

UNION BUDGET 2018

DIRECT TAX PROPOSALS



SEQUENCE OF TOPICS

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RATES OF TAX AND PERSONAL TAXATION

Tax Rates – Individuals/HUF

w.e.f. 01.04.2019

Income	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
A) General (other than Senior citizens & Very senior citizens):		
Upto Rs.2,50,000*	NIL	NIL
Between Rs. 2,50,001 and Rs. 5,00,000*	5.15%	5.2%
Between Rs. 5,00,001 and Rs. 10,00,000	20.60%	20.80%
Between Rs. 10,00,001 and Rs. 50,00,000	30.90%	31.20%
Between Rs. 50,00,001 and Rs.1 crore	33.99%	34.32%
Above Rs.1 crore	35.53%	35.88%
B) Senior citizens - Resident (aged 60 years or above but less than 80 years):		
Upto Rs. 3,00,000*	NIL	NIL
Between Rs. 3,00,001 and Rs. 5,00,000*	5.15%	5.2%
Between Rs. Rs. 5,00,001 and Rs. 10,00,000	20.60%	20.80%
Between Rs. 10,00,001 and Rs. 50,00,000	30.90%	31.20%
Between Rs. 50,00,001 and Rs. 1 crore	33.99%	34.32%
Above Rs.1 crore	35.53%	35.88%

Tax Rates – Individuals/HUF

w.e.f. 01.04.2019

Income	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
C) Super Senior Citizen – Resident (aged 80 years or more)		
Upto Rs. 5,00,000	NIL	NIL
Between Rs. 5,00,001 and Rs. 10,00,000	20.60%	20.80%
Between Rs. 10,00,001 and Rs. 50,00,000	30.90%	31.20%
Between Rs. 50,00,001 and Rs. 1 crore	33.99%	34.32%
Above Rs. 1 crore	35.53%	35.88%
* <u>NOTE:</u> Rebate - maximum of Rs.2,500 from the tax payable would be admissible under section 87A of the Act to those individuals whose total income does not exceed Rs.3,50,000 p.a.		

Tax Rates – Domestic Companies

w.e.f. 01.04.2019

Total Turnover	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
<u>Upto Rs. 10 crores</u> - Income upto Rs. 1 crore - Income above Rs.1 crore (inclusive of surcharge @ 7%)	25.75% 27.55%	26% 27.82%
<u>Rs.10 crores to Rs.250 crores</u> - Income upto Rs.50 crores (inclusive of surcharge @12%) - Income above Rs.50 crores (inclusive of surcharge @ 12%)	28.84% 34.61%	29.12% 29.12%
<u>Above Rs.250 crores</u> Income above Rs.250 crores (inclusive of surcharge @ 12%)	34.61%	34.94%

Tax Rates – Foreign Company

w.e.f. 01.04.2019

Total Turnover	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
<u>Upto Rs. 1 crores</u>	41.2%	41.6%
<u>Rs.1 crores to Rs.10 crores</u> (inclusive of surcharge @ 2%)	42.02 %	42.43%
<u>Above Rs.10 crores</u> (inclusive of surcharge @ 5%)	34.61%	34.94%

Tax Rates – Local Authority/ Firm

w.e.f. 01.04.2019

Total Turnover	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
<u>Upto Rs. 1 crores</u>	30.9%	31.2%
<u>Above Rs.10 crores</u> (inclusive of surcharge @ 12%)	34.61%	34.94%

Tax Rates – Co-operative Society

w.e.f. 01.04.2019

Income	Existing Slabs (A.Y. 2018-19)	Proposed Slabs (A.Y. 2019-20)
<u>Upto Rs. 10,000</u>	10.3%	10.4%
<u>Rs.10,000 to Rs.20,000</u>	20.6 %	20.8%
<u>Rs.20,000 to Rs.1 crore</u>	30.9%	31.2%
<u>Above Rs.1 crores</u> (inclusive of surcharge @ 12%)	34.61%	34.94%

Changes in Tax Rates

[Chapter II & First Schedule]

(w.e.f. 01.04.2019)

- ❖ Cess has been proposed to be increased by 1% from earlier 3% to 4% (Health and Education Cess on income tax).
- ❖ Tax rate of 25% is applicable if turnover of the domestic company in the financial year 2016-17 does not exceed Rs.250 Cr. (increased from Rs.50 Cr.)

Reliefs/ Benefits to Senior Citizen(s)

[Clauses 24, 25, 29, 30 & 47]

Finance Bill has brought bunch of benefit for senior citizens:

❖ **Deduction under Section 80D (w.e.f 1.04.2019)**

Maximum deduction in respect of medical expenditure of a senior citizen has been raised from existing Rs.30,000 to Rs.50,000.

❖ Deduction shall be allowed on proportionate basis in respect of single premium health insurance policies having cover of more than one year.

Reliefs/ Benefits to Senior Citizen(s) (cont.)

[Clauses 24, 25, 29, 30 & 47]

❖ Deduction under Section 80DDB (w.e.f 1.04.2019)

Maximum monetary limit of deduction allowable to assessee for payment of medical treatment of senior citizen/ very senior citizen is proposed to be enhanced from existing Rs.60,000/ Rs.80,000 to Rs.1,00,000

❖ Deduction under Section 80TTB (w.e.f 1.04.2019)

Deduction to the extent of Rs.50,000 shall be allowed to senior citizen on the interest income from bank/ PO deposits as against Rs.10,000 u/s 80TTA.

Reliefs/ Benefits to Senior Citizen(s) (cont.)

[Clauses 24, 25, 29, 30 & 47]

❖ Increased limit in Section 194A (w.e.f 1.04.2018)

Consequential amendment is proposed in section 194A providing for non-deduction of tax at source on interest to the extent of Rs.50,000 payable to senior citizen

Standard deduction to salaried individuals

[Clauses 7 & 8]

(w.e.f. 01.04.2019)

- ❖ Section 16 provides for certain deductions while computing income under the head ‘salaries’.
- ❖ It is proposed to insert clause (ia) in section 16 to provide standard deduction of lower of Rs.40,000 or the amount of salary in place of exemption of transport allowance (except in case of differently abled persons) [Section 10(14)(ii) read with rule 2BB(2)] and reimbursement of medical expense [clause (v) of the proviso to section 17(2)].

Standard deduction to salaried individuals (cont.)

[Clauses 7 & 8]

(w.e.f. 01.04.2019)

Comments/ Observations:

- ❖ Proposed to reduce burden on salaried employees and lower gap between the average of taxes paid by the salaried taxpayer and business/ professional taxpayer.
- ❖ Impact of standard deduction of Rs.40,000 would be marginal on account of withdrawal of deductions aggregating to Rs.34,200 (Rs.19,200 for travelling allowance and Rs.15,000 towards reimbursement of medical expenses).

PROFITS & GAINS OF BUSINESS OR PROFESSION

Conversion of stock in trade into capital assets

[Clauses 3, 9 & 18]

(w.r.e.f. 01.04.2019)

- ❖ Presently, section 45(2) provides mechanism for taxation on conversion of a capital asset into stock-in-trade, but there is no specific provision dealing with a situation where stock-in-trade is converted into a capital asset.
- ❖ It is now proposed to amend section 28 of the Act to provide that the fair market value of the inventory as on the date of conversion or such treatment shall be taxable as business income.
- ❖ Further, while section 49 is proposed to be amended to treat fair market value on the date of conversion to be the cost of acquisition, section 2(42A) is proposed to be amended to reckoning the period of holding of such capital asset from the date of conversion.

Conversion of stock in trade into capital assets (cont.)

[Clauses 3,9 & 18]

(w.r.e.f. 01.04.2019)

Comments/ Observations:

- ❖ In the absence of any specific provision dealing with conversion of stock-in-trade into capital asset, there was no clarity with regard to taxation of profits arising on conversion and subsequent transfer of the capital asset.
- ❖ In **CIT-I vs. Abhinandan Investment Ltd.: 282 CTR 466 (Del HC)** the Court held that difference between the value at which the asset was held as stock-in-trade and the market value on the date of its conversion as investment would have to be treated as business income/ loss and the difference between the market value of the asset as on the date of conversion and the value at which it is sold would be in the nature of capital gains.
- ❖ The aforesaid observations of the Delhi High Court is proposed to be incorporated in the statute by amending sections 28 and 49 of the Act.
- ❖ However, the High Court in aforesaid ruling, had deferred tax on fair market value on date of conversion of stock till the date of sale of the capital asset (after conversion). While the proposed amendment requires tax on difference between value at which the asset was held as stock-in-trade and the market value on the date of its conversion to be paid in the year of conversion itself.

