



## GENERAL ANTI AVOIDANCE RULES

INSERTED BY FINANCE ACT 2012 AS AMENDED BY FINANCE ACT 2013

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# GENERAL ANTI AVOIDANCE RULES

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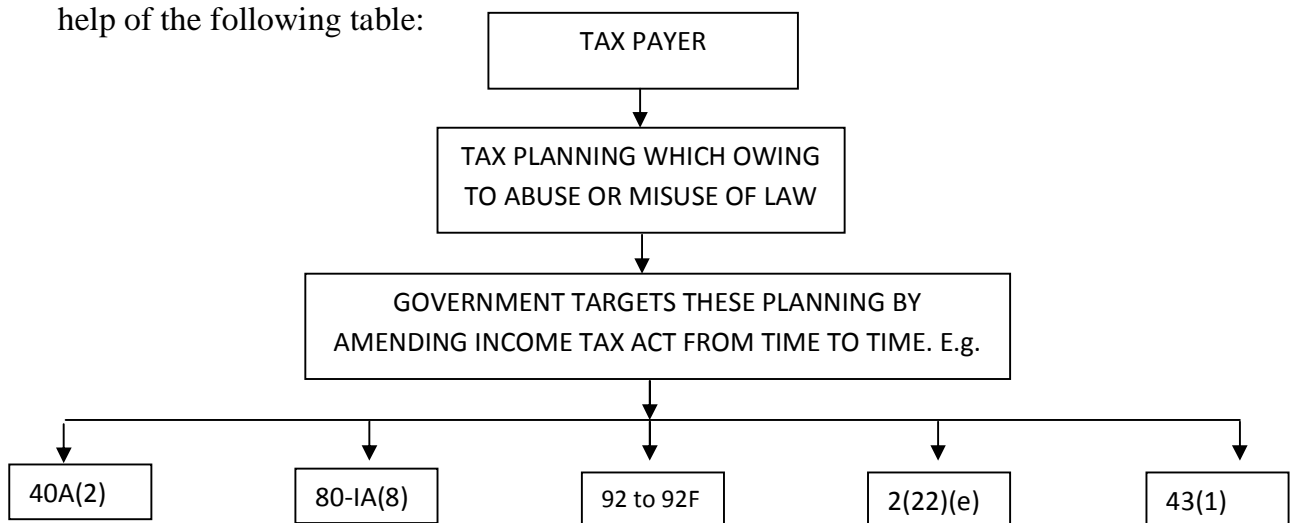
## INTRODUCTION

Tax Evasion and avoidance is a main problem in every country. Taxpayer can choose any tax efficient method but that method should not for the purpose to obtain tax benefit. General Anti Avoidance Rules (*hereinafter referred to as GAAR*) has been introduced by Government to overcome from these problems. GAAR provisions aims at reducing or preventing “impermissible tax avoidance”.

These provisions were made applicable by the Finance Act, 2012 with effect from 1-4-2014 (i.e., assessment year 2014-15). Since a number of representations were received against the GAAR, an expert committee (Shome Committee) was appointed. The Shome Committee submitted its report. Based on the report, certain decisions to make amendments to GAAR were announced by Government on 14-1-2013. Thus, amendments to GAAR were expected in the Finance Act, 2013. And true to expectations, the Finance Act, 2013 has substituted Chapter X-A with a new Chapter X-A with effect from assessment year 2016-17.

GAAR is intended to target tax evaders, especially Indian companies and investors trying to route investments through Mauritius or other tax havens in order to avoid taxes. GAAR is typically a statutory rule that empowers a revenue authority to deny taxpayers the benefit of an arrangement that they have entered into for an impermissible tax-related purpose.

Presently, Indian income tax act contains Specific Anti Avoidance rules (*hereinafter referred to as SAAR*) to prevent tax avoidance. This can be better understood with the help of the following table:



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Now let us understand the purpose for which GAAR was introduced and how it was framed:

### **PURPOSE OF GAAR**

The purpose of GAAR was first time explained by the New Zealand Court. In case of *CIR v. BNZ Investments [2002] 1 NZLR 450*, the court held that:

- GAAR is an essential pillar of the tax system.
- It provides a line between legitimate tax planning and improper tax avoidance

The purpose was also further explained by explanatory memorandum to finance bill, 2012:

- Apart from specific anti-avoidance provisions, general anti-avoidance has been dealt only through judicial decisions in specific cases.
- Legal form should be dispensed with & taxation provisions should be applied on substance of a transaction.

Therefore, there is a need for statutory provisions 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.

### **APPLICABILITY OF GAAR**

- Finance Act, 2012 amended the Income-tax Act by inserting new Chapter X-A titled 'General Anti- Avoidance Rule' comprising sections 95 to 102. These provisions were made applicable by the Finance Act, 2012 with effect from 1-4-2014 (*i.e.*, assessment year 2014-15).
- An expert “Shome Committee” was appointed. Certain decisions regarding amendments to GAAR were announced by Government on 14-1-2013 based on the Committee report.
- The Finance Act, 2013 has substituted Chapter X-A with a new Chapter X-A with effect from assessment year 2016-17, thus deferring application of GAAR by 2 years.
- GAAR is Applicable to all assessees, whether companies, firms, trust or individuals (section 95); & is applicable irrespective of the residential status of the assessee.

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The main objective of GAAR is to dispense the taxpayer characterization of transaction for tax purposes, but to look for a real substance in the transaction.

