

INAUGURAL SESSION OF TWO-DAY NATIONAL TAX CONFERENCE ON 6.7.2013 - SPEECH DELIVERED BY HON'BLE SHRI JUSTICE R.K. AGRAWAL ACTING CHIEF JUSTICE, HIGH COURT OF MADRAS.

Hon'ble Shri Justice Anil R. Dave, Judge, Supreme Court of India, Dear Brother Mr. Justice Kalyan Jyoti Sengupta, Chief Justice of Andhra Pradesh, Shri S.K. Poddar, President, All India Federation of Tax Practitioners and the Office Bearers of the Federation, Dr.MVK Moorthy and Shri S.S. Satyanarayana, Chairman and Secretary of All India Federation of Tax Practitioner – Southern Zone, Presidents of A.P. Sales Tax Bar Association and Twin City's Tax Practitioners Association, senior advocates, advocates, Experts from the field of Income Tax and Commercial Tax, ladies and gentlemen,

Good Morning to all of you,

I am very happy to be in the midst of this august gathering, for it gives me an opportunity to update my knowledge on my favourite subject – tax. In a shortwhile, we are going to deliberate on the subject 'Global Economy – Wider Vistas in Taxation'. The topics namely Service Tax, VAT & GST, Domestic

Transfer Pricing, Tax Accounting Standards etc. will explore the future vistas in taxation laws.

When we trace back the history of taxation, it was first introduced in Ancient Egypt around 3000 BC in the first dynasty of Old Kingdom. Our very own Kautilya's Arthashastra deals with taxation in great detail, almost reducing it to a science. Taxation is a continuously evolving field, and when wrongly applied, has the potential of causing irreversible historical changes, such as the American revolution, which led to the famous slogan of "no taxation without representation".

Due to globalization, taxation has acquired a new prominence today. In today's world, capital flies to countries where the cost of production is the lowest, and correspondingly, the ability to make profits, is more. Much of manufacturing has moved from the West to the East, most notably from America and Western Europe to China, and to a smaller extent, to India. Services are also following the same pattern – many multinational corporations have established huge offices in economies like India and Phillipines, where skilled employees and internet connectivity is available in abundance.

In a way, taxation in today's globalized world faces similar behaviour. Shareholders are concerned only with their return on investment, measured in terms of profits generated and dividends returned. To satisfy this demand of the shareholders, it is not uncommon for multinationals to make use of complex transactions and different holding structures to ensure that their profits are maximized in countries with the lowest effective tax rates.

One may argue that there is nothing wrong in this. If the legal system provides for tax credits, deductions, write-offs etc. why should there be a hue and cry when, taking a recent instance as an example, it was found that Starbucks Corporation was paying hardly any corporate profit tax in the United Kingdom? If there is no equity about tax, why should one even debate the lack of tax payments made by Starbucks in United Kingdom? After all, Starbucks would have employed several people, taken several locations on lease by paying rent, and also generated significant amounts of VAT through sale of beverages and other consumables. All of this would surely benefit the local economy. Why must one insist for it to also pay tax on its corporate profits arising out of its business in the

UK? The same controversy surrounds Apple and Google, both of which are found to pay very little tax relative to their profits.

Or for that matter, why should the Vodafone transaction in India generate so much interest? Would the Indian authorities be right in affixing capital gains liability on Vodafone only for acquiring an asset whose almost all value is derived from Indian operations – are they correct in seeking to tax the transfer based on the value of the underlying Indian asset?

Some, such as the Nobel laureate Joseph Stiglitz, have argued that not just the profits generated by these multinationals, but even the ability to generate these profits, has been enabled due to the expenditure incurred by the governments – without internet (a publicly funded and developed project), much of the globalized world as we know today would not exist; without armies of well trained/educated individuals graduating from State funded universities, much of the private sector workforce would not be employable. Without a strong and effective regulatory/legal system and a stable administrative environment, the ability of multinationals to reap the benefits of globalization would be questionable.

These scholars advocate the introduction of a corporate tax responsibility, something like corporate social responsibility, which would go beyond the strict legal obligation of a multinational company and involve the payment of taxes as a social responsibility. The impact of this debate is such, that it is pushing the boundaries of the distinction between tax avoidance and tax planning.

Although this push for greater taxation of corporate profits in the globalized scenario comes in the context of falling tax revenues amidst poor growth in Western economies, the debate that has been generated is equally relevant in our own context. As a developing economy, India has also found its needs to be far more than what our means can comfortably finance – we are also a nation perennially short of revenue (even adjusting for wasteful expenditures or leakages in funds allocated for public schemes).

