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Doing Away with Retrospective Tax

Why in news?

- The Union Finance Minister recently introduced the Taxation Laws (Amendment) Bill in the Lok Sabha.
- A key provision was doing away with the contentious retrospective tax law of 2012.

What is a retrospective tax?

- A retrospective tax taxes a transaction that took place prior to the law being framed.
- It can be a new or additional charge on transactions done in the past.
- Countries use this form of taxation to rectify any deviations in the taxation policies.
- Retrospective tax affects companies that had unknowingly or knowingly used the tax rules differently.

What is India's retrospective tax law of 2012?

- The retrospective tax provision was introduced in 2012 as an amendment to the Income Tax Act, 1961.
- It allowed the government to tax companies on mergers and acquisitions (M&As) that happened before 2012.
- In effect, it aimed to bring past indirect transfer of Indian assets under the ambit of taxation.
- The law was thus used to raise large tax demands on foreign investors like Vodafone and Cairn Energy.
- It was hence blamed for impairing India's investment climate.

What are the two major cases in this regard?

- UK-based telecom giant Vodafone bought a 67% stake in Hong Kong-based Hutchison Whampoa for $11 billion.
- To this transaction, the Indian government raised a demand of Rs 7,990 crore in capital gain.
- It said the company should have deducted the tax at source before making a payment to Hutchison.
- The company took the matter to the Supreme Court.
- The Court ruled in favour of Vodafone saying that it could not be taxed retrospectively.

- To overcome the legal hurdle, the retrospective taxation law was introduced.
- With this, the I-T department slapped Rs 3,100 crore tax notice on Vodafone India.
- Anothersuchmove was also made against the 2006 internal corporate restructuring carried out by UK-based Cairn Energy.
- Both Cairn and Vodafone filed lawsuits in international courts against India's retrospective tax.
- Separate international arbitration tribunal verdicts in the Vodafone and Cairn cases have ruled

against India’s retrospective tax demands.
- The tax amendment now has been prompted by Cairn Energy’s relentless pursuit to enforce the arbitration award.

What are the current changes?

- The Taxation Laws (Amendment) Bill nullifies the relevant retrospective tax clauses introduced in 2012.

- As per the proposed changes, any tax demand made on transactions that took place before May 2012 shall be dropped.
- And any taxes already collected shall be repaid, albeit without interest.
- To be eligible, the concerned taxpayers would have to drop all pending cases against the government.
- They should also promise not to make any demands for damages or costs.
- Going ahead, India needs to demonstrate greater clarity and consistency in policy across the board (trade tariffs, GST, etc.,) to fix its broken credibility.

Source: The Hindu, Business Standard

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