



Darya Ganj CPE Study Circle



SEMINAR ON GENERAL ANTI AVOIDANCE RULES (GAAR)

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Presented by

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INDEX OF CONTENT

- Tax Planning vs Tax Avoidance vs Tax Evasion
- Judicial approach to tax avoidance
- Introduction to GAAR Rules
- History of Indian GAAR
- GAAR under Income Tax Act, 1961
- GAAR Rules
- GAAR procedure
- Certain other issues
- GAAR around the world

GENERAL AVERSION TO PAY TAX



- Tax is as old as civilization itself !
- Tax resistance has probably existed ever since the beginning of civilization; imposition of tax
- Wikipedia page “List of historical acts of tax resistance” lists 330 revolts and revolutions caused due to tax
- Some of the prominent ones are
 - French Revolution, American Revolution
 - Dandi march (1930)

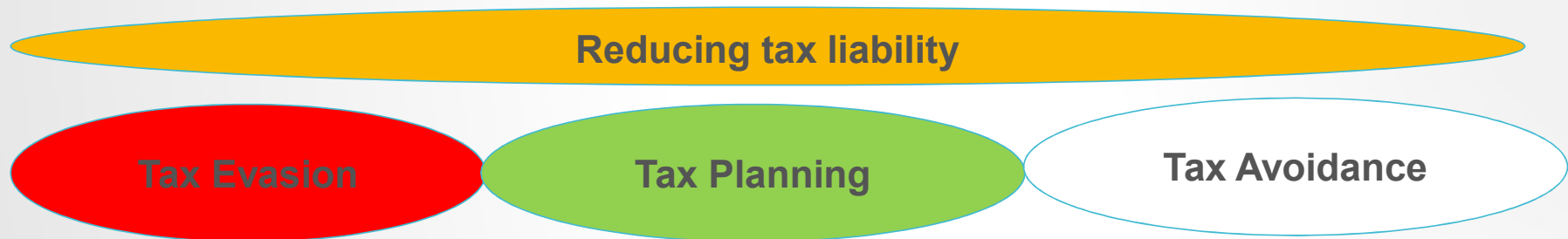
Tax Planning

Vs

Tax Avoidance

Vs

Tax Evasion



Tax evasion	Tax planning	Tax avoidance
Illegal and unacceptable	Legal	Not illegal per se – but “possibly” against the spirit of law
Availing tax benefits through unfair means	Availing tax benefits through compliance in law and in spirit	Availing tax benefits by taking advantage of loopholes in law
Stating an untrue statement knowingly, submitting misleading documents, suppression of facts, omission of material facts, etc.	Minimizing tax outgo by use of fiscal incentives available under tax legislation	Involves the legal exploitation of tax laws to one’s own advantage

TAX EVASION, PLANNING OR AVOIDANCE?



JUDICIAL APPROACH TO TAX AVOIDANCE

JUDICIAL APPROACH TO TAX AVOIDANCE

- **Duke of Westminster (1935): Westminster Principle**
 - Every man is entitled if he can, to order his affairs so that the tax 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.
- **Shah J in CIT Vs A Raman and Company (1967) 67 ITR 11 (SC)**
 - Avoidance of tax liability by so arranging commercial affairs that charge of tax is reduced is not prohibited
 - A taxpayer may resort to a device to divert the income before it arises or accrues to him.
 - Effectiveness of the device depends not upon considerations of morality, but on the operation of the Income-tax Act

JUDICIAL APPROACH TO TAX AVOIDANCE

- **Ramsay v IRC [1982] AC 300 – Ramsay Principle**
 - Where a transaction has pre-arranged artificial steps that serve no commercial purpose other than to save tax, the proper approach is to tax the effect of the transaction as a whole.
- **SC in McDowell (154 ITR 148), 5 member bench**
 - Tax planning is legitimate if within the framework of law
 - Colorable devices cannot be a part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods (4 member decision)
 - It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges
 - Principle in Duke of Westminster (taxpayer can arrange his affairs so as to reduce tax liability) is “dead”, principle in Ramsay (tax avoidance schemes not to be ignored) is the right approach (fifth member – Justice Chinnappa Reddy)

JUDICIAL APPROACH TO TAX AVOIDANCE

- **SC in Azadi Bachao (263 ITR 706)**
 - An act which is otherwise valid in law cannot be treated as *non est* merely on the basis of some underlying motive supposedly resulting in some economic detriment or prejudice to the national interests
 - Citizen is free to carry on his business within the four corners of law and tax planning, without any motive to evade taxes through colorable device is not frowned upon
- **SC in Vodafone case**
 - Westminster principles continues - Departure only in case of artificial/colourable device
 - No conflict between Ramsay, Westminster, McDowell and Azadi
 - Taxpayer entitled to arrange its affairs so as to reduce tax incidence
 - Legitimate tax planning within the framework of law is permissible.
 - Colourable devices cannot form part of tax planning
 - Ramsay doctrine not discarded – but merely applied it in the context of a colourable device

