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## ADR in Taxation Disputes: A Comparative Analysis of India and Foreign Jurisdictions

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*This paper explores the role of arbitration and other Alternative Dispute Resolution (ADR) mechanisms in resolving tax disputes, with a particular focus on the evolving landscape in India and a comparative analysis with foreign jurisdictions. Traditionally, tax disputes have been considered non-arbitrable in many countries, including India, due to the sovereign nature of tax collection. However, as global trade increases and cross-border transactions become more complex, there is a growing recognition of the need for more efficient and effective dispute-resolution mechanisms beyond traditional litigation.*

*In India, arbitration in tax disputes remains largely underutilized and is typically excluded from the scope of arbitrable matters. This is rooted in the perception that tax disputes involve public interest and state revenue, making them inappropriate for private resolution. However, international experiences, particularly from countries like the United States, the United Kingdom, and certain European nations, demonstrate that arbitration and ADR mechanisms can play a significant role in resolving tax disputes, particularly in the context of international tax matters and transfer pricing disputes.*

*This paper conducts a comparative analysis of the position of arbitration in tax disputes in India and foreign jurisdictions. It examines the legal frameworks, the types of tax disputes considered arbitrable, and the practical experiences in countries where arbitration is a viable option. The analysis reveals that while India remains cautious, other jurisdictions have progressively*

*embraced arbitration for certain tax matters, balancing the need for state control with the benefits of swift and expert resolution. The paper also offers suggestions for integrating tax disputes into the ambit of arbitrable matters in India. These suggestions include legislative reforms to redefine the scope of arbitrability, establishing specialized tax arbitration tribunals, and learning from international best practices. The conclusion highlights the potential benefits of including tax matters in arbitrable disputes, such as reducing the backlog in courts, fostering a more investor-friendly environment, and enhancing the efficiency of tax administration.*

**Keywords:** *adr, taxation, arbitration, arbitral tribunals.*

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## INTRODUCTION

In an era of globalization, the rapid expansion of cross-border trade and investment has led to increasingly complex tax structures and transactions. This complexity has, in turn, resulted in a surge in tax disputes worldwide. India, like many other jurisdictions, has traditionally relied on litigation for tax dispute resolution. However, this approach has led to an overburdened judicial system, prolonged resolution timelines, and uncertainty for both taxpayers and revenue authorities. The inefficiencies of conventional litigation have intensified calls for more effective, time-efficient, and investor-friendly mechanisms for resolving tax disputes.

Despite the global trend of incorporating arbitration and other Alternative Dispute Resolution (ADR) mechanisms into tax dispute frameworks, India has been reluctant to embrace these reforms due to the long-standing perception that tax disputes are inherently sovereign matters. The prevailing legal stance considers taxation to be a public law issue, which places it outside the domain of private adjudication. This assumption, however, is being challenged by international experiences. Countries such as the United States, the United Kingdom, Japan, and several European nations have successfully integrated arbitration and mediation into their tax frameworks, demonstrating that ADR can function without undermining state sovereignty or public interest.

This paper critically examines India's limited adoption of arbitration in tax disputes and presents a comparative analysis of foreign jurisdictions that have successfully incorporated ADR in their

tax dispute resolution mechanisms. By evaluating these international models, the paper explores the legislative and procedural reforms necessary for India to modernize its tax administration. Key considerations include the establishment of specialized tax arbitration tribunals, the expansion of arbitrability definitions, and safeguards to maintain public interest protections. If implemented effectively, such reforms could reduce judicial congestion, improve investor confidence, and align India's tax regime with global best practices, ultimately fostering a more efficient and predictable tax environment.

### **HISTORY OF ADR AND TAXATION AND CLASHES BETWEEN THEM**

Alternative Dispute Resolution (ADR) methods, particularly arbitration, mediation, and conciliation, have become significant tools in resolving disputes, especially in the commercial realm. In the context of adversarial proceedings, it is an adjudicatory process in which parties present their disagreements to an impartial arbiter for resolution. It is like litigation, but the proceedings are quicker, less expensive, more private, and have more latitude in how the rules of evidence are applied.<sup>1</sup> The Indian Legal system, with its overworked courts, has increased the use of ADR as a dispute resolution mechanism to speed up resolution and lower litigation expenses.

**Development of ADR Within India:** India has a prolonged tradition of resolving disputes outside the formal system of courts. Three phases can be identified while examining the dispute resolution tradition in India: a) the indigenous phase; b) the colonial period; and c) the post-independence age. The evolution of dispute settlement mechanisms in the Indian legal system has undergone several changes. In the historical era or indigenous phase, even though the king and his administrative group had the highest hierarchy, the king was prohibited from interfering in many disputes regarding local customs, norms which used panchayats, elder leadership in the community, or the intervention of the locally dominant caste chief as their own dispute resolution procedures.<sup>2</sup> However, the British colonial era saw the formalisation of

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<sup>1</sup> Madhu Sweta, 'Alternative Dispute Resolution in India: A Brief Overview' (*S&P*, 08 January 2020) <<https://singhania.in/blog/alternative-dispute-resolution-in-india-a-brief-overview>> accessed 25 October 2024

<sup>2</sup> Laju P. Thomas, 'Dispute Resolution In Rural India: An Overview' (2016) 2(5) *Journal Of Legal Studies And Research* <<https://thelawbrigade.com/wp-content/uploads/2019/05/Laju.pdf>> accessed 25 October 2024

alternative dispute resolution (ADR) in the contemporary legal system. The Arbitration Act of 1940<sup>3</sup>, which established a legal framework for settling disputes outside of court, was the first comprehensive piece of legislation addressing arbitration. However, this law was perceived as antiquated, onerous, and tardy in promoting efficient conflict settlement.

