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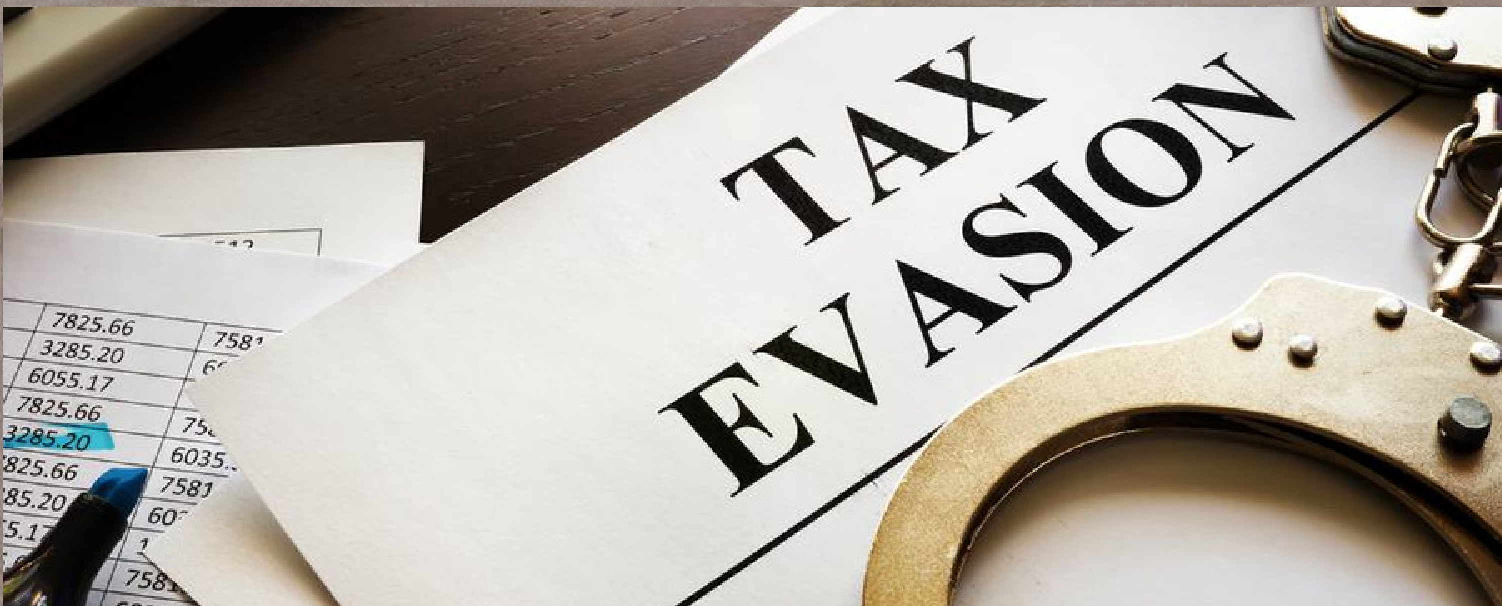
DIRECT TAX NEWS

GAAR PROBE BEGINS ON COMPANIES SUSPECTED OF TAX AVOIDANCE



The revenue department has launched investigations under the anti-tax avoidance law, General Anti-avoidance Rule (GAAR), into companies and entities that may have used creative methods to avoid paying taxes. A Hyderabad-based company, Ekge Retail, has received a notice in which the department has applied Section 96(1)(d) of the Income-tax Act, which deals with impermissible agreements undertaken to avoid taxation. The company has now approached the high court for state of Telangana at Hyderabad challenging the applicability of the section for some transactions undertaken by it in 2018 and 2019. The notice was issued to the company in February 2. GAAR was first introduced in 2012, but it was considered controversial and there was a demand that the government put in proper checks and balances.