INTRODUCTION TO GAAR

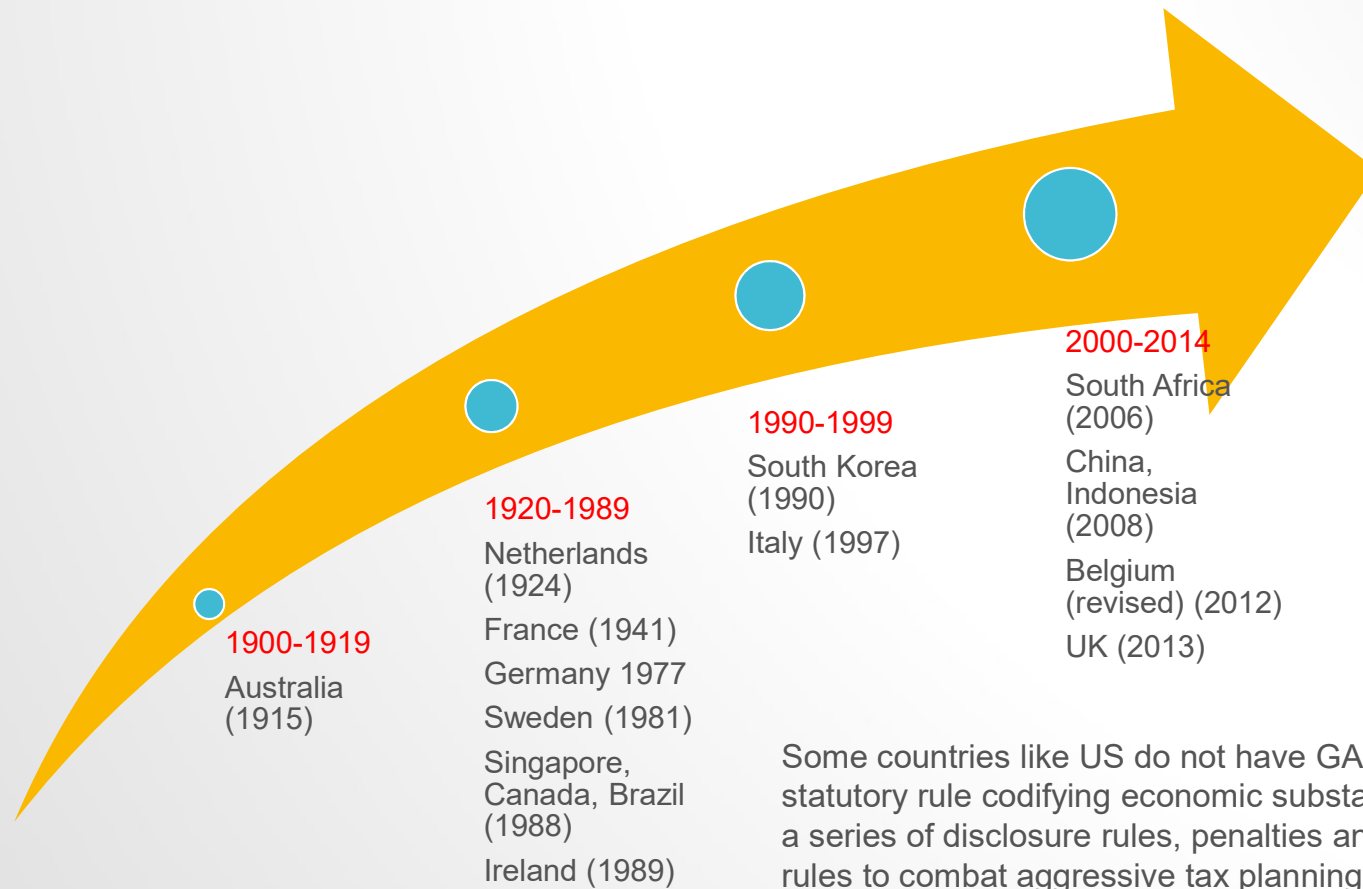
GAAR DEFINITION

- An anti-avoidance measure, generally statute based, providing criteria of general application. i.e. not aimed at specific taxpayers or transactions, to combat situations of perceived tax avoidance – IBFD International Tax Glossary (Revised 6th Edition)
- A general anti-avoidance rule (GAAR) is a set of broad principles-based rules within a country's tax code designed to counteract the perceived avoidance of tax.
- GAAR is a concept within law that provides the taxing authority a mechanism to deny the tax benefits of transactions or arrangements believed not to have any commercial substance or purpose other than to generate the tax benefit(s) obtained – EY Report GAAR Rising (Feb 2013)

WHY GAAR?

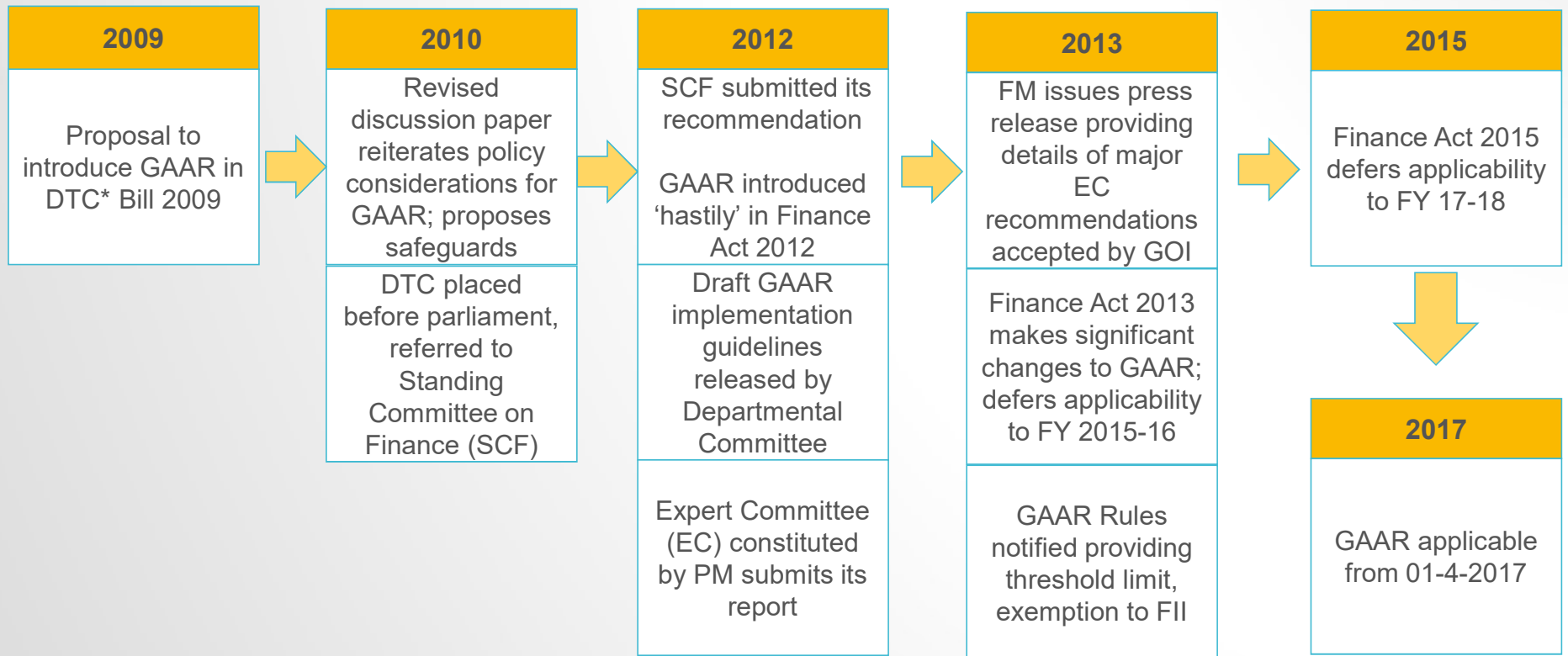
- Increased focus on tax avoidance across the world
- Tax avoidance viewed as a 'moral crime'; a breach of social obligation
- Tax avoidance and tax evasion a global issue
 - Impacts developed and developing countries
- Objectives of GAAR
 - Codify meaning of what constitutes abuse or avoidance of tax
 - Target transactions which give tax benefits but are against spirit of law
 - Provide the tax authority with a mechanism to eliminate the tax benefits claimed
 - Allow the imposition of special assessments, penalties and interest where violations are determined

