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India's GAAR in Action: From Formal Compliance to Commercial Substance

Shaily Gupta
Khaitan & Co

For years, India's General Anti-Avoidance Rule (GAAR) occupied an unusual place in the tax landscape: broad in design but relatively limited in visible enforcement. Recent developments, however, suggest that this is changing.

India's GAAR, codified under Chapter X-A of the Income-tax Act, 1961 (Act), marks a decisive pivot towards substance over form in Indian tax enforcement, empowering tax authorities to declare an arrangement as an impermissible avoidance arrangement (IAA) where its main purpose is to obtain a tax benefit and it satisfies one or more tainted elements ie lack of commercial substance, absence of arm's length dealings, misuse of the Act's provisions, or absence of bona fide business purpose. Once invoked, authorities may recharacterise, disregard, or re-allocate the tax consequences.

Since coming into force on 1 April 2017, GAAR has seen relatively limited visible enforcement in its initial years. However, recent proceedings and rulings suggest that this position is changing, with the framework entering a more consequential phase characterised by closer scrutiny of commercial substance, transaction purpose, and the evidence underlying tax-driven structures.

At the heart of this shift is a change in the nature of the inquiry. This shift is reflected across recent matters involving domestic reorganisations, cross-border investment structures, and treaty-based claims. The proceedings in Hinduja Global Solutions Limited (HGSL), Vedanta Holdings Mauritius II Limited (VHML), Hareon Solar Singapore Pte. Ltd. (Hareon Solar) and, most significantly, the Supreme Court of India's decision in CIT v. Tiger Global International II Holdings [(2026) 6 SCC 47] (Tiger Global), provide important insights into the application of these principles in practice.

Tiger Global: Treaty Entitlement Subject to Substance-Based Scrutiny

The Supreme Court's judgment in Tiger Global is a significant development in the evolution of India's anti-avoidance jurisprudence. The case concerned a claim to capital gains protection under the India–Mauritius tax treaty in relation to the sale of shares of Flipkart Singapore to Walmart in 2018. The Supreme Court allowed the Revenue's appeals and overturned the Delhi High Court's decision in favour of the taxpayers.

The Court emphasised that tax treaties are intended to prevent double taxation and not to facilitate tax avoidance, and therefore treaty benefits cannot be granted where the arrangement lacks economic substance. It further held that possession of a tax residency certificate is not conclusive where legislative changes and the introduction of GAAR permit examination of the underlying purpose and substance of the arrangement. In this context, the Court departed from the earlier approach reflected in Circular No. 789 of 2000 and the decision in Azadi Bachao Andolan, signalling a shift towards a stricter review of treaty entitlement.

The Court also observed that the grandfathering protection under GAAR for investments made prior to 1 April 2017 would not automatically apply where the tax benefit arises from an arrangement implemented after that date. Further, even in the absence of formal invocation of GAAR, the authorities are not precluded from applying judicial anti-avoidance principles to deny treaty benefits where the structure is found to be artificial or lacking commercial substance.

Subsequent to the Tiger Global ruling, the Central Board of Direct Taxes issued Notification dated 31 March 2026 [Income-tax (Tenth Amendment) Rules, 2026], amending Rule 10-U of the Income-tax Rules, 1962. This notification provides significant clarification that GAAR (Chapter X-A) shall not be invoked in respect of income arising from the transfer of investments made before 1 April 2017. The explanatory memorandum to the notification clarifies that the amendment is intended to ensure that the provisions of Chapter X-A shall not be invoked on or after the date of publication of the notification where income accrues, arises, or is received by any person from transfer of investments made prior to 1 April 2017.

The ruling in Tiger Global demonstrates a clear shift towards substance-based evaluation of cross-border structures and reflects a judicial approach that operates in parallel with, and in support of, the statutory GAAR framework.

Hareon Solar: Treaty Exemption Denied on Lack of Substance

The Delhi Bench of the Income Tax Appellate Tribunal (Tribunal) in Hareon Solar provides perhaps the clearest illustration of how the substance of a cross-border structure may be tested through detailed factual evidence.

The Singapore-incorporated taxpayer claimed capital gains exemption under the India–Singapore tax treaty for grandfathered investments made before 1 April 2017. The tax authorities questioned its treaty entitlement under the treaty's limitation-of-benefits provisions, alleging that it functioned as a conduit without sufficient commercial substance in Singapore.

The authorities examined a wide range of evidence, including the taxpayer's expenditure, employees, physical infrastructure, board composition, directors' residence, bank-account signatories, source of funding and the location of investment decision-making. The absence of meaningful operations in Singapore and the extent to which its affairs were managed from outside the jurisdiction were relied upon to challenge the structure's substance.

The Tribunal upheld the denial of treaty exemption. The case is particularly instructive because it demonstrates that substance is not assessed through a single indicator. Rather, authorities may consider the cumulative picture emerging from an entity's operations, management, financial autonomy, and role within the wider group structure. Consistent with Tiger Global, the Tribunal also treated the tax residency certificate as non-conclusive, emphasising that treaty entitlement must be assessed against the surrounding facts and the actual substance of the arrangement.

Evidence in a GAAR Proceeding: Substance Must Be Demonstrated

The recent developments also highlight an important practical feature of GAAR: the assessment of an arrangement's purpose and commercial substance is necessarily evidence-intensive.

Section 96 of the Act requires the main purpose of an arrangement to be the obtaining of a tax benefit, together with the satisfaction of one or more specified conditions. Determining these elements requires examination of the arrangement as a whole and the circumstances in which it was undertaken.

Accordingly, the evidentiary record may extend well beyond formal transaction documents. Board minutes, investment papers, valuation reports, feasibility studies, internal approvals, financing documents, and regulatory filings may help establish the commercial rationale for a transaction. Equally, emails, internal correspondence, contemporaneous communications, and statements recorded during proceedings may provide evidence of the actual purpose behind an arrangement.

This makes contemporaneous evidence particularly important. A commercial rationale developed only after a GAAR proceeding has commenced may carry less weight where the contemporaneous record points in a different direction. Similarly, the existence of an otherwise legitimate business purpose may not be sufficient if the actual conduct of the parties is inconsistent with that stated purpose.

At the same time, the existence of a tax benefit should not, by itself, determine the outcome. Tax considerations can legitimately form part of commercial decision-making. The relevant inquiry is whether the arrangement falls within the statutory conditions for an IAA and whether the evidence supports the Revenue's conclusion regarding its purpose and substance.

The practical significance of the emerging approach is therefore not that taxpayers must satisfy a prescribed checklist of employees, expenditure, or physical presence. Rather, taxpayers should be able to demonstrate that the structure they adopted, the decisions taken, and the conduct that followed are consistent with the commercial rationale on which the arrangement is said to have been based.

The Enforcement–Certainty Balance

The recent developments indicate that the Indian tax administration and courts are increasingly willing to examine the commercial reality behind tax-efficient structures. For taxpayers and investors, this means that commercial substance cannot simply be documented after a dispute arises; it must be reflected in the structure's design, conduct, and contemporaneous evidence from the outset. For policymakers, the corresponding challenge lies in ensuring that the emerging approach remains sufficiently clear and consistent to allow legitimate businesses and investors to structure their transactions with confidence.

India's GAAR landscape is therefore entering a more consequential phase. The emerging jurisprudence does not suggest that legal form has become irrelevant; rather, it indicates that legal form is increasingly being tested against commercial substance, purpose, and conduct. The manner in which that boundary is drawn in future cases will determine whether GAAR develops into a predictable and effective anti-avoidance regime – one capable of addressing artificial arrangements without creating undue uncertainty for genuine commercial activity.

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