Inching towards Tax Certainty: Neoteric Domestic Dispute Mechanism for Cross-Border Taxation

Research Committee
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Foreword

Certainty in tax is the quintessential part for a sound taxation system. However, in a globalised world, disputes emerging from trade, investments and tax are inevitable which sometimes creates uncertainty. This Research work focuses on two major factors leading to uncertainty in taxation system i.e., dispute resolution and international taxation. Generally, tax uncertainty in disputes can be addressed through an effective domestic dispute mechanism and through an international tax treaty resolution mechanism.

The report focuses mainly on the domestic dispute mechanism rather than the international tax treaty resolution mechanism as it involves the cooperation of other countries and international organizations following the principles of Public International Law. The scope of report involves assessment of the existing dispute mechanism under the Indian domestic law and to give recommendations in order to bolster certainty in tax.

I am very pleased that the Research Committee of the Institute under the 'ICAI Research Project Scheme 2020' undertook the Research Project on the topic of "**Inching towards Tax Certainty: Neoteric Domestic Dispute Mechanism for Cross-Border Taxation"**.

I would like to take this opportunity to express my thanks to CA. Anuj Goyal, Chairman, Research Committee and CA. Kemisha Soni, Vice-Chairperson, Research Committee, who took the initiative to introduce 'ICAI Research Project Scheme 2020' to encourage research-based activities. I would also like to take this opportunity to express my gratitude to members of the Research Committee who have made invaluable contribution through their expert guidance in the finalisation of the Research Report.

I am confident that this Research Report will be extremely useful for the members and other stakeholders as well.

New Delhi	**CA. Atul Kumar Gupta**
February 2, 2021	**President, ICAI**

Preface

The Research Report on "**Inching towards Tax Certainty: Neoteric Domestic Dispute Mechanism for Cross-Border Taxation"** revealed that the prevailing dispute mechanism in India on cross border taxation matters has its flaws and has certainly not fostered tax certainty. Significant disputes have been rising exponentially year on year due to rapid growth of Multi National Entities (MNE). Further, the main causes of tax disputes are "inconsistent application or interpretations, unclear tax policies and rules, resource constraint, complex administration procedures, insufficient understanding of international tax law, enforcement not in accordance with tax treaties, unintended consequence of domestic practice, inadequate transparency etc."

Considering the significance that tax certainty brings, the existing state of affair is not sustainable and does not augur well for all the stake holders concerned. Therefore, a change in the existing approach or introducing new alternative mechanisms may be considered for a better future. The research work also throws light on the architecture of the dispute mechanism framework consisting three layers of structure (Dispute Prevention, Containment and Resolution Mechanism) to fuel the said purpose.

I am thankful to CA. Atul Kumar Gupta, President, ICAI and CA. Nihar N. Jambusaria, Vice President, ICAI who inspired me and Research Committee to introduce 'ICAI Research Project Scheme' and undertake research projects on contemporary and relevant topics.

I would also like to extend my thanks to CA. Kemisha Soni, Vice-Chairperson, Research Committee and all the members of the Research Committee.

Further, I would like to take this opportunity to congratulate CA. K Sudarshan for writing Research Report on the topic of "**Inching towards Tax Certainty: Neoteric Domestic Dispute Mechanism for Cross-Border Taxation"** and to express my thanks to Mr. S.P. Singh, Expert for providing his valuable comments and suggestions for improvement of technical and presentation aspect of the Research Report. I also acknowledge the assistance and co-operation rendered by Dr. Amit Kumar Agrawal, Secretary, Research Committee and CA Rahul Paul, Project Associate who gave their valuable inputs during preparation of this Research Report.

I believe and trust that this Research Report will be immensely useful to the members and to others interested.

New Delhi | **CA. Anuj Goyal**
February 2, 2021 | **Chairman, Research Committee**

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Abbreviations

AAR	Authority for Advance Ruling
APA	Advance Pricing Agreement
BAR	Board for Advance Ruling
BEPS	Base Erosion and Profit Shifting
BIT	Bilateral Investment Treaty
CBDT	Central Board of Direct Taxes
CIT-A	Commissioner of Income Tax (Appeals)
DCM	Dispute Containment Mechanism
DPM	Dispute Prevention Mechanism
DRM	Dispute Resolution Mechanism
DRP	Dispute Resolution Panel
G-20	Group of 20 Countries
GAAR	General Anti-Avoidance Rules
IBFD	International Bureau of Fiscal Documentation
ICAI	The Institute of Chartered Accountants of India
IMF	International Monetary Fund
ITAT	Income Tax Appellate Tribunal
LTU	Large Tax-Payer Unit
MAP	Mutual Agreement Procedure
MLI	Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS
MNE	Multinational Enterprise
OECD	Organization for Economic Co-operation and Development
PE	Permanent Establishment

SAAR	Specific Anti-Avoidance Rules
SHR	Safe Harbour Rules
TADAT	Tax Administration Diagnostic Assessment Tool
TPO	Transfer Pricing Officer
UN	United Nations
USA	The United States of America
WTO DSS	World Trade Organization Dispute Settlement System

Scope of the Report

- Certainty in tax is the cornerstone for a sound tax system. In an era where uncertainty is the new normal, the search for certainty in taxation is well and truly on. This report focuses on two significant aspects leading to tax uncertainty, i.e., dispute resolutions on issues arising under cross-border taxation. Tax administrations address tax uncertainty in cross-border tax disputes through an effective domestic dispute mechanism and an international tax treaty dispute mechanism. Dispute mechanism refers to process or mechanics by which parties address their disputes.
- **In-scope:** The report focuses only on the domestic dispute mechanism as they are unilateral and unlike the international tax treaty resolution mechanism. It involves cooperating with other countries and international organizations following Public International Law principles. The report's scope is to assess the existing dispute mechanism under the Indian domestic law and give recommendations to bolster certainty in tax. However, a particular portion of the report briefly suggests areas where international tax treaty dispute resolution can take a cue from non-tax areas for resolving disputes.
- **Exclusion:** This report's scope excludes tax-treaty dispute mechanism for resolving cross-border tax disputes.
- **In-scope contents:** The report has four parts with relevant sub-chapters under them.
  - Part I of this report sets the tone on tax certainty and how a proper dispute mechanism can bolster tax certainty.
  - Part II of this report broadly identifies the effectiveness of the existing domestic dispute mechanism currently in vogue through an online-survey of cross-border tax experts from the industry and practice based on their experience. The survey will act as a qualitative research tool to determine the effectiveness of the existing domestic dispute mechanism.

- Part III of the report suggests an effective dispute mechanism framework for future consideration by the Government of India based on the survey findings in Part II of this report. These suggestions will bolster the tax certainty quotient.
- Part IV of the report provides the concluding remarks to sign off for a better future.

Part I
Setting the Tone for Certainty

Introduction

"The longing for certainty... is in every human mind. But certainty is generally illusion."

Justice Oliver Wendell Holmes

1.1. The quote by Justice Holmes mentioned above, emphasizes the need for certainty in general and how it remains an illusion. Uncertainty has been an integral feature in one's existence. The enigmatic future with what is in store tomorrow accentuates the element of uncertainty. On a philosophical note, the man's quest to determine certainty has been part of this game called life. This quest is exacerbated in recent times due to the pandemic, Covid-19 wherein uncertainty has taken a quantum leap.

1.2. In this elusive quest to determine certainty on various facets, the area of taxation is no exception. Discussion on taxes and certainty cannot go forward, without quoting the cliched but famous lines by Benjamin Franklin, the USA's founding father *"…nothing is certain, except for Death and Taxes"*.[1]

1.3. Tax is certain and inevitable. As Lord Bramwell puts it succinctly *"Like mothers, taxes are often misunderstood, but seldom forgotten"*. Therefore, there is an element of certainty when it comes to levying taxes by a State, but the certainty buck stops there. The functional features of taxation have led to various complexities, eventually paving tax uncertainty. Many empirical studies have time and again established the presence of tax uncertainty.[2] Tax uncertainty is a cause of concern for both the taxpayer and the tax administration. The craving for tax certainty originates from the age-old 'Rule of Law' principle. The rule of law has various definitions attributed to it, Lord Bingham[3] in his seminal book on Rule of Law identified various features associated with the rule of law, with one of them being.

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1 https://www.adamsmith.org/blog/death-and-taxes

2 Hassett, K. and G. Metcalf (1999), "Investment with uncertain tax policy: does random tax policy discourage investment?" *Economic Journal,* Vol. 109, pp. 372-393; Hanlon, M., E.L. Maydew, and D. Saavedra (2016), "The taxman cometh: does tax uncertainty affect corporate cash holdings," *Social Science Research Network*. http://papers.ssrn.com/sol3/Papers.cfm?abstract_id=2292020; etc.

3 T. Bingham, The Rule of Law (Penguin Press 2010).

"The law must be accessible and so far, as possible, be intelligible, clear and predictable; Questions of legal right and liability should ordinarily be resolved by application of the law and not by the exercise of discretion".

One of the universal principles identified by the World Justice Project in its definition on Rule of Law is Just Laws, i.e. "the laws are clear, publicized and stable"[4]. Therefore, certainty and simplicity are hallmarks on the rule of law.

Tax Certainty – Core Principle of Tax Law

1.4. As legal certainty is one of the fundamental pillars of law[5], tax certainty is a fundamental principle of (international) tax law. Certainty is one of the main ingredients for a good tax policy. As a matter of fact, on tax laws, certainty and simplicity are imperative considering that taxation is a significant feature for a state to use its coercive power to collect taxes from its citizen[6]. Taxation, therefore, impinges on the citizen's liberty. Hence, to ensure that the State does not unreasonably impose and collect taxes from its citizen, the rule of law must prevail to constrain the State from exercising its unfettered coercive powers. Therefore, tax certainty plays a significant factor as the taxpayer wants to know precisely how much tax he owes to his country. Similarly, the design of the rule of law principles must ensure that tax shenanigans do not evade in paying their share of taxes by using loopholes or vagueness in the tax law.

1.5. Apart from various benefits tax certainty brings to the table, one core aspect is that it promotes faith in the system, which is an absolute need of the hour in the Indian context.

Defining Tax Certainty

1.6. Tax laws have often faced taxpayers' wrath for being complicated, leading to uncertainty. The USA ex-Senator, Max Baucus, quoted that "Tax complexity itself is a kind of tax". Therefore, simplicity, stability, predictability and clarity are vital for tax law. As per the IBFD Glossary7 , the indicia for tax

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4 https://worldjusticeproject.org/sites/default/files/documents/WJP-ROLI-2020-Online_0.pdf

5 Leawood, Heather (2000). "Gustav Radbruch: An Extraordinary Legal Philosopher". Washington University Journal of Law & Policy. 2: 489

6 Vijay Kelkar and Ajay Shah (Nov. 2019). In Service of the Republic: The Art and Science of Economic Policy. Penguin Allen Lane

7 Fundamentals of Taxation: An Introduction to Tax Policy, Tax Law and Tax Administration (2019), Pistone, Roeleveld & Others edition, IBFD Publication,

certainty is that *"the taxpayer should know exactly what is being taxed, how much he has to pay and how and when he has to pay it, meaning that the law should be clear and unambiguous and the tax authorities' interpretation of it should be readily available"*.

1.7. Tax certainty can be determined in the cross-border investment framework as the capacity to determine the tax costs associated with an investment in a country during its lifecycle[8]. The Indian Supreme Court in the famous Vodafone judgement emphasized on the need for tax certainty as *certainty is integral to the rule of law. Certainty and stability form the necessary foundation of any fiscal system. Tax policy certainty is crucial for taxpayers (including foreign investors) to make rational economic choices most efficiently… Investors should know where they stand."*[9]

Global Agenda on the Need for Tax Certainty

1.8. The global financial crisis in 2009, saw the downfall of the global economy, which eventually saw the rise of G20 as a significant economic policy player. The emergence of G20 as a policy player has been significant, especially on the global economic front.[10] With many initiatives helmed by the G20 on the cross-border taxation front, one significant issue in this regard pertains to the heightened concern about the uncertainty in tax matters and its impact on cross-border trade and investment.[11] Other empirical studies have revealed that tax uncertainty is a cause of concern for investors.[12] Understanding the significance of tax certainty in the international taxation domain, the G20 leaders mandated the OECD and the IMF in identifying areas to strengthen tax certainty.[13]

Netherlands.

[8] THE ROLE OF TAX CERTAINTY IN PROMOTING SUSTAINABLE AND INCLUSIVE GROWTH By Prof. Dr. Jeffrey Owens

[9] Vodafone International Holdings B.V. v. Union of India & Anr., Civil Appeal No. 733 of 2012, arising out of S.L.P. (C) No. 26529 of 2010, Supreme Court of India

[10] Allison Christians, Taxation in a Time of Crisis: Policy Leadership from the OECD to the G20, 5 Nw. J. L. & Soc. Pol'y. 19 (2010).

[11] Devereux, M. (2016), “Measuring corporate tax uncertainty across countries: evidence from a cross-section survey,” Mimeo, Oxford University Center for Business Taxation.

[12] Gulen, H. and M. Ion (2016), “Policy uncertainty and corporate investment,” Review of Financial Studies, Vol. 29, pp. 523-564.

[13] G20 2016 Summit, Hangzhou, China

Economic Uncertainty leading to Tax Uncertainty

1.9. In this present globalized, neo-liberal world that seeks free trade movement of goods and services, tax certainty is a major component to achieve its objective. Considering the uncertain economic world and conflicts between all stakeholders, more so exacerbated by the global pandemic, Covid-19 has led to fiscal uncertainty. With the increasing need to raise revenues and achieve the UN Sustainable Developmental Goals[14], countries are in dire need of revenues and are keen on promoting trade & investments. On the cross-border investment front, legal certainty is a foundational factor in attracting investment and relies, in no small degree, on strengthening the consistency of the international tax system.

India and Tax Certainty

1.10. India was ranked #1 on a global survey conducted in 2016, measuring corporate tax uncertainty across countries. [15] The table in figure 1 is an extract from the survey where the respondents representing MNEs have indicated India as the most uncertain jurisdiction in the corporate tax regime.

Table 6. How uncertain is corporation tax in … ?

On a scale of 1=very uncertain to 5=very certain

Rank	Country	Mean
1	India	1.4
2	Brazil	1.6
3	Russia	1.9

Figure 1 – Extract from the survey [16]

1.11. The global survey findings reflect the dismal State of tax certainty in India and the dire need to improve the tax certainty aspect.

[14] UN Sustainable Developmental Goals, THE 17 GOALS | Sustainable Development (un.org)

[15] Michael Devereux, Measuring corporation tax uncertainty across countries: Evidence from a cross-country survey

[16] ibid

Chapter 2

Dispute Mechanism – Key ingredient for tax certainty

"No matter how thin you slice it, there will always be two sides." -Baruch Spinoza[17]

2.1. Dispute mechanism refers to process or mechanics by which the parties address their disputes. Dispute mechanism includes dispute resolution, dispute preventions etc. In the context of tax-disputes, the OECD-IMF report on tax certainty calls for clear, simple rules and regulations that minimize disputes.[18] The report also highlighted that tax uncertainty creates a risk of discouraging investment. Inter-alia, the major factors leading to tax uncertainty identified in the report based on a survey conducted by the OECD are[19]

- Tax Policy Design
- Tax Administrability
- Dispute Resolution
- Specific International Tax Issues

Of the various factors that mushrooms tax uncertainty, the OECD-IMF report identifies ineffective dispute resolution mechanism as an essential driver of tax uncertainty. Further, the report also indicates that specific international tax issues as a significant factor leading to tax uncertainty. This paper's scope referred to earlier tries to address these two factors to ensure an adequate dispute mechanism to solve cross border tax disputes.

