



KPMG IN INDIA

Direct Tax Code 2009 - Highlights

TAX

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General Provisions



- The Direct Tax Code ('DTC') 2009 is to come into force on 1 April, 2011, if enacted
- The concept of previous year has been replaced with a new concept of financial year which inter alia means a period of 12 months commencing from the 1st day of April
- Every person is liable to pay income-tax in respect of his total income for the financial year at the rates / conditions specified in the Schedules to the DTC after allowing credit for pre-paid taxes (including foreign tax credits)
- Income has been proposed to be classified into two broad groups: Income from Ordinary Sources and income from Special Sources
- Income from Ordinary Sources refers to:
 - Income from employment
 - Income from house property
 - Income from business
 - Capital Gains
 - Income from Residuary Sources
- Income from Special Sources to include specified income of non-residents, winning from lotteries, horse races, etc.
- Losses arising from Ordinary sources to be eligible for set off or carry forward and set-off against income only from ordinary sources without any time limit. Similar treatment for set off and carry forward of losses from Special sources.

Corporate Tax



Tax Rates		
Category	Existing Rate	As per DTC
Income-tax	30 percent	25 percent
Minimum Alternative Tax	Levied at 15 percent of the adjusted book profits in the case of those companies where income-tax payable on the taxable income according to the normal provisions of the Act is lesser than the same.	Tax on gross assets introduced as under: - 0.25 percent of gross assets for Banking companies - 2 percent of gross assets for other companies
Dividend Distribution Tax	15 percent	15 percent

- A company is considered to be a resident in India if it is an Indian Company or if its place of control and management at any time during the year is situated wholly or partly in India
- In the case of a Company, its liability to pay income-tax is to be the higher of the two:
 - The amount of income-tax liability on its Total Income is calculated at the specified rates
 - The amount of income-tax liability calculated at the prescribed rates on gross assets (refer to the table above)
- Income of distinct and separate businesses i.e. where there is no interlacing, inter-dependence and unity of businesses as stipulated, is to be computed separately
- The ambit of business income has been widened to cover:
 - Profit on sale of business capital assets (fixed assets), undertaking under a slump sale and consideration with respect to a transfer of any self-generated business asset
 - The reduction, remission or cessation of any liability by way of loan, deposit, advance or trade credit
 - Amount accrued or received either as advance or security deposit or otherwise from the lease of assets for not less than 12 years, or agreements which provide for extension(s) of the lease terms for not less than 12 years

Corporate Tax

- The Tax Deprecation regime stipulates (key changes in depreciation rates are given in the annexure):
 - Depreciation to lessee in case of a finance lease and payments for lease rents to be treated as payments towards principal and interest
 - Many new Block of Assets / categories introduced such as Rails, Scientific Research Assets, Family Planning Assets, Deferred Revenue Expenditure for e.g. Non-compete, Voluntary Retirement Scheme and other items such as Preliminary Expenses, etc.
 - Allowance of depreciation even where all the assets in the block of asset are demolished, destroyed, discarded or transferred
- Any expenditure on which withholding tax is paid after two years after the end of the financial year in which the tax was deductible at source, is not to be allowed as a deduction
- Specific provisions continue for change in shareholding of unlisted public companies / private companies impacting carry forward and set-off of losses.



International Tax



Tax Rates

Category	Existing Rate	As per DTC
Foreign Company	40 percent	- 25 percent - For branches of foreign companies in India, an additional branch profits tax of 15 percent (on after tax total income) is also payable resulting in Effective Tax Rate of 36.25 percent

- A foreign company is considered to be a resident in India if its place of control and management at any time during the year is situated wholly or partly in India
- Income from the transfer, directly or indirectly of a capital asset situated in India shall be deemed to accrue in India
- Income would be deemed to accrue in India even if the payment is made outside India or services are rendered outside India and in other stipulated cases
- The ambit of Fees for technical services (FTS) has been widened to include development and transfer of design, drawing, plan and software or similar services
- The ambit of Royalty has been widened to include the consideration for use / right to use of transmission by satellite, cable, optic fibre, ship or aircraft and live coverage of any event.
- The net basis of taxation in respect of royalty income / FTS earned by non-residents seems to be done away with.
- Detailed anti-abuse provisions introduced under the head 'General Anti Avoidance Rule' (GAAR) in order to curb the increasing use of sophisticated tax avoidance mechanisms and mis-utilisation of tax avoidance agreements. The trigger points for GAAR, inter-alia, include lack of commercial substance, misuse or abuse of beneficial provisions, lack of bonafide business intent while entering into arrangement.
- The manner to arrive at the trigger points have been elaborated with distinct illustrations and citing various incidents. Definitions of key terms and concepts also provided to help in analysis/interpretation/application of GAAR. Finally, the GAAR is to override treaty provisions on the pretext of corrective action against tax evasions

