HIGHLIGHTS OF INDIA’S UNION BUDGET
2017-18

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Foreword

1 February 2017

The Finance Minister had to tread a very fine line in finalising the tax proposals for this year's Budget. On the one hand, there was an expectation that the demonetisation exercise warranted granting of a fiscal largesse to taxpayers, both individuals and corporates, through lower rates and increased deductions. On the flip-side, there was a view that as the fiscal benefits of demonetisation were yet to crystalise, talk of a bonanza for taxpayers was premature.

This tightrope walking is evident as one goes through the fine print of the Budget proposals. The changes are largely not radical. Nonetheless, what is apparent in the proposals is a resolve on the part of the Government to reduce the parallel or cash economy to a bare minimum and increase India's global standing on ease of doing business.

The proposal to reduce acceptance of cash donations by political parties is a most heartening one. The Government was criticised on its move to demonetise high denomination notes, which was seen as adversely affecting the middle class and the poor without bringing about any corresponding accountability at a political level. The Budget seeks to address this concern by limiting cash donations and proposing a radical concept of electoral bearer bonds, which can be purchased by taxpayers and transferred to political parties. This should see significant transparency in the accountability of political parties.

It would also be pertinent to mention that there have been some misses in the Budget proposals basis India Inc's expectations. For one, the headline corporate tax rate remains unchanged (except in the case of micro, small and medium enterprises). This has surprised many, considering the Finance Minister's 2015 roadmap for reduction of corporate tax rates from 30% to 25%. Whether this will translate to a sizeable cut in corporate tax rates next year or not remains to be seen.

The Income-tax Simplification Committee (the Justice Easwar Committee) presented its report to the Finance Minister late last year. With no significant simplification measures on the income-tax side in the current budget proposals, one is left guessing as to how many of the recommendations of the Committee find favour with the Government.

As was widely expected, the General Anti Avoidance Rule (GAAR) has not been deferred. This important measure will come into force on 1 April 2017. Similarly, the Place of Effective Management (POEM) test for corporate residency, as well as the provisions of the Income Comptutation and Disclosure Standards (ICDS) remain in place, despite calls for deferral or even an outright repeal.

Nonetheless, it is indeed a positive Budget on many fronts. The proposed abolition of the Foreign Investment Promotion Board (FIPB) paves the way for easier foreign investment into the country. The focus on affordable housing is commendable. The listing of security receipts issued by Asset Reconstruction Companies is a welcome move. Clarifications on the non-applicability of the indirect transfer provisions to FPIs will give the markets something to cheer about. However, the provisions that limit the availability of the long-term capital gains exemption to listed shares which are acquired without the payment of STT are a dampener.

On the indirect tax front, the Finance Minister did not make any significant changes, in view of the impending introduction of GST.

Overall, a good and balanced budget, shorn of big bang announcements, but one that keeps India firmly on track towards addressing its long term economic aspirations.

Dinesh Kanabar

CEO

Direct Tax Proposals

[slated to be effective from 1 April 2018 (i.e. Assessment Year (AY) 2018-19), unless indicated otherwise]

Tax rates

Individuals

- For Individuals, Hindu Undivided Families (HUFs) and Association of Persons (AOP), the tax rate is reduced from 10% to 5% in respect of income between INR 250,000 and INR 500,000.
- For senior citizens (60 years to 80 years) tax rate reduced from 10% to 5% in respect of incomes between INR 300,000 and INR 500,000.
- Surcharge of 10% of tax introduced for incomes between INR 5 million to INR 10 million in case of Individuals, HUFs and AOP.

Companies

- Corporate tax rate reduced to 25% for companies with a turnover of less than INR 500 million in FY 2015-16. No other change in corporate tax rates.
- No change in Minimum Alternate Tax (MAT) rate.

Deductions and rebates for individuals

- The limit of deduction by way of contribution to the National Pension Scheme (NPS) for individuals (other than salaried individuals) increased to 20% of gross total income from the existing limit of 10%.
- Exemption provided in respect of partial withdrawal from NPS upto 25% of the contribution made.
- Taxpayers having gross total income of less than INR 1.2 million were entitiled to a deduction of upto INR 25,000 for three consecutive assessment years for investments in an equity savings scheme subject to fulfilment of certain conditions. This deduction has been discontinued going forward and will be phased out from Financial Year (FY) 2019-20.
- Tax rebate available to eligible resident individuals reduced from INR 5,000 to INR 2,500 in respect of incomes below INR 350,000.
- Interest income received by individuals from Non-Resident External (NRE) Accounts is exempt. The definition of ‘a person resident outside India’ for the purposes of this exemption is now aligned with the Foreign Exchange Management Act, 1999.