GAAR AROUND THE WORLD - TIMELINE



HISTORY OF INDIAN GAAR

EVOLUTION OF INDIAN GAAR



GAAR UNDER INCOME TAX ACT - OVERVIEW

Section	Particulars
Section 95	<ul style="list-style-type: none">• Non obstante section – overrides the entire ITA• GAAR applicability - Arrangement may be declared to be an impermissible avoidance arrangement
Section 96	<ul style="list-style-type: none">• What is an Impermissible Avoidance Arrangement (IAA)
Section 97	<ul style="list-style-type: none">• When can an Arrangement be deemed to lack commercial substance
Section 98	<ul style="list-style-type: none">• Consequence of Impermissible Avoidance Arrangement
Section 99	<ul style="list-style-type: none">• Treatment of connected person and accommodating party
Section 100	<ul style="list-style-type: none">• Clarifies GAAR is applicable in addition to or in lieu of any other basis for determination of tax liability
Section 101	<ul style="list-style-type: none">• Power of CBDT to notify guidelines and conditions subject to which GAAR can be applied
Section 102	<ul style="list-style-type: none">• Definitions
Section 144BA	<ul style="list-style-type: none">• GAAR procedure

SECTION 95 - IMPERMISSIBLE AVOIDANCE ARRANGEMENT (IAA)

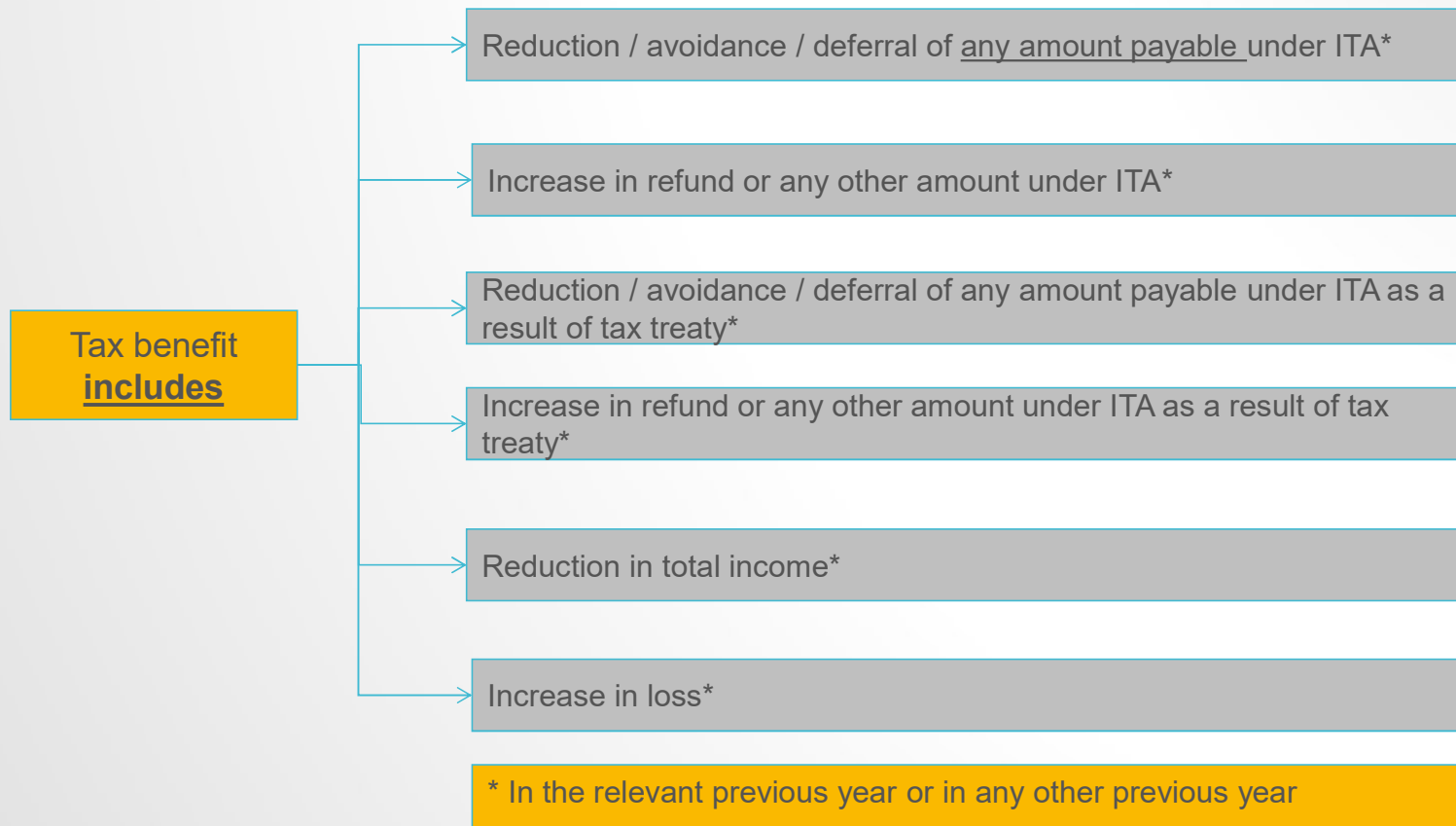
- Basic section that provides the tax authority power to declare an arrangement entered into by a tax payer as an impermissible avoidance arrangement
- Overrules the entire Act “*Notwithstanding anything contained in the Act ...*”
- Sec 90(2A) - Specifically provides that GAAR provisions will apply even in cases where relief is DTAA

APPLICABILITY THRESHOLD

Rule 10U - In cases where tax benefit in an AY, in aggregate, to all the parties to the arrangement does exceed

Rs. 3 crores.