The applicability of GAAR depends upon following terms:

TAX EVASION	TAX MITIGATION	TAX AVOIDANCE
<p>The OECD has defined 'tax evasion' as encompassing 'illegal arrangements through or by means of which liability to tax is hidden or ignored,'</p> <p><i>Examples-</i> A deliberate failure by a 'cash' business to report the full amount of revenue received or the deliberate claiming of a deduction by a business for expenditure it has neither incurred nor paid.</p>	<p>'Tax planning' or 'Tax Mitigation' is concerned with the organization of a taxpayer's affairs (or the structuring of transactions) so that they give rise to the minimum tax liability within the law</p> <p><i>Example-</i> Setting up of a business undertaking by a taxpayer in a Special Economic Zone (SEZ). In such a case the taxpayer is taking advantage of a fiscal benefits offered to him by the Income-tax Act, use of an individual savings account; transfer of wealth or assets between spouses.</p>	<p>Income tax is avoided and a tax advantage is derived from an arrangement when the taxpayer reduces his liability to tax without involving him in the loss or expenditure which entitles him to that reduction.</p> <p>In this there is "impermissible tax avoidance".</p> <p><i>Example-</i> Individuals receiving income as a non-re-payable loan to avoid income-tax.</p>

GAAR applies to **tax avoidance** which is an **"impermissible avoidance arrangement"**.

The following Table summarizes the meanings of 'tax evasion', 'tax avoidance' and 'tax mitigation' and applicability of GAAR to them:

	Meaning	GAAR's Applicability
Tax Evasion	Tax evasion is generally the result of illegality, suppression, misrepresentation and fraud.	The GAAR provisions do not deal with cases of tax evasion. Tax evasion is clearly distinct from tax avoidance and is already prohibited under the current provisions of the Income-tax Act.
Tax Avoidance	Tax avoidance is the result of actions taken by the assessee, none of which or no combination of which is illegal or	GAAR applies to tax avoidance which is an <i>impermissible avoidance arrangement</i> .

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	forbidden by the law itself.	
Tax Mitigation	"Tax mitigation" is a situation where the taxpayer takes advantage of a fiscal incentive afforded to him by the tax legislation by actually submitting to the conditions and economic consequences that the particular tax legislation entails.	Tax mitigation, as distinct from tax avoidance, is allowed under the tax statute. The GAAR provisions also do not deal with case of tax mitigation.

SOME IMPORTANT FACTS FOR INDIAN GAAR

- 1. Onus:** Onus is on the assessing officer to show that a particular act is an impermissible tax avoidance arrangement.
- 2. What happens to investments made before GAAR comes into force?**
  - The Expert Committee's Final Report has recommended that *"All investments (though not 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 on exit (sale of such investments) on or after this date, GAAR provisions are not invoked for examination or denial of tax benefit."*
  - However, Government's Press Release dated 14-1-2013 states that Government has decided that *"Investments made before August 30, 2010, the date of introduction of the Direct Taxes Code Bill, 2010, will be grandfathered."*
- 3. Whether any monetary threshold limit will apply for invoking GAAR?**
  - The Press Release dated 14-1-2013 and opinion of expert committee states that *"A monetary threshold of Rs. 3 crore of tax benefit in the arrangement will be provided in order to attract the provisions of GAAR."*
  - In case of tax deferral, tax benefit shall be determined based on the present value of money.
- 4. Will same income be double taxed by invoking GAAR?**

The Press Release dated 14-1-2013 clarifies that *"it will be ensured that the same income is not taxed twice in the hands of the same tax payer in the same year or in different assessment years."*

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**5. Whether GAAR can be invoked where SAAR is applicable?**

Govt. Press Release dated 14-1-2013 states that "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."

**6. Applicability of GAAR to FIIs and non-resident investors in FIIs?**

The Press Release dated 14-1-2013 clarified that "GAAR will not apply to such FIIs that choose not to take any benefit under an agreement under section 90 or section 90A of the income-tax Act, 1961. GAAR will also not apply to non-resident investors in FIIs".

**7. Options available to Assessing Officer for invoking GAAR**

An arrangement would be regarded as IAA if, *inter alia*, the main purpose is to obtain tax benefit [section 96(1)]. However, so far as an assessee is concerned it is not sufficient that the main purpose of the whole arrangement is not to obtain a tax benefit; if the main purpose of even a step in, or a part of the arrangement is to obtain a tax benefit, then the arrangement shall be presumed to have been entered into, or carried out, **unless it is proved to the contrary by the assessee**, for the main purpose of obtaining a tax benefit.

On a combined reading of *Explanation* to section 95, section 96(1) and 96(2), it appears that the Assessing Officer has three options for invoking GAAR. An illustration is given to explain the proposition: *Suppose an arrangement has four steps; a1, a2, a3, a4.*

show that the main purpose of any of the steps a1 to a4 is to obtain a tax benefit and proceed to hold such step as an IAA under *Explanation* to section 95 read with section 96(1),

show that the main purpose of any of the steps a1 to a4 is to obtain a tax benefit and use the statutory presumption under section 96(2) to show that the whole arrangement is entered into for the main purpose of obtaining a tax benefit,

Show that the main purpose of the entire arrangement 'A' is to obtain a tax benefit and proceed to hold the whole arrangement 'A' as an IAA, under section 96(1).

