

Budget should throw fresh light on GAAR and BEPS

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By TIOL Edit Team

TIME

has come for the Finance Ministry to revisit twice-deferred General Anti Avoidance Rule (GAAR) under Income-Tax Act keeping in view latest developments abroad.

Three such major developments are: 1) International Monetary Fund's (IMF's) technical note introducing GAAR issued on 3 rd February 2016; 2) European Commission's anti-avoidance directive dated 28 th January 2016 factoring in final package of Base erosion and profit shifting (BEPS) and 3) Australia's amendments to its GAAR to factor BEPS concerns.

Final BEPS package was issued by Organisation for Economic Co-operation and Development (OECD) in October 2015 and later endorsed by G20 Summit. India, as G20 member, is committed to implementing BEPS package.

Another reason why the Ministry should rework GAAR is its plan to phase-out many tax incentives. This coupled, with any specific anti-avoidance rules (SAAR), should pave way for smaller, simpler and effective GAAR.

The Ministry might like to compare the notified but deferred GAAR with the sample GAAR that appears as annexure in IMF's technical note. It would be prudent on part to see how Australia has made its GAAR compliant with BEPS package.

As put by the IMF note,

"Whatever the form of a GAAR, it should give effect to a policy that seeks to strike down blatant, artificial or contrived arrangements which are tax driven. However, the GAAR should be designed and applied so as not to inhibit or impede ordinary commercial transactions in respect of which taxpayers can legitimately take advantage of opportunities available to them when structuring or carrying out those transactions."

A more relevant observation made in the technical note relates to GAAR's applicability to bilateral treaties. The Note says: ***"A GAAR when introduced in domestic law needs to be carefully designed and drafted to achieve consistency with the country's existing international legal obligations such as those embodied in existing tax treaties."***

This has direct implication for 'treaty shopping' loopholes that India created by design or oversight in different bilateral Double Taxation Avoidance agreements (DTAA). The Ministry must expedite completion of negotiations with concerned countries to amend respective DTAAs to prevent aggressive tax avoidance strategies by multinational corporations.

India, for instance, must complete immediately its negotiations with Mauritius for amending bilateral DTAC. The negotiations have dragged for almost a decade under the framework of a Joint Working Group (JWG).

Any further laxity in amending DTAAs might be construed by GAAR-committed countries as India's unwillingness to embrace BEPS in letter and spirit.

A generic concern on this count has already been emphatically stated by European Commission (EC). In its recommendations to EU member states on the implementation of measures against tax treaty abuse, EC observes:

"Tax treaties should not create opportunities for non- or reduced taxation through treaty shopping or other abusive strategies which only frustrate the purpose of such conventions and undermine the tax revenues of the Contracting States. The European Commission lends its full support to the efforts to tackle tax treaty abuse."

EC, in its recommendations/directive has also pitched for General anti-avoidance rule based on a principal purpose test (PPT).

With this background in view, corporate tax payers would naturally expect Finance Minister Arun Jaitley to provide fresh insights into India's maiden GAAR regime. When would it be revised for implementation with effect from 31 March 2017, a revised timeline that was announced by Mr. Jaitley in 2015-16 budget?

Noting the concern voiced by stakeholders over GAAR, the Budget indicated that the Government would like to incorporate in GAAR the final BEPS recommendations from OECD.

The budget documents stated:

"Accordingly, it is proposed that implementation of GAAR be deferred by two years and GAAR provisions be made applicable to the income of the financial year 2017-18 (Assessment Year 2018-19) and subsequent years by amendment of the Act. Further, investments made up to 31.03.2017 are proposed to be protected from the applicability of GAAR by amendment in the relevant rules in this regard."

Apart GAAR, there are several other elements of BEPS. The forthcoming Budget should thus shed some light on the timelines for implementation of 15 action points of BEPS package.

Put simply, Mr. Jaitley must strike a balance between wooing investment and plugging revenue leakages. We expect him to keep in mind the trade-off between additional investments and additional revenue.