Taxation of House Property

- Annual Letting Value of building or land appurtenent thereto held as stock in trade (and not let out) will be taxed after a period of one year from the end of the financial year in which the completion certificate for the same is received.
- Set-off of loss under the head ‘Income from House Property’ against income from other heads is restricted to INR 200,000.

Taxation of Business income

- Tax deduction in respect of profit of units operating in a Special Economic Zone (SEZ) to be restricted to the total income of the taxpayer.

Disincentivising cash payments

- Any expenditure incurred in cash exceeding INR 10,000 for the acquisition of any asset to be ignored for the purposes of determination of actual cost of such asset.
- Any payment in cash above INR 10,000 to a person in a day to be denied deduction.
- Rate of 'presumptive income' reduced from 8% to 6% in respect of receipts through banking channels.
- Cash donations above INR 2,000 will not be allowed as deduction under section 80G.
- Cash transactions of INR 300,000 or more are prohibited. Person receiving cash of INR 300,000 or more is subject to penalty of an equal amount.

Banking sector

- Tax deduction in respect of provision for bad and doubtful debts increased from 7.5% to 8.5% for banks.
- Interest on loan from a co-operative bank to be allowed as a deduction only on payment basis. The payment should be made on or before the due date of furnishing the return of income.

Deductions and Exemptions

- Where a deduction claimed under section 35AD in respect of certain capital spends is subsequently withdrawn, depreciation will be allowable on the the actual cost of the capital asset as reduced by the notional depreciation calculated from the date of its acquisition.
- Currently, eligible start-ups have an option to claim 100% tax holiday for any three consecutive years out of five assessment years since incorporation. This time limit of five years has been increased to seven years.
- To promote development of the affordable housing sector, following relaxations are proposed:
  - While computing the size of residential unit "carpet area" to be considered instead of "built-up area"
  - The restriction of 30 square meters on the size of residential units to apply only to projects located within the municipal limits of Chennai, Delhi, Kolkata or Mumbai.
  - The time limit for completing the project increased from existing three years to five years.

Carry forward and set-off of loss in case of eligible start-ups

- Accumulated losses of closely held companies lapse in case of a change in shareholding beyond 51%. This provision has been relaxed in the case of start-ups. This is subject to the condition that the original shareholders continue to hold their shares from the year in which loss is incurred, to the year in which the loss is proposed to be set-off. Thus, any change in shareholding of start-ups due to capital infusions by new investors will not affect accumulated losses.
- This relaxation applies only to losses incurred during the period of seven years from the date of incorporation.

Maintenance of books of accounts and tax audits

- Individuals and HUFs carrying on business or profession no longer required to maintain books of account if their income is below INR 250,000 and sales / turnover / gross receipts is below INR 2.5 million.
- Any person opting for the presumptive taxation scheme for specified businesses is not required to get his books of accounts audited if his total sales, turnover or gross receipts in business for the previous year does not exceed INR 20 million.

Minimum Alternate Tax (MAT)

- Book profits for MAT to be computed in line with Indian Accounting Standards (Ind AS) with effect from AY 2017-18 for companies to which Ind AS applies.
- Starting point for computation of book profit to be Net profit before Other Comprehensive Income (OCI).
- Items in OCI not be reclassified to P&L for items such as Revaluation of Property, Plant, Equipment, Intangible assets, Financial Instruments etc. to be included in book profits at the time of disposal / retirement / transferred.
- On first time adoption, 'transition amount' to be included in book profit over a period of 5 years.
- In case of demerger, impact of fair value accounting under Ind AS to be ignored.
- MAT / AMT credit allowed to be carried forward for 15 years (from the existing 10 years)
- FTC in excess of MAT to be ignored for MAT / AMT carry forward purposes

Foreign Portfolio Investors (FPIs)

- The provisions of indirect transfer will not be applicable to Category-I or Category-II FPIs (with retrospective effect from AY 2012-13).
- The Finance Minister in his budget speech mentioned that a clarification will be issued that the indirect transfer provisions will not apply in case of redemption of shares or interest arising out of redemption or sale of underlying investments in India which are chargeable to tax in India.
- Concessional withholding tax rate of 5% on interest payment in case of rupee denominated bonds issued to FPIs will now be available for interest payable upto 1 July 2020.

International Taxation

- In respect of double tax avoidance agreements entered into with countries or specified association in certain territories, if any term is not defined under the agreement, it shall be assigned the meaning as definition in the Act or any explanation issued by the Central Government.

