the date when provisions of Sec 51(1) comes into force with respect to persons specified under clause (a) and (b) of Sec 51(1) and also specifies following persons under clause (d) of the said section, who will be liable to deduct TDS:

(a) an authority or a board or any other body set up by an Act of Parliament or a State Legislature or established by any Government with fifty one per cent or more participation by way of equity or control, to carry out any function;

(b) society established by the Central Government or the State Government or a Local Authority under the Societies Registration Act, 1860;

(c) public sector undertakings

Date with effect from which the provisions will be applicable will be notified subsequently.

34/2017 – Central Tax, dt. 15-9-2017 (Seventh amendment to GST Rules, 2017)

Option to opt for composition scheme w.e.f. 1st October to be exercised on or before 30-9-2017.

35/2017 – Central Tax, dt. 15-9-2017 (Filing of GSTR 3B extended up to December)

GSTR 3B return to be continued to be filed up to December 2017. Due date will be 20th of next month.

36/2017 – Central Tax, dt. 29-9-2017 (Eighth Amendment to CGST Rules)

Date of application for cancellation of registration for persons registered under the existing laws extended from 30th September to 31st October u/r. 24(4).

The time limit for filing of Form TRAN-1 under Rules 118, 119 and 120 of "ninety days from the appointed day" is substituted as "the period specified in Rule 117 or such further period as extended by the Commissioner".

In Rule 120A, the marginal heading "Revision of declaration in FORM GST TRAN-1" shall be inserted.

CGST Act (Rate)

24/2017 – Central Tax (Rate), dt. 21-9-2017 (GST rate reduced on specified supplies of Works Contract Services)

CGST Rate for Works Contract services provided to the Central Government, State Government, Union Territory, a local authority or a governmental authority for specified contracts of construction, repair etc. of non-commerce use civil structure, educational or medical etc. reduced to 6% (i.e. 12% total GST).

25/2017 – Central Tax (Rate), dt. 21-9-2017 (Right to admission to the events organized under FIFA U-17 World Cup 2017 exempted)

26/2017 – Central Tax (Rate), dt. 21-9-2017 (Certain supplies to NPCIL exempted)

Intra-state supply of heavy water and nuclear fuels to Nuclear Power Corporation of India Ltd exempted from the whole of GST.

27/2017 – Central Tax (Rate), dt. 22-9-2017 (Certain GST rates amended)

In Schedule I [CGST 2.5%], meaning of "branded goods" for specified entries enlarged to "bearing a brand name on which an actionable claim or enforceable right in a court of law is available". Also Entry No. 29A Walnuts; 33A Tamrind; 100A Roasted Gram; 198A Grass; 201A Duty Credit Script; 219A Corduroy fabric; 219B Saree Fall; 257A Cotton quilts of value less than ₹ 1,000; 259A worked corals and 263A Rosaries and Hawan Samagri are added and a few other entries amended.

In Schedule II [CGST 6%], the items added in other schedules are correspondingly omitted from Schedule II. Batters including Idli and

Dosa batter. Entry No. 85A Rubber Bands; 92A Idols of wood, stone and metals; 99A Wooden Tableware and Kitchenware; 171A Textile Caps; 176 Stone inlay work; 176A Statues, figures of animals, paper weights etc., other ornamental goods essentially of stone; 177A Pots etc. for conveyance/packing of ceramic; 177B & 177C Household articles etc; 177D Statues and other ornamental articles;189A Non-electric bells, statues, photograph, frame etc. of base metal; 195A Nozzles for drip irrigation equipment or sprinklers; 224A Cotton quilts of sale value exceeding ₹ 1,000; 231A Animal carving material and articles thereof, articles of coral are added.

In Schedule III [CGST 9%], the items added in other schedules are correspondingly omitted from Schedule III. Entry No. 111 Medical disposable gloves, plastic raincoats; 123A rice rubber rolls; 157 Kites etc.; 384 Computers monitors not exceeding 20 inches; 449A kitchen gas lighters are added or amended.

In Schedule IV [CGST 14%], the items added in other schedules are correspondingly omitted from Schedule III. Entry No. 154 Computer monitors exceeding 20 inches

CGST on unsorted diamonds reduced from 1.5% to 0.125%.

28/2017 – Central Tax (Rate), dt. 22-9-2017 (Certain GST exemptions amended)

Meaning of "branded goods" for specified entries enlarged as given in Notification No. 27/2017. Entry No. 102A Cotton seed oil cake; 130A Khadi Fabrics; 135A Clay Idols; 138 Charkha for hand spinning of yarns are added/amended. Exemption under Entry No. 143 Indigenous handmade musical instruments is amended and Annexure II specifying list of such instruments is notified.

29/2017 – Central Tax (Rate), dt. 22-9-2017 (Amendment to Notification No. 5 dt 28-6-2017 regarding restriction of refund on corduroy fabrics)

Entry No. 6A inserted to include corduroy fabrics. No refund of excess ITC, where accumulation of such ITC is on account higher rate of tax on inputs than that on outputs.

IGST Act

07/2017 – Integrated Tax, dt. 14-9-2017 (Job workers making inter-state supply of services to registered person exempted from the requirement of obtaining registration)

The exemption is however not applicable where the aggregate turnover exceeds the threshold limit. Also, it is not applicable to job work of jewellery, goldsmiths' and silversmiths' wares and other articles.

Compensation Cess (Rate)

05/2017 – Compensation Cess (Rate), dt. 11-9-2017 (Rate of Compensation Cess on various motor vehicles)

Rate of Compensation cess on specified types of motor vehicles is amended as listed in the notification.

CGST – Orders

Order-02/2017 – GST, dt. 18-9-2017

Time limit for submitting revised declaration in Form TRAN 1 u/r. 120A of CGST Rules, 2017 extended up to 31-10-2017.

Order-03/2017 – GST, dt. 21-9-2017

Time limit for submitting declaration in Form TRAN 1 u/r. 117 of CGST Rules, 2017 extended up to 31-10-2017.

Order-04/2017 – GST, dt. 29-9-2017

Time limit for intimation of details of stock held on the date preceding the date from which the option for composition levy is exercised in FORM GST CMP-03 extended upto 31st October.

CGST – Circulars

07/2017, dt. 1-9-2017

Detailed procedure laid down for reconciliation of information furnished in Form GSTR 3 and Form GSTR 3B.

PRESS RELEASE

On Blockage of Working Capital of Exporters dt. 22-9-2017

The press release has detailed the issues relating to blockage of exporters refund due to extension in due date of filing GSTR 3 for the month of July and August. It is hereby clarified that CBEC is trying to find a way of giving refund by linking Form GSTR 1 with Form GSTR 3B and, therefore, for the month of July, where Form GSTR 1 is already filed, the authorities would be in a position to process the refund applications. Therefore, the exporters, who have not yet filed Form GSTR 1 for July 2017, may be advised to file it immediately and not to wait till the deadline.

It has also requested the authorities of State Governments as well as Central Government to clear the pending refund claims of Central Excise and VAT for the pre-GST period, so that the exporters will get immediate relief.

Payment of service tax in transitional period dt. 28-9-2017

It has been clarified that in cases where service was received before 1-7-2017 and payment for the value of the service was also made before 1-7-2017, but the service tax under RCM was paid by 5th /6th July 2017, details of such credit should be indicated by filing a revised return under service tax. Such revised return can be filed within 45 days from 31-8-2017 i.e., up to 15-10-2017. The assessee may also file details in Original or Revised Form GST TRAN-1.

Facility of furnishing Letter of Undertaking extended to more exporters dt. 29-9-2017

To facilitate exports under GST, the facility of furnishing Letter of Undertaking, in place of a bond, for exporting goods or services or both shall be allowed to exporters and no bank guarantee will be required. The relevant notification for this shall be issued in due course.

Janak C. Pandya, *Company Secretary*

CORPORATE LAWS
Company Law Update

Case Law # 1

[2017] 204 Comp Cas 169 (Delhi)

[In the Delhi High Court]

Mondelez Foods P. Ltd vs. Regional Director (North) Ministry of Corporate Affairs and Others.

The registered proprietor of a trade mark also includes a person authorised by the registered proprietor of such trade mark to use its trade mark in its corporate name. Thus, even though such person is not an owner of trade mark, still it can apply to the Regional Director for seeking direction for change of name of another company, having similar name on the ground of its undesirability.

Brief Facts

Mondelez Foods P. Ltd ("Petitioner") has filed the petition under Article 226 of the Constitution of India. The petition has been filed against order of the Regional Director, Respondent No. 1 ("RD") for rejecting the Petitioner's application for giving directions to Respondent No. 2 for change of its corporate name.

The summary of facts and contentions are as follows.

1. Petitioner's name is part of trade mark of Mondelez International Inc., ("Mondelez") the worlds largest snacks company.
2. Petitioner is a subsidiary of Mondelez.
3. Mondelez has filed applications for registration of the marks "Mondelez International" and Mondelez International (logo) across the globe including in India.
4. Respondent No. 2, ("R2") which was incorporated with another name, has applied to the Registrar of Companies ("RoC") for availability of name "Mondelez India P. Ltd" and also applied with the Trade Mark Registry for trade mark and logo on the same name.
5. RoC has approved the name based on necessary resolution passed by the Respondent No. 2 and issued a fresh Certificate of Incorporation to that effect.
6. The Petitioner has sent a legal notice to R2 for rectifying the name.
7. The Petitioner also filed a rectification petition with the RD seeking direction from the Central Government as per power conferred under section 22(1)(ii)(b) of the Companies Act.
8. The Petitioner as well as the owner of the international trade mark, also filed a civil suit against the R2 and others for restraining them from using trade mark or corporate name.

9. The said suit was decreed in favour of the Petitioner and trade mark owner.

10. The Petitioner has elaborated on the provisions of section 20 and 21 as to use of similar name and the Central Government powers as to ratification of such name.

11. RD has declined to issue any such directions for the reason that (a) the Petitioner is not the owner of the trade mark and (b) period of 12 months from the change of name by R2 has elapsed.

The further submission made by the Petitioner is as follows.