SECTION 102(10) - TAX BENEFIT



TAX BENEFIT

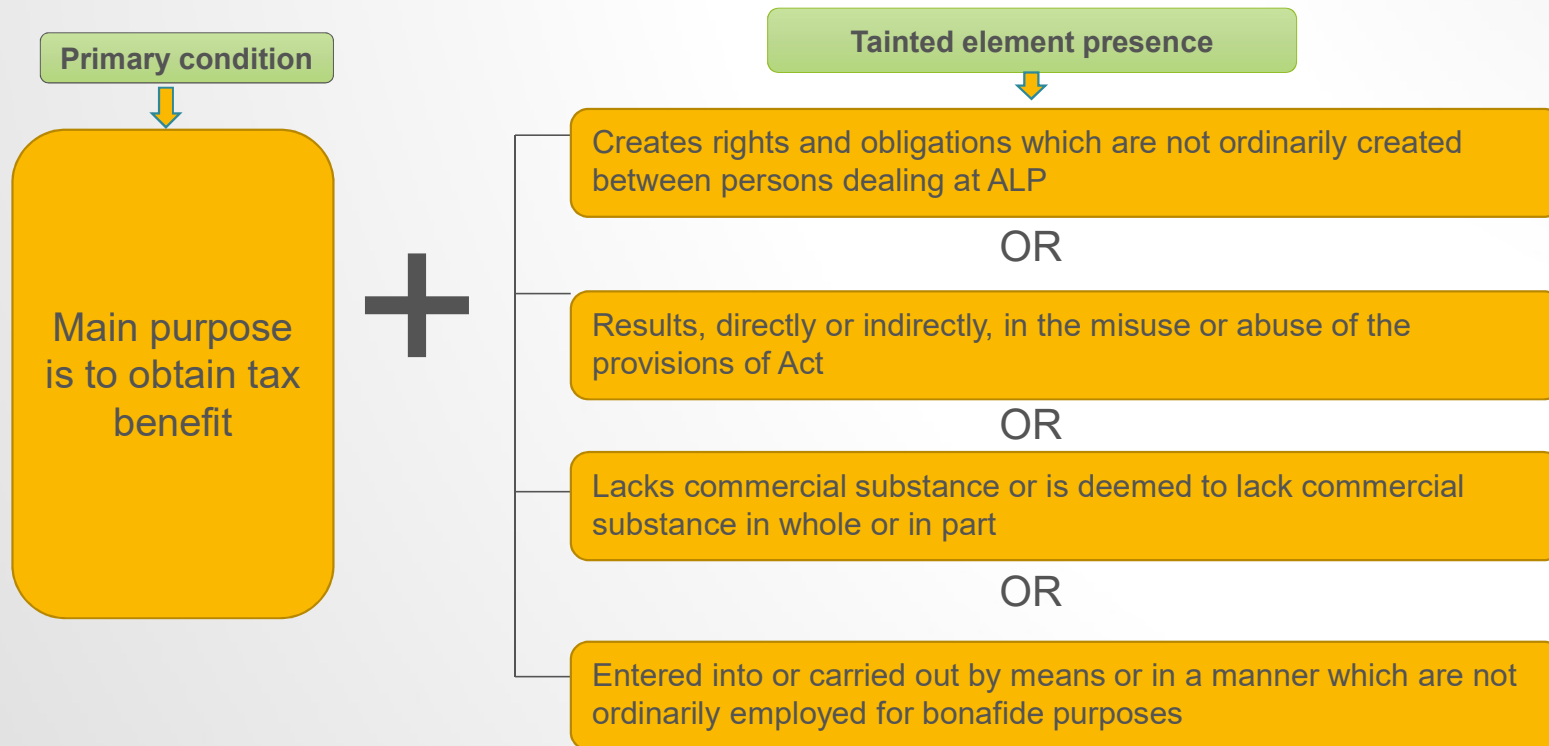
- Tax benefit covers any amount payable under ITA
 - Covers interest, penalty, income tax, Minimum Alternate Tax, TDS
 - EC had recommended that only tax amounts be reckoned for determining tax benefit – **NOT ACCEPTED**
- Whether availing incentive provisions under ITA is a “tax benefit”?
- No guidelines on computation of tax benefit in case of tax deferral
 - EC had recommended tax benefit be determined w.r.t present value in case of tax benefit
- Can tax benefit cover notional income?
 - Non charging of interest on loan to subsidiary
- Can tax authority allege tax benefit to one of the parties and apply GAAR when no tax benefit arises on a combined basis?
 - EC had recommended non applicability of GAAR to intra group transactions without overall tax benefit - **NOT ACCEPTED**

TAX BENEFIT COMPUTATION - ILLUSTRATION

- Situation 1 – Group tax neutrality
 - A Co makes payments of Rs 10 crores to its group company for various services like HR, IT, accounting, management fee etc which reduces the profit of A Co which is offered to tax by B Co
 - Tax authority may apply GAAR only on A Co and consider tax benefit on a stand alone basis
 - Rule 10U(1)(a) suggests tax benefit is to be determined in aggregate to all the parties of the arrangement – no tax benefit in this case on an overall basis
 - EC recommended that intra group transactions which are tax neutral be kept out of GAAR purview
- Situation 2 – Deferral of tax
 - A Co borrows Rs 100 crores from Mr A – interest payable is claimed by A Co as a deduction in FY 2015-16 but Mr A offers it to tax on receipt basis on actual receipt in FY 2018-19
 - Tax benefit covers deferral of tax
 - Tax benefit = entire amount of tax deferred?
 - EC recommended that tax benefit should be computed on net present value of money based on interest rates charged under ITA

SECTION 96 - IMPERMISSIBLE AVOIDANCE ARRANGEMENT (IAA)

An arrangement is an IAA if:



