

Oh my GAAR!

Have general tax anti-avoidance rules
changed the way we approach tax planning?

4th March 2024



Speaker Details

Sangna Chauhan

Sangna advises families on how they should hold their assets. In doing so, she works with families across generations, together with their trusted advisers. Her clients are generally very international, with the family and assets being split across various countries. Within this context, she advises on their lifetime planning, together with implementing strategies that mean assets will pass smoothly on death. She believes in an integrated approach to planning: that it should encompass the family's values and purpose, relevant succession laws and asset protection considerations, as well as purely tax-driven strategies. Sangna has a particular focus on US-UK estate and tax planning, having acted for many clients exposed to both tax and estate planning regimes.



Ron Choudhury

Ron Choudhury has a multi-dimensional tax practice. He is among a handful of tax practitioners whose expertise includes both income tax and sales tax. Ron's income tax practice focuses primarily on corporate tax, tax planning for high net-worth individuals, and executive compensation issues, while his sales tax practice is geared towards the real estate industry, charities and not-for-profits, and non-residents. Ron is the Leader of Miller Thomson's Corporate Tax Group.



Seth J. Entin

Seth J. Entin is a Tax shareholder in Greenberg Traurig's Miami office. He focuses his practice on the international taxation of high-net-worth individuals and families, international corporate taxation, Internal Revenue Service international tax audits, and Internal Revenue Service voluntary disclosures. Seth is currently ranked Band 1 in Tax for Florida and has been noted by *Chambers* for his "practical approach" and "strong knowledge base" that is always "focused on achieving the best possible results".



Michaël Khayat

Michaël advises entrepreneurs and families, French and foreigners, in national and international contexts. He practices in the following areas: estate planning, complex international successions & real estate investment, Michaël has developed a unique expertise for situations involving UK and US aspects.



Shreya Rao

Shreya runs a boutique firm which specialises in complex tax and private client matters, with international tax as a strong area of focus. Her clients include some of the most well-known Indian and Indian origin families, some of whom also retain her in an external general counsel capacity. Shreya's work is rated Band 1 by the Chambers HNW guide, while Legal 500 (2023) notes her ability to handle "the most difficult, emotional and intellectually challenging issues with grace and apparent ease".



Sonia Velasco

Sonia Velasco's crossborder practice involves advising private clients on their investments including real estate investments, estate planning, family governance and business succession, executive compensation and pension plans. She is well versed in vehicles such as trusts, which do not have a precise counterpart in Spanish law. She also often advises private equities, venture-capital and strategic investors, and family offices on their investments in startups and scaleups.



GAAR in the UK

Is the main purpose of the tax arrangement to obtain a tax advantage?

Tax arrangements "...are **abusive**" if they cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances"

"Intended legislative choice"
HMRC accepts "established practice"
"Situations where the law deliberately sets precise rules or boundaries"

