

General Anti-Avoidance Rule in India

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Government of India

Fourth IMF-Japan High-Level Tax Conference, Tokyo, 2013

Evolution of GAAR in India

- ❑ Diverse judicial decisions
- ❑ Draft Direct Taxes Code 2009 and DTC Bill 2010
- ❑ Income Tax Act, 1961 amended in 2012 to incorporate GAAR effective April 1, 2014
- ❑ A number of representations were received
- ❑ An Expert Committee on GAAR constituted to undertake stakeholder consultations and give report
- ❑ Expert Committee submitted its Final Report in September, 2012
- ❑ Government considers the Report and announces decision to bring modification
- ❑ Finance Bill, 2013 proposes to insert Chapter X-A in Income Tax Act, 1961

GAAR in India

- Finance Bill, 2013 proposes to insert Chapter X-A (Sec. 95–102) of Income Tax Act, 1961 effective 1-4-2016 (Ass. Year 2016–17) replacing the earlier provisions.
- Notwithstanding anything contained in the Act, an arrangement entered into by an assessee may be declared to be an *impermissible avoidance arrangement*, and the *consequence* in relation to tax arising there from may be determined subject to the provisions of this Chapter “(Sec. 95)”.
- The provisions of this Chapter may apply to any step in, or a part of the arrangement.

‘Impermissible Avoidance Arrangement’

- ❑ Means an arrangement, the *main purpose* of which is to obtain a *tax benefit*,
and it:
 - creates rights and obligations – not at arm’s length; or
 - results in abuse/misuse of provisions of this Act (directly/indirectly); or
 - lacks/is deemed to lack commercial substance; or
 - is carried out in a manner which is not ordinarily employed for *bona fide* purposes.
- ❑ Arrangements to be presumed mainly for benefit (unless proved otherwise by taxpayer) —if the main purpose is to obtain tax benefit—even though the main purpose of whole arrangement is not to obtain tax benefits.

'Deemed to Lack Commercial Substance'

- ❑ Substance/ effect of arrangement as a whole differs significantly from individual steps; (or its parts).
- ❑ It involves:
 - round trip financing;
 - accommodating party;
 - elements offsetting/cancelling each other;
 - disguising the value, location, source, ownership; or
- ❑ It involves the location of asset/residence of any party only for obtaining tax benefit; or
- ❑ It does not have a significant effect upon the business risks or net cash flows of any party to the arrangement.
- ❑ Relevant factors may include: time period/tax payment/exit route for determining lack of commercial substance.

Connected Person

Person connected directly/indirectly to another person, including:

1. Relative of an individual
2. Director/Director's relative in the case of a company
3. Partner/Member (or his or her relatives) in the case of firms
4. Member of HUF/his or her relative
5. Entities carrying businesses having substantial interest in other businesses or persons related to such entities

Consequences of Impermissible Avoidance Arrangement (IAA)

- ❑ Consequences of the arrangement shall be determined by keeping in view the circumstances of the case.
- ❑ Consequences, not exhaustive, include:
 - Disregarding/combining/recharacterizing IAA
 - Treating IAA as if not entered into
 - Disregarding accommodating party
 - Deeming persons connected as all one and the same
 - Reallocation among the parties to the arrangement any accrual, receipt, expenditure, etc.
 - Determining place of residence/situs of asset
 - Looking through the arrangement by disregarding any corporate structure.
- ❑ For this purpose:
 - Recharacterizing equity as debt, capital as revenue, and vice versa
 - Recharacterizing any expenditure, deduction, relief, or rebate

Structure of GAAR Regime Under Finance Bill—2013

- Sec. 95 – 100 : Basic GAAR Taxation Provisions
- Sec. 101 : Guidelines/conditions to be prescribed
- Sec. 102 : Definition of Terms
- Sec. 144 BA:(1) to (14) : Procedural aspects for applying GAAR
- Sec. 144 BA (15) – (20) : Provisions related to Approving Panel
- Sec. 144 BA (21) : Power to make rules related to Approving Panel

Indian GAAR – A Snapshot

“Main Purpose” is to Obtain a “Tax Benefit”

AND

Not at
“Arm’s Length”

OR

“Misuse/Abuse” of
Tax Provisions

OR

Lacks “Commercial
Substance”

OR

Not for Bona Fide
Purposes

Impermissible Avoidance Arrangement

Consequences

**Disregard/Re-
characterize the
Arrangement**

**Disregard
Corporate
Structure**

**Deny Treaty
Benefit**

**Reassign Place
of Residence/
Situs of Assets
or Transaction**

**Reallocate
Income,
Expenses,
Relief, etc.**

**Recharacterize
Equity-Debt,
Income-Expense,
Relief, etc.**

Applies to both Indian Residents and Non-Residents

GAAR: Procedure - I

- The Assessing Officer shall make a reference to the Commissioner.
- The Commissioner shall hear the taxpayer, and if he is satisfied with the reply of the taxpayer that the GAAR is not to be invoked, he shall pass order it accordingly and inform AO.
- If the taxpayer furnishes no objection, the Commissioner may issue such an order as deemed fit.
- If the Commissioner is not satisfied by the reply of taxpayer and is of the opinion that GAAR provisions are to be invoked, he shall refer the matter to a high-level Approving Panel.

GAAR: Procedure - II

Approving Panel

- ❑ The Approving Panel shall consist of:
 - a Chairperson who is/has been a Judge of a High Court;
 - one Member of the Indian Revenue Service not below the rank of Chief Commissioner of Income Tax; and
 - one Member who shall be an academic or scholar having special knowledge of matters such as direct taxes, business accounts, and international trade practices.
- ❑ AO shall decide after examining material and making any further inquiry
- ❑ Directions to be issued within a 6-month period shall give a hearing to taxpayer the and AO before giving directions

GAAR: Procedure – II (cont'd)

- ❑ The directions issued by the Approving Panel shall be binding on the assessee and the income tax authorities; there is no appeal against such directives.
- ❑ There may be one or more Approving panels.
- ❑ The final order shall be passed by AO only after obtaining the approval of the Commissioner.

Safeguards/ Proposed Guidelines

- ❑ Guidelines and conditions will be framed after the Finance Bill 2013 is passed.
- ❑ The following issues will require consideration:
 - i. Prescribing statutory forms for various procedures
 - ii. Prescribing time limits for various actions under GAAR by different authorities
 - iii. To ensue that same income is not taxed twice in the same taxpayer's hand
 - iv. Whether investment made before a certain date to be grandfathered from GAAR perspective
 - v. Whether to exempt any category from GAAR (e.g., FII not taking DTAA benefits, NRI investor in FII, etc.)

Safeguards/ Proposed Guidelines (cont'd)

- vi. Whether to prescribe a monetary threshold below which the GAAR would not apply
- vii. Where a part of the arrangement is an impermissible avoidance arrangement, whether the GAAR will be restricted to the tax consequence of that part which is impermissible and not to the whole arrangement
- viii. Where GAAR and SAAR are both in force, how the two will operate

THANK YOU!

Questions?