Tax disputes leading to uncertainty

2.2. It is no wonder that tax regulations' uncertainty is a breeding ground for disputes and legal conflicts. Legal disputes are inevitable, as the laws get interpreted through words, words are capable of multiple meanings depending

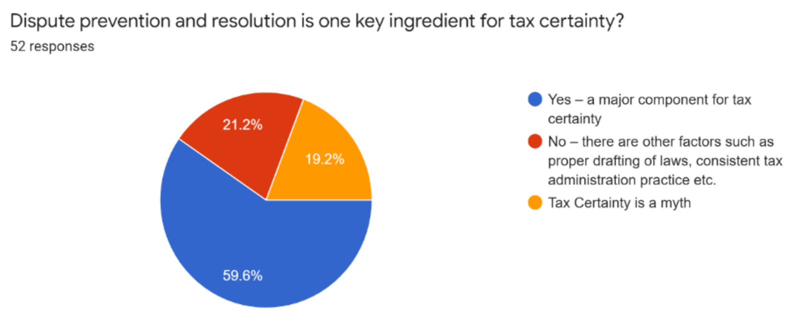
[17]Renowned Dutch Philosopher.

[18] Report on Tax Certainty – IMF & OECD (2017)

[19] Ibid pg.31

on the context.[20] As the famous legal philosopher HA Hart puts it *"words have a penumbra of uncertainty"*. Tax laws are no exception to it, especially considering its dynamic nature. More so in cross-border transactions considering the international tax system's nature, two different tax systems interact with a treaty.

2.3. On the survey undertaken as part of this report which is explained in the next part, 60% of the respondents indicated that dispute prevention and resolution are vital ingredients for tax certainty. Buttressing the fact that an effective dispute mechanism plays a significant role in bolstering tax certainty, an ineffective dispute mechanism will only exacerbate the uncertainty.



Tax disputes stifle India's economic growth

2.4. The Income-tax department is the largest litigant in the economic liigation landscape, with almost 85% of the total number of appeals are filed by the tax department. 21 The figure in Table 1 is an extract from India's economic survey, reflecting the appeals' success rate, which is abysmally low, at losing 65% of its cases. The mounting tax disputes due to protracted litigations have severe ramifications identified in Table 2 for the Indian economy. Therefore, an effective domestic dispute regime augurs well for the Indian economy to bolster tax certainty and a much-needed shot in the arm for attracting foreign investments.

[20] Pagone, Gaetano. 2009. Tax Uncertainty. Melbourne University Law Review 33: 886–907

[21] Chapter 9, Ease of Doing Business' Next Frontier: Timely Justice, India's Economic Survey 2017-18 pg 131-144

Table 1 - Tax Administration's success rate of tax disputes in India

	Direct Tax Cases	
Court	**Success Rate[19]**	**Petition Rate[20]**
Supreme Court	27%	87%
High Courts	13%	83%
ITAT/CESTAT	27%*	88%*

Source: Extracted from The Economic Survey Report, 2017-18[22]

Table 2: Tax Disputes Stabbing the Economy

- High legal costs to the exchequer
- High litigation costs to the taxpayer
- Reduction of investments
- Dent in ease of doing business.
- Promoting legal uncertainty
- Stalling of public infrastructure projects
- Significant burden of judiciary especially the High Courts and the Apex Court.
- Negative public perception as a litigant community

Measuring Tax Certainty through Disputes

2.5. Having discussed the need for tax certainty and how the existing dispute mechanism has contributed to tax uncertainty, we move next to measure certainty. As the modern-day management influencer, Peter Drucker quoted- *"If you can't measure it, you can't improve it"*, therefore, to improve certainty we need to measure it.

2.6. In the search for tax certainty, it is imperative to understand that it is impossible to attain absolute tax certainty due to the tax law's vagaries. An element of uncertainty around is inevitable.[23] Absolute certainty in tax law will remain utopian.

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[22] Ibid

[23] Gribnau, Hans. 2013. Legal Certainty: A Matter of Principle. In Retroactivity of Tax Legislation. Tilburg Law School Research Paper No. 12/2014.

2.7. Nevertheless, as FA Hayek points out *'complete certainty of the law is an ideal which we must try to approach but which we can never perfectly attain'.*[24] Therefore, tax administration should make consistent efforts to achieve tax certainty to ensure economic efficiency and equality in the tax policy. Relative certainty is much desirable than absolute certainty. [25]The degree of certainty can be measured by yardstick which FA Hayek offers: *'the disputes which do not lead to litigation because the outcome is practically certain as soon as the legal position is examined'*. [26]Vanessa Mak also defines this concept as *"the predictability of outcomes in legal disputes."* [27]

2.8. Hence, an efficient dispute mechanism will offer a more considerable degree of tax certainty for all stakeholders concerned with this paper's theme. Therefore, this core part of the paper explores mechanisms that the Indian tax administration can consider invoking to handle cross-border taxation disputes to achieve a certain degree of tax certainty in an uncertain future.

[24] F.A. Hayek, The Constitution of Liberty (Chicago: The University of Chicago Press, 1960), at pp. 208-210

[25] Alexander V Demin, Certainty and Uncertainty in Tax Law: Do Opposites Attract?, MDPI, 2020

[26] ibid supra note 16, at p. 208.

[27] Mak, Vanessa. 2013. Standards in European Private Law: A Model for European Private Law Pluralism. Tilburg Private LawWorking Paper Series, No. 015/2013. July 29. Available online: http://ssrn.com/abstract=2302562

Chapter 3
Cross-Border Tax Disputes: Factors

3.1. In a globalized world, disputes emerging from trade, investments and tax are inevitable. Further, MNE's rapid growth signifies the importance of globalization and the free market. Still, it also brings along, significant disputes and the disputes have been rising exponentially year on year. Dispute mechanism is placed at both the domestic level as well as at the international level through bilateral or multilateral treaties.

3.2. In the view of Thomas, Lai and Kyte,[28] the leading causes of tax disputes are "inconsistent application or interpretations, unclear tax policies and rules, resource constraint, complex administration procedures, insufficient understanding of international tax law, enforcement not following tax treaties, an unintended consequence of domestic practice, inadequate transparency, and other, including non-tax factors."

3.3. Apart from the complexities mentioned, various other factors lead to tax disputes, one of which is legal language due to lousy drafting of laws. Unclear tax law with vague terminologies leads to more disputes.[29] As Christe puts it her seminal paper[30] *"[T]he slightest trace of vagueness will be exploited. Once vagueness has been found, one is free to choose the interpretation of which one approves*". Further, with tax laws being complicated, even if the intentions are right and the law is followed in spirit, there is still a possibility of violation leading to disputes. [31] Further, the tax law apart from being substantive is also

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[28]Rob Thomas, Becky Lai and Justin Kyte, "Discussion Paper on Improving Dispute Settlement among 'Belt and Road' Jurisdictions" in BRITACOM Special Edition, Building a Growth-Friendly Tax Environment in Collaboration with International Taxation in China (April 2019)

[29] Edmiston, Kelly, Shannon Mudd, and Neven Valev. 2005. Tax Structures and FDI. The Deterrent Effects of Complexity and Uncertainty.

[30] Christie, George. 1964. Vagueness and Legal Language. Minnesota Law Review 48: 885–911.

[31] Lawsky, Sarah. 2009. Probably? Understanding Tax Law's Uncertainty. University of Pennsylvania Law Review 157: 1017–74.

procedural, the procedural aspects which complement the substantive aspect of the law, many times leads to tax disputes owing to onerous compliance norms.

3.4. Regarding taxation, cross-border tax disputes are prevalent for various reasons. Some of the factors due to which cross-border direct taxation disputes arise are as follows:

Disputes on account of domestic law	Disputes on account of tax treaty
• Unilateral measures. • Divergent interpretation of tax treaties. • Unilateral Transfer Pricing adjustments. • They are withholding tax issues. • Treaty overrides through Domestic law. • Wrong Qualification and Characterization of incomes due to different interpretations of provisions in a tax treaty. • The heterogenous signing of bilateral tax treaties with different countries' features leads to disputes. • The interpretation conflict between tax treaties and domestic tax laws. • Foreign tax credit denial • Tax avoidance claims due to GAAR and SAAR. • Tax administration issues such as qualified resource, adversarial administration and setting high revenue target collections leading to disputes.	• Tax Treaty Entitlement • BEPS Issues • Issues on account of the interplay between MLI and the bilateral tax treaty. • Double non-taxation through treaty avoidance mechanism such as treaty shopping. • Discrimination • Economic double taxation issues. • Lack of interpretative notes from competent authorities on treaty interpretation. • Very generally worded treaties leading to varied interpretations. • Lack of agreements reached by countries (i.e. Protocols to a tax treaty) to clarify tax treaties or lack authoritative interpretations to tax treaties.

• Procedural infirmities are arising out of domestic law requirement. • Lack of inconsistency in domestic law judicial precedents on cross-border taxation issues.	

3.5. To understand the nature of tax issues common in cross-border taxation, the tax certainty survey undertaken on cross border tax disputes (discussed detailed in Part II, Chapter 5) will be a useful indicator. Unsurprisingly, 83% of the respondents identified transfer pricing dispute as the most common cross-border tax disputes followed by PE issues and treaty entitlement. The OECD MAP statistics also corroborate that transfer pricing dispute garners the largest share on cross-border tax disputes. [32] Figure 2 provides a snapshot of the common cross-border tax issues.

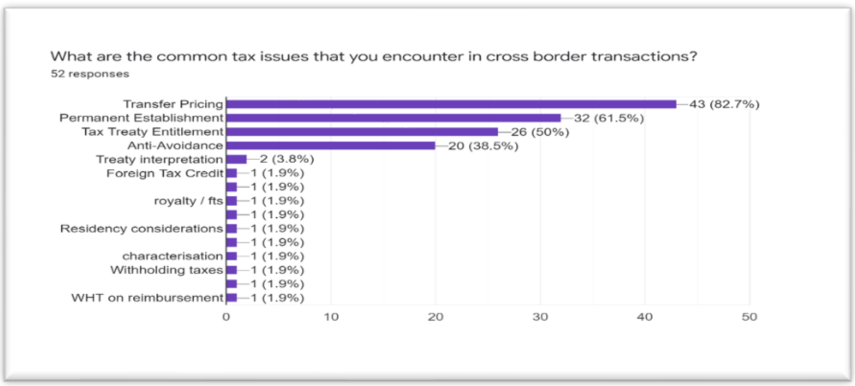


Figure 2- Snapshot of the common cross-border tax issues

3.6. Given the increasing number of cross-border tax disputes, the introduction of tax avoidance tools such as the MLI and the digital economy taxation conundrum will further exacerbate cross-border tax disputes with tax uncertainty looming large. Therefore, it is essential to have an effective dispute mechanism for handling cross-border taxation matters both at the domestic level (in-scope of this report) and the international level.

[32] OECD MAP Statistics, 2019 available https://www.oecd.org/tax/dispute/mutual-agreement-procedure-statistics.htm

Part II
Existing Domestic Dispute Mechanism & its Effectiveness

Chapter 4

Domestic Dispute Mechanism - Current State of Play

4.1. Dispute mechanisms refer to process or mechanics by which parties address their dispute for cross-border taxation issues at the domestic and international levels. Prevention and resolution of disputes at the international tax law level are available in the form of MAP present in the respective bilateral tax treaties. The domestic dispute mechanism is available under the Indian Income-tax Act, 1961 specifying recourse mechanism to prevent and resolve tax disputes.

4.2. The existing dispute prevention and dispute resolution mechanism tools that are in vogue is depicted diagrammatically as in figure 3

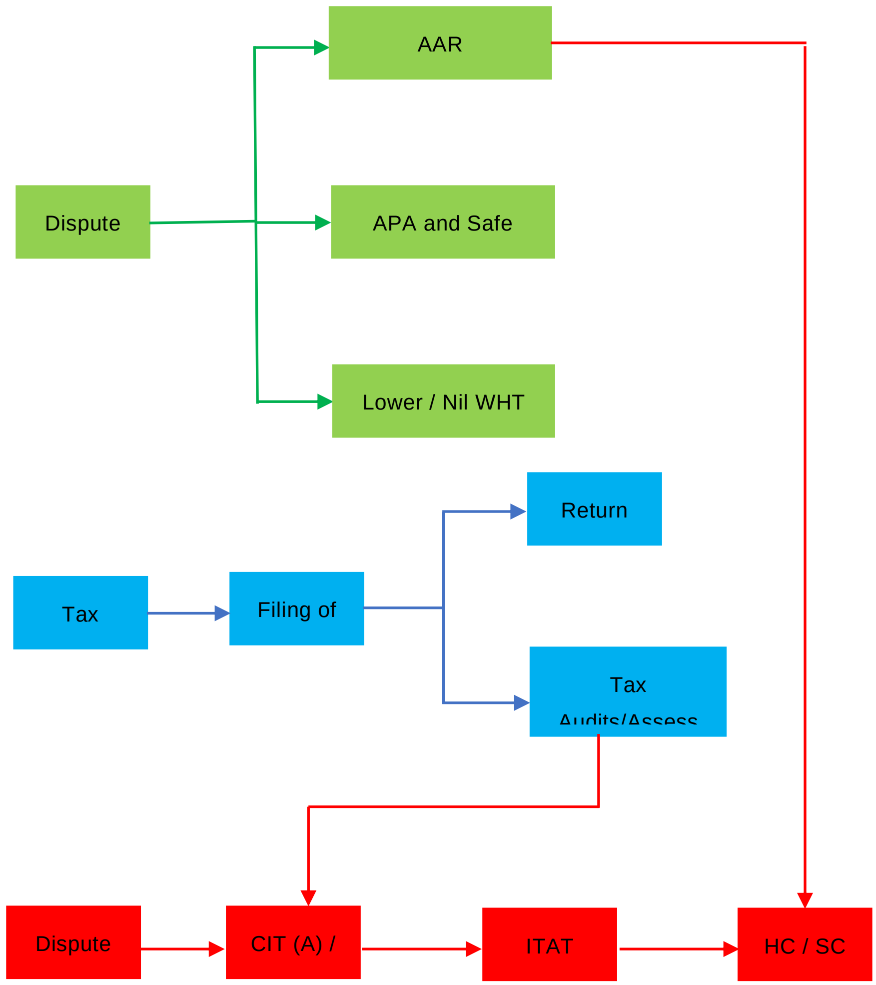
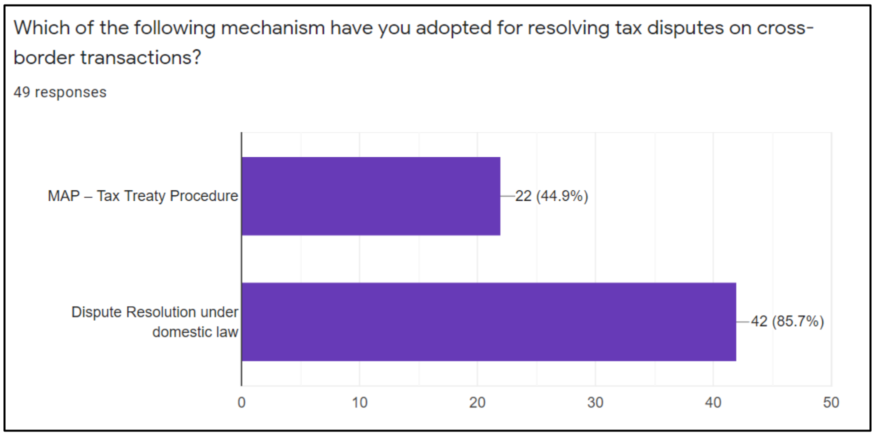


Figure 3

4.3. As part of the survey undertaken in this report, around 86% of the respondents appearing in Table 5, indicated that they have resorted to dispute resolutions under the domestic legislation over tax treaty dispute resolution (MAP). Thereby signifies the importance of having an effective domestic dispute mechanism to curtail cross-border tax disputes.