Conversion of stock in trade into capital assets (cont.)

[Clauses 3,9 & 18]

(w.r.e.f. 01.04.2019)

❖ In **ACIT vs. Bright Star Investment (P) Ltd.:** (2008) 24 SOT 288 (Mum), the Tribunal held that in the absence of a specific provision, the following two formulas were evolved and it was held that the assessee could adopt any one of them which was more favourable:

1. Formula A: Difference between the book value and the market value on the date of conversion be taxed as business income and the difference between the sale price and the market value on the date of conversion, be taken as capital gains.
2. Formula B: The entire difference between the sale price and the original cost of acquisition with indexation from the date of conversion be taxable as capital gains.

Conversion of stock in trade into capital assets (cont.)

[Clauses 3,9 & 18]

(w.r.e.f. 01.04.2019)

- ❖ In **Deensons Trading Co. (P.) Ltd. vs. ITO : [2017] 81 taxmann.com 71 (Chennai - Trib.)** the assessee builder changed its business and converted its stock-in-trade, i.e., property, into investment. The Tribunal held that the holding period was to be reckoned from date of conversion and not from date of acquisition, for computation of capital gains.
- ❖ Pertinently, as per the proposed amendment, taxation of FMV on date of conversion of stock is not deferred till the date of sale of the capital asset (after conversion) and hence, unrealised amount shall be taxable as business income on the date of conversion.

Taxation of compensation

[Clauses 3,9 & 21]

(w.r.e.f. 01.04.2019)

- ❖ Under the existing provision of clause (ii) section 28 of the Act, following amounts of compensation are liable to tax as business income:
 - On termination of management or modification of terms of management of Indian Company or any other company in India;
 - On termination of agency in India or modification of its terms and conditions;
 - On vesting of management of any property or business in the Government.
- ❖ In order to expand the scope of the aforesaid section, it is proposed to provide that any compensation received or receivable by the assessee, “in connection with termination or modification of terms and conditions, of any contract relating to his business” shall be taxable as business income”.
- ❖ It is further proposed to amend section 56 to provide for levy of tax on any compensation received or receivable in connection with termination or modification of terms & conditions of any contract relating to employment.

Taxation of compensation (cont.)

[Clauses 3,9 & 21]

(w.r.e.f. 01.04.2019)

Comments/Observations:

- ❖ Proposed amendments are wide sweeping inasmuch as the same cover any compensation received on termination or modification of any contract relating to business, notwithstanding the fact that the same is capital or revenue in nature.
- ❖ The proposed amendment overrules the following decisions :
 - Order dated 21 December, 2015 in **CIT vs. HCL Infosystems Ltd.: ITA 167/2003**, wherein compensation received on termination of joint-venture agreement was held to be capital receipt not liable to tax.
 - **Elegant Chemicals Enterprises Private Limited:[TS-808-HC-2014 (TEL&AP)]** wherein compensation upon termination of contract for specialized machinery was held to be capital receipt not taxable.
 - **CIT vs. Pritam Das Narang : 381 ITR 416 (Del)**, wherein the High Court held that amount received by the assessee from prospective employer as compensation for non-commencement of employment was not in nature of “profit in lieu of salary” but capital receipt not chargeable to tax.

Tax treatment of trading transactions in agricultural commodity derivatives

[Clause 12]

(w.e.f. 01.04.2019)

- ❖ Clause (5) of section 43 defines speculative transactions. Under clause (e) of the proviso to clause (5), trading in commodity derivatives carried out in a recognized stock exchange, which is chargeable to Commodity Transaction Tax (“CTT”) is classified as non-speculative transaction
- ❖ Presently, CTT is not levied on agricultural commodity derivatives and therefore, transactions in respect of trading in such derivatives are held to be speculative transactions

Tax treatment of trading transactions in agricultural commodity derivatives (cont.)

[Clause 12]

(w.e.f. 01.04.2019)

- ❖ With a view to encourage trading in agricultural commodity derivatives, it is proposed to insert another proviso in clause (5) of section 43 to provide that requirement of chargeability of CTT shall not apply in respect of said derivatives
- ❖ Accordingly, w.e.f. 01.04.2019, transactions in respect of trading in agricultural commodity derivatives will be treated as non-speculative transaction

Presumptive taxation in case of heavy good vehicles

[Clause 16]

(w.e.f. 01.04.2019)

- ❖ Presently, under section 44AE, in case of an assessee engaged in the business of plying, hiring or leasing of goods carriages and owning not more than 10 goods carriages, an amount equal to Rs.7,500 per month per goods carriage is deemed as income, irrespective of the capacity of the carriage.
- ❖ It is proposed to amend the aforesaid section to provide that in respect of heavy goods carriage, having more than 12MT gross vehicle weight, deemed income shall be equal to Rs.1,000 per ton of gross vehicle weight or unladen weight, as the case may be, per month.

Income Computation and Disclosure Standards (ICDS)

Amendments in relation to notified ICDS

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

- ❖ In terms of section 145 of the Act, business income and income from other sources is to be computed in accordance with cash or mercantile system of regularly followed by the assessee. Section 145(2) of the Act empowered the Central Government (“CG”) to notify the accounting standards to be followed by any class of assesseees or in respect of any class of income.
- ❖ The Central Board of Direct Taxes (“CBDT”), in exercise of the powers conferred under section 145(2) of the Act vide Notification No. 87/2016 dated 29-09-2016, which was effective from assessment year 2017-18 onwards, notified 10 ICDS for the purpose of computing income chargeable to tax under the head “Profit and gains of business or profession” or “Income from other sources” for all assesseees following mercantile system of accounting.

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

- ❖ In respect of treatment prescribed in ICDS on certain issues, there was no corresponding provision in the Act and therefore, ICDS were subject matter of challenge.
- ❖ Recently, the **Delhi High Court** in the case of **Chamber of Tax Consultants v. Union of India: 299 CTR 137**, while upholding the constitutional validity of ICDS, read down/struck down certain part(s) of ICDS which ran contrary to the provisions of the Act or binding judicial precedents holding that the CG cannot override binding judicial precedents through notification of ICDS without amending the Act.

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

- ❖ To overcome the aforesaid lacunae, the following retrospective amendments have been proposed in the Act:

Amendment in the Act	Impact of the Amendment
Re: Treatment of marked to market loss or expected loss	
• Clause (xviii) is proposed to be inserted in section 36(1) of the Act to provide that deduction or allowance in respect of marked to market loss or other expected loss shall be allowed in the manner as specified under the ICDS. • Corresponding amendment proposed in section 40A to provide that no deduction or allowance shall be allowed in respect of marked to market loss or other expected loss except to the extent permissible under section 36(1) (xviii) of the Act.	• ICDS permits recognition of MTM gain and losses in respect of “monetary items” like cash, receivables, payables, etc.

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act	Impact of the Amendment
Re: Taxation of foreign exchange fluctuation gain or loss	
• Section 43AA is proposed to be inserted to provide that subject to provisions of section 43A, any gain or loss arising due to change in foreign exchange rates in respect of specified foreign currency transactions (viz, monetary and non-monetary items, translation of financial statements of foreign operations; forward exchange contracts and foreign currency translation reserves) shall be computed in the manner provided in accordance with ICDS.	• On acquisition of depreciable asset outside India out of moneys borrowed in foreign currency, provisions of section 43A the Act continue to apply. • ICDS VI on “Effects of changes in foreign exchange rates” does not make distinction between forward exchange contracts for capital or revenue purposes. • If forward cover is taken for capital assets, foreign exchange loss will be capitalized [ACIT vs. Elecon Engg. Co. Ltd.: 230 CTR 1 (SC)].