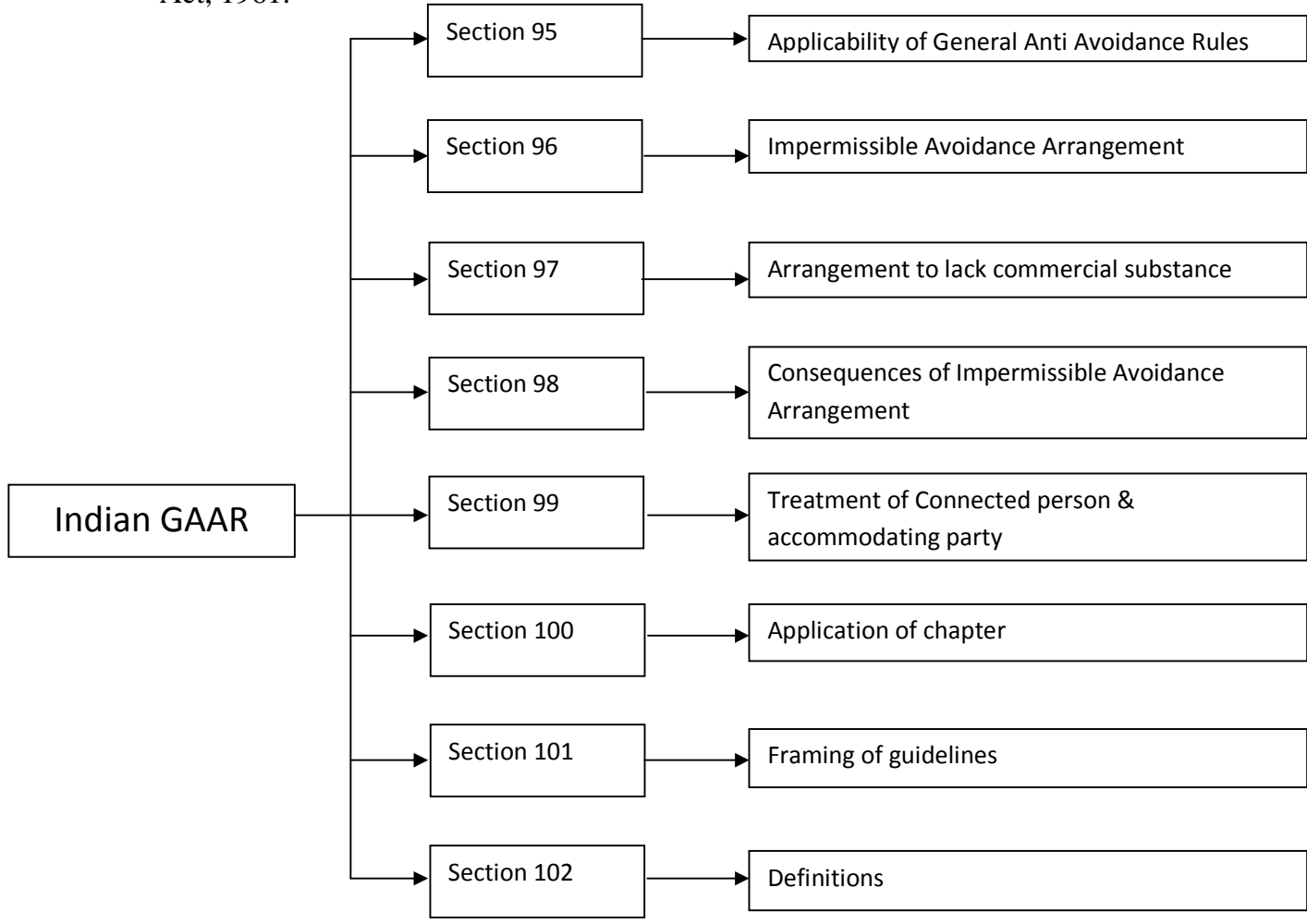
Options to Assessing officer



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**INDIAN GAAR**

A new Chapter X-A, consisting of sections 95 to 102, has been inserted in the Income-tax Act, 1961.



Essentially, above section provide as follows:

- a) the provisions will apply notwithstanding anything contained in any provisions of the Act
- b) there is an arrangement as defined in section 96(1)
- c) the arrangement is 'entered' into by an assessee [section 95]
- d) the arrangement is an impermissible avoidance arrangement (IAA) as defined in section 96(1)

If the aforesaid conditions (a) to (d) are satisfied, then the arrangement may be declared to be an IAA subject to the provision of section XA. Let us analyze it in detail.

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**SECTION 95: APPLICABILITY OF GAAR**

“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”.

*Explanation.—For the removal of doubts, it is hereby declared that the provisions of this Chapter may be applied to any step in, or a part of, the arrangement as they are applicable to the arrangement*

**Analysis:**

- a) Section 95 overrules everything in the act.
- b) Section 95 provides that an arrangement 'entered into' by an assessee may be declared to be an IAA. The word 'enter' has been explained as follows:

*“in Dr. A. R. Shukla v. CGT [1969] 74 ITR 167 (Guj.) it was observed that what section 2(xxiv)(d) of the Gift Tax Act requires is that the donor must 'enter into a transaction' and that can only be with some person. The words 'enter into a transaction' cannot be equated with 'do an act or abstain from doing an act'”*
- c) Finance act 2013, provides treaty override provisions by making consequential amendments to section 90 and 90A which provides that GAAR shall override treaty even if treaty provisions are more beneficial.
- d) If arrangement made by assessee is declared to be an impermissible avoidance arrangement, then its tax treatment shall be determined by applying section 96 to section 102.
- e) Explanation clarifies that these provisions may be applied to any step in, or a part of the arrangement as they are applicable to the arrangement. However, definition of arrangement itself includes any step in, or a part of the arrangement/transaction etc. ***Hence even without the explanation, a step of a transaction may be declared to be an IAA.***

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**SECTION 96: IMPERMISSIBLE AVOIDANCE ARRANGEMENT**

(1) An ***impermissible avoidance arrangement*** means an arrangement, the main purpose of which is to obtain a tax benefit, and it—

(a) creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length;

(b) Results, directly or indirectly, in the misuse, or abuse, of the provisions of this Act;

(c) Lacks commercial substance or is deemed to lack commercial substance under section 97, in whole or in part; or

(d) Is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for bona fide purposes.