As we deliberate on these issues, we need to realize that taxation is more than just economics – it is a tool for social redistribution of resources. Taxation, or the lack of it, is one of the most powerful incentives ever used to spur development in a region, or of particular sectors of industry. No incentive

other than reduced taxation could have lead to the creation of huge manufacturing zones in the hill states of Uttarakhand and Himachal Pradesh. No incentive other than accelerated depreciation could have resulted in mass installations of wind-mills in India, leading to the creation of an environment friendly means to alleviate our chronic power shortages.

However, before a government can make such choices of redistribution of resources by foregoing revenue, it has to have sufficient revenue to finance its other public schemes. There must be enough for the government to continue financing its Universities and other institutes of excellence, to continue building public infrastructure etc. It is in this context, that payment of taxes by all becomes important. After all, tax is a payment made by all to ensure an orderly society, one which benefits all, not just the rich and the powerful, but also the poor and the downtrodden.

As individuals, as corporates, as anybody, we expect fairness from everybody in their dealings – we expect the government to frame fair regulations and implement them properly, we expect our counterparties to be fair in their

transactions and perform their obligations. The legal system exists to actually enforce of a fair and just order.

When we think of taxation in a globalized world, our ideas must have as their fundamental underpinnings, the same notion of fairness. Is legality different from fairness, righteousness, or do they share a common domain? Should fairness come from both sides, or is it a unilateral obligation purely of the State? Is it really fair for a multinational corporation, to make use of clever transactional structures to deprive a nation of its legitimate share of taxes? Apart from the conduct of the multinational corporation being fair in itself, is this conduct fair relative to all others, who have duly discharged their tax burden, and in purely economic terms, can now be said to be at a competitive disadvantage with these corporations?

In a globalised world, we also need to simplify our tax enforcement and administration structures. It is only proper that the net income be taxed by allowing various deductions, allowances and incentives. Sometimes, these deductions etc. are necessary to incentivise certain forms of savings or investments. But sometimes, these are exploited to inflate

expenditures, leading to loss of tax revenue and generation of black money. Such a system also requires a huge administrative machinery to check the abuses of the system. We need to think of innovative ways in which such complex systems can be simplified. For example, one way could be by introducing a concessional rate of tax for those who agree to waive all allowances, deductions etc, and agree to be taxed on the basis of their gross receipts. The assessee does not have to maintain voluminous records regarding deductions etc.; the tax authorities only need to look at the bank account of the assessee to determine their liability, and not investigate the genuineness of the deductions claimed. Perhaps such an approach would free up significant resources that could then be better deployed elsewhere.

In this new global economic scenario, administrators have to equip themselves to adapt to the new environment. Nations must cooperate with each other through regular exchange of information and coordinated investigation/assessments in the case of corporate taxpayers.

Before parting, let me add that the primary responsibility of all of us is to protect the integrity of the tax system. There

must not be a dichotomy between the strict letter of the law and the spirit of the law – otherwise, corporations such as Starbucks, Apple and Google, and transactions such as Vodafone, will continue to generate significant controversy and debate. Vodafone has attracted such attention because as the Hon. Supreme Court ruled, the transaction was beyond the letter of the law. Attempts to now tax it, upsets fundamental assumptions regarding the consistency of legal rules and the integrity of the taxation system, and alters the very basis on which businesses base their decisions. This strikes at the core of the integrity of the tax system.

To align the letter of the law with its spirit, various alternative models of taxation have been suggested. Some have advocated the introduction of a global corporate profit tax, i.e., a system of taxation whereby the global profits of a company are taxed in the country where its registered office is, after allowing some credit for the taxes paid by that country elsewhere. Some others have advocated a system of turnover based tax, wherein the overall turnover of the multinational company is proposed to be subject to a small tax. A possible mid-way could be the Minimum Alternate Tax (MAT) regime

that we already have in our Income Tax Act, wherein the book profits of a company are subject to tax, irrespective of the fact that the company may eventually not have to shoulder any tax burden at all due to the various incentives/deductions etc. that can be availed by it.

It is always a struggle to come up with the taxing provision that precisely balances these various competing priorities and practicalities. Each system has its own merits and demerits. The Direct Tax Code that is to be introduced shortly, takes a step forward on the subject – however, while it improves the state of affairs in one aspect, it is subject to criticism on other aspects.

We have a series of lectures behind me who will elaborate on these various facets of taxation law and principles. Like you, I am also eagerly waiting to hear them speak, and before my own address becomes too taxing for the audience, I must thank the organisers for giving me an opportunity to share my thoughts on this occasion.

Thank you very much. Jai Hind.