1. RD's rejection of application on two reasons as stated above is not sustainable.

2. Even though, Petitioner is not an owner of trade mark, it is duly authorised to use the name "Mondelez.". Further, as per section 22(1) of the Act, "registered proprietor of a trade mark" also include a person authorised by the registered proprietor of such trade mark.

3. The Petitioner has made a representation within 12 months and therefore it could not be prejudiced by any delay on the part of RD.

4. Proviso to section 22(1) of the Companies Act, 1956 also allows the registered proprietor of a trade mark to make an application after five years of becoming aware of registration of the company with an undesirable name.

Judgment

The Hon. High Court has accepted the petition and directed the RD to issue necessary direction to R2 to change its name to any other name, which is not identical to or resembles the Petitioner or any other existing company.

The following analysis and observations are made by the Hon. High Court.

1. The analysis of section 20 and section 22(1) undisputably provides that the change of name by R2 is "undesirable".

2. On limited question as to whether RD has a delegated power to direct for change of name after a period of twelve months, as provided in section 22(1)(ii)(b) it has observed that section 22 of the Companies Act, 1956 was amended by virtue of the Trade Marks Act, 1999. As per said amendment, a proviso was inserted in section 22(1)(ii)(b) allowing the proprietor of a registered trade mark to make an application within five years of becoming aware of existence of such undesirable name of a company. Thus, this indicates, that RD can act even after a period of twelve months from the registration of a company with undesirable name.

3. Section 16 of the Companies Act, 2013, the Central Government is empowered to issue direction to a company to change its name.

4. The name of the R2 too nearly resembles the name of the Petitioner, therefore RD is empowered to direct R2 to change its name.

Live as if you were to die tomorrow. Learn as if you were to live forever.

— *Mahatma Gandhi*

CS Kaushik Jhaveri

CORPORATE LAWS – RECENT DEVELOPMENTS

Fast Track Merger

Merger/amalgamation is a restructuring tool which helps companies in expansion and diversification of their business and to achieve their underlying objectives. In commercial parlance, merger essentially means an arrangement whereby one or more existing companies merge their identity into another to form a new and different entity which may or may not be one of those existing entities.

The Companies Act, 2013, has introduced, **Fast Track Merger (FTM)** and provisions of Section 233 dealing with FTM was notified on 15th December, 2016 and it is applicable for the merger/amalgamation to be entered between small companies, between a holding company and its wholly owned subsidiary and such other classes as and when introduced. This introduction is Government's initiative towards "Ease of doing Business" scheme.

In the erstwhile Act, merger between small companies and for merger between wholly owned subsidiary companies and Holding Company was filed with jurisdictional High Court(s) and approval would generally take 6-8 months. Launch of FTM ensures speedy the completion of the merger.

The brief overview is as under:

1) **SECTION AND RULE COVERED:** Section 233 of the Companies Act, 2013 read with Rule 25 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

2) **APPLICABILITY**

   a. Two or more ***Small Companies***** or

   b. Between a ***holding Company and its wholly-owned subsidiary Company*** or

   c. Such ***other class or classes of Companies*** as may be prescribed

** Small Company : As per Section 2(85) of the Companies Act, 2013 – "Small Company" **other than a public company, —**

(i) **paid-up share capital** of which **does not exceed fifty lakh rupees** or such higher amount as may be prescribed which **shall not be more than five crore rupees; AND**

(ii) **turnover** of which as per its **last profit and loss account does not exceed two crore** rupees or such higher amount as may be prescribed **which shall not be more than twenty crore rupees:**

Provided that nothing in this clause shall apply to —

(a) a holding company or a subsidiary company;

(b) a company registered under section 8; or

(c) a company or body corporate governed by any special Act.

BRIEF PROCEDURE

Steps	Activity	Time Period	Forms	By Whom
1	Convene a BM to approve the scheme and get the necessary approvals from Board	As an when company plans for such merger/ amalgamation, meeting can be held by giving notice of 7 days or shorter notice	–	Both (Transferor and Transferee Companies)
2	File Form MGT-14	Within 30 days of passing Board resolution	MGT-14	Transferor and Transferee Companies that are public company
3	Send Notice ***(in Form CAA.9)*** inviting objections or suggestions for the Scheme from : a) Registrar of Companies [within whose jurisdiction the Registered office is situated] b) Official Liquidator [within whose jurisdiction the Registered office is situated] c) Person Affected [This may include Office of Income Tax, Creditors, Other Statutory Authorities, as applicable] *** Objections/ suggestions to be received within 30 days of Notice	After holding the Board Meeting	Form GNL 1 with office of ROC [Including physical copies] For other authorities physical copy of the Scheme	Both (Transferor and Transferee Companies)
4	File Declaration of solvency **(in Form CAA.10)** with ROC	It should be filed before convening the meeting of members and creditors	Form GNL 2	Both (Transferor and Transferee Companies)

<table>
<tr><th>Steps</th><th>Activity</th><th>Time Period</th><th>Forms</th><th>By Whom</th></tr>
<tr><td>5</td><td>Convene General Meeting of Members and creditors :
The notice convening such meeting shall be accompanied by :
a) a statement, disclosing the details of the compromise or arrangement.
b) Declaration of solvency made in Form No. CAA.10;
c) copy of the scheme.
d) copy of the objections and suggestions received by Company, if any.
The scheme shall be approved by members holding 90% of total numbers of shares and creditors representing 90% of the creditors value.</td><td>On receipt of No objection / suggestions, clear 21 days notice shall be served to convene the meeting of members and creditors</td><td>–</td><td>Both (Transferor and Transferee Companies)</td></tr>
<tr><td>6</td><td>Filing of the Scheme:
a) File a copy of Scheme and report on the result of each of the meetings with the Regional Director.
b) A copy of the scheme along with Form CAA. 11 shall
also be filed with :
(i) the ROC in Form GNL 1;
(ii) the Official Liquidator through hand delivery or by registered post or speed post.</td><td>Within 7 days from the conclusion of the meeting of members or creditors</td><td>Form GNL-1
Form CAA – 11</td><td>Transferee Company</td></tr>
<tr><td>7</td><td colspan="4">Approval of the Scheme by the Regional Director</td></tr>
<tr><td></td><td colspan="4">a. On receipt of the scheme, if the ROC or the Official Liquidator has no objections or suggestions to the scheme, the Regional Director shall register the same and issue a confirmation thereof to the companies.
b. If the ROC or Official Liquidator has any objections or suggestions, they may communicate the same in writing to Regional Director within a period of 30 days. If no such communication is made, it shall be presumed that he has no objection to the scheme.</td></tr>
</table>

Steps	Activity	Time Period	Forms	By Whom
	c. If the Regional Director after receiving the objections or suggestions or for any reason is of the opinion that such a scheme is not in public interest or in the interest of the creditors, it may file an application before the Tribunal in **Form No. CAA.13 within a period of 60 days** of the receipt of the scheme stating its objections and requesting that the Tribunal may consider the scheme under section 232. d. On receipt of an application from the Regional Director, if the Tribunal, for reasons to be recorded in writing, is of the opinion that the scheme should be considered as per the procedure laid down in section 232, the Tribunal may direct accordingly or it may confirm the scheme by passing such order as it deems fit. e. Where no objection or suggestion is received to the scheme from the ROC and Official Liquidator or where the objection or suggestion of ROC and Official Liquidator is deemed to be not sustainable and the Regional Director is of the opinion that the scheme is in the public interest or in the interest of creditors, the Regional Director shall issue a confirmation order of such scheme of merger or amalgamation in Form No. CAA. 12.			
8	Filing of confirmation order with the ROC	Within 30 days of the receipt of the order of confirmation of the scheme.	Form INC-28	Both (Transferor and Transferee Companies)

Companies falling within the purview of fast track merger may at their discretion, opt to undertake such schemes under sections 230 to 232 of the Act.

4) **EFFECT OF REGISTRATION OF SCHEME:** The registration of the scheme shall have the following effects:

I) **Dissolution of Transferor Companies:** Upon registration of the scheme, Transferor Company or Companies shall be deemed to have the effect of dissolution without process of winding-up.

Transfer of property or liabilities: Transfer of property or liabilities of the transferor company to the transferee company so that the property becomes the property of the transferee company and the liabilities become the liabilities of the transferee company.

Charge: Charges, if any, on the property of the transferor company shall be applicable and enforceable as if the charges were on the property of the transferee company.

Legal Proceeding: Legal proceedings by or against the transferor company pending before any court of law shall be continued by or against the transferee company.

Additional Liability: Where the scheme provides for purchase of shares held by the dissenting shareholders or settlement of debt due to dissenting creditors, such amount, to the extent it is unpaid, shall become the liability of the transferee company.

II) **Tra**nsferee company compl**iances**

a) **Restrictions on holding shares in its own name by Transferee Companies**

A transferee company shall not, on merger or amalgamation, hold any shares in its own name or in the name of any trust either on its behalf or on behalf of any of its subsidiary or associate company and all such shares shall be cancelled or extinguished post merger or amalgamation.

b) **Authorised Capital**

The transferee company shall file an application with the Registrar along with the scheme registered, indicating the revised authorized capital.

c) **Registration Fee**

The fee, if any, paid by the transferor company on its authorised capital prior to its merger or amalgamation with the transferee company shall be set-off against the fees payable by the transferee company on its enhanced authorised capital due to merger or amalgamation balance if any shall be paid.

d) **Other Compliances :** Following other compliances included in the scheme which needs to be carried out :

a) Alteration of Capital Clause

b) Allotment of Shares

c) Change of Name

d) Change of Object

e) Any other process to be done to make scheme effective

Conclusion

The simplification of process will encourage corporate entities to undertake merger/amalgamation activities and help them to achieve their underlying objectives. Time taken to complete the merger/amalgamation through NCLT process and the cost involved in it is saved substantially under Fast track route. Fast track merger will help small companies in strengthening their position in the outside market. Such companies will become more competitive and exhibit a better bargaining power in the market.