(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.

**Analysis:**

- Impermissible avoidance arrangement means an “***arrangement***”, let us understand the meaning of arrangement,

*"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;"*

→ *"Step includes 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 definition although exhaustive is very wide:

- a) It encompasses all types of arrangements, including genuine and legal arrangements, and whether enforceable or not.
- b) It covers not only a transaction or a scheme but also any step in or any part of such transaction

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- c) The definition of step is inclusive and hence, apart from the activities specified in the definition, any step as normally understood would constitute an arrangement.

The words 'transaction', 'scheme', 'agreement', 'operation', 'understanding' have not been defined in the Act.

TERMS	MEANING
Transaction	<p><i>“The term 'transaction' is a word of wide import. In the <b>Shorter Oxford Dictionary</b> the word 'transaction' is interpreted as 'that which has been transacted; a piece of business, the action of passing or making over a thing from one person, thing or state to another”</i></p> <p><b>[Karumuthu Thiagaraja Chetty &amp; Co. [1961] 42 ITR 788 (Mad.).]</b></p>
Scheme	<p><i>A 'scheme', according to the dictionary meaning of that word, is 'a carefully arranged and systematic program of action', a 'systematic plan for attaining some object', 'a project', 'a system of correlated things' (see <b>Webster's New World Dictionary, and Shorter Oxford English Dictionary, Vol. II</b>)</i></p> <p><b>[State of West Bengal v. Swapan Kumar Guha AIR 1982 SC 949].</b></p>
Agreement	<p><i>Every promise and every set of promises forming the consideration for each other is an agreement [section 2(e) of <b>Indian Contract Act, 1872</b>]. There is mutual assent to the proposal when the proposal is accepted and in the result an agreement is formed</i></p> <p><b>[Andhra Sugars Ltd. v. State of A. P. AIR 1968 SC 599].</b></p>
Operation	<p><i>“An act or instance, process, or manner of functioning or operating. A particular process or course; mental operations. A business transaction, esp. one of a speculative nature; deal: a shady operation.”</i></p>
Understanding	<p><i>The word means something quite different from a binding legal contract; at most the word connotes a gentleman's agreement</i></p> <p><b>[Milner v. Percy Bilton [1966] 2 All ER 894.</b></p>

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- GAAR is triggered only if there is an **Impermissible avoidance arrangement (IAA)**

There is an IAA, if following conditions are satisfied:

- there is an arrangement as defined above and
- the main purpose of the arrangement or any step in it, or a part of it is to obtain a **tax benefit** as defined in section 102(10) ('tax benefit condition' or 'main purpose test')

3. And arrangement satisfied anyone of the following:

- It creates rights which are not ordinarily created between persons dealing at arm's length,
- It creates obligations which are not ordinarily created between persons dealing at arm's length
- It results, directly or indirectly, in the misuse or abuse of the provisions of the Act
- It **lacks commercial substance** in whole or in part
- It is deemed to lack commercial substance in whole or in part within the meaning of section 97
- It is entered into by means, or in a manner, which are not ordinarily employed for **bonafide** purposes
- It is carried out by means, or in a manner, which are not ordinarily employed for *bona fide* purposes

Let us understand the above by way of example:

