I N D E X

1. Corporate Tax

1.1 Exemption under section 10(1) of the Income-tax Act, 1961

Section 10(1) of the Income-tax Act, 1961 ('Act') provides for exemption on income earned from agricultural operations. Currently, there is long-drawn litigation on the eligibility of seed grower companies to claim the aforementioned exemption. Courts have taken divergent views on this issue. As a result substantial amount of tax-payers money is getting locked up with the Government treasury with no hope of an early resolution. The key contentions of the revenue authorities in denying the claim of exemption under section 10(1) of the Act are on account of various reasons such as company not owning land, prohibition under state laws on company to own or lease land, composite payment made to farmers linked to output, no separate payment made for lease of land and other services, post-production activities lead to value addition, company has entered into agreement with farmers for purchasing seeds at fixed price etc.

Income earned from agricultural operations is eligible for exemption under section 10(1) of the Income-tax Act, 1961 ('Act'). The benefit of this exemption is claimed by agriculturists/cultivators, including those engaged in seeds and plantation activities. Further as per Explanation 3 to section 2(1A) of the Act, 'agricultural income' includes income derived from saplings and seedlings grown in nursery.

The claim of seed grower companies engaged in growing of Hyrbid Seeds stands on much better footing as compared to nursery activities as it includes undertaking basic agricultural activities like sowing, tilling, irrigation, harvesting, etc. on land.

Since the activities undertaken by seed companies (i.e. involved in growing high yielding hybrid seeds) are similar to agricultural operations undertaken by cultivators/agriculturists, the income earned thereon should be treated as exempt from tax under section 10(1) of the Act.

The Directorate General of Income-tax (Research) ['DGIR'] conducted study on the subject in December 2002 named "Production of Hybrid Seeds – Possibility of Taxation of Non-Agricultural Income". Post consultation with various stakeholders (including Ministry of Agriculture, Department of Agriculture and Cooperation, Seeds Division,) the DGIR had recommended that a rule in line with rules 7A, 7B, and 8 for Tea, Coffee and Rubber plantation activities may be inserted in the Income-tax Rules to prescribe a certain percentage of total income which should be treated as agricultural income.

To take forward the Recommendation of the DGIR, IDF (a research organization led by experts with very high credentials) had been appointed to undertake a detailed study in order to determine evidence based percentage of the income of seed companies that should be treated as exempt from tax. IDF studied, the agricultural processes and business model carried on by certain private Seed Companies with the assistance of the farmers, principles as laid down in various judicial precedents and analysis of cost data obtained from public sources. Thereafter, IDF recommended a rule-based approach and inferred that 90% of the profit earned by Seed Companies from integrated activity may be considered as exempt from tax.

Recommendations

In order to provide certainty on taxability for companies engaged in cultivation and sale of hybrid seeds, following 2002 study conducted by the DGIR and IDF, AmCham recommends that new rule may be inserted to compute the proportion of non-agricultural income out of the total income earned by the assessee's engaged in the business of hybrid seed similar to coffee and tea businesses. Further an explanation may also be inserted in the Act clarifying that income earned by the assessee's engaged in the business of cultivation of hybrid seeds would constitute agricultural income eligible for exemption under section 10(1) of the Act. The proposed amendments relating to taxation of part of the income earned from cultivation / production of seeds as business income being clarificatory in nature should apply for all open years which are pending either for assessment or for adjudication before Appellate Authorities or Courts.

An expert committee may be constituted to review the studies undertaken in past and recommend an appropriate portion eligible for exemption as agricultural income under section 10(1) of the Act.

1.2 Withdrawal of Minimum Alternate Tax ('MAT') as a result of phase out of deductions and exemptions

The provisions of MAT were introduced as a result of certain deductions and exemptions available to the taxpayers under the Act. While introducing these provisions, it was mentioned in the memorandum explaining the provisions of the Finance Bill 1987 that certain companies making huge profits were managing their affairs in such a way as to avoid payment of income tax. It appears that the availability of tax incentives have played a major role in minimising the tax liability which has resulted in introduction of MAT provisions.

Recommendations

It is suggested that with the amendment made by FA 2016 laying down the roadmap to phase out the specified deductions and exemptions, MAT provisions should be withdrawn immediately. This will obviate the need to amend MAT to address Ind-AS challenges – an issue on which Ind-AS MAT Committee is yet to reach to a final conclusion.

If MAT provision are not withdrawn immediately atleast rate of MAT ought to be reduced considering various amendments for phasing out of tax deductions have already been enacted in the Finance Act 2016.

1.3 Reduction in tax rates

In the 2015 Budget Speech, the Hon'ble Finance Minister had announced a roadmap for reduction of corporate tax rates from 30 percent to 25 percent over the next 4 years.

In the other Asian countries, the prevailing maximum tax rate in case of companies ranges from 16%-25%.

Recommendations

- It is suggested that the corporate tax rate should be reduced to an all-inclusive rate of 22-23%.

- Further, reduction in tax rates should be extended to all businesses (and not just to new manufacturing set ups and to all assesses and not just new ones) and other forms of unincorporated bodies/ business entities like partnerships, LLPs, AOPs and co-operative societies to ensure horizontal equity between different legal forms in which business is carried on.

1.4 Surcharge on corporate tax rate for domestic companies

The prevailing tax rate for companies is already very high (30%). Moreover, vide Finance Act, 2015 the rate of surcharge for domestic companies with income exceeding INR 10 crores was further increased from 10% to 12%, resulting in additional tax burden on domestic companies.

Recommendations

- The rate of surcharge for domestic companies with income exceeding INR 10 crores should be rolled back to 10%.
- Further, to ensure horizontal equity between different legal forms in which business is carried on, the rate of surcharge even for other unincorporated entities (LLP, Partnership, etc.) should be restored back to 10%.

1.5 Abolition of DDT

DDT levy leads to double taxation on corporate sector and hence, should be done away with. Further, introduction of super-rich dividend levy u/s 115BBDA leads to additional hardship for the taxpayers.

Recommendations

- It is suggested that it is high time to do away with the additional income tax in the form of DDT under section 115-O of the Income-tax Act, 1961.
- Alternatively, DDT rate is recommended to be reduced to 10% from the current effective rate of 20% (after including education cess, surcharge and grossing up of DDT).
- Alternatively, a basic exemption limit, say 10% of profits/capital, may be provided where the company distributing dividend is not made liable to DDT up to such specified limit.

1.6 Rationalization of section 14A and Rule 8D provisions

Section 14A of the Act provides for disallowance of expenses incurred in connection with earning of exempt income. As per the current provisions, direct as well as indirect expenses are subject to this disallowance. However, indirect expenses are generally overhead expenses that are required to be incurred irrespective of whether the income is taxable or not or irrespective of the level of income.

The modified Rule 8D provides for a new method for computation of disallowance of expenditure which, in addition to amount of expenditure directly relating to exempt income, also includes an amount equal to 1% of annual average of monthly averages of the opening and closing balance of the value of investment which gives rise or may give rise to exempt income.

Recommendations

- It is requested that indirect expenses should be excluded in the computation of expenses incurred in relation to exempt income.
- Disallowance @ 1% of average monthly value of investment is too high, and hence, it should be limited to 0.5%.
- Further, the disallowance is linked to the value of assets and not to the income, hence the disallowance should be 1% of the exempt income and that too, the exempt income which is derived from the assets acquired out of the borrowed funds.

1.7 Amortisation of capital expenditure

Presently, there is no provision in the act for amortization of capital expenditure such as fees paid for increase in authorized share capital and payment made towards elimination of competition or premium paid on acquisition of leasehold rights in land etc. Such expenditure being capital in nature cannot be charged to revenue as there is no provision for claiming these expenses in computing the income.

Recommendations

It is suggested that provisions may be incorporated in the Act to allow amortisation of such capital expenditures which are essential to run the business.

1.8 Deduction for Corporate Social Responsibility (CSR) expenditure

Finance Act 2014 has amended provisions of section 37 of the Act to provide that any expenditure incurred on activities relating to corporate social responsibility (CSR) referred to in section 135 of the Companies Act 2013 shall not be deemed to be an expenditure incurred for the purposes of business.

On the other hand, the Companies Act, 2013 has mandated every company fulfilling certain criteria to spend at least 2% of its average net profit for the immediately preceding three financial years on CSR activities. Since there is statutory obligation of companies to spend specified sum on CSR activities, such expenditure represents an integral part of conducting business operations of the tax payer company. Furthermore, allowing tax deduction may encourage corporates to incur expenditure in excess of the prescribed sums. While donation for specified purposes entitles the payer to deduction under section 80G provisions, where CSR expenditure deduction is not allowed, this shall be discriminatory for corporates who may be carrying out CSR activities in-house in their own defined areas.

Recommendations

- A deduction of the expenditure on community/ social development (both capital and revenue) be introduced, covering critical focus areas for CSR such as education, health, women empowerment, etc.
- Even in cases where the company has its own trust or foundation, the deduction in respect of entire expenditure incurred for CSR activities should be allowed.
- Such expenses however may be subject to a limit of say 5% of total income.
- In case the above recommendations are not practically feasible at this stage, then specific clarification should be provided that any expenditure on CSR which is not claimed by the companies to fulfill their compliance obligation under section 135 of the Companies Act should be allowed as deduction in full under section 37.

1.9 Section 28(iv) – Income Chargeable under the head Profits and Gains of Business or Profession

Clause (iv) of Section 28 seeks to tax income in the nature of any benefit or perquisite, whether convertible into money or not, under the head 'Profits and Gains of Business or Profession'. Section 28(iv) only refers to the 'income' which can be charged under the head 'profits and gains of business or profession' and therefore, when a particular advantage, perquisite or receipt is not in the nature of income, there cannot be any occasion to bring the same to tax under section 28(iv). Further it settled law that a capital receipt, in principle, is outside the scope of income chargeable to tax.

It has been seen that Revenue is widely interpreting this section so as to charge to tax even the receipts which are purely of capital nature and which does not arise in the regular business dealings of the assese.

Recommendations

It is recommended that Government should suitably clarify as to the scope of section 28(iv) specifying absolute exclusion to capital receipts (arising out of the transfer of capital assets) which are covered under charging section 45 or waiver of loans taken for capital purposes which is otherwise not taxable under the Act.

1.10 Amortisation of mining expenses under section 35E

Presently, the expenditure incurred wholly and exclusively on prospecting, extraction or production of any mineral during 4 years prior to the start of commercial production is eligible for amortization over a period of 10 years starting from the year of the commercial production. Any expense incurred prior to 4 years gets lapsed and no deduction for the same can be claimed as per section 35E.

The Income Tax Act provides a special mechanism for taxation of income of entities, which enter into a contract with the Government of India for exploration and production of oil and gas in India. Section 42 of the IT Act provides that the taxable profits of a person, who has entered into an agreement (i.e. a Production Sharing Contract- PSC) with the Government for its association/

participation in the business of prospecting, exploration or production of mineral oil, will be determined in accordance with the special provisions contained in the PSC (and the provisions of the Act are deemed to be modified to the extent these agreements provide for certain deductions/ allowances in excess of those provided under the Act).

Exploration and drilling expenditure (as defined in the Model PSC), both capital and revenue in nature, is 100% tax deductible. All such allowable expenditure is required to be aggregated till year of commencement of commercial production and is allowed to be carried forward and set off for a future period of 8 years. Alternatively, such expenditure may be amortized equally over a 10 year period. All unsuccessful exploration costs from other PSCs are permitted to be set off against income arising under the relevant PSC.

Thus, the oil and gas sector has been greatly benefited by the specific provision in the IT Act, which allows deduction for all expenses incurred prior to commercial production, including capital expenditure.

Recommendations

It is suggested that all pre-mining costs of all years prior to commercial production including acquisition of deposits, site or rights should be allowed for amortization over minimum lease period or lesser period at the option of the lessee.

1.11 Section 35D - Amortisation of certain preliminary expenses

Section 35D provides deduction to Indian Companies for certain expenditure incurred before the commencement of business or after the commencement in connection with the extension of the undertaking or in connection with setting up a new unit. The benefit of deduction under Section 35D is limited to the expenditure in the nature of legal charges and registration fees etc. incurred for incorporating the Company.