> The difference between what we do and what we are capable of doing would suffice to solve most of the world's problem.
>
> — *Mahatma Gandhi*



CA Mayur Nayak, CA Natwar Thakrar &
CA Pankaj Bhuta

OTHER LAWS
FEMA Update and Analysis

In this article, we have discussed FEMA provisions under Master Direction No. 8 – Other Remittances dated January 8, 2016 updated up to February 11, 2016

1. Introduction

As a part of its obligation under the WTO Agreement, India agreed to relax exchange control regulations on Current Account transactions. In line with this commitment, Section 5 of the Foreign Exchange Management Act, 1999 (FEMA) authorises any person to sell or draw foreign exchange to or from an Authorised Person if such sale or drawal is a Current Account transaction. However, section also authorises the Central Government, in public interest and in consultation with the Reserve Bank of India (RBI), to impose restrictions on Current Account transactions.

In exercise of powers under Section 5, the Government of India *vide* Notification No. G.S.R. 381(E) dated May 3, 2000 notified "Foreign Exchange Management (Current Account Transactions) Rules, 2000". These rules have been amended from time-to-time through amendment notifications to incorporate changes in the regulatory framework.

Within the contours of these Rules / Regulations, RBI issues directions to Authorised Persons under Section 11 of the FEMA to lay down modalities as to how foreign exchange business has to be conducted by the Authorised Persons with their customers/constituents.

Instructions / directions issued by RBI on remittance facilities for residents have been compiled in Master Direction No. 8 – Other Remittances. Whenever necessary, RBI may issue further directions to Authorised Persons through A.P. (DIR Series) Circulars. RBI has announced that it shall also amend Master Direction suitably and simultaneously with issuance of instructions/directions.

Remittance facilities covered in Master Direction No. 8 are as under:

A. Release of Foreign Exchange by Authorised Dealers

The Foreign Exchange Management (Current Account Transactions) Rules, 2000 dated 3rd May, 2000 as amended from time-to-time classifies Current Account transactions as under:

1. Prohibited transactions

(a) Transactions specified in **Schedule I**, or

(b) Travel to Nepal and/or Bhutan, or

(c) Transactions with a person resident in Nepal or Bhutan.

Release/Drawal of foreign exchange is not permitted for travel to and transactions with these countries.

2. Transactions which require prior approval of the Government of India

Transactions specified in Schedule II (except where the exchange is drawn from RFC/EEFC Accounts)

3. Transactions which require prior approval of RBI

(a) Transactions specified in Schedule III of the said Notification lists transactions which require prior approval of the RBI.

(b) In some cases prior permission is required only if the transaction value exceeds the limits specified therein (except where the exchange is drawn from RFC/RFC(D) Accounts)

It is important to note that all other Current account transactions *not mentioned in any of the above Schedules are freely permissible.*

As per the definitions provided in the notification, "Drawal" of foreign exchange also includes payments through use of International Credit Cards (ICC), International Debit Cards (IDC), ATM cards, etc.

Also, "Currency", has been defined to *inter alia* includes International Credit Cards, International Debit Cards and ATM Cards. Accordingly, all Rules, Regulations made and Direction issued under the Act apply to the use of ICC, IDC and ATM Cards as well.

B. Prohibition

Remittances in any form towards participation in lottery schemes or lottery like schemes existing under different names like money circulation scheme or remittances for the purpose of securing prize money/awards, etc. are prohibited.

C. Fraudulent offers

There is a spate of fictitious offers of cheap funds in recent times from fraudsters through letters, e-mails, mobile phones, SMS, etc. Communications on fake letterheads of the RBI and purportedly signed by its top executives / senior officials are also being sent to targeted people. The victims of the fraud have also been persuaded to deposit the amount in accounts with banks in India, and such amounts have been withdrawn immediately. Multiple accounts are being opened in the name of individuals or proprietary concerns, at different bank branches for collecting the transaction charges, etc. For this purpose, RBI has advised AD Cat - I banks to exercise due caution and to be extra vigilant while opening or allowing transactions in such accounts. Any person resident in India collecting and effecting / remitting such payments directly / indirectly outside India would make himself/ herself liable to be proceeded against with, for contravention of FEMA besides being liable for violation of regulations relating to Know Your Customer (KYC) norms / Anti Money Laundering (AML) standards.

D. Release of Foreign Exchange by Authorised Dealer Category II

RBI has granted licences to certain entities by authorising them as Authorised Dealer – Category II to undertake following non-trade current account transactions:

a) Private visits,

b) Remittance by tour operators / travel agents to overseas agents / principals / hotels,

c) Business travel,

d) Fee for participation in global conferences and specialised training,

e) Remittance for participation in international events / competitions (towards training, sponsorship and prize money),

f) Film shooting,

g) Medical treatment abroad,

h) Disbursement of crew wages,

i) Overseas education,

j) Remittance under educational tie up arrangements with universities abroad,

k) Remittance towards fees for examinations held in India and abroad and additional score sheets for GRE, TOEFL, etc.

l) Employment and processing, assessment fees for overseas job applications,

m) Emigration and emigration consultancy fees,

n) Skills / credential assessment fees for intending migrants,

o) Visa fees,

p) Processing fees for registration of documents as required by the Portuguese / other Governments,

q) Registration / subscription / membership fees to International Organisations.

E. Remittance facilities for resident individuals

a) A resident individual can remit up to USD 250,000 per financial year for any permitted current or capital account transaction or a combination of both for –

   i. Private visits to any country (except Nepal and Bhutan).

   ii. Gift or donation.

   iii. Going abroad for employment.

   iv. Emigration.

   v. Maintenance of close relatives abroad.

   vi. Travel for business, or attending a conference or specialised training or for meeting expenses for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/ check-up.

   vii. Expenses in connection with medical treatment abroad.

   viii. Studies abroad.

   ix. Any other current account transaction

b) For item nos. (iv) emigration, (vii) expenses in connection with medical treatment abroad and (viii) studies abroad covered under Para 1 of Schedule III, individuals may avail of exchange facility for an amount in excess of the overall limit prescribed under the LRS, if it is so required by a country of emigration, medical institute offering treatment or the university respectively.

c) A person who is resident but not permanently resident in India **and** (a) is a citizen of a foreign State other than Pakistan; or (b) is a citizen of India, who is on deputation to the office or branch of a foreign company or subsidiary or joint venture in India of such foreign company is allowed to make remittances up to his net salary in India (after deduction of taxes, contribution to provident fund and other deductions).

d) Out of the overall foreign exchange of USD 250,000 available per financial year to an individual traveller, exchange in the form of foreign currency notes and coins may be sold by ADs up to the limit indicated below:

   i. Travellers to countries other than Iraq, Libya, Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States – not exceeding USD 3,000 per visit or its equivalent.

ii. Travellers to Iraq or Libya – not exceeding USD 5,000 per visit or its equivalent.

iii. Travellers to Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States – full exchange may be released.

iv. Travellers for Haj/Umrah pilgrimage – full amount of entitlement in cash or up to the cash limit as specified by the Haj Committee of India, may be released.

v. ADs are authorised to remit foreign exchange up to a reasonable limit, at the request of a traveller towards his hotel accommodation, tour arrangements, etc., in the countries proposed to be visited by him.

e) Period of surrender of foreign exchange

i. Unspent/unused foreign exchange by a resident individual is required to be surrendered within a period of 180 days from the date of receipt/ realisation/ purchase/ acquisition/ date of return of the traveller.

ii. A returning traveller is permitted to retain with him foreign currency traveller's cheques and currency notes up to an aggregate amount of USD 2,000 and foreign coins without any ceiling beyond 180 days. Foreign exchange so retained can be utilised by the traveller for his subsequent visit abroad.

f) Unspent /unutilised foreign exchange can be utilised for any other eligible purposes for which drawal of foreign exchange is permitted under relevant rules/regulations.

RBI has advised that where a person approaches an Authorised Person for surrender of unspent/unutilised foreign exchange after the prescribed period of 180 days, Authorised Person should not refuse to purchase the foreign exchange merely on the ground that the prescribed period has expired.

F. Meeting of medical expenses of NRI close relatives by resident individuals

Where the medical expenses in respect of NRI close relative (relative as defined in Section 6 of the Companies Act, 1956) are paid by a resident individual, such a payment being in the nature of a resident to resident transaction may be covered under the term "services related thereto" under Regulation 2(i) of Notification No. FEMA 16 /2000-RB dated May 3, 2000.

G. Use of International Credit Cards/ Debit Cards/Store value cards etc.

a) International Credit Cards (ICCs)

i. The restrictions contained in Rule 5 of the Foreign Exchange Management (Current Account Transactions) Rules, 2000 are not applicable for use of International Credit Cards (ICCs) by residents for making payment towards expenses, while on a visit outside India.

ii. Residents can use ICCs on internet for any purpose for which exchange can be purchased from an AD in India, e.g. for import of books, purchase of downloadable software or import of any other item permissible under Foreign Trade Policy (FTP). However, ICCs cannot be used on internet or otherwise for purchase of prohibited items, like lottery tickets, banned or proscribed magazines, participation in sweepstakes, payment for call-back services, etc.

iii. Use of ICC for payment in foreign exchange in Nepal and Bhutan is not permitted.

B. International Debit Cards (IDCs)

International Debit Cards (IDCs) can be used by a resident for drawing cash or making payment to a merchant establishment overseas during his visit abroad. IDCs can be used only for permissible current account transactions and the limits as mentioned in the Schedules. The IDCs cannot be used on internet for purchase of prohibited items like lottery tickets, banned or proscribed magazines, participation in sweepstakes, payment for call-back services, etc.

C. Redemption of unutilised balance on prepaid travel cards

Resident Indians purchasing travel cards are permitted refund of the unutilised foreign exchange balance only after 10 days from the date of last transaction. Since these cards are expected to act as substitutes for cash/Travellers Cheques, the facilities available to the user will have to be similar. APs shall redeem the unutilised balance outstanding in the cards immediately upon request by resident Indians to whom the cards are issued subject to retention of:

a) Amounts that are authorised and remain unclaimed/not settled by the acquirers as of the date of redemption till the completion of the respective settlement cycle;

b) A small balance not exceeding US $ 100, for meeting any pipeline transactions till the completion of the respective settlement cycle; and

c) Transaction fees/service tax payable in India in Rupees;

d) For the amount that are authorised but unclaimed/not settled by the acquirer, the issuer of such cards can hold such amounts until such transactions are processed/settled by the acquirers within the prescribed settlement timeframe.