1.	Suppose a person invests in bonds issued by NHAI/REC for the purpose of obtaining capital gains exemption under section 54EC. In such a case, the main purpose could be to obtain a tax benefit; however, the investment does not result in any of the alternate conditions being satisfied and hence the investment cannot be construed as an IAA.
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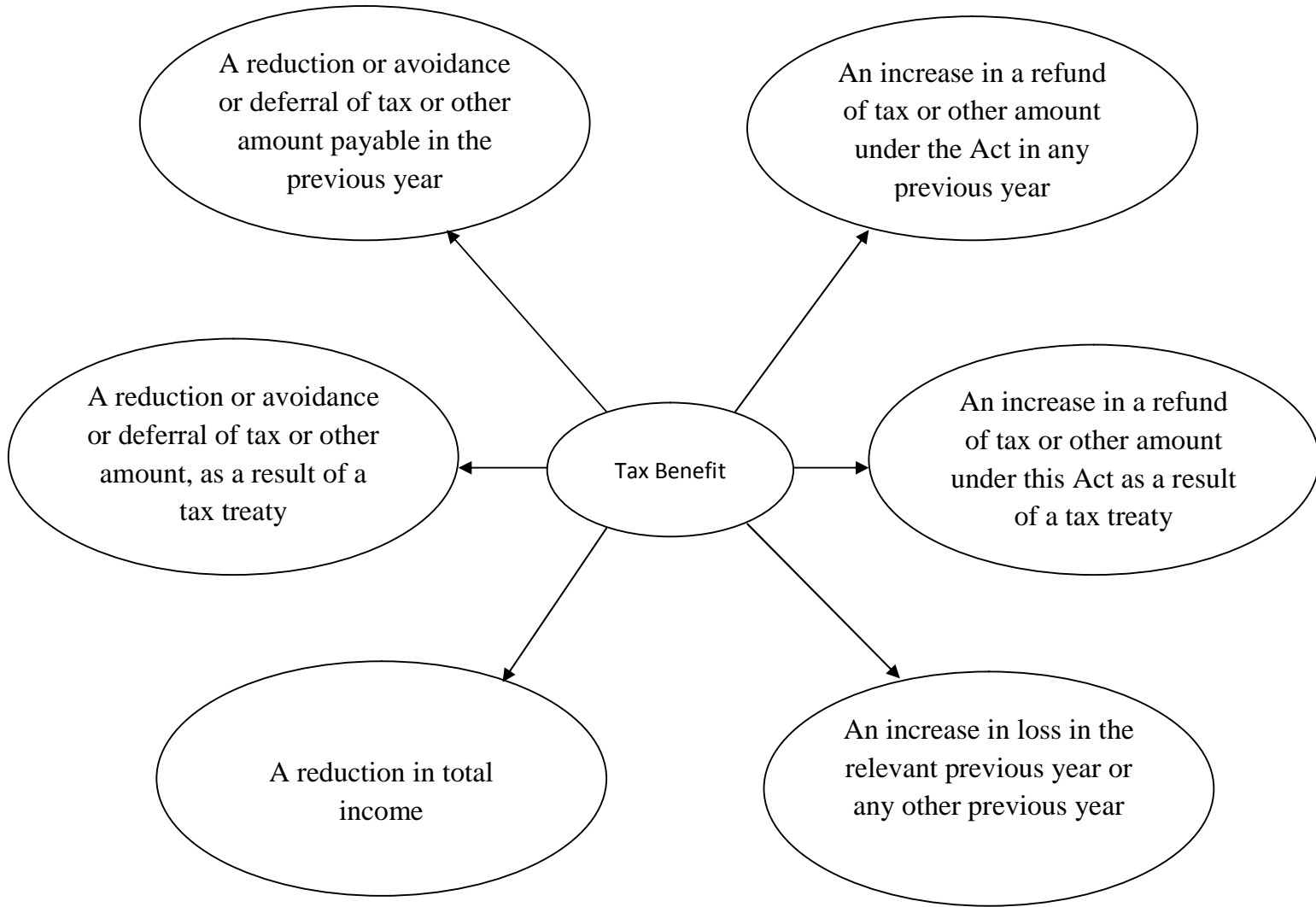
2.	Alternately, suppose a lawyer decides to render free services to a relative. In such case it could be argued that it created an obligation upon him which is not ordinarily created between a lawyer and a client and hence the alternate condition is satisfied. However, having regard to the relation between the two, it is quite plausible that the lawyer would not charge fees and that the main purpose was not to obtain a tax benefit. In the circumstances, the main purpose test is not satisfied and the transaction should not be declared as an IAA.
3.	To take further illustration, suppose a company owns an asset as stock in trade; instead of the company selling its asset (which could be subject to tax @ 30% plus DDT) the shareholders transfer their entire shareholding to an unrelated person. In such a case, it may or may not be possible to rebut the presumption that the main purpose is to avoid tax benefit. However, share purchase is a usual means of acquisition and hence, if there is a genuine and <i>bona fide</i> share purchase and the covenants are what are found usually in a share purchase agreement, there being no unusual rights or obligations, the transaction may not satisfy any alternate condition, and it should not be regarded as an IAA.

- **Tax Benefit:** There could be an IAA only if the main purpose is to obtain tax benefit, which term has been defined in section 102(10) to include:
  - a reduction or avoidance or deferral of tax or other amount payable under the Act in the relevant previous year or any other previous year ('any previous year'); or
  - an increase in a refund of tax or other amount under the Act in any previous year; or
  - a reduction or avoidance or deferral of tax or other amount that would be payable under the act, as a result of a tax treaty in any previous year; or
  - an increase in a refund of tax or other amount under this Act as a result of a tax treaty in any previous year; or
  - a reduction in total income; or
  - An increase in loss in the relevant previous year or any other previous year.

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Following can also be represented with the help of diagram.



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The definition of tax benefit can be better understood by the following analysis:

- The definition is very wide and it would cover practically every transaction. To illustrate an interest free loan to a group company (reduction in total income/amount of tax payable) could result in tax benefit as defined.
- Determining whether any tax benefit is obtained or not, one has to consider an assessee on a standalone basis and not on combined basis along with some other assessee.

To illustrate, suppose a company sells goods to a tax paying Group Company at a price lower than the fair value. In this case on a combined basis there is no tax benefit since the reduction in tax payable by the company is exactly offset by the increase in tax payable by the group company. However, the increase in tax payable by the group company cannot be considered in determining whether the transferor company has obtained tax benefit or not.

- The definition refers to 'under this Act' and hence, there would be a tax benefit only if there is a reduction, etc., of tax payable under the Act and so on. It is not relevant if benefit is obtained under some other statute.
- In order to ascertain whether a tax benefit is obtained or not, one will have to follow a two step approach for each of the relevant previous year :
  - (a) Determine the total income, tax payable, refund of tax payable, etc., if the arrangement in question had not been entered into;
  - (b) Determine the corresponding total income, tax or refund upon implementation of the arrangement.

If the difference between the total income or tax payable in step (a) and (b) is a positive figure or the difference between refunds is a negative figure, then the arrangement has resulted in a tax benefit.



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**STATUTORY PRESUMPTION [SECTION 96(2)]**

Let us now consider sub section (2) of section 96, statutory presumption,

The statutory presumption is a rebuttable presumption that arrangement is to obtain tax benefit if main purpose of a step in or part of the arrangement is to obtain tax benefit [section 96(2)].