In the 1990s, The Arbitration and Conciliation Act of 1996<sup>4</sup> was introduced as part of India's economic liberalization and reform. This legislation was based on the UN model of law to make the law in accordance with the United Nations Commission on International Trade Law (UNCITRAL).<sup>5</sup> This act aimed to modernize the laws governing arbitration, conciliation, and mediation. It offered flexibility, confidentiality, and quicker conflict settlement, and lessened the load on the legal system. Since then, the 1996 Arbitration and Conciliation Act has been instrumental in advancing ADR in India, particularly in business disputes. In industries including corporate law, international trade, infrastructure, and construction, arbitration and mediation have grown in popularity. These mechanisms have also been supported by the courts, especially in light of Section 89<sup>6</sup> of the Civil Procedure Code of 1908, which permits courts to refer conflicts to ADR procedures such as conciliation and mediation.

## INDIA'S TAXATION NATURE

Taxation is one of the keys of the Indian government, representing its sovereign authority to levy and collect taxes to finance infrastructure and public services. Statutory legislation such as the Income Tax Act 1961<sup>7</sup> and the Goods and Services Tax (GST) Act, which has established the parameters for tax assessment, collection, and dispute resolution, regulate taxation in India.<sup>8</sup>

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<sup>3</sup> The Arbitration Act 1940

<sup>4</sup> Arbitration and Conciliation Act 1996

<sup>5</sup> Hemant More, 'Salient Features of Arbitration and Conciliation Act, 1996' (*The Fact Factor*, 08 March 2021)

<[https://thefactfactor.com/facts/law/civil\\_law/alternate-dispute-resolution/arbitration-and-conciliation-act-1996/16477/#google\\_vignette](https://thefactfactor.com/facts/law/civil_law/alternate-dispute-resolution/arbitration-and-conciliation-act-1996/16477/#google_vignette)> accessed 26 October 2024

<sup>6</sup> Code of Civil Procedure 1908, s 89

<sup>7</sup> Income Tax Act 1961

<sup>8</sup> Sriram Govind and Samira Varanasi, 'Dispute Resolution In Tax Matter: An India-UK Comparative Perspective' (2013) 9 *International Taxation*

<[https://www.nishithdesai.com/fileadmin/user\\_upload/pdfs/Research%20Articles/Dispute\\_Resolution\\_in\\_Tax\\_Matters.pdf](https://www.nishithdesai.com/fileadmin/user_upload/pdfs/Research%20Articles/Dispute_Resolution_in_Tax_Matters.pdf)> accessed 26 October 2024

The ITA legislation requires the taxpayer to conduct a self-assessment, and it is the taxpayer's responsibility to submit his income tax returns to the authorities within the time frame specified by the legislation.<sup>9</sup> Depending on the Assessing officer's (AO) jurisdiction, the return file is then forwarded to the appropriate assessing officer (AO), who has the authority to approve or reject the return, which is detailed in an assessment order.

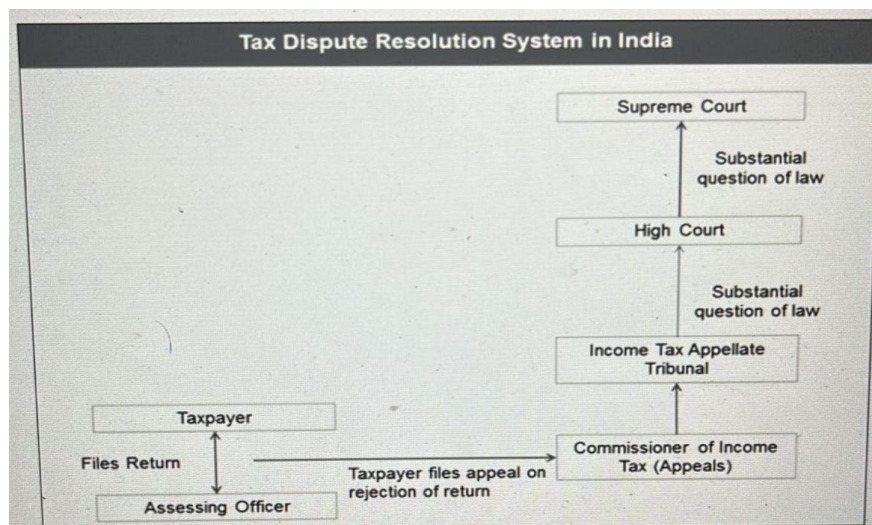
The dispute resolution arises in tax matters when the taxpayer is dissatisfied with the AO's assessment order. The taxpayer may file an appeal with the Commissioner of Income-tax (Appeals) (CIT(A)) if he feels wronged by the assessment order. The CIT(A) may issue an order that amends, denies, or improves the AO's order after providing the taxpayer with a fair hearing and considering the information at hand. Both the taxpayer and the revenue authorities, if they feel wronged, may file an appeal from the CIT(A) with the Income Tax Appellate Tribunal ('ITAT'). The ITAT allows for a thorough re-examination of the facts and evidence and serves as the ultimate fact-finding authority. From this point on, the parties can choose to appeal further to the High Court and ultimately to the Hon'ble Supreme Court. However, only 'substantial questions of law' are eligible for such appeals. Apart from this process, in situations where a miscarriage of justice occurs, a writ petition may also be filed to request judicial review from the High Courts or the Supreme Court of India.<sup>10</sup>

The fundamental idea behind tax disputes is that they involve public funds and policy and that they should be resolved in a transparent manner that is open to judicial review. As ADR is frequently viewed as a private form of conflict resolution, intended for commercial or contractual matters rather than public law issues like taxation, this assumption has historically kept ADR techniques like arbitration and mediation out of the tax dispute arena.