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act	Impact of the Amendment
Re: Taxation of income from construction contracts and other service contracts	
• Section 43CB is proposed to be inserted to provide for determination of profit and gains from: ✓ construction contracts or contracts for providing services on the basis of Percentage of Completion Method (POCM) [paragraph 16 of ICDS-III]; ✓ contracts for providing services having duration of not more than 90 days on the basis of Project Completion Method (PCM) [paragraph 7 of ICDS-IV]; and ✓ contracts involving indeterminate number of acts over a specified period of time on the basis of straight line method [paragraph 6 of ICDS-IV].	• The amendment seeks to overrule the settled judicial precedents so much so that: ✓ POCM as well as PCM have been held to be valid methods of accounting under the mercantile system of accounting [Refer: CIT v. Bilhari Investment Pvt. Ltd. [2008] 168 Taxman 95 (SC)]

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act	Impact of the Amendment
Re: Taxation of income from construction contracts and other service contracts contd..	
• For the purpose of the aforesaid proposed section, it is provided that – ✓ contract revenue shall include retention money [paragraph 10 of ICDS-III]; and ✓ contract costs shall not be reduced by incidental income in the nature of interest, dividend and capital gains [paragraph 12 of ICDS-III].	✓ retention money, the receipt whereof is uncertain/conditional, is held to be not taxable on accrual basis. [Refer: CIT v. Simplex Concrete Piles India (P) Ltd (1988) 179 ITR 8, CIT v. P&C Constructions (P) Ltd (2009) 318 ITR 113, Amarshiv Construction (P) Ltd v. DCIT (2014) 367 ITR 659]. ✓ any amounts which are inextricably linked with the process of setting up of plant and machinery shall go to reduce the cost of such asset [Refer : CIT v. Bokaro Steel Limited: (1999) 236 ITR 315].

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act

Re: Method of accounting in certain cases

- Present provisions of section 145A of the Act, which provides for adoption of the method of accounting regularly employed by the assessee for valuation of inventory, is proposed to be substituted by newly proposed sections 145A and 145B to provide as under:
 - ✓ Valuation of inventory shall be made at lower of actual cost or net realisable value computed in accordance with the ICDS [paragraph 3 of ICDS-II];
 - ✓ Valuation of purchase and sale of goods, services and inventory shall be adjusted to include the amount of tax, duty, cess or fee actually paid or incurred by the assessee to bring the goods or services to the place of its location and condition as on the date of valuation [paragraph 4 of ICDS-II];

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act

Re: Method of accounting in certain cases contd..

- ✓ The inventory of securities not listed, or listed but not quoted on a recognised stock exchange with regularity from time to time, shall be valued at actual cost initially recognised in accordance with the relevant ICDS [paragraph 4 read with 12 of ICDS-VIII];
- ✓ The inventory of listed securities shall be valued at lower of actual cost or net realisable value in accordance with the relevant ICDS and comparison will have to be done category wise;

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act	Impact of the Amendment
Re: Method of accounting in certain cases contd..	
• Section 145B is proposed to be inserted to provide that: ✓ the interest received by an assessee on any compensation or on enhanced compensation shall be deemed to be the income of the previous year in which it is received. ✓ the claim for escalation of price in a contract or export incentives shall be deemed to be the income of the previous year in which reasonable certainty of its realisation is achieved.	• The proposed amendment seeks to overcome the decision of the Supreme Court in the case of CIT vs. Excel Industries Ltd.: (2013) 358 ITR 295, wherein it was held that income from export incentive can be said to have accrued and recognized as income only in the year in which the claim is accepted by the Govt. in as much as it is at that stage that a right to receive the payment accrues in favour of the assessee, and corresponding obligation to pay fastens on to the Government.

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Amendment in the Act	Impact of the Amendment
Re: Method of accounting in certain cases contd..	
✓ assistance in the form of subsidy or grant or cash incentive or duty drawback/ waiver/ reimbursement specified under section 2(24) (xviii) of the Act shall be deemed to be the income of the previous year in which it is received, if not charged to tax for any earlier previous year.	• In alignment with paragraph 4(2) of ICDS- VII in terms whereof initial recognition of grants cannot be postponed beyond the date of actual receipt even though all the recognition conditions in accordance with AS are not met. The same is in conflict with the accrual system of accounting.

Amendments in relation to notified ICDS (cont.)

[Clauses 10, 11, 13, 15 & 45]

(w.r.e.f. 01.04.2017)

Comments/ Observations:

- ❖ The proposed amendments would be applicable with retrospective effect from 01.04.2017, i.e., the effective date of application of ICDS and would accordingly, apply in relation to assessment year 2017-18 and onwards.
- ❖ The decision of the Delhi the High Court was pronounced before the due date of filing of return by certain assesseees, viz. 30th November, 2017. In those cases, if the assessee(s) had taken a position in conformity with the decision of the Delhi High Court, such assessee(s) would be required to file revised return of income.

INTERNATIONAL TAXATION

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

[Clause 4]

(w.e.f. 01.04.2019)

- ❖ Section 9(1)(i) of the Act provides that:
 - ❖ all income accruing or arising, whether directly or indirectly, through or from any business connection in India shall be deemed to accrue or arise in India.
- ❖ In other words, section 9(1)(i) of the Act provides for taxation of business income of non-residents in India if they have a business connection in India.
- ❖ Under the existing provisions of Explanation 2 to clause (i) of sub-section (1) of section 9, "business connection" includes business activities carried on by non-resident through dependent agents.

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

- ❖ The scope of "business connection" under the Act is similar to the provisions of Dependent Agent Permanent Establishment (DAPE) in Article 5(5) of the DTAAs entered into by India with other countries.
- ❖ In terms of the DAPE rules in tax treaties, if any person acting on behalf of the non-resident, is habitually authorised to conclude contracts for the non-resident, then such agent would constitute a PE in the source country.
- ❖ However, in many cases, with a view to avoid establishing a PE under Article 5(5) of the DTAA, the person acting on the behalf of the non-resident, negotiates the contract but does not conclude the contract.

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

- ❖ The OECD under BEPS Action Plan 7 reviewed the definition of 'PE' with a view to preventing avoidance of payment of tax by circumventing existing PE definition by way of commissionaire arrangements or fragmentation of business activities.
- ❖ In order to tackle such tax avoidance scheme, the BEPS Action Plan 7 recommended modifications to Article 5(5) to provide that:
 - ❖ an agent would include not only a person who habitually concludes contracts on behalf of the non-resident, but also a person who habitually plays a principal role leading to the conclusion of contracts
- ❖ Further, with a view to preventing base erosion and profit shifting, the recommendations under BEPS Action Plan 7 have now been included in Article 12 of Multilateral Convention to Implement Tax Treaty Related Measures ('MLI'), to which India is also a signatory.⁴¹

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

- ❖ Consequently, these provisions will automatically modify India’s bilateral tax treaties covered by MLI, where treaty partner has also opted for Article 12 of the MLI.
- ❖ As a result, the DAPE provisions in Article 5(5) of India’s tax treaties, as modified by MLI, shall become wider in scope than the current provisions in Explanation 2 to section 9(1)(i) of the Act.
- ❖ The Finance Bill, 2018 proposes to expand the scope of ‘business connection’ as defined under section 9(1)(i) of the Act consistent with PE Rule as modified by BEPS Action Plan 7 and MLI by introducing the concept of “agent habitually playing principal role leading to conclusion of contract”

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

- ❖ The amendment proposed by the Finance Bill under section 9 of the Act (*the amendments have been made in bold italics and deletions have been made in strikethrough*) is extracted hereunder:

“Section 9. (1) The following incomes shall be deemed to accrue or arise in India :—

(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

Explanation 1: For the purposes of this clause—

(a) in the case of a business of which all the operations are not carried out in India, the income of the business deemed under this clause to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India ;

(b) in the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export;

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

Explanation 2: For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident:

~~a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or~~

a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident or habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by that non-resident and these contracts are

i. in the name of the non resident, or

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

- ii. *for the transfer of the ownership of, or for the granting of the right to use, property owned by that non resident or that non resident has the right to use, or*
- iii. *for the provision of services by that non resident*
- b) *has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or*
- c) *habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:*

Aligning scope of “business connection” with modified PE Rule as per Multilateral Instrument (MLI).

Provided that such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business”

Comments

- ❖ Accordingly, proposed amendment to section 9 of the Act will align the provisions of Act with provisions of DTAA as modified by MLI so as to make the provisions in DTAA effective.
- ❖ Whether the following activities can fall within the meaning of “habitually plays the principal role leading to conclusion of contracts”:
 - a) Identifying business opportunities for the non-resident principal while final negotiation is done by non-resident?
 - b) Acting as a communication channel and responding to the prospective client’s queries?

Comments

- c) Participation in the negotiations along with the principal?
- d) Providing price quotations and clarifications in this regard to the prospective customers?

