International Journal of Advanced Research in Commerce, Management &Social Science (IJARCMSS)
ISSN :2581-7930, Impact Factor : 6.809, Volume 06, No. 02(I), April-June, 2023, pp 26-30

RETROSPECTIVE TAX DEBACLE: A CASE STUDY OF VODAFONE IDEA LTD.

Vandana Yadav*
Dr. Amita Vijay**
Manoj***

ABSTRACT

Retrospective amendments are amendments which have backwards operation i.e., they come into apply from the previous date. In India the finance minister has recognized the power to legislate retrospective laws and amendments. But the question as to the constitutional legitimacy of such amendments is debatable; though it is held valid in certain situations but majorly it is held to be inconsistent. Thus, as a check on such amendments their use is restricted only to exceptional cases. Vodafone was considered to be one such exceptional case where the amendments introduced in Finance act 2012 were given effect from the past date. It was a revolutionary but a clever move made by the GOI to tax the Vodafone company but, the move faced severe criticism from the global investors. The arbitration also held it to be violative of the India-Netherlands BIT. Many experts opined their view on the retrospective amendments being a crusher of India's image in the minds of the overseas investors and citizens. They criticized the instability shown by the government. They stated that the prosperity of the country depends upon the economic and political institutions of the country, on their stability and transparency. Hence, though the government is granted the power to legislate laws and amendments with retrospective effect, its scope is restricted to exceptional cases and, therefore before making any retro operative law consideration of its necessity, applicability and effects is vital.

Keywords: *Vodafone, Retrospective Tax, Government, Arbitration.*

Introduction

Retroactive taxation allows countries to enact rules to tax certain products, items, services and transactions and charge businesses from dates after the date the law was enacted. In a nutshell, retroactive tax is a tax levied on past transactions and transactions.

Countries are using this tool to rectify tax policy anomalies that have historically allowed companies to exploit such loopholes. Governments often use post-tax amendments to "clarify" existing laws, which ultimately hurt businesses that intentionally or unwittingly misinterpreted tax laws. Besides India, many countries including the US, UK, Netherlands, Canada, Belgium, Australia and Italy have retroactively taxed companies that exploited loopholes in previous laws. **After** the amendment of "Income Tax provisions retrospectively in 2012, the international taxation arm of the finance ministry listed about 7-8 transactions, that **fell under India's retro tax**. Vodafone, Cairn, Sanofi- Shantha, 2009 Biotech Deal, 2005 AT&T Idea Cellular Deal, 2011 Kraft-Cadbury Deal etc to name a few. Among all Vodafone and Cairn were most high-profile cases, and the tax authorities claimed the taxes from these transactions

---

* Assistant Professor, Department of Business Administration, JNVU, Jodhpur, Rajasthan, India.
** Assistant Professor, Poddar Management and Technical Campus, Jaipur, Rajasthan, India.
*** Guest Faculty, Department of Business Finance & Economics, Jai Narain Vyas University, Jodhpur, Rajasthan, India.

would bring the Indian government more than crore Rs 40,000. The matter reached courts. Indian government won litigation in Bombay High Court Vodafone immediately appealed to the Supreme Court, which ruled in favor of the TELCO company in 2012".

Literature Review

Anushka Singh and Prashant Krishna (2021[i]), the study reveals "retrospective taxation is currently under scrutiny in a number of locations after India suffered two significant losses at the Perpectual Court of Arbitration, first to Vodafone and subsequently to Cairn. This begs the question of why the corporations are subjected to these retroactive taxes if India is moving towards privatization. The fact that India lost both cases by a unanimous vote indicates that not even the candidate that India nominated thought its argument had any substance. India modified its tax legislation retroactively in 2012, taking effect in 1962, and used that as a basis for collecting back taxes from these businesses. It is rare for legislation to be retroactive". By putting out a finance act change that would grant the "Income Tax Department the authority to retroactively tax such transactions. The act was approved by the Parliament that phase, Vodafone was now responsible for paying the taxes." By that time, the case had gained notoriety as the "retrospective taxation case."

Anish Dey (2021[ii]), this research analysis depicting "retrospective taxations constitutional validity with its impacts on direct and indirect taxes in context of the Vodafone case covered in detailed understanding."

Ojaitra Arora and Hemant Srivastava (2021[iii]), in their research study, "Impact of Abolishing Retrospective Taxation on Investment Space in India: fills in the gaps in India's systems' lack of readiness for a sustainable future and will aid us in understanding how taxes affect the national economy. The global financial crisis combined with onerous retroactive tax requirements has altered investor perceptions of how to allocate funds in India. These elements led investors to lose faith in India as a desirable investment location. Regulators must now carefully change the financial trajectory to one that is sustainable. The Indian systems intend to expand in the wake of COVID-19, the economy suffered and are prepared to transform crisis into opportunity. They intend to eradicate political complacency in order to continue executing strategic investor-friendly deals. We will need to put money into long-term profitabilty depends on long-run solutions for problems in the investor economy."