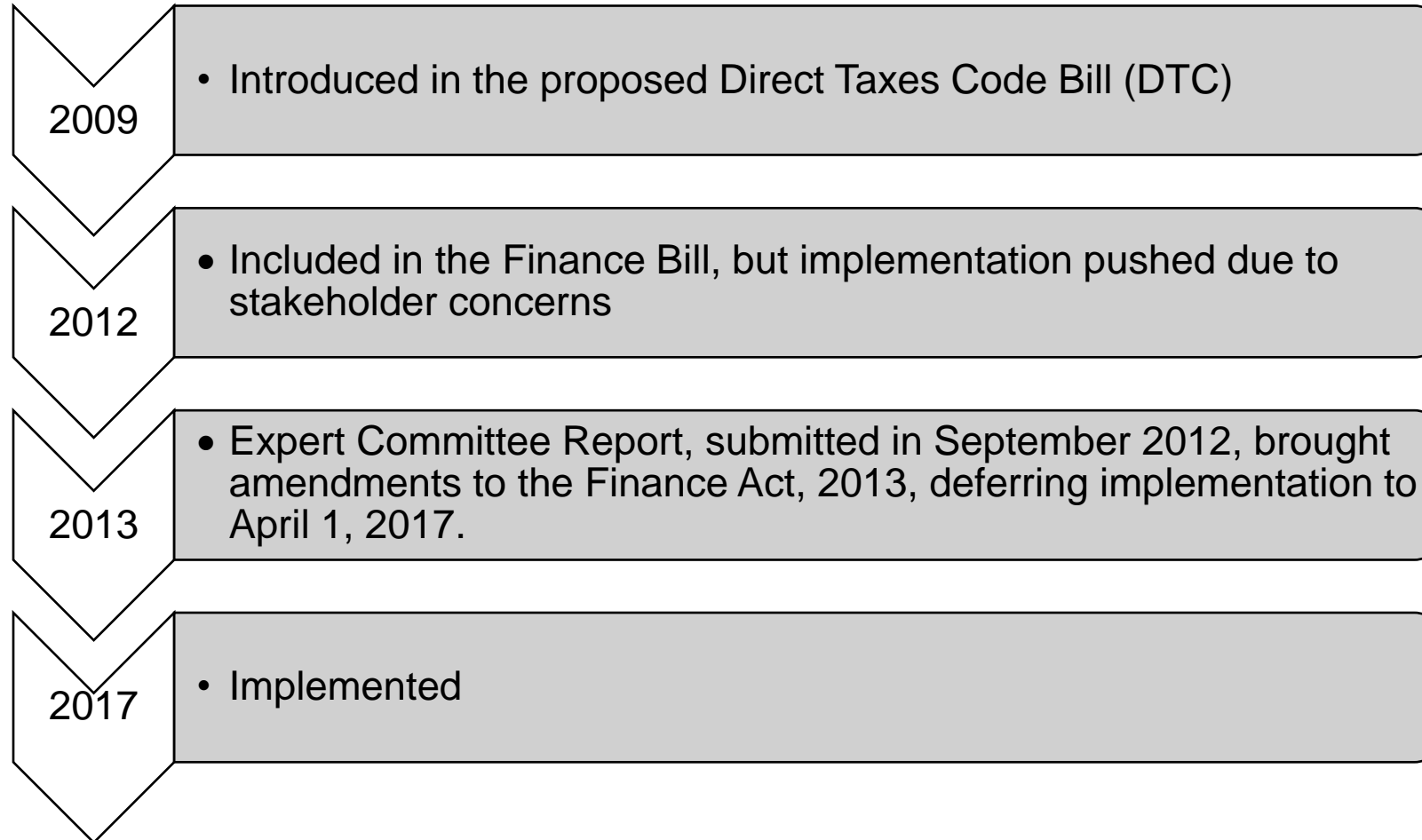
"Standard tax planning combined with some element of artificiality"
"Transactions that are demonstrably contrary to the spirit (or policy and wider principles) of the law"

"Exploiting a shortcoming in legislation whose purpose is to close down a form of activity"
"Arrangements that are contrived or abnormal and produce a tax position which is in no way consistent with the legal effect and economic substance of the underlying transaction"

Counteraction:

- To be just and reasonable
- If a straightforward cases, denial of the tax advantage sought
- In complex cases, enact the most likely non-abusive arrangements
- Penalties and accelerated payment notices

GAAR in India: A Timeline



GAAR in India: Some Examples

- **Reverse Age Health Services Pte Ltd. v. Deputy Commissioner of Income Tax Circle**
 - Issue: Whether a tax residency certificate was sufficient to claim benefits accorded to capital gains under the Singapore tax treaty?
 - Summary of ruling: The capital gains benefit to the taxpayer was lower than the GAAR threshold, and the investments made prior to the date of the GAAR. Consequently, the merits of applicability of GAAR were not examined in detail.
- **M/s JCT limited v. DCIT**
 - Issue: Availability of tax benefits to a court approved amalgamation between closely held companies. The amalgamation resulted in offset of losses against gains arising in the amalgamating company.
 - Summary of ruling: GAAR was not applicable in the relevant AY and so the ruling of the Tribunal was not based on GAAR provisions.