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<sup>9</sup> Income Tax Act 1961, s 139

<sup>10</sup> Govind (n 8)



### CLASH BETWEEN ADR AND TAX

**Sovereignty and Public Interest:** Taxation and Alternative Dispute Resolution (ADR) collide because of their fundamentally different natures. While ADR, especially arbitration, is based on private participation and flexibility and is perceived as privatizing tax adjudication and on the other hand taxation is a sovereign responsibility of the state that involves public law and policy issues. This calls into question the state's capacity to manage tax disputes, which have important ramifications for public policy.

The case of *Vodafone International Holdings B.V. v Union of India (2012)*<sup>11</sup> shows a perfect example of how tax disputes include state sovereignty. In this case, The Dutch corporation Vodafone acquired stock in a Cayman Islands business that indirectly owned telecom assets in India. According to the Indian tax authorities, Vodafone was required by Indian law to pay capital gains tax on this transaction. Vodafone, however, contested this in court, claiming that there were no Indian tax responsibilities associated with the purchase. The decision was in favour of Vodafone that there was no tax payable. The case was contested in the international arbitral tribunal where it was ruled in favour of Vodafone in 2020, posing issues regarding the boundaries of state sovereignty in taxation. This case shows how ADR mechanisms particularly arbitration can affect a state's sovereign power to tax transactions with foreign entities as the

<sup>11</sup> *Vodafone International Holdings BV v Union of India (2012) 6 SCC 613*

tribunal ruled in favour of Vodafone even after India retrospectively changed its tax laws to get Vodafone within the ambit of paying taxes.<sup>12</sup>

**Lack of Precedent:** Tax disputes often include complex interpretations of tax laws. Court rulings establish legal precedents that direct the uniform enforcement of tax legislation. ADR awards are not binding because arbitral rulings are private and only available to the parties involved. This lack of legal precedent can undermine the uniform application of tax laws.<sup>13</sup>

In the Vodafone case, the legal clarity offered by the Supreme Court's decision could not be consistently applied in subsequent instances involving comparable concerns of indirect transfers and tax obligation because there was no legally binding precedent established through arbitration. This case gave a resolution for the case of Cairn Energy PLC v Government of India (2020), but as there was an absence of binding legal precedent there was still uncertainty as to how retrospective tax law should be interpreted or applied to other countries' entities, the decision went in favour of Cairn energy.<sup>14</sup>

**Finality in Awards:** Arbitration awards are legally binding and can only be challenged on very limited grounds.<sup>15</sup> In India, an award may only be revoked under Section 34 of the Arbitration and Conciliation Act, 1996<sup>16</sup>, if certain requirements are satisfied, such as public policy violations, fraud, or corruption, or if the subject matter of the dispute is not arbitrable under Indian law. On the other hand, tax disputes go through multiple levels of appeals until and unless both parties get their fair hearing. The finality of the arbitration award may make it more difficult for the government to enforce tax law compliance and recover money.

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<sup>12</sup> *Ibid*

<sup>13</sup> 'ADR programs do not set precedent neither refine legal norms, establish broad community national standards, nor do they promote a consistent application of legal rules Explain' (*The Lawyers & Jurists*) <<https://www.lawyersjurists.com/article/adr-programs-do-not-set-precedent-neither-refine-legal-norms-establish-broad-community-national-standards-nor-do-they-promote-a-consistent-application-of-legal-rules-explain/>> accessed 25 October 2024

<sup>14</sup> *Ibid*

<sup>15</sup> 'Challenging Arbitration Awards: Grounds and Processes' (*Broderick Bozimo & Company*, 12 October 2023) <<https://broderickbozimo.com/challenging-arbitration-awards-grounds-and-processes/>> accessed 24 October 2024

<sup>16</sup> Arbitration and Conciliation Act 1996, s 34

## INTERNATIONAL COMPARISON AND ANALYSIS

### Japan -

**1. Administrative Review as Primary Mechanism:**<sup>17</sup> Japan uses an administrative review framework to resolve tax disputes as against the comprehensive Alternative Dispute Resolution system. This system is fundamentally anchored in the National Tax Tribunal, also known as the NTT. NTT is an autonomous entity consisting of tax specialists who render unbiased decisions in the complaints filed by taxpayers. This Japanese system is inclined to promote prompt administrative resolution before the escalation of disputes to the judicial level. The taxpayers who contest the tax assessment, are entitled to solicit a reinvestigation from the district director of the tax office. This is subsequently followed by a review with the National Tax Tribunal. If the taxpayers in this proceeding, are dissatisfied with the ruling of the National Tax Tribunal then, they can go for litigation however, this course of action is usually seen as a measure of last resort.<sup>18</sup>