Transfer pricing

- Transactions between two domestic related parties outside the scope of Specified Domestic Transaction provisions, except where one of the parties is claiming a profit-linked deduction.

- In order to align the transfer pricing provisions in line with OECD transfer pricing guidelines and international best practices, the assessee shall be required to carry out secondary adjustments where a primary adjustment to the transfer price has been made in certain circumstances.
- Where primary adjustment exceeds INR 10 million and funds have not been brought into India, such amount will be treated as an advance made and interest will be imputed thereon in the prescribed manner.
- Thin capitalization rules are proposed to be introduced in respect of interest (and other similar) payments exceeding INR 10 million paid to associated enterprises (not applicable to banking and insurance companies). Key aspects are as under:
    - Deduction of such interest is restricted to actual interest paid / payable or 30% of EBITDA, whichever is lower; and
    - Excess interest paid will be allowed to be carried forward for 8 years.

Capital Gains

Preventing abuse of the long-term capital gains exemption regime

- Exemption for long term capital gains on sale of listed shares will not be available for shares acquired on or after 1 October 2004 without payment of Securities Transaction Tax (STT). However, to protect the exemption in genuine cases where STT could not have been paid, such as acquisition of shares in an IPO, FPO, bonus, rights issue, preferential allotment to foreign investors, etc., appropriate exceptions will be notified.

Joint Development Agreement (JDAs)

- A relaxation has been provided from capital gains on deemed transfer of immovable property in JDAs in the hands of individuals and HUFs. The incidence of capital gains in such cases is deferred to the year in which the certificate of completion is issued for the whole or part of the project. It is also provided that the cash consideration (if any) received along with stamp duty value of the share in the project (land / building) as on the date of completion shall be the full value of consideration for computing the gains.
- However, in case the share in the project is transferred before completion, capital gains taxation will apply on such sale.

Transfer of unquoted equity shares

- In case of transfer of unquoted equity shares, gains will be calculated based on Fair Market Value (FMV) if the consideration received is lower than the FMV. The manner of determining FMV will be prescribed.

Tax incentive for development of the new capital city of Andhra Pradesh

- Andhra Pradesh government has come up with a land pooling scheme for the development of a new capital in Amaravati. The landowners are provided reconstituted plots or land as compensation for pooling of their land in this scheme.
- Capital gains earned by individuals or HUFs from the following transfers pursuant to the land pooling scheme is exempted with retrospective effect from 1 April 2015:
    - Transfer of land or building or both;
    - Sale of Land Pooling Ownership Certificates by Landowners (received in lieu of land transferred); and

- Sale of reconstituted plot or land by landowners (within two years from end of the financial year in the possession of such plot or land was handed over to them).

Conversion of preference shares to equity shares

- Conversion of preference shares into equity shares will not trigger capital gains tax. In such cases, the cost of acquisition and the period of holding of such equity shares shall be the same as that of the original preference shares.

Others

- Land and buildings will qualify as long term capital assets if held for two years.
- The base year for imputing fair value as the cost of acquisition for computing capital gains changed from 1 April 1981 to 1 April 2001.
- An exemption from transfer of mutual fund units on account of consolidation of mutual fund schemes was provided in the Finance Act, 2016. As a consequent amendment, it is now proposed that the cost of the units received consequent to consolidation (regarded as an exempt transfer) will be the same as the cost of the mutual fund unit which was transferred on consolidation.
- Transfer of rupee denominated bonds by one non-resident to another will not trigger capital gains. The benefit of exclusion of rupee appreciation on redemption of rupee denominated bonds has been extended to secondary holders (this was earlier available only to subscribers of such bonds).
- Long term capital gains to the extent of INR 5 million are exempt, if the taxpayer invests the whole or any part of capital gains in certain specified bonds of the National Highways Authority of India / Rural Electrificiation Corporation. It is proposed to widen the scope of this provision to also cover other bonds (having redemption period greater than three years) as may be notified by the Central Government.

Widening scope of 'income from other sources'

- The provisions of section 56(2)(vii) – relating to receipt of cash and other specified property without adequate consideration by indviduals / HUFs and provisions of section 56(2)(vii)(a) - relating to receipt of shares of closely held companies willl not apply from FY 17-18 onwards.
- Going forward, any specified property (including immovable property, listed / unlisted shares), received without adequate consideration by any assessee, will now be taxed under the head 'income from other sources'.
- Business reorganizations and other specified exclusions are carved out from the above provision.