Table 5


Which of the following mechanism have you adopted for resolving tax disputes on cross-border transactions?
49 responses
MAP – Tax Treaty Procedure
22 (44.9%)
Dispute Resolution under domestic law
42 (85.7%)
0
10
20
30
40
50

Chapter 5

Measuring India's Tax Certainty through Domestic Dispute Mechanism

5.1. As mentioned earlier, one of the ways to measure tax certainty is through the predictability of outcomes on tax disputes. Therefore, the effectiveness of the domestic dispute mechanism will be a perfect yardstick to measure tax certainty. An online survey undertaken amongst tax practitioners specializing in international taxation to determine the dispute mechanism's effectiveness on cross-border taxation matters. The ground-level perspective of the tax experts who are cross-border tax practitioners may reflect the effectiveness of the dispute mechanism tools currently in vogue.

Survey and respondents

5.2. Online surveys are an effective tool for qualitative research as they provide richness and depth on the research topic.[33] The present survey was aimed exclusively at cross-border tax professionals Pan-India, some of whom are tax experts from the industry and rest are tax advisors who act as external consultants/counsels. The survey respondents were sent a detailed questionnaire (Appendix II) with views sought on

- tax certainty,
- effectiveness of existing dispute prevention and resolution mechanism on cross-border taxation both at the domestic and international level,
- Future of cross-border tax disputes

5.3. The questionnaire was designed to cover the entire framework of the dispute mechanism beginning from the commonly faced cross-border tax disputes to the future of cross-border tax disputes, however with significant emphasis on effectiveness of the existing domestic dispute mechanism. Total

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[33] Virginia Braun, Victoria Clarke, Elicia Boulton, Louise Davey & Charlotte McEvoy (2020) The online survey as a qualitative research tool, International Journal of Social Research Methodology, DOI: 10.1080/13645579.2020.1805550

of 52 respondents, who are tax professionals from various regions of the country, responded to the questionnaire with their views. The professional background of the respondents was a blend of experts from the advisory as well as in the litigation practice. Table 3 highlights the background of the respondents.

Table 3: Background of the Survey Respondents

Number of respondents	52
In-house tax professionals	15
External consultants/advisors/counsel	37

Chapter 6

Survey Observation on the Effectiveness of the Existing Domestic Dispute Mechanism for Cross-Border Taxation

6.1 Dispute Prevention Mechanism

The DPM tools' broad features and the tool's effectiveness are provided in a tabular format to reflect the features of the DPM and compare its effectiveness as indicated by the survey respondents.

DPM Tools	Key Features	Effectiveness
Authority for Advance Rulings (AAR)[34]	• AAR is a quasi-judicial body introduced as a dispute avoidance mechanism majorly for the cross-border transaction. An applicant could seek clarity, i.e., private ruling on tax liability on particular cross-border transaction activity. • Private Rulings of the AAR are binding on the taxpayer (i.e. the applicant) and the tax authorities regarding the transaction for which the ruling was sought. • However, the ruling may	On the effectiveness of AAR as a DPM tool: (Chart 1 of Appendix I) • Almost **60% of** respondents indicated ***that AAR is ineffective*** due to various schemes' shortcomings. • Only 10% of the respondents indicated that it is effective and attributing certainty as a significant AAR feature.

[34] Chapter XIX-B of the Income tax Act, 1961

	be challenged before the High Court and subsequently before the Supreme Court at the instance of either applicant or the tax authorities.	
Advance Pricing Agreement (APA) [35]	• APA, as the name indicates, is an ahead of time agreement between a taxpayer and tax authority for determining the transfer price of certain transactions that may take place in the future • Taxpayers can enter into an APA for a full five years in the future and four years of past period (under roll-back). • Taxpayers can obtain certainty from a transfer pricing perspective for a maximum of nine years (including roll-back). • The taxpayer can prefer a multilateral/ bilateral or unilateral APA. Unilateral APA is a domestic mechanism; Bilateral/Multilateral APA is an international mechanism as it involves two or more tax authorities to interact.	Effectiveness of APA as a DPM tool: (Chart 2 of Appendix I) • **56%** of the respondents indicated that **APA is effective** on account of the following reasons: 1. The applications are disposed of in a time-efficient manner compared to other DRM. 2. APA team is pragmatic and knowledgeable compared to field officers. 3. Certainty in margins. 4. Compliance conditions / critical assumptions are spelt out clearly. The panel is receptive of business considerations and not purely revenue-driven.

[35] Section 92CC & 92CD of the Income Tax Act, 1961

Safe Harbour Rules for transfer pricing [36]	• SHR provides for circumstances in which a certain category of taxpayers can follow a simple set of rules under which the revenue authorites automatically accept the transfer prices. • The objective of SHR is to provide compliance relief, administrative simplicity, minimizing tax audit scrutiny and certainty thereby avoiding litigation.	Effectiveness of SHR: (Chart 3 of Appendix I) • **39%** of the respondents indicated that they have **never opted** for SHR. • **35%** of the respondents indicated that SHR is **effective** on account of the following reasons**:** 1. Certainty, 2. Reasonable rates for captive business units of MNE 3. Ideal for medium-sized business 4. Less complex
Lower / Nil Withholding tax certificates [37]	• In a case where a taxpayer/tax deductor consider that withholding tax rate is greater than the actual tax liability, then such taxpayer could file an application before the tax authority for a lower/nil withholding tax certificate. • Further, the payee could also apply to determine the income chargeable to tax in India.	Effectiveness and experience in obtaining withholding tax certificates: (Chart 4 of Appendix I) • **37%** of the respondents indicated that this mechanism is **ineffective** as it is prejudiced in favour of the revenue. • **27%** indicated that obtaining the certificate is **cumbersome and time-consuming.** • 17% indicated that the process is seamless and effective.

[36] Section 92CB of the Income Tax Act, 1961

[37] Section 195(2) and Section 197(1) of the Income tax Act, 1961

6.2 Dispute Resolution Mechanism

The table below highlights the broad key features of the dispute resolution mechanism tool and its effectiveness based on the survey results.

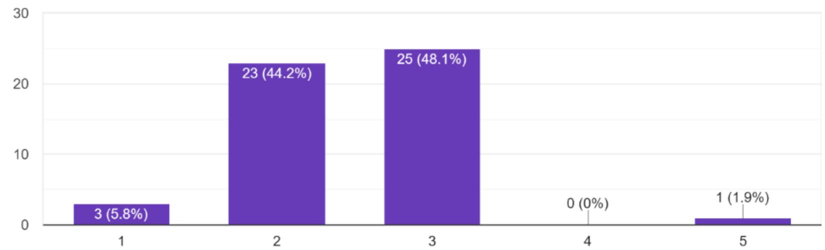
DRM tools	Key Features	Effectiveness
At the assessment stage	• In India, Onus is on the taxpayer to perform self-assessment and file the tax authorities' income tax return. • The Centralized Processing Center of Income-tax authorities would process the return filed. • Based on specific criteria and random sample basis, some taxpayers would be selected for a detailed tax audit by the tax authorities. • Upon examining documents/returns, the tax authorities would pass an order with demand/refund.	Effectiveness of handling the disputes at the tax audit level: (Chart 5 of Appendix I) • **92%** of respondents indicated that the dispute resolution at the tax audit level, i.e., tax authorities' assessment, is **ineffective and acts as a breeding ground for tax disputes**. • The two major reasons by the respondents for an ineffective tax assessment at the administration level is attributed to: 1. Unreasonable targets (89%) 2. Insufficient knowledge of the tax authority at the administration level (53%)
First Appeal - DRP & CIT (A)	**CIT (A)** As a traditional litigation process, a taxpayer, if he is not in agreement with the order passed by the Tax Authorities (i.e. Assessing Officer) could appeal against the order before the Commissioner	Preferred mode between CIT(A) and DRP: • **61%** of the respondents prefer **CIT(A**) & 39% opted for DRP. (Chart 6 of Appendix I) Effectiveness of DRP • **96%** of respondents mentioned that **DRP is ineffective** and failed to

	of Income-tax (A) • CIT(A) is a quasi-judicial body that has to dispose of the taxpayer's appeal. **DRP** • Alternatively, Certain taxpayers (foreign Companies or taxpayers having transfer pricing issue) have an option of approaching Dispute Resolution Panel ('DRP'), which is a collegium of three Commissioners of Income-tax. • The DRP is to dispose of disputes arising from tax audit in a time-bound manner, thereby acting as an alternative dispute resolution mechanism to other options such as CIT (A).	achieve its intended objective by often taking pro-revenue sides without fair adjudication. (Chart 7 of Appendix I) Effectiveness of CIT(A) • **79%** of the respondents indicated that **CIT(A) is ineffective**. (Chart 8 of Appendix I)
ITAT	• ITAT is the second appellate authority and a quasi-judicial institution set up by the Central Government under the Ministry of Law and Justice's auspices. • Any of the aggrieved party will file the	Effectiveness of the ITAT in resolving cross border taxation issues: (Chart 9 of Appendix I) • **67%** of the respondents indicated that **ITAT effectively resolves** tax disputes. • ITAT's effectiveness specifically on TP issues as the final fact-finding body:

	appeal before ITAT. There are monetary thresholds based on the tax effect for filing an appeal at the ITAT by the revenue authorities. • ITAT is the final fact-finding authority.	(Chart 10 of Appendix I) 1. **52%** of the respondents indicated that the **ball is shifted back** to the TPO for adjudication. 2. **35%** of the respondents indicated that the **ITAT effectively resolves TP disputes.**
iv) Judicial Level- High Courts and the Supreme Court	• Tax-payer or the Income-tax authorities if aggrieved by order of the ITAT and can file an appeal on a substantial question of law before the High Court. • Supreme Court is the final dispute resolution forum. Tax-payer / Tax authorities aggrieved by the High Court order could file an appeal before the Supreme Court. • There is a monetary threshold on tax effect to be crossed to appeal before the High Court and Supreme Court by the revenue authorities.	Effectiveness of the judicial forum in resolving cross-border tax disputes: (Chart 11 of Appendix I) • **77%** of the respondents indicated that the **judicial forums are effective** in resolving cross-border tax disputes. • Consistency in the interpretation of the law for fostering certainty on issues in cross border tax disputes: (Chart 12 of Appendix I) 1. **60%** of the respondents indicated that the judicial forums are **consistent in** their approach and follow the rule of law principle.

6.3 Tax Certainty under Existing Dispute Mechanism

- The survey respondents were to rate on the scale of 1-5 with Five (5) being 'extremely certain' to 1 being "no certainty" on how the existing dispute prevention and resolution mechanism for cross border taxation have fostered tax certainty.



The responses indicate the level between 2-3 to indicate that the existing dispute prevention and resolution mechanism does not offer even a moderate tax certainty level.

Chapter 7

Survey Results and Diagnosis

"Study the past if you want to define the future."

Confucious

The following aspects emerge concerning the domestic dispute mechanism's effectiveness for cross-border taxation on diagnosing the survey.

7.1 Dispute Prevention Mechanism – Findings

7.1.1. *AAR* is ineffective as a DPM and needs further strengthening to make it effective. The reasons for ineffectiveness and failure to achieve its objective in preventing disputes are due to:

- Time-consuming and inordinate delay in providing the ruling.
- Administrative infirmities – non-functioning owing to lack of resources.
- The ruling is not final and is appealed in the High Court and Supreme Court leading to protracted litigation.
- Lack of interpretative consistency in the rulings.
- Lack of competent judges to handle international taxation issues.

7.1.2. *APA* is the most effective DPM tools amongst the domestic dispute mechanism, as unilateral APAs are part of the domestic mechanism. With more than 300 APA signed, tax certainty quotient is undoubtedly high and augurs well for all the stakeholders concerned.

7.1.3. *Low/Nil withholding tax certificate* tool is ineffective as a dispute prevention mechanism to determine the transaction's taxability. With time-consuming and cumbersome process coupled with the unfair determination of taxability by the revenue, authorities have made this forum ineffective according to the majority of the respondents.

Table 4: Survey findings - DPM Effectiveness and Certainty

Tools	DPM - Effectiveness	Tax Certainty
AAR	Not Effective	No
APA	Effective	Yes
SHR	Neutral	Moderate
Withholding tax certificates-Low/Nil	Not Effective	No

7.2 Dispute Resolution Mechanism – Findings

7.2.1 Tax Assessment and audits by the tax administration are a significant cause of tax disputes, consequently paving the way for protracted tax disputes. Around 92% of the survey respondents indicated that dispute resolution is ineffective at the tax audit level and is the cause for rising tax disputes. Thereby demonstrates that the tax officers at the assessment stage are not effective in concluding the assessments for cross-border transactions. The tax assessment's ineffectiveness is due to the reasons showcased in figure 4. As can be observed, the biggest reasons attributed to ineffective tax assessment is due to

- unreasonable targets on tax authorities by the administration,
- Limited knowledge of the tax authorities absent sufficient training on cross-border transaction issues,
- Limited availability of time to complete the audits and
- Non-adherence to the rule of law.