**2. Focus on Efficiency and Reduced Litigation:** Japan's methodology showcases the significance of reducing judicial participation by providing a dependable administrative remedy which is less burdensome and more expedient as compared to the traditional/conventional way of litigation. This procedural approach safeguards the courts from being inundated with substantial quantities of tax cases because the system provides for resolution with the help of specialized knowledge.<sup>19</sup>

**3. Comparison with India:** Comparing India with Japan's dependence on administrative review, India's tax dispute resolution framework is characterized by heavy litigation which is further accompanied by limited avenues for non-judicial resolution. India is dependent on multiple tiers of appellate review which increases the case backlog while on the other hand,

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<sup>17</sup> Supriyo De, 'Direct Taxes Litigation Management and Alternate Dispute Resolution' (*National Institute of Public Finance and Policy*, 25 April 2023) <[https://nipfp.org.in/media/medialibrary/2023/04/WP\\_394\\_2023.pdf](https://nipfp.org.in/media/medialibrary/2023/04/WP_394_2023.pdf)> accessed 25 October 2024

<sup>18</sup> Act on General Rules for National Taxes 1962, art 23

<sup>19</sup> De (n 17)



Japan has a consolidated administrative framework which facilitates faster resolutions and mitigates court congestion.

**4. Feasibility for India:** India can consider the viability of instituting a corresponding administrative tribunal, comprising tax experts, to adjudicate routine tax disputes which would alleviate the burden on the appellate framework. Such an establishment which is a specialized administrative entity endowed with binding authority over lower-tier disputes could enhance the efficiency of dispute resolution. However, in contrast to Japan, India may mandate amendments to its tax law to confer binding power upon these entities, particularly in matters pertaining to revenue interests.

#### **Malaysia -**

**1. Mandatory Mediation and Facilitative Processes:** The Malaysian tax system has incorporated an Alternative Dispute Resolution mechanism through the establishment of Mandatory Mediation as an initial recourse for tax-related disputes. This is done with the objective of resolving the issues prior to escalation into litigation. This mediation process is conducted by trained mediators who typically are affiliated with the Malaysian Inland Revenue Board. This would further help in fostering a collaborative environment between the taxpayer and the tax authority which aims at achieving resolution. Further, Malaysia's ADR framework provides for Advance Rulings and Tax Audits which serve to elucidate clarifications in advance. These rulings mitigate misunderstandings and facilitate proactive compliance among taxpayers.<sup>20</sup>

**2. Efficiency and Taxpayer Confidence:** The Malaysian ADR system prioritizes the enhancement of taxpayer confidence and encourages proactive participation. The implementation of mandatory mediation helps in reducing adversarial mechanisms for the resolution of disputes, thus cultivating trust between taxpayers and tax authorities. This kind of approach is characterized by its efficiency and tax-payer-concerned nature. This significantly reduces the incidence of the cases escalating to the higher appellate levels.<sup>21</sup>

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<sup>20</sup> Mediation Act 2012

<sup>21</sup> De (n 17)

**3. Comparison with India:** In contrast, India's approach is devoid of a comparable mandatory mediation framework, largely dependent on the traditional litigation process, which is frequently perceived as adversarial and protracted. The limited ADR options available in India, predominantly pertain to international tax issues, whereas Malaysia has implemented ADR mechanisms applicable to a wider spectrum of disputes.

**4. Feasibility for India:** The adaptation of a mandatory mediation program similar to that in Malaysia may be viable for India, particularly considering lower-value or less complex tax disputes. The establishment of a mediation process which is under the guidance of trained tax officials would enable better resolution of disputes, resulting in conservation of time and resources for both taxpayers and the tax administration. The implementation of mandatory mediation would require frequent legislative modifications to the Indian Income Tax Act, in addition to an investment in the training of tax officials in mediation competency.

#### **Australia -**

**1. Coordinates ADR Program and in-house Assistance:**<sup>22</sup> Australia has an advanced ADR system, which is under the Australian Charge Office (ATO), which joins both in-house assistance and outside intervention. For reduced and minimal difficulty, the ATO gives inside facilitators who help citizens and case officers come to decisions early within the debate handle. For more complex cases, the ATO permits outside intervention where an unbiased third-party go makes a difference resolve the debate exterior of the court.<sup>23</sup> The ADR mechanism in Australia incorporates authoritative progress estimating understandings. It is present for complex exchange estimating cases. It is comparable to the US which anticipates future debates by setting up foreordained estimating exchanges between related substances.<sup>24</sup>

**2. Versatility and taking a toll Effectiveness:** Australia's ADR system allows the ATO to change the method to suit the complexity of the cases concerned. The in-house assistance for less complex cases is cost-efficient and it also reduces the time and cost of the conventional case.

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<sup>22</sup> *Ibid*

<sup>23</sup> Taxation Administration Act 1953, ss 14Z

<sup>24</sup> Income Tax Assessment Act 1997, ss 815

Outside intervention gives a free road for determination, making a difference keep up a lack of bias in high-stakes cases.

**3. Comparison with India:** Australia's ADR framework is well-integrated into its charge organization, differentiating from India's litigation-heavy approach. The Indian assessment debate handle needs the adaptability and case-specific approach that Australia's framework gives, as well as the alternative of in-house help for clear cases.