International Tax

- The provisions of the DTAA and the DTC have been brought on par and the provisions which are enacted at a later point in time to prevail
- Furnishing of Tax Residency Certificate in prescribed form made mandatory for claiming relief under the applicable DTAA
- The Central Government is to prescribe methods for computing the foreign tax credit, the manner of claiming credit and such other particulars as are necessary for the relief or avoidance of double taxation
- Tax due from non-residents could be recovered from any of his assets even if situated outside India or from any amount payable by any person to the non-resident.
- For non-residents, head office expenditure shall be restricted to one-half percent of the total sales, turnover or gross receipts
- Scope of income from shipping business carried on by non-resident shipping companies has been extended to include income from the arrangement of slot charter, space charter or joint charter. Further, the income of the foreign shipping companies to be taxed at the normal rate.



Tax Incentives



- The profit-linked tax incentives and other tax incentives not covered in the DTC are to be grandfathered.
- The DTC substitutes profit-linked incentives with a new scheme wherein any capital expenditure incurred for specified businesses will be allowed as a deductible expenditure and the loss shall be allowed to be carried forward till it is absorbed completely.
- The new scheme will apply to the following businesses:
 - Generation, transmission or distribution of power
 - Developing or operating and maintaining any infrastructure facility
 - Operating and maintaining a hospital in specified area
 - Processing, preservation and packaging of fruits and vegetables
 - Laying and operating of a cross country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of the network
 - Setting up and operating a cold chain facility
 - Setting up and operating a warehousing facility for the storage of agricultural produce
 - Exploration and production of mineral or natural gas
 - Developing a Special Economic Zone.

Capital Gains



- Definition of capital assets have been modified and replaced with the term investment asset. Investment asset does not include business assets like self generated assets, right to manufacture and other capital asset connected with the business
- All gains from sale of investment asset would be considered as capital gains without any distinction as to short term and long term and is to be taxable. Further, the indexation facility would be available to all investment assets held for more than one year
- The indexation base date is proposed to be changed from 1 April, 1981 to 1 April, 2000
- In respect of exemption on transfer of investment assets from holding company to Wholly Owned Subsidiary (WOS) and vice versa, the present lock in period of 8 years has been proposed to be replaced by providing that the 100 percent holding – subsidiary relationship should not cease at any point of time and the transferee should not convert the capital asset into stock in trade
- If the cost of acquisition/ cost of improvement of an asset is not determinable by the tax payer, for example in the case of self-generated assets, then such cost shall be taken as nil and capital gains to be computed.

Transfer Pricing Provisions



- Advance Pricing Agreement (APA) mechanism has been introduced. The CBDT granted authority for entering into an agreement in respect of the arm's length price with the tax payer for international transactions. The said agreement will be valid for a period upto five consecutive financial years unless there is a change in law or facts. The agreement will be binding on both - the tax payer and tax authorities
- Coverage of transfer pricing regulations has been expanded by making the definition of term "associated enterprises" more stringent and lowering the threshold limits. For example, share holding with 10 percent (earlier 26 percent) voting power; loan amounting 26 percent (earlier 51 percent) of total assets; nomination of one-third (earlier one-half) directors; purchase of two-third (earlier 90 percent) raw material and consumables; would constitute the entities as associated enterprises and hence be subject to transfer pricing regulations
- Report of International Transactions certified by a Chartered Accountant to be lodged directly with the Transfer Pricing Officer instead of the Assessing Officer. The Transfer Pricing Officer shall select cases for a detailed scrutiny audit based on risk management strategy framed by the Board, however such strategy or criteria will not be made public
- Transfer Pricing Officer shall have the power to make an adjustment to the arm's length price after due verification, however will not be subject to the specific conditions which were earlier applicable in case of adjustments made by a Transfer Pricing Officer or Assessing Officer.