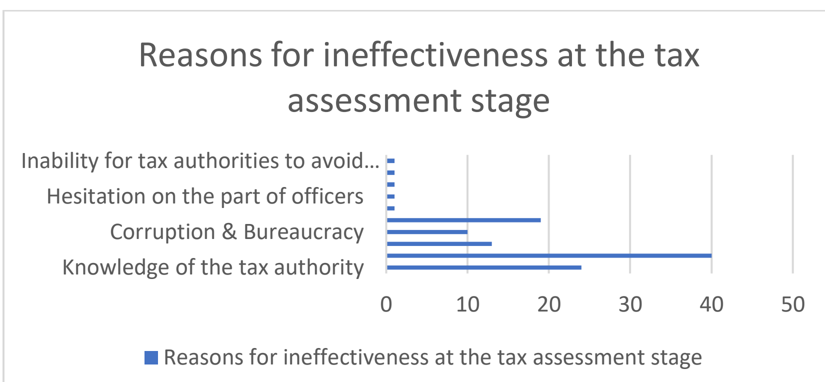


Figure 4 – Reasons for ineffectiveness at the tax assessment stage

7.2.2 DRP and CIT(A), the first appeal forums, are ineffective for resolving cross-border taxation disputes. Regarding the DRP, set up as an alternate dispute resolution mechanism for speedy disposal, almost the entire population of respondents (96%) indicated it as ineffective. The 4% of the survey population, which considers DRP has achieved its intended objective, perceives that DRP is better placed to appreciate the technical matters compared to CIT(A). Further, the respondents perceive that a certain degree of reasonableness and targets are also not the driving force for determining the outcome, thereby bringing neutrality. However, as can be observed, most of the respondents opine that DRP has not achieved its intended objective because DRP panel is biased against the taxpayer and works in favour of revenue and lacks independence.

7.2.3 ITAT is the final fact-finding body has been useful as a dispute resolution mechanism, according to the majority of the respondents. However, half the respondents (52%) opine that when it comes to transfer pricing disputes, the ITAT is passing the buck back to the TPO to redetermine the issues rather than prefer the ITAT to resolve the dispute attain finality instead of beginning the second innings.

7.2.4 Judicial forums such as the High Court and the Supreme Court have effectively resolved the disputes. However, the survey highlights that the High Court and Supreme Court are not consistent in approaching the tax issues, thereby leading to tax uncertainty by creating umpteen number of diversified precedents.

Table 4: Survey findings - DRM Effectiveness and Certainty

Tools	**DRM - Effectiveness**	**Tax Certainty**
Assessment Stage	Not Effective	No
DRP/CIT(A)	Not Effective	No
ITAT	Effective	Moderate
Judicial Forums- High Courts and the Supreme Court	Effective	No (due to lack of consistency and deviation from binding precedents)

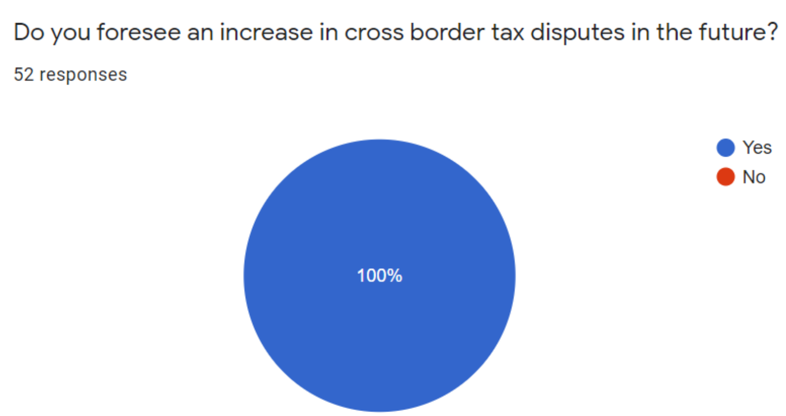
Part III
Certainty in an Uncertain Future

Chapter 8

Domestic Dispute Mechanism – Architecture and Philosophy

8.1. As already discussed above in Part I, one of the primary reasons for India's low tax revenue productivity is due to a significant amount of tax revenue held in disputes. These large tax disputes have dented the faith in the tax system, thereby fostering a hostile tax regime. Hence, if the tax administration can resolve tax disputes with an effective framework or if stakeholders can avoid disputes at the first instance, it will foster certainty, predictability and stability in the tax system from a taxpayer perspective. From a tax administration perspective, reducing tax disputes will pave the way for effective tax collection leading to a tax-gap ratio reduction. The certainty in the system will also broaden the tax base.

8.2. On the future of cross-border tax disputes, with the advent of a plethora of anti-avoidance rules both general and specific, the advent of MLI, Digital economy taxation, unilateral taxation measures, dynamic tax policies, dynamic business mechanics, the cross-border tax -disputes are bound to increase further. On the survey that we had undertaken for this report (in Part II) to understand the level of cross-border tax disputes in the future, 100% of the respondents indicated that there would be an increase in cross-border tax disputes. These results amplify further the need for an effective dispute mechanism is imperative.

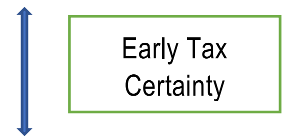


The architecture of the dispute mechanism framework consists of the three-layer structure of

i) *Dispute Prevention Mechanism*

ii) *Dispute Containment Mechanism* and

iii) *Dispute Resolution Mechanism.*



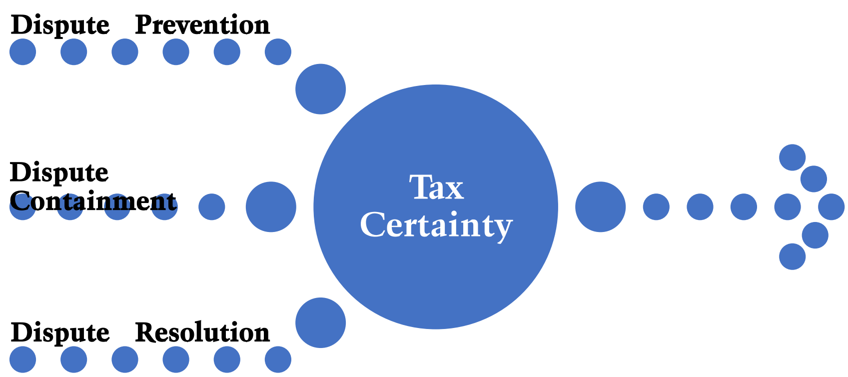


Figure 5: Tax Certainty -Horizontal Layer

8.3. The three-layered structured can be looked into as horizontal layers as depicted in figure 5 with each dispute mechanism independently paving the way for tax certainty. Alternatively, the three-layer structure may be depicted as a step-down process, as in figure 6. The three-layered design ensures that in the first layer on dispute prevention, tax disputes are prevented or avoided from occurring. The second layer on dispute containment, disputes are handled by the tax administration and resolved at an early stage to ensure it is not aggravated into a protracted litigation battle. The third and final layer on dispute resolution is to ensure tax disputes are resolved by the dedicated tax tribunal or judicial courts. The first two layers will mostly be in the purview of tax administration. They must ensure that majority of the disputes will be resolved within these two layers for an effective domestic dispute mechanism.

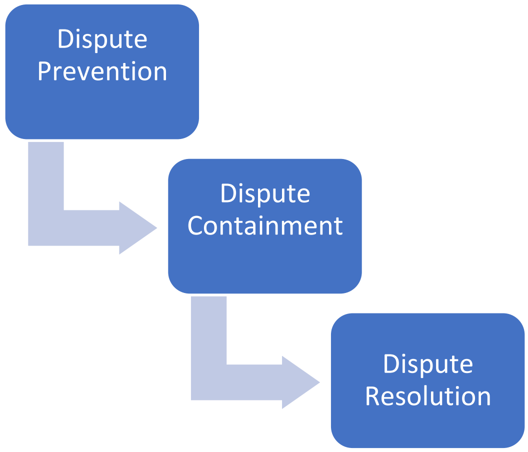


Figure 6 Tax Certainty – Vertical Layer

Early Tax Certainty

8.4. The domestic dispute mechanism's design ensures that significant focus must be on *the first two layers*, i.e., the dispute prevention & the dispute containment to ensure early tax certainty. Early tax certainty is imperative because any state's tax policy objective is to collect maximum revenues with minimum costs incurred on collection & compliance. Tax disputes have a two-pronged effect. On the one hand, it increases the cost collection in litigation costs. On the other hand, it creates economic distortions as tax disputes foster uncertainty and adversity in the system. Therefore, the earlier, the disputes can be resolved better for the State. The significance of dispute prevention and dispute containment in legal disputes is well summed up the United Kingdom's Civil Justice Council report in the context of civil disputes:[38]

"Paradoxically, at a time when saving costs is a government priority, we propose that the courts extend their scope— beyond dispute resolution to include both dispute containment and dispute avoidance. Our assumption is that better containment and avoidance of disputes will greatly reduce the number of disputes that need to be resolved by judges . . . This could be the legal world's 'fluoride moment'—

just as putting fluoride in the water in the 1950s radically reduced the need for dental work on tooth decay, then, similarly in law, appropriate

[38] ONLINE DISPUTE RESOLUTION FOR LOW VALUE CIVIL CLAIMS , Civil Justice Council, 2015, United Kingdom available at Online Dispute Resolution (judiciary.uk)

investment in containment and avoidance should greatly reduce the number of cases coming before our courts".

8.5. Therefore, the tax administration's emphasis on tax dispute prevention and containment will go a long way in bolstering tax certainty. The design summary is as follows –

Layer	Mechanism	Objective	Key Factor
I	Dispute Prevention	Preventing or avoiding *disputes* in the first instance.	Early Tax Certainty by Tax Administration
II	Dispute Containment	Extinguish disputes at the tax administration level to ensure the dispute doesn't spread further—d*e-escalation of disputes.*	
III	Dispute Resolution	*Resolution in this layer through the judicial Court should act as a last resort to resolve complex tax disputes to ensure consistency and law rule*.	Tax Certainty by Judicial and Quasi-Judicial forums

Chapter 9
Tax Administration – The Chief Architect for Tax Certainty

9.1. Before we get into the dispute mechanism options, the chief architect for an effective dispute mechanism is the tax administration. As much as tax laws cover the substantive aspect of what, who, and how much to levy, the tax law's procedural aspect governs the taxes' collection. The power to collect the taxes and enforce levy is on tax administration. [39]

Tax Administration is Tax Policy

9.2. The tax administration is tax policy and more so for developing economies.[40] The main objective of tax policy is to ensure taxes get collected with a minimal cost in terms of compliance and economic distortions. Therefore, a tax system's administrability is the cornerstone and core feature for a sound tax system. [41] A tax system can achieve its objectives, only when effectively and efficiently administered, thereby act as a protagonist for fostering tax certainty. [42]

9.3. Handling disputes is one of the tax administration's primary functions, as shown in figure 7. Access to timely and cost-effective dispute process is one factor in a rule of law system. The Tax Administration Diagnostic Assessment Tool,[43] an assessment tool for evaluating tax administration has

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[39] *Fundamentals of Taxation: An Introduction to Tax Policy, Tax Law and Tax Administration (2019), Pistone, Roeleveld & Others edition, IBFD Publication, Netherlands*

[40] Milka Casanegra de Jantscher. 1990. Value added taxation in developing Countries, World Bank Administering a VAT, M. Gills, C. S, Shoup and G. P. Sikat (eds)

[41] *Fundamentals of Taxation: An Introduction to Tax Policy, Tax Law and Tax Administration (2019), Pistone, Roeleveld & Others edition, IBFD Publication, Netherlands*

[42] M Govinda Rao and Sudhanshu Kumar, Envisioning Tax Policy

for Accelerated Development in India, NIPFP, New Delhi (2017)

[43] TADAT is a tool that has been developed by international development partners, with technical input from a wide range of experts, to help make tax administrations around the world more efficient and fair. It provides an independent, standardized,

identified, *'adequacy in resolving tax disputes'* as one of the performance outcome areas. [44] The desired outcome for TADAT is a fair, independent, time-bound dispute process which is accessible and useful in resolving tax disputes.[45] Therefore, dispute management is a building block for efficient and effective tax administration. India's tax administration adequacy in resolving tax disputes is not available as part of the TADAT assessment. Nevertheless, tax certainty is possible if the disputes are handled effectively and, in a time, bound manner.

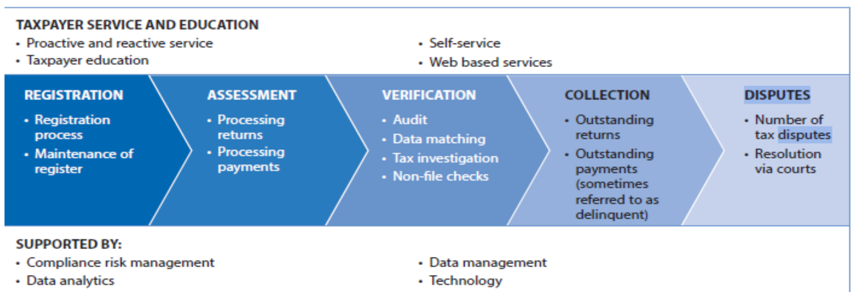

Figure 7: Functions of Tax Administration- Handling Disputes.

Source: OECD Tax Administration 2017: Comparative Information on OECD And Other Advanced And Emerging Economies.

evidence-based, quality-assured, all-round assessment of the performance of a tax administration system. Available at TADAT

[44] OECD (2016), *Tax Administrations and Capacity Building: A Collective Challenge*, OECD Publishing, Paris.

http://dx.doi.org/10.1787/9789264256637-en

[45] TADAT Field Guide, 2019 Edition

Chapter 10

Layer I -Dispute Prevention Mechanism

10.1 The adage *"Prevention is better than cure"* holds good not only for diseases but also for disputes. Disputes are akin to disease and cause significant distress to all the stakeholders concerned. The distress is in tax disputes creating socio-economic distortions for the State. One need not emphasize the significance of vaccination, especially in the current pandemic world. The pandemic has left an indelible mark by taking many lives and causing economic disruptions. Therefore, drawing an analogy from the medical field, adequate dispute prevention mechanisms act as a legal vaccination for the disease that the stakeholders are fighting in tax disputes.

A shot in the arm

10.2 Dispute prevention or dispute avoidance tools are a shot in the arm to foster tax certainty and stability in the modern-day world. Global trade is so intertwined and inter-connected with 60% of world trade taking place within multinational enterprises.[46] The advent and surge in MNE activities have been a major boost to commerce. Still, it also brought a migraine to the tax world in the form of transfer pricing disputes, which is one of the significant cross-border tax disputes that the tax-world is grappling with for quite some time. Therefore, there is a definite need for an effective dispute prevention mechanism for a seamless global trade.

[46] Available on http://oecdinsights.org/2012/03/26/price-fixing/ (last accessed on 12 February 2019).

DPM Tools

10.3 Authority for Advance Ruling 2.0 – Private Rulings

Constitution of BAR – Curing the symptom and not the disease

- **At the time of this report going for publication, the Indian Government in the Union Budget 2021, vide Finance Bill 2021, has proposed to abolish the existing AAR scheme under the Indian Income-tax Act.[47] The failure of the AAR has been duly noted by the Government in its memorandum to the finance bill. The AAR is replaced by the new Board for Advance Ruling (BAR). The BAR unlike the AAR will not have any retired judges of SC/HC and instead will consist of two tax officers not below the rank of chief commissioner. The rulings of the BAR is neither binding on the tax-payer applicant or the department. The effective date of BAR is yet to be notified.**
- **Even though the Government has replaced the ineffective AAR, the efficiency of the new constitution of the BAR will be under scrutiny especially that the BAR is comprised of revenue officers. The fear of BAR turning into a DRP is not far-fetched. One needs to take cognizance that the AAR was ineffective due to its administrative shortcomings such as appointment of judges etc, but from a justice perspective has a reputation of being bipartisan, neutral, and fair while delivering justice in its rulings as the AAR was headed by a retired judge of the Supreme Court.**
- **Notwithstanding the proposed new BAR, the Government may still consider the recommendations provided below and can revisit its stance for an effective AAR 2.0 which will serve as an effective tool for cross-border tax dispute prevention mechanism. The AAR 2.0 needs little tinkering and does not warrant a demolition as the foundations are strong.**

10.3.1. AAR has been one of the foremost dispute prevention mechanism tools deployed in many countries including India for cross-border taxation matters. The advanced ruling mechanism's core objective was to provide tax certainty to foreign investors in India and prevent tax disputes. The AAR's

[47] Finance Bill 2021, new section 245OB to be introduced in the Income Tax Act

private ruling procedure determines the taxability on particular transactions undertaken or proposed to be undertaken by a taxpayer.