Possibility for India: India can consider a similar ADR framework by having an in-house assistance group in the Salary Charge Division to intercede in scheduled debates. This group would act as an impartial party to assist citizens and assess authorities to reach a neighbourly settlement. This shall also reduce heightening to higher re-appraising bodies. Additionally, external intervention may be presented for high-stake or complex cases such as those which include MNCs. Having such a framework would need a cultural shift inside the tax organization. This shift has to be centered on collaborative determination which might be empowered through pilot programs and staged selections.

## **United States -**

**1. Expedited ADR with Fast-Track ADR, Mediation, and Arbitration by the IRS:**<sup>25</sup> The US Tax System which is regulated by the Internal Revenue Service (IRS) incorporates Alternative Dispute Resolution (ADR) mechanisms such as the Fast Track Settlement (FTS) and Post Appeals Mediation (PAM). These mechanisms provide for the resolution of disputes, particularly in intricate international tax contexts like transfer pricing, by doing timely intervention and without compulsorily resorting to full-scale litigation. The IRS engages in mediating tax disputes by bringing in tax specialists and trained appeals officers to function as neutral facilitators. These ADR mechanisms help in better efficiency of dispute resolution processes thereby, resulting in timely and expert-driven decisions achieved at lower

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<sup>25</sup> Priyanka and Ritanshi Jain, 'Comparative Analysis of Taxation Dispute Resolution Mechanism between different Countries India, USA, Europe and Canada' (2023) 26(7) Pen Acclaims  
<<http://www.penacclaims.com/wp-content/uploads/2023/07/Priyanka-and-Ritanshi-Jain.pdf>> accessed 26 October 2024

administrative levels. This further reduces the need for court intervention and curtails the costs which are associated with the traditional way of litigation.<sup>26</sup>

**2. Use of Arbitration for International Tax Disputes:** In the realm of international tax disputes, particularly those involving multinational entities, the United States uses Advance Pricing Agreements (APAs), which facilitate the preemptive settlement of transfer pricing matters to avoid future conflicts.<sup>27</sup> Arbitration is also accessible in specific unresolved international tax circumstances, notably in instances involving double taxation. This methodology mitigates the risks associated with double taxation and promotes adherence to tax obligations by offering predictability and transparency, particularly in transactions that cross national borders.<sup>28</sup>

**3. Comparison with India:** India's ADR framework governing tax disputes is relatively constrained. For the majority of domestic tax disputes, India relies on a multi-tiered appellate framework that may extend over several years for resolution. The operational efficiency of the US model, characterized by a diminished reliance on litigation, serves as a compelling example of how ADR can help in reducing the backlog of tax disputes whereas, India's litigation-heavy approach continues to be burdened by protracted cases.

**4. Feasibility for India:** The adaptation of the U.S. fast-tracks and APA methodologies for the Indian context could facilitate the streamlining of complex disputes and foster a culture oriented towards ADR-based resolutions. India could consider the implementation of a Fast-Track Mediation framework for high-stakes tax disputes, while further adaptation of the APA model could be explored to address domestic transfer pricing issues that frequently give rise to disputes. The successful implementation of these strategies would necessitate legislative modifications to render specific tax cases subject to arbitration. Additionally, the establishment of a Tax Mediation Division within the Income Tax Department, led by tax professionals, could ensure that ADR alternatives for intricate cases are accessible from the earliest stages.

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<sup>26</sup> Internal Revenue Code 1986

<sup>27</sup> Advance Pricing Agreements, Revenue Procedure 2015

<sup>28</sup> De (n 17)

## United Kingdom –

**1. Statutory Review and Formal Mediation:**<sup>29</sup> The HMRC of the United Kingdom administers a meticulously organized ADR framework. The Taxpayers are allowed to seek a Statutory Review, where an impartial officer, who is not involved in the initial decision-making process, properly examines the cases independently. This evaluation done by the officer acts as a preliminary mediatory mechanism as it provides for an early resolution of disputes. Further, the UK has a formal mediation initiative within HMRC and it proffers ADR alternatives which enhances the negotiation and settlement processes and is devoid of judicial intervention. This kind of approach reduces litigation costs and increases the speed of decision-making. This is particularly true in the cases which are characterized by substantial or intricate tax-related conflicts.<sup>30</sup>

**2. High-Risk Corporate Programme:** To address the high-value and multifaceted cases that pertain to MNCs, HMRC uses the High-Risk Corporate Programme which gives priority to expeditious resolutions with the help of negotiation and mediation.<sup>31</sup> The HRCP also allows the HMRC and corporate entities to solve disputes in a methodical and adaptable manner which also results in reduced protracted litigation.<sup>32</sup>

**3. Comparison with India:** The existing tax dispute resolution framework in India is deficient in structured mediation or review alternatives that are similar to the statutory review and formal mediation practices observed in the United Kingdom. The Indian ADR mechanism predominantly follows an adversarial model, with cases frequently going through multiple appellate stages. Moreover, India lacks a program that mirrors the HRCP, relegating high-stakes corporate disputes to conventional appellate procedures.

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<sup>29</sup> Govind (n 8)

<sup>30</sup> Taxes Management Act 1970, s 82

<sup>31</sup> Taxation (International and Other Provisions) Act 2010

<sup>32</sup> Govind (n 8)

The model adopted by the United Kingdom underscores the importance of specialized mediation options, thereby engendering a more adaptable and efficient ADR system that resolves cases before they escalate into litigation, in stark contrast to India.