Further, the deduction of this expenditure is restricted to 5 percent of the cost of project or capital employed at the option of the company.
However, legitimate expenditure incurred post incorporation for and until setting up of business, which are neither covered within Section 35D nor can be capitalized to the actual cost of fixed assets, gets permanently disallowed under the Act, even though they are incurred for the setting up the business and becomes sunk cost. Some of this expenditure could be office / sales employees' salary, audit fees, advertisement and business promotion expenditure incurred prior to setting up of business, etc. which cannot be capitalized to the cost of the asset.

This is more particularly in the case of companies having longer gestation period for setting up their business such as manufacturing entities, insurance business requiring multiple licenses, etc. This affects the cash flow and the spending capacity of the company.

Recommendations

Section 35D of the Act should be suitably amended to include all the expenses incurred by Companies post-incorporation but during the course of setting up of its business as eligible for deduction.

1.12 Balance 50% of additional depreciation u/s 32(1) (iia)

In the Finance Act, 2015 a proviso was inserted after the second proviso to sub section (1) of section 32 so as to provide that where an asset referred to in clause (iia) or the first proviso to clause (iia), as the case may be, is acquired by the assesse during the previous year and is put to use for the purposes of business for a period of less than one hundred and eighty days in that previous year and the deduction under sub-section (1) in respect of such asset is restricted to fifty per cent of the amount calculated at the percentage prescribed for an asset under clause (iia) for that previous year, then, the deduction for the balance fifty per cent of the amount calculated at the percentage prescribed for such asset under clause (iia) shall be allowed under sub-section (1) in the immediately succeeding previous year in respect of such asset. However, the amendment was made effective from F.Y. 2015-16 i.e. A.Y. 2016-17 and subsequent assessment years.

Recommendations

In order to dispose of the pending litigations in various stages of appellate authorities' w.e.f. AY 2006-07 on the same issue, the proviso introduced in Finance Act, 2015 needs to be made applicable from AY 2006-07 retrospectively.

1.13 Investment Allowance u/s 32AC

Finance Act 2016 proposed an amendment under section 32AC(1A). It provides that acquisition and installation of machinery or plant in excess of value of INR 25 crores need not be in the same year i.e., the twin conditions of "acquisition" and "installation" of assets in the same year has been dispensed with.

Subsection (1) of Sec 32AC introduced vide Finance Act 2013, provides for deduction for investment allowance, if the cost of new assets exceeds INR 100 Crores and the same is acquired and installed in stipulated time between 31st March 2013 and 1st April 2015. The limit of investment of INR 100 Crores suggests that the investment is expected to be made in large capital intensive projects. In such a case stipulation of acquiring and installing plant and machinery within a time frame of two years defeats the efficacy of the beneficial provision. Large capital intensive project normally take at least 3 to 4 years to get installed.

Recommendations

The amendment made in sub section (1A) should be extended to sub section (1) retaining the threshold of INR 100 Crores i.e. assets acquired even before 1st April 2013 but installed within stipulated two year period will qualify for benefit of investment allowance.

1.14 Investment allowance and enhanced depreciation to Companies engaged in manufacturing of articles / things catering to Defence sector

Currently, there is no provision under the Act for tax incentives for Company engaged in the defence sector. Defence sector is a 'Make in India' initiative and involves high cost and long gestation period. Thus, it is imperative that some tax incentive is given to such companies to attract private sector participation.

Recommendations

- Special tax incentive in the form of additional investment allowance and enhanced depreciation should be given for companies engaged in manufacturing of articles / things catering to defence sector.
- In order to ensure that only those companies which are catering to defence sector get an exemption, approval of projects can be entrusted on DIPP.

1.15 Deduction under section 80IB on profits and gains from certain industrial undertakings other than infrastructure development undertakings

The Government of India has identified electronics manufacturing as a focus sector to boost exports, import substitution, increasing manufacturing output and provide employment opportunities.

Recommendations

It is proposed to amend section 80IB of the Act to provide 50% deduction on profits and gains derived from business of an Electronics System and Design Manufacture ('ESDM') facility for a period of 10 consecutive assessment years.

1.16 Weighted deduction for in-house scientific research

The phased out reduction of R&D weighted deductions may have impact on innovation and could de-incentivise the industry from spending more on R&D.

Recommendations

Government should consider rolling back the phase out plan for weighted benefits available on the R&D expenditure.

1.17 R&D tax breaks

Companies engaging in in-house R&D facilities are provided weighted deduction @ 200% of the capital and revenue expenditure incurred by them. One of the key conditions is that the R&D activity should be carried out in-house. This effectively means that each and every kind of research activity, and really speaking every stage of the entire research activity, has to be conducted in-house and necessary capital and labour has to be deployed. However, there will always be cases of one-time or sporadic use in which scenario it will not be effective to create capacity and deploy labour since it will lead to a waste of scarce and critical labour and capital.

Recommendations

An exception may be provided that where the external R&D is only a small component of the entire R&D and is non-critical in nature, the same will continue to be considered for weighted deduction, provided the principal company continuously monitors and directs the program.

1.18 Certain R&D expenditure not eligible for weighted deduction

Presently, only expenditure, which are directly identifiable with approved R&D facility, shall be eligible for the weighted tax deduction. However, several types of expenditure such as the following are not allowable for weighted deduction:

- Expenditure purely related to market research, sales promotion, quality control, testing, commercial production, style changes, routine data collection etc.;
- Capitalised expenditure of intangible nature;
- Foreign patent filing expenditure, foreign consultancy expenditure, REACH compliance expenditure;
- Consultancy expenditure, retainership, contract manpower/ labour;
- Expenditure in the nature of cost of any land or building etc.

Recommendations

An amendment should be brought in to the effect that entire expenditure incurred in connection with R&D should be eligible for a weighted deduction to reduce complexity and make it a more attractive commercial proposition to invest in setting up R&D facilities in India.

1.19 Weighted deduction on internally developed intangible assets

The DSIR guidelines provide that eligible capital expenditure on R&D will include expenditure on plant, equipment or any other tangible item only. It also provides that capital expenditure of intangible nature is not eligible for weighted deduction.

Recommendations

- It is recommended to provide weighted deduction for expenditure incurred on internally developed intangible assets under Section 35(2AB) of the Act.
- It is also recommended that any initial cost paid for acquiring R&D related intangible assets, which are used in the R&D unit should also be allowed for weighted deduction under Section 35(2AB) of the Act.

1.20 Benefit under Section 35(1) (iia) to be increased to 200 per cent

Section 35(2AB) of the Act has been gradually amended to provide increased tax benefits on expenditure incurred towards in-house R&D facilities i.e. from 125 per cent to 200 per cent. However, Section 35(1)(iia) of the Act, which provides tax incentives in respect of payments made to R&D company, has remained same at 125 per cent. The conditions specified by the DSIR for grant of approval for a recognized R&D facility/ company under Section 35(2AB) and Section 35(1) (iia) are the same and hence, the tax benefits provided under Section 35(1) (iia) should be at par with the tax benefits provided under Section 35(2AB) of the Act.

Recommendations

It is recommended that the tax benefits under Section 35(1)(iia) should be increased to 200 per cent from the present level of 125 per cent and the amendment introduced by Finance Act 2016 to reduce the amount of deduction to 100 per cent w.e.f. 1/4/2018 should be omitted.

1.21 Deduction for employment generation under section 80JJAA

Deduction for employment generation shall be available in respect of cost incurred on any employee whose total emolument is less than or equal to INR 25000/- per month under section 80JJAA. The capping of salary limit will make the claim ineffective especially in case of Software Industry. The industry is absorbing the fresh talent from colleges/IIT/IIM's with attractive salaries as part of hiring process. Also one of the agenda of the Government is job creation; this capping will discourage the Industry from creating more jobs for the unemployed youth.

Recommendations

Government should either roll back the capping of salary limit to INR 25,000 per month or increase the limit to a minimum of INR 50,000 per month.

1.22 Exchange differences on money borrowed in foreign currency for acquisition of assets within India

Section 43A allows an assesse to make adjustment in "actual cost" of the asset after the acquisition of assets from a country outside India on account of exchange rate fluctuation arising either on liability payable towards such foreign asset or on account of money repayable in foreign currency utilized for acquiring such foreign asset. The adjusted "actual cost" becomes the base for claiming depreciation.

Section 43A allows adjustment in actual cost under Section 43(1) with respect to exchange differences on account of loan taken from outside India but utilized for the acquisition of assets outside India. However, the section does not specifically provide for such adjustment where the asset is acquired / constructed in India out of funds borrowed in foreign currency.

Recommendations

It is recommended that provisions of section 43A should be extended to allow for adjustment of foreign exchange fluctuation in “actual cost” even where the asset is acquired in India from foreign currency. This will bring parity between assets acquired from outside India and assets acquired / contructed within India and will also be in sync with “Make in India” concept.

It is imperative to highlight that ICDS on foreign exchange does not make any distinction between revenue / capital foreign exchange fluctuation in case of monetary items and allows adjustment of both in Profits and Loss account with the only exception of those cases which are covered by section 43A.

Therefore, to be bring parity between the provisions of the Act and ICDS, it is recommended that any forex which is not covered by section 43A and capital in nature should also be allowed as a deduction by making specific amendment within law.

1.23 Section 36(1) (va) –Employees’ contribution to Provident Fund

Section 43B of the Act allows deduction towards employer contribution to PF/ any other fund for the welfare of the employees if the same is deposited upto the date of filing the return of income. However, deduction for employees' contribution to PF/ ESI or any other fund is governed by Section 36(1)(va) of the Act which mandates that the employees’ contribution should be credited to the relevant fund by the due date specified under the relevant Act, rule, order or notification governing that fund.

Recommendations

It is recommended that suitable amendment should be made in the Act so as to bring the provisions relating to the Employees' contribution towards employee welfare funds in line with the employer's contribution towards such funds.

1.24 Deduction u/s 43B

The provisions of Sec. 43B were initially enacted in respect of statutory payments. It is noticed that its scope has now been extended even to contractual payments, such as expenditure on leave encashment by employees, interest payable to financial institutions etc.

Recommendations

It is suggested that the scope of Sec. 43B should not cover contractual payments, but should be restricted to statutory payments only and the section should be amended accordingly.

1.25 Carry forward of business losses on merger under section 72A of the Act

Carry forward of business losses on merger is limited to companies owning ‘Industrial undertakings”. The definition of Industrial Undertaking is extremely narrow and restricted; thus a number of sectors are impacted as their ability to carry forward losses is significantly compromised.

Further, the section also prescribes for stringent conditions such as continuity of holding of the assets by the amalgamating company pre transfer (2 years) and by the amalgamated company post transfer (5 years), etc.

Recommendations

- It is recommended that the definition of 'Industrial Undertaking' should be either done away with, so that all mergers are eligible for carry forward of losses.
- The section should be amended to replace the stringent conditions to liberal ones such as reducing the period of holding assets and carrying on of business from 5 years to 3 years.

1.26 Surrender of PAN for discontinued/ closed companies

Currently, there is no formal process for surrender of PAN upon discontinuance of business/ profession or cease to exist as assesse.

Recommendations

A procedure for surrendering PAN should be established to facilitate smooth closure.

1.27 Set – off - Deemed Speculation Loss in case of Companies – Explanation to Sec. 73

- As per the provisions of Sec. 73 of the Act, any loss, computed in respect of a speculation business carried on by the assesse, cannot be set off except against profits and gains, if any, of another speculation business.
- As per Sec.43(5) of the Act, "speculative transaction" means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips
- However, as per Explanation to Sec.73 of the Act, where any part of the business of a company consists of purchase and sale of shares of other companies, such company (with certain exception)is deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.
- Accordingly, as per the Explanation to Sec.73, in case of many companies, even delivery based share transactions are deemed to be speculative.

Recommendations

Automation of the trading mechanism and various measures initiated by SEBI over the last few years have brought total transparency in share trading, leaving little scope for manipulation of share trades by transfer of profits/losses from one person to another.

It is, therefore, suggested that the aforesaid Explanation to Sec.73 of the Act be deleted.

