GAAR: Legitimate tax planning?

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1. Introduction

Tax payer is always inclined to minimize his taxes within the framework of the Income Tax law of the state. In doing so, the structure or steps of transactions he plans to implement would be under scrutiny by the taxman. The taxman complains and finds fault that structure or part of structure is designed only to get tax advantage which has no commercial purpose. Whereas the taxpayer argues that the entire structure is within the four corners of law, hence, the same cannot be found fault. This dispute between both had been addressed by the Courts since long time. Taxpayer claims legitimacy of his transaction flow as being legal in its form whereas, taxman observes that the whole transaction in substance is entered only to gain tax advantage. In effect the dispute finally revolves around form and the substance of a transaction carried out by a taxpayer as a part of his business activity. Whether such structuring of transactions results in legitimate tax planning or in an abusive tax avoidance is a matter of concern before the Courts of law when the dispute is litigated. Unending tug-of-war between taxpayers' desire to reduce their taxes and aggressive approach of taxman to increase tax collections resulted in framing of anti-avoidance rules. A rule framed to target specific transactions in a specific context is explained as specific anti avoidance rule, such as Transfer pricing regulations and thin capitalization rules. The ingenuity of taxpayer in formulating sophisticated forms of tax avoidance kept the taxman helpless as such schemes of avoidance cannot be captured by Specific anti avoidance rules (SAAR). In this scenario, tax administrations are forced to contemplate of legislating a rule which can tackle any tax avoidance scheme. This approach resulted in formulating General anti avoidance rule by some tax jurisdictions like Australia, Canada and New Zealand etc. India also joined such group in bringing GAAR as part of its statute effective from the accounting year relevant to the assessment year 2018-19 onwards.

In this article I would like to touch upon the history and practice of GAAR by the early jurisdictions and the enacted legislation of GAAR in India. The journey of legislating the GAAR in India has witnessed various phases since 2010 and took a final shape after due consultative process becoming effective from AY 2018-19.

2. Conclusion

GAAR provisions enacted in the Indian tax laws are broadly based on South African GAAR provisions. The most pivotal factor to declare an arrangement as an Impermissible Avoidance arrangement (IAA) is to establish that the main purpose of arrangement is to obtain tax benefit, which burden of proof is on the Revenue. Such arrangement to be declared as IAA, it is further essential to demonstrate that one of the four tainted elements is present. As mentioned in the earlier portion of this article the second tainted element i.e. misuse or abuse of the provisions of the Act is very critical. It looks as though, the other three tainted elements are shades of "misuse or abuse of the provisions". In other words "creating rights or obligations which are not ordinarily created", "lacking commercial substance in the transaction" or "the manner in which

the transaction is carried out is not ordinarily employed for bonafide purposes" are instances which are most likely to arise when a taxpayer misuses or abuses the provisions of a law. There seems to be force in the argument that these three elements are offshoots or visible effects of misuse or abuse of the provisions. Thereby it may be possible to argue that misuse or abuse of provisions is the overarching ingredient to be demonstrated by the Revenue. It is also paramount that it is essential to demonstrate that the main purpose of the arrangement is to obtain tax benefit and is not just one of the main purposes. This requirement is very critical for invoking GAAR provisions under the Indian tax law. The above said approach can be seen as having been laid down as a ratio by the tax Court of South Africa in *Pienaar Brothers case (supra)* as discussed in the earlier paragraphs.

Memorandum explaining the provisions of Finance Bill 2012 wherein GAAR provisions were introduced, clearly explains that GAAR provisions are meant to target Aggressive tax planning. This obviously means legitimate tax planning is different and not targeted by GAAR provisions. If the tax planning is within the four corners of the law which meets both the letter and spirit of the law, the same is to be considered as legitimate/legal tax planning which is intended by the law to be availed by the tax payer. It is only such tax benefit which is unintended and which does not fit into the spirit of the law though it may comply with a letter of the law, the same is to be regarded as aggressive/abusive tax planning which is a clear target of GAAR provisions. One can draw support from jurisprudence coming up from the foreign Courts of early GAAR jurisdictions including South Africa (on which Indian GAAR provisions are broadly based) to take a view that GAAR provisions target abusive/aggressive tax planning and not the legal/legitimate tax planning of a tax payer. One can also take a view that jurisprudence of the Indian Courts including that of Hon'ble Supreme Court in the pre GAAR period still holds water in protecting the legitimate tax planning of a tax payer even under the GAAR regime.

The GAAR provisions in India are yet to be tested and interpreted before Indian Courts in the years to come.

The discussion in this article is purely the personal view of the author in respect of legitimate tax planning of a tax payer.