Mergers & Acquisitions



- Definition of amalgamation to include amalgamation of a firm, AOP, BOI into a company and other specified form of re-organisation
- The consideration for demerger to be in the form of 'equity' shares issued by the resulting company to shareholders of demerged company
- Profit on sale of an undertaking under 'slump sale' will not be treated as capital gains. Such profits shall form part of income from business income. Deduction is to be given to the extent of net worth of the undertaking sold
- DTC defines 'business reorganization'; 'amalgamation' (Reference to the Companies Act, 1956 incorporated); 'demerger', 'successor'; 'predecessor'.
- Successor can claim benefits of business losses of the predecessor, irrespective of the nature of business carried out by successor/ predecessor
- Even successors in case of a business re-organisation would be eligible for deduction of the losses of the immediately preceding fiscal year
- The present provision of providing exemption in respect of transfer of shares through the process of amalgamation/ demerger of a foreign company with another foreign company is proposed to be extended to all assets (i.e. investment assets).

Personal Taxation



Moderation of Tax Rates and increase in tax slabs

- New beneficial tax slabs are proposed to be introduced which will reduce the tax burden for individuals
- Peak rate of 30 percent applicable on income exceeding INR 25 lakhs.

Definition of Residency and Scope of income

- Definition of residence proposed to be changed. A separate category of “Not Ordinarily Resident” and additional condition of 729 days to ascertain residency, are proposed to be abolished
- Only two categories of taxpayers proposed viz. ‘Residents’ and ‘Non residents’
- Residents are proposed to be taxed only on India-sourced income for initial two years, if they qualify as a non resident in the preceding nine financial years.

Income from employment

- Employment income proposed to be computed as the gross salary less the aggregate of the specified deductions
- Popular exemptions such as house rent allowance, leave travel concession, leave encashment, tax on non monetary perquisite are to borne by the employer, medical reimbursements etc. are proposed to be deleted
- Payment in relation to Voluntary Retirement Scheme/ Gratuity/ Commuted Pension deductible from employment income if invested with permitted savings intermediaries.

Withholding tax on employment income

- Withholding tax on salaries is now proposed to be a part of the overall consolidated withholding tax provisions on all payments
- Tax to be withheld on payment/ credit.

Personal Taxation

Income from house property

- Gross Rent proposed to be calculated as higher of contractual rent or a presumptive rate of six percent of rateable value/ construction / acquisition cost
- Deduction towards interest on housing loan on self occupied property not available
- Deduction for repairs and maintenance reduced to 20 percent of the Gross Rent
- Service tax deductible on payment basis

Exempt-Exempt-Tax (EET) regime for savings scheme

- All long-term retiral savings schemes are proposed to be moved to the EET regime
- Contributions (both by employee and employer) of upto INR 3 lakhs to any account with permitted savings intermediaries is proposed to be deductible
- Accretion of income till withdrawal is exempt
- Any withdrawal made under any circumstances is taxable. Withdrawals pertaining to approved employee provident fund accumulated balance as on 31 March 2011 and accretions thereon not taxable
- Savings from one eligible savings scheme to another, is not to be treated as a withdrawal
- Permitted savings intermediaries to include approved provident and superannuation funds, life insurer and New Pension System Trust.

Other Deductions

- Aggregate deductions for above referred long term eligible savings along with tuition fees paid proposed to be increased from INR 1 lakh to INR 3 lakhs
- No further investments eligible.

Wealth Tax



- Individuals, HUF and Private Discretionary Trusts are liable to wealth tax
- Wealth to be taxable at 0.25 percent of net wealth
- Basic exemption limit has been enhanced to INR 500 million
- New concept of wealth includes all assets. Key exclusions from net wealth are :
 - assets located outside India of foreign citizens / non-residents individuals / HUF and
 - any one house or part of a house or a plot of land belonging to an individual or a HUF which is acquired or constructed before 1 April, 2000.

Compliance and Procedural Provisions

- National Tax Tribunal once established will exercise the powers of the High Court with certain exceptions
- Appeal does not lie before the Income-tax Appellate Tribunal against the order passed by the CIT directing the revision of the assessment order
- The Commissioner of Income-tax (Appeals) and the Income-tax Appellate Tribunal cannot condone the delay in filing of appeal if the delay is for more than a year.