1.28 Set-off of long-term and short-term capital losses against income under the same head

- The present scheme of set off of brought forward losses allows set off of loss under a particular head of income only against income under the same head in the subsequent year. This causes great hardship, especially to an assesse, who with a view to recouping loss made in business, sells a capital asset for revival of his business. In such a case, in spite of substantial brought forward business loss, he is required to pay tax on capital gains, limiting his capacity to reestablish himself in business. This problem has become more severe with the introduction of amended Sec. 50 and deletion of Sec. 41(2).
- Further, loss under the head 'Capital Gains' is not allowed to be set off against income under any other head of income even in the year in which loss is incurred. This is against the concept of taxation of 'real income'.
- Loss under the head 'Income from Other Sources' is not allowed to be carried forward at all.

1.29 Differentiated Securities Transaction Tax on FPIs in Lieu of Capital Gains Tax on Listed Securities

India is one of the fastest growing economies in the world, projected to grow between 7.4% and 8.5% in 2016. Increasing the ease of doing business in India, by attracting foreign investment and creating a vibrant Indian economy, is critical to continue this growth trajectory.

To make the Indian capital markets more attractive, and to increase the inflow of foreign investments in India, the need for a predictable tax treatment for transactions on the stock exchanges is of paramount importance. Capital markets require a very high degree of tax certainty as compared to other industries. Capital markets will operate efficiently only if each and every trade has a predictable result for investors and for the market participants.

Hence, the need to review the existing inefficiencies with respect to taxation of Foreign Portfolio Investors (FPIs).

India is one of the very few countries that imposes CGT on foreign portfolio investments in listed securities, and even rarer amongst countries that impose both CGT and higher securities transaction tax (STT), placing them with countries such as Pakistan and Bangladesh (Pakistan and Bangladesh imposes both CGT and STT on FPIs).

Further, current Indian tax framework for FPIs in India is very complex compared to other global markets which make investing into India more onerous relative to other markets:

1. Very complex capital gains tax regime;
2. GAAR Uncertainty - currently, there is no clarity on how GAAR will apply to FPIs availing DTAA benefits;
3. High Cost of Trading - India is 8th most expensive out of 46 countries in levying market charges (both tax and non-tax). Attached as Annexure 2 is a comparison table of the market charges;
4. Double Taxation - Imposition of CGT on FPIs results in double taxation to foreign investors.

Recommendation

The Government should therefore consider to replace the CGT earned by FPIs in the Indian capital market with a higher STT.

The imposition of higher STT in lieu

- Provide tax certainty, predictability, and ease of operation so critical to FPIs
- Create a level playing field for all FPIs investing from any jurisdiction
- Free up the resources of the Revenue due to simplification resulting in ease of administration, and allow tax officials to focus on other important areas
- Increase investment flows and liquidity into the Indian capital markets
- Allow corporate India to raise equity resources at higher valuations , lowering funding costs, and improving the Indian economy
- Will provide stability in tax revenue collection as STT is linked to transaction value and not on the income from transaction, i.e. tax revenue will not be impacted even if FPIs incur losses on account of market slowdown or otherwise
- Increase tax revenues significantly

  Investment/trading by FPIs constitute a significant part of the turnover on the exchanges and increase in FPI volume would increase the STT revenue significantly.

  While India ranks among the top ten by global GDP and total market capitalization, the cash trading volumes/ GDP s at sub 40% in India as compared to 1X-3X in many other markets.

  Raising the cash trading volume vs. GDP to a level equal to a Korea (144%) or Taiwan (148%) can triple the STT revenue.

  Further, a more liquid and active market will allow Indian corporates to raise equity at higher valuations, provide a means and incentive new companies to list on the exchanges, again raising STT revenue and have a positive multiplier impact on the Indian economy.

1.30 Transfer Sec 2(47)

- The Finance Act, 2012 has amended the definition of `transfer' with retrospective effect from 1 April 1962, by inserting Explanation 2 to Sec. 2(47). The Explanation so inserted clarifies that transfer includes and shall be deemed to have always included disposing of, parting with an asset or any interest therein, creating any interest in any asset in any manner whatsoever, directly or indirectly, absolutely, conditionally, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterized as being effected or dependent upon or flowing from the transfer of share or shares of a company registered or incorporated outside India
- Such a broad definition of the term has serious implications for even domestic transactions, which are otherwise not regarded as transfers. Transactions such as creation of a mortgage, grant of short-term leasehold rights, etc. may also fall within the definition of transfer, and

could have serious implications for genuine transactions carried out in the past by residents, which were otherwise not regarded as transfers and are not intended to be covered by the definition.

Recommendations

It is therefore suggested that the extended definition of "transfer" should apply only to transfer of shares of a foreign company having the effect of transferring an asset in India or creating an interest in any asset in India and it should apply prospectively.

2. Withholding Tax

2.1 Concessional rate of tax for Rupee denominated Overseas Bond (Masala Bond)

Concessional rate of tax @ 5% has been currently extended to Rupee denominated Overseas Bond vide CBDT Press Release but without incorporating under section 194LD in the Statute. Additionally, certain tax issues in relation to Masala Bonds to non-resident investors are required to be addressed.

Recommendations

- It is recommended that for the sake of clarity and certainty, concessional rate of 5% for rupee denominated bonds be incorporated in the statute itself by way of amendment to section 194LD.
- In addition, suitable amendments need to be made (a) Extension of exemption on forex gains even to the secondary subscribers and (b) provide capital gains exemption on trading gains.

2.2 Extension of concessional tax rate regime under sections 194LC and 194LD

The eligibility period for benefit of reduced tax rate of 5% available under sections 194LC and 194LD in respect of external commercial borrowings (ECB) and corporate bonds respectively is till 30 June, 2017.

Recommendations

With a view to boost the economy by way of continued interest from Indian borrowers for availing loans under ECB route or issuer of bonds, it is recommended to extend the date of concessional rate regime under section 194LC and 194LD by 3 years, to 30 June 2020. Further the benefit should be extended to even ECB denominated in Indian currency.

2.3 Time limit for TDS assessment in case of payments to non-residents

As per sub section (3) of section 201 of the Act, in respect of default in TDS on payment to a resident, no order u/s 201 has to be made after the expiry of 7 years from the end of the financial year. The same limitation does not apply in case of TDS default on payment to a non-resident and the assessment can be done for any financial year, which is unreasonable.

Recommendations

It is recommended that amendment should be made in sub section 3 to section 201 to include similar time limit of 7 years for assessment with respect to payments made to non-residents as in the case of payments to residents to bring in parity.

2.4 Generation of TDS certificates in case TDS is deducted @20% u/s 206AA

As per current instruction and configuration at TIN system, entries without PAN cannot be filed in the TDS return. For companies, it is now mandatory to generate TDS Certificate online. For deductees in the absence of PAN, TDS is deducted as per the provisions of Section 206AA of the Act. For these entries TDS certificate is not generated online through TIN system.

Recommendations

A clarification regarding the procedure for providing TDS Certificate to make the process easy and smooth and better compliance of the Act may be provided.

2.5 Applicability of TDS on Monthly Provision

Provisions for monthly expenses debited in the company's books of account only for the purpose of monthly MIS which are reversed in the beginning of subsequent month are in respect to-

- Expenses which are booked on account of identified payee and known amount but invoice copy from the party is to be received.
- Expenses which are booked on ad-hoc basis.

Recommendations

It is recommended that TDS should not be applicable on monthly provision which are mainly for MIS purpose and reversed on first day of next month.

2.6 TDS on International Interconnect Charge (IIC) paid to foreign operators

Finance Act 2012 brought in a retrospective amendment by introducing Explanation 5 and Explanation 6 to Section 9(1) (vi).

Royalty is defined in Explanation 2 which connotes exclusivity & the exclusive right in relation to an asset which should be with the grantor (be it physical or intellectual property) for which royalty is paid. In case of an intellectual property, it is generally associated with some discovery, invention, creation, specialized knowledge etc. emanating from human mind and is payable to the inventor/ grantor for allowing the usage of his invention or creation and having an exclusive right over it. "Process" needs to have an IPR.

Payment made for anything which is widely available (as standard product/ off the shelf product) in the open market to all those willing to pay may not constitute ‘royalty’ and is essentially in the nature of business income.

Further, when a service provider is using its own equipment/ process to render services to service recipient, it cannot be said that service recipient or any other person is using such equipment/ process at same point in time. The two situations are mutually exclusive.

The law has provided two separate provisions relating to ‘royalty’ [under section 9(1) (vi)] and ‘fees for technical services (u/s 9(1) (vii)) under the Act and the said provisions are mutually exclusive and do not overlap. The distinction which has been made by legislature between aforesaid concepts has to be maintained and given the intended effect. It is but obvious that even where services are not ‘technical’, the distinction between a service contract and royalty contract is still required to be maintained.

The amended provisions under the Act (including Explanations 5 & 6 to section 9(1) (vi)) shall have no relevance in so far as the definition of ‘royalties’ as contained in the Treaties is concerned. Under treaty, the process has to be a ‘secret process’ in form of Intellectual Property Right in order to fall within purview of royalty and there has to a direct usage of such ‘secret process’ by payer in order to qualify the payment as ‘royalty’ under Treaty. The term ‘royalty’ is already defined in all treaties.

There is no dispute on the fact that provisions of DTAA will prevail over Act to the extent they are more beneficial to the assesse. The treaties are binding on both countries and have to be interpreted in good faith.

Recommendations

- It is recommended that government should clarify by way of appropriate amendment to Explanation 5 & 6, that these Explanations would not have any bearing on standard services agreements by way of giving some examples which cannot fall within purview of royalty even after insertion of Explanation 5 & 6.
- Further, in any case, the Government should clarify that the retrospective amendment is not applicable on the transactions which were entered into before the amendment.
- It is recommended that government should clarify by way an amendment to Explanation 5 & 6 that these explanations would not have any bearing on the interpretation of treaty and the definition of “process” as defined in domestic tax law should not be imported into treaty. This view is acknowledged by various Indian Courts also and the same may be clarified in the statutory provision to avoid further disputes/ litigation.

2.7 Certificate for tax deducted at source

Vide section 203 of the Income Tax Act, the deductor has to furnish Form 16A/ Form 16 generated from TRACES, to the deductee within the prescribed time. Earlier deductor had to furnish the certificate in the prescribed form. Now deductor has to generate the certificates from TRACES website and the same should be issued to the deductee.

Recommendations

Considering the volume of transactions and in order to reduce the compliance burden, Form 16A/Form 16 should be made available directly to the deductees. This can be done in either of the following ways:

- Sending Form 16/Form 16A directly by TDS Processing Centre (TRACES) to the deductees' mail id registered under his PAN; or
- Making a provision and facilitating downloading of these forms by deductee himself from e-filing site/TRACES site similar to Form 26AS.

2.8 TDS Credit

The E-TDS system is undergoing issues and there is mismatch of data between TDS certificates issued by deductors, TDS statements uploaded on TIN system and bank payment details, PAN of the deductees. As a result, deductees do not get the full credit for tax deducted. Further, based on the mismatch the tax authority is issuing orders upon the deductor thereby causing unnecessary adversity to the deductor/ taxpayer.

The E-TDS system mandates all the deductors of taxes to process TDS Certificates in Form 16A's only through TIN- NSDL website. The software of the tax department automatically picks up the address of the deductee from the address appearing in the PAN database maintained by the tax department. As a result, all the TDS certificates are getting issued at the address declared in the PAN application made by the deductee. This has resulted into severe hardship for the companies which have a multi locational set up, since all the TDS certificates get accumulated at the Registered office of the company (being PAN based address) and such accumulation makes it difficult to co-relate/ reconcile them with the accounts which are maintained at different locations and also the units are not able to identify whether the TDS certificate is received from the party or not.

Recommendations

- It is suggested that TDS certificates issued by the deductors, which are furnished by the deductees in the tax assessment, should be given due cognizance and refund claims based on such TDS certificates should be processed. Further, the tax officer can suitably issue proper notice for the clarification rather than hurriedly issuing orders to the taxpayer concerned.
- It is recommended that suitable instructions be issued by the lawmakers providing an option to the deductee to indicate their TAN in the invoice and further a column/ field may be added in the TDS returns asking the payers to furnish the TAN against each deductee (this should however be an optional column), wherever TAN has been provided by the deductee, at the time of submission/ filing of TDS returns by the payers.
- It is recommended that E-TDS software of the tax department may be amended so that when the TDS returns are processed to generate the TDS certificates, the address should first be automatically picked from the TAN database in respect of the deductee maintained by the tax department and in case no TAN is mentioned in the TDS return, then the address should be picked from the PAN database. This would facilitate generation of the TDS certificate at the TAN address, wherever TAN is provided by the deductee.