The government has now specified a procedure in which GAAR notices can be issued. It was decided that before issuing a notice, a tax officer must escalate the matter to a tax commissioner. If the commissioner is convinced, then it will be forwarded to a panel, which will have to give its approval before any action is taken. The GAAR framework was put in abeyance for a while, presumably due to the pandemic, and the fresh investigations mean several M&As or corporate transactions could now be questioned if they are specifically designed as part of tax planning. Tax experts point out that GAAR has existed in its current form in the regulations since 2017-18, but its effective implementation started this year only after the constitution of the panel. The main objective of this panel is to ensure that it is invoked fairly and to avoid subjectivity at the level of officers to pick up cases, say experts. GAAR would go into effect if the tax department thinks that some transactions or structures in or outside of India were set up or done just to avoid paying income tax. Any decision by a company to set up an office in another country or undertake a merger or acquisition merely as part of tax planning could attract GAAR.

FOREIGN INVESTORS FROM MAURITIUS LIKELY TO KEEP TAXMAN AT BAY

Foreign investors coming from Mauritius are often denied capital gains tax relief on the grounds that persons controlling the tax haven companies are based in other countries. This may change now. One such attempt by the Income tax (I-T) department to lift the 'corporate veil' was struck down this week by a court which ruled that the tricky subject of 'beneficial ownership' (BO) of the Mauritian entity cannot be linked to capital gains.

The ruling by Income tax Appellate Tribunal (ITAT), a quasi-judicial authority, relating to Blackstone FP Capital Partners Mauritius V Ltd, pertains to financial year 2015-16 when it booked capital gains of over Rs 900 crore after selling stocks of CMS Info Systems

The tax officer's contention was that the effective control of the company in Mauritius lay with entities in the Caribbean tax haven Cayman Islands. Thus, Blackstone cannot derive the capital gains tax benefits - with no tax required to be paid for sale of stocks bought before 2017 - as provided in the amended treaty between India and Mauritius. The tax officer believed it was a fit case to lift the proverbial corporate veil to point fingers at the real BOs.

The Tribunal has held that the Treaty does not require the BO test to be met for capital gains tax exemption. The (apex tax body) CBDT had already issued Circular no. 789 in 2000 stating that wherever a Certificate of Residence is issued by the Mauritian Authorities, such a Certificate will constitute sufficient evidence for accepting the status of residence as well as BO for applying the Treaty. This circular has been upheld by the Supreme Court in the case of Azadi Bachao Andolan as well as in Vodafone.

There is a raging debate globally on BO in the context of treaties. Against this backdrop, ITAT feels it's not at the whim or fancy of a tax authority to decide what constitutes BO. Agreeing that the Tribunal has rightly observed that requirement of being a BO is not present under Article 13(4) of the Treaty.

GST COUNCIL RECOMMENDATIONS NOT BINDING ON CENTRE, STATES: SC

The Supreme Court on Thursday held that the recommendations of the GST Council are not binding on the Union or States. It also struck down the levy of Integrated Goods & Services Tax (IGST) on ocean freight in big relief to importers.

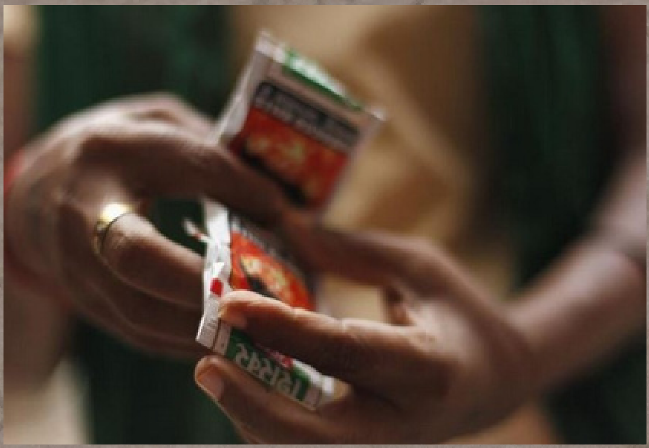
The judgment on GST not being binding on the Union or States was welcomed by the Opposition-ruled States, particularly those that interpreted it as a reiteration of the States' right to legislate on taxation, thereby starting a public debate on whether the concept of "one nation, one tax" itself was under question. The Centre, on its part, ruled out any change in the functioning of GST. The Centre also claimed that the Apex Court has merely established the legal position. Legal experts expect the Centre to file a review petition.