H. Remittance facilities for others

1. The following remittances by persons other than individuals shall require prior approval of the Reserve Bank of India.

   i. Donations exceeding one per cent of their foreign exchange earnings during the previous three financial years or US D 5,000,000, whichever is less, for –

      i. Creation of Chairs in reputed educational institutes,

      ii. Contribution to funds (not being an investment fund) promoted by educational institutes; and

      iii. Contribution to a technical institution or body or association in the field of activity of the donor company.

   ii. Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or five per cent of the inward remittance whichever is more.

   iii. Remittances exceeding USD 10,000,000 per project for any consultancy services in respect of infrastructure projects and USD 1,000,000 per project, for other consultancy services procured from outside India.

   iv. Remittances exceeding five per cent of investment brought into India or USD 100,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses."

Schedule I
Transactions which are Prohibited (see Rule 3)

1. Remittance out of lottery winnings.
2. Remittance of income from racing/riding etc. or any other hobby.
3. sweepstakes, etc.
4. Payment of commission on exports made towards equity investment in Joint Ventures / Wholly Owned Subsidiaries abroad of Indian companies.
5. Remittance of dividend by any company to which the requirement of dividend balancing is applicable.
6. Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.
7. Payment related to "Call Back Services" of telephones.
8. Remittance of interest income on funds held in Non-Resident Special Rupee (Account) Scheme. 19

Schedule II
Transactions which require prior approval of the Central Government

(See Rule 4)

	Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
1.	Cultural Tours	Ministry of Human Resources Development, (Department of Education and Culture)
2.	Advertisement in foreign print media for the purposes other than promotion of tourism, foreign investments and international bidding (exceeding USD 10,000) by a State Government and its Public Sector Undertakings	Ministry of Finance, (Department of Economic Affairs)
3.	Remittance of freight of vessel chartered by a PSU	Ministry of Surface Transport, (Chartering Wing)
4.	Payment of import through ocean transport by a Govt. Department or a PSU on c.i.f. basis (i.e. other than f.o.b. and f.a.s. basis)	Ministry of Surface Transport, (Chartering Wing)
5.	Multi-modal transport operators making remittance to their agents abroad	Registration Certificate from the Director General of Shipping
6.	Remittance of hiring charges of transponders by (a) TV Channels (b) Internet Service providers	Ministry of Information and Broadcasting Ministry of Communication and Information Technology

	Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
7.	Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping	Ministry of Surface Transport (Director General of Shipping)
8.	Omitted	
9.	Remittance of prize money/sponsorship of sports activity abroad by a person other than International / National / State Level sports bodies, if the amount involved exceeds USD 100,000.	Ministry of Human Resources Development (Department of Youth Affairs and Sports)
10.	Omitted	
11.	Remittance for membership of P&I Club	Ministry of Finance (Insurance Division)

SCHEDULE III
(See rule 5)
Notified by GOI Notification No. G.S.R. 426(E) dated May 26, 2015

Facilities for individuals—

1. Individuals can avail of foreign exchange facility for the following purposes within the limit of USD 2,50,000 only. Any additional remittance in excess of the said limit for the following purposes shall require prior approval of the Reserve Bank of India.

i. Private visits to any country (except Nepal and Bhutan).

ii. Gift or donation.

iii. Going abroad for employment.

iv. Emigration.

v. Maintenance of close relatives abroad.

vi. Travel for business, or attending a conference or specialised training or for meeting expenses for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/check-up.

vii. Expenses in connection with medical treatment abroad.

viii. Studies abroad.

ix. Other current account transaction

Provided that for the purposes mentioned at item numbers (iv), (vii) and (viii), the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalised Remittance Scheme as provided in regulation 4 to FEMA Notification 1/2000-RB, dated 3rd May, 2000 (hereinafter referred to as the said Liberalised Remittance Scheme) if it is so required by a country of emigration, medical institute offering treatment or the university, respectively:

Provided further that if an individual remits any amount under the said Liberalised Remittance Scheme in a financial year, then the applicable limit for such individual would be reduced from USD 250,000 (US Dollars Two Hundred and Fifty Thousand Only) by the amount so remitted:

Provided also that for a person who is resident but not permanently resident in India and –

a. is a citizen of a foreign State other than Pakistan; or

b. is a citizen of India, who is on deputation to the office or branch of a foreign company or subsidiary or joint venture in India of such foreign company,

may make remittance up to his net salary (after deduction of taxes, contribution to provident fund and other deductions).

Explanation: For the purpose of this item, a person resident in India on account of his employment or deputation of a specified duration (irrespective of length thereof) or for a specific job or assignments, the duration of which does not exceed three years, is a resident but not permanently resident:

provided also that a person other than an individual may also avail of foreign exchange facility, *mutatis mutandis,* within the limit prescribed under the said Liberalised Remittance Scheme for the purposes mentioned hereinabove.

Facilities for persons other than individual –

2. The following remittances by persons other than individuals shall require prior approval of the Reserve Bank of India.

(i) Donations exceeding one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less, for –

  a. creation of Chairs in reputed educational institutes,

  b. contribution to funds (not being an investment fund) promoted by educational institutes; and

  c. contribution to a technical institution or body or association in the field of activity of the donor company.

(ii) Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or five per cent of the inward remittance whichever is more.

(iii) Remittances exceeding USD 10,000,000 per project for any consultancy services in respect of infrastructure projects and USD 1,000,000 per project, for other consultancy services procured from outside India.

Explanation:– For the purposes of this sub-paragraph, the expression "infrastructure' shall mean as defined in explanation to para 1(iv)(A)(a) of Schedule I of FEMA Notification 3/2000-RB, dated May 3, 2000.

(iv) Remittances exceeding five per cent of investment brought into India or USD 100,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses."

3. Procedure

The procedure for drawal or remit of any foreign exchange under this Schedule shall be the same as applicable for remitting any amount under the said Liberalised Remittance Scheme.

Note: The principal rules were published in Part II, Section 3, Sub-section (i) of Gazette of India, Extraordinary, *vide* G.S.R. 381(E), dated the 3rd May, 2000.


CA Hemal Shah & CA Juhi Virwani

In Focus – Accounting and Auditing

Property, Plant and Equipment – Key changes under Ind AS (Part II)

In the previous article, we have discussed few major changes brought by Ind AS in the area of fixed assets. The changes brought are quite significant in different aspects as compared to Indian GAAP.

Major changes brought by Ind AS are as below:

1. Component Accounting
2. Spare parts, stand by equipment, service equipment
3. Treating major inspection and overhaul expenses as a separate component
4. Provision for decommissioning liability/ site restoration costs and capitalisation of these costs.
5. Option of Cost model or Revaluation model
6. Arrangements containing lease

Also there are few exemptions available to the companies at the time of adoption of Ind AS for the first time. Exemptions available under Ind AS 101 for fixed assets are as follows:

a. Use of fair valuation or revaluation as deemed cost on Ind AS transition date
b. Use of previous GAAP carrying value on Ind AS transition date

Impact of many of these significant GAAP differences was neutralised by Ind AS 101 Exemption for Property, Plant and Equipment, especially allowing companies to use previous GAAP carrying values without any adjustment. Hence, according to a research recently conducted, only 27% of the companies which adopted Ind AS for financial year ended March 31, 2017, reported adjustments related to Property, Plant and Equipment.

Formation of 'Ind AS Transition Facilitation Group' (ITFG)

On initial application of the Ind AS, preparers, users and other stakeholders have come across various issues on which clarification or explanations were/are required. Hence the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India has constituted 'Ind AS Transition Facilitation Group' (ITFG) on January 11, 2016. The objective behind formation of the group is to provide clarifications on various issues related to the applicability and implementation of Ind AS under the Companies (Indian Accounting Standards) Rules, 2015. The group has come out with 11 bulletins so far comprising of many clarifications. The issues majorly pertain to clarifications required on application of Ind AS or issues pertaining to interpretation of the same.

Through this article, we have tried to cover clarifications issued by ITFG and FAQs issued by ASB which are related to fixed assets.

FAQ issued by ASB

- **Use of previous GAAP carrying value as deemed cost**

One of the additional exemptions given under Ind AS as compared to IFRS pertains to the option of continuing with previous GAAP carrying value as deemed cost subject to adjustments required for asset retirement obligation. Paragraph D7AA of Ind AS 101 provides that carrying value for all of Property, Plant and Equipment as recognised in the financial statements as at the date of transition to Ind ASs, measured as per the previous GAAP could be used as deemed cost as a starting point as on the date of transition. The objective of the exemption was to ensure smooth transition to Ind AS by allowing to continue fixed assets at the same value as that of the previous GAAP. However, while drafting this exemption under para D7AA, use of the words "carrying value" created major interpretation issues within the industry and professional circles. Since carrying value is generally referred for written down value and paragraph D7AA specified carrying value to be the starting point for Ind AS opening balance sheet, two divergent views emerged. One view was to take original cost being same as original cost of previous GAAP whereas contrary view was written down value under the previous GAAP to be considered as original cost as a starting point as the exemption given under Ind AS 101 used the words "carrying value". To take an example, if the Company which is in operation for more than 10 years has original cost of fixed assets as ₹ 100 and accumulated depreciation of ₹ 60, then following exemption under para D7AA, deemed original cost under Ind AS is taken as 40 which represents written down value under the previous GAAP. This means value of accumulated depreciation and provision for impairment if any under previous GAAP would now be treated as nil on the date of transition.

This issue was referred to the Accounting Standards Board (ASB) by Ind AS Transition Facilitation Group of Ind AS (IFRS) Implementation Committee. Accordingly, ASB has considered the issue and issued FAQ on the same.