“Business connection” to include “Significant Economic presence”

[Clause 4]

(w.e.f. 01.04.2019)

- ❖ BEPS Action Plan 1 on “*Addressing the tax challenges of the digital economy*” recommended modifying existing definition of PE to provide that:
 - ❖ An enterprise engaged in fully de-materialized digital activities would constitute a PE if it maintained a significant digital presence in another country's economy
 - ❖ Virtual PE would be constituted when an enterprise maintains its website on a server of another enterprise located in a jurisdiction and carries on business through that website

“Business connection” to include “Significant Economic presence”

- ❖ BEPS Action Plan 1 also recommended that countries may introduce the following safeguards in their domestic laws to prevent BEPS:
 - (i) A new nexus rule based on the concept of “significant economic presence”
 - (ii) Withholding tax on certain types of digital transactions
 - (iii) An equalization levy
- ❖ The scope of existing provisions of clause (i) of sub-section (1) of section 9 is restrictive as it essentially provides for physical presence based nexus rule for taxation of business income of the non-resident in India - territorial nexus
- ❖ Emerging business models such as digitized businesses, which do not require physical presence of itself or any agent in India, is not covered within the scope of clause (i) of sub-section (1) of section 9 of the Act.

“Business connection” to include “Significant Economic presence”

- ❖ In view of the above, the Finance Bill, 2018, proposes to insert following ‘Explanation 2A to clause (i) of sub-section (1) of section 9 of the Act to further expand the scope of “business connection” to include “significant economic presence”.
- ❖ “Significant economic presence” for this purpose shall mean:
 - ❖ any transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India if
 - ❖ the aggregate of payments arising from such transaction or transactions during the previous year exceeds the amount as may be prescribed; or
 - ❖ systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.

“Business connection” to include “Significant Economic presence”

- ❖ The proposed ‘Explanation 2A to clause (i) of sub-section (1) of section 9 of the Act is extracted hereunder:

“Explanation 2A: For the removal of doubts, it is hereby clarified that the significant economic presence of a non-resident in India shall constitute “business connection” in India and “significant economic presence” for this purpose, shall mean

a) transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed; or

“Business connection” to include “Significant Economic presence”

b) systematic and continuous soliciting of business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means:

Provided that the transactions or activities shall constitute significant economic presence in India, whether or not the non-resident has a residence or place of business in India or renders services in India

Provided further that only so much of income as is attributable to the transactions or activities referred to in clause (a) or clause (b) shall be deemed to accrue or arise in India”

Comments

- ❖ The proposed amendment will encourage Indian digital enterprises and give them a level playing field and also drive their foreign peers to set up shop here.
- ❖ The proposed amendment will apply to all online advertisements, online searches, cloud services and other digital products, and ensure that profits of these firms attributable to Indian users is taxed in India.
- ❖ This could bring firms like Google, Facebook and Netflix, Amazon USA, besides app developers such as Uber Inc., with huge consumer bases in India into the tax net.

Comments

- ❖ The proposed amendment comes at the back of equalisation levy @ 6 percent imposed by Finance Act 2016, on online advertising payments to foreign entities not having a PE in India
- ❖ Accordingly, companies selling digitally goods or services in India and whether or not having a taxable presence in India may fall within the garb of this proposed amendment
- ❖ The threshold limit of “revenue” and the “users” in India will be decided after consultation with the stakeholders.

Comments

- ❖ The revenue based factor and user based factor approach proposed by the Finance Bill to determine nexus based on the concept of significant economic presence is in line with Action Plan 1.
- ❖ However, guidelines in this regard prescribing the conditions and the threshold limits are yet to be issued.
- ❖ Countries such as Israel, Italy, Kuwait, Saudi Arabia have introduced the concept of "significant economic presence".

Comments

- ❖ Further, Action Plan 7 also proposes to incorporate a new anti-fragmentation rule to:
 - ❖ prevent the use of the specific activity exemptions in paragraph 4 to artificially avoid PE status by fragmenting a cohesive operating business into several small operations in order to argue that each part is merely engaged in preparatory or auxiliary activities.
 - ❖ The said anti-fragmentation rule is also proposed to be introduced in Explanation 2A “.... significant economic presence shall exist if aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed”

Issues

Question 1:

- ❖ Whether the proposed amendment is applicable from retrospective effect?

Answer 1:

- ❖ The Finance Bill clearly specifies that the amendment is applicable from assessment year 2019-20.
- ❖ However, the proposed amendment states that “For the removal of doubts, it is hereby clarified that” which may give a handle to the Revenue to argue that the amendment is clarificatory in nature and is applicable to years preceding assessment year 2019-20 thereby bringing the foreign companies in tax net with which India does not have a DTAA (like Hong Kong)

Issues

- ❖ Since the amendment seeks to significantly expand the scope of business connection, therefore, it cannot have a retrospective operation [Reference: CIT vs. Vatika Township Pvt. Ltd.: 367 ITR 466 (SC)]

Question 2:

- ❖ Whether income earned by Amazon Inc. from goods purchased by an Indian user on the website of Amazon.com (which is incorporated in USA) would fall within the definition of significant economic presence?

Answer 2:

- ❖ Amazon.com will be considered to have significant economic presence in India since Amazon Inc, will be considered to undertake systematic and continuous soliciting of its business activities in India through digital means provided the threshold of user base factor is satisfied.

Issues

Question 3:

- ❖ Whether income earned by a foreign company from sale of software/ data reports through its website would fall within the definition of significant economic presence?

Answer 3:

- ❖ Yes, since significant economic presence in India includes any transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India provided the threshold of revenue factor is satisfied.

Issues

Question 4:

- ❖ Whether exploring business opportunities by a liaison office in India would constitute significant economic presence?

Answer 4:

- ❖ Significant economic presence includes systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.
- ❖ Accordingly, if the liaison office is exploring business opportunities through digital means (by soliciting customers through online advertising), then,
 - ❖ the foreign company may be held to have significant economic presence subject to satisfaction of user base factor.

TRANSFER PRICING

Section 286 – Rationalization of provisions relating to Country by Country Reporting (‘CbCR’)

[Clause 53]

(w.r.e.f 01.04.2017)

- ❖ India has been an active member of the Base Erosion and Profit Shifting (‘BEPS’) initiative of the Organization for Economic Cooperation and Development (‘OECD’) and is part of the consensus
- ❖ The Finance Act, 2016 inserted section 286 providing for furnishing of Country by Country Report (‘CbCR’)
- ❖ Under the existing provisions, the parent company or the alternate reporting entity of an international group resident in India is required to furnish CbCR in form 3CEAD on or before the due date for filing of the Income Tax Return, i.e., by 30th November

Section 286 – Rationalization of provisions relating to CbCR (cont.)

[Clause 53]

(w.r.e.f 01.04.2017)

- ❖ The time limit for submitting CbCR for financial year 2016-17 was extended to March 31, 2018 vide Circular no. 26/2017 by CBDT
- ❖ It has now been proposed to extend the time allowed for furnishing CbCR to twelve months from the end of the reporting accounting year i.e. by 31st March next following
- ❖ OECD BEPS Action Plan 13 recommends that the CbCR may be furnished within one year from the end of the fiscal year of the ultimate parent of the MNE group (ref. Para 31)

Section 286 – Rationalization of provisions relating to CbCR (cont.)

[Clause 53]

(w.r.e.f 01.04.2017)

- ❖ However, the US prescribes filing of CbCR by the date of filing the tax return, i.e., April 15th and China requires filing of CbCR by May 31st.
- ❖ Other countries generally prescribe filing of CbCR within one year from the end of the relevant fiscal year
- ❖ The proposed change in the due date for furnishing CbCR is in line with the recommendation of the OECD

Section 286 – Rationalization of provisions relating to CbCR (cont.)

[Clause 53]

(w.r.e.f 01.04.2017)

- ❖ Under the existing provisions, the following Indian entities having non resident parent were required to furnish CbCR:
 - The parent company is a resident of country with which India does not have an agreement for exchange of CbCR, or
 - There has been a systematic failure of the country of residence of the parent company in exchanging CbCR with India and such failure has been communicated to the Indian entity
- ❖ It is now proposed to extend the requirement of filing CbCR to Indian entities having non resident parent company in case the parent company has no obligation to file CbCR in its country of residence

Section 286 – Rationalization of provisions relating to CbCR (cont.)

