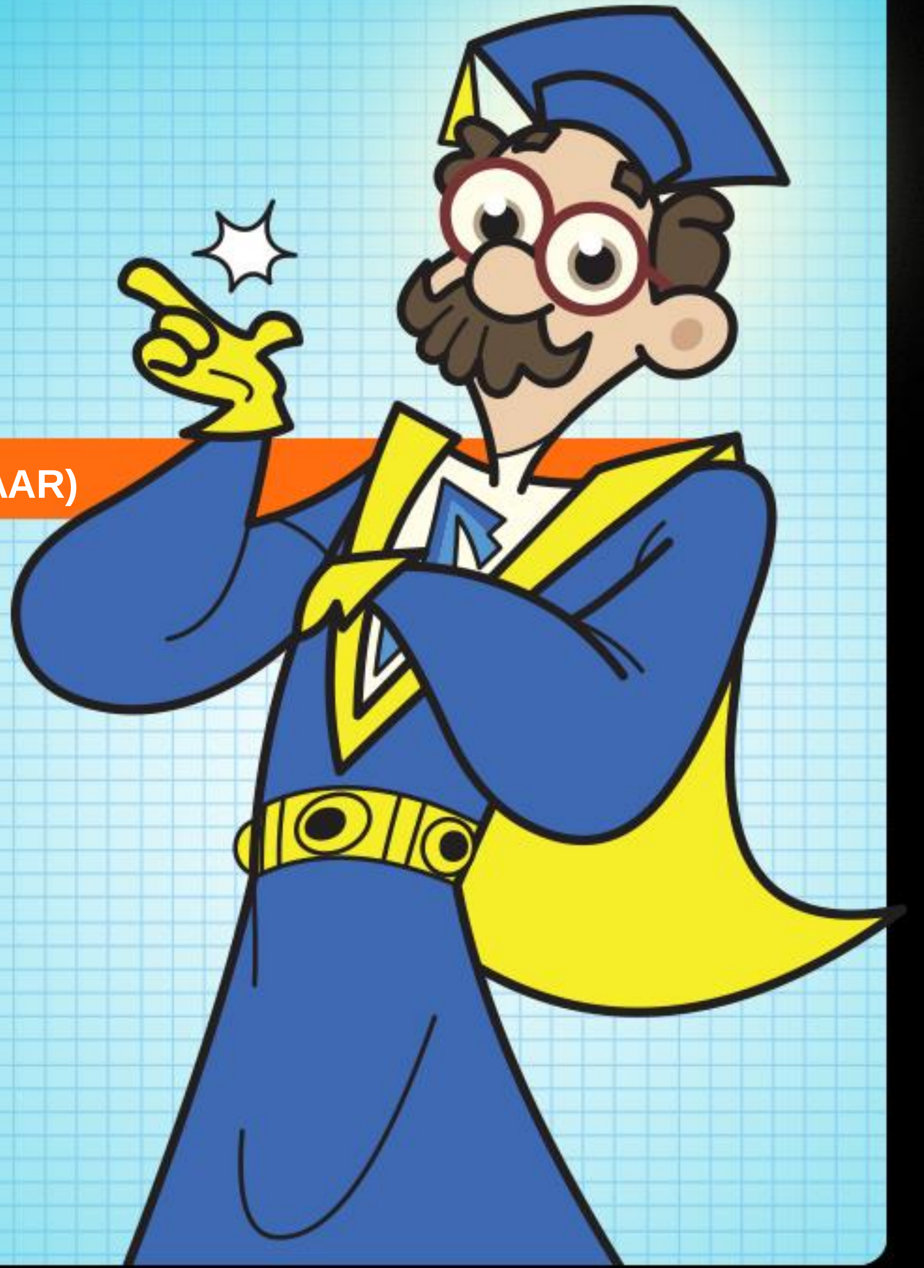
GENERAL ANTI-AVOIDANCE RULES (GAAR)



Understanding

General Anti-Avoidance Rules

(GAAR)

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

In this lesson we will re-visit GAAR (General Anti Avoidance Rules) that has become the center of discussion for many investors.

We will also look at the proposed changes that hopefully would ward off investor's mistrust that had set in after the announcement in the Union Budget.

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

So let us understand the reason

why the government came out

with GAAR in the first place.

And this we will do with an example.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

Let's say a company has a policy to help employees reach home on time for a better work/life balance.

It states, "Employees who stay beyond 20 kilometers from the office can leave 30 minutes early."

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

Every office has people that bend the rules in their favor. Some clever employees who had a second home more than 20 kms. away, decided to change their address so they could leave early every day.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

A system implemented with a good intent was quickly abused.

These acts are also witnessed on public buses where seats are reserved for the elderly but are taken by those who can very well stand and travel.

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

In this case, we have seen that even a law designed for a specific purpose can get undermined by elements that seek loopholes to create an unfair advantage for themselves.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

GAAR is a simple rule which allows the Indian tax authorities to levy tax if the arrangement or transactions done are 'impermissible avoidance arrangements.'

<u>This simply means, a tax levied because the company had in the past avoided paying tax, citing a tax exempt provision which was not due to them.</u>

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

Here are some tax avoidance policies that the government has formulated, subjected to certain conditions:-

GENERAL ANTI-AVOIDANCE RULES (GAAR)

1. **Companies should not be formed in a specific manner just for the sake of tax avoidance**

2. **Companies should not collude with subsidiaries with the sole objective of avoiding taxes**

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

The intent of GAAR is to ensure that companies do business in letter as well as in spirit of the law.

However, this law leaves a lot to be desired and can be misused.

The provisions made under GAAR still do not have much clarity. And this may impact many companies.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

GAAR has led to negative sentiments in the environment. Foreign Institutional Investors, for example, who were net buyers in the initial months in 2012, turned into sellers as there is still uncertainty about their investments.

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

Also, there has been recent news that investments through the Mauritius route will come under the watchful eye of GAAR. Many foreign institutional investors route funds through Mauritius in order to avoid paying capital gains tax in India.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

So, although the intent of the proposed law may be justified, the lack of clarity has hampered investor sentiments.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

The fear that law enforcers can misinterpret the law and penalize companies has impacted the economy by weakening investor sentiments.

The government is aware of the situation and has acted with swiftness to allay the fears of the investors.

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

The Shome Committee, set up by Prime Minister Manmohan Singh to address the concerns of foreign investors on GAAR, has recommended the postponement of the controversial tax provision by three years to 2016-17. In effect, GAAR would apply from assessment year 2017-18.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

The committee, headed by Parthasarathi Shome, has recommended that

1. **GAAR be applicable only if the monetary threshold of tax benefit is Rs. 3 cr & more**

2. **Abolition of short term and long term capital gains tax for sale of listed securities for both resident and non-resident investors. However, a slight increase in Securities Transaction Tax to make good some of the short fall has been recommended.**

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

He has also recommended that "GAAR provisions shall not apply to examine the genuineness of the residency of an entity set up in Mauritius". In other words, as long as a Tax Residency Certificate from Mauritius exists, that is enough to override GAAR provisions.

GENERAL ANTI-AVOIDANCE RULES (GAAR)

The objective of this lesson is not to take a political position on GAAR. The idea was to bring conceptual clarity about this widely covered subject in media.

There may be many aspects of GAAR that have been deliberately left out so that the focus remains on conceptual understanding only while leaving out the fine print.

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GENERAL ANTI-AVOIDANCE RULES (GAAR)

Hope this story has clarified GAAR

Thinking of Investment

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