The FAQ clarified that as per the definition of deemed cost, it is the amount used as a surrogate for the cost or depreciated cost and for the purpose of subsequent depreciation or amortisation, this becomes the starting point. Accordingly, from the date of transition, the deemed cost, i.e., carrying values of Property, Plant and Equipment (PPE) as per the previous GAAP is the cost and any accumulated depreciation and provision for impairment under previous GAAP have no relevance.

This has far reaching implications as discussed below:

- Firstly, all the companies will now have to maintain new records or change existing records like Fixed Assets Register for capturing revised original cost as deemed cost under paragraph D7AA of Ind AS 101. However apart from revised cost as discussed, original purchase price/ acquisition cost may be relevant and will have to be maintained to comply with other legal requirements e.g. a question arises as to which original cost should be considered for calculating profit under Section 198 of the Companies Act, 2013. Formula presribed by Section 198 for calculating profit is used for deriving maximum managerial remuneration that can be paid, for calculating CSR expense obligation, etc. Sub-section 3(d) of Section 198 specifies that if profit of any entity includes any gain from sale of immovable property or fixed asset of a capital nature, credit shall be given for so much of the excess as is not higher than the difference between the original cost of that fixed asset and its written down value. Whether original cost referred to in sub-section 3(d) means original purchase cost or original cost now considered as per deemed cost exemption under Ind AS 101. Since Section 198 requirement is a legal requirement, one would go by original purchase/ acquisition cost and not by original cost which is deemed cost under Ind AS 101 of previous GAAP carrying value.

Considering this, record keeping and tracking of multiple values are now inevitable.

- Secondly, though written down values remain same, original costs of the assets would reduce significantly in most of the cases especially when fixed assets were not recently acquired. This may lead to issues from lenders/bankers who would have extended finances after giving weightage to original investment in the fixed assets.
- Thirdly, this may also make comparison of company's performance as against other industry peers distorted especially when any ratios are based on original cost of the assets. This is because all the companies may not have opted for this deemed cost exemption of previous GAAP carrying value under para D7AA.
- Lastly, the deemed cost exemption takes written down value on the date of adoption of Ind AS as the starting point. Hence in the past, if provision for impairment was created, the deemed cost exemption under D7AA paragraph takes the value after impairment provision as the cost. Considering this, provision for impairment loses its identity and the same cannot be reversed in future.

Clarifications issued by ITFG

Following are few of the clarifications issued by ITFG which are relevant for fixed asset. For readers' easy reference, we have given references to bulletin numbers and issue numbers dealing with the matters below each heading. E.g. B.1 – I.3 in the first case given below refers to Issue No. 3 from Bulletin No. 1.

- **Foreign exchange differences pertaining to fixed assets and borrowings related to fixed assets**

  (B.1 - I.3, B.7 – I.1 and B.2 – I.1)

(i) According to Indian GAAP, an entity was permitted by paragraph 46/46A of AS 11 to capitalise foreign exchange differences arising from long term foreign currency monetary items where such monetary item has arisen for purchase of fixed assets. On availing this option, such exchange gains or losses would be capitalised in cost of Property, Plant and Equipment or accumulated in a reserve named as Foreign Currency Monetary Item Translation Difference Account (FCMITDA).

Transitional exemptions under Ind AS 101 (paragraph D13AA) allows continuation of recognition of exchange differences arising from translation of long term foreign currency monetary items in the same way it was accounted before the beginning of the first Ind AS financial reporting period. This option once exercised, companies may continue to treat the exchange differences on foreign currency loans as either adjustment to the value of fixed assets or accumulate this in FCMITDA.

A question was raised whether this option be availed for loans taken only prior to Ind AS transition date or even other loans taken after the Ind AS transition date. It was clarified by ITFG that the wordings used in paragraph D13AA are "....exchange differences arising from translation of long term foreign currency monetary items recognised **in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period**

as per the previous GAAP". Considering this, this exemption can be availed only for loans which are taken up to the date of Ind AS transition date and not for the loan taken subsequent to the Ind AS transition date which is the first day of the comparative Ind AS financial statement.

(ii) A further question was raised where the part of the loan (say 70% was drawn before the Ind AS transition date). However remaining sanctioned loan of 30% was drawn after the Ind AS transition date e.g. after April 1, 2015 for a company adopting Ind AS for the first time in financial year 2016-17 with 2015-16 being comparative year. Whether the treatment allowed under Ind AS will continue to apply after the transition date for the undrawn part of the loan.

The ITFG clarified that the exemption under Ind AS 101 is available only for exchange differences arising on long term foreign currency loans that have been recognised in the financial statements prior to first Ind AS financial reporting period. Therefore the exemption would not apply to any loan taken subsequent to the date of adoption to Ind AS and also the undrawn part of the foreign currency loan for the loans sanctioned earlier and the foreign exchange differences arising on these cases would be taken to statement of profit and loss.

This means exchange differences for the same asset can have two different treatments based on the date on which the sanctioned loan amounts are actually drawn.

However for the purpose of Income-tax Act, companies will still be governed by provisions of Section 43A of the Income -tax Act, 1961.

(iii) Another relevant question for loan borrowed prior to Ind AS transition date in case of companies who have opted for recognising the differences in FCMITDA is whether the amortisation of balance in FCMITDA needs to be taken to profit or loss or other comprehensive income.

The ITFG clarified that since the amortisation of exchange differences under the existing policy (as per the previous GAAP) would be recognised in the statement of profit and loss affecting the profit or loss for the period, amortisation of balance of FCMITDA shall also be routed through profit or loss and not through Other Comprehensive Income (OCI).

- **Treatment of capital spares (B.3 – I.9 and B.5 – I.6)**

  An entity has classified capital spares as inventory under previous GAAP and now on application of Ind AS, the entity decides to capitalise the spares as it meets the definition of Property, Plant and Equipment under Ind AS 16. Whether the same is allowed as per Ind AS if the entity has adopted the option of using carrying value of assets as deemed cost under paragraph D7AA of Ind AS 101 on the transition date. This question is relevant as there is a conflict between requirements of Ind AS 16 which requires recognition of stores and spares as assets provided they are held for use in the production of supply of goods and are expected to be used during more than one period and on the other hand paragraph D7AA of Ind AS 101 does not allow any adjustment to the carrying value as per previous GAAP if previous GAAP carrying value option is selected.

  The ITFG clarified that Ind AS 16 allows the capitalisation of stores and spare parts if it meets the definition of PPE as per the standard and the transitional exemption does not prevent a company to recognise spares as part of Property, Plant and Equipment whose recognition is required by Ind AS on the date of transition.

This is an important clarification as it gives clarity that choosing deemed cost exemption for PPE does not mean changes to the value of PPE is completely ruled out specially when the changes are made to comply with the provisions of Ind AS. If any changes in the values are required to comply with Ind AS 16 provision, then these changes are necessary to reflect correct values under Ind AS.

In addition to above, if stores previously considered in inventory is to be capitalised, at what amount the same should be recognised and depreciation should be charged from what period i.e. from the date when the same became available for use or the date of actual use.

Clarification by ITFG is as below:

Ind AS 101 provides the use of carrying value of Property, Plant and Equipment as deemed cost. However, the above exemption cannot be used for such spare parts in the given case since the same were not recognised as fixed assets in the previous GAAP. Hence the entity should apply Ind AS 16 retrospectively to measure the amount that will be considered for recognition of such spare parts on the date of transition to Ind AS. With regard to deprecation, Ind AS 16 provides that the depreciable amount of an asset shall be allocated on a systematic basis over its useful life over which an asset is expected to be available for use. Spare parts are generally available for use from the date of its purchase and hence should be depreciated from the date of purchase.

- **Value of Capital Work in Progress under deemed cost exemption (B.3 – I.11)**
  The issue under consideration was whether a company electing the option of using previous GAAP carrying value of asset as deemed cost as per paragraph D7AA under Ind AS 101 can extend this exemption to items of capital work in progress.

  ITFG has clarified that the above exemption is applicable to PPE under Ind AS 16, intangible assets covered by Ind AS 38, and investment property covered by Ind AS 40.

  Capital work in progress is in the nature of Property, Plant and Equipment under construction and accordingly, provisions of Ind AS 16, Property, Plant and equipment apply to it. Hence, in the given case, option under Ind AS 101 for deemed cost exemption is available with regard to capital work in progress also.

- **Application of exemption related to service concession arrangements to toll road companies (B.3 – I.13)**
  In case of companies running the business of construction and maintenance of toll roads, the transitional exemption of Ind AS 101 allows the first time adopter to continue with the amortisation policy adopted under previous GAAP for amortisation of the intangibles recognised in the financial statements for the period ending before transitional period.

  However a question arises where the company has entered into an arrangement before transitional period and the toll road is under construction even after Ind AS transition date, will the company be able to apply the transitional exemption?

  The ITFG clarified that the said exemption is only applicable to those intangibles which have been recognised in the financial statements before the transition period. Since the toll road is still under construction, the recognition of the same would not have taken place and hence the said exemption is not allowed.

- **Application of deemed cost exemption to assets held for sale (B.10 – I.4)**
  An entity had recognised few assets as assets held for sale and disclosed the same under current assets instead of fixed assets under

the previous GAAP as these assets were retired from active use and held for sale and hence met the requirement of paragraphs 73 and 74 of AS-10. However, on transition to Ind AS, the said asset could not fulfil the criteria of assets held for sale prescribed under Ind AS 105 – Non-current Assets Held for Sale and Discontinued Operations, hence the same needs to be classified as PPE. The issue under consideration is whether the deemed cost exemption can be applied to these assets?

ITFG in the present case clarified that as per Ind AS 101, the deemed cost exemption is applicable to PPE as defined under Ind AS 16 and recognised as Fixed Assets in the financial statements at the transitional date irrespective of whether these were disclosed separately since the entity had only disclosed it separately and had not eliminated the same from the books, it can avail the deemed cost exemption for such type of assets as well.