- It is recommended that credit for TDS should be allowed to the taxpayer in the year in which such TDS certificate is issued to the taxpayer/ payee or in the year in which TDS credit appears on the online database of the payee without having the requirement to claim tax credit in the year in which corresponding income has been offered to tax. This would address the various problems being faced by the payees today in claiming due credit for TDS.

2.9 Statutory Refund mechanism for excess paid / wrongly paid TDS amounts

Currently there is no specific provision in the statute which governs the procedure to be followed for application of refund for excess paid/ wrong paid TDS amount.

Recommendations

Under Chapter XVII of the Income tax Act, 1961 (dealing with TDS) proper provisions & procedures may be made for refund of excess paid TDS / wrongly paid TDS.

2.10 Penalty for failure to furnish information or furnishing inaccurate information under Section 195

The Finance Act, 2015 has introduced penalty under Section 271-I of the Act in case of failure to furnish information or furnishing of inaccurate information as required to be furnished under Section 195(6) of the Act, to the extent of INR one lakh. It is not clear whether the penalty is qua the payment made or qua the transaction or qua the contractual obligations for a specific financial year.

Recommendations

The same should be clarified in a suitable manner.

2.11 Penalty imposed on deductors for quoting invalid PAN in e-TDS Returns

As per the section 139A(5B) of the Income Tax Act, deductor has to quote the PAN of the deductee in the electronic TDS Return filed and TDS Certificate issued by it. As per section 272B, penalty will be levied on the deductor for failure to comply with the provisions of section 139A.

Recommendations

- It is suggested to make suitable amendments in the Income Tax provisions so that deductors are not penalised under circumstances when the deductees provide wrong/invalid PAN to the deductors
- It is suggested to take a liberal view in levying penalty in case of those deductors who have inadvertently quoted invalid PAN only in very few cases as compared to the total number of deductees and total TDS deposited.

2.12 Year of credit for Tax Deducted at Source (TDS)

Under the current system, credit for TDS is granted to the deductee in the year in which the relevant income is assessable. This system has created a large number of issues. Deductees are struggling for getting credit for the TDS. This has led to creation of wrong demands, avoidable applications for rectifications, wastage of time in follow-up actions by the deductees etc. The Department also has made various genuine attempts to clear this mess but without any substantial result.

Recommendations

It is therefore suggested that Sec. 199 should be amended to grant tax credit in the assessment year immediately following the financial year in which tax has been deducted at source irrespective of whether the same has been paid by the deductor to the Government or not. This will ensure that the tax credit claimed by the taxpayer and tax deducted at source reflected in Form 26AS will match, reducing substantial amount of time wasted in unnecessary rectifications and follow-up of incorrect demands and will avoid punishing the assessee who has no control over the payment of the amount deducted by the deductor.

2.13 Tax Deduction at Source in respect of Payment to Non-residents – Sec. 195(7)

Notwithstanding anything contained in sub-section (1) and sub-section (2), the Board may, by notification in the Official Gazette, specify a class of persons or cases, where the person responsible for paying to a non-resident, not being a company, or to a foreign company, any sum, whether or not chargeable under the provisions of this Act, shall make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of sum chargeable, and upon such determination, tax shall be deducted under sub-section (1) on that proportion of the sum which is so chargeable."

Recommendations

It is suggested that the provisions of sub-section (7) of Sec.195 be suitably amended to empower the Board to notify only certain class of cases where sum payable to a nonresident is chargeable to tax. Empowering the Board to notify even those cases where the sum payable is not chargeable to tax is unnecessary, will lead to harassment, hardships and would also lead to delay in payments and litigation.

3. Return/ Assessment/ Problem Procedures

3.1 Filing of tax returns by non-residents having income from Royalty or Fees for Technical Services (FTS) in India

As per section 206AA, TDS from payment of Royalty & FTS to a non-resident will be as per rates in force i.e. 10%, on fulfilling the prescribed conditions, even if the non-resident does not have PAN in India, if the deductee furnishes the details and the documents as prescribed under Rule 37BC. However, section 139 required a foreign company to file tax returns in India. There is no exemption to foreign company from filing the returns, if their income from India is only of Royalty / FTS. This makes the foreign companies to mandatorily have the Pan in India and do tax compliance of returns filing, though the full tax has been paid by way of TDS.

Recommendations

It is recommended to amend section 115A(5)(a) to provide that a foreign company having only Royalty / FTS income in India, is not required to file tax returns in India.

Further the exemption from return filing which is currently given in relation to interest earned from foreign exchange borrowing should also be extended to interest income in case of foreign borrowings which are denominated in rupee.

3.2 Carry forward of losses in case of belated returns

Currently, losses cannot be carried forward in case of a belated return.

Recommendations

It is suggested that to address the genuine hardship faced by assesses, loss declared in returns filed late under section 139(4) may be allowed to be carry forward.

3.3 Claim made during the assessment proceedings

The tax officers reject the claims made by the taxpayers during the course of the assessment proceedings which are inadvertently omitted to be claimed by the latter in their return of income.

Recommendations

It should be suitably clarified in the Act that the tax officer is duty bound to allow the legitimate claim of the taxpayer made before him during the course of the assessment proceedings and assess the total income/ loss after allowing the said claim.

3.4 Adjustment of Outstanding Demands

Once the demand is raised by the Income Tax Department, Assessing Officer starts pressuring the tax payer for payment of the same, in spite of pending order giving effect giving rise to pending refunds from other orders or rectification applications filed by the tax payer under section 154 of the Act. Section 245 provides that AO should provide intimation in writing before adjusting refund arising out of earlier orders. However this process is not followed by the Revenue Authorities.

Recommendations

It is recommended that before collecting outstanding demand, AO should pass the pending Order Giving Effects and the rectification orders for earlier years.

3.5 - Demand of Income Tax where Assesse has applied for Stay of demand

Currently, in cases where assessments are completed pursuant to direction of DRP and demand is raised, the same is generally payable within 30 days of receipt of demand notice. However, the period available to the tax payer for filing the appeal before the appellate authority is 60 days.

Recommendations

It is suggested to align the period for payment of demand to 60 days instead of 30 Days. This will lead to parity in the number of days for appeal and the demand payment.

3.6 Interest under section 244A

The rate of interest payable to the assessee by the Income Tax Department is only 6% while the interest charged by the department is 12%. Interest is compensatory in nature and not penal. The loss of interest for the Income Tax Department as well as the assessee is same due to non-payment of dues in time. There is a need for equity.

Further the computation of interest on amount due to the assessee is an area of litigation. The assessee is not given the interest on “total amount due” (Tax plus interest thereon) to the assessee as per the last order.

Recommendations

- The rate of interest charged on the assesse as well as the rate of interest payable to the assesse should be the same.
- Interest should be granted to the assesse on amount of refund due (tax plus interest) which is due to the assesse on each order date but not granted by the department in full.

3.7 Delay in remitting refund even after issue of Assessment Order

As per the Act, scrutiny assessments can be completed within 24 months (now 21 months) from the end of the assessment year. When a Company’s Return is selected for scrutiny, practically the excess remitted tax amount is not remitted to the assesse until the assessment is completed. This results in undue hardship to the assesses due to the blockage of working capital in the name of pending assessment. When scrutiny assessment results into demand, the Department issues assessment order along with notice of demand with a specific due date for remittance to exchequer.

Recommendations

In line with notice of demand with specific due date for processing refund due as per return filed by taxpayer /arising out of assessment.

3.8 Time Limit for completion of Appeals

Currently there is no provision for providing time limits for disposal of Appeals at CIT(A) level and by other appellate authorities above it.

Recommendations

- The Act should provide clear time lines for disposal of appeal proceedings at all levels.
- Further internal time limits need to be provided for appointment of councils from the department side (wherever required).
- Application for adjournment on the ground that council needs to be appointed should be curtailed.
- The Government should direct the Appellate authorities / forums to adhere to the suggested timeline without attaching any importance to the value of the demand.

3.9 Authority for Advance Rulings

The Authority for Advance rulings (“AAR”) has a significant backlog of cases; therefore getting an advance ruling within a reasonable time has become extremely difficult.

Certain contrary recent judicial precedents (including of AAR rulings) has created an ambiguity on maintainability of AAR in case of return of income has been filed.

Recommendations

- It should be ensured that the time limit prescribed for passing orders should be adhered to by the AAR.
- Considering that the objective behind AAR is to provide faster dispute resolution mechanics, therefore, a specifc provision be made in law to the effect that mere filing of income tax return should not debar the taxpayer in approaching the AAR.

3.10 Section 68 – Scrutiny examination of funds infused by non–residents

Section 68 of the Act provides that if any sum is found credited in the books of an assesse and the assesse fails to offer an explanation about the nature and source of money or explanation offered is found not to be satisfactory, then such income can be taxed as (unexplained) income in the hands of the assesse. Vide Finance Act 2012, section 68 was amended to provide that the nature and source of any sum credited, as share capital, share premium etc., in the books of a closely held company shall be treated as explained only if the source of funds is also explained by the assesse company in the hands of resident shareholder/ investo.

But the Assessing Officers have been utilizing the amended provision for non – resident investors (of International Repute) also, which have not been covered by the amendment. The non-resident investors are compelled to submit even such information to the AO’s during the course of scrutiny assessment proceedings of Investee Companies, over which AO has no jurisdiction or is totally irrelevant from the assessment perspective.

Additionally, section 56(2)(viib) of the Act provides that share premium received by an unlisted company upon issue of shares in excess of the fair market value shall be treated as income in the hands of such company and subject to tax accordingly. This law is applicable w.e.f. AY 2013-14.

Section 68 can be invoked in a situation wherein nature and source of funds remain unexplained by the recipient and the contributor. If the nature and source of funds stands explained, tax department could then have recourse under section 56(2)(viib) only in situations where difference in technical aspect of valuation exist. However, the converse may not be true i.e. if Section 56(2)(viib) is invoked to tax the difference in technical aspect of valuation, the test of nature and source of funds stand automatically satisfied. The rigors of Section 68 should stop with the investigation into nature and source of funds and not extend to cater to the technical aspect of valuation dealt specifically under section 56(2)(viib) as the Legislature may not have intended to provide two sections i.e. Section 56(2)(viib) and Section 68 to be used interchangeably. Section 68 also cannot be invoked in cases of genuine issue of shares by a company to joint venture partners or financial investors, i.e., private equity, venture capital funds etc.

Recommendations

- It is recommended that the scope and depth of examination / scrutiny with respect to financial affairs of the non-resident investors needs to be restricted. Especially considering that vast reporting requirements are prescribed for non-residents such as Section 195(6) reporting, CbCR, TRC, Liaison Office reporting, requirement to quote PAN u/s. 206AA, reporting u/s. 285BA under FATCA etc.
- Moreover the Government can also clarify that before the Assessing officer can get into further in-depth examination of financial affairs relating to source of funds of a non – resident investor, the same should be allowed only with the pre-approval of CIT / Pr. CIT on the basis of tangible material / evidence brought on record by the AO.
- Provisions of section 56(2)(viib) and section 68 should be suitably amended to provide safeguards against its invocation interchangeably. Only if the tests laid down in section 68 do not stand to be fulfilled, section 68 can be invoked. Furthermore, once section 56(2)(viib) has been invoked, then the test of section 68 should be considered as automatically satisfied.

3.11 Clarity on section 271G penalty

The said section has extended the power to the TPO to levy penalty. As the provision exists today, after the TPO's order the AO has to pass the final assessment order. The AO is also vested with power to levy Penalty on the Final Order. With this the TPOs Authority to levy penalty can be dropped. This will help in reducing multiple appeals arising on account of parallel proceedings carried out by the AO & the TPO Separately.

Recommendations

Clarity should be given as to whether TPO is required to only give a direction to levy penalty to the AO or a parallel penalty proceedings need to be initiated by the TPO.

