

Tax demands on firms help govt raise cheaper funds

Amount locked up in appeals is Rs 2.42 lakh crore

Sachin Mampatta | Mumbai January 03, 2014 Last Updated at 00:31 IST



The increasingly aggressive tax demands by the government is acting as a cheap source of funds for the sovereign.

Companies that challenge a tax claim have to first pay at least half of the disputed amount before going for litigation. As the government is required to pay only six per cent interest if the case goes against it, any disputed claim acts as a source of funds with an interest rate that is three per cent lower than the market borrowing rate.

The government pays an interest of more than nine per cent on capital if it wants to raise funds at current rates. But, it seems, the government can raise cheaper capital through its tax demands.

“Whenever a tax claim is challenged, the tax authorities insist that that at least 50 per cent of the claim is paid upfront,” said Nishith Desai, founder of Nishith Desai Associates. “In a number of cases, taxpayers win the case at the appellate courts, in which case the tax authorities have to refund the money with six per cent interest. Considering the scale of tax litigation and potential refunds with interest, it is quite similar to a sovereign debt offering that is not reflected in the Budget.”

Interestingly, experts told Business Standard that almost 80 per cent of cases in appellate courts go against the government.

Some of the high-profile income tax notices include one for Rs 5,357 crore to IBM, a Rs 11,200-crore notice to Vodafone, a demand of around Rs 5,400 crore to Shell and a Rs 2,100-crore notice to Nokia.

“Further, it’s highly unfair to offer six per cent interest on taxpayer refunds but charge 12 per cent interest on outstanding claims. Penalties in India are disproportionate and may go up to 300 per cent. Taxpayers need to bear heavy litigation costs, which are not compensated even if they win. Government litigation costs are also indirectly borne by the taxpayer,” added Desai.

PROMINENT TAX DISPUTES

Company–disputed amount (₹crore)

Vodafone	11,200	<div style="width: 100%;"></div>
Shell	5,400	<div style="width: 48%;"></div>
IBM	5,357	<div style="width: 47.5%;"></div>
Nokia	2,100	<div style="width: 18.7%;"></div>
Infosys	1,750	<div style="width: 15.6%;"></div>

Source: News reports

The effective rate of borrowing for the government is even lower than the six per cent figure pointed out an expert. “The interest paid to the company is taxable, so the effective interest paid comes down to four per cent,” said a senior official at a major tax firm.

The amount locked up in appeals at higher levels —

including the Income Tax Appellate Tribunal, the high court and the Supreme Court — was Rs 1.63 lakh crore, according to the 2013 report of the Comptroller and Auditor General of India which had figures till March 31, 2012.

Appeals at the lower level are higher and the proportion of appeals pending decision has shown a rising trend. “Appeals pending with CIT(A) [Commissioner of Income Tax (Appeals)] increased from 67.2 per cent in FY08 to 75.3 per cent in FY12. The amount locked up in appeal cases has also increased to Rs 2.42 lakh crore (equivalent to 61.4 per cent of the revised revenue deficit of the Government of India) in FY12 from Rs 1.99 lakh crore in FY09,” added the CAG report.

N C Hegde, partner, Deloitte Haskins & Sells, said transfer pricing norms and the lack of accountability in the system have been at the root of an increase in disputed amounts. “The volume may have increased, but it is also on account of disputes over taxation related to transfer pricing. It could also be because of the lack of accountability in the system as often tax officials are not held accountable for passing orders which are clearly not in conformity with the law,” he said.

CHEAP FUNDS

- Government meets most of its spending needs through borrowings
- Market rate for government borrowing is nine per cent
- Companies have to pay a significant portion of capital up front in case of tax disputes
- Government only pays six per cent if appeal goes against it, three per cent cheaper than its usual borrowing rate
- The six-per cent interest paid is taxable, so effective rate of interest is closer to four per cent