- **Adjustments to the carrying value of PPE**
  - **Processing fees of loan (B.5 – I.4 and B.10 – I.2)**

    An entity had obtained a loan prior to transitional period. The processing fees on the loan were capitalised as part of the relevant fixed assets as per the previous GAAP. At the time of adoption of Ind AS, it has chosen to avail deemed cost exemption as per Ind AS 101, i.e., to continue with carrying value of Property, plant and equipment as per the previous GAAP. However, the loan needs to be restated to its amortised cost as per Ind AS 109 and hence the cost of PPE needs to be reduced by the amount of processing fees. Whether the said adjustment is allowed as per transitional exemption.

    As per Ind AS 101, if the carrying value is considered as the deemed cost, no further adjustments are allowed to the deemed cost of the Property, Plant and Equipment. However Ind AS 101 also states that except for the mandatory exceptions and voluntary exemptions provided in Ind AS 101, measurement of all assets and liabilities will be done basis other Ind AS. Since Ind AS 101 does not state any mandatory exception or voluntary exemption regarding this, the carrying amount of loan is required to be restated to its amortised cost and hence the said adjustment in the value of PPE is allowed and required to be made.

  - **Government grant against fixed asset (B.5 Revised – I.5)**

    An entity received a Government grant against capital item purchased and hence the cost of Property, Plant and Equipment was reduced to the extent of the grant received as per the previous GAAP. However as per Ind AS 20, such a grant is required to be accounted by treating the grant as deferred income on the date of transition and the deduction of the same from the carrying amount of the asset is not allowed. Question was raised whether the value of fixed assets should now be changed under Ind AS if the deemed cost exemption is availed by the entity.

    Applying the same principle as above, since there is no mandatory exception or voluntary exemption in Ind AS 101, the cost of PPE will be increased to the extent of grant amount and the same will be shown as deferred income as per Ind AS 20.

    Though there has been a change in thought process by ITFG as in the original bulletin 5, it stated that the deemed cost value as per previous GAAP should not be changed and the corresponding value for recognising grant receivable should be in retained earnings as on the date of transition. However by issuing Revised Bulletin No. 5 it clarified that the change in the value of deemed cost is to be made under paragraph D7AA of Ind AS 101 considering there is no mandatory exception or voluntary exemption for this aspect in Ind AS 101.

- **Capitalisation of asset not meeting the criteria of Ind AS 16 (B.8 – I.4)**

  An entity had capitalised an item of Property, Plant and Equipment in the previous GAAP even though it did not meet the definition of an asset and it opts to adopt the transitional exemption of previous GAAP deemed cost. Whether this asset cost can also be continued to be capitalised under deemed cost exemption was raised before ITFG for its consideration.

  The ITFG clarified that the as per Ind AS 101, an entity should:

  – recognise all assets and liabilities whose recognition is required by Ind ASs

  – not recognise items as assets or liabilities if Ind ASs do not permit such recognition

  – reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with Ind ASs; and

  – apply Ind ASs in measuring all recognised assets and liabilities

  Applying the second point above, the item which does not fall under the definition of PPE as per Ind AS should not be taken into consideration for the recognition of the same as PPE.

  Also if an entity becomes aware of errors made under previous GAAP, the same needs to be shown in the reconciliation items separately from those which have undergone a change due to change in accounting policies.

- **Capitalisation of cost incurred for the assets used as a support for building/ creation of main asset (B.11 – I.8)**

  An entity is setting up a new refinery outside the city limits and hence an additional expenditure is incurred for construction of railway siding, road and bridge. Whether the cost of the support assets created should be capitalised with the main cost of the asset was an issue raised before ITFG.

  Ind AS 16 states that the cost of an item of Property, Plant and Equipment comprise any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Since in the given case, the railway siding, road and bridge are required to facilitate the construction of the refinery and for its operations and also expenditure on these items will help the entity to get future economic benefits, the aforesaid expenditure is directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. In this case, even though the company may not be able to recognise expenditure incurred on these assets as an individual item of Property, Plant and Equipment as it may not be able to restrict others from using it, entire expenditure incurred may be capitalised as a part of overall cost of the project.

  The above clarification on "enabling asset" is a major relief for Companies which have undertaken big projects where expenditure on these enabling assets is quite significant.

- **Treatment of revaluation reserve in case of adoption of deemed cost (B.8 – I.7)**
  A company which is a first time adopter of Ind AS, has opted for deemed cost exemption under paragraph D7AA to continue with previous GAAP carrying value and also elected the cost model under Ind AS 16 for subsequent measurement. However the company had "revaluation reserve" created in the past in the previous GAAP. Question was raised as to what should be the accounting treatment for such revaluation reserve created under the previous GAAP.

  ITFG clarified that paragraph 11 of Ind AS 101 provides that, the accounting policies that an entity uses in its opening Ind AS balance sheet may differ from those that it used for the same date using its previous GAAP. The resulting adjustments arise from events and transactions before the date of transition to Ind AS. Therefore, an entity shall recognise those adjustments directly in retained earnings (or, if appropriate, another category of equity) at the date of transition to Ind AS.

  As per the above requirements, the revaluation reserve can be added to retained earnings or any other appropriate category of equity. This is because after the transition, the Company is no longer applying the revaluation model of Ind AS 16, instead it has elected to apply the cost model approach. However, requirement of the Companies Act, 2013 for declaration of dividend will be required to be evaluated separately.

  The Company will also have to create deferred tax balance based on the difference between carrying amount and tax base of assets.

Conclusion

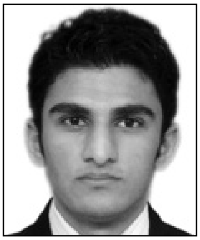
From the above clarifications issued by ITFG, it is clear that use of deemed cost exemption of continuing with previous GAAP carrying value is now not a simple and easy exercise since many adjustments may be required to these values based on the discussions above. An entity choosing deemed cost exemption under paragraph D7AA needs to clearly understand these clarifications to correctly transition the value of Property, Plant and Equipment from previous GAAP to Ind AS.

Study of companies which have adopted Ind AS in Phase 1

Following is the extract of an analysis of 75 companies out of BSE's top 100 Companies which have adopted Ind AS in phase 1 -

- 68 Companies have adopted the transitional exemption under Ind AS 101 and 7 Companies have followed the fair value method under Ind AS 16. Due to adoption of either methods, there is a mixed impact on the net worth and profit of the Companies. However there is increase in net worth of 7 Companies adopting fair value by INR 17,300 crores. Also the increase in net worth would lead to high depreciation in further years.
- Due to capitalisation of spares now falling in definition of PPE, the net worth of 8 Companies increased by INR 700 crores.
- Decrease in profits due to increase in depreciation charge on revised values of PPE.
- Below is the summary of impact on net worth and profit in the standalone financials of March 31, 2016 (in number of companies):

Impact	Net worth	Profit
Positive	8	36
No Impact	59	10
Negative	8	29



Rahul Sarda, *Advocate*

BEST OF THE REST

1. Arbitration proceedings – On the same issue, an arbitration proceeding brought by group company pending – Grant of stay

M/s. Hutchinson Telecommunications International Limited earned capital gains on the sale of stakes to Vodafone International Holdings B.V (VIHBV) in an Indian company by the name of Hutchinson Essar Limited (HEL). The acquisition of stake in HEL by VIHBV was held liable for tax deduction at source under Section 195 of the Income-tax Act, 1961 and since VIHBV failed to honour its tax liability, a demand under Sections 201(1)(1A)/220(2) for non-deduction of tax was raised on VIHBV. However, the Apex Court quashed the said demand.

Subsequently, a retrospective amendment to Section 9(1) and Section 195 of the Income Tax Act read with Section 119 of the Finance Act, 2012 re-fastened the liability on VIHBV.

Aggrieved by the imposition of retrospective tax, VIHBV, the subsidiary of Vodafone Group PLC United Kingdom (i.e. the Defendant herein) invoked the arbitration clause provided under the Bilateral Investment Promotion and Protection Agreement (BIPA) between the Republic of India and the Kingdom of Netherlands for the promotion and protection of investments through a notice of dispute dated 17th April, 2012 and subsequent notice of arbitration dated 17th April, 2014.

While the said arbitration proceedings were pending, the Defendant herein served a notice of dispute dated 15th June, 2015 and notice of arbitration dated 24th January, 2017 upon the Union of India (i.e. the Plaintiff herein) for resolution of an alleged dispute under the India-UK BIPA primarily in respect of the same income tax demand that VIHBV had identified as protected investment under the India-Netherlands BIPA and which were already under adjudication before the Arbitral Tribunal constituted under BIPA.

The Court came to the *prima facie* view that there was duplication of the parties and the issues and further that India constituted the natural forum for the litigation of the Defendants' claim against the Plaintiff.

In fact, the reliefs sought by the defendants under the India-UK BIPA and by the VIHBV the subsidiary of defendants under the India-Netherlands BIPA are virtually identical. The Defendants and as their subsidiary VIHBV, *prima facie*, seemed to be one single economic entity. As the claimants in the two arbitral proceedings form part of the same corporate group being run, governed and managed by the same set of shareholders, they could not file two independent arbitral proceedings as that amounts to abuse of process of law. There was also a risk of parallel proceedings and inconsistent decisions by two separate arbitral Tribunals. Hence, the Defendants were restrained from initiating arbitration.

Union of India vs. Vodafone Group PLC United Kingdom [2017] 84 taxmann.com 224 (Del.)

2. Insolvency & Bankruptcy Code – Infrastructure Company – Committed Returns – Default in Payment – Financial Creditor – Debt due

The appellants executed agreements with respondent Corporate Debtor for purchase of units being a residential flat, shop and office space in the projects, which were being developed by and promoted by the Corporate Debtor. Under the "Committed Return Plan", the appellants were to pay a substantial portion of the total sale consideration upfront at the time of Execution of the agreement, and the Respondent undertook to pay a particular amount to the buyer/purchaser appellants each month, as committed returns till the time the actual physical possession of the unit was handed over to the buyer/purchaser. In the said projects the appellants also had an option to choose the construction/time linked payment plan as per which they were required to pay a certain percentage of the sale consideration amount at various stages of construction of the project in which the respondent defaulted. In an application under section 7 of the I&B Code, the Adjudicating Authority i.e. the NCLT held that the appellants were not "financial creditors" as defined under section 5(7). The NCLT further held that as many winding up petitions were pending before the Delhi High Court against the respondent and Financial Liquidator had been appointed, the application preferred by appellants for triggering insolvency process was not maintainable.