[Clause 53]

(w.r.e.f 01.04.2017)

- ❖ The above requirement of filing CbCR by Indian entity having non resident parent, will not be applicable if the alternate reporting entity of the group has furnished the CbCR in accordance with the regulation of the country in which such alternate reporting entity is resident

**RATIONALIZATION OF
CERTAIN PROVISIONS FOR
COMPANIES UNDER IBC**

Rationalization of certain provisions for companies under Insolvency and Bankruptcy Code (IBC), 2016

[Clauses 22 & 43]

(w.e.f. 01.04.2018)

- ❖ Existing provisions of section 79, prohibits carry forward and set off of losses in the hands of a closely held company, if in a previous year there is change in share holding beyond 50% of voting power
- ❖ In order to facilitate restructuring and rehabilitation of a company seeking insolvency resolution under Insolvency and Bankruptcy Code, 2016 (“IBC”), it is proposed that the rigors of section 79 would not apply to a company where change in shareholding is pursuant to resolution plan approved under the IBC, after providing a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner
- ❖ Section 140 of the Act is also proposed to be amended to permit verification of return of income of companies whose application has been admitted by the adjudication authority appointed under IBC by the Insolvency Resolution Professional (“IRA”) appointed by such Adjudicating Authority

Rationalization of certain provisions for companies under Insolvency and Bankruptcy Code (IBC), 2016 (Cont.)

[Clauses 22 & 43]

(w.e.f. 01.04.2018)

- ❖ Presently, while computing book profits under section 115JB, deduction in respect of loss brought forward or unabsorbed depreciation, whichever is lower, is provided
- ❖ Accordingly, where either of loss brought forward or unabsorbed depreciation is Nil, no deduction is allowed, for computing book profits
- ❖ It is proposed to insert clause (iih) in Explanation 1 to section 115JB to provide deduction of the aggregate amount of unabsorbed depreciation and loss brought forward for computing book profit, in case of a company against whom application for corporate insolvency resolution process under the IBC has been admitted by the Adjudicating Authority

Rationalization of certain provisions for companies under Insolvency and Bankruptcy Code (IBC), 2016 (Cont.)

[Clauses 22 & 43]

(w.e.f. 01.04.2018)

- ❖ Reference can be made to the decision of the Ahmedabad Bench of the Tribunal in the case of Surat Textile Mills Ltd vs DCIT: 159 ITD 373:
 - In that case, in the book of accounts, the assessee had adjusted the debit balance of profit and loss account including unabsorbed depreciation by transferring it to rehabilitation scheme account to the extent of credit balance available therein, on recommendation of the BIFR
 - In the return of income, the assessee computed the book profit as Nil after reducing loss available as per accounts prepared as per Schedule VI of Companies Act
 - The assessing officer disallowed the adjustment of unabsorbed depreciation made by the assessee as per clause (iii) of the Explanation to section 115JB(2) of the Act while computing book profit

Rationalization of certain provisions for companies under Insolvency and Bankruptcy Code (IBC), 2016 (Cont.)

[Clauses 22 & 43]

(w.e.f. 01.04.2018)

- ❖ The Tribunal held that impact of restructuring adjustments would not extinguish unabsorbed depreciation from accounts of assessee in actual terms and therefore, its reduction should be allowed while computing book profit of the assessee.
- ❖ This decision was later confirmed by Gujarat High Court in 246 Taxman 206
- ❖ The proposed amendment however seeks to provide greater benefit by allowing reduction of aggregate amount of unabsorbed depreciation and loss brought forward from the book profit, rather than lower of the two

Rationalization of certain provisions for companies under Insolvency and Bankruptcy Code (IBC), 2016 (Cont.)

[Clauses 22 & 43]

(w.e.f. 01.04.2018)

- ❖ Key issue remains unaddressed, viz., whether write back of debt towards financial institutions in the books of the distressed company, subsequent to takeover of such company by acquirer and repayment of such debt by said acquirer shall be included while computing MAT liability?

AMENDMENTS RELATING TO ASSESSMENT PROCEDURES

New Scheme of scrutiny assessments

[Clause 44]

(w.e.f. 01.04.2018)

- ❖ In order to impart greater efficiency, transparency and accountability, it is proposed to amend the existing provisions of section 143 by inserting sub-section (3A) enabling the Central Government to prescribe new scheme for conducting scrutiny assessments.
- ❖ The aforesaid objective is proposed to be achieved by:
 - a) eliminating interface between the assessing officer and the taxpayer to the extent technologically feasible;
 - b) optimizing utilization of the resources;
 - c) introducing a team-based assessment with dynamic jurisdiction

New Scheme of scrutiny assessments (cont.)

[Clause 44]

(w.e.f. 01.04.2018)

- ❖ Sub-section (3B) provides that the Central Government for the purpose of giving effect to the new assessment scheme, may by notification in Official Gazette, direct that any of the provisions of this Act relating to assessment shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified in the notification.
- ❖ Every notification issued under sub-section (3A) and (3B) by the Central Government must be laid before the Parliament.
- ❖ No notification shall be issued after 31.03.2020.

New Scheme of scrutiny assessments (cont.)

[Clause 44]

(w.e.f. 01.04.2018)

Comments/ Observations:

- ❖ As part of e-governance initiative, earlier in 2016 and vide Notification dated 29th Sept' 2017, Government launched a pilot project to conduct scrutiny assessments electronically, which was extended to 102 cities. The said e-assessment scheme was optional
- ❖ Proposed new scheme of e-assessment is to be mandatory
- ❖ The interface/ interaction between the taxpayer and the AO may significantly reduce.

New Scheme of scrutiny assessments (cont.)

[Clause 44]

(w.e.f. 01.04.2018)

Comments/ Observations:

- ❖ Whether the assessment by the AO holding jurisdiction over the location of the assessee would be given a go by under the concept of team based dynamic jurisdiction?
- ❖ Substantial training and attitudinal change of the assessing authorities would be required particularly where no occasion of explaining the case is given to the taxpayer assessee in case of electronic assessments

Amendment under section 143(1)

[Clause 44]

(w.e.f. 01.04.2018)

- ❖ Existing clause (vi) to section 143(1) provides for adjustment by way of addition of income appearing in Form 26AS/ Form 16 or 16A which is not included in the total income.
- ❖ Proviso is proposed to be inserted to the effect that no adjustment shall be made in the aforesaid clause for returns filed for assessment years 2018-19 onwards.
- ❖ The aforesaid amendment is proposed to avoid erroneous additions to income merely on account of mismatches of returned income with amounts reflected in Form 26AS or TDS certificates.

CAPITAL GAINS

LTCG on sale of listed equity shares

[Clauses 5 , 31 &32]

(w.e.f. 01.04.2019)

- ❖ LTCG arising from transfer of a long term capital asset, being a listed equity share in a company or a unit of an equity oriented fund is exempt from tax under section 10(38)
- ❖ It is proposed to amend section 10(38) and insert a new section 112A, in order to withdraw the existing exemption and to impose tax @ 10% on LTCG arising from transfer of equity share on or after 01.04.2018 in excess of Rs.1,00,000
- ❖ To avail the aforesaid concessional rate of 10%, STT must be paid :-
 - ✓ in case of equity shares – on acquisition as well as on transfer of such shares;
 - ✓ in case of unit of an equity oriented fund – on transfer of such unit
- ❖ The Central Government may notify transactions on which the condition for payment of STT on acquisition shall not apply

LTCG on sale of listed equity shares (cont.)

[Clause 5 , 31 &32]

(w.e.f. 01.04.2019)

- ❖ For purposes of the aforesaid section, LTCG shall be computed without giving the benefit of indexation of the cost of acquisition and the benefit of computation of capital gains in foreign currency in the case of a non-resident, as contained in first and second proviso to section 48 of the Act
- ❖ LTCG arising from investments made before 01.02.2018 have been grand-fathered, in as much as, cost of acquisition thereof shall be deemed to be the higher of -
 1. the actual cost of acquisition of such asset; and
 2. the lower of -
 - (i) the fair market value of such asset; and
 - (ii) the full value of consideration received or accruing on such transfer

LTCG on sale of listed equity shares (cont.)

[Clauses 5 , 31 &32]

(w.e.f. 01.04.2019)

- ❖ FMV has been defined to be computed as per the following:
 - I. In case of a listed equity share, the highest price of such share quoted on the stock exchange as on 31.01.2018;
 - II. In case of a listed equity share, where no trading happened on stock exchange as on 31.01.2018, the highest trading price at which transaction took place on a date immediately preceding 31.01.2018;
 - III. In case of a unit in equity oriented fund, being not listed on a recognized stock exchange, the NAV of such unit as on 31.01.2018

LTCG on sale of listed equity shares (cont.)