**4. Feasibility for India:** India can consider the implementation of a Statutory Review framework and it can be used as an introductory ADR mechanism. It is particularly for the disputes that have ascended to the appellate stage. Similar to the UK model, a Tax Mediation Team could undertake an independent review of cases which provides for a non-adversarial environment which is conducive to negotiation.

The bringing of a program which is similar to the HRCP in India would be beneficial, particularly for intricate or high-stakes corporate disputes. Such a program would provide for properly structured mediation and negotiation processes for large corporate entities. This would result in the promotion of swifter resolutions and reduce the burden on higher judicial courts. To get the full benefit of it, India would have to bring amendments to the Income Tax Act to incorporate mediation protocols and to constitute a specialized corporate tax mediation team.

## European Union -

**1. Mutual Agreement Procedure for International Tax Disputes:** The Mutual Agreement Procedure was established by the European Union and it serves as a mechanism for ADR which aims at adjudicating tax disputes amongst member states. This procedure is often used in cases of double taxation and various cross-border tax complications which permits the tax authorities of distinct nations to come together and formulate case-specific resolutions devoid of litigation. Mutual Agreement Procedure promotes collaborative dispute resolution typically within a biennial timeframe which provides expeditious resolutions which circumvents protracted judicial processes.<sup>33</sup>

**2. Binding Arbitration as a Secondary Mechanism:**<sup>34</sup> In cases where MAP is not effective in the resolution of a dispute, the EU uses binding arbitration through an Advisory Commission which

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<sup>33</sup> Council Directive 2017

<sup>34</sup> Priyanka (n 26)

comprises tax specialists who deliver a conclusive resolution. This framework is particularly beneficial in cases where there is a need for an impartial adjudication to uphold fairness and consistency across disparate jurisdictions. The determination rendered by the arbitration panel is obligatory and it ensures that the disputes are conclusively resolved. It is specifically used in intricate international matters where mutual consensus is not available.<sup>35</sup>

**3. Comparison with India:** India's ADR framework is deficient in the binding arbitration mechanism afforded by the EU. Indian MAP cases often encounter delays attributable to constrained resources and substantial caseloads. While the EU's methodical MAP and arbitration model facilitates swifter resolutions. The EU focuses on collaborative, expedient, and binding ADR which is a stark contrast to India's constrained and slower MAP process which sometimes culminates in unresolved cases due to a lack of sufficient binding authority.

**4. Feasibility for India:** The adoption of a binding arbitration mechanism for cases unresolved by MAP could significantly enhance the efficacy of India's international tax dispute resolution framework. This would ensure that cross-border disputes are addressed in a definitive and time-sensitive manner, thereby diminishing the likelihood of protracted disputes.

The implementation of binding arbitration would necessitate amendments to India's DTAs to allow for arbitration as a final recourse in instances where MAP proves ineffective. Establishing a National Advisory Commission on International Tax Disputes, staffed by tax experts, could bolster binding arbitration and expedite the resolution of intricate international cases involving multinational entities.

## **ARBITRATING TAX DISPUTES: A VIABLE PATH OR A THREAT TO SOVEREIGN TAXATION?**

### **Current Dispute Resolution Regime -**

The international comparison drawn has sown the seed for a conversation to be had for alternate dispute resolution modes in India for taxation. The amounts suffered by assesseees in litigation

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<sup>35</sup> Council Directive 2017, ss 14

have increased to rampant amounts as the sole resolution lies to the court. If it involves cases of tax evasion or criminal proceedings, the case should not be dealt with alternate modes of resolution as criminal cases are explicitly excluded from arbitration and if so included, they would violate the justice system.

Trends seen with the latest assessment of 2019-2020, the Central Board of Direct Taxes showed the amount locked up in solely direct tax cases. It was nearly Rs. 3 lakh crores<sup>36</sup>. The total number of cases received by ITAT, High Courts and Supreme Courts has by approximately 76% from 2015-2016 to 2019-2020<sup>37</sup>. The current procedure for tax litigation is provided in a flowchart below with the estimated average time frames at each phase of litigation after computation by the assessing officer.



Thus, if an amount of income tax is to be challenged by the Apex Court, it will require a minimum time frame of 20 years. No individual wants to suffer for 20 years leading their efforts in vain if the case is unsuccessful and neither does everyone have the resources to achieve these recourses. Thus, the mandate of alternate dispute resolutions becomes apparent. The question arises as to whether has India made strides towards these methods.

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<sup>36</sup> De (n 17)

<sup>37</sup> *Ibid*



## Several Attempts by India -

**International Taxpayers:** The structure for these attempts can be divided into two categories of people. The first is for international taxpayers.

These are known as limited dispute resolution mechanisms. These are not in a tiered structure and can be approached by any person internationally paying tax in India at any stage. The first is the Board of Advanced Rulings which replaced the Authority for Advanced Rulings in 2021<sup>38</sup>. This means a written decision by an authority empowered to render it. This process is similar to indirect taxes specifically GST. The next is the Mutual Agreement Procedure which is primarily available in several Double Tax Avoidance Agreements the limitation in this is that the role of taxpayer in presenting their dispute is restricted in nature. The third mechanism is the Advance Pricing Agreement which is between the taxpayer and the tax authority for pricing methodology for a specific duration of time over a set of transactions. The last alternate mode is the Dispute Resolution Panel which deals with transfer pricing disputes and objections filed by non-residents after the draft assessment order by the assessing officer. However, one issue is all these alternate modes primarily deal with transfer pricing disputes.<sup>39</sup>