Withering on the vine

10.3.2. Being an independent quasi-judicial body, the AAR's foundations laid in 1994 when introduced as a dispute prevention scheme were strong and solid. The procedure met the taxpayers' expectations, paving way for tax certainty and reducing disputes. However, the initial good work withered away slowly and was on hibernation mode at one point in time. A promised start that did not last long.

10.3.3. The Government of India made efforts to revamp the AAR function by waking it up from its slumber by increasing the benches, however the system is not fully active yet due to infrastructural and administration infirmities. As the foundations are well laid, AAR 2.0 has a new avatar can emerge if few leakages are plugged for the betterment of all stakeholders including tax administration as it will prevent disputes apart from bringing in certainty. The shortcomings led to taxpayers looking at other mechanism to resolve disputes, which was evident from the fact that the AAR received only a record low of twenty-eight applications during the FY 2018-19.[48] Therefore, the Government must focus on additional strengthening measures to ensure AAR does not wither on the vine.

10.3.4. Strengthening of AAR mechanism in India – AAR 2.0

S.no	Measures	Recommendation
A	Timelines	• Strict adherence to the timeline specified under the statute to deliver the ruling within six months from the receipt of the application by the AAR.[49] The timeline within which the ruling must be pronounced was an eye-catching feature and strengthened the tax certainty factor. Since advance rulings are also sought for transactions that are ex-ante events, the rulings will

[48] Annual Report 2018-19, Ministry of Finance, India, available at Annual Reports | Department of Economic Affairs | MoF | GoI (dea.gov.in)

[49] The time limit is only recommendatory in nature.

		provide much-needed certainty in preventing tax disputes.
B	Capacity building – for consistency	• Currently, the time limit specified for providing a ruling by the AAR is being delayed due to resources and judges' inability to adjudicate the ruling. Even though efforts are made by the Government of India to revamp the AAR function by increasing the benches, the timely appointment of the adjudicating members will help in providing ruling within the recommended statutory time limit. • Apart from the personnel resource, other capacity-building programmes like regular training programmes for members in the AAR by cross-border tax experts from other jurisdictions, support staff by young cross-border tax professionals as researchers, etc. will give teeth for its functioning. The objective of the AAR must ensure there is consistency in its rulings despite the fact that the precedents have only persuasive value. Nevertheless, a rigid or mechanistic application has to be avoided.
C	Institutionalization	• The advantage of institutionalization is transparency, predictability and independence. Even though the existing framework has been institutionalized, there is scope for strengthening it further. The ITAT, which is also a quasi-judicial body, is a benchmark for AAR to emulate. Further retired ITAT members can also be appointed as judges for the AAR to address the shortfall.

		• With a proper functioning secretariat with case rosters, adequate members permanently appointed, regular publication of all the rulings, frequent interaction with the taxpayer community to hear grievances etc. are hallmarks of institutionalization.
D	Use of Technology	• Technology has been a silver lining amidst the pandemic cloud. With 'online courts', 'virtual hearings' becoming a new normal and common phenomenon, the AAR can embrace virtual hearings on a regular basis. Apart from the speedy delivery of the rulings, litigation cost to the Government can be reduced. With benches functioning only in limited jurisdiction currently, online AAR court can be a panacea for clearing the backlog of cases in a time-bound manner especially for taxpayers present in other jurisdictions who can avoid travel for safety reasons and also avoid adjournments. Further, these hearings will boost *'information transparency'* (subject to privacy guidelines). The hearings transcripts can also be made available, enabling a more transparent system and can be utilized for the next stages of the dispute.
E	Infrastructural collaborations	• On the physical hearing front, the AAR can conduct short camps similar to the ITAT in other cities where benches are not established. The ICAI had recently offered its campus to the ITAT for

		conducting camps.[50] The ICAI, through its offices in various locations of the country, can offer similar such facilities to the AAR as well for hearings and expedite the rulings. Legal universities equipped with courtroom facilities for moot sessions can also be an option. These collaborative approaches will arrest the infrastructural shortcomings, save costs to the Government, and incidental benefits for aspiring tax professionals to learn from witnessing the hearings on real-time at their campuses.

10.4. Diagnostic Tools to Prevent Disputes - Public Rulings, Public Advice, Legal Companion Note etc.

10.4.1. Tax diagnostic tools in the form of Public Rulings, guidance notes, and public advice will be an effective mechanism to prevent disputes and provide clarity to the taxpayers. These are invaluable resources that a taxpayer will seek to ascertain the tax position. Currently, the CBDT guides specific tax issues in circulars, frequently asked questions (FAQs), guidance note etc. This CBDT advice and guidelines are a much-needed tool for dispute preventions as they provide the tax administration's perspective on how the law is applied.

10.4.2. For example, the recent guidance issued on MAP [51] is a convenient and helpful tool for the taxpayers as these guidance notes are desirable since it provides certainty and clarity to taxpayers. However, these guidance notes are far and few between when it comes to cross-border taxation matters.

10.4.3. Therefore, the following aspects are worth considering by the CBDT as part of the taxpayer service, a win-win proposition for both the significant stakeholders concerned. It will prevent disputes and bolster certainty. Further, even if the disputes advance, the guidance tools may act as interpretative tools for the judiciary in resolving the tax disputes.

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[50] http://icaitv.com/news/1105/icai-offers-its-infrastructure-itat

[51] F.No. 500/09/2016-APA-I dated 7th August 2020. Available at MAP-GUIDANCE-7th-August-2020.pdf (incometaxindia.gov.in)

S.no	Tool	Objective
A	**Co-operative Compliance Scheme -** *Lessons from the failure of the Large Taxpayer Unit*	• Co-operative compliance entails resolving disputes through a collaborative approach between the taxpayers and the tax administrations. The cooperation will improve tax compliance mechanisms, and dependency on tax audits will reduce. For the taxpayers, early tax certainty is possible. • As per the OECD-IMF[52] "*Co-operative compliance programs are compliance risk management strategies used by revenue bodies that focus on effectively influencing and improving taxpayer compliance behaviour. Designed to establish voluntarily a relationship based on cooperation and trust between taxpayers and revenue bodies".* These resolutions at the tax administration level provide for containment of disputes bolstering early tax certainty. Co-operative compliance mechanism, the essence is on the relationship between the taxpayers and the tax administration, is mutual trust and cooperation. Many countries across the globe have already introduced this mechanism. • Co-operative compliance schemes are designed primarily for large corporates being the major contributors to the revenue kitty. India in 2005 introduced and established Large Taxpayer Units (LTU). The LTU, set up as a single-window clearance point for direct and indirect taxes at the central level. The objective of LTU was to strengthen the relationship of the tax administration with the taxpayers, where the tax administration

52 Tax Certainty, IMF/OECD Report for the G20 Finance Ministers, 2017

		nominated a client executive to liaise with large taxpayers for seamless functioning. The taxpayers could be part of the LTU without any compulsion. • Unfortunately, the LTU failed to achieve its desired objectives viz., preventing disputes, increased tax revenues, strengthening the taxpayer's relationship, etc. The scheme's failure was also buttressed with low patronage amongst the large taxpayers to opt for the LTU fearing harassment on tax collection. The failure could be due to increasing tax revenue targets, wherein the large taxpayers could prove to be cash cows to milk revenues resulting in more disputes. • With faceless assessment and the advent of technology, India's scene is perfect for reintroducing co-operative compliance mechanisms for large taxpayers who are generally MNE, especially on cross border taxation matters. With international taxation jurisdiction outside the scope of faceless assessments, an effective compliance model will produce intended objectives of preventing disputes and providing early tax certainty. • An effective co-operative compliance model will provide the following results: a) ***Tax Certainty*** – Early tax certainty helps, as the taxpayer will determine tax positions for complex issues and avoid substantial tax demands. Assurance from tax authorities will mitigate tax risks. Further, tax audits will be precise and straightforward without any harassment. The system works on a reciprocal arrangement wherein the tax administration commits making tax compliance more straightforward and more secure. On the other hand, taxpayers must

		act in good faith, minimizing exposure to penalties and interest. This process means that, rather than looking retrospectively at past returns and transactions, both taxpayer and tax administration focus on the present and the future.[53] These features augur well for the overall investment framework for the country as well. b) ***Transparency*** – Increase transparency between the taxpayer and the administration with proper disclosures leading to reporting uncertain tax positions, which will help determine certainty from the tax administration. c) ***Improved Compliance –*** *An i*mproved tax compliance from the taxpayer certainly fosters tax certainty. The tax-payers compliance behaviour will effectively manage compliance risks in exchange for transparency. Compliance costs will reduce for both the stakeholders, which is an essential feature of a sound tax system. In the USA, Tax-payers estimate they save 48% by using this process instead of the traditional audit.[54] d) ***Better tax policies and system*** – Co-operative compliance scheme will help provide real-time feedback by the taxpayers to the tax administration on account of a better trust-based relationship between the

[53] The 2020 Annual Plan of the Dutch tax authorities states that the current HTM agreements concluded by the Dutch tax authorities with the hundred largest and most complex companies will be terminated. An individual tax monitoring plan will replace these HTM agreements. The medium-sized companies according to Dutch accounting law can conclude an HTM agreement under stricter requirements and for a limited duration of three years.

[54] https://www.irs.gov/businesses/fact-sheet-pre-filing-agreement-pfa-program

		two stakeholders due to frequent interactions. These inputs will help improve and design a better tax system that is taxpayer-friendly. • **No more chalk and cheese:** Since India has prior experience with the LTU and based on the negative lessons learnt, Indian tax authorities may consider reintroducing a refined version of co-operative compliance scheme. The scheme shall have an adequate taxpayer feedback system and quality assurance check to help prevent disputes, early tax certainty and increased tax collection. Further, when the Government is keen on transitioning from the adversarial regime to a taxpayer-friendly regime, such compliance schemes will bolster a healthy trust-based relationship between the two stakeholders. • The survey observation in Part II indicated that 90% of the respondents believed that the tax assessment is a breeding ground for disputes. Co-operative compliance scheme will be a preventive tool for non-breeding of the disputes.
B	**Public Rulings & Advice**	• As private rulings through a quasi-judicial body in the form of AAR are available to taxpayers on specific transactions. The public rulings are where the tax administration' interpretationed on common cross border taxation issues are much desirable introduced by the CBDT. • Public rulings are common in some countries such as Australia, Greece, Kenya etc. For example, the Australian Tax Office recently issued a public ruling on applying arm's length debt test in its thin capitalization

		rules.[55] These rulings assist as interpretative guidance for taxpayers, thereby fostering tax certainty. Foreign taxpayers often refer to these rulings by the ATO to understand tax administration perspective. • Singapore's e-tax guide[56] is another prominent example of guiding various cross border tax issues that regularly understand the taxpayers' obligations. Even legacy issues are updated frequently to keep it up to speed with the modern-day business dynamics. • Even though circulars, instructions are provided by the CBDT, albeit on a sporadic basis. Hence a guidance note in the form of guides can be also be provided for practical compliances more so for cross-border taxation matters. For example, FAQ or a guidance note on availing foreign tax credit based on the concerned rule [57] will be a handy tool for taxpayers to understand the practical issues that emerge. These will undoubtedly prevent disputes and also foster certainty. • Ideally, the public rulings or advice must be binding on the administration as it will add sanctity to these notes apart from fostering certainty and protection to the taxpayer. Nevertheless, a non-binding ruling or advice is also desirable as it will provide a guidance tool to understand the tax administration's interpretation of cross border taxation issues.

[55] TR 2020/4 | Legal database (ato.gov.au)

[56] IRAS | e-Tax Guides

[57] Rule 128 – Foreign Tax Credit, Income Tax Rules, 1962

C	**Frequent Stakeholder Consultations**	• The CBDT may consider pro-active diagnostic measures by providing public consultation notes before introducing new cross-border tax provisions. For example, the draft CBDT report for public consultation on an amendment to rules on attribution of profits to PE is a welcome step. It enabled the stakeholders to digest, discuss and provide their views on the proposed rules. • Report similar to the draft rules on attribution of profit to PE must not be a sporadic phenomenon rather than a regular phenomenon. These best administrative practices will bridge the trust deficit gap between the taxpayer and the administration.
D	**Legal Companion Memorandum for amendments in the tax legislation**	• Subset to public rulings, the legal companion memorandum can be provided as an extension to explanatory memorandum while introducing new substantive taxation provisions. These notes can act as guidance and interpretative versions from the tax administration, outlining the application of the newly amended provisions. • The explanatory memorandum that tags with the finance bill helps to determine the intention or rational. Still, it remains abstract and insufficient to understand the proposed amendment's technical nuances, interpretation, and relevant practical aspects. • Therefore, the legal companion memorandum can clarify the interpretation of legal provisions to be introduced, especially for cross-border tax provisions having significant impact and complexity. Since these notes will accompany the Union Budget documents, this provides an opportunity for the taxpayers to provide their suggestions and feedback for rectifying any apparent anomalies in the Finance Act.

		• These notes and the explanatory memorandum will foster tax certainty and prevent disputes on new provisions that the income tax law introduces. • To give a practical illustration of the significance of legal companion memorandum, the Finance Act 2020 had expanded the scope of Equalization Levy, resulting in a significant amount of confusion and questions. [58] The EL 2.0 resulted in more questions than answers leading to tax uncertainty. • A legal companion memorandum by the tax administration on the amendment's scope and the related key features of the provisions to comply would have provided a large amount of clarity for taxpayers & signalled a rational policy statement justifying the need for a unilateral taxation measure at the global level. • The legal companion memorandum can also be introduced in the form of Joint interpretative note for tax treaties that India signs in order to understand the positions taken by the countries while negotiating or revising a tax treaty. Even if bilateral joint note is not possible, at least the Government can consider a technical explanation note which is already a set precedent in many countries. The technical explanation memorandum need not be binding, but it will endeavour to act as a guidance note.
E	**Technical Advisory Panel**	• The CBDT may consider setting up a technical advisory panel in its Foreign Tax and Tax Research Division which a senior tax officer can chair. The panel may consist of a

[58] Colloquially referred as EL 2.0, Section 165A of the Finance Act 2020

		diversified team by empanelling tax academicians, industry representatives, tax experts from other countries, indirect tax officers and experts from other interdisciplinary areas such as economists. The technical panel can provide its views on CBDT circulars, guidelines before they are released. • The panel will act only in an advisory role following a strict code of conduct norms for external experts to adhere to in the panel, including minimum time for the panel's cause. • The panel may consist of experts from across the country, and meetings can be held virtually for transparency reasons, saving operational costs. • The panel views will provide an inclusive and multiple perspectives and interpretations, which will help the CBDT adopt the correct position and avoid disputes.