4. Capital Gains

4.1 Amendment requirement in section 47(xiiib) of the Income-tax Act

Many companies are now converting themselves to LLP. There is a need to popularize the concept of LLP and also in view of the fact that such provision should apply to all cases of revenue neutral conversions from one form of entity to another form of entity.

Recommendations

- There should be no threshold on turnover or on value of assets, to avail the benefit under section 47(xiiib)
- Alternatively, the turnover limit of INR 60 lacs and limit on asset value of INR 5 Crores should be substantially enhanced

4.2 Cost of acquisition with reference to assets acquired under demerger

Section 49(1) refers to certain modes of acquisition wherein the cost would be substituted by the cost of the previous owner. Section 49(1)(iii)(e) covers corporate restructurings such as amalgamations, but does not include a reference to a demerger which is exempt u/s 47(vic).

Recommendations

It is suggested that Section 49(1)(iii)(e) should be amended to include reference to demerger which is exempt under Section 47(vic).

4.3 Business Reorganisation

There are issues on the regulations relating to Buyback Tax under section 115QA.

In numerous M&A deals a part of consideration is deferred and may be contingent on future factors such as the future revenues of the target company. The deferred amount (in part or full) may in reality never be received by the seller owing to milestones not being met. There is no provision in the Act for the tax payer to claim back the excess capital gains tax paid upfront on the higher amount.

In case where the amalgamated foreign company is a parent company of the amalgamating foreign company, the first condition of section 47(via) of the IT Act cannot be complied with, as 25% of the shareholders of amalgamating foreign company (being amalgamated foreign company) will not become shareholders of amalgamated foreign company since the amalgamated foreign company cannot become its own shareholder.

Recommendations

- In case of non-residents, the Buyback Tax may result in double taxation of income, hence, appropriate mechanism for availability of credit to shareholders should be introduced.

- It is recommended that capital gains tax payment should be triggered as and when the contingent consideration is received by the sellers and not on the date of transfer itself.
- It is suggested that such amalgamation, where the amalgamated foreign company is a parent/ holding company of the amalgamating company, should be specifically brought within the purview by section 47(via) of the Income Tax Act.

4.4 Capital Gain on Conversion of Foreign Currency Exchangeable Bonds (FCEB) and other Bonds & Debentures

Sec. 47 (xa) read with Sec. 49(2A) effectively provide that conversion of FCEB in to shares of any company will not give rise to capital gain and for the purpose of computing capital gain arising on sale of such shares at subsequent stage, cost of acquisition shall be taken as the relevant part of cost of FCEB. There is no corresponding provision for taking holding period of the shares from the day of acquisition of the Bonds [FCEB]. Similar difficulty exists in case of conversion of debentures and other bonds in to shares for which also similar provision exists in Sec.47(x).

Recommendations

Therefore, it is suggested that appropriate amendment should be made in Sec. 2(42A) to provide that holding period of such shares should be taken from the date of acquisition of FCEB/debentures / other bonds and not from the date of allotment of shares.

5. Minimum Alternate Tax ('MAT')

5.1 Removal of MAT/ realignment of MAT rates

With the removal of incentives, the scope for taxable income being lower than the book profits has considerably reduced. The only major difference between the book profits and normal taxable income arises on account of depreciation rates. The difference in depreciation also gets reduced if the company is not expanding and a stage is reached when the tax depreciation is lower than the book depreciation.

On the other hand, the MAT rate has gone up to as high as 21.34%, which can even be considered as closer to the corporate tax rate of 34.61% on taxable profits.

Recommendations

- At the outset, there is a need for a fundamental rethink on MAT at a conceptual level. MAT appears to be inconsistent with the current tax policy of low corporate tax rate of 25% and withdrawal of corporate tax incentives. MAT may therefore be withdrawn or significantly modified at the earliest.
- Even where it is decided to continue the MAT levy, following may be considered:
- A roadmap may be announced for reduction in MAT rates to 7.5% of book profit (from current rate of 18.5%) over a period of five years.
- MAT may be made applicable to only those entities which avail specified tax incentives in the normal computation (similar to section 115BA introduced by Finance Bill, 2016 which

provides for 25% corporate tax rate to new domestic manufacturing companies who are willing to sacrifice specified tax incentives).

- Alternatively, MAT may be levied in the form of Alternate Minimum Tax (AMT) currently applicable in case of non-corporates which is a simple basis involving add-back of tax incentives in the computation of total income and allowance of depreciation at normal rates.
- MAT credit should be allowed to be carried forward indefinitely as against the current law where the MAT credit is allowed to be carried forward for 10 years.

5.2 Recommendation on MAT- IndAS Committee Report

The Government has constituted Accounting Standards Committee, a Committee to suggest amendments to MAT provisions under section 115JB in view of transition to Ind-AS as notified by Ministry of Corporate Affairs (MCA). The Committee is yet to bring out its final report.

In its first interim report dated 18 March 2016, the Committee had inter alia recommended that items which are directly transferred to Retained Earnings on first time adoption (FTA) of Ind-AS and are not reclassified to Profit & Loss Account (P&L) in future should be picked up for MAT in the first year of Ind-AS adoption.

To address concerns raised by stakeholders that upfront MAT levy on FTA adjustments recorded in Retained Earnings may cause significant hardship resulting in MAT levy on unrealized gains/losses, the Committee issued second interim report dated 23 July 2016 which recommends the following along with other Recommendation

1. The FTA adjustments in Retained Earnings in respect of Property, Plant & Equipment (PPE) and Intangible Assets be ignored for MAT computation in first year but picked up in year of realization/disposal/retirement of such assets ; and
2. The FTA adjustments in Retained Earnings in respect of other items like lease equalization reserve, financial instruments fair valued through P&L, etc. be spread over three years for MAT computation, starting from the first year of Ind-AS adoption.

Recommendations

- In regard to the Committee's Recommendation to spread over MAT impact of FTA adjustment in respect of lease equalization over 3 years, we submit that three year period is very short considering that the lease is usually for long term. In these cases, higher MAT credit will arise due to upfront levy of taxes on notional gains and the companies may be unable to utilise MAT credit to set off against normal tax liability. Hence it should be included in the book profits over the unexpired lease period.
- In line with the Recommendation for Fair Valuation of investments in equity instruments through Other Comprehensive Income (OCI), it should be included in the book profits at the time of realization.

5.3 MAT on exempt income

MAT is payable even on those incomes that are exempt such as sale of listed equity shares under section 10(38) and incomes that are not taxable under regular provisions such as Capital Receipts. This results into accumulation of MAT credit and blockage of funds for businesses.

Recommendations

It is submitted that levy of MAT should be restricted to those incomes that are taxable under regular provisions and incomes that are exempt under normal provisions such as LTCG on sale of listed equity shares or incomes that are not taxable such as Capital Receipts, should be kept out of the ambit of MAT.

5.4 MAT on foreign dividend

The Finance Act 2011 introduced a new Section 115BBD in the Act which provided that dividend paid by a foreign company to an Indian company, in which the Indian company holds 26% or more of the equity share capital, would be taxed in the hands of the Indian company at the rate of 15% (plus applicable surcharge and cess).

Further, in order to remove the cascading effect in respect of dividend received by an Indian company from a foreign company, an amendment was introduced in Section 115-O of the Act. As per the said amendment, where an Indian company pays tax on dividend received from a foreign company under Section 115BBD and thereafter, such Indian company distributes dividend to its shareholder, then the dividend on which tax has already been paid by the Indian company (i.e. under Section 115BBD) shall be reduced from the amount of dividend on which Dividend Distribution Tax ('DDT') is payable by the Indian company.

Domestic dividend is specifically exempt from the applicability of MAT provisions under Section 115JB. However, similar exemption is not available under Section 115JB in case of foreign dividend which suffers tax under section 115BBD.

The consequence of this would be that Indian companies will end up paying an effective tax of 21.34% on foreign dividend due to applicability of MAT provisions as against the effective rate of 17.30% stipulated under the provisions of section 115BBD. Further, since the Indian companies have made outbound investments through investment companies which generally do not have any other source of income, the companies would not be able to utilize the MAT credit.

The higher rate of tax under MAT provisions would remain a disincentive for repatriating the funds to India and partially defeats the very purpose for which section 115BBD was introduced.

Recommendations

It is recommended that just like domestic dividend, foreign dividend should also be exempt from MAT.

5.5 Exemption of SEZ profits from MAT calculation

Finance Act, 2011 has widened the scope of MAT by bringing SEZ units under the ambit of MAT, thereby significantly diluting benefits offered under the popular SEZ Scheme. Now, tax is also required to be paid on profits of SEZ units, though these were envisaged to be tax free when the provision was enacted.

Recommendations

It is recommended to remove SEZ profit from MAT calculation, thereby, reducing taxation impact on the Companies and leaving profits with the Companies for further investment. This will provide a significant relief to exporters who are already finding it difficult to sell their products in the wake of a struggling global economy.

5.6 Exemption of Profits earned by startups from MAT calculation

Finance Act, 2016 by including section 80-IAC in the Act has provided a deduction of 100 per cent of the profits and gains derived by an eligible start-up from a business by involving innovation development, deployment or commercialization of new products, processes or services driven b technology or intellectual property. However, no corresponding amendment has been made in the provisions of MAT.

Recommendations

It is recommended to remove profits earned by start-ups from MAT calculation, as this would hamper the aim of the government to provide an impetus to start-ups and facilitate their growth in the initial phase of their business.

5.7 Carry forward of MAT credit by amalgamated company

There is no clarity under the Act, whether on amalgamation/merger of companies, MAT credit available to amalgamating company can be availed by amalgamated company post amalgamation.

Recommendations

Specific provisions should be introduced for carry forward of MAT credit by the amalgamated company.

5.8 Rationalization of MAT provisions for infrastructure companies

The benefit available to the infrastructure companies and other entities eligible for deduction under Chapter VI-A of the Act, gets neutralized since the companies are required to pay MAT on their book profits.

In order to promote investments in the infrastructure sector, the Government has provided tax holiday u/s 80-IA. However, this benefit is substantially diluted due to the MAT to be paid by the

Companies. Though MAT credit can be accumulated, there is a restriction on the quantum & period of its utilization.

Recommendations

To attract more and more investment in power and infrastructure sector, such infrastructure companies should be kept outside levy of MAT.

6. Provisions in respects of Units established in Special Economic Zones

Under section 10AA of the Income tax Act, 1961, an SEZ Unit is eligible for a deduction (for a period of 5 consecutive assessment years) of 50% of SEZ Reinvestment Reserve, created by the assessee after expiration of 10 year tax holiday period. Creation of a re-investment reserve hampers the ability of an SEZ unit, especially ones in the manufacturing process. Presently, SEZ Units need to commence operations/ manufacturing on or before 31st March 2020 to claim tax benefit.

Further, Companies operating in capital goods, infrastructure / manufacturing industries have made huge investments to create local job opportunities as well as to boost domestic industry. Tax holiday period has been provided to, inter alia, enable them to recover their investments faster. Due to subdued market performance, they have not been able to recover their investments due to lower than anticipated profits and most of the companies have either exhausted the period of 5 years or are close to exhausting the said period.

Recommendations

- Sunset clause for units in SEZ should be removed. Time limit for commencement of operations for SEZ units should be extended beyond 2020 to encourage exports and generate employment.
- In line with the Government of India's 'Make in India' initiative, it is recommended that the provision of creation of SEZ Reinvestment Reserve be done away with for SEZ Units engaged in manufacturing activities.
- It is recommended to enhance the 100% holiday limit to 10 years so that the Companies can recover the investment faster and also provide additional funds for expansion / modernisation as well as job creation, thereby contributing to the welfare of the country.

7. Transfer Pricing/ International Tax

7.1 Transfer pricing requirement for Non-resident

At present non-resident assesse are required to obtain a Transfer Pricing Audit report U/S 92E of the Income Tax Act. The non-resident assesses are also required to maintain and justify the arm's length value of transactions for all transactions taken with resident (Indian) assesse.

When transaction is once assessed under transfer pricing regulations, reported and assessed for resident assesse, it is duplication of work to assess the same transaction under transfer pricing regulations for non-resident assesse.

Recommendations

The non-resident assesse should be exempted from Transfer Pricing provisions, if the same transactions are declared by resident (Indian) assesses.