Taxes Deduction at source



Residential status of deductee	Particulars of expenditure	Existing rates	Rates proposed by DTC
Resident	Payment for non - compete fees	10 percent	10 percent
	Amount received as remuneration or prize for rendering any services	Nil ¹	10 percent
	Rent for use of plant or machinery or equipment	2 percent	1 percent
	Payment to a Individual/ HUF contractor for works contract	2 percent	1 percent
	Any other income	Nil	10 percent
Non Resident	Royalty and Fee for technical services	10 percent	20 percent
	Capital gains	- 40 percent, in case of short term capital gains - 20 percent, in case of long term capital gains	30 percent
	Any other income (i.e. other than income on which specified rate is prescribed)	40 percent	35

¹ Existing rate for professional or technical services is 10 percent

Taxes Deduction at source

- Provisions relating to tax withholding from various payments as well as rates of tax withholding from payments to residents and non-residents have been included in separate schedules instead of independent sections. Further, the scope of tax withholding from various payments to residents has been expanded to include non-compete fees and any other income
- Disallowance of expenditure for non withholding of tax or non payment of tax has been extended to all payments. If the tax has been deducted from any payments during the last quarter of the financial year (as against last month of the financial year as existed hitherto) and such tax is paid before the due date of the filing of return of income, such payments shall be allowable for computing business income. No deduction would be granted in respect of the expenditure where the tax thereon has not been paid within the two years immediately succeeding the financial year
- The scope of withholding tax at source for resident deductee has been widened by covering all categories of income in case of residents unless specifically exempted², and uniformity has been achieved by covering all persons as the deductor unless specifically exempted. (viz. Individuals and HUF not subject to tax audit.)
- The Central Government will prescribe the framework and rules in relation to tax withholding provisions, viz.,
 - obtaining nil withholding tax certificate
 - granting nil withholding tax certificate
 - filing return for taxes deducted at source
 - reporting of payments with respect to interest payable to residents without withholding taxes
 - provide credit of taxes withheld at source
- The DTC does not provide for obtaining a lower tax withholding certificate from the Assessing Officer.
- The benefit of self-declaration by a person for non withholding of tax at source from certain payments viz. interest income, income on units of mutual funds, income from NSS deposit, etc. is not available.

² Section 200 of the Proposed DTC

Taxes Deduction at source

Return of Income and Assessment

- The due date for filing the return of income for non-corporate taxpayers is to be 30 June of the year following the financial year and for other assesses is to be 31 August
- Belated / Revised return can be filed within 21 months from the end of the financial year as stipulated
- Notices are to be issued to taxpayer (referred to in DTC as stop-filer) who has filed his return or who has been assessed in the preceding financial year, but has not filed his return for the relevant financial year
- An electronic acknowledgement to be issued on receipt of each return of tax bases and initial processing to be completed within 12 months from the month in which the return is filed
- Selection of cases for scrutiny will be made within four months from the end of the year in which the return is furnished in accordance with a risk management strategy framed by Central Board of Direct Taxes, which will not be revealed to any member of the public
- The time limit for rectification of mistake in the order / intimation is to be two years from the end of the year in which the order / intimation is passed
- Assessment to be generally completed within 21 months from the end of the financial year in which the return is furnished
- Assessment of taxes after search and seizure operations to be treated as tax base escaped assessment and would be subject to re-opening.

Penalty & Prosecution

- Maximum amount of penalty that can be levied is reduced to 2 times from the existing 3 times of the tax sought to be evaded
- In the case of individuals and cooperative societies, penalty will be calculated at the maximum marginal rate of tax

Taxes Deduction at source

- In certain cases, authority to pass penalty order is also given to CIT and CIT (Appeals)
- Penalty of amount upto INR 200,000 proposed for non-maintenance / non-furnishing of certain documents / information including those relating to international transactions and Accountant's Reports
- Commissioner's power to reduce or waive penalty and grant immunity from penalty and prosecution has been removed
- Every offence under the DTC is now punishable with the both imprisonment and fines apart from monetary penalties
- The threshold limits for compulsory maintenance of accounts has been changed. Persons, carrying on business, are required to compulsory maintain accounts, if:
 - his income from business exceeds INR 200,000 or
 - his turnover or gross receipts exceeds INR 10,00,000 in any one of the preceding three financial years
 - where the business is newly set up in the financial year, his income from business is likely to exceed INR 200,000 or his turnover or gross receipts exceeds INR 10,00,000 during such a financial year.

Trusts / Related Provisions

- All financial intermediaries such as mutual fund, venture capital fund and venture capital companies, etc. granted pass through status and investors therein to be taxed on income earned from such entities
- Private discretionary trust having shares of beneficiaries indeterminate and which are not non-profit organizations and not registered under stipulated statutes made liable to wealth tax in respect of assets owned.