Retrospective Tax and the Vodafone Case in India

In May 2007, Vodafone bought a 67 percent stake in Hutchison. The government raised a taxclaim of Rs 7,990 crore in capital gains and withholding tax. Vodafone impeached the importunity notice in the Supreme Court. The Judgment was in favor of the Vodafone group. The court judgment said that - India's retroactive claim of Rs 22100 crore in capital gains and withholding tax imposed on the British telecommunications company in a 2007 deal violated its "guarantee of fair and equitable treatment". Therefore, it was not required to pay tax on the purchase, as "the Supreme Court has ordered India not to pursue tax claims against Vodafone Group". Tax office suffered losses of around Rs 14000 crore had to circumvent the Supreme Court's ruling, thus then UPA government and then Finance Minister Mr. Pranab Mukherjee in Budget 2012 introduced modification of section 9 of the Income Tax Act, through the Finance Act to give powers to tax authorities to retrospectively tax such deals. Thus the deals executed after 1962 involving transfer of shares in a foreign entity which had assets in India all were retrospectively taxed. The law passed Parliament earlier this year, shifting responsibility for paying taxes to Vodafone. The lawsuit is now infamous as the "retroactive tax lawsuit." The rationale for this law is to give India the right to retroactively tax mergers and acquisitions between foreign companies that have a majority of their underlying assets in India, i.e. a few years after the transaction is completed given."

Aftermath of the Retrospective Taxation Law

Since 2012, parliament passed a bill to amend the Finance Act, imposing a tax liability on Vodafone. The change drew criticism from investors around the world, who said the law change was "perverted" in nature. BML Munjal University Law Dean Nigam Nuggehali said the amendments that overturned the country's Supreme Court decision were overall poor drafts and perverted obsessions. According to international criticism, "India has been trying to resolve the issue amicably with Vodafone, but has been unable to achieve this." He said he did not intend to impose new tax obligations on companies that do. retroactive taxation. By 2014, all attempts by telecom companies and the Treasury Department to solve the problem had failed. The Vodafone Group then invoked Article 9 of the Bilateral Investment Treaty (BIT) signed between India and the Netherlands in 1995. "

Table below clearly shows that the net profit margins of the company have been declining continuously and the company's financial health has been disastrous since March 2019. Currently the net profit margin of the company is zero which speaks volumes about the profit margins of the company. At present the debt- equity ratio of the company is at rock bottom. PBIT and PBT margins are at the lowest levels, and return on net worth is zero. The condition of the company couldn't be worst with return on capital employed and return on assets in the negative. If the government doesn't come to rescue of the company we will lose on more company in the already struggling telecom market.

Table: 1 Showing Key Financial Ratios of Vodafone

KEY FINANCIAL RATIOS OF VODAFONE IDEA LIMITED (in Rs. Cr.)															
	21-Mar	20-Mar	19-Mar	18-Mar	17-Mar	16-Mar	15-Mar	14-Mar	13-Mar	12-Mar	11-Mar	10-Mar	9-Mar	8-Mar	7-Mar
PBDIT Margin (%)	40.04	35.11	13.43	22.46	29.07	33.71	32.37	28.04	23.39	22.37	20.4	25.08	30.4	34.19	31.54
PBIT Margin (%)	-14.92	-18.3	-25.65	-7.41	7.25	16.33	16.85	12.37	9.53	9.07	7.53	13.54	19.28	22.93	18.63
PBT Margin (%)	-111.13	-139.29	-47.99	-25.01	-4.02	11.36	13.87	9.97	5.84	4.36	5.91	8.96	10.86	16.41	11.25
Net Profit Margin (%)	-111.08	-163.55	-38.13	-16.02	-2.35	7.39	8.98	6.46	3.71	2.99	5.5	9.03	10.15	15.54	11.21
Return on Networth / Equity (%)	0	-812.45	-22.13	-14.56	-3.5	10.68	12.83	10.83	5.83	4.45	6.84	9.38	8.87	29.48	22.47
Return on Capital Employed (%)	-4.53	-6.11	-5.27	-2.26	3.24	4	6.85	4.7	3.07	2.54	4.11	5.75	5.64	11.39	8.44
Return on Assets (%)	-22.79	-31.95	-6.03	-4.37	-0.86	3.36	4.87	3.84	2.37	1.86	2.95	4.77	4.45	8.12	5.65
Total Debt/Equity (X)	-4.18	10.71	1.71	1.86	2.18	1.52	0.74	1.14	0.8	0.78	0.75	0.57	0.67	1.84	1.95
Asset Turnover Ratio (%)	20.51	19.53	15.81	27.29	36.83	45.51	54.23	59.35	64.03	62.21	53.55	52.81	43.87	52.28	50.39