GAAR in Canada: History and Perspective

- GAAR (s.245 of *Income Tax Act* (Canada)) received Royal Assent on September 13, 1988
- Applies to direct or indirect misuse of Tax Act, Regulations, treaties, ITAR, or other relevant enactments in computing tax
- Also applies to direct or indirect abuse having regard to the same provisions
- Operative provision stated that where transaction is anti-avoidance transaction, tax consequences shall be determined as is reasonable in order to deny tax benefit
- Significant changes limited over the years – GAAR was amended to apply to other legislation beyond Tax Act
- GAAR Committee established in 1988 to review GAAR applications in rulings and assessments

GAAR in Canada: Recent Amendments

- Most significant GAAR amendments on course for Royal Assent in 2024 (applicable from Royal Assent)
- Proposed amendments add a preamble:
 - Confirms application to deny tax benefit of avoidance transactions resulting in misuse or abuse
 - Asserts balance between need to protect tax base and fairness and taxpayer need for certainty in planning
- Changes threshold for avoidance transaction (from “primary” to “one of the main purposes”)
- New provision stating that transaction lacking in economic substance “tends to indicate” transaction results in misuse or abuse
- New provision establishing when transaction (or series) lacking in economic substance
- New provision establishing GAAR penalty
- Concurrent change allowing for voluntary filing of reportable transaction information return in respect of transaction potentially subject to GAAR – may remove penalty and extended reassessment period for GAAR (now an additional 3 years)

GAAR in Canada: Jurisprudence

- Numerous decisions of Tax Court of Canada, Federal Court of Appeal and Supreme Court of Canada on GAAR – established jurisprudence but Courts have deviated from their own established principles
- Supreme Court heard GAAR in *Kaulius* (2005), *Canada Trustco* (2005), *Lipson* (2009), *Copthorne* (2011), *Alta Energy* (2021), *Deans Knight Income Corp* (2023)
- Corporate and private client/individual tax issues heard by courts
 - Capital gains exemption
 - Surplus strip
 - Estate freeze
 - Dividends
 - Trusts
 - Inter-spousal planning

GAAR in Canada: Takeaways

- GAAR is applied frequently – specific transactions (e.g., surplus strips) susceptible
- New GAAR (with penalties and longer reassessment period) aimed at applying GAAR to wider avoidance situations, creating economic substance concept, and adding GAAR penalty
- Taxpayers likely more successful in court cases but ambit of new GAAR may reverse trend
- Coupled with new mandatory disclosure rules, GAAR may have significant impact on future tax planning
- Practitioners expected to be more circumspect

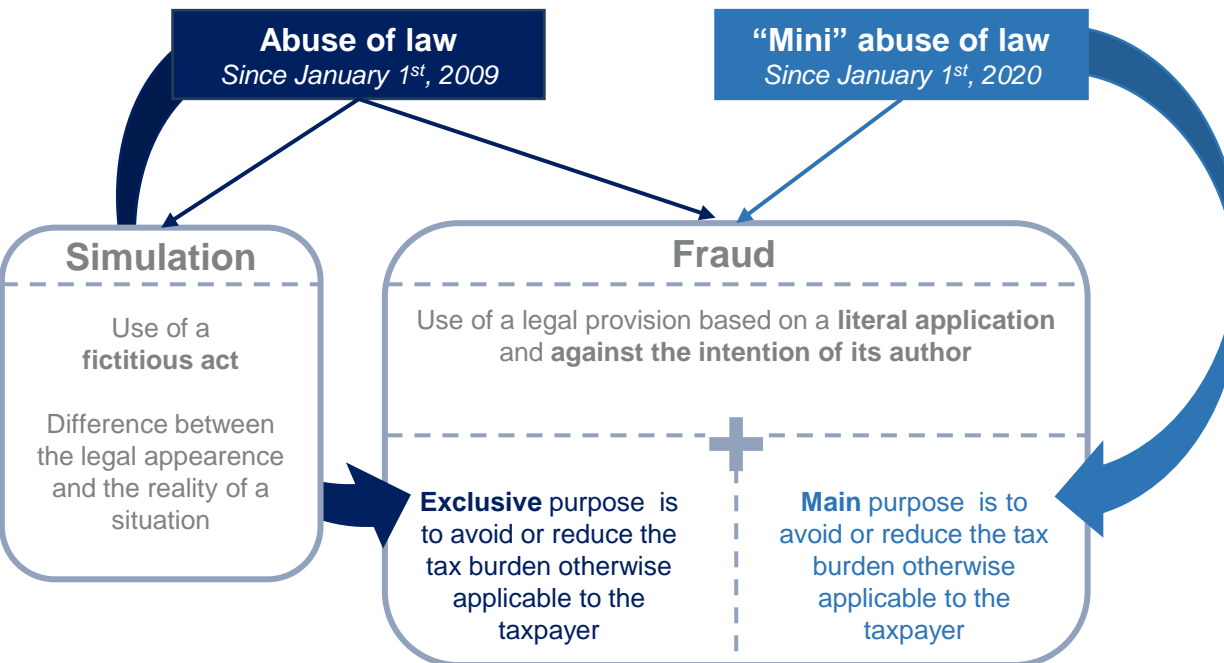
GAAR in France: definitions and consequences