Other Residuary Provisions



- Securities Transaction Tax is proposed to be abolished
- The provision of granting of waiver of interest in specified circumstances is reinstated and the CBDT has been granted powers to prescribe the circumstances, the manner and other matters in relation to waiver of the interest. The said powers also encompass the waiver of interest receivable by the tax payer from the tax department. The aggregate of amount to be waived cannot exceed 50 percent of the total interest liability
- It appears that the DTC does not contain any provisions with respect to the Settlement Commission
- Uniform tax rates have been prescribed for collection of tax at source for various transactions
- Formula for computing the income for the purpose of tonnage tax has been prescribed as:

The profits of the business of operating a qualifying ship for a financial year shall be determined in accordance with the formula i.e. $A + B - C$

Where

- A = the total tonnage income of the financial year
- B = the aggregate of the amounts calculated as daily tonnage income multiplying the number of days of the ships operations
- C = the amount of negative profit computed in respect of the business of operating a qualifying ship, for any financial year immediately preceding the relevant financial year

- A concept of deemed service of notice, summon, requisition or any other communication is proposed. Such communication can be served by post or an approved courier or e-mail, facsimile, etc. Where such communication is sent in an approved manner, it shall be deemed to have been served
- The DTC lays down the functioning of the CBDT - its constitution, management, delegation, functions, grants, accounts and audit in one Act instead of a separate Act

Other Residuary Provisions

- CBDT has been specifically restrained from issuing any order or instruction or direction or circular so as to :
 - Extend the date specified under DTC for completion of any proceedings or issuing any notice or taking any action by any income-tax authority
 - Relax any requirement or condition contained in any of the provisions of the DTC in relation to the grant of any deduction or any other relief under DTC
 - Admit any application or claim for any exemption, deduction, refund or any other relief under this DTC after the expiry of the period specified by or under the DTC for making the application or claim
 - Exempt any income, partly or fully, liable to tax under the DTC, unless otherwise provided
- All internal orders, instructions, directions and circulars issued by CBDT will be published in a tax bulletin or on the intranet of the Department
- In case of change in officer or jurisdiction, the succeeding officer has to continue any proceedings from where the earlier officer has concluded the proceedings. This is likely to reduce the hardships to the taxpayers in case of change in officers
- No interest on cash seized during search and seizure operations
- More clarity in power to share and disclose taxpayer's information especially in light of the Right to Information Act
- The Managing Director or any Manager shall be jointly and severally liable for the tax dues from any company if the amount cannot be recovered from the company unless he proves that non-recovery cannot be attributed to any neglect, misfeasance or breach of duty on his part.

Annexure

Key Changes in Depreciation Rates

Sr No	Class of Assets	Block of assets	Depreciation allowance as a percentage of WDV	
			Existing	Proposed
1	Building	Buildings used as, or for hotels or boarding houses, railway station, airport, sea port or bus terminal	10	15
		Buildings acquired on or after the 1st day of September, 2002 for installing machinery and plant forming part of water supply project or water treatment system and which is put to use for the purpose of business of providing infrastructure facilities under clause (i) of Section 80-IA(4)	100	10
2	Vehicles	Commercial vehicles for the purpose of business or profession - depending on the date of acquisition and put to use	40 / 50/ 60	15
3	Machinery and Plant	- Returnable packages used in field operations (above ground) distribution by petroleum or natural gas concerns - Plant used in field operations (below ground) by petroleum or natural gas concerns	15	60
		Machinery and plant, acquired and installed on or after the 1st day of September, 2002 in a water supply project or a water treatment system and which is put to use for the purpose of business of providing infrastructure facility under clause (i) of Section 80-IA(4)	100	15
4	Scientific research assets	All assets, other than land, used for scientific research	-	100
5	Intangible assets	Prescribed preliminary expenses incurred before the commencement of business or in connection with extension of business or in connection with the setting up of new business	-	25
		Asset or project constructed, erected or set up by the assessee if, benefit or advantage arises to the assessee over a fixed period not exceeding ten years; and asset is not owned by the assessee	-	20
		Asset or project constructed, erected or set up by the assessee if, benefit or advantage arises to the assessee over a fixed period exceeding ten years; and asset is not owned by the assessee	-	15
6	Deferred revenue expenditure	- Non-compete fee - Premium for obtaining any asset on lease or rent - Voluntary retirement payment made in accordance with any scheme of voluntary retirement - Expenditure incurred by an Indian company wholly and exclusively for the purposes of business reorganisation - Expenditure incurred by a person resident in India wholly and exclusively on any operations relating to prospecting for any mineral or the development of a mine or other natural deposit of any mineral, to the extent prescribed	-	25
				25
				25
				15

Note: The above information / detail is as per the draft Direct Tax Code 2009 as released by the Finance Minister on 12 August 2009 for public comments (www.finmin.nic.in)

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