Source: www.moneycontrol.com

Bilateral Investment Treaty of India and Netherlands

On 6 November 1995, ``India and the Netherlands have signed a BIT to encourage and protect the investment of their companies in each other's jurisdictions." It stipulated that efforts should be made to promote and protect Facilitate ``favorable conditions for investors" in partner countries. Under the BIT, the two countries will ensure that companies based in each other's jurisdiction "will always receive fair and equal treatment and enjoy full protection and security within each other's territory." Although the "India-Holland" agreement existed, Vodafone invoked it because its Dutch subsidiary, Vodafone International Holdings BV, owned Hutchinson Telecommunications International's Indian operations. bought. This was a deal between a Dutch company and an Indian company. BIT between India and the Netherlands expired on 22nd September, 2016."

Ruling of the Enduring Court of Arbitration at the Hague

"One of the main reasons the arbitration panel decided in favor of Vodafone was its violation of the BIT and the United Nations Commission on International Trade Law (UNCITRAL). Vodafone Group initiated arbitration proceedings under Article 9 of her BIT between India and the Netherlands when he initiated arbitration proceedings against India at the Court of Arbitration in 2014. Article 9 of the BIT states "a dispute between an investor of either party and the other party." "Parties involved in investing in the territory of another Party" shall be resolved amicably through negotiation whenever possible. The other is Article 3 of the UNCITRAL Arbitration Rules, which states, inter alia: "The composition of the arbitral tribunal shall not be hampered by any controversy over the adequacy of the notice of arbitration, the Arbitral Tribunal shall make the final decision".

Disposal of the Retro Tax

It all started with "Cairn UK winning a case against India in an international court", which also allowed Cairn to seek $1.2 billion in damages from the Indian government. As payments remained unpaid, the company began identifying overseas assets held by the Indian government. In fact, Cairn also won a judgment confiscating 20 Indian state assets in the UK. The government said it would appeal the ruling, but pressure mounted. Along with a bill to abolish the retroactive tax, the government has also proposed a conditional refund of major taxes imposed by the companies suing."

The (2021, Taxatation Laws Amendment BilL) is expected to bring about "the elimination of all tax claims previously made against businesses using the 2012 law." The current government has criticized the tax law, but no major efforts have been made to change it. In some ways, the timing of the move is a bit disappointing, given the government's setbacks at the International Court of Justice. Cairn had refused to pay taxes and challenged India's position in the arbitration. Now, the Cairn recently received an affirmative court order against the seizure of 20 Indian government-owned properties in the UK. .”

The retroactive tax problem may continue for some time. According to the bill, the government is now offering litigants to repay the full amount of the principal, but "agrees to withdraw the lawsuit against the company and not to claim any costs, damages or interest. “looking for If the companies agreed to the above, the government would probably have to part with about crore Rs 8000. This also means forfeiting an estimated Rs 1.1 lakh crore in taxes that could have been collected to ease the budget during difficult times.”

Conclusion

Withdrawing such a measure is a good signal for companies looking to invest in India. Around a dozen companies have been impacted by such measures. This is a big regulatory risk that the players face when investing in any country where laws change. This cannot be avoided but making them effective retrospectively is never a good idea even though it does look tempting for governments.

Tax laws are probably even more important as they affect companies directly. Companies always run the risk of tax laws changing in any domain, and that is acceptable. However, making any new tax law effective from an earlier date is not acceptable as the regulatory cost increases and sends a wrong signal.

P.M. Modi said retrospective tax as a "mistake of the past" and its abolition is likely to strengthen investors' confidence and increase trust between government and industry. This government is doing reforms not out of compulsion but out of conviction. Late Arun Jaitley always criticized the type of tax. Vodafone’s fortunes in India, though, have dwindled.

Tax arrears and price wars sparked by petrochemical tycoon Mukesh Ambani's 2016 entry into the telecoms business have hampered the local company's plans to go public. After merging with metal magnate Kumar Mangalam Birla's mobile phone service in 2018, it once again found itself on the wrong side of the state. This time, the government has filed a court-approved claim of US$7.8 billion as part of Vodafone Idea Limited's past earnings. With $30 billion in debt, the telecom company is on the brink. If the service provider, which has 280 million subscribers, goes bankrupt, India, widely regarded as the most insidious telecommunications market in the world, would suffer even more notoriety.