[Clauses 5 , 31 &32]

(w.e.f. 01.04.2019)

❖ Illustration: Assuming transfer of long term capital asset on 01.05.2018

Transaction	1	2	3
Cost of acquisition	100	80	120
FMV as on 31.01.2018	120	100	80
Sale consideration	130	90	150
LTCG under section 112A	10 (130-120)	0 (90-90)*	30 (150-120)

- No loss can arise due to higher FMV.
- Amendment is proposed to be effective from AY 2019-20. Thus for transfers made upto March 2018, exemption shall be available.

LTCG on sale of listed equity shares (cont.)

[Clauses 5 , 31 &32]

(w.e.f. 01.04.2019)

Comments/ Observations:

- ❖ The beneficial rate of 10% (as against 20%) is available only if STT was paid at the time of acquisition of the equity share.
- ❖ Similar condition was imposed for availing complete exemption from LTCG tax under section 10(38). The Central Government had issued notification dated 5th June 2017 exempting certain acquisitions without payment of STT for availing exemption under section 10(38) of the Act.
- ❖ Loss on transfer of listed shares can now be claimed as set off as per Chapter VI.

Measures to promote International Financial Services Centre (IFSC)

[Clauses 17, 36 & 37]

(w.e.f. 01.04.2019)

- ❖ International Financial Services Centre (IFSC) has been set up in the country for promoting world class financial infrastructure
- ❖ It is proposed to insert clause (viiab) in section 47 to provide that transactions undertaken by a non-resident on a recognized stock exchange located in any IFSC shall not be regarded as transfer, provided the :

(1) transactions are undertaken in the following assets:

- i. Bond or Global Depository Receipt, as referred to in section 115AC(1); or
- ii. Rupee denominated bond of an Indian company; or
- iii. Derivative

and,

(2) consideration is paid or payable in foreign currency

Measures to promote International Financial Services Centre (IFSC) (cont.)

[Clauses 17, 36 & 37]

(w.e.f. 01.04.2019)

- ❖ It is further proposed to amend section 115JC to reduce levy of Alternate Minimum Tax on such units located in an IFSC from 18.5% to 9%
- ❖ Consequential amendment is also proposed to be made in section 115JF

Rationalization of the provisions of section 54EC

[Clause 20]

(w.r.e.f. 01.04.2019)

- ❖ Section 54EC provides exemption of long-term capital gains arising on transfer of any capital asset in case of investment of the capital gain in certain specified assets, subject to fulfilment of conditions specified therein.
- ❖ It is now proposed to restrict benefit of the aforesaid section to long-term capital gains arising on transfer of land and/ building only.
- ❖ It is further proposed to provide for investment on or after 1.04.2018 in bonds redeemable after 5 years as against existing period of 3 years.

DEEMED DIVIDENDS

Scope of “accumulated profits” widen for levy of Dividend

[Clause 3]

(w.r.e.f. 01.04.2018)

- ❖ Section 2(22) of the Act enumerates various situations/ circumstances wherein payment made by the company to its shareholders, though not in the form of dividend, is, to the extent of accumulated profits (whether capitalised or not), regarded as deemed dividend.
- ❖ Explanation 2 to section 2(22) defines the term “accumulated profits” to mean all profits of the company up to the date of distribution or payment or liquidation, as the case may be.

Scope of “accumulated profits” widen for levy of Dividend (cont.)

[Clause 3]

(w.r.e.f. 01.04.2018)

- ❖ It is now proposed to insert Explanation 2A in the said section to provide that in case of an amalgamated company, accumulated profits (whether capitalised or not), or losses as the case may be, shall be increased by the accumulated profits (whether capitalised or not) of the amalgamating company as on the date of amalgamation.

Comments/Observations:

- ❖ Pertinently, the amendment applies retrospectively from assessment year 2018-19 onwards.
- ❖ Proposed amendment seeks to prevent arrangements undertaken to mitigate deemed dividend provisions by offsetting losses of one company by profits of another company, thereby reducing the quantum of accumulated profits.
- ❖ The aforesaid is illustratively explained as under:

Illustration 1.

Particulars	Amounts as per balance sheet of amalgamating company	Amounts as per balance sheet of amalgamated company	Consolidated balance sheet of amalgamated company post-merger
Equity Share capital	1,000	12,000	13,000
Reserves	9,000	(10,000)	(1,000)
Liabilities	500	750	1,250
Total Liabilities	10,500	2,750	13,250
Assets (including cash)	2,500	2,050	4,550
Land and Building	7,000	-	7,000
Inventory	1,000	700	1,700
Total Assets	10,500	2,750	13,250
• Accumulated profits : Rs.8,000 [(1,000) + 9,000] - ????			

Illustration 2.

Particulars	Amounts as per balance sheet of amalgamating company	Amounts as per balance sheet of amalgamated company	Consolidated balance sheet post fair value merger
Equity Share capital	1,000	2,000	3,000
Reserves:			
(A) Profit and Loss	9,000	NIL	NIL
(B) Securities Premium	NIL	4,000	16,500
Liabilities	500	750	1,250
Total Liabilities	10,500	6,750	20,750
Assets (FV-3,000)	2,500	3,050	6,050
Land and Building (FV- 10,000)	7,000	-	10,000
Inventory	1,000	3,700	4,700
Total Assets	10,500	6,750	20,750

• Accumulated profits : Rs.9,000 (Nil + Rs.9000) - ????

Scope of “accumulated profits” widen for levy of Dividend (cont.)

[Clause 3]

(w.r.e.f. 01.04.2018)

❖ The proposed amendment nullifies the following decisions holding that surplus arising on amalgamation cannot be regarded as part of “accumulated profits”:

- CIT vs. Bharat Development (P) Ltd.: 135 ITR 456 (Del)
- Spencer & Co. Ltd. vs. ACIT: 137 ITD 141 (Chennai) (TM)
- Quintegra Solutions v. ITO: ITA No. 1263 to 1266 & 1629/2010
- ACIT vs. Gautam Sarasbhai Trust No. 23: 75 TTJ 151 (Ahd)
- ITO vs. United Estate (P) Ltd.: 51 SOT 61 (Mum)

Levy of DDT on deemed dividend u/s 2(22)(e)

[Clauses 38 & 39]

(w.r.e.f. 01.04.2018)

- ❖ Any loan or advance given by a company in which public is not substantially interested to a shareholder holding 10% or more of voting power or to a concern in which such shareholder has substantial interest, is regarded as deemed dividend u/s 2(2)(e).
- ❖ Presently, Dividend Distribution Tax under section 115-O is not applicable to amount considered as deemed dividend under clause (e) of section 2(22).
- ❖ It is proposed to bring deemed dividend under section 2(22)(e) within the scope of Dividend Distribution Tax under section 115-O.

Levy of DDT on deemed dividend u/s 2(22)(e) (cont.)

[Clauses 38 & 39]

(w.r.e.f. 01.04.2018)

Comments/ Observations:

- ❖ Pertinently, amendment applies retrospectively from assessment year 2018-19 onwards.
- ❖ Presently, there is ongoing judicial controversy whether deemed dividend under section 2(22)(e) is leviable in the hands of the shareholder or the recipient of loan and in what proportion.
- ❖ The Supreme Court in the case of **CIT vs. Madhur Housing and Development Company** in Civil Appeal No. 3961/ 2013, held that deemed dividend is taxable in the hands of the shareholder and not recipient of the loan.
- ❖ Recently, the Supreme Court in **National Travel Services vs. CIT in C.A. NO. 837 of 2018 @ S.L.P. (C) NO. 27245/ 2017**, however, referred the aforesaid issue to a larger bench.
- ❖ Proposed amendment bypasses the aforesaid controversy by imposing DDT in the hands of the payer company.

Levy of DDT on dividends to unit holder in an equity oriented fund

[Clauses 40,41 & 214]

(w.r.e.f. 01.04.2018)

- ❖ Presently, under the existing provisions of section 115R of the Act, Dividend Distribution Tax is not payable on distribution of income by equity oriented fund.
- ❖ It is proposed to substitute the existing section with a new section, which includes levy of additional tax @10% on the income distributed to any person by equity oriented fund.