Definition (simplified)

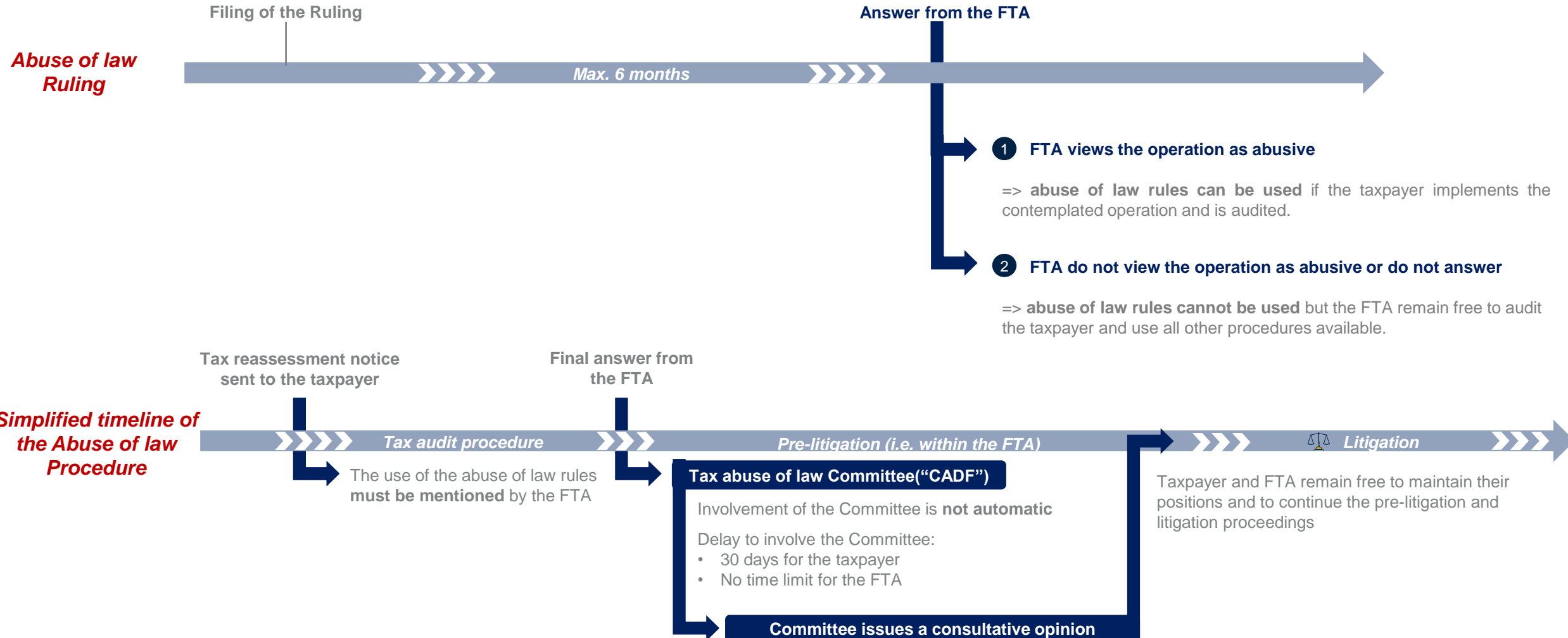


Consequences



| | Abuse of law | "Mini" abuse of law |
|---|--|--------------------------|
| For taxpayers | | |
| Tax avoided | ✓ | ✓ |
| Penalties 40%, possibly 80% | Automatically applied | Possibly applied |
| Late interest 0.20% / month | ✓ | ✓ |
| All parties jointly liable | ✓ | x |
| File forwarded to the national financial prosecutor | Automatically forwarded if penalty of 80% is applied | General rules applicable |
| For advisors | | |
| Specific fine of 50% of the income derived from the service provided to the taxpayer with a minimum of €10,000 | | |
| Conditions = (i) the 80% penalty if applied to the taxpayer + (ii) the advisor intentionally delivered the advice allowing the fraud | | |

GAAR in France: ruling and overview of procedure



GAAR in Spain: Introduction



- 1) Right to **choose the most favorable or convenient legal option** among those available and compatible with the law.
- 2) **Legitimate** tax optimization.
- 3) The Spanish Constitutional Court has ruled that citizens have the right to **seek the least burdensome tax alternative** within the legal framework.

GAAR in the Spanish General Law:

- 1) **Substance over form principle (art. 13 GTL)** to qualify a taxable event.
- 2) **Conflict in the application of tax law (art. 15 GTL)** Previously, fraud of Law (changed in 2004).
- 3) **Sham/simulation (art. 16 GTL)**

Not interchangeable, each one must be used for the purposes for which it was created (Spanish Supreme Court).

GAAR in Spain: Conflict in the application of tax law

CONCEPT