“Cairn can expect substantial cash from the elimination of retroactive taxation, but Vodafone cannot. Until solutions are found to the survival challenges facing Indian companies, CEO Nick Read is unlikely to provide a large bailout fund. So the finance ministry’s belated attempt to atone for the previous government's mistakes is becoming a kind of PR tool to limit the damage.”

“Retrospective Taxes are just one aspect of state arbitrariness. More legal minefields await multinationals investing billions of dollars and lured by the potential of India's 1.4 billion market. Walmart is battling draft consumer protection regulations that threaten to undermine the business model of local e-commerce site Flipkart, which it acquired in 2018 for $16 billion. Facebook's WhatsApp service has taken the Indian government to court over a rule that would abolish end-to-end message encryption, which it says would keep the economy open and transparent and maintain a rules-based economy. It should have been enough to show India's intentions. There is still a lot more work to do. Some of this, such as the Supreme Court of India's decision allowing Singapore's arbitration award to be enforced in India, could be dealt with by the judiciary, giving Amazon.com a significant relief. Emergency arbitrators have blocked the $3.4 billion sale of financially troubled Indian retailer Future Retail at Amazon's request. Stopped at Ambani's Reliance Industries. But political cadres will also need to strive for a more level playing field. Abolition of retroactive taxation is a welcome first step.”

References

[i] Anushka Singh and Prashant Krishna, *India’s Retrospective Taxation and Self-Inflicted Lose to Vodafone and Cairn*, 4 (2) IJLMH Page 2895 - 2901 (2021), DOI: http://doi.one/10.1732/IJLMH.26628

ii https://www.jlsrjournal.in/retrospective-taxation-by-anish-dey/

iii https://www.ijllr.com/post/impact-of-abolishing-retrospective-taxation-on-investment-space-in-india

iv https://www.biicl.org/files/6722_panel_two_harish_salve.pdf

v Aryan. (2021, August 16). Retrospective taxation: The Vodafone case, and the Hague court ruling | Explained News, The Indian Express.

vi https://indianexpress.com/article/explained/retrospective-taxation-the-vodafone-case-and-the-hague-court-ruling-6613799/

vii IANS. (2021, August 15). Retro tax scrapping revived foreign interest in India's privatisation plan. *Business Standard India*. https://www.business-standard.com/article/economy-policy/retro-tax-scrapping-revived-foreign-interest-in-india-s-privatisation-plan-121081500207_1.html

viii India, P. T. of. (2021, August 16). FM Sitharaman says rules on retrospective tax to be framed soon. Business Standard India. https://www.business-standard.com/article/economy-policy/fm-sitharaman-says-rules-on-retrospective-tax-to-be-framed-soon-121081601274_1.html

ix https://www.researchgate.net/publication/274196112_Taxation_and_Saving_-_A_Retrospective

x Patnaik, I. & Pandey, Radhika. (2021, August 13). Retrospective tax is good riddance. But Modi govt can do more to attract foreign investors. *ThePrint*. https://theprint.in/ilanomics/retrospective-tax-is-good-riddance-but-modi-govt-can-do-more-to-attract-foreign-investors/714180/

xi Pranav, M., Achal, M., & Verma, S. (2021, August 11). Retrospective tax policy: NDA called it tax terror; took 7 years and adverse verdicts to course-correct. *The Indian Express*. https://indianexpress.com/article/explained/retrospective-tax-policy-nda-called-it-tax-terror-took-7-yrs-adverse-verdicts-to-course-correct-7440548/

xii Retrospective Tax Law: All You Need To Know. (2021a, August 12).

xiii Https://Www.Outlookindia.Com/. https://www.outlookindia.com/website/story/business-news-retrospective-tax-law-all-you-need-to-know/390695

xiv Retrospective Tax Law: All You Need To Know. (2021b, August 14).

xv Https://Www.Outlookindia.Com/. https://www.outlookindia.com/website/story/business-news-retrospective-tax-law-all-you-need-to-know/390695

xvi Sabnavis, M. (2021, August 5). Removal of retro tax will send positive signal to foreign investors. *Business Standard India*. https://www.business-standard.com/article/economy-policy/removal-of-retro-tax-will-send-positive-signal-to-foreign-investors-121080501383_1.html

xvii Team, B. W. (2021, August 11). Abolition of retro tax to strengthen investors' confidence: PM at CII event. *Business Standard India*. https://www.business-standard.com/article/economy-policy/at-cii-event-pm-modi-emphasises-on-role-of-industry-in-india-s-growth-121081101255_1.html (N.d)

xviii https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3782726