## DOMESTIC TAXPAYERS

Now what is to be seen is dispute resolution modes for domestic taxpayers. The Income Tax Settlement Commission deals with settlement application by assesseees for undisclosed income from search and seizures. However, this established Commission ceased to operate from 1<sup>st</sup> February 2021<sup>40</sup>. Ad-hoc dispute resolution schemes are one-time attempts to resolve tax disputes which involve a leeway to taxpayers for some amount or no penalties. Another scheme was the Direct Taxes Dispute Resolution Scheme which aimed at reducing the backlog of cases

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<sup>38</sup> Deepak Chopra, 'BAR: The Unfulfilled Promise of AAR?' (*AZB Partners*, 04 July 2023) <<https://www.azbpartners.com/bank/bar-the-unfulfilled-promise-of-aar/>> accessed 27 October 2024

<sup>39</sup> De (n 17)

<sup>40</sup> 'Scrapping of Income-Tax Settlement Commission' (*Shankar IAS Parliament*, 24 February 2021) <<https://www.shankariasparliament.com/current-affairs/scrapping-of-income-tax-settlement-commission>> accessed 02 November 2024

pending before the CIT(A). However, this scheme was waived off after 6 months<sup>41</sup>. There was another renowned scheme, the Vivad Se Vishwas Scheme 2021 which was also a scheme based on a fast-track procedure as dispute dispute-resolving mechanism thus leading to a reduction of tax disputes. It helped in settling more than 1.48 lakh cases and recovered 54% of nearly Rs 1 Lakh crores amount in litigation left. There are no permanent modes of dispute resolution followed in other countries mediation, negotiation, or primarily arbitration. The reason why the term 'Attempts' has been put in quotations is to require more permanent models for these attempts to succeed for a long haul rather than a short ride.

The model studied for international taxpayers in India is based on the OECD Model guidelines for international taxpayers. OECD has also evolved to include arbitration clauses for resolving tax disputes. Though there is sufficient recourse for international taxpayers, domestic taxpayers might feel neglected as they solely rely on litigation. But what is the rationale for not applying these OECD Model guidelines to domestic taxpayers as well for dispute resolution? India must adopt a special or better known as alternate dispute resolution like other countries to work for a better tax administrative structure with the primary focus being on arbitration. These include resolution modes such as mediation with India making strides by implementing the Mediation Act 2023. Arbitration is another mode which is being promoted time and time by OECD countries for the resolution of disputes. It is not like any arbitration and there will be certain tweaks required. The tribunal must comprise erudite personnel in tax with departmental officers and tax officials who have been in practice for a prescribed period.

### **IF AAR WORKS, WHY NOT ARBITRATION?**

The direct tax reforms for international taxpayers are through BAR and for indirect tax reforms, there is a similar forum, but for domestic taxpayers which is the Authority for Advance Ruling or better known as AAR. In GST there is one major issue faced where though we do have a forum for clarification and it works as a quasi-judicial forum, after this there is one appellate authority which is the Appellate Authority for Advance Ruling or AAAR. Since the institution

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<sup>41</sup> Ministry of Finance, 'Direct Tax Dispute Resolution Scheme, 2016 which has come into force from 1st June, 2016, can be availed up to 31st December, 2016' (*Press Information Bureau*, 15 September 2016) <<https://pib.gov.in/newsite/PrintRelease.aspx?relid=149797>> accessed 04 November 2024

of the GST regime, after 7 years as well, the Goods and Service Tax Appellate Tribunal has not yet been implemented due to contingencies not being fulfilled from time to time. Thus, for the taxpayers, the sole authority for adjudication is these AAR and AAAR and then directly move to the High Courts. When we consider the functioning of an AAR, they work as a clarificatory forum as well as a quasi-judicial forum where people reach for disputes between assessing officer and assessee. This work forum works like arbitration as this decision does not hold any binding value for other people. It has some persuasive value but the issue is that as well as every state has a different perception and every state on the same issue has given conflicting judgements. For instance, regarding the classification of goods. One state's AAR places it in the 12% category while the other state's AAR places it in the 18% category. Who is to decide which AAR interpreted the law better and what decision should be relied upon? Another issue is that AAR is not dealing with all the questions. Under section 97 of the CGST Act<sup>42</sup> provides an exhaustive list for questions that can be put before the Authority by procedure of application. This means that no other question can be brought before the authority and for other questions, only the courts must be approached which not only is a time-consuming process but also a resourceful process which not every small business or shopkeeper will possess.

With all the plausible solutions in hand, one does not apply their intellect to think of a similar procedure which is arbitration. In arbitration as well, the decision is binding only on the two parties in agreement for arbitration. The arbitration process works like authority, but in this case, the agreement will state exactly what question is to be presented before the arbitral tribunal. Since arbitration clauses work as separate agreements as stated in section 7(2) of the Arbitration and Conciliation Act<sup>43</sup>. The assessing officer while drafting the show cause notice, especially stating the key issues in the assessment, in the end, can have an arbitration clause which as stated will not be mandatory. The assessee may follow the procedure of filing objections through several forms and wait for nearly a period of 7 to 8 months for this process to complete or sign the arbitration clause, fulfilling the voluntary requirement.