Chapter 11

Layer II - Dispute Containment

11.1 As the name suggests, containment of dispute contains the disputes from aggravating further. In the words of Professor Susskind – "*Dispute containment concentrates on preventing disagreements that have arisen from escalating excessively".* [59]In the context of cross-border tax disputes, this ensures that the tax administration resolve disputes at their level. Consequently, only complex disputes that require judicial or quasi-judicial intervention may proceed to the next layer, i.e. the dispute resolution layer.

Nip it in the bud

11.2 India's economic survey mentioned in their report that *"There is substantial avoidable litigation in the tax arena which government action could reduce"*[60]. The survey also revealed that more than seven lakh crores are stuck in tax disputes; therefore, an early-stage resolution of tax disputes is the need of the hour. Time taken to resolve the disputes is significantly high due to many cases lying unresolved before the courts waiting for its turn. Time is of the essence and more so for economic subjects as it has significant ramification for the State's developmental goals. Disputes don't age like wine; it turns into an economic mess.

11.3 Therefore, the dispute containment mechanism is pivotal for an effective domestic dispute mechanism to resolve cross-border taxation matters. Hence, tax administration must ensure that disputes be resolved by nipping them in the bud to betterment all the stakeholders concerned and ensure that only complex tax issues go to the dispute resolution layer. For example, the co-operative compliance scheme recommended in the previous chapter under dispute prevention will also work as an effective dispute containment tool.

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[59] Richard Susskind, Online Courts and Future of Justice (2019), OUP London.

[60] India's Economic Survey , 2017-18 Available at http://mofapp.nic.in:8080/economicsurvey/

Effective domestic dispute containment tools for early tax certainty

11.4 Dispute Resolution Panel – Failure to provide substantive justice

11.4.1 The DRP was set up by the Government of India in 2009, as an alternative dispute resolution mechanism within the Income-tax Department to resolve disputes arising out of transfer pricing matters and disputes on tax adjustments made for non-residents by the revenue authorities. [61] The DRP objective was to dispose of disputes arising from tax audit in a time-bound manner and endeavour to act as an alternative dispute resolution mechanism to other options such as CIT (Appeals). In essence, DRP was like a surrogate Mediation mechanism with tax administrators acting up like mediators to resolve disputes arising from tax audits.

DRP – Game that is not worth the candle

11.4.2 However, after a decade of its existence, the DRP mechanism has not been an effective alternative dispute resolution mechanism. A whopping 96% of the survey respondents in Part II have mentioned that the DRP failed to achieve its objective as a dispute resolution tool. The DRP orders were highly prejudiced in favour of the revenue, thereby eventually escalating the tax disputes to the next level due to tax-payers aggrievement that the DRP failed to deliver substantive justice.

11.4.3 Fairness is a critical component of substantive justice, with disputes resolving substantially in favour of the revenue, the element of fairness appears to be missing. With this flawed process, the DRP has lost its sheen as an effective dispute resolution tool. The DRP has been spinning its wheel for a decade and needs serious introspection.

11.4.4 Despite the DRP's failure to resolve disputes and provide substantive justice to taxpayer's disputes, the taxpayers still prefer the taxpayers as a via-media to escalate the disputes at the ITAT in a speedy time-bound manner as the CIT (appeals) process consumes more time. The DRP acts as a speedy route to the ITAT. The ploy by taxpayers to resort to DRP only as a via-media to ITAT for speedy disposal defeats the ultimate purpose of setting up DRP. The objective is for a timely justice and not timely injustice. Further, an unfair advantage on the time factor for DRP vis-à-vis CIT (A) is also against tax law principles.

[61] Section 144C of the Income Tax Act, 1961.

11.4.5 Suggestions for an effective DRP mechanism –

Options	Recommendation	Objective
A	**DRP replaced by the GAAR Approving Panel – Substantive justice**	• The main criticism of DRP is that it is pro-revenue. Invariably disputes are resolved in favour of the tax-administration, leaving taxpayers frustrated for not being a neutral body. • The existing panel in the DRP consisting of tax administrators may be replaced by or a similar to the GAAR approving panel. Currently, the GAAR approving panel consists of three members including the chairperson who is or has been a judge of a High Court, and One member shall be a member of Indian Revenue Service not below the rank of Chief Commissioner of Income Tax, and One member shall be an academic or scholar having special knowledge of matters, such as direct taxes, business accounts and international trade practices) • Being a diversified panel with broad expertise and a neutral approach will be ideal for the DRP to be an effective dispute containment mechanism. These will also reduce the number of cases escalating to the ITAT, which already is loaded with many cases.

B	**The merger of DRP with CIT (Appeals)**	• With the survey results in Part II indicating the ineffectiveness of DRP and dwindling interest from taxpayers in adopting DRP, it is futile to continue with this alternative dispute mechanism. The dwindling interest is evident from our survey, where 61% of the respondents mentioned that they opt for CIT(appeals) as a forum over the DRP to resolve their disputes. • The better sense will prevail if the Government abolishes DRP, thereby allowing the taxpayer to resort to the traditional appeal mechanism under the domestic law with the CIT(Appeals). The CIT(A) may be an effective alternative dispute resolution tool with the introduction of faceless appeals. The Government can also reduce the timelines in line with the DRP timelines to make it more time-bound for speedy disposal.

11.5 Tax Ombudsman 2.0 - Effective Mediation Procedure

11.5.1 In general, Ombudsman enquires into grievances or complaints regarding the functioning of a public authority.[62] Tax Ombudsman is an alternative dispute resolution mechanism where the Ombudsman plays the role akin to a mediator in solving disputes between taxpayer and the tax administration at an early stage. They act as a watchdog to ensure tax laws are implemented appropriately and act on taxpayer grievances. The tax

[62] Income Tax Department, Taxpayer Information Series -40, available at ombudsman-publication.pdf (incometaxindia.gov.in)

ombudsman scheme's primary advantage is that the low unit costs for the Government and cases could be solved quickly, leading to early tax certainty. Tax Ombudsman mechanism is present in various countries, such as Australia, Denmark, Mexico[63], Finland, Ireland, Pakistan etc., proving to be an effective mediation settlement process for disputes between taxpayer and administration.

Tax Ombudsman - Indian Experience

11.5.2 India is no stranger to tax ombudsman scheme as it had its tax ombudsman scheme including a detailed guideline on the functioning of tax ombudsman.[64] However, the ombudsman scheme got abolished due to failure to 'achieve its objectives'.[65] Another reason for removing the ombudsman scheme was the availability of alternative grievance redressal mechanism viz. the Centralized Public Grievance Redress and Monitoring System (CP Grams). Also, there was general apprehension amongst the taxpayer fraternity for approaching the Ombudsman, which may antagonize the regular assessing officer and impact its audit.

Tax Ombudsman 2.0 – As an effective mediation forum for cross-border taxation

11.5.3 Considering the importance of global trade and foreign investment, a refreshed and revamped tax ombudsman scheme can be introduced specifically for cross-border taxation matters. The grievances can be concerned with the following:

- Unfair tax claims
- Disputes under lower or nil withholding tax certificate under Section 195 of Income Tax Act, 1961.
- Assistance in approaching advance ruling

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[63] Mexico's PRODECON is a well-established precedent for taxpayer rights and grievances. PRODECON has been successful in mediating disputes between taxpayer and the administration, thereby resolving disputes at an early stage.

[64] The Income Tax Ombudsmen Guidelines 2010, available at ANNEXURE-I (incometaxindia.gov.in)

[65] Cabinet approves Abolition of Institution of Income-Tax Ombudsman and Indirect Tax Ombudsman, PIB release, available at https://pib.gov.in/Pressreleaseshare.aspx?PRID=1562982

- Withholding tax dispute
- MAP grievances
- Wrong application of tax treaty principles by the Assessing Officer
- Transfer pricing disputes
- Foreign tax credit related disputes
- Determination of dual residency
- Refunds, Demand collection, facilitating appeals and other procedural infirmities faced by the taxpayer
- Exchange of information related
- Any unlawful action by the tax authorities

Tax Ombudsman also as an advocate for taxpayer rights

11.5.4 Tax Ombudsman could be an independent body from India's tax administration. She could act as a medium for promulgating taxpayers' rights to counterbalance the tax administration's power. Hence tax ombudsman can also be labelled as a taxpayer's advocate. With the Indian Government legislating taxpayer rights through tax charter, the Government can appoint an independent taxpayer advocate to ensure the taxpayer's legal rights are duly given effect. Apart from the grievances, the taxpayer advocate can also undertake the following activities:

- *Policy Advisor:* Investigate and identify the systematic problems of the taxpayers and to propose to the Tax Authority suggestions for their better solution; propose to the Tax Authority the proper amendments to its internal strategies; Bridge the gap between taxpayers and tax administrators. Hold meetings with tax officials and taxpayers' organizations to discuss and propose different solutions to their main problems.
- *Taxpayer Rights Advisory Panel:* An advisory panel may be constituted consisting of the taxpayer advocate, revenue officers, legal scholars, tax academicians, tax practitioners, economists, civil-society groups, retired judges, public volunteers etc. to identify cross-border tax issues that need clarification and more importantly have severe economic effect for the State. With increasing tax evasion and tax avoidance, these inclusive advisory panels can be consulted frequently to ensure

that the tax system's leakages are plugged. These initiatives may deter tax shenanigans from dodging taxes as the taxpayer rights advisory panel as a representative of tax-payers advocates in promoting tax fairness and ethics to taxpayers.

11.6 Tax Treaty Dispute Containment Mechanism- Mutual Agreement Procedure

11.6.1 Strengthening the existing mechanism

- Tax treaty dispute mechanism is not in this report's scope, as the report focuses on improvement on domestic legislation for an effective dispute mechanism on cross border taxation. However considering the significance of MAP as a dispute containment mechanism available under the tax treaties, some recommendations to strengthen the existing MAP framework is discussed below.

India's MAP framework

- India's MAP inventory is the fourth largest among the countries with a MAP framework in their tax treaties. The huge number of cases indicates India's aggressive position on cross-border tax issues. Apart from the domestic dispute mechanism available for the aggrieved taxpayer to resolve tax treaty issues, the MAP is the only recourse for resolving disputes bilaterally from an international tax treaty perspective. Hence, an effective MAP is essential in containing disputes elevating to the domestic judiciary. India's MAP framework suffered from infirmities in the past[66] and thereby was inefficient leading to clogging of cross-border tax disputes to be resolved at the domestic level. The inflexion point in India's MAP framework and many other countries has been the G-20 OECD BEPS project and, more specifically, the minimum standard implementation, Action 14[67].
- As a stock-taking measure, the OECD peer review report on MAP effectiveness in India reflected its concern on the average timelines to

[66] Sriram Govind and Shreya Rao, Designing an Inclusive and Equitable Framework for Tax Treaty Dispute Resolution: An Indian Perspective, Intertax, Volume 46, Issue 4 , 2018.

[67] OECD (2015), Making Dispute Resolution Mechanisms More Effective, Action 14 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/9789264241633-en

resolve MAP disputes which were extremely high regarding miscellaneous cases[68] taking close to 68 months. [69] The report highlighted that India's competent authority is short of resources and need to strengthen its resource to ensure a quick turnaround in resolving MAP disputes.

- Pursuant to implementing the BEPS measures from 2016, India's MAP framework has become very efficient and acts as an effective dispute containment procedure. The MAP guidance released by the CBDT is a very handy tool and much-needed guidance for taxpayers on resorting to MAP to resolve disputes. The recent OECD award to India for effective MAP cooperation with its counterpart in Japan for resolving transfer pricing disputes stands testimony to India's MAP effectiveness presently. [70]

Improving MAP efficiency

- The Government may consider some of the following aspects for improving MAP efficiency.
  - ***Capacity building -*** The upcoming handbook by the United Nations Tax Committee on Dispute Avoidance and Resolution will be a useful tool for discussion on changes to be made in the MAP framework and capacity building exercise in providing training to tax administrators on implementing best practices. [71]Training programmes at regular intervals will help address the practical issues immediately and enable the administrators to resolve MAP disputes quickly.
  - ***Non-binding Arbitration or Mediation* -** Further as a supplement to the MAP, alternative dispute resolution mechanisms such as arbitration and mediations may be considered.

[68] Other than Transfer Pricing cases

[69] OECD (2019), Making Dispute Resolution More Effective – MAP Peer Review Report, India (Stage 1): Inclusive Framework on BEPS: Action 14, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/c66636e8-en.

[70] MAP 2019 Awards, OECD, Mutual Agreement Procedure 2019 Awards - OECD

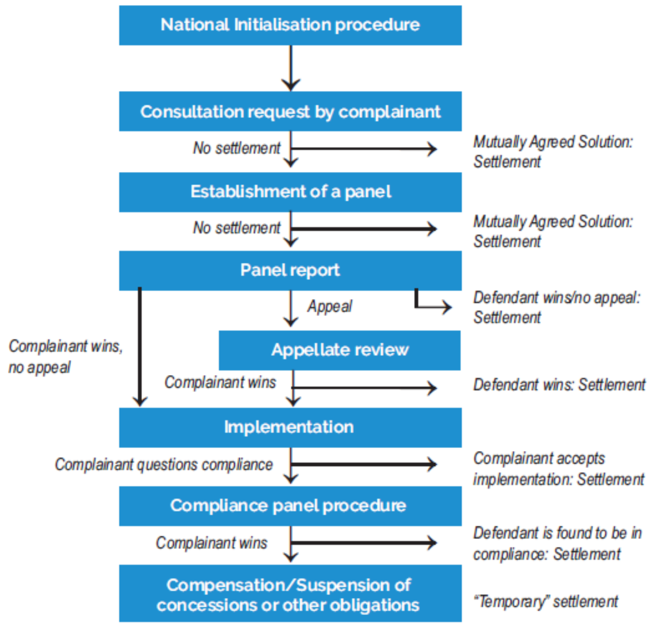
[71] Subcommittee on Dispute Avoidance and Resolution | Financing for Sustainable Development Office (un.org)

- **Joint Multilateral framework agreement** – An agreement could be entered between the competent authorities for handling MAP. Framework agreement may address procedural or administerial issues relating to the MAP. Further specific substantive treaty issues can also be addressed, considering it is possible to determine the common issues that may arise within the regular country partners in the MAP. These processes will enable us to arrive at a quicker resolution on the specific substantive treaty issues. Furthermore, this multilateral framework can also help implement an effective Multilateral Co-operative Compliance scheme, for seamless exchange of information sharing and quick resolution of tax treaty-related issues. This may also act as a catalyst in the longer term for effective joint audits of multinational enterprises with the MAP partner countries.