Held, a person to whom a "financial debt" was owed including a person whom such debt has been legally assigned or transferred to was a "financial creditor". From the agreement, it was clear that the appellants were "investors" and had chosen "committed return plan". The respondent in their turn agreed upon to pay monthly committed return to investors. Thus, the amount due to the appellants come within the meaning of 'debt' as defined in section 3(11). From the Annual Return of the respondent and Form 16A, it is found that the corporate debtor' treated the appellants as 'investors' and borrowed the amount pursuant to sale purchase agreement for their commercial purpose treating at par with 'loan' in their return. Thereby, the amount invested by appellants come within the meaning of "financial debt", as defined in section 5(8)(f) subject to satisfaction as to whether such disbursement against the consideration is for time value of money.

It was also held that the NCLT erred in holding the arrangement as a "pure and simple agreement of sale and purchase of a piece of property and has not acquired the status of a financial debt as the transaction does not have consideration for the time value of money". Therefore, the judg ment of the NCLT was set aside and matter was set aside to the NCLT to admit the application preferred by appellants and pass appropriate order, if the application under section 7 was otherwise complete.

Nikhil Mehta & Sons vs. AMR Infrastructure Ltd. [2017] 84 taxmann.com 163 (NCLT - New Delhi)

3. Insolvency & Bankruptcy Code – Pendency of winding up proceeding – Whether bar to insolvency proceedings

Applicant-financial creditor of respondent company filed petition for winding up of Respondent company. During the pendency of winding up petition, State Bank of India and its associates in their capacity as Financial Creditors filed petition to initiate insolvency resolution process under the Insolvency and Bankruptcy Code. It was a case of the Applicant that when winding up proceedings were at an advanced stage before High Court, any order passed at different forum would lead to conflicting orders and therefore filed an intervention application in the proceedings initiating insolvency. Held, pendency of winding up proceeding before admission of insolvency proceeding would not bar either initiation or continuation of such insolvency proceedings. And, on admission of the proceedings triggering insolvency process, the Applicant (who had filed the winding up petition) could as well represent its claim before Interim Insolvency Resolution Professional. Therefore, the application for intervention in proceeding for triggering insolvency resolution process was to be dismissed.

Industrial & Commerce Bank of China vs. Alok Industries Ltd. - [2017] 84 taxmann.com 56 (NCLT - Ahd.)

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Tax Articles for Your Reference

Articles published in Taxman, Current Tax Report (CTR), The Tax Referencer (TTR), Income Tax Report (ITR), ITR's Tribunal Tax Reports (ITR (Tribunal), The Bombay Chartered Accountant Journal (BCAJ), The Chamber's Journal (C J), The Chartered Accountant Journal (CAJ), All India Federation of Tax Practitioners Journal (AIFTPJ), Company Case, Times of India and Economic Times for the period August to September 2017 has been arranged and indexed topic-wise.

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Valuations				
Taxman questions experts over Start-up's Valuations	Sachin Dave & Vishal Dutta	ET	9/13/2017	9
VAT				
Works contract *vis-à-vis* Consumables	G. G. Goyal & C. B. Thakar	BCAJ	49-A/Part 5	71

CA Ketan Vajani & CA Nishtha Pandya
Hon. Jt. Secretaries

The Chamber News

Important events and happenings that took place between 8th September, 2017 to 7th October, 2017 are being reported as under.

I. Admission of New Members

1) The following new members were admitted in the Managing Council Meeting held on 6th October, 2017.

Life Membership

1	Manoj Kumar Ganapath Raj	CA	Bengaluru
2	Gada Vishal Vassanji (Shifted from Orinary to Life)	CA	Ahmedabad
3	Shah Chirag Mahendrabhai	CA	Ahmedabad
4	Momaya Mayur Kishor	CA	Mumbai
5	Neeraj Krishnakumar	CA	New Delhi

Ordinary Membership

1	Seth Rajiv	CA	Mumbai
2	Chaturvedi Rahul Umakant	CA	Bengaluru
3	Shinde Arvind M.	Advocate	Pune
4	Ms. Rajgor Mansi Paresh	CA	Mumbai
5	Ms. Fofaria Khushboo Tushar	CA	Mumbai
6	Mr. Rao Purnachandra P.	CA	Nellore
7	Mr. Shukla Satish Devnarayan	ITP	Nashik
8	Mr. Jain Niraj Popatlal	CA	Mumbai
9	Mr. Kuber Anant Arun	CA	Pune
10	Mr. Tiwari Jayprakash	CA	Mumbai

Student Membership

1	Mr. Vyas Sharvan Kumar Kantilal	Student	Mumbai
2	Ms. Thakkar Ruchi Ramesh	Student	Mumbai
3	Mr. Domadia Dhanesh P.	Student	Mumbai

II. Past Programmes

1. ALLIED LAWS COMMITTEE JOINTLY WITH CORPORATE CONNECT COMMITTEE

Seminar on The Insolvency & Bankruptcy Code, 2016 held on 7th October, 2017 at Walchand Hirachand Hall, IMC. The Keynote address at the Seminar was given by Shri Mukul Shrawat, Hon. Member of NCLT. The Seminar was addressed by CA Abizer Diwanji, Ms. Jyoti Singh, Advocate and Dr. Rajendra Ganatra.

2. INDIRECT TAX AND IT CONNECT COMMITTEE

Half day Seminar on "GST Return Filing: Practical Issues: Q & A Session" was held on 16th September, 2017 at Jai Hind College. The Seminar was addressed by CA Ashit Shah, CA Mitesh Katira, CA Alok Jajodia and Mr. Arvind Sinha – Officer from Central Tax Office. The Seminar was attended by 92 participants.

3. INTERNATIONAL TAXATION COMMITTEE

Public Lecture Meeting on Recent Developments in International Taxation held on 5th October, 2017 at Babubhai Chinai Hall, IMC. The Lecture Meeting was addressed by CA Himanshu Parekh.

4. LAW & REPRESENTATION COMMITTEE

Pre-Budget Suggestions

The Chamber intends to make exhaustive Pre-Budget representation. For this, the Chamber is in process of preparing Pre-Budget Memorandum, which may be followed by personal meetings with the key officials of the Ministry of Finance, along with Chairman of CBDT. The Chamber, therefore, invites suggestions from the members on any aspect of direct or indirect taxes for which representation is desired.

The Chamber also intends to make representation on various other fiscal and allied laws, like Companies Act, SEBI, RBI, ROC, Stamp Act, etc., for which various sub-committees have been formed. The Chamber solicits views and suggestions from the members in this regard also.

Kindly send your suggestions for pre-budget representation in the following format, using font Arial and font size 12 in word file latest by 11th November, 2017 on office@ctconline.org.

PRE – BUDGET MEMORANDUM (Format)

Sr. No.	Issue		Justification
	Existing Provision	Suggestion	

5. **MEMBERSHIP & PUBLIC RELATION COMMITTEE**

Full day Seminar on GST, Tax Audit Issues under ICDS & Form 3CD Changes & Supreme Court Decisions was held on 23rd September, 2017 at Hotel Tripur, Solapur. The Seminar was organised jointly with Solapur CA Branch of WIRC of ICAI and ITP & STP Association, Solapur The seminar was addressed by CA Sumit Jhunjhunwala, CA Deepak Thakkar, CA Abhitan Mehta and CA Anish Thacker.

Half Day Seminar on GST was held on 2nd October, 2017 at Rotary Sunrise Community Hall, Kolhapur. The Seminar was organised jointly with Tax Consultants Association, Kolhapur. The Seminar was addressed by CA Mayur Parekh.

III. Future Programmes

1. **ACCOUNTING & AUDITING / ALLIED LAWS / DIRECT TAXES COMMITTEE**

3 days Conference on Real Estate Laws – Combating Challenges arising out of various laws scheduled to be held on 11th, 18th and 25th November, 2017 at IMC.

2. **INDIRECT TAXES COMMITTEE**

6th Residential Referencer Course on GST scheduled to be held from 25th to 28th January, 2018 at The Ananta, Udaipur.

3. **RESIDENTIAL REFRESHER COURSE & SKILL DEVELOPMENT COMMITTEE**

41st Residential Refresher Course scheduled to be held from 22nd to 25th February, 2018 at Taj Swarna, Amritsar.

(For details of the future programmes, kindly visit www.ctconline.org or refer The CTC News of September, 2017)

Study Circle & Study Group Committee

Study Group Meeting on Judgments Relating to ICDS & Tax Audit held on 11th September, 2017 at SNDT Committee Room, SNDT College

CA Anish Thacker addressing the participants

Study Circle Meeting on ICSD–VI – Effects of changes in Foreign Exchanges Rates, ICDS–X – Provisions, Contingent Liabilities & Contingent Assets held on 12th September, 2017 at SNDT Committee Room, SNDT College

CA Abhitan Mehta addressing the participants

Membership & Public Relations Committee jointly with The Tax Consultants Association, Kolhapur Branch

Half Day Seminar on GST held on 2nd October, 2017 at Rotary Sunrise Community Hall, Kolhapur

Dignitaries on Dais – Seen from L to R: Mr. Arun Baheti, Vice Chairman, Tax Consultant Association, Kolhapur Mr. Dhiraj Shah - Advocate, (Member, Membership & PR Committee) CA Mayur Parekh (Speaker) and Mr. Sachin R. Gandhi (Co-Chairman – Membership & PR Committee)

CA Mayur Parekh addressing the participants

Indirect Taxes Committee

Study Circle Meeting on Issues in Valuation and Time of Suply in GST held on 4th October, 2017 at A.V. Room, Jai Hind College, Mumbai.