MAIN PURPOSE

- GAAR applicable only if main purpose of arrangement is to obtain a tax benefit
- if taxpayer can demonstrate other benefits which are more important than tax benefit, GAAR may not apply
- Para 27 of 2011 UN Model Commentary to Article 1
 - “the determination of whether a main purpose for entering into transactions or arrangements is to obtain tax advantages should be based on an objective determination, based on all the relevant facts and circumstances, of whether, without these tax advantages, a reasonable taxpayer would have entered into the same transactions or arrangements”.
- Some dictionary meanings:
 - ‘Main’ – chief in size or extent; constituting the bulk; the chief part; of pre-eminent importance; principal; chief; leading
- The “quantum” of tax benefit vis-à-vis other parameters are seen by the Courts to determine whether the ‘main purpose’ was to obtain a tax benefit

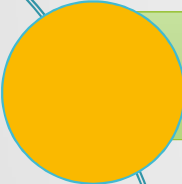
ARRANGEMENT

- Section 102(1) - “arrangement” means 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
 - Wide scope of definition may include business, non business as well as personal dealings, written as well as oral, constructive, deemed etc
- Tax authority has power to apply GAAR to “part” of the arrangement
 - Rule 10UA clarifies that where part of arrangement is regarded as IAA, tax consequences restricted to such part

SECTION 96(2) - ONUS OF PROOF


- Sec 96 (2) An arrangement shall be presumed,
 - unless it is proved to the contrary by the assessee,
 - to have been entered into, or carried out, for the main purpose of obtaining a tax benefit,
 - if the main purpose of a step in, or a part of, the arrangement is to obtain a tax benefit,
 - notwithstanding the fact that the main purpose of the whole arrangement is not to obtain a tax benefit.
- Onus of AO – Prove a step or part has main purpose of tax benefit
- Presumption – Presumed whole arrangement's main purpose is tax benefit unless proven contrary by assessee
- Eg – TATA Motors acquisition of Jaguar through Singapore entity

SEC - 97 - ARRANGEMENT LACKING COMMERCIAL SUBSTANCE



Substance/ effect of arrangement as a whole is inconsistent with or differs significantly from its individual steps or parts

OR



It involves or includes

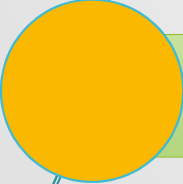
a) Round trip financing (see next slide)

b) Accommodating party (see next slide)

c) Offsetting or self cancelling elements

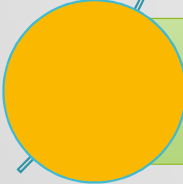
d) Transaction which disguises value, location, source, ownership or control of funds which are subject matter of transaction

OR



It involves location of an asset /transaction /place of residence of any party which would not have been so located for any substantial commercial purpose other than obtaining a tax benefit

OR



It does not have a significant effect on business risk or net cash flows of any party to the arrangement apart from the tax benefit that would be obtained

SEC - 97 - ARRANGEMENT LACKING COMMERCIAL SUBSTANCE

Round trip financing includes
[Section 97(2)]

- Transfer of funds among parties to the arrangement in a series of transactions
- **AND**
- such transactions do not have any substantial commercial purpose other than obtaining a tax benefit
- No regard given to whether funds can be traced, time and sequence of transfer or the means, manner and mode in which funds are transferred

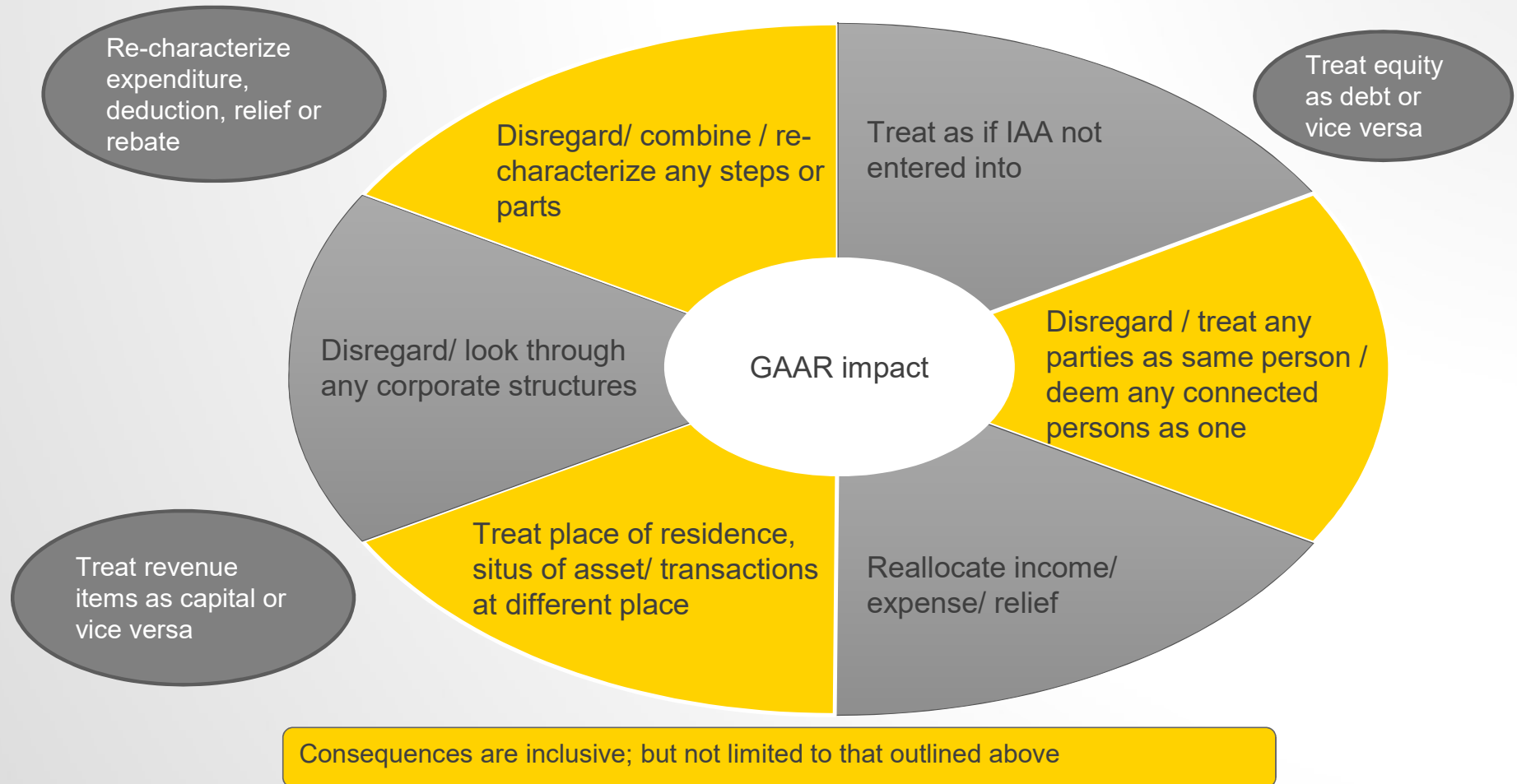
Accommodating party
[Section 97(3)]