- **Inspiration from non-tax treaties for tax treaty dispute management**

  - **WTO Dispute Settlement System –** The DSS governs the trade disputes in the WTO, and the framework has received a positive response from the stakeholders in handling disputes which are often textured with political overtones. The framework of the DSS is as follows[72]:

[72] Aarshi Tikrey, The WTO Dispute Settlement System: An Analysis of India's Experience and Current Reform Proposals, 2019, ORF Occasional Paper #209



Source: Thomas A. Zimmerman, "WTO Dispute Settlement: General Appreciation of the Role of India" in WTO and Dispute Resolution, ed. K. Padmaja, (Hyderabad: The Ifcai University Press, 2007), 151.

- The WTO DSS's effectiveness is due to an efficient appellate review body that reviews panel decisions based on an appeal. Therefore, taking a cue from the WTO, a similar dispute settlement body may be introduced for MAP arising out of tax treaty disputes. An appellate body can be constituted, which will hear matters on MAP issues that are not resolved within the timelines to ensure MAP effectiveness. With significant global tax disputes, the UN tax committee can endeavour to be a primary dispute resolution body to ensure speedy, unbiased and fair dispute resolutions on international tax matters. Under the UN's auspices, a Global Tax Dispute Settlement Centre may be set up as a self-standing international tax dispute resolution body, more so as mandatory dispute settlement.[73]

[73] Jeffrey Owens, Arno E. Gildemeister, and Laura Turcan, Proposal for a New Institutional Framework for Mandatory Dispute Resolution, *Tax Notes Int'l*, June 6, 2016, p. 1001.

- **Bilateral Investment Treaties [74]–** India recently entered into a bilateral investment treaty with Brazil. [75] One of the vital provisions in BIT is the Investor-State Dispute Settlement (ISDS) mechanism. Under ISDS, a foreign investor in a host country can resolve its dispute against the host state for violating/breaching the BITs. It is interesting to note that the India – Brazil BIT contemplates only state-state dispute settlement mechanism similar to the MAP framework in the tax treaty, where only competent authorities of both the states resolve disputes arising from the tax treaty. The India-Brazil BIT proposes a certain mechanism for preventing and resolving disputes, such as the following:

- **Joint committee –** [76]As part of dispute prevention mechanism, a joint committee will be set up consisting of government representatives from both the countries. The joint committee shall be responsible for the BIT's effective functioning and discuss to resolve disputes arising out of the BITs. Under the tax treaty, the MAP procedure can also consider similar mechanisms to resolve tax treaty disputes.

- **National Focal Point or Ombudsman as Dispute Prevention Procedure-**[77] The BIT mandates setting up an ombudsman from both the countries to prevent disputes arising from the BIT. Similar such mechanism can be made under the tax treaties for taxpayers to approach Ombudsman for resolving tax treaty disputes before invoking the MAP as a dispute prevention procedure.

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[74] **Bilateral Investment Treaties (BITs)** are agreements between two Countries (States) for the reciprocal promotion and protection of investments in each other's territories by individuals and companies situated in either state. In simple terms, BITs is a primary legal mechanism for protecting foreign direct investment (FDI) around the World. There are more than 3000 BITs entered between States and many between developed and developing countries

[75] Investment Cooperation and Facilitation Treaty with Brazil - English_0.pdf (dea.gov.in)

[76] Article 13 of the India-Brazil BIT, available at Investment Cooperation and Facilitation Treaty with Brazil - English_0.pdf (dea.gov.in)

[77] Article 14, ibid

Chapter 12

Layer III- Dispute Resolution Mechanism – As a last resort

12.1 Under the DRM layer, only those tax disputes that are complex or issues that require the Court's intervention on answering a question of law must reach this layer. Unfortunately, all the tax disputes currently reach this layer, leading to overburdening the judicial forums and the quasi-judicial forum like the ITAT. Ideally, this indicates that a majority or substantial amount of tax disputes must be settled before reaching the ITAT or the judicial forums viz. the courts.

12.2 The survey undertaken as part of this report on the effectiveness of the domestic dispute mechanism for cross-border taxation matters indicated that the judicial forums and quasi-judicial forums have been effective. Therefore, the judicial and quasi-judicial forum like the ITAT has been instrumental in resolving tax disputes. Further, the role of ITAT in international tax jurisprudence has been phenomenal, especially with some path-breaking landmark judgements.

12.3 The time limit in disposing cases at the ITAT and the judicial courts is on the decline, especially in the courts where dedicated tax benches have been allotted for disposing of tax matters. The ITAT has also set up a dedicated international tax bench handling international tax and transfer pricing disputes.

12.4 However, areas where the existing dispute resolution mechanism at the ITAT level can be strengthened, are as follows:

- **Consistency in the judgements**- The ITAT can have a roster of members for fixed period handling only international taxation and transfer pricing matters. Even if the member is transferred to another jurisdiction, he may be allotted the international tax bench. These ensure consistency in the judgments being rendered on International tax and TP matters.
- **Not to remand TP matters**- The ITAT as a final fact-finding authority can endeavour to resolve the TP disputes as much as possible and remand only those matters which require the AO's re-intervention. This

will avoid the second and multiple innings of tax disputes, which often comes back to ITAT. These will provide certainty and reduce the protracted litigation cycle.

- **Online Judging** – Thanks to Covid-19 pandemic, online court/ virtual hearings are a new normal. The ITAT can effectively use the technology to hear matters for speedy disposal. Further e-courtroom facilities can be set up, to have a dedicated platform for virtual hearings, which will include all the documents on the case available in the platform for viewing and discussion. Australia's 'e-CourtRoom' is a model to emulate in this regard.
- **Asynchronous Hearing**- Asynchronous hearing can be promoted wherein; there is no need for live hearings and the parties' physical presence as in conventional hearing. Asynchronous hearing can be rendered for straightforward issues through e-mail communication or a dedicated platform. The advantage of asynchronous hearing is there is no specified time for the hearing, and the arguments can happen over e-mail at any point in time. It is useful, especially in the modern epoch as the parties' presence is not needed and is location agnostic.

12.5 Regarding the judicial courts, the High Courts and the Apex Court, the only recommendation will be to follow the rule of law and other common law doctrines such as binding precedents. In the survey, most of the respondents indicate that the judicial courts are not consistent in their approach, leading to tax uncertainty. This report does not comment about the functioning of India's court system as that is outside the scope. The report's objective is to ensure that tax disputes are either avoided or prevented early. Only very complex tax disputes or disputes where the rule of law is compromised must reach the judicial courts. These will help the courts focus on non-tax disputes, which have plagued our judiciary's effective functioning. With very few cases, going to the judiciary will help increase tax collections and reduce needless litigation costs for the stakeholders concerned.

Part IV
Concluding Summary:
Better over Perfect

Chapter 13

Effective Dispute Mechanism for a Better Future

"The best is the enemy of the good".
-Voltaire

13.1 This report in paragraph 1.1. began with a survey where the respondents ranked India as #1 amongst countries on tax uncertainty. The same survey also indicated how uncertainty had a serious impact on business decisions impacting them frequently. Unsurprisingly, India ranks the top in this table, as shown in figure 8. The change in decisions on account of tax uncertainty frequently is against the major principles of tax law, i.e., stability, consistency and simplicity.

Table 8. In your experience, how frequently has uncertainty about corporation tax had a serious impact on business decisions in ...

On a scale of 1=-very frequently to 5=never

Rank	Country	Mean score
1	India	2.1
2	Brazil	2.3
3	Russia	2.5
4	China	2.6

Figure 8 – Extract from the survey [78]

13.2 Analysis and results from Part II of this paper revealed that India's prevailing dispute mechanism on cross border taxation matters has its flaws and has certainly not fostered tax certainty. Considering the significance of tax

[78] ibid

certainty, the existing State of the affair is not sustainable and does not augur well for all the stakeholders concerned. Therefore, the Government may consider for a change in the existing approach or introduce new alternative mechanisms for a better future. However, changing systems or processes are always met with resistance. Resistance to change is agnostic to any field or domain. The famous French philosopher Voltaire quoted that *"the best is the enemy of the good"* indicating that its critics often shun changes by benchmarking with idealistic solution, thereby maintaining the status quo.

Change is inevitable; the struggle is optional.

13.3 In his recent book, Professor Richard Susskind, a legal futurist who is an ardent advocate of legal technology in dispute resolution, [79] advocates the need for the legal community to embrace technology. His plea comes because the existing court system is ineffective and not sustainable for dispute resolution leading to failure in delivering justice. To promulgate the change in the system and to shun the critics who are resisting change, Professor Susskind tweaks Voltaire's quote as *"the best is the enemy of the better"* whereby indicates that benchmarking new solution with a perfect idealistic solution will take us nowhere and instead solution which will make the existing system better has to be the path.

Taming the Schrödinger's Cat – Inching towards Tax Certainty

13.4 The Indian Government in the recent past has been taking measures to foster tax certainty which is also evident from the recent Finance Bill 2021. As the efforts of the Government marches towards tax certainty the suggestions mentioned in the report may assist in accelerating its pace to reach the desired destination. The suggestions here may not necessarily be perfect; however, if the proposed suggestions in part III reflects a better framework for solving disputes and leading towards tax certainty, they may deserve some attention. ***After all, what is coming is better than what is gone***. [80]

[79] Richard Susskind, Online Courts and Future of Justice (2019), OUP London.

[80] Arabic Proverb.