CA Shreyas Sangoi (Speaker) addressing the participants. Seen from L to R: CA Bharat Oza (Convenor), CA Atul Mehta (Vice-Chairman), Mr. Ajay R. Singh, Advocate (President), CA Naresh Sheth (Chairman) and CA Sumit Jhunjhunwala (Convenor)

Chamber of Tax Consultants jointly with BCAS, Dharma Bharati Mission and Friends of VSSM & Dharampur

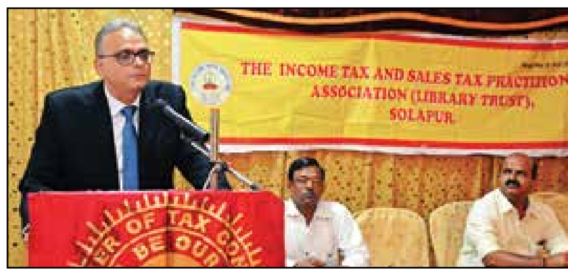
Meeting to pay tribute to Late Shri Pradeep N. Shah held on 10th September, 2017 at BCAS Conference Room

Membership & Public Relations Committee jointly with Solapur Branch of Western India Regional Council of The Institute of Chartered Accountants of India and The Income Tax & Sales Tax Practitioners' Association (Library Trust)

Full Day Seminar on GST, Tax Audit Issues under ICDS and Form 3CD Changes & Supreme Court Decisions held on 23rd September, 2017 at Hotel Tripur Sundari, Gandhi Nagar, Solapur

Mr. Ajay R. Singh, Advocate (President) lighting the lamp. Seen from L to R: Mr. S. A. Jamkhandi, Advocate (Secretary – IT & STPA, Solapur), Mr. Sunil Ingle (Chairman – Solapur CA Branch, WIRC), Mr. Sanjeev Konshirsagi, Advocate (President – IT & STPA), CA Chandrakant Injamuri (Chairman – IT & STPA, Solapur) and CA Daresh Patil (IPP Solapur CA Branch)

Mr. Ajay R. Singh, Advocate (President) giving opening remarks. Seen from L to R: Mr. Sunil Ingle (Chairman – Solapur CA Branch, WIRC) and Mr. Sanjeev Konshirsagi, Advocate (President – IT & STPA)



CA Anish Thacker (Speaker) addressing the participants Seen from L to R: Mr. S. A. Jamkhandi, Advocate (Secretary – IT & STPA, Solapur) and Mr. Pawan Shah, Advocate (Session Chairman)

CA Abhitan Mehta (Speaker) addressing the participants. Seen from L to R: CA Nandkishor Udgiri (Vice-Chairman, Solapur CA Branch) and CA Bora (Session Chairman)

CA Deepak Thakkar (Speaker) addressing the participants

CA Sumit Jhunjhunwala (Speaker) addressing the participants. Seen from L to R: Mr. Sanjeev Konshirsagi, Advocate (President – IT & STPA) and Mr. Deshpande, Advocate (Session Chairman)

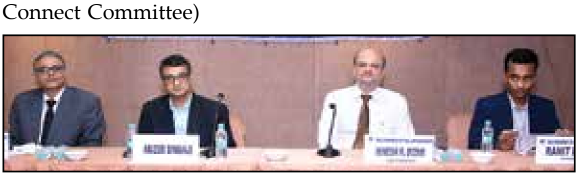
Allied Laws Committee jointly with Corporate Connect Committee

Seminar on The Insolvency & Bankruptcy Code, 2016 held on 7th October, 2017 at Walchand Hirachand Hall, IMC

Guest of Honour Hon'ble Shri Mukul Shrawat - Member, NCLT, lighting the lamp. Seen from L to R: CA Abizer Diwanji (Speaker), CA Anish Thacker (Chairman – Corporate Connect Committee), Ms. Jyoti Singh, Advocate (Speaker), Mr. Rahul Hakani, Advocate (Chairman – Allied Laws Committee), Mr. Ajay R. Singh, Advocate (President), CA Apurva Shah (Convenor – Corporate Connect Committee) and CA Ketan Vajani (Hon. Jt. Secretary)

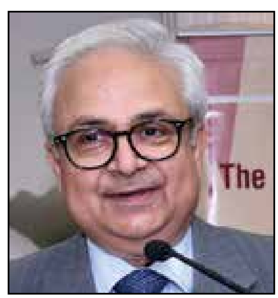
Mr. Ajay R. Singh, Advocate (President) giving opening remarks. Seen from L to R: Mr. Rahul Hakani, Advocate (Chairman – Allied Laws Committee) and Hon'ble Shri Mukul Shrawat

Shri Rahul Hakani, Advocate (Chairman – Allied Laws Committee) welcoming the Speakers. Seen from L to R: Hon'ble Shri Mukul Shrawat, Mr. Ajay R. Singh, Advocate (President) and CA Anish Thacker (Chairman – Corporate Connect Committee)



Dignitaries on Dais. Seen from L to R: CA Anish Thacker (Chairman – Corporate Connect Committee), CA Abizer Diwanji (Speaker), CA Hinesh R. Doshi (Vice-President) and Mr. Ranit Basu, Advocate (Convenor – Allied Laws Committee)

CA Anish Thacker (Chairman – Corporate Connect Committee) welcoming the Speakers. Seen from L to R: Mr. Rahul Hakani, Advocate (Chairman – Allied Laws Committee), Hon'ble Shri Mukul Shrawat and Mr. Ajay R. Singh, Advocate (President)



Hon'ble Shri Mukul Shrawat – Member NCLT addressing the participants

CA Abizer Diwanji (Speaker) addressing the participants. Seen from L to R: CA Anish Thacker (Chairman – Corporate Connect Committee), CA Hinesh R. Doshi (Vice-President) and Mr. Ranit Basu, Advocate (Convenor – Allied Laws Committee)

Allied Laws Committee jointly with Corporate Connect Committee

Seminar on The Insolvency & Bankruptcy Code, 2016 held on 7th October, 2017 at Walchand Hirachand Hall, IMC.

Dignitaries on Dais. Seen from L to R: CA Apurva Shah (Vice-Chairman – Corporate Connect Committee), Ms. Jyoti Singh, Advocate (Speaker), Mr. Ajay R. Singh, Advocate (President) and Mr. Parvin Veera (Advisor – Allied Laws Committee)

Ms. Jyoti Singh, Advocate (Speaker) addressing the participants.

Dignitaries on Dais. Seen from L to R: Dr. Rajendra Ganatra (Speaker), CA Rahul Hakani (Chairman – Allied Laws Committee) and CA Vitang Shah (Convenor – Corporate Connect Committee)

Dr. Rajendra Ganatra (Speaker) addressing the participants. Seen from L to R: CA Premal Gandhi (Convenor – Corporate Connect Committee), CA Rahul Hakani (Chairman – Allied Laws Committee) and CA Vitang Shah (Convenor – Corporate Connect Committee)

Panel Discussion – Panellist seen from L to R: Mr. Ankoosh Mehta, Advocate (Moderator), Dr. Rajendra Ganatra, CA Abizer Diwanji and Ms. Jyoti Singh, Advocate .

Student Committee

Webinar on Hacks to Clear Chartered Accountancy Exam held on 29th September, 2017

CA Atul Bheda addressing the participants

CA Harshit Shah addressing the participants

International Taxation Committee

Lecture Meeting on Recent Developments in International Taxation held on 5th October, 2017 at Babubhai Chinoy Hall, IMC.

CA Rajesh P. Shah (Chairman) welcoming the Speaker. Seen from L to R: CA Kartik Badiani (Vice-Chairman), CA Himanshu Parekh (Speaker), Mr. Ajay R. Singh, Advocate (President), CA Rajesh L. Shah (Co-Chairman) and CA Shreyas Shah (Convenor)

CA Himashu Parekh addressing the participants

Indirect Taxes Committee jointly with IT Connect Committee

Half Day Seminar on GST Return Filing: Practical Issues: Q & A Session held on 16th September, 2017 at A. V. Room, Jain Hind College.

Mr. Ajay R. Singh, Advocate (President) giving opening remarks

CA Dinesh Tejwani (Chairman) welcoming the Speakers. Seen from L to R: CA Alok Jajodia (Moderator), CA Mitesh Katira (Speaker), Mr. Ajay R. Singh, Advocate (President), CA Ashit Shah and CA Atul Mehta (Vice-Chairman)

Speakers

CA Ashit Shah addressing the participants

Mr. Arvind Sinha (Officer from Central Tax Office) addressing the participants

CA Mitesh Katira addressing the participants

CA Alok Jajodia (Moderator) addressing the participants

Section of Delegates

International Taxation Committee jointly with Study Circle & Study Group Committee

Intensive Study Group on Overview of MLI and India's position on MLI (Part II) held on 15th September, 2017 at CTC Conference Room

CA Monika Wadhani addressing the participants

Direct Taxes Committee

Intensive Study Group meeting was held on 5th October, 2017 at CTC Conference Room

Mr. Harsh Kapadia, Advocate addressing the participants.

THE CHAMBER'S JOURNAL

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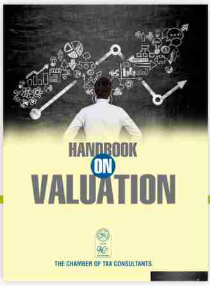

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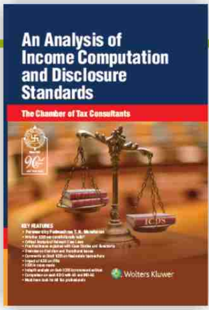

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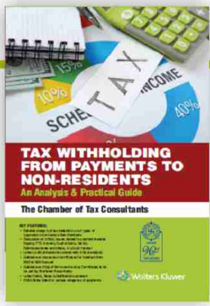

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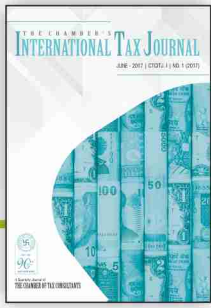

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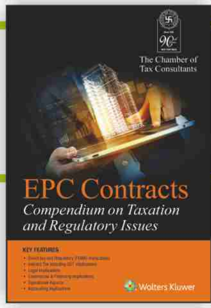

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