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<sup>42</sup> Central Goods and Service Tax Act 2017, s 97

<sup>43</sup> Arbitration and Conciliation Act 1996, s 7(2)

## SUGGESTED FRAMEWORK

The arbitral tribunal will comprise of three arbitrators minimum. The first arbitration or the presiding arbitrator will be a retired Judge of the High court in which the assessee resides. The second arbitrator will be a retired tax department official either direct or indirect depending upon the tax issue at hand and he must be retired so that an unbiased point of view is taken by the majority. Lastly an advocate of the High court in which the assessee resides. Bringing such a large project to implementation will require specific tweaks and amendments for this specific purpose of including tax disputes in the ambit of arbitration, but the ethos of it remains the same, a speedy resolution process binding on both parties. Another advantage is that it will not work in an appealable process, and the award by the tribunal will only be set aside by an exhaustive list of circumstances under section 34 of the Arbitration and Conciliation Act<sup>44</sup> thus this would not allow every appeal on a decision of the arbitral award. To clarify lucidly, criminal proceedings to tax disputes will not be arbitrable explicitly. Thus, this process works like an AAR saving time as well as resources for the assessee, and for the government since arbitration has specified time restrictions it will leak the clogged-up money in tax disputes pending in courts.

## IS SOVEREIGNTY TRULY UNDER THREAT?

The right to tax is a sovereign right of a country. This is one of the primary reasons argued by India for keeping the subject matter of taxation outside of arbitration or even other alternate dispute resolution methods. This is the reason India, has unilaterally terminated bilateral investment treaties with about 57 countries including the Netherlands which is of significance as seen later<sup>45</sup>. This is due to again; the sovereign right India has been reiterating and it is a consequence of a few cases opposing India as these treaties had arbitration clauses and India has never been able to digest someone trying to 'Challenge their authority.'

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<sup>44</sup> Arbitration and Conciliation Act 1996, s 34

<sup>45</sup> 'India terminates bilateral investment treaties (BITs)' (*Both Ends*, 11 August 2016)

<https://www.bothends.org/en/Whats-new/News/India-terminates-bilateral-investment-treaties-BITs-/>

accessed 03 November 2024

Everyone as a law enthusiast or in the corporate field must have heard of the Vodafone Holdings Case. The Apex Court in our country held that the action of Vodafone was not subject to tax in India under section 9 of the Income Tax Act<sup>46</sup>. India always being a tax-favouring country, made a retrospective amendment targeting Vodafone within the tax ambit, though not specifically stating it, the language of the amendment shows the same. Vodafone applying the Bilateral Investment Treaty (BIT) between India and the Netherlands initiated arbitration in the Permanent Court of Arbitration titled Vodafone Holding v Republic of India<sup>47</sup>. The Permanent Court of Arbitration ruling in favour of Vodafone Holding stated India has acted in a discriminatory manner towards Vodafone and India has no right to collect taxes from Vodafone interpreting Article 4(1) of the BIT<sup>48</sup>. Another case by Cairn as well as Vedanta with nearly 15 cases being filed by investors using bilateral investment treaties in the Permanent Court of Arbitration regarding retrospective taxation, with all awards not being in favour of India and half being withdrawn by settlement<sup>49</sup>. This shows India's fear stemming from arbitration in taxation. But the question remains, if companies outside use arbitration clauses in treaties where the parties are the foreign investor and the government of India, what is the difference when an individual taxpayer does it with the government of India? The Permanent Court of Arbitration is deciding upon a matter regarding Indian taxation and the same will be done within India by Indian arbitrators. If anything, this reduces the scope of foreign intervention and India has control over their arbitration proceedings in accordance with law.

## CONCLUSION

It is clear from our research that India will not be the first country to step up and consider ADR methods for tax disputes. Arbitration is not the sole recourse for tax dispute resolution; alternative mechanisms such as Negotiation, Mediation, and Conciliation may also be effectively incorporated within India's legal framework, ensuring a more comprehensive and

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<sup>46</sup> Income Tax Act 1961, s 9

<sup>47</sup> *Vodafone Holding v Republic of India* (2016) PCA Case No 2016-35

<sup>48</sup> India-Netherlands Bilateral Investment Treaty 2016, art 4(1)

<sup>49</sup> Kshama A. Loya and Vyapak Desai, 'The Cairn Energy v India Saga: A Case of Retrospective Tax and Sovereign Resistance Against Investor State Awards' (*Kluwer Arbitration Blog*, 02 July 2021)

<<https://arbitrationblog.kluwerarbitration.com/2021/07/02/the-cairn-energy-v-india-saga-a-case-of-retrospective-tax-and-sovereign-resistance-against-investor-state-awards/>> accessed 04 November 2024

structured approach to dispute adjudication. The framework need not be as stated above but can lay the groundwork for the head start of such a mechanism. It is time for India to stop playing catch-up with other countries and realise this tax litigation does not help either the assessee or the government. Alternate Dispute Resolution methods are the future and with India being pro-arbitration in the last few years, it must make strides to bring several ambits of economics, one of which is primarily taxation. Just like a DTAA or a bilateral investment treaty, a provision for this needs to be incorporated. India can borrow from the countries as stated above and establish a groundwork solid for great architecture for the future. The country's repertoire in the international framework will also be appreciated. Taxes are till death but while waiting for tax disputes to be resolved, death beats them in the race. ADR is an evolving mechanism and it is the need of the hour. India has set up the groundwork, including this mechanism in disputes and it is time to take a step forward in taxation disputes.