On a plain reading, if the AO shows that the main purpose of a step, etc., the arrangement is to obtain a tax benefit then the arrangement *shall be presumed* to have been entered into or carried out for the main purpose of obtaining a tax benefit [section 96(2)]. However, it is pertinent that Finance Minister in his Speech in the Parliament on 7th May, 2012 has said that the onus of proof is removed entirely from the taxpayer to the revenue department before any action can be initiated under GAAR.

The observation in case of *Hiten P. Dalal v. Bratindranath Banerjee AIR 2001 SC 3897* is very much relevant for understanding the word “**Shall be presumed.**”

From the aforesaid discussion, it appears that the following inferences can be drawn:

- The presumption in section 96(2) against the assessee is a rebuttable provision.
- The rebuttal requires furnishing of proof by the assessee.
- Proof does not mean conclusive proof.
- The assessee has to produce material which can demonstrate that his plea is reasonably probable, the standard of reasonability being that of a prudent/reasonable man.
- Documentation, exchange of correspondence with counter party, between employees, with advisors, minutes, etc., would become relevant.

**SECTION 97: ARRANGEMENT TO LACK COMMERCIAL SUBSTANCE**

*(1) An arrangement shall be deemed to lack commercial substance, if—*

*(a) The substance or effect of the arrangement as a whole, is inconsistent with, or differs significantly from, the form of its individual steps or a part; or*

*(b) It involves or includes—*

*(i) **Round trip financing;***

*(ii) **An accommodating party;***

*(iii) **Elements that have effect of offsetting or cancelling each other; or***

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- (iv) *A transaction which is conducted through one or more persons and disguises the value, location, source, ownership or control of funds which is the subject matter of such transaction; or*
- (c) *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 other than obtaining a tax benefit (but for the provisions of this Chapter) for a party; or*
- (d) *it does not have a significant effect upon the business risks or net cash flows of any party to the arrangement apart from any effect attributable to the tax benefit that would be obtained (but for the provisions of this Chapter).*
- (2) *For the purposes of sub-section (1), **round trip financing** includes any arrangement in which, through a series of transactions—*
- (a) *Funds are transferred among the parties to the arrangement; and*
- (b) *Such transactions do not have any substantial commercial purpose other than obtaining the tax benefit (but for the provisions of this Chapter), without having any regard to—*
- (A) *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;*
- (B) *The time, or sequence, in which the funds involved in the round trip financing are transferred.*
- (C) *The means by, or manner in, or mode through, which funds involved in the round trip financing are transferred or received.*
- (3) *For the purposes of this Chapter, a party to an arrangement shall be an **accommodating party**, if the main purpose of the direct or indirect participation of that party in the arrangement, in whole or in part, is to obtain, directly or indirectly, a tax benefit (but for the provisions of this Chapter) for the assessee whether or not the party is a connected person in relation to any party to the arrangement.*

It means that where a party is included in an arrangement mainly for obtaining tax benefit to the taxpayer, then such party may be treated as an accommodating party and consequently the arrangement shall be deemed to lack commercial substance. Also, it is not necessary that such party should be connected to the taxpayer.

- (4) *For the removal of doubts, it is hereby clarified that the following may be relevant but shall not be sufficient for determining whether an arrangement lacks commercial substance or not, namely:—*

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- (i) *The period of time for which the arrangement (including operations therein) exists;*
- (ii) *The fact of payment of taxes, directly or indirectly, under the arrangement;*
- (iii) *The fact that an exit route (including transfer of any activity or business or operations) is provided by the arrangement.*

**Analysis:**

1. Commercial substance is also referred to as 'economic substance and can be defined as  
*“It is an economic reality that underlies a transaction or arrangement regardless of its legal or technical denomination”.*

Let us understand the above term by way of an example

1.	A company may sell an office and then immediately lease it back; the commercial substance may be that it has not been sold."
2.	An assessee sells shares in a listed company to take benefit of short term loss and on the next day repurchases the same quantity of shares. In this case it could be said that on a combined basis, the transactions lack commercial substance and except for the brokerage and small fluctuation in price, there is no commercial detriment to the assessee.

2. Substance of an arrangement is different from what is intended to be shown by the form of the arrangement, and then tax consequence of a particular arrangement should be assessed based on the "substance" of what took place. In other words, it reflects the inherent ability of the law to remove the corporate veil and look beyond form.
3. For the above purposes section 102(4) provides that '*connected person*' means any person who is connected directly or indirectly to another person and includes-

Status	Connected Person
Individual	Any relative of the person
Company	Any director of the company or any relative of such director
Firm or AOP or BOI	Any partner or member of a firm or AOP or BOI or any relative of such partner or member

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HUF	Any member of HUF or any relative of such person.
Individual	Having <b><i>substantial interest</i></b> in the business of the person or any relative of such individual
Company, Firm, AOP, BOI (whether incorporated or not) or HUF	Having substantial interest in the business of the person or any director, partner, or member of the company, firm or AOP or BOI or family, or any relative of such director, partner or member
Company, Firm, AOP, BOI (whether incorporated or not) or HUF	Director, partner, or member has a substantial interest in the business of the person, or family or any relative of such director, partner or member
Any other person who carries on a business	a) the person being an individual, or any relative of such person, has a substantial interest in the business of that other person; or ii) the person being a company, firm, AOP, BOI, whether incorporated or not, or a HUF, or any director, partner or member of such company, firm or AOP or BOI or family, or any relative of such director, partner or member, has a substantial interest in the business of that other person

A person shall be deemed to have a ***substantial interest*** in the business, if—

In a case where the business is carried on by a company, such person is, at any time during the financial year, the beneficial owner of equity shares carrying twenty per cent or more, of the voting power

OR

In any other case, such person is, at any time during the financial year, beneficially entitled to twenty per cent or more, of the profits of such business.