EXEMPTIONS / DEDUCTION

Incentives for employment generation

[Clause 27]

(w.r.e.f. 01.04.2019)

- ❖ Presently, section 80JJAA provides that deduction @30% (in addition to normal deduction @100%) would be admissible in respect of “additional wages” paid to new employees employed for a minimum period of 240 days during the previous year.
- ❖ Vide the Finance Act, 2017, the minimum period of employment was relaxed to 150 days in case of apparel industry. It is now proposed to extend the said relaxation period of 150 days to footwear and leather industry.
- ❖ It is further proposed to provide that where the new employee(s) is employed for less than 240 (or 150) days in the year of employment, but such employee is employed for such minimum period of 240 (or 150) days in the immediately succeeding year, then, for the purpose of deduction, such employee shall be deemed to be employed in the succeeding year.

Incentives for employment generation (cont.)

[Clause 27]

(w.r.e.f. 01.04.2019)

- ❖ Presently, section 80JJAA provides that deduction @30% (in addition to normal deduction @100%) would be admissible in respect of “additional wages” paid to new employees employed for a minimum period of 240 days during the previous year.
- ❖ Vide the Finance Act, 2017, the minimum period of employment was relaxed to 150 days in case of apparel industry. It is now proposed to extend the said relaxation period of 150 days to footwear and leather industry.
- ❖ It is further proposed to provide that where the new employee(s) is employed for less than 240 (or 150) days in the year of employment, but such employee is employed for such minimum period of 240 (or 150) days in the immediately succeeding year, then, for the purpose of deduction, such employee shall be deemed to be employed in the succeeding year.

Measures to promote start-ups

[Clause 26]

(w.e.f. 01.04.2018)

- ❖ Under section 80IAC, 100% deduction is available, at the option of the assessee, for any three consecutive assessment years out of 7 years beginning from the year in which the eligible start-up, being a company or a LLP is incorporated, subject to fulfilment of, inter alia, the following conditions:
 - a) Such start up is incorporated between 1.04.2016 to 31.03.2019;
 - b) Turnover of its business does not exceed Rs.25 cr. between 1.04.2016 and 31.03.2021.

Measures to promote start-ups (cont.)

[Clause 26]

(w.e.f. 01.04.2018)

- ❖ In order to improve the effectiveness of the scheme, it is proposed to make the following changes in the taxation regime for start-ups:
 - a) The period of allowability has been extended to start ups incorporated on or after 01.04.2019 but before 01.04.2021;
 - b) The requirement of the turnover not exceeding Rs.25 crores is now proposed to be applicable to 7 previous years commencing from the date of incorporation in place of during the period between 1.04.2016 and 31.03.2021;
 - c) The definition of “eligible business” has been widened to now include business of innovation, development or improvement of products or processes or services, or a scalable business model with a high potential of employment generation or wealth creation.

Deduction in respect of income of Farm Producer Companies

[Clause 28]

(w.e.f. 01.04.2019)

- ❖ Section 80P provides 100% deduction in respect of profits of co-operative society providing assistance to its members engaged in primary agricultural activities.
- ❖ It is now proposed to extend similar benefit to Farm Producer Companies (FPC) for a period of 5 years, having total turnover upto Rs.100 crores and whose gross total income, includes any income from –
 - marketing of agricultural produce grown by its members; or
 - purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for the purpose of supplying them to its members, or
 - processing of agricultural produce of its members.

Exemption of income of foreign company from sale of leftover stock of crude oil on termination of agreement

[Clause 5]

(w.e.f. 01.04.2019)

- ❖ The existing provisions of clause (48B) of section 10 provide exemption to a foreign company in respect of income arising from sale of leftover stock of crude oil after the expiry of agreement or arrangement, subject to such conditions as may be notified by Central Government
- ❖ It is proposed to amend the aforesaid clause to extend the benefit of tax exemption in respect of income from left over stock of crude oil, even if the agreement or arrangement is terminated in accordance with the terms mentioned therein

Payment of royalty and FTS by National Technical Research Organization (NTRO) to a non-resident

[Clause 5]

(w.e.f. 01.04.2018)

- ❖ It is proposed to insert clause (6D) in section 10 to provide that income arising to a non-resident (not being a company or a foreign company), by way of royalty or fees for technical services rendered in or outside India, paid by NTRO, will be exempt from income-tax
- ❖ As a result, NTRO will not be required to deduct tax at source on such payments

Exemption to non-employee subscribers of NPS

[Clause 5]

(w.e.f. 01.04.2019)

- ❖ Under the existing provisions of clause (12A) of section 10, an employee who has contributed to National Pension System Trust (“NPS”) is entitled to exemption @ 40% of the total amount payable to him on closure of his account or on his opting out of the same.
- ❖ It is proposed to amend clause (12A) to extend the benefit of aforesaid exemption to all subscribers of NPS, whether he is an employee or not.

Exemption to specified income of class of body, authority, Board, Trust or Commission in certain cases

[Clause 5]

(w.e.f. 01.04.2018)

- ❖ The existing provisions of clause (46) of section 10 empower the Central Government (“CG”) to exempt, by notification, specified income arising to a body, authority, Board, Trust or Commission, subject to conditions mentioned therein. CG is required to notify each case separately even if they belong to same class of cases, which results in considerable delay in the approval process
- ❖ It is proposed to amend clause (46) of section 10 so as to enable the CG to also exempt, by notification, a “class” of such body, authority, Board, Trust or Commission (by whatever name called)

Exemption on transfer between parent and subsidiary

[Clause 21]

(w.r.e.f. 01.04.2018)

- ❖ Section 56(2)(x) provides for taxation of any money, movable property or immovable property without consideration or for inadequate consideration, subject to certain exemptions as specified therein.
- ❖ Presently, transfer of a capital asset between a parent company and wholly owned Indian subsidiary, which is exempt under sections 47(iv) and 47(v), is not excluded from the scope of section 56(2)(x).
- ❖ It is now proposed to amend section 56 to exclude the aforesaid transactions of transfer of money and property between a wholly owned subsidiary and its parent company.

Exemption on transfer between parent and subsidiary (cont.)

[Clause 21]

(w.r.e.f. 01.04.2018)

Comment / Observation

- ❖ Although, transfer of capital asset between a wholly owned subsidiary and the parent company was exempt from tax under section 47, in the absence of any specific exemption, there was exposure of the same being taxed as “income from other sources” in the hands of the recipient company under section 56(2)(x) at its fair market value.

Deductions allowable only on filing income tax return by due date

[Clause 23]

(w.e.f. 01.04.2018)

- ❖ Presently, section 80AC permits claim of deduction u/s 80-IA, 80-IAB, 80-IB and 80-IC on filing of income tax return on or before the due date specified under section 139(1) of the Act.
- ❖ No such burden is cast upon assessee claiming deductions under several other similar provisions under Chapter VI-A, viz., sections 80-IAC, 80-IBA, 80JAA, etc.
- ❖ It is now proposed to expand the scope of the said section to the entire class of deductions under the heading “C.—Deductions in respect of certain incomes” in Chapter VIA of the Act.

MISCELLANEOUS

TDS compliance for charitable organizations

[Clauses 5 & 6]

(w.e.f. 01.04.2019)

- ❖ It is the settled legal position that income of a charitable organization has to be computed on commercial principles for the purposes of claiming exemption of income applied towards charitable purposes under section 11 or 10(23C) of the Act [Refer: DIT vs. NASSCOM: 345 ITR 362 (Del)]
- ❖ In view of the aforesaid legal position the provisions of section 40(a)(ia) relating to disallowance of expenses for non-deduction of tax at source or cash payment exceeding Rs.10,000, etc. were not applicable for computing income of the charitable organization the purpose of claiming exemption under the aforesaid sections. [Refer: ITO vs. Kalinga Charitable Trust: 155 ITD 291 (Hyd.); ITO vs. Mother Theresa Educational Society: 158 ITD 473 (Vishak.)]

TDS compliance for charitable organizations (cont.)