The Apex Court, while disposing of an appeal filed by the Centre against a Gujarat High Court ruling, listed three reasons why the recommendations of the GST Council are not binding on the Union and States. "The 'recommendations' of the GST Council are the product of a collaborative dialogue involving the Union and States. They are recommendatory in nature. A Bench comprising Justices Dhananjaya Y Chandrachud, Surya Kant, and Vikram Nath held that "To regard them as binding edicts would disrupt fiscal federalism, where both the Union and the States are conferred equal power to legislate on GST." The Bench said that"Indian federalism is a dialogue between cooperative and uncooperative federalism where the federal units are at liberty to use different means of persuasion ranging from collaboration to contestation." Further, the deletion of Article 279B and the inclusion of Article 279(1) by the Constitution Amendment Act, 2016 indicates that Parliament intended the recommendations of the GST Council to only have a "persuasive value," particularly when interpreted along with the objective of the GST regime to foster cooperative federalism and harmony between the constituent units.

The Bench said that the government, while exercising its rule-making power under the provisions of the CGST Act and IGST Act, is bound by the recommendations of the GST Council. However, "that does not mean that all the recommendations of the GST Council made by virtue of the power contained in Article 279A (4) are binding on the legislature's power to enact primary legislation," it said.

In the present matter, the bone of contention was whether an Indian importer can be subject to the levy of IGST on the component of ocean freight paid by the foreign seller to a foreign shipping line, on a reverse charge basis. The Bench said that such a levy would be a violation of the GST law and, accordingly, rejected the appeal by the Centre against the High Court ruling which had ruled no levy.

GST LEVY BASED ON CAPACITY ON PAN MASALA, GUTKHA UNLIKELY



A plan to levy goods and services tax (GST) on pan masala and gutkha on the basis of installed manufacturing capacity may be dropped due to the difficulties in administering the input tax credit (ITC) mechanism.

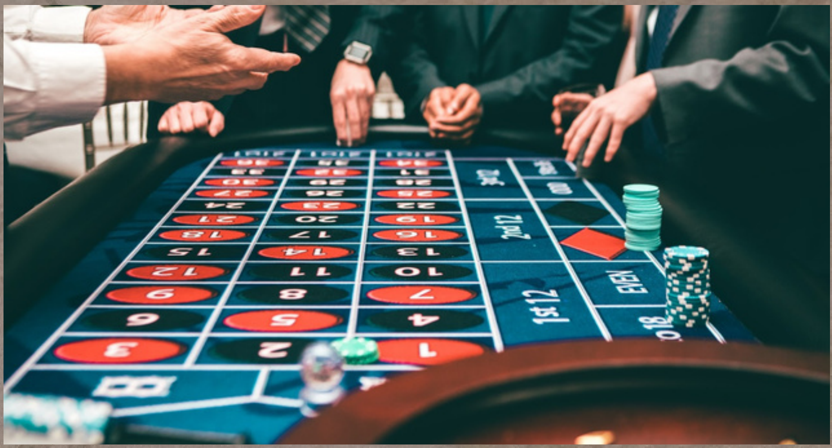
In May 2021, the GST Council had set up a group of ministers (GoM), led by Odisha finance minister Niranjan Pujari, to examine the feasibility of levying GST on products such as pan masala and gutkha, on the basis of the installed capacity, rather than actual production. This was in view of large-scale tax evasion detected by under-reporting of output by the units.

The GoM is yet to submit to its report to the council.

Currently, assorted tobacco items and pan masala attract the highest GST rate of 28% and also the 'compensation cess'. The rate of cess on tobacco products is 290%, while that on pan masala is 135%.

Since GST works on a value chain basis, the capacity-based taxation will also make it difficult to administer ITC as wholesalers and retailers don't operate in a capacity based mechanism.

GROUP OF MINISTERS FOR RAISING GST ON ONLINE GAMING TO 28%



A group of ministers (GoM) has recommended raising the goods and services tax (GST) on online gaming from 18% to 28%, to bring the skill game tax rate on a par with chance games involving gambling and betting, sources said.

However, it was not immediately clear whether the enhanced GST rate would be on the full contest entry amount (platform fee and prize pool) or only on the platform fee. A member of the GoM told FE that it may be levied on the "initial gaming amount", but he did not elaborate.

A gaming industry representative said the concept of the initial gaming amount could lead to disputes, as the initial amount can be lowered to a bare minimum (Rs 1 or Rs10) while the subsequent amounts could be raised to Rs 1 crore.