7.2 Narrow interpretation of Rule 10B(1)(e)(iii)

- If the Transactional Net Margin Method (TNMM) is adopted then under Rule 10B(1)(e)(iii) an assessee is eligible for adjustments to be made to the profit margins so as to enable the assessee to make comparison with the comparable margins of the comparable companies.
- Rule 10B(1)(e) states as under: transactional net margin method, by which,—
  - (i) The net profit margin realized by the enterprise from an international transaction or a specified domestic transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;
  - (ii) The net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;
  - (iii) The net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market"
- Practically adjustment in the comparable uncontrolled transaction is not possible as the details of the comparable entities available in the public domain are less. The TPO takes stricter interpretation and no adjustment is granted if the assessee wants to adjust its own margins to make the comparison more meaning full.

Recommendations

Considering the intention and spirit of the law, it is suggested that under sub-clause (iii) of Rule 10B(1)(e) the adjustment should also include a reference to the net profit margin referred to in sub clause (i) to clear the ambiguity in interpretation of the law.

7.3 Contradiction between Customs and Transfer Pricing

Customs and Transfer Pricing are based on arm's length principle, whose objective is to ensure that taxable values of imports are correct and taxes are paid appropriately on arm's length value. However, intention under both the regulations drives in opposite directions i.e. the Customs Cell would prefer to increase the import value of goods to increase tax while the tax department would prefer to reduce purchase price of goods to increase taxable profits. The diverse end-results create ambiguity and uncertainty in pricing.

Recommendations

There is a need for harmonization between these two conflicting regulations. Guidance may be provided for acceptability of transfer prices by one arm of the Government, in case the other arm had accepted the price at arm's length.

7.4 Intra-group services

Intra-group services (also referred to as management services) are collection of services provided by any company of a MNC group to other affiliates (on a centralized basis) for a service fee, in its endeavour to improve synergies and leverage experience, knowledge and in-depth understanding of the company in relation to the industry best practices, market perception, vendor expectation, etc. However, the Indian transfer pricing regulations do not provide any explicit guidance on the transfer pricing treatment of intra-group services.

It is increasingly becoming a matter of concern as to how these services are audited for transfer pricing purposes. Most cases suffer with the extreme views taken by the tax office holding that such services have not resulted in any benefit to the taxpayer, and therefore, the arm's length price is determined to be nil.

Recommendations

- The Government should provide examples of services that could be considered as deemed to be shareholder services and therefore, should not be charged for by the group.
- It is suggested to provide a definition of cost base that may be allocated for common group services.
- It is suggested to provide guidance as well as detailed list of acceptable allocation keys for common group services.
- It is recommended to prescribe a format of third party certification that should be acceptable by the tax office to establish the appropriateness of the cost base and appropriateness of allocation for common group services.
- It is suggested to provide an acceptable range of mark-ups on costs vis-à-vis support services availed from group companies.
- It is suggested to provide an exhaustive list of documents acceptable to substantiate receipt of services by the Indian affiliate.
- It is recommended to provide guidance towards documents to be maintained for substantiation/ quantification of benefits received in India from the intra-Group services, as most of these services are in the nature of support services.

7.5 Comparison of tested transactions with controlled transactions

In many instances, the tax authorities have taken an approach of determining the arm's length price by comparing the tested transaction with another controlled transaction (i.e. transaction undertaken between 2 entities of the same MNC). This is clearly against the basic principles of determining the arm's length price. The Indian judicial precedents also do not give a clear view on the issue.

Recommendations

There needs to be guidance not to do a comparison with controlled transaction which will avoid needless litigation on this issue and would also be in line with the Indian transfer pricing legislation as well as the OECD principles.

7.6 Safe Harbor Rules

Safe Harbor Rules provide for circumstances in which a certain category of taxpayers can follow a simple set of rules under which transfer prices are automatically accepted by the revenue authorities. Essentially, safe harbor provisions offer benefits to taxpayers and tax administrators in the form of compliance relief, administrative simplicity and certainty. However, these rules have not been extended to banking transactions.

Recommendations

- Banking related transactions like FCY loans, and FX transactions are quite voluminous and homogeneous across Banks. Considering its voluminous data, the Banking sector requires safe Harbour Rules which will provide them certainty and at the same time do away with the need to maintain contemporaneous documentation.
- Further, the Rules give the benefit of safe harbour only to the 'eligible assessee' which has opted to be governed by the Rules for its 'eligible transaction'. As the 'eligible transactions' have corresponding tax impact on the associated enterprises, it is recommended that such safe harbour rules should also be accepted by the income-tax authorities for such associated enterprises as otherwise it will result into double taxation of the same income in hands of two enterprises and will not meet the intended objective.

7.7 Penalty for non-furnishing of Country by Country report

Section 271GB of the Act prescribes stringent penalty for non-furnishing of Country by Country (CbC) report as prescribed in section 286 by the due date. The deadline for filing the CbC report in India is 30 November 2017 for first covered FY 2016-17 i.e. only 8 months post the end of FY 2016-17 have been provided to the taxpayers to prepare and furnish the CbC report.

Recommendations

There is a need to rationalise penalty for the filing requirements in the first year at least as even OECD's guidelines under BEPS Action Plan 13 provide for a 12 month period in the first year of filing. Accordingly, partial relief from the stringent penalties should be provided for the first year of CbC report filing, such that penalty is applicable for CbC report filed on or after 1 April 2018.

7.8 - Introduction of Master File requirement but no clarity on its threshold

Though the Memorandum to Finance Bill mentions about Master File requirements and provides that detailed nature of information would be required to be furnished in the Master File, detailed provisions or rules for Master File have not been prescribed. Further no threshold for preparation and filing of Master File has been prescribed

It would be an additional burden on the taxpayers requiring investment of lot of time, efforts and resources to compile the information required in Master File (as detailed in OECD BEPS guidelines). Further without any knowledge about what would be the threshold of master file requirement, taxpayers are unable to plan their affairs in advance.

Recommendations

Draft rules should be released for public consultation (giving adequate time) detailing Master File requirements and applicable threshold, which should be considerably higher.

7.9 Clarity on adoption of Local File

There is no clarity on whether the OECD Recommendation on Local file would be adopted as is in the Indian TP regulations or not and whether there would be any threshold for the same. This would create uncertainty for taxpayers.

Recommendations

Draft rules should be released for public consultation (giving adequate time) detailing Local File requirements and applicable threshold, which should be higher than the currently prescribed threshold for TP documentation i.e. INR 1 crore.

7.10 Indirect Transfer of assets

The Income Tax Act, 1961 through the Finance Act, 2012, provides that share or interest in a foreign company or entity that derives its value 'substantially' from assets located in India would be deemed to be situated in India. As such, a completely offshore transfer of such foreign shares would be brought within the Indian tax net.

In this regard, additional measures are required to ensure that the law is not adversely contrary to the global practices.

Recommendations

- In addition to small shareholder exemption, exemption should also be provided for (a) transfer of shares listed outside India (b) income on Offshore Derivative Instruments/ Participatory notes (c) all forms of intra-group restructuring outside India (presently the provisions cover only amalgamation and demergers).
- It is recommended that suitable exemption should be provided to avoid multi taxation that may arise in case of multi-tier structure.
- The acquisition of rights/control and management is by virtue of additional issue of shares to either existing or new shareholders (could be rights shares issuance, or fresh shares issued to a new shareholder, etc.). It is recommended that such cases should not be covered under the

definition of 'capital asset' and 'property' (see the discussion under Para 3.3 of the Expert Committee Report).

- The valuation rules also remain silent on what criteria should be used when determining whether a particular methodology is internationally accepted or not. This may leave otherwise accurate FMV determinations, open to litigation.
- In view of the impracticality of tracking and reporting of all transactions, it should be clarified that the reporting be restricted to those transactions (a) whose income is covered within the ambit of indirect transfers which are deemed to accrue or arise in India. (b) reporting entity would be the foreign transferor entity.
- Further, the Indian concerns are required to furnish information or documents under section 285A of the Income Tax Act r.w. Rule 114DB and the same is too onerous for the Indian counterparts. Accordingly, the requirement of reporting of transactions by the Indian concerns should be relaxed, since the Indian concern may not even be aware of a change in shareholding coupled with various other impossibilities.
- Clarification with respect to cost of acquisition to be taken for computation of income under the head Income from Capital Gains especially in case intermediary foreign company[1] has made investment in Indian Company[2] by acquiring loans or borrowings.
- To address the aforesaid issues, it is suggested that the clarificatory circular be rolled out for public consultation.

7.11 Interest payment by India branch to Head Office

Finance Act 2015 amended the law that the payment of interest by the India branch to the Head Office or any branch outside India shall be chargeable to tax in India and liable withholding tax in India. As Head Office and branch(es) are part of the same legal entity, the taxability of the intra-group interest income would be against the principle of mutuality.

Recommendations

It is recommended that the amendment regarding taxability of interest paid by India branch to Head Office should be withdrawn.

7.12 Indian branch of foreign company

As per Section 115A, income (royalty and fees for technical services) earned by foreign person gets taxed at concessional rate when the payment is made by an Indian concern.

Recommendations

In order to provide level playing field, Indian branch of foreign company should be considered as "Indian concern" for the purposes of this section.

[1] whoes shares are sold
[2] being an underlying asset

7.13 Rollback of APA

The CBDT introduced the rollback rules under the APA program on 14 March 2015. There were some ambiguities about the implementation of the rollback rules, and therefore, CBDT issued Frequently Asked Questions (FAQs) clarifying certain issues.

The international transaction proposed to be covered under the rollback is to be the same as covered under the main APA. The term 'same international transaction' implies that the transaction in the rollback year has to be of the same nature and undertaken with the same AEs, as proposed to be undertaken in the future years and in respect of which APA has been reached.

Recommendations

- It is recommended that this provision should be relaxed to the extent that the taxpayers with similar transactions with no substantial changes in the functional, asset and risk profile should be allowed to take benefit of this provision. Further, if the same/ similar transaction is undertaken with another AE, the benefit of rollback should be provided. The provision should be made applicable to similar nature of transactions and with different AEs.
- Further, the rules provide that if the applicant does not carry out any actions prescribed for any of the rollback years, the entire APA shall be cancelled. It is recommended that this provision should be relaxed and should not result in the cancellation of the entire APA.

7.14 Requirement for non-residents having no place of business in India to comply with TDS obligations

The Finance Act, 2012 extended the obligation to withhold taxes to non-residents irrespective of whether the non-resident has— (i) a residence or place of business or business connection in India; or (ii) any other presence in any manner whatsoever in India." The aforesaid amendment was introduced with retrospective effect from 1st April 1962.

The amendment has resulted in a significant expansion in the scope of withholding provisions under the Act and covers all non-residents, regardless of their presence/connection with India resulting into extra-territorial taxation.

Recommendations

It is recommended that applicable rules of statutory interpretation read with Section 1(2) of the Act, which indicate Section 195 of the Act as currently in force, should not apply to non-residents unless there is some territorial nexus with India as explained by Hon'ble Supreme Court in the case of GVK Industries [2011] 332 ITR 30 (SC).

7.15 TDS from payments to Non-residents having Indian branch/ fixed place PE

The corporate tax rate for non-resident companies being 40% (plus surcharge and education cess) results in requiring a non-resident company to file return of income to claim refund of excess taxes deducted. This creates cash flow issues for the non-resident company having operations through an Indian branch unviable, when compared with its Indian counterparts.

Recommendations

It is recommended that payments which are in the nature of business income of non-residents having an India branch office or 'a place of business within India' should be subject to similar TDS requirements as in case of payments to domestic companies.

7.16 Removal of cascading effect of Dividend Distribution Tax (DDT) in a multi-tier structure

Vide Finance Act 2012 the benefit of removal of cascading effect of DDT was extended to a multi-tier corporate structure where multiple corporate entities are involved. This was sought to be done by simultaneous amendments in sub-section (1A) of Section 115O at two places – firstly, by removing the restrictive condition in clause (c) of sub-section (1A) that the domestic company should not be a subsidiary of any other company and secondly, by providing that the tax base for DDT is to be reduced by the amount of dividend received from its subsidiary if such subsidiary has paid the tax which is payable on such dividend.