4. *Clause (c)* means if a particular location is selected for an asset or transaction or residence, and such selection has no substantial commercial purpose, then such arrangement shall be deemed to lack commercial substance.
5. *Clause (d)* implies that besides having a commercial purpose, the taxpayer should also have commercial substance in the arrangement, which mean change in economic position of the taxpayer by altering the business risks or net cash flow to him.

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**SECTION 98: CONSEQUENCES OF IMPERMISSIBLE AVOIDANCE ARRANGEMENT**

*(1) 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 benefit under a tax treaty, 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:—*

- (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—*
  - (i) Any accrual, or receipt, of a capital nature or revenue nature; or*
  - (ii) Any expenditure, deduction, relief or rebate;*
- (f) Treating—*
  - (i) The place of residence of any party to the arrangement; or*
  - (ii) 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.*

*(2) For the purposes of sub-section (1),—*

- (i) Any equity may be treated as debt or vice versa;*
- (ii) Any accrual, or receipt, of a capital nature may be treated as of revenue nature or vice versa;*
- (iii) Any expenditure, deduction, relief or rebate may be recharacterised.*

**GENERAL ANTI AVOIDANCE RULES**

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**Analysis:**

1. The power of the AO is very wide and is also coupled with a duty to exercise where the circumstances of the case so require.
2. The tax consequences have to be determined in such manner as is deemed "appropriate".  
Thus, the tax consequences have to be as applicable, right in the circumstances and correct.
3. It is provided that equity may be treated as debt or *vice versa*. Equity normally refers to 'the ordinary share capital' (risk capital of a company).  
Preference shares may not be treated as debt under this clause.
4. It is not in every case of an IAA that the Assessing Officer is bound to determine the tax consequences. Discretion has been conferred on the AO and the said discretion may be exercised keeping in view the facts and circumstances of the particular case.

**SECTION 99: TREATMENT OF CONNECTED PERSON & ACCOMMODATING PARTY**

*For the purposes of this Chapter, in determining whether a tax benefit exists,—*

- (i) *The parties who are connected persons in relation to each other may be treated as one and the same person;*
- (ii) *Any accommodating party may be disregarded;*
- (iii) *The accommodating party and any other party may be treated as one and the same person;*
- (iv) *The arrangement may be considered or looked through by disregarding any corporate structure.*

**SECTION 100: APPLICATION OF CHAPTER**

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

GAAR shall apply in addition to, or in lieu of, any other basis for determination of tax liability; hence on a literal reading, it could apply even if the parties have effected a transaction at arm's length price within the meaning of Section 92, if the conditions of Section 96 are satisfied.