- Realization of the taxable event is totally or partially avoided or the tax base or the tax debt is reduced by means of acts or transactions which:
 - a) **Taken singly or jointly are notoriously artificial or inadequate to achieve the obtained result.**
 - b) **Have no relevant legal or economic effect other than tax saving.**

CONSEQUENCES

- Applying the rule that **should have been applied** to the usual or appropriate acts or operations and eliminating the tax advantages obtained.
- **Penalties can not be applied** if no similar public precedent exists (50 – 150%).
- Late payment interest.

IN PRACTICE

- It is usually applied on legal entities rather than on individuals. In particular, most cases involve **CORPORATE INCOME TAX / NON-RESIDENTS' INCOME TAX OR VALUE ADDED TAX.**
- Tax Audits / Tax Inspections are not so keen in applying the conflict in the application of the tax law f due to the need to obtain a **POSITIVE REPORT** of the Committee.
- The STA has the **BURDEN OF PROOF**. It must prove the existence of tax avoidance and the taxpayers must prove sound business/commercial reasons.
- The reports are **BINDING** on the tax administration and **CANNOT BE APPEALED**. They are also **PUBLISHED** on the website of the Tax Administration.

GAAR in Spain: Simulation/Sham

CONCEPT

- Declaration of will with a consciously **false content**, issued by agreement between the parties with the aim of deceiving, producing the **appearance of a legal transaction that does not exist** (absolute simulation) or is different from the one that has actually been carried out (relative simulation).