This was introduced in contradistinction to the expression which existed in the pre-amended section i.e. 'the subsidiary has paid the tax under this section on such dividend. Thus, while the pre-amended clause mandated the actual payment of DDT by the subsidiary but the amended clause only mandates that the subsidiary should have paid the tax which is payable. Thus, it is evident that the intent of bringing in simultaneous amendments in sub-section (1A) was to extend the benefit of DDT paid by the bottom most subsidiary company, to the top most holding company, in a multi-tier holding structure and avoid the cascading of DDT.

While the amendments brought about by Finance Act, 2012 aims and intends to remove the cascading effect of DDT in a multi-tier corporate structure on absolute basis i.e. at every tier but the Revenue may raise doubts and may attempt to restrict the benefit in a multi-tier corporate structure effectively upto two-levels only by placing reliance on the Proviso to sub-section (1A).

Further, it is evident that the principle applied for removing the cascading effect of DDT is 'tax should be paid once on the same income'. But this has been applied in a limited context as when a company which holds less than 50% shares in another company, receives and pays dividend has to pay DDT on both the receipt and payment separately, though to the extent of receipt it is same dividend (income) only.

Recommendations

It is recommended that an appropriate explanation be inserted clarifying that the benefit of DDT paid by a subsidiary company is available at each company level in a multi-tier corporate structure so as to avoid the cascading impact of DDT.

It is recommended that the existing provision should be amended to provide uniform and simplified taxation regime so as to provide for the DDT credit irrespective of the stipulating condition that one company should hold more than 50% of the share capital of the company declaring, distributing or paying the dividend.

7.17 Section 9(1)(i) – Transfer of minority stake within the same group

The Finance Act 2012, amended Section 9(1)(i) of the Act, retrospectively w.e.f. 01 April 1962 to insert an explanation that seeks to clarify that the situs of capital assets being shares / interests in foreign entity, directly or indirectly deriving value substantially from the assets located in India shall be deemed to be in India. Further vide amendments by Finance Act 2015, an Explanation 7 was inserted which provides that if the transferor does not hold the right of management or control of such company; nor holds the share capital or voting power in excess of 50% of the total capital or voting power of the foreign company, the deeming provision shall not apply.

Presently under Section 47 of the Act, the transactions of transfer of capital assets between holding and subsidiary company are not regarded as transfer and consequently no capital gains tax is levied. Further in recent rulings, High Courts have held in context of section 79 that it will not be triggered where there is a change in shareholding and where 51% of the shares or voting power is beneficially held by the same group of shareholders.

In both the above scenarios, it can be seen that in case the control of the asset ultimately lies in the hands of same controlling group then the same is not regarded as a transfer.

Recommendations

It is recommended that Explanation 6 to Section 9(1)(i) should provide relaxation in case of transfer of minority stakes which does not result into transfer of control of underlying Indian asset and also the transfer of stake within the same group thereby permitting group reorganization.

7.18 Deputation of employees

Increasing globalisation has resulted in fast growing mobilization of labour across various countries. Typically, the company deputing the personnel (home employer) initially pays the salary and other costs on behalf of the company to which such personnel are deputed (host company), which are thereafter reimbursed by the host company. The issue which had cropped up before the Indian tax authorities and courts due to the increasing deputation agreements being entered cross border was whether such reimbursements made by the host company in India to an overseas entity (home employer) towards salary and other costs in relation to the deputed employees should be taxable in India as being payment in the nature of fees for technical services. Further, the main issue in such arrangements is whether the deputed employee is rendering services in India on behalf of the home employer resulting in FTS taxation or a taxable presence for home employer in India.

Recommendations

In order to put an end to this uncertainty and litigation, it is recommended that guidance should be provided on factors relevant to determine whether deputation of employees results into provision of services by the employee on behalf of the home employer. Tax administrations in various jurisdictions have provided similar guidelines e.g. Guidelines of Canada Revenue Agency on Employment, Denmark's revenue authority (SKAT) guide on "international hiring out of labour" dated 24 October 2013, China SAT's Announcement No.19, 2013 etc.

7.19 Tax Residency Certificate (TRC)

The Finance Act, 2012 had provided that in order to be eligible to claim relief under the tax treaty, a taxpayer is required to produce a Tax Residency Certificate (TRC) issued by the Government of the respective country or the specified territory in which such taxpayer is resident, containing certain prescribed particulars. Obtaining a TRC certificate may also be a time consuming/difficult process. TRC requirement increases the administrative difficulty for non-residents, especially from the perspective of non-residents having very few/limited transactions connected to India.

As per the new Rule an Indian resident who wishes to obtain TRC from Indian income tax authorities, is required to make an application in Form No. 10FA to the tax officer, containing prescribed details. However, no time limit for issue of TRC is specified from the date of application by the assessee. Furthermore, the issue of TRC in Form No. 10FB has been left to the discretion of satisfaction of the tax officer, without providing a substantive definition for satisfaction in this regard.

Also, it has not been specified as to who shall sign Form 10F.

Recommendations

Despite being an additional compliance, TRC is useful in many cases to claim treaty benefits and avoid unnecessary rejection from tax authorities. Significance of TRC is upheld by the Hon'ble SC in the case of Azadi Bachao Andolan (263 ITR 706) and various Courts have upheld granting of treaty benefits e.g. under the India-Mauritius treaty, based on the TRC.

- Without prejudice, even if the requirement to obtain TRC must stay, it is recommended that the TRC shall be made mandatory only for cases where the total payment to a non-resident exceeds Rs. 1 crore in a financial year and it should be clarified that in other cases, treaty benefits will not be denied based on residency alone.
- Further, it should be clarified who is authorized to sign the form 10F.

7.20 Foreign tax credit

As per section 40(a)(ii) taxes paid are not deductible. This section defines taxes to include sum eligible for relief u/s 90 or 91. Further, section 91(1) provides that the relief shall be equal to Indian taxes payable on the income that has suffered taxation. Similarly, most of the DTAAs restrict the relief in India, to the extent of Indian taxes payable on such doubly taxed income. Reading both sections together, if the taxes paid in foreign country are in excess of the relief available u/s 91(1), the deductibility of the surplus is not clear in the law.

As per recent FTC Rules, FTC shall be the aggregate of amounts of credit computed separately for each source of income arising from a particular country or specified territory.

Recommendations

- It is suggested to add explanation to section 40(a)(ii) that the surplus of foreign taxes paid, over the relief available u/s 90 or 91, shall be allowed as deduction while computing taxable income.
- It is suggested to specify procedure for income calculation based on Profit/Sales ratio as per financials.

8. Other Provisions

8.1 Income Computation and Disclosure Standards (ICDS)

ICDS is effective from F.Y. 2016-17. These standards are applicable to the computation of income under the heads "Profits and gains of business or profession" and "Income from other sources". The preamble states that if there is any conflict between the provisions of the Act and the ICDS, the latter will prevail. It is pertinent to note that taxpayers are already grappling with regulatory changes of the Companies Act, 2013, Ind-AS, BEPS Action Plans and the proposed GST.

Recommendations

- At the outset, ICDS should be scrapped.
- Subject to the above, it should be clarified that test of 'reasonable certainty of ultimate collection' applies not only to revenue from sale of goods but also to interest and royalty income to avoid any ambiguity. There should be no compulsion to recognize interest income which is doubtful of recovery.
- It is recommended to clarify that ICDS will not override the existing jurisprudence and accordingly, interest income will be recognized on accrual basis.
- Further, clarity is required on application of ICDS in cases falling under the DTAA, where interest/ royalty is taxable on "receipt basis".
- Since the Act does not recognise the concept of Deferred Revenue Expenditure, it is recommended to clarify that the post-trial run expenditure should be written off in full in year of incurrence.
- ICDS should align with judicially settled position under the Act and recognize differences on MTM basis.
- It is recommended to clarify that exchange fluctuation loss on borrowings for acquisition of local assets (from India) is allowable as revenue expenditure.
- Since there is material departure from methodology of capitalization as per ICAI AS-16, CBDT should provide guidance with the help of illustrations on how general borrowing cost should be capitalized under ICDS IX.

8.2 Place of Effective Management (PoEM)

Finance Act 2016 deferred the implementation of POEM based on the residence test by one year and to apply from the Financial Year 2016-17. Transaction pertaining to period starting from 01-04-2016 will be evaluated as per the provisions of PoEM. The government is to notify the income computation mechanism in case of a foreign company having a POEM in India.

Recommendations

- It should be clarified that decisions which affect the fundamental existence of the Company itself or the rights of the shareholders and which are to be taken by shareholders should not be relevant in determining PoEM. Non-binding guidance provided by shareholder / Parent company for providing guidance to group entities should not be a conclusive factor for determining PoEM.
- Income in the nature of royalty, interest or similar income should not be considered as passive income if it is arising out of active conduct of trade or business of the assessee.
- For the purpose of determining the characterization of income, regard should be had to the characterization of such income in the books of account of the company and not to the income tax definition.
- Clarification should be provided that gross income as per books of accounts is to be considered for determining the total income and passive income under the 50% criteria.
- Income from the transactions of purchase and sale of goods even with associated enterprise should not be considered as passive income.
- Alternatively, for avoidance of doubt, it should be clarified that if either purchase or sale of goods is from / to unrelated entities, then it will not be considered as passive income. The clarification will make it abundantly clear that income earned by companies which may be purchasing from third party and selling to group companies or vice versa is not passive income.
- Holding companies having investment in “Active Companies” in the same jurisdiction should also be considered as “Active Companies”. Accordingly, dividend or capital gains derived by such holding companies from active companies should not be considered as passive income.
- It is recommended that meaning of term “management and commercial decisions” should be clarified to aid the understanding of both the taxpayers and the tax authority.
- PoEM should not be considered to be in India in case the foreign company is incorporated in a jurisdiction which is not a ‘low tax jurisdiction’. Low tax jurisdiction may be defined as per the Controlled Foreign Company provisions under draft Direct Taxes Code Bill, 2010 or a jurisdiction which has a base tax rate of less than 15% or 20%.
- The Guidelines should further provide a safe harbour provision for companies listed outside India on any of the recognized stock exchanges.
- The Guidelines on PoEM should clearly provide a mechanism for claiming FTC in case a foreign company creates a PoEM in India.
- A mechanism should be provided to avoid double taxation of the same income in the hands of different companies creating PoEM in India in a multi-layer structure. Further, dividends from companies whose PoEM is held to be in India may also be subject to dividend taxation under section 115BBD of the ITA.
- The transactions between the foreign company (PoEM in India) and the Indian company should not be considered to be within the ambit of Specified Domestic Transactions under Indian transfer pricing regulations. Transactions between the foreign company (PoEM in India) and

its group companies outside India should also not be considered within the ambit of International Transactions under Indian transfer pricing regulations. In any case, if the Transfer pricing compliances are to be undertaken for transactions between the foreign company (PoEM in India) and its group companies (within or outside India), it should be applicable only once the status of the foreign company is established as having PoEM in India.

- In the absence of guidelines, the implementation of POEM should be deferred to next financial year in order to facilitate a smooth implementation and compliance with the POEM provisions.

8.3 General Anti Avoidance Rules (GAAR)

The Government has received inputs from the stakeholders on GAAR and is yet to come out with the final guidelines

Recommendations

- The tax administration may identify prominent methodologies of tax abuse which are the areas of concern for tax administration. A specific anti-avoidance rule may be introduced to control such abuse instead of open ended GAAR.
- Arrangements covered under existing rules should be assessed as per such specific provisions and there should not be overlapping with the provisions of GAAR. Balance Impermissible Avoidance Arrangements (IAA) may be assessed under GAAR.
- It is submitted that primacy of Tax Treaty over GAAR should be maintained and the arrangement entered after compliance of the conditions spelt out in treaty should be kept out of the provisions of the GAAR.
- All arrangements entered into prior to the date of introduction of GAAR should be grandfathered.
- The term “tax benefit” should be explained by giving illustrations.
- Also it needs to clarified that grandfathering will protect the allotment of bonus shares/right share, dividend etc. from grandfathered investment. Also shares received upon tax neutral merger/demerger/re-organisation in lieu of grandfathered investment should enjoy the same immunity.
- It is submitted that a specific and explicit clarification may be provided that the onus should be on the tax authorities to demonstrate that the main purpose of an arrangement is to obtain tax benefit.
- To avoid frivolous cases and reduce the administrative burden on taxpayers and the Income Tax Department and to avoid large scale litigation, a reasonable threshold of about Rs.50 Crores should be provided in the Act itself (as against currently provided threshold of INR 3 crores in Rules).
- If the above Recommendation is not accepted, it is submitted that threshold should be provided at participant level instead of arrangement level, comprising of all the parties. The invocation of GAAR for a particular year per se should not lead to the reopening of cases that belong to the earlier years.