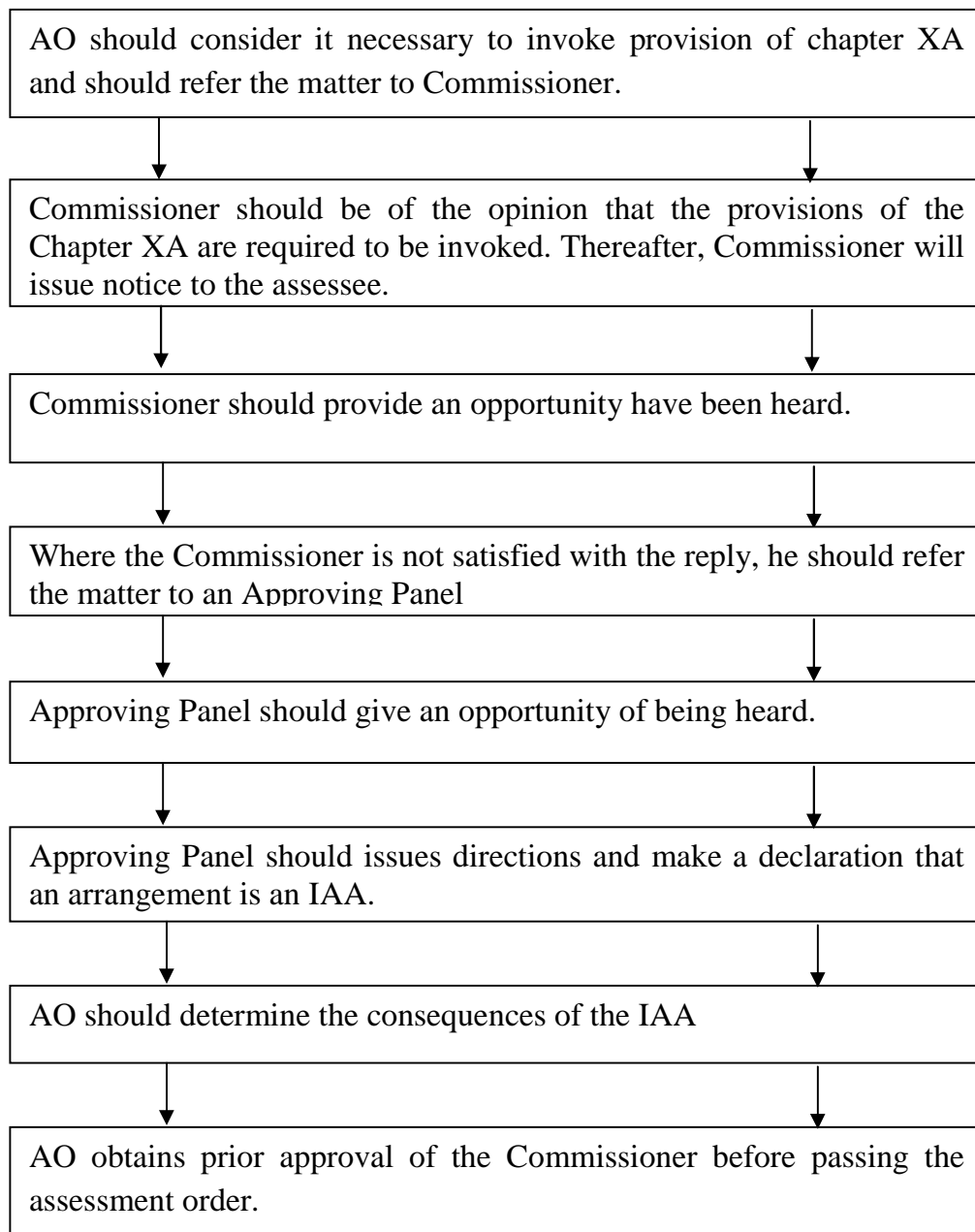
**GENERAL ANTI AVOIDANCE RULES**

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**SECTION 101: FRAMING OF GUIDELINES**

*The provisions of this Chapter shall be applied in accordance with such guidelines and subject to such conditions, as may be prescribed.*

**PROCEDURE REGARDING APPLICATION OF GAAR BY INCOME TAX DEPARTMENT**



## MISCELLANEOUS ISSUES

### ❖ Whether order passed above by assessing officer is appealable?

Section 253(1)(e) applicable w.e.f. 1-4-2016 provides that the following orders are appealable before the tribunal and not before Commissioner (Appeals):

- An order passed by an Assessing Officer under section 143(3)/147/153A/153C with the approval of the Commissioner as referred to in section 144BA(12).
- An order passed under section 154 or 155 in respect of above referred order.

### ❖ Whether advance ruling can be obtained in respect of an impermissible avoidance arrangement?

Any person (resident or nonresident) can make an application to the Authority for Advance Ruling (AAR) for determination of whether an arrangement is an impermissible avoidance arrangement or not.

### ❖ Circumstances in which domestic anti avoidance provision cannot be invoked

Commentaries provide that the domestic anti abuse provisions should be invoked only if there is clear evidence that the treaties are being abused.

### ❖ Applicability of GAAR to court sanctioned schemes

The definition of arrangement is very wide and includes schemes; hence, on a literal reading, even a Court approved Scheme could be considered as an arrangement. However, a different view has also been considered in case of *Asstt. CIT v. Gautam Sarabhai Trust No. 23 [2002] 81 ITD 677 (Ahd. - Trib.)*

*"Various amalgamations and mergers have been duly approved by the High Court and after such amalgamations have been sanctioned as made in conformity with the requirements under the Companies Act, no such allegation of tax planning or tax evasion can be leveled by the Revenue against the assessee"*

**Conclusion:** The matter is not free from doubt. One may also need to see whether the Court approved scheme can be assailed as aggressive tax planning or satisfying the intent behind the introduction of GAAR as specified in the Finance Minister's speech/Explanatory memorandum.



**GENERAL ANTI AVOIDANCE RULES**

❖ **Assessment of Representative Assessee (Section 163)**

<b>ONE VIEW</b>	<b>ANOTHER VIEW</b>
While completing the assessment of the representative assessee the AO can invoke GAAR, although it would be very difficult for a representative assessee (especially if the principal is unrelated) to have the records pertaining to the nonresident.	AO cannot invoke GAAR while completing the assessment of the representative assessee as GAAR is a very highly fact driven provision. In most cases a representative assessee cannot ordinarily be expected to have factual information

❖ **Does assessee have to consider the GAAR for making a deduction under chapter XVII-B?**

<b>FOR SECTION 195</b>	<b>FOR SECTIONS (OTHER THAN 195)</b>
<p>There may be a situation where income may not be taxable as per DTAA, however with the application of GAAR, the income becomes taxable.</p> <p>On a literal reading, the payer has to deduct tax on a sum chargeable under the provisions of the Act which would include the provisions of GAAR and hence a payer is required to deduct tax on the sum that could be taxable after considering.</p> <p>Another view is that, GAAR can only be invoked in the assessment or reassessment proceedings; hence, it cannot be invoked in TDS proceedings which are neither assessment nor reassessment proceedings. The later view is more logical and rational.</p>	<p>So far as other sections are concerned, they do not refer to any sum chargeable under the provisions of the Act; they require deduction of the amount paid (section 192), or amount credited/paid (section 193) or income credited/paid (section 194A) or any sum paid/credited (section 194C/section 194J); in other words, they would apply to the amount of credit/payment to the payee.</p> <p>Hence, it could be argued that in respect of these sections the payer is required to be governed by these provisions alone and he does not have to take into cognizance the effect of GAAR.</p>

**GENERAL ANTI AVOIDANCE RULES**

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❖ **What will the tax auditor have to report regarding GAAR?**

The tax auditor will be required to report any tax avoidance arrangement.

The Final Report of Expert Committee has recommended that "the tax audit report may be amended to include reporting of tax avoidance schemes above a specific threshold of tax benefit of Rs. 3 Crores or above which is considered by the tax auditor as more likely than not to be held as an impermissible avoidance arrangement under the Act."

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