Trusts and Political parties

Application for fresh registration of trusts in case of change of objects

- If a registered trust has adopted or undertaken modifications of its objects which are not in conformity with the conditions of registration, such trust must now obtain a fresh registration by making an application within a period of thirty days from the date of such adoption or modifications.

Tax return

- Exemption to income of trusts / political parties will not be available unless the trust/political party has furnished its return of income for the previous year under consideration, within the specified time limit.

Cash donations to Political Parties

- Political parties cannot accept cash donations exceeding INR 2,000

Exemption of income of certain Relief Funds

- Income of the Chief Minister's Relief Fund and the Lieutenant Governor's Relief Fund will be exempt from tax with retrospective effect from 1 April 1998.

Corpus donations

- Voluntary contribution towards corpus by any fund or trust or institution or university or educational institution or any hospital or other medical institution to any registered trust or institution shall not be treated as application of income to the objects of such donors.

Withholding tax

- Individuals or HUF (other than those liable to tax audit) shall be liable to withhold tax of 5% in case of rent payments exceeding INR 50,000 per month paid to a resident.
- Payment of money under a JDA to individuals or HUF liable to withholding tax at the rate of 10%.
- Taxes shall be withheld at the rate of 2% on the payment for professional or technical services, made to a payee engaged only in the business of operation of call centre.
- Any payment made in respect of award or agreement which has been exempt from levy of income-tax by virtue of the provisions of the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013, shall be exempt from withholding tax provisions.
- Concessional withholding tax rate of 5% on interest payment in case of moneys borrowed in foreign currency from non-residents will now be available for borrowings made before 1 July 2020. Similar benefit has been extended to interest payable to a non-resident on 'masala bonds' with retrospective effect from AY 2016-17.
- No withholding tax in case of payments in the nature of insurance commission where the payee furnishes a declaration in the prescribed form (with effect from 1 June 2017).

Compliance and Procedures

- Time limit to file revised returns reduced to 12 months from the end of the relevant financial year.
- Filing of belated return of income to attract a late filing fee. Maximum late filing fee of INR 10,000 proposed.
- Interest at 0.5% per month payable on TDS refunds due to a deductor.
- Penalty of INR 10,000 (per report / certificate) to be imposed on merchant bankers / registered valuers / accountants for furnishing incorrect information in any report or certificate

Rationalisation of Tax Collection at Source and Interest on Advance Tax

- Sale of jewellery in cash will not be subject to tax collection at source.
- Specified buyers such as Central and State Governments, Embassy, High Commission, local authority, public sector company engaged in business of carrying passengers etc. exempted from provision of tax collection at source on purchase of motor vehicle.
- Buyers (other than non-residents not having permanent establishment) subject to tax collection at source shall furnish Permanent Account Number, failing which, tax to be collected at source shall be higher of, twice the rate specified or 5%.
- No interest on deferment of advance tax payable, if shortfall is on account of dividend income which is subject to additional tax of 10%.

Procedures

- Time limit for completion of regular assessment proceedings to be reduced in a phased manner from AY 2018-19 onwards:
    - AY 2018-19: 18 months from the end of the relevant AY (from existing 21 months)
    - AY 2019-20: 12 months from the end of the relevant AY (from existing 21 months)
- Return of income has to be processed within the prescribed time-limit (and refunds are to be issued) unless prior approval of higher authorities is sought by the Assessing Officer. This is effective in respect of the return of income filed for AY 2017-18 and onwards.
- Credit for foreign taxes not granted earlier (on the basis that such tax payment was in dispute) will be granted by way of rectification of the relevant intimation/ assessment order upon settlement of dispute subject to furnishing of evidence of tax payment/ settlement of dispute within the prescribed time frame.
- Charitable Trusts to be included within the purview of a survey.
- During the course of a search, Authorized Officer empowered to:
    - Provisionally attach property belonging to the Assessee for a period of 6 months subject to approval from the higher authorities
    - Make reference to a Valuation Officer for estimation of FMV.
- Scope of initiation of assessment / reassessment proceedings pursuant to a search extended to ten years from the existing six years subject to prescribed conditions.
- Reason to believe / reason to suspect not to be disclosed to any person / authority or Appellate Tribunal in cases of search proceedings to ensure confidentiality of such cases.
- The Central Board of Direct Taxes empowered to issue necessary directions in respect of levy of penalty for non-compliance with provisions relating to deduction / collection of taxes at source
- The Authority for Advance Ruling for income-tax, central excise, customs and service tax will be merged.
- Order passed by Commissioner of Income-tax (Exemption) in case of Charitable Funds / Institutions or any trust or institution set up wholly for public religious purposes and / or charitable purposes will be appealable before the Income Tax Appellate Tribunal.