- If the main purpose of direct or indirect participation of a party to the arrangement in whole or in part is to obtain a tax benefit directly or indirectly for the taxpayer
- Applies irrespective of whether the party is a connected person in relation to any of the parties to the arrangement

SEC - 97 - ARRANGEMENT LACKING COMMERCIAL SUBSTANCE

- Following factors may be relevant but not sufficient while determining whether an arrangement lacks commercial substance :
 - Period or time for which the arrangement (including operations therein) exists
 - Fact of payment of taxes, directly or indirectly, under the arrangement
 - Fact that an exit route (including transfer of any activity or business or operations) is provided by the arrangement
- As per FA 2012 these factors were not to be taken into account while determining if an arrangement lacks commercial substance
- FA 2013 amendment impact – less harsh when compared with FA 2012 amendment; nevertheless, taxpayers need to produce additional supporting evidence to establish commercial substance

SECTION 98 - CONSEQUENCES OF GAAR



SECTION 99 - TREATMENT OF CONNECTED PERSON AND ACCOMMODATING PARTY

- Following powers available with tax authority in determining whether a tax benefit exists:

Treat parties who are connected persons as one and the same person

Disregard an accommodating party

Treat accommodating party and other party as the same person

Disregard any corporate structure by looking through the arrangement

RECAP..

- GAAR applicability – main purpose test + tainted element test
- Tainted element test (One of the four conditions)
 - Creates rights and obligations which are not ordinarily created between persons dealing at ALP
 - Results, directly or indirectly, in the misuse or abuse of the provisions of Act
 - Lacks commercial substance or is deemed to lack commercial substance in whole or in part
 - Entered into or carried out by means or in a manner which are not ordinarily employed for bonafide purposes
- Definitions of tax benefit, arrangement lacking commercial substance, arrangements deemed to lack commercial substance
- Wide powers to tax authority

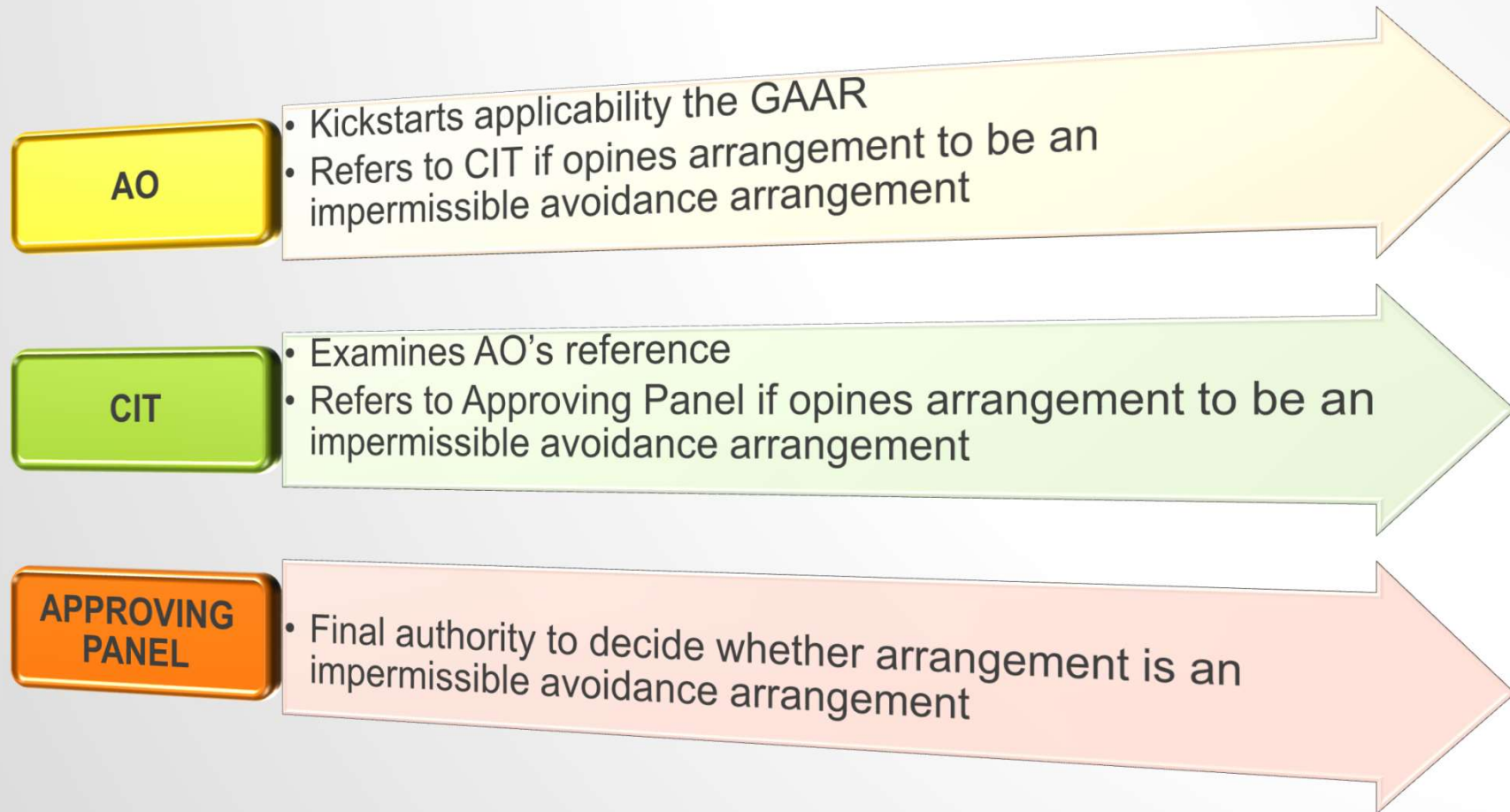
GAAR RULES

GAAR RULES, APPLICABILITY OF GAAR

- **Rule 10U(1)(d) - Investment made before 01-04-2017**
- Income derived from transfer of investments made prior to 01-04-2017 to be grandfathered and protected from GAAR and governed by normal provision of ITA
- Shares brought into existence by way of split or consolidation of holdings, or by bonus issuances in respect of shares acquired prior to 1st April 2017 in the hands of the same investor would also be eligible for grandfathering
- **Rule 10U(2) – Arrangement made before 01-04-2017**
- Tax benefit on or after 01-04-2017 from an arrangement – GAAR Applicable
- Immaterial whether arrangement entered before or after 01-04-2017