- If there is a case of reopening of assessment, such reopening will be guided by existing statutory provisions and judicial precedents.
- Specific provision should be provided to the effect that where an arrangement is treated as an impermissible avoidance arrangement, to ensure that the same income is not taxed twice in the hands of the same taxpayer in the same year or in different assessment years.
- When any transaction/arrangement is disregarded in full or part then consequential adjustment should be allowed in case of other parties to the said transaction so that there is no double taxation on the "disregarded component".
- Section 144BA(1&7) provides that the term of the approving panel shall ordinarily be for one year and may be extended up to a period of 3 years. This is unjustified as one cannot expect an Approving Panel to change every year and to do justice in one year. In fact, considering the complexities involved, the minimum term for such Approving Panel should be 3 Years and it should be extendable up to 5 Years.

9. Personal Taxation

9.1 Revision of basic exemption limit for individual Tax Payers

Considering the steep rise in cost of living due to inflation it is suggested that basic limit for exemption and other income slabs should be enhanced to give benefit to low income group. The income trigger for peak rate in other countries is significantly higher.

The Parliamentary Standing Committee on Finance (PSC) in its Report on the Direct Taxes Code Bill 2010 (DTC Bill) has appropriately recommended the following revised tax slabs for individual taxpayers.

Income Slab (Amount in INR)	**Tax Rate**
0-3 Lakhs	NIL
3-10 Lakhs	10%
10-20 Lakhs	20%
Beyond 20 Lakhs	30%

Recommendations

- There is need to revise the tax slabs as appropriate.
- Further, the highest tax rate should be reduced to 25%.

9.2 Amendment in definition of 'Short-term capital asset' - Section 2(42A)

Expats who become tax resident in India who will now have to pay Short Term capital gains on their "home" portfolios if held for less than 36 months due to note that only recognizes stock exchanges "in India" to qualify for a 12 month holding period.

(42A) "short-term capital asset" means a capital asset held by an assesse for not more than thirty-six months immediately preceding the date of its transfer:

Provided that in the case of 21[a security (other than a unit) listed in a recognized stock exchange in India] or a unit of the Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963) or 22[a unit of an equity oriented fund] or a zero coupon bond, the provisions of this clause shall have effect as if for the words "thirty-six months", the words "twelve months" had been substituted:

23[Provided further that in case of a share of a company (not being a share listed in a recognised stock exchange) or a unit of a Mutual Fund specified under clause (23D) of section 10, which is transferred during the period beginning on the 1st day of April, 2014 and ending on the 10th day of July, 2014, the provisions of this clause shall have effect as if for the words "thirty-six months", the words "twelve months" had been substituted.]

The primary notes are as follows:

1. Any Capital asset held by an assessee to be a short term capital gains, the period of holding should not be more than 36 months.

2. Only case of those securities which are listed in Stock exchanges in India the period of holding to be less than 12 months to constitute as Short Term capital gains.

Recommendations

Restore definition as existed prior to July 2014 i.e.: 12 months.

9.3 Revival of Standard Deduction

A standard deduction was earlier available to the salaried individuals from their taxable salary income. However, the same was abolished with effect from AY 2006-07. On the other hand, business expenses continued to remain as permissible deductions from taxable business income. It has to be appreciated that standard deduction is not a personal allowance and used to be given as a lump sum for meeting employment related expenses.

Recommendations

The standard deduction for salaried employees should be reinstated to at least INR 100,000 to ease the tax burden of the employees and keeping in mind the rate of inflation and purchasing power of the salaried individual, which is dependent on salary available for disbursement.

9.4 Deduction under section 80C

Currently, deduction under section 80C of the Act is restricted to Rs 150,000. Further, contribution to provident fund has been included in the deduction under section 80C limit.

Equity Linked Savings Scheme (ELSS) which is an open-ended equity mutual fund is qualified for deduction under section 80C with lock-in period of three years. Further, dividend and capital gain are tax exempt.

To make the term deposits at par with ELSS, the lock in period for 80C should be reduced from present five years to three years. To induce long term savings through fixed deposits it is essential to remove the tax arbitrage. Further, this would be revenue neutral as there will be no loss to the Revenue.

Recommendations

- Limit of deduction under section 80C may be increased from INR 150,000. A new section should be inserted under Chapter VI-A which provides for deduction of contribution to provident fund from the gross total income in addition to deduction under section 80C. This would encourage investments in other schemes provided in section 80C and increase the liquidity and investments in the country.
- Lock-in period for term deposits should be reduced from five years to three years.

9.5 Deduction of Principal Repayment of Housing Loan Borrowed by an assessee from his employer being a Private Company

Currently the assessee is restricted to claim deduction U/s 80C(xviii) of the principal amount for amount borrowed for purchase etc. of a House Property. It is common that the employees in private sector are provided loans at concessional rates by employer. The employees are also charged to income tax on the concessional part of the loan provided under perquisites.

Recommendations

It is suggested to include the repayment of loan by the employee in private sector to the employer for deduction under section 80C (xviii) of the Income Tax Act.

9.6 Consideration of FTC while computing TDS to be deducted from salary payments

With globalisation, most companies have internationally mobile employees. These employees may be subject to tax in overseas countries and taxes are withheld on behalf of such employees and deposited as per the local provisions of the overseas jurisdiction.

When the employees are deputed back in India or any payment is made by the Indian employer of such employees, presently there is no mechanism to extend foreign tax credit to such employees while deducting their taxes in India. The new tax return forms have facility to consider foreign tax credit, which supports that income tax authorities recognize granting of foreign tax credit. However, as no mechanism exists for allowing credit while deducting tax, such employees have to claim the credit for taxes withheld in foreign jurisdictions only in their return of income and claim refund for excess tax withheld which creates undue hassle for such employees.

Recommendations

It is recommended that suitable amendment should be made to section 192 to explicitly clarify the employer to consider foreign tax credit while deducting tax at source from salary income of the employee.

9.7 Deduction in respect of Health Insurance Premia under Section 80D

Currently, a deduction up to INR 55,000 (25,000 for self/ family and 30,000 for senior citizen parents) is available to an individual under Section 80D of the Act from taxable income, towards health insurance premium paid by him. The limit for parents is increased to INR 30,000 if the parents are senior citizens. Unlike many other countries, India does not have a comprehensive health-care system for its citizens. There are Government hospitals but the facilities available are woefully inadequate while the private hospitals are very expensive. Also, the penetration and awareness of health insurance in India is very slow. Most individuals buy insurance only to save taxes.

Recommendation

There is a need to raise the above limit to achieve two-fold objective of giving a tax incentive while also encouraging people to obtain larger healthcare cover in wake of the rising costs.

9.8 Restoration of section 80CCF of the Income Tax Act

Section 80CCF was introduced in 2010, providing Income Tax deduction for two assessment years viz. A.Y. 2011-12 and A.Y. 2012-13 for subscription to long term infrastructure bonds issued by LIC, IFCI, IDFC and NBFCs classified as Infrastructure Finance Companies (IFCs) on investments up to INR 20,000, over and above the Rs.100,000 deductions available under other sections. The investor would have a minimum lock-in period of 5 years in the long term bonds. The objective was to promote savings of retail investors in bonds and raise funds for infrastructure.

Recommendation

This exemption is justifiable with a limit of INR 50,000 in spite of a minimal loss (of tax) to government given that this would support infrastructure projects. At the same time, it would enable raising of lower cost long term funding as well as participation of retail investors.

9.9 Revision of minimum exemption limit for allowances

- The transport allowance granted by the employer to the employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty is currently tax exempt up to INR 1,600 per month in terms of Section 10(14) of the Act read with Rule 2BB of the Rules. This exemption limit seems quite nominal considering the ever rising fuel costs and resultant conveyance costs.
- The education allowance granted by the employer to the employee to meet the cost of education expenditure up to two children is currently tax exempt up to INR 100 per month per child in terms of Section 10(14) of the Act read with Rule 2BB of the Rules. This exemption limit was fixed in 2000 with retrospective effect from 1 August 1997 and seems quite nominal considering the ever rising cost of education.

Recommendation

- The exemption limit of INR 1,600 per month needs to be considerably raised upwards, say to minimum of INR 5,000 per month to bring it in line with the rising conveyance costs.
- The exemption limit of INR 100 per month needs to be considerably raised upwards, say to minimum of INR 2,000 per month to bring it in line with the rising inflation and cost of education.

9.10 Leave Travel Concession

At present the leave travel concessions for employees are based on calendar year.

Further, Section 10(5) allows exemption for assistance or concession received from employer for employee and his family on leave to any place in India. There is no provision in the Act which covers the travel outside India.

Recommendation

To be in line with the concept of “financial year” adopted by other provisions of the Income tax Act, it is suggested that the concept of calendar year should be replaced with financial year.

Section 10(5) should be amended to exempt the concession/assistance received from the employer for foreign travel as in case of domestic travel.

9.11 Reimbursement of Medical Expenditure - Section 10

Any sum paid by the employer in respect of any expenditure incurred by the employee on the medical treatment of self/ family is currently exempt from tax, to the extent of INR 15,000 per annum.

Recommendation

The current tax exemption limit of INR 15,000 per annum needs to be increased to at least INR 50,000 per annum. This could to some extent help to bring the exemption up to speed with the rising medical costs.

9.12 Rent Free Accommodation

There is no beneficial perquisite of rent free accommodation provided in a campus accommodation where factory is located in remote areas.

Recommendation

It is suggested that due consideration should be given to the facts where accommodation is provided by the employer in factory campus and staying there is a need of employment. In such cases, accommodation should be valued at NIL / or lower rate of 5% of Salary.

9.13 Meals and meal vouchers provided by employers

Para (iii) of sub-rule 7 of Rule 3 prescribes the valuation norms for free food and non-alcoholic beverages provided by the employer to an employee during working hours. A limit of INR 50 per meal has been prescribed up to which the said benefit is not taxable in the hands of the employee. This limit of INR 50 was introduced in 2001.

Further, it may be noted that provision of electronic meal card to employees is not specifically included in Rule 3(7)(iii), however, the same was mentioned during the FBT regime. Accordingly, confusion arises whether or not electronic meal cards are covered by Rule 3(7)(iii).

Recommendation

- Keeping in mind that the original limit was set over 15 years ago and the significant increase in food prices in the past 15 years, it is suggested that the limit should be increased to a minimum of Rs.200 per meal in line with the inflation since 2001.
- It may be specifically clarified that benefit of INR 50 per meal shall be extended even to electronic meal cards as was extended in the FBT regime.

9.14 Gifts provided by employers

Para (iv) of sub-rule 7 of Rule 3 prescribes the valuation norms for gifts given by employers to employees or members of their household on ceremonial occasions or otherwise. The value of perquisite is taken as nil where the aggregate value of such gifts during the previous year is below INR 5,000.

Recommendation

Keeping in mind that this limit has been constant for quite many years and the impact of inflation on prices, it is suggested to revise the limit to INR 18,000.

9.15 Taxation of specified security or sweat equity shares allotted to employees under Employee Stock Option Plans ('ESOPs') in case of migrating employees - Section 17(2)(vi)

Taxation of ESOPs creates an issue in the case of migrating employees, who move from one country to another, while performing services for the company during the period between the grant date and the allotment date of the ESOP. The domestic tax law is unsettled on the taxation of such migrating employees and does not clearly provide for such cases.

During the erstwhile Fringe Benefits Tax (FBT) regime, there was a specific clarification on the taxability, where the employee was based in India only for a part of the period between grant and vesting. However, there is no specific provision in this regard under the amended ESOP taxation regime from 1 April 2009.

Recommendation

The Government may look at providing clarity on the taxability of ESOP's for such mobile employees.