Appendix – I

Chart 1 – Effectiveness of AAR

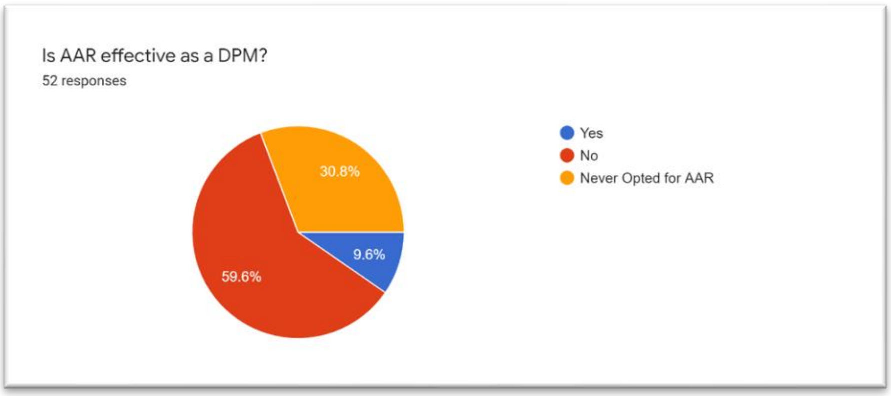


Chart 2 - Effectiveness of APA

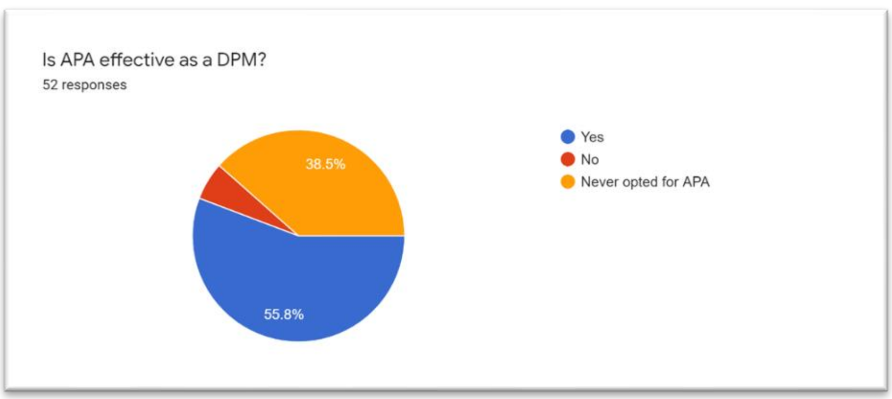


Chart 3 - Effectiveness of SHA

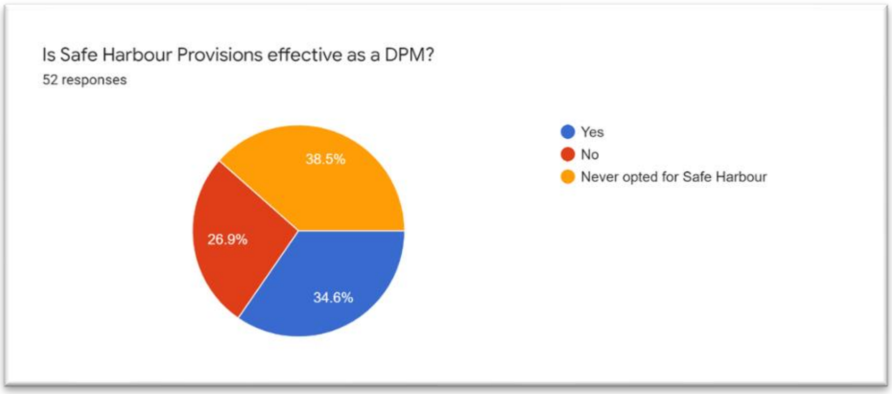


Chart 4 - Effectiveness of Withholding Tax Certificates

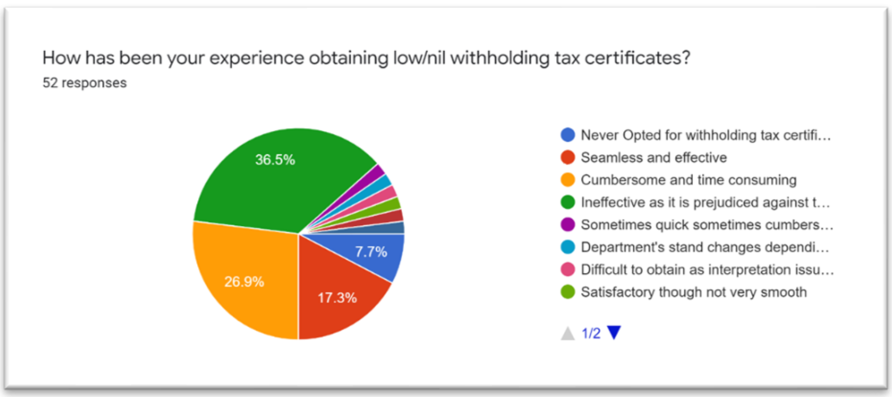


Chart 5 - Effectiveness of Tax Assessments

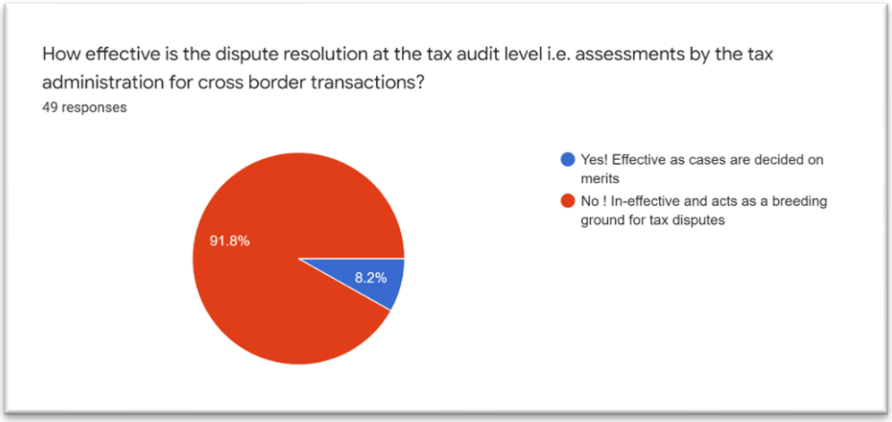


Chart 6 – Preferred Mode of First Appeal

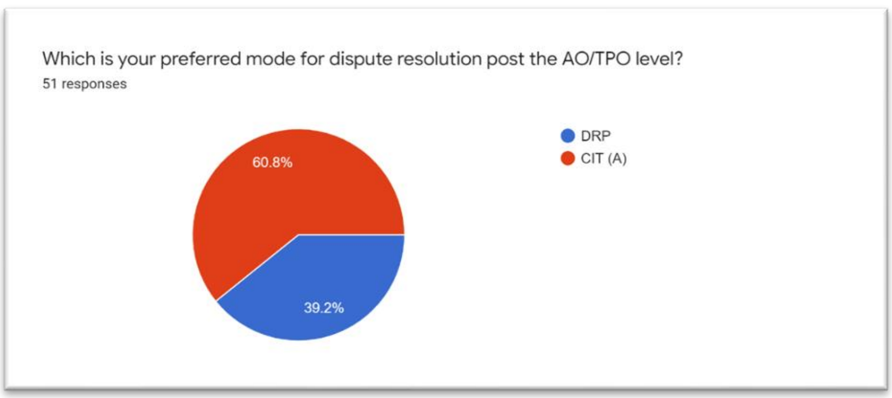


Chart 7 – Effectiveness of DRP

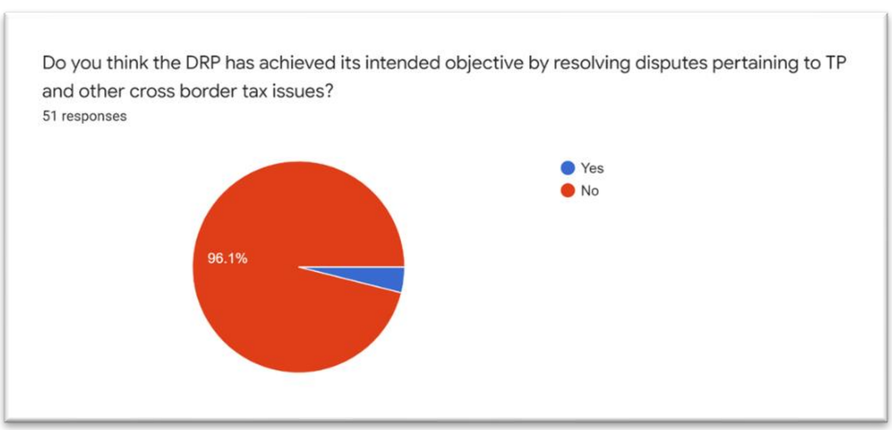


Chart 8 - Effectiveness of CIT(A)

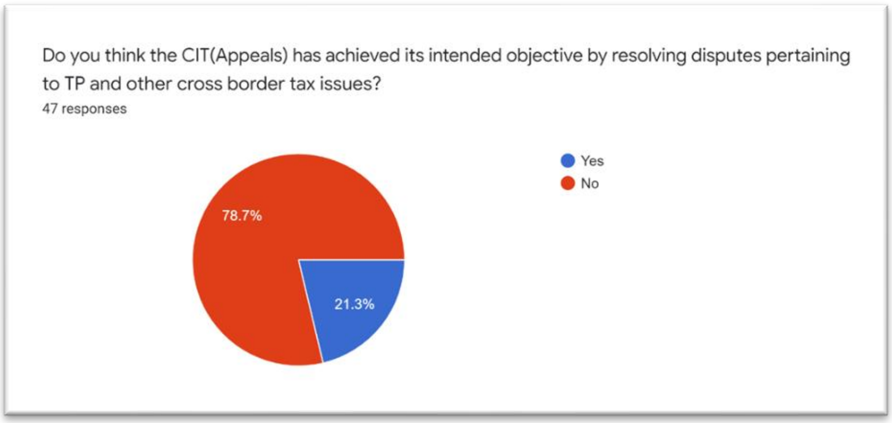


Chart 9 - Effectiveness of ITAT

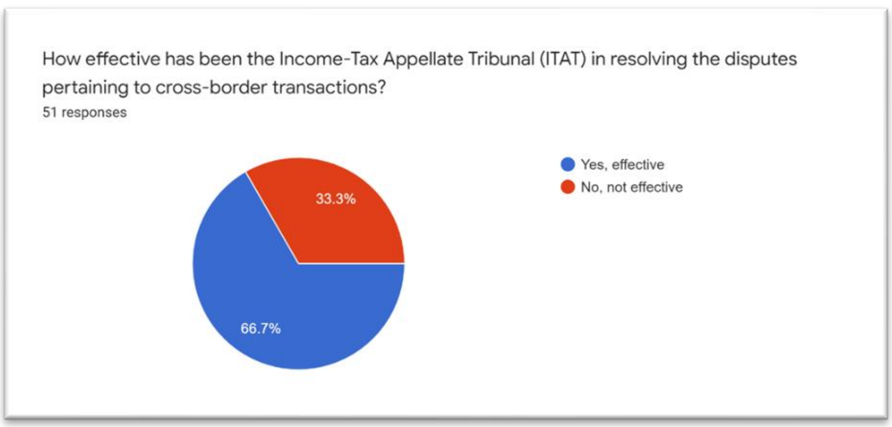


Chart 10 – ITAT in TP Disputes

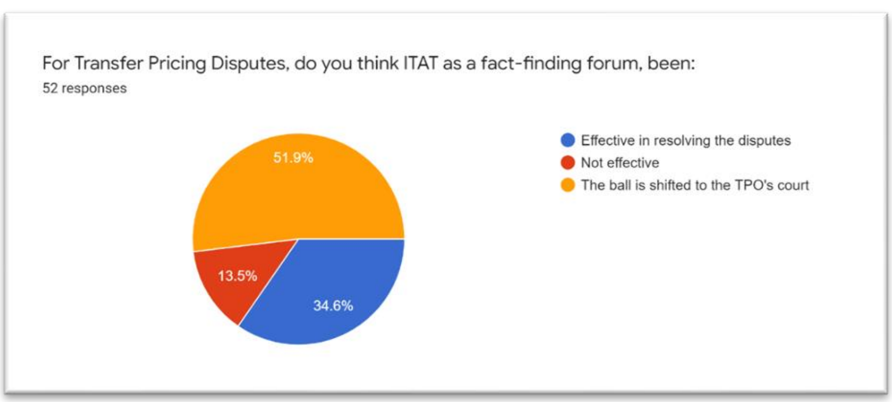


Chart 11 - Effectiveness of HC/SC

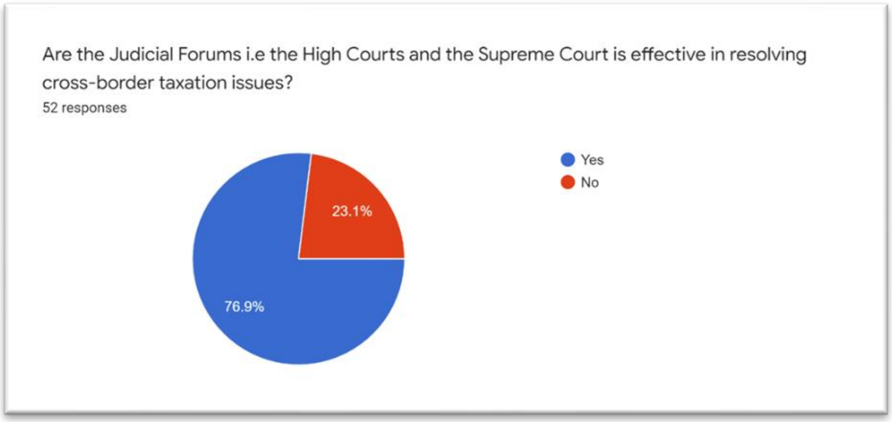
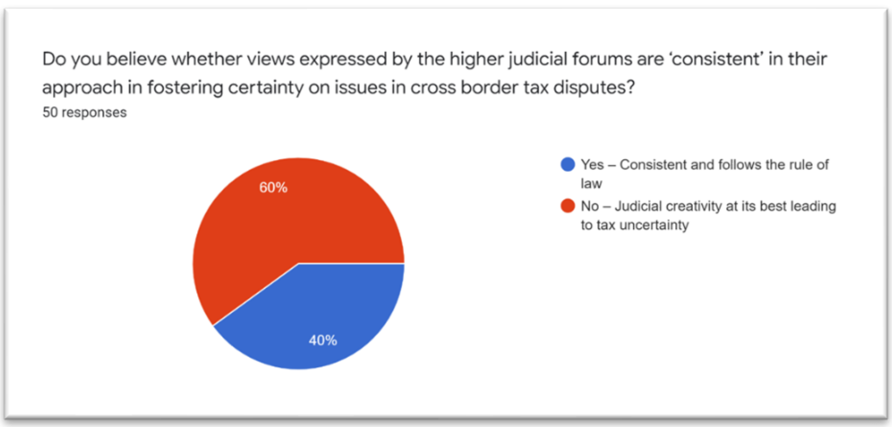


Chart 12 - Consistency in interpretation of law



Appendix II

What are the common tax issues that you encounter in cross border transactions? *

Please choose all that apply:

- [ ] Transfer Pricing
- [ ] Permanent Establishment
- [ ] Tax Treaty Entitlement
- [ ] Anti-Avoidance
- [ ] Other: ______

What is the major reason for cross border tax disputes in India? *

- [ ] Due to the interpretation and application of tax treaty
- [ ] Lack of understanding on the facts and circumstances (especially for transfer pricing disputes)
- [ ] International tax law is outdated not in sync with modern business dynamics
- [ ] Procedural Issues
- [ ] Other: ______

Do you believe Dispute Prevention Mechanism (DPM) tools provide tax certainty?
*

- ◯ Yes
- ◯ No

Have you ever opted for any of the following DPM available under the Income-tax law for cross-border transactions?

- ☐ Section 195(2)/197 – Predetermined Withholding Tax Certificate
- ☐ Advance Pricing Agreement (APA) for TP issues
- ☐ Authority for Advance Rulings
- ☐ None of the Above
- ☐ Safe Harbour for TP Issues
- ☐ Other: ____________

Authority for Advance Rulings (AAR)

Is AAR effective as a DPM?

- ◯ Yes
- ◯ No
- ◯ Never Opted for AAR

Advance Pricing Agreement (APA)

Is APA effective as a DPM?

- ◯ Yes
- ◯ No
- ◯ Never opted for APA

Safe Harbour Provisions

Is Safe Harbour Provisions effective as a DPM?

- ◯ Yes
- ◯ No
- ◯ Never opted for Safe Harbour

Lower / Nil Withholding Tax Certificates

How has been your experience obtaining low/nil withholding tax certificates?

- ◯ Never Opted for withholding tax certificates
- ◯ Seamless and effective
- ◯ Cumbersome and time consuming
- ◯ Ineffective as it is prejudiced against taxpayer
- ◯ Other: ____________________

Tax - Dispute Prevention Mechanism (DPM)

Do you think the existing tools as DPM is sufficient?

- ◯ Yes
- ◯ No

Tax Dispute Resolution

Which of the following mechanism have you adopted for resolving tax disputes on cross-border transactions?

- [ ] MAP – Tax Treaty Procedure
- [ ] Dispute Resolution under domestic law

If you have not adopted the MAP under the tax treaty to resolve disputes, why?

- [ ] Majority of cross border transactions with non-treaty country
- [ ] Lack of guidance to approach MAP
- [ ] Faith in the domestic judicial mechanism to resolve the disputes
- [ ] MAP is time-consuming and inefficient
- [ ] Non-involvement of tax payer
- [ ] Other: ____________________

Tax Audit Level

How effective is the dispute resolution at the tax audit level i.e. assessments by the tax administration for cross border transactions?

- ○ Yes! Effective as cases are decided on merits
- ○ No ! In-effective and acts as a breeding ground for tax disputes

If ineffectiveness at tax assessment level, what is one major reason for your answer?

- [ ] Knowledge of the Tax Authority
- [ ] Unreasonable targets on Tax Authority by Administration
- [ ] Less time for audit completion
- [ ] Corruption & Bureaucracy
- [ ] Non-Adherence to Rule of Law
- [ ] Other: ____________________

Commissioner of Income-tax (Appeals) [CIT(A)] / Dispute Resolution Panel (DRP)

Which is your preferred mode for dispute resolution post the AO/TPO level?

- ○ DRP
- ○ CIT (A)

Do you think the DRP has achieved its intended objective by resolving disputes pertaining to TP and other cross border tax issues?

- ○ Yes
- ○ No

Income-tax Appellate Tribunal (ITAT)

How effective has been the Income-Tax Appellate Tribunal (ITAT) in resolving the disputes pertaining to cross-border transactions?

- ◯ Yes, effective
- ◯ No, not effective

For Transfer Pricing Disputes, do you think ITAT as a fact-finding forum, been:

- ◯ Effective in resolving the disputes
- ◯ Not effective
- ◯ The ball is shifted to the TPO's court

Judicial Forums

Are the Judicial Forums i.e the High Courts and the Supreme Court is effective in resolving cross-border taxation issues?

- ◯ Yes
- ◯ No

Do you believe whether views expressed by the higher judicial forums are 'consistent' in their approach in fostering certainty on issues in cross border tax disputes?

- ◯ Yes – Consistent and follows the rule of law
- ◯ No – Judicial creativity at its best leading to tax uncertainty

Future - Cross Border Tax Disputes

Do you foresee an increase in cross border tax disputes in the future? *

- ◯ Yes
- ◯ No

Do you think the existing MAP framework will serve as an adequate dispute resolution mechanism in a tax treaty situation reducing cross border taxation disputes? *

- ◯ Yes - it will reduce the dependence of domestic dispute resolution mechanism
- ◯ No – Existing MAP framework is not sufficient to resolve cross border taxation disputes

What measures are to be taken to improve the existing Dispute Prevention and Resolution framework in India for cross border taxation issues

- ☐ Guidance Note from the CBDT on major issues
- ☐ Adherence to Rule of Law
- ☐ Fostering trust between taxpayer and tax-administration
- ☐ Frequent stakeholder consultation
- ☐ Other: ____________

What other Alternate Dispute Resolution Mechanism would you like to be implemented for managing cross border disputes?

- ☐ Nothing- Existing Mechanisms are sufficient to handle the disputes
- ☐ MAP - Arbitration under the Tax Treaty
- ☐ MAP - Mediation under the Tax Treaty
- ☐ Tax Dispute Settlement Body under the UN
- ☐ Other: ____________

Dispute prevention and resolution is one key ingredient for tax certainty? *

- ○ Yes – a major component for tax certainty
- ○ No – there are other factors such as proper drafting of laws, consistent tax administration practice etc.
- ○ Tax Certainty is a myth

On the tax certainty scale of 1-5 with 5 being 'extremely certain' to 1 being " no certainty" please indicate how the existing dispute prevention and resolution mechanism for cross border dispute mechanism have fostered tax certainty. *

1	2	3	4	5
○	○	○	○	○