GAAR PROCEDURE

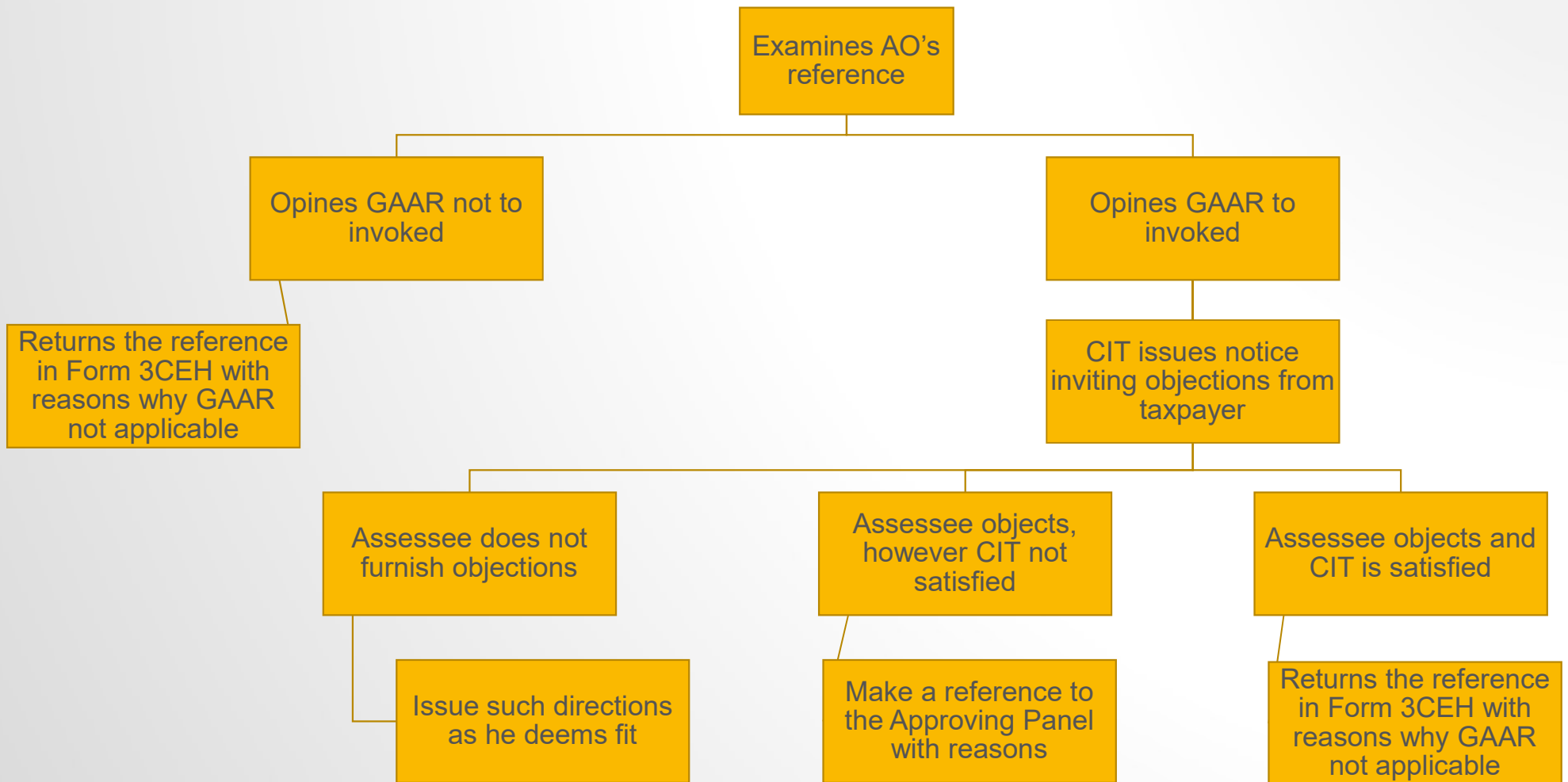
SECTION 144BA - GAAR PROCEDURE - OVERVIEW



SECTION 144BA - ASSESSING OFFICER

- AO during the course of assessment or reassessment proceedings
 - considers that it is necessary to declare an arrangement as an impermissible avoidance arrangement
 - make a reference to the CIT in Form No. 3CEG.
- Before making a reference to the Commissioner, grant the assessee an opportunity of being heard through issue of a notice in writing for seeking his objections
- Notice shall contain the following –
 - Details of the arrangement proposed to be declared as an IAA
 - The tax benefit arising under the arrangement
 - The basis and reason for considering that the main purpose of the identified arrangement is to obtain tax benefit
 - The basis and the reasons why the arrangement is an IAA as per section 96 of the Act
 - the list of documents and evidence relied upon by the AO

SECTION 144BA - CIT



SECTION 144BA - APPROVING PANEL

- Composition of AP
 - Chairperson who is or has been a judge of HC
 - One member from IRS not below rank of CCIT/Principal Chief Commissioner (PCC)
 - One member shall be an academic or scholar having special knowledge of matters, such as direct taxes, business accounts and international trade practices
- AP can issue such directions as it deems fit in respect of declaration of an arrangement as an IAA specifying previous years for which such directions apply
 - Directions issued after giving taxpayer and AO an opportunity of being heard
 - Power to institute further enquiry, call for records
 - AP has powers of a civil court similar to powers vested in AAR
- AP members differ in opinion - Opinion of majority to prevail

SECTION 144BA - AO TO COMPLETE ASSESSMENT

- AO, on receipt of directions of
 - CIT [u/s 144BA (3) of the Act] or
 - the Approving Panel [section 144BA (6)],
- shall proceed to complete the assessment or reassessment proceedings in accordance with such directions and the provisions of Chapter X-A.
- Where direction of Approving Panel specifies that the IAA is applicable for any other AY,
 - AO to complete assessment or reassessment proceedings of such other AY in accordance with Approving Panel's directions.
 - No need for AO to seek fresh direction on the issue for the such other AY.
- Section 144BA(12) - If any tax consequences have been determined by invocation of GAAR provisions, such assessment or reassessment order shall be passed with prior approval of CIT.