Miscellaneous

- It is proposed to tax all categories of taxpayers who receive income by way of dividend in excess of INR 1 million at the rate of 10%. The provisions of this section will not be applicable to domestic companies and certain funds, trusts, institutions, etc.
- Gross income received from transfer of carbon credits proposed to be taxed at 10%. No expenditure or allowance can be claimed against such income under the Act.
- The amendment made in the Finance Act, 2016 extending the concessional rate of 10% on long term capital gains arising to non-residents from the sale of private company shares has been made retrospectively applicable from FY 2012-13 onwards

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Indirect Tax Proposals

Goods & Services Tax (GST)

With the focus on implementing GST in FY 2017-18, the Government has made minimal legislative changes in existing indirect tax laws. Although the Finance Minister referred to the consensus on GST and the readiness of the IT infrastructure in his Budget Speech, he did not lay down any concrete timetable in this regard. He has however, in the past, stated that 1 July 2017 will be the likely date for introduction of GST.

Tariff Rate

- No change in peak rate of Customs, Excise & Service Tax
- Changes in Customs Duty / Excise duty rates on account of the following**:**
    - To incentivize domestic value addition - 'Make in India' (e.g. LNG, parts of LED)
    - To address problems of inverted duty structure (e.g. solar tempered glass)
    - To provide protection to the domestic industry (e.g. PCBs for mobile)
    - To promote cashless transactions and domestic manufacturing of device (POS card reader, micro ATM, Scanner & components)
    - To improve ease of doing business and export promotion (e.g. increase in limit of duty free import of inputs for leather / synthetic footwear)
    - Anti-avoidance measures (e.g. silver coins)

Customs – Key legislative changes

- Meaning of 'importer' and 'exporter' amended to include a beneficial owner. 'Beneficial owner' is defined to mean any person on whose behalf the goods are being imported or exported or who exercises effective control over the goods being imported or exported
- Meaning of 'Customs station' is amended to include international courier terminal and foreign post office.
- Bill of entry needs to be filed within the next working day of arrival of vessel / aircraft / vehicles. Delay in filing would attract charges as may be prescribed.
- Payment of Customs duty is to be made at the time of presentation of Bill of Entry in case of self-assessment and within one working day (currently - 2 days) from the day of return of bill of entry by the Customs officer in case of assessment, reassessment or provisional assessment
- The facility of storing dutiable goods (pending clearance) in a public warehouse now stands extended to goods meant for warehousing. Further, for goods meant for home consumption (pending clearance), the facility of storing such goods in private warehouse stands withdrawn.

Service Tax – Key legislative changes

- Retrospective exemption from 1 June 2007 to 21 September 2016 for upfront lease payment for services by way of leasing of industrial plots for a period of 30 years or more by State Government corporations / undertakings to industrial units. For Service tax collected, refund applications can be made within 6 months from the date of Finance Bill receiving presidential assent.
- Rule 2A of the Service Tax (Determination of Value) Rules, 2006 has been amended to exclude value of land while calculating value of works contract service. In case where value of land is not identifiable, the value shall be considered as 25% / 30% of the total consideration as applicable.

Common legislative changes

- Amendment in Advance Ruling provisions (Customs, Central Excise & Service Tax)
  - Common Authority for Advance Rulings for Income Tax, Customs, Central Excise, Service tax. Pending cases on the date of assent of Finance Bill, 2017 would be transferred to the common authority,
  - Time limit for pronouncement of advance ruling increased from 90 days to 6 months.
- Application for Settlement has also been extended to co-noticees.
- Settlement Commission can amend its order within three months to rectify any error apparent on record.
- Research & Development Cess repealed effective 1 April 2017.

CENVAT Credit

- A proviso has been inserted to Explanation-I(e) of the Rule 6(3D) of the CENVAT Credit Rules, 2004 (CCR) to exclude banks, financial institutions (including NBFCs). The said amendment requires value of interest or discount to be considered for the purpose of reversal of CENVAT Credit under Rule 6(3) and Rule 6(3A) of the CCR. The amendment would be effective 2 February 2017.
- Rule 10 of the CCR has been amended requiring an assessee to make an application for transfer of credit in case of sale, merger, demerger, amalgamation etc. The said application shall be allowed within a period of 3 months from date of receipt of application. Further, an extension may be sought by Deputy/Assistant Commissioner for further period of six months from Principal Commissioner on providing sufficient cause/reasons.

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