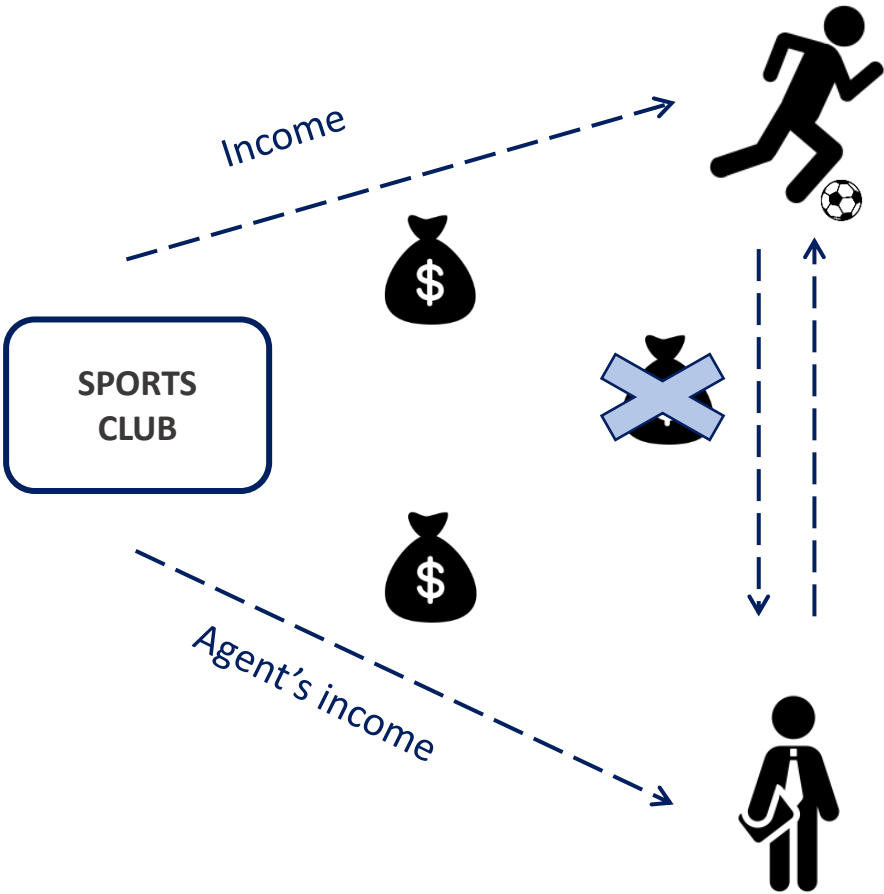
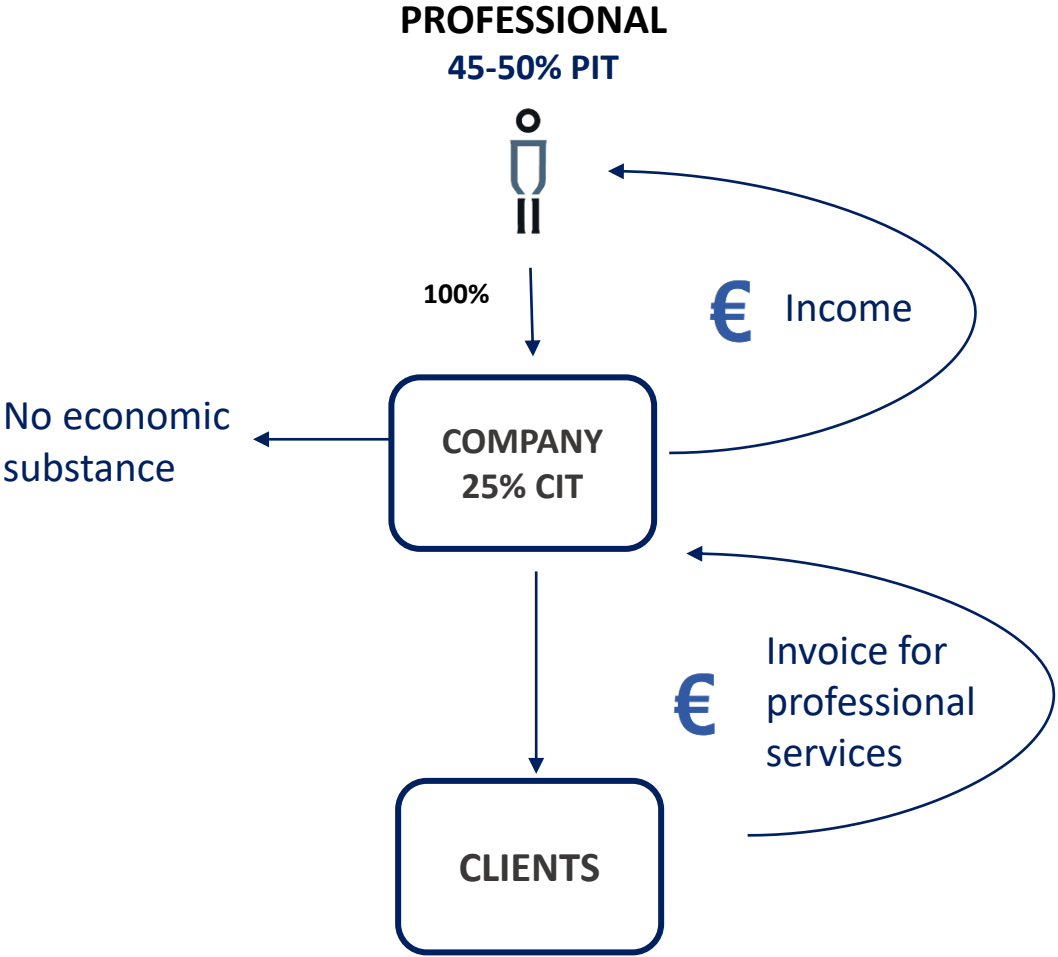
CONSEQUENCES