SECTION 144BA - APPEAL

- Appeal against directions of AP – Section 144BA(14)
 - **Directions of AP binding both** on assessee and income-tax authorities
 - Notwithstanding anything contained in any other provision of the Act, no appeal under the Act shall lie against such directions.
- Section 253 provides that where tax consequences have been determined by invoking GAAR provisions, appeal directly to ITAT
- However, ITAT can't examine directions of AP
- ITAT can only examine direction by CIT under section 144BA(3)

Ques - Since, no appeal possible under Act, whether AP's directions would be FINAL ??

Ans – No. May exercise Constitutional remedy under Article 226 by approaching High Court under its Writ jurisdiction

TIME LIMITS IN GAAR PROCEDURE

Action	Time limit for action
Issue of notice by Tax Authority to taxpayer seeking objection, if any, on application of GAAR	Not specified
Reference by Tax Authority to the Commissioner	Not specified
Commissioner is satisfied that GAAR is not to be invoked based on reference by Tax Authority	One month from the end of the month in which the reference from Tax Authority is received
Commissioner is of the opinion that GAAR applies and notice to be issued to the taxpayer to submit objections, if any	As specified in the notice, not to exceed 60 days
Where taxpayer does not raise any objections, Commissioner to issue such directions as he deems fit for Tax Authority to apply GAAR	One month from end of the month in which time permitted for taxpayer to raise objections before the Commissioner
Commissioner is satisfied that GAAR provisions are not to be invoked based on response by taxpayer	Two months from end of month in which final submission of taxpayer is received by the Commissioner
Commissioner records satisfaction that GAAR applies and makes a reference to Approving Panel	
Approving Panel gives directions as appropriate	Six months from the end of the month in which reference from Commissioner is received excluding any court stay, time taken to obtain information from competent authority outside India

CERTAIN OTHER
ISSUES

CERTAIN OTHER ISSUES

ISSUE 1 – GAAR vs SAAR

View 1 – GAAR will apply regardless of SAAR

- ▶ GAAR starts with non obstante clause
- ▶ Sec. 100 states “The provisions of this Chapter shall apply in addition to, or in lieu of, any other basis for determination of tax liability”

View 2 – where SAAR is applicable, GAAR will not apply

- ▶ Specific provision (lex specialis) prevails over general provision (lex generalis)

CBDT in Circular No.7 of 2017 dated 27-1-2017 while answering the question "Will GAAR be invoked if SAAR applies?" said that -

'It is internationally accepted that specific anti avoidance provisions may not address all situations of abuse and there is need for general anti-abuse provisions in the domestic legislation. The provisions of GAAR and SAAR can coexist and are applicable, as may be necessary, in the facts and circumstances of the case.'

CERTAIN OTHER ISSUES

ISSUE 2 – GAAR vs DTAA

- Section 90(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*

ISSUE 3 – GAAR vs DTAA in which LOB clause exists

- Dr. Shome Committee suggested non applicability of GAAR to deny treaty benefits where treaty has LOB clause
- CBDT in Circular No.7 of 2017 dated 27-1-2017 said adoption of 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 domestic anti-avoidance rules. If a case of avoidance is sufficiently addressed by LOB in the treaty, there shall not be an occasion to invoke GAAR.

CERTAIN OTHER ISSUES

ISSUE 4 – Will GAAR interplay with the right of the taxpayer to select or choose method of implementing a transaction?

- CBDT in Circular No.7 of 2017 dated 27-1-2017 said GAAR will not interplay with the right of the taxpayer to select or choose method of implementing a transaction.

ISSUE 5 – Will GAAR be invoked if arrangement is sanctioned by an authority such as the Court, NCLT?

- CBDT in Circular No.7 of 2017 dated 27-1-2017 said that where the Court has explicitly and adequately considered the tax implication while sanctioning an arrangement, GAAR will not apply to such arrangement.

CERTAIN OTHER ISSUES

ISSUE 6 – Compensating adjustments – If adjustment is made on one of the party, whether there would be corresponding adjustment in the hands of another party.

- CBDT in Circular No.7 of 2017 dated 27-1-2017 said that if adjustment is made in the hands of one of the party as a result of GAAR, corresponding adjustment in the hands of another participant will not be made.
- GAAR is an anti-avoidance provision with deterrent consequences and corresponding tax adjustments across different taxpayers could militate against deterrence.

GAAR AROUND THE
WORLD

GAAR AROUND THE WORLD

Particulars	South Africa	UK	Canada	Australia
Onus of proof	Tax authority	Tax authority	Taxpayer to prove no tax benefit or no avoidance transaction; Tax authority to show abuse or misuse.	Taxpayer
Obligation to provide counter factual	No need to provide counter factual	Yes, such alternative need not be the one which gives rise to highest tax liability	Generally, yes (as part of judge made law) – but, not a statutory mandate	Yes

GAAR AROUND THE WORLD

Particulars	South Africa	UK	Canada	Australia
Corresponding adjustment for counterparty	Yes as part of Act (between assesses)	Present	Yes as part of Act as also examples	Yes, as part of Act as also example. (between assesses)
Does GAAR override treaty	Tax treaty benefit subject to GAAR	GAAR can be used against abusive arrangements under the treaty	Treaty benefit subject to GAAR.	Treaty benefit subject to GAAR
Interplay with SAAR	SAAR is applied first as a rule – GAAR will apply if abuse not addressed by SAAR	If abuse addressed by Targeted Anti Avoidance Rules, GAAR will not apply – else, GAAR will apply	SAAR is applied first as a rule	SAAR is applied first as a rule

A grayscale world map is shown in the background, centered on the Atlantic Ocean. The word "QUESTIONS?" is written in a large, bold, black, sans-serif font across the middle of the map.

QUESTIONS?

THANK YOU



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