[Clauses 5 & 6]

(w.e.f. 01.04.2019)

- ❖ In order to encourage a less cash economy, it is proposed to amend the existing provisions of section 10(23C) and section 11 to extend the obligation of deduction of tax at source from payment to residents contained in section 40(a)(ia) and not to make cash expenditure exceeding Rs.10,000 contained in section 40A(3)/(3A)
- ❖ Accordingly, expenses incurred without deducting tax at source or in cash for amount exceeding Rs.10,000, shall not be treated as application of income for the purposes of granting exemption to charitable organization under section 10(23C)/11 of the Act

TDS on interest received from securities under section 193

[Clause 46]

(w.e.f. 01.04.2018)

- ❖ Under the existing provisions of clause (iv) of Section 193, tax is required to be deducted @ 10% on interest payable on 8% Saving (Taxable) Bonds, 2003 if the payment or credit of interest to the resident is exceeding Rs.10,000/- during the financial year
- ❖ The said 8% Savings (Taxable) Bonds, 2003 are proposed to be discontinued and replaced by 7.75% GOI Savings (Taxable) Bonds, 2018
- ❖ The amendment proposed provides for tax deduction at source @ 10% from interest income exceeding Rs.10,000 from such bonds

Rationalization of deeming fiction for circle rate in case of immovable property

[Clause 14, 19 & 21]

(w.e.f. 01.04.2019)

- ❖ Under the existing regime, if an immovable property is transferred for consideration less than the circle rate of such property, the difference between the circle rate and the actual consideration is brought to tax in the hands of transferor under section 43CA (for stock in trade) and 50C (for capital asset), and in the hands of transferee under section 56(2)(x) of the Act
- ❖ It is proposed to amend all the aforesaid three sections to provide that the deeming fiction in the aforesaid section will not apply, if the circle rate does not exceed 105% of the actual consideration
- ❖ In other words, the variation between the circle rate and sale consideration has been permitted upto 5% of the sale consideration
- ❖ It is stated that the aforesaid relaxation has been permitted to cover variation occurring in the price of properties in the same area on account of variety of factors like shape of the plot, location, etc.

Relief from MAT for foreign companies earning presumptive income

[Clause 35]

(w.r.e.f. 01.04.2001)

❖ Retrospective clarificatory amendment is proposed in section 115JB to provide that MAT provisions shall not be and shall be deemed never to have been applicable to a foreign company if its total income comprises solely of profits and gains from business referred to in any of the following sections:

- 44B (shipping business);
- 44BB (business of exploration etc. of mineral oils);
- 44BBA (business of operation of aircrafts);
- 44BBB (business of civil construction etc. in certain turnkey power projects);

and such income has been offered to tax at the rates specified in the said section

Relief from MAT for foreign companies earning presumptive income (cont.)

[Clause 35]

(w.r.e.f. 01.04.2001)

- ❖ Under the existing Explanation 4 to section 115JB, foreign companies being residents of countries with which India has DTAA and not having permanent establishment in India are outside the purview of MAT.
- ❖ The proposed amendment also seeks to extend the benefit to the other non-resident companies paying taxes under presumptive scheme as specified above.

Mandatory for certain entities to obtain PAN

[Clause 42]

(w.e.f 01.04.2018)

- ❖ Existing provisions of section 139A (clauses (i) to (iv) of sub-section 1) mandate certain person(s) to obtain PAN based on taxable income, sales/ turnover, charitable status, etc.
- ❖ With a motive to use PAN as Unique Entity Number for entities other than individuals, it is proposed to amend section 139A(1) to mandate non-individual entities entering into any financial transaction of amount not less than Rs.2.5 lakh to obtain PAN.

Mandatory for certain entities to obtain PAN (cont.)

[Clause 42]

(w.e.f 01.04.2018)

- ❖ Further, to link financial transactions with natural persons, it is also proposed that managing director, director, partner, trustee, author, founder, karta, chief executive officer, principal officer or office bearer or any person competent to act on behalf of such entities shall also obtain their PAN.

Mandatory for certain entities to obtain PAN (cont.)

[Clause 42]

(w.e.f 01.04.2018)

Comments/ Observations:

- ❖ The amendment has been proposed to monitor financial transactions routed through non-individual entities and for better administration of tax base and to curb tax evasion
- ❖ Under the existing provisions also, there is a mandatory requirement to quote PAN in respect of various financial transactions specified in Rule 114B which includes, inter alia, purchase of vehicles, deposit of more than Rs.50,000 in banks, payment to hotels/ restaurant exceeding Rs.50,000, etc.

Rationalization of provisions relating to Commodity Transaction Tax

[Clause 215]

(w.e.f. 01.04.2018)

- ❖ Presently, clause (7) of section 116 of the Finance Act, 2013 defines “taxable commodities transactions” as transaction of sale of commodity derivatives in respect of commodities, other than agricultural commodities, traded in recognised association
- ❖ In order to align the aforesaid definition with instruments allowed for transaction in commodity derivatives, it is proposed to amend aforesaid clause (7) to bring “options in commodity futures”, hitherto excluded, within the ambit of “taxable commodities transactions”

Rationalization of provisions relating to Commodity Transaction Tax (cont.)

[Clause 215]

(w.e.f. 01.04.2018)

- ❖ Commodities transaction tax is proposed to be levied at the following rates on the value of such transactions:

S. No.	Taxable commodities transaction	Rate	Payable by
1.	Sale of a commodity derivative	0.01%	Seller
2.	Sale of an option on commodity derivative	0.05%	Seller
3.	Sale of an option on commodity derivative, where option is exercised	0.0001%	Purchaser

Rationalization of provisions relating to Commodity Transaction Tax (cont.)

[Clause 215]

(w.e.f. 01.04.2018)

- ❖ For the purpose of CTT, the value of taxable commodities transaction is proposed as follows :

S. No.	Taxable commodities transaction	Value
1.	Sale of commodity derivative	Price at which commodity derivative is traded
2.	Sale of an option on commodity derivative	Option premium
3.	Sale of an option on commodity derivative, where option is exercised	Settlement price

Rationalisation of provisions of section 115BA relating to certain domestic companies

[Clause 33]

(w.r.e.f. 01.04.2017)

- ❖ Section 115BA (introduced w.e.f 01.04.2017) provided for taxation of total income of a ‘newly set up domestic company’ engaged in the business of manufacturing or production of article or thing or research or distribution in relation thereto @ 25% at the option of the assessee
- ❖ However, certain incomes such as short term and long term capital gains covered by section 111A and 112 were subject to a scheduler tax rate which was lower or higher than the rate of 25%

Rationalisation of provisions of section 115BA relating to certain domestic companies (cont.)

[Clause 33]

(w.r.e.f. 01.04.2017)

- ❖ The proposed amendment seeks to clarify that application of the preferential rate of taxation @ 25% under section 115BA shall be restricted to income from business of manufacturing or production or research or distribution and remaining income shall continue to be taxed as per the scheduler rates.

Failure to furnish return of income

[Clauses 52]

(w.e.f. 01.04.2018)

- ❖ The existing provisions of section 276CC provide exemption from prosecution for failure to furnish return of income for any assessment year commencing on or after the 1st day of April, 1975, if the tax payable by the relevant person (including companies), on the total income determined on regular assessment as reduced by the advance tax, if any, paid and any tax deducted at source, does not exceed **three thousand rupees**
- ❖ In order to prevent abuse of the said proviso by shell companies or by companies holding Benami properties, it is proposed to amend the provisions of the said sub-clause, so as to withdraw the aforesaid exemption of Rs.3,000 from punishment to a company

Penalty - failure to furnish statement under section 285BA

[Clause 51]

(w.e.f. 01.04.2018)

- ❖ It is proposed to increase the existing penalty leviable for failure to furnish a statement of financial transactions or reportable account under sub-section (1) of section 285BA from Rs.100 per day to Rs.500 per day for each day of continuing default
- ❖ It is further proposed to increase the existing penalty leviable for failure to furnish the statements within the time specified in the notice issued under sub-section (5) of section 285BA from Rs.500 per day to Rs.1000 per day for each day of continuing default

Amendments to the structure of Authority for Advance Rulings (AAR)

[Clauses 48 & 49]

(w.e.f. 01.04.2018)

- ❖ Section 245-O of the Act provides for the constitution of AAR and constitution of its benches, for giving advance rulings under:
 - ❖ Chapter XIX-B of the Act or
 - ❖ Chapter V of the Customs Act, 1962 or
 - ❖ Chapter IIIA of the Central
 - ❖ Excise Act, 1944 or
 - ❖ Chapter VA of the Finance Act, 1994

- ❖ In view of the proposed constitution of new Customs AAR under section 28EA of the Customs Act, it is proposed to amend the provisions of section 245-O so as to provide that
 - ❖ such Authority shall cease to act as an AAR, and shall act as an Appellate Authority for the purpose of Chapter V of the Customs Act, 1962 from the date of appointment of Customs Authority for Advance Rulings under section 28EA of the Customs Act, 1962.

Amendments to the structure of AAR

[Clauses 48 & 49]

(w.e.f. 01.04.2018)

- ❖ It is further proposed that such Authority shall:
 - ❖ not admit any appeal against any ruling or order passed earlier by it in the capacity of AAR after the date of appointment of Customs AAR under section 28EA of the Customs Act, 1962.

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