- Disregard of the simulated or concealed taxable event.
- The taxed taxable event will be **the one actually carried out by the parties**.
- Penalties ranging 50 – 150% on the unpaid taxes and late payment interests.
- It could be, in certain cases, a criminal offence

IN PRACTICE

- Equally applied on legal entities and individuals.
- Typical cases: individuals providing services through **SHELL COMPANIES**.
- The Tax Authorities are currently imposing 125% penalties. Courts may lower the penalty to 75%.
- There is **NO SPECIAL PROCEDURE** to declare the existence of simulation.
- **BURDEN OF PROOF** relies on the STA who must provide sufficient evidence of the discrepancy between the legal form and the economic reality of the transaction or arrangement

GAAR in Spain: Typically challenged structures



Tax anti-avoidance in the US: Judicial Doctrines

- Tax avoidance vs. tax evasion.
 - Judge Learned Hand: “[A] transaction, otherwise within an exception of the tax law, does not lose its immunity, because it is actuated by a desire to avoid. . . taxation. Any one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one’s taxes.”
 - Judicial doctrines (interrelated and overlapping):
 - Substance over form.
 - Economic substance.
 - Business purpose.
 - Step transaction.
 - Sham transaction.

Tax anti-avoidance in the US: Statutory Rules

- Targeted statutory and regulatory anti-abuse provisions.
- Section 7701(o) (2010): “Clarification of economic substance.”
 - *“In the case of any transaction to which the economic substance doctrine is relevant, such transaction shall be treated as having economic substance only if—(A) the transaction changes in a meaningful way (apart from Federal income tax effects) the taxpayer's economic position, and (B) the taxpayer has a substantial purpose (apart from **Federal income tax** effects) for entering into such transaction.”*
 - Penalties (20%, or 40% if inadequate disclosure)

Tax anti-avoidance in the US: Statutory Rules (Con't)

- When is the economic substance doctrine “relevant”?
 - Legislative history: § 7701(o) does not apply to certain “basic business transactions that, under longstanding judicial and administrative practice are respected, merely because the choice between meaningful economic alternatives is largely or entirely based on comparative tax advantages.”
 - Examples:
 - Choice between capitalizing a business enterprise with debt or equity.
 - Choice between utilizing a foreign corporation or a domestic corporation to make a foreign investment.
 - Corporate organization or reorganization.
 - Related party transactions, if arm’s length standards are satisfied.
- *Liberty Global Inc. v. United States* (Oct. 31, 2023) (taxpayer loss in district court; on appeal).
 - Dismissive of prerequisite that economic substance be “relevant.”

Questions

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