Online gaming is taxed at 18% of the platform fee, which works out to 5-20% of the contest entry amount. The gaming industry has been urging the government to keep the online gaming tax rate at 18% to promote the industry.

Currently, chance gaming such as racing, betting and lotteries are taxed at 28% of the contest entry amount (platform fee and prize pool).

Industry body IndiaTech.org has recommended that only gross gaming revenue (GGR or platform fee) alone should continue to be considered as the value of supply, as per current practice. Additionally, if there are other formats/revenue models followed by platforms such as subscription fee, in-game revenue, etc, in such cases GST should be applicable.

FINANCE MINISTRY TO CLARIFY DOUBTS ON APPLICABILITY OF TDS ON PERKS RECEIVED IN BUSINESS, PROFESSION

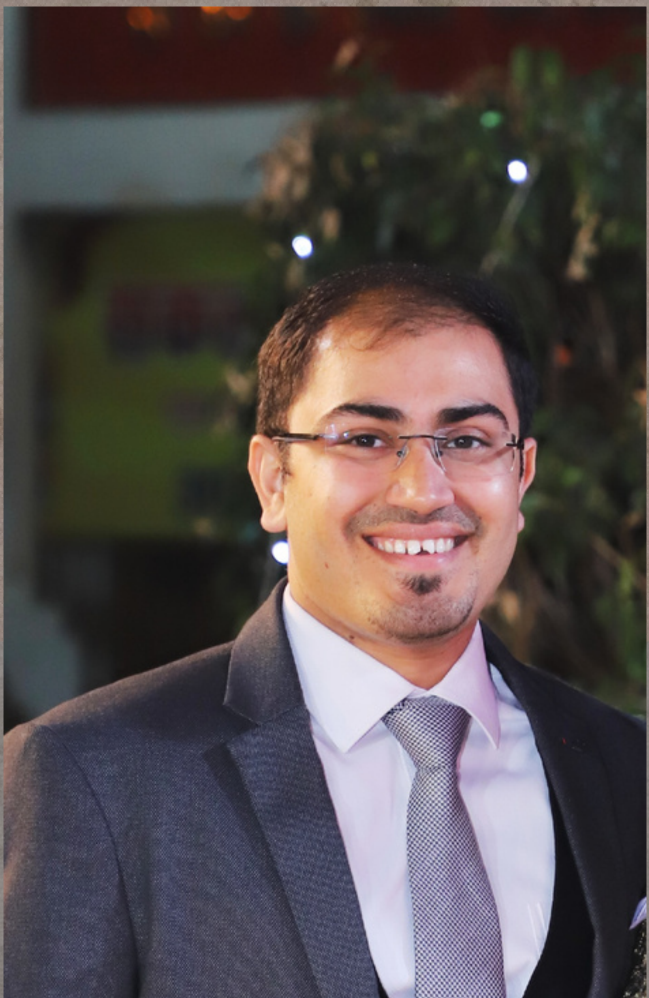
The finance ministry will clarify doubts on the applicability of new TDS provision regarding benefits or perquisites received in a business or profession, a senior tax official said on Wednesday. Joint Secretary in the finance ministry Kamlesh C Varshney said that such benefits and perquisites are income and were always taxable whether received in cash or kind. The Budget 2022-23 brought in the provision of tax deducted at source (TDS) on such income to check tax revenue leakage. The Budget brought in a new section, 194R in the I-T Act which requires deduction of tax at source at the rate of 10 per cent, by any person, providing any benefit or perquisite, exceeding Rs 20,000 in a year to a resident, arising from the business or profession of such resident.

The new provision comes into effect from July 1. "This (benefits and perquisites) is one area where nobody was paying taxes despite receiving benefits and perquisites in the course of business and profession... There is definitely a leakage here and therefore this section 194R. Whatever are the doubts, we are going to clarify the practical difficulties before July 1," Varshney said while interacting with the members of industry chamber Assocham. He said benefits like free medicine samples received by doctors, or free IPL tickets, foreign flight ticket received in the course of business or profession are income and should be disclosed in the income tax return.

TODAY'S QUOTE

"If you're waiting until you feel talented enough to make it, you'll never make it."

-Criss Jami



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