Tax Disputes

Litigation remains high in India amid corporate cash concerns

Tax directors said the vivad se vishwas scheme could help reduce pending litigation, but corporate participation is limited as many businesses struggle to navigate a global economic slowdown.

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Companies are re-assessing whether to trap funds in lengthy tax disputes

India has thousands of direct tax disputes locked in appellate forums, with some estimated to take up to 25 years. While the government is trying now to limit the time it takes to reach a decision across several cases, companies are using these delays as an opportunity to manage cashflow during the coronavirus pandemic.

Jimmy Spencer, CFO at Chemtex Group, said court delays are frequent because of a limited infrastructure to attend and close ongoing tax cases in India: “There is a shortage of judges, even in the high courts. Tribunal hearings are often adjourned due to the bench not functioning if either of the parties plead that they cannot argue the case because their counsel is indisposed or attending another court matter.”

The Indian government announced the vivad se vishwas scheme on February 1 to settle such cases pending at various levels of litigation across direct tax matters by allowing corporates to pay their disputed tax bill with the penalties and interest waived. Cases settled under this scheme will not be reopened under any law. The success of sabka vishwas, a similar scheme for indirect tax matters, led the government to expand the dispute resolution process to direct tax cases as well.

The scheme is applicable to all the appeals filed by taxpayers or the income tax department and pending in the judiciary system, including Commissioner of Income-tax, Income-tax Appellate Tribunal, the high courts, or Supreme Court. Eligible taxpayers under the vivad se vishwas scheme will need to use a cost-benefit analysis on pending disputes, submit declarations to close litigation on chosen cases, and foreclose the possibility of further proceedings.

Kamlesh Varshney, India's joint secretary for tax policy legislation at the Ministry of Finance, told *ITR* that once a large number of cases are settled through the scheme, it will then be possible to address the remaining volume.

However, remote working conditions under Covid-19 have made it difficult for companies to collate data and deliberate over the cost-benefit analysis of submitting pending disputes under the vivad se vishwas scheme. Some taxpayers worry there is still not enough time to prepare to utilise the scheme despite the Indian government extending the deadline to make submissions and settle disputes from March 31 to June 30.

Cash flow concerns limit vivad se vishwas scheme participation

There are also more immediate corporate concerns such as financing ongoing operations that prevent taxpayers from utilising the scheme.

Taxpayers with short-term cash flow concerns are less likely to sign up to the scheme because they would have to commit funds to settle the disputed tax bill while knowing a case in appeal can take several years to resolve. As such, businesses are prioritising their cash flows amid ongoing Covid-19 disruptions and are not opting into the scheme so they can avoid paying for the full disputed tax bill in the near term.

"No businessman would block his cash in taxes and borrow corresponding funds from the bank to run his business," said Spencer. "Corporates with weak [direct tax] cases may weigh their options and selectively opt for the scheme."

The length of ongoing disputes is an area tax directors are looking at because penalties and interests may rise even higher than the original tax bill. Although the scheme would waive most of this additional financial burden on businesses, it still results in a cost.

The Indian government is open to suggestions for better implementation of the vivad se vishwas scheme to bring in greater participation, according to Pramod Chandra Mody, chairperson of the Central Board of Direct Taxation (CBDT). Some tax professionals suggest the government should extend the payment deadline again to the end of the year.

"Few tax practitioners will have enough time to go through the contents closely with a fine tooth comb to understand the entire scheme," said one head of tax at a multinational consumer electronics company about the limitations in utilising the dispute resolution process at this stage.

However, there has been renewed interest in the scheme after the Indian government extended the payment deadline to June 30 and waived the 10% penalty charge on any already delayed payments.

Foreign subsidiaries show interest in vivad se vishwas scheme

Advisors are seeing more foreign taxpayers with appeal cases interested in the scheme because of the favourable fluctuations in the value of the Indian rupee against the US dollar in the past three months. The incentive to opt into the scheme is higher for businesses when they can settle their tax bill at the present value of the Indian rupee because it reduces the long-term financial burden.

Tax professionals said that the differences in the currency rates may help some parent companies of Indian subsidiaries save up to 15% on their tax bill in effective terms and even offset foreign exchange losses on imports.

While many taxpayers said the scheme is largely positive, there are ongoing governmental concerns about how to improve corporate participation further. India-based tax directors expect most jurisdictions to expand their tax base to refill their coffers following wide ranging relief programmes to address Covid-19. The Indian tax administration is no different and aims for direct tax revenues to increase from more than INR 10 trillion ($134 billion) to more than INR 13 trillion between financial year (FY) 2020 and FY 2021 under the scheme.

“It’s too early to say whether the government will meet its targets on tax revenue,” said the head of tax. “The target depends on how long the lockdown stretches and how industries cope.”

In an effort to better implement the scheme, the Income Tax Appellate Tribunal (ITAT) plans on pursuing video conferencing technical sessions while remote working with its members and other Indian bar association members on expanding the vivad se vishwas scheme for direct tax.

Business participation has been mixed so far as tax directors support the scheme but face budget, time, and other resource constrains to limit participation under deadline. However, the rising corporate cost to continue Indian tax disputes for years may incentivise further participation in the scheme.